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## **Management Forum: Corporate Social Responsibility**

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### **Report of the APO Top Management Forum on Corporate Social Responsibility**



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# TOP MANAGEMENT FORUM

## Corporate Social Responsibility



ASIAN PRODUCTIVITY ORGANIZATION

Report of the APO Top Management Forum on Corporate Social Responsibility

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## Foreword

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Today, businesses are expected to extend their attention beyond stockholders, customers, and employees to include other stakeholders such as the community and environment. The concept of corporate social responsibility (CSR) emerged from such expectations and now consists of transparent organizational management; careful consideration of the global environment, human rights, and employment; and, in particular, compliance with ordinances, regulations, and laws.

Broadly defined as a “responsibility for business corporations to observe the social rules and contribute to the society within their scope,” CSR can lead to more sustainable corporations by encouraging good relationships with society. Although it appears natural to expect corporations to conduct business in a manner that maintains good relations with various stakeholders and improves the environment, it is not easy for all to achieve the required level of CSR.

Establishing CSR is not a simple task, nor is it free from risks and problems. CSR requires support not only from shareholders and investors but also from customers, employees, and communities. One conclusion drawn from both successful and failed examples of attempts to practice CSR is that top management must have a strong belief in the role of CSR within the organization. A lack of such belief has often led corporations to lose brand value and a good corporate image built up over many years. Bankruptcy may be even result.

Establishing sound CSR systems needs the involvement of a wide range of stakeholders, such as workers, customers, and shareholders as well as the community. Workers’ rights must be respected, and customers’ needs must be satisfied. Shareholders’ dividends must be guaranteed, and the community must be convinced of the merit of corporate activity. CSR weighs all these divergent interests and tries to strike an appropriate balance among them. I hope that the sharing of their experiences by the excellent speakers at the Top Management Forum held in March 2005 and now published in this volume will provide you with opportunities to study CSR so that your corporation can achieve long-term higher productivity and competitiveness.

I would like to take this opportunity to express my deep gratitude to the distinguished speakers at the forum. We were fortunate to have Professor Iwao Taka of Reitaku University as a keynote speaker and Mr. Hideo Suzuki from the Japanese Ministry of Economy, Trade and Industry as a special speaker. Both reminded the audience that the issue of CSR is relevant to all countries, developed or developing.

I also wish to express our thanks to the Japanese government for financial support and to the Japan Productivity Center for Socio-Economic Development for its assistance in organizing the forum.

I hope that readers will gain new insights from this publication on how CSR should be interpreted and implemented in the ever-developing global economy.

Shigeo Takenaka  
Secretary-General

Tokyo  
May 2006

## Introduction

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The term “corporate social responsibility” (CSR) is not newly coined jargon. It appeared in the Japanese media often in the 1960s, when environmental pollution problems were prevalent. The concept itself can be traced back to the merchants of the Edo period. Even at that time, those merchants believed business should ultimately benefit sellers, buyers, and the society at large.

The advent of sophisticated information and communication technology has completely changed ways of doing business. As such, companies cannot ignore the voices of various stakeholders. Particularly in today’s globalizing market when business activities easily transcend beyond national boundaries, companies must take into account every possible impact of their business activities.

It is not easy to define CSR. A main reason for this is the presence of various stakeholders. With the globalization of the economy, such issues as environmental degradation and violations of human rights are adding new meanings to the concept of CSR. As a result, despite the mounting interest in CSR worldwide, it appears the concept still lacks a clear-cut definition. Overall, however, it may be inferred CSR contains both negative and positive connotations. The negative one relates to legal compliance, which is associated with compulsory or regulatory features. The positive connotation is associated with social contributions to local, regional, national, or even global society. It is suggested that CSR can resolve the contradictory desires of employers, investors, and other stakeholders which stem from the unequal aspects of information exchange among them.

In view of the global interest in CSR, the APO’s “Top Management Forum” for the year 2005, which was the 21<sup>st</sup> in this series, took up the subject of CSR as its focus. The Forum was held in Tokyo, Japan, on 28 February–3 March 2005. Thirty participants including top executives of private companies from 16 member countries discussed how business corporations could strengthen their global competitiveness by fulfilling their social responsibilities. This publication contains the presentations made by the distinguished speakers comprising renowned executives and personalities from Japan. A prognosis on CSR by Mr. Arif Zaman, advisor of the Commonwealth Business Council, and Rapporteur of the Forum, is provided at the end to further reflect on the direction of the CSR in the future.

An overview of the CSR situation in Japan can be seen from results of a survey on CSR conducted by the Japan Productivity Center for Socio-Economic Development (JPC-SED) in 2005. The survey reveals almost 80% of Japanese listed companies were already implementing CSR activities. However, the level of their activities differ, which can be classified into three levels. Most, around 45%, evaluated their CSR as being at the level of legal compliance, while 36% reported that it was at the corporate ethics level, and 14% that it was at the social contribution level. Overall, the survey results indicate that Japanese companies have just begun to incorporate CSR activities in day-to-day business activities.

In line with the JPC-SED survey, Professor Iwao Taka of Reitaku University also referred to three phases: legal compliance, ethical practices, and social contributions. Legal compliance is the most basic, minimum requirement in modern society and is easy to understand, although simply abiding by the rules and regulations appears to mean that anything not explicitly prohibited by law could be engaged in. Ethical practice is also

understood relatively easily, because good companies often comply not only with the letter of the law but also with its spirit and background. However, the third concept of social contribution is viewed differently depending on geographic location. In Professor Taka's definition, social contributions are how companies act to help others and have positive impacts on the community, environment, and for future generations. When it comes to environmental issues, it is very clear because it is commonly understood that without actions to reduce, for example, the emission of carbon dioxide, serious global warming will occur. Overall, activities related to environmental protection are visible and tangible. However, a positive impact on the community or on future generations is difficult to gauge. This may be the main area that causes misunderstanding of CSR.

As Mr. Hiroshi Hirano of Sampo Japan Insurance Inc. and Ms. Mariko Kawaguchi of Daiwa Institute of Research Ltd. put it, corporate value is judged based not only on financial performance but also on environmental and social performance. Here again, social performance is not a clear concept. This may be the reason for the belief held by some that companies engaged in philanthropy are automatically good corporate citizens. This may not always be the case.

The basic point of CSR is that it leads to higher productivity. Mr. Hideo Suzuki of the Japanese Ministry of Economy, Trade and Industry, referring to the theory of Mr. Eiichi Shibusawa, founder of modern Japanese capitalism who stressed the importance of harmony between morality and the economy, and argued that "as long as it is called business, it must profit oneself as well as society and the nation." Ms. Kawaguchi also pointed out that the recent trend toward socially responsible investment (SRI) is based on economic return, not social return as in the past. As such, SRI performance is better than that of conventional investments. After numerous corporate scandals worldwide, investors realized that looking at financial data alone is insufficient. To avoid investment risk, it is necessary to examine a company's environmental management and ethical and social behavior.

The International Standards Organization (ISO) is now in the process of establishing guidelines for social responsibility (SR). In this context, Mr. Minoru Inaoka of Ito-Yokado Co., Ltd. argued there must be an Asian version of CSR because Confucian ethics and values are universal in East Asia. In the same line, Mr. Morio Ikeda of Shiseido Co., Ltd. also cited Confucianism as the basis of the Asian spirit.

Although the guidelines on SR by the ISO have yet to be released, the most important element in CSR is for corporations to be proactive, not passive. They should not engage in CSR activities because of external pressure but to create greater corporate value, which cannot be judged from a short-term perspective. In addition, CSR issues are not only relevant to developed economies but to developing ones as well, since all business activities are interlinked in the worldwide supply chain.

Takuki Murayama  
Director, Research & Planning Department  
Asian Productivity Organization

# Corporate Social Responsibility: Current Context and Future Directions

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*Iwao Taka*  
*Reitaku University*

At the outset it is important to relate corporate social responsibility (CSR) to the sustainable development of societies. This is best approached from five distinct areas:

1. The kind of issues the concept of CSR covers;
2. Why CSR is required, especially in relation to business organizations;
3. Major challenges at the global level, such as the United Nations (UN) Global Compact and also the International Organization for Standardization (ISO) initiative;
4. Institutional changes involving CSR underway in Japan; and
5. ECS2000, an evolving Japanese ethical/legal compliance management system standard.

## Scope of CSR

What issues does CSR cover? There are three groups of issues: legal compliance, ethical practices, and social contributions. Legal compliance means corporate acts that comply with the letter of laws and regulations, including those that are related to human rights, environment, labor, or consumer protection. Ethical practices denote corporate acts that comply with not only the letter but also the spirit of laws and regulations. Social contributions are how companies act to help others and bring about positive impacts and influences in the community, environment, and for future generations. Recently, the concept of social contribution is likely to be understood in a much broader sense, going beyond a purely monetary donation to include action to overcome ethical dilemmas that a business organization might face.

Table 1 explains how those three groups of issues are related. It shows two dimensions. Justice means that CSR covers issues of justice, right or wrong, and fair or unfair. Humanity means issues of good/bad for others, and helpful/harmful for others. Basic means an organization's basic commitment to CSR.

Using these two axes, there are four boxes:

- Phase 1, Legal Compliance: The compliance section or the ethics office is mainly concerned with establishing the legal way to avoid the application of laws. The objective is to find the loophole that makes it possible to avoid the reach of the law. If international agreements are ratified and codified into domestic laws, companies at this level will try to comply with international agreements; but other than that, companies will not comply with such agreements willingly.
- Phase 2a, Ethical Practices (the upper box on the right): Companies try to avoid any action resulting in a negative impact on others and any action that might cause harm or damage to others.
- Phase 2b, Ethical Practices (bottom box on the left): Companies comply with not only the letter but also the spirit of the law. Even if international agreements are



not ratified or codified into domestic laws, companies at this level will try to understand and put those spirits into practice.

- Phase 4, Social Contributions: Companies exert positive influences and impacts to help others or, for example, develop environmentally friendly technologies.

Table 1. Three phases in CSR

Basic	Phase 1. Legal compliance  Do no wrong Do not be deceptive Do not steal Letter of the law	Phase 2a. Ethical practices  Do not harm others Do not harm community Respect human rights Be considerate
	Phase 2b. Ethical practices  Do right Be honest Be fair Spirit of the law	Phase 3. Social contribution  Help others Improve community Promote human dignity Be courageous
Justice		Humanity

Source: Adapted and developed from Lynn Sharp Paine, *Value Shift: Why Companies Must Merge Social and Financial Imperatives to Achieve Superior Performance*, McGraw-Hill Education, 2003.

Moving beyond this framework, an actual business case relating to anticorruption shows how these issues are related when the company aims to avoid unfair benefits to foreign officials. With regard to legal compliance, in Japan, there is a law that bans corporations from providing unfair benefits to foreign officials or politicians with the intent to receive unfair favors from them in return. Until 2004, this law was enforced only if elements of the offence occurred within Japan. Therefore, a dishonest company could avoid application of this law merely by issuing a simple instruction to employees that when they are out of Japan, if they are asked some favor by foreign officials, they should not ask Japanese headquarters but decide which course of action to take by themselves. In practical terms, this means that receiving an e-mail or a fax would show that elements of the offence occurred in Japan. At this level, the company is adhering to legal compliance. If it progresses to the second phase of ethical practices, it takes into account why those laws were created and tries to avoid providing unfair benefits to foreign officials. If the company behaves according to “Ethical Practices” (upper box on the right in Table 1), it is likely to think that an act of bribery is the kind of action that can cause harm to the country in which it is operating. Because, for example, if the company provides unfair benefits to foreign officials in order to make a successful bid for a national infrastructure project, then those foreign officials or persons with privilege would become richer than in the case when the company did not provide such unfair

benefits. In addition, the cost of the project would probably be significantly greater than in the case when the company did not provide a bribe to foreign officials. The higher cost of that project would probably be covered by taxpayers and, therefore, an act of bribery will harm society. Providing bribes might distort fair income distribution, thereby destroying the justice and the welfare of the country. This would provide the rationale for companies at this level to refrain from providing unfair benefits to foreign officials.

As previously mentioned, social contribution is not just providing monetary donations but includes practical or creative action making it possible to overcome ethical dilemmas. Here is a real example. One American multinational wanted to do business in a developing country. It submitted materials for approval, but a couple of weeks before signing a contract, a representative of that company was asked to provide a favor to a high-ranking official of that country. The representative faced an ethical dilemma. He knew only too well that this kind of action is clearly against American law (i.e., the Foreign Corrupt Practices Act,) but at the same time the company was eager to do business there. After an intensive series of discussions among senior management, the company decided to provide money to the foreign official but in a creative manner. They provided the money transparently, in a way that everybody knew the money transaction through the foreign official was for a national environmental protection project. In this case, the company benefits because it can do business in a country. The second party, the foreign official, even if he did not receive any money, still benefited because the people in the country thought that project was promoted thanks to the official's efforts. Therefore, the second party also benefited from this decision. The third party—society and the future generations—also benefited from the project, and thus it created win-win situation.

### **Why CSR Is Necessary**

Why is CSR required? There are two levels of reasons. The first relates to globalization itself. In a sense, globalization is the creation of a new business era when a business corporation can enjoy an enormous amount of freedom. There is no single government or single law enforcement body to apply the same laws and regulations to all players. International agreements exist but can easily be ignored in a number of countries. In addition, most developing countries have very comprehensive laws and regulations but lack effective infrastructure to enforce them. Some developing countries might deregulate their standards or regulations in the fields of environment and labor because they want to attract more foreign capital. Thus business corporations that are operating worldwide enjoy an enormous amount of freedom today. However, freedom should be followed by responsibility. In the absence of responsibility, globalization itself might come to a dead end. This is one reason why business corporations are now trying to develop CSR policies and also trying to establish internal systems that make it possible to reduce negative impacts and increase the positive influences over external stakeholders.

The second driver of CSR varies from country to country and region to region. Each society has different issues to be solved with the help of a business corporation. People in the USA suggest that American corporations have been externalizing costs in order to report ever-increasing quarterly earnings, with costs passed on to everybody except for shareholders, such as consumers, workers, or the environment and community. In order to rectify such an excessively shareholder-centered management style in the USA, CSR is emphasized.

In Japan too, excessive CEO-centered management styles have also been criticized. Shareholders' meetings do not work properly and boards of directors are not functioning

as the Japanese commercial law expected. Even labor unions do not play their own role properly. The problem was that CEOs had excessive power and could decide whatever they wanted. Until the early 1990s, this characteristic of Japanese management worked to the benefit of Japanese corporations because, with a long-term perspective, top managers could decide whatever they wanted very quickly. However, after the mid-1990s and especially after the long-lasting recession, this trait began to work to the detriment of Japanese corporations and society. In order to protect their own personal position, some top managers in companies began to be involved in unethical or illegal activity. As a consequence, in Japan, society expects business corporations to be much more ethical and more accountable than ever. The issue now is how to establish integrity in business corporations.

### **Drivers and Changes at the Global Level**

CSR is reflected in major global challenges. One of most well-known is the UN Global Compact. This was started in response to a keynote address made by UN Secretary General Kofi Anan at the World Economic Forum in Davos in 1999. In his address, Anan asked world business leaders to make more efforts to solve world issues in the fields of labor, environment, and human rights. The UN then set up the Global Compact Initiative and asked a number of business organizations to participate. The Global Compact was drawn from nine principles based upon international agreements, such as the UN Declaration of Human Rights, the International Labour Organisation's core conventions, and the Rio Declaration on Environment and Development. A tenth principle, the UN convention against corruption, was added in 2004. There are now more than 1,500 organizations participating in this initiative.

One of the challenges that the UN Global Compact has is that the participants do not have any specific obligations. Companies simply have to report on their commitment to CSR in their annual report once a year. This is a purely voluntary initiative. People have called for a framework that convinces us how seriously business organizations commit to CSR activities. One of the possible means might be an ISO approach.

In 2002, the Consumer Policy Committee (COPOLCO), one of the major councils of the ISO, recommended at the annual meeting that the ISO should explore the desirability and feasibility of CSR standards. In response, the ISO Council established the Strategic Advisory Group (SAG). This group discussed the desirability/feasibility of an ISO/CSR standard for more than one and a half years and failed to reach a conclusion. Its report highlighted the advantages and disadvantages of creating a new standard.

The opposing group insisted that we do not have a commonly held definition of CSR. How can we create a third-generation standard without having a definition, without a common understanding of elements of CSR? The supporting group insisted that the definition and a common understanding over elements are not so important. In the past, ISO14000 was created when there was the same debate that "we do not have a common definition or understanding of environmental protection." Therefore, it is possible to develop a third-generation standard even if we do not have a commonly held definition of CSR or a common understanding of its elements. The supporting group also insisted that if the ISO does not take the leadership role in developing CSR standards, and there are already more than 11 national CSR standards from both developed and developing countries, there is a risk that one of the existing national standards might become the *de facto* international standard. This is not desirable, as all countries and ISO member bodies want to participate in the process of developing a CSR standard.

However, if one of the existing standards were to become the international standard, the rest of the member bodies would eventually be excluded from the development processes. To avoid this, the ISO should take a leadership role in developing an ISO/CSR standard.

In response, the opposing group argued that what is needed in the field of CSR is not the old-type management system standard, like ISO9000 or ISO14000. Those standards were process oriented and required organizations to establish internal processes, conduct education, and promote communication among members. However, even with ISO9000 or ISO14000 certification, organizations only have a certificate attached to the wall of the building entrance. Performance of quality or the performance of environmental protection has not been improved at all. The opposing group, mainly from industry, wanted to avoid the same mistake. If ISO wants to create a new standard, it should be result oriented, not process oriented. Moreover, the 11 CSR national standards already created by national bodies are all process oriented. If the objective is to create an international standard, this will probably not be a result- but a process-oriented standard. Therefore, it is not worth creating a standard.

In any case, after the publication of the report and an international conference, the ISO formally decided the following in June 2004:

1. The ISO should create a guidance document but this should not be used as a third-party certification framework.
2. The ISO should facilitate experts from NGOs, consumers, and industries to participate in the standard development processes (this is the key.)
3. The ISO expects the project to be conducted under the leadership of developed and developing countries. This involves "twin leadership" from Brazil and Sweden in developing an SR standard (the ISO called this standard an SR standard because it will be applied not only to business organizations but to all types of organizations.)
4. The ISO expects the SR guidance document to be published in early 2008.

Thus we have reached a point where the ISO's decision cannot easily be reversed.

### **Institutional Changes Involving CSR in Japan and ECS2000**

(Japanese ethical/legal compliance management system standard)

Merely proclaiming the importance of CSR is not enough to motivate or encourage business corporations to pursue CSR activities. It is necessary to create new social or legal regulatory environments where business people can really feel that organizational commitment to CSR constitutes an important element in maintaining a competitive edge in the market. This has provided the context for facilitating institutional changes by the private and public sectors in Japan, of which three stand out.

The first institutional change is the creation of an ethical/legal compliance management system known as ECS2000. In 1991, Keidanren, Japan's most influential business roundtable, published its charter of business conduct and asked member corporations to adopt it. In 1996, Keidanren revised that charter to make it easier for member corporations to use it in a daily business context. However, the following year, it came to light that some of the major Keidanren corporations had long been involved in wrongdoing. As a result, Keidanren was criticized by many in Japan and could not take any further action on this model at that time. In the light of this impasse, another business roundtable, Kankeiren with headquarters located in the Kansai area, started its new Business and Society Project. In its report, it concluded that publishing codes of conduct

is not enough for business corporations. What is needed are effective internal systems and processes, which make it possible for business organizations to comply with not only the letter but also the spirit of the law and regulations.

In response to that conclusion, I organized my project at Reitaku University called the ECS2000 Initiative. This was created with the help of 22 experts including lawyers, certified public accountants, business practitioners, and business consultants. In 1999, we published the ethical/legal compliance management system standard that showed what corporations have to do to establish effective internal systems. In 2000, after receiving feedback from business practitioners, we revised the ECS2000 and published the Guidance Document, which shows how to apply ECS2000 to a daily business context. There are now more than 500 Japanese listed corporations using ECS2000 to establish and improve their internal systems.

After the publication of ECS2000, the public sector started similar projects. The Cabinet Office published the Codes of Conduct Guidelines which requires business organizations to develop their own codes of conduct and also establish effective internal systems enabling those codes of conduct to be put into practice. At the same time, the Ministry of Economy, Trade and Industry also published the Internal Control Guidelines as a basis of risk management. Consequently, Japanese corporations are changing very rapidly.

Another institutional change is the legislation of Public Interests Disclosure Act, a whistle-blower protection act. In recent years, Japan has witnessed an increasing number of whistle-blowing cases, which looks set to increase further. While some Japanese criticized whistle-blowing as an act of treachery, whistle-blowing continues to play a very important role in making society fairer and safer. This led to the Public Interests Disclosure Act which used British law as its basis. Its key elements are:

1. When whistle-blowers report wrongdoing, they must do it in the public interest. If this is done for their own personal benefit and the report discloses wrongdoing, the damage caused by the company might not be recovered from.
2. When a whistle-blower discloses wrongdoing, he or she must do it internally. If he or she does not report it internally first and reports it to the mass media or third-party agencies, the damage caused by the company might not be recovered from.
3. If a number of conditions are satisfied, whistle-blowers do not need to report the wrongdoing internally and they can report it externally. The first requirement is if reporters reasonably feel that an act of reporting would cause direct or indirect damage to them, they do not need to report internally and they can report it externally. The second requirement is if reporters reasonably foresee that an act of reporting would cause a distraction of evidence, data, or documents, or the falsification of data, then they do not need to report it internally and they can report it externally. Finally, after having reported the wrongdoing internally, if the reporters do not receive any response from the internal section within a certain period of time, then they can report it externally.

As a result of the Public Interests Disclosure Act, an increasing number of Japanese corporations have been establishing effective internal systems and ethics hotlines. In order to protect the privacy and confidentiality of reporters, a number of Japanese corporations have also been using outside, third-party service providers.

The third institutional change is the rise of the Japanese version of socially responsible investment (SRI). SRI is a new type of investment movement in response to social expectations of investors. Social investors are people who want to improve conditions in society by investing their money in shares, by divesting their money from shares, or by exercising shareholders' rights. For example, in the USA in the early 20th century, Christian groups began to ask financial institutions not to invest their money in so-called sinful industries, such as tobacco companies, alcohol businesses, gambling-related businesses, excessive loan providers, nuclear power plants, and weapon-related businesses. Based upon a religious belief, they therefore made decisions about which industries they should invest in. This movement has expanded to include not only Christian groups but also investment groups who want to change society not only in terms of Christian values, but also in terms of human rights, labor, and environment.

In Japan, it is likely that this type of SRI would not be welcomed by a majority of people. The American type of SRI is basically Christian value oriented, and the method of excluding some businesses from the SRI portfolio is called negative screening. This is not rational as such because it is only based upon religious values. Japanese implicitly think that this might promote social discrimination against specific industries or jobs. In Japan, what kind of products and services companies are providing is secondary. The key point is how sincerely and how faithfully corporations and workers are performing.

Even so, after the mid-1990s, Japanese society as a whole showed a much keener interest in how corporations are ethical and accountable. Moreover, society expects that the ethics of a corporation should be established on unshakable integrity. Taking into account this Japanese cultural trait, and also ever-increasing expectations, led to the R-BEC001 project. This is the name of a new type of screening method and framework with focus on the integrity of business organizations. This framework is public, and any rating agency can use it freely. In this way the R-BEC001 framework enables companies' rating agencies to evaluate how seriously top management are committed to CSR and how their ethical/legal compliance internal systems are functioning. Japanese corporations are taking into account evaluation by R-BEC001 and improving their internal systems. In 2004, Daiwa Securities released a new type of SRI fund which is the biggest in Japan, except for the environmental fund, because Daiwa Securities' SRI fund is based on R-BEC001.

As a consequence of these institutional changes in Japan, an increasing number of corporations has been promoting a commitment to CSR and especially improving integrity in their accountability. What does ECS2000 require companies to do? First, companies need to create codes of conduct but unfortunately most tend just to imitate or copy other companies'. With regard to codes of conduct, the first thing that the corporation has to do is to analyze what kind of risk they have, any infringement of relevant laws and regulations, and any deviancy from social norms or international agreements. The code of conduct may be drafted or revised only after analyzing and understanding the risk.

In this connection, there is an interesting study. After Enron collapsed, its code of conduct was sold by its employees on the Internet auction site "eBay" with a comment saying: "it is brand-new because it has never been read." What I want to say is if companies simply copy each other's codes of conduct, then it is likely that they too will never be read by employees and ethics will never be taken seriously by them.

Subsidiaries are likely to have more risks than the parent company as they might more often be involved in conflicts of interest. Working conditions in subsidiaries might

not be as good as those in the parent company. However, if all subsidiaries are using the same brand as the parent company, one single wrongdoing in a subsidiary will affect the entire corporate group, including the parent company. This is a kind of collateral risk that can affect corporate reputation. In industry, most assemblers try to externalize their work to suppliers but if they do so without adequate controls and monitoring mechanisms, then assemblers might increase infringement or deviancy risks because suppliers might use illegal materials, or substandard workforce methods. For example, the final product might be made of hazardous materials or some parts might be made by child or forced labor. Even if assemblers are not involved in this process directly, once those products are manufactured in such a way they could be blamed. Supply chains carry risks.

When businesses start to use new technologies or start businesses overseas, they can create another set of new risks because a new type of technology can be followed by a new set of standard regulations. If a new business is set up overseas, a new set of laws and regulations may need to be taken into account. Therefore, when businesses innovate and attempt something new, they must analyze and understand newly emerging risks comprehensively.

After creating codes of conduct and also creating implementation plans, the organization will probably have to establish an ethics office or another section in charge of ethical/legal compliance. Employees will almost intuitively know how seriously top management is committed to CSR by judging how those sections are created and how much authority is given to them. If enough resources, budget, or talent is not assigned to these areas, employees will intuitively know the company's commitment to CSR is just a part of its public persona and is not grounded in what it really believes and values, even if top management uses the right soundbites to the public.

The ethics office or team must provide training to managers and employees. This needs to be based on risk analysis, too. To meet the needs of each section and each job, ethics training should be differentiated and provided to different sections and job functions. For example, retailers have register counters. At the register counter, there is usually a donation box. If every time money in the register machine is short, the manager takes money out of the donation box to make the account "balance," this means that the ethics training program for those stores needs to address the manager's responsibility and donation box.

No matter how comprehensive and sophisticated the ethics training given to managers and employees, there is always the possibility that at some point someone might be involved in unethical activity. It is inevitable. Therefore, the organization must have some mechanism in place to prevent such a development from arising or worsening which can identify facts or symptoms of wrongdoing. This is where there is a role for an ethics helpline or hotline. When employees discover wrongdoing and report it, they should do so under their real names. If they report the wrongdoing anonymously, the company can face real difficulties, because after the first round of investigations based upon the original reporter's report, and if the company cannot find anything wrong, no further investigation can be made. This is not desirable for the reporter and the company itself. As employees may hesitate to report under their real names, there should be reliable internal systems that make it possible for the ethics office personnel to communicate with reporters while safeguarding their privacy and confidentiality.

One possibility is using third-party providers, such as lawyers and independent research companies. In recent years, an increasing number of Japanese independent research companies have started services for ethics hotlines. They do not give any advice

to reporters but receive reports from employees of the companies they have contracted with. After receiving the report, they transfer it to the company without revealing e-mail addresses or the reporters' names. In this way, the privacy and confidentiality of the reporters is protected, with the independent research companies taking the role of mere conduits of the information.

In summary, the basics of business have been radically changing at the same time as the prevalent policies of government. These changes are prompting business organization to be involved in CSR. Whether we wait and see what will happen next or whether we take a leadership role is in our hands. However, I hope that business leaders and policymakers take collective leadership to contribute to the realization of sustainable development in Asia and across the world.



# Policies to Promote Corporate Social Responsibility

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*Hideo Suzuki*

*Director*

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Corporate social responsibility (CSR) is a very topical issue. Within the Ministry of Economy, Trade and Industry (METI), a study group on CSR has been established with the support of large companies, small business enterprises, small NGOs, and consumer associations. The study group examined how governments should handle CSR issues and why CSR is important for corporations and for society.

## **History of CSR in Japan**

In Japan, a form of CSR can be traced to the Edo era in the 18<sup>th</sup> century in the ideas of the Ohmi merchants, who recognized that it was important for three parties, sellers, buyers, and the public, to benefit from transactions. The moral and economic teachings of Sontoku Ninomiya (1787-1856) toward the end of Edo era suggested that an economy without morality was criminal and that morality without an economic context had no meaning. These concepts formed the basis for the activities of corporations in Japan during the Edo era and in modern times after the Meiji Restoration. Eiichi Shibusawa (1840-1931) was the founder of modern Japanese capitalism. He advanced a theory of harmony between morality and the economy arguing, that “as long as it is called business, it must profit oneself as well as society and the nation.” These ideas and concepts were probably derived from Confucianism, but Shibusawa was influenced by Christianity. After the Second World War, the Keizai Doyukai (Japan Association of Corporate Executives) adopted “awareness and practice of social responsibility by management” at its national conference in 1956, declaring that, “The era when the profit of individual companies is harmonized with the benefits of society has disappeared. If management does not actively strive to coordinate the two, neither national economic prosperity nor corporate development will be realized.” Konosuke Matsushita (1894-1989), an outstanding entrepreneur in the Showa era and the founder of Panasonic, said that, “Your work is not yours for yourself but your work is the people’s work which they give you [in trust] to do.”

Those business leaders touched upon CSR-related concepts that were developed into a Corporate White Paper by the Keizai Doyukai in March 2003 on the “Evolution of Market and Socially Responsible Management.” Nippon Keidanren (Federation of Japanese Economic Associations), the largest association of corporation, issued the “Charter of Corporate Behavior” in May 2004, reflecting practices and discussions of CSR in Europe, the USA, and elsewhere. It stated that: CSR contributes to sustainable mutual development of corporations and society; is an investment which should be positioned as the core of business; and is comprised of voluntary activities.

**Nippon Keidanren Charter of Corporate Behavior (excerpt)**  
**(established in September 1991 and amended in May 2004)**

Member corporations of Nippon Keidanren (hereafter referred to as “Members”) believe that corporations exist not only as economic entities designed to pursue profits through fair competition, but also as social entities which must make a contribution to society at large. Members are expected to respect human rights and to conduct themselves in a socially responsible manner toward the creation of a sustainable society, observe both the spirit as well as the letter of all laws and regulations applying to their activities both in Japan and abroad in accordance with the following ten principles.

1. Members, by the development and provision of socially beneficial goods and services in a safe and responsible manner, shall strive to earn the confidence of their consumers and customers, while taking necessary measures to protect personal data and customer related information.
2. Members shall promote fair, transparent, free competition and sound trade. They shall also ensure that their relationships and contacts with government agencies and political bodies are of a sound and proper nature.
3. Members shall engage in communication not only with shareholders but also with members of society at large, including active and fair disclosure of corporate information.
4. Members shall strive to respect diversity, individuality and differences of their employees, to promote safe and comfortable workplaces, and to ensure the mental and physical well-being of their employees.
5. Members shall recognize that a positive involvement in environmental issues is a priority for all humanity and is an essential part of their activities and their very existence as a corporation, and shall therefore approach these issues more proactively.
6. As “good corporate citizens,” members shall actively engage in philanthropic activities, and other activities of social benefit.
7. Members shall reject all contacts with organizations involved in activities in violation of the law or accepted standards of responsible social behavior.
8. Members shall observe all laws and regulations applying to their overseas activities and respect the culture and customs of other nations and strive to manage their overseas activities in such a way as to promote and contribute to the development of local communities.
9. Management of members shall assume the responsibility for implementing this charter and for taking all necessary action in order to raise awareness in their corporation and inform their group companies and business partners of their responsibility. Management shall also heed the voice of their stakeholders, both internally and externally, and promote the development and implementation of systems that will contribute to the achievement of business ethics.
10. In the case of incidents contrary to the principles of this charter, management of members must investigate the cause for the incident, develop reforms to prevent recurrence, and make information publicly available regarding their intended actions for reform. After the prompt public disclosure of information regarding the incident, responsibility for the event and its effects should be clarified and disciplinary action should be taken, including the highest levels of management where necessary.

In parallel with the work of the private sector, the government undertook efforts to achieve CSR, although this was limited as it is believed that CSR must be promoted mainly by companies. The Cabinet Office issued the "Corporate Code of Conduct" at the subcommittee of the Consumer Policy Committee of the Quality-of-Life Policy Council in December 2002. This was mainly concerned with consumer confidence as there had been scandals concerning contaminated milk and consumer confidence in business had eroded. The report was titled "Building Up Consumer Confidence in Business: Guidelines for Corporate Codes of Conduct" and set guidelines to promote the establishment and implementation of corporate codes of conduct.

The Ministry of Agriculture, Forestry and Fisheries also responded to corporate scandals. It established a study group to promote transparent relationships between consumers and producers (a report was issued in March 2004) and proposed the promotion of corporate management emphasizing social responsibility related to food security and safety and increasing consumers awareness of safety and security efforts.

The Ministry of Health, Labor and Welfare established the Research Council on CSR in Labor and published an intermediate report in June 2004 on CSR for employees and labor relations between corporations and trade unions. The council suggested that consideration should be given to employees based on changes in their social conditions and the role of the government in the promotion of CSR in labor issues.

The Ministry of the Environment also established its Research Council on Social Responsibility (sustainable environment and economy) with a report due in March 2005 and proposed the ideal model for a sustainable environment and economy and how corporations should respond to environmental protection and global warming. That council proposed a draft act concerning the promotion of business activities and the environmental protection in specific sectors. That would involve the disclosure of environmental information by listing the items to be covered in companies' environmental reports. However, this proposal was strongly criticized by the private sector, and the Cabinet Legal Office believed that the ministry could not prove the need for legal legislation. Therefore, the Ministry of the Environment withdrew its proposal and requested Japanese Governmental agencies to report their activities in the environmental area.

METI has been active on a number of fronts. It has established the Study Groups on CSR (September 2004) and Study Group on Risk Management and Internal Controls (2002-2003). In the wake of repeated corporate scandals, a report was compiled as guidelines for internal controls and risk management. METI has promoted awareness among small and medium enterprises of social issues through nationwide presentations and seminars. It initiated an award system for outstanding corporations in 1990 with a minister's annual award for outstanding corporations with a fully developed consumer-oriented structure as well as awards for individuals and groups contributing to a consumer-oriented attitude among companies. Environmental reporting guidelines have been issued that emphasize the corporate accountability to stakeholders. The basic concept on the creation and disclosure of environmental reporting was summarized, and guidelines for environmental reporting were established in June 2001. In relation to socially responsible investment (SRI), low-interest loans were introduced by the Development Bank of Japan in 2004, which select screens and assess corporations where management demonstrates a commitment to the environment. International views have been exchanged at the APEC International Symposium held in Tokyo in January 2005.

## **METI Study Group on CSR**

The report of the METI Study Group on CSR was particularly significant. This group consisted of a range of stakeholders, such as corporations, business groups, consumers, NPO staff, employees, academics, and representatives of the media. A consensus was reached on key components of CSR.

The main message of the report was that CSR is fulfilled through communication with various stakeholders such as consumers, employees, investors, local residents, and NGOs. It is not only about communication with external stakeholders, but also organizational structures. It pertains not only to compliance with a minimum level of legislation, but also covers various activities that include ensuring the safety of products and services closely related to business, environmental protection including countermeasures to protect the global environment and waste recycling, improvement of the labor environment, human resource development, respect for human rights, anti-corruption measures, fair competition, local contribution, regional investment, support for arts and cultural activities, and philanthropy.

CSR varies according to the value system, culture, economy, and social conditions of countries and regions and their stage of development. Voluntary action, diversity, and the strategic efforts of corporations are important with regard to the contents and efforts of CSR. The important elements in efforts supporting the reliability of CSR are information disclosure, accountability, and communications with stakeholders.

Internal aspects of CSR involve identifying and analyzing corporate risk and reducing risk through the implementation of countermeasures. CSR activity can increase morale among directors and employees by clarifying corporate behavior. It can help to achieve higher productivity by eliminating waste and risk, and allocating appropriate resources through the revision of the management and organizational structure to promote CSR efforts. Its link with productivity is one reason why the APO's Top Management Forum organizers selected CSR as its theme in 2005.

One of the main aspects of CSR is the creation of new markets by considering environmental countermeasures and the safety of products and services. CSR activities help to build corporate reputations and improve brand value by ensuring the safety of products and services. CSR can help develop a complete corporate risk management system and allow corporations to engage in philanthropy beyond the basic framework of the business. In contrast, deficient products and services and corporate scandals lead to consumer boycotts and reduce brand power and value over time. CSR can provide a better working environment, develop human resource and respect for human rights, help in recruiting well-qualified employees, and enhance human potential and capabilities in the company. All these activities will increase the corporate value, which results in higher and stabler stock prices.

CSR activities matter to society. As a whole, they can help to overcome factors restricting economic growth such as environmental considerations, energy, and fewer children and an aging society and achieve sustainable growth for corporations and society. CSR can allow worry-free consumption by providing safe products and services. It can reduce financial burdens through deregulation and the principle of self-responsibility. CSR also has a role to play in overcoming North-South problems by helping to solve social problems in developing countries.

The METI Study Group on CSR also assessed how CSR activities can be implemented effectively. In this area, the drive should come from the private sector. CSR activities must be pursued under clear guidelines, without which it will not work

effectively. Company management must establish clear, action-orientated guidelines on CSR and solicit the active participation by employees. Top management commitment to CSR is necessary, but all employees should understand the guidelines that affect all activities. At the same time, management and employees need to work together in clarifying the concept of CSR, developing action guidelines, and undertaking specific initiatives. The sharing of values, along with a sense of enthusiasm and mission, can facilitate CSR through a system that encourages active employee participation.

It is very important for a company to develop a core CSR promotion unit and to establish an internal corporate control system. Centralized control of CSR efforts can prove effective, and the company will need to communicate its CSR action guidelines to all employees through the construction of an internal control mechanism and carry out business in line with this mechanism. Collaboration with affiliated companies, group companies, and business partners is also a key. Promotion of CSR should be carried out within the corporate group under the corporate brand to target overall group companies and the overall supply chain. CSR guidelines can be developed, and employees and top management asked to comply with them, but guidelines may not always be appropriate and/or need to be changed in the light of external conditions. The plan, do, check, and action cycle can help ensure that guidelines are appropriate for CSR through reviews and revisions.

Sharing and promoting best practices of corporate initiatives through information exchanges among companies can improve CSR activities. Such networks exist in Europe and an Asian CSR international network may be needed. This cannot only give companies fresh ideas and help build on best practices but also help NGOs, trade unions, and other stakeholders to understand what occurs in corporations and in communities.

Communication with external stakeholders is essential for promoting CSR with full disclosure and accountability. In terms of disclosure, management commitment to CSR is the first priority, with the willingness to deal with adverse information. For effective communication, it is important to construct a mechanism to provide feedback in the form of requests, opinions, and assessments of stakeholders in the review and development of CSR guidelines.

The METI Study Group on CSR also considered the actions government should take concerning CSR. It concluded that the government should have a very "soft touch." The foundation for CSR should be voluntary efforts by corporations, business groups, SRI firms, and NGOs taking the initiative in promoting and encouraging CSR. The government is best equipped to provide secondary assistance to those organizations in various ways. It can collect and analyze examples of CSR from which people can learn domestically and promote best practices and establish opportunities to exchange opinions between various stakeholders and corporations or among corporations themselves internationally.

CSR should not be seen or pursued as a short-term fad. Communication should be enhanced instead of creating a confrontational atmosphere between corporations and their stakeholders. In addition to corporations, NPOs, NGOs, educational organizations, and governments all have important roles to play. An independent, voluntary style should be adopted instead of the problem-solving style.

There is a need for individual awareness of social responsibility. It is not enough to focus on expectations of corporate behavior alone. It is also necessary to increase the awareness of social responsibility among stakeholders who support the efforts of corporations such as consumers, researchers, and all segments of society.

## **Social Responsibility Developments in the ISO and Japan's Initiatives**

The International Organization for Standardization (ISO) is a private entity. In Japan, the national standard body is directly supported by the government, with METI serving as the secretariat of the national standard body. The current president of the ISO is Japanese and a former METI official, and thus there are strong ties with the activities of the ISO.

In January 2005, the Social Responsibility (SR) Guideline (Japanese draft) was presented to the ISO. There were a number of prerequisites derived from the ISO/Strategic Advisory Group on CSR recommendations, international conferences, and ISO Technical Management Board resolutions. The guidelines define SR and facilitate its common understanding; provide practical guidance but do not intend to establish third-party certification; be applicable to all types of organizations and written in language that is clear and easy to understand even by nonexperts; support SR implementation in an organization while respecting differences in culture, society, environment, statutory and regulatory requirements, and economic development; emphasize results and performance improvement; and be consistent with existing documents, international agreements, conventions, and existing ISO standards.

Intended characteristics of the guidance document were also set out. The guidance document should promote the SR of all organizations, provide effective guidelines as a means of self-improvement, create new added value; respect national, regional, and local context and cultures; exemplify what is necessary for raising the effectiveness of SR activities; respect the autonomy of organization, adapt flexibly to the systems in place; establish an organization that is most appropriate to its objectives, vision, and culture; be compatible, consistent and complementary with existing SR initiatives and guidelines; and place importance on communication with stakeholders as an organization promotes SR activities.

The guidance document needed to be applicable to organizations of all sizes and types no matter where they operate, and regardless of differences in culture, society, and environment. Furthermore, each organization, in the process of pursuing its essential mission, should recognize the SR it bears and perform its activities in a manner that fulfils that responsibility. For example, a wide range of organizations have a strong social impact and should be aware of SR and act to fulfil their activities. These include national and local governments, international agencies, corporations, labor unions, educational institutions, consumer associations, civil society associations, nonprofit organizations, NGOs, the media, and SRI rating organizations.

The SR Guideline (Japanese draft) was based on six SR principles:

1. Respecting autonomy and flexibility: An organization should identify those SR subjects and issues that are significant to achieving its sustainable development and continuity and address them voluntarily and flexibly.
2. Maintaining continuity: To make SR activities effective, the organization should make continuous efforts for better performance.
3. Maintaining transparency: The organization should disclose information on its structure and activities and thereby enhance transparency.
4. Respect for human dignity and diversity: The organization should respect differences in race, sex, age, ideology, culture, region, physical ability, and other categories of human diversity, and should refrain from and discourage discrimination on such grounds.

5. Special attention to communication with stakeholders: The organization should promote two-way communication with stakeholders who are affected by its activities and take their interests into consideration.
6. Contributing to building a better society: In implementing SR activities, the organization should collaborate with diverse parties to have a positive impact on solving social problems and building a better society.

Subjects and issues falling under SR were identified as:

1. Legal enforcement and compliance: An organization must ensure that it enforces or complies with relevant international regulations and legislation when carrying out its activities.
2. Human rights: The organization should address issues of human rights within the scope of its capacity to do so.
3. Employment: The organization should engage in people-oriented management and work to maintain and expand good human relationships.
4. Products and services: The organization should provide products and services of declared quality and strive to maintain and improve the quality of its products and services to ensure the confidence and satisfaction of beneficiaries.
5. Safety/information security: The organization should consider the safety and security within its control of stakeholders on whom it has direct and indirect impacts.
6. Environment: The organization should engage in environmentally conscious activities to advance the goal of achieving its own sustainable development and that of society at large.
7. International contribution: The organization should work to improve the welfare of people around the world, contributing, for example, to regional economic development in developing countries.

The Japanese draft guidelines also touch upon other areas. Communication with stakeholders was also felt to be important. In essence, organizations should raise the confidence and satisfaction of those affected by its activities during communication with stakeholders. Examples of important stakeholders are clients, consumers, beneficiaries, shareholders, investors, taxpayers, donors, employees, suppliers, partners, collaborators, communities, national governments, and local governments.

Examples of activities to understand the expectations of stakeholders are the establishment of “consultation windows” for encouraging stakeholders’ communication on SR, surveys on stakeholder expectations, and collaboration and opinion exchanges with stakeholders. Reporting to and the participation of stakeholders are vital. In reporting to stakeholders, organizations should appreciate the importance of accountability with respect to SR activities and their results and report on the organization’s structure and SR activities to internal and external stakeholders. In the participation of stakeholders, organizations should promote the engagement of stakeholders when necessary in carrying out its SR activities.

### **CSR in the USA, Europe, and Japan**

There are some differences in CSR activities among the USA, Europe, and Japan. In the USA, CSR has been historically influenced by religious values and corporate scandals.

Negative screening came from the management of church-operated funds that “refrain from investing in industries related to alcohol, tobacco, gambling, or military weapons.” This came to influence the code of conduct of pension funds and beyond. More recently, the tendency to pursue corporate ethics has grown stronger in response to corporate scandals. Another aspect of CSR in the USA is the importance of philanthropy and contribution to local communities. Traditionally, activities positively affecting society are highly regarded, and prominent businesspeople and companies are expected to contribute actively. CSR is characterized by less direct involvement of government and significant contributions by companies in addressing social issues in communities. In addition, not only the parent company, but all group companies are expected to observe their own code of conduct. Beyond the framework of the entire group, the tendency is to demand compliance with one’s own code of conduct and this has recently cascaded down the supply chain. Key developments include child labor issues revealed at a Nike subcontracting factory in Vietnam in 1996, the report of huge off-the-book liabilities and subsequent company collapse, leading to enactment of the Sarbanes-Oxley Act and the tightening of company audits and internal control systems mandated in 2002.

In Europe, CSR developed against the political background of European unification. In the process of the unification, unemployment increased in various countries but fiscal restraint was necessary as a condition for unification. This resulted in the reduced role of the governments while increasing the expectation that “corporations should contribute more to solving social issues.” The other influence on CSR has come from pressure to pursue a stakeholder-based approach in society. Each time a corporate scandal occurs, distrust in corporations rises. This has led to companies and society working together to achieve sustainable development through active assessment and actions by stakeholders such as consumers, employees, and investors. In Europe, CSR is characterized by compliance, and corporate ethics are considered normal obligations for corporations and often not recognized as CSR. In addition, CSR is often refers to situations where corporations participate in solving social issues, and companies are expected to explain their efforts. The UK and German Governments appoint ministers responsible for CSR, and in some countries laws have been enacted to promote CSR.

In Japan, the situation is different in a number of respects. A sense of company responsibility and CSR concepts existed in the past, but after the Second World War and especially in recent years, companies have had to develop relationships with a range of stakeholders through their ordinary activities, not only shareholders but also consumers and NGOs. More companies pursue CSR in policy and practice. METI has conducted research showing that 60% of top managers believe that CSR is a form of cost. At the same time, because about 50% believe that CSR is very important and a vehicle to enhance the value and the sustainability of companies, it is likely that the latter view will prevail in Japan. As more attention focuses on CSR activities, there will be increasing opportunities to share these experiences with companies in Asia. The idea of CSR is becoming more global rather than local, and the ISO’s SR standard will need to incorporate ideas from Japan and other countries in Asia. That is one reason why METI has taken such an active role in ISO working groups to ensure that the SR standard takes into account Asian values.



Table 1. The UN global compact

Human rights	1. Businesses should support and respect the protection of internationally proclaimed human rights
	2. Businesses should ensure that they are not complicit in human rights abuses
Labor standards	3. Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining
	4. All forms of forced and compulsory labor should be abolished
	5. Child labor should be abolished
	6. Discrimination in respect of employment and occupation should be abolished
Environment	7. Businesses should support a precautionary approach to environmental challenges
	8. Businesses should undertake initiatives to promote greater environmental responsibility
	9. Businesses should encourage the development and diffusion of environmentally friendly technologies
Anticorruption	10. Businesses should work against all forms of corruption, including extortion and bribery

# CSR Management and Corporate Value

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*Hiroshi Hirano*  
*President and CEO*  
*Sompo Japan Insurance Inc.*

Sompo Japan Insurance Company is one of the oldest fire and marine insurance companies in Japan that was founded in 1888. We conduct business through 544 domestic and 41 overseas offices and a workforce of 15,529 employees as of March 2004. In July 2002, the former Yasuda Fire and Marine and Nissan Fire and Marine merged to establish Sompo Japan. In December of the same year, the former Taisei Fire and Marine also joined us. In re-inventing the company in 2002, a new set of management philosophy was instituted.

- We take pride in offering excellent risk ‘solutions’ to individuals and corporations.
- We create shareholder value and grow together with our employees by offering services that always exceed customer expectations.
- We will continue to be a high-profile Japanese corporate group with progressive strategies and dynamic business activities.

As a non-life insurance company, Sompo Japan offers solutions that give a sense of security against risk. It is the firm’s employees who provide the best quality services and their growth will lead to the growth of the company; this is one of the management philosophies of Sompo Japan. Our corporate social responsibility (CSR) effort initially addressed environmental issues. Non-life insurance companies offer protection for various risks, and therefore, we pay special attention to environmental issues which could lead to major disasters. As Table 1 shows, all natural disasters that resulted in large sum of insurance payment occurred after the 1990s.

In the fiscal year 2004, Japan was hit by the largest-ever number of typhoons. A total of 10 typhoons hit Japan. The amount of insurance loss paid due to flooding and other disasters was estimated about 500 billion yen according to General Insurance Association of Japan. Now we find there is an increasing trend of natural disasters worldwide. This may or may not be due to global warming. But the point is action should not be postponed due to insufficient scientific evidence. If serious results can be foreseen, I believe we should act on the ‘precautionary principle.’ Indeed as risk management lies at the heart of our business, insurers should take the initiative in tackling the global warming with conviction and commitment.

Table1. Property and casualty insurance and environmental issues

How climate changes affect the insurance industry

World's top 10 insurance losses between 1970 and 2003

Insurance loss* (US\$ million)	No. of casualty	Date of occurrence	Cause	Countries affected
21,062	3,025	2001.9.11	Terrorist attacked on World Trade Center, Pentagon, and others	USA
20,900	43	1992.8.23	Hurricane Andres	USA and Bahamas
17,312	60	1994.1.17	Northridge earthquake, California	USA
7,598	51	1991.9.27	Typhoon Mireille	Japan
6,441	95	1990.1.25	Winter storm Daria	France, UK, and others
6,382	110	1999.12.25	Winter storm Lothar	France, Switzerland, and others
6,203	71	1989.9.15	Hurricane Hugo	Puerto Rico, USA, and others
4,839	22	1987.10.15	Storms and floods	France, UK, and others
4,476	64	1990.2.25	Winter storm Vivian	Central and Western Europe
4,445	26	1999.9.22	Typhoon Bart	Japan

⇒ All occurred in the 1990s and after

*Note:* \*Prices indexed for 2003, and the figures are losses for damage covered by insurance.

*Source:* Developed by Sompo Japan from *Swiss Re sigma*, 1st issue in 2004.

Insurance companies consume a great deal of papers such as insurance certificates, brochures, and photocopies. They also spend a large amount of energy for their information communication networks, air conditioning, lighting at offices, and motor vehicles for sales activities. For this reason, it is important first to conserve energy and resources and thereby reduce the burden being added to the global environment. As a mechanism to promote environmental management activities, in 1997, Sompo Japan took measures to acquire ISO14001 certification at its computer center. It was the first Japanese financial institution to acquire ISO14001. In 1999, the head office building also acquired certification. Since then the various regional headquarters and branch offices nationwide have developed a unique Sompo Japan version of environment management system taking into account ISO requirements. At the corporate level, the company is taking action to reduce the burden on the environment. Between 1997 and 2003, it reduced heating and lighting expenditure by 13% or 500 million yen.

What is important for an insurance company or a financial institution is to emphasize the need to develop products and services related to the environment. Sompo Japan has three guiding principles to tackle environmental issues:

1. to provide new products and services related to the environment, e.g., insurance that deal with soil contamination; trust fund called "Beech Forest" eco-fund to invest in equities of environment-friendly companies; and consulting services to companies trying to acquire ISO certification;
2. to promote resource conservation activities; and
3. to contribute to society.

CSR plays an important role in the scope of business of the financial institutions. Between December 2002 and June 2003, Sompo Japan participated in the roundtable discussions on environment and economic activities convened by the Ministry of the Environment which emphasized the 'virtuous cycle of environment and economy.' This concept formed the foundation of the environmental administration in Japan. In the past, the environment and economy were seen as being conflicting ideas. According to this new paradigm, however, these two concepts are integrated in which the improvement of the environment stimulates economy and the revitalization of the economy improves the environment. By creating this kind of virtuous cycle, society can be improved. Sompo Japan made three proposals during these discussions:

1. Utilization of insurance to manage environmental risks;
2. Raising awareness of the financial sector on environmental issues; and
3. Promotion of socially responsible investment (SRI).

The expected role of financial institutions is very significant to create virtuous cycle of environment and economic activities. SRI, now popular in Europe and the USA, is a method of investment which takes into consideration not only the financial factors but also the contribution to the environment and the society. Based on an evaluation of these elements, decisions whether to invest or not would be taken. Evaluation of social, financial, and environmental performance for investment decisions means evaluation of the companies is made from the CSR perspective. SRI can be described as promotion of CSR from the viewpoint of the financial markets.

Why does SRI exist and why is its underlying idea supported? These needs to be seen in the context of the triple bottom-line concept. For many years, there was only one yardstick for measuring corporate value—financial performance. Recently, a new paradigm has emerged—global warming or sustainable development. This also extends to cover human rights issues such as child labor and compliance and transparent information disclosure. These areas have also been attracting much attention among ordinary citizens. Thus against this backdrop of a global trend, it is now necessary to consider the social performance and the environmental performance as an equally important yardstick. As one of the integral members of society, companies have to respond to these three aspects of corporate evaluation. SRI pays attention not only to financial performance but also to social and environmental performance, so SRI represents the manifestation in investment of triple bottom line concept.

Sompo Japan, as one of the members of financial institutions in the market, launched eco-fund called "Beech Forest" in 1999, which was considered SRI in a broad sense. "Beech Forest" eco-fund considers that the environment-friendly company has great potential in the medium and long term and also there is a greater possibility of the contribution to the value of the company. Based upon this, Sompo Japan invested in such companies as part of the mutual fund products. As of 18 February 2005, this eco-fund has outperformed the TOPIX by 9.48 %. This is an example of how we are contributing to the creation of virtuous cycle of environment and economy by increasing the evaluation of the stock market.

In December 2004, Sompo Japan also developed and launched another new SRI fund for investing into the companies to promote CSR. In response to the diversified needs of investors, we have to have a variety of SRI funds. Incidentally we are also an institutional investor of the capital market. As of February 2005, as an institutional

investor, Sampo Japan joined the Carbon Disclosure Project. This project started three years ago in the UK. Institutional investors involved in this initiative sent a questionnaire to the top 500 global companies in the world on global warming and requested information disclosure aimed at further promotion of countermeasures against global warming. Year by year, the number of the institutional investors subscribing to this idea increased. As of 2005, 143 companies including Sampo Japan are jointly sending the questionnaire to the top 500 companies and the response rate has been improving year by year. Therefore, the Carbon Disclosure Project has been increasing its impact steadily among companies. Thus through exercising the impact as an institutional investor, we are promoting and encouraging companies to increase their information disclosure. In this sense, this project, taking advantage of the function of financial institutions has been making its contribution towards the creation of the virtuous cycle of the environment and economy.

Sampo Japan has been participating in global CSR initiatives. It is the only financial institution in Japan which is a member of World Business Council for Sustainable Development (WBCSD) and actively participates in its activities and projects. As a member, in September 2002, we participated in the WBCSD statement on the financial sector in Johannesburg UN summit meeting. Also we are the only financial institution in Japan that is a member of UNEP financial initiatives together with other global institutional investors. We have been actively participating in research and making proposals on solutions to environmental issues. Actively participating in global activities and exerting leadership for sustainable development of the global economy is one of the key factors that are now expected of financial institutions.

CSR activities cover a wide spectrum and each company has to make its own distinctive contribution. Our approach is to pay attention to people who support CSR. Sampo Japan emphasizes communication with a wide spectrum of stakeholders. If employees provide service with rewarding feelings and job satisfaction and the service surpass the expectation of customers, we call that 'impressed quality services.' We would like to establish a virtuous cycle of feedback of the voice of customers who are satisfied by recognizing employees who provided this level of service. That will drive further employee motivation. This kind of virtuous cycle cannot be created overnight and requires steady and long-term effort. Participation by all, continuing and steady effort and also autonomy independency are part of the consistent motto of our company.

One of the major characteristics of Sampo Japan's CSR is a human-oriented, people-centered approach. We focus on both outside and internal stakeholders in implementing CSR. Even though the company is required to be socially responsible, it is actually all the executives and employees that carry out corporate activities. Unless people can act and think on their own, the company will not be able to fulfil its responsibility. Another reason comes from the fact that our main line of business is insurance. In the case of a manufacturing company, customers will buy its products and judge the value of the product. The product itself will speak for itself. In the case of an insurance company, core business is something which is not visible. We are offering a sense of comfort and service, which is not visible. It is our employees who actually create the value of our service. The core of our corporate management is people. When employees grow, this provides vitality to the company and brings about corporate growth. CSR is not something independent but corporate management itself. In this context, the core of CSR should also be human development.

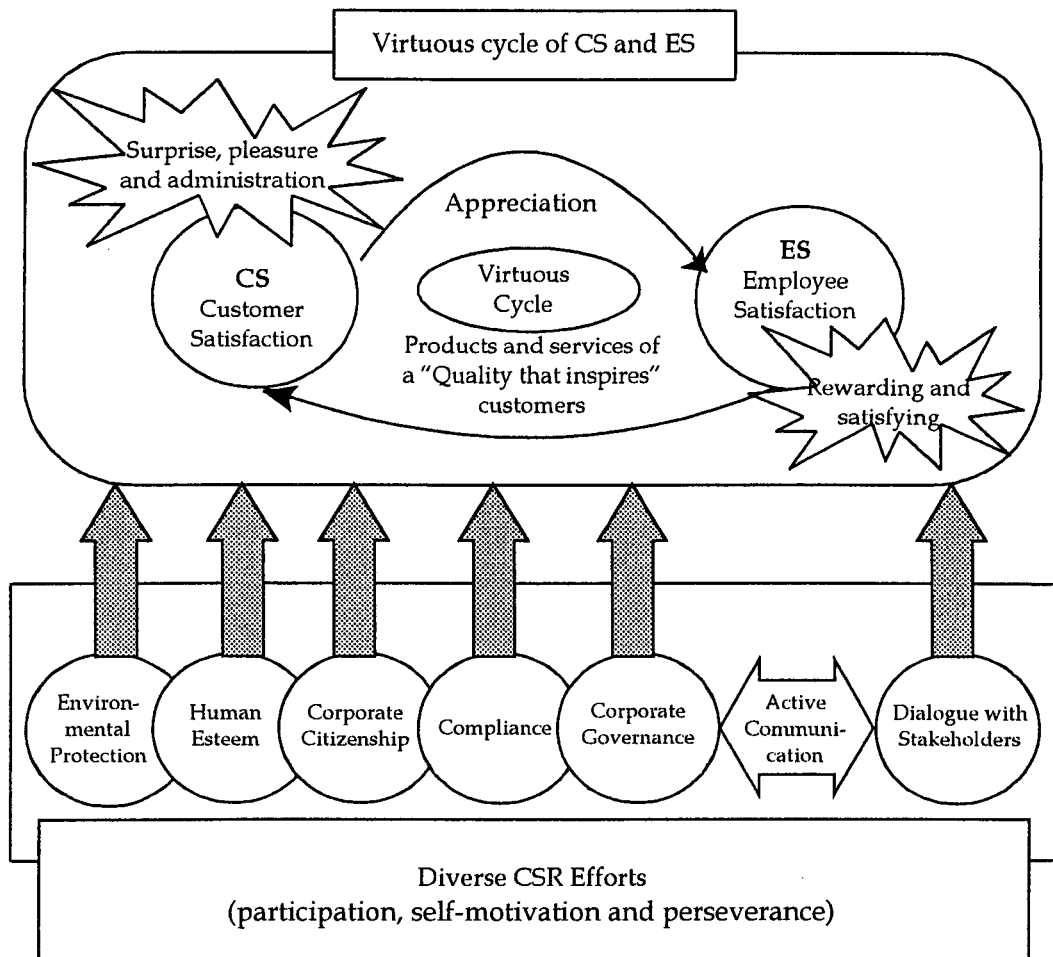


Figure 1. CSR initiatives at Sompo Japan

Our people-centered CSR approach has been carried out under the initiative of our human esteem promotion headquarters. This serves as the core, and in the background was the merger that took place in 2002, when employees of three companies with different corporate cultures, each having their own long and continuing history and style, came together and the new company, Sompo Japan was created. In order for these employees to work effectively together and to realize management plans, we recognized that it was best to unite them under a new set of common values. For this reason, we focused on people to enhance employee motivation. We set out human esteem as the common value to boost our employees' morale, and the human esteem promotion headquarters was established for this purpose. This focuses on four main areas:

1. Human rights awareness promotion;
2. Health and well-being promotion;
3. Working hours management; and
4. Gender equity promotion.

These are indispensable to extract the capability of our employees which is the source of our competitiveness.

Corporate responsibility – undertaken by our employees

Insurance company – our products and services are intangible but provide our customers a sense of security

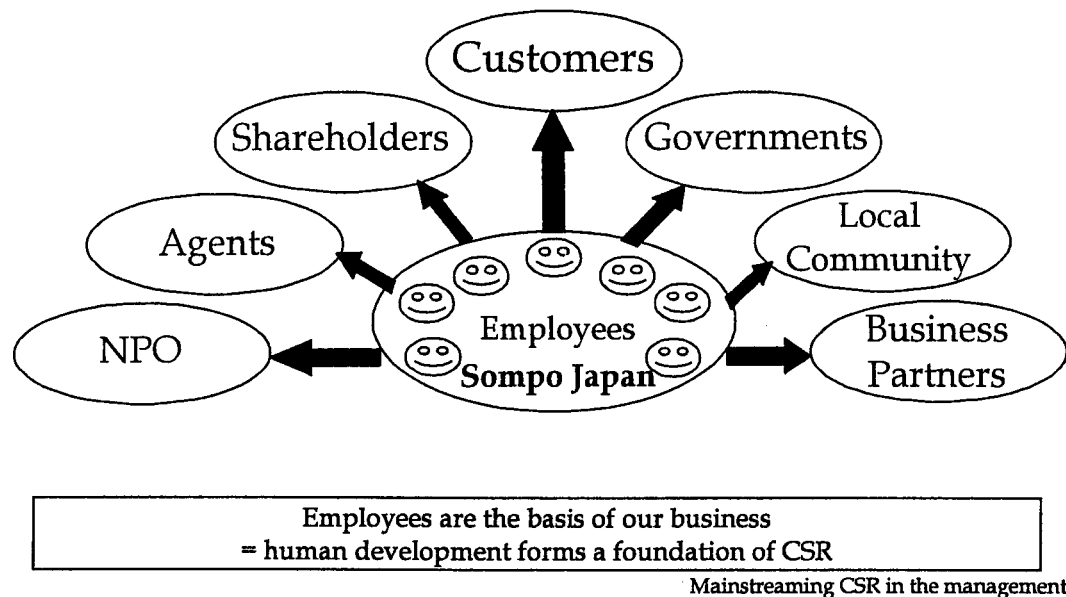


Figure 2. People-centered approach supporting CSR initiatives

Gender equality promotion deserves a particular mention. Unfortunately, like many other Japanese companies, Sampo Japan was not doing a good job in terms of gender equity. Thus in 2002, we decided to set up a Women's Committee to capture female employee voices into our planning. In phase one, we started out with 16 female employees in Tokyo Metropolitan area. At the Women's Committee, the female employees themselves came up with proposals on the personnel system and the committee is very active today carrying out various activities. We also set up a dedicated group to focus on gender equity and this gender equity promotion group was set up within the personnel department in 2003. This group listens to the opinions of the Women's Committee and implement various activities for promoting the status of women, e.g., encourage managers to read through the manual which gives information on legal requirements and case studies related to gender equity. This is a major challenge that our management needs to continue to address.

The second characteristic of our CSR is that we are carrying out wide range of communications with our various stakeholders and this applies to communication with people outside of our company. Our CSR report which plays an important role in carrying out this communication and an abridged version in Japanese is distributed to all our over-15,000 employees because they are important stakeholders. We want as many people as possible to read our CSR report and give us feedback on our activities. We believe that this is a very important tool for communication.

The target audiences for our CSR activities are our customers, investors, and employees, but they are not the only ones. Many citizens and non-profit organizations in which the citizens are very active are also important. We call non-profit organizations, NPOs or civil society organizations, CSOs. In order to establish a sustainable society, we should not just focus on our companies but we also need to ensure citizens are involved.

We have established the Sampo Japan Environment Foundation. From 2000, we have introduced the CSO learning scholarship program in which university students can take part in environmental CSO activities as interns. Young students can accumulate their precious experience working at these organizations. At the same time, this is a form of assistance to the CSOs in terms of human resources, which often face serious shortage of manpower. Through this experience at the CSO, we come to understand the roles which CSOs play in environmental issues. Also they can deepen the understanding and awareness towards various global environmental issues. Environmental NPOs and Sampo Japan are working together so as to educate future generations.

As an example of communication with the communities, the Sampo Japan Earth Club was set up in 1993 where our employees work as volunteers. All our employees are members of this club and they are voluntarily taking part in various activities in the community. The following is just an example. In Shizuoka near Mt. Fuji, an employee who had experienced the great Kobe Hanshin Earthquake came out with an idea to put on a puppet show called '*Inamura-no-hi*', that means 'setting a fire on a pile of paddy.' This is the story that appears in the textbooks of primary school children which teaches the importance of disaster prevention. The Shizuoka prefectural government and Shizuoka NPOs entered into a partnership to stage this puppet show. To explain the story, there was a squire who sensed that a tsunami wave was about to attack the area and decided to set fire on a pile of paddy that villager had just harvested, because the villagers were preparing for a festival at the low end of the village. In this way he succeeded in gathering them to come up to the hill top and saving their lives.

This illustrates the importance and value of people's lives, the importance of mutual help and provides a lesson that in the event of a tsunami you have to escape to a location which is high in altitude. This is a classic story, and in January last year, it was first shown in Shizuoka. After carrying out this show in a series of different locations, the puppet show was shown in Kobe at this year's World Conference on Disaster Reduction of the United Nations. Sampo Japan has been supporting this event. Many primary school children were impressed by this show and likewise the school teachers. The great earthquake of the coast of Sumatra and also the massive tsunami wave of the Indian Ocean have prompted some people to think about the possibility of translating this puppet show into English. We want to continue to support people's efforts to realize this. Our communication should not be limited to the local community, but should be spread worldwide on a global basis.

The third characteristic of our CSR activity is full participation. Even if I as the president, were to give instructions to this person-in-charge of CSR at the head office, we cannot realize CSR in the true sense. True CSR is one in which all employees of the company recognize CSR as something that they need to do. It is important that everyone participates and promotes CSR powerfully. In September 2004, I asked all 38 board members to come up with ideas and proposals for promoting CSR. This is because it is important that board members think independently and communicate their message to their subordinates in their own words. I wanted people in different sections to promote CSR on their own, and the executives/board members to give the instructions to their



subordinates, on their own. I asked them to submit a report. All the board members came out with ideas and proposals and, based on this, we had all employees of our affiliated companies talk about the CSR challenges that they face in their workplace. This is what we call the CSR literacy training. Once all the employees can talk about Sampo Japan CSR in their own words to stakeholders and they think and act on their own, it can be said that CSR has truly taken root.

Up until now CSR has been seen as a cost to the company. However, efforts to improve CSR should be seen not as a cost but an investment for the next round of business activities. Then why can business activities that take into account the triple bottom line contribute to raising corporate value? One of our business philosophies is that we are trying to provide services which exceed the expectation of customers and that the company grows together with employees. Not only by meeting customer expectations but also by impressing them through achieving better performance than expectation, Sampo Japan would like to grow together with the employees who work with vigor and pride. The service quality which evokes a positive emotional feeling of customers can only be provided by employees who are equipped with high confidence in their company, high morality, and vigorous attitude toward work. Evaluation and support from various stakeholders including customers for quality of products and services can promote the growth as well as the delight of employees. That is how customers' and employees' satisfaction can reinforce each other and we can create a virtuous cycle between them. This takes time but once the virtuous cycle is generated and starts growing, you can increase the vitality of the company, increase its competitive edge, continue its high performance and ultimately contribute to the improvement of corporate value.

The external evaluation given to our CSR activities is very positive. High evaluation of the CSR initiative of Sampo Japan means that we have trust of a wide spectrum of the stakeholders and we can expect their support and further assistance. It can also improve the corporate reputation and also it is very helpful for acquiring talented people to work for the company. Another reason that CSR is helpful for improving the corporate value is the global expansion of SRI. The SRI index Dow Jones Sustainability Indexes (DJSI) has total assets of about 3 billion euro. Sampo Japan is one of 314 selected companies from the perspective of economic, environmental and social performance. It is the only Japanese insurance company listed in the 314 indexed companies and has been a part of the index for five consecutive years. Being listed in this kind of SRI index means a higher possibility of increasing the company's equity valuation. Thus CSR initiatives can have a direct and positive impact for improving corporate value.

*Wall Street Journal* carried on 17 June 2004, the article selecting Sony and Sampo Japan as examples which are successfully increasing equity values by positively grappling with the CSR. This is very encouraging because they are in 100% agreement with my conviction of the CSR and corporate values. If you look at the equity price movement from April 2000 to October 2004, the price has increased by 130%, while Nikkei 225 Index has declined by 44%. This is simply because the market appreciated the company's performance.

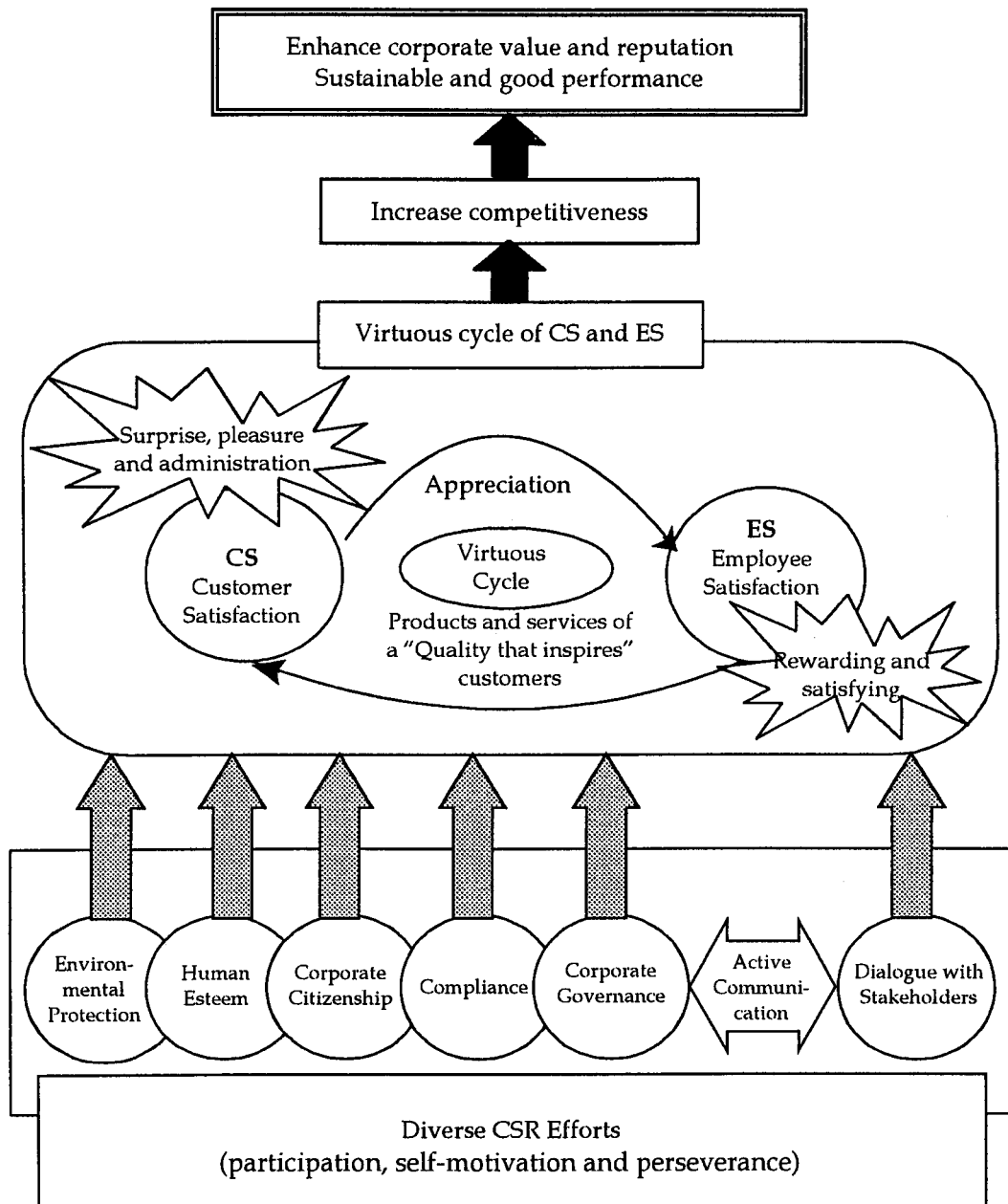


Figure 3. Our vision of CSR

In concluding my presentation, I would like to touch upon two points. Firstly, I introduced to you that social, financial, and environmental aspects; triple bottom lines are new yardstick for the corporate evaluation. Reflecting the change of the voice of the society and the market, the SRI fund was expanded. The companies have to be aware of the changes of the society and take advantage of them. We have to listen to the changing voices of the market. Of course, financial aspect remains to be very important because this reflects the business performance. However, the social and environmental sides are

almost equally important. CSR activity is the initiative for improving this triple bottom line index and the company who are trying to boost up the triple bottom line can continuously improve and increase the corporate values and be therefore competitive.

Secondly, I also touched upon the features and contents of the CSR activities of Sampo Japan in three points. Energetic, aggressive, and organizational CSR activities definitely lead to the significant and tangible results. Based upon the motto of "participation by all, steady and step-by-step continuation, and independence autonomy," there should be the organization-wide continuous work and efforts. It takes long time until the CSR activities bear fruits and generate results, in terms of the increase of the competitive edge and corporate values. That is exactly why you have to start up the CSR as quickly as possible.

Lastly but not the least, I would like to refer to the future possibility of the development of the CSR from the personal viewpoint of a Japanese manager. Globalization is taking place in every corporate activities, and procurement, manufacturing, sales, and investment have been conducted on a global basis. Now, the initiatives and efforts for the CSR are considered as one of the criteria for the procurement and investment decision making, and, therefore, they have a direct impact on the international competitive edge of the companies. This trend will build up through the standardization efforts by ISO and the evaluation of the companies by the SRI-related organizations. On the other hand, it takes time to expect the tangible results and effect to be generated from the CSR activities. Therefore, we have to positively introduce and tussle with the CSR and link this activity to the innovation of the management. This is an excellent chance for generating the new area of the competitive edge in the global market.

Recently, a lot of attentions have been paid to the CSR. However, social responsibility is not limited to companies. This is not the responsibility that only companies can take. The government agencies, consumers, NPOs, and communities can also be the stakeholders of the social responsibility. Those constituting society and economic system have to heighten the awareness of social responsibility. And through the mutual dialogues, we have to collaborate with each other for successfully playing the role of social responsibility. In other words, for creating a sustainable society, we cannot impose CSR just on company activities, but you have to involve consumers, NPOs, regional societies, or the government agencies, and many other stakeholders, and consider CSR as integral part of social and economic system. I think that we have to see more and more collaborations as well as continuous efforts by way of promoting dialogue between/among the different sectors. But it takes time and you have to be prepared for that. It is our responsibilities to listen to the voice of society and market for sustainable development. I am deeply committed to this obligation.

# My Management Philosophy and Corporate Social Responsibility

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*Morio Ikeda*  
*President*  
*Shiseido Co., Ltd.*

Today, when I look at not only Japan but elsewhere in the world, I cannot help but feel that public confidence in companies is being substantially undermined. This is not a problem only of companies but of the society as a whole. The sense of trust is disappearing from individuals, companies and social organizations as well as from all kinds of relationships. And behind the disappearing sense of trust lies the problem we face today.

I believe that gaining the trust and confidence of society is the very basis of corporate management and the sense of trust is the key to fostering and maintaining a corporate brand. From another point of view, this means that our efforts to enhance our ties and relationship with all the members of society lead to the mutual trust between different organizations. Our company, Shiseido, is a manufacturer. We are hoping to be of use to our customers through the sale of cosmetics, thereby contributing to society at large. Shiseido's history of some 130 years, however, has not always been smooth sailing. There are many things that are outdated but left unchanged to this date. We have been unable to fix them in accordance with the changing environment due probably to our arrogance and conceit about our past success. I would like to proceed with the rest of my speech, referring to such history of our company from time to time.

It was June 2001 that I took over the management of the company. In the later half of the 1990s, we had a big problem. Not only Shiseido but the whole cosmetic industry was facing the big challenge of structural change of retail business. In the cosmetic industry, over-the-counter sale, in which a salesperson would explain and recommend specific items to a specific customer, has been normal business practice. In the later half of the 1990s, however, some people began to say that such business practice might be in violation of the Antimonopoly Law, and the whole cosmetic industry spent so much time to cope with this problem. As it turned out, the court fully upheld our argument that such a face-to-face sale is a valid selling method based on the unique characteristics of cosmetics. Hence, the stage was set for the whole cosmetic industry to take a step forward into a new age. Thus, Shiseido decided to end preparatory work and begin to finalize management reform plans with an eye on the full scale implementation of the reform.

So, the concrete reform plans have been set. But we could not find any spiritual foundation to support the implementation of these reform plans. This problem was not unique to our company but common to the whole Japanese society. I felt that something like a spiritual backbone that serves as a linchpin was missing. In the 20<sup>th</sup> century, we placed ourselves in a goods-oriented society. It was a society in which the system of mass production, mass consumption, and mass disposal was tolerated and I was greatly troubled with the idea that corporate activities are based on such a system.

Feeling troubled and without the sense of fulfillment, I walked into the first day of the new millennium (21<sup>st</sup> century). And one day, while I was reading the *Sankei Shimbun*,

I came across an article that caught my attention. The article was about Mr. Inazo Nitobe who is known as an author of *"Bushido: The Soul of Japan."* The article quoted his words preaching the dignity of justice, courage, benevolence, courtesy, sincerity, honor, and loyalty. These seven virtues are related to the *Bushido* (way of the warrior) spirit, which is based on the Confucian spirit.

*Bushido*—or I should rather call it the Confucianism—is based on the virtues of benevolence, loyalty, honor, and trust. Also, this is the spiritual foundation of the Japanese people. You may think that *Bushido* is a thought about swords and battle. But it is, in fact, about the spirit or soul of the Japanese people that has been nurtured through our long history. So, this is about Japan but it applies to all the people in Asia. The virtues of sincerity, kindness and gratitude are spoken of throughout the whole teaching of *Bushido*, which is the very spirit we need to call back to our society today in order to build a new Japan in the 21<sup>st</sup> century. Such was the message of this article. Without wasting time, I took up the book and reread it. Then, I found another phrase that caught my mind. It was about tree grafting, i.e., joining a young tree branch to a rootstock. Several months after that, I became president and I thought, inspired by the term "tree grafting" mentioned by Mr. Nitobe, that Shiseido needs to return to the founding spirit of the company and build new thoughts and activities for the 21<sup>st</sup> century based on the foundation of the founding spirit as if joining a young branch to a rootstock. I was assured that this is the way we should go in the 21<sup>st</sup> century.

As such, the founding spirit is what constitutes the foundation of management reform. If we are to carry out reform, we must first go back to the founding spirit. Shiseido was founded in 1872 with a western style prescription pharmacy opened in the Ginza district of Tokyo. The founding spirit was to be of use to our customers by helping them enhance their beauty and health, thereby contributing to society at large. The term "*shisei*" in the company name has been taken from the ancient Chinese text "*I Ching*" or "the Book of Changes." What is meant by these Chinese characters is that new values need to be generated from natural resources in order to contribute to society and people. Therefore, our mission is to quest for beauty and health so as to be of use to our customers. Then, specifically what should we do to achieve that end? The answer is to utilize all the resources we have to create new values.

In 1900, the founding president of Shiseido visited World Expo in Paris. So shocked and amazed at what he saw there, he launched cosmetic business after returning to Japan. Then, he set out corporate ideals: "let's products speak for themselves," "everything must be rich," and "brands must be viable internationally." These ideals have been passed on and still remain the underlying principles governing our manufacturing operations.

In 1921, the corporate philosophy consisting of the following Five Management Principles was laid down:

1. Quality first: Shiseido makes a big commitment to quality;
2. Coexistence and co-prosperity: Shiseido seeks to share its benefits with all persons associated with Shiseido;
3. Respect for consumers: Shiseido is committed to be of use to customers;
4. Management stability: Shiseido practices sound management at all times based on firm foundation and eyeing on long-term goals.
5. Sincerity: Shiseido at all times operates its business loyally, honestly, respectfully and sincerely.

Among these, the second principle of coexistence and co-prosperity is playing the pivotal role. For 84 years since 1921, Shiseido has always been looking at the customers, aiming to become a truly consumer-oriented and consumer-conscious company.

Two years after that, Shiseido introduced the “Chain Store Network,” the first-ever voluntary chain system in Japan. The system was launched because we wanted to better serve our customers together with retail storeowners sharing the same spirit. The second president of our company visited all the stores selling our products and explained this spirit to storeowners. Then, we concluded a chain store contract for the sale of our products only with those who truly understood this spirit. Thus, the Chain Store Network system was established based on the idea that consumers, retailers and producer of products should be sharing this spirit of coexistence and co-prosperity. This is our philosophy of sales activities.

Another pillar supporting our company is the spirit of contributing to society at large, which may be described as constituting part of the present day idea of corporate social responsibility (CSR). We have been supporting art and cultural activities. This may be defined as part of corporate “mecenat” activities of today but it was back in 1919, as early as 86 years ago, that we opened the Shiseido Gallery on the top floor of our headquarters building in Ginza for the purpose of supporting art and cultural activities. And we began to provide a place for little-known, poorly-financed but talented artists to present their works.

As a corporate entity, we must generate profits. At the same time, however, the founder of our company always believed in the need to pursue achievements in cultural and social aspects. Thus, we have always been striving to gain full trust and confidence of society, and to gain such trust and confidence through our day-to-day activities. Because corporate philosophies and activities differ from one company to another, I believe that it is necessary for each company to make efforts, based on its own ideas, to quest for various values so as to contribute to the creation of a truly affluent society. From the standpoint of this idea, in 1997, we adopted “The Shiseido Way,” a declaration of principles of corporate behavior established on the basis of the Five Management Principles. This is Shiseido’s declaration of its commitment to serve and contribute to our customers and society at large so as to enhance our CSR activities.

So, such are the principles and philosophies of our company. But it is hard to say that we have been able to live up to such principles and philosophies in the last half of the 20<sup>th</sup> century. Shiseido was no exception in having been misled into the general idea of tolerating mass production, mass consumption, and mass disposal. By nature, cosmetics are a kind of products that must be produced with warm and thoughtful care. They should not be mere goods or physical objects. But in reality, even though we were putting up lofty principles and philosophies, we have been unable to steadily put them into practice. We have been treating our products as mere goods and we have been unable to share the spirit of being of use to and serving our customers with our important business clients. That is how this organization called Shiseido has fallen to become a mere mechanism for selling products.

It was necessary to go back to the basics and reform ourselves so as to prepare for the new age. Thus, under the catchword “storefront-oriented,” we began to reform our activities starting from those at storefront. We set benchmark standards for all of our activities at storefronts, where our customers, business clients and Shiseido meet face to face with each other. Then, we reexamined all the institutional and organizational aspect leading to storefronts, namely, the forefront of retail sales activities, thereby proceeding

to reform our marketing procedures, supply chain management and organizational climate.

Such activities are not limited to Japan. We have expanded our business overseas where we have been operating our sales activities under the same spirit as in Japan. In China, we have been providing a wide variety of products to our Chinese customers for 20 years. About 10 years ago, we launched the department store sale of the “Aupres,” an exclusive brand for China that has been developed in consideration of the living style of Chinese consumers as well as of the climate of China. Then, after taking enough time to make the presence of our company known to Chinese customers, we decided to introduce in China the voluntary chain system (Chain Store Network) that we launched in Japan 82 years ago, hoping to serve more customers there. We began to implement the system in China in 2003. The number of chain stores reached 300 in 2004 and we are aiming to increase the number to 1,000 by the end of 2005. In this process, we hope to enter into a chain store contract only with those who truly understand the founding spirit of our company, just like we have done in Japan, so that we can work together to serve our local customers. So far, we have been operating our chain stores in Shanghai, Fujian, Sichuan, Zhejiang, Liaoning, and Beijing. These cities and provinces are the core regions for our Chinese operations and we intend to further expand our sales network in China.

In 2004, I visited Hangzhou and met with local government officials. And I was told that cosmetic stores are playing a significant role in vitalizing local shopping districts and communities. So, stores are playing a social role. And through such social activities, we are hoping to gain trust of our customers and people in the local communities. Also, on the basis of these activities, we would like to further expand our business.

We are not looking at China from a short-term viewpoint. Whatever country we may be in, maintaining our own management philosophy and marketing strategy is the key to gain support from local customers. Corporate activities must be focused not only on economic aspects but also on social aspects, that is, not only on quantity but also on quality. I believe that this idea of prioritizing quality matches the spirit of CSR.

CSR also relates to personal quality. If we compare corporate activities to a person, sales and profits would be, so to speak, the appearance and look of the person whereas CSR would be the heart and personal quality of the individual. In order to make a company perpetually prosper and develop, it is important not only to try to build up physical strength but also to self-training in the mental and spiritual aspects, just as is the case for us human beings. Through such efforts, we will be able to win people’s trust.

In Japan, the idea of comparing a company to personal quality like this was established more than 300 years ago in the Edo period as the “spirit of commerce.” This is the idea that delivering pleasure to customers will bring part of the pleasure back to the merchant. It is represented by the Japanese term “*sanpo yoshi* (good for three sides),” meaning that sellers, buyers and society are happy. This principle of *sanpo yoshi* is the very spirit of CSR that we should be pursuing today.

The spirit of mutual trust and consideration to others are nothing but the Asian mind. The attitude of always respecting others is commonly observed all across the Asian continent. It is also a common characteristic of us, Asian people, to never forget the sense of gratitude. When we look at the Japanese society today, however, we cannot help but notice that people are becoming neglectful of these Asian virtues. It is becoming more and more important to make all the relationships in our life—relationships among family members and between parents and children, those among coworkers at workplace and among different companies, and nation-to-nation relationships—warmer and heartier.

As such, CSR is no new concept. It has been practiced in each country or region based on its inherent ideas fostered through its history and culture. Today, however, in the era of market economy and globalization, we are being required to conduct our behavior, not only based on our own ideas, but also in compliance with certain international principles and standards. With respect to human rights, the environment, legal and ethical issues, and the labor standards, we need to have common philosophies. The concept of the “Global Compact” advocated by the United Nations exactly embodies this idea and it is the minimum standards that all the companies must comply with. At the same time, corporate activities also need to be conducted in the spirit of harmony and coexistence, for which we must take a local viewpoint and respect diverse culture and characteristics. I believe that only when we successfully carry out these activities, we will be able to generate new and original values that provide the source of growth of our company.

Since 2002, I have been engaged in efforts at Nippon Keidanren (Japan Business Federation) to amend the Charter of Corporate Behavior. Nippon Keidanren has been working on the issue of corporate social responsibility since the 1970s. In 1991, following the revelation of a series of corporate scandals, the federation enacted the Charter of Corporate Behavior. Then, in 2002, the charter was reviewed from compliance viewpoint. The principles set forth under the charter are meant to be the minimum standards that member companies must observe. Later on, we began to discuss CSR, whereby we have come to see corporate activities from a broader viewpoint. In 2004, we decided to review the charter from the viewpoint of CSR. Thus, we can call it “CSR Guidelines.” The idea consistently pursued by Nippon Keidanren in the review was that CSR activities are not something that should be standardized under the leadership of the government or any business organization, that is, such activities should be promoted under the initiative of the private sector with decisions on specific undertaking left to individual corporations. That was a major premise for the delivery of the revised charter.

**<Charter of Corporate Behavior>  
— Nippon Keidanren —**

(established in September 1991 and amended in May 2004)

Member corporations of Nippon Keidanren (hereafter referred to as “Members”) believe that corporations exist not only as economic entities designed to pursue profits through fair competition, but also as social entities which must make a contribution to society at large. Members are expected to respect human rights and to conduct themselves in a socially responsible manner toward the creation of a sustainable society, observe both the spirit as well as the letter of all laws and regulations applying to their activities both in Japan and abroad in accordance with the following ten principles.

1. Members, by the development and provision of socially beneficial goods and services in a safe and responsible manner, shall strive to earn the confidence of their consumers and customers, while taking necessary measures to protect personal data and customer related information.
2. Members shall promote fair, transparent, free competition and sound trade. They shall also ensure that their relationships and contacts with government agencies and political bodies are of a sound and proper nature.



3. Members shall engage in communication not only with shareholders but also with members of society at large, including active and fair disclosure of corporate information.
4. Members shall strive to respect diversity, individuality and differences of their employees, to promote safe and comfortable workplaces, and to ensure the mental and physical well-being of their employees.
5. Members shall recognize that a positive involvement in environmental issues is a priority for all humanity and is an essential part of their activities and their very existence as a corporation, and shall therefore approach these issues more pro-actively.
6. As “good corporate citizens,” members shall actively engage in philanthropic activities, and other activities of social benefit.
7. Members shall reject all contacts with organizations involved in activities in violation of the law or accepted standards of responsible social behavior.
8. Members shall observe laws and regulations applying to their overseas activities and respect the culture and customs of other nations and strive to manage their overseas activities in such a way as to promote and contribute to the development of local communities.
9. Management of members shall assume the responsibility for implementing this charter and for taking all necessary action in order to raise awareness in their corporation and inform their group companies and business partners of their responsibility. Management shall also heed the voice of their stakeholders, both internally and externally, and promote the development and implementation of systems that will contribute to the achievement of business ethics.
10. In the case of incidents contrary to the principles of this charter, management of members must investigate the cause for the incident, develop reforms to prevent recurrence, and make information publicly available regarding their intended actions for reform. After the prompt public disclosure of information regarding the incident, responsibility for the event and its effects should be clarified and disciplinary action should be taken, including the highest levels of management where necessary.

CSR has two aspects, namely, defense and offense. From the global viewpoint, we need to take a “defensive” approach primarily in the domain of compliance. That is, we are required to follow rules and comply with laws. At the same time, in operating in a certain country or region, we need to take an “offensive” approach, respecting local values and demonstrating the originality to the fullest extent. Such activities must be carried out as a spontaneous action and in such a manner to make it visible to the local community who is undertaking the activities. Thus, excessive uniformity must be avoided. The International Organization for Standardization (ISO) started working on the development of guidance documents on CSR in 2004. However, the development of such an international guidance may lead to the standardization of CSR activities. So, Nippon Keidanren has been actively participating in the work at the ISO and expressing its opinions so that the ISO guidance would allow individual corporations to undertake diverse CSR activities under their spontaneous initiative.

The time is changing drastically. In Japan, we must shift from a society based on mass production and mass consumption to a new society that respect diversity and individual characteristics. For that, it would be necessary to first destroy the conventional

model of society that has supported the steady economic growth in the postwar Japan so that we can create and shift to a model suitable for the new society. I suppose the same idea applies to many other countries in Asia.

I feel now is the time that we must reflect on what has happened in the last half of the 20th century and start working to create a society where we can pursue the true purpose of life, setting targets on the quality of individual life and the richness of mind, rather than on the economy of scale. In order to create such a society in each country or region, we would like to pursue CSR management based on mutual trust with all of you.

## **Building a “New Snow Brand Milk Products Co. Ltd.” Goal: to Establish Compliance Management**

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***Makoto Wakita***  
*Managing Director*  
*Snow Brand Milk Products Co., Ltd.*

A number of books and reports have been written about the food poisoning accident caused by one of the products from the Snow Brand Milk Products Company. In the past four years and a half following the accident, we have done many efforts to improve the management of the company.

The incident took place in Osaka, on 27 June 2000, when initial cases of nausea and diarrhea started coming in. In just one week, more than 10,000 people reported similar symptoms. In the end, the number of recognized patients came to 13,420. This was an unprecedented large number of food poisoning. In actuality the number was even larger. The company received more than 30,000 claims. The 6,000 Snow Brand staff working in Osaka could not cope with the problem. An additional 10,000 staff from Tokyo were dispatched to help to address the problem.

Many reports referred to unclean management of the factories as the main cause of the poisoning. However, it was the low-fat milk which was the real culprit. More specifically, the ingredient for the low-fat milk, namely, the powdered skim milk, was contaminated. This led to the very large number of food poisoning cases.

The accident was aggravated further by several reasons. In the first place, there was a delay in properly detecting the accident. From 27 June when the first case was reported until 28 June, seven reports of poisoning cases were filed. But, each case was dealt with separately and in isolation of the other. In other words, each of the office receiving the report and the persons responsible were attempting to address the problem at hand without knowing that similar cases were simultaneously occurring elsewhere. This had led to a delay in the crisis detection.

Moreover, on 28 June, the company had a shareholders' meeting in Sapporo city, Hokkaido. The head office of the Snow Brand Milk Products was registered in Hokkaido. Following the code of commerce, we had to send all our board members to Sapporo city, in northern Japan, for the purpose of the shareholders' meeting. What happened in the West, in Osaka, was on 27 June. There was this distance between Osaka and Sapporo. This has led to confusion on the information about the crisis.

The second reason for the increase in the number was the delay in identifying the cause. That year the company was celebrating its 80th anniversary. Among the dairy product manufacturers, we were the top manufacturer back then. We had a powerful brand. Our company was thought to be of high quality. This was part of our appeal to society. But then the reality came to light as a result of this incident.

The powdered skim milk which is an ingredient of the low-fat milk is produced in Taiki factory, Hokkaido. The powder was delivered to Osaka to produce the low-fat milk, the final product. The records of the various problems that occurred at the factory and also the daily record keeping of the production process were insufficient. There were some records missing, or it could have been that there had been some alteration of the

records. It was not just limited to the Taiki factory in Hokkaido. We inspected all of our factories and we found that in almost all the factories, the appropriate document management was not being carried out. So we came to understand this problem through this incident.

The third cause of the problem was the inconsistent information disclosure. Our profits were more or less high but this was not reflected in our stock prices. We were an excellent company but we took it for granted and underestimated the media. Therefore, there were many unprepared statements. We also confused facts with what actually was our own speculation when answering the questions. There were many careless statements made, which triggered criticism against Snow Brand Milk. Overall, the situation seriously undermined the reputation of the company.

In terms of risk management we were very inadequate. Snow Brand Milk Products had become a company faced with multiple major problems. Over our 80-year history we started out with butter and dairy products. We started a cheese business in which we have a 70-year history. We sell ice cream, milk, yogurt, juice, powdered milk for babies, and infant milk. We export our products to Asian countries and also we sell frozen food. We next started to run restaurants and sell beef. We also started our flour business. As the business expanded, Snow Brand Milk Group lost its identity. Because we started so many new businesses, we did not have a “scrap and build” system within our company. That has changed now.

What we did not have back then was a system to assess new businesses. The new businesses we started were not of the nature where they would immediately succeed. In most cases, those new businesses caused deficits. The market environment was deteriorating at that time and about half our sales were coming from milk. Yet, in terms of operating profit, we were posting a deficit in our milk business. What generated our profits? There were only two categories: dairy products and baby milk. This led to the sales of some 580 billion yen, and our profit on a current basis, was somewhere around 10 billion yen. Our profitable businesses had to compensate for the deficit-ridden businesses.

As a result, in order to continue to generate profit the dairy and infant milk products had to come out with good products. However, there was an excessive cost reduction and excessive control of yield. Furthermore, in an attempt to curb capital investment, we continued using machines that have gone beyond their depreciation age.

We came to realize we had this quality-related problem occurring at the Taiki factory. Back then, it was only a small quantity of the skim milk that was contaminated. If they had disposed of this powdered skim milk, this problem would not have occurred. But they failed to do so. As the factory tried to cut down the costs by millions of yen, it led to a major disaster. There was also the view that one should never let negative information be leaked from the organization. That negative information was, for some reason, kept and forgotten at that organization. Instead, it was necessary for us to learn from our failures but management had forgotten this fact.

A year and a half later, there was another incident that took place at a subsidiary, namely, the Snow Brand Food. It was the so-called disguised beef incident. The problem of Bovine Spongiform Encephalopathy (BSE) was familiar in Europe, especially in Britain. There was a major outbreak which created a big sensation. In Japan, this outbreak occurred at the end of 2001. Japan entered into a panic and everyone was scared to eat beef. What did the government do for Japanese beef which did not sell? Because this beef could not be sold, it was decided that the government would buy up the domestic beef using taxpayers' money. Before that there was a very negative impression of imported

beef which was very large in stock. This led to a very large inventory of imported beef in addition to the domestic beef. At the chain supermarkets you could see that the beef section was almost empty, because beef did not sell.

Snow Brand was engaged in a number of new businesses. Within Snow Brand Milk we started new businesses and sometimes set up subsidiaries to manage them. On a consolidated basis, this represented some 120 million yen. Within the food industry, we were the largest in terms of our consolidated position. All the subsidiaries carried with the name of Snow Brand such as Snow Brand logistics, a Snow Brand drinkable yogurt, and a Snow Brand lorry. We also established wholesaler companies dealing in sausage, ham, and raw meat known as Snow Brand Food.

As a result of the food poisoning, all these companies that carried the corporate brand of Snow Brand suffered a decline in their revenue. The situation was especially severe for the Snow Brand Milk Products, having both cases of food poisoning and the disguised beef incident. Many mothers said they would not let their babies consume dangerous products such as butter, margarine, cheese, milk, as well as infant milk that we produced. As a result, most of our products disappeared from the market.

In sum, Snow Brand failed to take its social responsibility in these two areas of quality and compliance. People were questioning whether Snow Brand had any value in society. We struggled in answering these. Given this situation, there was no choice for us but to change accordingly.

Thus, we started the business reform. Our main business lines were re-identified which include milk, powdered milk, frozen foods, ice cream, infant milk, and pharmaceuticals. We divided all these businesses and we were helped by the number one companies in the respective industries. Although we had our products, we needed a new brand. Since then we have been implementing reforms in business, financial, and corporate structures.

Even under great attack, many people were willing to support us. Financial institutions, the government, and all the dairy farmers' organizations, they all encouraged us to start afresh. Although Snow Brand Milk Products' debt exceeded its revenue, in 2002, we were able to write off our debt and survive with everyone's support.

One priority area in the corporate structure reform is the development of new corporate guidelines. We decided to put together a code of conduct. We are aiming to offer a smile. That is our ultimate goal. Smiles do not come just because our products taste good but because the food is safe and good for people's health. It also comes from the fact that people have a true feeling of satisfaction. The smile is an appeal to the people to give us another chance—the last chance to regain people's trust.

Snow Brand Milk Products had a very powerful brand in the past. It carried out market surveys periodically and when asked if they have ever consumed our products, more than 90% of people said yes. Everyone had consumed one of our products. Babies, children and other consumers were all enjoying our ice cream, butter and cheese, among others. Despite this, our brand collapsed instantaneously. What happened? The Snow Crystal, our brand, our logo, was something we thought would sell. Hence, we did not bother to listen to the voices of our customers. There were many customers who not only complained, but also came up with proposals. But we did not listen to them—we were not that type of company. This was the cause of our problems and gradually we experienced erosion of sales and market confidence. We discussed this again and again internally, and we decided to listen to outside voices. Since then, we have tried to incorporate external views and even today, we are struggling in trying to realize this.

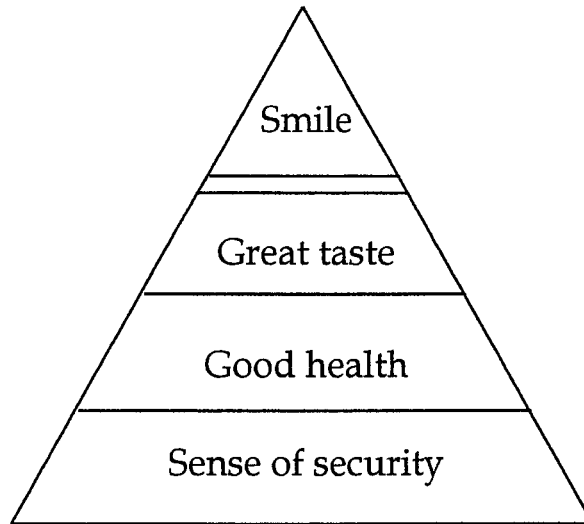


Figure 1. Corporate brand architecture

We appointed Ms. Nobuko Hiwasa, former Secretary-General of the National Consumer Group as an outside director. Earlier, she had said that "Snow Brand has no reason to exist. It is better to dissolve the company." However, we needed to appoint her as an outside director in order to be able to rebuild our company. She had a number of demands in accepting this offer. She said no matter how negative the information might be, it had to be disclosed to her. She said that we should not restrict her from taking any action and insisted that she would take part from a consumer's perspective. This was accepted. It was agreed that if she came out with a number of proposals which have to be implemented by the company, the president would agree to them.

Ms. Hiwasa also became the chairperson of the corporate ethics committee and every month six external committee members and four internal members met to discuss and receive a number of proposals. Staff also participated and this related to customer service and quality-related issues. We frequently inspected our factories and all management challenges that we were facing at that time were taken up. We asked people to come up with any proposals and ideas, and reflected those in our management.

We established the Customer Center. At that time complaints were recorded by area and they were confined in each area. Whatever was happening in Osaka was seldom communicated or only after a long period. Now, it is different. All the complaints from all over the country are unilaterally being concentrated to the fifth floor of our home office in Yotsuya via CTI (computer telephony integration,) the integrated system of the computer and telephone. Wherever the complaints take place from Kyushu to Hokkaido, they all come to our Yotsuya headquarters. Moreover, in this system if there are two complaints related to the same lot and same batch then an alarm is set off which indicates that urgent countermeasures are necessary. We accept any complaints from all over Japan. To satisfy the customers' requests we lend our ear to the customers. Specifically, these are the complaints, opinions, and proposals from the customers. For example, frozen butter is very hard. Some of the complaints told us to make it easier to handle. Based on this, we

cut the butter into sections of 10 grams each so the customers can use it piece by piece. This was welcomed by the customers and the technique is widely used thereafter.

There are also customer monitors. Every year there are 20 monitors in Tokyo and 20 monitors in Osaka. They evaluate new products or make proposals if there is a problem with new products or new recipes. Each year we select different monitors. In 2004, they identified five items that could be improved in the previous year's products.

There is also regular dialogue with the dairy farms and producers. Employees are criticized if they know nothing about the frontline. Many employees have never touched a cow in their lives. Many thought that the dairy cows produce milk every day of the year until the day of their death. That was surprising given that some relatives were on dairy farms. Some people were shocked to find the understanding of Snow Brand employees was quite different. We came to the conclusion that we have to go back to the basics of production to revitalize the company.

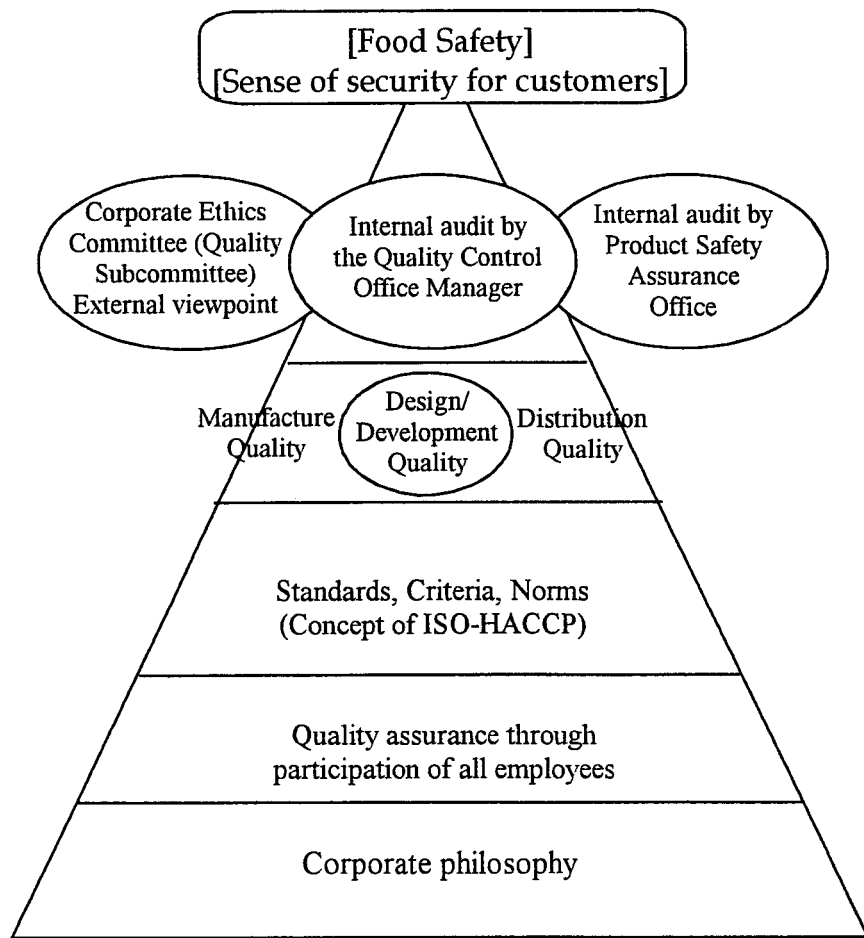
Furthermore, the board, at that time, seldom went to the factories. They made their judgment on indirect information from the frontline. It is different now so that often our board members go to the factories, frontlines, or sales offices of the local areas, to understand the problems from them and facilitate two-way communication. We have an "open factory day" when the factory is open to all customers. For the past three years, more than 30,000 customers have visited our factories to see how Snow Brand factory or how the managerial style of the production line has been changed. Previously, almost all factories were off-limits to the customers or outsiders.

The risk management at Snow Brand had failed but we learned a great deal from these two incidents. We are now trying to construct a system to address risk management. There was a delayed understanding of the board and so delayed communication to the board. Therefore, any information that can be related to risk management should be detected at an early stage.

We had generated quality-related problems. We now have a joint project with the Hazard Analysis and Critical Control Point (HACCP) and International Organization for Standardization (ISO) Snow Brand Quality Assurance System. There are two dimensions to quality assurance. One is positive—any of the products not conforming to specific criteria may never be shipped outside of the factory. During the food poisoning incident, we knowingly shipped sub-standard products which should never be allowed.

The second dimension of quality assurance is about valuing outsiders' opinions. Checking the production line in the plant is not the plant's business alone. We have a Quality Subcommittee in the Corporate Ethics Committee in which outside experts participate. They regularly visit our factories and sometimes they have very strong views. This is a tripartite monitoring system where we watch the factory from three points of view—HACCP, ISO and the Corporate Ethics Committee.

We also developed a crisis management system. We prepare for worst case scenario. In that way, our speed of response is much faster. Fortunately, we have not faced any major incidents recently with the Snow Brand Quality Assurance System (SQS) in place. With a risk management approach, we have to proactively find out what is understood by our employees and that is the purpose of the hotline.



#### [SQS Characteristics]

- (1) With the strong commitment and leadership of the top executive, all employees ensure quality assurance.
- (2) Listen to and reflect "Customer opinions" on products and processes.
- (3) "Quality assurance" and "quality improvement" through ongoing improvement.
- (4) Develop the corporate culture to ensure quality through strict quality assurance education.
- (5) Enhance the audit system through multiple parties.

Figure 2. Snow Brand quality assurance system (SQS)



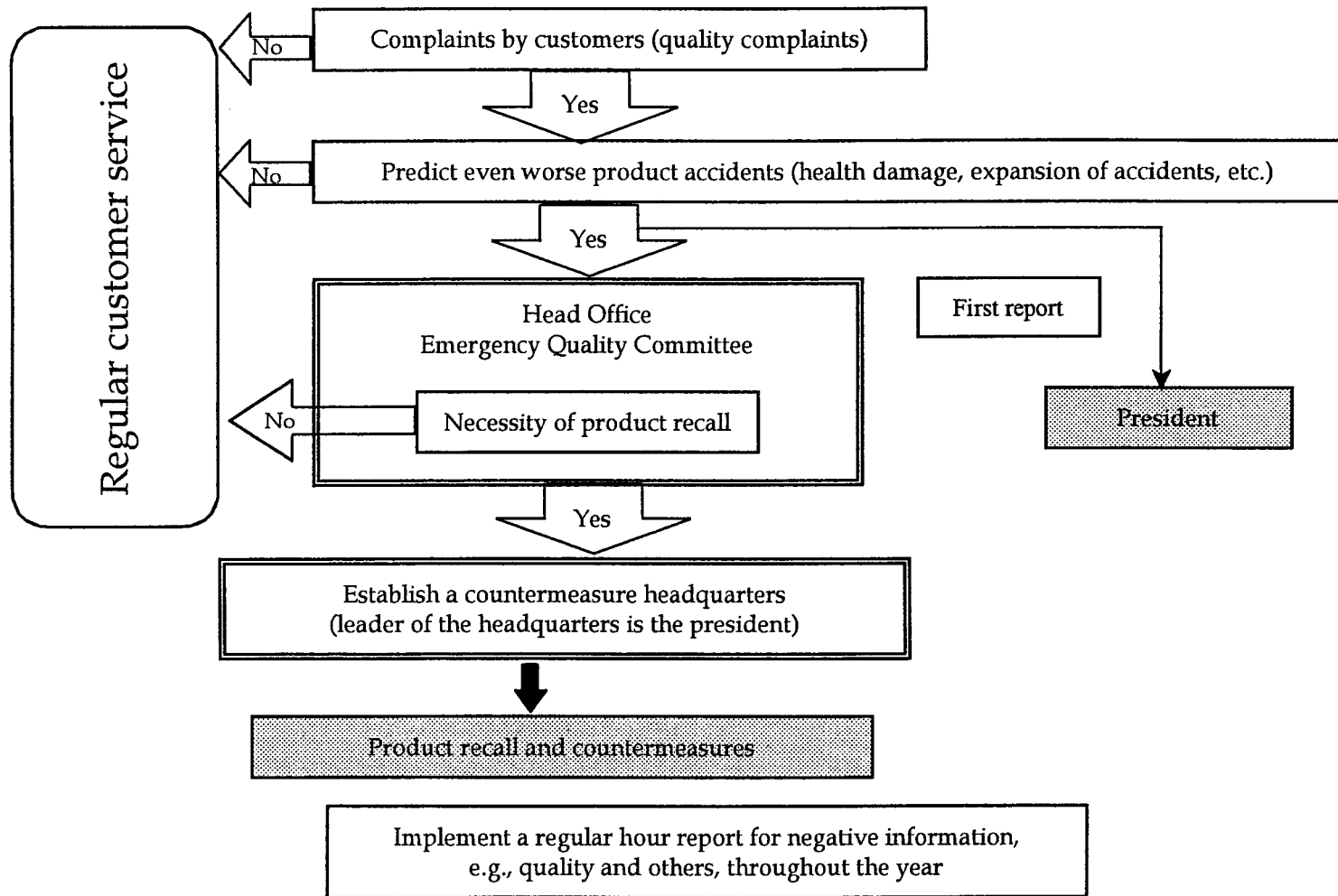


Figure 3. Development of a crisis management system

There are employees who cannot speak up on their own, so we encourage them to access this hotline as much as possible. We try to address this risk upfront and we have installed this hotline in our group companies. The incorporation of corporate ethics is a key priority but we have not done enough and we are only halfway to our goal being achieved.

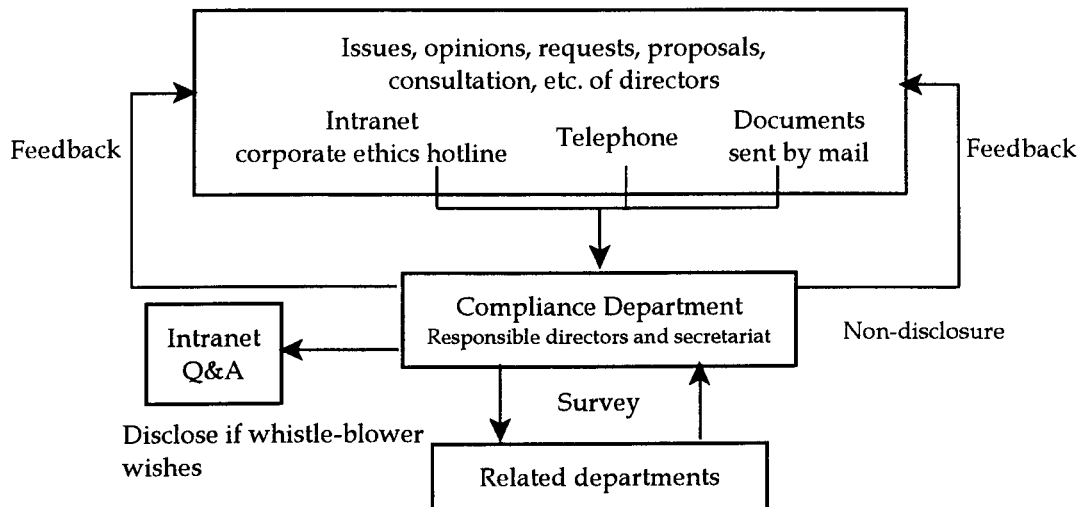


Figure 4. Corporate ethics hotline

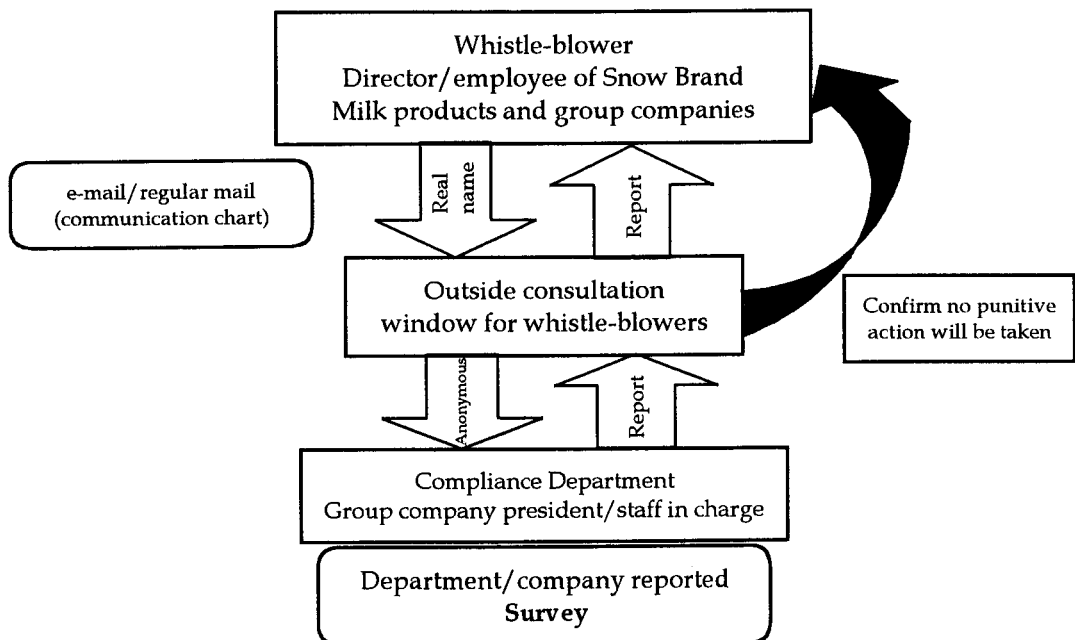


Figure 5. Snow hotline

In establishing the code of conduct we have a very simple and easy to understand brochure. This sets out five points with an emphasis on creation and observation by all employees as follows:

1. Commitment to remember the two incidents through the President's message;
2. Attitude towards customers and consumers, essentially in the first chapter;
3. All employees including the President must pledge;
4. Checkpoints for conduct; and
5. Disclose on the homepage, and within the company in booklet form.

We also have a pledge sheet. Every employee is required to submit a pledge indicating their commitment to the code which is also posted on our website. There are already some 35,000 copies of this brochure delivered to consumers and people in society. Whether or not this has really taken root has to be monitored. So, we carry out questionnaire every year. Corporate Ethics Committee members also visit various places regularly to listen to the voices of our employees and encourage them to share their problems with us.

Twice a year we set days for activities to remember the infamous incidents. The disguised beef incident took place on 23 January. The food poisoning took place and the first complaint was delivered to us on 27 June. These two days are designated as days of remembering the incidents. We revisit the mass media's communication or the news stories so that we prevent the memories from fading away from the heads and minds of our employees.

In our CSR, we emphasize transparent management. By disclosing information widely to the general public, we would like to show people how the managerial style of Snow Brand is changing and much of our management information, product information, or our compliance activities are widely disclosed on our homepage.

The product label is an important information source when customers select products. This is promoted through the work of the Label Subcommittee of the Corporate Ethics Committee. We evaluate the product labels from external and customers' viewpoints to ensure there is no customer misunderstanding or misconception. This consists of three external and five internal members to enhance the checking of the labels. Safe and good tasting products are something expected of us, but easy to understand labels which prevent misunderstanding and misconception should be developed, which is something that we are working hard towards.

There are many such kind of discretionary labels and description in Japan. For example, there are many products called 'Hokkaido.' Hokkaido has a sense of freshness, something very fresh. Therefore, sometimes even though it is not really from Hokkaido, if the label says Hokkaido cheese people think of a spacious ranch, fresh air, fresh and well-tasting cheese and this sells. The law says 60% or more of the raw materials must come from Hokkaido to carry the label of Hokkaido, so the threshold is 60% of local procurement. Many companies state the local content at the back of their packages in small letters. But we do it on the front page in bold letters. Some people are concerned about salt content of cheese so we have created a cheese with less salt content with 'Less Salt, Six Piece Cheese' as the product name. Customers asked what we meant and we responded by saying that this meant a 20-% reduction in the sodium equivalent of the salt content which is explained clearly on the label. If we include the butter contents in margarine, consumers always came back to ask how much and 15% is clearly stated on

the label. This may not seem to be a clever marketing strategy, but we would like to be honest about the contents. Sometimes we have to say something negative from the marketing point of view. Attractiveness is an intangible property of the product and is always the intention of the product developers. However, we have to be honest at the same time.

With regard to the SQS, we have surprise checks and regular on-the-spot inspections. Ms. Hiwasa was often involved and visited the factories or sales offices. Once a very critical person against the Snow Brand, she became a great fan of Snow Brand.

We have regular feedback discussion on the results of the on-the-site inspection. We have a new Consumer Subcommittee, Corporate Ethics Committee, Consumer Subcommittee, Quality Subcommittee and Products Safety Assurance Office. Over a long period, we suffered a lot of criticism from consumers. Sometimes this was deserved. Our interest is to reduce the distance between us and the consumer groups. It took courage for us to create this regular monthly forum to exchange views with the consumers, but it was necessary. On 23 January 2005 we convened a three-hour meeting in Osaka, the site of the incident. There were harsh words from our customers but several people representing opinion leaders and consumer associations said, 'to a certain degree we are beginning to understand how Snow Brand is changing. Good luck to you.' That moved me to tears to hear that. We had a serious food poisoning incident but our efforts were now beginning to be paid off.

In 2004, the Customer Association in Tokyo asked customers to complete a survey questionnaire of our corporate activities. Previously we had the worst record. Out of 98 foodstuff top companies they selected seven "A-rank" companies, which were disclosed to the newspapers. Indeed, Snow Brand was selected as one of these companies. At that time we were on the brink of bankruptcy but thanks to the encouragement of many consumers and others, many consumers came back to us. From a company in deficit, we turned into a profitable company. This fiscal year we are expecting not to suffer a deficit although profitability will be less than expected on a consolidated basis. We are not qualified yet to say we are a CSR-oriented company. However, today no company is viable without assuming the responsibility of CSR.

There are three commitments we made to society. One, in fiscal year 2003, was that we would make a surplus, which we did. The next fiscal year (calendar year 2005) is that we still have the accumulated deficit, which will be eliminated. In the fiscal year 2006, we are going to pay a dividend. If a company fails to pay dividends, then it is not qualified to say anything about its CSR.

Against this backdrop the legal environment has been changing in a very significant way in Japan. This covers food, sanitation, and the basic law. There is also the Consumer's Protection Basic Law. The Personal information Protection Law and the Whistleblower Protection Law will come into effect from April 2005 and April 2006, respectively. Thus increasingly we have to be oriented to the consumer. The consumer is not an entity to be protected; rather consumers are the entities that are clearly entitled to have their rights protected legally. This is a major change in society. We have to assume responsibility for what is legally stipulated.

A consumer-oriented management is one way to move towards CSR-oriented management. With our code of conduct, each and every employee of Snow Brand sees and has to understand identical things that are written on the card. There are check points for conduct where employees should always ask themselves if their deed will earn

respect for them as members of the Snow Brand Group. They are asked what they would do in order to fulfil the following situations:

1. Meeting the corporate philosophy.
2. Not violating the law.
3. Following the norms of society.
4. Not causing shame to the family.
5. Being truly justified

This is something each and every employee has to carry around and ask by oneself in order to meet our corporate philosophy and not violate the law. This is our commitment and our determination.

## Positive Aspects of the CSR Debate in Japan in Comparison with Europe and America

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Asian approaches to corporate social responsibility (CSR) are different from those in the USA and Europe. The debate on CSR in Japan originally started from environmental concerns. At the end of the 1980s, people's awareness of the environment increased. With the Rio Earth Summit in 1992 environmental issues became hotly debated during the 1990s. Towards the latter half of the 1990s, environmental issues and the environmental framework were broadened to include sustainable development and then CSR.

In the USA and Europe, and also in Japan, the CSR became a hot issue at one point in the summer of 2002. What happened in the summer of 2002 in the USA? From the autumn to the winter of 2001 and towards the spring of 2002, there were major scandals concerning Enron and WorldCom. Arthur Andersen, with a history of more than 90 years in business suddenly collapsed overnight which was a shocking development in the US capitalism. Enron was supposed to have good corporate governance as well, but in the summer of 2002, the President had to sign the Sarbanes-Oxley Law.

At the same time, in the USA, the very high salaries for CEOs were being criticized by the public. The Nobel Prize Laureate, Professor Joseph Stiglitz of Columbia University, said that "in the depth of the international community, the trust towards the US model was being shattered, and the high salaries for CEOs were seen as stealing from the economy." According to *Forbes* magazine's annual survey of CEO salaries, Richard Ford received 15 billion yen at Lehman Brothers, and Steve Jobs of Apple Computer Company received 10 billion yen worth in remuneration. At Exxon-Mobil and Merrill Lynch, CEOs received about four billion yen worth in only one year. CEOs in Japan receive just 1/100th of this.

What is very interesting about the debate on CSR in the USA is that it is quite different from that in Japan and Europe. For example, in the USA, the keyword on CSR in 2003 was said to be homosexuality. The Federal Supreme Court's decision stating that ban on homosexuality was against Constitution led to the elimination of discrimination against homosexual workers at the companies. Massachusetts became the first state in the whole of the USA to legally approve homosexual marriages. This issue was hotly debated even during the last Presidential election. The background is the USA's religious value—Americans are the sons or the descendents of the Pilgrim Fathers and feel that they should strictly abide by the teachings of the bible. In addition, domestic violence or violence against women have been taken up by companies and one in four women are said to be victims of domestic violence.

In Europe, there is a strong will to promote CSR through the single European Union. This movement of CSR in Europe dates back to 1989 at the time of the fall of the

Berlin Wall. After the Soviet Union collapsed, there were a large number of refugees who fled to various parts of Europe. Civil wars ensued intensively in a number of locations. There is a five-fold gap between wages in Eastern and Western Europe. In 2004, the European Economic Community was enlarged from 15 to 25 members and there was an expansion towards the East. Such economic integration aims to enhance the productivity of the region. However, since they are working under the same economic system there is bound to be massive social friction. Therefore in Europe, we often hear the word “social cohesion,” which means uniting people together for the development of their economies. In the European Union, CSR is being used like a banner to integrate Europe. European CSR focuses on legislation and social policies. It does have impact on various legislation as well as social policies.

What has been happening in Japan during the same time? From the autumn of 2001 to the beginning of 2002, several food and car companies experienced corporate scandals. People started to question company attitudes towards customers and the corporate accountability. For the first time in half a century, the Corporate Law was revised. When the Corporate Law was revised, people questioned the relationship between the board members and stakeholders.

There is a demand for better corporate governance. George Hara, the famous venture capitalist in Japan, argues that US capitalism could force the vital companies in society to collapse. He also argues that management people in the USA are just focusing on expanding and increasing their personal profit and not the companies. Once a CEO is appointed, then the past cumulative losses are written off as well as future debts. Naturally share prices then go down. However, this is what CEOs want. If they were to reduce the cost, then profits would increase and then share prices would go up. If they were to exercise the option, they would be able to gain much profit. This is the reality of corporate governance in the USA and the true image of CEOs who are thought to be godly figures.

In Britain and other European countries, corporate governance is discussed in such a way that it reflects their version of CSR. In Britain, they are also revising their corporate law which is in line with what they call ‘enlightened shareholder value.’ In other words, you have to have not only a short-term but also a long-term vision. This is what is required of board members and they need to develop a relationship with all the stakeholders incorporating a wider scope of management.

On this point, Norman Boyd, Professor of Minnesota University, has suggested there are three models of capitalism. There is an American type of capitalism which attaches importance to the stockholders, the shareholders, and their profit. It is a short-term profit-oriented capitalism. At the US business schools, they teach as though this is the only effective model. Therefore, CSR focuses only on maximizing profit. This implicitly says that rich people should be engaged in charity activities through philanthropy. In the second model, there is a need to balance the profit of stakeholders as well. CSR strives to reflect this balance of a win-win situation between the company and shareholders. The third model is sustainability which has three aspects—economic and financial success, consideration to the environment, and social responsibility (‘the triple bottom line’.) In Europe, sustainability and CSR are considered to be equal. Thus, corporate governance is taken up in the same debate with CSR. ISO is now trying to standardize SR rather than CSR, because social responsibility encompasses more than just corporations.

In Japan, environmental reports are being issued by more than 100 companies. However, this environmental report is changing. Our company also has been releasing environmental reports for about 10 years. In 2002, we called it the sustainability report and in 2003, we started to call this the CSR report. We are addressing the environment issue and all other relationships with our stakeholders in this report. This kind of thinking is now spreading in Japan. One thing that supports CSR is socially responsible investment (SRI). According to 2003 data, three trillion dollars are being invested in SRI with 2.16 trillion dollar in the USA. Japanese companies cannot just watch on the sidelines what is happening in the USA. In Japan also, there are many SRI funds being used in investments.

Figure 1 looks at the CSR debate in Japan right now where the main focus is compliance. Corporate governance, business ethics, and organizational integrity are also being debated. In CSR, the local society, human rights, employment and also providing equal opportunity to participate in the society, and consideration for the environment and all stakeholders are being debated. The debate in Japan is still at an early stage and we do not have a clear cut picture of how the CSR debate will develop in Japan.

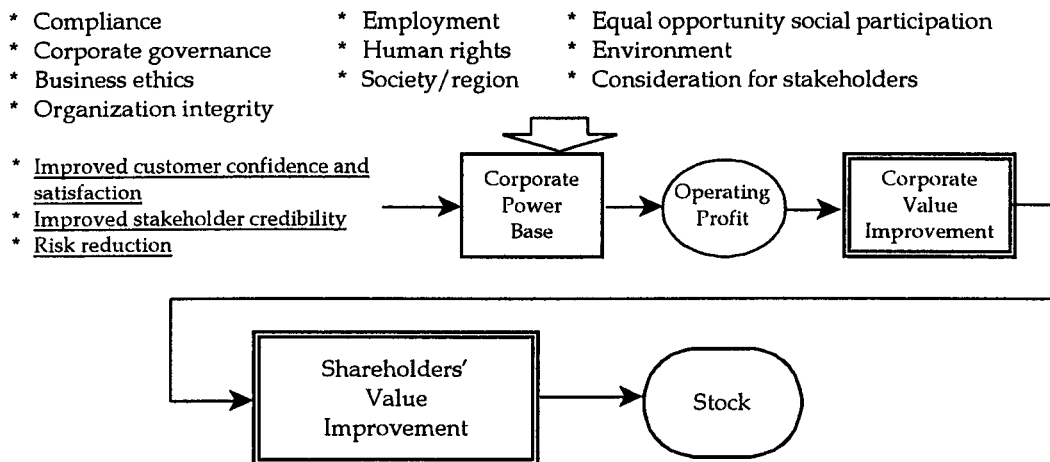


Figure 1. Spread of CSR debate

At the bottom of Figure 1, it is clear that if confidence and satisfaction of the customer and stakeholder improved while risk is reduced, then the power base of the corporation will be strong which would lead to profit. Theoretically and logically, that means there would be an improvement in the corporate value which will then be reflected in shareholder value. Logically, stock prices will go up.

Perhaps CSR will be largely related to building up the framework of the Japanese society of the future. Japan has never experienced a civil revolution. Even the Meiji Restoration and the end of World War II was not a revolution. It was a change of the system and top-down revolution. Today in Japanese society, there is a change in awareness and change of systems in parallel and there is a connection with CSR here.

Fifty years after World War II what was happening in Japan? On the surface, Japan appeared to experience a historic economic recovery and rapid economic growth. In thirty or forty years, the landscape of Japan has dramatically changed. Even villages high up in the mountain and urban sceneries have changed. Attitudes toward life and the



people's lifestyles have also changed. In the half century, we have seen the greatest change ever experienced in Japan. The economic recovery and the economic growth provided, according to Professor Yukio Noguchi of Tokyo University, the seniority system and lifetime employment, and labor unions were established within the company. This was the systematic framework that provided this economic recovery and growth. Professor Noguchi calls this the 1940 system.

What was 1940 like? It was the year when Japan was bracing itself for the coming Pacific War. It was trying to devote all the resources it had for the coming war and Japan was changing its system to a wartime system. That framework was seniority, lifetime employment, and also labor unions within the company. The psychological or mental framework that supported the economic recovery and growth was the village society and Confucian ethics and values. "Village society" may be difficult to understand and seem to be a very vague concept but it is different from a nomadic society. Villagers grow rice, and when harvest time comes, all of the villagers would help each other to harvest rice. When you sow seeds, the whole village comes out to help each other. Water used for the rice paddies will be allocated based on discussions of the villagers. They would establish the rules for using the water, and the village leader will be in charge of determining all of these facts. If anybody does something against the village rules, they would be outlawed and they will be sent off from the village. It would not be accepted within the village. However, if you abide by the rules of the village, you would be protected by the village from the time you are born until you die. That is the kind of village society that supported the seniority system after World War II. The company was once like a village. After you leave school and enter a company, the company will protect you until you retire from that company. Unless you break the rules of the company or as long as you do your job you would be protected by the company and you would never lose your job.

Confucian ethics and values are universal in Asia in a sense. Takahiro Hosaka, a philosopher, has said that the Japanese are Confucianists, meaning that Confucianism is the religion of Japan. Professor Makoto Kurozumi of Tokyo University said that Confucianism came to the surface rather recently in the Tokugawa period from the 17<sup>th</sup> century to the 18<sup>th</sup> century under the fourth or fifth Tokugawa shogun. It has a history of about 200 years. In China, it has 1,000 years of history. However, the ethics of Confucianism is reflected very strongly in the behavior of the Japanese people and that is seen in the seniority system. People of older age and of a higher rank are people you cannot oppose. You cannot deprive that person of his or her work.

Yet after the World War II and 60 years later this systematic framework dramatically collapsed. Interestingly, it is sixty years from the Meiji restoration to the Manchurian Incident, and during this time, Japan entered into the international community and as a result of the Manchurian Incident, there was criticism from overseas. This led to Japan being isolated. Sixty years in modern history might be the life span of a system but what is happening now in Japan could be that we are seeing a collapse of a system and this mentality of a village society collapsing.

Thus on the one hand, the system is collapsing, people's mindset and consciousness is following likewise very dramatically on the other. There is no company which can assure lifetime employment and they cannot follow the seniority system anymore. For 60 years people have expressed loyalty to the company but young people today cannot embrace the same type of loyalty to the company.

## Hypothesis: Perhaps CSR has possibilities that are largely related to future framework building in Japanese society

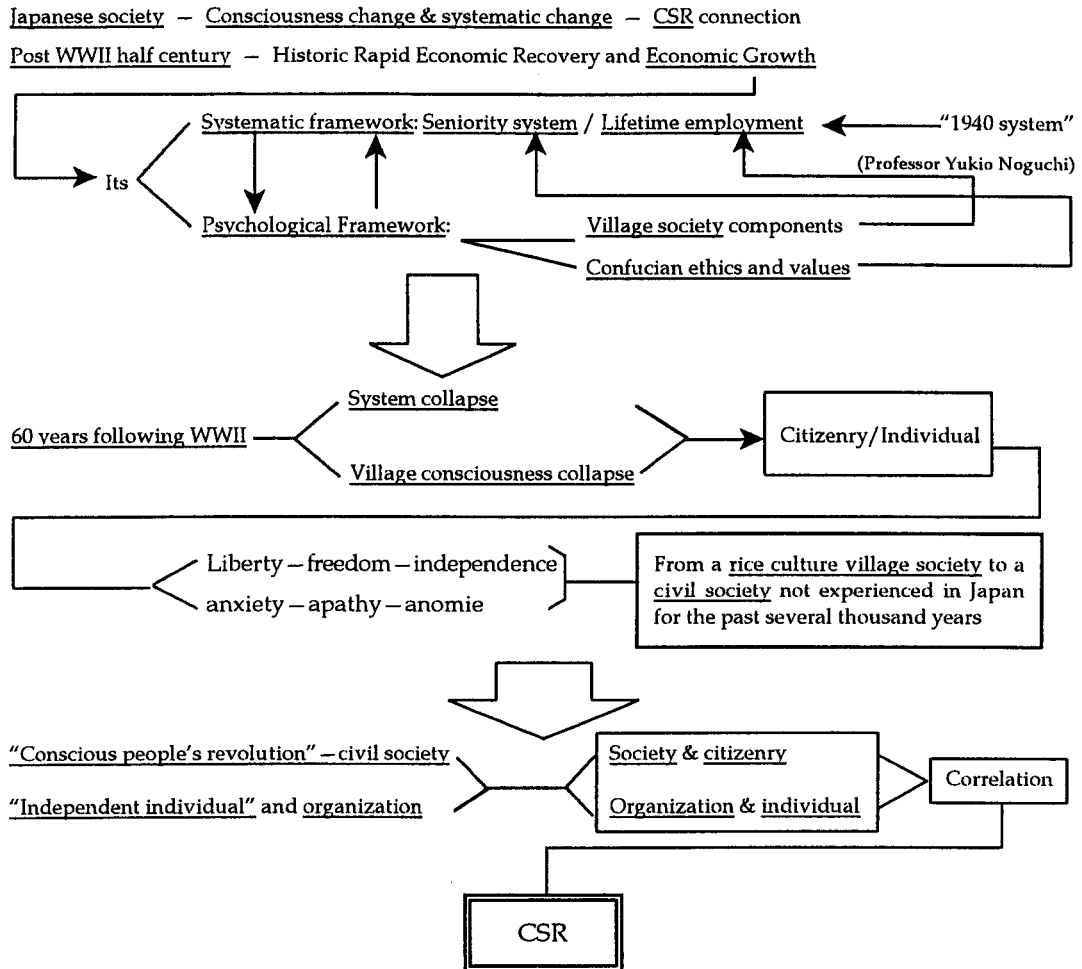


Figure 2. CSR and the future of Japanese society

What happens to people who are excluded from the village? They are no longer villagers but citizens and now for the very first time in Japanese history we are starting to see the emergence of such citizens. Becoming a citizen, becoming an individual, and living as an individual on the one hand means liberty, freedom, and independence. You do not have to abide by the rules of the company and the government, and you do not have to be concerned about every detail of these rules. You are free and independent so it is really liberating. At the same time you will feel anxiety, apathy or anomie. There is no one there to protect you and you have to protect your own self to live through this very scary society. Thus people feel anxiety and if they fail, they would enter into a state of apathy and could become a social dropout.

Present-day Japan is changing from a rice culture, or village society to a society which Japan has never experienced in the past. In other words we are now shifting to a civil society. What is happening now is a civil revolution at the awareness level. Every day we are gradually witnessing a shift from village society to civil society where the individual and organization have to be independent. It could be a company, a local government, a national government, a non-profit organization (NPO), or media but these organizations have to become self-sustainable.

As citizens in a society and individuals of an organization, we have to see how to establish a relationship with each other. If in Japan, we were to witness a collapse of the system with civil revolution at the consciousness level, CSR could be said to be the framework for establishing a new system. If that happens, it will be very interesting to observe how the debate on CSR develops.

We need to watch very carefully how the discussion on CSR will develop in the USA as well as Europe. Europe is becoming a block of its own and the USA is also developing its own version of CSR. At ISO they are trying to standardize social responsibility. That being the case, we should not just let the Americans and the Europeans debate on this subject. We, in Asia, should be discussing our version of CSR. The timing is right for us to discuss and research an Asian version of CSR which will be very beneficial to all of us. From Asia, we can export our own version of CSR and there is real potential here. Taking into account our virtues, traditions and history, Asia can research and communicate to others our version of CSR.

## **Socially Responsible Investment in Japan**

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Socially responsible investment (SRI) is a very important tool to promote corporate social responsibility (CSR). SRI and CSR are now becoming very popular in Japan, and many people are very confused by many three-letter abbreviations. Some people refer to this as sustainable and responsible investment. This is generally understood as an investment approach that integrates social, ethical, and environmental considerations into investment decisions in addition to financial considerations. This is the generally understood SRI definition relating to investment, excluding savings, etc. In a broader sense, SRI can be described as investments, savings, loans, or any flow of money which considers social impacts. This can include both investments, savings, and money flows directed toward sustainable development on a global basis. In the Asian context, the broader sense is more appropriate because the generally understood sense is more applicable to the Western type of financial markets, which are more mature and developed.

Why are financial considerations not enough in making investment decisions? People want to reflect their ethical and personal values in their investments decisions rather than just considering financial results. SRI could also be used as a tool for social activities. For example, company management can be changed using the power of shareholders.

Financial considerations are not enough because financial statements alone do not give the total picture of a corporation, so it is vital to measure and assess corporate value from social and environmental aspects. This is a new way of thinking. Traditional investors think that they can assess corporate value from the financial data alone, such as the balance sheet and profit-and-loss statement. However, we now know that corporate value cannot be assessed by financial data alone but also by brand value and intangible assets. These are becoming more important and considered to be the origin of corporate value. Recently, because of many company scandals, people have begun to believe that the social and sometimes the environmental aspects are crucial to corporate value. SRI is also a powerful tool to promote CSR itself because companies sometimes perform this promotion spontaneously. However, outside pressure is sometimes necessary to promote CSR, and investors are considered to be one of the main pressure groups.

From the narrower definition, there are several types of SRI and the largest one is socially screened portfolios. When forming an investment portfolio, various financial data are considered to determine how safe and profitable companies are. In addition to indicators such as return on equity (ROE), return on asset (ROA), and other balance sheet data, social or environmental data, such as the company's environmental management or its policy on human rights, are additionally considered.

In addition to financial scrutiny, a social and environmental assessment is undertaken through the stock portfolio, and the best companies are selected. In this screening of portfolios, there are two types: pension funds and mutual funds. The

difference is that mutual funds are mostly invested in by individual investors who want to have their values reflected in their investment decisions. In the case of pension funds, each fund compensates employees, who cannot decide how their investments are made. It is the company or the pension fund itself which decides how the investment is made and third-party professionals manage the portfolio. In the case of mutual funds, this reflects individual investors' desire to invest in socially screened portfolios.

The second type of SRI is shareholder advocacy. If you are a shareholder, you are a part-owner of a company. Thus, theoretically, you have an opportunity to have a dialogue with management and a chance to ask the management why it is pursuing a particular strategy. In addition, you have a right to have a shareholder proposal and to vote at the annual shareholders' meeting. In the 1970s in the USA, a famous social activist asked General Motors to have a diversified board and a shareholder proposal was submitted. Although this vote was not passed at the annual meeting of shareholders, General Motors acknowledged this to be a very serious problem and subsequently employed outside board members who were African-American. A shareholder proposal was passed at Dow Chemical Co. to stop producing a pesticide used in the Vietnam War. Thus shareholder advocacy and activism can be a powerful tool for a social movement.

Another part of SRI is community investment. This is capital flow directed to communities that are not adequately served by traditional financial services compared with large capital markets. This mainly occurs in the USA where many poor people do not have access to financial services and who cannot as a result borrow money from traditional banks. Community investment is a tool to help them. Examples include mortgage loans for lower-income people or developing slums and other community areas that are not prosperous. These three definitions of SRI are based on the USA. However, in Asian contexts, SRI should include microfinance, which probably is one of the largest areas of SRI in Asian market.

SRI is said to have started in the 1920s in the USA, when churches decided not to invest in businesses prohibited by their religion, such as tobacco, weapons, and alcohol. In the 1960s, active shareholders came to be seen as a driving force in protesting or demanding improvement in social issues such as human rights and the environment. Until then, SRI was considered to be a very niche market consisting of religious investors or social activists. Their investments aimed for social and not economic return. The third movement came in the late 1990s, when social and environmental aspects were recognized as important for evaluating corporate value. This started from the eco-management movement when many companies, especially in Japan, began to use the environmental management system ISO14000. Until then, environmental management was considered to be a burden on corporate management because it adds cost. For example, to meet higher air diffusion criteria bigger purifying machines must be installed. However, after many companies introduced environmental management systems they found out that eco-management was not only a cost but it could also improve their efficiency and sometimes productivity. Reducing an environmental burden reduces costs for energy and materials. By reorganizing their manufacturing flow, companies could reduce time and waste and raise production yields. Thus, environmental management was seen as a way to improve corporate efficiency.

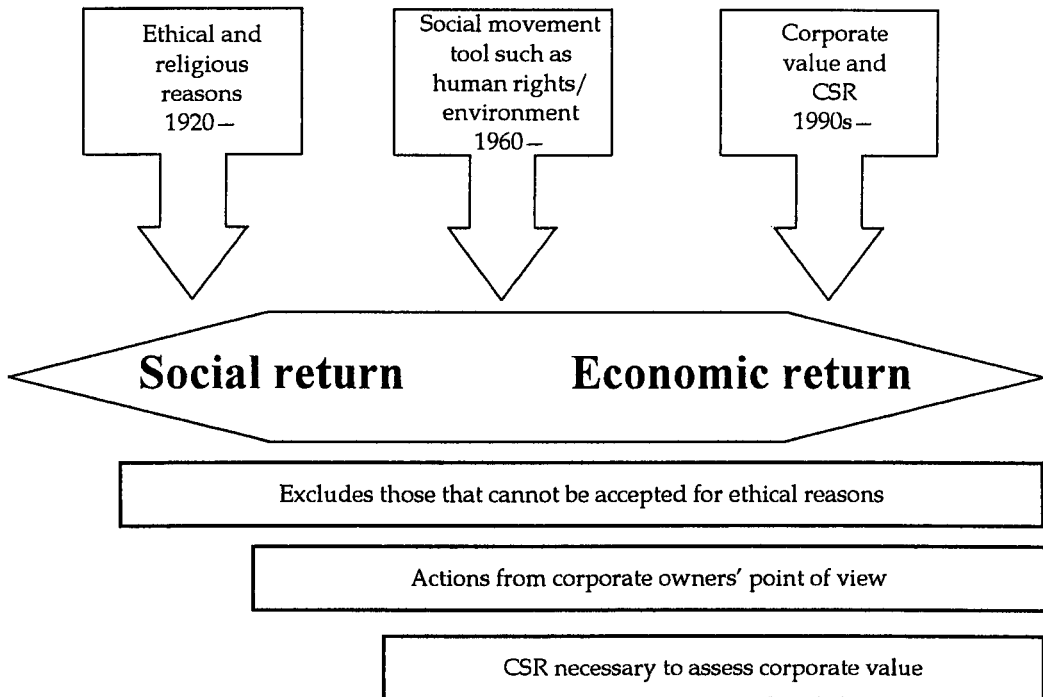


Figure 1. History of SRI development

If you are an investor and want to find a very efficient company, you can look only at the financial data to see whether this company is efficient. However, if you are looking at environmental management data and if you think that environmental management is very efficient, that will also probably lead you to conclude that the company is efficient. It is looking at the same company from a different perspective. Many investors started taking environmental management into their investment decisions in a positive way. In 1999 in Japan, a mutual fund called the Eco-fund was launched with the idea that it would choose the best-in-class companies in environmental management in each industry. This was different from an environmental business fund that selects stocks of waste management industries. In Eco-funds, one can choose automobiles and electric utilities but must select the best companies in terms of environmental management in each industry. This is a different concept from the environmental business fund.

Many company scandals have occurred in Japan, the USA, and Europe. In companies with scandals, social and environmental management were not managed very well, and people did not understand what was happening in those areas. For example, Enron was considered to be a financially excellent company, but people who actually were close to the company knew that its ethical and social behavior was poor. Consequently many people began to think that even if the financial statement looked fine, there could be other problems occurring on the social or environmental side which cannot be detected by looking at the financial data. It is necessary to look at the social and environmental side in order to reduce the risk of investment. In this way, the aim of SRI becomes economic return. By considering the social and environmental aspects of a company, you can achieve a better return or reduce the risk of investment. As this aim

has changed from social to economic return, it is attracting more investors. Previously SRI was a very niche market attracting a very special type of investor. Now, with the acknowledgement of the importance of CSR in evaluating corporate value, it attracts ordinary investors. That is why SRI has increased rapidly in the last five to 10 years.

In the USA in 1995, total SRI assets were US\$639 billion but by 2003 this had increased to US\$2,164 billion, a growth of more than three-fold in eight years. Moreover, in 1995, most SRI was shareholder engagement (shareholder activism) at US\$529 billion. Social activists were dominating the market and screened portfolios were very small. By 2003, screened portfolios were more than 90% of the total. Some funds perform screening and engagement. Thus, in the last eight years, more ordinary investors joined this market. The size of the SRI market is about 10% of the total capital market managed by professional fund managers. It is certainly too large to neglect, but more is needed to have more social power.

In Europe, the UK market soared 10-fold from 1997 to 2001. In the Netherlands, the SRI market grew more than three-fold during the same period. The total SRI by institutional investors is €336 billion. SRI funds for private and individual investors stand at €12 billion, for a total of €350 billion. The biggest SRI markets in Europe are the Netherlands and the UK, because they have policy measures to support SRI.

When Japan is compared with the financial markets of the USA and Europe, it is probably one of the second largest markets. However, if compared in terms of SRI markets, the SRI market in Japan is very small. It is less than 0.1% of the US SRI market and less than 0.3% of that of Europe. On the other hand, it is now very fast growing and has received more public attention recently.

People who are interested in CSR are also interested in SRI. The Japanese SRI market was initially led by eco-funds that chose stocks with good environmental performance. Now it is expanding to social factors. The Japanese market is still an individual investor-oriented market. Institutional investors have not joined this SRI market yet. Mutual funds using SRI screening with environmental management increased in the past year; there were 11 SRI funds in Japan in 2003 and 16 in 2004. This reflects growing interest in SRI.

There are common reasons why SRI markets are growing so fast in the USA, Europe, and Japan. There is growing global concern for CSR. There are some regulations to support SRI as well as rising individual investors' demand for SRI. In addition, SRI indices have been developed to help institutional investors undertake SRI. SRI performance has also been relatively good, attracting more investors.

In terms of government policy, an epoch-making regulation was the UK Pension Fund Law amendment in 2000. The amendment requires pension funds to disclose whether they take social, ethical, and environmental factors into their investment policies. This amendment did not require pension funds to pursue SRI but to disclose their investment policies and whether their investment policies have an SRI element in it. After three months, 70% of pension funds employed such investment policies with social, ethical, and environmental considerations. However, "investment policy" on its own is merely a paper commitment. It is necessary to have the tools to define and implement such a policy.

Table 1. SRI funds in Japan

Asset management Co.	Name	Fund type	Inception date	SRI screen	2003.12		2004.12	
					Par value	Total assets	Par value	Total assets
Nikko AM	Nikko Eco-fund	Domestic EQ	1999/8/20	Environment	6,413	39,240	6,928	37,327
Sompo Japan AM	Bunanomori	Domestic EQ	1999/9/30	Environment	7,405	8,435	8,190	12,987
DLIBJ AM (DIAM)	Eco-fund	Domestic EQ	1999/10/29	Environment	6,503	5,226	6,950	5,136
UBS Global AM	Eco-hakase	Domestic EQ	1999/10/29	Environment	6,704	4,364	7,349	4,218
UFJ Partners AM	Midorinotsubasa	Domestic EQ	2000/1/28	Environment	5,865	2,896	6,148	2,657
Asahi Life AM	Asunohane	Domestic EQ	2000/9/28	Consumer philanthropy	8,238	4,228	8,898	4,133
Sumitomo Mitsui AM	Umitosora	Domestic BL	2000/10/31	Environment	8,601	1,238	8,920	1,088
Nikko AM	Nikko Globe A	Global EQ	2000/11/17	DJSAM Index	8,309	1,354	9,005	1,193
Nikko AM	Nikko Globe B	Global EQ	2000/11/17	DJSAM Index	6,567	833	6,766	729
Daiwa SB Investments	Mrs Green A	Global EQ	2001/6/15	Environment	7,927	2,147	8,185	1,714
Daiwa SB Investments	Mrs Green B	Global EQ	2001/6/15	Environment	8,181	3,359	8,699	2,750
UBS Global AM	UBS Global 40	Global EQ	2003/11/7	DJSAM Index	10,384	11,682	10,954	6,569
STM AM	Good Company	Domestic EQ	2003/12/26	DJSAM Index	10,255	1,662	10,860	21,678
Shinkin AM	Fukoku SRI Fund	Domestic EQ	2004/4/27	Environment, social, ethical			9,591	2,877
Daiwa AM	Daiwa SRI Fund	Domestic EQ	2004/5/20	Integrity			10,147	28,113
Nomura AM	Nomura Global SRI 100	Global EQ	2004/5/28	FTSE4Good			10,276	5,120
Nomura AM	MorningStar SRI Index Open	Domestic EQ	2004/7/30	MorningStar Index			10,089	3,440
Mitsubishi AM	Family Friendly	Domestic EQ	2004/12/3	Family Friendly			10,345	1,105
Total						86,664		142,834



According to one study, 20–30% of pension funds are actually implementing SRI in their final managers' decisions. Although not yet widespread, many investors now recognize the term SRI. Thus the policy development was a valuable way of promoting SRI in the investment community. Similar regulations exist in other countries such as Australia, Germany, and other European countries. Some people in Japan are considering introducing similar regulations to promote SRI from the pension fund point of view. The reason why pension funds promote SRI is that it is the money of employees and it is a long-term investment. For long-term investment, companies with stronger and more durable brands and higher-quality people will perform better in the long term. In short-term performance there are many incidents like price changes but in the long term, people value the quality of the management, people, products, and services as well as the corporate brand.

There is also growing demand for SRI. In the USA, there is no regulation to promote SRI but there are demands from individual investors. There are more than 63 million lifestyle of health and sustainability (LOHAS) consumers. These are people who eat organic food and do yoga on their holidays and they make up about one-third of Americans. These are the consumers who prefer SRI. Probably 10% of the total population in the USA buys SRI financial products. According to the SRI institute, 70% of individual investors prefer SRI to conventional investments.

In the USA, 401K plans are defined as contribution pension fund plans where the employees can choose the investment style. If you are working in a company and joining a pension fund plan, you are given a list of the pension fund investment products that you can choose. There are several SRI types of investment plans. Research shows that 70% of employees choose SRI instead of ordinary funds. Thus the SRI concept is preferred by the general public. Research by the Environmental Agency on SRI shows that 75% of Japanese prefer SRI to conventional investments. From investors' points of view, SRI fits their philosophy. Another reason is the supply side and development of SRI indices.

The stock index is very important when undertaking investment, especially for fund managers. To evaluate fund managers' results, you first need a benchmarking index. Whether you beat the benchmark index depends upon the quality of the fund manager. For example, if you invest for one year and gain 10%, that may seem good. However, if the general market average grew 20%, then you actually lost 10%. By doing nothing you could gain 20% because the market grew 20%, but if you ask one fund manager to manage the fund and he only gained 10%, that is a loss of 10%. If one fund manager loses 20% in one year, that may seem bad, but if the market drops 50% during the same period, he did very well. Without the fund manager, you could probably lose half of your money, but with him, he could save 30% of your money. This is how fund managers are evaluated. It is thus important to have an index to evaluate fund managers.

Three indexes have been developed in the last five years. The first is the Dow-Jones Sustainable Index. Another is the FTSE4Good Index developed by FTSE, and EIRIS, a research firm in the UK. The following year, the Ethibel Sustainability Index was developed by Ethibel, and Standard and Poor's, a rating company. Stock indexes are very useful tools for fund managers to undertake SRI. As a result of these SRI indexes, fund managers can pursue SRI more easily.

Some say that SRI is burdened by nonfinancial considerations covering social and environmental factors. Social and environmental criteria can be broken down into two types: negative and positive. Negative criteria consists of things like tobacco, alcohol, gambling, pornography, arms, and nuclear activity, and companies involved in these

industries are first excluded from investment. However, this has a risk of limiting returns by narrowing the investment scope.

There is another kind of SRI that uses positive criteria (as in eco-funds) and considers environmental stewardship, products, labor conditions, supply chain management, human rights, community involvement, respect for local needs and culture, corporate governance, etc. This does not limit the investment scope as it does not exclude tobacco, alcohol, or gambling. It is possible to choose a great environmental stewardship gambling company, although this may be very difficult to explain. This happens in eco-funds in Japan. Toyota is a good example. It is a company in which many eco-funds in Japan have invested, but there has been a great deal of criticism. Some people choose Toyota to invest in, because the car company introduced the Prius, a hybrid car with very low petrol requirements. However, from another point of view, it is one of the largest car companies producing vehicles that contaminate the environment with CO<sub>2</sub> and other gases. There are, therefore, two ways of thinking: if you think that car companies are not eco-friendly, you cannot choose Toyota. However, you can also choose the best environmentally managed car company or the one with the best environmental products.

There are various tools available in SRI to promote CSR. There are several investment communities that acknowledge the power of the investor to change the world, such as the Carbon Disclosure Project. More than 80 global investors in the USA, Europe, and Japan are asking 500 major global companies worldwide to disclose the impact of climate change on their earnings and assets. They are making reports that state that climate change is affecting various companies' earnings via risks, etc. in the long term and short term. This project is now in its third year and the report is available on the Web (<http://www.cdproject.net/>.) The reason why the project is doing this is that most conventional investors make investment decisions without considering the risk of climate change. In one example, a company with a factory based on the sea coast may be damaged by the rising of sea levels due to global warming. These issues are not considered by conventional investors, but there are risks due to the climate change, and these risks should be included in investment decisions. This project is making a report in which it argues that conventional investors should consider the risk of climate change in their investment decisions.

Another project is Pharmaproject.org. This brings together 10 major European investors requesting healthcare companies to disclose their marketing strategies in developing countries, especially in Africa. In Africa, there are many AIDS patients, and pharmaceutical companies are making a great deal of money with high drug prices. Investors argue that it is not fair to make money from low-income AIDS-suffering African countries and that companies should charge poor African countries a fair price for retroviral agents.

The Extractive Industries Transparency Initiative is led by George Soros. He asks major oil companies to disclose their royalty and other payments to developing countries. Major companies disclose their royalty payments in one column on their balance sheets. The oil companies are being asked how much they pay to Angola and other countries. In this way, how much the Angolan Government or Angolan politicians benefit from each oil company can be seen. This shows how corrupt some governments are, as some of the money may not be going into the government budget.

The Equator Principles are led by Citigroup and require environmental assessments when banks make project finance decisions. This is an initiative through shareholder activism in the USA. Two years ago, an NGO asked Citigroup to employ

environmental assessments in making project financial decisions via a shareholder proposal. As a result, Citigroup decided that it will undertake environmental assessments whenever making project financial decisions. It asked all other major financial institutions to join and this became the Equator Principles requiring most large financial institutions to perform environmental assessments when making major project decisions.

There is evidence of good SRI performance. From 1998 to 1999, SRI performance exceeded that of the conventional type. From 1998 to 2000, SRI performance also exceeded the conventional type. Only from 1998 to 2001, after three years of performance, was SRI inferior to the conventional type. Looking at the Japanese stock market index (TOPIX) from September 2001, companies producing an environmental report outperformed the general market most of the time, and actually outperformed by 20% in more than two years. Thus if you are investing this way in the long term, you can make more money than in the general market.

Many investors are still not convinced that CSR and corporate value are connected. The biggest challenge for the SRI community is whether there is a clear link between CSR and corporate value. In the longer term, in a qualitative sense, CSR is connected to corporate value. However, you cannot quantify this and say how much it contributes to next year's earnings. For example, how much does a better environmental management and a better human rights policy contribute to next year's earnings? This is a question no one can answer. The results of surveys of UK pension fund trustees on whether factors such as environmental management have an impact on short- or long-term earnings are shown in Table 2.

Table 2. Impact of each CSR activities on major UK companies

(Unit: Percent)

		Significant plus	Plus	None	Negative	Significant negative	Not known
Environmental management	Short term	3	59	26	9	0	3
	Long term	26	56	12	3	0	3
Good employment	Short term	8	61	25	4	0	2
	Long term	20	61	15	2	0	2
Respecting developing countries' needs	Short term	1	38	51	7	0	3
	Long term	9	52	30	6	1	2
Corporate governance	Short term	33	54	11	0	0	2
	Long term	42	49	7	0	0	2
Communication and transparency	Short term	5	56	34	2	1	2
	Long term	23	56	18	0	1	2
Good relation with customers	Short term	26	52	19	0	0	3
	Long term	38	52	8	1	0	2

Note: "Short" is one year and "long" is five to 10 years. Survey of 130 UK pension fund trustees.

Source: "Will UK Pension Funds Become More Responsible?" *Just Pensions*, January 2004.

As is clear from Table 2, many people agree that qualitative factors have an impact on corporate value, but it is very difficult to quantify. Thus CSR has an impact on long-term corporate value. For example, in the case of good working conditions and environment, this would lead to high employee motivation and loyalty, then to product development and good service, then to customer satisfaction, and product premium, and all will lead to better earnings. Although easy to understand, it is difficult to say how

much earnings are attributable to each factor. However, the short-term impact is not as obvious. A good labor standard does not tell you how much this will improve next year's earnings, and this is an obstacle to SRI development on a global basis. As many mainstream investors require scientific data, it is difficult to persuade such people. Further, the importance of CSR activities varies among different societies. Approaches and perceptions of CSR vary according to different people, as highlighted in Table 3.

Table 3. CSR activities taken into account by individual investors

(Unit: Percent)

CSR activity	Japan	USA	UK
Environment	70.4	54.2	62.8
Product safety and health considerations	68.1	45.1	43.4
Consumer protection	60.3	53.5	45.7
Anticorruption measures	51.0	61.6	58.1
Stable employment	30.4	54.9	37.2
Employee health and safety	30.0	53.9	53.5
Relations with labor unions	27.4	51.4	42.6
Equal opportunity and diversification	24.6	42.3	38.8
Commitment to community	16.3	42.6	34.1
Avoidance of child labor/forced labor	14.9	54.2	57.8
Others	0.9	1.8	3.5
No answer	3.2	14.1	14.3

Source: Ministry of Environment.

The Association for Sustainable and Responsible Investment in Asia (ASrIA) is an association to promote SRI in Asian countries. The ASrIA Conference in July 2004 could be summarized by three key terms: emerging markets, private equity, and microfinance. Not all Asian markets are similar but they share some common features. There is less chance for SRI screening of portfolios of listed companies because stock markets are smaller.

In terms of money flow, which integrates social considerations, public entities, such as the International Finance Corporation (IFC), have a large role to play. In some cases, SRI is misunderstood as a risky investment. In Europe and Japan, SRI is considered to be safe. It is not clear why SRI is misunderstood to be risky in Asia. Corporate governance and transparency are a more serious problem in Asian markets, or for Asian companies. As a result of corporate governance and transparency problems, investors who want to do SRI research have difficulty in obtaining information. However, in the Hong Kong and Singapore markets, which are more developed, there are some SRI funds. In Hong Kong, there are six foreign SRI funds operated by UK financial management companies. One domestic fund, Kingsway Fund Management, is a Hong Kong-based fund management company for individual investors, mainly the wealthy, women, the elderly, and the religious. In Singapore, recently one domestic SRI fund, operated by United Overseas Bank, has been launched and another foreign company that manages SRI funds is available.

In terms of challenges and problems in the Asian SRI market, private equity and the IFC have a very important role. The sustainable standard for environmental assessment is used widely and in the Equator Principles as well. Another important tool is microfinance, especially to support economic independence and development. This is

very different from the type of SRI screening in Japan and the USA. However, considering the context, the concept of SRI should be reflected in microfinance and probably in private equity at this stage. Thus, to promote SRI in Asian countries, measures to promote money flows through private equity and microfinance are necessary. What is needed is a level of high transparency and information disclosure. Good corporate governance is also needed to attract money flows of the SRI type from overseas.

In support of microfinance, other money flows to improve society are necessary. Cooperating with NGOs and nonprofit organizations might be necessary to make microfinance more credible. One example is the Sumatra Tsunami Disaster Long-term Rehabilitation Plan. Due to the Sumatra tsunami, many companies are supporting various types of aid globally. Recently, Daiwa has decided to pay 100 million yen for 10 years for the rehabilitation plan after the tsunami disaster in partnership with NGOs in Sri Lanka and other Asian countries, which includes microfinance. The tsunami aid first concentrated on the initial needs, but is now shifting to rehabilitation or long-term development. What was decided is that, because of this long-term commitment, 100 million yen should be paid, which means 10 million yen each year for NGOs operating microfinance in other projects in several Asian countries. The reason why microfinance is included in Daiwa's aid is because it can accumulate experience in how microfinance works as an effective aid plan and also as a good financial measure in those countries.

SRI offers real potential in the Asian market. In its wider definition, SRI, the flow of money which considers social impacts, has the potential to improve society in both developed and developing countries. In developed countries, there are many investment decisions being made in the financial market every day, so what is necessary is to integrate more social-environmental aspects into ordinary investment decision making. In developing countries, money flows into financial needs must first be created to address social goals, and microfinance could be an effective tool to achieve this.

# Corporate Social Responsibility

## –Why It Matters, What It Means and Where It Is Going

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Tepco, Parmalat and Enron—These names, by the admission of senior executives in all companies, are now synonymous with corporate irresponsibility. Indeed, the issue of trust—in business, governments, media and pressure groups in particular—is perhaps one of the most urgent challenges of our time and one that has no borders. This was highlighted at successive Davos Economic Summits and can also be seen in the broader context of confidence—by customers, employees, shareholders, and also communities—in business policy and its translation into practice. Corporate social responsibility (CSR) and socially responsible investment (SRI) have provided opportunities for companies to align their activities with broader societal expectations. But there is still a view that this is window-dressing and does not go to the heart of the business. CSR refers to business practices characterized by extensive disclosure and transparency, which companies initiate to fulfil ethical responsibilities towards employees, communities, and the environment. The emphasis is on creating not only sustainable shareholder value but also sustainable social value. SRI is an investment approach which, in addition to conventional financial criteria, evaluates and selects companies on the basis of social and ethical criteria such as legal compliance, employment practices, human rights, consumer issues, contribution to community, and environmental issues, while seeking stable returns. However, SRI also includes financing motivated by social justice and community contribution and the exercise of shareholders' rights.

A number of major global trends in CSR and SRI can be identified. There is a growing connection to corporate governance through reporting—for example in the U.K., changes to company law suggest that information about a company's relationships with its employees, as well as its policies and performance on environmental, social, and community issues can be subjected to an informed assessment by investors and others. The G8 Summit in Evian concluded that “sound social frameworks and attention to the long-term impacts, including on the environment, of investment decisions, and business processes are also important for sustainable growth.” There is also increasing development of major global voluntary standards such as ISO and OECD Guidelines for Multinational Enterprises. Though interest in SRI is increasing, more importantly social issues now increasingly influence mainstream investors such as Nomura, Nikko Salomon Smith Barney or Standard Life Investments.

Table 1. Comparative categories for SRI categories

EIRIS (UK)	KLD (USA)	Asahi Shimbun Foundation (Japan)
1. Corporate ethical guidelines	1. Contributions	1. Consideration towards employees
2. Customer/supplier relationship	2. Diversity of employment	2. Emphasis on families
3. Workplace safety/cleanliness	3. Labor relations	3. Ease of work for women
4. Workers' rights	4. Operations outside the U.S.	4. Employment of physically disabled
5. Equal opportunity/diversity in employment	5. Product considerations	5. Globalization of employment
6. Employee compensation	6. Executive compensation	6. Consumer orientation
7. Training and development of employees	7. Excluded items (alcohol, tobacco, gambling, defence, nuclear power)	7. Harmony with community
8. Job creation and security		8. Support for society
9. Community service activities		9. Environmental preservation
10. Supply chain		10. Disclosure
11. Human rights at overseas operations		11. Corporate ethics

These developments in CSR and SRI have now reached Japan. Some characteristics of CSR in Japan can be seen in Table 1 which compares categories for SRI in each of the financial centers of the UK, USA, and Japan. While UK and USA approaches emphasize human rights and excluded items, the criteria in Japan specify consumer orientation and disclosure. Most Japanese SRI funds include strong consumer corporate brands such as Sony and Toyota. This—together with a number of high profile scandals—has meant that corporate responsibility in Japan has been strongly associated with relationships with customers, as individuals make judgements about companies in relation to their “experience” as customers but in their “behavior” as investors.

CSR is about companies taking into account their complete impact on society and the environment, not just their impact on the economy.

There are seven reasons why CSR matters:

1. Moral and ethical reasons—to ‘do the right thing’
2. Sustainability of the markets companies rely upon for income
3. Brand image/reputation
4. Employee/stakeholder motivation
5. To enable the company to respond proactively to changing stakeholder agendas and be able to cooperate effectively under a range of business conditions
6. To account positively on its performance to stakeholders in a way that will enhance the company’s reputation
7. To provide managers with a framework for managing the business in a more holistic manner.

# The Business in Society

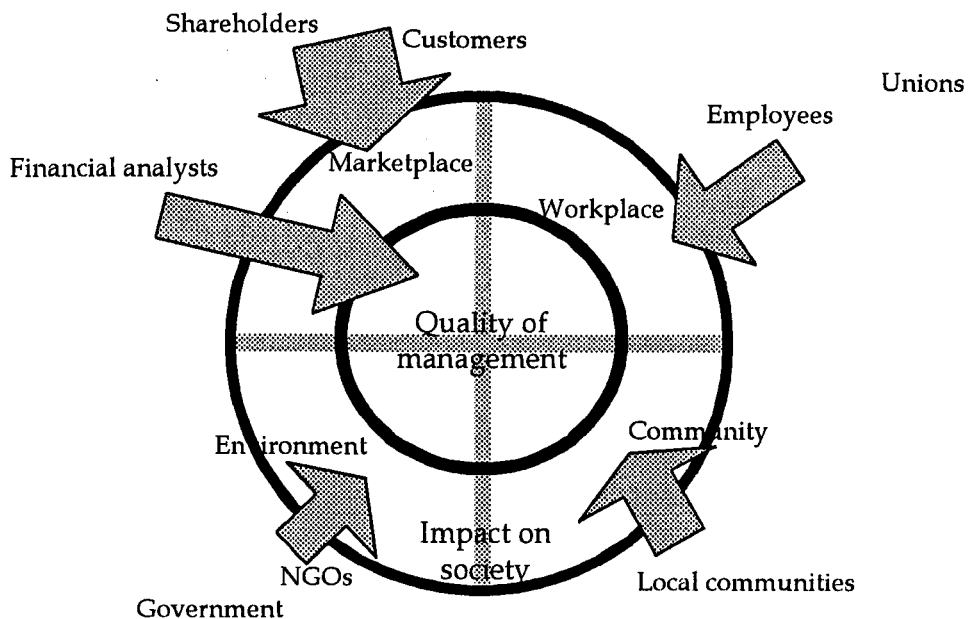


Figure 1. Stakeholders and society

Source: Diagram by Mallen Baker, use freely.

There is currently an almost bewildering array of international CSR initiatives. However, stakeholders such as governments, businesses, and civil society groups have identified a range of significant weaknesses in current approaches to promoting CSR:

- An over-proliferation of CSR initiatives at the international level and lack of clarity about how these initiatives relate to each other;
- An excessive focus on getting businesses to make commitments to CSR and not enough focus on enabling them to implement them;
- An absence of credible monitoring and verification processes;
- A lack of effective mechanisms of redress for communities affected by companies that flout national or international norms on sustainable development or human rights;
- A lack of engagement with developing country governments and their sustainable development priorities (e.g., economic development and poverty reduction);
- A failure to bridge the governance gap created by weak public sector governance of the private sector in many developing countries;
- Limited impact on sustainable development goals; and
- A lack of government involvement and/or investment in international CSR initiatives, which is contributing significantly to their underperformance.

Despite the volumes of paper and the number of events, the CSR (and corporate governance debate) in Europe and the USA while contributing to heightened awareness of the issues has significant drawbacks which are seldom acknowledged.



1. Reputational risks of CSR advocates: The experience of Shell and Ahold, by their own admission and among others, has underlined the limitations of pursuing CSR in a context in which corporate governance and leadership is weak. It has also fuelled the charges of CSR by some as corporate spin or 'greenwashing,' justifiably or not. At the same time, variable standards and a lack of transparency by a growing number of (western) NGOs which undertake advocacy, consultancy and third-party auditing, all too often in tandem, continues to constrain confidence in the processes involved.
2. A lack of understanding of how corporate governance links to CSR: While there is much noise there is still surprisingly little that sets out, in succinct and clear language, how the two are related. There is an imbalance in the CSR debate which fails to distinguish where CSR relates—and does not relate—to corporate governance. In this area recent developments in the UK at the Commonwealth Business Council in particular, and also the OECD are of note as well as policy-orientated research at Henley Management College. At the same time, the significance of developments in Asia, especially Japan, which links the two areas is being increasingly recognized.<sup>1</sup> Moreover, in developing countries it is important to highlight not just why but how responsible behavior and good governance can contribute to a more favorable investment climate.
3. A lack of understanding of what CSR means—and how it is perceived—in an Asian context: This has several dimensions. As Canon in Japan recently noted, 'the Anglo-Saxon debate on corporate responsibility seems to be centered only on their historical and social criteria, which naturally deal with Catholicism, Protestantism and Western European Individualism.'<sup>2</sup> In addition, there is a risk that a strong and sustained focus on China and India does not crowd out visibility for innovative practice—and an appetite to learn—in other markets. Moreover, there is an increased need, post Iraq and a revived Doha trade development round in July 2004, to address a perception that, in the absence of dialogue, CSR is a simple extension of western standards as a proxy global standard and CSR operating as a non-tariff barrier to trade. This is especially sensitive in Asia with the ending of textile quotas from 2005 which will both accelerate competition among major exporting countries but pose particularly acute challenges for the dozen or so poor economies that depend heavily on clothing and textiles production. As the Department for International Development (DFID, UK) recently noted, 'inappropriate codes of conduct become a form of protectionism that prevents goods from the South being sold in the North. Exporters in developing countries can find the proliferation of regulations and standards hard to comply with. They often fear that "process standards" on the way products are made (such as the standards on labor, the working environment, or animal welfare) will lock their products out of developing country markets.'<sup>3</sup> As one UN Security Council member from a

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<sup>1</sup> A. Zaman, 'Made in Japan – Converging Trends in Corporate Responsibility and Corporate Governance,' Royal Institute of International Affairs, London, 2003. See: <http://www.riia.org/pdf/research/sdp/MadeInJapan.pdf> (research undertaken at the Royal Institute of International Affairs 2002-03 funded by Henley Management College, Marks & Spencer with travel support from British Airways.)

<sup>2</sup> *Sustainability Gearing Up* (report for UN Global Compact Meeting 24/06/04)

<sup>3</sup> *DFID and Corporate Social Responsibility*, DFID 2003.

developing country asks, 'How can developing countries get those social standards, if they cannot earn enough? If there are no jobs, how can we have good jobs? How can we have good labor standards when there is no labor in the developing countries? There is no investment.'<sup>4</sup> The language of CSR in the West increasingly needs to address 'a visible commitment to capacity building in the developing countries to enhance their ability to expand exports and trade as a means of promoting development...[and] poverty alleviation through trade.'<sup>5</sup>

4. A weak understanding of the dynamics of international trade and how diversified exports from developing countries for supply chains of global companies can contribute to SME development and poverty alleviation: The private sector is the main driving force of industrial development in virtually all countries and—through changing patterns of international production, investment and trade—shapes the economic globalization process. A vibrant private sector building on the combined strength and linkages and relationships between large, medium, small and micro enterprises is an essential prerequisite for triggering economic dynamism, enhancing productivity, transferring and diffusing new industrial technologies, maintaining competitiveness, contributing to entrepreneurship development and ultimately poverty reduction—and reduced social and business risk.
5. A lack of sectoral specific context: While the Extractive Industries Transparency Initiative (EITI) in the UK has relevance for a BP it is less clear what this means for an established international listed company in the financial services, media, retail or transport and logistics sectors where the consumer experience is so different. A profusion of questionnaires from a growing number of (western) rating agencies with a 'one size fits all' approach for diverse sectors is resulting in questionnaire fatigue on the part of companies.
6. A lack of explicit focus on productivity: Traditionally, the productivity debate has focused on its input-oriented economic and technological aspects. This view is being increasingly challenged and is a priority of the Dutch Presidency of the EU in 2004. The increasing focus on sustainable development, corporate governance, social responsibilities and ethics, and social auditing and standards represents a significant shift in the growth paradigm which acknowledges that social conditions also affect the rates of productivity growth. Productivity is more than working longer hours but also the about climate of trust that exists and the strength of relationships through which companies create value for key stakeholders such as employees, customers and shareholders and, increasingly, demonstrably responsive to society.

In the productivity debate in Europe, there is an excessive focus on the US experience rather the vibrant economies which have seen fast growth in Asia since 1961 when the intergovernmental organization, the Asian Productivity Organization (APO), was established and which are currently among the strongest worldwide (e.g., Japan, Malaysia, Thailand, Vietnam, India and Pakistan).

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<sup>4</sup> Address by Munir Akram, Pakistan Ambassador to the UN and formerly to the WTO, to the SAARC Chamber of Commerce, 29/07/03, Islamabad.

<sup>5</sup> Statement by Pakistan's Ambassador to the UN, Munir Akram, on Agenda Item 91(a): International Trade and Development in the Second Committee of the General Assembly (November 03, 2003). See: <http://www.un.int/pakistan/00home090803>

7. An insufficient focus on capacity-building, training, and development, especially in developing countries: A unique gathering of global companies, major investors and international policymakers at the UN in Tokyo in November 2003<sup>6</sup> agreed that there has been too little focus in CSR and governance in these areas. Management education can play a critical role—by building the human capacity and management capability to understand the issues in emerging markets and work towards solutions both for in-country personnel and local people. It is also one way to link to the next generation of leaders and board members. However, events on CSR and corporate governance whether in Europe or Asia where experts parachute in with set piece presentations are no substitute for activities which build the confidence and trust as well as develop the capabilities and harness the creativity of those directly involved, especially decision-makers among policymakers, companies, and investors from developing countries. In this, a trusted regional intergovernmental intermediary such as the APO which now spans a range of 20 Asian countries is key and much-needed.<sup>7</sup> The issue of training and development on corporate governance and CSR is not limited to Asian countries: UK pension schemes recently acknowledged that only 25% of their trustees took part in formal training programs other than induction training.<sup>8</sup>

However, it is clear that the CSR agenda also has some important strengths, including:

- the high levels of commitment shown by some key leadership companies;
- the capacity for innovation and openness to change shown by a range of international CSR initiatives;
- the openness of leadership companies and CSR initiatives to working in partnership with a wide range of stakeholders, including the UN, governments, other businesses and civil society organizations, including at the local level in developing countries; and
- the growing recognition by leadership companies and organizations of the need for the CSR agenda to address public sector governance issues and to scale up the impact of CSR activities so that they can improve the delivery of sustainable development at a systemic level.

A wide range of CSR initiatives has emerged in recent years and include:

- \* voluntary codes and standards for corporate behavior;
- \* voluntary reporting guidelines;
- \* auditing/verification of reports, production processes, supply chain standards or products;

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<sup>6</sup> UN report available at <http://www.henleymc.ac.uk/henleyres03.nsf/pages/corr>. Meeting supported by UK Embassy in Japan, UN, Cable & Wireless, Japan Business Council in Europe and Reuters.

<sup>7</sup> Interestingly the APO organized a conference on social responsibility in Asia, involving six countries, as far back as 1982 which examined the practice of both foreign and local companies.

<sup>8</sup> *The Myners Principles and Occupational Pension Schemes*, Volume 2 of '2. Findings from Quantitative Research,' 2004. See: <http://www.dwp.gov.uk/asd/asd5/summ2003-2004/213summ.pdf>

- \* policy frameworks, including reporting requirements, tax incentives, and enabling legislation;
- \* multi-stakeholder partnerships;
- \* work with supply chains; and
- \* dissemination of best practice.

Japanese companies are also increasingly conscious of CSR. In 2004, more than 20 of the firms on the *Morningstar* SRI index mentioned it in their reports to shareholders, compared with only three in the previous year. Last June, the ISO decided to standardize the social responsibility of businesses as global citizens. In Japan, the Ministry of Economy, Trade and Industry has been asking companies to cooperate by offering proposals and advice to the ISO. At the same time, Nippon Keidanren and its European counterpart, the Union of Industrial and Employer's Confederations of Europe (UNICE), recently agreed that the voluntary initiatives of companies are more important than setting up an international yardstick for CSR. One positive development is Mitsubishi Corporation's moves in sustainable development reporting and stakeholder engagement.

In Japan, however, the weakest link in CSR and SRI overall remains is its international application. This is reflected in decisions by asset managers to reduce their holdings in particular companies because of a shift to offshore manufacturing locations in more low-cost environments. Why should a company be any less responsible if it is closing down its operations in Malaysia and developing its activities—and employing local people—in Vietnam or India?

In fact, providing local producers with access to international markets is one way of reducing poverty. Support for small- and medium-sized enterprise development can be an important part of the CSR commitment of large companies. And improvements in social and environmental impact can go hand in hand with improvements in quality and management. Supporting enterprise development through long-term trading relationships and community investment is one of the most important ways that internationally-listed companies can contribute to the fight against world poverty.

This is very relevant for Japan. Japan does not wholly accept the mainstream thinking of the Western aid community about development. It continues to believe that the East Asian development experience, to which Japan itself has made a significant contribution through aid, trade, and investment, provides a useful model. Japan's aid program focuses on growth strategies, including industrial promotion and infrastructure development. These are, interestingly, exactly the areas where there appears to be an emerging consensus in approaches by the U.K., the U.S., and Japan.

What is now needed is greater coordination between foreign direct investment (FDI) and development assistance policies and practice. Efforts by governments, NGOs, and donor agencies to build human capital typically lack the input of private sector expertise in countries that need that expertise most. There is an opportunity for large enterprises, impelled by skill shortages or social responsibility goals, to assist local firms and entrepreneurs in upgrading proficiency. There is also a role for partnerships in helping public institutions understand and adapt to the needs of local firms and larger companies. In a number of cases, Japanese corporate activities in poor countries are groundbreaking (such as Toyota's social investment in northern Pakistan.) Japan has made strong commitment to promote development via the UN and also through the Japan Bank for International Cooperation (JBIC) and the Japan International Cooperation Agency (JICA). Top Japanese manufacturing companies have also made FDI in some of

the poorest countries in Asia. These commitments generate real potential (and relatively little effort) for SRI in Japan to link better with aid programs to increase capital flows to emerging markets and help build domestic capacity, reduce poverty and mitigate social risk. Indeed, Vietnam is increasingly looking to foreign private sector companies to demonstrate their commitment to reducing poverty.

Despite a perception that Western SRI funds support global development, recent evidence suggests that they singularly fail to do so. For Japan, CSR and SRI would have enormous potential if it were to become more closely aligned to mainstream development issues. The reality is that in the short to medium term four countries in Asia will be of increasing importance to Japan for their combination of trade potential, manufacturing costs, and the relative stages they have reached in economic and social development for regional security: China and India, but also Vietnam and Pakistan. These countries are also characterized by real and urgent challenges of social development and so provide an opportunity to rise to the challenge posed at Chatham House in January 2003 by Gordon Brown, the U.K. Minister of Finance, that “we should not judge our results just by the input and the community involvement we seek to have, but by the difference we make to poverty reduction on the ground in the developing world.” In other words, CSR needs to be measured by output not by input; not by the broadly defined contributions that companies make, but by the impact they make on reducing social risk and supporting sustainable development.

### **Commonwealth Business Council Guidelines for Corporate Citizenship**

There are many different definitions of “corporate citizenship” and “corporate social responsibility.” The Commonwealth Business Council (CBC), established by the Commonwealth Heads of Government in 1997 to involve the private sector in the promotion of trade and investment, uses the term corporate citizenship with a definition developed from the work of the World Business Council on Sustainable Development: “Corporate citizenship is the commitment of business to contribute to sustainable economic development, working with employees, their families, the local community, and society at large to improve the quality of life of all their stakeholders.”

Business in the Commonwealth has become increasingly aware of its role in helping to make globalization work in a way that combines economic advance with social development. Indeed, many Commonwealth companies are leading the way by demonstrating good corporate citizenship in action, “living out” the business principles that they have established and articulated in different ways.

The CBC Guidelines for Corporate Citizenship provide guidelines of good corporate citizenship derived from CBC corporate members in Asia and beyond. They are a useful template for an international approach to CSR which has relevance and rigor in an Asian context.

#### **1. Values**

The company will be guided by values and work towards reflecting them in its business operations:

- **Core values**—having clear values and a Code of Ethics such as honesty, integrity, fairness, and openness, clearly stated and followed in practice;
- **Transparency**—being actively open in structure, process and disclosure; establishing and maintaining communication with key stakeholders;
- **Tackling corruption**—adopting agreed codes, being persistent in enforcing them internally and in external dealings; and
- **Human rights**—recognizing the implications for the business of a respect for human rights; having a policy and acting on it.

#### **2. Corporate Governance**

The company will manage its business with strong and effective corporate governance implemented by the board according to the following principles:

- **Compliance**—ensuring that the corporation complies with all relevant laws, regulations, and corporate commitments;
- **Profitability**—ensuring that the company is profitable and provides a reasonable return on the assets it employs;
- **Leadership**—exercising leadership, enterprise, integrity and judgement in directing the corporation so as to achieve continuing prosperity for the corporation and acting in a manner based on transparency, accountability, and responsibility;
- **Accountability and responsibility**—recognizing and differentiating accountability linkages (to shareholders and statutes) and responsibility linkages (to other stakeholders); and establishing reporting mechanisms to support these linkages;

- **Board qualifications**—ensuring that through a managed and effective process, board appointments are made that provide a mix of directors, each of whom is able to add value;
- **Checks and balances**—ensuring that no one person or block of persons has unfettered power and that there is an appropriate balance of power and authority on the board which is, *inter alia*, usually reflected by separating the roles of chief executive officer and chairman, or by having a balance between executive and non-executive directors;
- **Management**—appointing the chief executive officer and at least participating in the appointment of senior management, ensuring the motivation and protection of intellectual capital intrinsic to the corporation, ensuring that there is adequate training in the corporation for management and employees, and a succession plan for senior management;
- **Strategy**—determining the corporation’s purpose, values and strategy, and implementing its values in order to ensure that it survives and thrives, and ensuring that procedures and practices are in place that protect the corporation’s assets and reputation;
- **Monitoring**—monitoring and evaluating the implementation of strategies, policies, management performance criteria, and business plans;
- **Evaluation**—regularly reviewing processes and procedures to ensure the effectiveness of its internal systems of control, so that its decision-making capability and the accuracy of its reporting and financial results are maintained at a high level at all times; regularly assessing its performance and effectiveness as a whole; and that of the individual directors, including the chief executive officer;
- **Risk management**—identifying key business risk areas including technology and performance indicators of the business enterprise and monitoring these factors; and
- **Disclosure**—providing shareholders and markets with necessary and timely information material to the company’s performance and risks.

### 3. Relationships

The company will seek to develop and maintain strong relationships with its stakeholders and communicate effectively with them:

- **Customers**—recognizing the primacy of customers to business success; ensuring that product safety, effectiveness and value are maximized;
- **Shareholders**—recognizing shareholders as the primary stakeholder with a need for a good return on investment and growth in the medium term; understanding particularly the position of those with smaller shareholdings;
- **Employees**—respecting employees; treating them fairly and with cultural sensitivity; enabling them to develop their potential through skill and technology transfer; recognizing employees’ contribution to company success; recognizing international agreements on the right to freedom of association and collective bargaining; eliminating all forms of forced labor; and dealing with the problem of child labor;
- **Suppliers**—conducting relationships fairly; disseminating information on corporate citizenship to them; assisting them to achieve continued improvement against agreed codes of practice in areas such as health and safety, human rights in the workplace; and sharing knowledge, technology and ideas;

- **Local communities**—engaging in dialogue with relevant community representative organizations and seeking to contribute to long-term development;
- **Government**—engaging in open and constructive dialogue to improve the policy and practice environment for business and to assist government to foster corporate citizenship in the business community; and
- **Civil society**—engaging with civil society organizations on a basis of respect, and within a framework in which both sides are committed to be open, transparent, and accountable with respect to their financial and public support base.

#### 4. **Impact**

The company will assess and seek to minimise any potential adverse impacts on the environment and local communities:

- **Environment**—practicing and encouraging environmental responsibility and minimizing environmental footprint;
- **Consumer awareness and product impact**—raising awareness of consumers regarding contents, safe use, and disposal of products;
- **Building capacity**—working to build capacity in dealings with host, local, and national communities; and
- **Impact on other species**—recognizing and limiting negative impacts on other species.



Top Management Forum on Corporate Social Responsibility  
(27 February–4 March 2005, Tokyo, Japan)

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Reitaku University

Mr. Hideo Suzuki  
Director, Corporate Affairs Division  
Ministry of Economy, Trade and Industry

Mr. Hiroshi Hirano  
President and Chief Executive Officer  
Sompo Japan Insurance Inc.

Mr. Morio Ikeda  
President & CEO  
Shiseido Company, Limited

Mr. Makoto Wakita  
Managing Director  
Snow Brand Milk Products Co., Ltd.

Mr. Minoru Inaoka  
Managing Director  
Managing Executive Officer  
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Ms. Mariko Kawaguchi  
Senior Analyst

Managing Strategy Research Department  
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Mr. Arif Zaman  
Research Fellow  
Henley Management College and  
Adviser  
Commonwealth Business Council

Top Management Forum on Corporate Social Responsibility  
(27 February–4 March 2005, Tokyo, Japan)

**Program and Itinerary**

**Monday, 28 February 2005**

09:00–09:30      Opening Session

10:00–11:30      **Keynote Speech**  
“The Current Situations and Future Directions of Corporate Social Responsibility”  
by Iwao Taka, Reitaku University

11:45–12:45      **Special Speech**  
“Promotion Policies for Corporate Social Responsibility”  
by Hideo Suzuki, Director, Corporate Affairs Division, Ministry of Economy, Trade and Industry

14:00–15:30      **Session I**  
“CSR Management and Corporate Value”  
by Hiroshi Hirano, President and Chief Executive Officer, Sompo Japan Insurance Inc.

15:45–17:15      **Session II**  
“My Philosophy of Business and Corporate Social Responsibility”  
by Morio Ikeda, President & CEO, Shiseido Company, Limited

**Tuesday, 1 March 2005**

09:00–10:30      **Session III**  
“Building a ‘New Snow Brand Milk Products Co., Ltd.’  
—Goal to Establish Compliance Management”  
by Makoto Wakita, Managing Director, Snow Brand Milk Products Co., Ltd.

10:45–12:15      **Session IV**  
“Positive Prospects of the CSR Debate in Japan In Comparison with Europe and America”  
by Minoru Inaoka, Managing Director, Managing Executive Officer, Administration Division, Ito-Yokado Co., Ltd.

**<JPC's 50<sup>th</sup> Anniversary of Productivity Movement>**

- 12:30–13:30      **Commemorative Speech**  
“The Vision for the 21<sup>st</sup> Century and Productivity Movement for the Future”  
by Hiroshi Kato, President, Chiba University of Commerce
- 16:40–17:30      **Commemorative Speech**  
“Issues Tackled by Japan for the 21<sup>st</sup> Century”  
by Tadao Ando, Architect and Professor Emeritus of Tokyo University

**Wednesday, 2 March 2005**

- 09:30–11:00      **Session V**  
“Socially Responsible Investment in Japan”  
by Mariko Kawaguchi, Senior Analyst, Management Strategy Research Department, Daiwa Institute of Research Ltd.
- 11:30–13:00      Presentation on “Business Performance of the Company after Participating in the Program” by representatives from Indonesia
- 14:00–15:30      Group Discussion
- 15:30–17:00      Presentations of Group Discussion  
Summing-up Session
- 17:00–17:30      Closing Session

**Thursday, 3 March 2005**

- 10:00–12:00      Observational visit to Shiseido Company, Limited (Kamakura Factory)