The Evolution of Corporate Social Responsibility in Japan (Part 2)—How CSR "Swells" Have Impacted Corporate Values

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Introduction

The concept of corporate social responsibility (CSR) is not new in Japan. It first emerged 50 years ago, undergoing significant developments or "swells" in the 1970s and 2000s. This paper assesses the impact of the CSR swells on corporate management values, analyzes the three approaches of Japan's CSR, and touches on the "Japan Agenda."

Figure 1　Evolution of CSR in Japan

Stage 1 (1960s)
Industrial pollution triggers public distrust, evil corporate image
Civic movements arise, site-by-site response

Stage 2 (1970s)
Post-oil shock corporate profiteering is censured
Companies set up anti-pollution offices, and foundations for social contribution

Stage 3 (1980s)
Bubble economy heats up, land prices soar
Corporate citizens engage in philanthropy, Messena charities

Stage 4 (1990s)
Bubble collapses; corporate ethics and global environment issues arise
Keidanren drafts Corporate Behavior Charter, sets up global environment office

Stage 5 (2000s)
Corporate improprieties proliferate; stakeholders become prominent
Emergence of SRI funds, establishment of CSR organizations
2003 is called the "first year of the CSR management era"

Sources: NLI Research Institute

1. CSR Swells—the 1970s and 2000s

The swells of Japan's CSR coincide with major social developments causing social values to shift. This coincidence has occurred twice—in the 1970s, and since 2000. In both cases, corporate excesses caused serious damages that were criticized by the market and society.

1. The 1970s

Corporate excesses—As a result of the rapid economic growth of the 1960s, industrial pollution emerged as a serious and widespread problem across the country. In 1970, the government reluctantly set up a central office to deal with pollution. The problems were severe and fomented social unrest, as exemplified by an incident at the annual stockholders' meeting of Chisso Corporation in 1971, when security guards responded violently to protests by mercury poisoning victims.

Furthermore, land prices began surging against the backdrop of Prime Minister Kakuei Tanaka's plan to remodel the Japanese archipelago in 1972. Land speculation by companies and commodities speculation by trading companies became prominent social issues. Then in the first oil shock in 1973, price hikes by oil distributors prompted opportunistic price hikes by companies in other industries, fueling inflation in daily consumer goods. Corporate ethics came under scrutiny, with the Petroleum Association of Japan being investigated for violating the anti-monopoly law in 1974, and numerous product defects surfacing. Rampant inflation was intensively debated in the national Diet.

CSR evaluation standards—As criticism of corporate behavior escalated in the 1970s, numerous books and articles were published on the social responsibility of companies (the term CSR was not yet widespread). Several organizations proposed corporate evaluation standards and began to apply them. Below we describe three prominent examples (Figure 2).

In 1974, Nihon Keizai Shimbun issued "evaluation standards for corporate social responsibility," containing 70 minimum standards of corporate activity, and 30 standards of voluntary contribution. Along with financial indicators and compliance indicators, the standards are characterized by qualitative indicators that recognize the interests of stakeholders.

Also in 1974, the Japan Productivity Center issued "comprehensive social responsibility indicators," which rely on quantitative indicators as much as possible. Evaluation standards are grouped into three categories—management responsibility, employee welfare responsibility, and social responsibility narrowly defined—to three groups of stakeholders—shareholders, employees, and consumers, residents and business partners. In all, 42 indicators are evaluated.

Finally, in 1976 the Ministry of Trade and Industry developed an evaluation system from the perspective of management strength. Top management, organization, products, and management foundation are evaluated based on their impact on the local community, consumers and users, employees, and society.

Figure 2 CSR Evaluation Standards in the 1970s

Evaluation standards for corporate social responsibility (Nikkei, 1974)

① **Minimum standards of corporate profit**
Profitability, stability, and growth (financial indicators)

② **Minimum standards of employee welfare**
Workplace safety, living standards, work comfort, organizational flexibility, leisure time, labor relations

③ **Minimum standards of consumer welfare**
Stable supply, prices and fees, services and public relations, market trends

④ **Minimum standards of social responsibility**
Pollution & accidents, legal violation, consideration of the weak, geographic concentration, political ties

⑤ **Minimum standard of international cooperation**
Exports and imports, overseas activity

⑥ **Standards of social contribution**
Pollution policy, community contribution, consideration of the weak, policy to alleviate geographic concentration, disclosure, product development (energy & resource saving, and recycling), budgeting for initiatives, systematied social contributions, sustained charity donations, participationin management decisions by consumers & residents

⑦ **Standard of international contribution**
International cooperation, exports & imports

Comprehensive Social Responsibility Indicators (Japan Productivity Center, 1974)

① **Management responsibility indicators**
Profitability, safety, productivity, growth (financial indicators)

② **Employee welfare responsibility indicators**
Economic welfare: scheduled cash earnings, welfare expenses that are not legally prescribed, average retirement allowance, retirement age, income disparity of workers

Work environment: overtime, annual leave consumption, management participation, work accident rate

Living environment: floor space of company housing, maximum housing loan provided to employees, availability of post-retirement programs

Culture and education: education &training expenses, cultural & physical education expenses

③ **Narrowly defined social responsibility indicators**
For consumers: complaint processing system, external monitoring system by society, external advertisement monitoring system, compliance with anti-monopoly laws

For residential areas: waste disposal, pollution liaison agency, external pollution monitoring system, anti-pollution expenditures, participation in community

For business partners: rate of increase of subcontractor's unit price, use of written agreement with subcontractor, subcontractor payment period

For international operations

New Corporate Management Indicators (MITI 1976)

① **Local community**
Disclosure of wate materials, disaster preparedness, employment of local residents, anti-pollution facilities, improvement of local environment

② **Consumers and users**
Preventing excessive sales competition, advertisement monitoring, factory visits, safety checks, preventing opportunistic price hikes

③ **Employees**
Wage level, employees' welfare, recession countermeasures, mandatory retirement age, recruitment of female managers

④ **Society**
Value added, consideration of developing countries, consideration of subcontractors, employment of disabled, energy and resource savings

Source: Compiled from Mitsuo Morimoto, *Management Research on Corporate Social Responsibility* (1994).

Corporate response to CSR—While the global perspective of companies was not very strong 30 years ago, CSR evaluation was conducted with the same awareness of stakeholders as today. However, companies responded in ways that did not alter them fundamentally, but instead mainly set up anti-pollution offices and foundations to return some profits to society.

The 1970s saw an active debate drawing in economic organizations on applying CSR to corporate law in the Commercial Code. One side advocated drafting a general clause, while the other side sought a more restricted approach. Ultimately, neither side won—the matter was dismissed from serious debate on the grounds that the ambiguity and flexibility of CSR made it suspect as a legal concept.

2. The 2000s

During the so-called "lost decade" of the 1990s, large companies were frequently caught paying off *sokaiya* racketeers. But corporate scandals then took a turn for the worse in 2000. New developments pushed the CSR envelope: food poisoning at Snow Brand Milk Products, concealed product recalls at Mitsubishi Motor Company, and the bankruptcy filing at Sogo Department Store.

In 2002, insiders blew the whistle on a series of corporate scandals, including deceptive labeling of beef products at Snow Brand Foods and Nippon Ham, cover-up of nuclear power plant problems at Tokyo Electric Power. In 2003, Toyota Sales was caught leaking test problems on the mechanic's qualification test, and Nippon Television was caught bribing viewers to boost ratings. Then in 2004, Mitsui & Co. confessed it had lied about the performance of its top-selling diesel exhaust filter, while Seibu Railway was delisted for filing false reports on holdings of its shareholders. Meanwhile, in the U.S., failures in corporate governance were revealed at Enron at WorldCom, including illegal accounting practices and illegal compensation of executives.

CSR evaluation and CSR management—As scandals rocked the foundation of corporate trust, the pressing need for structural review of companies was recognized by economic organizations, financial institutions, institutional investors, auditors, NPOs and the government. In 2003, Ricoh led a vanguard of progressive companies in shifting to CSR management, launching the "first year of the CSR management era." Also around this time, evaluation organizations at home and abroad started to engage in SRI (socially responsible investment) in earnest. Below we look at the evaluation standards of Keizai Doyukai (Japan Association of Corporate Executives) and the Global Reporting Initiative (GRI), a third party NPO.

Figure 3 CSR Evaluation Standards in the 2000s

Keizai Doyukai (Corporate Evaluation Standards, 2003)	GRI Sustainability Reporting Guidelines (2002)
Corporate social responsibility (CSR) ① Market Sustained value creation and creation of new markets Providing value to customers Providing value to shareholders Free, fair and transparent business and competition Building trust of market ② Environment Establishment of environmental management system Reduction of environmental burden Disclosure and communications Building trust ③ People Employing and utilizing highly skilled and competent personnel Improving employability Creating a family-friendly work environment Creating a pleasant work environment ④ Society Promoting activites for contribution to society Disclosure and partnership Establishing proper relations with politics and government Cooperation with global community Building trust of society **Corporate governance (CG)** 1. Principles and leadership 2. Management systems 3. Compliance 4. Disclosure and communication	**Economic performance indicators** *Impacts on stakeholders and on economic systems:* customers, suppliers, emplyees, investors, public sector **Environmental performance indicators** *Impacts on living and non-living natural systems:* energy, materia and water use; biodiversity; waste generation and gas emissions; suppliers; products and services; legal compliance; environmental programs and expenditures; etc. **Social performance indicators** *Labor practices:* hiring, labor relations, health and safety, training & development, diversity, opportunity *Human rights:* strategy and management, anti-discrimination policy, freedom of collective bargaining, child labor, forced labor, imposed labor, disciplinary practices, security practices, rights of native inhabitants *Broader social issues:* community relations, bribery and corruption, political donations, competition and price setting *Product liability:* customers' health and safety, products and services, advertising, protection of privacy

Sources: Keizai Doyukai, *Corporate Social Responsibility (CSR) in Japan: Current Status and Future Challenges* (2003); Global Reporting Initiative, *Sustainability Reporting Guidelines* (2002).

In its *15th Corporate White Paper* (2003), Keizai Doyukai proposed a new corporate evaluation standard for CSR based on its vision for the 21st century society. To promote CSR management, a central feature of the standard is the introduction of a self-assessment tool, which companies use to mark their present status and set goals. CSR is separated into the categories of market, environment, people, society, and corporate governance.

The GRI's *Sustainability Reporting Guidelines 2002* consists of three parts: using the Guidelines, reporting principles, and report content. The report content includes five sections, including the company's vision and strategy, profile, governance structure and management systems, GRI content index (a cross-referenced table of the report's content), and performance indicators.

2. CSR Swells and the Impact on Corporate Management Values

Against the backdrop of changes in the environment surrounding companies, the basic values and principles underlying corporate management have started to shift. That is, a new CSR "swell" is causing corporate management values to change.

1. Transformation of Japan's Company-Centered System

Until recently, shareholders and other stakeholders had only a weak voice in corporate management. This is attributed to the way that social and economic institutions developed in the postwar era of high economic growth. To facilitate growth, stakeholders' interests were subsumed into the company's, so that their fate became one with the company. Since corporate growth was associated with social prosperity, the company's primacy was blindly accepted. As a result, no mechanisms were constructed for stakeholders to independently monitor corporate management.

But since around 2000, this arrangement started to change as stakeholders of all types grew in influence. Shareholders are playing a larger role in financing, led by foreign shareholders (buying unwound cross-shareholdings), while pension funds are speaking out. As traditional employment practices crumble and labor moves about more freely, employees are rethinking their relationship with companies. Consumers are starting to look not only at price but at environmental and safety considerations when purchasing goods. Market competition is forcing companies to review keiretsu relationships and actively engage in green purchasing. Communities are starting to collaborate with companies as residents increase awareness and seek diverse lifestyles.

2. Global Community Recognizes Common Issues

In the 1990s, the global environment and economic globalization became prominent issues. As Japanese companies moved into Asian markets, they created conditions requiring a more global perspective in overseas operations and corporate management. Specifically, corporate activity was aggravating a broad range of problems, including global warming and destruction of the ecology, economic gap between industrialized and developing economies, human rights, and destruction of local communities. In response, domestic and foreign NGOs and NPOs, as well as international organizations expanded their activities.

The 1992 Earth Summit in Rio de Janeiro and 2002 Johannesburg Summit significantly expanded the expected role of (large) companies. Recognizing the importance of CSR, they called on companies to play a more prominent role in solving local and global issues by partnering with government and civic sectors. From the late 1990s, CSR also took center stage at the Davos Conference, where companies and executives were called on to commit themselves to a sustainable global community by addressing issues such as the global environment, north-south issue, poverty, and human rights.

3. Achieving Economic and Social Functions

Under CSR, companies are expected to perform economic functions (producing and allocating economic value according to laws and market forces) and social functions (implementing voluntary initiatives to contribute to society). In the past, people debated whether CSR should be limited to economic functions (maximizing shareholder value), or should also include social functions (contributing to society). While the latter position now prevails, the former position still commands a strong following.

However, considering two irreversible trends in the environment surrounding companies—globalization and the rising influence of stakeholders—corporate values have shifted to accept the importance of both social and economic functions as a self-evident axiom.

3. Three Approaches of Japan's CSR

CSR can be complex and difficult to understand because it comprises a variety of perspectives and also means different things to different people at different times. However, by tracing their origins, we find that several different approaches merged simultaneously to form CSR in contemporary Japan. Below we examine the three approaches, which are based on corporate ethics, stakeholders, and sustainability (Figure 4).

1. Corporate Ethics Approach

As explained above, when corporate scandals led to bankruptcies and poor performance after 2000, it raised alarms and raised the imperative of establishing better corporate ethics. As long as companies exist, corporate ethics will always be an issue affecting not only risk management, but compliance and corporate governance.

Focusing on corporate sustainability, this approach puts corporate ethics at the center of CSR, and seeks effective strategy formulation and implementation. Corporate ethics, of course, includes the problem Japanese companies are notorious for—concealment and secrecy.

2. Stakeholder Approach

In Japan's company-centered economy and society, companies were able to coerce stakeholders to put the company's interests first and foremost. Companies thus largely neglected investor relations, and did little to fill the information gap with consumers. Large companies offered long-term employment, and in return demanded loyalty from employees. They also held suppliers and contractors captive in the pyramid-shaped keiretsu structure.

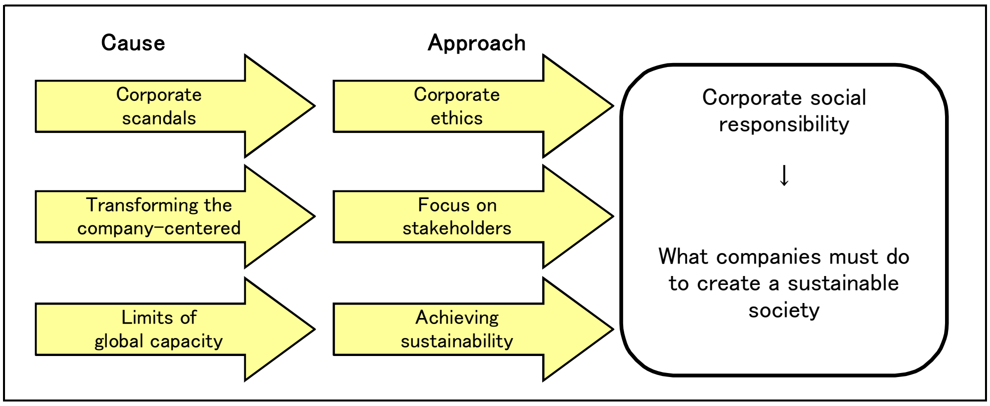
However, the corporate scandals revealed that moral problems among executives and employees and the corporate culture were at fault. To correct these problems and reestablish trust, accountability to stakeholders and transparency and fairness (disclosure) were perceived as essential. Meanwhile, the status of stakeholders who are social minorities in the corporate society—women, part-timers, the elderly, disabled, and foreigners—has gradually risen.

3. Sustainability Approach

Sustainability at the global level addresses two issues—the global environment and ecology, and global community. Indeed, the term sustainability itself derives from the biological sciences. As the limits of the earth's capacity become clear, the CSR debate has transcended individual societies and focused on how companies should act with respect to the global environment and ecology.

The sustainability argument originated in the Club of Rome in 1972 (*Limits to Growth*), which predicted the predicament of mankind with numerical predictions for energy depletion, environmental pollution, population explosion, and food shortage. Then in 1984, the UN World Commission on Environment and Development issued a report (*Our Common Future*) proposing a new concept called sustainable development. To satisfy the demands of both present and future generations, sustainable development requires an economic system that balances environmental and social needs.

Figure 4 Three Approaches of Japan's CSR



Source: NLI Research Institute

In the late 1990s, sustainability gained further acceptance against the backdrop of globalization. With their growing social impact, companies are expected to contribute more to constructing a global community that balances environmental, social and economic needs. This includes addressing issues such as human rights protection in the workplace, social fairness, slum revival, and development aid to reduce economic disparities and poverty.

Stated differently, this approach seeks to eradicate factors impeding the sustainability of the global ecology and community. It is an approach that Japanese companies find particularly difficult to adopt.

4. Implementation Issues of Japan's CSR

We have described how three approaches have merged in Japan's CSR, each representing an important aspect of CSR. When implementing CSR management, companies need to determine which to prioritize depending on their characteristics and situation.

Finally, the implementation issues of Japan's CSR can be divided into a global agenda and local agenda. The global agenda primarily involves issues to ensure sustainability of the global environment and ecology and global community, as described above.

On the other hand, the local or "Japan agenda" refers to implementation issues for companies in addressing problems peculiar to Japanese society. The structure is essentially the same as that of the EU local agenda, where CSR is used as a tool to promote the goals of economic and social cohesion. However, we leave this matter for discussion in a future paper.