

**COMPREHENSIVE SUPERVISORY GUIDELINES
FOR
FINANCIAL INSTRUMENTS FIRMS, ETC.**

The Financial Services Agency September 30, 2007;
Partially amended on July 3, 2009; 4 March 2010; 31 March 2010; April 16, 2010; August 4, 2010;
September 22, 2010; September 27, 2010; and March 18, 2011.

I. Fundamental Concept

I-1 Fundamental concept for supervision over financial instruments firms, etc.

I-1-1 Purposes to supervise financial instruments firms, etc. and role of supervisory division

A fair and efficient financial instruments market is the major premise for investors' active investment management of assets and corporations' smooth financing, and financial instruments firms, etc. (which mean financial instruments firms and registered financial institutions; hereinafter the same) play important roles as intermediaries of such financial instruments market.

The purposes to supervise financial instruments firms, etc. shall be to ensure sound and appropriate management of businesses of persons carrying out financial instruments business, fair issuance of securities and transactions, etc. of financial instruments, etc., smoothen distribution of securities and promote fair price formation, etc. of financial instruments, etc. by means of fulfillment of function of the capital market through appropriate fulfillment of market intermediary function, so as to contribute to the sound development of the national economy and the protection of investors.

The proper combination of "on-site" monitoring conducted by the inspection division (which means the administration bureau of the Securities and Exchange Surveillance Commission and the inspection bureau of the Financial Services Agency, etc.; hereinafter the same) and "off-site" monitoring conducted by the supervisory division is necessary for effective supervision, and each of the two divisions are required to fulfill respective functions accurately under the proper coordination between the two divisions in order to achieve highly effective financial supervision.

Within the above framework, the role of the supervisory division is to conduct continuous collection and analysis of information and discover such problems related to business soundness or appropriateness of financial instruments firms, etc. at an early stage even during the inter-inspection period as well as to take supervisory measures such as administrative dispositions when needed, so as to encourage improvement prior to the escalation of problems.

In concrete terms, the supervisory division's important role can be to require financial instruments firms, etc. to comply with various laws and regulations, etc. thoroughly including measures for the protection of investors, etc. and to recognize business conditions of financial instruments firms, etc. properly through periodical and continuous exchange of opinions with financial instruments firms, etc. as well as to accumulate and analyze various information provided by financial instruments firms, etc. and to encourage voluntary efforts toward the sound management of business.

Particularly, the supervisory division is positioned to know not only conditions of each financial instruments firm, etc. but also overall conditions of financial instruments firms, etc. widely. It is, therefore, important to recognize the industry-wide situation of the financial instruments firm, etc. concerned accurately based on the analysis of comparison with other financial instruments firms, etc. and to encourage the improvement of problems through giving back of the result of such analysis to, and holding a hearing for, such financial instruments firm, etc.

* This English version is a translation of the original Japanese text. The original Japanese text will prevail should there be any difference in meaning between the English and Japanese versions.

I-1-2 Fundamental concept in supervising financial instruments firms, etc.

Based on the above, the fundamental concept in supervising financial instruments firms, etc. is as follows.

(1) Ensuring appropriate coordination with the inspection division

It is important to ensure the appropriate coordination between the supervisory division and the inspection division while paying respects to the independency of each division, and to combine on-site monitoring and off-site monitoring properly in order to achieve highly effective supervision over financial instruments firms, etc. Therefore, the supervisory division shall promote the coordination with the inspection division with the following remarks.

- ① With respect to problems found through inspections, the supervisory division shall ensure the follow-up of improvement of such problems in order to lead it to the complete solution. The supervisory division shall take supervisory measures such as administrative dispositions in a strictly fair manner when needed.
- ② The supervisory division shall give information of problems found through off-site monitoring to the inspection division for the utilization in the next inspection.

(2) Ensuring thorough communication with financial instruments firms, etc.

It is important, in supervising financial instruments firms, etc., for the supervisory division to recognize and analyze information of business management of financial instruments firms, etc. accurately and, when needed, lead it to the timely and proper supervisory response. Therefore, it is necessary for the supervisory division to collect information actively on a routine basis through thorough communication, etc. in addition to reports made by financial instruments firms, etc. In concrete terms, it is necessary to make an effort to keep every day communication with a financial instruments firm, etc. and recognize various information of not only financial conditions but also business management through periodical exchange of opinions with financial instruments firms, etc.

(3) Respect to voluntary efforts by financial instruments firms, etc.

The supervisory authority is positioned to verify, based on the laws and regulations, etc., the management judgment made by financial instruments firms, etc., which are private corporations, conforming the principles of self-responsibility and to encourage improvement of problems. In supervising financial instruments firms, etc., the supervisory authority shall, based on the above position, pay respects to voluntary efforts by financial instruments firms, etc. for business management.

(4) Ensuring efficient and effective supervision

The supervision must be conducted efficiently and effectively in light of effective utilization of limited resources of the supervisory authority and financial instruments firms, etc. Accordingly, the supervisory authority shall make an effort to improve the efficiency by, in the case of requiring financial instruments firms, etc. to make a report or provide information, limiting such report or information that is truly necessary for the supervision, and always check the necessity, method, etc. for the current supervision and improve it when needed.

Further, the supervisory authority shall, as financial instruments firms, etc. diversify businesses, make an effort to carry out supervisions appropriate for type of business. With respect to a financial instruments firm group (which means a group as defined in IV-5) having international activity, particularly, it is necessary to supervise in views stated in the Financial Conglomerate Supervisory Guidelines in addition to the supervision over the sole financial instruments firm.

In addition, with respect to supervising financial instruments firms, etc., a financial instruments firms association (which means approved financial instruments firms association or recognized financial instruments firms association; hereinafter the same) and financial instruments exchange which are self-regulatory organizations under the Financial Instruments and Exchange Act (hereinafter referred to as "F.I. Act") have self-regulatory functions through self-regulating financial instruments firms, etc. as professionals of the markets to gain the trust of investors. The supervisory authority shall, therefore, cooperate with self-regulatory organizations closely on supervision.

I-2 Purposes for preparation of supervisory guidelines

I-2-1 Purposes for preparation of supervisory guidelines

Acceleration of shifting from too heavily weighted indirect financing to direct financing or market-type indirect financing, so-called flight "from saving to investment," is an important agenda for sustainable development of Japan's economy. Such acceleration of shifting is considered to contribute to the stabilization of Japan's financial system, establishment of a market attractive to domestic and foreign investors, growth of corporations and development of economy through mainly the following four routes.

- ① Establishment of a financial system having persistent and sophisticated risk sharing ability by means of changing to the structure that many market participants widely bear risks according to their abilities (prevention of vulnerability of the financial system arising from concentration of risks into indirect financing).
- ② Smoothing of supply of risk money and acceleration of innovation by corporations.
- ③ Enhancing efficiency of capital and improvement of profitability of corporations in Japan by means of shifting of money from saving financing to investment financing and establishment of a market having the depth to enable to observe managements of corporations.
- ④ Establishment of varied and wealthy society in the society with falling birth rate and aging population by means of proving investors with various investment vehicles.

In order to achieve the above-mentioned goal, it is necessary for financial instruments firms, etc. to gain nation's trust as well as for the financial administrator to design appropriate system and to give financial instruments firms, etc. motivation appropriately to strengthen their governance with the conscious of the protection of investors and appropriate risk control.

Looking back to the history of reforming the financial and capital market in Japan, various measures have been taken to vitalize securities markets such as facilitation of entry into securities business and liberalization of business, diversification of providers of securities service since financial system reform in 1998 which was campaigned by the words of free, fair and global. It has begun to result in the achievement of diversified financial instruments and sales channels and further the development of a change in circumstances of securities businesses, etc. and internationalization of financial and capital markets.

Despite of such achievement or development, the protection of users, user-friendliness and trust-worthiness of markets in Japan have remained to be the important agenda. In the cases, for example, where retail customers suffer damages because of fraudulent sale, etc. of financial instruments which are not subject to regulations, systematic measures have been taken by means of individual expansion of investor protection measures such as amendment to the Financial Futures Trading Law to introduce regulations into foreign exchange margin transactions (enforced in July 2005).

In such circumstances, the reformation of the Securities and Exchange Law into the Financial Instruments and Exchange Act (enforced in 30 September 2007) aims to accelerate financial innovation to develop further the achievement of the previous reforms and to promote appropriate protection of users by means of implementation of cross-sectional and comprehensive rules for the protection of investors.

From now on, accurate supervisory responses to financial instruments firms, etc. which are diversifying businesses are required in order to take advantage of the achievement of the past reforms and accelerate the flight "from saving to investment" under such cross-sectional legal framework.

Under such circumstances, the authority has reorganized systematically supervisory guidelines and administrative guidelines used to be prepared for each type of business and arranged supervisory concept, focus points, remarks and concrete supervisory methods for financial instruments firms, etc. comprehensively and cross-sectionally in order to carry out daily supervisory operations.

These Supervisory Guidelines were prepared based on the current situation of financial instruments firms, etc. in order to respond to various cases, and therefore do not require each financial instruments firm, etc. to comply with all supervising valuation items listed in these Supervisory Guidelines in a single uniform way.

Therefore, these Supervisory Guidelines shall be applied with the remarks that the failure of literal satisfaction of each valuation item is not always referred as inappropriate unless there is a problem in the public interests or to protect investors and in consideration to avoid mechanical or uniform operation.

Even if, on the other hand, valuation items are formally conformed, there could be cases where it is not always sufficient in the public interest and to protect investors, etc.

Each local finance bureau (including Fukuoka Finance Bureau and Okinawa General Bureau; hereinafter the same) shall conduct supervision over financial instruments firms, etc. over which

the local finance bureau has the jurisdiction based on these Supervisory Guidelines, and the same applies to the division in charge in the Financial Services Agency. "Comprehensive Supervisory Guidelines for Securities Companies," "Comprehensive Supervisory Guidelines for Financial Futures Firms," "Administrative Guidelines (Remarks in Supervision, etc. over Investment Trust Management Firms and Investment Corporations, etc. and Securities Investment Advisory Firms, etc.)," "10. Trust Beneficial Interest Sales Business" of "Comprehensive Supervisory Guidelines for Trust Companies, etc.," "6. Commodity Fund Business" of "Remarks in Financial Supervision, etc. (Administrative Guidelines) Part 3: Finance Companies" shall be repealed, following the preparation of these Supervisory Guidelines.

I-2-2 Composition of these Supervisory Guidelines

These Supervisory Guidelines are prepared with the intention to be comprehensive for the use of the supervision of various financial instruments firms, etc. and to lessen duplication.

For the above purpose, "I. Fundamental Concept" and "II. Remarks on Administration in Supervising Financial Instruments Firms, etc." shall in principle cover financial instruments firms (persons engaged in the first-type financial instruments business, in the second-type financial instruments business, investment management business or investment advisory and agent business) or registered financial institutions and intend to include persons carrying out eligible institutional investors, etc. business subject to special provisions, foreign securities firms, financial instruments intermediary firms, securities finance companies, investment corporations and commodity investment sales firms.

"Supervisory valuation items and procedures" following thereto contains supervisory remarks common to financial instruments firms as "III. Common Part" and the further following "IV" to "VII" contain additional remarks specific to each type of firms.

Accordingly, a person who supervises such financial instruments firms, etc. shall refer to the following tables and refer first to "III Common Part" and further refer to "IV" to "VII" which contain remarks specific to the type of firms according to the types of firms subject to the supervision.

Further, the authority shall refer to the part "VIII" or thereafter, because such part contains supervisory valuation items and procedures for registered financial institutions, persons carrying out eligible institutional investors, etc. business subject to special provisions, foreign securities firms, financial instruments intermediary firms and securities finance companies in the forms to apply the first-mentioned part respectively.

(Reference) Comprehensive supervisory guidelines for financial instruments firms, etc. (Table)

Firms	Financial instruments firm				Registered financial institution	Special provisions business	Foreign securities firm	Financial instruments intermediary firm	Securities finance company
	First-type business	Second-type business	Investment management business	Advisory and agent business					
Items of Supervisory Guidelines									
I. Fundamental Concept	○	○	○	○	○	○	○	○	○
II. Remarks on Administration in Supervising Financial Instruments Firms, etc.	○	○	○	○	○	○	○	○	○
III. Supervisory Valuation Items and Procedures (Common Part)									

Valuation items (common part)	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>						
Procedures (common part)	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>						
IV. Supervisory Valuation Items and Procedures (First-Type Financial Instruments Business)										
Valuation items (first-type financial instruments business)	<input type="radio"/>									
Procedures (first-type financial instruments business)	<input type="radio"/>									
V. Supervisory Valuation Items and Procedures (Second-Type Financial Instruments Business)										
Valuation items (second-type financial instruments business)		<input type="radio"/>								
Procedures (second-type financial instruments business)		<input type="radio"/>								
VI. Supervisory Valuation Items and Procedures (Investment Management Business)										
Valuation items (investment management business)			<input type="radio"/>							
Procedures (investment management business)			<input type="radio"/>							
VII. Supervisory Valuation Items and Procedures (Investment Advisory and Agent Business)										
Valuation items (investment advisory and agent business)				<input type="radio"/>						
Procedures (investment advisory and agent business)				<input type="radio"/>						
VIII. Supervisory Valuation Items and Procedures (Registered Financial Institution)										
Valuation items (registered financial institution)					<input type="radio"/>					
Procedures (registered financial institution)					<input type="radio"/>					
IX. Supervisory Valuation Items and Procedures (Eligible Institutional Investors, etc. Subject to Special Provisions Business)										
Valuation items (eligible institutional investors, etc. subject to special provisions business)						<input type="radio"/>				
Procedures (eligible institutional investors, etc. subject to special provisions business)						<input type="radio"/>				
X. Supervisory Valuation Items and Procedures (Foreign Securities Firm)										
Valuation items (foreign securities firm)							<input type="radio"/>			
Procedures (foreign securities firm)							<input type="radio"/>			
XI. Supervisory Valuation Items and Procedures (Financial Instruments Intermediary Firm)										
Valuation items (financial instruments intermediary firm)								<input type="radio"/>		
Procedures (financial instruments intermediary firm)								<input type="radio"/>		
XII. Supervisory Valuation Items and Procedures (Securities Finance Company)										
Valuation items (securities finance company)									<input type="radio"/>	
Procedures (securities finance company)									<input type="radio"/>	

II. Remarks on Administration in Supervising Financial Instruments Firms, etc.

II-1 General administration

II-1-1 General supervisory administration

- (1) Determination and publication of matters to be emphasized in the supervision during the operational year

The authority shall determine and publish policies of supervision for a new operational year at the beginning of the operational year in order to clarify matters to be emphasized in the supervision,

- (2) Periodical hearings

The authority shall hold the following hearings for financial instruments firms periodically as part of off-site monitoring.

The authority shall make an effort to conduct efficient and effective monitoring with originality and ingenuity, because periodical hearings may not fit to some type of business, considering necessity of supervision and efficiency of supervisory operation.

- ① Account closing hearing

The authority shall hold hearings for account closing and financial issues, etc. for each interim or quarterly period.

In holding each hearing, the authority shall make an effort to make it efficiently by means such as selecting a firm to be heard according to financial condition, business, etc. of financial instruments firms.

- ② Comprehensive hearing

The authority shall, based on the state of account closing, etc. of a financial instruments firm, hold a hearing on management strategies and policies for business development, control system of various risks and revenues, construction of governance, etc. of the firm. Executive officials of the supervisory division shall hold a top hearing for the management team of a financial instruments firm, when needed.

- (3) When needed monitoring

The authority shall hold when needed hearings including top hearing for the management of a financial instruments firm as part of off-site monitoring if such hearing is required for supervision such as when business performance or business strategy has been changed, economic circumstances such as interest rates or asset prices have been changed or a problem of the protection of investors has arisen or events to raise concerns on sound business or appropriate management of business of a financial instruments firm have occurred.

- (4) Submission of monitoring survey sheet

- ① The authority shall require a financial instruments firm, etc. to submit a monitoring survey sheet under Article 56-2.1 of the F.I. Act regarding the following matters as part of off-site monitoring.

- ② When the director-general of a local finance bureau (including the director of Fukuoka Finance Branch and the director of Okinawa General Bureau; hereinafter the same) has received the following monitoring survey sheets, the director-general of the local finance bureau shall conduct operations related to the off-site monitoring report based on instruction by the Commissioner of the Supervisory Bureau of the Financial Services Agency. The director-general of the local finance bureau shall coordinate with the division in charge of the Financial Services Agency to conduct operations:

[Monitoring persons carrying out the first-type financial instruments business]

- ① capital requirement ratio;
- ② business and accounting;
- ③ segregation of customers' properties;.
- ④ market risk;
- ⑤ counterparty risk;
- ⑥ operational risk; and
- ⑦ liquidity risk.

[Monitoring persons engaged in public offer, etc. (for each fund)]

- ① the name of the fund;
- ② classification of the firm;
- ③ handling business;
- ④ type of funds;.

- ⑤ matters regarding investment management period;
- ⑥ type of sale;
- ⑦ matters regarding interest holder (which means a person holding the interest referred to in (5) or (6) of Article 2.2 of the F.I. Act; in II-1-1 (4) and IX-1-2, the same);
- ⑧ the amount of public offer, etc. during the latest one year;
- ⑨ matters regarding the amount of properties under investment management;
- ⑩ matters regarding the amount of net assets;.
- ⑪ matters regarding classification of instruments;
- ⑫ matters regarding object of investment;

(Note) "Person engaged in public offer, etc. of funds" who is required to submit a monitoring survey sheet shall be:

- a person who conducts public offer or private placement as a business for certificates of a beneficial interest of trusting person directing type investment trust as defined in Article 2.1 of the Law on Investment Trust and Investment Corporation (hereinafter referred to as "Investment Trust Law" among beneficial interests of investment trusts as defined in Article 2.1 (10) of the F.I. Act (excluding the matters under ⑦, ⑨~⑫);
- a person who handles public offer or handles private placement as a business for beneficial certificate of investment trust as defined in Article 2.1 (10) of the F.I. Act and investment certificate as defined in Article 2.1 (11) of the F.I. Act (excluding the matters under ⑦, ⑨~⑫);
- a person who handles public offer or handles private placement as a business for certificates similar to investment certificates issued by a foreign investment corporation among beneficial certificate of foreign investment trust as defined in Article 2.1 (10) of the F.I. Act and foreign investment certificate as defined in Article 2.1 (11) of the F.I. Act (excluding the matters under ⑦, and with respect to ⑨~⑫, in the case where an acting association member as provided in Article 21.3 of the Japan Securities Dealers Association rules "Rules for Transactions of Foreign Securities") is appointed, limited to such acting association member;
- a person who conducts public offer or private placement as a business for the interests referred to in (5) or (6) of Article 2.2 of the F.I. Act;
- a person who handles public offer or handles private placement as a business for the interests referred to in (5) or (6) of Article 2.2 of the F.I. Act.

[Monitoring persons engaged in investment management of funds (for each fund)]

- ① the name of the fund;
- ② classification of the firm;
- ③ handling business;
- ④ type of funds;.
- ⑤ matters regarding investment management period;
- ⑥ matters regarding interest holders;
- ⑦ matters regarding the amount of properties under investment management;
- ⑧ matters regarding the amount of net assets;.
- ⑨ matters regarding classification of instruments;
- ⑩ matters regarding object of investment;

(Note1) "Person engaged in investment management of funds" who is required to submit a monitoring survey sheet shall be:

- a person who enters into the contract referred to in Article 2.8 (12) (a) of the F.I. Act and conducts as a business investment management (including the direction thereof) of money or other properties as an investment in interests in securities or derivatives transactions based on the investment judgment based on analysis of value, etc. of financial instruments under such contract;
- a person who perform as a business the act referred to in Article 2.8 (14) of the F.I. Act;
- a person who conducts as a business investment management of money or other properties contributed by a person who holds the interest referred to in Article 2.8 (15) (c) of the F.I. Act as an investment in mainly interests in securities or derivatives transaction based on the investment judgment based on analysis of value, etc. of financial instruments;
- a person who files a notification under Article 16.1 (10) (e) of the Cabinet Office Ordinance on Definition as Defined in Article 2 of the Financial Instruments and Exchange At ("Definition Ordinance");

(Note2) It shall be noted that business carried out by financial institutions approved under Article 1.1 of the Law on Trust Business by Financial Institution as Other Business

Engagement (financial institution engaging in trust business), which concerns the business to perform the acts referred to in (14) and (15) of Article 2.8 of the F.I. Act (limited to holding money or other properties provided in these provisions as trust properties to perform such act) shall not be subject to monitoring survey sheet.

(5) Remarks on public notice for administrative dispositions

A public notice of administrative dispositions under Article 54-2 of the F.I. Act shall state:

- ① the name or trade name;
- ② the location of the principal business office, etc.;

(Note) The principal business office, etc. means the principal business office or other type of office (in the case of a foreign juridical person or an individual residing in a foreign jurisdiction, the principal business office or other type of office in Japan; hereinafter the same).

- ③ the registration number;
- ④ the date of registration;
- ⑤ the date of the administrative disposition; and
- ⑥ the details of the administrative disposition.

(6) Recognition of real state related to unregistered firms, etc. or persons who use similar trade names

When the authority has found a person who is suspected to carry out financial instruments business, etc. without registration or notification or a person who uses a name or trade name which may cause false impression that such person were a financial instruments firm through grievances from investors, enquiries from investigative authorities, information from financial instruments firms or financial instruments firms association, etc. or advertisement on news papers or website, etc., the authority shall make an effort to recognize the real state positively by means of referring to the police or local consumer centers, etc. or confirming the firm directly by telephone.

Particularly when there have been grievances, etc. from investors or enquiries from investigative authorities, the authority shall not limit the action only to the response thereto.

(7) Responses to unregistered firms, etc.

When the authority has obtained information of unregistered firms, etc., the authority shall make an effort to make the following responses to prevent expansion of damages:

The same responses shall be made to a person who carries out eligible institutional investors, etc. business subject to special provisions without notification:

① Receipt of grievances, etc.

When the authority has received information of a person who carries out financial instruments business without registration from investors, etc., the authority shall respond as follows after hearing on the details as much as possible (such as the name of the firm, the location, the name of the representative, the telephone number, business activities, the name of the provider of the information, whether the information can be reported to investigative authorities, etc.).

- (a) When the authority has received information of unregistered firm which has the head office in a place where an other local finance bureau has the jurisdiction, the authority shall convey the information to such local finance bureau after hearing on the information (such local finance bureau to which the information was conveyed shall make response in principle after the information was conveyed).
- (b) In the case of a firm whose contact place is unknown, the authority shall make an effort to collect further information.
- (c) When an information provider requests not to report to the firm or other organization, the authority shall handle with remarks not to cause disbenefit to the information provider.
- (d) If a firm is suspected to carry out business without registration, the authority shall suggest the information provider to provide information to investigative authorities.
- (e) The authority shall prepare "Ledger (Form II-6)" and record the details of grievances and enquiries from investors, instruction by the authority to the firm and responses by the firm, etc. in the order of timings.

② The case where likeliness of carrying out business without registration has been found

In the case of a firm the name and contact place of which is known and the business activities of which are known to some extent based on information received directly or information, etc. provided by an other division of the Financial Services Agency, the authority shall make an effort to recognize the real state by means of telephoning to the firm or by other means, and, in the case where as a result of such effort, it has been found that the firm likely

carries out financial instruments business without registration (including the case of inability to communicate because of absence, etc.), the authority shall issue documents made on Form II-5 and make the following responses.

- (a) If the firm has no intention or malice to carry out business without registration and the firm does not constitute a failure of the protection of investors, the authority shall require the firm to register immediately.
- (b) If the firm has intention or malice to carry out business without registration and otherwise it is deemed necessary for the protection of investors, the authority shall inform it to investigative authorities and warn in writing by Supervisory Guidelines Form II-4 to require halting such act.

If, without issuing documents made on Form II-5, it is clear that the firm carries out financial instruments business without registration, the authority shall issue warning by documents made on Form II-4.

- ③ The case where a person does not correct despite of warning
If a person does not correct despite of the warning by Form II-4, the authority shall accuse such person to investigative authorities when needed.

- ④ Report to the Financial Services Agency

The director-general of a local finance bureau who has taken measures of "warning" or "accusation" shall promptly send a copy of the "ledger," "warning documents," etc. to the Commissioner of the Financial Services Agency. Upon the receipt of the report, the Financial Services Agency shall publish the name, etc. of the person to whom the warning was made on the website of the Financial Services Agency.

(Note) If a response to unregistered firm, etc. causes interference to investigation of the investigative authority, such case shall be excluded. It shall be noted that enquiry whether registered or not for such firm from the investigative authority shall not be judged to mean the case of interference to investigation of the investigative authority.

- (8) Responses to firms which use similar trade names

- ① With respect to a person who obviously uses similar trade name (fore example, "○○ Securities," "○○ △ type of financial instruments firm," "○○ Investment Corporation," etc.), the authority shall warn by documents made on Form II-1 and make a direct contact by means of telephone or interview to require correction. The authority shall communicate with investigative authorities and exchange information.

- ② With respect to a person who uses a trade name similar in appearance to a financial instruments firm (Note), the authority shall warn by documents made on Form II-2 and investigate the business by means of referring to the police and local consumer center, etc., confirmation by direct telephoning, etc.

Except for the case where the business of such firm is clearly different from a financial instruments firm as a result of the investigation, the authority shall warn again by documents made on Form II-3 and contact by telephone or interview, etc. directly to require correction.

- ③ If such person does not correct despite of the warning by Form II-1 and II-3, the authority shall accuse such person to investigative authorities when needed.

- ④ When the director-general of a local finance bureau has taken the measures of ① to ③, the director-general shall report the name of the firm, the name of the representative, the location of a business office, etc., the type and scale of business to the Commissioner of the Services Agency immediately. Upon the receipt of the report, the Financial Services Agency shall publish the name, etc. of the person to whom the warning was made on the website of the Financial Services Agency.

- ⑤ The director-general of a local finance bureau shall prepare "Ledger (Form II-6)" for a user of the similar trade name, etc. and record the details of grievances and enquiries from investors concerning such firm, instruction by the authority to the firm and responses by the firm, etc. in the order of timings.

(Note) "Examples of trade names which may give false impression as financial instruments firms"

A financial instruments firm registered under Article 28 of the former Securities and Exchange Act as at the time of the enforcement of the F.I. Act (deemed registered first-type of financial instruments firm) and a financial instruments firm engaged in securities related business after the enforcement of the F.I. Act may use the word "Securities" for its trade name. A person using a trade name similar to such financial instruments firm which uses the word or letter "Securities" in the trade name (hereinafter referred to as "special provision securities firm, etc.") shall be reviewed individually depending on the existence of "likeness of giving false impression to be a special provision securities firm, etc." The followings are examples of the

use.

- (a) A trade name in which the word "Securities" and other words are combined and which gives false impression to be a special provisions securities firm, etc.

Examples:

○○ Securities Transaction, ○○ Securities Trade, ○○ Securities Brokerage, ○○ Securities Investment, ○○ Securities Commercial, ○○ Securities Money, ○○ Securities Management, ○○ Securities Intermediary, ○○ Securities Agent

However, the trade name "○○ Securities Printing" which is obviously different from special provisions securities firm, etc. shall be excluded.

- (b) A trade name in which the word "Securities" is not used but which gives false impression to be a special provisions securities firm, etc.

Examples:

○○ Stock Management, ○○ Stock Investment, ○○ Stock Brokerage, ○○ Stock Trade, ○○ Stock Transaction, ○○ Stock Agent (same for debt securities), ○○ Financial Instruments Transaction

II-1-2 Coordination between supervisory divisions

- (1) Coordination between Financial Services Agency and Local Finance Bureau

It is necessary for the Financial Services Agency and local finance bureaus to exchange information which is regarded as necessary for the supervision over financial instruments firms, etc. appropriately and share the information of the existence of risks and common awareness of the issues. Both of the Financial Services Agency and local finance bureaus shall make an effort to enhance coordination such as providing information timely and properly or objective exchange of opinions for information, etc. other than discussion, etc. related to internally delegated operations referred to in II-1-5. When a local finance bureau which has found unpublished existence of risks or problems, etc. about a financial instruments firm, etc. under the jurisdiction of other local finance bureau shall give such information to such other local finance bureau or the Financial Services Agency and make an effort to enhance coordination.

- (2) Communication with competent director-general of local finance bureau, etc.

- ① When the Commissioner of the Financial Services Agency or the director-general of a local finance bureau has accepted a notification of establishment, change of location, change of name, closure, halting or resumption of business in respect of a business office of a financial instruments firm in the area under the jurisdiction of the director-general of other local financial bureau, the Commission or the first-mentioned director-general shall send a copy thereof to such director-general of other local finance bureau having the jurisdiction over the location of such business office.
- ② When the Commissioner of the Financial Services Agency or the director-general of a local finance bureau has made a disposition under Articles 51 to 54 of the F.I. Act to a business office, located in the jurisdiction of the director-general of other local finance bureau, of a financial instruments firm, etc. under the jurisdiction of the Commissioner or the first-mentioned director-general, the Commissioner or the first-mentioned director-general shall report the details of the disposition to such director-general of other local finance bureau having the jurisdiction over the location of such business office immediately.
- ③ When the director-general of a local finance bureau has accepted a notification under Article 32 of the F.I. Act from a major shareholder of a financial instruments firm under the jurisdiction of the Commissioner of the Financial Services Agency or the director-general of other local finance bureau, the first mentioned director-general shall send the original of the notification to the Commissioner of the Financial Services Agency or such director-general of other local finance bureau. The same treatment shall be made in the case of accepting a notification under Article 32-3 of the F.I. Act.
- ④ When the Commissioner of the Financial Services Agency or the director-general of a local finance bureau has issued an order under Article 32-2 of the F.I. Act to a major shareholder of a financial instruments firm under the jurisdiction of such Commissioner or director-general, the Commissioner or the director-general shall inform the director-general of a local finance bureau (if such major shareholder is a non-resident, the director-general of Kanto Finance Bureau) having the jurisdiction over the location of the principal business office or the principal office of such major shareholder (if such major shareholder is an individual, the address or place of residence) of the details of the order.
- ⑤ If there is a financial instruments firm, etc. under the jurisdiction of the Commissioner of the

Financial Services Agency or the director-general of a local finance bureau which commissions to carry out business to a financial instruments intermediary firm located in an area under the jurisdiction of the director-general of an other local finance bureau, the Commissioner of the Financial Services Agency or the first-mentioned director-general of the local finance bureau shall make an effort to coordinate with the second-mentioned director-general of the local finance bureau such as giving information useful for the supervision over such financial instruments intermediary firm.

II-1-3 Coordination with inspection division

As it is important to achieve highly effective supervision through appropriate coordination between the supervisory division and the inspection division while paying respects to independency of each division and combining on-site monitoring and off-site monitoring. Remarks shall be made on the followings for the coordination of the supervisory division and the inspection division.

- (1) Giving information of problems found through off-site monitoring to the inspection division
With respect to problems of a financial instruments firm, etc. found by the supervisory division through off-site monitoring, such information shall be given to the inspection division for the utilization in the next inspections.
In concrete terms, the supervisory division shall explain to the inspection division about the current state, etc. of the financial instruments firm, etc. such as:
 - ① major development of the financial instruments firm, etc. for the period from the previous inspection until such time (such as alliance with other companies, increase in capital, change in management team, etc.);
 - ② with respect to a financial instruments firm, etc. planning system integration, etc. associated with business restructuring such as merger, etc., the schedule, etc. for such business restructuring;
 - ③ the result of analysis of the latest account closing;
 - ④ the result of analysis regarding off-site monitoring for risk information, etc.;
 - ⑤ the result of comprehensive hearing;
 - ⑥ the state of taking and follow-up of supervisory measures (such as collection of report, administrative dispositions, etc.);
 - ⑦ matters that the supervisory division thinks to be emphasized in the inspection; and
 - ⑧ others.
- (2) Supervisory response to problems found through inspection
Following the inspection to a financial instruments firm, etc. performed by the inspection division, making administrative dispositions or taking other measures shall be considered under II-5 in order to reflect the result of inspection properly to supervision.
- (3) Inspection and supervision coordination meeting
 - ① A inspection and supervision coordination meeting shall be held in order to promote appropriate coordination between the supervisory division and the inspection division. This meeting shall be held at the commencement of the operational year in principle and when needed.
 - ② This meeting shall exchange opinions, etc. about the issues such as important matters for inspection of and supervision over financial instruments firms, etc. for the new operational year.

II-1-4 Coordination with self-regulatory organizations

The authority shall supervise financial instruments firms, etc. with remarks that it is necessary to emphasize on the rules of each self-regulatory organization in addition to the laws and regulations. The authority and self-regulatory organizations shall exchange information which is deemed necessary for the supervision over financial instruments firms, etc. to the extent of the purpose to ensure the fair transactions and the protection of investors, and make an effort to share information of the existence of risks and have common awareness of the issues through active exchange of opinions. Further, the authority shall participate to meetings for coordination between self-regulatory organizations and assist self-regulatory organizations to strengthen their self-regulatory functions.

The authority shall promote coordination with relevant organizations through the Securities Security Liaison Conference to reject crime groups from financial instruments business.

II-1-5 Internal delegation

- (1) Discussion with the Commissioner of the Financial Services Agency
Before handling matters delegated to the director-general of a local finance bureau related to the supervision over financial instruments firms, etc., the director-general of a local finance bureau shall discuss with the Commissioner of the Financial Services Agency for the following matters; *provided*, that the details of examination and opinions of the local finance bureau shall be referred to such discussion:
 - ① refusal of registration under Article 29-4.1 or 33-5 of the F.I. Act;
 - ② approval for engaging in approved business under Article 30.1 of the F.I. Act;
 - ③ administrative disposition to major shareholders under Article 32-2 of the F.I. Act (including the *mutatis mutandis* application under Article 32-4 of the F.I. Act);
 - ④ approval for other business engagement under Article 35.4 of the F.I. Act (limited to the first approval in the area under the jurisdiction of such local finance bureau);
 - ⑤ approval for exclusion of application of measures to prevent the negative effects under the proviso to Article 44-3.1 or the proviso to Article 44-3.2 of the F.I. Act;
 - ⑥ taking administrative dispositions to issue an order to improve business management, order to suspend business, revocation of registration or revocation of approval under Articles 51, 51-2, 52.1 or 52-2.1 of the F.I. Act;
 - ⑦ taking dispositions to remove an officer (in the case of a foreign corporation, limited to an officer stationed in a business office or other type of office in Japan or the representative in Japan) under Articles 52.2 and 52-2.2 of the F.I. Act;
 - ⑧ taking dispositions to issue an order to improve business management in respect of capital requirement ratio under Article 53 of the F.I. Act;
 - ⑨ taking dispositions to revoke registration of a financial instruments firm, etc. which has been halting business for long time under Article 54 of the F.I. Act;
 - ⑩ issuance of order to prepare, or amend, internal rules to financial instruments firms, etc. which are not members, etc. of an association, etc. under Article 56-4.2 of the F.I. Act;
 - ⑪ approval of preparation of, change in or elimination of internal rules of financial instruments firms, etc. which are not members, etc. of an association, etc. under Articles 56-4.3 and 56-4.4 of the F.I. Act;
 - ⑫ taking dispositions necessary for the investigation under Article 187 of the F.I. Act;
 - ⑬ approval for analysis of interest rate sensitivity under Article 8.1 of the Announcement regarding Computation Basis for Market Risk Equivalent Amount, Counterparty Risk Equivalent Amount and Operational Risk Equivalent Amount of Financial Instruments Firms (hereinafter referred to as "Capital Requirement Regulation Announcement");
 - ⑭ approval of the internal measurement approach under Article 12 of the Capital Requirement Regulation Announcement; and
 - ⑮ taking dispositions to revoke an approval under Article 15.4 of the Capital Requirement Regulation Announcement.
- (2) Report to the Commissioner of the Financial Services Agency
Upon handling matters delegated to the director-general of a local finance bureau related to the supervision over financial instruments firms, etc., the director-general of the local finance bureau shall:
 - ① send the original of an application for registration and attachments to the Commissioner of the Financial Services Agency immediately after a financial instruments firm, etc. under the jurisdiction of the Financial Services Agency has registered under Article 29-3.1 of the F.I. Act or Article 33-4.1 of the F.I. Act;
 - ② make a report of the state of major shareholders (which means major shareholders as defined in Article 29-4.2 of the F.I. Act) as of the end of each quarter to the Commissioner of the Financial Services Agency by Form II-7 no later than 20th of the following month of the end of the quarter;
 - ③ put together accident confirmations (the proviso to Article 39.3 of the F.I. Act) each interim year and report to the Commissioner of the Financial Services Agency by Form II-8 (Confirmation Processing Report) no later than 15th of the following month of the end of the interim year;
 - ④ upon accepting the following documents, send a copy thereof promptly to the Commissioner of the Financial Services Agency:
 - (a) report of international business (Article 173 (2) of the Cabinet Office Ordinance on

- Financial Instruments Business, etc. (hereinafter referred to as "F.I. Business Ordinance"));
- (b) notification of establishment or closing of a representative office (Article 199 (11) (h) of the F.I. Business Ordinance);
 - ⑤ upon accepting a notification under Article 50-2.1 or 50-2.7 of the F.I. Act, send a copy thereof promptly to the Commissioner of the Financial Services Agency;
 - ⑥ upon giving a notice under Article 57.3 of the F.I. Act (limited to the case where a notice to the Minister of Finance is required under Article 194-4.1 of the F.I. Act), send a copy thereof promptly to the Commissioner of the Financial Services Agency;
 - ⑦ upon accepting a notification under Article 15.1 or 15.2 of the Capital Requirement Regulation Announcement, send a copy thereof promptly to the Commissioner of the Financial Services Agency;
 - ⑧ investigate the state of the payment of registration and license tax (registration and license tax as defined in Article 2 of the Registration and License Tax Law) as of the previous business year in respect of financial instruments firms, etc. under the direct jurisdiction of the local finance bureau and make a report to the Commissioner of the Financial Services Agency no later than 30th of April each year.
- (3) Further delegation to directors of local financial offices, etc.
- The director-general of a local finance bureau may delegate the following operations among operations delegated to the director-general of a local finance bureau under Article 42 of the Financial Instruments and Exchange Act Enforcement Order (hereinafter referred to as "F.I. Act Enforcement Order") to the director of local finance office or the chief of Otaru Sub-Branch Office or Kitami Sub-Branch Office if the principal business office, etc. of the applicant or financial instruments firm, etc. is located within the jurisdiction of any of them:
- ① operations regarding acceptance of a registration application under Articles 29-2.1 and 33-3.1 of the F.I. Act;
 - ② operations regarding acceptance of an approval application under Article 30-3.1 of the F.I. Act;
 - ③ operations regarding acceptance of an approval application under Article 35.4 of the F.I. Act;
 - ④ operations regarding acceptance of a notification under Articles 31.1, 31.3, 33-6.1, 33-6.3, 31-2.5, 31-2.8, 35.3, 35.6, 46-6.1, 50.1, 50-2.1 and 50-2.7 of the F.I. Act;
 - ⑤ operations regarding acceptance of a notification under Articles 32.1, 32.3, 32-3, 32-4 and 57-26.1 of the F.I. Act; and
 - ⑥ operations regarding acceptance of documents filed under Articles 46-3.1, 46-3.2, 47-2, 48-2.1, 48-2.2, 49-3.1 and 49-3.2 of the F.I. Act.
- (4) Remarks
- ② to ④, ⑧ and ⑬ to ⑮ of (1), ②, ④ and ⑦ of (2), ②, ③ and ⑤ of (3) of II-1-5 shall not apply to operations of supervisory operations over registered financial institutions.

II-2 Responses to request for consultation, grievances, etc.

- (1) Primary response
- Although the Financial Services Users Consultation Office at the Financial Services Agency and the division in charge at each local finance bureau shall be the primary contact place for requests for consultation, grievances, etc. concerning financial instruments firms, etc. and financial instruments transactions, such contact place shall explain to persons who made such request for consultation, grievances, etc. clearly that the authority is not positioned to arbitrate individual transactions and that the duties of the authority is to ensure the sound management of financial instruments firms, etc. under the laws and regulations, and introduce a financial instruments firms association or recognized investor protection organization as an organization to handle a request for consultation, grievances, etc. under the F.I. Act.
- If, among requests for consultation, grievances, etc., the person who made the request for consultation or grievances, etc. agrees to provide information to the financial instruments firm, etc., the supervisory division shall provide information to such financial instruments firm, etc. in principle.
- (2) Accumulation of information
- Each local finance bureau shall record requests for consultation, grievances, etc. regarding financial instruments firms, etc. which are deemed to be useful to ensure sound management of financial instruments firms, etc. (Form II-9), and make a report of particularly important information to the division in charge of the Supervisory Bureau of the Financial Services

Agency promptly.

(3) Coordination with the Financial Services Users Consultation Office

The Supervisory Division shall take the following responses to promote appropriate reflection to supervisory operations on requests for consultation, grievances, etc. filed with the Financial Services Users Consultation Office.

- ① analysis of request for consultation, grievances, etc. referred from the Consultation Office;
- ② exchange of information with the Consultation Office.

II-3 Response to external enquiries such as legal interpretation

II-3-1 Enquiries about laws and regulations

(1) Scope to accept enquiries

The authority shall accept only enquiries about the laws and regulations under the jurisdiction of the Financial Services Agency such as the F.I. Act and laws and regulations related thereto. The authority shall keep strictly from making comments for enquiries related to laws or regulations which are not under its jurisdiction.

(2) Manner to reply to enquiries

- ① With respect to an enquiry which can be replied by existing materials such as these Supervisory Guidelines, council reports, etc., a reply shall be made accordingly.
- ② With respect to an enquiry for which a local finance bureau cannot make judgment, the local finance bureau shall prepare a communication memorandum (Form II-10) and discuss with the division in charge in the Financial Services Agency through an electronic mail or FAX, etc. (hereinafter referred to as "electronic mail, etc.").
- ③ If, with respect to the laws or regulations under the jurisdiction of the Financial Services Agency, a general enquiry which meets the criteria provided in the following (a) or (b) was made by business firms to which the laws or regulations under the jurisdiction of the Agency apply directly or by a business firms organizations ^(Note) composed of such business firms, and the authority deems appropriate to reply in writing and publish it in light of better estimation of application of the laws or regulations, the director in charge in the Agency shall reply in writing and publish it.

(Note) A business firms organization means an organization or alliance of organizations (if there is a superior body such as federation and central council, limited to the most superior body in principle) put together by a considerable number of business firms engaging in the same type of business to which the laws and regulations under the jurisdiction of the Agency apply directly for the principal purpose of increasing common interests.

(a) Scope of enquiries subject to these procedures:

Enquiries eligible to these procedures shall meet all of the following criteria:

- a. an enquiry about general legal interpretation which is not an enquiry whether the laws or regulations are applicable to specific transactions, etc. conducted by a specific business firm (limited to those for which the legal application prior confirmation procedures are not available);
- b. an enquiry which is not related to fact-finding;
- c. an enquiry related to common transactions, etc. for business firms (in the case where the enquirer is an organization, business firms composing such organization) to which the laws or regulations under the jurisdiction of the Financial Services Agency apply directly and matters about which many enquiries from business firms can be expected; and
- d. an enquiry for matters which are not clear from the operational guidelines, etc. published in the past.

(b) Written statement of enquiry (including an electronic method)

An enquirer wishing to use this procedures shall submit a written statement containing the following matters, and the enquirer may be requested to modify the contents of the written statement of the enquiry and provide additional statements and information in order to judge the details of the enquiry and matters stated in the above (a):

- a. clauses of the laws or regulations for which the enquiry was made and concrete points of the issue;
- b. the views of the enquirer on the enquiry and the basis therefor; and
- c. consent to publishing the enquiry and the reply.

(c) Enquiry place

The enquiry place to accept a written statement of enquiry shall be the division in charge in the Financial Services Agency having the jurisdiction over the laws and regulations related to the enquiry or the division in charge in the local finance bureau having the jurisdiction over the enquirer. If the division in charge in the local finance bureau has accepted a written statement of enquiry, such division shall send the written statement of enquiry promptly to the division in charge in the Financial Services Agency by an electronic mail, etc.

(d) Reply

a. The director in charge in the Financial Services Agency shall make an effort to reply to an enquirer within two months in principle after the arrival of the written statement of enquiry from the enquirer at the enquiry place, and if it is not possible to reply within two months, the director in charge shall explain the reasons to the enquirer and show the estimated time of reply.

b. A written statement of reply shall contain the followings as a note:

"This reply shows the general and current view regarding the laws and regulations, for which the enquiry was made, based on only information contained in the written statement of enquiry from the position having the jurisdiction over such laws and regulations, and therefore this reply shall neither judge the application to individual and specific case nor bind the judgment by investigative organizations or legal judgment."

c. If a reply under these procedures are not made, the division in charge in the Financial Services Agency shall explain to the enquirer of the fact and reasons therefor.

(e) Publication

Upon the reply under the above (d), the Financial Services Agency shall publish the enquiry and the reply on the website of the Financial Services Agency.

④ With respect to enquiries to which ③ does not apply but which are frequently made, a contact memorandum (Form II-11) shall be prepared when needed, and circulated to the relevant bureau or division and kept by the planning section of the division in charge in the Financial Services Agency or the division in charge in a local finance bureau.

⑤ If the enquirer wishes to be replied in writing for the enquiry from the Financial Services Agency and the legal application advance confirmation procedures under II-3-2 (2) can be used, the authority shall advise the enquirer to use the legal application advance confirmation procedures.

II-3-2 Legal application advance confirmation procedures (No-action letter system)

Legal application advance confirmation procedures (hereinafter referred to as "no-action letter system") means the system that, regarding concrete acts related to the business activities which a private corporation, etc. wishing to achieve, such private corporation, etc. confirms with administrative organization having the jurisdiction over the specific laws or regulations in advance whether specific provisions of such specific laws or regulations apply to such acts, and such organization replies and publishes the reply. The Financial Services Agency sets out the detailed rules for legal application advance confirmation procedures. This part shall prescribe operational procedures for no-action letter system, and in the case of using this system, "the Detailed Rules for Legal Application Advance Confirmation Procedures at the Financial Services Agency" shall be referred.

(1) Enquiry place

The enquiry place shall be the General Affairs Division of the Supervisory Bureau of the Financial Services Agency.

When a written statement of enquiry meeting requirements described in the entry guidelines under (2) ③ below has arrived, the General Affairs Division of the Supervisory Bureau of the Financial Services Agency which is the enquiry place shall accept the written statement of enquiry promptly and refer it to the division in charge having the jurisdiction over the laws or regulations for which the enquiry has been filed.

A financial institution, etc. under the jurisdiction of a local finance bureau shall make enquiry to such local finance bureau. Upon accepting an enquiry, the local finance bureau shall send the written statement of enquiry to the General Affairs Division of the Supervisory Bureau of the Financial Services Agency by an electronic mail, etc. promptly in principle.

(Note) In sending the written statement of enquiry to the General Affairs Division of the Supervisory Bureau of the Financial Services Agency, the local finance bureau shall attach the examination opinion in principal.

(2) Stream of operations after the acceptance of written statement of enquiry

After the receipt of a written statement of enquiry, the division in charge shall determine whether a reply should be made, after confirming particularly about the following ① to ③. If the enquirer cannot use this system for the enquiry, the authority shall inform the enquirer of the fact. If any modification or addition of written statements are necessary, the authority may request the enquirer to make necessary response.

Provided, That the written statements to be added shall be minimum and the authority shall make an effort to prevent putting excessive burden to an enquirer.

① Objects of enquiry

Whether a private corporation, etc. which is planning to engage in new business or transactions makes the following enquiries about the laws under the jurisdiction of the Agency and the Cabinet Order and the Office Ordinances thereunder (hereinafter referred to as "object laws or regulations (clauses)") listed on the website as the objects of these procedures:

- (a) whether the engagement in such business or transactions is regarded as unlicensed engagement of the business, etc.;
- (b) whether the engagement in such business or transactions is regarded as unnotified engagement of the business, etc.;
- (c) whether the engagement in such business or transactions is subject to suspension of business or revocation of license, etc. (disbenefit disposition);
- (d) whether the engagement in such business or transactions causes direct obligation or limitation of rights.

② Eligible enquirer

Whether an enquirer is a person enquiring about the application of object laws or regulations (clauses) to concrete acts related to its business activities which the enquirer wishes to achieve or a lawyer, etc. commissioned by such person, has submitted the written statement of enquiries complying with entry manners under ③, and has given a consent to publishing the enquiry and the reply.

③ Entry manners on entry in written statement of enquiries

Whether the written statement of enquiry (including an electronic method) meets the following requirements:

- (a) the written statement of enquiry contains individual and concrete facts related to proposed acts;
- (b) the written statement of enquiry specifies clauses of the laws or regulations, among object laws or regulations (clauses), which the enquirer wishes to confirm whether they are applicable;
- (c) the written statement of enquiry contains the statement that the enquirer gives a consent to publishing, the enquiry and the reply; and
- (d) the written statement of enquiry contains the view of the enquirer and the basis therefor regarding the application of clauses of the laws or regulations specified in the above (b) clearly.

④ Reply

The director of the division to which the enquiry is referred shall reply to the enquirer within 30 days in principle after the arrival of the written statement of enquiry from the enquirer at the enquiry place; *provided*, that in each of the following cases, the period specified in such case shall be the period for reply; further, in any case, the director shall endeavor to reply as soon as possible including modification period:

- (a) the case where a careful judgment is required because the enquiry relates to sophisticated financial technologies, etc. — within 60 days in principle;
- (b) the case where there are so many enquiries which exceed the process capacity of the division in charge and may cause serious interference on operations — reasonable period exceeding 30 days; and
- (c) the case of an enquiry related to co-jurisdiction with other cabinet offices or ministries — within 60 days in principle.

In the case where the authority requests the modification of the written statement of enquiry, such days required for the modification shall not be counted into the period for the reply. If the authority does not reply within 30 days, the authority shall explain the reasons therefor and show the estimated time of reply.

⑤ Publication of enquiry and reply

The Financial Services Agency shall publish the details of all of the enquiries and the replies on the website of the Financial Services Agency within 30 days after the reply in

principle.

Provided, That, in the case where the enquirer has noted in the written statement of enquiry that the enquirer desires the publication for a period exceeding a specified period from the reply with the reasons therefor and the time when the publication will be permitted and the authority deems such reasons reasonable, the authority may publish them for the period exceeding the specified period from the reply. In this case, it does not necessarily require to postpone the publishing until the time when the enquirer desires, and the authority may publish it after giving such a notice to the enquirer if such reasons to postpone the publishing have disappeared. If the enquiry or reply contains information subject to non-disclosure as provided in the items of Article 5 of the Law on the Disclosure of Information Held by Administrative Organization, the authority may exclude such matters in publishing.

II-4 Remarks, etc. on administrative instruction, etc.

II-4-1 Remarks, etc. on administrative instruction, etc.

In making administrative direction, etc. (administrative direction, etc. includes, in addition to administrative direction as defined in Article 2 (6) of the Administrative Procedures Law, giving information, consultation, advice, etc. which is not clearly distinguished from administrative direction) to a financial instruments firm, etc., the authority shall comply with the laws or regulations, etc. such as the Administrative Procedures Law. When an administrative direction, etc. is made particularly, remarks shall be made on the followings.

- (1) General principles (Article 32 of the Administrative Procedures Law)
 - ① Whether the administrative direction, etc. is achieved by the voluntary cooperation of the counterparty.

For example, the followings shall be noted:

 - (a) Whether the authority gains understanding from the counterparty about the details and operations of administrative direction, handling manner of the person in charge, etc.; and
 - (b) whether the authority continues the administrative direction against the clearly shown intent by the counterparty not to cooperate with the administrative direction, etc.
 - ② Whether the authority treats the counterparty which disobeyed the administrative direction, etc. unfavorably:
 - (a) It shall be noted that "unfavorable treatment" may apply to the publication of the fact of disobeying an administrative direction, etc. without legal ground, considering that such treatment may result in social sanction such as economic loss;
 - (b) If it is not clear at the time of administrative direction whether the power of making dispositions will be exercised but such power may be exercised under the conditions that requirements for the exercise of the power of making dispositions may be met depending on the state after the administrative direction, etc., making such administrative direction, etc. with showing such fact shall not necessarily be denied.
- (2) Administrative direction, etc. related to application (Article 33 of the Administrative Procedures Law)

Whether the authority prevents an applicant from exercising the right of the applicant by continuing the administrative direction, etc. against the applicant's intent to disobey the administrative direction, etc.

 - ① Even if the applicant does not show explicitly the intent to disobey an administrative direction, etc., the authority shall judge whether the counterparty has the intent to refuse the administrative direction, etc. after considering the background of the administrative direction, etc. or the change in objective circumstances, etc.
 - ② It shall be noted that, even if the applicant responds to an administrative direction, etc., the applicant does not necessarily give a voluntary consent to the authority's reservation to judgment or response to the application.
 - ③ For example, the followings shall note:
 - (a) whether the authority forces the applicant to follow an administrative direction, etc. and prevent the applicant from exercising the right of the applicant;
 - (b) whether, in the case where the applicant has not shown clearly the intent to disobey an administrative direction, etc., the authority reserves the examination or response to the application for the reasons of making administrative direction, etc.; and

- (c) whether, in the case where the applicant has shown the intent to disobey an administrative direction, etc., the authority ceases the administrative direction, etc. and response to the applicant quickly and properly.
- (3) Administrative direction, etc. related to power of licensing, approval, etc. (Article 34 of the Administrative Procedures Law)
- Whether the authority forces the counterparty to follow an administrative direction, etc. by emphasizing that, despite the fact that the authority cannot exercise, or has no intention to exercise, the power to license, approve, etc. or the power to make dispositions under such power to license, approve, etc., the authority can exercise such power.
- For example, the followings shall be noted:
- ① Whether the authority requires a certain act or omission by showing that the authority can make a disposition to refuse licensing, approval, etc., despite the fact that the authority cannot make such disposition to refuse licensing, approval, etc.
 - ② Whether the authority compels the counterparty to follow an administrative direction, etc. by suggesting that the authority will exercise the power soon if the counterparty disobeys the administrative direction, etc. or indicating that the authority will treat the counterparty unfavorably.
- (4) Manners of an administrative direction, etc. (Article 35 of the Administrative Procedures Law)
- ① Whether the authority shows the purposes, details and the responsible person of an administrative direction, etc. clearly to the counterparty in making the administrative direction, etc.
- For example, the followings shall be noted:
- (a) whether the authority shows clearly the details of acts or omission that the counterparty is required to perform;
 - (b) whether the authority shows who is responsible for the administrative direction, etc.;
 - (c) whether, in making an administrative direction, etc. based on a specific law, the authority shows the clauses of such law; and
 - (d) whether, in making an administrative direction, etc. without basis of a specific law, the authority informs of the purpose of the administrative direction, etc. in order to gain understanding to the necessity of such administrative direction, etc.
 - ② Whether the authority furnishes a written statement containing the purpose, details and responsible person of an administrative direction, etc. in principle to the extent that there is no special interference with the administrative operations when the authority was requested to furnish such written statement from the counterparty (excluding the cases referred to in the items of Article 35.3 of the Administrative Procedures Law).
 - (a) a written statement shall be furnished as promptly as possible when requested;
 - (b) the case of "special interference with the administrative operations" which constitutes the reason for the refusal of furnishing a written statement means the case where showing in written statements the purpose, details and responsible person of the administrative direction, etc. will cause gross interference with administrative operations such as the case where an administrative purpose cannot be fulfilled by the usage, interpretation, etc. of the written statement regardless of the intent of the person who has prepared such statement; and
 - (c) it shall be noted that the case of "special interference with the administrative operations" does not necessarily apply to the case where the authority has simply many matters to be processed or must simply be quick.

II-4-2 Remarks on holding interview, etc.

Remarks shall be made on the followings when an official holds an interview, etc. (which means communication by interview, telephone, electronic mail, etc.; hereinafter the same) with officers, employees, etc. of a financial instruments firm, etc.

- ① Whether an official participating to the interview, etc. always keeps morals and dignity and participates with moderate and calm attitude.
- ② Whether the official confirms the purpose of the interview, etc., the name, belonging, etc. of the counterparty.
- ③ Whether the method, the place, time, participating officials and counterparties of the interview, etc. are suitable for the interview, etc. in light of the purpose of and matters subject to the interview, etc.
- ④ Whether the official confirms the common recognition of the matters subject to, and the

result of, the interview, etc. between the parties when needed, and whether, particularly in the case where the matters subject to, or the result of, the interview, etc. are subject to confidentiality obligations, such fact is known clearly to both parties.

- ⑤ Whether, in the case where the official is required to obtain the judgment of the supervisor about matters subject to the interview, etc., the official obtains the judgment from the supervisor prior to, and makes a report promptly after, the interview, etc. according to the situation; and whether, in the case where the official holds an interview, etc. separately with more than one counterparty for the similar issue, the official gives consideration to the integrity and transparency.

II-4-3 Communication and consultation procedures

In making an administrative direction, etc. through interview, etc., the authority shall communicate with the division in charge of the Financial Services Agency and discuss about the response when needed, in the case where the authority was unable to make a decision about the appropriateness of such administrative direction, etc. in light of the Administrative Procedures Law.

II-5 Remarks, etc. on administrative disposition

II-5-1 Responses to Inspection Result, etc.

(1) Responses to inspection result

The authority shall reflect the result of inspections to financial instruments firms, etc. conducted by the Inspection Division to supervisory operations in an appropriate manner as follows.

- ① When the authority deems necessary and appropriate with respect to acts violating the laws or regulations and other doubtful acts or state in the public interest and to protect investors regarding business management and financial conditions of a financial instruments firm or business management of a registered financial institution which has been pointed out in the inspection report, and important matters which have been pointed out in the previous inspection and which has not been improved, the authority shall order the financial instruments firm, etc. to submit a report containing the confirmation of the fact about matters pointed out in such report, analysis of causes, measures for improvement or response and others within one month (or shorter period for some items when needed) pursuant to Article 56-2.1 of the F.I. Act.

When the authority deems necessary and appropriate in the case where a financial instruments firm, etc. planning system integration, etc. because of a merger, etc. has been pointed out regarding the control system of system integration risk, the authority shall order to submit a report under Article 56-2.1 of the F.I. Act for measures to perform accurately the plan of such system integration, etc., internal control system for system risk (including internal audit).

The above order to submit reports shall be made by Form II-12.

- ② When the report is submitted, the authority shall hold substantial hearings for the financial instruments firm, etc. In holding a hearing, the authority shall coordinate with the Inspection Division closely.
- ③ When a certain period is required to take measures for improvement and response stated in the report or improvement of matters pointed out, the authority shall make an effort to follow up through periodical hearings, etc.
- ④ Based on the result, etc. of an on-site inspection, if the Securities and Exchange Commission recommends to take "administrative dispositions or other measures" under the provisions of Article 20.1 of the Financial Services Agency Establishment Law, the supervisory division shall review the recommendation and consider the issuance of an order to make a report under Article 56-2.1 of the F.I. Act, administrative dispositions under Articles 51 to 52-2 of the F.I. Act or taking other appropriate measures.

(2) Collection of report based on off-site monitoring, etc.

- ① The authority shall require to make a report of the fact recognition, analysis of causes for occurrence, measures for improvement or response and other matters deemed necessary under Article 56-2.1 of the F.I. Act in the case where it is determined that there is a problem in the risk control system, compliance system, business management system, etc. of a financial instruments firm, etc. through an off-site monitoring, etc.

- ② The authority shall require additional reporting under Article 56-2.1 of the F.I. Act if it is determined necessary to investigate further as a result of verifying the report.
- ③ The authority shall conduct follow-up of the reported measures of improvement and response through voluntary hearing in the case where there is no grave problem in the public interest and to protect investors as a result of verifying the above report and it is possible to require a financial instruments firm, etc. to make voluntary effort for improvement.
- ④ The authority shall require periodical reports and conduct follow-ups under Article 56-2.1 of the F.I. Act when needed.

II-5-2 Administrative Dispositions under Articles 51 to 52-2.1 of the F.I. Act (Issuance of order to improve business, issuance of order to suspend business, etc.)

If it is determined that there are grave problems in the public interests or to protect investors as a result of comprehensive verification in light of valuation items, etc. referred to in these Supervisory Guidelines in respect of reports from a financial instruments firm, etc. or recommendation, etc. from the Securities and Exchange Surveillance Commission, the authority shall, considering the matters referred to in the following (1) to (3), examine whether there is other factors and determine administrative dispositions after examining:

- whether it is appropriate to leave the efforts for improvement to voluntary effort of a financial instruments firm, etc.;
- whether it is necessary to require concentration on business improvement for a certain period because considerable efforts are required for improvement;
- whether it is appropriate that the financial instruments firm, etc. continues the business.

(1) Gravity and maliciousness of such act

① Degree of users' damages

Whether a financial instruments firm, etc. harms public interests grossly such as forming and providing gravely inappropriate products in light of, for example, appropriate disclosure of a customer's financial conditions, and losing trust on the financial market.

② Degree of damages on users

Whether broad and many users have suffered damages; the degree of damage that each user has suffered.

③ Maliciousness of Act

Whether acts of the financial instruments firm, etc. were malicious such as the act of continuing to sell the same type of products despite the fact that many users file grievances.

④ Length and repetitive nature of acts

Whether the acts were performed for long time or short time. Whether the acts were performed only once or repeatedly and continuously. Whether the same type of violating acts have been made in the past.

⑤ Willfulness

Whether the acts were performed willfully knowing that such acts were unlawful and inappropriate, or inadvertently.

⑥ Organizational involvement

Whether the acts were performed at individual person's judgment on the spot or there was involvement of a controller. Whether there was involvement of the management team.

⑦ Cover-up

Whether there were cover-ups after the recognition of problems. Whether, if there were cover-ups, such cover-ups were made organizationally.

⑧ Involvement of Antisocial forces

Whether there were involvements of antisocial forces. If there were such involvements, the degree thereof.

(2) Appropriateness of management controlling system and business management system which caused such acts

① Whether recognition and effort of compliance by representative directors or the board of directors are sufficient.

② Whether the internal control system is sufficient, and whether the internal control system works appropriately.

③ Whether the system of the compliance division or risk control division sufficient, and whether the system works appropriately.

④ Whether a person in charge recognizes compliance sufficiently. Whether in-house training

is sufficient.

(2) Reasons to lessen punishment

In addition to the above (1) and (2), whether there are reasons to lessen punishment such as the fact that the financial instruments firm, etc. is making an effort to contribute to the protection of users voluntarily in advance to the response by the administration.

II-5-3 Remarks on making dispositions to registered financial institutions

If an inappropriate case has been found in respect of securities related business carried out by a registered financial institution, the authority shall coordinate with the division in charge of the Banking Supervisory Bureau, etc. based on the view of soundness of business management under the Banking Law, etc. in addition to the view of the protection of investors, etc. under the F.I. Act to collect reports and issue an order to improve business management when needed.

II-5-4 Typical process time-frame for supervisory disposition based on the result of inspection

An order of supervisory dispositions under Articles 51 to 52-2 of the F.I. Act shall be issued:

- ① within one month in principle (if discussion between the director-general of a local finance bureau and the Commissioner of the Financial Services Agency is necessary or the disposition is made under laws or regulations having the joint jurisdiction with other ministry or office, two months in principle) since the acceptance of a recommendation or inspection result report (copy) from the inspection division;
- ② within one month in principle (if discussion between the director-general of a local finance bureau and the Commissioner of the Financial Services Agency is necessary or the disposition is made under laws or regulations having the joint jurisdiction with other ministry or office, two months in principle) since the acceptance of such report, if the authority has collected a report from the financial instruments firm, etc. or other person. for the purpose of the confirmation of facts in respect of matters pointed out in such recommendation or inspection result report.

(Note1) Remarks shall be made on the followings for judging "since acceptance of reports".

(a) It means, in the case of issuing an order to make a report under Article 56-2.1 of the F.I. Act more than one time (limited to the case of issuing an order to make a report within the above period since the acceptance of the latest report), since acceptance of the latest report.

(b) It means, in the case of requiring the amendment or addition, etc. of information, (excluding minor amendment or addition, etc.) regarding the report submitted, since such amendment or addition, etc. was made.

(Note2) The period required for pleading or hearing, etc. shall be excluded in the typical process time-frame.

(Note3) The typical process time-frame applies to each information which is the basis for examination of disposition.

II-5-5 Release from obligation to make report of performance of business improvement under Article 51 or 51-2 of the F.I. Act

In issuing an order to improve business management under Articles 51 or 51-2 of the F.I. Act, the authority shall require to make a report of performance of business improvement plan submitted by a financial instruments firm, etc. in principle in order to follow-up the effort of the financial instruments firm, etc. to improve the business and to encourage such effort based on such order with the following remarks:

- (1) If the authority requires the financial instruments firm, etc. to which the authority has issued an order to improve business management under Article 51 or 51-2 of the F.I. Act to make a report of performance of the business improvement plan submitted by the firm with a specified deadline, the financial instruments firm, etc. shall be released from the obligation to make a report when the deadline has arrived.
- (2) If the authority requires the financial instruments firm, etc. to which the authority has issued an order to improve business management under Article 51 or 51-2 of the F.I. Act to make a report of performance of the business improvement plan submitted by the firm continuously without fixing the deadline, the financial instruments firm, etc. shall be released from the obligation to make a report of performance of such plan if it is determined that sufficient measures for improvement have been taken in line with the business improvement plan for the

problem which has caused the issuance of the business improvement order. The authority shall judge whether the release is appropriate or not based on the efforts of improvement recognized from such report, etc

II-5-6 Relation with Administrative Procedures Law, etc.

(1) Relation with the Administrative Procedures Law.

It shall be noted that, in making a disbenefit disposition including issuance of a business improvement order or business suspension order or revocation of registration or approval, the authority shall hold a hearing under Article 57.2 of the F.I. Act.

In any case, it shall be noted that the authority shall show reasons for the disposition under Article 14 of the Administrative Procedures Law.

(2) Relation with Administrative Appeal Law

It shall be noted that, in issuing an order to make a report, an order to improve business management or an order to suspend business or making dispositions to revoke a registration or approval, the authority shall enlighten the party in writing that a financial instruments firm, etc. under the jurisdiction of a local finance bureau may file an appeal for examination under Article 5 of the Administrative Appeal Law and that a financial instruments firm, etc. under the jurisdiction of the Financial Services Agency may file an appeal for examination under Article 6 of the Administrative Appeal Law.

(3) Relation with Administrative Case Litigation Law

It shall be noted that, in making dispositions of collection of report order, issuance of a business improvement order or business suspension order or revocation of registration or approval, the authority shall enlighten the party in writing that the party may file an appeal for revocation of the disposition under Article 8 of the Administrative Case Litigation Law.

II-5-7 Exchange of opinions

In the case where a disbenefit disposition is made, it will be beneficial to promote the common recognition about the fact causing and the importance, etc. of the proposed disposition through the exchange of opinions at multiple levels between the authority and a financial instruments firm, etc. when requested by the financial instruments firm, etc., apart from procedures for holding hearings or giving opportunities to plead under the Administrative Procedures Law.

If, in the course of hearing, etc. related to collection of reports under Article 56-2.1 of the F.I. Act, the authority is requested by a financial instruments firm, etc. which has recognized the high probability of disbenefit disposition to set an opportunity of exchange of opinions^(note 1) between executives of the supervisory authority^(note 2) and executives of such financial instruments firm, etc. and the supervisory authority will be likely making a disbenefit disposition involving in hearing or giving opportunities to plead, the authority shall set an opportunity of the exchange of opinions about the fact causing and the importance of such proposed disbenefit disposition before giving the notice of hearing or the notice of giving opportunities to plead except for the case where an emergency disposition is necessary.

(Note 1) A request by a financial instruments firm, etc. for setting opportunity of exchange of opinions shall be limited to those made during the period from the acceptance by the supervisory authority of reports, etc. under Article 56-2.1 of the F.I. Act about the fact causing such disbenefit dispositions until the notice of hearing or the notice of giving opportunities to plead.

(Note 2) Examples of executives of the supervisory authority: the director of a division in charge in the Financial Services Agency or local finance bureau, etc.

II-5-8 Communication with relevant authorities and overseas supervisory authorities, etc.

In making a disbenefit disposition including the issuance of an order to make a report of a business improvement order or business suspension order or revocation of registration or approval, the authority shall communicate with relevant authorities or foreign supervisory authorities, etc. when needed.

II-5-9 Concept for publication of disbenefit disposition

(1) It shall be noted that, when the authority issued an order to suspend business or revoke

registration or approval, the authority shall give a public notice of such order by the official gazette under Article 54-2 of the F.I. Act.

- (2) It shall be noted that publication other than (1) shall be made based on the concept provided in I-5 (Transparency) of "Principles of Financial Supervision and Understanding by Officials of Supervisory Division (Codes of Conduct)".

In making a disbenefit disposition including issuance of a business improvement order, the authority shall publish the fact which has caused the disposition and the details of the disposition in order to enhance predictability for other financial institutions, etc. and to inhibit the occurrences of similar cases, except for the matters which may harm improvement of business management of the financial instruments firm, etc. as a result of the publication such as making a disbenefit disposition regarding financial resources.

II-6 *Mutatis Mutandis* Application

- (1) *Mutatis mutandis* application to persons carrying out eligible institutional investors, etc. business subject to special provisions

The provisions of II-2, II-3, II-4 and II-5 shall apply *mutatis mutandis* to operational process for persons carrying out eligible institutional investors, etc. business subject to special provisions. The text shall be amended in reading in the case of Forms accordingly.

- (2) *Mutatis mutandis* application to financial instruments intermediary firms

The provisions of II-1-1 (6), II-1-1 (7), II-1-3, II-1-5, II-2, II-3, II-4 and II-5 shall apply *mutatis mutandis* to operational process for financial instruments intermediary firms, and the provisions of ① and ② of II-1-2 (2) shall apply *mutatis mutandis* to coordination with the competent director-general of a local finance bureau for supervisory operations over financial instruments intermediary firms. The text shall be amended in reading in the case of Forms accordingly.

- ① In supervising a financial instruments intermediary firm the belonging financial instruments firm of which is a financial instruments firm, etc. under the jurisdiction of the Commissioner of the Financial Services Agency or an other director-general of a local finance bureau, the director-general of a local finance bureau shall make an effort to coordinate including providing the Commissioner of the Financial Services Agency or the director-general of a local finance bureau having the jurisdiction over such belonging financial instruments firm, etc. with information necessary for the supervision over the belonging financial instruments firm, etc.

- ② The director-general of a local finance bureau shall, if there is a business office or other type of office of a financial instruments intermediary firm over which an other director-general of a local finance bureau has the jurisdiction in the area for which the first-mentioned director-general of a local finance bureau has the jurisdiction, the first-mentioned director-general of a local finance bureau shall make an effort to coordinate including providing the director-general of a local finance bureau having the jurisdiction of such financial instruments intermediary firm with information necessary for the supervision over the financial instruments intermediary firm.

- (3) *Mutatis mutandis* application to securities finance companies

The provisions of II-1-3, II-2, II-3, II-4 and II-5 shall apply *mutatis mutandis* to operational process for securities finance companies

- (4) *Mutatis mutandis* application to investment corporations

The provisions of II-1-1 (6), II-1-1 (7), II-1-3, II-2, II-3, II-4 and II-5 shall apply *mutatis mutandis* to operational process for investment corporations. The text shall be amended in reading in the case of Forms accordingly.

- (5) *Mutatis mutandis* application to commodity investment sales firms

The provisions of II-1-2 (1), II-1-2 (2) ②, II-1-3, II-1-4, II-1-5 (1), II-2, II-3, II-4 and II-5 (excluding II-5-9 (1)) shall apply *mutatis mutandis* to operational process under the Law on Regulations of Business related to Commodity Investment related to commodity investment sales firms. The text shall be amended in reading in the case of Forms accordingly.

III. Supervisory Valuation Items and Procedures (Common Part)

III-1 Business management (common part)

It is important that each financial instruments firm makes an effort to implement the compliance system and carries out business management to prevent the failure of the protection of investors in order to promote sound development of markets. In carrying out daily supervisory operations, it is necessary to verify desirable business management of a financial instruments firm from a perspective of whether the management team of the financial instruments firm supervises its business execution effectively or whether the supervisory control over the management team works effectively.

(1) Main focus points

It is necessary for effective functioning of business management control over financial instruments firms that all officers and employees of each financial instruments firm recognize that financial instruments firms have important social responsibility as participants of financial instruments markets, and understand fully of the roles given to such officers and employees and participate to business management. Particularly, representative directors, directors, the board of directors, auditors, the board of auditors and internal control division have important duties.

It is needless to say that a representative director is a director authorized to represent the financial instruments firm and has the duties of the chief executive of business management of the financial instruments firm. The board of directors is authorized to make concrete decisions of business operations as the top decision-making body of the financial instruments firm, and have the function to supervise business operations by a representative director or a director in charge. An auditor or the board of auditors has broad and powerful authorization to supervise business operations carried out by directors, etc. who have important duties on business management of the financial instruments firm, and has important duties on supervising management.

Therefore, the authority shall verify whether a representative director, a director, the board of directors, an auditor or the board of auditors fulfills the function appropriately and performs the given missions with, for example, the following remarks.

(Note) In the case of a financial instruments firm having a committee, it is necessary to verify considering whether an organ, etc. such as the board of directors, each committee, an executive officer, etc. execute given powers appropriately. In this case, the authority shall verify realistically based on the principles of these Guidelines.

① Representative director

- (a) Whether a representative director ranks matters related to implementation and maintenance of compliance and internal control system as well as matters related to business promotion as one of the most important issues of business management, and, in order to implement such matters, works on the creation of principles and thorough performance sincerely and takes initiatives.
- (b) Whether a representative director recognizes fully that viewing the risk control division as less important will cause influence on corporate profit grossly, and emphasizes the risk control division.
- (c) Whether a representative director recognizes the importance of the internal audit, establishes the purposes of the internal audit, constructs the function that the internal audit division fulfills its function (including ensuring the independency of the internal audit division) and confirms the fulfillment of the function periodically. Further, a representative director approves the principles of an internal audit plan such as audit policies, important items, etc. based on the risk control, etc. in a division to be audited. Further, whether a representative director takes appropriate measures for the result, etc. of the internal audit.
- (d) Whether a representative director recognizes fully that it is essential to cut off, and reject the relationship with, antisocial forces in a determined attitude for the purpose to maintain public trust on the financial instruments firm and to ensure appropriate and sound business of the financial instruments firm, and declare to the inside and outside of the firm the policies decided by the board of directors based on "Guidelines for Prevention of Damages of Corporations by Antisocial Forces" (Common Consent by Board Meeting of Cabinet Conference for Crime Countermeasures dated June 19, 2007; hereinafter in III-1, referred to as "Government Guidelines").

② Director and the board of directors

- (a) Whether a director checks and controls a dogmatic decision by a representative director, etc. who executes operations and participates to decision making on business operations at the board of directors and the supervision over business operations by a director positively.
- (b) Whether the board of directors implements business management policies clearly based on

the overall picture, etc. that the financial instruments firm aims. Further, whether the board of directors makes the management plan clearly in line with the business management policies and inform it to the entire organization. Further, whether the board of directors verifies, and reviews when needed, the degree of the achievement periodically.

- (c) Whether the board of directors ranks matters related to implementation and maintenance of compliance and internal control system as well as matters related to business promotion as one of the most important issues of business management, and, in order to implement such matters, makes sincere effort and takes initiatives on the creation of the principles and thorough performance. Further, the board of directors informs of the policies internally. Further, whether the board of directors decides policies based on the Government Guidelines, implements the system to fulfill the policies, and ranks the prevention of damages by antisocial forces clearly as matters of compliance and risk control including verifying the effectiveness of the policies periodically.
 - (d) Whether the board of directors recognizes fully that viewing the risk control division as less important will cause influence on corporate profit grossly, and considers the risk control division as important. Particularly, whether the director in charge understands where risks exist and the type of risks and have deep recognition and understanding about measurement of various types of risks, methods of monitoring and control, etc.
 - (e) Whether the board of directors implements the policies to control various risks based on the strategic goal clearly. Whether the board of directors reviews the risk control policies periodically or to follow a change in the strategic goal or to meet the development of risk controlling methods, etc. Whether the board of directors uses risk information obtained for business operations and maintenance of control system, etc. such as necessary decision making with a report related to information of risks periodically.
 - (f) Whether the board of directors understands that segregation of customer assets contributes to the protection of investors and the sound development of a financial instruments market, and recognizes the importance of the segregation of customer assets. Whether the board of directors receives reports of segregation of customer assets periodically or when needed, and uses such reports to maintain the system to segregate customer assets appropriately.
 - (g) Whether the board of directors recognizes the importance of internal audit, establishes the purposes of internal audit appropriately, builds up the functioning for the internal audit division to fulfill the function fully (including ensuring the independency of the internal audit division), and confirms the functioning periodically. Further, the board of directors approves the principles of an internal audit plan such as audit policies, important items, etc. based on the risk control, etc. in a division to be audited. Further, whether the board of directors takes appropriate measures for the result, etc. of the internal audit.
- ③ Auditor and the board of auditors
- (a) Whether the board of auditors is independent in accordance with its purposes.
 - (b) Whether the board of auditors exercises the given broad power appropriately and performs the audit of business operations in addition to the audit of accounting.
 - (c) Whether, even if the board of auditors is organized, each auditor is aware that the auditor is an organ of singularity and performs auditing actively based on the responsibility.
 - (d) Whether the board of directors receives reports of the results of external audits according to the types of external audits and makes an effort to ensure the effectiveness of its auditing.
- ④ Internal audit division
- The internal audit division shall have the purpose to contribute to the fulfillment of the management goal of the financial instruments firm, shall be independent from divisions to be audited, verify or value the state of business operations, appropriateness, effectiveness, reasonability, etc. of internal control or internal governance based thereon, shall make an advice or recommendation, etc. to the management team, and shall be one of the most important corporate activities to ensure the self-reliant corporate management of the financial instruments firm. Considering such importance, the internal audit division shall verify whether the internal audit works effectively, with for examples the following remarks.
- (a) Whether the internal audit division is independent from divisions to be audited in order to check the divisions to be audited and is organized to perform effective internal audit.
 - (b) Whether the internal audit division audits all businesses and operations of the financial instruments firm and makes an internal audit plan after recognizing the risk management and types of risks at divisions to be audited.
 - (c) Whether the internal audit division performs efficient and effective internal audit on a division to be audited based on the internal audit plan.

- (d) Whether the internal audit division makes a report of important matters obtained or pointed as a result of an internal audit to a representative director and the board of directors without delay.
- (e) Whether the internal audit division controls the improvement of matters pointed as a result of an internal audit by a division audited appropriately, and reflects it to subsequent internal audit plan.
- ⑤ Use of external auditing

A financial instruments firm shall be audited by an accounting auditor for the balance sheet, etc. under the regulations, but is not obliged to be audited for its business by an external auditor (including an audit by the headquarter, group, etc.). However, ensuring of effective use of such external audit by an accounting auditor, etc. is desirable in the same way as an internal audit by the financial instruments firm in order to acquire corporate profit or control risk or to ensure the effectiveness of the internal control system, and the authority shall verify, for example, such external audit with the following remarks.

 - (a) Whether important matters recognized or pointed by an external audit is reported to the board of directors or the board of auditors without delay.
 - (b) Whether divisions audited improve matters pointed as a result of an external audit within a certain period, and the internal audit division recognizes or verifies the improvement appropriately.
- (2) Supervisory methods and response

The authority shall verify the management control through the following hearings and ordinary supervisory operations.

 - ① Comprehensive hearings (refer to II-1-1 (2))

The authority shall hold a hearing on issues of business management, strategies for business management, various risks involved therein and governance through comprehensive hearings. The authority shall hold a top hearing directly for the management team when needed.
 - ② Hearings on internal audit

The authority shall hold a hearing on the internal control system, the state of performance of internal audits and improvement of problems, etc. for the internal audit division of a financial instruments firm when needed in order to recognize the state of the fulfillment of functioning of internal audits. The authority shall hold a hearing for an auditor and external director of a financial instruments firm, when particularly needed.
 - ③ Verification of business management control through ordinary supervisory operations

In addition to the above hearings, the authority shall verify the effectiveness of business management control through, for example, follow-ups of business improvement report concerning matters pointed as a result of an investigation, ordinary supervisory operations of acceptance, etc. of financial instruments accidents, etc. notification.
 - ④ Record of result of monitoring

The authority shall prepare and keep the record of such monitoring for significant matters based on the result of such monitoring for the effective use of supervisory operations after the above monitoring.
 - ⑤ Methods of Supervision and responses

The authority shall, if the effectiveness of management control becomes doubtful, know the state of voluntary business improvement of a financial instruments firm through holding a hearing in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed concerning the reason and the improvement plan, etc. The authority shall, if a gross problem in the public interests and to protect investors has been found, make responses such as the issuance of an order to improve business management under Article 51 of F.I. Act. The authority shall, further if a violation of laws and regulations of a particularly grave nature has been found, consider necessary responses including the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2 Appropriateness of business (common part)

III-2-1 Compliance with laws and regulations, etc. system

- (1) Implementation of compliance with laws and regulations, etc. ("compliance") system

It is necessary that financial instruments or services are provided by appropriate methods on

fair, transparent and efficient markets for the growth of finance and economy in Japan, and gaining users' trust on financial instruments firms is one of the most important elements therefor. Each financial instruments firm is strongly requested to comply rigidly with the laws, regulations and various rules for business operations and to make an effort to conduct sound and proper business management. The authority shall verify the implementation of the compliance system of a financial instruments firm according to its scale with the following remarks.

- ① Whether compliance is positioned as one of the most important issues of business management and whether the financial instruments firm has established the policies for the enforcement, compliance program or codes of conducts (ethics rules, compliance manual), etc.; and further, whether the financial instruments firm ensures all officers and employees to be aware of and understand fully such policies, etc. including the existence and the details thereof and puts them in practice in the course of daily business operation;
- ② Whether a financial instruments firm values and follows up the compliance program or code of conducts periodically or when needed; and further, whether the financial instruments firm reviews the program or code of conducts;
- ③ Whether a financial instruments firm implements a system to communicate and make a report of information related to compliance accurately among divisions in charge of sales (which mean all of the divisions which mainly carry out business to make profits; hereinafter referred to as "business division"), compliance division/ persons in charge and the management team;
- ④ Whether a financial instruments firm establishes training or education program regarding compliance and makes an effort to build and improve compliance mind of officers and employees; and further, whether the financial instruments firm values and follows up the effect of training and makes an effort to ensure the effectiveness by reviewing it;
- ⑤ Whether a financial instruments firm implements a system to fulfill the function of a person in charge of controlling the compliance of the financial instruments firm (which means a person as defined in Article 15-4 (1) of the F.I. Act Enforcement Order) in order to contribute to the enhancement of the internal control system of the financial instruments firm and appropriate carrying out of business; and further, whether the financial instruments firm values and follows up the fulfillment of the function of internal controllers, etc.

(2) Supervisory methods and response

With respect to the issues for the compliance system of a financial instruments firm found through daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses including the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-2 Supervisory response to financial instruments accident, etc.

Supervisory responses to financial instruments accident, etc. ^(Note) shall be dealt as follows.

(Note) Financial instruments accidents, etc. mean any of the followings; hereinafter the same:

- (a) an act in violation of the laws or regulations specified in Article 199 (7) of the F.I. Business Ordinance;
 - (b) accusation, etc. against a financial instruments firm or its officer or employee; or
 - (c) other act which will, or will likely, impair sound and appropriate business management of a financial instruments firm and is equivalent to the acts under (a) or (b).
- (1) Main focus points
- ① First report when a financial instruments accident, etc. has been found
When a financial instruments accident, etc. has been found at a financial instruments firm and the financial instruments firm has made the first report, the authority shall confirm the followings. When a financial instruments firm has filed a notification without making the first report, the same applies.
 - (a) Whether a quick report has been made to the internal control division and the internal audit division and a report has been made to the board of directors, etc. in accordance with

- compliance rules, etc.
- (b) Whether, with respect to the fact likely constituting the violation of criminal laws or regulations, a report has been made to relevant organizations, etc. including the police, etc.
 - (c) Whether investigation or clarification of the accident is made by a division (such as internal audit division, etc.) independent from a division where the accident has occurred.
- ② Verification of appropriateness of business
- Verification of the relationship between financial instruments accidents, etc. and the appropriateness of business of a financial instruments firm shall be made based on the following focus points.
- (a) Whether any of officers involved in the accident, etc. or involvement was organized.
 - (b) How such accident, etc. influences on business management, etc. of the financial instruments firm, and influences on customers or financial instruments markets.
 - (c) Whether the internal mutual checking system works properly.
 - (d) Whether preparation of improvement measures for recurrence prevention or self-cleansing function are sufficient, and the responsibility of a division or person is clarified.
 - (e) Whether the response after the founding of such accident, etc. was appropriate.
 - (f) Whether, in the case of providing financial profit to compensate the whole or part of loss caused by the accident, etc., the financial instruments firm prepares books and records of financial profit to be provided and the basis for the computation; and whether the financial instruments firm implements the system that the internal audit division, etc. independent from sales divisions checks the compensation.
- (2) Supervisory methods and responses
- When the authority has recognized a financial instruments accident, etc. through a report or notification, etc. from a financial instruments firm, the authority shall recognize voluntary improvement of the business operation of the financial instruments firm through hearing for the fact, analysis of causes, improvement, measures for responses, etc. and collection of reports under Article 56-2.1 of the F.I. Act when needed.
- Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary response including the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-3 Solicitation and explanation system

III-2-3-1 Fitness standards

It is necessary for a financial instruments firm to ensure appropriate investment solicitation according to the particulars, etc. of each customer with remarks on types of transactions or trading conditions suitable for the knowledge, experience, financial resources, investment purpose or ability to judge risks of each customer under Article 40 of the F.I. Act.

Therefore, it is important to implement a customer control system to recognize accurately particulars, etc. and actual conditions of transactions of each customer, and verify it with the following remarks (particularly, the financial instruments firm shall pay due attention in the case of an Internet trading, considering its non-face-to-face nature).

- (1) Main focus points
 - ① Accurate recognition of particulars, etc. of customers and thorough control of customer information
 - (a) Whether a financial instruments firm makes an effort to recognize information of particulars, etc. of each customer such as the investment purposes and investment experience by means of maintenance of a customer card, etc., and ensure that each officer or employee makes an effort to make appropriate solicitation according to such particulars, etc. of each customer; and
 - (b) Whether the internal control division of a financial instruments firm makes an effort to recognize the state of the recognition of particulars, etc. of each customer and control of customer information, and verify whether appropriate solicitation is conducted when needed according to particulars, etc. of each customer, and makes an effort to build the system to ensure the effectiveness through reviewing the control methods of customer information.
 - ② Accurate recognition of actual trading conditions of customers and effective use thereof
 - (a) Whether, with respect to recognition of actual trading conditions of customers, a financial

instruments firm refers to trading conditions such as trading loss, valuation loss, frequency of transactions and fees for each customer account;

- (b) Whether a financial instruments firm, with respect to recognition of actual trading conditions of a customer for whom direct confirmation of trading conditions are necessary, makes an effort to perform timely and appropriate interview with such customer by the controller, etc. of each sales division (including a person responsible who is an internal controller and division manager and office manager; hereinafter the same), and recognizes trading conditions accurately. Whether a financial instruments firm makes a similar effort to recognize actual conditions of derivatives transactions, etc. in which the period of trading lasts long after the entering into a contract; and
 - (c) Whether the internal control division makes an effort to implement concrete methods for interview, etc. with customers by the controller, etc. at each sales division, inform all of the directors and employees of the method, recognize and verify the state of interview with customers and construct the system to ensure the effectiveness such as reviewing such method.
- (2) Supervisory methods and responses
- With respect to the issues for the system of a financial instruments firm regarding the fitness principles, etc. found through daily supervisory operations and notification of accidents, etc., the authority shall recognize the state of voluntary improvement at the financial instruments firm through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed. If a gross problem in the public interest and to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act. Further, if a violation of laws and regulations, etc. of a particularly grave nature has been found, the authority shall consider necessary responses including the issuance of an order to suspend business under Article 52.1.

III-2-3-2 Sales representative control system

It is important for a financial instruments firm to recognize the real state of solicitation by its sales representatives and to ensure the thorough compliance by sales representatives with the laws and regulations in order to ensure appropriate solicitation according to the particulars, etc. of each customer. Remarks shall be made on the followings for thorough compliance.

- (1) Main focus points
 - ① Recognition and improvement of manners, etc. of solicitation by sales representatives
 - (a) With respect to recognizing the real state of solicitation, whether, for example, the controller, etc. of each sales division makes an effort to recognize such manners through direct interviews with customers when needed and to take appropriate measures.
 - (b) Whether, with respect to handling securities intended to be placed with specific investors, the controller, etc. of each sales division makes an effort to recognize the actual real state by means such as making just enough responses in respect of giving a notice or furnishing written statements provided in Articles 40-5.1 and 40-5.2 of the F.I. Act, considering that small to medium sized corporations are included in specific investors and takes appropriate measures.
 - (c) Whether an internal control division sets out concrete method to recognize the real state of solicitation under (a) and (b) above and ensure to inform all officers and employees of such method, and recognizes and verifies the situation, when needed, and constructs the system to ensure the effectiveness such as reviewing such method.
 - ② Ensuring all officers and employees to have compliance mind
 - (a) Whether, with respect to ensuring all officers and employees to have compliance mind, a financial instruments firm, etc. conducts a case example training or external training, etc. suitable for training purposes and trainees, etc. to ensure all officers and employees to have compliance mind.
 - (b) Whether an internal control division takes measures to enhance the effectiveness through recognizing and verifying various training programs and performance and reviewing them.
 - (2) Supervisory method and response
- With respect to the issues of the system to control sales representatives of a financial instruments firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth or collection of reports under Article 56-2.1

of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses including the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-3-3 Regulations for advertisement, etc.

Representation of advertisements, etc. (which means advertisements, etc. as defined in Article 73.1 of the F.I. Business Ordinance; hereinafter the same) by a financial instruments firm is a gateway of investment solicitation of investors and providing information by clear and accurate representation is the most important in order to ensure the fulfillment of appropriate investment solicitation. This shall be achieved with the following remarks.

(Note) Advertisements, etc. include providing information to many persons by means of solicitation materials, websites on the Internet, postal mail, mail delivery, fax, electronic mail, leaflets, pamphlets or other methods. The judgment whether advertisements, etc. are applicable should not be made by appearance such as communication by an electronic mail, etc. with investors, image CM, gift with logos, etc., but be made individually and concretely considering the actual effect.

(1) Main focus points

① Remarks on important matters which influence on judgments of customers

- (a) Whether a financial instruments firm makes representation which will likely give customers false impression that services were free of charge including fees, remuneration, consideration or costs payable by customers, or significantly lower than actual charge.
- (b) Whether, if there is likeliness of incurring losses of principal or there is likeliness of incurring losses in excess of the initial capital, a financial instruments firm shows the fact clearly.

② Clear and accurate representation

Remarks shall be made on the followings for the judgment whether representation of the matters specified in Article 37 of the F.I. Act in advertisements, etc. is regarded as "clear and accurate representation" under Article 73.1 of the F.I. Business Ordinance.

- (a) Whether letters used in the representation are improperly less visible compared with letters used for other matters in the advertisement, etc. in terms of size, shape and color.
Particularly, in the case where the movement of indices such as interest rates and market prices will likely cause losses directly, such indices, the fact that there is likeliness of incurring losses, reasons therefor, and in the case where there is likeliness of incurring losses in excess of the principal, the direct reason, the fact and reasons that there is likeliness of incurring losses in excess of the principal are represented by letters and figures which are not significantly different, in size from other letters or figures on the advertisement.
- (b) Whether the advantage of transactions are emphasized and the disadvantage are less visible.
- (c) Whether, in the case where the advertisement, etc. is made on screen, time period necessary to read all of the matters required to be represented are ensured.

③ Remarks on exaggerated advertisement

- (a) Whether a financial instruments firm makes definitive presentation concerning the direction of movement of prices, value or considerations of securities, etc., or makes a presentation which gives false impression that profits would arise with certainty and stimulates the willingness of investment inappropriately.
- (b) Whether a financial instruments firm makes a presentation to guarantee the yield or bear the whole or part of losses, or makes a presentation to give false impression that such guarantee or bearing would be made.
- (c) Whether a financial instruments firm, in the case where the period for offering, number of persons to be offered are unlimited, makes a representation to give false impression that such period or number were limited.
- (d) Whether a financial instruments firm, because of the registration, makes a representation to give false impression that the Prime Minister, the Commissioner of the Financial Services Agency or other public organization recommend the firm or guarantee the contents of the advertisements, etc.

- (e) Whether a financial instruments firm makes a representation which violates or likely violates the Law against Unjustifiable Premiums and Misleading Representations, codes of prefecture and city governments under the Outdoor Advertisements Law or other laws or regulations.
- (f) Whether a financial instruments firm makes a representation which may be criticized as over-hyped advertisements socially.
- ④ Gathering customers for the purpose of solicitation
 - (a) Whether, before a financial instruments firm holds a seminar, etc. (regardless of the name such as lecture meeting, workshop, explanatory meeting, etc.; hereinafter the same) to gather retail customers, etc. and solicits such retail customers, etc. to enter into a financial instruments transactions contract (including explanation of specific products for the purpose of solicitation), the financial instruments firm states in advertisements, etc. or invitation letters, etc. for such seminar, etc. clearly that there is a purpose of solicitation to enter into a financial instruments transactions contract.
 - (b) "State clearly that there is a purpose of solicitation to enter into a financial instruments transactions contract" under (a) shall include not only the statement that the name of a seminar, etc. shows the relation with financial instruments transactions clearly, but also the clear statement that there is a purpose of solicitation.
- ⑤ System to examine advertisements, etc.
 - Whether a financial instruments firm has a person in charge of advertisements, etc. examination who conducts examination of advertisements, etc. and performs appropriate examination based on the examination standards in light of compliance with the provisions of Article 37 of the F.I. Act.
- (2) Supervisory method and response
 - With respect to the issues of advertisement, etc. by a financial instruments firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.
 - Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-3-4 Explanation to customers

Financial instruments firms are required to perform obligations for explanation such as disclosure of information necessary for judgment to customers, etc. accurately and equally because some of financial instruments transactions require a certain level of professional knowledge and all retail customers do not have sufficient professional knowledge or experience, etc. Accordingly, remarks shall be made on the followings for the explanation to customers.

(Note) It shall be noted that "explanation, etc. " includes explanation at a seminar, etc. in the case of gathering customers to the seminar, etc. to make solicitation effectively.

- (1) Main focus points regarding explanation system
 - ① Arrangement of explanation system based on suitability principles
 - Whether a financial instruments firm chooses properly the method and degree necessary for a customer to understand considering the knowledge, experience and financial resources of the customer and purpose of transactions in furnishing a written statement furnished prior to transactions, and ensures to implement a system to make an appropriate explanation based on the suitability principles by means such as preparing internal rules, etc.
 - ② Appropriate explanation of products and services, etc.
 - (a) Whether only merits of transactions are emphasized and explanation of demerits such as occurrence of losses or risk, etc is insufficient.
 - (b) Whether there is false or definite judgment in sales talk, etc.
 - (c) Whether explanation of products and transactions are objective; Whether there are arbitrary or subjective explanations.
 - (d) Whether the details of products or transactions (such as the basic nature of products and risks involved, type or factors of price movements) are explained to help for full

understanding; and particularly;

Whether a financial instruments firm makes an effort not to cause a customer to lose motivation to understand by means such as explanation of important matters to influence on customers' judgment first based on the purpose, etc. of the provisions regarding the order of entries into a written statement furnished prior to transaction.

- (e) Whether a financial instruments firm makes explanation which may give false impression regarding the financial instruments transactions, or makes explanation which may give false impression that a financial instruments firm, etc. would guarantee the principal. Whether a financial instruments firm, etc. makes explanation which gives false impression that, despite of the existence of likelihood of requirement for additional margin (which means guarantee money required to be deposited additionally if the total amount of guarantee money deposited by a customer becomes smaller than the amount of margin requirement; hereinafter the same) as a result of movement of market prices, etc., such likelihood were significantly small or the amount of additional margin were significantly smaller compared with the actual products in the case of derivatives transactions.
- (f) Whether, in the solicitation using materials containing the outlook of market prices, etc. prepared by a third party (including articles of news papers and analyst reports), the financial instruments firm uses only biased outlook of market prices arbitrarily.
- (g) Whether a financial instruments firm makes solicitation of products or transactions which causes improper burden to customers or lacks economic rationality, or the explanation lacks matters important for investment judgment.

③ Explanation of trade details, etc.

Whether a financial instruments firm, etc. shows the details of trade (the date and time of trade, the amount of trade or trade value, etc.) to its customer properly by a written statement furnished at the time of the conclusion of transactions if the customer so requested, after the conclusion of the financial instruments transactions.

④ Remarks on over-the-counter derivatives transactions, etc.

Whether a financial instruments firm conducts over-the-counter derivatives transactions such as currency options transactions and interest rate swap transactions with a corporate customer with the following remarks. Whether a financial instruments firm treats transactions with risk characters similar to over-the-counter derivatives transactions (such as sale of structured debt securities) in a manner equivalent thereto.

- (a) Whether a financial instruments firm makes appropriate and sufficient explanation concerning the details of products and risks of such over-the-counter derivatives transactions by means such as furnishing a written statement which explains concretely and in a manner that investors understand easily including the followings:
 - a. Whether a financial instruments firm explains the assumed largest amount of loss under the worst scenario (scenario based on reasonable resumption such as data in the event of stress in the past; hereinafter the same) regarding the level, etc. of a financial instrument, etc. which is an underlying object of such over-the-counter derivatives transactions (including the level of volatility when needed; hereinafter the same) including the possibility that the loss will expand further under the conditions different from the presumption in a manner that customers can understand.
 - b. Whether, if a customer confirms the amount of loss acceptable for the over-the-counter derivatives transactions and there is a possibility that a customer may suffer the amount of losses exceeding the acceptable amount even in the case where the above worst scenario is not realized, a financial instruments firm explains such fact in a manner that the customer can understand.
 - c. Whether a financial instruments firm explains the possibility of influencing on business management or financial conditions grossly by such over-the-counter derivatives transactions under specific conditions of a financial index, etc. in a manner that customers understand.
 - d. Whether, if a financial instruments firm uses examples, etc. different from actual over-the-counter derivatives transactions by necessity for explanation, the financial instruments firm explains that the examples, etc. are different from actual transactions.
- (b) Whether a financial instruments firm makes appropriate and sufficient explanation concerning the cancellation before the maturity and the amount of cancellation settlement money of such over-the-counter derivatives transactions by means such as furnishing a written statement which explains concretely and in a manner that investors understand easily including the followings:

- a. Whether, if such over-the-counter derivatives transactions cannot be canceled before the maturity in principle, a financial instruments firm explains the fact in a manner that customers can understand.
 - b. Whether, if cancellation of the over-the-counter derivatives transactions before the maturity results in payment or receipt of cancellation settlement money, a financial instruments firm explains the fact and the detail of such cancellation settlement money (including the estimated amount of cancellation settlement money under the worst scenario for the level, etc. of a financial index, etc. and, if there is a possibility that such cancellation settlement money will exceed the estimated amount, such fact) in a manner that customers can understand.
 - c. Whether, if a customer confirms the acceptable amount of cancellation settlement money for the over-the-counter derivatives transactions and there is a possibility that the customer may suffer the amount of loss exceeding the acceptable amount even in the case other than the worst scenario, a financial instruments firm explains such fact in a manner that the customer can understand.
- (c) Whether, if the over-the-counter derivatives transaction is proposed for hedging purpose, a financial instruments firm confirms the followings and makes appropriate and sufficient explanation of the result of the confirmation in a concrete manner and a manner that customers understand easily:
- a. Whether a financial instruments firm confirms that the over-the-counter derivatives transaction works as an effective hedging tool for continuous business management even considering the customers' business conditions and competitive situation in the market. (Note 1)
 - b. Whether a financial instruments firm confirms that the functioning as a hedging tool mentioned above is expected to continue until the end of the contract. (Note2)
 - c. Whether a financial instruments firm confirms that such over-the-counter derivatives transactions will not cause the difficulty for the customer to look into the future business management. (Note 3)
- (Note 1) With remarks to judge, for example, the existence, etc. of price bargaining power or pricing power to reduce the influence of the movement of foreign exchange rates or interest rates comprehensively.
- (Note 2) With remarks that, even if hedging tool itself does not carry losses, hedging needs of a customer are influenced by a change of business conditions, etc. of the customer such as shrinkage of presumed business scale or effective functioning of hedging may not continue until the end of the contract period for such needs.
- (Note 3) With remarks that the stabilization of the purchase price, etc. by hedging may influence on the price competitiveness of the customer.
- (d) Whether a financial instruments firm takes measures such as collecting acknowledgment, etc. from a customer and keeping it in order to acknowledge that the explanation was made to the customer based on the matters referred to in the above (a) to (c).
 - (e) Whether, with respect to solicitation of over-the-counter derivatives transactions to a customer which is exempt from prohibition of unrequested solicitation, a financial instruments firm confirms hedging needs through the trading record of the customer and solicits to enter into a contract within the scope of its needs based on the laws and regulations (Note).
- (Note) "Juridical person engaging in the foreign trade or other business regarding foreign exchange transactions" (Article 116 (2) of the F.I. Business Ordinance) which is exempt from prohibition of unrequested solicitation shall include a construction firm in Japan who imports, for example, lumber from overseas in effect through a trading firm in Japan without direct trading with an overseas exporter, but does not include purchase of imported lumber from a firm in Japan.
- (f) Whether, if a customer requests, periodically or when needed, a financial instruments firm provides or gives a notice of market price information of the customer's positions or the amount of cancellation settlement money (including, if a customer requests to inform that the amount of positions reached a certain amount of loss or cancellation settlement money, such fact) as of such time.
 - (g) Whether, with respect to confirmation of a customer's intention to enter into a contract for such over-the-counter derivatives transactions, a financial instruments firm implements a system for confirmation of intention considering a decision-making process of the customer in accordance with the details and scale of the contract, the types and scale of the business,

business management system, etc.

It shall be noted that, if, for example, the over-the-counter derivatives transactions the contract of which a customer wishes to enter into may have big influence on the future business management, it is important to confirm whether such entering into such contract has been decided by the board of directors, etc. of the customer.

⑤ Method to explain by Internet

In the case where financial instruments transactions are conducted through the Internet, "explanation to the customer by methods and to the extent necessary for the customer to understand" as provided in Article 117.1 (1) of the F.I., Business Ordinance, the financial instruments firm shall be deemed to have made such explanation, if a customer reads the explanation represented on the screen of the customer's computer and the customer's understanding is confirmed by the method that the customer clicks a button on the screen after the customer has understood the contents.

(2) Remarks on explanatory documents

① The authority shall instruct a financial instruments firm to keep explanatory documents provided in Articles 46-4 and 47-3 of the F.I. Act (in III-2-3-4 (2), III-3-1 (9) and V-2-2-2 (2), referred to as "explanatory documents") accessible upon a customer's request.

② The date on which a financial instruments firm kept at business offices shall be recorded in explanatory documents, when needed.

③ Nothing shall preclude each financial instruments firm from adding disclosing matters based on such financial instruments firm's judgment to matters specified by the laws and regulations in explanatory documents.

(2) Supervisory method and response

With respect to the issues of a system of explanation to customers by a financial instruments firm, etc. found through the daily supervisory operations or notification of accident, etc., the supervisory authority shall, based on the above focus points, recognize voluntary improvement of business management of the financial instruments firm through collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-4 Control of customer information

Information regarding customers is the basic of financial instruments transactions, and therefore it is very important to ensure appropriate control of customer information.

Particularly, information regarding customers who are individuals shall be handled appropriately in compliance with the Law regarding Protection of Information of Individuals (hereinafter referred to as "Individuals Information Protection Law"), the F.I. Business Ordinance, Guidelines regarding Protection of Information of Individuals in Financial Area (hereinafter referred to as "Protection Law Guidelines") and the Operational Guidelines for Security in the Guidelines regarding the Protection of Information of Individuals in the Financial Area (hereinafter referred to as "Operational Guidelines").

(1) Main focus points

① Whether a financial instruments firm sets out concrete standards for handing of customer information and ensure all officers and employees to be aware of the standards thoroughly; and particularly whether a financial instruments firm establishes the standards for transferring such information to other parties after full consideration that procedures are taken in compliance with the above laws, regulations, Protection Law Guidelines and Operational Guidelines.

② Whether a financial instruments firm implements a system to conduct timely and appropriate verification of the control of customer information including thorough control of access to customer information and measures to prevent taking out customer information by internal persons, constructs stronger information control system such as defense from unlawful access from outside.

③ Whether, with respect to the security and supervision over employees regarding information of customers who are individuals under Article 123.1 (6) of the F.I. Business Ordinance, the following measures are taken as measures necessary and appropriate for preventing leakage,

loss or damage of such information:

(Measures necessary and appropriate for security)

- (a) measures under Article 10 of Protection Law Guidelines; and
- (b) measures under I and Schedule 2 of Operational Guidelines.

(Measures necessary and appropriate for supervisions over employees)

- (a) measures under Article 11 of Protection Law Guidelines; and
- (b) measures under II of Operational Guidelines.

- ④ Whether a financial instruments firm, etc. takes measures to use information about races, creed, family origin, domicile of origin, health care or criminal background or other special undisclosed information ^(note) of customers who are individuals only for the cases listed in the items of Article 6.1 of the Protection Law Guidelines under Article 123.1 (7) of the F.I. Business Ordinance.

(note) other special undisclosed information means:

- (a) information about membership of labor unions;
- (b) information about ethnic group; and
- (c) information about sex life.

- ⑤ Whether a financial instruments firm implements a system, in the event that leakage, etc. of customer information has occurred, to inform customers concerned and make a report to the authority and publish quickly and appropriately in order to prevent the secondary damage, etc.

- (2) Supervisory method and response

With respect to the issues of the customer information control system of a financial instruments firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-5 Settlement of grievance system

The quick and appropriate response by financial instruments firms to grievances or enquiries from customers and winning customers' understanding has the meaning to supplement ex-post facto obligation for explanation to investors and is one of the most important activities for financial instruments firms to protect investors. The authority shall verify the settlement of grievance systems of financial instruments firms with the following remarks.

- (1) Main focus points

- ① Approach to grievances, etc. by firms

Whether the board of directors recognizes the likeliness of suffering disbenefit such as the downfall of credit by grievances, etc. from customers and takes appropriate measures.

- ② Implementation of grievance, etc. settlement system

Whether a financial instruments firm establishes a division in charge of grievances, etc. and procedures for the settlement clearly and implements a system to make a quick and appropriate settlement and response. Whether a financial instruments firm implements a system to share information among persons concerned according to the case such as making a report of grievances, etc. which may have a significant impact on business to the internal audit division or the board of directors promptly.

- ③ Performance of explanation to customers

Whether a financial instruments firm makes full explanation for matters for which the customers filed grievances, etc. Whether a financial instruments firm implements the follow-up system for the response to grievances, etc.

Whether appropriate disclosure, etc. is made in accordance with the Individual Information Protection Law, etc. in the case where a customer requests the disclosure of information of the customer's trading record, etc.

- ④ Feed back

Whether the substance of grievances, etc. is recorded and kept appropriately and accurately, and such records are used for improvement of manners of solicitation and the business

operation system and implementation of measures to prevent the recurrence through the accumulation and analysis of such records.

Whether a financial instruments firm confirms consultation for grievances, etc. regarding products or trading the contract of which the customer entered into after making an effort to improve the solicitation system or operational process or preparation, etc. of measures to prevent reoccurrence and confirms the effectiveness of such effort.

(2) Supervisory method and response

With respect to the issues of the grievance settlement system of a financial instruments firm found through the daily supervisory operations, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, the authority shall consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-6 Identification and notification of doubtful transactions

It is impermissible that a financial instruments firm which takes an important role as an intermediary, etc. on markets involves in, or is used by, an organized crime, for example, payoff scandals to corporate extortionists.

It is necessary to construct company-wide and strong compliance system in order to prevent a financial instruments firm from being used for organized crimes, money laundering or financing of terrorism and contribution to the expansion of crime proceeds.

Particularly, construction of identification under the Law on Prevention of Transfer of Profits by Crimes (hereinafter referred to as "Crime Profit Law") and internal control system regarding "notification of suspicious transactions" has important meaning to prevent misuse of financial services by organized crimes and to ensure the trust on financial and capital markets in Japan.

(1) Main focus points

The authority shall verify the system to perform identification and "notification of suspicious transactions" under the Crime Profit Law with the following remarks.

① Whether a system to perform identification under the Crime Profit Law accurately is implemented:

(a) Whether a financial instruments firm implements the system and procedures to perform identification clearly by its internal rules, etc., and whether a financial instruments firm informs all of its officers and employees of the system and procedures and ensures that the officers and employees understand them fully.

Particularly, the followings should be clarified:

- a. the division in charge, responsible person and its role in respect of identification;
 - b. the judgment of appropriateness of, and recognition, verification and analysis of the state of performance of, the identification conducted by the division in charge, and the division having the overall control, the responsible person (including a person who makes the final judgment in the firm regarding the operations) and its role;
 - c. the reporting system at the divisions a. and b. above (including the coordination system among relevant divisions);
 - d. recording of the identification of each customer and timely and appropriate preparation and retention of records of transactions with each customer;
- (b) Whether, in making identification, the financial instruments firm recognizes the particulars of each customer appropriately and confirms the believability and reasonability by means of providing identification documents. Whether a financial instruments firm makes responses and control appropriately if a problem, etc. is found regarding a customer.

Whether, with respect to identification information recognized from a customer, a financial instruments firm makes continuous effort to recognize the particulars of the customer through continuous monitoring, etc. of transactions for customer account regularly and updates customer information:

Measures to recognize particulars of customers include, for example, the followings:

- a. A financial instruments firm conducts name identification of customer accounts which have the same telephone numbers and e-mail addresses periodically, and takes measures

such as extraction of customer accounts having different addresses and family names or customer accounts having the same pass words, and confirm that the counterparty is the identical person by means of recognizing the actual transactions of such customer or communication with the customer.

- b. A financial instruments firm recognizes a change in identification information such as the address timely by means of, for example, informing all customers periodically that, if there is a change in identification information, the customer is required to inform the financial instruments firm of the change.
 - (c) Whether a financial instruments firm establishes the policies to accept customers in its internal rules, etc. Whether such policies to accept customers apply accurately to the particulars of customers recognized through taking identification procedures.
 - (d) Whether, if a financial instruments firm has doubts about the truth or validity on identification information acquired in the past or doubts that the counterparty masquerades as a nominee for trading, the financial instruments firm identifies the customer again by means of, for example, collecting identification documents.
 - (e) Whether, in identifying a customer, the financial instruments firm takes measures suitable for the trading methods (such as non-face-to-face transaction, etc. through the Internet).
 - (f) Whether, in recruiting officers or employees, the financial instruments firm makes selection considering, among others, appropriate money laundering measures.
 - (g) Whether a financial instruments firm conducts training and education of officers and employees concerning identification periodically and continuously. Whether a financial instruments firm conducts valuation and follow-ups for the degree of understanding by officers and employees who have been trained, including the practices in the course of daily operations.
 - (h) Whether a financial instruments firm ensures the effectiveness of identification by means of recognizing and verifying the identification and reviewing the identification methods, through periodical internal checking and internal audits.
- ② Whether the system to perform "notification of doubtful transaction" under the Crime Profit Law has been implemented:
- (a) Whether a financial instruments firm implements the internal system and procedures to perform "notification of doubtful transactions" by its internal rules, etc. Whether a financial instruments firm ensures all of its officers and employees be aware of the system and procedures thoroughly and the officers and employees understand them fully.
Particularly, the followings should be clarified:
 - a. the division to find "doubtful transactions", a responsible person and its role;
 - b. the division to supervise the finding of "doubtful transactions" in the firm such as the judgment of appropriateness of "doubtful transactions" recognized under the above (a), recognition, verification, analysis, etc. of the performance thereof, a responsible person (including a person who makes the final judgment in the firm for such notification) and such person's role; and
 - c. the reporting system in the divisions in the above a. and b. (including the coordination system with other relevant divisions).
 - (b) Whether it is ruled that, if any transaction is judged to be "doubtful transactions," the supervising division files a notification with the authority promptly.
 - (c) Whether, in judging that "doubtful transactions" is applicable to a transaction, judgment of necessity of notification is made after considering comprehensively identification information and the circumstances at the time of trading acquired by a financial instruments firm and other concrete transaction related to such trading held by the financial instruments firm. Whether the financial instruments firm, if any problem, etc, is found in respect of such trading, etc., makes responses or manages appropriately.
- (Note) Although it is one of useful methods that a financial instruments firm accumulates information which triggers "doubtful transactions" or establishes formal standards, it is desirable that a financial instruments firm, in establishing stylized internal standards, takes measures to judge types and forms of each trading comprehensively in order to prevent dependence only on such standards and losing of substances of notification.
- (d) Whether the types and scale of business of a financial instruments firm and the particulars of a customer are considered to judge "doubtful transactions".

The particulars of a customer to be considered could include the nationality (for example, countries and areas which are uncooperative to money-laundering measures published by FATF), politically exposed persons or not, customer's business, etc., trading

volume, trading types and modes such as frequency, etc. and domestic trading or overseas trading.

- (e) Whether, in recruiting an officer or employee, selection is made with the consideration of appropriate performance of money-laundering measures.
- (f) Whether a financial instruments firm trains or educates its officers or employees regarding "notification of doubtful transactions" periodically and continuously. It could be useful for acceleration of understanding by officers or employees that "reference cases of doubtful transactions" (refer to the website of the Financial Services Agency) should be referred or used as education materials, etc. concerning cases to which "notification of doubtful transactions" could be applicable or cases, etc. for which the financial instruments firm has filed a notification in the past in such opportunities of training, etc.

Further, whether valuation and follow-ups are conducted at an appropriate timing concerning the degree of understanding by officers and employees trained or educated based on practices in the course of daily operations.

- (g) Whether, with respect to "notification of doubtful transactions," a financial instruments firm recognizes and verifies the performance thereof and reviews the performance methods through periodical checking or internal audit in the firm in order to ensure the effectiveness.
- ③ Whether a financial instruments firm recognizes fully that identification and "notification of doubtful transaction" has interrelation and recognizes basic information of customers by means of accurate performance of identification and judges after considering such information and trading types and modes, etc. of customers comprehensively, and has built up integrated and unified internal system, etc. in order to ensure "notification of doubtful transactions".
- (2) Supervisory method and response

With respect to the issues of the internal control system regarding the performance of obligation of identification and obligation of notification of doubtful transactions by a financial instruments firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-7 Operational risk control system

(1) Operational risk control

Operational risk means the risk that customers or financial instruments firms may suffer losses arising from the negligence of accurate operation or accident or unlawful acts, etc. by officers or employees. As a financial instruments firm must make an effort to gain the trustworthiness through proper implementation of the internal control system for operational risks and sound and appropriate management of business, the financial instruments firm shall verify it with the following remarks.

① Main focus points

- (a) Whether a financial instruments firm understands that an operational risk exists in every business and implements an appropriate operational risk control system.
- (b) Whether a financial instruments firm recognizes that it is important to reduce operational risks and takes concrete measures to reduce operational risks.
- (c) Whether a financial instruments firm implements a system to ensure mutual checking including the system that the control division is independent from sales divisions; whether rules for operations are set out clearly; and whether such rules are reviewed appropriately when needed.
- (d) Whether the internal audit division performs internal audit appropriately in order to audit the operational risk control system; whether the control division of operational risks takes measures to check the operational control system at sales divisions and sales offices; whether both of the divisions coordinate and promote the improvement of operational level of sales divisions and sales offices.

(2) Outsourcing of operations

In the case of outsourcing operations, the financial instruments firm shall be liable to the

ultimate responsibility for such outsourced operations, and therefore the financial instruments firm shall ensure the protection of investors and sound business management with, for example, the following remarks according to the scale of business. In addition to the following general focus points, each financial instruments firm needs to verify some more specific points according to the outsourced operations.

① Main focus points

- (a) Whether a financial instruments firm sets out policies and procedures clearly for the selection of operations to be outsourced and outsourcee;
- (b) Whether a financial instruments firm implements a system to control risks for outsourced operations fully;
- (c) Whether a financial instruments firm takes measures to prevent obstruction, which may arise from outsourcing, for the performance of obligations to the supervisory authority such as inspection, report and providing of records;
- (d) Whether a financial instruments firm ensures outsourcing not to influence on rights and obligations between the financial instruments firm and its customers and to keep the same right as the right given to the customer when the financial instruments firm conducts operations by itself;
- (e) Whether a financial instruments firm implements a system to prevent interfering convenience for customers in the event that contractual services are not provided for outsourced operations;
- (f) Whether, if the financial instruments firm outsources handling of information of customers who are individuals, the financial instruments firm takes the following measures which are necessary and appropriate to prevent leakage, loss or damage of such information regarding supervising of such outsourcee; and
 - a. measures under Article 12 of the Protection Law Guidelines; and
 - b. measures under III of the Operational Guidelines; and
- (g) Whether, with respect to complaints, etc. for outsourced operations, the financial instruments firm implements an appropriate grievance consulting system through establishing a contact place for customers to communicate directly with the financial instruments firm.

(3) Supervisory method and response

With respect to the issues of the operational risk control system and outsourcing control system of operations of a financial instruments firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth of the financial instruments firm or its outsourcee or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-8 System risk control system

System risk means risks that customers or a financial instruments firm may suffer losses arising from a defect, etc. in a system such as failure or malfunction of a computer system and risks that customers or a financial instruments firm may suffer losses arising from unlawful use of computer. The risk of unlawful access to or leakage of important information is increasing because of upgrading and more complexity of information system of a financial instruments firm as a result of the system integration subsequent to management realignment, development of new products, expansion of services and the expansion of computer network.

Stable and safe performance of a system is requisite to gain the trust on financial instruments markets and financial instruments firms, and it is very important to enhance and strengthen a system risk control system.

(1) Main focus points

The authority shall verify the system risk control system with the following remarks according to the scale of business of a financial instruments firm (with respect to the details of focus points, refer to the securities investigation manual when needed).

- ① Recognition, etc. of system risk
 - (a) Whether the board of directors, etc. recognizes the system risk fully and company-wide policies of risk control has been established.
 - (b) Whether a financial instruments firm implements a system to make a report of information of system risk to the management appropriately.
- ② Building up of appropriate risk control system
 - (a) Whether policies of system risk control has been established and such control system has been constructed.
 - (b) Whether the location and type of risk to be controlled is identified in accordance with concrete standards.
 - (c) Whether the system risk control system is effective such as maintaining appropriate quality by lowering the frequency and scale of system failure according to system circumstances through recognition and analysis of its business situation and system failure, etc.
- ③ System auditing
 - (a) Whether a system-savvy audit staff in the internal audit division independent from the system division audits the system periodically.
 - (b) Whether auditing covers the overall business having system risk.
- ④ Implementation of security measures
 - (a) Whether policies for security are set out.
 - (b) Whether a financial instruments firm appoints a security controller who controls security appropriately in accordance with established policies, standards and procedures; and whether a security controller supervises the overall control of system, data and network.
- ⑤ Control of outsourced system

Whether the risk control on outsourced system is performed appropriately.
- ⑥ Contingency plan
 - (a) Whether a contingency plan is set out and an emergency system is constructed.
 - (b) Whether the effectiveness of the contingency plan is maintained through continuous reviewing according to the business situation or system circumstances, etc.
- ⑦ System integration risk
 - (a) Whether officers and employees of a financial instruments firm recognize system integration risk fully and a control system for such risk is implemented.
 - (b) Whether a testing system is implemented. Whether the testing plan fits the system development associated with system integration.
 - (c) Whether, in the case of outsourcing of business operations, the financial instruments firm constructs the system that the firm takes initiative to involve in the system integration.
 - (d) Whether a financial instruments firm uses valuation by the third party such as auditing by a system auditor in judging about important matters for system integration.
 - (e) Whether a financial instruments firm maintains a contingency plan, etc. to encounter unexpected contingency.
- ⑧ Response to system failure
 - (a) Whether a financial instruments firm has taken appropriate measures to prevent customers' unnecessary confusion when a system failure occurs.
 - (b) Whether a financial instruments firm has analyzed causes for system failures which have occurred in the past and has taken countermeasures.
 - (c) Whether a financial instruments firm implements a system to report to the authority promptly after a system failure occurs.
- (2) Supervisory method and response
 - ① When a problem was recognized:

With respect to the issues of the system risk control system of a financial instruments firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth to the financial instruments firm and its outsourcee or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 or 52.1 of the F.I. Act.
 - ② When systems are integrated:

When a financial instruments firm has announced system integration as a result of business management realignment such as a merger or announced system integration, etc., the authority shall, when needed, require to provide information of the schedule etc. and progress for the

system integration, a concrete plan for smooth system integration, etc., internal control system (including internal audit) for system integration risk and other matters, and to make a report under Article 56-2.1 of the F.I. Act periodically for the period from the announcement of the merger, etc. until the completion of such system integration.

(3) Response to system failure

① The authority shall, promptly after the financial instruments firm has recognized the occurrence of computer system failure, require to make a report of the fact to the authority and require to submit "Failure Occurrence, etc. Report" (Form III-1) to the authority.

The authority shall, at the time of recovery or clarification of causes, require making a report of the fact again. (If, however, the cause for recovery has not been clarified, reporting of the current situation shall be made within one month.)

Upon receiving a report, the local finance bureau shall immediately inform the division in charge of the Financial Services Bureau.

(Note) A financial instruments firm shall make a report of a system failure which is:

regardless of causes, failure of systems or machines and their equipments (both hardware and software) effectively used by the financial instruments firm or a person commissioned by the financial instruments firm to conduct operations, and which causes or will likely cause influence on financial instruments transactions, settlement, debt or credit of money, cash management, recognition of financial conditions, other convenience of users.

However, the case where, even if such influence on a part of system or machines or equipments are seen, such influence does not occur effectively by being replaced by other system or machines or equipments quickly (for example, the case where, even if an order entry system fails to work during non trading session, an alternative system equivalent to such order entry system begins to work before the opening of such trading session) is excluded.

Reporting shall be required in the case where a failure has not occurred but the failure described above will likely occur because of the advance notice of cyber attack or detection of cyber attack.

② The authority shall require additional reporting under Article 56-2.1 when needed, and if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-9 Crisis control system

Risks that financial instruments firms expose are being diversified and more complex in these years and, coupled with the changes in business circumstances surrounding financial instruments firms such as the advancement of informationization, possibility that crises beyond the ordinary risk control will occur cannot be denied, and therefore crisis control becomes more important. Even when such various crises become real, it is desirable that financial instruments firms make efforts to prevent unnecessary confusion in the markets or society through maintaining the function of financial instruments firms as much as possible in light of the public nature of their business. In supervising financial instruments firms, based on the above, the authority shall verify, according to the scale of business, with the following remarks.

(1) Main focus points

① Responses at ordinary time

(a) Whether a financial instruments firm recognizes what are crises and makes an effort to prevent crises by periodical checking and training at ordinary time whenever possible (with respect to crises unavoidable, takes measures).

(b) Whether a financial instruments firm prepares a crisis control manual. Whether the crisis control manual is reviewed constantly according to the actual conditions of the firm and the risk circumstances surrounding the firm to maintain its effectiveness. It is desirable that, in preparing a crisis control manual, the financial instruments firm designs the crisis control manual on the basis of judging the objective level.

(Reference) Examples of possible crises

- natural disaster (earthquake, wind and flood damage, abnormal climate, infection, etc.);
- terrorism, war (including meeting in foreign countries);
- accident (large scale blackout, computer accident, etc.);

- rumor (word-of-mouth, Internet, electronic mail, guessing report, etc.);
 - crimes aiming at corporations (threats, intervention by antisocial forces, data steal, kidnapping of officers or employees);
 - business trouble (responses to grievances or request for consultation, typing error, etc.);
 - personnel trouble (accidents, crimes, internal strife, sexual harassment, etc. in respect of officers and employees);
 - labor trouble (whistle-blowing, death by overwork, industrial disease, loss of specialist, etc.).
- (c) Whether the crisis control manual emphasizes initial responses such as objective assessment of the situation by accurate recognition of the situation at the initial stage of crisis occurrence and sending information.
- (d) Whether the crisis control manual clarifies the responsibilities at the time of crisis occurrence and implements a reporting and communications system internally and to parties concerned (including the relevant authorities or the time of crisis occurrence). Whether a financial instruments firm implements the communication system to overseas supervisory authorities and other relevant organizations according to the possibility of influencing abroad and the level and types of crises. It is desirable that a financial instruments firm implements a system of responses to occurrence of crises for each of divisions, business offices, etc. under the task force to supervise the entire organization according to the level and types of crises.
- (e) Whether a financial instruments firm makes daily efforts to send information or collect information on a detailed basis.
- ② Responses at the time of crisis occurrence
- (a) In the event that a crisis situation has occurred or will likely occur, the authority shall make an effort to recognize the situation through periodical hearings or confirming conditions at the place where the crisis has occurred whether responses to the crisis by the financial instruments firm (system to control crises, communication with persons concerned, sending information) are made sufficient for the level or type of the crisis and collect reports under Article 56-2.1 of the F.I. Act when needed until the situation calms down.
- (b) In the above event, the authority shall make a report to the division in charge of the Financial Services Agency and make close communication among divisions.
- ③ Responses after the calm-down of the situation
- If the authority deems it necessary to verify the responses at the time of the occurrence of crises after the crisis situation for a financial instruments firm has calmed down, the authority shall collect reports under Article 56-2.1 of the F.I. Act from the financial instruments firm concerning the outline of the case, responses, analysis of the source of crises and efforts to prevent the recurrence.
- ④ Crisis control system in respect of rumors
- (a) Whether a financial instruments firm implements the system to respond to rumor risk. Whether a financial instruments firm implements the provisions for the methods to respond at each division of the head office and business offices at the time of the occurrence of rumor. It is desirable to study the method to respond at the time of the occurrence of the rumor of other firm or trading partner.
- (b) Whether a financial instruments firm checks rumors periodically for each of media which are used to spread rumors (for example, Internet, conjecture articles, etc.).
- (2) Supervisory method and response
- With respect to the issues of the risk control system of operations of a financial instruments firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.
- Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

III-2-10 Measure to prevent financial instruments intermediary firms from violation of laws or regulations

(1) Remarks on prevention of the violation of laws or regulations by financial instruments intermediary firm

It is important that, in commissioning business to a financial instruments intermediary firm, the financial instruments firm instructs the financial instruments intermediary firm to implement a customer control system to recognize the particulars, etc. of each customer and trading conditions accurately and requires the financial instruments intermediary firm to comply with the laws and regulations thoroughly after recognizing the real state of investment solicitation in order to ensure appropriate investment solicitation according to the particulars, etc. of each customer. The authority shall verify the system to prevent the violation of the laws or regulations with the following remarks.

① Accurate recognition of particulars, etc. of customers and thorough control of customer information

(a) Whether a financial instruments firm, with respect to particulars, etc. of customers such as investment purposes and investment experience, etc. of each customer, makes an instruction to a financial instruments intermediary firm necessary to share, and recognize timely, customer information after obtaining a consent from the customer and implements concrete methods to require the financial instruments intermediary firm to make an effort to make appropriate solicitation to fit such customer particulars, etc. in the investment solicitation and informs all of financial instruments intermediary firms concerning such methods and ensures the compliance.

(b) Whether a financial instruments firm, with respect to the control of customer information such as particulars, etc. of customers, establishes concrete handling standards to require a financial instruments intermediary firm to comply after full consideration in light of secrecy obligation, etc. and informs all financial instruments intermediary firms concerning such standards and ensures the compliance.

(c) Whether the division in charge of the control of a financial instruments firm makes an effort to recognize the state of recognizing customer particulars, etc. and the control of customer information by a financial instruments intermediary firm, verifies the appropriateness of solicitation in light of customer particulars, etc. when needed, and makes an effort to construct a system to ensure the effectiveness such as requiring the review of methods to control customer information.

② Recognizing the real state of investment solicitation by financial instruments intermediary firm and improvement thereof

(a) Whether, with respect to recognizing the actual state of investment solicitation by a financial instruments intermediary firm, the responsible person, etc. in a division in charge of control makes an effort to recognize the real state and takes appropriate measures through, for example, holding interview, etc. with a customer when needed.

(b) Whether the division in charge of the control of a financial instruments firm implements concrete methods to recognize the real state of investment solicitation by a financial instruments intermediary firm, informs all financial instruments intermediary firms of the methods and ensures the compliance, and recognizes and verifies the enforcement state when needed and makes an effort to construct the system to ensure the effectiveness through reviewing the methods.

(c) Whether the division in charge of the control of a financial instruments firm recognizes the state whether a financial instruments intermediary firm explains appropriately and takes measures such as requiring the improvement when needed.

③ Ensuring financial instruments intermediary firm to have compliance mind

(a) Whether, with respect to ensuring the compliance mind of a financial instruments intermediary firm, a financial instruments firm conducts case training and external training, etc. considering the purpose of training and trainee, etc. and makes an effort to improve compliance mind of a financial instruments intermediary firm.

(b) Whether the division in charge of the control of a financial instruments firm recognizes and verifies the details and state of various types of training and makes an effort to enhance the effectiveness of training in respect of a financial instruments intermediary firm.

(2) Supervisory methods and responses

With respect to the issues of measures of a financial instruments firm to prevent a financial instruments intermediary firm from the violation of the laws or regulations found through daily supervisory operations and notification of accidents, etc., the authority shall recognize the state of voluntary improvement at the financial instruments firm through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed. If a gross problem

in the public interest and to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act. Further, if a violation of laws or regulations of a particularly grave nature has been found, the authority shall consider necessary responses including the issuance of an order to suspend business under Article 52.1.

III-2-11 Prevention of damages by antisocial forces

(1) Significance

It is very important issues to reject antisocial forces from the society in order to ensure the orderliness and safety of the society and it is necessary and important for corporations to promote an effort to reject the relationship with antisocial forces in order to fulfill the social responsibilities. Particularly, a financial instruments firm has publicness and economically important functions, and therefore it is required to reject antisocial forces from financial instruments transactions in order to prevent not only a financial instruments firm itself and its officers and employees but also various stakeholders such as customers, etc. from suffering damages.

It is essential to encounter antisocial forces according to laws and regulations without bowing to antisocial forces, and therefore a financial instruments firm needs to make an effort to construct the system to reject the relationship with antisocial forces for the purpose to maintain public trust on the financial instruments firm and to ensure appropriate and sound business of the financial instruments firm based on the purpose of "Guidelines for Prevention of Damages of Corporations by Antisocial Forces" (Common Consent by Board Meeting of Cabinet Conference for Crime Countermeasures dated June 19, 2007).

Particularly, antisocial forces acquire funds in an increasingly sophisticated manner recently and construct trading partnership skillfully by using group companies to dissemble ordinary economic trading and cause troubles later. It is seen that antisocial forces such as organized crime groups intervene the financial instruments market to earn money through initial public offerings on emerging markets or equity financing on public stock markets. Decisive responses and concrete responses by the management team are necessary to encounter such cases appropriately.

It shall be noted that postponement of concrete effort for solution of problems with the excuse of the danger of unexpected situation such as the threatening of the safety of employees may result in larger final damages to the financial instruments firm and its officers and employees, etc.

(Reference) "Guidelines for Prevention of Corporations from Damages by Antisocial Forces" (Common Consent by Board Meeting of Cabinet Conference for Crime Countermeasures dated June 19, 2007)

① Principles to prevent damages by antisocial forces

- responses as an organization;
- coordination with external specialized organization;
- complete cut-off of relations including trades;
- legislative responses for civil affairs and criminal affairs in the emergency situation;
- prohibition of backstage trades or giving funds.

② Identifying antisocial forces

In order to identify "antisocial forces" which are groups or individuals and use violence, power or fraudulent methods to seek economic profit, it is important to focus on particulars such as crime groups, crime group related corporations, corporate extortionist, bullies claiming as social activists, bullies claiming as political activities and intellectual crime groups and also focus on acts such as violent demanding and unreasonable demanding exceeding legal obligation. (Refer to Instructions issued by the Deputy Director-General of the National Police Agency dated October 25 of 2008 "Organized Crime Countermeasure Outline")

(2) Main focus points

The authority shall verify the system to cut off the relationship with antisocial forces, considering individual trades with the following remarks.

- #### ① Whether, if a financial instruments firm did not have any relationship with antisocial forces but has had a relationship with a party without knowing that the party is an antisocial force, the financial instruments firm makes an effort to dissolve such relationship as soon as possible at the time when the financial instruments firm knew that the party is an antisocial force with the following remarks:

- (a) prevention of becoming a trading partner of an antisocial force by making a preliminary review appropriately to prevent a trading with an antisocial force or introduction of clauses to reject crime groups in a contract or a trading agreement when needed;
 - (b) appropriate control of shareholder information by confirming trading conditions of shares of the stock of the financial instruments firm or particulars information, etc. of shareholders periodically; and
 - (c) refusing funds to, or conduct inappropriate or unusual trading with, a party which has been found to be an antisocial force for any reason.
- ② Whether a financial instruments firm establishes a division to make the overall control over the responses in the event that an antisocial force makes unreasonable demanding (hereinafter referred to as "antisocial forces response division") and a unified control system is constructed to prevent suffering damages by antisocial forces and works.
- Whether a financial instruments firm constructs a unified control system with the following remarks.
- (a) Whether, in the event that an antisocial force made unreasonable demanding, a financial instruments firm implements the system to make a report to, or consult with, the antisocial forces response division concerning such information. Whether a financial instruments firm implements a system to ensure the safety of a person in charge who actually responds to an antisocial force at the antisocial forces response division and to help the division in charge.
 - (b) Whether a financial instruments firm implements the system to make unified control and accumulation of information of antisocial forces at an antisocial forces responses division and to use such information at the time of examining a trading partner or judging the particulars of shareholders of such financial instruments firm by means of constructing a data bases which aggregates such information.
 - (c) Whether a financial instruments firm implements the system to ensure the effectiveness of an effort to reject the relationship with antisocial forces such as preparing response manual or continuous training at the antisocial forces responses division and constructing close coordination system with an external specialized organization such as the police, the Violence Banning Campaign Promotion Center, lawyers, etc. at ordinary time. Whether, particularly, a financial instruments firm builds up the communication with the police at ordinary time and implements the system to inform the police immediately when probability of danger of threat or violence is high and emergency is required by constructing organizational communication system and cooperation at the time of the occurrence of problems.
- ③ Whether, when an antisocial force made unreasonable demanding, the management team such as directors involves in it and make responses as an organization without leaving the matter only to a person in charge or a division in charge. Whether the financial instruments firm responds at such time with the following remarks.
- (a) making a report of information that an antisocial force made unreasonable demanding to the management team such as directors, etc. through the antisocial forces response division and making responses by appropriate instruction or involvement of the management team;
 - (b) consulting with external specialized organizations such as the police, the Violence Banning Campaign Promotion Center, lawyers, etc. positively and making responses based on unreasonable demanding responses methods, etc. provided by the Violence Banning Campaign Promotion Center, etc.; when the probability of thereat or violence is high and emergency is required, informing the police immediately; and
 - (c) taking all civil legal counter measures and making unfaltering responses without hesitating to make the case subject to criminal investigation by, for example, filing damage report positively.
- ④ Whether, when an antisocial force makes an unreasonable demanding for the reason of scandals in the course of business or scandals of an employee, a division in charge of scandals investigates the fact with the request by the antisocial forces response division.
- (3) Supervisory method and response
- With respect to the issues of the system to cut off the relationship of a financial instruments firm with antisocial forces found through the result of inspection, daily supervisory operations, the authority shall recognize voluntary improvement of business management of the financial instruments firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. If the internal control system is extremely weak and, for example, appropriate response to dissolve the relationship is not made despite that the financial instruments firm recognizes providing funds to an antisocial force or inappropriate trading

relationship with an antisocial force, and a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses of rigid disposition under Article 52.1 of the F.I. Act.

III-2-12 Disclosure, etc. of Corporate Social Responsibility (CSR)

(1) Significance

- ① CSR is generally understood as economic, environmental and social responsibility recognized in the relationship between a corporation and various stakeholders and an effort based on such responsibility, and is thought that enhancing the sustainability of a corporation through such effort is significant.
- ② With respect to CSR of financial instruments firms, each financial instruments firm as a private corporation essentially makes an effort and disclosure based on the business management judgment in accordance with self-responsibility principles, and the valuation thereof is left to various stakeholders including users under the market discipline.
- ③ However, timely and appropriate disclosure of CSR in a simple manner is thought to make accessing to useful information easier in order to judge the sustainability of a financial instruments firm and financial products and services provided by the financial instruments firm when a user selects a financial instruments firm. In such terms, clarification of focus points and showing the minimum framework in the disclosure of CSR by a financial instruments firm encourages the useful and appropriate disclosure for users.

(2) Main focus points

Whether, with respect to CSR of a financial instruments firm, appropriate disclosure is made to enable various stakeholders including users to value appropriately and contribute to the improvement of the convenience of users of a financial instruments firm with the following points.

① Fitness of purpose

Whether CSR reports cover areas of economy, environment and society comprehensively, and fit to the purpose of responding accurately to the needs of various stakeholders including users such as comprehensive description and reflecting social circumstances. Whether the disclosure is made timely and effectively.

② Reliability

Whether CSR reports are prepared through transparent process and the data or information is accurate, neutral and verifiable, and therefore CSR reports are reliable and acceptable for many stakeholders.

③ Simplicity

Whether CSR reports are as simple as possible and can be understood by various stakeholders including users. Whether the contents of CSR reports are consistent and the comparability with the past report of such financial instruments firm is taken into consideration.

(3) Supervisory method and response

Efforts to emphasize on CSR by a financial instruments firm and its disclosure shall be made voluntarily based on business management judgment in accordance with the self-responsible principles of a financial instruments firm, and the authority does not take supervisory measures even if a financial instruments firm fails to make a report based on the above focus points.

If a financial instruments firm makes inaccurate and inappropriate disclosure which may give false impression to users however, the authority shall verify the appropriateness of business.

III-3 Procedures (common part)

III-3-1 Registration

(1) Seal on application for registration

The case where the seal may be replaced with signature as stated in the remarks on entries shall apply to the case of the representative who has no custom to use a seal.

- (2) Trade name
The authority shall confirm that the trade name stated on the application does not violate Article 25.2 of the Supplementary Provisions of the Law to Amend Part of Securities and Exchange Law (hereinafter referred to as "Amend Law").
Further, the authority shall ensure that the name of a securities company, financial futures firm, investment trust management firm, investment advisory firm, etc. which existed in the past is not used if it is possible, except for the case where a firm which has business continuity because of business assignment, etc. uses the name.
- (3) Business office or other type of office
Business offices or other types of offices required to be stated in an application for registration mean a certain facilities or equipments operated in order to carry out the whole or part of financial instruments business, and exclude representative offices, liaison offices or other facilities for the use other than financial instruments business.
With respect to unattended business offices or other types of offices, the number of such offices located in the jurisdictional area of each local finance bureau and the name, etc. of the business office or other type of office which makes the overall control of such unattended offices shall be stated.
It shall be noted that the requirement for posting of a sign under Article 36-2.1 of the F.I. Act shall be applicable to unattended business offices or other types of offices, too.
- (4) Attachments to application for registration
- ① An abridged copy of the resident's card shall contain the followings:
 - (a) the address;
 - (b) the name;
 - (c) the date of birth.
 - ② A copy of the foreign resident's registration card or foreign resident's registered certificate submitted by a foreigner who resides in Japan and a copy of resident's card in the home country submitted by a foreigner who does not reside in Japan or a written statement equivalent thereto (in the case where it is written in a foreign language, together with Japanese translation) shall be regarded as "a written statement equivalent thereto" as provided in Articles 9 (2) (b) and 9 (3) (b) and Article 38 (1) of the F.I. Business Ordinance.
- (5) Remarks for the period until registration
- ① The authority shall call for attention an applicant for registration not to involve in business activities until the applicant is registered in the financial instruments firm, etc. registry book.
 - ② In the case where the applicant for registration is engaged in other business related to the laws or regulations under the jurisdiction of the Financial Services Agency and such other business is subject to an administrative disposition, the authority shall confirm the details of such disposition and confirm, when needed, the state of improvement measures through hearings, etc.
If such administrative disposition is related to a compliance system, III-2-1 shall be noted.
- (6) Handling of registration number
- ① Registration numbers shall be serial numbers for each director-general of a local finance bureau (*provided*, that 4, 9, 13, 42, 83, 103 and 893 shall not be used) and the registration number to be stated in the financial instruments firm registry book shall be:
Director-General of ○○ Finance Bureau (Financial Instruments) ○○
 - ② When registration loses its effect, the registration number shall be left as the missing number and such number shall not be used.
 - ③ the registration number shall be controlled by the financial instruments firm registration number book made on Form III-2.
- (7) Notice to applicant for registration
Upon the registration on the financial instruments firm registry book, the authority shall furnish the applicant for registration with the notice of registration made on Form III-3.
- (8) Refusal of registration
- ① In the case of the refusal of registration, the authority shall furnish the applicant for registration with the registration refusal notice made on Form III-4 stating the reasons for such refusal and the applicant's right to appeal to the Commissioner of the Financial Services Agency for the examination and file a petition with the government for revocation.
 - ② The authority shall show, in the registration refusal notice, an item applicable to the reason for the refusal under Article 29-4.1 of the F.I. Act or false statements on important matters or omission of important facts in the application for registration and attachments concretely and clearly.

- (9) Financial instruments firm registry book
- ① A copy of Page 2 to Page 12 of the application for registration shall be used for the preparation of the financial instruments firm registry book.
 - ② When a notification of a change in the matters stated in the application for registration has been filed, the relevant page in the application for registration attached to the notification shall be replaced with the page related to the change in the financial instruments firm registry book.
A notification of change in the amount of capital as a result of the exercise of the share warrants of a financial instruments firm which issues share certificates or corporate debt security with share warrants shall be filed for the amount of capital as of the end of each month no later than 15th day of the following month, and the relevant page of the financial instruments firm registry book shall be replaced each month.
 - ③ When a notification of change in any of the matters stated in the application for registration has been filed from a financial instruments firm under the direct jurisdiction of the Agency, the Agency shall send the pages of the application for registration subject to such change to the local finance bureau which has registered the financial instruments firm in a lot each month no later than 20th of the following month;
 - ④ A financial instruments firm registry book shall be accessible for the public inspection on days other than holidays of administrative agencies as defined in Article 1 of the Law on Holidays of Administrative Agencies for hours specified by the director-general of a local finance bureau; *provided*, that such days and hours may be changed when needed for fixing up of the financial instruments firm registry book or for other reasons;
 - ⑤ Persons who inspect a financial instruments firm registry book shall state stipulated matters on the financial instruments firm registry book inspection list made on Form III-5;
 - ⑥ A financial instruments firm registry book shall not be taken out of the inspection place designated by the director-general of a local finance bureau;
 - ⑦ The authority may suspend or refuse the public inspection if the inspecting person falls under any of the followings:
 - (a) ④ or ⑥ above or a person who does not follow the instruction of the authority;
 - (b) a person who has defaced or damaged, or will likely deface or damage, the financial instruments firm registry book; or
 - (c) a person who has inconvenienced, or will likely inconvenience, other inspecting persons.
 - ⑧ When there has been an application for public inspection of a financial instruments firm registered by the director-general of an other local finance bureau, the authority shall advise such applicant that such public inspection is served at such local finance bureau which has registered such financial instruments firm and documents for explanation are kept at all business offices and other types of offices of a financial instruments firm and accessible for the public inspection: *Provided*, That the authority shall refer the registered matters to the director-general of the other local finance bureau and respond to such application for public inspection if there is unavoidable reasons such as the reason that the business office of the financial instruments firm is located at a distant place.

III-3-2 Notification

Remarks shall be made on the followings for accepting and processing notifications provided by the F.I. Act.

- (1) Change of the location of the principal business office to the area covered by other local finance bureau
 - ① The director-general of a local finance bureau who accepted a notification of a change of the location of the principal business office to the area covered by an other local finance bureau shall send the notification of change provided in Article 20.2 of the F.I. Business Ordinance and a copy of the application for registration and its attachments and the report of inspection conducted immediately before the filing of the notification as other documents together with the part related to the financial instruments firm in the financial instruments firm registry book to the director-general of such other local finance bureau who will handle the registration.
 - ② When the director-general of the local finance bureau who has received the above documents has registered such financial instruments firm, the director-general of the local finance bureau shall send a copy of the notice of registration to the director-general of the local finance bureau who has made the previous registration.
 - ③ The director-general of the local finance bureau who has made the previous registration and

received the copy of the notice of registration shall erase the registration of such financial instruments firm.

- (2) Remarks on notification of cessation of business, etc.
 - ① When the authority has accepted a notification from a financial instruments firm under Article 50.1 (7) or Article 50-2.7 of the F.I. Act and Article 199 (5) of the F.I. Business Ordinance, the authority shall confirm the followings through inspection, etc.:
 - (a) the financial instruments firm which has filed the notification does not have causes for revocation of registration under Article 52.1 of the F.I. Act;
 - (b) the complete repayment of debt to customers is expected with certainty; and
 - (c) whether the authority has confirmed that there is no contingency liabilities by means such as checking the balance of debts and credits in respect of customers.
 - ② If a financial instruments firm has filed a notification under Article 119 (11) (g) of the F.I. Business Ordinance and the reason to cease commissioning to a financial instruments intermediary firm is that the financial instruments intermediary firm abolishes the financial instruments intermediary business, the authority shall confirm at the time of filing of the notification that the financial instruments firm has confirmed the non-existence of the causes for revocation of registration under Article 66-20.1 of the F.I. Act in respect of such financial instruments intermediary firm.

III-3-3 Matters related to books and records of business operations

Books and records of business operations (hereinafter referred to as "books and records" (excluding VI-3-2-4, VI-3-3-4, VIII-2-3 and XI-2-3)) shall reflect the business and financial conditions of a financial instruments firm accurately and the laws and regulations provide for the requirement for preparation and retention of such books and records to contribute to the protection of investors by means such as verifying the appropriateness of business and soundness of financial resources. The authority shall verify books and records based on these purposes and with the following remarks.

- (1) Basic remarks
 - ① With respect to books and records, one set of books and records can be used for other books and records to the reasonable extent; a part of the books and records can be filed as separate book; the names provided in Articles 157 and 181 of the F.I. Business Ordinance can be replaced with other names. *Provided*, That this shall apply only if all matters required to be stated in the books and records according to the types are stated.
 - ② For the purpose of III-3-3, the principal business office shall be read as the principal business office or other type of office in Japan, and a branch office shall be read as other business office or other type of office in Japan in the case of a foreign juridical person.
 - ③ "Order acceptance" in Article 158 of the F.I. Business Ordinance shall be read as "order placement" in the case of preparing an order ticket for an order placement of transactions for house account.
 - ④ With respect to matters required to be stated in books and records which do not match directly with the relevant matters, equivalent matters shall be stated, and with respect to matters which do not match, statement of such matters may be omitted.
 - ⑤ A copy of a written statement provided in Article 157.1 (1) (a) (iv) of the F.I. Business Ordinance (written statement furnished prior to transactions as provided in Article 37-4.1 of the F.I. Act) shall be prepared by mechanical process at the same time as such written statement and can be replaced with other books and records stating all matters required to be stated in such written statement.
 - ⑥ In the case of preparing an order ticket, a trading record for intermediary or agent, a trading record for public offer, public sale or private placement, a trading record for handling of public offer or public sale or handling of private placement and a trading record for intermediary or agent for entering into investment advisory contract or discretionary investment contract where a contract of transactions are entered into at the time of transaction, a contract of transaction stating all matters required to be stated in each of books and records can be used as relevant books and records. Such contract of transactions shall be filed separately.
 - ⑦ With respect to matters required to be stated in books and records, a code including brevity code can be used if the financial instruments firm uses such code in a uniform manner.
 - ⑧ If a part of matters required to be stated in books and records is linked to a contract of transactions containing the same matters by means such as contract number and kept together,

- such matters can be treated as such books and records as a unit.
- (2) Preparation and retention of books and records by microfilm
 - ① If three years have passed after the preparation of books and records and the inspection division has inspected during such period, such books and records may be kept in the form of microfilm prepared in accordance with the preparation standards which are deemed generally reasonable.
 - ② Books and records may be prepared and kept in the form of microfilm from the beginning in the following cases:
 - (a) the case where such books and records are those referred to in (1) (a) (iv), (9), (11), (16) (limited to (b) and (c)) and (17) (excluding (a)) of Article 157.1 of the F.I. Business Ordinance;
 - (b) the case where written books and records can be prepared at each business office within a reasonable period in the inspection, etc. conducted by the inspection division; and
 - (c) the case where a person responsible for preparation and retention of the microfilm is appointed and procedures for controlling are implemented.
 - (3) Centralized retention of books and records at the principal business office
 - ① With respect to the place of retention of books and records, if three years have passed after the preparation and the inspection division has inspected during such period, the principal business office (including an operational center, etc. in ②, the same) can be the central place to keep such books and records.
 - ② A financial instruments firm may centralize the retention of books and records at the principal business office or at a company to which the financial instruments firm has commissioned the preparation of books and records as from the time of preparation on the conditions that the following requirements are met.
 - (a) the financial instruments firm implements a system to make a quick reply to an enquiry by customers;
 - (b) the financial instruments firm implements a system to make the public inspection of books and records available at the principal business office or branches within a reasonable period; and
 - (c) there is no interference to internal audit.
 - (4) Preparation by inputting order tickets directly to computers

Remarks shall be made on the followings if a financial instruments firm prepares order tickets by inputting directly to computers:

 - ① inputting the details of an order to a computer simultaneously with the acceptance of an order (or placement of an order, in the case of order placement for house account);
 - ② making it possible to make a quick reply to a customer's enquiry;
 - ③ preparation and retention of the back-up of input data;
 - ④ arranging a system to record the time of input automatically;
 - ⑤ arranging a system, in the case of cancellation or modification of the input made in the past, to carry over records of such cancellation and modification of input;
 - ⑥ in the cases where it is impossible to prepare the books and records by inputting directly to a computer simultaneously with the receipt of an order such as the case where the details of an order are transmitted to the executing office by telephone, the case of accepting orders for the next day after the termination of operation of a computer and the case where a computer cannot be used because of natural disaster, etc., preparing order tickets by hand writing at the time of the receipt of order as before; *provided*, that additional notes to a hand written order ticket may be avoided in the case of retaining the written order ticket prepared at the time of order acceptance together with the order ticket prepared by a computer containing trade results, etc. prepared by inputting the details of the order later; and
 - ⑦ arranging a system to respond to internal audit.
 - (5) Preparation by inputting order placement ticket directly to computers

Remarks shall be made on the followings for preparing order placement tickets by inputting directly to computers:

 - ① inputting the details of an order to a computer simultaneously with order placement;
 - ② if it is impossible to prepare an order placement ticket by inputting directly to a computer simultaneously with order placement such as the case where the computer is unusable because of natural disaster, etc., such order placement ticket shall be prepared in writing at the time of order placement; *provided*, that additional notes to a hand written order placement ticket may be avoided in the case of retaining the written order placement ticket prepared at the time of order placement together with the order placement ticket prepared by a computer containing the

- details of the order placement prepared by inputting the details of the order placement later;
- ③ in addition to ① and ② above, ③ to ⑤ and ⑦ of (4) shall apply.
- (6) Retention of books and records by electronic media
- In keeping books and records by electronic media, the financial instruments firm shall:
- ① keep books and records prepared by hand writing as image data;
 - ② use electronic media for retention with durability of the period provided in Articles 157.2 and 181.3 of the F.I. Business Ordinance;
 - ③ keep one of electronic media used for data retention as "original" and clarify it (the state of retention of books and records is judged by this "original");
 - ④ prepare the back up of the "original" under (3) and keep such back up as "duplicate";
 - ⑤ implement a system to make a quick response to enquiries by customers;
 - ⑥ implement a system to prepare books and records by hard copy for the retained data during a reasonable period;
 - ⑦ implement a system, in the case of cancellation or modification of the data input in the past, to carry over records of such cancellation and modification;
 - ⑧ implement a system to respond to internal audit;
 - ⑨ appoint a person responsible for preparation and retention and implement internal rules for such preparation and retention; and
 - ⑩ if addition or supplement, etc. has been made by hand writing to the hard copy of books and records prepared by a computer system, retain such hard copy as image data, and if such hard copy is not retained as image data, keep such hard copy as original.

III-3-4 Matters related to the Law on Special Measures concerning Revitalization and Innovation of Industrial Activities

Remarks shall be made on the followings, in accordance with the entry methods of accounting documents, etc. of a financial instruments firm, for entries regarding a plan of reconstruction of business, a plan of restructuring, a plan of reuse of business resources and a plan of introduction of facilities of business innovation as provided by the Law on Special Measures concerning Revitalization and Innovation of Industrial Activities (hereinafter referred to as "Industry Vitalization Law").

- (1) Definition of business innovation under Article 2.2 (2) of the Industry Vitalization Law and Articles 6, 8 and 9 of the Guidelines for Enforcement of the Law on Special Measures concerning Revitalization and Innovation of Industrial Activities (hereinafter referred to as "Guidelines for Industry Vitalization Law")
 - ① "The total amount of sales from such new services becomes at least 1% of sales of all businesses" under Article 6 of the Guidelines for the Industry Vitalization Law means, for example, the total amount of operating profits from such new services becomes at least 1% of operating revenue from all businesses.
 - ② "Reduction of selling expenses per such service by at least 5%" under Article 8 of Guidelines for the Industry Vitalization Law means, for example, reduction of selling and general administrative expenses per operating profit or operating revenue by at least 5%.
 - ③ "The value as expressed in percentage of growth rate of sales of such services during the business reconstruction period exceeds the value as expressed in percentage of the actual growth rate of sales from the business type related to such services during the past three business years by at least 5" under Article 9 of the Guidelines for Industry Vitalization Law means, for example, that the value as expressed in percentage of growth rate of operating profit from such services during the business reconstruction period exceeds the value as expressed in percentage of the actual growth rate of operating profit from the business type related to such services during the past three business years by at least 5.
- (2) Criteria for recognition of business reconstruction under Article 3.6 (1) of the Industry Vitalization Law and (2) (b) of the Basic Guidelines for Revitalization of Industrial Activities in Japan (hereinafter referred to as "Basic Guidelines")
 - ① "return on equity after completion of business reconstruction — return on equity before business reconstruction ≥ 2 " under Article (2) (b) 1 ① of the Basic Guidelines means, for example, the increase of return on equity by at least 2.
 - ② "(Turnover ratio of tangible fixed assets after completion of business reconstruction / turnover ratio of tangible fixed assets before business reconstruction) $\times 100 \geq 105$ " under (2) (b) 1 ② of the Basic Guidelines means, for example, increase of the value of operating profit divided by the book value of tangible fixed assets by at least 5%.

- ③ "(Added value per employee after completion of business reconstruction / added value per employee before business reconstruction) × 100 ≥ 106" under (2) (b) 1 ③ of the Basic Guidelines means, for example, that increase of added value (total amount of operating profit, employment cost and depreciation) per employee by at least 6%.
- (3) Definition of the goal regarding improvement of financial soundness under Article 3-2.2 (2) of the Industrial Vitalization Law and (1) (c) 2 ③ of the Basic Guidelines
- ① "Total amount of interest-bearing debts" under (1) (c) 2 ③ (a) of the Basic Guidelines means, for example, all debt financing.
- ② "Recurring revenue" under (1) (c) 2 ③ (b) of the Basic Guidelines means, for example, the total amount of operating revenue and non-operating revenue, and "recurring expenses" means, for example, the total amount of operating cost and non-operating cost.
- (4) Definition of matters regarding criteria for types, etc. which are subject to excess supply structure under Article 2-2.2 (3) of the Industrial Vitalization Law and (3) (b) of the Basic Guidelines
- "Sales" under 2-2.2 (3) of the Basic Guidelines means, for example, operating revenue.
- (5) Criteria for recognition of joint business restructuring under Article 2-2.2 (3) of the Industrial Vitalization Law and (3) (c) of the Basic Guidelines
- III-3-4 (2) ② apply *mutatis mutandis* to 2 and (3) (c) 2 ① of the Basic Guidelines respectively.
- (6) Criteria for recognition of business resources reuse under Article 2-2.2 (4) of the Industrial Vitalization Law and (4) (b) of the Basic Guidelines
- ② and ③ of III-3-4 (2) apply *mutatis mutandis* to 2 and 3 of (4) (b) of the Basic Guidelines respectively.

IV. Supervisory Valuation Items and Procedures (First-Type Financial Instruments Business)

IV-1 Business management (first-type financial instruments business)

The authority shall verify the business management of a financial instruments firm (limited to a person who carries out the first-type financial instruments business; in IV, the same) with the following remarks

For the purpose of applying "III-1 Business management (common part)" to a foreign juridical person who carries out the first-type financial instruments business, the representative director and the board of directors, etc. shall be read as the representative in Japan and the supreme decision making body at a business office or other type of office in Japan, respectively.

IV-1-1 Officers of financial instruments firms

(1) Main focus points

Whether the followings are considered appropriately in the process of the determination of the agenda for the selection of a director, executive officer or auditor of a financial instruments firm (in the case of a foreign juridical person, including the representative in Japan; hereinafter referred to as "officer").

- ① the candidate is not, or was not at the time of registration, subject to causes for disqualification (as provided in (a) to (g) of Article 29-4.1 (2) of the F.I Act).
- ② the candidate does not violate the laws or regulations (excluding Article 46-6.2 of the F.I. Act) for financial instruments business or business incidental thereto or administrative disposition taken under the laws or regulations.
- ③ the candidate is not subject to the fact to harm the interests of investors in the operation of investment advisory and agent business or investment management business.
- ④ the candidate is not subject to commitment of an unlawful or grossly improper act of a particularly grave nature regarding the financial instruments business.
- ⑤ the candidate does not violate the conditions attached to an approval under Article 30.1 of the F.I. Act.

(3) Supervisory method and response

If an officer of a financial instruments firm has fallen under any of (a) to (g) of Article 29-4.1 (2) of the F.I. Act, has been found to have fallen under any of (a) to (g) of Article 29-4.1 (2) of the F.I. Act already at the time of registration under Article 29 of the F.I. Act or has fallen under

(6) or (8) to (10) of Article 52.1 of the F.I. Act, the authority shall consider the disposition of the issuance of an order to remove the officer under Article 52.2 of the F.I. Act.

The authority shall hold a hearing in depth on the determination process, etc. for the selection agenda of an officer of such financial instruments firm, require to make a report under Article 56-2.1 of the F.I. Act when needed, and further if a gross problem is found for the business management system of such firm and it is necessary and appropriate in the public interest or to protect investors, the authority shall consider dispositions such as the issuance of an order to improve business.

IV-1-2 Personnel structure sufficient to carry out financial instruments business accurately

(1) Main focus points

Whether a financial instruments firm ensures personnel structure sufficient to carry out financial instruments business (limited to the first-type financial instruments business; in IV, the same) accurately, considering the following criteria for an officer or employee of the financial instruments firm.

- ① ensuring the employment of a person who has knowledge and experience sufficient to understand and perform focus points of business management provided in regulations related to the F.I. Act or the Supervisory Guidelines and knowledge and experience regarding compliance and risk control necessary for fair and accurate carrying out of financial instruments business;
 - ② being not a member (including a person who was a member of a crime group in the past) of a crime group (which means a member of a crime group as defined in Article 2 (6) of the Law on Prevention of Improper Act by Member of Crime Group; hereinafter the same);
 - ③ having no close relationship with a crime group (which means a crime group as defined in Article 2 (2) of the Law on Prevention of Improper Act by Member of Crime Group; hereinafter the same);
 - ④ having no experience of the violation of the regulations for finance in Japan such as the F.I. Act or the laws or regulations in a foreign jurisdiction analogous thereto and being fined (including a criminal penalty under the laws or regulations analogous thereto in a foreign jurisdiction);
 - ⑤ having no experience of the violation of the provisions of the Law on Prevention of Improper Act by Member of Crime Group (excluding the provisions of Article 32-2.7 of said Law) or the provisions under the laws or regulations analogous thereto in a foreign jurisdiction, or commitment of crimes under the Criminal Code or the Law on Violence, etc. Punishment and being fined (including a criminal penalty under the laws or regulations analogous thereto in a foreign jurisdiction);
 - ⑥ having no experience of being punished by a criminal penalty of imprisonment or severer (including criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto) (particularly, the case of crimes under Articles 246 to 250 of the Criminal Code (fraudulence, fraudulence using a computer, breach of trust, quasi-fraudulence, threat, attempted crime) shall be noted).
- (2) Supervisory method and response

The criteria listed in ① to ⑤ above are part of criteria for comprehensive consideration to examine whether a financial instruments firm is determined to be a person who lacks personnel structure sufficient to carry out financial instruments business accurately and a person is not determined to be unsuitable for the reason that the specific criterion applies to the person. A financial instruments firm should, first of all, make an effort to ensure the appropriate personnel structure considering such criteria at the firm's responsibility.

Provided, That, if it is determined that such criteria is not considered fully in the selection process, etc. of an officer or employee of a financial instruments firm and it is determined to be necessary and appropriate in the public interest and to protect investors regarding the business management of a financial instruments firm, the authority shall hold a hearing in depth on the recognition by the financial instruments firm regarding such personnel structure and the selection process, etc. of an officer or employee, and collect reports under Article 56-2.1 of the F.I. Act when needed.

If, as a result of collection of reports, a gross problem is found for the business management system of such financial instruments firm and it is necessary and appropriate in the public interest or to protect investors, the authority shall consider to take dispositions such as the issuance of an order to improve business management under Article 51 of the F.I. Act.

If, as a result of collection of reports, it is determined to lack personnel resources sufficient

to carry out financial instruments business accurately, the authority shall consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-1-3 Implementation of system to control conflicts of interest

(1) Basic concept of implementation of system to control conflicts of interest

Diversification of services provided by financial institutions and global financial conglomeratization results in the existence of multiple interests which compete and conflict each other within a financial institution or financial group and likely causes conflicts of interest. Under such circumstances, a securities firm, etc. (which means a person who carries out the first-type financial instruments business (limited to securities related business); hereinafter the same) is required to control transactions which will likely cause conflicts of interest according to the types, characters and scale of business of each securities firm, etc. and group firms not to harm the interests of customers improperly.

Therefore, it is important for a securities firm, etc. to implement an appropriate system to control conflicts of interest at the firm itself and its subsidiary financial institutions, etc. under Article 36.2 of the F.I. Act.

A securities firm, etc. is allowed to exchange undisclosed information with its parent juridical person, etc. or subsidiary juridical person, etc. (hereinafter referred to as "parent and subsidiary juridical person, etc.") under certain conditions. Based on this, it is desirable to make business management with remarks on conflicts of interest which could occur for all businesses (including business other than financial instruments business) carried out within such securities firm, etc. and its financial group. It is desirable also to make business management with remarks on not only likeness to harm interests of customers directly but also the likeliness to suffer reputation risk (which means risks to damage social reputation or credit in financial markets; hereinafter the same) as a securities firm, etc. or financial group.

On the other hand, the level and depth to control conflicts of interest by a securities firm, etc. is not necessarily uniform, considering that there may be a group firm of a securities firm, etc. which carries out business unrelated to customers of such securities firm, etc. If a securities firm, etc. takes measures not to share undisclosed information with group firms, the securities firm, etc. could be considered to have taken necessary and sufficient measures for controlling conflicts of interest with such group firms. If a securities firm, etc. differentiates the level and depth of controlling conflicts of interest within the group, it is necessary to note that the securities firm, etc. is required to make full explanation externally.

If a parent firm, etc. of a securities firm, etc. controls conflicts of interest which the securities firm, etc. is required to perform and the securities firm, etc. recognizes the controlling methods and the state of performance accurately and involves therein appropriately when needed, such securities firm, etc. could be considered to have taken necessary and sufficient measures.

Based on the above, the authority shall supervise with the following remarks.

(2) Implementation of system to identify transactions which likely causes conflicts of interest

- ① Whether a securities firm, etc. in advance identifies transactions which will likely cause conflicts of interest and groups them.
- ② Whether a securities firm, etc. implements the system to identify the transactions which will likely cause conflicts of interest reflecting the types, characters and scale, etc. of businesses carried out by the securities firm, etc. and its parent financial institution, etc. or subsidiary financial institution, etc. appropriately.
- ③ Whether a securities firm, etc. implements the system to verify the appropriateness of new business periodically, for example, in commencing such business in respect of transactions identified as transactions which will likely cause conflicts of interest.

(3) Methods to control conflicts of interest

- ① Whether a securities firm, etc. implements the system which enables to choose or combine appropriate methods to control conflicts of interest according to the characters of transactions identified as transactions which will likely cause conflicts of interest, for example, with the following remarks.
 - (a) Whether, if a securities firm, etc. controls by means of separation of divisions, the securities firm, etc. takes measures for rigid blocking of information between such divisions (access restriction or measures to block physically).
 - (b) Whether, if a securities firm, etc. controls by means of change in conditions or methods of transactions or suspension of transactions of one party, the securities firm, etc. clarifies the authorities or responsibility including the case where an officer, etc. of a parent financial

- institution, etc. or subsidiary financial institution, etc. involves in the judgment of such change or suspension.
- (c) Whether, if a securities firm, etc. controls by means of disclosing the likeliness of conflicts of interest to a customer, the securities firm, etc. explains to such customer the details of possible conflicts of interest and reason for choosing such method (including the reason for not choosing other methods) no later than entering into the contract for such transaction in a manner that such customer can understand fully according to the particulars of the customer.
 - (d) Whether, if a securities firm, etc. controls by means of monitoring a person sharing information, the independent division, etc. of the securities firm, etc. monitors transactions conducted by such person appropriately.
- ② Whether, when a securities firm, etc. and its subsidiary financial institution, etc. conduct new transactions, the securities firm, etc. implements the system to make necessary confirmation whether there are transactions which will cause conflicts of interest with such new transactions.
 - ③ Whether a securities firm, etc. implements the system to verify the method to control conflicts of interest periodically in light of ensuring the effectiveness.
- (4) Implementation, and publication of the summary, of the conflicts of interest control policies
- ① Whether the conflicts of interest control policies (which mean policies as defined in Article 70-3.1 (3) of the F.I. Business Ordinance; hereinafter the same) state, after considering the types, characters, scale, etc. of business of a securities firm, etc., its parent financial institution, etc. and its subsidiary financial institution, etc., the types of transactions which will likely cause conflicts of interest, main examples of transactions, process to identify such transactions, methods to control conflicts of interest (if the level and depth to control conflicts of interest are differentiated, including the details and reasons), the system to control conflicts of interest (the duties of a person who supervises the overall control system to identify transactions which will likely cause conflicts of interest and control of conflicts of interest in the firm (hereinafter referred to as "conflicts of interest controller") and the independency and the system to verify the methods to identify transactions which will likely cause conflicts of interest and to control conflicts of interest) and the scope of the corporations subject to the control of conflicts of interest. Whether, in this case, the types of transactions which will likely cause conflicts of interest, examples of transactions and methods to control conflicts of interest are stated in a correspondence manner.
 - ② Whether the summary of the conflicts of interest control policies to be published state, after considering the types, characters, scale, etc. of business of a securities firm, etc., its parent financial institution, etc. and its subsidiary financial institution, etc., the types of transactions which will likely cause conflicts of interest, methods to control conflicts of interest, the system to control conflicts of interest, and the scope of the corporations subject to the control of conflicts of interest in an easy-to-understand manner.
 - ③ Whether the summary of the conflicts of interest control policies is published appropriately by means of posting, making available for public inspection, at a business office or putting on the website.
- (5) Personnel structure and business management system
- ① Whether an officer of a securities firm, etc. and its subsidiary financial institution, etc. makes an effort to recognize the importance of the control of conflicts of interest and perform faithfully and with initiative.
 - ② Whether the procedures for business management based on the conflicts of interest control policies are clarified in writing, etc. Whether a securities firm, etc. ensures to inform all of the officers and employees of the securities firm, etc., and its subsidiary financial institution, etc. concerning conflicts of interest control by means of training, etc. concerning the conflicts of interest control policies and such procedures, etc.
 - ③ Whether a securities firm, etc. implements the unified system to identify transactions which will likely cause conflicts of interest and to control conflicts of interest by means such as appointing a conflicts of interest controller, etc.
 - ④ Whether a conflicts of interest controller, etc. performs the identification of transactions which will likely cause conflicts of interest and controls conflicts of interest accurately in accordance with the conflicts of interest control policies, and verifies the effectiveness.
 - ⑤ Whether a conflicts of interest controller, etc. ensures its independency from sales divisions and checks sales divisions fully.
 - ⑥ Whether a conflicts of interest controller, etc. aggregates information necessary for the conflicts of interest control including transactions of its parent financial institution, etc. or

subsidiary financial institution, etc. and implements the system to control conflicts of interest appropriately.

⑦ Whether a system to verify periodically the personnel structure and business management system for the conflicts of interest control is implemented.

(6) Supervisory method and response

The conflicts of interest control system should be, first of all, implemented by each securities firm, etc. according to the types, characters, scale, etc. of business of the securities firm, etc., and matters listed in (1) to (5) above show the basic framework.

Each securities firm, etc. is required to implement appropriate conflicts of interest control system according to the types, characters, scale, etc. of business of the securities firm, etc., its parent financial institution, etc. and its subsidiary financial institution, etc. respectively

Provided, That, if it is determined that customers' interests are harmed improperly and it is necessary and appropriate in the public interests and to protect investors regardless of the implementation of the conflicts of interest control system by a securities firm, etc., the authority shall hold a hearing in depth and collect reports under Article 56-2.1 or 56-2.3 of the F.I. Act when needed, and if, as a result of collection of reports, a gross problem is found for conflicts of interest control system of a securities firm, etc. and it is necessary and appropriate in the public interest or to protect investors, the authority shall consider necessary responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act and an order to suspend business under Article 52.1 of the F.I. Act.

IV-2 Financial soundness, etc. (first-type financial instruments business)

The purpose of capital requirement for financial instruments firms, etc. is to, based on the fact that financial instruments firms engage in business which is easily affected by changes in market environment, stabilize the financial soundness of financial instruments firms, even if a financial instruments firm faces the decrease of the revenue associated with drastic changes in market prices or the decline of value of asset holdings and make assurance doubly sure on the protection of investors. Financial instruments firms shall recognize and control, as a whole, the risks involved in their business through maintaining appropriate capital requirement ratio, and maintain liquid assets (i.e., unlocked capital) sufficient to cope with losses in the event that various risks have emerged. The authority shall encourage voluntary efforts by financial instruments firms to maintain their financial soundness through off-site monitoring as the supplement to maintenance of appropriate capital requirement ratio under the principles of self-responsibility.

IV-2-1 Accuracy of capital requirement ratio

The authority shall verify the accuracy of the computation of the capital requirement ratio with due consideration of Article 46-6.1 of the F.I. Act and the provisions of the F.I. Business Ordinance with the following remarks.

(1) Eligibility of subordinated debt and corporate debt securities with special provisions of subordination

① Whether, if there has been a notification that a financial instruments firm has borrowed loans with special provisions of subordination or issued corporate debt securities with special provisions of subordination under Article 50.1 of the F.I. Act (Article 199 (12) of the F.I. Business Ordinance), such debt or corporate debt securities have contract terms to the effect that senior creditors take precedence effectively with the legally structured condition that, in the event that the state of subordination has occurred because of bankruptcy and company rehabilitation, the effectiveness of claims for payment held by subordinated creditors is suspended and the effectiveness of claims for payment held by subordinated creditors arises again on the conditions that senior creditors have received the full amount of payment.

② Whether such debt or corporate debt securities have all of the natures listed in the items of Article 176.2 or the items of 176.3 of the F.I Business Ordinance.

③ Whether such debt or corporate debt securities have contract terms which nullify any change against the benefit of senior creditors or payment in violation of the special provisions of subordination;

④ Whether, in the following cases, the finance is deemed to be provided on purpose to lenders of loans with special provisions of subordination or holders of corporate debt securities with special provisions of subordination as defined in Article 176.4 (3) of the F.I. Business

Ordinance and the amount of funds is deducted:

- (a) the case of borrowing loans with special provisions of subordination to such lenders or such holders or holding corporate debt securities with special provisions of subordination issued by such lenders or holders (excluding the case where a financial instruments firm engaging in securities business has acquired such corporate debt securities with special provisions of subordination as a result of underwriting activities and holds them for six months or shorter and the case of holding them temporarily for the purpose of market making);
 - (b) the case of making loans to such lender or such holder for the purpose of aiding management reconstruction, assistance or capital reinforcement; or
 - (c) the case of taking share certificates or other securities, etc. issued by such lenders or holders newly for the purpose of aiding business reconstruction, assistance or capital reinforcement (excluding the case, other than aiding business reconstruction, assistance or capital reinforcement where such share certificate or other securities, etc. have been bought from the secondary market, etc. and are held for the purpose of pure investment, etc., the case where a financial instruments firm has acquired such corporate debt securities with special provisions of subordination as a result of underwriting activities and holds them for six months or shorter and the case of holding them temporarily for the purpose of market making).
- (2) Collateral money, etc. to be deducted from deductible assets
- In the case of deducting current value, etc. of land and buildings under Articles 177.2 and 177.3 of the F.I. Business Ordinance or the case of deducting the current value of collateral money or other assets under Articles 177.5 of the F.I. Business Ordinance and Article 2.2 of the Capital Requirement Notification, the financial instruments firm shall confirm the appropriateness of the deducted amount with the following remarks.
- ① Whether the current value of land or buildings is properly computed in the case of deducting the current value, etc. of such land or buildings.
 - ② Whether collateral money or other assets are suitable for collateral and whether the current value and market risk equivalent amounts deductible from such current value are properly computed, in the case of deducting the current value of such collateral money or other assets.
- (3) Recognition of risk equivalent amounts
- The authority shall confirm whether a financial instruments firm recognizes market risk equivalent amounts and counterparty risk equivalent amounts each business day by reasonable methods appropriate for the type of business under Article 178.2 of the F.I. Business Ordinance with the following remarks.
- ① Whether a financial instruments firm recognizes market risk equivalent amounts properly based on the current value of all securities, etc. holdings (the current value shall be verified as of the month-end in an objective manner); *provided*, that approximation at the time other than month-end may be used for those which is not important such as constantly small amount of position relative to the amount of unlocked capital.
 - ② Whether a financial instruments firm recognizes counterparty risk equivalent amounts properly based on credit equivalent amounts of all transactions or assets, etc. which are subject to the computation; *provided*, that money receivable and uncollected revenue related to financial revenue and accounted on the trade date transitionally may be excluded at the time other than month-end (excluding those unpaid on the settlement date or delivery date).
 - ③ Whether a director responsible for the risk control knows market risk equivalent amounts and counterparty risk equivalent amounts each business day.
- Particularly whether a financial instruments firm conducting transactions of foreign exchange which can be settled in cash difference by accepting the deposit of a certain rate of margins (guarantee money) relative to the trade value from customers (hereinafter referred to as "so called foreign exchange margin transaction") implements a risk control and internal control system which enables the financial instruments firm to recognize the influence of drastic movement in foreign exchange markets on the financial soundness and capital accurately and properly.
- (4) Confirmation of securities lending
- Whether a financial instruments firm computes market risk equivalent amounts, in addition to counterparty risk equivalent amounts, for securities holdings which were lent.

IV-2-2 Supervisory response to case where capital requirement ratio of financial instruments firm has dropped below statutory level

"Early warning level" of the capital requirement ratio are prescribed under Article 46-6.1 of the F.I. Act as a method to ensure sound management of financial instruments firms and financial instruments firms shall make continuous effort to improve business management in order to maintain and improve further the soundness of management.

If the capital requirement ratio has dropped below the statutory level, the following measures are taken as supervisory purpose to encourage such financial instruments firm to make early improvement.

- (1) In the event that a notification has been filed under Article 179.3 of the F.I. Business Ordinance, the authority shall confirm the "plan for concrete measures to be taken by the financial instruments firm in order to maintain the state of the capital requirement ratio" attached to the notification and confirm the outlook of the capital requirement ratio in the foreseeable future through hearings, etc. and encourage voluntary improvement.

If the capital requirement ratio stays under 140% for long time or repeatedly drops under 140%, the authority shall make an effort to recognize the state of the capital requirement ratio of the financial instruments firm by means such as collecting reports under Article 56-2.1 of the F.I. Act.

The authority shall make an effort to recognize the state of the capital requirement ratio or the state of each risk of the financial instruments firm through confirming the notification regarding the capital requirement ratio filed each business day and hearing, etc. for the period until a notification is filed under Article 179.5 of F.I. Business Ordinance.

- (2) If the capital requirement ratio is below 120% in the above notification, the authority shall confirm the "plan for concrete measures to be taken by the financial instruments firm in order to recover the state of the capital requirement ratio" attached to the notification and recognize concrete measures and timing for the recovery of the capital requirement ratio, segregation of customer assets and cash position by measures such as collecting reports under Article 56-2.1 of the F.I. Act when needed, and encourage efforts to improve such state.
- (3) If (2) is applicable and the authority deems it necessary and appropriate in the public interest and to protect investors based on the conditions of the financial instruments firm found through the collection of reports and hearing, etc., the authority shall issue an order under Article 53.1 of the F.I. Act according to the necessity regarding:
 - ① planning and enforcement of measures for recovery and constant maintenance of the statutory level of the capital requirement ratio (including the concrete details and timing of enforcement);
 - ② preparation for unanticipated situation and formulation of full of measures for the protection of investors by means such as appropriate securing of securities, etc. and money and detailed cash management;
 - ③ keeping from performing improper acts which consume the company's properties; and
 - ④ preparation of the daily balance sheet, cash management and estimated capital requirement ratio reflecting concrete measures for the recovery of the capital requirement ratio.

IV-2-3 Market risk management system

Market risk means a risk combining the risk of loss arising from the fluctuation of prices of assets holdings (including positions related to off-balance transactions) as a result of a change in risk factors in various markets such as prices of securities, etc., interest rate and foreign exchange and the credit risk, etc. incidental thereto. It is important for financial instruments firms to manage the market risk properly.

- (1) Main focus points

Whether a financial instruments firm controls the market risk properly through the implementation of a comprehensive risk control system, appropriate risk recognition and valuation, appropriate setting and management of position limit, etc., construction of mutual checking system by dividing duties and clarifying of authorization.

- (2) Supervisory methods and response

The authority shall make an effort to recognize the conditions of the market risk and the risk control system through monthly off-site monitoring reports and hearing, etc. based thereon, and shall collect reports under Article 56-2.1 of the F.I. Act when needed and encourage improvement.

(3) Concrete handling

① Risk control of trading business for house account

A financial instruments firm, etc. shall, in addition to recognizing market risk equivalent amounts under Article 178.2 of the F.I. Business Ordinance each business day, recognize and control the market risk of trading of shares of stock for house account with the following remarks:

(a) Appropriate risk control of trading of shares of stock for house account

The financial instruments firm, etc. shall:

- a. set the maximum permissible amount of market risk or reasonable limits or risk amounts equivalent thereto which can be allocated to the trading of shares of stock for house account (hereinafter referred to as "permissible market risk amounts, etc.") after setting appropriate capital requirement ratio considering the firm's financial conditions, etc.;
- b. monitor whether daily trading of shares of stock for the house account is conducted within the permissible market risk amounts, etc. properly; and
- c. take necessary measures such as reviewing the permissible market risk amounts, etc. on a timely basis in light of maintaining set capital requirement ratio according to changes in the firm's financial conditions such as profit or loss from trading for house account,.

(b) Proper control of trading business for house account during the day time

- a. the financial instruments firm shall implement a system to control trading of shares of stock for the house account not to exceed the permissible market risk amounts, etc.;
- b. the control of trading of shares of stock for the house account not to exceed the permissible market risk amounts, etc. during daytime may be made by, in lieu of (a), approximation using, for example, the following position amounts after considering the current control method for trading business for the house account:
 - i) method to confirm on a timely basis that the amount computed by multiplying the total amount of position amounts as at each time during daytime by the loss-cut price range during daytime which was set internally in advance does not exceed the permissible market risk amounts, etc.;
 - ii) method to confirm on a timely basis that the amount computed by multiplying the accumulated amount of position amounts until each time during daytime by the loss-cut price range during daytime which was set internally in advance does not exceed the permissible market risk amounts, etc.; and
 - iii) method, after allocation of the position limits based on the permissible market risk amounts, etc. which was set in (a) to each trader or each unit, to confirm the compliance with such position limits on a timely basis.

(c) A financial instruments firm shall implement a system to take appropriate measures when the financial instruments firm has confirmed the state influencing seriously on the financial soundness.

② Confirming reasonable reason to choose market risk computation method

In the case where the standardized approach or the internal measurement approach is chosen for each risk category and for each type of business under Article 4.4 of Capital Requirement Notification for the computation of market risk equivalent amounts, the financial instruments firm shall confirm whether such choice is reasonable with the following remarks.

(a) The case of choosing the computation method of market risk equivalent amounts for each risk category

- a. Whether a financial instruments firm recognizes the market risk more properly by choosing different computation method for each risk category.
- b. Whether the division in charge of recognizing the overall market risk on an integrated basis is independent from other divisions.

(b) The case of choosing the computation method of market risk equivalent amounts for each type of business

- a. Whether a financial instruments firm recognizes the market risk more properly by choosing different computation method for each type of business.
- b. Whether a financial instruments firm implements a system that the division in charge of recognizing the overall market risk on an integrated basis recognizes market risk equivalent amounts for each risk category.

③ Representative stock indices in designated countries

In computing equity risk equivalent amounts by the standardized method using stock indices other than the following stock indices as the representative stock index in a designated country, the financial instruments firm shall confirm such stock index is suitable as a

representative stock index in such country, after considering trading conditions, etc:

- a. Japan — Nikkei Average Stock Prices, Nikkei 300 Index, TOPIX;
 - b. the United States of America — S&P 500;
 - c. Republic of Italy — MIB 30 Index;
 - d. Commonwealth of Australia — ASX 200 Index;
 - e. the Netherlands — AEX Stock Index;
 - f. Canada — S&P Toronto Composite Index;
 - g. the United Kingdom of Great Britain and Northern Ireland — FT 100 Index;
 - h. Swiss Confederation — SMI Index;
 - i. Kingdom of Sweden — OMX Index;
 - j. Spain — IBEX Index;
 - k. Federal Republic of Germany — DAX Index;
 - l. Republic of France — CAC 40 Index;
 - m. Kingdom of Belgium — BEL 20 Index; and
 - n. Hong Kong Special Administrative Region — Hang Seng Index.
- ④ Multilateral Organizations

For the purpose of the computation of interest rate risk equivalent amounts by the standardized method, International Bank for Development and Reconstruction, International Finance Corporation, Multilateral Investment Guarantee Agency, Asian Development Bank, Inter-American Development Bank, African Development Bank, European Investment Bank, Nordic Investment Bank, European Bank for Reconstruction and Development Bank, Caribbean Development Bank, Islamic Development Bank and Council of Europe Development Bank shall be multilateral organizations.

- ⑤ Confirmation of result of external audit for internal measurement approach

A financial instruments firm using the internal measurement approach shall confirm the result of external audit with respect to the process of risk measurement for the previous business year and risk measurement model each year.

- ⑥ Pre-bidding trading of national government bonds

Remarks shall be made on the followings for computing the capital requirement ratio prior to the announcement of coupon rate, etc. in the case of pre-bidding trading of national government bonds:

- (a) in the computation of risk equivalent amounts, a financial instruments firm shall use interest rate reasonably computed after considering the real price in the secondary market as at the time of computation or coupon rate of the latest new issue of government bonds with the same maturity years and the same issuing type as national government bonds which are the objects of the transactions (in the case of national government bonds interest rate of which is fixed at "base interest rate $-\alpha$," "the latest base rate $-\alpha$ of the previous issue") as temporary coupon rate, and, in using it, continue to use such computation method; and
- (b) when a bidding for such national government bonds has been conducted and the name of issue and coupon rate, etc. have been announced, a financial instruments firm shall recompute based on such coupon rate again and apply it to the computation of the capital requirement ratio on or after such date of announcement of the coupon rate without delay.

IV-2-4 Counterparty risk control system

Counterparty risk means the risk of loss which is associated with credit exposure to a counterparty and a financial instruments firm may suffer if the counterparty fails to perform the obligations.

It is important for a financial instruments firm to control the counterparty risk properly.

- (1) Main focus points

Whether a financial instruments firm controls the counterparty risk properly through the implementation of a comprehensive risk control system, appropriate risk recognition and revaluation, performance of internal verification at the time of introduction of new products or new business, construction of a mutual checking system by dividing duties and clarifying authorization.

- (2) Supervisory methods and response

The authority shall make an effort to recognize the conditions of the counterparty risk and risk control system through monthly off-site monitoring reports and hearing, etc. based thereon, and shall collect reports under Article 56-2.1 of the F.I. Act when needed and encourage

improvement.

(3) Concrete handling

① Confirmation of collateral money, etc. deducting from credit exposure equivalent amounts

In the case of deducting the valuation amount of collateral money or other assets under Articles 17.5 and 17.6 of the Capital Requirement Notification, the financial instruments firm shall confirm whether the amount of such deduction is appropriate with the following remarks:

- (a) Whether such collateral money or other assets are suitable as collateral; and
- (b) Whether a financial instruments firm computes the valuation amount of such collateral money or other assets and market risk equivalent amounts to be deducted from the valuation amount properly.

② Confirmation of legal effectiveness of mutual netting contract

If a financial instruments firm computes credit equivalent amounts based on the amount after offsetting in respect of transactions under legally effective mutual netting contract in the computation of counterparty risk equivalent amounts, the financial instruments firm shall confirm the followings:

- (a) Whether, with respect to its legal effectiveness, a financial instruments firm confirms in writing a legal opinion expecting the competent court or supervisory organization to judge reasonably that, in the case of the deterioration of the counterparty of transactions or in the case of the conflict with the counterparty of transactions, the credit exposed by the financial instruments firm remains at or less than the amount offset under such netting contract in light of relevant laws.
- (b) Whether, with respect to relevant laws, the followings are examined:
 - a. laws in the jurisdiction that has granted a license or approval of establishment to the counterparty of transactions and laws in the jurisdiction where the business office or other type of office outside of Japan of the counterparty of transactions is located;
 - b. laws related to individual transaction which is the object of netting and the basis of netting; and
 - c. laws related to a contract necessary for netting and the basis of netting.

③ Confirmation of forward guarantee

Regardless of form or name, a financial instruments firm shall confirm whether counterparty risk equivalent amounts are computed assuming the contract agreeing the conclusion of a debt guarantee contract in the future as forward guarantee. In this case, even if the name is a letter of awareness (which means a written statement issued to a creditor, at the time that a subsidiary, etc. makes borrowing from a financial institution, etc., recognizing the supervisory responsibility over the subsidiary, etc. and agreeing to perform management guidance etc. to such subsidiary, etc.), such letter shall be regarded as forward guarantee if the legal effectiveness of which is regarded as those similar to debt guarantee or forward guarantee based on the statements in the letter and which is required to be noted in the balance sheet under Article 58 of the Regulations of for Terms, Forms and Preparation Method of Financial Statement, etc. (hereinafter referred to as "Financial Statement, etc. Regulations").

④ Confirmation of corporation determined as a corporation with net capital deficiency

Regardless of whether it was publicly announced or not, a corporation determined as a corporation with net capital deficiency as a result of the inspection by the inspection division or external audit shall be a "corporation determined as a corporation with net capital deficiency in objective terms" under Note 3 (4) of Schedule 18 of Article 17.3 (1) of the Capital Requirement Notification.

⑤ Confirmation of consolidated financial statement submission company

A consolidated subsidiary for which counterparty risk equivalent amounts can be computed based on a designated rating granted to the consolidated financial statement submission company as defined in Note 1 of Schedule of Article 17.3 (3) of the Capital Requirement Notification means a corporation subject to consolidated accounting. It shall be noted that such consolidated accounting is externally audited properly and such fact is confirmed by an audit report on a timely basis. With respect to the computation of credit equivalent amounts and counterparty risk equivalent amounts exposed to affiliates, its appropriateness shall be monitored on a timely basis by referring the contract and audit reports, etc.

⑥ Multilateral Organizations

For the purpose of the computation of counterparty risk equivalent amounts by the standardized method, International Bank for Development and Reconstruction, International

Finance Corporation, Multilateral Investment Guarantee Agency, Asian Development Bank, Inter-American Development Bank, African Development Bank, European Investment Bank, Nordic Investment Bank, European Bank for Reconstruction and Development Bank, Caribbean Development Bank, Islamic Development Bank and Council of Europe Development Bank shall be multilateral organizations.

IV-2-5 Liquidity risk control system

Liquidity risk is composed of risks of becoming unable to make necessary financing and having a cash-flow problem and risks to be forced to finance at an extremely higher interest than usual because of deterioration in earnings, etc. of a financial instruments firm (funding risks) and risks of inability to make transactions on a market because of market turmoil, etc. or risks suffering losses as a result of transactions at an extremely worse price than usual (market liquidity risk). It is important for a financial instruments firm to control the liquidity risk appropriately.

(1) Main focus points

Whether a financial instruments firm controls the liquidity risk by means such as taking the following measures according to the business and scale in order to ensure implementation of comprehensive risk control system, appropriate risk recognition and valuation and construction of the mutual checking system by dividing roles and clarification of authorization.

- ① control of daily funding and drawing up and control of medium to long term outlook of funding;
- ② setting and control of the amount of limit for each type of assets;
- ③ integrated control of yen denominated transaction, foreign currency denominated transaction, domestic transaction or overseas transaction;
- ④ securing of financing source (reserve assets) to prepare for abrupt change of business or market environment; and
- ⑤ authorization of collecting information and business control to a person in charge of the liquidity risk control.

(2) Supervisory methods and response

The authority shall make an effort to recognize the conditions of the liquidity risk and the risk control system through monthly off-site monitoring reports and hearing, etc. based thereon, and shall collect reports under Article 56-2.1 of the F.I. Act when needed and encourage improvement.

IV-2-6 Early warning system

There are "early improvement measures" under Article 46-6.1 of the F.I. Act as a method to ensure the soundness of business management of a financial instruments firm. A financial instruments firm which is not subject to the measures is required to make an effort to continue to improve business management in order to maintain and improve the soundness.

If a financial instruments firm has met the preset standards in respect of the following changes in the capital requirements ratio, movement, etc. of the prices of securities, the authority shall identify risks at an early stage by means of holding hearings or collection of reports under the early warning system.

(Note) The authority enforces supervisory responses such as holding a hearing for a financial instruments firm subject to individual standards under the framework of the early warning system. In such case, the business management of such financial instruments firm is not automatically regarded as unsound, and the authority does not necessarily require the improvement of business management immediately.

The authority shall conduct monitoring of early warning flexibly according to the scale and risk characters of a financial instruments firm, considering the cost of the firm and efficiency of the supervisory administration.

(1) Changes in capital requirement ratio

The authority shall recognize the range of changes and ratio of changes each month in respect of the capital requirement ratio based on the data, etc. of off-site monitoring, and analyze actualized risks.

(2) Movement of prices of securities

The authority shall recognize the amount of securities holding of a financial instruments firm based on the data, etc. of off-site monitoring, and analyze market risks based on a stress testing with the assumption of a certain price movement.

(3) Influence by movement of foreign exchange rates

With respect of a financial instruments firm carrying out over-the-counter financial futures transactions, the authority shall recognize the influence by movements of foreign exchange rates based on the data, etc. of off-site monitoring, and analyze risks, etc. to damage capital as a result of movements of foreign exchange rates, considering the methods of segregation, leverage ratio, trading type, etc.

(4) Supervisory methods and response

If a financial instruments firm has met the preset standards for each state based on the data under (1) to (3) above, the authority shall identify risks at an early stage through holding hearings and collection of reports, etc. based on the early warning system in respect of such financial instruments firm.

If it is determined that it is necessary to require enforcement of improvement measures with certainty, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act.

IV-3 Appropriateness of business (first-type financial instruments business)

IV-3-1 Appropriateness of business for securities related business

IV-3-1-1 Compliance system

Securities firms, etc. have the functions as market intermediaries and the roles to facilitate smooth transactions when individual investors, institutional investors and corporations which are issuers of securities access to the financial instruments markets. Such business is accompanied by high publicness and securities firms, etc. are required to fulfill their market intermediation function efficiently and stably by ensuring appropriate protection of investors and carrying out reliable business. For that purpose, securities firms, etc. are also required to manage sound and appropriate business with high self-discipline as market players.

The authority shall make responses to such compliance systems of securities firms, etc. by focus points of system implementation and supervisory methods under III-2-1 in principle, as well as verify widely including the state of compliance with self-regulatory rules prepared in light of appropriate fulfillment of market intermediation function, etc.

IV-3-1-2 Solicitation and explanation system

(1) Remarks on explanatory documents

"Summary of state of internal control" in explanatory documents provided in Article 46-4 of the F.I. Act (Article 174 (4) of the F.I. Business Ordinance) shall contain concrete methods to handle a request for consultation and grievances from customers and internal audit system.

(2) Remarks on notice of delivery of securities or other information

In the case where a securities firm, etc. fails to give a notice of the following matters to a customer in an appropriate manner (including the case of a notice in the manner agreed by a customer in respect of ④), "the state of being determined to have failed to furnish properly a customer with the state of delivery or other information necessary for the customer regarding purchase or sale or other type of transaction, etc. of a security conducted by the customer" under Article 123.1 (8) of the F.I. Business Ordinance shall apply to such case.

① matters required to be stated in a written statement concerning concluded transactions provided in Article 37-4.1 of the F.I. Act;

② if a customer made pre-bidding transaction of a government bond and after the auction was concluded for such national government bond, the issue name, price and amount of money for such transaction and matters for which a notice was given in a trading report at the time of conclusion of the transaction (excluding scheduled redemption date and trade yield);

③ if a customer made pre-bidding transaction of a national government bond and conditions for suspension were not fulfilled, such fact and matters related to the success or failure of such transaction (excluding the case where a customer has given a consent for not giving notice); and

④ in addition to the matters referred to in ① to ③, matters regarding the delivery of money or securities (excluding, in the case where the delivery of money or securities is not made directly with a customer such as the case of delivery of money through a financial institution and the case of delivery of securities through book-transferred settlement, matters regarding

- such delivery).
- (3) Remarks on explanation of important matters regarding switching of investment trust
- In the case where a securities firm, etc. fails to explain the following matters regarding switching and is determined to fail to construct an internal control system such as preparation and keeping of internal records or monitoring concerning the performance of explanation, "the state of failure, in soliciting to make a switch of investment trust beneficial interest certificate, etc., to give explanation of important matters regarding such switch to a customer" provided in Article 123.1 (9) of the F.I. Business Ordinance shall apply to such case.
- ① the types and particulars (name, nature, etc.) of an investment trust or investment corporation (hereinafter referred to as "investment trust, etc.");
 - ② the state (approximate estimation of profit and loss) of the investment trust, etc. to be canceled;
 - ③ cost for the switch (such as cancellation fee and acquisition fee);
 - ④ matters regarding favorable treatment for the redemption and switch; and
 - ⑤ other matters to influence a customer's investment judgment, considering the nature of an investment trust, etc., customer's needs, etc. .
- (4) Remarks on explanation of important matters regarding public sale, etc. of debt securities
- ① If it is determined that the securities firm, etc. fails to make an explanation of the following matters at the time of causing acquisition or selling to a customer (excluding a specific investor) who is individual a debt security (which means a security as defined in Article 123.1 (11) of the F.I. Business Ordinance; in (4), the same) by means of an act under (8) or (9) (excluding handling of private placement) of Article 2.8 of the F.I. Act, "the state of failure, to explain to a customer who is an individual (excluding a specific investor) concerning an important event, which has occurred during the offering period of acquisition or purchase of such security and influences investment judgment" provided in Article 123.1 (11) of the F.I. Business Ordinance shall apply to such case:
 - (a) if the yield of such debt security is significantly unfavorable to a customer compared with the yield of similar debt security issued by the same issuer as the first-mentioned debt security, such fact; and
 - (b) if the debt security has the method that the conditions for redemption of such debt security are determined according to the market price or other index on a financial instruments market (hereinafter referred to as "index, etc.") and the conditions for such index, etc. at the time of causing acquisition or selling of such debt security are unfavorable to a customer compared with such index, etc. which became the basis for setting issuing conditions or public sale conditions of such debt security, such fact.
 - ② With respect to ① (a) above, the following shall be noted:
 - (a) "Such debt security" shall mean a debt security, etc. intended to be placed with individuals to which "debt security, etc. intended to be placed with individuals" as defined in "Publication, etc. of Information of Over-The-Counter Indication Price of Corporate Debt Security, etc. Intended to be Placed with Individuals" in the Board Meeting Resolution of the Japan Securities Dealers Association; hereinafter the same) is applicable.
 - (b) "Similar debt security" means a corporate debt security, etc. to be placed with individuals maturing within six months after the maturity date of such debt security (new issue), which will mature most recent from the maturity date of such debt security (new issue) (if there is more than one issue name with such maturity date, an issue name issued most recently).
 - (c) "Significantly unfavorable to a customer" shall be judged, after considering the interest rate level or other circumstances as of the public offer (public sale), based on, for example, the following value (α):

$$\alpha = X \text{ (value equivalent to credit spread of similar debt securities)} - Y \text{ (value equivalent to credit spread of such debt security (new issue))}$$

$$X = \text{(average value of reported value (value published as of the date immediately preceding the date of public offer) by "over-the-counter indication information publication system for corporate debt security, etc. to be placed with individuals" related to similar debt securities (Note))} - \text{(average simple yield of public and corporate debt security trading reference statistic value published by the Japan Securities Dealers Association of national government bonds with maturity date which is nearest to the maturity date of similar debt securities (value published on the same date as the date of public offer))}$$

$$Y = \text{(yield to subscribers (simple yield) of such debt security (new issue))} - \text{(average simple yield of public and corporate debt security trading reference statistic value of national government bonds with maturity date which is nearest to the maturity date of such$$

debt securities (new issue) (value published on the date immediately following the date of fixing the conditions))

(Note) "Average value of reported value by "over-the-counter indication information publication system for corporate debt security, etc. to be placed with individuals" related to similar debt securities" means the simple average of reported value (simple yield) of each reporting members related to such similar debt securities reported to, and published by, the Japan Securities Dealers Association based on "over-the-counter indication information publication system for corporate debt security, etc. to be placed with individuals."

- ③ With respect to ① (b) above, the followings shall be noted:
- (a) "Unfavorable to a customer" shall mean the state that the theoretical price of a debt security as at the time when a securities firm, etc. fixed a certain range of price in advance and causes acquisition or sell the debt security (or based on the last price, etc. of the issue name on the immediately preceding date) drops beyond such range from the public offer (public sale) price.
 - (b) The theoretical price under (a) above shall be computed by computation formula based on which the issuing (public sale) conditions of a debt security has been fixed, the range of price shall be fixed based on the level fixed by the internal rule for a sale after the public offer or public sale period (fixed price limit), the record of computation formula, etc. of a theoretical price shall be maintained and kept and an appropriate internal control system such as the implementation of internal rules for such handling shall be implemented.
 - (c) With respect to "unfavorable to a customer" for a debt security the conditions of redemption of which are determined by the market prices on stock markets such as a corporate debt security convertible into shares of stock of an other corporation, a Nikkei average linked debt security with special provisions for redemption is applicable (hereinafter referred to as "EB, etc."), in lieu of the method under (a), the price of the issue name concerned as at the time of causing acquisition or selling of EB, etc. (or the last price of the issue name concerned as of the immediately preceding date) can be lower than the initial price (which means the price of the issue name which was used as the base for fixing the issue conditions or the price determined by each firm as equivalent thereto) by 7% or more (limited to the case where using such method is determined before the public offer (public sale) period).
 - (d) If, in selling RB, etc. after the public offer or public sale period, the financial instruments firm fails to quote appropriate trading prices computed based on the internal rule, such failure may be violation of Article 117.1 (2) of the F.I. Business Ordinance, regardless of which method above is used, during the public offer or public sale period.
- ④ With respect to an explanation provided in Article 123.1 (11) of the F.I. Business Ordinance, if a commissioning contract provides that a securities firm, etc. performs an "act to cause acquisition", the securities firm, etc. shall perform such explanation.
- (5) Remarks on sale of securitized products (ensuring traceability of securitized products)
- There are securitized products which have complex structure and for which multiple persons concerned involve in the course of composition and sale. If information is not conveyed from composers of underlying assets, composers of securitized products, distributors (in some cases secondary distributors) and to investors concerning the details of underlying assets or risks appropriately, it is likely that investors cannot recognize risks accurately.
- Although securitized products are traded between professionals (securities firms, etc. and eligible institutional investors, etc.) in principle and are, therefore, unlikely subject to statutory disclosure requirements or explanatory obligations for firms, remarks shall be made on the followings for sale of such securitized products, considering the focus points above, based on "Rules for Sale, etc. of Securitized Products" of the Japan Securities Dealers Association.
- It is desirable that, even if a securities firm, etc. assumes limited roles such as intermediary of purchase or sale, the securities firm, etc. shall cooperate to the extent effectively possible considering that the securities firm, etc. is a contact point.
- ① Whether a securities firm, etc. collects and analyzes information of the details and risks of the underlying assets to make appropriate explanation possible before the sale.
 - ② Whether a securities firm, etc. implements internal procedures and rules, and implements necessary system, to convey information of risks of the underlying assets and liquidity risks, etc. which is not reflected to rating without relying only on rating at the time of sale.
 - ③ Whether a securities firm, etc. implements internal procedures and rules, and implements necessary system, to convey information to facilitate a customer's tracing of information of the details and risks of the underlying assets appropriately if the customer who is an investor so

desire.

- ④ Whether a securities firm, etc. implements the system to value and compute theoretical prices, etc. and quote to customers smoothly and accurately even when specifying market prices has become difficult. Whether, in valuing and computing such theoretical prices, etc., the securities firm avoids arbitrary computation, etc. giving preferences to a user of information for the specific and intentional use.

(6) Supervisory method and response

With respect to the issues of the solicitation and explanatory system of a securities firm, etc. found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a securities firm, etc. through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-3-1-3 Discretionary trading contract, etc.

(1) Remarks on discretionary trading contract with affiliated foreign securities firm

Remarks shall be made on the followings for accepting a notification to enter into a contract under Article 16.1 (8) (b) of the Definition Ordinance.

- ① Whether the division executing transactions under such contract and the division accepting and executing other customer orders shall be separated clearly.
- ② Whether it is ruled that books and records are prepared by the method to show that such transactions are conducted under such contract.

(2) Scope of specific consent of securities firms, etc.

Specific consent under (b) and (c) of Article 123.1 (13) of the F.I. Business Ordinance shall include a consent to:

- ① the specific price (including the price fixed by a pre-determined method) or more (in the case of sale), or the specific price or less (in the case of purchase);
- ② the price with appropriate range from the specific price as base value;
- ③ the price determined by a securities firm, etc. which has been requested to make a best execution during one day trading at the discretion of the securities firm, etc. (so called CD order); and
- ④ The target price determined by the method fixed in advance such as trading volume weighted average prices during one day. (including so called "VWAP target order").

(3) Supervisory method and response

With respect to the issues regarding the transactions listed in (a) to (e) of Article 123.1 (13) of the F.I. Business Ordinance found through the daily supervisory operations and notification of accident, etc., the authority shall recognize voluntary improvement of a securities firm, etc. through holding hearings in depth and collection of report under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-3-1-4 Giving to and receipt from parent or subsidiary juridical persons undisclosed information

(1) Offer of an opportunity of opt-out to a corporate customer

A securities firm, etc. is allowed to give a corporate customer an opportunity of an opt-out (which means that, in the case where a customer who was given a notice to share undisclosed information in advance does not want to share it, the customer requests not to give the undisclosed information to its parent or subsidiary juridical person, etc.; hereinafter the same) under (7) and (8) of Article 153.1 and Article 153.2 of the F.I. Business Ordinance and give and receive undisclosed information of such corporate customer with its parent or subsidiary

juridical person, etc. The authority shall verify the appropriateness to offer a corporate customer an opportunity of an opt-out.

- ① Whether a securities firm, etc. gives a notice to a corporate customer in advance of the scope of undisclosed information to be given to or received from a parent and subsidiary juridical person, etc., the scope of a parent or subsidiary juridical person, etc. whom undisclosed information is given to or received from, the method of giving or receiving of undisclosed information, the method to control undisclosed information at a party which was given the undisclosed information, the purpose of using undisclosed information at a party which was given the undisclosed information and the method to control undisclosed information in the case of suspension of giving to or receiving from a parent or subsidiary juridical person, etc. undisclosed information. If a securities firm, etc. arranges easy access by a corporate customer to necessary information such as clarifying in a notice to a corporate customer the fact that the details of the matters described above are posted accessible at business offices or on a website and the enquiry place, such notice could be considered to be given appropriately even if such notice does not contain the details of the matters described above.
- ② Whether, if there has been a minor change in the details of a notice given to a corporate customer, a securities firm, etc. does not need to give the notice each time of such change but makes a corporate customer accessible to necessary information, for example, posting the updated information on a website continuously and explanation to a corporate customer of the fact appropriately.
- ③ Whether a securities firm, etc. gives a notice of an opportunity of an opt-out by means that a corporate customer can recognize an opportunity of an opt-out clearly such as a notice in writing, etc. at the time of entering into a contract. Whether, in the case where a securities firm, etc. does not give a notice of an opportunity of an opt-out to a corporate customer for about one year or longer such as the case of entering into a long-term contract, the securities firm, etc. give such notice again regardless of the state of transaction with such corporate customer.
- ④ Whether a securities firm, etc. secures a period necessary for a corporate customer to judge whether the corporate customer opts out or not during the period after the notice of an opportunity of an opt-out to the corporate customer until the commencement of giving or receiving undisclosed information related to the corporate customer with a parent or subsidiary juridical person, etc.
- ⑤ Whether a securities firm, etc. clarifies that a corporate customer is given an opportunity of an opt-out continuously by an individual notice and by means that information of an opportunity of an opt-out is given by posting or making accessible at business offices or on a website and, for example a corporate customer can opt out any time through a website or setting a contract place in an internal control division continuously where a corporate customer can opt out.
- ⑥ Whether, in the case where there is a corporate customer to whom a securities firm, etc. does not give an opportunity of an opt-out and gives to or receives from a parent or subsidiary juridical person, etc. undisclosed information only if the corporate customer opts in (which means giving a positive consent in writing to sharing of undisclosed information; hereinafter the same), a securities firm makes it possible for each corporate customer to recognize easily whether the corporate customer is a customer entitled to an opportunity of an opt-out easily through posting at business offices or on a website of information to which type of corporate customer the securities firm, etc. gives (or does not give) an opportunity of an opt-out.

(2) Remarks on giving to and receipt from parent or subsidiary juridical person, etc. undisclosed information

Remarks shall be made on the followings when the securities firm, etc. gives to or receives from a parent or subsidiary juridical person, etc. undisclosed information of a customer under (7) and (8) of Article 153.1 and Article 153.2 of the F.I. Business Ordinance, in addition to III-2-4.

- ① Whether the scope of undisclosed information to be given to or received from a parent or subsidiary juridical person, etc. is specified in advance.
- ② Whether sufficient information control is made for thorough accessing control, measures for the prevention of taking out by a person concerned and prevention of fraudulent outward access for undisclosed information to be given to or received from a parent or subsidiary juridical person, etc.
- ③ Whether the system to make integrated control of undisclosed information such as the appointment of a responsible person in charge of the control of undisclosed information at the

internal control division of each of a securities firm, etc. and a parent or subsidiary juridical person, etc. whom undisclosed information is given to or received from is implemented. Whether undisclosed information of a corporate customer who opted out or a customer who has not opted in (hereinafter referred to as "unshared information") is controlled separately from other unshared information. Further, whether a system to verify the control of undisclosed information and unshared information periodically is implemented.

- ④ Whether the following, for example, measures are taken in order to allow a responsible person, etc. in charge of the control of undisclosed information appointed at an internal control division to fulfill sufficient checking function over sales divisions, etc.:
 - (a) not to allow concurrent holding of duties between employees at internal control divisions and employees at sales divisions or other divisions using undisclosed information to carry out businesses;
 - (b) having accurate checking authorization such as the precedence of judgment of an internal control division over judgment of sales divisions, etc. in respect of matters regarding the control of undisclosed information;
 - (c) prevention of accepting instruction or order issued by sales divisions, etc. (excluding a person responsible for business management) in respect of matters regarding the control of undisclosed information.
- ⑤ Whether a securities firm, etc. clarifies authorization or responsibilities of a responsible person, etc. to control undisclosed information and procedures for handling undisclosed information in writing. Whether, particularly, procedures for handling by sales divisions, etc. of unshared information are provided concretely. Whether, further, a securities firm, etc. inform all officers and employees thoroughly of such procedures through training, etc. to officers and employees of such securities firm, etc. and its parent or subsidiary juridical persons, etc.
- ⑥ Whether the following measures have been taken for officers or employees of sales divisions of a securities firm, etc. or a parent or subsidiary juridical person to which gives, or from which receives, undisclosed information or other divisions using undisclosed information to carry out businesses:
 - (a) such employees are not allowed to access to unshared information other than unshared information controlled by one juridical person, etc. among such securities firm, etc. or parent or subsidiary juridical person which undisclosed information is given to or received from;
 - (b) such officers or employees are not allowed to use such unshared information to solicit a customer the unshared information of whom are controlled by a juridical person, etc. other than a juridical person, etc. controlling accessible unshared information.
- ⑦ Whether a securities firm, etc. takes measures to prevent leakage of undisclosed information (such as making provisions for secrecy and information control, etc.) at the time of personnel reshuffling between a division handling undisclosed information and a division not handling undisclosed information. Whether a securities firm, etc. takes similar measures for personnel reshuffling between a sales division handling unshared information or an other division using undisclosed information to carry out business and a sales division or an other division using undisclosed information to carry out businesses of its parent or subsidiary juridical person, etc.
- ⑧ Whether, in the case where a securities firm, etc. outsources business operations, the following measure are taken, in addition to III-2-7 (2), to prevent providing unshared information to a parent or subsidiary juridical person, etc. through the outsourcee:
 - (a) taking measures to prevent providing of unshared information to a parent or subsidiary juridical person by means such as controlling unshared information separate from other customer information at the outsourcee;
 - (b) taking measures, in the case of providing services to a customer through the outsourcee, to prevent giving the customer false impression that such services were provided by a parent or subsidiary juridical person, etc. of such securities firm, etc.;
 - (c) appropriate control by a securities firm, etc. over the outsourcee to ensure appropriate enforcement of the measures under (a) and (b).
- (3) Remarks on giving and receipt of undisclosed information necessary for internal control operations, etc.

A securities firm, etc. and its parent or subsidiary juridical person, etc. is allowed to give or receive undisclosed information (including unshared information and excluding, with respect to operations of internal control, the case where a securities firm, etc. gives to a parent or subsidiary juridical person, etc. other than specific concerned person) necessary for carrying out operations of maintenance or control of an electronic data processing and network system or

internal control (hereinafter in (3), such operations are referred to as "internal control operations, etc.") under (g) or (i) of Article 153.1 (7) of the F.I. Business Ordinance if the securities firm, etc. takes measures to prevent undisclosed information from leakage from a division in charge of internal control operations, etc. (such division is referred to as "internal control division, etc.") accurately. Remarks shall be made on the followings for such giving and receipt of undisclosed information.

- ① The following operations of a securities firm, etc. are, for example, regarded as "operations of compliance" under Article 153.3 (1) of the F.I. Business Ordinance.
 - (a) consideration of legal issues related to products and services;
 - (b) responses to grievances or enquiry from customers, etc. and settlement of disputes with customers, etc.;
 - (c) control of conflict of interests and control of undisclosed information;
 - (d) responses to the supervisory authority;
 - (e) control of the violation of laws or regulations, etc. in the course of trading, etc. by sales divisions (including consideration of internal penalties);
 - (f) control and monitoring of information of a juridical person (Article 1.4 (14) of the F.I. Business Ordinance) to prevent illegal act such as insider trading, etc.
 - (g) verification of operations in light of reputation risk and corporate ethics;
 - (h) other operations necessary for performance of obligations under laws or regulations.
 - ② The following operations of a securities firm, etc. are, for example, regarded as "operations to control risk of loss" under Article 153.3 (2) of the F.I. Business Ordinance.
 - (a) control of the market risk (risk of suffering loss associated with the fluctuation, etc. of prices of securities, etc. holding);
 - (b) control of the credit risk (risk of suffering loss associated with the default of a counterparty or for other reasons);
 - (c) control of the operational risk (risk of suffering loss associated with the daily business operation such as error of operational process);
 - (d) control of the liquidity risk;
 - (e) establishment or control of business continuity management in the event of natural disaster, etc.
 - ③ Whether the following measures, for example, are taken accurately to prevent leakage of undisclosed information at internal control divisions, etc.
 - (a) prohibition of concurrent holding of duties between an employee of an internal control division, etc. and an employee of a sales division or other division using undisclosed information to carry out business;
 - (b) taking measures to prevent the leakage of undisclosed information (such as making provisions for secrecy and information control, etc.) at the time of personnel reshuffling between an internal control division, etc. and an other division;
 - (c) if there is an employee holding the concurrent duties in an internal control division, etc. and a division not handling undisclosed information, measures equivalent to (a) and (b) above are taken at the division not handling undisclosed information.
 - ④ Receipt by an officer, etc. (which means an officer or employee having sufficient knowledge and experience of compliance and responsible for guidance to and supervision over other employees; hereinafter in ④, the same) of unshared information other than unshared information controlled by one juridical person, etc. for whom the officer works in order to carry out business management control or operations of internal control is not considered to be leakage of unshared information. Whether, in this case, the following measures, for example, are taken:
 - (a) prevention of leakage of such unshared information from such officer, etc.;
 - (b) prohibition of such officer, etc. from using such unshared information for the purpose other than the purpose of carrying out operations of business management or internal control (for example, sales purpose).
 - ⑤ Whether internal rules for measures under ③ and ④ above are implemented and a system to verify the state of compliance with such internal rules is implemented.
- (4) Prevention of abuse of dominant bargaining position by concurrent holding of positions
- In the case where an employee of a sales division of a securities firm, etc. holds a position concurrently as an employee of a sales division of a parent bank, etc. or subsidiary bank, etc. (hereinafter in (4), referred to as "parent or subsidiary bank, etc.") and gives or receives undisclosed information, the authority shall supervise with the following remarks considering that an act to use the dominant bargaining position on trading of the parent or subsidiary bank,

etc. is prohibited under Article 153.1 (10) of the F.I. Business Ordinance.

- ① Whether, if a customer refuses entering into a contract to perform a financial instruments transaction act (hereinafter referred to as "financial instruments transactions contract"), an employee holding a concurrent position in a parent or subsidiary bank, etc. suggests the customer to suspend transactions related to loan, etc. or to make unfavorable treatment related to such transaction and forces the customer effectively to enter into such financial instruments transactions contract.
 - ② Whether, if a customer enters into a financial instruments transactions contract with a competitor (other financial instruments firm), an employee suggests the customer to suspend transactions related to bank business of the parent or subsidiary bank, etc. with which the employee is holding a position concurrently or to make unfavorable treatment for such transaction and disturb entering into such contract with the competitor.
 - ③ Whether a securities firm, etc. establishes a division, or appoints a person, responsible for taking measure to prevent an act to use the dominant bargaining position improperly and implements internal control system to verify taking appropriate measure to prevent such act by such division or person.
 - ④ Whether trainings are conducted by a person with knowledge of banking business operations and work experience periodically and when needed to prevent an act to use the dominant bargaining position improperly.
 - ⑤ Whether a securities firm, etc. implements the system to respond to grievances such as the clarification of a contact place for grievances from customers for acts using the dominant bargaining position improperly, establishing a grievances settlement division and making grievances settlement procedures, etc.
- (5) Interpretation of Article 32 of the F.I. Business Ordinance
- ① "Operations to carry out financial instruments business, etc. or financial instruments intermediary business" as provided in Article 32 (1) of the F.I. Business Ordinance means the following operations for which judgment, etc. on business management for financial instruments business, etc. or financial instruments intermediary business is not involved.
 - (a) operations of acquisition, possession, lease, maintenance, security and control of real estate and equipment such as shop;
 - (b) operations of control such as maintenance and operating, etc. of automatic cash dispenser, etc.;
 - (c) preparation, implementation, maintenance, dispatching and delivery of books, records, calculation sheet, tickets;
 - (d) computer related operations (system development, maintenance, data keeping, computer processing, etc.);
 - (e) computation operations (including accounting operations such as payroll accounting and monthly accountings);
 - (f) operations related to the control and arrangement of securities;
 - (g) handling of name transfer;
 - (h) operations to demand principals and interests payment of public or corporate debt securities and investment trust;
 - (i) delivery settlement operations of securities at a financial instruments exchange or inter-financial instruments firms, etc.;
 - (j) welfare operations for officers and employees such as counseling of employees and package purchase and control of office equipments and services;
 - (k) administrative assistance such as preparation of documents for personnel affairs (including operations regarding labor dispatch service to financial instruments firms, etc. or financial instruments intermediary firms);
 - (l) operations of education and training of officers and employees;
 - (m) advertisement and public relation operations;
 - (n) driving, maintenance and checking of cars;
 - (o) operations of preparation of statistics;
 - (p) operations to provide public information such as publications;
 - (q) printing, book binding, dispatching and delivery of documents, etc.
 - ② "Operations exclusively for the purpose that any of the following persons carries out business" as provided in Article 32 (2) of the F.I. Business Ordinance means the operations listed in ① (excluding (c)) for which business control judgment, etc. is not involved.

In the application, ① (d) above shall be read as "computer related operations (system development, maintenance, control of hardware and software for the purpose of data keeping,

computer processing, etc.)," ① (f) above shall be read as "operations regarding control and arrangement of securities (limited to securities held as own assets of a parent or subsidiary juridical person, etc.)," ① (g) above shall be read as "handling of name transfer (limited to securities held as own assets of a parent or subsidiary juridical person, etc.)" and ① (j) above shall be read as "clerical assistant operations such as preparation of documents regarding personnel affairs (including operations of labor dispatch service to financial instruments firms, etc. or financial instruments intermediary firms and a parent or subsidiary juridical person, etc.)."

- ③ It shall be noted that the operations referred to in ① (c) (excluding operations of shipping and delivery), data keeping under ① (d) and operations referred to in (f) to (i) are operations closely related to carrying out such financial instruments business, etc. or financial instruments intermediary business and banking business, etc., and such operations therefore is not allowed in principle to be outsourced other than to a parent or subsidiary juridical person, etc. of the financial instruments firm, etc. or financial instruments intermediary firm or a corporation provided in (1) or (2) of Article 32 of the F.I Business Ordinance in principle, except for the case where there is a reasonable cause, and that the business operations are supervised.

It shall be noted that a financial instruments firm (limited to a person carrying out the first-type financial instruments business or investment management business) shall obtain an approval for other business as provided in Article 35.4 of the F.I. Act to be commissioned to carry out the business referred to in ② and carry out businesses referred to in (a), (b), (e) and (j) to (q) of ① above.

- ④ It shall be noted that, in the case of outsourcing the businesses referred to in ① and ② above from such financial instruments firm, etc. or financial instruments intermediary firm, such financial instruments firm, etc. or financial instruments intermediary firm shall not be released from liabilities to customers and administrative liabilities regarding such businesses.

(6) Supervisory method and response

With respect to the issues regarding giving and receipt of undisclosed information between a securities firm, etc. and parent or subsidiary juridical person, etc. found through the daily supervisory operations and notification of accident, etc., the authority shall recognize voluntary improvement of a securities firm, etc. through holding hearings in depth and collecting reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-3-1-5 Measures to prevent false recognition

(1) Remarks on measures to prevent false recognition as other financial institution

The authority shall verify with the following remarks in order to prevent customers to recognize a securities firm, etc. as other financial institution

- ① Whether a securities firm, etc. explains to a customer fully in respect of the followings if the securities firm, etc. carries out businesses in the principal business office or other business office located in the same building as an other financial institution:
- (a) the securities firm, etc. is a different juridical person from the financial institution or its parent or subsidiary juridical person, etc.;
 - (b) the fact that products or services related to securities related business provided by the securities firm, etc. are not provided by the financial institution or its parent or subsidiary juridical person, etc.;
- ② Whether the following measures are taken appropriately in the case where an employee of a sales division of a securities firm, etc. holds a position in a sales division of its parent or subsidiary juridical person, etc. concurrently:
- (a) the arrangement that a customer who visits the securities firm, etc. can easily recognize the details of products or services provided by an employee in the same business office and the name of the juridical person who provides the products and services by means such as posting them at such business office;
 - (b) the arrangement that the employee clarifies to a customer the scope of a parent or subsidiary juridical person, etc. where the employee holds a position concurrently in a manner that the customer understands easily; particularly, it is desirable that, in the case of

business offered to unlimited and many customers such as business provided at a reception desk, the scope of main products and services provided by the employee and the concurrent holding of positions by the employee are always clarified to customers by means such as positing at the reception desks;

- (c) in the case where the employee solicits a new customer or solicits a new product or service to a customer particularly, the concurrent holding of positions of the employee and the scope of products or services provided by the employee shall be explained fully;
 - (d) ensuring to provide a customer with an opportunity that, in the case of entering into a contract with a customer, the customer can recognize the name of a juridical person who is the counterparty of the contract accurately by means such as confirmation by a written statement, etc.
- (2) Supervisory method and response

With respect to the issues regarding measures to prevent false recognition of a securities firm, etc. found through the daily supervisory operations and notification of accident, etc., the authority shall recognize voluntary improvement of a securities firm, etc. through holding hearings in depth and collecting reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-3-1-6 Business continuity management (BCM)

- (1) Significance and responses

It is very important for lives of people and national economy that a securities firm, etc. performing an important role as an intermediary on financial instruments markets takes prompt recovery measures and makes appropriate responses such as ensuring the continuity of requisite minimum business in the event of the occurrence of crisis. It is therefore necessary to establish the business continuity management (BCM) and prepare manuals for crisis management (CM) during ordinary times. In this aspects, the authority shall verify the appropriateness in supervising securities firms, etc. according to the scale of the businesses with the following remarks.

- (2) Main focus points

Whether the business continuity plan (BCP) enables early recovery from damage and continuity of requisite minimum business to maintain the functioning of the financial system in the event of a terror, large scale disaster, etc. Whether a securities firm, etc. implements the system of responding with coordination with a financial instruments firms association, other securities firms, etc. and relevant organization, etc. based on the result of the review at the Securities Market BCP Forum, etc. Whether the plan responds to worldwide business disruption according to the state of business.

For example:

- ① Whether security measures for customer data, etc. to be ready for disasters, etc. (computerization of paper information, back-up of computerized data files and programs, etc.) are taken.
- ② Whether security measures for the computer system center, etc. (location of back-up centers according to necessity, ensuring personnel and communication network) are taken.
- ③ Whether such back-up systems avoid geographical concentration.
- ④ Whether a securities firm, etc. has a concrete plan of target hour to recover important operations (payment of money to customers, cancellation of MRF or MMF, sale order of shares of stock, etc. on deposit, margin transactions, order to settle futures or options, settlement of concluded but undelivered transactions) from temporary measures (hand working, processing at a back-up center, etc.) in light of maintenance of life of customers, economic activities and functioning of financial instruments markets.
- ⑤ Whether the board of directors has approved the preparation and important review of the business continuity plan. Whether an independent organization such as internal audit or external audit verifies the business continuity management.
(Reference) "Arrangement of Business Continuity Management of Financial Institution" (Bank of Japan July 2003)
"Principles of Business Continuity" (Joint Forum August 2006)

III-2-9 shall apply in principle.

IV-3-1-7 Financial measures in the event of Disaster

(1) Financial measures for disaster area

Financial Services Agency Anti-Disaster Measures Plan under Article 36.1 of the Disaster Countermeasures Law and Financial Services Agency Civilians Protection Plan under Articles 33.1 and 182.2 of the Law on Measures to Protect Civilians from Armed Attack (hereinafter referred to as "Civilian Protection Law") provide for financial measures. In the event that a disaster (which means a disaster provided in Article 2 (1) of the Disaster Countermeasures Law or armed attack disaster provided in Article 2.4 of the Civilians Protection Law or a disaster in the event of an emergency event provided in Article 183 of the Civilization Protection Law; hereinafter the same) has occurred or will likely occur, the authority shall make close communication with relevant organizations according to the state of disaster in the area and demand for money, etc. and take the following measures to securities firms, etc. appropriately within the scope deemed necessary in a timely fashion.

- ① providing convenience as much as possible in the event of losing a notified seal;
 - ② cooperation for reissuance measures in the event of losing securities;
 - ③ providing convenience as much as possible in the event that a sufferer customer of disaster requests for payment of sale proceeds or cancellation proceeds of securities on deposit on the same day;
 - ④ informing, when a securities firm, etc. has taken measures of suspension of reception desk operations, etc., trading persons thoroughly by means of giving notice by means of posting of a poster stating the names of business offices where operations are suspended at business offices and putting such fact on newspapers and the website; and
 - ⑤ other consideration of responses to customers fully.
- (2) Various financial measures inside and outside of area subject to Tokai Earthquake disaster countermeasures

The Law on Large Scale Earthquake Countermeasures Special Measures requires designated administration agencies to take measures to prevent the occurrence of an earthquake disaster and a secondary disaster and prevent the expansion of disaster when areas subject to earthquake disaster countermeasures are designated pursuant to said Law.

The authority shall make close communication with relevant organizations according to the demand for money, etc. in the area and take the following measures for securities firms, etc. appropriately in respect of operations of financial instruments business as response to Tokai Earthquake because of mechanization and dissemination of unattended service network and difficulty of responding in various areas separately.

- ① Response by a securities firm, etc. having business offices or other type of offices in the Tokai Earthquake disaster countermeasures area at the time of warning:
 - (a) if an warning was issued during the business hour, the authority shall request a securities firm, etc. to suspend operations at a reception desk of the business office or other type of office;
 - (b) with respect to methods to inform all of trading persons of suspension of operations, etc., the authority shall request a securities firm, etc. to give a notice by means of posting a poster stating the names of business offices, etc. which suspend operations, etc. at the business office or other type of office and putting the fact on a newspaper or website;
 - (c) if a warning was issued on holiday, before or after the business hour, the authority shall request a securities firm, etc. not to commence or resume operations at reception desks in order to ensure smooth operations of the securities firm, etc. after the occurrence of disaster;
 - (d) others:
 - a. if the warning has been cleared, the authority shall request a securities firm, etc. to commence ordinary operation as soon as possible;
 - b. with respect to emergency measures of a securities firm, etc. after the occurrence of a disaster, the authority shall request to take accurate measures under IV-3-1-7 in a timely manner;
- ② Response by a securities firm, etc. having business offices or other type of offices outside the countermeasures area at the time of warning:

Even if a business office or other type of office of a securities firm, etc. located in an earthquake disaster countermeasure area has taken measures to suspend operations, the authority shall request other business offices or other type of offices located outside of such

countermeasure area subject to measures for suspension of operations to continue ordinary operations.

(3) Administrative report

When the authority has taken the above financial measures, the authority shall report it to the Director-General of the Supervisory Bureau without delay.

IV-3-2 Appropriate fulfillment of market intermediation function, etc. of securities firms, etc.

A securities firm, etc. takes roles including a function of market intermediation on financial instruments markets associated with high publicness. A securities firm, etc. participates to a financial instruments market as a market player.

The systematic reform has born fruit since the Financial Bigbang. On the other hand, subsequent to sequent large scale false orders on a financial instruments market and system failure at a securities firm, etc., unfair transactions by an investor such as manipulation and insider transaction, improper act by an issuer such as false statement, etc. of securities reports, "Council on Market Intermediation Function of Securities Firm" was set up in March 2008 and "Consolidation of Arguments" has been prepared and published in June.

Recommendations, etc. regarding the four issues stated in the "Consolidation of Arguments" which are (1) improvement of the reliability of operations as a market intermediary, (2) fulfillment of the checking function of securities firms, etc. over issuers, (3) fulfillment of the checking function of securities firms, etc. over investors and (4) maintenance of the self discipline of securities firms, etc. as market players should be achieved as self-regulatory rules, etc. prepared by self-regulatory organizations such as the Japan Securities Dealers Association in principle. It is important that the authority makes necessary responses with the following focus points and supervisory methods considering self rules, etc. in light of improvement of reliability of financial instruments markets by means of appropriate fulfillment of the market intermediation function, etc. of securities firms, etc.

IV-3-2-1 Improvement of reliability of operations as market intermediaries

(1) Remarks on order control system

① Whether a securities firm, etc. implements internal rules appropriately and ensures informing all of the officers and employees thoroughly based on the Resolution of the Board of Directors of Japan Securities Dealers Association "Implementation of Order Control System of Member Firms".

② Whether the system to prevent false order works sufficiently such as the installment of order limit in a system including hard limit or soft limit for buy or sell order.

③ Whether enhancement, improvement and strengthening maintenance of the functioning of the order control system is ensured through personnel allocation including the appointment of CIO who supervises the buy or sell order system, training and periodical inspection.

④ Whether the system that a controller involves in the order limit or cancellation of warning is appropriately implemented, and such system works appropriately. Whether a wholesale division handles it appropriately.

⑤ Whether crisis response measures for a large scale false order have been implemented and all of officers and employees are informed of the system thoroughly.

⑥ Whether, even in the event of the occurrence of a false order, a system to take appropriate measures is implemented in order to prevent a failure at the due time of settlement on a settlement day.

(2) Remarks on change of ratio applicable to securities used as margins for margin transactions

Whether a securities firm, etc. makes prior explanation or information to customers concerning the change, etc. of ratio, giving notice to customers at the time of changing ratios, setting information period at the time of change, implementation of internal rules, etc. in an appropriate manner based on Resolution of the Board of Directors of Japan Securities Dealers Association "Handling of Change, etc. in Ratio of Securities used as Customer Guarantee Money for Margin Transactions."

(3) Remarks on control of an electronic data processing and network system of securities firm, etc.

The "state that control of an electronic data processing and network system is insufficient" under Article 123.1 (14) of the F.I. Business Ordinance is applicable to the case where any of the

following facts is found in respect of the control of an electronic data processing and network system of a securities firm, etc.

- ① the case of the failure of appropriate checking periodically such as system auditing by a professional of an electronic data processing and network system in respect of the firm's electronic data processing and network system;
- ② the case of the failure of making sufficient system responses to prevent a false order placement such as the failure of inclusion of order limit into the system including hard limit or soft limit regarding placement of an order of purchase or sale;
- ③ the case where it is determined that an appropriate system has not been implemented in light of the matters, etc. listed in III-2-8.

IV-3-2-2 Fulfillment of checking function over issuers

- (1) Remarks on examination of underwriting, etc.
 - ① Whether a securities firm, etc. implements appropriate rules for the examination of matters to contribute to the suitability judgment whether to underwrite or not such as financial conditions and business performance of the issuer based on the self-regulatory rules of the Japan Securities Dealers Association "Rules for Underwriting, etc. of Securities" and such examination is performed effectively.
 - ② Whether a securities firm, etc. relies on the examination of other securities firm, etc. which is a co-lead manager and does not examine by itself.
 - ③ Whether a securities firm, etc. ensures system implementation to make appropriate examination, such as ensuring of the independency of a division in charge of examination from sales divisions appropriately from the view of functioning or effectiveness.
 - ④ Whether a securities firm, etc. has the functioning to verify or value the conflict of interest with other divisions in the securities firm, etc. in underwriting and whether, as a result of such functioning, the securities firm, etc. implements the system to prevent conflict of interests appropriately.
 - ⑤ Whether a securities firm, etc. implements appropriate rules for the methods to compute prices, etc. and implements a system to make appropriate decision on conditions of underwriting based on the laws and regulations and self-regulations in order to prevent underwriting on the materially inappropriate conditions in terms of volume, price or other conditions.
- (2) Remarks on underwriting of share certificates, etc. issued by parent or subsidiary juridical person, etc.

Whether, in the case where a securities firm, etc. acts as the lead manager of underwriting of shares certificates, etc. issued by its parent or subsidiary juridical person, etc. under Article 153.1 (4) (c) of the F.I. Business Ordinance, the following measures are taken to ensure appropriate involvement by an other securities firm, etc. regarding the determination of the issue price for such underwriting:

 - ① The followings shall be stated clearly in an agreement for underwriting examination procedures entered into between such securities firm, etc. which is the lead manager of underwriting and the issuer:
 - (a) an other securities firm, etc. which involves in determining the issue price (hereinafter in (2), referred to as "independent underwriting manager") has authorization equivalent to the lead manager;
 - (b) an independent underwriting manager can express its opinion on the appropriateness of underwriting examination to the issuer and externally;
 - ② A securities firm, etc. having sufficient experience of underwriting business in light of the followings shall be assigned as an independent underwriting manager:
 - (a) engagement in underwriting business for at least five years;
 - (b) experience of a lead manager within the past two years. It is desirable, in the case of share certificates, warrant certificates or corporate debt securities with warrants, that the securities firm, etc. has the record of a lead manager for underwriting of share certificates, warrant certificates or corporate debt securities with warrants issued by a person who belongs to the same type of business as the issuer of the share certificates, warrant certificates or corporate debt securities with warrants. It is desirable, in the case of corporate debt securities, that the securities firm, etc. has the record of a lead manager for underwriting of corporate debt securities issued by a person who belongs to the same type of business as the issuer of the corporate debt securities.

(Note) The type of business of each issuer could be classified by "large classification" classified and published by the Securities Code Committee.

(3) Remarks on underwriting and purchase of privately placed CB, etc.

Allocation of new shares of stock to a third party for the capital increase and so called privately placed CB (including MSCB), etc. could be considered effective as a method of financing for corporate revival, etc. but, on the other hand, has a risk to cause disbenefit to existing shareholders because of the dilution depending on issue conditions and uses. Based on this, in the case where a securities firm, etc. deals such issues (including the case of purchase by the securities firm, etc. or its affiliate, the case of purchase by other funds, etc.), remarks shall be made to ① whether appropriate product engineering based on the influence, etc. on existing shareholders is made, ② sufficient explanation of the product according to the degree of understanding of product to the issuer (or its management) is made, ③ appropriate disclosure is made by the issuer.

(4) Remarks on issuers related to antisocial forces

A securities firm, etc. is, in order to prevent listing of shares of stock, etc. of an antisocial force or a corporation closely related to antisocial forces, desired to coordinate with relevant authorities or Japan Securities Dealers Association, etc., recognize the fact appropriately by the examination of underwriting, etc., and make responses such as refusing such underwriting, etc. in some cases.

IV-3-2-3 Fulfillment of checking function over investors

(1) Remarks on trade control system to prevent customer's unfair transaction

It is necessary for a securities firm, etc. to prevent an act to accept an order, etc. for purchase or sale transaction, etc. of securities by a customer despite knowing that such order will form artificial market which does not reflect actual market or an act to accept an order, etc. for purchase or sale transaction, etc. of securities by a customer despite knowing that such order is likely insider transaction, so as to fulfill the checking function on investors. Remarks shall be made on the followings for controlling trades to prevent unfair transactions by a customer based on the Board of Directors Resolution of Japan Securities Dealers Association "Implementation of Trade Control System by Association Member to Prevent Unfair Transactions by Customers". (Particularly, the securities firm, etc. shall pay due attention in the case of an Internet trading, considering its non-face-to-face nature).

- ① Accurate recognition of the trend of purchase or sale by a customer and thorough control
 - (a) Whether a securities firm, etc. implements concrete handling methods to recognize a customer's trend of purchase or sale such as instruments to be bought or sold, trading methods and trading type, and recognizes accurately the reason, etc. for purchase or sale through monitoring, etc. in a timely manner based on such handling method.
 - (b) Whether an internal control division ensures officers and employees to know such handling methods thoroughly and implements the system to ensure its effectiveness such as reviewing when needed.
 - (c) Whether a securities firm, etc. makes an effort to arrange insider registration cards through performing periodical checking in respect of all customers to confirm the registration or check the details of registration with information obtained from an external information vendor in order to ensure the accuracy of insider registration.
 - (d) Whether a securities firm, etc. makes an effort to specify the original person who placed an order or the real investor in respect of transactions with an investment enterprise association and an order from foreign jurisdiction in order to prevent manipulative behavior or insider transaction, etc.
 - (e) Whether, when a securities firm, etc. recognizes the likeliness that a customer uses false name account, the securities firm, etc. makes an effort to clarify the real trader and to monitor with special attention.
- ② Establishment and effective use of trade examination standards
 - (a) Whether a securities firm, etc. establishes concrete extraction standards considering up-down ratio, market participation ratio of the securities firm, etc. and trading condition by a specific customer, etc. in respect of individual issue name in order to ensure the fairness of transactions by customers, and makes appropriate extraction based on such standards.
 - (b) Whether a securities firm, etc. establishes concrete examination standards for extracted issue names and makes an appropriate trade control such as taking measures necessary (such as enquiry to customers, calling for attention, suspension of transaction, etc.) to reject unfair

transactions such as artificial market formation.

- (c) Whether a securities firm, etc. implements the system to ensure the effectiveness of the extraction standards, the examination standards and the state of taking measures at the internal control division by means of verification of consistency with the real state in a timely manner and reviewing when needed.

③ Others

- (a) Whether, with respect to orders for margin transactions to establish new short positions conducted by a customer continuously for a short time which are determined that the customer has the purpose to violate the price limit effectively without formal violation, a securities firm, etc. informs all customers of the purpose of restriction on short selling such as the fact that the transaction provided in Article 14 (2) of the Cabinet Office Ordinance on Regulation on Transactions, etc. of Securities is not applicable to such orders.

- (b) Whether a securities firm, etc. conducts appropriate control such as taking measures such as checking of orders in a timely manner and taking measures such as enquiry to customers, warning, suspension of transactions, etc. when needed in order to prevent accepting an order for the violation of price limit effectively without formal violation.

- (c) Whether it is ruled that, if a customer is suspected to conduct insider transactions, the securities firm, etc. shall notify the supervisory authority promptly based on the provisions of Article 9 of the Crime Profit Law.

(2) Remarks on pre-hearing

Whether it is ruled that, if a securities firm, etc. holds a pre-hearing by itself or on commission to a third party, the securities firm, etc. makes by itself or requires a third party to make, ① an approval by its compliance division, ② entering into purchase or sale, etc. of the securities, etc. and a contract to agree not to provide the corporate related information with the person subject to the investigation, ③ preparation and retention of written records based on the F.I. Business Ordinance and the Board of Directors Resolution of Japan Securities Dealers Association "Appropriate Pre-Hearing by Association Member".

(3) Remarks on antisocial forces related investors

It is desirable that a securities firm, etc. makes sufficient trade control and trade examination concerning investors which have possibility to have relationship with antisocial forces under the coordination with relevant authorities and Japan Securities Dealers Association, etc.

IV-3-2-4 Maintenance of self-discipline as market player

Businesses of securities firms, etc. as market players have been diversified and become more complex such as principal investment, M&A advisory business, proposal for financing with complex nature of products and securitized transactions. On such background, businesses of securities firms, etc. have been increasingly problematic in light of contingent conflict of interest and corporate ethic.

Based on such circumstances, remarks shall be made on the followings for the maintenance of self-discipline s of a securities firm, etc. as a market player.

- ① Whether a securities firm, etc. prepares internal policies and rules and implements an appropriate internal control system (including internal audit system) in order to prevent conflicts of interest and comply with ethical standards. Whether a securities firm, etc. implements compliance system appropriately by means such as informing all officers and employees through training, etc.

- ② Whether a securities firm, etc. sorts out transactions, etc. which are thought to have a risk of conflicts of interest;

- ③ Whether a securities firm, etc. divides the internal organization when needed and implements an appropriate pre-examination system from the view independent from a sales division (decision of appropriateness to conduct such transactions, etc. after examination) in order to prevent conflicts of interest;

- ④ Whether a securities firm, etc. conducts appropriate explanation or disclosure to customers or investors concerning the state of conflicts of interest when needed.

(Reference) (Examples of problematic cases for (contingent) conflicts of interest, etc.)

- purchase of shares of stock, taking advantage of a false order for shares of stock, despite knowing that the order is false;
- underwriting operations as the lead manager at the time of listing of shares of stock by

unlisted corporation in which a securities firm, etc. (or another company within the same group) invests, and sale of such shares of stock after the listing;

- an act to form securitized products created from underlying assets that a securities firm, etc. (or another company within the same group) acquired for principal investment and sell it to other investors without making sufficient explanation (risk transfer);
- proposal and consideration of securitization scheme for which the purpose of manipulation of accounting or purpose of tax evasion using SPC, etc. is suspected.

IV-3-2-5 Supervisory methods and responses

The authority shall encourage appropriate fulfillment of the market intermediary function, etc. of securities firms, etc. under the coordination with relevant organizations including a financial instruments firms association based on the above focus points. If the authority deems necessary for public interest and to protect investors, the authority shall recognize the state of voluntary improvement of business management at the securities firm, etc. through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed. If a gross problem in the public interest and to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act. Further, if a violation of laws and regulations, etc. of a particularly grave nature has been found, the authority shall consider necessary responses including the issuance of an order to suspend business under Article 52.1.

IV-3-3 Appropriateness of businesses related to over-the-counter derivatives business

IV-3-3-1 Compliance system

It is important to ensure investors' trust on over-the-counter derivatives firms (which means first-type financial instruments firms carrying out as a business the act referred to in Article 2.8 (4) of the F.I. Act; hereinafter the same) that an over-the-counter derivatives firm recognizes its role as a provider of over-the-counter derivatives transactions fully and makes an effort to carry out sound and appropriate business management in strict compliance with the laws and regulations and various rules for businesses.

The authority shall make responses to such compliance systems of over-the-counter derivatives firms by focus points of system implementation and supervisory methods under III-2-1 in principle, as well as, in addition, verify widely including the state of compliance with self-regulatory rules prepared by a self-regulatory organization.

- (1) Remarks on customer assets separation by currency related over-the-counter derivatives transactions, etc. firm

The authority shall supervise with the following remarks in the case where an over-the-counter derivatives firm controls money or other guarantee money for currency related over-the-counter derivatives transactions, etc. (which mean the act referred to in Article 143.3 (2) of the F.I. Business Ordinance; hereinafter the same).

- ① Whether an over-the-counter derivatives firm controls trusts provided in Article 143.1 (1) of the F.I. Business Ordinance (separate customer money trust) separate clearly from trusts provided in Article 141.1 of the F.I. Business Ordinance (segregated customer money trust).
- ② Whether an over-the-counter derivatives firm computes the amount of individual separate customer money (which means the amount of money or guarantee money deposited by each customer) and the required amount of customer separate money (total amount of individual separate customer money) as defined in Article 143-2.1 (6) of the F.I. Business Ordinance in an appropriate manner.

In the computation of the required amount of separate customer money, the over-the-counter derivatives firm adds or deducts the following amounts to or from money or guarantee money deposited by customers.

- (a) realized profit or loss;
 - (b) valuation profit or loss;
 - (c) swap profit or loss.
- ③ Whether an over-the-counter derivatives firm judges whether the value amount of the principal of trust properties under Article 143-2.1 (6) of the F.I. Business Ordinance is short from the required amount of separate customer money on the date in Japan, as the base date, to which the time that the required amount of separate customer money is computed belongs.

Whether, for example in the computation of the required amount of separate customer money for transactions from 7:00 a.m. on a specific day in Japan hour till 7:00.a.m. of the immediately following day (hereinafter in IV-3-3-1, referred to as "computation date") as of 7:00 a.m. of the computation date, the over-the-counter derivatives firm adds the shortage within two business days since the day immediately following the computation date.

- ④ Whether it is ruled that trust assets always exceed the required amount of separate customer money even if a financial institution, etc. which is the trustee of a separate customer money trust issues a letter of guarantee, etc. (hereinafter referred to as "LG") to a covering transaction party and payment is made based on the LG. Whether, when a separate customer money trust expires as a result of filing a petition, etc. for commencement of bankruptcy proceedings, rehabilitation proceedings or reorganization proceedings in respect of the over-the-counter derivatives firm, the contract provides for the return of money or guarantee money to customers has the precedence over the payment to the covering transaction party.
 - ⑤ Whether an over-the-counter derivatives firm controls the state of customer assets separation appropriately by means of, for example, periodical external auditing or internal auditing by an independent division.
- (2) Remarks on segregation by securities related over-the-counter derivatives transactions firm
- IV-3-3-1 shall apply to remarks on the control of money or other guarantee money for securities related over-the-counter derivatives transactions (which means transactions provided in Article 117.1 (29) of the F.I. Business Ordinance; hereinafter the same) by an over-the-counter derivatives firm, and it shall be noted that the amount of interest adjustment and the amount of dividends adjustment in the computation of the required amount under IV-3-3-1 (1) ② are added or reduced.
- (3) Supervisory methods and responses
- ① The authority shall require an over-the-counter derivatives firm to submit materials evidencing the balance of trusts such as balance certificates, etc. issued by a trust bank and a written statement to compute the required amount of control as of the computation date at least once a week in principle in order to confirm the appropriateness of the control of money or other guarantee money related to currency related over-the-counter derivatives transactions, etc. and securities related over-the-counter derivatives transactions targeting individual customers.
 - ② The authority shall require an over-the-counter derivatives firm to make a report of external auditing or internal auditing periodically or when needed in order to confirm the appropriateness of the control of money or other guarantee money related to currency related over-the-counter derivatives transactions, etc. and securities related over-the-counter derivatives transactions targeting individual customers.
 - ③ In addition, with respect to the issues regarding compliance system of an over-the-counter derivatives firm recognized in the course of daily supervisory operations, the authority shall recognize the state of voluntary business improvement at the over-the-counter derivatives firm through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed. If it is determined that there is a gross problem in the public interest or to protect investors, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act. Further, if a violation of laws and regulations, etc. of a particularly grave nature has been found, the authority shall consider necessary responses including the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-3-3-2 Solicitation and explanation system

- (1) Remarks on advertisement, etc.
 - ① Whether, in the case where, even if there is a contract to the effect that, in the event that a loss exceeds a certain ratio, unsettled positions are settled by offsetting transactions automatically (hereinafter referred to as "loss-cut rules"), losses may exceed the amount of customer margins or other guarantee money due to drastic movement of market prices, an over-the-counter derivatives firm represents such fact appropriately; and
 - ② Whether an over-the-counter derivatives firm leads (or forced effectively) a customer to continue to attend to a seminar, etc. despite the fact that the customer has shown the intent not to desire to continue to attend the seminar, etc. during the seminar, etc. In this case, it shall be noted that the provisions of Article 38 (6) of the F.I. Act (so called "prohibition of resolicitation") shall apply.
- (2) Remarks on explanatory documents

"Outline of internal control" in explanatory documents under Article 46-4 of the F.I. Act shall contain concrete methods to handle a request for consultation and grievances from a customer and internal auditing system.

- (3) Remarks on furnishing of warning statements regarding solicitation methods, etc. of over-the-counter derivatives transactions

When an over-the-counter derivatives firm conducts over-the-counter derivatives transactions, whether the over-the-counter derivatives firm gives warning to customers appropriately by means of furnishing brief statements (warning statements) informing ① application of unrequested solicitation regulations, ② warning on risks, ③ the contract place, etc. of a designated ADR organization, etc. in the event of a trouble in a manner easily understandable and in large letters and make an explanation according to each customer's attribute based on "Rules for Investment Solicitation, Customer Control, etc. by Association Members" of the Self-regulatory Rules of the Japan Securities Dealers Association and "Financial Futures Business Conduct Rules" of the Financial Futures Association of Japan. Whether the over-the-counter derivatives firm has the system to confirm the state of implementation appropriately.

(Note) It shall be noted whether a financial instruments firm treats the sale of complex structured debt securities or investment trust similar to on-market derivatives transactions or over-the-counter derivatives transactions in a manner equivalent to the above.

- (4) Remarks on explanatory obligation of over-the-counter financial futures firm

① Showing values quoted at the time of trading, etc.

(a) In showing prices of a financial instrument, financial index or option quoted at the time of trading to a customer who has requested to show such prices in respect of over-the-counter financial futures transaction under Article 123.1 (21) of the F.I. Business Ordinance, the over-the-counter financial futures firm may show the open, high, low and close each trade date.

(b) An over-the-counter financial futures firm shall keep prices of a financial instrument, financial index or option quoted at the time of trading for at least three years.

② Transaction to create offsetting positions

(a) Whether, in accepting an order, etc. for over-the-counter financial futures transactions (limited to transactions for which margins or other guarantee money are deposited), the over-the-counter financial futures firm solicits a customer, or performs other similar act, to conduct transactions opposite to transactions conducted by the customer (which means transactions to reduce losses arising from such opposite transactions; so-called "transactions to create offsetting positions").

(b) When a customer has shown a positive intention to conduct transactions to create offsetting positions or when a customer has made an enquiry whether the customer is allowed to conduct transactions to create offsetting transactions, informing the customer the possibility to conduct transactions to create offsetting transactions will not directly fall under Article 117.1 (26) of the F.I. Business Ordinance. If, in accepting an order for transactions to create offsetting transactions, an over-the-counter financial futures firm fails to suggest that "there are demerits for customers such as the fact that fees are doubled, interest differential adjustment amount between currencies (hereinafter referred to as "swap point") might turn to be negative spread, price differential between selling price and buying price (so called "spread that an over-the-counter financial futures firm receives") double the costs to the customer and such transactions lack economic rationality" and makes the statement or representation above, such act shall be an "other act similar thereto" provided in Article 117.1 (26) of the F.I. Business Ordinance.

③ Transactions with customers and covering transaction parties

Whether an over-the-counter financial futures firm makes appropriate explanation of the followings when requested by customers:

(a) the method to place an order for covering transactions;

(b) the execution standards for covering transactions;

(c) the responses when a system error has occurred with a covering transaction party.

④ Responses when market prices have moved abruptly

Whether an over-the-counter financial futures firm makes appropriate explanation of the responses when market prices have moved abruptly when requested by customers.

⑤ Internal control system for transactions for house account

Whether an over-the-counter financial futures firm makes appropriate explanation whether the firm conducts transactions for house account and, if the firm conducts such transactions,

risk control system, etc. when requested by customers.

⑥ Customer assets separation

Whether an over-the-counter financial futures firm makes appropriate explanation of the separate customer money trust provided in Article 143.1 (1) of the F.I. Business Ordinance when requested by customers.

⑦ Loss-cut transactions

Whether, in conducting currency related over-the-counter derivatives transactions, etc., the over-the-counter financial futures firm makes appropriate explanation of the fact that loss-cut transactions (which mean transactions provided in Article 123.1 (21-2) of the F.I. Business Ordinance; hereinafter the same) are facilitated and of the details thereof. The over-the-counter financial futures firm makes appropriate explanation of likelihood of incurring losses in the case where loss-cut transactions is not executed as scheduled.

⑧ Low spread transactions

Whether any of, for example, the following likelihood arises if a currency related over-the-counter derivatives, etc. firm which offers transactions with extremely low spread or fees (hereinafter referred to as "low spread transaction") makes representation to emphasize that the spread or fees are low in its advertisement, etc.

- (a) likelihood to give false impression that, despite of the fact that there are fees, remuneration or other consideration or cost payable by customers, considerations or costs payable by customers were considerably lower than actual conditions;
 - (b) likelihood that differential between rates designated by a customer at the time of placing an order and rates at which a transaction is concluded actually (slippage) arises and transactions are concluded with larger spread than spread represented by an advertisement, etc.
- (5) Remarks on obligation of explanation for securities related over-the-counter derivatives firm (4) above shall apply to remarks on explanation to customers by a securities related over-the-counter derivatives firm targeting individuals.
- (6) Remarks on obligation of explanation for over-the-counter derivatives firm which conducts currency options transactions, interest rate swap transactions, etc.

Whether, in cases where (4) and (5) are not applicable, an over-the-counter derivatives firm conducts over-the-counter derivatives transactions, for example, currency options transactions and interest rate swap transactions with the following remarks:

(Note) It shall be noted whether a financial instruments firm treats the same of complex structured debt securities or investment trust similar to over-the-counter derivatives transactions in a manner equivalent to the above.

① Whether an over-the-counter derivatives firm makes appropriate and sufficient explanation concerning the details of products and risks of such over-the-counter derivatives transactions by means such as furnishing a written statement which explains concretely and in a manner that investors understand easily including the followings;

(a) Whether an over-the-counter derivatives firm explains the assumed largest amount of loss under the worst scenario (scenario based on reasonable resumption such as data in the event of stress in the past; hereinafter the same) regarding the level, etc. of a financial instrument, etc. which is an object of such over-the-counter derivatives transactions (including the level of volatility when needed; hereinafter the same) including the possibility that the loss will expand further under the conditions different from the presumption in a manner that customers can understand.

(b) Whether an over-the-counter derivatives firm confirms that the amount of losses arising from such over-the-counter derivatives transactions is acceptable to a customer and such amount of loss does not influence on business management or financial conditions grossly, and, if there is a possibility that a customer may suffer the amount of losses exceeding the amount that a customer confirms as acceptable even in the case where the above worst scenario is not realized, explains the relationship between the conditions of the financial index, etc. and the result thereof in a manner that the customer can understand.

(c) Whether, if an over-the-counter derivatives firm uses examples, etc. different from actual over-the-counter derivatives transactions by necessity for explanation, the over-the-counter derivatives firm explains that the examples, etc. are different from actual transactions.

② Whether an over-the-counter derivatives firm makes appropriate and sufficient explanation concerning the cancellation before the maturity and the amount of cancellation settlement money of such over-the-counter derivatives transactions by means such as furnishing a written statement which explains concretely and in a manner that investors can understand easily including the followings:

- (Note) In the case of sale of structured debt securities, for example, "cancellation before the maturity" and "cancellation settlement money" shall be read as "sale before the maturity" and "assumed amount of loss as are result of sale before the maturity," respectively. It is desirable to explain with the estimate of the worst scenario as much as possible in explaining (b) below even if estimation of assumed amount of loss as a result of sale before the maturity is difficult.
- (a) Whether, if such over-the-counter derivatives transactions cannot be canceled before the maturity in principle, an over-the-counter derivatives firm explains the fact in a manner that customers can understand.
 - (b) Whether, if cancellation of the over-the-counter derivatives transactions before the maturity results in payment or receipt of cancellation settlement money, an over-the-counter derivatives firm explains the fact and the details of such cancellation settlement money (including the estimated amount of cancellation settlement money under the worst scenario for the level, etc. of a financial index, etc. and, if there is a possibility that such cancellation settlement money will exceed the estimated amount, such fact) in a manner that the customer can understand.
 - (c) Whether, if an over-the-counter derivatives firm confirms the amount of cancellation settlement money acceptable to a customer for the over-the-counter derivatives transactions and there is a possibility to suffer the amount of loss exceeding the acceptable amount even if the worst scenario above is not realized, an over-the-counter derivatives firm explains such fact in a manner that the customer can understand.
- ③ Whether, if the over-the-counter derivatives transaction is proposed for hedging purpose, an over-the-counter derivatives firm confirms whether a customer understands that the followings are necessary, and makes appropriate and sufficient explanation based on the result of the confirmation:
- (a) functioning as an effective hedging tool to carry out continuous business management considering the state of the customer's business and competition in the market. (Note 1)
 - (b) functioning as an effective hedging tool mentioned above is expected to continue until the end of the contract. (Note2)
 - (c) not causing the customer's difficulty to see the future business management. (Note 3)
- (Note 1) It shall be noted to judge comprehensively, for example, the existence, etc. of price bargaining power or pricing power to reduce the influence of the movement of foreign exchange rates or interest rates.
- (Note 2) It shall be noted that, for example, even if a hedging tool itself does not carry losses, hedging needs of a customer are influenced by a change of business conditions, etc. of the customer such as shrinkage of presumed business scale or effective functioning of hedging may not continue until the termination of the contract for such needs.
- (Note 3) It shall be noted that the stabilization of purchase price, etc. by hedging may influence on price competitiveness of the customer.
- ④ Whether an over-the-counter derivatives firm takes measures such as collecting an acknowledgment, etc. from a customer and keeping it in order to acknowledge that the explanation was made to the customer based on the matters referred to in the above ① to ③.
- ⑤ Whether, with respect to solicitation of over-the-counter derivatives transactions to a customer which is exempt from prohibition of unrequested solicitation, it is ruled that an over-the-counter derivatives firm confirms hedging needs through the trading record of the customer and solicit to enter into a contract within the scope of its needs based on the laws and regulations (Note).
- (Note) "Juridical person engaging in the foreign trade or other business regarding foreign exchange transactions" (Article 116 (2) of the F.I. Business Ordinance) which is exempt from prohibition of unrequested solicitation shall include a construction firm in Japan who imports, for example, lumber from overseas in effect through a trading firm in Japan without direct trading with an overseas exporter, but exclude the case of purchase of imported lumber from a firm in Japan.
- ⑥ Whether an over-the-counter derivatives firm provides a customer with information necessary for account settlement or judgment of cancellation, if a customer requests, periodically or when needed such as providing or giving a notice of market price information of the customer's positions or the amount of cancellation settlement money as of such time.
 - ⑦ Whether, with respect to confirmation of a customer's intention to enter into a contract for such over-the-counter derivatives transactions, implements a system to enable confirmation of intention with remarks on a decision-making process to meet the details and scale of the

contract, the business, scale, business management system, etc. of the customer.

It shall be noted that, if, for example, the over-the-counter derivatives transactions the contract of which a customer wishes to enter into will likely make big influence on the future business management of the customer, it is important to confirm whether such entering into such contract has been decided by the board of directors, etc. of the customer.

- (7) Remarks on furnishing of written statements prior to entering into contract
- ① "Reason for likeliness that a loss exceeds the principal" as provided in Article 82 (4) (b) of the F.I. Business Ordinance shall, if there is a loss-cut rule but there is likeliness that the amount of loss exceeds the amount of customer margins or other guarantee money as a result of abrupt movement of market prices, include such fact.
 - ② "Cause of termination for such financial instruments transaction contract" as provided in Article 82 (8) of the F.I. Business Ordinance shall include matters regarding loss-cut rules.
 - ③ "The types of, and computation method of the amount of, customer margins or other guarantee money which a customer is required to deposit regarding the derivatives transactions, etc." as provided in Article 93.1 (4) of the F.I. Business Ordinance shall include matters regarding minimum margins and matters regarding guarantee money required to be added in the event that the total amount of guarantee money is short from the required amount as a result of movements of market prices, etc. (hereinafter referred to as "additional margin").
 - ④ In the case of currency related transactions, "important terms and other basic matters regarding derivatives transactions" as provided in Article 93.1 (7) of the F.I. Business Ordinance shall include matters regarding methods to price financial instruments, etc. and swap points. In the case of swap points, if there are the case that a customer receives and the case that a customer pays and, as a result, there is likeliness to cause losses, the explanation to that effect shall be represented appropriately.
 - ⑤ In stating "covering transaction party" as provided in Article 94.1 (1) of the F.I. Business Ordinance, all covering transaction parties shall be stated if there is more than one covering transaction party. If, however, a participant to inter-bank foreign exchange market (so called "inter-bank market") conducts such transactions in the inter-bank market and cannot specify covering transaction parties, stating such fact shall suffice.
 - ⑥ "Places where to deposited" as provided in Article 94.1 (4) of the F.I. Business Ordinance shall contain the trustee of a customer segregation trust in the case where of securities related over-the-counter derivatives transactions or the concrete names of places where to deposit guarantee money, etc. referred to in (1) or (2) (a) to (2) (d) of Article 143.1 of F.I. Business Ordinance in the case of over-the-counter derivatives transactions, etc. other than securities related over-the-counter derivatives transactions, etc.
- (8) Remarks on furnishing of written statements for receipt of customer margins or other guarantee money
- The date of payment or the immediately following day, etc. may be used as "date on which the financial instruments firm, etc. has received guarantee money" provided in Article 114.1 (4) of the F.I. Business Ordinance based on the agreement between each firm and its customer.
- (9) Remarks on prohibition of unrequested solicitation
- With respect to solicitation of over-the-counter financial futures transactions, there are cases that a customer began transactions passively without full understanding of risks or mechanics after solicitation by means of a door-to-door call or telephoning in the past, which caused troubles and developed into social issues. Based on this, Article 38 (4) of the F.I. Act prohibits an over-the-counter derivatives firm or its officer or employee to solicit, by means of a visit or telephoning, a customer who has not requested the solicitation for entering into a contract for over-the counter derivatives transactions (limited to over-the-counter derivatives transactions with customers who are individuals in the case of transactions other than over-the-counter financial futures transactions; hereinafter in (9), the same), to enter into a contract for over-the-counter derivatives transactions (so called "unrequested solicitation").
- However, an act to solicit a customer with whom an over-the-counter derivatives firm has a continuous trading relationship to enter into a contract for over-the-counter derivatives transactions and an act to solicit a juridical person engaging in the foreign trade or other business regarding foreign exchange transactions to enter into an over-the-counter financial futures transactions contract for the purpose of reducing the risk of loss arising from the fluctuation of exchange rates related to the juridical person's assets and liabilities are excluded from prohibition under Article 116 of the F.I. Business Ordinance.
- In order to ensure the above treatment, it is important for an over-the-counter derivatives firm to implement a customer control system which enable to recognize the state of request

from customers accurately in order to ensure appropriate performance of solicitation responding to requests by customers. The authority shall supervise with the following remarks.

- ① Whether unrequested solicitation is applicable
 - (a) "An act to solicit to enter into a financial instruments transactions contract by means of a visit or telephoning" as provided in Article 38 (4) of the F.I. Act shall include an act to ask whether solicitation can be made.
 - (b) "Person having the balance of unsettled over-the-counter financial futures transactions" as provided in (1) of Article 116.1 of the F.I. Business Ordinance, "person having the balance of unsettled securities related over-the-counter derivatives transactions" as provided in (4) of said Article 116.1 and "person having unsettled over-the-counter derivatives transactions" as provided in (5) of said Article 116.1 shall include a person having an option the exercise period of which has not expired.
 - (c) If a customer who looked at an advertisement has made enquiring on general matters or requested materials on the summary of transactions with an over-the-counter derivatives firm, such enquiry or request cannot be regarded as "request for solicitation to enter into a financial instruments transactions contract."
- ② Recognition of state of requests by customers
 - (a) Whether an over-the-counter financial futures firm makes an effort to recognize the state of request by a customer and the past trading records in a timely manner by means of, for example, maintenance of customer cards. In soliciting, the over-the-counter financial futures firm ensures all officers and employees to make an effort to make appropriate solicitation according to the state of request by such customer and the past trading records.
 - (b) An over-the-counter financial futures firm shall establish concrete methods to control customer information such as the state of request by a customer and the past trading records and inform such methods to all officers and employees. With respect to customer information, particularly, whether an over-the-counter financial futures firm establishes such methods after sufficient consideration in light of secrecy obligation, etc.
 - (c) Whether an internal control division makes an effort to implement the system to ensure the effectiveness through making an effort to recognize the state of requests by customers and the past trading records and the state of the control of customer information, and verify whether appropriate solicitation is conducted when needed, and reviewing the method to control customer information.
- (10) Remarks on solicitation of complex structured debt securities or investment trust similar to over-the-counter derivatives transactions (reasonable ground suitability and standards for commencement of solicitation)

The number of troubles are increasing between a over-the-counter derivatives firm and customers, particularly individual customers, because of the problems that risks, etc. are difficult for such customers to understand for the sale of complex structured debt securities and investment trust similar to over-the-counter derivatives transactions. Based on this, It is important for a financial instruments firm which solicits individual customers such structured debt securities and investment trust to ensure appropriate solicitation based on suitability principles, etc. in light of ensuring the protection of investors. The authority shall, for example, verify with the following remarks:

- ① Whether the over-the-counter derivatives firm verifies in advance the suitability of instruments to be offered to investors (reasonable grounds suitability) based on "Rules for Investment Solicitation, Customer Control, etc. by Association Members" of the Self-regulatory Rules of the Japan Securities Dealers Association;
 - ② Whether the over-the-counter derivatives firm establishes standards for commencement of solicitation according to risk characteristics of instruments and characters of customers based on "Rules for Investment Solicitation, Customer Control, etc. by Association Members" of the Self-regulatory Rules of the Japan Securities Dealers Association, and conducts appropriate solicitation in accordance with such standards;
- (11) Supervisory method and response

With respect to the issues of the solicitation and explanatory system of an over-the-counter derivatives firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an over-the-counter derivatives firm through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the

authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-3-3-3 Discretionary trading contract, etc.

- (1) Remarks on discretionary trading contract with affiliated foreign financial futures firms, etc.
Remarks shall be made on the followings for accepting a notification to enter into a contract under Article 16.1 (8) (b) of the Definition Ordinance.
 - ① Whether the division executing transactions under such contract and an other division accepting and executing other customer orders are separated clearly.
 - ② Whether it is ruled that books and records are prepared by the method to show that such transactions are conducted under such contract.
- (2) Scope of specific consent of over-the-counter derivatives firms
Specific consent under (b) and (c) of Article 123.1 (13) of the Business Ordinance shall include a consent to:
 - ① specific price or trade value (including the price and trade value fixed by a pre-determined method) or more, or specific price or trade value or less;
 - ② price or trade value fixed with an appropriate range from a specific price or trade value as base value; and
 - ③ an over-the-counter derivatives firm which has been requested to make a best execution during one day trading determines the price or trade value at the firm's discretion.
- (3) Supervisory method and response

With respect to the issues regarding the acts listed in (a) to (e) of Article 123.1 (13) of the F.I. Business Ordinance of an over-the-counter derivatives firm found through the daily supervisory operations and notification of accident, etc., the authority shall, based on the above focus points, recognize voluntary improvement of business management of an over-the-counter derivatives firm through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-3-3-4 Risk control system related to currency related over-the-counter derivatives transactions

As, with respect to currency related over-the-counter derivatives transactions targeting individual customers (which mean currency related over-the-counter derivatives transactions as defined in Article 123.4 of the F.I. Business Ordinance; hereinafter the same), the control of risks exposed to an over-the-counter derivatives firm is important, the authority shall supervise the implementation of a risk control system and carrying out business operations with the following remarks.

- (1) Remarks on transactions with a customer and a covering transaction party
 - ① Whether, if there is a possibility of a time lag between a trade with a customer and a covering transaction, an over-the-counter derivatives firm implements a risk control system to prepare for abrupt movement of market prices during such time lag.
 - ② Whether, if an over-the-counter derivatives firm conducts covering transactions at regular time interval or for a fixed amount or by judgment of a dealer instead of conducting covering transactions each time of a transaction with a customer, the over-the-counter derivatives firm implements a risk control system, considering the time lag between the trade with a customer and the covering transaction, to prepare for abrupt movement of market prices during such time lag.
 - ③ Whether, if an over-the-counter derivatives firm conducts covering transactions after the conclusion of an order for limit order or loss-cut order for a customer account after the judgment of indication, etc. of market prices shown by an information vendor, etc., the over-the-counter derivatives firm implements a risk control system to prepare for abrupt movement of market prices during such time lag.

- ④ An over-the-counter derivatives firm shall respond to system risk involved in systematic covering transaction with remarks on system implementation under III-2-8 in principle. Whether an over-the-counter derivatives firm implements, considering that there are cases where making transactions is impossible because of system error with a covering transaction party at the time of covering transaction, a risk control system to prepare for abrupt movement of market prices during such system error prepare.
- ⑤ Whether an over-the-counter derivatives firm recognizes the details of a contract entered into with a covering transaction party fully and implements a system to enable smooth and appropriate response at the time of the occurrence of a trouble.
- (2) Remarks on transaction in the case where market prices move abruptly
Whether an over-the-counter derivatives firm establishes the policies for concrete risk control such as suspension of transactions for the house account and refusing acceptance of an order from customers in the case where transactions with a covering transaction party cannot be made, and implements a system for such cases for the preparation of the event that market prices move abruptly.
- (3) Remarks on transaction for house account
Remarks shall be made on the followings if an over-the-counter derivatives firm conducts transactions for house account other than transactions to cover customer transactions.
- ① Whether the over-the-counter derivatives firm implements internal rules for position limit, stop loss limit (daily and monthly), over-night position limit, etc. in respect of a person in charge of transactions for house account.
- ② Whether the over-the-counter derivatives firm sets soft limit and hard limit to prevent making a false order regarding an order placement for transactions conducted by a person in charge for transactions for house account.
- ③ Whether the over-the-counter derivatives firm implements a system to monitor all the time in the back office concerning compliance with internal rules for transactions conducted by a person in charge.
- (4) Remarks on loss-cut transactions
- ① Whether an over-the-counter derivatives firm sets a level to execute loss-cut transactions considering price movement risk or liquidity risk, etc. in order to prevent a customer's suffering the amount of losses exceeding the amount of margins deposited by the customer.
- ② Whether an over-the-counter derivatives firm makes internal rules, etc. providing the agreements regarding loss-cut transactions clearly and reflects the internal rules, etc. to contracts with customers.
- ③ Whether an over-the-counter derivatives firm recognizes positions of each customer as of each time point during the trading hour appropriately and executes loss-cut transactions without exception when the level referred to in ① has been touched.
- ④ Whether an over-the-counter derivatives firm reports to the board of directors, etc. of the state of execution of loss-cut transactions periodically and when needed.
- (5) Remarks on low spread transactions
A currency related over-the-counter derivatives firm which offers low spread transactions services may worsen financial conditions unless the firm maintains considerable trading volume. On the other hand, such firm needs to implement a system to control trading volume sufficient to ensure the stability of business management appropriately.
Whether a currency related over-the-counter derivatives firm implements the sufficient risk control system including the following points.
- ① Whether, in implementing a company-wide risk control system (for example, establishing risk control policies, etc.), the currency related over-the-counter derivatives firm recognizes risks associated with low spread transactions fully and reflects such risks appropriately.
- ② Whether, in commencing the services of low spread transactions, the currency related over-the-counter derivatives firm decides spreads or fees after considering whether sufficient profitability is ensured in light of the earnings structure and trading volume. Whether a currency related over-the-counter derivatives firm verifies the decision periodically and reviews it when needed based on a change, etc. to earnings structure and trading volume of the firm. Whether a currency related over-the-counter derivatives firm clarifies such procedures by its internal rules, etc.
- ③ Whether a currency related over-the-counter derivatives firm which offers low spread transactions services recognizes influence, etc. on trading volume of such transactions, the details of the transactions and its financial conditions of the firm, and implements a system to report to the board of directors timely and appropriately.

- ④ Whether a currency related over-the-counter derivatives firm which offers low spread transactions services implements a hard and soft system and other system sufficiently necessary for achievement of assumed earnings structure. Whether such firm verifies the actual earnings conditions periodically and reviews such system appropriately.
- (6) Supervisory method and response
 - ① The authority shall recognize the details of products or transactions (such as spread and fees) offered by a currency related over-the-counter derivatives firm through hearings, etc. in order to confirm the appropriateness of the risk control system of the currency related over-the-counter derivatives firm.
 - ② With respect to the issues regarding the risk control system of a currency related over-the-counter derivatives firm found through the daily supervisory operations and notification of accident, etc., the authority shall recognize voluntary improvement of business management of a currency related over-the-counter derivatives firm through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

IV-3-3-5 Risk control system related to securities related over-the-counter derivatives transactions

IV-3-3-4 shall apply to the implementation of a risk control system and carrying out of business management related to securities related over-the-counter derivatives transactions targeting individual customers.

IV-3-4 Remarks on supervision over firms which are not members of association, etc.

- (1) Main focus points
 - ① Whether a financial instruments firm which is not a member of a financial instruments firms association or a member or trading participant of a financial instruments exchange (hereinafter in IV-3-4, referred to as "firm which is not a member of an association, etc.") implements internal rules appropriately taking the articles of incorporation or other rules of a financial instruments firms association or a financial instruments exchange (hereinafter referred to as "association, etc. rules") into consideration.
 - ② A firm which is not a member of an association, etc. implements a system to ensure appropriate compliance with internal rules (such as informing all officers and employees or verification of their compliance with internal rules).
 - ③ Whether it is ruled that, when there has been an amendment, etc. to association, etc. rules, a firm which is not a member of an association, etc. reviews the internal rules immediately after, and according to, the amendment, etc.
- (2) Supervisory method and response
 - ① If a firm which is not a member of an association, etc. fails to prepare, and is not expected to prepare voluntarily, internal rules for which association, etc. rules have been taken into consideration, the authority shall order the firm to prepare appropriate internal rules under Article 56-4.2 of the F.I. Act. In this case, the authority shall, when there has been an amendment, etc. to association, etc. rules, require the firm to review the internal rules immediately after, and according to, the amendment, etc.
 - ② If reviewing internal rules of a firm which is not a member of an association, etc. is required in light of association, etc. rules and the firm is not expected to review voluntarily, the authority shall order the firm to make an amendment to internal rules under Article 56-4.2 of the F.I. Act.
 - ③ If it is determined that there is a problem for the preparation of, amendment to and compliance with internal rules of a firm which is not a member of an association, etc., the authority shall make an effort to recognize the real state through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act. Further, the authority shall make appropriate supervision considering association, etc. rules under Article 56-4.1 of the F.I. Act such as the issuance of an order to improve business management under Article 51 of the F.I. Act and the issuance of an order to suspend business under Article 52.1 of the F.I. Act when

needed.

IV-4 Procedures (first-type financial instruments business)

IV-4-1 Registration

(1) Trade name

A local finance bureau which has accepted the application shall refer to the Financial Services Agency or other local finance bureau when needed in order to confirm that the trade name stated in the application does not violate Article 29-4.1 (6) (b) of the F.I. Act.

(2) Items of examination of system

In examining whether the applicant is a corporation having personnel resources insufficient to carry out financial instruments business properly as provided in Article 29-4.1 (1) (d) of the F.I. Act, the authority shall refer to the application for registration and the attachments and hold a hearing to confirm the followings.

① Whether it is determined that the applicant ensures the employment of officers and employees having sufficient knowledge and experience of the proposed business and the system of organization to carry out such business appropriately in light of the followings:

- (a) the management is qualified to carry out the business in a fair and accurate manner as a financial instruments firm in light of the career, ability, etc.;
- (b) a full-time officer understands, and has knowledge and experience sufficient to perform, focus points of business management provided by relevant various regulations such as the F.I. Act and the Supervisory Guidelines, and has sufficient knowledge and experience of compliance and risk control necessary for fair and accurate carrying out the financial instruments business;
- (c) there is more than one person with at least three years experience of the proposed first-type financial instruments business among full-time officers and full-time employees;
- (d) organization and personnel structure that personnel necessary for carrying out proposed business accurately is allocated to each division, and a person responsible for internal control, etc. is allocated properly (particularly in carrying out primary underwriting business, ensuring the system and personnel that enable to carry out such business in a fair and accurate manner);
- (e) whether a compliance division (person) independent from sales divisions is established and a person having knowledge and experience is appointed as a person in charge; and
- (f) personnel required for the following system implementations is ensured for the proposed business:
 - a. preparation and control of books and records, reports, etc.;
 - b. disclosure;
 - c. segregation of customer properties;
 - d. risk control;
 - e. computer system control;
 - f. trade control, customer control;
 - g. examination of advertisement;
 - h. customer information control;
 - i. settlement of grievances and troubles; and
 - j. internal audit.

② Whether the applicant has a person with inappropriate qualification for business management among officers and employees as a result of comprehensive consideration of the following matters as a relationship with a crime group or a member of a crime group or other circumstances, which will likely result in the downfall of the credit of financial instruments business.

- (a) the applicant is a member of a crime group (including a person who was a member of a crime group in the past);
- (b) the applicant has a close relationship with a crime group;
- (c) the applicant has an experience of the violation of the laws or regulations for finance in Japan such as the F.I. Act or the laws or regulations in a foreign jurisdiction analogous thereto and being fined (including a criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto);
- (d) the violation of the provisions of the Law on Prevention of Improper Act by Member of Crime Group (excluding the provisions of Article 32-2.7 of said Law) or the provisions of the

- laws or regulations in a foreign jurisdiction analogous thereto, or commitment of crimes under the Criminal Code or the Law on Violence, etc. Punishment and being fined (including a criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto);
- (e) the applicant has an experience of being punished by a criminal penalty of imprisonment or severer (including criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto) (particularly, the case of crimes under Articles 246 to 250 of the Criminal Code (fraudulence, fraudulence using a computer, breach of trust, quasi-fraudulence, threat, attempted crime) shall be noted).;
- (Note) It shall be noted that the case where it is determined that, as a result of comprehensive consideration of the matters, etc. referred to in (a) to (e) of ② in respect of a major shareholder of a financial instruments firm, inappropriate exercise of influencing power held by the major shareholder will likely result in the downfall of the credit of financial instruments business may be determined that such financial instruments firm "have personnel resources insufficient to carry out financial instruments business accurately."
- (3) Documents stating the type of business and manner of operations
In the case of handling currency related over-the-counter derivatives transactions and securities related over-the-counter derivatives transactions targeting individuals, the authority shall confirm that documents stating the type of business and manner of operations states the fact in the place to state the types of derivatives transactions conducted as a business.
- (4) Entry of approved matters in financial instruments firms registry book
An entry that an approval has been made under Article 30.1 of the F.I. Act shall be made for the place of approved matters in a financial instruments firms registry book. When the Agency grants an approval to a financial instruments firm, etc. under the direct jurisdiction of the Agency, the Agency shall notify the local finance bureau which has registered the financial instruments firm in a lot each month no later than 15th of the following month.
- (5) Remarks on firms which have no plan to become a member of a financial instruments firms association or to become a member or trading participant of a financial instruments exchange
The authority shall give the following notices to a firm which has no plan to become a member of a financial instruments firms association or to become a member or trading participant of a financial instruments exchange at the time of filing an application for registration and require such firm to make appropriate responses.
- ① If it is determined that there is no appropriate internal rules for which association, etc. rules have been taken into consideration, such firm shall be ordered to prepare internal rules immediately after the registration in principle.
- ② There is a case that a firm which is not a member of an association, etc. is ordered to amend internal rules taking association, etc. rules into consideration.
- ③ A firm which is not a member of an association, etc. shall, when ordered to prepare or amend internal rules, prepare or amend such internal rules within 30 days and obtain an approval from the Prime Minister.
- ④ A firm which is not a member of an association, etc. shall, when it wishes to amend or abolish internal rules approved under ③, obtain an approval from the Prime Minister.
- ⑤ It is ruled that the authority shall make an appropriate supervision over business of a firm which is not a member of an association, etc. considering association, etc. rules not to harm public interests or constitute a failure of the protection of investors.
- (6) Remarks on application for new registration
The authority shall require a firm applying for new registration to file in principle the following documents and confirm whether such firm is subject to refusal criteria, etc.
The original certificate shall be used for the certificate of the balance of deposit, etc. issued by a financial institution among evidences.
- ① Written evidences computing the amount of net assets (which means the amount of net assets provided in Article 29-4.1 (5) (b) of the F.I. Act).
- ② Written evidences computing the ratio provided in Article 29-4.1 (6) (a) of the F.I. Act.
- ③ Written evidences computing the amount of net assets and the capital requirement ratio for the latest month.
- ④ In the case of a firm wishing to conduct currency related derivatives transactions, etc. (which means currency related derivatives transactions provided in Article 143.3 of the F.I. Business Ordinance) as a business, a copy of a trust contract for a trust account established with a trust company or a financial institution operating trust business for the purpose of separate control of money or a written statement equivalent thereto.

IV-4-2 Approval and notification, etc.

IV-4-2-1 Approval

Proprietary Trading System (PTS) has a function similar to an exchange, and business operating a PTS is kept subject to an approval under the F.I. Act, continuously from the Old Securities and Exchange Law. In approving the business provided in Article 2.8 (10) of the F.I. Act, based on such fact, the authority shall consider based on the following remarks

- ① Remarks shall be made on the followings when the authority judges whether the system is PTS or not.
 - (a) A system which provides services to act as a broker for purchase or sale of securities on an on-exchange financial instruments market or over-the-counter traded securities market or provides services to act as a broker for purchase or sale of securities to an other single financial instruments firm shall not be a proprietary trading system or on-exchange financial instruments market, etc.;
 - (Note) For example, proprietary trading system or on-exchange financial instruments market, etc. shall not apply in principle to a system to make broking of the same amount volume of a purchase order and sale order of two customers simultaneously to an on-exchange financial instruments market conducting transactions by means other than auction. On the other hand, there is a possibility that proprietary trading system or on-exchange financial instruments market, etc. applies to a system to make broking of a customer order to an on-exchange financial instruments market conducting transactions by means other than auction in the case where concentration or setoff is made in the system.
 - (b) A system to conduct transactions of securities with a customer for which the system acts as a counterparty may be a proprietary trading system or on-exchange financial instruments market, etc. if such system concludes purchase or sale based on quotations which summarize the demand and supply of securities by a large number of orders;
 - (c) A financial instruments firm or information vendor providing stock prices or financial information shall be deemed to engage in financial instruments business (intermediary) and shall obtain an approval for PTS business together if such firm or vendor provides methods to agree trading conditions such as viewing indications quoted by multiple financial instruments firms, etc. (competition of indications), distribution of exclusive information terminals or providing a link, etc. for placing an order or a negotiation.
- ② Remarks shall be made on the followings when the authority approves such business.
 - (a) Internal control

Whether the followings are arranged for the system of internal control for such business.

 - a. a person responsible to control such business shall have in principle at least 5 years experience of securities related business and a division carrying out such business has an organization, or has personnel resources, necessary to carry out such business;
 - b. the method to identify customers is established for such business;
 - c. the method and system to, without handling margin transactions, clear off purchase or sale, etc. harming fair trading such as insider transactions, manipulation, artificial price formation, short selling violating short selling regulations if it is made on an on-exchange financial instruments market, shall be established. Such method and system are stated in the type of business and manner of operations as "important matters to ensure fairness of trading" as provided in Article 17 (12) of the F.I. Business Ordinance
 - d. in the case of handling securities intended to be placed with specific investors in such business, the method and system to prohibit transactions restricted under Article 40-4 of the F.I Act shall be established. In this case, such matters are stated in the type of business and manner of operations subject to an approval as "criteria for commencement of trading with a customer and method to control such customer" as provided in Article 17 (5) of the F.I. Business Ordinance.
 - e. internal rules shall be implemented for such business in accordance with the laws and regulations and various rules such as the F.I. Act.
 - (b) Explanatory obligation, etc. to customers

Whether, in making explanation related to such business to a customer, the PTS implements the system to enable prior explanation fully concerning the following matters.

 - a. the method to determine a trading price;
 - b. rules for trading which begins from placing an order, conclusion of trade and ending by settlement;

- c. handling in the event of default;
 - d. possibility of conclusion at the price quoted.
 - (c) Ensuring security and certainty such as system capacity
 - Whether the following matters are arranged concerning the security and certainty such as system capacity for such business.
 - a. reasonable assumption of orders in the future, the number of trades, etc. and ensuring system capacity to meet such assumptions;
 - b. sufficient testing based on the above assumption;
 - c. implementation of method and system of supervision to prevent, and to find at an early stage, the occurrence of the excess, error, etc. of system capacity;
 - d. implementation of method, and system, to encounter (explanation to. and method, etc. to communicate with, customers) the occurrence of extraordinary situation of the system;
 - e. a back up is arranged for system;
 - f. security and certainty such as system capacity has been confirmed by valuation by a third party (external organization) concerning the above matters.
 - (d) Preventive measures for secrecy maintenance of trading information
 - Whether sufficient measures are taken including the following matters in respect of the secrecy of trading information of customers related to such business.
 - a. a person engaging in such business division is clearly separated from a person in other division;
 - b. it is prohibited that a person engaging in such business uses information regarding other business to carry out such business, or a person engaging in other business uses information regarding such business to carry out other business;
 - c. measures to prevent leakage of trading information of customers are taken accurately;
 - d. internal rules are implemented for the above measures.
- ③ In granting an approval for such business, the authority shall impose the following conditions.
- (a) Publication of price information, etc. (limited to the case where such business is carried out for share certificates, etc. (which means securities provided in the items of Article 14 of the Cabinet Office Ordinance on Financial Instruments Firms Association, etc.))
 - "The best indicative prices, trading prices, etc. on such proprietary trading system shall be published in the form comparable to other proprietary trading system by the method accessible freely from outside in real time.
 - Before arranging the publication in the form comparable to other proprietary trading system, however, publication shall be made by the method accessible freely from outside."
 - (b) Volume standard for trading volume
 - The trading volume on a proprietary trading system shall be used for the volume standard for trading volume. It shall be noted not to violate the volume standard for values computed from the trading volume on a proprietary trading system network (which means a proprietary trading system and, in the case where an order placed on a proprietary trading system can be concluded with an order placed on an other proprietary trading system using an electronic data processing and network system, a network composed of such other proprietary trading system) to which the first-mentioned proprietary trading system belongs.
 - a. the case where a proprietary trading system business which determine prices by means other than auction trades share certificates or corporate debt securities with warrants (limited to those listed on a financial instruments exchange or registered under Article 67-11.1 of the F.I. Act);
 - "1 If the ratio of daily average trade value of share certificates and corporate debt securities with warrants (limited to those listed on a financial instruments exchange and those registered under Article 67-11.1 of the F.I. Act) to the total value of trade value on all on-exchange financial instruments markets and all over-the-counter traded securities markets during the past six months has become 10% or more of any of individual issue and 5% or more in respect of all of such share certificates and corporate debt securities with warrants, the following measures shall be taken.
 - (a) A system of trading control and examination (organization and personnel) shall be enhanced and implemented in order to ensure fairness of trading.
 - (b) A system similar to a default loss reserve system of a financial instruments exchange shall be implemented in order to ensure certainty of performance of settlement.
 - (c) A system shall be checked fully and periodically in order to ensure security and certainty of system capacity.

- 2 If such ratio has reached 20% in respect of any of individual issue and 10% for all of such share certificates and corporate debt securities with warrants during the past six months, the proprietary trading system shall obtain a license to open and operate a financial instruments market.
- 3 In response to the increase of trading volume, etc., new standards may be established, if necessary in the public interest or to protect investors, to such necessity."
 - b. other cases

"In response to the increase of trading volume, etc., new standards shall be established, if necessary in the public interest or to protect investors, to such necessity."
 - (c) Report of trading volume
 - a. The case of a proprietary trading system which makes price determination by means of auction

"A financial instruments firm shall make a report of the ratio, etc. provided in (1) or (2) of Article 1-10 of the F.I. Act Enforcement Order as of the end of each month to the Commissioner of the Financial Services Agency or the director-general of a local finance bureau having the jurisdiction over such financial instruments firm no later than 20th of the immediately following month."

(Note) Reporting of "total trading volume" on a proprietary trading system provided in (1) and (2) of Article 1-10 of the F.I. Act Enforcement Order shall be made for values computed under the proviso to the above "(b) Volume standard for trading volume", too.
 - b. The case of a proprietary trading system which makes price determination by means other than auction

"A financial instruments firm shall make a report of the ratio, etc. provided in (b) a. 1. and (b) a. 2. as of the end of each month to the Commissioner of the Financial Services Agency or the director-general of a local finance bureau having the jurisdiction over such financial instruments firm no later than 20th of the immediately following month."
 - (d) "New conditions may be imposed, if necessary in the public interests or to protect investors, to such necessity".
- ④ Remarks shall be made on the followings for the supervisory responses after the approval of such business.
 - (a) The authority shall confirm the sufficiency level to meet conditions for the approval by a report, etc. of trading volume.
 - (b) The authority shall confirm the performance of various measures examined at the time of the approval by collection of report, etc. when needed.
 - (c) If a proprietary trading system wishes to make a change in the manner of operations, etc. such as method of price determination of trade price, delivery or other method of settlement after the approval, the authority shall require to file an application for an approval of the change promptly.

IV-4-2-2 Approval

Remarks shall be made on the followings when the authority approves other business engagement under Article 35.4 of the F.I. Act.

- (1) Whether the engagement in such business does not violate the relevant laws or regulations.
- (2) Whether it is ruled that the computation method of risk equivalent amounts for such business is deemed to be reasonable and the risk equivalent amounts computed shall be reflected properly to the capital requirement ratio of the financial instruments firm applying for the approval.
- (3) Whether the division computing and controlling risk equivalent amounts for such business is independent from sales divisions.
- (4) Whether the financial instruments firm implements concrete measures necessary for the protection of investors. in entering into such contract, etc. in respect of business involving entering into contracts, etc. with customers.
- (5) The financial instruments firm implements internal rules for such business.
- (6) The capital requirement ratio of the applying financial instruments firm is at least 140%.

IV-4-2-3 Notification

Remarks shall be made on the followings for accepting or dealing various notifications provided by the F.I. Act. The authority shall, particularly, accept a notification of business provided in Article 35.2 of the F.I. Act with the remarks whether procedures necessary under the laws or regulations for such business have been taken, and, with respect to the following businesses, whether the followings are consistent with the types, manners, etc. of the following businesses. For this purpose, furnishing of a written statement and procedures in writing in respect of matters required to be contained shall be made by means using an electronic data processing and network system or other method using information technology in lieu of furnishing, etc. of such written statement after obtaining an approval from a customer. The authority shall require to apply for an approval pursuant to Article 35.4 of the F.I. Act for a business inconsistent therewith.

(1) Business of purchase or sale of gold bullion or acting as an intermediary, broker or agent therefor

① Products

Whether the product is gold bullion or gold coins which have high purity and high liquidity the market of which is globally established.

② Purchase of stock

Whether, in entering into a contract with a supplier, it is ruled that the contract provides that

① the financial instruments firm does not keep stock in principle and ② the supplier will accept the request for repurchase of the actuals bought as stock, and the financial instruments firm or its affiliate, etc. will not own excessive stock. A contract entered into with a supplier on sale and repurchase of gold bullion, with the provisions that such gold bullion will be bought-back for the consideration of the amount provided by such contract (hereinafter referred to as "forward transaction") provides that the performance of forward agreement is secured.

③ Business with customers

(a) Sales methods

Whether the followings are complied in respect of sales methods.

a. the financial instruments firm limits the sale to actuals and does not handle futures transactions;

b. the financial instruments firm shall make a sale by the method of cumulative investment in an appropriate manner such as furnishing a written statement clarifying the mechanics in advance to customers and making full explanation;

(b) Solicitation

An investor should invest in gold by the investor's judgment and responsibility, and whether the financial instruments firm complies with the followings in the solicitation.

a. the financial instruments firm shall not solicit by providing definitive judgment regarding the movement of the gold price;

b. the financial instruments firm shall make appropriate investment solicitation suitable to an investor's intent, knowledge and experience of gold investment and the amount and the nature of investment funds;

c. the financial instruments firm shall not agree to compensate losses or provide special profit in soliciting investment;

d. the financial instruments firm shall not solicit frequent purchase or sale for a short period (including purchase or sale to switch between securities and gold);

e. the financial instruments firm shall not conduct purchase or sale for a customer's account for which the customer gives the financial instruments firm discretion for the distinction of purchase or sale, volume and determination of prices;

(c) Furnishing customers with certificates, etc.

Whether the followings are complied for furnishing a customer with a certificate, etc.

a. Furnishing a safe custody certificate, etc.

A financial instruments firm shall furnish a customer with certificates, etc. necessary to clarify rights and obligations with the customer or to smoothen transactions such as a safe custody certificate (limited to the case of safe custody transactions), delivery account statement and repurchase demanding statement (in the case of actuals delivery transaction, documents attached to actuals to clarify that the financial instruments firm accepts buy-back of actuals) according to respective case of safe custody transactions or actuals delivery transactions.

With respect to forward transactions, however, furnishing of a safe custody certificate may be replaced with furnishing of an account statement if such account statement is furnished for each of deliveries in respect of the details of purchase or sale and the deposit

balance. Furnishing of a safe custody certificate and delivery account statement may be omitted if a notice stating the history of purchase of gold bullion and the balance of safe custody is furnished at least once per six months in respect of transactions to sell a fixed amount of gold bullion to a customer periodically by means provided by a contract in advance (hereinafter referred to as "gold bullion cumulative investment").

b. Furnishing of gold bullion transactions agreement

A financial instruments firm shall furnish a customer with a gold bullion transaction agreement clarifying matters, etc. related to rights and obligations with customers at the time of the commencement of transactions and at the time of making a change to such agreement in order to prevent accidents arising from gold bullion transactions and to protect investors in both cases of safe custody transactions and actuals delivery transactions.

(d) Determination, etc. of prices

Whether the followings are complied in determining prices, etc.

a. The price of purchase or sale shall be denominated in Yen and shall be determined appropriately in consideration of trading prices on domestic and overseas markets, foreign exchange rates, etc. The price of purchase from a supplier for forward transactions shall be the current market price and resale price and the price of purchase or sale with a customer shall be computed based thereon.

b. A financial instruments firm shall post the prices of purchase or sale at all offices handling such transactions each trading day and conclude transactions at such prices and shall not accept an advance order or a market order.

④ Safe custody

Whether the followings are complied in respect of custody.

(a) A financial instruments firm shall not assign or pledge a deposit certificate issued based on the deposit of actuals such as a safe custody certificate, exchange ticket for actuals and receipt of actuals.

(b) When a financial instruments firm which handles actuals conducts safe custody transactions, the financial instruments firm shall secure actuals for the amount corresponding to the amount for deposit business and keep it in safe custody.

(c) A financial instruments firm shall give a notice of the balance of safe custody to a customer by a reconciliation notice at least once per year.

⑤ Buying back

Whether, if a customer has demanded a financial instruments firm to buy back gold bullion sold by the financial instruments firm (including the case of a safe custody certificate), the financial instruments firm buys it back at a reception desk of its business office in principle.

⑥ Agent business, etc.

Whether a financial instruments firm limits the agent business or intermediary business for an order of purchase or sale of gold bullion (hereinafter referred to as "agent business, etc.") to agent business, etc. for forward transactions and gold bullion cumulative investment conducted in the following manners.

(a) Agent business, etc. for an order of forward transactions

a. The scope of agent business, etc. related to forward transactions shall be to act as a broker for an order of a customer to be placed with an offering financial instruments firm or a gold wholesaler (hereinafter referred to as "offering financial instruments firm, etc.") and carry out the whole or part of business related to forward transactions between the customer and the offering financial instruments firm, etc. on behalf of the offering financial instruments firm, etc. A financial instruments firm carrying out agent business, etc. for forward transactions shall enter into a contract for such agent business, etc. with the offering financial instruments firm, etc.

b. A financial instruments firm carrying out the business shall comply with the followings:

i) A financial instruments firm carrying out agent business, etc. for forward transactions shall explain to a customer fully that the forward transactions for which an order is placed are conducted with an offering financial instruments firm, etc., and obtain a consent from the customer in advance.

ii) A financial instruments firm carrying out agent business, etc. shall reconcile the details of the customer's transactions with the offering financial instruments firm, etc. periodically.

(b) Agent business, etc. for an order of gold bullion cumulative investment

a. The scope of agent business, etc. for gold bullion cumulative investment shall be to act as a broker for an order of a customer to be placed with an offering financial instruments

firm, etc. and carry out the whole or part of business for gold bullion cumulative investment between the customer and the offering financial instruments firm, etc. on behalf of the offering financial instruments firm, etc. A financial instruments firm carrying out agent business, etc. for gold bullion cumulative investment shall enter into a contract for such agent business, etc. with the offering financial instruments firm, etc.

- b. A financial instruments firm carrying out the business shall comply with the followings:
 - i) A financial instruments firm carrying out agent business, etc. for gold bullion cumulative investment shall explain to a customer fully that the gold bullion cumulative investment for which an order is placed are conducted with an offering financial instruments firm, etc. and obtain a consent from the customer in advance.
 - ii) A financial instruments firm carrying out agent business, etc. shall reconcile the details of the customer's transactions with the offering financial instruments firm, etc. periodically.
- (2) Entering into an association contract as defined in Article 667 of the Civil Code or business related to acting as an intermediary, broker or agent therefor and business related to acting as an intermediary, broker or agent for entering into a contract of undisclosed association as defined in Article 535 of the Commercial Code (excluding businesses to perform the act referred to in Article 2.8 (9) of the F.I. Act).

Whether a financial instruments firm or an officer or employee of a financial instruments firm explains to a customer fully concerning the contract in soliciting a customer to enter into a contract of association and makes appropriate solicitation suitable to the customer's intention, knowledge and experience of such association and financial resources and the nature of the funds to be invested. Whether the financial instruments firm or an officer or employee of a financial instruments firm prepares a written statement explaining the details of the contract and furnish a customer with it before entering into the contract.

- (3) Entering into a loan participation contract or business related to acting as an intermediary, broker or agent therefor
 - ① Products
A loan participation contract shall mean a product assumed by "accounting and presentation of loan participation" published by Japan Certified Public Accountant Association on June 1, 1995.
 - ② Management, etc. of business
Whether business is managed in compliance with the followings.
 - (a) paying due attention to the protection of original debtor and assignee in carrying out the business;
 - (b) full explanation to an assignee of the nature, details, etc. of the claims, etc.;
 - (c) implementation of valuation system of claims, etc. and appropriate formation of prices;
 - (d) appropriate solicitation in light of the intention, experience and financial resources of an assignee;
 - (e) preparation of a written statement for the details of a contract and furnishing an assignee with such written statement before entering into a contract.

IV-4-2-4 Remarks on cumulative investment business

The authority shall verify the business to enter into a cumulative investment contract as defined in Article 35.1 (7) of the F.I. Act with the following remarks.

- (1) Types of securities used for cumulative investment business
 - ① national government bonds;
 - ② local government bonds;
 - ③ bank debenture or debt securities issued by a juridical person under special laws;
 - ④ corporate debt securities which are deemed to be issued for certain amount periodically such as corporate debt securities, etc. issued by electric utility companies;
 - ⑤ Investment trust beneficial certificates (excluding listed investment trust beneficial certificates; in IV-4-2-4, the same);
 - (a) unit trust investment trust;
 - (b) open-end type investment trust (excluding public or corporate debt securities investment trust; in IV-4-2-4, the same);
 - (c) public or corporate debt securities investment trust;
 - ⑥ foreign investment trust beneficial certificates;

- ⑦ investment certificate of an investment corporation (excluding listed investment certificates; in IV-4-2-4, the same);
 - ⑧ foreign investment certificate;
 - ⑨ share certificates (limited to share certificates listed on a financial instruments exchange or share certificates registered on an over-the-counter traded securities registry kept by the Japan Securities Dealers Association which are subject to (10); in IV-4-2-4, the same);
 - ⑩ listed investment trust beneficial certificate (limited to those subject to (11); in IV-4-2-4, the same);
 - ⑪ listed investment certificates (limited to those subject to (12); in IV-4-2-4, the same).
- (2) Methods to buy securities for cumulative investment business
- ① Only securities newly issued shall be bought (this does not apply to share certificates, listed investment trust beneficial certificate and listed investment certificate), and types and methods to use money deposited for purchase shall be provided in a contract for in advance. *Provided*, That, in the case where there is no new issue for the period of purchase scheduled by a contract or otherwise newly issued securities are not available for purchase, the same type of already issued securities may be bought in a manner provided by a contract.
 - ② When the amount of money paid by a customer or money deposited with a financial instruments firm born based on receipt of fruit or redemption of securities deposited by a customer (hereinafter such securities are referred to as "deposited securities" and such money deposited is referred to as "money paid, etc.") has reached the value of purchase of securities to be bought by the customer (or its integral multiple), the financial instruments firm shall buy such securities without delay: *Provided*, That a customer may any time instruct the financial instruments firm to stop the purchase of securities.
 - ③ The value of purchase of securities shall be defined as follows:
 - (a) in the case of national government bonds, local government bonds, bank debentures or debt securities issued by a juridical person under special laws and corporate debt securities, the value of public offering or public sale: *Provided*, That, in the case where the proviso to ① is applicable, market value on a financial instruments exchange designated by a contract in advance or other appropriate value;
 - (b) in the case of the following investment trust beneficial certificates, the following value:
 - a. unit type investment trust — offering value;
 - b. open-end type investment trust — base price as of the day immediately preceding the day of purchase (in the case of an open-end type investment trust which collects trust assets reservation value at the time of purchase, the total amount of such trust assets reservation value and base value);
 - c. open-end type public and corporate debt securities investment trust — base value as of the day of purchase or the day immediately preceding the day of purchase;
 - (c) in the case of foreign investment trust beneficial certificates, base value as of the day immediately preceding the day of purchase;
 - (d) in the case of an investment certificate or foreign investment certificate, the value provided in a contract or a written statement equivalent thereto;
 - (e) in the case of share certificates, the market value on the financial instruments exchange designated by a contract in advance (if there is more than one trade price on the exchange for such issue name, the weighted average thereof);
 - (f) in the case of listed investment trust beneficial certificate, the market value on a financial instruments exchange designated by a contract in advance (if there is more than one trade price on an exchange for such issue name, the weighted average thereof);
 - (g) in the case of a listed investment certificate, the market value on the financial instruments exchange designated by a contract in advance (if there is more than one trade price on an exchange for such issue name, the weighted average thereof);
- (3) Methods to pay money and to control money on deposit for cumulative investment business
- ① A customer may pay the whole or part of consideration for purchase of securities any time: *Provided*, That other methods shall apply to (8) to (12).
 - ② Money paid, etc. paid by a customer shall be accounted separately as cumulative investment money on deposit and fruit from such money on deposit such as interest, etc. shall not be paid to a customer.
- (4) Timing of transfer and assignment of ownership of securities for cumulative investment business
- In the case of joint purchase, the joint holding shall terminate when the code or number of securities purchased has been fixed for such customer, and the ownership of such securities

- shall be transferred to the customer. The claim for which the customer is entitled in respect of fruit or principle of such securities shall take effect as from the day of such purchase.
- (5) Method of safe custody of securities for cumulative investment business
- ① Securities bought in the course of cumulative investment business shall be kept in custody in the following manners:
 - (a) the balance, new deposit and redemption of securities based on cumulative investment business shall be segregated from other securities; in this case, securities held by a financial instruments firm and its customer jointly shall be further segregated;
 - (b) Securities may be redeposited with a securities finance company, bank or trust company in the name of a financial instruments firm in lieu of keeping such securities by itself; a financial instrument firm may deposit or redeposit the securities in the form of a large amount denominated certificate after obtaining a consent from a customer if the financial instruments firm determines that it will not harm the right or interests of the customer;
 - (c) A contract may provide that, if deposited securities are returned in response to a customer's request, the return of such securities may be made by the return of proceeds from the sale of the securities at the market price (including predetermined fee) in lieu of the return of securities.
 - ② Securities bought without relying on a cumulated investment contract may be kept in custody as securities under a cumulated investment contract if a customer so requests; *provided*, that such securities shall be limited to the same type of securities to be bought under such cumulative investment contract.
- (6) Cancellation of a contract for cumulative investment business
- ① A contract shall be cancelled when a customer requests. A customer may request such cancellation any time.
 - ② A contract shall be cancelled when a customer fails to pay the whole or part of consideration for purchase of securities for more than one year continuously. *Provided*, That this shall not apply, if a customer deposits securities with a financial instruments firm under a cumulative investment contract and a customer may buy securities within one year from the previous purchase for the considerations of only money deposited which are fruit or redemption of such securities, to such contract and a contract provided in the below (7).
 - ③ A contract shall be cancelled if a financial instruments firm cannot continue the cumulative investment business.
 - ④ In addition to the above, a financial instruments firm may cancel a contract if a customer fails to make the whole or part of the payment of the considerations of purchase for more than three months continuously; *provided*, that this shall not apply if there is a contract provided in the proviso to ② above (excluding the case where all of the conditions under the following (a) to (d)) are not.
 - (a) A report, etc. to a customer is returned because the new address is unknown.
 - (b) The whereabouts of the customer is unknown despite of an effort of confirming it.
 - (c) There is no payment of the considerations for purchase, or sale, for more than one year after the return of a report, etc. under the above (a).
 - (d) There is a small amount of the balance (less than ¥10,000).
- (7) A financial instruments firm may enter into a contract to return a part of deposited securities and the whole or part of fruit or redemption of such securities periodically if a customer so requests.
- (8) Joint purchase cumulative investment business of national government bonds may be carried out as follows.
- ① A financial instruments firm shall, with respect to national government bonds, enter into a contract that the financial instruments firm buys such national governments bonds for cumulative investment business with a customer who offers purchase jointly with other customers. In this case, notwithstanding (3) ①, the amount of money less than the minimum amount of payment for the money paid, etc. for second payment or after may be accepted, and if the total amount of money paid, etc. from one customer and the money paid, etc. from other customers reaches the purchase value (or its integral multiple), the financial instruments firm shall buy such national government bonds without delay.
 - ② In the case of the above ①, if there is an amount less than the purchase value of national government bonds for the total amount of money paid, etc. from customers, the financial instruments firm shall pay the difference between the minimum unit of purchase value and such amount, and buy jointly with customers.
 - ③ Each of customers who bought jointly (including, in the case of the above ②, a financial

- instruments firm) shall acquire (jointly) the right of a shared ownership in proportion of respective share.
- ④ A financial instruments firm shall open an account for each customer and process through such account in order to control joint ownership of customers or the receipt of fruit or redemption of national government bonds jointly owned by customers and money paid, etc.
- (9) Business of cumulative investment based on the Law on the Promotion of Workers' Property Ownership Formation (hereinafter such Law is referred to as "Property Formation Law" and such investment is referred to as "property formation saving") may be carried out as follows.
- ① Notwithstanding the above (2) ③ (b) b., the following methods shall be used for purchase value of the securities referred to in the above (1) ⑤ (b) among methods to buy securities:
- (a) In the case of purchase based on a workers' property ownership formation saving contract as provided in Article 6.1 of the Property Formation Law, base value as of the day of purchase (in the case of an open-end type investment trust which collects trust assets reservation amount at the time of purchase, the total amount of such trust assets reservation amount and the base value);
- (b) In the case of purchase based on a workers' property ownership formation pension saving contract as provided in Article 6.2 of the Property Formation Law and a workers' property ownership formation housing saving contract as provided in Article 6.4 of said Law, the base value as of the day of purchase.
- ② Notwithstanding ① and ② of (3), payment of money and control of money on deposit shall be made as follows:
- (a) The amount of money paid by a customer to be used for the considerations of purchase of securities shall be at least ¥1,000 (at least ¥1 for the payments referred to in b. to e. of (b) below).
- (b) Payment of money shall be made in the following manners based on a contract entered into in advance between a business proprietor and a financial instruments firm:
- payment of money which is deducted from wage and salary payable to such customer;
 - payment of money to such customer account for the purpose of promoting property formation saving by a business proprietor;
 - payment of money from such customer's property formation benefits or property formation fund benefits;
 - payment of money from a property formation savings handling organization of a business entity before an occupational change as a result of the customer's occupational change;
 - payment of money of return saving money provided in Article 6.1 of the Property Formation Law by a business proprietor to such customer's account.
- (c) Money paid, etc. by a customer shall be accounted as property formation saving money.
- (d) Money paid, etc. by a customer shall be used for the considerations for purchase of securities on behalf of such customer after the addition of ordinary deposit interest equivalent amount. *Provide*, That fruits such as interests shall not be paid to a customer from money on deposit arising from the receipt of fruits or redemption of deposited securities.
- ③ When, after the purchase of national government bonds for a customer in respect of property formation saving jointly with other customers, the total amount of the purchase balance of such national government bonds for one customer and money paid, etc. has reached the amount equal to the integral multiple of ¥10,000, such government bonds may be sold and a contract to purchase corporate debt securities for one customer for the unit equivalent to the integral multiple of ¥10,000 jointly with other customers may be entered into. In this case, the provisions of ② to ④ of (8) above shall apply to the purchase of corporate debt securities.
- ④ The balance of deposit and the amount of redemption of securities for property formation saving business shall be segregated from securities for other cumulative investment business. Such securities may be redeposited with a securities finance company, bank or trust bank in the name of a financial instruments firm in lieu of keeping such securities by itself.
- ⑤ Notwithstanding the above (6), cancellation shall be made as follows.
- (a) A contract for property formation saving shall be cancelled when:
- a customer so requests; a customer may request such cancellation any time;
 - a customer fails to meet requirements for property formation savings provided by the Property Formation Law;
 - a financial instruments firm becomes unable to carry out "property formation saving" business.
- (b) In addition to the above a., if 3 years have passed in the case of a workers' property

formation saving contract, 5 years have passed in the case of a workers' property formation pension saving contract or a workers' property formation housing saving contract after the first payment by a customer and the customer fails to pay the whole or part of the considerations for purchase of securities for another one year, such contract may be cancelled:

Provided, that this shall not apply, if a customer deposited securities with a financial instruments firm, etc. based on such contract and such contract provides that securities may be bought for the considerations of only money on deposit arising from fruits or redemption of such securities, to such contract within one year since the day of the previous purchase.

- ⑥ Reporting, etc. of the balance to a customer may be made through the business proprietor of such customer.
- (10) Joint purchase cumulative investment business of share certificates may be carried out as follows.
 - ① With respect to share certificates, a contract that such share certificates are bought for cumulative investment business may be entered into with a customer who offers the purchase jointly with other customers.

In this case, a financial instruments firm shall enter into a contract with the provisions of purchase issue, the amount of each payment by a customer, timing of execution of purchase, etc. with a customer in advance and execute purchase, etc. based on such contract.
 - ② If the total amount of money paid, etc. by one customer and money paid, etc. by other customers reaches the purchase value (or its integrated multiple) of share certificates, purchase of such share certificates shall be made without delay.
 - ③ In the case of the above ②, there is an amount less than purchase value of share certificates in the total amount of money paid, etc. by one customer and money paid, etc. by other customers, the financial instruments firm shall accept the deposit of such fraction until the time of the next purchase or otherwise pay the difference between the minimum purchase value and such amount and buy share certificates.
 - ④ With respect to share certificates purchased, customers (including, in the case of share certificates jointly bought by a financial instrument firm and customers under the above ③, the financial instruments firm) shall acquire the right of the shared ownership jointly (joint ownership) and own shared ownership in proportion of the respective amount of payment (excluding, if the financial instruments firm accepts the deposit of the amount of fraction in the case of above ③, such amount). The nominal owner of the share certificates bought jointly by such customers shall be the financial instruments firm; and if the share jointly owned by one customer has reached the unit number of shares, such share jointly owned shall be split to a unit share no later than the base date under Article 124.1 of the Corporation Law such as the first end of a term of the issuer of such share certificates thereafter, and this cumulative investment contract shall not apply to such unit share.
 - ⑤ Dividends paid for share certificates jointly owned by customers shall be appropriated in proportion of share ownership of each customer and reinvested.
 - ⑥ Share certificates jointly owned by customers shall be segregated from other securities, and an account shall be opened for each customer to control share ownership of each customer and dividends, etc. from share ownership.
- (11) Joint purchase cumulative investment business of listed investment trust beneficial certificates may be carried out as follows.
 - ① With respect to listed investment trust beneficial certificates, a financial instruments firm may enter into with a customer who offers the purchase jointly with other customers a contract that such listed investment trust beneficial certificates are bought for cumulative investment business.

In this case, the financial instruments firm shall enter into a contract with the provisions of purchase issue, the amount of each payment by a customer, timing of execution of purchase, etc. with a customer in advance and execute purchase, etc. based on such contract.
 - ② The minimum amount of paid money for a customer shall be ¥10,000 each time.
 - ③ If the total amount of money paid, etc. by one customer and money paid, etc. by other customers reaches the purchase value (or its integrated multiple) of listed investment trust beneficial certificates, purchase of such listed investment trust beneficial certificates shall be made without delay.
 - ④ In the case of the above ③, there is an amount less than purchase value of listed investment trust beneficial certificates in the total amount of money paid, etc. by one customer and money paid, etc. by other customers, the financial instruments firm shall accept the deposit of such

- fraction until the time of next purchase or otherwise pay the difference between the minimum purchase value and such amount and buy listed investment trust beneficial certificates.
- ⑤ With respect to a listed investment trust beneficial certificate bought, customers (including, in the case of listed investment trust beneficial certificates jointly bought by a financial instrument firm and customers under the above ④, the financial instruments firm) shall have shared ownership and own shared ownership in proportion of the respective amount of payment (excluding, if the financial instruments firm accepts the deposit of the amount of fraction in the case of above ④, such amount). The nominal owner of the listed investment trust beneficial certificates bought jointly by such customers shall be the financial instruments firm; and if the share jointly owned by one customer has reached the unit number of shares, such share jointly owned shall be split to a unit share, and the cumulative investment contract shall not apply to such unit share.
 - ⑥ A financial instruments firm shall appropriate, and reinvest, dividends paid for listed investment trust beneficial certificates jointly owned by customers in proportion of share ownership of each customer.
 - ⑦ A financial instruments firm shall segregate listed investment trust beneficial certificates jointly owned by customers from other securities and open an account for each customer to control share ownership of each customer and dividends, etc. from share ownership.
- (12) Joint purchase cumulative investment business of listed investment certificates may be carried out as follows.
- ① With respect to listed investment certificates, a financial instruments firm may enter into with a customer who offers the purchase jointly with other customers a contract that such listed investment certificates are bought for cumulative investment business.
In this case, a financial instruments firm shall enter into a contract with the provisions of purchase issue, the amount of each payment by a customer, timing of execution of purchase, etc. with a customer in advance and execute purchase, etc. based on such contract.
 - ② If the total amount of money paid, etc. by one customer and money paid, etc. by other customers reaches the purchase value (or its integrated multiple) of listed investment certificates, purchase of such listed investment certificates shall be made without delay.
 - ③ In the case of the above ②, there is an amount less than purchase value of listed investment certificates in the total amount of money paid, etc. by one customer and money paid, etc. by other customers, the financial instruments firm shall accept the deposit of such fraction until the time of next purchase or otherwise pay the difference between the minimum purchase value and such amount and buy listed investment certificates.
 - ④ With respect to listed investment certificates bought, customers (including, in the case of listed investment certificates jointly bought by a financial instrument firm and customers under the above ③, the financial instruments firm) shall acquire (jointly) the right of shared ownership jointly and own shared ownership in proportion of the respective amount of payment (excluding, if the financial instruments firm accepts the deposit of the amount of fraction in the case of above ③, such amount). The nominal owner of the listed investment certificates bought jointly by such customers shall be the financial instruments firm; and if the share jointly owned by one customer has reached the unit number of shares, such share jointly owned shall be split to a unit share no later than the base date under Article 77-3.2 of the Investment Trust Law such as the first end of a term of the issuer of such listed investment certificates thereafter. This cumulative investment contract shall not apply to such unit share.
 - ⑤ A financial instruments firm shall appropriate, and reinvest, dividends paid for listed investment certificates jointly owned by customers in proportion of share ownership of each customer.
 - ⑥ A financial instruments firm shall segregate listed investment certificates jointly owned by customers from other securities, and open an account for each customer to control share ownership of each customer and dividends, etc. from share ownership.

IV-4-3 Registration of sales representative

- (1) Scope of sales representatives required to be registered
Persons required to be registered in the sales representative registry book under Article 64.1 of the F.I. Act among officers and employees engaging in in-house business (including reception operations) of a financial instruments firm shall be persons engaging in any of the following business operations:
 - ① explanation of financial instruments transactions, etc. for the purpose of solicitation;

- ② solicitation of financial instruments transactions, etc.;
 - ③ acceptance of orders;
 - ④ providing of information, etc. for the purpose of solicitation (excluding providing information related to back office operations and objective information based on the requests by customers); or
 - ⑤ a person who performs the act referred to in (1) or (2) of Article 64.1 of the F.I. Act.
- (2) Matters to be notified

It shall be noted that Article 64-4 (3) of the F.I. Act shall not apply in the case where a person has halted business operations as a sales representative temporarily for the reason of personnel reshuffle of a financial instruments firm.

IV-4-4 Financial instruments transactions liabilities reserve

It shall be noted that the withdrawal of funds from the financial instruments transactions liabilities reserve provided in Article 46-5 of the F.I. Act is permitted only if:

- ① there is a finding that an officer or employee of a financial instruments firm has committed illegal or improper acts, etc.; and
- ② the amount to be withdrawn is appropriate to cover the required amount of compensation for losses.

IV-5 Designated parent corporation group

With respect to a financial instruments firm group engaged in large scale and complex business, contingent risk which may influence on the financial system through the concentration of risks is increasing. On the other hand, the place where overall risks of the group exist is becoming uncertain particularly for internationally active groups because much larger and verticalized organization causes difficulty of business management of the entire group. In the case where a financial instruments firm carries out large scale and complex business as a unit of the group, therefore, financial or business problems, etc. originated from a parent corporation, subsidiary corporation or sister corporation in the group may result in sudden collapse of the financial instruments firm, and cause the market intermediation function of the financial instruments firm to fail, and create adverse influence on wide range of investors and, furthermore, create adverse influence on financial system.

Based on the above, a financial instruments firm carrying out large scale and complex business as a unit of the group is regulated and supervised on a consolidated basis. A large financial instruments firm which is determined to carry out financial business as a unit of the group is regulated and supervised on a consolidated based for the entire group including the parent corporation (so-called "upriver consolidation").

It is important therefore that a designated parent corporation group subject to this upriver consolidation makes strong and comprehensive risk control on a group basis under appropriate business management control, and the authority shall supervise based on the focus points stated in the Financial Conglomerate Supervising Guidelines with particularly the following remarks.

"Designated parent corporation group" shall mean a group comprised of a designated parent corporation and its subsidiary juridical persons, etc..

IV-5-1 Business management control

The authority shall verify the business management control of a designated parent corporation group with the following remarks.

- ① Whether a director of the designated parent corporation is a person having knowledge and experience for the business control of group member corporations including overseas business units accurately, fairly and efficiently and having sufficient social credit.
- ② Whether the designated parent corporation establishes the business management policies and business management plan based on the entire picture that the group aims and informs them to the entire group including overseas business units. Whether the designated parent corporation verifies the degree of the achievement of the plan including overseas business units periodically and reviews them including its significance and positioning thereof in the group when needed.
- ③ Whether the designated parent corporation understands the increasing complexity of the

organization associated with the formation of a designated parent corporation group and implements an appropriate business management system. Particularly whether the designated parent corporation combines the direct control by the designated parent corporation and empowerment to the management of an overseas business unit as a system to ensure appropriate business management of overseas business units, and clarifies the segregation of responsibilities.

- ④ Whether the designated parent corporation implements a system that the internal audit division of the entire group or an overseas business unit performs internal auditing appropriately, after the consideration of business and risk character, etc. of the overseas business unit. Whether the designated parent corporation takes appropriate measures based on the result, etc. of internal audits.
- ⑤ Whether the designated parent corporation implements the sufficient internal control system for an overseas business unit based on the positioning of each overseas business unit and its business strategy and business plan and considering the actual business and risk character, etc.
- ⑥ Whether the designated parent corporation recognizes the business and financial conditions of the entire group including overseas business units, and recognizes the risk conditions appropriately and takes necessary responses after full understanding of the risk character of each business unit.

IV-5-2 Appropriateness of business management

The authority shall verify the appropriateness of business management of a designated parent corporation group with the following remarks.

- ① Whether the group implements an appropriate compliance system such as ensuring of necessary personnel structure in the local jurisdiction (such as allocation of officers and employees with knowledge of relevant laws and regulations) and preparation of internal rules according to the scale of a overseas business unit or business character in order to ensure thorough compliance with relevant laws and regulations in each jurisdiction as the entire group. Whether the designated parent corporation continuously verifies whether each overseas business unit, etc. ensures such system sufficiently.
- ② Whether the designated parent corporation confirms the degree of knowledge of officers and employees of overseas business units concerning relevant laws and regulations in the local jurisdiction, and verifies continuously the implementation of the system to perform training or education appropriately when needed.
- ③ Whether, in order to prevent the violation of laws or regulations or other inappropriate business management, the group clarifies the division of roles of the designated parent corporation and overseas business units, etc., and implements a system to fulfill checking function or monitoring function over sales divisions, etc. appropriately.
- ④ Whether, if a problem has been found in an overseas business unit, the group makes information sharing between the designated parent corporation and the overseas business unit and necessary responses promptly, and implements a system to make a prompt report to the supervisory authority in Japan and relevant supervisory authorities.

IV-5-3 Capital adequacy

The authority shall verify the capital adequacy of a designated parent corporation group with the following remarks.

(Note) In the case where a group to which a designated parent corporation group is not applicable and is required by the supervisory authority in a foreign jurisdiction where the group is engaged in business that the supervisory authority in Japan monitors the financial soundness of the group (on a consolidated basis, etc.) compute the total capital and required capital under Financial Conglomerate Supervisory Guidelines II-2-1 (2) ② and a financial instruments firm in the group is approved to use internal measurement approach under Article 12 of the Capital Requirement Announcements, the group may compute market risk equivalent amount among amounts of required capital as a group using such approach.

IV-5-3-1 Appropriateness of capital of ultimate designated parent corporation (quality)

It is very important that the ultimate designated parent corporation ensures capital adequacy

and hold sufficient financial ground according to risks in order to gain confidence from markets, etc. The ultimate designated parent corporation should have the process to value the degree of overall capital adequacy considering the characteristics of risks and take appropriate measures to maintain sufficient capital.

IV-5-3-1-1 Directors and board of directors

- (1) Whether directors understand the nature and level of risks exposed by the ultimate designated parent corporation and the relationship between the risks and the appropriate level of capital.
- (2) Whether directors or the board of directors understand that, in order to achieve a strategic goal, a capital plan suitable thereto is requisite, and prepare a capital plan appropriate for the strategic goal.
- (3) Whether the board of directors, in preparing the business plan, analyses the amount of capital necessary now and in the future connected with a strategic goal, and show the summary of the level of capital desirable considering the strategic goal, the necessary amount to be financed and the appropriate method of financing in the business plan.
- (4) Whether directors are involved fully in taking appropriate measure to maintain the process to value the degree of overall capital adequacy in light of risk characteristics and sufficient capital in terms both quality and quantity.

(Note) The authority shall verify in respect of the ultimate designated parent corporation which is a corporation having a committee from the point of view of whether organs such as the board of directors, each committee and executive officer exercise the respective given authorities appropriately. In this case, the authority shall verify according to the reality based on the purpose of these Supervisory Guidelines.

IV-5-3-1-2 Valuation of capital adequacy

- (1) Whether the system for the ultimate designated parent corporation to value the degree of overall capital adequacy in light of risk characteristics includes the followings and is appropriate:
 - ① principles and procedures for recognizing, valuing and measuring every risk with certainty and reporting;
 - ② process to value the degree of capital adequacy in comparison with risks recognized, valued and measured under ①;
 - ③ process to establish the target of capital in comparison with risks after considering strategic goal and business plan;
 - ④ process of internal control including the verification by the internal audit division to ensure that the overall risk control process of the ultimate designated parent corporation is appropriate.
- (2) Whether the ultimate designated parent corporation analyses the quality of capital as well as the quantity of capital in valuing the capital adequacy. Whether, particularly, the ultimate designated parent corporation which computes the consolidated capital requirement ratio under Article 3 of "Announcement regarding Establishing Standards to Judge Whether Capital Adequacy of Ultimate Designated Parent Corporation and its Subsidiary Juridical Person, etc. Is Appropriate Considering Assets, etc. Held by the Ultimate Designated Parent Corporation and Its Subsidiary Juridical Person, etc. (hereinafter referred to as "Ultimate Designated Parent Corporation Announcement")" analyses the quality of capital including the following matters:
 - ① Whether core capital (Tier 1) is the core composition of capital;
 - ② Whether ordinary shareholders equity is the core composition of the core capital (Tier 1). For example, major part of the core capital (Tier 1) is composed of paid-in capital, capital surplus and profit surplus (excluding the amount equivalent to stock other than ordinary stock (including preference stock convertible to ordinary stock) among paid-in capital and capital surplus);
 - ③ Whether the risk that excessive reliance on capital subject to the limit of inclusion in capital to compute the consolidated capital requirement ratio (preference capital contribution certificates issued by an overseas special purpose corporation, stock, etc. having probability of redemption such as attachment of special provisions for premium of step-up interest, etc., supplementary capital, quasi-supplementary capital) to lower the consolidated capital requirement ratio is necessary;
 - ④ Whether the ultimate designated parent corporation which has financed lends the proceeds

of such finance to a lender of a loan with special provisions of subordination through a bypass loan, etc.

(3) Deferred tax assets

A large ratio of deferred tax assets to capital may, as matters related to the quality of capital, cause problems for the soundness of the ultimate designated parent corporation. The following shall be noted therefore:

- ① Whether deferred tax assets are accounted appropriately for the purpose of accounting standards, etc. for tax effect accounting considering the weakness that the nature of assets of such deferred tax assets relies on taxable income in the future;
- ② Whether, with respect to the ground to recognize deferred tax assets and computation procedures therefor, the ultimate designated parent corporation discloses the following items (a) to (f) and gives easy-to-understand explanation according to the computation procedures, etc. based on disclosed figures concerning corporations, etc. in the group which are important for the computation of consolidated deferred tax assets at the time of publishing a short report of the account settlement (including interim settlement) or at other appropriate timing (X years) in order to increase the reliance on the amount accounted as deferred tax assets:
 - (a) the ground to recognize deferred tax assets (if the judgment is made mainly based on the past business performance, etc., classification of example of the Practical Guidelines (Note) (including nonrecurring and special reason in the case of the proviso to (4))) and the period for estimation of taxable income in the future;
 - (b) taxable income for the past five years (actual values of each business year before the use of amounts of losses carried forward);
 - (c) the estimated amount of net operational profit based on which the estimation was made (the total amounts for X years);
 - (d) the estimated amount of net profit before tax based on which the estimation was made (the total amounts for X years);
 - (e) the estimated amount of taxable income before adjustment (the total of amounts for X years);
 - (f) With respect to reasons for major occurrence of deferred tax assets and liabilities, items required to be commonly disclosed:
 - a. deferred tax assets: allowance for bad debt, taxable depreciation of securities, valuation profit or loss of other securities, accrued employees retirement benefit, loss carried forward, others;
 - b. deferred tax liabilities: gain on contribution of securities to employees retirement benefit trust, valuation profit or loss of other securities, unrealized profit related to lease transaction, others.

(Note) "Audit on Judgment of Collectability of Deferred Tax Assets" (Japanese Institute of Certified Public Accountants November 9, 1999)

IV-5-3-1-3 Confirmation whether eligibility of financing instruments as capital is Appropriate to compute capital requirement ratio

In the case where, in relation to the valuation of capital adequacy for the ultimate designated parent corporation computing consolidated capital requirement ratio based on Article 3 of the Ultimate Designated Parent Corporation Announcement, there is a notification of the issuance, etc. related to financing instruments such as preferred capital contribution certificates issued by an overseas special purpose corporation, borrowing money with special provisions of subordination and corporate debt security with special provisions of subordination, confirmation shall be made for the eligibility as capital on regulations for consolidated capital requirement ratio based on the purpose of Ultimate Designated Parent Corporation Announcement and Basel Accord and "Instruments Eligible for Inclusion in Tier 1 Capital" (Basel Committee on Banking Supervision 1998). III-2-1-1-3 of the Comprehensive Supervisory Guidelines for Major Banks, etc. concerning the details of focus points when needed.

IV-2-1 (1) shall be referred concerning confirmation of eligibility of borrowing money with special provisions of subordination and corporate debt security with provisions of subordination of the ultimate designated parent corporation computing the consolidated capital requirement ratio under Article 4 of the Ultimate Designation Parent Corporation Announcement.

IV-5-3-1-4 Accuracy of consolidated capital requirement ratio (intentional holding and proportionate consolidation)

- (1) Based on the reminding in the Basel Accord to the effect that financing within the financial system (so called double gearing) "weaken the financial system because a problem in one financial institution is transmitted to other financial institution quickly," intentional holding of shares of stock or other financing instruments of other financial institution, etc. in order to improve capital of such other financial institution, etc. (hereinafter referred to as "intentional holding") must be deducted from the capital of the ultimate designated parent corporation computing the consolidated capital requirement ratio as "deducted items" under Article 3 of the Ultimate Designated Parent Corporation Announcement according to Article 8 of the Ultimate Designated Parent Corporation Announcement in Japan.

III-2-1-2-2 of the Comprehensive Supervisory Guidelines for Major Banks, etc. shall be referred concerning the details of focus points for the judgment of "intentional holding," when needed.

- (2) III-2-1-2-2 (4) of the Comprehensive Supervisory Guidelines for Major Banks, etc. shall be referred in the case of the notification of the use of methods of proportionate consolidation in respect of affiliate corporations, etc. engaged in financial business at the time of computing the consolidated capital requirement ratio, when necessary.

IV-5-3-2 Sufficiency of capital of ultimate designated parent corporation (quantity)

The computation of risk assets for the consolidated capital requirement ratio shall be checked with the following remarks.

IV-5-3-1 Computation method of risk assets

- (1) Whether, if assets has been securitized, effective assignment has been made such as transferring risks to the assignee fully even if such securitization is legally treated to be assignment.
- (2) Assignment of claims with repurchase right is allowed to cause effectiveness of reduction of risk assets in principle.

Assignment of claims with repurchase right for consecutive account settlement terms, however, is not allowed to cause effectiveness of reduction of risk assets if such assignment is associated with entering into a contract to give an incentive to exercise the right for repurchase within one year after such account settlement term.

Notwithstanding the above, assignment of claims with repurchase right is not allowed to cause effectiveness of reduction of risk assets if such assignment is made with the intention to raise the consolidated capital requirement ratio temporarily.

- (3) Claims with bank guarantee, etc. held for consecutive account settlement terms or as of the date of an account settlement are allowed to cause effectiveness of reduction of risk assets only if the remaining period of the claims and the period of such guarantee, etc. are equal in principle.

If the remaining period of the guarantee, etc. is shorter than the remaining period of the claims, however, such claims are allowed to cause effectiveness of reduction of risk assets if there is a reasonable cause for such guarantee, etc. and reduction of credit risk is expected continuously (Note).

Notwithstanding the above, assignment of claims with bank guarantee, etc. is not allowed to cause effectiveness of reduction of risk assets if a contract of such bank guarantee, etc. is entered into with the intention of raising the consolidated capital requirement ratio temporarily.

(Note) The remaining period of guarantee, etc. for one year or longer is applicable for the time being (claims with guarantee, etc. with remaining period of one year or longer, however, is not allowed to cause effectiveness of reduction of risk assets if a contract is entered into to give an incentive to cancel the guarantee contract, etc. within one year effectively.)

- (4) Foreign exchange positions held for the purpose of maintaining the consolidated capital requirement ratio among positions subject to the computation of foreign exchange risk at the time of the computation of market risk equivalent amount of the ultimate designated parent

corporation computing the consolidated capital requirement ratio under Article 3 of the Ultimate Designated Parent Corporation is allowed to be excluded from foreign exchange risks for the time being.

IV-5-3-2-2 Internal control, etc. regarding assets and transactions for trading business

In the case of the ultimate designated parent corporation computing the consolidated capital requirement ratio under Article 3 of the Ultimate Designated Parent Corporation, transactions subject to market risk regulations comprise a major part of assets and liabilities related to trading business as provided in Article 11 of the Ultimate Designated Parent Corporation Announcement. The ultimate designated parent corporation shall clarify transaction subject to market risk regulations and exclude inappropriate transactions (Note), and shall control transactions subject to market risk regulations appropriately. The authority shall confirm the followings based on the above view.

- (1) Whether the ultimate designated parent corporation clarifies, by writing statements, transactions subject to market risk regulations and the controlling method thereof (including the methods to value the prices appropriately according to the characteristics of the transactions based on the expected holding period and probability that the holding period exceeds the expectation).
 - (2) Whether the ultimate designated parent corporation confirms appropriate management by such written statement through periodical internal audits (with respect to the appropriateness of the methods to value the prices and management thereof, internal audit and accounting audit).
- (Note) "Application of Basek II and the Treatment of Double Default Effects" (Basel Committee on Banking Supervision 2005) exemplifies open equity stakes in hedge fund and private placement stock, etc. as inappropriate (Paragraph 271).

IV-5-3-3 Disclosure of capital adequacy

- (1) The purposes of the disclosure of capital adequacy under the Third Pillar (Market Discipline) of Basel II are to supplement the First Pillar (Minimum Capital Requirement Ratio) and the Second Pillar (Self-control of Financial Institutions and Supervisory Review Process) and maintain the sound management of financial institutions by disciplining external valuation by markets. When the ultimate designated parent corporation computing the consolidated capital requirement ratio under Article 3 of the Ultimate Designated Parent Corporation Announcement discloses, therefore, under "Announcement regarding Matters Required to be Stated in Written Statement of Capital Adequacy by Ultimate Designated Parent Corporation in Case Determined by Commissioner of Financial Services Agency" (hereinafter referred to as "Disclosure Announcement"), the ultimate designated parent corporation shall disclose important matters appropriately in light of business management and risk characteristics which is to discipline external valuation by markets.
- (2) With respect to matters which are not necessarily important considering business management and risk characteristics, etc. of the ultimate designated parent corporation, on the other hand, it cannot be denied that detailed disclosure of such information may possibly interfere the purpose of the Disclosure Announcement which is to discipline external valuation by markets. If there is an item which is not important considering business management and risk characteristics, etc., disclosure of items which were not disclosed and the reasons, etc. for judging that such items are not important shall suffice.
- (3) With respect to information having property values and information subject to secrecy obligation, if there is likeliness that disclosure of such information may damage the status of the ultimate designated parent corporation, disclosure of items, in addition to more general information regarding such items, which were not disclosed and the reasons therefor shall suffice.
- (4) In confirming the state of disclosure, the authority shall not focus on coverage of items prescribed by the Disclosure Announcement, but confirm that important items in light of business management and risk characteristics of the ultimate designated parent corporation are disclosed appropriately and the contents are useful for discipline of external valuation by markets.

IV-5-3-4 Early improvement measures

IV-5-3-4-1 Significance

It is very important that the ultimate designated parent corporation ensures capital adequacy voluntarily and hold sufficient financial grounds according to risks in order to ensure financial soundness. The authority shall, as a role of supplementing the effort of the ultimate designated parent corporation, use a consolidated capital requirement ratio as objective standards, issue a necessary improvement measure order timely and appropriately and promote early improvement of business management of the ultimate designated parent corporation.

IV-5-3-4-2 Supervisory methods and responses

Early improvement measures, the concrete measures of which are provided in "Announcement for Determining Classification of Business Management Soundness of Ultimate Designated Parent Corporation and its Subsidiary Juridical Person, etc. and Order According thereto" (hereinafter referred to as "Classification Announcement") shall be managed as follows:

- (1) Consolidated capital requirement ratio which is the basis for the issuance of an order:
A consolidated capital requirement ratio according to the classification of the Tables under Articles 1 and 3 of the Classification Announcement shall be the following consolidated capital requirement ratio.
 - ① After filing a written statement containing the soundness of business management under the provisions of Article 57-17.2 of the F.I. Act, the consolidated capital requirement ratio so reported;
 - ② Other than the period during which the above ① has been reported, after the discussion between the ultimate designated parent corporation and an audit juridical person, etc. based on the inspection result, etc. of the authority, the consolidated capital requirement ratio reported by such ultimate designated parent corporation;
- (2) Order based on the classification of the Table under Article 1 of the Classification Announcement
 - ① Difference among an order under the classification 1, an order under the classification 2 and an order under the classification 3

The purpose of "submission of a plan (including measures for capital reinforcement in principle) which are deemed to be reasonable to ensure soundness of business management and the issuance of an order to enforce the plan" under the classification 1 is to ensure the steady achievement of the level at least 8% of the consolidated capital requirement ratio as standards that the soundness of business management is ensured. The authority shall, therefore, emphasize that the entire plan aims to ensure the soundness of business management and respect the self-initiative of the ultimate designated parent corporation in principle for the enforcement of the plan.

The purpose of "the issuance of an order related to measures to contribute to capital adequacy of the ultimate designated parent corporation and its subsidiary juridical person, etc. referred to in the following items" under the classification 2 is to improve the consolidated capital requirement ratio which is substantially lower than the level to ensure the soundness of business management at an early time. The authority shall, therefore, determine the measures by its judgment although an opinion of such ultimate designated parent corporation is considered for individual measures because of the necessity of considering business management of such ultimate designated parent corporation. The ultimate designated parent corporation shall fulfill an order for each of measures in principle in enforcing such measures.

The purpose of "the issuance of an order to take measures, after the selection of any of measures for capital adequacy of the ultimate designated parent corporation and its subsidiary juridical person, etc., merger or measure to cease to be a parent corporation (which means a parent corporation as defined in article 57-2.8 of the F.I. Act; hereinafter in this Article and the following Article, the same) of an object special financial instruments firm for a pecified period but not less than three months, for such selection" under the classification 3 requires the ultimate designated parent corporation suffering significant undercapitalization to improve immediately or give up the continuation of business as the ultimate designated parent corporation.

- ② Period until the improvement

With respect to the period required for the improvement of consolidated capital requirement ratio, a plan, etc. prepared by the ultimate designated parent corporation for improvement of business management shall be sufficient for immediate maintenance and recovery of confidence of markets, etc. on the ultimate designated parent corporation. A plan, etc. that the consolidated capital requirement ratio recovers to 8% or more within at least one year (no later than the immediately following account settlement period in principle) is required.

The period required for the improvement of the above consolidated capital requirement ratio shall not include the period for the improvement of the consolidated capital requirement ratio under (3) with certainty exceeding the range of consolidated capital requirement ratio in the classification under the Table to which the ultimate designated parent corporation is applicable if the ultimate designated parent corporation has submitted a plan which is determined to be reasonable for the improvement of its consolidated capital requirement ratio exceeding the range of consolidated capital requirement ratio in the classification in the Table under Article 1 of Order Determining Classification, etc. to which the ultimate designated parent corporation is applicable with certainty pursuant to the provisions of Article 2.1 of the Classification Announcement and the authority issues to the ultimate designated parent corporation the order referred to in the classification under said Table for consolidated capital requirement ratio exceeding the range of consolidated capital requirement ratio in the classification in the Table to which the ultimate designated parent corporation is applicable.

- (3) Judgment standards for reasonableness provided in Article 2.1 of the Classification Announcement

Judgment standards for reasonableness of "plan which is determined to be reasonable for the improvement exceeding the range of the classification with certainty" provided in Article 2.1 of the Classification Announcement" shall be:

The plan shall include the concrete capital enhancement plan, etc. to ensure sound and appropriate management of business of the ultimate designated parent corporation and to keep the confidence by markets, etc. on such ultimate designated parent corporation and be a plan to improve with certainty the consolidated capital requirement ratio exceeding the range of consolidated capital requirement ratio in the classification in the Table under Article 1 of the Classification Announcement to which the ultimate designated parent corporation is applicable within three months in principle.

(Note) The intention of the prospective capital contributors, etc. shall be clear in the case of capital increase, etc.

- (4) Consolidated capital requirement ratio based on which an order is classified

For the purpose of application of Article 2.1 of the Classification Announcement, an "order provided in the classification (excluding non-classified classification) under the Table at or lower than the consolidated capital requirement ratio expected after the enforcement" shall be the order referred to in the classification (excluding non-classified classification) for the level of the consolidated capital requirement ratio expected with certainty after three months in principle.

- (5) Report of progress of plan, etc.

The authority shall require to report the progress of a plan each term (including interim term) until the completion of the enforcement and, if the state of enforcement of the plan does not differ significantly from the plan thereafter, shall not issue a new order during the period of the plan in principle: *Provided*, That, in the case of an ultimate designated parent corporation to which an order under the Classification 3 has been issued and, thereafter, the consolidated capital requirement ratio has reached the range of 2% or more and less than 8%, the authority may issue an order referred to in the classification of the consolidated capital requirement ratio as of such time, and, in the case of an ultimate designated parent corporation to which an order under Classification 2 has been issued and, thereafter, the consolidated capital requirement ratio has reached the range of 4% or more and less than 8%, the authority may issue an order under Classification 1 as of such time.

If the ultimate designated parent corporation, pursuant to the provisions of Article 2 of the Classification Announcement, submits a plan which is determined to be reasonable to improve with certainty the consolidated capital requirement ratio exceeding the range of the consolidated capital requirement ratio in the classification in the Table under Article 1 of the Classification Announcement to which the ultimate designated parent corporation is applicable and the authority has issued to the ultimate designated parent corporation an order referred to in the classification in said Table for consolidated capital requirement ratio exceeding the range of the consolidated capital requirement ratio in the classification in said Table to which the

ultimate designated parent corporation is applicable, the authority shall, in principle immediately after the passing of the period required for procedures for capital increase, if the consolidated capital requirement ratio of such ultimate designated parent corporation has not reached the level of the consolidated capital requirement ratio or more in the classification of said Table in which the order issued to such ultimate designated parent corporation is referred to, the authority shall issue an order referred to in the classification in said Table for consolidated capital requirement ratio as of such time.

(6) Standards for valuation of assets referred to in Article 2.2 of the Classification Announcement

① (1) "Securities"

"Published last price" under Article 2.2 (1) of the Classification Announcement means on-exchange traded price, base indication price, base price, etc. "Value computed by reasonable methods as the price equivalent thereto" mean the valued amount obtained as current price information as of the date of computation from a financial instruments firm, etc. or value computed by the valuation method of the ultimate designated parent corporation and is determined to be reasonable.

The computation shall be made with the following remarks.

(a) Shares of stock or corporate debt securities the redemption of which is grossly uncertain because of large negative net worth of the issuer shall be valued and computed according to the reality;

(b) foreign currency denominated securities shall be translated to Japanese Yen at TT mean rate as of the date of the computation;

② (2) "Tangible fixed assets"

(a) Land

Valued amount which is computed referring to appraisal value (appraised within one year) or the latest road side land price, announced land price, standard land price and objective examples of trade and determined as reasonable.

(b) Building and movable assets

Book value in principle.

③ (3) "Assets other than assets referred to in (1) and (2)"

Securities (including foreign securities) invested as trust properties by a trust of money (limited to a trust managed alone for the main purpose of investment in securities) shall be valued in accordance with Article 2.2 (1) of the Classification Announcement and the above ①. The computation of a trust of money including derivatives transactions shall include unsettled valuation profit or loss for such transactions.

(7) Others

① An order under Articles 1 and 2 of the Classification Announcement shall be issued pursuant to the provisions of the Administration Procedures Law, etc. with remarks of the requirement of taking appropriate procedures for giving an opportunity of hearing under Article 13.1 (2) of said Law.

② An ultimate designated parent corporation with less than 4% of consolidated capital requirement ratio shall compute the assets referred to in each item of Article 2.2 of the Classification Announcement by the methods provided in such item in principle, and submit the revised balance sheet (with respect to forms, at its discretion).

② An early improvement measures shall be issued assuming that the consolidated capital requirement ratio represent the financial conditions of the ultimate designated parent corporation appropriately. The authority shall, therefore, require the ultimate designated parent corporation to avoid intentional manipulation of the consolidated capital requirement ratio to escape from the issuance of early improvement measures.

(8) Order issued under the classification of the Table under Article 3 of the Classification Announcement

With respect to early improvement measures under Article 3 of the Classification Announcement of, IV-2-2 shall be referred when needed.

IV-5-3-5 Early warning system

(1) Fundamental concept

"Early improvement measures" are provided using the consolidated capital requirement ratio under Article 57-21.3 of the F.I. Act as the method to ensure the soundness of business

management of an ultimate designated parent corporation. It is necessary for an ultimate designated parent corporation which is not subject to this measures to make an effort of continuous improvement of business management in order to ensure the maintenance and further improvement of the soundness of business management. For this purpose, the authority shall take administrative preventive measures at an early stage (early warning system).

(2) Hearing

- ① The authority shall always know, and analyze, the state of profitability and profit control system, etc. through semiannual account settlement hearing and comprehensive hearings, etc.
- ② The authority shall confirm the business strategy for improvement of profitability and policies for business restructure, etc. with the management of an ultimate designated parent corporation through top hearings conducted when needed.
- ③ The authority shall, when an ultimate designated parent corporation has prepared "medium-term business plan," conduct hearing when needed and verify an effort, etc. for business strategy and business restructure.

(3) Early warning system

With respect to an ultimate designated parent corporation which is required to improve profitability as standards of fundamental profit indicators, the authority shall conduct hearings in depth concerning the reason and improvement plan, etc. and encourage steady improvement through the collection of reports under Article 57-23 of the F.I. Act when needed. The authority shall issue a business improvement order under Article 57-19 of the F.I. Act of reliable enforcement of the improvement plan is required.

IV-5-4 Risk control system

The authority shall verify the risk control system of a designated parent corporation group, in addition to valuation items regarding risk control system of the single unit of a first-type financial instruments firm (IV-2-3 to IV2-5), with the following remarks based on the scale and business complexity of the group.

- ① Whether, in the case where the group arranges the framework to control the market risk, credit risk, liquidity risk, etc. on a group basis, the group considers the actual business and risk character, etc. of overseas business units in such framework, and considers the risks specific to each overseas business unit appropriately.
- ② Whether, in applying the framework of the risk control on a group basis, the role of overseas business units and the controlling framework applicable to overseas business units is reasonable based on the positioning of overseas business units in the group and actual business and risk character, etc.
- ③ Whether, even if the revenue control and risk control is made vertically for each business line as a group basis, the group ensures reasonable profitability and implements a system to control risks appropriately for each overseas business unit, etc. (Whether there is a weak overseas business unit, etc. which runs losses continuously.)
- ④ Whether the group controls transactions which are concluded by a business unit in Japan and controlled for the account of an overseas business unit appropriately considering the framework of the risk control on a group basis after clarifying the positioning of relevant overseas business units for the entire group. Whether the group fixes the transfer price for such transactions between the designated parent corporation and related overseas business unit in advance, clearly and reasonably.
- ⑤ Whether, if transactions concluded by an overseas business unit is controlled for the account of a business unit in Japan, the group implements a system to recognize appropriately the details, risks, etc. of such transactions, in addition to ③ above, at the business unit in Japan.

(Note) III-2-3-2-5 and III-2-3-3 of the Comprehensive Supervisory Guidelines for Major Banks, etc. shall be referred concerning the details of focus points when needed.

IV-5-4-1 Comprehensive risk control system

Whether, with respect to a designated parent corporation group which computes the consolidated capital requirement ratio under Article 3 of the Ultimate Designated Parent Corporation Announcement, the authority shall confirm that the group recognizes risks which

are not reflected to the consolidated capital requirement ratio such as interest rate risk and large-lot credit risk to assets and liabilities which are not subject to the computation of the market risk equivalent amounts and other various risks exposed by each business division holistically and quantitatively by means of constructing an integrated risk control system in the group, and further confirm that the group ensures the maintenance of capital sufficient, in quantity and quality, to holistic risk so recognized.

(Note) III-2-1 and III-2-3 of the Comprehensive Supervisory Guidelines for Major Banks, etc. shall be referred for the details of focus points when needed.

IV-5-4-2 Liquidity risk control system

The authority shall verify the liquidity control of a designated parent corporation group (particularly a designated parent corporation group which compute the consolidated capital requirement ratio under Article 3 of the Ultimate Designated Parent Corporation Announcement) with the following remarks.

- ① Whether the designated parent corporation establishes the policies for the degree of the liquidity risk acceptable to the group and the liquidity risk control reflecting the business policies, business strategies and funding capability of the entire group including overseas business units, and reviews them periodically.
- ② Whether the group recognizes the state of liquidity for the entire group including overseas business units accurately and implements a system to control appropriately with the coordination of the risk control division. Whether, for example, the group implements the system to quantify funding cost, etc. considering the degree of influence on liquidity in the event of stress, and use the result for budgeting process, business performance measurement, approval of new products, etc.
- ③ Whether the group implements a system to recognize the state of assets (the amount of stable funds required to be financed based on the state of composition, character and diversification of the assets), the current state of financing (the state of composition, character and diversification of financing sources) and financing capability for additional funds (including the state of collateral compared with assets holding and the eligibility of collateral for the central bank) of the entire group including overseas business units for each business unit and each currency appropriately.
- ④ Whether the group implements a system to recognize the state of the daytime liquidity and risk for each business unit appropriately considering legal and operational restriction regarding movement of funds.
- ⑤ Whether the designated parent corporation confirms the level that financing is possible from each financing method periodically based on the recognized state of the liquidity of the entire group, and makes an effort such as diversification of financing methods and maturity dates.
- ⑥ Whether the designated parent corporation exercises stress testing of the state of the liquidity of the entire group including overseas business units periodically reflecting the state of the risk character of each overseas business unit and conditions of overseas markets appropriately, and identifies contingent risk.
- ⑦ Whether the designated parent corporation clarifies diversified and urgent financing methods, etc. to maintain liquidity in the event of stress based on the result of stress testing, and establishes a contingency plan which provides for concrete procedures, etc. Whether the designated parent corporation confirms and renews the contingency plan periodically to ensure that such contingency plan works appropriately.

(Note 1) It is desirable that the designated parent corporation publishes the degree of the liquidity risk acceptable for the group, policies to control the liquidity risk and the state of liquidity progressively and periodically based on the international best practice.

(Note 2) III-2-3-4 of the Comprehensive Supervisory Guidelines for Major Banks, etc. and Financial Investigation Manuals shall be referred for the details of focus points when needed.

IV-5-5 Compensation scheme

It is possible that a designated parent corporation group designs and operates a compensation scheme considering international employment and compensation practice. It is possible, on the other hand, that such design and operation may give an officer or employee higher incentive to take risk and, if it becomes excessive, may lead to a gross problem for risk control, etc. of the entire group.

There are discussions internationally on the design and operation of the compensation scheme of financial institutions at a place such as the Financial Stability Board, and it is necessary for a designated parent corporation group to consider such international movement and ensure that a compensation scheme does not trigger excessive risk taking by an officer or employee. The supervisory authority shall supervise compensation schemes of such groups based on the international guidelines (Note) at the Financial Stability Board with particularly the following remarks. The authority shall conduct actual supervision with the remarks on avoiding supervision in an automatic and standardized manner based on the scale, complexity of business and establishment, etc. of overseas business units of the group.

A designated parent corporation group shall consider, in addition to the compensation scheme which will likely trigger excessive risk taking by an officer or employee, employment convention or personnel appraisal system which may have similar likeliness. The management shall keep in mind that the management is assigned to take important duties including business management and receive remuneration for such duties and therefore naturally is required to conduct appropriate business operations.

- (Note)
- Financial Stability Forum "Principles for Sound Compensation Practice" April 2009)
 - Financial Stability Board ""Principles for Sound Compensation Practice" Implementation Standards" (September 2009)

(1) Role of Remuneration Committee, etc.

- ① Whether the group establishes a committee, etc. to oversee the compensation scheme of an officer and employee or other system to fulfill the function to check the management to ensure the appropriate design and operation of the compensation scheme (hereinafter referred to as "remuneration committee, etc."). Whether the remuneration committee, etc. has the authorization and organization, etc. necessary to fulfill the overseeing and checking function independent from sales divisions, etc. (including an officer in charge).
- ② Whether the remuneration committee, etc. ensures that the overall compensation level is consistent with the maintenance of the group's sound capital base and strengthening of its capital base, and does not influence grossly on future capital adequacy.
- ③ Whether the remuneration committee, etc. values the appropriateness of the design and operation of the compensation scheme with remarks on the risk control such as close coordination with the risk control division.
- ④ Whether the remuneration committee, etc. confirms through overseeing the compensation scheme that problems such as excessive linkage of the amount of remuneration with gaining short term profit and reflecting to excessive performance based remuneration do not arise.

(2) Pay structure and risk alignment

- ① Whether the remuneration to an employee in a risk control division and compliance division is determined independently from other business division and is reflected by the significance of the duties. Whether performance related to the remuneration to such employee is measured by, in addition to the degree of the achievement of the risk control and compliance, contribution to building up of the risk control system or compliance system.
- ② Whether the proportion of the size of the variable compensation pool and its allocation for officers and employees (in respect of employees, employees whose actions have a material impact on the risk exposure of the entire group; hereinafter in IV-5-5, the same) within the group is appropriate based on, in addition to the duties and actual operations of officers and employees, financial soundness of the entire group and policies, etc. for the degree of risks that the group can take.
- ③ Whether, if a substantial proportion of remuneration to officers and employees is variable, the compensation scheme is designed based on financial risk exposure during the period until the amount of remuneration is fixed (estimation of required capital and liquidity).
- ④ Whether subdued or negative financial performance of the group generally leads to a considerable contraction of the variable compensation.
- ⑤ Whether a substantial proportion of variable compensation is awarded by a remuneration payment method to create incentives aligned with long-term value creation (such as payment in the form of shares or granting stock options) according to the duties and actual operations of each officer and employee and the time horizons of risk (for example, restriction of assignment for a certain period in the case of payment in the form of shares, exercise period in the case of granting stock options, deferral of remuneration period or return in the case of subdued or negative financial performance of the group).

- ⑥ Whether a compensation scheme which may influence adversely on the risk control (guaranteed bonuses over multiple period, large contractual payments related to a termination of employment) is reexamined and appropriate measures for improvement are taken.
 - ⑦ Whether, even if a compensation scheme consistent with risk control is designed, the group implements the system to oversee or check the likeliness that an officer or employee commits an act to damage the purpose of such design (transactions to reduce risks on the surface, etc.) appropriately.
- (3) Publication of design and operation of compensation scheme
- It is desirable to publish positively useful information regarding the consistency of the compensation scheme and the risk control of the group including the following items based on the internationally accepted best practice.
- ① information on the remuneration committee, etc.;
 - ② important information on the design of the compensation scheme (in respect of variable compensation particularly, the summary of the measurement method of performance, method to reflect of performance to the amount of remuneration and payment method);
 - ③ important information on the operations of the compensation scheme (particularly, total amount of remuneration to officers and employees, ratio of variable compensation to the total amount, matters regarding actual payment methods, etc.).

IV-5-6 Supervisory methods and responses

- (1) The authority shall hold a hearing on the state of responses to the issues specified based on international movements, etc. regarding the business management, appropriateness of business, appropriateness and adequacy of capital, risk control system and compensation scheme on a group basis periodically and continuously. The authority shall use positively the framework of cooperation with overseas authorities, and hold a hearing in depth on the issues, etc. of overseas business units recognized through such framework.
- (2) The authority shall require the designated parent corporation to make a report for the following items under Article 57-23 of the F.I. Act and make an effort to recognize the financial soundness, etc. of the group.

If it is determined that improvement is necessary for the financial soundness, etc. of a group, the authority shall make an effort to recognize the situation through a hearing in depth based on a report and encourage voluntary improvement.

 - ① Risk control policies of a designated parent corporation group (reporting is required without delay if there has been a change).
 - ② Budget distribution and financing policies of the designated parent corporation group (reporting is required each business year).
 - ③ In the case of an ultimate designated parent corporation computing the consolidated capital requirement ratio under Article 3 of the Ultimate Designated Parent Corporation Announcement, a report that the consolidated capital requirement ratio of the designated parent corporation group has dropped below 8% (in the case of dropping under 8%, immediate report).
 - ④ In the case of an ultimate designated parent corporation computing the consolidated capital requirement ratio under Article 4 of the Ultimate Designated Parent Corporation Announcement, a report that the consolidated capital requirement ratio of the designated parent corporation group has dropped below 140% (in the case of dropping under 140%, immediate report).
- (3) The authority shall require a report under Article 57-23 of the F.I. Act when needed, if a problem is found on the business management or internal control system, etc. of the designated parent corporation group has been found through off-site monitoring, investigation result and accident notification, etc. under (1) above (excluding items referred to in (2)).
- (4) The authority shall make responses such as the issuance of an order to improve business management under Article 57-19 of the F.I. Act based on a report under (2) or (3) above and if it is necessary for the improvement.

IV-6 Special financial instruments firm group

IV-6-1 Fundamental concept

A financial instruments firm group carrying out large scale and complex business as a unit of

the group shall be subject to regulation and supervision as a consolidated basis. Therefore, in the case of a large financial instruments firm, such financial instruments firm and its subsidiary juridical person, etc. shall be subject to consolidated regulation and supervision (so called "downriver consolidation").

IV-2 shall apply to the soundness, etc. of financial conditions of a special financial instruments firm group which is subject to downriver consolidation.

"Special financial instruments firm group" shall mean a group composed of a special financial instruments firm and its subsidiary juridical person.

(Note) IV-5-3-4-2 (1) shall be referred concerning the consolidated capital requirement ratio which is the assumption for the issuance of early improvement measures requiring the special financial instruments firm group to take concrete measures, etc. under "Announcement for Determining Classification of Soundness of Business Management of Special Financial Instruments Firm and its Subsidiary Juridical Person, etc. and Order According thereto," when needed.

IV-6-2 Supervisory methods and responses

(1) The authority shall conduct hearings periodically and continuously concerning the financial soundness, etc. on a group basis.

(2) The authority shall require a special financial instruments firm to make a report concerning the following items under the provisions of Article 56-2.1 of the F.I. Act and make an effort to know the financial soundness, etc. of the group.

The authority shall make an effort to know the state through hearings, etc. in depth based on a report and encourage voluntary improvement if the financial soundness, etc. of a group is determined that improvement is necessary.

A report that the consolidated capital requirement ratio of a special financial instruments group has dropped below 140% (if dropped below 140%, immediate report).

(3) The authority shall require to make a report under the provisions of Article 57-10 of the F.I. Act when needed, if the authority found problems on business management or internal control system, etc. of a special financial instruments firm through off-site monitoring, inspection result and accident notification, etc. under (1) above (excluding items referred to in (2)).

(4) The authority shall make responses such as issuance, etc. of business improvement order, etc. under the provisions of Article 51 of the F.I. Act if it is determined that further improvement is necessary based on the reports under (2) and (3) above.

IV-7 First-type financial instruments firm which is a business unit in Japan of foreign holding company, etc. group

With respect to a foreign holding company, etc. group (which means "foreign holding company, etc. group") stated in I-1 (4) of Financial Conglomerate Supervisory Guidelines; in IV-7, the same), realization of a problem of business management or risk control by the group head quarter, etc. (which means a company to make overall control over the entire group or group companies including a business unit in Japan; hereinafter in IV-7, the same) may cause direct influence on the first-type financial instruments firm which is a business unit in Japan of such group. There was a financial institution group which substantially relied on the market in respect of financing, expanded the business with excessive leverage and sought excessive short-term profits under insufficient risk control faced a problem of financial soundness or liquidity. There was an example that such problem affected directly and seriously on the continuity of business of the first-type financial instruments firm which was its business unit in Japan.

The authority shall, therefore, supervise a first-type financial instruments firm which is a business unit in Japan of a foreign holding company, etc. group in accordance with IV-1 to IV-4 with the following remarks in addition to focus points stated in Financial Conglomerate Supervisory Guidelines.

Foreign holding company, etc. groups are various, and have different characteristics, in respect of control systems of entire groups reflecting variety of risk characters and multiplying process. With respect to the roles, etc. of business units in Japan, some groups have reasonable number of staff and scale of assets and deploy a business model with taking large risks, some groups have small-sized personnel and assets and specialize in services related to the mother

country. If a first-type financial instruments firm which is a domestic business unit takes a form of a branch office, etc. of a foreign juridical person, attention shall be paid to the particular that such business unit belongs directly to a foreign juridical person to whom the Financial Instruments and Exchange Act or other relevant laws or regulations in Japan are not applicable directly. The authority shall conduct actual supervision based on the business character of each group and characteristics of business, etc. of a business unit in Japan with remarks to avoid supervision in an automatic and standardized manner.

IV-7-1 Business management control

The authority shall verify the business management control of a first-type financial instruments firm which is a business unit in Japan of a foreign holding company, etc. group with the following remarks.

- ① Whether the business policies and business plan, etc. of the entire group prepared by the group head quarter, etc. clarify the significance to establish the business unit in Japan and positioning thereof in the group. Whether the business policies and business plan of the business unit in Japan are consistent with the business policies and business plan of the entire group and sustainable.
- ② Whether the division of responsibility between the group head quarter, etc. and the management of the business unit in Japan is clarified and the management of the business unit in Japan is granted the authorization necessary to ensure appropriate business management of the business unit in Japan by the group head quarter, etc. Whether the authorization and responsibility is allocated appropriately in the business unit in Japan to ensure appropriate business control by the management.
- ③ Whether the internal audit division of the business unit in Japan implements a system to performs internal auditing appropriately considering the business and risk character, etc. of the business unit in Japan. Whether the management of a business unit in Japan takes appropriate measures based on the result, etc. of internal auditing.
- ④ Whether the internal control system of the business unit in Japan is sufficient based on the positioning of the business unit in Japan in the group and its business strategy and business plan, considering the actual business and risk character, etc.
- ⑤ Whether it is ruled that the group head quarter, etc. recognizes business and financial conditions of the business unit in Japan and recognizes the state of risk of the business unit in Japan appropriately after understanding fully the risk character that the business unit in Japan exposes, and make necessary responses.
- ⑥ Whether the management team of the business unit in Japan confirms sufficiency for ①～⑤ above, and responses appropriately after the discussion with the group head quarter, etc. when needed.

IV-7-2 Appropriateness of business management

The authority shall verify the appropriateness of business management of a first-type financial instruments firm which is a business unit in Japan of a foreign holding company, etc. group with the following remarks.

(Note) If a bank, etc. is established in addition to the first-type financial instruments firm as a business unit in Japan and there is an officer or employee concurrently holding the positions in both of the firm and the bank, etc., IV-3-1-4 for appropriateness, etc. of business management shall be referred alternatively.

- ① Whether the group implements an appropriate compliance system such as ensuring necessary personnel structure and preparation of internal rules as a business unit in Japan in order to ensure thorough compliance with the F.I. Act and relevant laws and regulations. Whether responses such as allocation of officers and employees with knowledge of the Financial Instruments and Exchange Act and other relevant laws and regulations and trading practices in Japan based on the possibility that the group head quarter, etc. does not have detailed knowledge of such laws or regulations are made.
- ② Whether the group confirms the degree of knowledge of officers and employees of the business unit in Japan concerning the Financial Instruments and Exchange Act and other relevant laws and regulations thoroughly, and implements a system to perform training or education appropriately when needed.
- ③ Whether, in order to prevent the violation of laws or regulations or other inappropriate

business management, the group clarifies the division of roles of the group head quarter, etc. and the business unit in Japan, and implements a system to fulfill checking function or controlling function of the business unit in Japan over sales divisions, etc. appropriately.

- ④ Whether, if a problem has been found in the business unit in Japan, the group makes information sharing between the group head quarter, etc. and the business unit in Japan and necessary and prompt responses, and implements a system to make a prompt report to the supervisory authorities in Japan and relevant supervisory authorities.

IV-7-3 Appropriateness and adequacy of capital

The authority shall verify the appropriateness (quality) and adequacy (quantity) of the capital of a first-type financial instruments firm which is a business unit in Japan of a foreign holding company, etc. group with the following remarks.

- ① Whether the group head quarter, etc. recognizes financial conditions of the business unit in Japan appropriately, and implements necessary system to ensure the appropriateness and adequacy of capital.
- ② Whether, in the case of the business unit in Japan which has the substantial scale of inter-group trading, the appropriateness and adequacy of the capital of the entire group is considered in ensuring the appropriateness and adequacy of the capital of the business unit in Japan.
- ③ Whether, in the case where stress testing or preparation of contingency plan, etc. regarding the appropriateness and adequacy of capital is made on a group basis, the risk character of the business unit in Japan and conditions of Japanese market are reflected appropriately.
- ④ Whether, in the case of verifying the appropriateness and adequacy of the capital of the business unit in Japan, risks associated with transactions for the account of an overseas business unit to which the business unit in Japan is liable contingently are reflected appropriately.

IV-7-4 Risk control system

The authority shall verify the risk control system of a financial instruments firm which is a business unit in Japan of a foreign holding company, etc. group, in addition to valuation items regarding the risk control system of the single unit of a first-type financial instruments firm which is a business unit in Japan (IV-2-3 to IV2-5), with the following remarks based on the scale and business complexity of the group.

- ① Whether, in the case where the group arranges the framework to control the market risk, credit risk, liquidity risk, etc. on a group basis, the group considers the actual business and risk character, etc. of the business unit in Japan in such framework, and considers the risks unique to the business unit in Japan appropriately.
- ② Whether, in applying the framework of the risk control on a group basis, the role of the business units in Japan and the controlling framework applicable to the business unit in Japan is reasonable based on the positioning of the business unit in Japan in the group and actual business and risk character, etc.
- ③ Whether, even if the revenue control and risk control is made vertically for each business line on a group basis, the group ensures reasonable profitability as the business unit in Japan and implements a system to control risks appropriately. (Whether the business unit in Japan runs losses continuously.)
- ④ Whether, if the group controls transactions which are concluded by the business unit in Japan for the account of an overseas business unit, the business unit in Japan takes an appropriate role in the framework of the risk control on a group basis after clarifying the positioning of the business unit in Japan for the entire group. Whether the group fixes the transfer price for such transactions between the group head quarter, etc. and the business unit in Japan in advance, clearly and reasonably.
- ⑤ Whether, if transactions concluded by an overseas business unit is controlled for the account of the business unit in Japan, the group implements a system to recognize appropriately and control appropriately the details, risks, etc. of such transactions, in addition to ④, at the business unit in Japan.

IV-7-4-1 Liquidity risk control system

The authority shall verify the liquidity risk control system of a first-type financial instruments firm which is a business unit in Japan of a foreign holding company, etc. group with the following remarks.

- ① Whether the group head quarter, etc. recognizes the financial conditions of the business unit in Japan appropriately and implements a system necessary to ensure the appropriateness and adequacy of liquidity.
- ② Whether a first-type financial instruments firm which is the business unit of a foreign group knows the supply of liquidity to the business unit in Japan of the group from member corporations of the group appropriately, and make a necessary effort to ensure appropriate and sufficient liquidity of the business unit in Japan.
- ③ Whether, in the case of a business unit in Japan which has the substantial scale of inter-group trading, the appropriateness and adequacy of the liquidity of the entire group is considered to ensure the appropriateness and adequacy of the liquidity of the business unit in Japan. Whether necessary responses are made such as preparation of a contingency plan, etc. based on the expectation of influence on the liquidity of the entire group in the event of stress after assuming the number of days that business continuity is possible as the business unit in Japan.
- ④ Whether, if the group makes stress testing or preparation, etc. of contingency plan regarding the appropriateness or adequacy of liquidity on a group basis, risk characters of the business unit in Japan or conditions of Japanese market are reflected appropriately.
- ⑤ Whether, in the case of verifying the appropriateness and adequacy of the liquidity of the business unit in Japan, risks associated with transactions for the account of an overseas business unit to which the business unit in Japan is liable contingently are reflected appropriately.

IV-7-5 Compensation scheme

With respect to the design and operation of the compensation scheme of a foreign holding company, etc. group, the authority in the mother country shall conduct appropriate supervision on a group basis to prevent excessive incentive to risk taking by an officer or employee.

On the other hand, the authority shall conduct monitoring on the design and operation of the compensation scheme of a first-type financial instruments firm which is a business unit in Japan in order to cooperate with the supervision appropriately by the authority in the mother country. In the case where there is likeliness, etc. to trigger excessive risk taking by an officer or employee in the business unit in Japan, the authority shall verify in depth a problem on risk control and make necessary responses such as expressing concerns actively to the authority in the home country.

(Note) IV-5-5 shall be referred for focus points in conducting such monitoring when needed.

IV-7-6 Supervisory methods and responses

- (1) The authority shall hold a hearing on business management, appropriateness of business, appropriateness and adequacy of capital, risk control system and compensation scheme of a first-type financial instruments firm which is a business unit in Japan based on the characters of the business of the business unit in Japan periodically and continuously when needed. The authority shall make an effort to share the recognition of issues, etc. at the entire group and a business unit in Japan at the opportunity to have a discussion directly with the group head quarter, etc. The authority shall use positively the framework of cooperation with overseas authorities, and hold a hearing in depth on the issues, etc. of the entire group or responses on the business unit in Japan recognized through such framework.
- (2) The authority shall require to make a report under Article 56-2.1 or 56-2.2 of the F.I. Act when needed, if it is determined that there is a problem on business management or internal control system, etc. for a first-type financial instruments firm which is a business unit in Japan through off-site monitoring under (1) above, the result of investigation and notification of accidents, etc. Further, if it is deemed necessary for improvement, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act.

V. Supervisory Valuation Items and Procedures (Second-Type Financial Instruments Business)

V-1 Business management (second-type financial instruments business)

The authority shall verify the business management of a financial instruments firm (limited to a person who carries out the second-type financial instruments business; in V, the same) with the following remarks

V-1-1 Officers of financial instruments firms

(1) Main focus points

Whether the followings are considered appropriately in the process of determination of the agenda for the selection of an officer of a financial instruments firm,.

- ① the candidate is not, or was not at the time of registration, subject to reasons for disqualification (as provided in (a) to (g) of Article 29-4.1 (2) of the F.I Act).
- ② the candidate does not violate the laws or regulations for financial instruments business or business incidental thereto or administrative disposition taken under the laws or regulations.
- ③ the candidate is not subject to the fact to harm the interests of investors in the operation of investment advisory and agent business or investment management business.
- ④ the candidate is not subject to commitment of an unlawful or grossly improper act of a particularly grave nature regarding the financial instruments business.

(2) Supervisory method and response

If an officer of a financial instruments firm has fallen under any of (a) to (g) of Article 29-4.1 (2) of the F.I. Act, has been found to have fallen under any of (a) to (g) of Article 29-4.1 (2) of the F.I. Act at the time of registration under Article 29 of the F.I. Act or has fallen under (6) or (8) to (10) of Article 52.1 of the F.I. Act, the authority shall consider the disposition of the issuance of an order to remove the officer under Article 52.2 of the F.I. Act.

The authority shall, in addition, make hearing in depth on the determination process, etc. for the selection agenda of an officer of such financial instruments firm, require to make a report under Article 56-2.1 of the F.I. Act when needed, and if a gross problem is found for the business management system of such firm and it is necessary and appropriate in the public interest or to protect investors, the authority shall consider dispositions such as the issuance of an order to improve business management.

V-1-2 Personnel structure sufficient to carry out financial instruments business accurately

(1) Main focus points

Whether a financial instruments firm is determined to ensure personnel structure sufficient to carry out financial instruments business (limited to the second-type financial instruments business; in V, the same) accurately from the following criteria for an officer or employee of a financial instruments firm.

- ① ensuring the employment of a person who has knowledge and experience sufficient to understand and perform focus points of business management provided by relevant regulations such as the F.I. Act or the Supervisory Guidelines and sufficient knowledge and experience regarding compliance and risk control necessary for fair and accurate carrying out of financial instruments business;
- ② being not a member of a crime group (including a person who was a member of a crime group in the past);
- ③ having no close relationship with a crime group.
- ④ having no experience of the violation of the laws or regulations for finance in Japan such as the F.I. Act or the laws or regulations in a foreign jurisdiction analogous thereto and being fined (including a criminal penalty under the laws or regulations analogous thereto in a foreign jurisdiction);
- ⑤ having no experience of the violation of the provisions of the Law on Prevention of Improper Act by Member of Crime Group (excluding the provisions of Article 32-2.7 of said Law) or the provisions under the laws or regulations analogous thereto in a foreign jurisdiction, or commitment of crimes under the Criminal Code or the Law on Violence, etc. Punishment and being fined (including a criminal penalty under the laws or regulations analogous thereto);
- ⑥ having no experience of being punished by a criminal penalty of imprisonment or severer (including criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto) (with remarks, particularly, of the case of crimes under Articles 246 to 250 of the

Criminal Code (fraudulence, fraudulence using a computer, breach of trust, quasi-fraudulence, threat, attempted crime therefor) shall be noted).

(2) Supervisory method and response

The criteria listed in ① to ⑤ above are part of criteria for comprehensive consideration to examine whether a financial instruments firm is determined to be a person who lacks personnel structure sufficient to carry out financial instruments business accurately, and a person is not judged to be unsuitable only if the specific criterion applies to the person. A financial instruments firm should, first of all, make an effort to ensure the appropriate personnel structure considering such criteria at the firm's responsibility.

Provided, That, if it is determined that such criteria is not considered fully in the selection process, etc. of an officer or employee of a financial instruments firm and it is determined to be necessary and appropriate in the public interest or to protect investors regarding the business management of the financial instruments firm, the authority shall hold a hearing in depth on the recognition by the financial instruments firm regarding such personnel structure and the selection process, etc. of an officer or employee, and require to make reports under Article 56-2.1 of the F.I. Act when needed.

If a gross problem is found for the business management system of such financial instruments firm and it is necessary and appropriate in the public interest or to protect investors as a result of collection of reports, the authority shall consider dispositions such as the issuance of an order to improve business management under Article 51 of the F.I. Act.

If it is determined that the financial instruments firm has not sufficient personnel structure to carry out financial instruments business accurately as a result of collection of reports, the authority shall consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

In the case of a financial instruments firm which is an individual, the authority shall verify the credentials of such individual in light of the above focus points, judge, equally as a juridical person, whether there are personnel resources sufficient to carry out financial instruments business accurately, and take necessary supervisory responses.

V-2 Appropriateness of business management (second-type financial instruments business)

V-2-1 Appropriateness of business management for deemed-securities sales business, etc.

V-2-1-1 Solicitation and explanation system

(1) Remarks on notice of delivery of securities and other necessary information

In the case where a deemed securities sales firm, etc. (which means a person who carries out as a business an act provided in (1) of Article 28.2 of the F.I. Act (hereinafter referred to as "proprietary offering firm") or a person who carries out as a business an act provided in (2) of said Article 28.2 (hereinafter referred to as "deemed securities sales firm") to which a person who carries out eligible institutional investor, etc. business subject to special provisions as provided in Article 63.2 of the F.I. Act is not applicable) fails to give a notice of the following matters to a customer in an appropriate manner, the provisions of Article 123.1 (8) of the F.I. Business Ordinance, "the state of being determined to have failed to furnish properly a customer with the state of delivery or other information necessary for the customer regarding purchase or sale or other type of transaction, etc. of a security conducted by the customer" shall apply to such case:

- ① matters required to be stated in a written statement concerning concluded transactions provided in Article 37-4.1 of the F.I. Act;
- ② matters required to be stated in a trading balance reports referred to in the items of Article 108.1 of F.I. Business Ordinance;
- ③ in addition to the matters referred to in ① and ②, matters regarding delivery of money or securities (excluding, in the case where delivery of money or securities is not made directly with a customer such as the case of delivery of money through a financial institution and the case of delivery of securities through book-transferred settlement, matters regarding such delivery).

(2) Remarks on explanation of important matters regarding switching of investment trust

In the case where a deemed securities sales firm, etc. fails to explain the following matters regarding switching and it is determined that the deemed securities sales firm, etc. fails to construct an internal control system such as preparation and keeping of internal records or

monitoring concerning the performance of explanation, "the state of failure, in soliciting to make a switch of investment trust beneficial interest certificate, etc. to give explanation of important matters regarding such switch to a customer" provided in Article 123.1 (9) of the F.I. Business Ordinance shall apply to such case.

- ① the types and particulars (name, nature, etc.) of an investment trust, etc.;
 - ② the state (approximate estimation of profit and loss) of the investment trust, etc. to be canceled;
 - ③ cost for the switch (such as cancellation fee and acquisition fee);
 - ④ matters regarding favorable treatment for the redemption and switch; and
 - ⑤ other matters to influence a customer's investment judgment, considering the nature of an investment trust, etc., a customer's needs, etc.
- (3) Remarks on explanatory obligation regarding funds

(5) and (6) of Article 2.2 of the F.I. Act define comprehensively interests related to collective investment schemes (funds) and its share. There could be, among persons who engage in sale, solicitation or public offering or private placement of such interests, a person who is not a securities firm, etc. and is not subject to the supervision of the authority before the enforcement of the F.I. Act or a person who handles funds which lack transparency or liquidity and is extremely difficult for investors to recognize or value the real state.

It shall be noted, based on the above, whether, when a deemed securities sales firm or proprietary offering firm handles such interests, such firm explains to investors about the summary of an association contract, etc., business which is currently carries out by the funds, or risks on interests based on such contract fully.

Particularly, if the multilevel marketing provided in Article 33.1 of the Law on Specific Commercial Transactions applies to the real state of the business, the authority shall make appropriate responses with coordination with relevant organizations such as the Ministry of Economy, Trade and Industry when needed with the remarks that appropriate explanation is given based on the F.I. Act or said Law. The authority shall, with the remarks that the Endless Money Chain Prevention Law is applicable to the real state of the business, and if the authority determines that there is such likeliness, the authority shall take appropriate responses such as providing information to relevant organizations such as the National Police Agency.

- (4) Remarks on sale of securitized products (ensuring traceability of securitized products)

There is a person who carries out as a business an act provided in Article 28.2 (2) of the F.I. Act for trust beneficial interests provided in (1) and (2) of Article 2.2 of the F.I. Act among deemed securities sales firms (hereinafter such person is referred to as "trust beneficial interest sales firm"). It is important to provide investors appropriately with information of underlying assets of trust beneficial interests which are handled by such persons and have the similar nature of securitized products. Remarks shall be made on the followings in accordance with self-regulatory rules of the Japan Securities Dealers Association "Rules for sale, etc. of securitized products" in the case where a trust beneficial interest sales firm makes sale, etc. of such trust beneficial interest.

Even if a trust beneficial interest sales firm assumes limited roles such as an intermediary of purchase or sale, it is desirable that the trust beneficial interest sales firm shall cooperate to the extent effectively possible considering that the trust beneficial interest sales firm is a contact point with investors.

- ① Whether a trust beneficial interest sales firm collects, and analyzes, information of the details and risks of the underlying assets to explain appropriately before the sale.
 - ② Whether a trust beneficial interest sales firm implements internal procedures and rules, and implements necessary system, to convey information of risks of the underlying assets and liquidity risks, etc. which is not reflected to rating without relying only on rating at the time of sale.
 - ③ Whether a trust beneficial interest sales firm implements internal procedures and rules, and implements necessary system, to convey information to enable a customer to trace the details and risks, etc. of the underlying assets if customers who are investors so desire.
 - ④ Whether a trust beneficial interest sales firm implements the system to value and compute theoretical prices, etc. and quote to customers smoothly and accurately even when it becomes difficult to specify market prices. Whether, in valuing and computing such theoretical prices, etc., arbitrary computation, etc. is made to give preference to a user of information for the specific and intentional use.
- (5) Supervisory method and response

With respect to the issues of the solicitation and explanatory system of a deemed securities

sales firm, etc. found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a deemed securities sales firm, etc. through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

V-2-1-2 Discretionary trading contract, etc.

- (1) Remarks on discretionary trading contract with affiliated foreign securities firms
Remarks shall be made on the followings for accepting a notification to enter into a contract under Article 16.1 (8) (b) of the Definition Ordinance.
 - ① Whether a division executing transactions under such contract and a division accepting and executing other customer orders shall be separated clearly.
 - ② Whether books and records for business are prepared by a method to show that such transactions are conducted under such contract.
- (2) Scope of specific consent of deemed securities sales firms, etc.
Specific consent under (b) and (c) of Article 123.1 (13) of the F.I. Business Ordinance shall include a consent to:
 - ① specific price (including the price fixed by a pre-determined method) or more (in the case of sale order), or specific price or less (in the case of purchase order);
 - ② price with appropriate range from the specific price as base value;
 - ③ a deemed securities sales firm, etc. which has been requested to make a best execution during one day trading determines the price at the firm's discretion (so called CD order); and
 - ④ the target price shall be the price determined by a method fixed in advance such as trading volume weighted average prices, etc. during one day (including so called "VWAP target order").
- (3) Supervisory method and response
With respect to the issues regarding the transactions referred to in (a) to (e) of Article 123.1 (13) of the F.I. Business Ordinance in respect of a deemed securities sales firm, etc. found through the daily supervisory operations and notification of accident, etc., the authority shall recognize voluntary improvement of a deemed securities sales firm, etc. through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed.
Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

V-2-1-3 Measures to prevent false recognition

- (1) Remarks on measures to prevent false recognition as other financial institution
The authority shall verify with the remarks whether a deemed securities sales firm, etc. explains to a customer concerning the followings fully to prevent customers from recognizing falsely the deemed securities sales firm, etc. as an other financial institution if the deemed securities sales firm, etc. carries out businesses in the principal business office or other business office located in the same building as such other financial institution:
 - ① the deemed securities sales firm, etc. is a different juridical person from the financial institution;
 - ② the fact that products or services related to securities related business provided by the deemed securities sales firm, etc. are not provided by the financial institution.
- (2) Supervisory method and response
With respect to the issues regarding measures to prevent false recognition of a deemed securities sales firm, etc. found through the daily supervisory operations and notification of accident, etc., the authority shall recognize voluntary improvement of a deemed securities sales firm, etc. through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

V-2-2 Appropriateness of businesses related to market derivatives business

V-2-2-1 Compliance system

It is important to ensure investors' trust on a market derivatives firm (which means a person who carries out as a business an act under Article 28.2 (3) of the F.I. Act; hereinafter the same), and further ensure investors' trust on a derivatives market that the market derivatives firm recognizes its role as a provider of a derivatives market fully and makes an effort to carry out sound and appropriate business management in strict compliance with the laws and regulations and various rules for businesses.

The authority shall make responses to such compliance systems of market derivatives firms by the focus points of system implementation and supervisory methods under III-2-1 in principle, as well as verify widely including the state of compliance with self-regulatory rules prepared by a self-regulatory organization.

In the case where a market derivatives firm accepts the deposit of money from customers for currency related market derivatives transaction, etc. (which means the acts referred to in (1) and (3) of Article 143.3 of the F.I. Business Ordinance; hereinafter the same), it shall be noted that securities, etc. control business is applicable to such act and such firm is required to register as the first-type financial instruments business. IV-3-3-1 shall apply to remarks and supervisory methods for the compliance system in the case where a market derivatives firm keeps money deposited by customers for currency related market derivatives transactions, etc. without depositing such money with an exchange.

V-2-2-2 Solicitation and explanation system

- (1) Remarks on advertisement, etc.
 - ① Whether a market derivatives firm makes representation to give false impression about a derivatives market or overseas derivatives market, etc. for which the market derivatives firm can act as a broker, etc.
 - ② In the case where, even if there is a loss-cut rules, losses may exceed the amount of customer margins or other guarantee money due to drastic movement of market prices, whether such fact is stated properly.
 - ③ Whether a market derivatives firm leads (or forced effectively) a customer to continue to participate to a seminar, etc. despite the fact that the customer has shown the intent not to desire to continue during the seminar, etc. It shall be noted that the provisions of Article 38 (5) of the F.I. Act (so called "prohibition of resolicitation") are applicable to such case.
- (2) Remarks on explanatory documents

"Outline of internal control" shall state concrete methods to handle a request for consultation and grievances from customers and internal auditing system.
- (3) Remarks on furnishing of warning statements regarding solicitation methods, etc. of market derivatives transactions

IV-3-3-2 (3) shall apply to remarks on warning made by a market derivatives firm to customers for conducting market derivatives transactions.
- (4) Remarks on furnishing of written statements prior to entering into contract
 - ① "Reason for likeliness that a loss exceeds the principal" as provided in Article 82 (4) (b) of the F.I. Business Ordinance shall, if there is a loss-cut rule but there is likeliness that a loss exceeds the amount of customer margins or other guarantee money as a result of abrupt movement of market prices, include such fact.
 - ② "Cause of termination for such financial instruments transaction contract" as provided in Article 82 (8) of the F.I. Business Ordinance shall include matters regarding loss-cut rules.
 - ③ "The types of, and computation method of the amount of, customer margins or other guarantee money which a customer is required to deposit regarding the derivatives transactions, etc." as provided in Article 93.1 (4) of the F.I. Business Ordinance shall include matters regarding minimum margins.

- ④ In the case of currency related transactions, "important terms and other basic matters regarding derivatives transactions" as provided in Article 93.1 (7) of the F.I. Business Ordinance shall include matters regarding methods to price financial instruments, etc and swap points. With respect to swap points, if there is a case that a customer receives and a case that a customer pays, and a case that as a result there is likeliness to cause losses, explanation to that effect shall be represented appropriately.
- (5) Remarks on explanatory obligation of a currency related market derivatives, etc. firm
 IV-3-3-2 (4) ⑥ shall apply to remarks on explanation in the case where a currency related market derivatives, etc. firm keeps money deposited by customers without depositing such money with an exchange. IV-3-3-2- (4) ⑦ shall apply to remarks on explanation regarding loss-cut transactions conducted by a currency related market derivatives, etc. firm
- (6) Supervisory method and response
 With respect to the issues of the solicitation and explanatory system of a market derivatives firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a market derivatives firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.
 Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

V-2-2-3 Discretionary trading contract, etc.

- (1) Remarks on discretionary trading contract with affiliated foreign financial instruments firms
 Remarks shall be made on the followings for accepting a notification to enter into a contract under Article 16.1 (8) (b) of the Definition Ordinance.
- ① Whether the division executing transactions under such contract shall be separated clearly from divisions accepting and executing other customer orders.
- ② Whether books and records for business are prepared by the method to show that such transactions are conducted under such contract.
- (2) Scope of specific consent of market derivatives firm
 Specific consent under (b) and (c) of Article 123.1 (13) of the F.I. Business Ordinance shall include a consent to:
- ① specific price or trade value (including the price and trade value fixed by a pre-determined method) or more, or specific price or trade value or less;
- ② price or trade value with appropriate range from a specific price or trade value as base value;
- ③ a market derivatives firm which has been requested to make a best execution during one day trading determines the price or trade value at the firm's discretion.
- (2) Supervisory method and response
 With respect to the issues regarding the transactions referred to in (a) to (e) of Article 123.1 (13) of the F.I. Business Ordinance in respect of a market derivatives firm found through the daily supervisory operations and notification of accident, etc., the authority shall, based on the above focus points, recognize voluntary improvement of business management of a market derivatives firm through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act when needed.
 Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

V-2-2-4 Risk control system related to currency related market derivatives transactions

With respect to currency related market derivatives transactions (which mean currency related market derivatives transactions as defined in Article 123.3 of the F.I. Business Ordinance) and currency related foreign market derivatives transactions (which mean currency related foreign market derivatives transactions as defined in Article 123.5 of the F.I. Business Ordinance) with a customer as a counterparty, (4) and (6) ② of IV-3-3-4 shall apply to the

implementation of a risk control system and carrying out business operations because the control of risks taken by a market derivatives firm is important.

V-2-3 Responses in the event of the receipt of information related to continuity problem

Even an individual is qualified for a financial instruments firm and only minimum capital (in the case of an individual, business guarantee money) are required as financial resources, and a certain financial instruments firm is not subject to monitoring of net assets or capital requirement ratio. It shall be noted that there is a likeliness of filing petition of commencement of bankruptcy proceedings, rehabilitation proceedings and reorganization proceedings (hereinafter referred to as "petition for bankruptcy, etc. proceedings commencement") by a financial instruments firm before the supervisory authority recognizes the accurate financial conditions of the financial instruments firm. Further, if the authority recognizes, for example, that a financial instruments firm becomes net capital deficiency and will likely be insolvent, the authority shall make an effort to confirm the fact in order to verify the necessity of responses fully to protect investors.

Based on the above, the supervisory authority shall make an effort to ensure the investor protection by making the following responses in addition to III-3-2 in such cases as the case of the recognition of net capital deficiency or likeliness of insolvency of a financial instruments firm, the case of the acceptance of notification of filing petition for bankruptcy, etc. proceedings commencement or the case of the recognition of the likeliness of filing petition for bankruptcy, etc. proceedings commencement.

Each local finance bureau shall make an effort to make responses according to the real state for each issue, and inform the Financial Services Agency of the fact situation for each of such issues and policies for responses and make coordination for responses.

- (1) Responses in the case of recognizing financial problems of financial instruments firm
 - ① The authority shall hold a hearing on the financial conditions of the firm concerned and the state of a contract with a customer (including the state of business currently carried out by the fund dealt by a deemed securities sales firm, etc. in the case of a deemed securities sales firm, etc. or the state of underlying assets of trust beneficial interest dealt by a trust beneficial interest sales firm in the case of a trust beneficial interest sales firm) and confirm the fact and encourages establishing the method to eliminate the likeliness of insolvency.
 - ② The authority shall, if a problem for the protection of investors has been found as a result of hearings, issue an order to make reports under Article 56-2.1 of the F.I. Act promptly for the fact and measures to solve the current state.
 - ③ The authority shall follow up the state of the progress of elimination measures after the acceptance of the report and, if improvement is not seen, consider responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act.
- (2) The case of recognizing information of filing petition for bankruptcy, etc. proceedings commencement
 - ① The authority shall confirm whether a notification under Article 50.1 (7) of the F.I. Act has been filed and require responses promptly when needed.
 - ② The authority shall recognize promptly, in addition to the fact situation for such issues, financial conditions of such financial instruments firm, the state of a contract with a customer (if there is money deposited by a customer, the concrete details thereof), responses to customers and policies, etc. of business continuity through an order to make reports under Article 56-2.1 of the F.I. Act.
 - ③ The authority shall follow-up the performance of the reports under ② above, and require due investigation of the policies of business continuity when needed. In such case, the authority shall consider responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act.
- (3) The case of recognizing information of filing petition of bankruptcy, etc. proceedings commencement by parent companies, etc.

If a person who could have material influence on business management of a financial instruments firm as a result of filing a petition for bankruptcy, etc. proceedings commencement (hereinafter in V-2-3, referred to as "parent company, etc.") has filed a petition for bankruptcy, etc. proceedings commencement, the authority shall promptly recognize financial conditions, trading relation with the parent company, etc., the state of a contract with a customer (if there is money deposited by a customer, the concrete details thereof) and policies, etc. regarding the business continuity based on the latest state of such parent company, etc. through the issuance of

- an order to the financial instruments firm to make reports under Article 56-2.1 of the F.I. Act.
- (4) The case of ruling of bankruptcy proceedings commencement
 - ① The authority shall recognize whether a notification under Article 50-2.1 (4) of the F.I. Act has been made and require prompt responses when needed.
 - ② If necessary for the investor protection, the authority shall make an effort to coordinate with a bankruptcy receiver.
 - (5) The case where a business office cannot be identified

If the authority notifies such fact publicly under Article 52.4 of the F.I. Act and such financial instruments firm fails to request after 30 days have passed since the day of such public notice, the authority shall revoke the registration of such financial instruments firm.
 - (6) other case where the authority received information which will likely develop into a problem of the continuity of a financial instruments firm or its parent company, etc.
 - ① The authority shall recognize promptly, in addition to the fact situation of such information, financial conditions, the state of a contract with a customer (if there is money deposited by a customer, the concrete details thereof) and policies, etc. regarding the business continuity in respect of the financial instruments firm through voluntary hearings.
 - ② In the case where such financial instruments firm refuses the hearing under the above ① or the authority determines that there is a concern on the business continuity of such financial instruments firm though hearings under the above ①, the authority shall recognize the fact situation promptly through the issuance of an order to make reports under Article 56-2.1 of the F.I. Act. If necessary for the investor protection, the authority shall consider responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act.

V-3 Procedures (second-type financial instruments business)

V-3-1 Registration

- (1) Items of examination of system

In examining whether the applicant is a person having personnel resources insufficient to carry out financial instruments business accurately as provided in Article 29-4.1 (1) (d) of the F.I. Act, the authority shall refer to the application for registration and the attachments and hold a hearing to confirm the followings.

 - ① Whether the applicant ensures the employment of officers and employees having sufficient knowledge and experience of the business and has organization and it is determined that the applicant is able to carry out such business appropriately in view of the followings:
 - (a) the management is qualified to carry out the business in a fair and accurate manner as a financial instruments firm in light of the career, ability, etc.;
 - (b) a full-time officer understands, and has knowledge and experience sufficient to perform, focus points of business management provided by relevant various regulations such as the F.I. Act and the Supervisory Guidelines, and has sufficient knowledge and experience of compliance and risk control necessary for fair and accurate carrying out the financial instruments business;
 - (c) organizational structure and personnel structure that personnel necessary for carrying out the proposed business accurately is allocated to each division, and persons responsible for internal control, etc. are allocated properly;
 - (d) whether a compliance division (person in charge) independent from sales divisions is established and a person having knowledge and experience is appointed as a person in charge.
 - (e) personnel required for the following system implementations is ensured for the proposed business:
 - a. preparation and keeping of books and records, reports, etc.;
 - b. disclosure;
 - c. risk control;
 - d. computer system control;
 - e. trade control, customer control;
 - f. examination of advertisement;
 - g. customer information control;
 - h. settlement of grievances and troubles; and
 - i. internal audit.
 - ② Whether the applicant has a person with inappropriate qualification for business

management among officers and employees as a result of comprehensive consideration of the following matters as a relationship with a crime group or a member of a crime group or other circumstances, which will likely result in the downfall of the credit of financial instruments business.

- (a) the applicant is a member of a crime group (including a person who was a member of a crime group in the past);
 - (b) the applicant has a close relationship with a crime group;
 - (c) the applicant has an experience of the violation of the regulations for finance in Japan such as the F.I. Act or the laws or regulations in a foreign jurisdiction analogous thereto and being fined (including a criminal penalty under the laws or regulations analogous thereto in a foreign jurisdiction);
 - (d) having no experience of the violation of the provisions of the Law on Prevention of Improper Act by Member of Crime Group (excluding the provisions of Article 32-2.7 of said Law) or the provisions under the laws or regulations analogous thereto in a foreign jurisdiction, or commitment of crimes under the Criminal Code or the Law on Violence, etc. Punishment and being fined (including a criminal penalty under the laws or regulations analogous thereto in a foreign jurisdiction);
 - (e) the applicant has an experience of being punished by a criminal penalty of imprisonment or severer (including criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto) (particularly, the case of crimes under Articles 246 to 250 of the Criminal Code (fraudulence, fraudulence using a computer, breach of trust, quasi-fraudulence, threat, attempted crime) shall be noted).
- (Note) In the case of a financial instruments firm who is an individual, the authority shall verify the qualification of such individual considering the matters referred to in the above ① and ②.

V-3-2 Registration of sales representative

- (1) Scope of sales representatives required to be registered
Persons required to be registered in the sales representative registry book under Article 64.1 of the F.I. Act among officers and employees engaging in in-house business (including reception desk operations) of a financial instruments firm (limited to a market derivatives firm; in V-3-2, the same) shall be persons engaging in any of the following business operations:
 - ① explanation of financial instruments transactions, etc. for the purpose of solicitation;
 - ② solicitation of financial instruments transactions, etc.;
 - ③ acceptance of orders;
 - ④ providing of information, etc. for the purpose of solicitation (excluding providing information related to back office operations and objective information based on the requests by customers); or
 - ⑤ a person who performs the act referred to in (3) of Article 64.1 of the F.I. Act.
- (2) Matters to be notified
It shall be noted that Article 64-4 (3) of the F.I. Act shall not apply in the case where a person has halted business operations as a sales representative temporarily for the reason of personnel reshuffle of a financial instruments firm.

V-3-3 Remarks on deposit, etc. of business guarantee money

- (1) If a financial instruments firm files, after making new deposit, such original deposit certificate in order to replace articles already deposited, the authority shall certify the issuance of the original deposit certificate by Form V-I for the original deposit certificate already accepted and kept and return the original deposit certificate already accepted and kept.
- (2) If a financial instruments firm has filed, after filing an application for substitute deposit or attached deposit with a deposit office, the original certificate of acceptance in order to make replacement deposit of redemption of securities already deposited by the financial instruments firm, the authority shall furnish a certificate of safe keeping in accordance with (5) below and return the master original deposit certificate already accepted and kept to the financial instruments firm.
- (3) If a financial instruments firm files an application for an approval of a change or cancel of a contract to be replaced with business guarantee money and the authority judges that the investor protection will not be harmed, the authority shall approve such application by a guarantee

contract change approval made on Form V-2 or a guarantee contract cancellation approval made on Form V-3.

- (4) A public notice for the recovery of business guarantee money shall be given by Form V-4.
- (5) A certificate of safe keeping made on Form V-5 shall be furnished in the case of the acceptance of the original deposit certificate.
- (6) The authority shall inform all applicants for registration that, if a business guarantee money is deposited in the form of national government bonds under Article 31-2.9 of the F.I. Act, negative prescription is completed after a certain period pursuant to the Law on National Government Bonds, and the deposit loses effectiveness.

VI. Supervisory Valuation Items and Procedures (Investment Management Business)

VI-1 Business management control (investment management business)

The authority shall verify the business management of a financial instruments firm (limited to a person who carries out investment management business; in VI, the same) with the following remarks.

VI-1-1 Officers of financial instruments firm

(1) Main focus points

Whether the followings are considered appropriately in the process of the determination of the agenda for the selection of an officer of a financial instruments firm.

- ① the candidate is not, or was not at the time of registration, subject to causes for disqualification (as provided in (a) to (g) of Article 29-4.1 (2) of the F.I. Act).
- ② the candidate does not violate the laws or regulations or administrative disposition taken under the laws or regulations for financial instruments business or business incidental thereto.
- ③ the candidate is not subject to the fact to harm the interests of investors in the operation of investment advisory and agent business or investment management business.
- ④ the candidate is not subject to commitment of an unlawful or grossly improper act of a particularly grave nature regarding the financial instruments business.

(2) Supervisory method and response

If an officer of a financial instruments firm has fallen under any of (a) to (g) of Article 29-4.1 (2) of the F.I. Act, has been found to have fallen under any of (a) to (g) of Article 29-4.1 (2) of the F.I. Act already at the time of registration under Article 29 of the F.I. Act or has fallen under (6) or (8) to (10) of Article 52.1 of the F.I. Act, the authority shall consider the disposition of the issuance of an order to remove the officer under Article 52.2 of the F.I. Act.

The authority shall hold a hearing in depth on the determination process, etc. for the selection agenda of an officer of such financial instruments firm, to made reports under Article 56-2.1 of the F.I. Act when needed, and further if a gross problem is found for the business management system of such firm and it is deemed necessary and appropriate in the public interest or to protect investors, the authority shall consider dispositions such as the issuance of an order to improve business management.

VI-1-2 Personnel structure sufficient to carry out financial instruments business accurately

(1) Main focus points

Whether a financial instruments firm ensures personnel structure sufficient to carry out financial instruments business (limited to investment management business; in VI, the same) accurately from the following criteria for an officer or employee of a financial instruments firm.

- ① ensuring the employment of a person who has knowledge and experience sufficient to understand and perform focus points of business management prescribed in relevant regulations such as the F.I. Act or the Supervisory Guidelines and sufficient knowledge and experience regarding compliance and risk control necessary for fair and accurate carrying out of financial instruments business;
- ② being not a member of a crime group (including a person who was a member of a crime group in the past);
- ③ having no close relationship with a crime group.
- ④ having no experience of the violation of laws or regulations for finance in Japan such as the

- F.I. Act or the laws or regulations in a foreign jurisdiction analogous thereto and being fined (including a criminal penalty under the laws or regulations analogous thereto in a foreign jurisdiction);
- ⑤ having no experience of the violation of the provisions of the Law on Prevention of Improper Act by Member of Crime Group (excluding the provisions of Article 32-2.7 of said Law) or the provisions under the laws or regulations analogous thereto in a foreign jurisdiction, or commitment of crimes under the Criminal Code or the Law on Violence, etc. Punishment and being fined (including a criminal penalty under the laws or regulations analogous thereto in a foreign jurisdiction);
 - ⑥ having no experience of being punished by a criminal penalty of imprisonment or severer (including criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto) (particularly, the case of crimes under Articles 246 to 250 of the Criminal Code (fraudulence, fraudulence using a computer, breach of trust, quasi-fraudulence, threat, attempted crime thereto) shall be noted).
- (2) Supervisory method and response

The criteria listed in ① to ⑤ above are part of criteria for comprehensive consideration to examine whether a financial instruments firm is determined to be a person who lacks personnel structure sufficient to carry out financial instruments business accurately and personnel structure is not judged suitable or unsuitable only if the specific criterion applies to the person. A financial instruments firm should, first of all, make an effort to ensure the appropriate personnel structure considering such criteria at the firm's responsibility.

Provided, That, if it is determined that such criteria is not considered fully in the selection process, etc. of an officer or employee of a financial instruments firm and it is determined to be necessary and appropriate in the public interest and to protect investors regarding the business management of a financial instruments firm, the authority shall hold a hearing in depth on the recognition by the financial instruments firm regarding the personnel structure and the selection process, etc. of an officer or employee, and require to make a report under Article 56-2.1 of the F.I. Act when needed.

If a gross problem is found for the business management system of such financial instruments firm as a result of collection of reports and it is deemed necessary and appropriate in the public interest or to protect investors, the authority shall consider the dispositions such as the issuance of an order to improve business management under Article 51 of the F.I. Act.

If further it is determined that the financial instruments firm has not sufficient personnel structure to carry out financial instruments business accurately as a result of collection of reports, the authority shall consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2 Appropriateness of businesses (investment management business)

VI-2-1 Compliance system

A financial instrument firm which plays an important role for investment management for investors owes trustee obligation to investors who have commissioned investment management, and is under faithful obligation, good care and good management obligation, segregation obligation, etc. under the F.I. Act. A financial instruments firm is required to carry out business in a sound and appropriate manner as a market player in a financial instruments market.

The authority shall make responses to such compliance systems of such financial instruments firms by focus points of system implementation and supervisory methods under III-2-1 in principle, as well as, in addition, verify widely including the state of compliance with self-regulatory rules.

VI-2-2 Appropriateness of businesses related to discretionary investment business

The authority shall verify the appropriateness of businesses of a discretionary investment firm (which means a person who carries out as a business the act referred to in Article 2.8 (12) of the F.I. Act based on a discretionary investment contract (which means a contract provided in Article 2.8 (12) (b) of the F.I. Act; hereinafter the same); hereinafter the same) with the following remarks.

VI-2-2-1 Business operation system

(1) Investment management and control of properties under investment management

The authority shall verify whether a discretionary investment firm makes investment management and control of properties under investment management appropriately with the following remarks. The followings shall be judged comprehensively based on the type and scale, etc. of business, and the failure of satisfaction of a part of valuation items does not necessarily mean inappropriate.

- ① Whether matters regarding an internal organization to make the decision of investment management policy (including concrete decision making process) are prescribed appropriately.
- ② Whether methods to invest properties under investment management (which means properties under investment management provided in Article 35.1 (15) of the F.I. Act; hereinafter the same) have been established concretely in the investment management division.
- ③ Whether a control system is implemented appropriately for transactions of securities, etc. between properties under investment management or between properties under investment management and properties belonging to the firm or a third party.
- ④ Whether, in the case where the whole or part of the authority to make investment management on behalf of an interest holder (which means an interest holder provided in Article 42.1 of the F.I. Act; hereinafter the same) under Article 42-3 of the F.I. Act is commissioned to an other person (including the case where a part of authority commissioned to such other person is commissioned further), selection criteria for, or communication methods with, the commissioned party are established appropriately. Whether a system to confirm the business operation ability or compliance with contractual provisions of a commissioned party continuously is implemented. Whether procedures for response in the case where there is a problem on the business operation ability of a commissioned party (such as the instruction to improve business, cancellation of further commissioning) are implemented clearly.
- ⑤ Whether matters regarding trading execution ability, compliance, credit risk and trading cost, etc. are identified appropriately as matters to be considered regarding the selection of a party with whom an order is placed or a party to which business is commissioned.
- ⑥ Whether a system to make a periodical verification by a division independent from investment management division has been implemented whether properties under investment management are managed appropriately in accordance with a discretionary investment contract and investment management guidelines, etc. including the appropriateness of the process for investment judgment (including whether records of investment management are kept).

(2) Execution of trades

In executing trades, the discretionary investment firm shall choose a trading type which will be most profitable to a customer, considering overall execution cost including trading prices. The authority shall verify execution conditions of trades by a discretionary investment firm in view of the current situation where trading types are increasingly diversified because of the development of financial technologies with the following remarks.

- ① Transactions at the average price (which mean transactions at the average price of multiple trades with different prices for each issue name and purchase or sale for transactions with the same trade date and delivery date).
 - (a) Separation of divisions
Whether a division in charge of investment judgment is separated from a division in charge of order placement. Whether, if organizational separation is difficult, the roles of both divisions are separated at the level of persons in charge at least.
 - (b) Verification of transaction
Whether a control division, etc. implements a system to verify a series of operation process, etc. for transactions at the average price appropriately.
 - (c) Disclosure to a customer and consent from a customer
Whether a discretionary investment firm conducts transactions at the average price after the disclosure to a customer and with a consent from a customer. Whether, in placing an order associated with the trade allocation related to multiple properties under investment management, the discretionary investment firm explains appropriately to a customer about the allocation standards at the time of partial execution.
- ② Transactions by package order
Whether, with respect to multiple properties under investment management, if a package order is placed for orders with the same issue names and the distinction of purchase or sale and the trade allocation is made to each of properties under investment management based on the allocation standards established in advance by a discretionary investment firm after the trades are summed separately for each issue name and each of purchase or sale, the implementation of

a system in accordance with the above ① is made in order to ensure the fairness among customers.

③ Transactions between properties under investment management

Whether the system that the control division, etc. can verify the transactions referred to in Article 129.1 (1) of the F.I. Business Ordinance (exclusion of application of prohibition of transactions between properties under investment management) appropriately is implemented.

"Case where it is determined necessary and reasonable" provided in Article 129.1 (1) (a) (iv) of the F.I. Business Ordinance shall mean the case where a discretionary investment firm ensures the formation of fair prices with the remarks on the exclusion of arbitrariness for inter-fund transactions by, for example, the following methods, etc. because of calling for ensuring the fairness among customers and best execution obligation or faithful ness obligation to customers.

- (a) transactions executed by a trader for an order of purchase or sale based on the investment judgment made by different fund managers (limited however, if there is no likeliness to influence on price formation considering the liquidity, etc. of such issue name and the same trader conducts transactions, to transactions for which such trader is not given discretion for execution);
 - (b) transactions for which the order for both purchase and sale is placed at market price before opening of a market (limited, however, to transactions which will unlikely influence on price formation considering liquidity, etc. of such issue name);
 - (c) transactions for which the orders for purchase and sale of which are placed at a considerable interval during a continuous session (limited, however, to transactions which will unlikely influence on price formation considering liquidity, etc. of such issue name);
 - (d) transactions, etc. related to index funds which are managed systematically based on the provisions of a contract or trust contract, etc. (limited, however, to transactions which will unlikely influence on price formation considering liquidity, etc. of such issue name);
 - (e) VWAP transactions or discretionary transactions, etc., the timing and prices, etc. of an order placement for individual transactions of which are left to a third party other than a discretionary investment firm (limited, however, to transactions which will unlikely influence on price formation considering liquidity, etc. of such issue name);
 - (f) futures transactions, etc. if it is difficult to avoid orders for the same contract because of the lack of the number of contracts (limited, however, to transactions which will unlikely influence on price formation considering liquidity, etc. of such contract);
- (3) Supervisory method and response

With respect to the issues of the business operation system of a discretionary investment firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a discretionary investment firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-2-2 Solicitation and explanation system

(1) Prohibition of exaggerated advertisement, etc.

① Whether a discretionary investment firm represents without showing the ground that its performance records or methods of investment management are extremely more excellent than other financial instruments firm.

② Whether, when a discretionary investment firm makes advertisement showing its performance records, the discretionary investment firm makes representation to give investors false impression by emphasizing a part of performance records. (Advertisement showing performance records must make appropriate and easy-to-understand representation in light of the investor protection. The authority shall make necessary confirmation, for example, whether the valuation method of investment management and reasons why the particular benchmark is used are explained clearly; whether the explanation that the performance records of investment management are records in the past and do not promise the future performance is made appropriately.)

- ③ Whether, when a discretionary investment firm makes representation showing the simulation of investment management, the discretionary investment firm makes representation to give investors false impression by imposing arbitrary preconditions. (Advertisement showing the simulation of investment management must make appropriate and easy-to-understand representation in light of the investor protection. The authority shall make necessary confirmation, for example, whether reasons for preconditions, etc. of the simulation are explained clearly; whether the explanation that the simulation is made based on certain precondition and do not promise the future performance is made appropriately.)
- (2) Remarks on furnishing of written statements prior to entering into contract
- ① If a discretionary investment firm carries out business other than discretionary investment business and collects remuneration for business related to discretionary investment business and fees, etc. for business other than the business related to discretionary investment business as a unit in one contract, "matters regarding considerations payable by a customer for such financial instruments transactions contract" as provided in Article 37-3.1 (4) of the F.I. Act shall clarify the distinction of the amount of remuneration for business related to discretionary investment and the amount of fees, etc. to business other than such business related to discretionary investment.
- ② "Methods of investment and types of transactions" as provided in Article 96.1 (1) of the F.I. Act shall include concrete types of methods of investment management (individual investment management, identical investment management (which means investment management of the same issue names of securities, etc. which are objects of investment management, the same distinction of sale or purchase and the same timing for multiple customer assets and kept individually for each customer by the same assets custodian; hereinafter the same), collective investment management (which means investment management of multiple customer assets collectively and kept collectively; hereinafter the same) and other types of concrete investment management methods) and, in the case of identical investment management or collective investment management, including the following matters according to the classification of the followings:
- (a) identical investment management:
- a. matters regarding an organization controlling properties under identical investment management;
- b. matters regarding allocation standards of properties acquired as a result of identical investment management;
- (b) collective investment management:
- a. customer attribute and types of customer assets under identical investment management and matters regarding standards for identical investment management;
- b. matters regarding an organization controlling properties under collective investment management;
- c. matters regarding allocation standards for properties acquired as a result of collective investment management;
- d. matters regarding valuation methods of properties under collective investment management and computation methods of each customer's share for properties under collective investment management (including the case of early-withdrawal from collective investment management).
- ③ "Matters regarding the scope of discretion of investment judgment and performance of investment" as provided in Article 96.1 (3) of the F.I. Business Ordinance shall include the trade name, address and the name of the representative of the persons referred to in the items of Article 16-12 of the F.I. Act Enforcement Order (hereinafter referred to as "further commissioned party") and the scope of types of further commissioning.
- (3) Remarks on furnishing of written statements concerning concluded transaction
- ① In the case of collective investment management, "details and amount of a customer's assets under a contract of discretionary investment" as provided in Article 107.1 (6) of the F.I. Business Ordinance shall include the total amount of properties under collective investment management and the ratio of such customer's properties to properties under collective investment management at the time of the commencement of collective investment management.
- ② "Methods of investment and types of transactions" as provided in Article 107.1 (8) of the F.I. Business Ordinance shall include types of concrete methods of investment management (individual investment management, identical investment management, collective investment management and other types of concrete investment management methods) and, in the case of

identical investment management or collective investment management, including the following matters according to the classification of the followings:

- (a) identical investment management:
 - a. matters regarding an organization controlling properties under identical investment management;
 - b. matters regarding allocation standards of properties acquired as a result of identical investment management;
- (b) collective investment management:
 - a. matters regarding the size of properties under collective investment management;
 - b. customer attributes and types of customer assets under collective investment management and matters regarding standards for collective investment management;
 - c. matters regarding an organization controlling properties under collective investment management;
 - d. matters regarding allocation standards for properties acquired as a result of collective investment management;
 - e. matters regarding valuation methods of properties under collective investment management and computation methods of each customer's share for properties under collective investment management (including the case of early-withdrawal from collective investment management).
- ③ "Methods of investment and types of transactions" as provided in Article 107.1 (8) of the F.I. Business Ordinance shall include "methods of investment and types of transactions" of the further commissioned party.
- (4) Supervisory method and response

With respect to the issues of the solicitation and explanatory system of a discretionary investment firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a discretionary investment firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-2-3 Measures to prevent the negative effects and faithful obligation

- (1) Remarks on carrying out more than one type of businesses

The authority shall verify the measures to prevent the negative effects according to the scale of business in the case where a discretionary investment firm carries out more than one type of businesses (which means types of businesses provided in Article 29-2.1 (5) of the F.I. Act) considering to ensure the appropriateness of business such as the prevention of conflicts of interest with the following remarks.

 - ① Whether an appropriate measures have been taken such as the implementation of an internal control system for the prevention of the negative effects according to the types of business as measures to prevent the negative effects between different types of businesses.
 - ② Whether, with respect to "undisclosed information" under Article 147 (2) of the F.I. Business Ordinance, effective information control is ensured by the implementation of information controlling measures, etc. through the appointment of a controller and implementation of rules for control, etc. and appropriate recognition and verification of the usage of such information and reviewing the information control method.
- (2) Remarks on prevention of conflicts of interest, etc. in investment management business

Whether appropriate measures have been taken such as the implementation of an internal control system for the prevention of the occurrence of the negative effects according to the types of business in order to prevent an act to harm interests of an interest holder for other business for the purpose of benefiting a specific interest holder.
- (3) Faithful obligation to interest holders

It shall be noted that, if a discretionary investment firm has caused damages to an interest holder because of the negligence of the firm such as a clerical mistake, etc. in the course of investment management of properties and does not compensate for such damages, there is a possibility of the violation of faithful obligation. This shall apply if a discretionary investment firm liable to an interest holder does not compensate damages of the interest holder despite that

a clerical mistake, etc. has occurred at a commissioned party.

(4) Supervisory method and response

With respect to the issues of measures to prevent the negative effects taken by a discretionary investment firm found through the daily supervisory operations or notification of accident, etc., because it will likely disbenefit an interest holder, and it is possible that the violation of laws or regulations, etc. such as the violation of faithful obligation or due care and good management obligation, the authority shall recognize voluntary improvement of business management of a discretionary investment firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-2-4 Measures to prevent agent or intermediary firm from violation of laws or regulations

It is important that a discretionary investment firm shall instruct an agent or intermediary firm (which means a person engaged in an agent or intermediary business (which means business provided in Article 2.8 (13) of the F.I. Act; hereinafter the same); hereinafter the same) to implement a customer control system to recognize attributes, etc. of customers and trading situation accurately and require such agent or intermediary firm thorough compliance after recognizing investment solicitation situation of the agent or intermediary firm in order to ensure appropriate investment solicitation according to customer attributes, etc. when the discretionary investment firm commissions the agent or intermediary firm to carry out business. The authority shall verify the system to prevent the violation of laws or regulations with the following remarks.

VI-2-2-4-1 Selection, etc. of agent or intermediary firm

(1) Remarks on selection of agent or intermediary firm

- ① Whether, in entering into a contract to commission agent or intermediary business, the discretionary investment firm considers fully positioning on business control and methods, etc. of the recognition of various risks and risk control associated with such commissioning.
- ② Whether a discretionary investment firm considers fully whether an agent or intermediary firm has credentials to carry out the business in a sound and appropriate manner. Whether, in the case where an agent or intermediary firm engages in other business particularly, the discretionary investment firm considers whether the engagement in such other business will unlikely harm not only the social reputation as an agent or intermediary firm, but also the reputation, etc. of a belonging firm (which means a discretionary investment firm entering into a discretionary investment contract for which the agent or intermediary firm acts as an agent or intermediary; in VI, the same) fully.

(2) Supervisory method and response

With respect to the issues regarding the selection of an agent or intermediary firm by a belonging firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a belonging firm, etc. through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-2-4-2 Measures to ensure appropriateness, etc. of business of agent or intermediary firm by a belonging firm

(1) Implementation of internal control system for supervision of agent or intermediary firm

- ① Whether a belonging firm implements a system to make appropriate supervision over an agent or intermediary firm such as the establishment of a division responsible for taking measures to ensure sound and appropriate business management of business related to agent or

- intermediary business or appointment of a person in charge (including business auditing system over an agent or intermediary firm).
- ② Whether a belonging firm implements an internal control system to verify whether measures to ensure the appropriateness, etc. of business related to business or intermediary business carried out by each agent or intermediary firm are taken appropriately by such division or person in charge.
 - (2) Remarks on measures for necessary and appropriate supervision, etc. over an agent or intermediary firm
 - ① Whether a belonging firm takes the following measures and perform monitoring of the performance of such measures in order to ensure sound and appropriate management of business related to agent or intermediary business carried out by an agent or intermediary firm.
 - (a) measures to hold training, or make instruction, concerning agent or intermediary business to ensure an agent or intermediary firm and its employees to comply with the laws and regulations, etc. for agent or intermediary business; and
 - (b) measures to make necessary and appropriate supervision, etc. over an agent or intermediary firm such as verifying whether the agent or intermediary firm carries out such agent or intermediary business accurately by means such as confirming periodically or when needed the real state of investment solicitation related to agent or intermediary business carried out by the agent or intermediary firm and other performance of business and require improvement when needed.
 - ② Whether a belonging firm implements a system such as reflecting the result, etc. of the above monitoring of appropriate business instruction by a belonging firm and appropriate business management of an agent or intermediary firm such as verification by a division responsible for the belonging firm and reporting to the management team when needed.
 - (3) Measures to cancel agent or intermediary business commissioning contract

Whether, if a problem has been found as a result of monitoring, etc. over an agent or intermediary firm, a system to take appropriate measures has been implemented such as the instruction to the agent or intermediary firm and cancellation of commissioning contract. Whether a system to ensure appropriate protection of customers has been implemented in the cancellation of a commissioning contract.
 - (4) Measures for settlement of grievances

Whether an agent or intermediary firm implements a system for responses to grievances such as the clarification of a contact place for customers' grievances for agent or intermediary business carried out by an agent or intermediary firm, establishment of a division for the settlement of grievances, preparation, etc. of procedures for processing grievances.
 - (5) Supervisory method and response

With respect to the issues regarding measures to ensure the appropriateness, etc. of business of an agent or intermediary firm by a belonging firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a belonging firm, etc. through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-2-5 Other remarks

- (1) Account for settlement of transactions
 - ① It shall be noted that a discretionary investment firm shall not use an account for the settlement of transactions in connection with the act under the proviso to Article 42-5 of the F.I. Act for transactions for house account.
 - ② It shall be noted that "using such account for the purpose other than such settlement of transactions" under Article 130.1 (11) of the F.I. Business Ordinance shall apply to using such settlement account for the purpose of placing a packaged order for transactions for investment based on discretionary investment judgment for customer account and transactions for house account.
- (2) Supervisory method and response

With respect to the issues regarding accounts for the settlement of transactions found through

the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a discretionary investment firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

(3) Interpretation of Article 2.8 (12) (b) of the F.I. Act

A discretionary investment contract provided in Article 2.8 (12) (b) of the F.I. Act shall not apply to contracts provided in (b) to (e) of Article 123.1 (13) of the F.I. Business Ordinance.

VI-2-3 Appropriateness of business related to investment trust management business, etc.

The authority shall verify the appropriateness of business of an investment trust management firm, etc. (which means a person carrying out investment trust management business, etc. (which means, among financial instruments businesses, a business to perform as a business an act referred to in (12) of Article 2.8 of the F.I. Act (excluding an act of establishing or directing a foreign investment trust directly from Japan) based on a contract provided in (a) of said (12) or an act provided in (14) of said Article 2.8); hereinafter the same) with the following remarks.

VI-2-3-1 Business operation system

(1) Investment management and control of properties under investment management

The authority shall verify with the following remarks whether an investment trust management firm, etc. makes investment management and control of properties under investment management appropriately. The followings shall be judged comprehensively based on the type and scale, etc. of business, and the failure of satisfaction of a part of valuation items does not necessary mean inappropriate.

- ① Whether matters regarding an internal organization responsible for the decision of investment management policies (including concrete decision making process) have been implemented appropriately.
- ② Whether concrete methods to invest properties under investment management have been established in the investment management division.
- ③ Whether a control system has been implemented appropriately for transactions of securities, etc. between properties under investment management or between properties under investment management and properties belonging to the firm or a third party.
- ④ Whether, in the case where the whole or part of the authority to make investment management on behalf of an interest holder under Article 42-3 of the F.I. Act is commissioned to an other person (including the case where a part of authority commissioned to such other person is commissioned further), selection standards or communication methods with the commissioned party are established appropriately. Whether a system to confirm the business operation ability and compliance with contractual provisions of a commissioned party continuously has been implemented. Whether procedures for response in the case where there is a problem on the business operation ability of a commissioned party (such as the instruction to improve business management, cancellation of further commissioning, etc.) are implemented clearly.
- ⑤ Whether matters regarding trading execution ability, compliance, credit risk and trading cost, etc. have been prescribed appropriately as matters to be considered regarding the selection of a party with whom an order is placed or a party to which business is commissioned.
- ⑥ Whether a system to make a periodical verification by a division independent from an investment management division has been implemented whether properties under investment management are invested appropriately in accordance with an investment trust agreement, investment management contract or investment management guidelines, etc. including the appropriateness of the process for investment judgment (including whether records of investment management are kept).

(2) Execution of trades

In executing trades, the investment trust management firm, etc. shall choose a trading type which will be most profitable to an interest holder, considering overall execution cost including trading prices. The authority shall verify, for example, execution conditions of trades by an

investment trust management firm, etc. in view of the current situation where trading types are increasingly diversified because of the development of financial technologies with the following remarks.

- ① Transactions at average prices (which mean transactions at the average price of multiple trades with different prices for each issue name and purchase or sale for transactions with the same trade date and delivery date).
 - (a) Separation of divisions
Whether a division in charge of investment judgment is separated from a division in charge of order placement. Whether, if organizational separation is difficult, the roles of both divisions are separated at the level of persons in charge at least.
 - (b) Verification of transaction
Whether a control division, etc. implements a system to verify a series of business process, etc. for transactions at the average price appropriately.
 - (c) Disclosure to interest holder and consent from interest holder (limited to the case of an investment management contract with an investment corporation)
Whether an investment trust management firm, etc. conducts transactions at the average price after the prior disclosure to an interest holder and with a consent from the interest holder. Whether, in placing an order associated with the trade allocation related to multiple properties under investment management, the investment trust management firm, etc. explains to an interest holder about the allocation standards at the time of partial execution appropriately.
- ② Transactions by package order
Whether, if a package order is placed for orders with the same issue names and the distinction of purchase or sale and the trades are summed for each issue name and each of purchase or sale and the trade allocation is made to each of properties under investment management based on the allocation standards established in advance by an investment trust management firm, etc. in respect of multiple properties under investment management, the implementation of a system in accordance with the above ① is made in view of ensuring the fairness among properties under investment management.
- ③ Transactions between properties under investment management
Whether a control division, etc. implements a system to verify the transaction referred to in Article 129.1 (1) of the F.I. Business Ordinance (exclusion from prohibition of transaction between properties under investment management) appropriately.
"Case where it is determined necessary and reasonable" provided in Article 129.1 (1) (a) (iv) of the F.I. Business Ordinance shall mean the case where an investment trust management firm, etc. ensures to form fair prices with the remarks on the exclusion of arbitrariness for inter-fund transactions by, for example, the following methods, etc. because of calling for ensuring the fairness among customers and best execution obligation or faithful ness obligation to customers.
 - (a) transactions executed by a trader for an order of purchase or sale based on the investment judgment made by different fund managers (limited however, if there is no likeliness to influence on price formation considering liquidity, etc. of such issue name and the same trader conducts transactions, to transactions for which such trader is not given discretion for execution);
 - (b) transactions to place orders for both purchase and sale at market prices before opening of a market (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such issue name);
 - (c) transactions the orders for purchase and sale of which are placed at a considerable interval during a continuous session (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such issue name);
 - (d) transactions, etc. related to index funds which are managed systematically based on the provisions of a contract or trust contract, etc. (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such issue name);
 - (e) VWAP transactions or discretionary transactions, etc. the timing and prices, etc. of an order placement for individual transactions of which are left to a third party other than an investment trust management firm, etc. (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such issue name);
 - (f) futures transactions, etc. if it is difficult to avoid orders for the same contracts because of the lack of the number of contracts (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such contracts);

(3) Supervisory method and response

With respect to the issues of the business operation system of an investment trust management firm, etc. found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an investment trust management firm, etc. through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-3-2 Solicitation and explanation system to beneficiaries, etc.

(1) Prohibition of exaggerated advertisement, etc.

① Whether an investment trust management firm, etc. represents without showing the ground that its performance records, types or methods of investment management are extremely more excellent than other financial instruments firms.

② Whether, when an investment trust management firm, etc. makes advertisement showing its performance records, the investment trust management firm, etc. makes representation to give investors false impression by emphasizing a part of performance records. (Advertisement showing performance records must make appropriate and easy-to-understand representation in light of the investor protection. The authority shall make necessary confirmation, for example, whether valuation method of investment management and reasons why the benchmark are used are explained clearly; whether an explanation that the performance records of investment management are records in the past and do not promise the future performance is made appropriately.)

③ Whether, when an investment trust management firm, etc. makes advertisement showing a simulation of investment management, the investment trust management firm, etc. makes representation to give investors false impression by imposing arbitrary preconditions. (Advertisement showing a simulation of investment management must make appropriate and easy-to-understand representation in light of the investor protection. The authority shall make necessary confirmation, for example, whether reasons for preconditions, etc. of the simulation are explained clearly; whether an explanation that the simulation is made based on certain precondition and do not promise the future performance is made appropriately.)

(2) Furnishing beneficiaries, etc. with written statements in the case of likeliness of conflicts of interest

In the case of furnishing a beneficiary with a written statement under Article 13.1 of the Investment Trust Law, the terms shall be interpreted as follows, and enquiries, etc. therefor shall be responded appropriately.

① Interpretation of "same type of properties"

"Same type of properties" provided in (1) and (2) of Article 13.1 of the Investment Trust Law and Article 19.1 of the Law on Investment Trust and Investment Corporation Enforcement Order (hereinafter referred to as "Investment Trust Law Enforcement Order") shall not include the case where, because restrictions are imposed on specific properties which are objects of investment under an investment trust agreement or an agreement of an investment corporation, such specific properties and specific properties which are objects of investment by other trusting person direction type investment trust or investment corporation do not compete.

② Interpretation of "commissioning of control"

"Commissioning of control" provided in of Article 19.3 (1) of the Investment Trust Law Enforcement Order means commissioning of renewal of a lease contract with a tenant of real estate and tenant controlling operations of receipt of rents, and shall not include commissioning of guarding or maintenance of building, etc. to an external professionals.

(3) Furnishing investment corporations, etc. with written statements in the likeliness of conflicts of interest

The above (2) shall apply to remarks on furnishing investment corporations, etc. with written statements under Article 203.2 of the Investment Trust Law.

(4) Supervisory method and response

With respect to the issues of the solicitation and explanation to beneficiaries found through

the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an investment trust management firm, etc. through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-3-3 Measures to prevent the negative effects and faithful obligation

(1) Remarks in the case of carrying out more than one type of businesses

The authority shall verify the measures to prevent the negative effects according to the scale of business in the case where an investment trust management firm, etc. carries out more than one type of businesses (which means types of businesses provided in Article 29-2.1 (5) of the F.I. Act) considering to ensure the appropriateness of business such as the prevention of conflicts of interest with the following remarks.

- ① Whether an appropriate measures have been taken such as the implementation of an internal control system for the prevention of the negative effects according to the types of business as measures to prevent the negative effects between different types of businesses.
- ② Whether, with respect to "undisclosed information" under Article 147 (2) of the F.I. Business Ordinance, effective information control is ensured by the implementation of information controlling measures, etc. such as the appointment of a controller and preparing rules for control, etc. and appropriate recognition and verification of the usage of such information and reviewing of information controlling methods.

(2) Remarks on prevention of conflicts of interest, etc. in investment management business

Whether appropriate measures have been taken such as the implementation of an internal control system for the prevention of the occurrence of the negative effects according to the types of business in order to prevent an act to harm interests of an interest holder for other business for the purpose of benefiting a specific interest holder.

(3) Faithful obligation to interest holders

It shall be noted that, if an investment trust management firm, etc. has caused damages to an interest holder because of the negligence of the firm such as a clerical mistake, etc. in the course of investment management of properties and does not compensate the interest holder for such damages, there is a possibility of the violation of faithful obligation. This shall apply if an investment trust management firm, etc. liable to an interest holder does not compensate the interest holder for damages despite that a clerical mistake, etc. has occurred at a commissioned party.

(4) Supervisory method and response

With respect to the issues of measures to prevent the negative effects taken by an investment trust management firm, etc. found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an investment trust management firm, etc. through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed because it will likely disbenefit an interest holder directly and there is a possibility that the violation of laws or regulations such as the violation of faithful obligation or due care and good management obligation. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-3-4 Business continuity management of investment trust management company (BCM)

(1) Significance and responses

It is very important for lives of people and national economy that an investment trust management firm performing important roles as an intermediary on financial instruments markets takes prompt recovery measures and makes appropriate responses such as ensuring the continuity of requisite minimum business in the event of the occurrence of crisis. It is

therefore necessary to establish business continuity management (BCM) and prepare manuals for crisis management (CM) during ordinary times. In this aspect, the authority shall verify the appropriateness according to the scale of the businesses with the following remarks in supervising an investment trust management firm.

(2) Main focus points

Whether the business continuity plan (BCP) enables early recovery from the damage and continuity of requisite minimum business to maintain the functioning of the financial system in the event of a terror, large scale disaster, etc. Whether an investment trust management firm implements the system of responding with coordination with a financial instruments firms association, securities firms, etc. and relevant organization, etc. Whether the plan responds to worldwide business disruption according to the state of business.

For example:

- ① Whether security measures for customer data, etc ready for disasters, etc. (computerization of paper information, back-up of computerized data files and programs, etc.) are taken.
- ② Whether security measures for computer system center, etc. (location of back-up centers according to necessity, ensuring personnel and communication network) are taken.
- ③ Whether such back-up systems avoid geographical concentration.
- ④ Whether an investment trust management company has a concrete plan of a target hour to recover important operations (aggregate calculation, communication (receipt of cancellation, informing of cancellation from a sales firm, aggregate calculation, informing to a trustee bank, etc.) associated with cancellation order of investment trust (including MMF and MRF), computation of base value, publication operation, recognition of existing positions, requisite minimum investment direction and cancellation operation for direct sales customers (reception operations such as receipt of cancellation from direct sales customers) and legal responses to carry out such operations (including preparation and filing of securities notification, etc.), control of organizations, system control and crisis control operations, etc. (including explanation to customers), from temporary measures (hand working, processing at a back-up center, etc.) in light of the maintenance of lives of customers, economic activities and functioning of financial instruments markets.
- ⑤ Whether the board of directors has approved the preparation and important review of the business continuity plan. Whether an independent entity such as the internal audit or external audit verifies the business continuity management.

(Reference) "Arrangement of Business Continuity Management of Financial Institution" (Bank of Japan July 2003)

"Principles of Business Continuity" (Joint Forum August 2006)
III-2-9 shall apply in principles.

VI-2-4 Appropriateness of business related to foreign investment trust management business

The authority shall verify the appropriateness of management business establishing or directing a foreign investment trust directly from Japan in accordance with VI-2-3 (excluding (2) and (3) of VI-2-3-2 and VI-2-3-4).

VI-2-5 Appropriateness of business related to fund management business

The authority shall verify the appropriateness of business of a fund management firm (which means a person carrying out fund management business (which means, among financial instruments businesses, a business to perform as a business the act referred to in Article 2.8 (15) of the F.I. Act; hereinafter the same); hereinafter the same) with the following remarks.

VI-2-5-1 Business operation system

(1) Investment management and control system of properties under investment management

The authority shall verify with the following remarks whether a fund management firm makes investment management and control of properties under investment management appropriately. The followings shall be judged comprehensively based on the type and scale of business, and the failure of satisfaction of a part of valuation items does not necessarily mean

inappropriate.

- ① Whether matters regarding an internal organization responsible for the decision of investment management policies (including concrete decision making process) have been prescribed appropriately.
- ② Whether concrete methods to invest properties under investment management have been established in the investment management division.
- ③ Whether a control system has been implemented appropriately for transactions of securities, etc. between properties under investment management or between properties under investment management and properties belonging to the firm or a third party.
- ④ Whether, in the case where the whole or part of the authority to make investment management on behalf of an interest holder under Article 42-3 of the F.I. Act is commissioned to an other person (including the case where a part of authority commissioned to such other person is commissioned further), selection criteria or communication methods with the commissioned party are established appropriately. Whether the system to confirm the business operation ability or compliance with contractual provisions of a commissioned party continuously is implemented. Whether procedures for response in the case where there is a problem on the business operation ability of a commissioned party (such as the instruction to improve business management and cancellation of further commissioning) are implemented clearly.
- ⑤ Whether matters regarding trading execution ability, compliance, credit risk and trading cost, etc. have been prescribed appropriately as matters to be considered regarding the selection of a party with whom an order is placed or a party to which business is commissioned.
- ⑥ Whether a system to make a periodical verification by a division independent from an investment management division has been implemented in respect of whether properties under investment management are invested appropriately in accordance with a capital contribution contract with the capital contributor and investment management guidelines, etc. as provided in Article 2.2 (5) of the F.I. Act including the appropriateness of the process for investment judgment (including whether records of investment management is kept).

(2) Execution of trades

In executing trades, the fund management firm shall choose a trading type which will be most profitable to a customer, considering the overall execution cost including trading prices. The authority shall verify execution conditions of trades by a fund management firm in view of the current situation where trading types are increasingly diversified because of the development of financial technologies with, for example, the following remarks.

- ① Transactions at average prices (which mean transactions at the average prices of multiple trades with different prices for each issue name and each of purchase or sale for transactions with the same trade date and delivery date).
 - (a) Separation of divisions
Whether a division in charge of investment judgment is separated from a division in charge of order placement. Whether, if organizational separation is difficult, the roles of both divisions are separated at the level of persons in charge at least.
 - (b) Verification of transaction
Whether a control division, etc. implements a system to verify a series of business process, etc. for transactions at the average price appropriately.
 - (c) Disclosure to a customer and consent from a customer
Whether a fund management firm conducts transactions at the average price after the prior disclosure to a customer and with a consent from the customer. Whether, in placing an order associated with the trade allocation related to multiple properties under investment management, the fund management firm explains to a customer about the allocation standards at the time of partial execution appropriately.
- ② Transactions by package order
Whether, if a package order is placed for orders with the same issue names and the same distinction of purchase or sale and the trades are summed for each issue name and each distinction of purchase or sale and the trade allocation is made to each of properties under investment management based on the allocation standards established in advance by a financial instruments firm in respect of multiple properties under investment management, the implementation of a system in accordance with the above ① is made in view of ensuring the fairness among customers.
- ③ Transactions between properties under investment management
Whether a control division, etc. implements a system to verify the transaction referred to in

Article 129.1 (1) of the F.I Business Ordinance (exclusion from prohibition of transaction between properties under investment management) appropriately.

"Case where it is determined necessary and reasonable" provided in Article 129.1 (1) (a) (iv) of the F.I Business Ordinance shall mean the case where a fund management firm enhances to form fair prices with the remarks on the exclusion of arbitrariness for inter-fund transactions by, for example, the following methods, etc. because of calling for ensuring the fairness among customers and best execution obligation or faithful ness obligation to customers.

- (a) transactions executed by a trader for an order of purchase or sale based on the investment judgment made by different fund managers (limited however, if there is no likeliness to influence on price formation considering liquidity, etc. of such issue name and the same trader conducts transactions, to transactions for which such trader is not given discretion for execution);
 - (b) transactions to place an order for both purchase and sale at market prices before opening of a market (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such issue name);
 - (c) transactions the orders for purchase and sale of which are placed at a considerable interval during a continuous session (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such issue name);
 - (d) transactions, etc. related to index funds which are managed systematically based on the provisions of a contract or trust contract, etc. (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such issue name);
 - (e) VWAP transactions or discretionary transactions, etc. the timing and prices, etc. of an order placement for individual transactions of which are left to a third party other than a fund management firm (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such issue name);
 - (f) futures transactions, etc. if it is difficult to avoid orders for the same contract because of the lack of the number of contracts (limited, however, to transactions which have no likeliness to influence on price formation considering liquidity, etc. of such contracts);
- (3) Supervisory method and response

With respect to the issues of the business operation system of a fund management firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a fund management firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-5-2 Solicitation and explanation system

- (1) Prohibition of exaggerated advertisement, etc.
 - ① Whether a fund management firm represents without showing the ground that its performance records, types or methods of investment management are extremely more excellent than other financial instruments firm.
 - ② Whether, when a fund management firm makes advertisement showing its performance records, the fund management firm makes representation to give investors false impression by emphasizing a part of performance records. (Advertisement showing performance records must make appropriate and easy-to-understand representation in light of the investor protection. The authority shall make necessary confirmation, for example, whether valuation method of investment management and reasons why the benchmark is used are explained clearly; whether an explanation that the performance records of investment management are records in the past and do not promise the future performance is made appropriately.)
 - ③ Whether, when a fund management firm makes advertisement showing the simulation of investment management, the fund management firm makes representation to give investors false impression by imposing arbitrary preconditions. (Advertisement showing the simulation of investment management must make appropriate and easy-to-understand representation in light of the investor protection. The authority shall make necessary confirmation, for example, whether reasons for preconditions, etc. of the simulation are explained clearly; whether an explanation that the simulation is made based on certain precondition and do not promise the

- future performance are explained appropriately.)
- (2) Remarks on furnishing written statements prior to entering into a contract
In the case where a fund management firm engages in business other than business related to investment management business (other business engagement) and collects remuneration for investment management business and fees, etc. for the other business engagement together as one unit in the same contract, the fund management firm shall clarify the distinction of the amount of remuneration for investment management business and the amount of fees, etc. for other business engagement in respect of "matters regarding considerations payable by a customer regarding such financial instruments transactions contract" under Article 37-3.1 (4) of the F.I. Act.
 - (3) Supervisory method and response
With respect to the issues of the solicitation and explanation system of a fund management firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a fund management firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-5-3 Measures to prevent the negative effects and faithful obligation

- (1) Remarks in the case of carrying out more than one type of businesses
The authority shall verify the measures to prevent the negative effects according to the scale of business in the case where a fund management firm carries out more than one type of businesses (which means types of businesses provided in Article 29-2.1 (5) of the F.I. Act) considering to ensure the appropriateness of business such as the prevention of conflicts of interest with the following remarks.
 - ① Whether appropriate measures have been taken such as the implementation of an internal control system for the prevention of the occurrence of the negative effects according to the types of business as measures to prevent the negative effects between different types of businesses.
 - ② Whether, with respect to "undisclosed information" under Article 147 (2) of the F.I. Business Ordinance, effective information control is ensured by the implementation of information controlling measures, etc. by means such as the appointment of a controller and implementation of rules for control and by means such as appropriate recognition and verification of the usage of such information and reviewing of its information control method.
- (2) Remarks on prevention of conflicts of interest, etc. in investment management business
Whether appropriate measures have been taken such as the implementation of an internal control system for the prevention of the occurrence of the negative effects according to the types of business in order to prevent an act, etc. to harm interests of an interest holder for other business for the purpose of benefiting a specific interest holder.
- (3) Faithful obligation to interest holders
It shall be noted that, if a fund management firm has caused damages to an interest holder because of the negligence of the firm such as a clerical mistake, etc. in the course of investment management of properties and does not compensate the interest holder for such damages, there is a possibility of the violation of faithful obligation. This shall apply if a clerical mistake, etc. has occurred at a commissioned party and a fund management firm liable to an interest holder does not compensate the interest holder for damages.
- (4) Supervisory method and response
With respect to the issues of measures to prevent the negative effects taken by a fund management firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a fund management firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed because such negative effects will likely disbenefit interest holder or properties under investment management directly and, in some cases, cause violation of laws or regulations such as the violation of faithful obligation and due care and the violation of good management obligations. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to

improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-6 Particular remarks on real estate related fund management firm

Real estate related funds including real estate investment trusts are financial instruments with a structure to invest funds of wide range of investors including individual investors in real estate (including financial instruments the underlying assets of which is real estate; in VI, the same) as a principal investment object. The purpose of the supervision over a financial instruments firm carrying out investment management of such financial instruments (hereinafter referred to as "real estate related fund management firm") shall be to ensure the appropriateness of, among others, the performance of due process, information disclosure, the prevention of conflicts of interest transaction, etc. which are requisite of the investor protection and the fulfillment of the appropriate price formation function in real estate market, so as to require to carry out the duties faithfully to investors and carry out the duties with due care and good management.

Supervisory focus points and supervisory methods and responses provided by VI-2-2 to VI-2-5 shall apply to the supervision over a real estate related fund management firm according to the type of investment management and, additionally, remarks shall be made on the followings. The authority shall verify with particular remarks concerning the firm because it is necessary for such firm to carry out the duties in a sound and appropriate manner after full understanding and recognition of characteristics, different from other instruments, of real estate and risks associated with characteristics at the time of investment. The authority shall conduct such supervision with remarks that such supervision does not intend to influence on individual real estate price.

VI-2-6-1 System to comply with laws and regulations

The authority shall make responses to such compliance systems of such real estate related fund management firm by focus points of system implementation and supervisory methods under III-2-1 in principle, as well as, in addition, verify widely including measures to prevent conflicts of interest which is unique to business of real estate related fund.

VI-2-6-2 Internal control system

A real estate related fund management firm is subject to good care and good management obligation and faithful obligation, and therefore is required to construct a sufficient compliance system and risk control system. The management team of a real estate related fund management firm is required to prepare various rules for thorough compliance and various risk control rules to analyze and value risks for real estate investment and enable appropriate risk control, and confirm the compliance with such rules.

It shall be noted that the management team shall implement an internal control system including due diligence system based on characteristics of real estate is required.

VI-2-6-3 Valuation items for business of real estate related fund management firm

(1) Valuation items for due diligence system at the time of acquisition and sale of real estate

The authority shall verify the appropriateness of due diligence of real estate with the following remarks because due diligence is an important work to recognize appropriate investment value of real estate.

The management team shall be aware of, and maintain the conditions to enable any time through internal audit recognition of, the state of the performance of measures and the effectiveness of the examination function to ensure the appropriateness of due diligence.

- ① Whether the estimate for various renovation and renewal cost, etc. is examined appropriately and reflected to the valuation of real estate considering the scale of influence on the future cash flow.
- ② The DCF method seeks the value based on cash flow and is typical and effective method to value real estate. The DCF method, however, may become less clear because of many preconditions based on outlook. Whether, in using the DCF method therefore, the real estate fund manager makes necessary confirmation of the followings and prepare records of confirmation.

- (a) reasonability of applicable values (particularly those based on outlook) and grounds for judgment;
 - (b) reasonability of the entire scenario and grounds for judgment;
 - (c) comparison and balancing between the result from application of the DCF method and the result from application of other methods.
- ③ Remarks shall be made on the followings for commissioning the preparation of an engineering report (hereinafter referred to as "ER") and appraisal report and the receipt thereof.
- (a) Whether an ER preparation firm and real estate appraisal firm are selected from among third parties through selection, etc. based on objective criteria.
 - (b) Whether a real estate related fund management firm provides an ER preparation firm and real estate appraisal firm with necessary information, etc. in commissioning ER and real estate appraisal; whether such providing information, etc. is controlled appropriately.
 - (c) Whether a real estate related fund management firm makes necessary verification about the state of reflection of information, etc. under the above (b) and makes confirmation in view of the followings at the time of the receipt of ER the preparation of which was commissioned.
 - a. Whether, with respect to the examination of soil pollution and harmful materials, necessary examination has been made and the examination result is guaranteed by objective grounds.
 - b. Whether, in the case of estimating various renovation or renewal cost, etc., a real estate related fund management firm confirms the details of renovation and the grounds for the computation for individual parts of a building.
 - c. Whether a real estate related fund management firm makes necessary verification about the illegality of the object covering not only laws but also regulations of local governments such as a district plan.
 - (d) A real estate related fund management firm makes necessary verification about the state of reflection of the information, etc. under the above (b) and confirms it in view of the followings at the time of the receipt of an appraisal report from an appraiser to whom valuation has been commissioned.
 - a. Whether the idea of ER has been considered or reflected; whether the reason and grounds have been confirmed for matters which have not been reflected.
 - b. Whether, in the case of using the DCF method, the reasonability is verified after the estimation of the future revenue and expense and operating rate, etc. based on objective data; whether the reasonability of the level is verified for the estimate of discount rates and terminal rate which are preconditions in the same manner.
 - c. Whether necessary examinations have been made for items which may influence on the liquidity of real estate and cash flow born from the real estate.
 - (e) Whether, in computing the price of acquisition or sale based on the result of due diligence, the real estate related fund management firm verifies the reasonability of used values, etc. and keeps the records of the grounds in the case where the contents of an ER and appraisal reports are not used.
- (2) Conflicts of interest prevention system

The management team shall recognize risks of causing conflicts of interest and, after recognizing not only persons concerned provided by the laws or regulations but also counterparties with which conflicts of interest may occur, construct a control system appropriate for transactions with such persons, and verify for example with the following remarks.

- ① Whether, in the case where there is a policy that the trade price for acquisition of the object is fair if such price is the value computed by adding a certain range to or reducing it from the appraisal value as a standard, a system to review periodically is implemented for the appropriateness of the range so added or reduced in view of market conditions.
Whether such policy (in the case of reviewing such policy, including the reason therefor) provides for the implementation of a system to publish (in the case of a privately placed fund, a notice to a person who entered into a contract) appropriately.
- ② Whether a real estate related fund management firm implements a system to make unified control of real estate for sale information (including the state of negotiation, etc. for purchase or sale) and a person in charge of compliance is able to control the state of negotiation, etc. for purchase or sale in order to prevent conflicts of interest.
- ③ Whether, if a real estate related fund cannot acquire real estate owned by a third party at the time that the seller desires and uses warehousing function, the real estate related fund management firm recognizes the likeliness of risks of conflicts of interest and makes

- clarification of negotiation and dividing roles and due diligence appropriately.
- (3) Remarks in the case where the same real estate related fund management firm is commissioned for investment management of real estate related properties from multiple funds
- It shall be noted that, in the case where the real estate related fund management firm is commissioned for investment management from multiple funds, whether the real estate related fund management firm takes measures to avoid competition in acquisition among funds under investment management at the time of the acquisition of purchase or sale information and whether a system to make independent decision for each fund is implemented.
- (4) Others
- ① The scope of "acquisition of real estate", etc.
- "Acquisition of real estate" provided in Article 193.1 (3) of the Investment Trust Law does not include housing land development or construction of buildings by an investment corporation, but includes becoming an order placing person for a service contract of housing land development or construction of buildings by an investment corporation. The same shall apply to the idea of the scope of primary business (investment in real estate trust beneficial interest) and notification business (investment in real estate) of a real estate related fund management firm.
- It shall be noted, however, that, in the case where becoming an order placing person for a service contract of housing land development or construction of buildings is not suitable to an investment corporation such as the following cases, such act is not included in "acquisition of real estate".
- (a) the case where large renovation or repairing work, etc. causes requiring tenants to exit for a certain period and fluctuation of cash flow in such case influences on the entire portfolio too much;
- (b) the case where, if an investment corporation buys a vacant site and constructs a new building, the entire portfolio is excessively influenced considering that it imposes various risks related to the development of real estate (development risk, approval risk, completion risk, tenant risk, price movement risk, interest rate movement risk during the development and large natural disaster risk, etc.) on investors is an investment which does not bear cash flow.
- ② Forward commitment, etc. by investment corporation
- An investment corporation shall note the followings if the investment corporation makes forward commitment, etc. (which means a contract of purchase and sale with forward dating, which provides that the settlement and delivery is made after at least one month has passed since entering into the contract or a contract similar thereto; hereinafter in ②, the same). The same shall apply in the case of declaration of intent, etc. of purchase with forward dating which binds transactions effectively:
- (a) Whether influence on financial conditions of the investment corporation is clarified such as publishing the conditions for cancellation appropriately in the case where forward commitment, etc. cannot be performed.
- (b) Whether a real estate related fund management firm prepare rules for the acquisition amount of an object subject to forward commitment, etc. and the limit of the period from entering into a contract until the delivery of an object and method to finance settlement money after considering circumstances such as the market conditions, financing conditions and individual circumstances of an investment corporation and complies such rules. Whether a listed investment corporation particularly implements a system to consider carefully a forward commitment, etc. which requires excessive cancellation penalty charges compared with resources for dividend payment based on requirements for delisting.
- (c) Whether a real estate related fund management firm publishes the result of continuous appraisal, etc. of an object (if the object is uncompleted building and not available for appraisal, the result of price examination) together with continuous appraisals, etc. of the object held considering that an object for which forward commitment, etc. has been made is accounted off-balance until the settlement and price movement risk of such object belongs to the investment corporation during such period.
- ③ Issuance of subordinated investment corporation debt security by investment corporation
- If an investment corporation issues subordinated investment corporation debt securities, the investment corporation shall consider carefully the necessity of financing by such issuance or reasonability, etc. of issuing conditions based on likeliness that such issuance may harm the interest of investors depending on issuing conditions (such as yield) with remarks whether such information is published appropriately.

④ Outsourcing control system

A real estate related fund management firm is commissioned by such fund to make investment management and outsources a part of business to various firms such as ER firm, appraiser, trust bank, property management firm and building management firm. Accordingly, appropriate supervision over such outsourcees is requisite for a management firm to fulfill faithfulness obligation, etc. It is necessary to construct an appropriate outsourcing control system by means such as enhancing various reports receiving from outsourcees directly or through trust banks, etc. and performing effective monitoring periodically after preparing various rules or criteria including selection criteria for outsourcees in order to make the supervision effective. It shall be noted that the clarification of dividing roles between the management firm and the outsourcee is requisite for an appropriate outsourcing control system.

⑤ Capital contribution, etc. to development SPC

Whether analysis and risk control is performed appropriately for various risk (such as development risk, approval risk, completion risk, tenant risk, price movement risk, interest rate movement risk during the development and large natural disaster risk, etc.) associated with development of real estate. Whether business progress is monitored appropriately. Considering that capital contribution to such development SPC by a person other than funds specialized in capital contribution in development type project does not bear cash flow immediately, it shall be noted that the entire portfolio shall be kept from excessive exposure.

⑥ Information control system

It is necessary for a real estate related fund management firm managing a listed real estate investment corporation to control information appropriately after taking measures to keep secrecy of information before decision making, before transaction and before disclosure of investment judgment, etc. (decision making, etc. related to acquisition and sale) based on assets investment management commissioning contract, etc.

⑦ Remarks on investment in real estate for house account

It shall be noted that a real estate related fund management firm which makes real estate investment (including investment in real estate trust beneficial interest and association interest) for the house account and an approval for business as other engagement is required to conduct transactions, for example, for the purpose of resale, etc. for the amount exceeding the amount of net assets frequently and continuously in some cases.

The authority shall confirm that the risk of loss is appropriate considering the amount of net assets and that a system to control the risk of loss is implemented fully, in approving such business.

(5) Supervisory method and response

With respect to the issues of the above valuation items found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a real estate related fund management firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-2-7 Appropriateness of business of investment corporation

VI-2-7-1 Matters regarding organizational management, etc. of investment corporation

(1) Remarks on management of the board of directors

- ① Whether the board of directors has lost substances with remarks on, for example, no attendance of officers or resolution by so called rotation.
- ② Whether an asset management firm provides appropriate information and full explanation in order to ensure the effectiveness of deliberation at the board of directors.
- ③ Whether the duties are divided clearly according to the business commissioned to a general operator and an asset management firm at the board of directors and confirmation is made whether fees are fixed appropriately according to such dividing.

(2) Role of executive officer

Whether an executive officer recognizes matters to be resolved at the board of directors and

make certain to refer such matters to the board of directors.

(3) Role of supervisory officer

Whether a supervisory officer recognizes that the *raison d'être* is to supervise executive officers as provided in Article 111.1 of the Investment Trust Law, and not only attends to the board of directors but also supervises business operation of executive officers.

Whether a supervisory officer requires executive officers, general operators, asset management firms and asset custody firms to make a report according to the situation or makes necessary examination.

(4) Supervisory method and response

With respect to the issues of the organizational management, etc. found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an investment corporation through holding hearings in depth or collection of reports under Article 213 of the Investment Trust Law when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 214 of the Investment Trust Law, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of revocation of registration under Article 216.1 of the Investment Trust Law.

VI-2-8 Other remarks

VI-2-8-1 Remarks on Investment Trust Law and Trust Law

The followings are remarks on the laws and regulations applicable to investment trust entrusted before the enforcement of the New Trust Law. The followings are definitions of terms under VI-2-8-1.

- ① "New Trust Law": Trust Law (Law No. 108 of 2006)
- ② "Trust Law Consolidation Law": Law on Consolidation, etc. of Relevant Laws Associated with Enforcement of the Trust Law (Law No. 109 of 2006)
- ③ "New Investment Trust Law": the Investment Trust Law after the amendment under Article 5 of the Amendment Law
- ④ "Old Investment Trust Law": Trust Law before the amendment under Article 25 of the Trust Law Consolidation Law
- ⑤ "New Law trust": investment trust entrusted after the enforcement of New Investment Trust Law and New Trust Law
- ⑥ "Old Law trust": investment trusts entrusted before the enforcement of New Investment Trust Law and New Trust Law

An Old Law trust may be replaced with a New Law trust under Article 3 or 26.1 of the Trust Law Consolidation Law. If such replacement is not made however, the provisions of Article 2 of the Trust Law Consolidation Law are applicable. As a result, with respect to the Old Law trust, the authority shall note that methods of public notice regarding beneficial interest directory, merger of a trust and investment trust, the system of which were consolidated by the New Trust Law and the Trust Law Consolidated Law are replaced with the methods of public notice to a trusting person and the provisions of the New Investment Trust Law, etc. regarding written resolution for investment trust agreement amendment, etc. and request, etc. for buying back by a beneficiary who has opposed at such written resolution (Articles 4.2 (17), 6.7, 16 (2), 17, 18, 20, 25, 49.2 (18), 50.4, Articles 16 (2), 17 and 18 which are applied *mutatis mutandis* under Article 54.1, Articles 16 (2), 17, 20 and 25 which are applied *mutatis mutandis* under Articles 57 and 59 of the New Investment Trust Law and penal rules regarding these provisions and the F.I. Act Enforcement Order and Cabinet Office Ordinances) do not apply to the Old Law Trust, and relevant Old Investment Trust Law, F.I. Act Enforcement Order and Cabinet Office Ordinances before the amendment to such provisions are applicable.

VI-2-8-2 Remarks on trusting person non discretionary type investment trust

VI-2-3-2 (2) shall apply to remarks on furnishing of a written statement to a beneficiary, etc. under Article 13.1 of the Investment Trust Law which is applied *mutatis mutandis* under Article 54.1 of said Law.

VI-2-8-3 Remarks on merger of investment corporation

It shall be noted that, in the case where an absorption merger is made and such absorption merger involves the payment of money such as merger ratio adjusted money or divided cover money, etc. (hereinafter referred to as "merger payment money") for merger ratio adjustment, etc. in order to compute an investment unit of a corporation which continues to exist after absorption-merger paid to investors of a corporation which has extinguished as a result of an absorption merger, the amount of merger payment money or its computation methods and matters regarding the amount of merger payment money allocated in the proportion of the number of units of investment units owned by an investor of a corporation which has extinguished as a result of an absorption merger shall be included as the matters referred to in Article 147.1 (2) of the Investment Trust Law.

VI-2-9 Remarks on supervision over firms which are not members of association, etc.

(1) Main focus points

- ① Whether a financial instruments firm which is not a member of a financial instruments firms association or a member or trading participant of a financial instruments exchange (hereinafter in VI-2-9, referred to as "firm which is not a member of an association, etc.") implements internal rules appropriately considering the association, etc. rules.
- ② Whether implementation of a system to ensure appropriate compliance with internal rules (such as informing all officers and employees and verification of their compliance with internal rules) is ensured.
- ③ Whether it is ruled that, when there has been an amendment, etc. to association, etc. rules, internal rules are reviewed immediately after, and according to, the amendment, etc.

(2) Supervisory method and response

- ① If a firm which is not a member of an association, etc. fails to prepare, and is not expected to prepare voluntarily, internal rules for which association, etc. rules have been taken into consideration, the authority shall order the firm to prepare appropriate internal rules under Article 56-4.2 of the F.I. Act. In this case, the authority shall, when there has been an amendment, etc. to association, etc. rules, require the firm to review the internal rules immediately after, and according to, the amendment, etc.
- ② If internal rules of a firm which is not a member of an association, etc. is required to be reviewed in light of association, etc. rules and voluntary reviewing cannot be expected, the authority shall order the firm to make an amendment to internal rules under Article 56-4.2 of the F.I. Act.
- ③ If it is determined that there is a problem for the preparation of, amendment to and compliance with internal rules of a firm which is not a member of an association, etc., the authority shall make an effort to recognize the state through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act. The authority shall make appropriate supervision considering association, etc. rules under Article 56-4.1 of the F.I. Act such as the issuance of an order to improve business management under Article 51 of the F.I. Act and the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VI-3 Procedures (investment management business)

VI-3-1 Registration

VI-3-1-1 Investment management business

(1) Items of examination of system

In examining whether the applicant is a corporation having personnel resources insufficient to carry out accurately financial instruments business as provided in Article 29-4.1 (1) (d) of the F.I. Act, the authority shall refer to the application for registration and the attachments and hold a hearing to confirm the followings.

- ① Whether it is determined that the applicant ensures the employment of officers and employees having sufficient knowledge and experience of the business and has organization, and the applicant is able to carry out such business appropriately in light of the followings.
 - (a) The management is qualified to carry out the business in a fair and accurate manner as an investment management firm in light of the career, ability, etc.

- (b) A full-time officer has knowledge and experience sufficient to understand and perform focus points of business management provided by relevant various regulations such as the F.I. Act and the Supervisory Guidelines, and has sufficient knowledge and experience of compliance and risk control necessary for fair and accurate carrying out of the financial instruments business.
- (c) A person responsible for investment management on behalf of an interest holder has knowledge and experience regarding assets to be invested in.
- (d) Whether a compliance division (person) independent from the investment management division is established and persons having sufficient knowledge and experience are appointed sufficiently as a person in charge.
- (e) Whether the applicant has, in addition to the above (c) and (d), an organizational system and personnel structure for which personnel necessary for accurate carrying out of the proposed business is allocated to each division and a person in charge of internal control, etc. is allocated appropriately.
- (f) Personnel required for the following system implementation is ensured for the proposed business:
 - a. preparation and retention of books and records (including books and records provided in VI-3-2-4), reports, etc.;
 - b. disclosure;
 - c. segregation of properties under investment management;
 - d. risk control;
 - e. computer system control;
 - f. investment management control, customer control by a control division;
 - g. corporate related information control;
 - h. examination of advertisement;
 - i. customer information control;
 - j. settlement of grievances and troubles;
 - k. execution of assets investment management by an investment management division;
 - l. internal audit;
 - m. in the case of investment management of investment trust properties, computation of investment trust properties and examination thereof.
- ② Whether the applicant has a person with inappropriate qualification for business management among officers and employees as a result of comprehensive consideration of the following matters as a relationship with a crime group or a member of a crime group or other circumstances, which will likely result in the downfall of the credit of financial instruments business.
 - (a) the applicant is a member of a crime group (including a person who was a member of a crime group in the past);
 - (b) the applicant has a close relationship with a crime group;
 - (c) the applicant has an experience of the violation of the laws or regulations for finance in Japan such as the F.I. Act or the laws or regulations in a foreign jurisdiction analogous thereto and being fined (including a criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto);
 - (d) the applicant has an experience of the violation of the provisions of the Law on Prevention of Improper Act by Member of Crime Group (excluding the provisions of Article 32-2.7 of said Law) or the provisions under the laws or regulations analogous thereto in a foreign jurisdiction, or commitment of crimes under the Criminal Code or the Law on Violence, etc. Punishment and being fined (including a criminal penalty under the laws or regulations analogous thereto in a foreign jurisdiction);
 - (e) the applicant has an experience of being punished by a criminal penalty of imprisonment or severer (including criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto) (with the remarks on, particularly, the case of crimes under Articles 246 to 250 of the Criminal Code (fraudulence, fraudulence using a computer, breach of trust, quasi-fraudulence, threat, attempted crime)).;
- (Note) It shall be noted that the case where, as a result of comprehensive consideration of the matters, etc. referred to in (a) to (e) of ② above in respect of a major shareholder of a financial instruments firm, inappropriate exercise of influencing power held by the major shareholder will likely result in the downfall of the credit of financial instruments business may be determined that such financial instruments firm "does not have personnel resources to carry out financial instruments business accurately."

- (2) Documents stating types of business and manner of operation
 The authority shall confirm that the followings are stated appropriately in the documents stating types of business and manner of operations.
- ① Types of financial instruments transactions act performed as a business;
 - ② Matters referred to in Article 8 (9) of the F.I. Business Ordinance;
 - ③ Policies regarding business management:
 - (a) matters regarding policies for business of an investment management firm and principles of business management;
 - (b) matters regarding policies of assets management;
 - (c) types of assets under investment management;
 - (d) matters regarding commissioning of investment management authorization;
 - (e) matters regarding financial soundness of an investment management firm.
 - ④ Manner of business operations:
 - (a) matters regarding manner of investment management;
 - (b) matters regarding solicitation of customers and entering into a contract, etc.;
 - (c) matters regarding the control of properties under investment management.
 - ⑤ Manner to divide business:
 Matters regarding an organization of an investment management firm.
 - ⑥ System for the settlement of grievances.
 - ⑦ The name of a financial instruments firms association of which the applicant becomes a member and matters regarding compliance with self-regulatory rules of the association.
- (3) Entries in documents under Article 9 (1) of the F.I. Business Ordinance (documents stating personnel structure for business and business operation system such as organization)
- ① Structure of officers and employees at the time of the commencement of investment management business (in the case of officers, including entries of knowledge and experience of each person regarding the direction of investment management or assets for which investment management is made), the organization chart and the summary of business for which each organization is in charge;
 - ② Business management system for investment management of assets:
 - (a) matters regarding an internal organization responsible for the decision of investment policies for investment management of assets;
 - (b) investment management system at each division carrying out investment management of assets;
 - (c) in the case of outsourcing (including further outsourcing) of investment management, matters regarding the selection of an outsourcee and the operational communication system regarding investment management of assets with the outsourcee;
 - ③ Knowledge and experience of a person carrying out investment management of assets:
 With respect to a person carrying out investment management of assets, knowledge and experience for assets under investment management shall be stated for each person.
 - ④ Knowledge and experience of compliance operations of a person in charge of compliance:
 With respect to a person in charge of compliance, knowledge and experience of compliance operation shall be stated.
 - ⑤ Internal control system such as internal investigation regarding investment management of assets and other operation
 Matters regarding the direction of investment management (in the case of outsourcing, including the direction of investment management or investment management by such outsourcee) and a division in charge of internal investigation, etc. regarding each of other divisions and detailed rules for each operational processing system, etc.
 - ⑥ Control system of corporate information:
 - (a) internal rules, etc. provide for a controller and there is an entry of such person;
 - (b) internal rules, etc. provide for a controlling system and a system that such rules fulfill the function fully;
 - ⑦ In the case of investment management of investment trust properties, knowledge and experience regarding computation operation of investment trust properties of a person carrying out such operation:
 - (a) with respect to persons carrying out computation operation of investment trust properties, knowledge and experience regarding such operation shall be stated for each of such persons;
 - (b) in the case of outsourcing computation operation of investment trust properties to a third party, knowledge and experience regarding such operation shall be stated for such third party;
- (4) Remarks on firms which have no plan to become a member of a financial instruments firms

association or which has no plan to become a member or trading participant of a financial instruments exchange

The authority shall give the following notices to a firm which has no plan to become a member of a financial instruments firms association or which has no plan to become a member or trading participant of a financial instruments exchange at the time of application for registration and require such firm to make appropriate responses.

- ① If it is determined that there is no appropriate internal rules for which association, etc. rules have been taken into consideration, such firm will be ordered to prepare internal rules immediately after the registration in principle.
 - ② There is a possibility that a firm which is not a member of an association, etc. is ordered to amend internal rules for which association, etc. rules have been taken into consideration.
 - ③ A firm which is not a member of an association, etc. shall, when ordered to prepare or amend internal rules, prepare or amend such internal rules within 30 days and obtain an approval from the Prime Minister.
 - ④ A firm which is not a member of an association, etc. shall, when it wishes to amend or abolish internal rules approved under ③ above, obtain an approval from the Prime Minister.
 - ⑤ The authority shall make an appropriate supervision over business of a firm which is not a member of an association, etc. considering association, etc. rules not to harm public interests or constitute a failure of the investor protection.
- (5) Case where registration is not required
- Notwithstanding Article 29 of the F.I. Act, a person may carry out investment management business if Article 61.2 of the F.I. Act applies (the case where a person who is a juridical person established under laws and regulations in a foreign jurisdiction and carries out investment management business in the foreign jurisdiction wishes to carry out investment management business only with a financial instruments firm (a person engaged in investment management business), etc. as a counterparty).
- (6) Remarks on application for new registration
- The authority shall require a firm applying for new registration in principle to file the following documents and confirm whether such firm does not meet registration refusal criteria, etc.
- The original certificate shall be used for the certificate of the balance of deposit, etc. issued by a financial institution among evidences.
- ① Evidences of written statements computing the amount of net assets (which means the amount of net assets provided in Article 29-4.1 (5) (b) of the F.I. Act).
 - ② Evidences of written statements computing the amount of net assets for the latest month.

VI-3-1-2 Investment corporation

- (1) Remarks in acceptance, etc. of investment corporation establishment notification
- Remarks shall be made on the followings when the director-general of a local finance bureau makes acceptance, etc. of an investment corporation establishment notification under Article 69.1 of the Investment Trust Law.
- ① Remarks on examination of establishment notification
 - (a) Page 2-1 of establishment notification: the trade name of the proposed investment corporation
Whether the trade name likely gives false impression to investors as public organization.
 - (b) Page 2-3 (4) of establishment notification: the amount of money contributed in the establishment
Whether the total amount of issued value of investment units is less than the total capital contribution amount provided in Article 57 of the Investment Trust Law Enforcement Order.
 - (c) Page 2-3 (7) of establishment notification: the summary of assets investment management of such investment corporation
Whether it is ruled that assets are invested mainly in specific assets.
 - ② Matters regarding examination of attachments to establishment notification
A written statement equivalent to a resident card in the home country provided by a foreigner who does not reside in Japan or a written statement equivalent thereto shall be "Written statement equivalent thereto" provided in Article 108.2 (5) of the Investment Trust Law Enforcement Regulations.
 - ③ Acceptance procedures, etc. of establishment notification
 - (a) Acceptance procedures

Upon the acceptance of an investment corporation establishment notification under Article 69.1 of the Investment Trust Law, the director-general of a local finance bureau shall return the duplicate of the notification and one set of agreements with the acceptance stamp and acceptance number pursuant to Form VI-1 to the financial instruments firm.

- (b) The director-general of a local finance bureau shall make an entry to an investment corporation establishment notification, etc. filing directory (Form VI-2) after the acceptance of an investment corporation establishment notification.
- (2) Remarks in acceptance, etc. of notification of failure of formation of investment corporation
The director-general of a local finance bureau shall take the following procedures in the acceptance, etc. of a notification of the failure of the formation of an investment corporation under Article 110.1 of the Investment Trust Law Enforcement Regulations.
 - ① hearing for a founding planner concerning the responses to a person who has offered investment units, and recording the fact.
 - ② making an entry of the date of the acceptance of a notification of the failure of the formation of an investment corporation in the investment corporation establishment notification, etc. filing directory and stating a brief reason for the failure of the formation of an investment corporation in the remarks column.
- (3) Remarks in acceptance, etc. of registration application by investment corporation
Remarks shall be made on the followings when the director-general of a local finance bureau makes the acceptance, etc. of a registration application (Form 9 of the Investment Trust Enforcement Regulations (hereinafter in (3), the same)) under Article 188.1 of the Investment Trust Law:
 - ① Remarks on examination of application for registration
 - (a) Pages 2 • 3 – 2. (5) of registration application: the minimum amount of net assets required to be continuously maintained
Whether the minimum amount of net assets is not less than the amount required under Article 55 of the Investment Trust Law Enforcement Order.
 - (b) Page 2 • 3 – 2. (6) of registration application: Objects and policies of investment management
Whether properties are invested mainly in specific assets.
 - (c) Page 6 – 9. (1) of registration application: the total amount of capital contributions
Whether the total amount of capital contributions at the time of the formation of an investment corporation is not less than the amount provided in Article 57 of the Investment Trust Law Enforcement Order.
 - ② Remarks on examination of attachments to registration application
A written statement equivalent to a resident card in the home country provided by a foreigner who does not reside in Japan or a written statement equivalent thereto shall be "written statement equivalent thereto" provided in Article 215 (4) of the Investment Trust Law Enforcement Regulations.
 - ③ Other remarks on acceptance, etc. of registration application
 - (a) The director-general of a local finance bureau shall, upon accepting an investment corporation registration application, make an entry of the date of the acceptance of an investment corporation registration application in the investment corporation establishment notification, etc. filing directory.
 - (b) If an investment corporation registration application or a notification of the failure of the formation of an investment corporation has not been filed even after the period usually required for the filing of an investment corporation registration application has passed after the offering period of investments units issued at the time of the establishment stated in the investment corporation establishment notification has passed, the director-general of a local finance bureau shall refer to the founding planner who has filed the investment corporation establishment notification, and recognize the real state.
 - ④ Procedures, etc. for registration
 - (a) Registration number
 - a. Registration numbers shall be serial numbers for each local finance bureau; *provided*, that 4, 9, 13, 42, 83, 103 and 893 shall not be used.
 - b. When a registration loses its effect, the registration number shall be left as the missing number and such number shall not be used.
 - c. The registration number shall be controlled by the registered investment corporation registration number book made on Form VI-3.
 - (b) Notice to applicant for registration

Upon the completion of examination of an investment corporation registration application, the director-general of the local finance bureau shall, if there is no deficiency in the investment corporation registration application and attachments and registration refusal criteria are not applicable, furnish the applicant for registration with a notice made on Form 14 of the Investment Trust Law Enforcement Regulation promptly.

⑤ Report to the Commissioner of the Financial Services Agency

Upon the registration of an investment corporation, the director-general of the local finance bureau shall report to the Commissioner of the Financial Services Agency in a lot each month no later than the 15th of the following month by Form VI-4.

⑥ Refusal of registration

The director-general of a local finance bureau shall, if refusing the registration, clarify, in the Form 15 of the Investment Trust Law Enforcement Regulation, the number of an item among the items of Article 190.1 of the Investment Trust Law applicable to the reason for the refusal or the place of a false statement or omission of an important fact in the application for registration and attachments concretely.

⑦ Keeping of registration application, etc.

An establishment notification, notification of the failure of the formation and attachments thereto shall be kept by the director-general of a local finance bureau with whom such notification has been filed, and a registration application, change notification, dissolution notification and attachments thereto shall be kept by the director-general of a local finance bureau with whom the registered investment corporation is registered effectively.

⑧ Registered investment corporation registry book

(a) A registered investment corporation registry book shall be made accessible for the public inspection, and require a public inspection applicant to state stipulated matters on the registered investment corporation registry book public inspection application made on Form VI-5.

(b) Public inspection of the registered investment corporation registry book shall be available on days other than holidays of administrative agencies as defined in Article 1 of the Law on Holidays of Administrative Agencies for hours specified by the director-general of a local finance bureau; *provided*, that such days and hours may be changed or public inspection can be suspended or refused when needed for fixing up of the registry book or for other reasons.

(c) A registered investment corporation registry book shall not be taken out of the inspection place designated by the director-general of a local finance bureau.

VI-3-2 Approval and notification, etc.

VI-3-2-1 Approval

Remarks shall be made on the followings for approving other business engagement under Article 35.4 of the F.I. Act.

- ① Whether such business does not violate the relevant laws or regulations.
- ② Whether there is likeliness that the amount of net assets of a financial instruments firm so applying becomes less than ¥50 million.
- ③ Whether, with respect to business involving entering into contracts, etc. with customers, the financial instruments firm implements concrete measures to prevent conflicts of interest necessary for the protection of investors in entering into such contract, etc.
- ④ Whether the financial instruments firm implements internal rules for such business.

VI-3-2-2 Notification

Remarks shall be made on the followings for accepting or dealing various notifications provided by the F.I. Act. The authority shall accept a notification of business provided in Article 35.2 of the F.I. Act particularly with remarks whether procedures necessary under the laws or regulations over such business have been taken, and remarks, with respect to the following businesses, whether the followings apply to the types, manners, etc. of the businesses. For these purposes, furnishing of a written statement and written procedures in respect of matters to be contained in the written statement may be made by methods using an electronic data processing and network system or other method using information technology in lieu of furnishing, etc. of the written statement after obtaining an approval from a customer. With respect to non-applicable

business, the authority shall require the financial instruments firm to file an approval application under Article 35.4 of the F.I. Act.

(1) Business of purchase or sale of gold bullion or acting as an intermediary, broker or agent thereof

① Products to be handled

Whether the product to be handled is gold bullion or gold coins which have high purity and globally established liquidity.

② Purchase of stock

Whether, in entering into a contract with a supplier, the contract provides that ① the financial instruments firm does not keep stock in principle and ② the supplier will accept the request for buy-back of the actuals purchased as stock, and as the result the financial instruments firm or its affiliate, etc. will not own excessive stock. A contract with a supplier on "forward transaction" provides that performance of forward agreement is secured.

③ Business with customers

(a) Sales methods

Whether sales methods comply with the followings.

- a. the financial instruments firm limits the sale to actuals and does not handle futures;
- b. the financial instruments firm shall make a sale by the method of cumulative investment in an appropriate manner such as furnishing customers with a written statement clarifying the mechanics and make full explanation to customers in advance;

(b) Solicitation

A customer should invest in gold by the customer's judgment and responsibility, and whether the financial instruments firm complies with the followings in the solicitation of investment.

- a. the financial instruments firm shall not solicit by providing definitive judgment regarding the movement of the gold price;
- b. the financial instruments firm shall conduct appropriate investment solicitation suitable to the intent, knowledge of gold investment and experience of an investor and the amount and the nature of funds available for investment;
- c. the financial instruments firm shall not agree to compensate losses or provide special profit in soliciting investment;
- d. the financial instruments firm shall not solicit frequent purchase or sale for a short period (including purchase or sale to switch between securities and gold);
- e. the financial instruments firm shall not conduct purchase or sale for a customer's account for which the customer gives the financial instruments firm discretion for the determination of the distinction of purchase or sale, volume and price;

(c) Furnishing customers with certificates, etc.

Whether the followings are complied in furnishing a customer with a certificate, etc.

a. Furnishing a safe custody certificate, etc.

The financial instruments firm shall furnish a customer with certificates, etc. necessary to clarify rights and obligations with the customer or to smoothen transactions such as a safe custody certificate (limited to the case of safe custody transactions), delivery account statement, purchase request statement (in the case of actuals deliver transaction, documents to clarify that the financial instruments firm accepts purchase of actuals) according to respective cases of safe custody transactions or actuals deliver transactions.

With respect to forward transactions, however, furnishing of a safe custody certificate may be replaced with furnishing of an account statement if such account statement is furnished each time of delivery in respect of the details of purchase or sale and the deposit balance. Furnishing of a safe custody certificate and delivery account statement may be omitted if a notice stating the history of purchase of gold bullion and the balance of safe custody is furnished at least once per six months in respect of gold bullion cumulative investment.

b. Furnishing of gold bullion transactions agreement

The financial instruments firm shall furnish a customer with a gold bullion transaction agreement clarifying matters, etc. related to rights and obligations with customers at the time of the commencement of transactions and at the time of making a change to such agreement in order to prevent accidents related to gold bullion transactions and to protect investors in both cases of safe custody transactions or actuals delivery transactions.

(d) Determination, etc. of prices

Whether the followings are complied in determining prices

- a. The price of purchase or sale shall be denominated in Yen and shall be determined appropriately in consideration of trading prices on domestic and overseas markets, foreign exchange rates, etc. The price of purchase from a supplier for forward transactions shall be the current market price and resale price and the price of purchase or sale with a customer shall be computed based thereon.
 - b. A financial instruments firm shall post the prices of purchase or sale at all offices handling such transactions each trading day and conclude transactions at such prices and shall not accept an advance order or market order.
- ④ Safe custody
- Whether the followings are complied in respect of safe custody.
- (a) A financial instruments firm shall not assign or pledge a deposit certificate issued based on the deposit of actuals such as a safe custody certificate, exchange ticket for actuals and receipt of actuals.
 - (b) In conducting safe custody transactions, the financial instruments firm which handles actuals shall secure actuals for the amount corresponding to the amount for deposit business and keep it.
 - (c) A financial instruments firm shall give a notice to a customer of the balance of safe custody by a notice of checking at least once per year.
- ⑤ Buying back
- Whether, if a customer has demanded buying back of gold bullion (including the case of a safe custody certificate) sold by a financial instruments firm, the financial instruments firm buys it back at a reception desk of its business office in principle.
- ⑥ Agent business, etc.
- Whether the agent business, etc. is limited to forward transactions and gold bullion cumulative investment conducted in the following manners.
- (a) Agent business, etc. for an order of forward transactions
 - a. A financial instruments firm which acts as a broker for transactions by a customer with an offering financial instruments firm, etc., carries out the whole or part of business related to forward transactions between the customer and the offering financial instruments firm, etc. on behalf of the offering financial instruments firm, etc. and carries out agent business, etc. for forward transactions shall enter into a contract for such agent business, etc. with the offering financial instruments firm, etc.
 - b. A financial instruments firm carrying out the business shall comply with the followings
 - i) A financial instruments firm carrying out agent business, etc. for forward transactions shall explain to a customer fully that the forward transactions for which an order is placed are conducted with an offering financial instruments firm, etc., and obtain a consent from the customer in advance.
 - ii) A financial instruments firm carrying out agent business, etc. shall recognize the details of the customer's transactions with the offering financial instruments firm, etc. periodically.
 - (b) Agent business, etc. for an order of gold bullion cumulative investment
 - a. The scope of agent business, etc. for gold bullion cumulative investment shall be to act as a broker for transactions by a customer with an offering financial instruments firm, etc. and carry out the whole or part of business for gold bullion cumulative investment between the customer and the offering financial instruments firm, etc. on behalf of the offering financial instruments firm, etc. and carry out agent business, etc. for gold bullion cumulative investment, and the financial instruments firm shall enter into a contract for such agent business, etc. with the offering financial instruments firm, etc.
 - b. A financial instruments firm carrying out the business shall comply with the followings
 - i) A financial instruments firm carrying out agent business, etc. for gold bullion cumulative investment shall explain to a customer fully that the gold bullion cumulative investment for which an order is placed are conducted with an offering financial instruments firm, etc. and obtain a consent from the customer in advance.
 - ii) A financial instruments firm carrying out agent business, etc. shall reconcile the details of the customer's transactions with the offering financial instruments firm, etc. periodically.
- (2) Entering into an association contract as defined in Article 667 of the Civil Code or business related to acting as an intermediary, broker or agent therefor and business related to acting as an intermediary, broker or agent for entering into a contract of undisclosed association as defined in Article 535 of the Commercial Code (excluding businesses to perform the act referred to in

Article 2.8 (9) of the F.I. Act).

Whether a financial instruments firm or an officer or employee of a financial instruments firm explains to a customer fully concerning the contract in soliciting a customer to enter into a contract of association and makes appropriate solicitation according to the customer's intention, knowledge and experience of such association and financial resources and the nature of the funds to be invested. Whether the financial instruments firm prepares a written statement explaining the details of the contract and furnish a customer with it before entering into the contract.

- (3) Entering into loan participation contract or business related to acting as an intermediary, broker or agent therefor
 - ① Products to be handled

A loan participation contract shall mean a product assumed by "accounting and presentation of loan participation" published by Japan Certified Public Accountant Association on June 1, 1995.
 - ② Management, etc. of business

Whether business is managed in compliance with the followings.

 - (a) taking due care to the protection of the original debtor and assignee in carrying out the business;
 - (b) full explanation to an assignee of the nature, details, etc. of the claims, etc. handled;
 - (c) Implementation of valuation system of claims, etc. handled and appropriate formation of prices;
 - (d) appropriate solicitation in light of the intent, experience and financial resources of an assignee;
 - (e) preparation of a written statement for the details of a contract and furnishing an assignee with such written statement before entering into a contract.

VI-3-2-3 Investment management report

- (1) Entries in investment management report for discretionary investment business
 - ① With respect to the entries in a report provided in Article 42-7.1 of the F.I. Act, the total amount of assets under collective investment management and money and issue names, number, price of securities, etc. composing such assets and the share of a customer and the amount equivalent to the share of such assets shall be included in the entries provided in Article 134.1 (2) of the F.I. Business Ordinance in the case where assets of multiple customers are invested collectively.
 - ② With respect to the entries provided in Article 134.1 (4) of the F.I. Business Ordinance, in the case where a contract for business related to a discretionary investment contract and securities related business are entered into as a unit and customer fees for purchase or sale and expenses of account controlling, etc. are collected separately from the remuneration for a discretionary investment contract, the breakdown therefor shall be stated.
 - ③ With respect to the details of transactions required to be stated under Article 134.1 (6) of the F.I. Business Ordinance, it is not necessary to state the value, volume, etc. for each of all concluded transactions, but it is possible to simplify according to the purpose and the nature of such transactions, and for example, entries of types of transactions between properties under investment management (such as requirements provided in the items of Article 129.1 of the F.I. Business Ordinance) shall suffice.
- (2) Entries in investment trust properties investment management report

An investment management report for investment trust properties under Article 14.1 of the Investment Trust Law should be represented in consideration that investors understand easily, and it shall be noted that the followings are methods to represent concretely the matters referred to in the items of Article 58.1 of the Regulations on Computation of Investment Trust Properties (hereinafter referred to as "Investment Trust Properties Computation Regulations"), and references, etc. shall be responded appropriately.

 - ① Progress of investment management of assets during computation period for such investment trust properties:
 - (a) The base value at the beginning of the term, the base value at the end of the term and the state of base value during the term shall be represented. In addition, investment management policies and relationship with "future investment management policies" represented in the investment management report for the previous term (for example, verification result, etc. whether investment activities were performed in line with the

- investment management policies) for investment trust properties of such investment trust are represented.
- (b) Future investment management policies are represented concretely based on investment management policies for investment trust properties of such investment trust.
 - (c) With respect to profit dividends for the current term, the grounds for decisions of dividends and future investment management policies for reserved profit shall be represented.
- ② Records of investment management
- (a) Performance records (which means performance records to judge the state of investment trust properties accurately such as base value, dividends, up-down ratio during the term, yield for beneficiaries, stock index, composition ratio of main properties under investment management and remaining ratio of principals) during the following periods are represented according to the classification of the followings:
 - a. unit-type investment trust: from the beginning of trusting of investment trust properties until the end of the computation period for such investment trust properties (hereinafter in (2), referred to as "end of the current term");
 - b. open-end-type period investment trust (excluding those to which the following c. and d. are applicable): at least 5 terms from or before the current term (in the case of Article 59.1 of the Investment Trust Properties Computation Regulations however, at least 5 preparing periods from or before the current preparing period);
 - c. open-end-type fixed-income investment trust (excluding those to which the following d. is applicable): at least 3 terms from or before the current term (in the case of Article 59.1 of the Investment Trust Properties Computation Regulations however, at least 3 preparing periods from or before the current preparing periods);
 - d. open-end-type fixed-income investment trust with one day computation period: at least 1 preparing period.
 - (b) In addition to up-down ratio of a computation period of a trust, if investment management policies for investment trust properties of such investment trust are to link with a specific index, etc. as a comparison of base values and the market conditions during the current term, the movement of such index, etc. shall be represented.
- ③ The number of shares of stock as of the end of the computation period immediately preceding a computation period of such investment trust properties (hereinafter in (2), referred to as "end of preceding term") and as of the end of the current term and market capitalization as of the end of the current term and the total number of purchase and sale and total amount of purchase and sale of shares of stock during a computation period of such investment trust properties for shares of stock and for each issue name.
- (a) Shares of stock include warrant certificates; for this purpose, "number of shares of stock" shall be read as "number of units".
 - (b) Representation is made for each type of currencies (If the currency is Euro, representation shall be made for each country).
 - (c) Representation is made for each issue name. Domestic shares of stock (excluding warrant certificates) shall be represented for each business type and the ratio of the market capitalization of each business type to the market capitalization of domestic shares of stock as of the end of the current term shall be represented together.
 - (d) With respect to the market capitalization of domestic shares of stock and the market capitalization of domestic warrant certificates as of the end of the current term, the ratio of each of them to the total amount of investment trust properties net assets shall be represented.
 - (e) With respect to the market capitalization of foreign shares of stock and the market capitalization of foreign warrant certificates as of the end of the current term, the ratio of each of them to the total amount of investment trust properties net assets shall be represented.
 - (f) The total number of purchase and sale and the total amount of purchase and sale of shares of stock during the computation period shall be represented for purchase or sale separately, and the increase or decrease as a result of capital increase or decrease, share split and change of face value shall be represented in a parenthesis as a superscription, and such fact shall be stated.
 - (g) The ratio of sale to purchase of shares of stock and customer fees for purchase and sale per beneficial interest during the computation period shall be represented.
- ④ The market capitalization as of the end of the current term and the total amount of purchase and sale of such investment trust properties during the computation period for public and corporate debt securities and for each of types and issue names;
- (a) Representation is made for each type of currencies (in the case of Article 59.1 of the

Investment Trust Properties Computation Regulations however, representation of its total amount shall suffice regardless of types of currencies. If the currency is Euro, representation shall be made for each country).

- (b) Types shall be classified into national government bonds, local government bonds, special debt securities, corporate debt securities with warrants and other corporate debt securities.
 - (c) Representation is made for each issue name.
 - (d) The total number of purchase and sale during the computation period shall be represented for purchase or sale separately, and the increase or decrease as a result of allocation of corporate debt securities with warrants, redemption and exercise of warrants shall be represented in a parenthesis as a superscription, and such fact shall be stated.
- ⑤ The matter referred to in Article 58.1 (5) of the Investment Trust Properties Computation Regulations for each issue name of a beneficial certificate of an investment trust (excluding a beneficial certificate of a parent investment trust; in (2), the same), beneficial certificate of a parent investment trust and investment certificate of an investment corporation
- (a) Representation is made for each currency (if the currency is Euro, representation shall be made for each country).
 - (b) Customer fee for purchase or sale per one unit of a beneficial certificate of a parent investment trust during such computation period shall be represented. In this case, with respect to customer fees for purchase or sale for an investment trust holding such parent investment trust beneficial certificate (hereinafter referred to as "child investment trust"), the part corresponding to such child investment trust of a parent investment trust shall be represented.
- ⑥ In the case where securities lending is made as of the end of the current term, the total number of shares of stock or the total amount of face value for each type
- Classification shall be made to shares of stock and corporate debt securities, and the total number of shares of stock in the case of shares of stock and total amount of face value in the case of public or corporate debt securities shall be represented.
- ⑦ In the case of derivatives transactions (which mean derivatives transactions as defined in Article 2.20 of the F.I. Act; hereinafter the same), the outstanding amount of contracts or the outstanding volume as of the end of the current term and the amount of traded contracts or the amount of transactions during the computation period of such investment trust properties for each type.
- With respect to securities related derivatives transactions (which means securities related derivatives transactions as defined in Article 28.8 (3) of the F.I. Act; hereinafter the same) among derivatives transactions, the outstanding amount of contracts or the outstanding volume as of the end of the current term and the amount of traded contracts or the amount of transactions during the computation period of such investment trust properties shall be classified into transactions related to shares of stock, transactions related into debt securities, etc. for representation. (Notwithstanding the above however, in the case of Article 59.1 of the Investment Trust Properties Computation Regulations, representation of the outstanding amount of contracts or the outstanding volume as of the day immediately preceding the last business day of each month and the total amount of traded contracts or the amount of transactions during the computation period of such investment trust properties may suffice.)
- With respect to derivatives transactions other than securities related derivatives transactions, the outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.
- ⑧ The matter referred to in Article 58.1 (8) of the Investment Trust Properties Computation Regulations for each of real estate, lease or superficies of real estate.
- The outstanding assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented separately for each of real estate, lease or superficies of real estate.
- ⑨ With respect to promissory notes provided in Article 3 (6) of the Investment Trust Enforcement Order, the amount of claims as of the end of the current term and the total amount of purchase and sale during the computation period of such investment trust properties
- The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.
- ⑩ With respect to money claims provided in Article 3 (7) of the Investment Trust Law Enforcement Order, for each type, the total amount of claims as of the end of the current term

and the total amount of purchase and sale of claims during the computation period of such investment trust properties for each type

The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.

- ⑪ With respect to undisclosed association capital contribution share provided in Article 3 (8) of the Investment Trust Law Enforcement Order, main details of investment management object assets as of the end of the current term for each type

The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.

- ⑫ With respect to commodities provided in Article 3 (9) of the Investment Trust Law Enforcement Order, the volume as of the end of the immediately preceding term and the end of the current term and the market capitalization as of the end of the current term and the total amount of purchase and sale of commodities during the computation period of such investment trust properties for each type

(a) Representation is made for each type of currencies (if the currency is Euro, representation shall be made for each country).

(b) The total amount of purchase and sale of commodities during the computation period shall be represented for purchase or sale separately.

(c) Ratio of purchase and sale of commodities and purchase and sale customer fees per one unit of a beneficial interest during such computation period shall be represented.

- ⑬ With respect to commodity investment, etc. transactions, the outstanding amount of contracts as of the end of the current term and the amount of traded contracts or the amount of transactions during the computation period of such investment trust properties for each type

The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.

- ⑭ With respect to assets other than specific assets, main details of such assets as of the end of the current term for each type

The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.

- ⑮ The ratio of the total amount of each of the specific assets referred to in (1) or (3) to (9) of Article 3 of the Investment Trust Law Enforcement Order or other assets to the total amount of investment trust properties as of the end of the current term

The ratio of the total amount of each of assets (in the case of a parent investment trust beneficial certificate, each issue name) to the total amount of investment trust properties shall be represented. The ratio of total amount of net assets for foreign currency denominated assets to the total amount of investment trust properties as of the end of the current term shall be noted.

- ⑯ If prices, etc. of specific assets has been examined under Article 11.1 of the Investment Trust Law, the name of a person who has so examined and the summary of the result and methods of such examination

With respect to the summary of the result and methods of the examination, the type of specific assets and matters for which the examination was made and the qualification, etc. of a person who has made such examination shall be included and represented in consideration that investors understand easily.

- ⑰ The state of assets, liabilities, principal and base value of beneficial certificates as of the end of the current term and the state of profits and loss during the computation period of such investment trust properties

If there are notes provided by the Investment Trust Properties Computation Regulations, such matters shall be represented as notes.

- ⑱ The state of trading with a person concerned, etc. and the total amount of purchase and sale customer fees paid to the person concerned, etc. during the computation period of such investment trust properties

The state of trading shall be classified into the amount of purchase and amount of sale for each type of securities, derivatives or other transactions and the amount of trading with the person concerned, etc. and the ratio of each of them to the total amount shall be represented.

- ⑲ In the case where an investment trust management firm, etc. carries out the first-type

financial instruments business or the second-type financial instruments business, the state of trading with such investment trust management firm, etc. and the total amount of purchase and sale customer fees paid to such investment trust management firm, etc. during the computation period of such investment trust properties

The state of trading shall be classified into the amount of purchase and amount of sale for each type of securities and derivatives transactions and the amount of trading with the firm and the ratio of each of them to the total amount shall be represented.

- ⑳ In the case where an investment trust management firm, etc. carries out real estate transaction business, the state of trading with such investment trust management firm, etc. which is a real estate transaction firm and the total amount of fees paid to such investment trust management firm, etc. during the computation period of such investment trust properties

The state of trading shall be classified into purchase and sale and lease, etc. for each type of real estate and the amount of trading with the firm and the ratio of each of them to the total amount shall be represented.

In the case where an investment trust management firm, etc. carries out real estate specific joint business, the state of trading with such investment trust management firm, etc. which is a real estate specific joint firm during the computation period of such investment trust properties

The state of trading shall be classified into purchase and sale and lease, etc. for each type of real estate and the amount of trading with the firm and the ratio of each of them to the total amount shall be represented.

- (21) In the case where the trust contract period of such investment trust properties has terminated, the investment trust properties management summary sheet

The outline of the progress of investment management from the beginning of trusting such trust properties until the end of the preceding term shall be represented together. If the outline of the progress of investment management under the above ① is represented, the outline of the progress of investment management may be omitted.

- (22) In preparing the sheet pursuant to Article 59.1 of the Investment Trust Properties Computation Regulations, "state as of the end of each computation period" in Form 2 of the Investment Trust Properties Computation Regulations may be read as "state as of the end of each preparing period".

- (23) In the case where an investment trust management firm, etc. carries out commodity transaction customer business, the state of trading with such investment trust management firm, etc. and the total amount of purchase or sale customer fees paid to such investment trust management firm, etc. during the computation period of such investment trust properties

The state of trading shall be classified into the amount of purchase and amount of sale for each type of commodities and commodities investment, etc. transactions and the amount of trading with the firm and the ratio of each of them to the total amount shall be represented.

- (3) Entries into investment management report of trusting person non-directing type investment trust

(2) above shall apply to concrete representing manner of the matters referred to in the items of Article 58.1 of the Investment Trust Properties Computation Regulations which is applied *mutatis mutandis* under Article 62 of the Investment Trust Properties Computation Regulations.

- (4) Entries into assets investment management report for investment corporation

An assets investment management report required to be represented pursuant to Article 129.2 of the Investment Trust Law shall be represented in consideration that investors understand easily. (2) above shall apply to concrete representing manner of the matters referred to in Article 71 of the Regulations on Computation of Investment Corporation (hereinafter referred to as "Investment Corporation Computation Regulations"). This shall not apply however, if there is likeliness that the conditions of properties and profit and loss of an investment corporation cannot be judged accurately.

In the case where an investment trust management firm, etc. which has entered into an assets investment management contract invests assets of an investment corporation jointly with other investment corporation, entries shall be made, as matters necessary to clarify the state of investment management of an investment corporation during such other business period provided in Article 73.1 (22) of the Investment Corporation Computation Regulations, for the total amount of assets subject to the joint investment management by such investment trust management firm, etc., types of such assets, share of such investment corporation related to such assets and the amount of money equivalent to the share.

VI-3-2-4 Books and records regarding investment trust properties, etc.

Books and records prepared and retained under the Investment Trust Law (hereinafter in VI-3-2-4, referred to as "books and records") shall be prepared and retained in accordance with III-3-3 (1) (excluding ②, ③, ⑤, ⑥ and ⑧), and remarks shall be made on the followings.

- (1) Books and records which are prepared and retained under the Investment Trust Law and subject to retention by electronic or magnetic methods, etc. shall be the books and records referred to in Articles 26.1, 254.1 and 255.1 of the Investment Trust Law Enforcement Regulations.
 - ① Remarks on preparation and retention of books and records in the form of microfilm
 - (a) Microfilm used for retention shall have a durability of the following period according to the following classification:
 - a. books and records regarding investment trust properties: 10 years after the termination of the computation period of such investment trust properties provided in Article 26.2 of the Investment Trust Law Enforcement Regulations or after the termination of the trust contract period;
 - b. books and records of an investment corporation: 10 years after an approval of the account settlement of such investment corporation provided in Article 254.2 of the Investment Trust Law Enforcement Regulations (in the case of commercial books and records, since the closure of the books and records);
 - c. books and records of an assets safe keeping firm: 10 years after an approval of the account settlement of such investment corporation provided in Article 255.2 of the Investment Trust Law Enforcement Regulations;
 - (b) Keeping one of microfilms used for data retention as "original" and clarifying the fact.
 - (c) Preparing the back up of the "original" under (b) and keeping such back up as "duplicate".
 - (d) It is possible to prepare books and records by hard copy for inspection, etc. by the inspection division within a reasonable period.
 - (e) Appointment of a person responsible for preparation and retention of microfilm and implementation of control procedures.
 - ② Remarks on preparation and retention of books and records by electronic or magnetic methods
 - (a) The above ① (a) shall apply to the durability of media used for retention.
 - (b) Whether ID, password, etc. control is used for inputting data, and the system prevents falsification or confusion.
 - (c) In addition to the above (a) and (b), and ①, ③, ④ and ⑥ to ⑩ of III-3-3 (6) shall apply.

VI-3-2-5 Entries in notification of foreign investment trust

Entries of the matters referred to in the items of Article 58.1 of the Investment Trust Law and the items of Article 96.2 of the Investment Trust Law Enforcement Regulations in a notification of a foreign investment trust shall be made as follows.

- (1) Matters regarding a trusting person (limited to the case of a trust similar to a trusting person directing type investment trust), trustee and beneficiary
 - ① Matters regarding a trusting person

The notification shall contain the name, amount of capital, type of business and summary of business of a trusting person (in the case where there is an investment management firm commissioned investment management of investment trust properties from a firm controlling a foreign investment trust, such firm controlling the foreign investment trust and investment management firm).
 - ② Matters regarding a trustee

The notification shall contain the name, amount of capital, type of business and summary of business of a trustee (safe keeping firm).
 - ③ Matters regarding a beneficiary

The notification shall contain the details of dividend receiving right, redemption receiving right, claims for repurchase and other right of such foreign investment trust (including the timing of taking effect and extinction of rights) and procedures for exercise of rights.
- (2) Matters regarding beneficial certificate

- ① The name of such foreign investment trust
- ② Form of foreign investment trust

The notification shall contain the distinction of registered form or bearer form, the distinction of par-value or non-par-value, the distinction of open-end type or closed-end type, exchange of registered form from/ to bearer form, name transfer of a registered beneficial certificate and reissuance of a beneficial certificate.
- ③ The number of issues (public sale)
- ④ The total amount of issued (publicly sold) value

In the case of filing a notification of a foreign investment trust without stating "issue price" or "public sale price", the notification shall contain the expected amount of such total amount as of the day of filing of such notification, and shall state the fact as notes.
- ⑤ The issue (public sale) price

In the case of filing a notification of a foreign investment trust without stating "issue price" or "public sale price", the notification shall contain the scheduled fixing timing and concrete method of fixing as notes.
- ⑥ Subscribing fee
 - (a) If fees are different among subscription places, the notification shall contain fees at each subscription place. If fees cannot be disclosed due to unavoidable reason, the notification shall contain the fact.
 - (b) If fees differ according to subscribing volume or amount of money, the notification shall contain such volume or amount of money and fees at each level.
- ⑦ Subscribing unit
- ⑧ Subscribing period
- ⑨ Others
 - (a) The notification shall contain the method of subscription, interests for subscription guarantee money, transfer of subscription guarantee money to investment trust properties and other matters necessary for subscription, etc.
 - (b) If offering of such foreign investment trust is made in an area other than Japan, the notification shall contain the number of issues (public sale), total amount of issuing (public sale) value, etc.
- (3) Matters regarding control and investment management of trust
 - ① Control of trust
 - (a) Matters regarding control until redemption of funds trusted with a trustee

The notification shall contain matters, etc. regarding preparation of reports, distribution methods of profits, partial cancellation regarding investment trust properties.
 - (b) Others

The notification shall contain matters regarding a change to agreements, procedures for renewal, etc. of contract with a firm concerned, disclosure methods in the case of change and other important matters.
 - ② Investment management of trust
 - (a) Policies of investment management

The notification shall contain the policies regarding investment management of investment trust properties concretely.
 - (b) Investment objects

The notification shall contain the type of assets to be invested in, investment standards and, if there is an investment plan for types or areas, etc., the percentage thereof.
 - (c) Investment limits
 - a. The notifying person shall state the grounds for all investment limits stated in laws or regulations, agreements, etc.
 - b. The notification shall contain whether a limit exists for underwriting of securities, margin transactions, loan, concentrated investment, investment in other funds and investment in illiquid assets, and if such limit exists, the grounds and details thereof.
 - (d) Policies of distribution

The notification shall contain the policies of distribution provided in the agreements, etc.
 - (e) Loan of assets

If assets acquired as investment trust properties are lent, the details thereof.
- (4) Matters regarding computation and distribution of profit of trust
 - ① Matters regarding computation of trust
 - (a) Valuation of assets

The notification shall contain the computation methods (including valuation of assets to be

invested in), computation frequency, publication methods, publication frequency and publication place for net assets value per unit of beneficial certificates of foreign investment trust.

(b) Controlling remuneration, etc.

The notification shall contain the computation method, payment amount, payment methods and payment timing for all remuneration and fees paid from investment trust properties of foreign investment trust for each payee.

(c) Others

The notification shall contain the lifetime of foreign investment trust, computation period of trust, additional issue or conditions to limit redemption regarding partial cancellation.

② Matters regarding distribution of profits

(a) The notification shall contain matters regarding computation methods of the amount of profits distributable.

(b) With respect to payment of profits or distribution of profits at the time of redemption, The notification shall contain the timing, place and method of payment from a trustee to a trusting person (limited to the case of those similar to trusting person directing type investment trust), immunity of a trustee and payment from a trusting person (limited to the case of those similar to trusting person directing type investment trust) to a trustee,.

(5) The notification shall contain matters regarding the assignment of the whole or part of business from a trusting person (limited to the case of those similar to trusting person directing type investment trust), procedures for business assignment, method to give a notice to a beneficiary and, if a beneficiary can file a petition of objection to business assignment, the details thereof.

(6) Matters regarding resignation and removal of trustee and selection of new trustee

The notification shall contain the procedures for resignation of a trustee and selection of a new trustee.

(7) In the case of commissioning the authority of directing investment management by a trusting person to an other person (limited to the case of those similar to trusting person directing type investment trust) or the case of commissioning the authority of investment management by a trustee to an other person (limited to the case of those similar to trusting person non-directing type investment trust), the details of such commissioning

The notification shall contain the concrete details of the authority to be commissioned and fees related to commissioning.

(8) The name of a financial instruments firm, etc. which conducts handling, etc. of public offering in Japan

The notification shall contain the names of all financial instruments firms, etc. which conducts handling, etc. of public offering.

VI-3-2-6 Representation method of investment trust properties investment management report of foreign investment trust

An investment trust properties investment management report under Article 14.1 of the Investment Trust Law which is applied *mutatis mutandis* under Article 59 of the Investment Trust Law shall be represented in consideration that investors understand easily, and the matters referred to in Article 63.1 of the Investment Trust Properties Computation Regulations shall be represented with the following remarks, and references, etc. thereto shall be responded appropriately.

(1) Progress of investment management of assets during the computation period of such investment trust properties of the foreign investment trust

① Base value at the beginning of the term, base values at the end of the term and the state of base value during the term shall be represented. In addition, the relationship with the investment management policies for investment trust properties of the foreign investment trust shall be represented.

② Future investment management policies are represented based on investment management policies for the investment trust properties of such foreign investment trust shall be represented.

③ Profit dividends per unit for which rights are fixed during the current term shall be represented.

④ In the case of an investment trust properties investment management report as of the termination of a trust, the outline of the progress of investment management from the

- commencement of the trust until the end of the immediately preceding term shall be represented.
- (2) Progress of investment management
 - ① Performance records for 10 terms from or before the current term (based value, dividends, etc.) are represented.
 - ② If investment management policies for investment trust properties of such foreign investment trust are to link with a specific index, etc. as a comparison of base values and the market prices during the current term, the movement of such index, etc. shall be represented.
 - (3) The balance sheet as of the end of the computation period of investment trust properties of such foreign investment trust (hereinafter in VI-3-2-6, referred to as "as of the current term") and profit and loss and surplus statement during the computation period and notes thereto
 - ① The balance sheet and its notes as of the end of the current term shall be represented.
 - ② Profit and loss and surplus statement during the computation period and their notes shall be represented. The amount of loss shall be represented together with Δ or minus or in a parenthesis.
 - (4) The net assets statement as of the end of the current term
 - ① The number of issued units of such foreign investment trust as of the end of the current term shall be stated clearly and the amount of net assets per unit of beneficial certificates of such foreign investment trust obtained from dividing the total amount of net assets as of the same time by the number of issued units as of the same time shall be represented.
 - ② If such items are represented in the balance sheet under the above (3), net assets statement may be replaced with such balance sheet.
 - (5) Main issue names of securities to be invested in
 - ① The name, volume, market capitalization and investment ratio for the largest 30 in terms of valued amounts among invested shares of stock as of the end of the current term or the latest day of the time of preparation of an investment trust properties investment management report shall be represented after classifying into areas of places of issuance or listing financial instruments exchange.
 - ② Notwithstanding the above, the amount and investment ratio of invested shares of stock and securities other than shares of stock as of the end of the current term or the latest day of the time of preparation of an investment trust properties investment management report for each type and each area of issued places of securities or listing financial instruments exchanges, etc. may be represented in lieu of the above ①.
 - (6) Main types of rights related to derivatives transactions to be invested in
The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented separately for each type of derivatives transactions.
 - (7) Main types of real estate, lease of real estate or superficies to be invested in
The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented separately for each of real estate, lease of real estate or superficies.
 - (8) Main types of money claims to be invested in
The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.
 - (9) Main types of promissory notes to be invested in
The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.
 - (10) Main types of specific assets referred to in Article 3 (8) of the Investment Trust Law Enforcement Order or other similar assets to be invested in
The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented in consideration that investors understand easily.
 - (11) Main types of commodities to be invested in
The name, volume, market capitalization and investment ratio for the largest 30 in terms of valued amounts among invested commodities as of the end of the current term or the latest day of the time of the preparation of an investment trust properties investment management report shall be represented after classifying into types of currencies.
 - (12) Main types of rights related to commodity investment, etc. transactions to be invested in

The outstanding amount of assets as of the end of the current term and the state of investment management during the computation period of such investment trust properties shall be represented separately for each type of commodities investment, etc. transaction.

- (13) In addition to those referred to in the above items, matters required to be represented in an investment management report prepared under the laws or regulations in a foreign jurisdiction where such foreign investment trust was established (if there is no special provisions in respect of an investment management report prepared under the laws or regulations in a foreign jurisdiction where such foreign investment trust was established, matters equivalent to matters required to be represented referred to in the items of Article 58.1 of Investment Trust Properties Computation Regulations)

If representation is made in accordance with Article 58.1 of the Investment Trust Properties Computation Regulations, VI-3-2-3 (2) shall apply.

VI-3-2-7 Entries in notification regarding foreign investment corporation

Entries of the matters referred to in the items of Article 220.1 of the Investment Trust Law and the matters referred to in the items of Article 261.2 of the Investment Trust Law Enforcement Regulations in a notification regarding a foreign investment corporation shall be made as follows.

- (1) Purpose, trade name and address
- ① Purpose
 - (a) The notification shall contain the purposes stated in the agreements of a foreign investment corporation or documents equivalent thereto.
 - (b) With respect to the number of issues (public sale), the total amount of issued (publicly sold) value, the issue (sale) price, subscribing fee, subscribing unit, subscribing period and others, entries shall be made in accordance with VI-3-2-5 (2).
 - ② Trade name and address

The notification shall contain the trade name or address stated in a registry book of a foreign investment corporation or its equivalent. (The name in an original language shall be noted.)
- (2) Matters regarding organization and officer
- ① Matters regarding organization
 - (a) The notification shall contain the name and the details of an organization of such foreign investment corporation.
 - (b) The notification shall contain the name and the summary of relevant business in respect of corporations concerned which involve in management of such foreign investment corporation in addition to issuing corporation of foreign investment certificates of such foreign investment corporation (such as a person equivalent to assets investment management firms, asset custody firms or a person equivalent thereto and general administrator or a person equivalent thereto).
 - ② Matters regarding officers

The notification shall contain the name, address and business in charge (business of a person equivalent to an executive officer or supervisory officer of an investment corporation) of an officer of such foreign investment corporation.
- (3) Matters regarding control and investment management of assets
- ① Matters regarding control of assets
 - (a) The notification shall contain matters regarding the control of assets until the dissolution of such foreign investment corporation.
 - (b) The notification shall contain the name, the amount of capital and business and the summary of business in respect of assets controlling firm or a person equivalent thereto.
 - (c) Others

The notification shall contain matters regarding a change to agreements or documents equivalent thereto, procedures for renewal, etc. of a contract with a firm concerned, disclosure methods for change and other important matters.
 - ② Matters regarding investment management of assets
 - (a) Policies of investment management

The notification shall contain the policies regarding investment management of assets concretely.
 - (b) Investment objects

The notification shall contain the type of assets to be invested in, investment criteria and, if

- there is an investment plan of types or areas, etc., the percentage thereof.
- (c) Investment limits
 - a. The notification shall contain the grounds for all investment limits stated in laws or regulations, agreements and documents, etc. equivalent thereto.
 - b. The notification shall contain whether a limit exists or not for underwriting of securities, margin transactions, loan, concentrated investment, investment in other funds and investment in illiquid assets, and if such limit exists, the grounds and details thereof.
 - (d) Policies of dividends

The notification shall contain the policies of dividends provided in the agreements or documents, etc. equivalent thereto.
 - (e) The notification shall contain the name, the amount of capital and types of business and the summary of business in respect of assets investment management firm or a person equivalent thereto.
- (4) Matters regarding computation and distribution of profit
- ① Matters regarding computation
 - (a) Valuation of assets

The notification shall contain the computation method (including valuation of assets to be invested in), computation frequency, publication methods, publication frequency and publication place for the amount of net assets per unit of foreign investment certificates.
 - (b) Controlling remuneration, etc.

The notification shall contain the computation method, payment amount, payment methods and payment timing for all remuneration and fees paid from assets of a foreign investment corporation for each payee.
 - (c) Others

The notification shall contain the lifetime of a foreign investment corporation, business year, limit of additional capital contribution or refund of capital contribution, conditions for dissolution, etc.
 - ② Matters regarding distribution of profits

With respect to the payment of profits at the time of the dissolution or distribution of profits at the time of each account settlement, the notification shall contain the timing, place and method of payment from an assets custody firm to a foreign investment corporation, immunity of an assets custody firm and payment from the trusting person to an investor or a person equivalent thereto.
- (5) Matters regarding rights represented by a foreign investment certificate
- The notification shall contain the details of voting rights, rights regarding investors or persons equivalent thereto, rights to receive dividends, rights to receive settled money (including the timing of taking effect and extinction of the right) and procedures of exercise.
- (6) Matters regarding refunding or buying back of a foreign investment certificate
- The notification shall contain the details of refunding or claims to buy by a foreign investment corporation (including the timing of taking effect and extinction of the right) and procedures of the exercise of rights.
- (7) Matters regarding assignment of the whole or part of business of a person equivalent to an assets investment management firm
- The notification shall contain the procedures for business assignment, method to give a notice to investors or persons equivalent thereto and, if an investor or a person equivalent thereto can file a petition of objection to business assignment, the details thereof.
- (8) Matters regarding resignation of person equivalent to assets custody firm and selection of a new assets custody firm or person equivalent thereto
- The notification shall contain the procedures for resignation of a person equivalent to an assets custody firm and selection of a new assets custody firm or a person equivalent thereto.
- (9) In the case of commissioning the authority of investment management of assets by a person equivalent to an assets investment management firm to an other person, the details of such commissioning
- The notification shall contain the concrete details of the authority to be commissioned and fees related to commissioning.

VI-3-3 Remarks on operation related to investment corporation

VI-3-3-1 Notification of change and dissolution of registered investment corporation

- (1) Registered investment corporation change notification
 - ① ① and ② of VI-3-1-2 (3) shall apply to a registered investment corporation change notification.
 - ② When the director-general of a local finance bureau accepted a registered investment corporation change notification pursuant to Article 191.1 of the Investment Trust Law (excluding a change notification in the case of changing of the location of the principal business office to an area where an other local finance bureau has the jurisdiction), the director-general of the local finance bureau shall report to the Commissioner of the Financial Services Agency in a lot each month no later than 15th of the following month by Form VI-6.
 - ③ In the case where it has been found through a change notification that a person who has newly become an executive officer falls under any of (2) to (5) of Article 98 of the Investment Trust Law, the case where it has been found that a person who has newly become a supervisory officer falls under any of the items of Article 100 of the Investment Trust Law or the case where it has been found that a person who has newly become accounting auditor falls under any of the items of Article 102.3 of the Investment Trust Law, the authority shall direct to improve promptly and, if prompt improvement has not been seen, the authority shall revoke the registration pursuant to Article 216.1 of the Investment Trust Law.
- (2) Change notification in the case of changing the location of the principal business office to an area where an other local finance bureau has the jurisdiction
 - ① When the director-general of a local finance bureau accepted a change notification to change the location of the principal business office to an area where an other local finance bureau has the jurisdiction, the director-general of the local finance bureau shall, in addition to the transfer procedures provided in Article 275.1 of the Investment Trust Law Enforcement Regulations, send such change notification together with an opinion statement of the local finance bureau made on Form VI-7 and a copy of a report of the latest investigation to the director-general of a local finance bureau which will have the authorization of registration newly.
 - ② The director-general of a local finance bureau which will have the authorization of registration newly shall, when the director-general of the local finance bureau made a registration of change pursuant to Article 275.2 of the Investment Trust Enforcement Regulations, communicate with the director-general of a local finance bureau who has made the previous registration by an electronic mail, etc. of the fact of change registration.
 - ③ The director-general of a local finance bureau who has been communicated from the director-general of a local finance bureau who has newly authorities of registration pursuant to Article 275.2 of the Investment Trust Law Enforcement Regulations shall erase the registration of such investment corporation.
 - ④ When the director-general of a local finance bureau who has newly authorities of registration made registration of a change, such director-general of the local finance bureau shall report to the Commissioner of the Financial Services Agency in a lot each month no later than 15th of the following month by Form VI-8.
- (3) Investment corporation dissolution notification

When the director-general of a local finance bureau has accepted an investment corporation dissolution notification (the Investment Trust Law Enforcement Regulations Form 17), the director-general of the local finance bureau shall report to the Commissioner of the Financial Services Agency in a lot each month no later than 15th of the following month by Form VI-9.

VI-3-3-2 Business report

When the director-general of a local finance bureau has accepted a business report pursuant to Article 212 of the Investment Trust Law, the director-general of the local finance bureau shall prepare a business report sheet and report to the Commissioner of the Financial Services Agency each business period (if such business period is less than six months, six months) by Form VI-10.

VI-3-3-3 Extraordinary report

The director-general of a local finance bureau shall take the following procedures.

- (1) Report to the Commissioner of the Financial Services Agency

When the director-general of a local finance bureau has accepted an extraordinary report pursuant to Article 215.1 of the Investment Trust Law, the director-general of the local finance bureau shall send a copy of the extraordinary report to the Commissioner of the Financial

Services Agency promptly.

(2) Warning to investment corporation

Before the director-general of a local finance bureau warns an investment corporation pursuant to Article 215.2 of the Investment Trust Law, the director-general of the local finance bureau shall discuss with the Commissioner of the Financial Services Agency.

In discussing, the director-general of a local finance bureau shall refer the result and opinion of consideration at the local finance bureau.

VI-3-3-4 Discussion, etc. with the Financial Services Agency for permission, etc. or administrative dispositions, etc. in respect of investment corporation, etc.

(1) Discussion, etc. with the Financial Services Agency for permission, etc. in respect of investment corporation, etc.

① The director-general of a local finance bureau shall discuss with the Financial Services Agency before granting the following permission or approval in processing matters delegated to the director-general of the local finance bureau for supervisory operation over an investment corporation:

- (a) permission under Article 81.4 of the Corporation Law which is applied *mutatis mutandis* under Article 73.4 of the Investment Trust Law;
- (b) permission under Article 82.4 of the Corporation Law which is applied *mutatis mutandis* under Article 73.4 of the Investment Trust Law;
- (c) permission under Article 297.4 of the Corporation Law which is applied *mutatis mutandis* under Article 90.3 of the Investment Trust Law;
- (d) permission under Article 318.5 of the Corporation Law which is applied *mutatis mutandis* under Article 94.1 of the Investment Trust Law;
- (e) permission under Article 371.2 or 371.4 (including the *mutatis mutandis* application under Article 371.5 of the Corporation Law) of the Corporation Law which is applied *mutatis mutandis* under Article 115.1 of the Investment Trust Law;
- (f) permission under Article 433.3 of the Corporation Law which is applied *mutatis mutandis* under Article 128-3.2 of the Investment Trust Law;
- (g) permission under Article 442.4 of the Corporation Law which is applied *mutatis mutandis* under Article 132.2 of the Investment Trust Law;
- (h) permission under Article 371.2 or 371.4 (including the *mutatis mutandis* application under Article 371.5 of the Corporation Law) of the Corporation Law which is applied *mutatis mutandis* under Article 154-3.2 of the Investment Trust Law;
- (i) permission under Article 500.2 of the Corporation Law which is applied *mutatis mutandis* under Article 157.3 of the Investment Trust Law;
- (j) approval under Article 117 (9) of the Investment Trust Law.

② The director-general of a local finance bureau shall discuss with the Financial Services Agency before exercising the following authorities in processing matters delegated to the director-general of the local finance bureau for supervisory operation over an investment corporation:

- (a) issuance of an order under Article 307.1 of the Corporation Law which is applied *mutatis mutandis* under Article 94.1 of the Investment Trust Law;
- (b) appointment of a person who shall perform the duties of an officer temporarily pursuant to Article 108.2 of the Investment Trust Law;
- (c) issuance of an order pursuant to Article 359.1 of the Corporation Law which is applied *mutatis mutandis* under Article 110.2 of the Investment Trust Law;
- (d) issuance of an order pursuant to Article 162 of the Investment Trust Law;
- (e) appeal to a court for the issuance of an order to dissolve an investment corporation pursuant to Article 824.1 of the Corporation Law which is applied *mutatis mutandis* under Article 144 of the Investment Trust Law;
- (f) appeal to a court for a disposition such as the appointment of a controller pursuant to Article 825.1 of the Corporation Law which is applied *mutatis mutandis* under Article 144 of the Investment Trust Law;
- (g) appointment of a liquidation executor or liquidation supervisor pursuant to Article 151.3 of the Investment Trust Law;
- (h) appointment of a liquidation executor or liquidation supervisor pursuant to Article 151.4 of the Investment Trust Law;
- (i) appointment of a liquidation executor or liquidation supervisor pursuant to Article 151.5 of the Investment Trust Law.

- the Investment Trust Law;
 - (j) removal of a liquidation executor or liquidation supervisor pursuant to Article 153.1 of the Investment Trust Law;
 - (k) appointment of a liquidation executor or liquidation supervisor pursuant to Article 153.1 of the Investment Trust Law;
 - (l) determination of the amount of remuneration of a liquidation executor pursuant to Article 154.2 of the Investment Trust Law or determination of the amount of remuneration of a liquidation supervisor pursuant to Article 154.2 of the Investment Trust Law which is applied *mutatis mutandis* under Article 154-2.2 of the Investment Trust Law;
 - (m) appointment of an appraiser of claims with uncertain value pursuant to Article 501.1 of the Corporation Law which is applied *mutatis mutandis* under Article 157.3 of the Investment Trust Law;
 - (n) appointment of a person who keeps books and records pursuant to Article 508.2 of the Corporation Law which is applied *mutatis mutandis* under Article 161 of the Investment Trust Law;
 - (o) appointment of a person who shall perform the duties of a temporary liquidity executor or temporary liquidity supervisor pursuant to Article 108.2 of the Investment Trust Law which is applied *mutatis mutandis* under Article 153.2 of the Investment Trust Law;
 - (p) immediate appeal pursuant to Article 872 of the Corporation Law which is applied *mutatis mutandis* under Articles 84.2, 139-9.8, 139-10.2, 141.3, 144, 149-3.4, 149-8.4, 149-13.4, 150 and 163 of the Investment Trust Law.
- ③ if the director-general of a local finance bureau has determined to permit or approve for the matters under the above ①, the director-general of the local finance bureau shall give a notice to an applicant for the permission or approval by Form VI-11, or if the director-general of a local finance bureau has determined not to permit or approve for the matters under the above ①, the director-general of the local finance bureau shall give a notice to an applicant for the permission or approval by Form VI-12.
- (2) Discussion, etc. with the Financial Services Agency for administrative dispositions, etc.
- ① The director-general of a local finance bureau shall discuss with the Financial Services Agency concerning the following matters before processing matters delegated to the director-general of the local finance bureau for supervisory operation over an investment corporation.
- The details of examination and opinions of the local finance bureau shall be referred to such discussion:
- (a) issuance of an order to improve business management under Article 214.1 of the Investment Trust Law;
 - (b) revocation of registration under Article 216 of the Investment Trust Law.
- ② If the director-general of a local finance bureau makes administrative dispositions to a founding planner or an investment corporation, etc., the director-general of the local finance bureau shall hear opinions in advance from, if the founding planner of an investment corporation in the process of its foundation or investment corporation or assets management firm, a person commissioned further from such assets management firm pursuant to Article 202.1 of the Investment Trust Law, assets custody firm or general administrator is located in an area under the jurisdiction of an other director-general of a local finance bureau, such other director-general of the local finance bureau in principle, and communicate concerning the result of such processing.
- (3) Notice to chief of relevant administrative organization
- Remarks shall be made on the followings when the authority gives a notice to the chief of a relevant administrative organization pursuant to Articles 132.6 and 135.1 of the Investment Trust Law.
- ① In the case of giving a notice concerning registration application under Article 187 of the Investment Trust Law, the notice shall be addressed to the relevant section of the relevant division of the relevant administrative organization promptly after the acceptance of the registration application.
 - ② In the case of giving a notice concerning the notifications under the items of Article 132.3 of the Investment Trust Law Enforcement Order, the notice of the details of the notification accepted during the same month shall be given to the relevant section of the relevant division of the relevant administrative organization no later than the end of the following month.
- (4) Further delegation to the director of a local finance office, etc.
- The director-general of a local finance bureau may delegate further to the director of a local

finance office, the chief of Otaru Sub-Branch Office or Kitami Sub-Branch Office which has the jurisdiction over the location of an applicant and an investment corporation for the following operations among operations delegated to the director-general of a local finance bureau pursuant to Article 135 of the Investment Trust Law:

- ① operations regarding acceptance of a notification of establishment under Article 69.1 of the Investment Trust Law;
- ② operations regarding acceptance of a notification under Article 152.1 of the Investment Trust Law;
- ③ operations regarding acceptance of a registration application under Article 188.1 of the Investment Trust Law;
- ④ operations regarding acceptance of a notification of a change under Article 191.1 of the Investment Trust Law;
- ⑤ operations regarding acceptance of a notification under Article 192.1 of the Investment Trust Law.

VI-3-3-5 Issuance of certificate

(1) Issuance of certificate to trust company, etc.

- ① Issuance of certificate for relief of registration and license tax on ownership transfer
Issuance, etc. of certificates provided in Article 31-5.2 of the Special Taxation Measures Law Enforcement Regulations in respect of trust companies, etc. for the relief of registration and license tax under Article 83-2.2 of the Special Taxation Measures Law in respect of trust companies, etc. shall be handled as follows.

It shall be noted that the day on which the provisions of Article 83-2.2 of the Special Taxation Measures Law are applicable in respect of such trust company, etc. shall be within one year after the acquisition of such specific assets.

- (a) An application for certifying the relief of registration and license tax for the transfer of ownership from a trust company, etc. and a certificate issued by the Commissioner of the Financial Services Agency shall be prepared by the Form VI-13.
- (b) The authority shall require the applicant to state stipulated matters in an application for certificate and require the applicant to attach a copy, etc. of real estate purchase and sale contract in order to confirm the date of entering into purchase and sale contract and the date of acquisition of real estate stated in an application;

In the case where there is a statement in the application that the type of building is a warehouse, a certificate by an administrative scrivener made on Form IV-13-2 shall be attached in order to confirm the ratio of floor space other than the warehouse.

(Note) In the case where there are only warehouses as the type of building, it shall be noted that a certificate shall not be issued because the provisions of Article 83-2.2 of the Special Taxation Measures Law are not applicable.

- (c) If an application for certificate has been filed, the authority shall confirm the following matters concerning the entries in the application by attached documents, etc. and issue the certificate:
 - a. In the case where there is a statement that the type of building is a warehouse, the ratio of floor space other than the warehouse shall be stated.
 - b. There is a statement in the investment trust agreements as the policies for investment management of the investment trust that the ratio of the total amount of values of specific real estate (which means specific real estate provided in Article 83-2.2 (1) of the Special Taxation Measures Law) to the total amount of values of specific assets among trust properties under such investment trust (hereinafter in (1), referred to as "ratio of specific real estate") shall be at least 75/ 100.
 - c. If funds are borrowed, such borrowing shall be made from an eligible institutional investor under Article 2.3 (1) of the F.I. Act.
 - d. Any of the following requirements shall be met:
 - i) The ratio of specific real estate shall be at least 75/ 100.
(If the ratio of specific real estate can be confirmed as at least 75/ 100 by filed assets investment management report, such requirement shall be deemed to be met.)
 - ii) The ratio of specific real estate is expected to be at least 75/ 100 as a result of the acquisition of real estate for which a trust company, etc. wishes to make it applicable by the application.
(If the requirements are met under VI-3-3-5, the authority shall require the attachment of

the state of specific assets made on Form VI-14 as of the application date, and confirm by such attachments.)

② Issuance of certificate for relief of real estate acquisition tax

Issuance, etc. of certificates provided in Article 7.9 of the Local Tax Law Enforcement Order Supplementary Provisions for the relief of real estate acquisition tax under Article 11.8 of the Local Tax Law Supplementary Provisions in respect of a trust company, etc. shall be handled as follows.

- (a) An application for certificate for the relief of real estate acquisition tax from a trust company, etc. and a certificate issued by the Commissioner of the Financial Services Agency shall be made on Form VI-15.
- (b) The authority shall, upon the acceptance of an application for certificate, confirm the following matters by attachments, etc. in respect of the entries in the application and issue the certificate.
 - a. There shall be a statement in the investment trust agreements as the policies of investment management of the investment trust that the ratio of specific real estate shall be at least 75/ 100 shall be made.
 - b. If funds are borrowed, such borrowing shall be made from, among eligible institutional investors under Article 2.3 (1) of the F.I. Act, those prescribed by the Ministry of General Affairs Ordinance.
 - c. Specific assets under investment management by such investment trust shall meet any of the following requirements:
 - i) The ratio of specific real estate shall be at least 75/ 100.
(If the ratio of specific real estate can be confirmed to be at least 75/ 100 by the submitted investment management report, such requirement shall be deemed to be met.)
 - ii) The ratio of specific real estate is expected to be at least 75/ 100 as a result of the acquisition of real estate for which a trust company, etc. wishes to make it applicable by the application.
(If the requirements are met under VI-3-3-5, the authority shall require attachment of the state of specific assets as of the application date made on Form VI-14, and confirm by such attachments.)

(2) Issuance of certificate to investment corporation

① Issuance of certificate for relief of registration and license tax on ownership transfer

Issuance, etc. of certificates provided in Article 31-5.3 of the Special Taxation Measures Law Enforcement Regulations for the relief of registration and license tax under Article 83-2.3 of the Special Taxation Measures Law in respect of an investment corporation shall be handled as follows.

It shall be noted that the day on which the provisions of Article 83-2.3 of the Special Taxation Measures Law are applicable in respect of such investment corporation shall be within one year after the acquisition of such specific assets.

- (a) An application for certificate for the relief of registration and license tax on ownership transfer from an investment corporation and a certificate issued by the director-general of a local finance bureau shall be made by Form VI-16.
- (b) The authority shall require the applicant to state stipulated matters in an application for certificate and require the applicant to attach a copy, etc. of a real estate purchase and sale contract in order to confirm the date of entering into purchase and sale contract and the date of acquisition of the real estate stated in an application;
In the case where there is a statement in the application that the type of building is a warehouse, a certificate by an administrative scrivener made on Form IV-13-2 shall be attached in order to confirm the ratio of floor space other than the warehouse.
(Note) In the case where there are only warehouses as the type of building, it shall be noted that a certificate shall not be issued because the provisions of Article 83-2.3 of the Special Taxation Measures Law are not applicable.
- (c) If an application for certificate has been filed, the authority shall confirm the following matters concerning entries in the application by attached documents, etc. and issue the certificate.
 - a. In the case where there is a statement that the type of building is a warehouse, the ratio of floor space other than the warehouse shall be stated.
 - b. There shall be a statement in the agreements as the policies of investment management of assets that the ratio of the total value of specific real estate (which means specific real estate provided in Article 83-2.3 (1) of the Special Taxation Measures Law) to the total value of

specific assets held by the investment corporation (hereinafter in (2), referred to as "ratio of specific real estate") shall be at least 75/ 100.

- c. Such applicant shall be a person registered under Article 187 of the Investment Trust Law.
- d. If funds are borrowed, such borrowing shall be made from an eligible institutional investor under Article 2.3 (1) of the F.I. Act.
- e. Any of the following requirements shall be met:
 - i) The ratio of specific real estate shall be at least 75/ 100.
(If it can be confirmed that the ratio of specific real estate is at least 75/ 100 by filed properties investment management report, such requirement shall be deemed to be met.)
 - ii) The ratio of specific real estate is expected to be at least 75/ 100 as a result of the acquisition of real estate for which an investment corporation wishes to make it applicable by the application.
(If the requirements are met under VI-3-3-5 (including the first fiscal year), the authority shall require the attachment of the state of specific assets made on Form VI-14 as of the application date, and confirm by such attachments.)

② Issuance of certificate for relief of real estate acquisition tax

Issuance, etc. of certificates provided in Article 7.11 of the Local Tax Law Enforcement Order Supplementary Provisions for the relief of real estate acquisition tax under Article 11.9 of the Local Tax Law Supplementary Provisions in respect of an investment corporation shall be handled as follows.

- (a) An application for certificate for the relief of real estate acquisition tax from an investment corporation. and a certificate issued by the director-general of a local finance bureau shall be made by Form VI-17.
- (b) The authority shall, upon the acceptance of an application for certificate, confirm the following matters concerning the entries in the application by attachments, etc. and issue the certificate.
 - a. There shall be a statement in the agreements as the policies of investment management of assets that the ratio of specific real estate shall be at least 75/ 100.
 - b. If funds are borrowed, such borrowing shall be made, among eligible institutional investors under Article 2.3 (1) of the F.I. Act, those prescribed by the Ministry of General Affairs Ordinance.
- c. Specific assets under investment management by such investment corporation shall meet any of the following requirements:
 - i) The ratio of specific real estate shall be at least 75/ 100.
(If it can be confirmed that the ratio of specific real estate is at least 75/ 100 by filed assets investment management report, such requirement shall be deemed to be met.)
 - ii) The ratio of specific real estate is expected to be at least 75/ 100 as a result of the acquisition of real estate for which an investment corporation wishes to make it applicable by the application.
(If the requirements are met under VI-3-3-5 (including the first fiscal year), the authority shall require the attachment of the state of specific assets made on Form VI-14 as of the application date, and confirm by such attachments.)

VII. Supervisory Valuation Items and Procedures (Investment Advisory and Agent Business)

VII-1 Business control (investment advisory and agent business)

The authority shall verify the business control of a financial instruments firm (limited to a person who carries out the investment advisory and agent business; in VII, the same) with the following remarks.

VII-1-1 Officers of financial instruments firms

(1) Main focus points

Whether the followings are considered appropriately in the process of the determination of the agenda for the selection of an officer of a financial instruments firm.

- ① The candidate is not, or was not at the time of registration, subject to reasons for disqualification (as provided in (a) to (g) of Article 29-4.1 (2) of the F.I Act).

- ② The candidate does not violate the laws or regulations or administrative disposition taken under the laws or regulations for financial instruments business or business incidental thereto.
- ③ The candidate is not subject to the fact to harm the interests of investors in carrying out investment advisory and agent business or investment management business.
- ④ The candidate has not committed an unlawful or grossly improper act of a particularly grave nature regarding the financial instruments business.

(2) Supervisory method and response

If an officer of a financial instruments firm has fallen under any of (a) to (g) of Article 29-4.1 (2) of the F.I. Act, has been found to have fallen under any of (a) to (g) of Article 29-4.1 (2) of the F.I. Act at the time of registration under Article 29 of the F.I. Act or has fallen under (6) or (8) to (10) of Article 52.1 of the F.I. Act, the authority shall consider the disposition such as the issuance of an order to remove the officer under Article 52.2 of the F.I. Act.

In addition, the authority shall hold a hearing in depth concerning determination process for the selection agenda of an officer of such financial instruments firm, require to make a report under Article 56-2.1 of the F.I. Act when needed, and if a gross problem is found for the business management system of such firm and it is necessary and appropriate in the public interest or to protect investors, the authority shall consider responses such as the issuance of an order to improve business management.

VII-2 Appropriateness of business (investment advisory and agent business)

The authority shall verify the appropriateness of business of a financial instruments firm with the following remarks.

VII-2-1 Appropriateness of business for investment advisory business

VII-2-1-1 Compliance system

An investment advisory firm (which means, among financial instruments firms, a person carrying out investment advisory business (which means business provided in Article 2.8 (11) of the F.I. Act; in VII, the same); in VII, the same) takes a role to contribute the formation of assets of a customer by means of providing the customer with information of investment judgment based on analysis of value, etc. of securities or value, etc. of a financial instrument. An investment advisory firm is required to think first of a customer's interest and carry out the business faithfully therefore, and needs to manage the business in a sound and appropriate manner under high self-discipline.

The authority shall make responses to such compliance systems of such financial instruments firms by focus points of system implementation and supervisory methods under III-2-1 in principle, as well as, in addition, verify widely including the state of compliance with self-regulatory rules.

VII-2-1-2 Solicitation and explanation system

(1) Prohibition of exaggerated advertisement, etc.

- ① Whether, in the case of an advertisement referring to each issue name in respect of performance records of advice, the investment advisory firm represents only issue name which is favorable to the investment advisory firm.
- ② Whether an investment advisory firm represents without showing the ground that its performance records, details or methods of advice are extremely more excellent than other investment advisory firm.
- ③ Whether, in the case where the period or the number of customers, etc. of solicitation to customers are not limited, the investment advisory firm represents to give a false impression that these were limited.
- ④ Whether an investment advisory firm which is not registered for investment management business makes representation to give investors false impression that such firm were allowed to carry out investment management business.

(2) Supervisory method and response

With respect to the issues of an advertisement of an investment advisory firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an investment advisory firm through

holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VII-2-1-3 Cancellation of investment advisory contract (cooling-off)

- (1) Remarks on cancellation of investment advisory contract (cooling-off)
 - ① "Amount of expense ordinarily required for entering into an investment advisory contract" provided in Article 115.1 (1) of the F.I. Business Ordinance means telephone bill, envelope fee, etc. and does not include travel expense, etc.
 - ② For the purpose of computing "number of days from the day on which a written statement concerning concluded transaction has been received until the cancellation time" provided in Article 115.1 (3) of the F.I. Business Ordinance, the day on which such written statement has been received and the day on which a written statement to cancel the contract has been dispatched shall be included.
- (2) Supervisory method and response

With respect to the issues of the cancellation of a contract (cooling-off) of an investment advisory firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an investment advisory firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VII-2-1-4 Measures to prevent the negative effects

- (1) Remarks in the case of carrying out more than one type of businesses

The authority shall verify the measures to prevent the negative effects according to the scale of business in the case where an investment advisory firm carries out more than one type of businesses (which means types of businesses provided in Article 29-2.1 (5) of the F.I. Act) considering to ensure the appropriateness of business such as the prevention of conflicts of interest with, for example, the following remarks.

 - ① Whether an appropriate measures have been taken such as the implementation of an internal control system for the prevention of the negative effects according to the type of business as measures to prevent the negative effects between different types of businesses.
 - ② Whether, with respect to "undisclosed information" under Article 147 (2) of the F.I. Business Ordinance, effective information control is ensured by the implementation of information controlling measures, etc. by means such as the appointment of a controller and implementation of rules for control, etc. and appropriate recognition and verification of the usage of such information and reviewing such information control method.
- (2) Supervisory method and response

With respect to the issues of measures to prevent the negative effects taken by an investment advisory firm which carries out more than one type of business found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an investment advisory firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VII-2-1-5 Measures to prevent agent or intermediary firm from violation of laws or regulations

It is important that the authority shall instruct an agent or intermediary firm to implement a customer control system to recognize attributes, etc. of customers and trading situation accurately and require such agent or intermediary firm thorough compliance with laws and regulations after recognizing its investment solicitation situation, in light of ensuring appropriate investment solicitation according to customer attributes, etc. when an investment advisory firm commissions the agent or intermediary firm to carry out business. The authority shall verify its system to prevent the violation of laws or regulations with the following remarks.

- (1) Selection of agent or intermediary firm
 - ① Remarks on selection of agent or intermediary firm
 - (a) Whether, in entering into a contract to commission agent or intermediary business, the investment advisory firm considers fully positioning on the business management control and methods, etc. of the recognition of various risks and risk control associated with such commissioning.
 - (b) Whether an investment advisory firm considers fully whether the agent or intermediary firm has credentials to carry out the business in a sound and appropriate manner. Whether, in the case where an agent or intermediary firm engages in other business particularly, the investment advisory firm considers fully not only whether the engagement in such other business has no likeliness to harm the social reputation as an agent or intermediary firm, but also the reputation, etc. of a belonging firm (which means an investment advisory firm entering into an investment advisory contract for which the agent or intermediary firm acts as an agent or intermediary; in VII, the same).
 - (2) Measures to ensure the appropriateness, etc. of business of agent or intermediary firm by a belonging firm
 - ① Implementation of internal control system for supervision of agent or intermediary firm
 - (a) Whether a belonging firm implements a system to make appropriate supervision over an agent or intermediary firm such as the establishment of a division or appointment of a person in charge responsible for taking measures to ensure sound and appropriate business management of business related to agent or intermediary business (including business supervision system over an agent or intermediary firm).
 - (b) Whether a belonging firm implements an internal control system to verify whether measures to ensure the appropriateness, etc. of business related to business or intermediary business carried out by each agent or intermediary firm are taken appropriately by such division or person in charge.
 - ② Remarks on measures for necessary and appropriate supervision, etc. over agent or intermediary firm
 - (a) Whether a belonging firm takes the following measures, and monitors the performance of, such measures in order to ensure sound and appropriate management of business related to agent or intermediary business carried out by an agent or intermediary firm.
 - a. measures to make instruction concerning agent or intermediary business and to hold training to ensure the compliance with laws and regulations, etc. for agent or intermediary business in respect of an agent or intermediary firm and its employees; and
 - b. measures to make necessary and appropriate supervision, etc. over an agent or intermediary firm such as verifying whether the agent or intermediary firm carries out such agent or intermediary business accurately by means such as confirming periodically or when needed the real state of investment solicitation related to agent or intermediary business by the agent or intermediary firm and the performance of other business engagement and require improvement when needed.
 - (b) Whether a belonging firm implements a system such as reflecting the result, etc. of the above monitoring of appropriate business instruction by a belonging firm and appropriate business management of an agent or intermediary firm such as verification by a division in charge of the belonging firm and reporting to the management team when needed.
 - ③ Measures to cancel a contract to commission agent or intermediary business

Whether, if a problem has been found as a result of monitoring, etc. over an agent or intermediary firm, a system to take appropriate measures has been implemented such as the instruction to the agent or intermediary firm and cancellation of a commissioning contract. Whether a system to ensure protection of customers appropriately has been implemented for the cancellation of a commissioning contract.
 - ④ Measures for settlement of grievances

Whether a response system for grievances such as the clarification of a grievances contact place for customers for agent or intermediary business carried out by an agent or intermediary

firm and the establishment of a division for the settlement of grievances, and the procedures for processing grievances are implemented.

(3) Supervisory method and response

With respect to the issues related to the selection, etc. of an agent or intermediary firm or measures by a belonging firm to ensure the appropriateness, etc. of business of an agent or intermediary firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a belonging firm, etc. through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VII-2-2 Appropriateness of agent and intermediary business

The authority shall verify the appropriateness of business of an agent and intermediary firm with remarks on, for example, the following supervisory focus points. It shall be noted that measures to ensure the appropriateness of business that an agent and intermediary firm is required shall be judged comprehensively based on the types and scale of business and other business engagement of the firm, and the failure of satisfaction of a part of supervising valuation items does not necessarily mean inappropriate.

VII-2-2-1 Compliance system

The creation of the system of agent and intermediary business is expected to contribute to ensuring and improvement of access to investment services by investors and efficient use of various sales channels by financial instruments firms, etc. On the other hand, sound and appropriate management of agent and intermediary business must be ensured in order to prevent unfair transactions using trading relationship as a general business operator.

In supervising agent and intermediary firms, the authority shall make timely and appropriate supervision over agent and intermediary firms and belonging firms in order to ensure appropriate and accurate carrying out of agent and intermediary business. Particularly, in the case where, for example, an agent and intermediary firm engages in other business such as the case where an existing general business operator enters into agent and intermediary business, it shall be noted that inappropriate treatment such as the abuse of the dominant bargaining position and using customer information for other purpose shall be prevented.

The authority shall respond to such compliance systems of agent and intermediary firms by focus points of system implementation and supervisory methods in principle under III-2-1, and in addition, makes wide range of verification including compliance with self-regulatory rules.

VII-2-2-2 System implementation by agent and intermediary firms

(1) Main focus points

- ① Whether the internal rules provide for methods of the solicitation of customers, explanation of a contract and furnishing of a written statement concerning concluded transactions concretely, and carrying out appropriate business in compliance with laws and regulations, etc.
- ② Whether methods, etc. for verifying compliance with laws and regulations appropriately are provided concretely.
- ③ Whether the employment of a person with sufficient knowledge regarding agent and intermediary business of the agent and intermediary firm is ensured appropriately.

(2) Supervisory method and response

With respect to the issues of system implementation by an agent and intermediary firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an agent and intermediary firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of

an order to suspend business under Article 52.1 of the F.I. Act.

VII-2-2-3 Providing information to protect investors

(1) Main focus points

- ① System to prevent explanation which may cause false recognition as the abuse of the dominant bargaining position

In the case where an agent and intermediary firm engages in other business, whether the agent and intermediary firm implements a system to prevent explanation which may cause false recognition as the abuse of the dominant bargaining position and cause doubt under the Anti-Monopoly Law in carrying out agent and intermediary business and other business management.

- ② System to prevent false recognition as deposit, etc.

In the case where an agent and intermediary firm is a financial institution such as a bank, etc., whether the agent and intermediary firm implements a system to prevent false recognition of financial instruments as deposit, etc. in acting as an agent or intermediary for entering into an investment advisory contract or discretionary investment contract.

(2) Supervisory method and response

With respect to the issues of providing information to protect investors by an agent and intermediary firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an agent and intermediary firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VII-2-2-4 Measures in the case of accepting agent and intermediary business from more than one belonging firm

(1) Explanation, etc. to customers

Whether, in the case where there are more than two belonging firms, an agent and intermediary firm clarifies the matters referred to in the following ① to ④ to customers in advance. Whether the method of explanation is a method for customers to understand easily as much as possible by means such as using written statements:

- ① if the amount of remuneration payable by a customer is different from the amount of remuneration payable to other belonging firm for the same type of contract, such fact;
- ② if an agent and intermediary firm acts as an agent or intermediary for entering into the same type of investment as a contract to be entered into by a customer on behalf of other belonging firm, such fact;
- ③ the details of the same type of contract under the above ② and other information for customers' reference in response to requests by customers;
- ④ the trade name of a belonging firm which becomes a counterparty for transactions of a customer finally.

(2) Supervisory method and response

With respect to the issues of measures in the case where an agent and intermediary firm accepts agent and intermediary business from more than one belonging firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an agent and intermediary firm through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VII-2-3 Responses in the event of the receipt of information related to continuity problem

Even an individual is qualified for a financial instruments firm and only business guarantee

money is required as financial resources in the case of an individual, and a certain financial instruments firm is not subject to monitoring of net assets or capital requirement ratio. It shall be noted that there is likeliness that a financial instruments firm files a petition for bankruptcy, etc. proceedings commencement before the supervisory authority recognizes the accurate financial conditions of the financial instruments firm. Further, if the authority recognizes, for example, that a financial instruments firm becomes net capital deficiency and will likely insolvent, the authority shall make an effort to confirm the fact in order to verify the necessity of responses fully to protect investors.

Based on the above, the authority shall make an effort to ensure the investor protection by making the following responses in addition to III-3-2, in the case of the recognition of net capital deficiency or likeliness of insolvency of a financial instruments firm, the case of the acceptance of notification of filing petition for bankruptcy, etc. proceedings commencement or the case of the recognition of the likeliness of filing petition for bankruptcy, etc. proceedings commencement.

Each local finance bureau shall make an effort to make responses meeting the real state for an individual case, and inform the Financial Services Agency of the fact situation for such individual case promptly and coordinate concerning policies for responses.

- (1) Responses in the case of recognizing financial problems of financial instruments firm
 - ① The authority shall hold a hearing on the financial conditions of the firm and the state of a contract with a customer (such as the contract period, remuneration and the state of maintenance of fees for cooling off contract) and confirm the fact and encourages establishing the method to eliminate the likeliness of insolvency.
 - ② The authority shall, if a problem for the protection of investors has been found as a result of hearings, issue an order to make reports under Article 56-2.1 of the F.I. Act promptly for the fact and measures to solve the current state.
 - ③ The authority shall follow up the state of the progress of elimination measures after the receipt of reports and, if improvement is not seen, consider responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act.
- (2) The case of recognizing information of filing petition for bankruptcy, etc. proceedings commencement
 - ① The authority shall confirm whether a notification under Article 50.1 (7) of the F.I. Act has been filed and require prompt responses when needed.
 - ② The authority shall recognize, in addition to the fact situation for such case, financial conditions of such financial instruments firm, the state of a contract with a customer (if there is money deposited by a customer, the concrete details thereof), responses to customers and policies, etc. of business continuity promptly through the issuance of an order to make reports under Article 56-2.1 of the F.I. Act.
 - ③ The authority shall follow-up the performance of the details in the reports under ② above, and require close investigation of the policies of the business continuity when needed. In such case, the authority shall consider responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act.
- (3) The case of recognizing information of filing petition of bankruptcy, etc. proceedings commencement by parent companies, etc.

If a person who could grossly influence on business management of a financial instruments firm as a result of filing a petition for bankruptcy, etc. proceedings commencement (hereinafter in VII-2-3, referred to as "parent company, etc.") has filed a petition for bankruptcy, etc. proceedings commencement, the authority shall recognize promptly financial conditions, trading relation with the parent company, etc., the state of a contract with a customer (if there is money deposited by a customer, the concrete details thereof) and policies, etc. regarding the business continuity based on the latest conditions through the issuance of an order to such financial instruments firm to make reports under Article 56-2.1 of the F.I. Act.

- (4) The case of ruling of bankruptcy proceedings commencement
 - ① The authority shall recognize whether a notification under Article 50-2.1 (4) of the F.I. Act has been filed and require prompt responses when needed.
 - ② If necessary for the investor protection, the authority shall make an effort to coordinate with a bankruptcy receiver.
- (5) The case where a business office cannot be identified

If such fact is notified publicly under Article 52.4 of the F.I. Act and such financial instruments firm fails to request after 30 days have passed since the day of such public notice, the authority shall revoke the registration of such financial instruments firm.

- (6) other case where the authority received information which will likely develop into a serious problem of the continuity of a financial instruments firm or its parent company, etc.
- ① The authority shall recognize, in addition to the fact situation of such information, financial conditions, the state of a contract with a customer (if there is money deposited by a customer, the concrete details thereof) and policies, etc. regarding the business continuity of the financial instruments firm promptly through voluntary hearings.
 - ② In the case where such financial instruments firm refuses the hearing under the above ① or there is a concern on the business continuity of such financial instruments firm through hearings under the above ①, the authority shall recognize the fact situation promptly through the issuance of an order to make reports under Article 56-2.1 of the F.I. Act. If necessary for the investor protection, the authority shall consider responses such as the issuance of an order to improve business management under Article 51 of the F.I. Act.

VII-3 Procedures (investment advisory and agent business)

VII-3-1 Registration

Remarks shall be made on the followings for accepting an application for registration. With respect to the judgment of the necessity of registration, and it shall be noted that the judgment should be made comprehensively based on the positioning of each act of a series of acts related to investment advisory and agent business, and it is inappropriate to make a quick judgment of necessity for registration considering only a part of a series of acts.

- (1) The case where registration is not required

Notwithstanding the provisions of Article 29 of the F.I. Act, investment advisory business may be carried out in the following cases.

 - ① The case where Article 61.1 of the F.I. Act is applicable

The case where a juridical person who was established under the laws or regulations in a foreign jurisdiction or an individual who resides in a foreign jurisdiction and carries out investment advisory business in a foreign jurisdiction wishes to carry out investment advisory business only with a person carrying out investment management business or other person provided by the F.I. Act Enforcement Order as a counterparty.
 - ② The case where Article 50-2.3 of the F.I. Act is applicable

The case where a person who is allowed to carry out investment advisory business pursuant to Article 50-2.3 of the F.I. Act carries out investment advisory business during stipulated period.
- (2) Acts to which investment and agent business is not applicable
 - ① Acts to provide unlimited and many persons with an investment judgment based on the analysis of the value, etc. of securities or value, etc. of financial instruments (hereinafter referred to as "investment information, etc.") by means that unlimited and many persons can buy any time.

For example, a person who provides investment information, etc. by means referred to in (a) to (c) below is not required to register for investment advisory and agent business.

Provided, That it shall be fully noted that providing investment information, etc. with high severalty and relativity by using information technology such as the Internet of purchase or use of investment information, etc. is available only for registered members, etc. (single purchase or use is not accepted) shall be required to register despite providing to unlimited and many persons.

 - (a) Sale of newspapers, magazines, books, etc.

(Note) The case where newspapers, magazines, books, etc. are displayed at a shop front of general bookshops, newsstands, etc. and accessible to anyone, at any time and can be bought after seeing them freely and judging. It shall be noted, on the other hand, that registration may be required for sale, etc. of reports, etc. which require subscription directly to the firm, etc.
 - (b) Sale of computer software such as investment analysis tool

(Note) The case where such software can be bought by anyone, at any time and freely at a shop front of a sales shop or by means of download sale, etc. through the network by judging investment analysis algorism and other function, etc. of a computer software. It shall be noted, on the other hand, that registration may be required if the use of such software requires continuous support, etc. from the sales firm, etc, such as data related to

investment information, etc.

- (c) Act to give an advice on value, etc. of financial instruments

(Note) With respect to financial instruments other than securities, an act to give an advice on the value, the amount of consideration for options, trend of indices without giving an advice on investment judgment based on such analysis or an act without entering into a contract to pay remuneration is not regarded as investment advisory business.

For example, giving an advice on average winter temperature in Japan for this year is not regarded as investment advisory business.

- ② Act which is not regarded as acting as an intermediary for entering into discretionary investment contract, etc.

Registration of investment advisory and agent business is not required to perform an act, which is not regarded as intermediary and is commissioned by an investment advisory firm or discretionary investment firm.

It could be thought for example that a person who is commissioned from an investment advisory firm or discretionary investment firm, and performs, only a part of operational processing of the acts referred to in the following (a) to (c) may not be required to register for investment advisory or agent business.

- (a) Simple distribution and furnishing of product introduction leaflet, pamphlet, contract subscription form, etc.

(Note) It shall be noted that the explanation of methods for entries in documents distributed or furnished may be regarded as acting as an intermediary, although informing the trade name or contact place, etc. of an investment advisory firm or discretionary investment firm is not regarded as acting as an intermediary.

- (b) Receipt and recovery of contract subscription form and its attachments, etc. (excluding confirmation, etc. of entries)

(Note) It shall be noted that an act of confirmation, etc. of the entries in a contract subscription exceeding operations of simple receipt or recovery of a contract subscription form or pointing out errors or omission or omission of attachments to documents may be considered to be acting as an intermediary.

- (c) General explanation of structure of, and method to use, financial instruments at a presentation meeting, etc.

VII-3-2 Remarks on deposit, etc. of business guarantee money

- (1) If an investment advisory and agent firm files, after making new deposit, the original deposit certificate in order to replace articles already deposited, the authority shall certify the issuance of the original deposit certificate made on Form V-I for the original deposit certificate already accepted and kept and return the original deposit certificate already accepted and kept to the investment advisory and agent firm.
- (2) If an investment advisory and agent firm files, after filing an application for substitute deposit or attached deposit with a deposit office, the original certificate of acceptance in order to replace redemption money already deposited, the authority shall furnish a certificate of safe keeping in accordance with (5) below and return the master original deposit certificate already accepted and kept to the investment advisory and agent firm.
- (3) If an investment advisory and agent firm files an application for an approval of a change in, or cancel of, a contract to be replaced with business guarantee money and the authority judges that the investor protection will not be harmed, the authority shall approve such application by a guarantee contract change approval made on Form V-2 or by guarantee contract cancellation approval by Form V-3.
- (4) A public notice for the recovery of business guarantee money shall be given by Form V-4.
- (5) A certificate of safe keeping by Form V-5 shall be issued in the case of the acceptance of the original deposit certificate.
- (6) The authority shall inform all registration applicants, etc. that, if business guarantee money is deposited in the form of national government bonds under Article 31-2.9 of the F.I. Act, negative prescription is completed after a certain period pursuant to the Law on National Government Bonds, and the deposit loses effectiveness.

VIII. Supervisory Valuation Items and Procedures (Registered Financial Institution)

VIII-1 Appropriateness of business (registered financial institution)

III-2 (excluding III-2-3-4 (2), III-2-6 (1) ②, III-2-8 (3) and III-2-9), IV-1-3, IV-3-1 (excluding IV-3-1-2 (1), IV-3-1-4 (4) and IV-3-1-5), IV-3-3 (excluding (1) to (3) of IV-3-3-1, ③ to ⑧ of IV-3-3-2 (4), IV-3-3-4 and IV-3-3-5; *provided*, that this shall not apply to the case where a registered financial institution conducts so called foreign exchange margin transactions as a business), VI-2 and VII-2 shall apply to the appropriateness of business of registered financial institutions, and remarks shall be made on the followings.

A theoretical price under (a) and (b) of IV-3-1-2 (4) ③ and a price computed or formulated by a commissioning financial instruments firm may be used for financial instruments intermediary business and internal rules under (b) and (d) of ③, respectively.

VIII-1-1 Appropriateness of individual business

- (1) Whether, in the case of a registered financial institution engaged in dealing operation of national government bonds, etc., short-term securities or asset finance type securities, such registered financial institution conducts trading operation, etc. as a unit for the investment purpose (in the case of a registered financial institution having specific trading account (in the case of a branch of a foreign bank, an account similar to a specific trading account; hereinafter the same), the case conducting for an account other than specific trading account; hereinafter the same) in respect of securities, etc. related to such dealing operations. Whether a registered financial institution introduces a customer between these divisions.
- (2) With respect to a registered financial institution conducting any of dealing operations of national government bonds, etc., futures brokerage business, operations of purchase or sale, etc. of short-term securities, purchase or sale, etc. of assets finance type securities:
 - ① Whether a registered financial institution clarify business and financial conditions by means of accounting and handling of securities related to such operations separate from accounting and handling of securities related to other operations.
 - ② Whether it is ruled that a registered financial institution shall not make the following inter-account transfers for securities handled in the course of such operations:
 - (a) In the case of a registered financial institution without specific trading account, inter-account transfer between a security for sale account and a security account other than a security for sale account;
 - (b) In the case of a registered financial institution with specific trading account, inter-account transfer between a security for sale account in a specific trading account and a security account other than a security for sale account in a specific trading account and inter-account transfer between a security for sale derivatives account in a specific trading account and a security derivatives account other than a security for sale derivatives account in a specific trading account.
- (3) Whether a registered financial institution conducting debt securities with option trading makes an effort to publish the indication of option premium of options with underlying assets of liquid national government bonds to investors by appropriate means such as posting at the front of its office.
- (4) Whether a registered financial institution does not grant credit automatically to customers for the purpose of concluding financial instruments transactions, making up losses arisen from financial instruments transactions or depositing customer margins (including additional margins) excluding the case provided in Article 149-2 of the F.I. Business Ordinance. Whether it is ruled that a registered financial institution does not grant credit clearly for the above purpose
 - (Note) It shall be noted that automatic credit granting applies to an overdraft.
For this purpose, for example the following measures shall be taken:
 - ① A registered financial institution carrying out futures broking business shall prohibit opening of a debt security futures trading account newly and arranging an overdraft for such account, and shall not make automatic transfer from an overdraft account to a debt security futures trading account with the same account holder name.
 - ② A registered financial institution carrying out financial instruments intermediary business shall not, in the case where transactions offered by a customer fails to be concluded because of the shortage of the balance at a securities account opened by the customer with a commissioning financial instruments firm, perform financial instruments intermediary act by granting, or promising to grant, credit automatically to conclude such transactions.

- (5) With respect to a registered financial institution conducting futures brokerage business:
- ① Whether, in the case of conducting transactions using a terminal controlled by GLOBEX Corporation, the registered financial institution states the fact clearly in the provisions for acts performed as a business, and provides handling rules for trading.
 - ② Whether it is ruled that, with respect to processing money credited for a debt security futures trading account, the registered financial institution appoints a person in charge for such customer in advance and register the name of such customer (or a person in charge of money handling of the customer) and obtains an agreement from the customer by telephone, etc. in advance each time.
- (6) Whether a registered financial institution carrying out business of short-term securities trading, etc. fulfills, at a division having overall responsibility of such business (order acceptance, trading and delivery), adequately blocking, etc. of outflow or inflow of so called subtlety information between business related to issuance and trading of commercial paper and short-term corporate debt securities, etc. (which means short-term corporate debt securities as defined in the Law on Book Transfer of Corporate Debt Security, etc., short-term corporate debt securities as defined in the Insurance Business Law, special short-term corporate debt securities as defined in the Law on Liquidation of Assets, short-term commerce and industry debt securities as defined in the Central Cooperative Bank for Commerce and Industry Law, short-term debt securities as defined in the Credit Institution Law and short-term agriculture and forestry debt securities as defined in the Agriculture and Forestry Central Bank Law) and loan business, etc.
- (7) With respect to a registered financial institution conducting sale of securities related products:
- ① Whether, in the solicitation of packaged sale of deposit and securities related products, the registered financial institution takes necessary measures to prevent a customer from having false impression.
 - ② Whether, in the sale of securities related products such as investment trust, the registered financial institution explains fully to customers concerning risks of price movement, etc. the different from deposit.
- (8) With respect to a registered financial institution carrying out financial instruments intermediary business:
- ① Whether it is ruled that an officer or employee, etc. responsible for the overall control of an organization performing both financial instruments intermediary business and loan business (limited to business handling undisclosed loan, etc. information of a customer which is the issuer of securities; in (8) and VIII-2-1 (2) ⑥, the same):
 - (a) prohibit providing undisclosed loan, etc. information received from a person engaged in loan business to a person engaged in financial instruments intermediary business; or
 - (b) prohibit using undisclosed loan, etc. information received from a person engaged in financial instruments intermediary business for loan business, or prohibit providing it to a person engaged in loan business.
 - ② Whether an internal controller (which means an internal controller as defined in the Japan Securities Dealers Association Self-Regulatory Rules "Rules for Internal Controller, etc. of Association Members"), etc. controls appropriately information related to loan business required to be given a notice to a customer in order to comply with laws or regulations by a person engaged in financial instruments intermediary business and the receipt or giving customer information with a commissioning financial instruments firm for the purpose of carrying out financial instruments intermediary business or compliance by the commissioning financial instruments firm.
- (9) Whether a registered financial institution carrying out business of handling private placement of securities fulfills adequately blocking, etc. of outflow or inflow of so called subtlety information between investment business and securities control business related to loan and securities and taking organizational measures, etc. in respect of a division responsible for business to handle private placement and carrying out thereof.
- Provided*, That this shall not apply to performing an act deemed to be handling of private placement of securities provided in Article 15.3 of the F.I. Act Enforcement Order Supplementary Provisions.
- (10) Whether, if a registered financial institution which is an insurance company commissions a person provided in any of the items (excluding (3)) of Article 15-21.2 of the F.I Act Enforcement Order (hereinafter in (10), referred to as "agent") to carry out specific financial instruments business under Article 33-8.2 of the F.I. Act, the registered financial institution may

commission the agent shop to which the agent belongs to assist such specific financial instruments business.

(11) Supervisory method and response

With respect to the issues of the appropriateness of individual business of a registered financial institution found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a registered financial institution through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed. Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51-2 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VIII-1-2 Prevention of abuse of dominant bargaining position

(1) Abuse of dominant bargaining position in respect of other business engagement

The authority shall supervise an act using the dominant bargaining position on trading in respect of other business engagement inappropriately, referring to Unfair Trading Method Associated with Relaxation of Classification of Business Type and Expansion of Business Area of Financial Institution (1 December 2004: Fair Trade Commission), and it shall be noted that the following acts for example could be considered to be an act using the dominant bargaining position on trading in respect of other business engagement. The authority shall, in the case where an employee of a registered financial institution is engaged in business of an other financial institution, etc., supervise an act using the dominant bargaining position on trading in respect of business of the firm for which the employment has engagement inappropriately.

- ① Whether, if a customer refuses to enter into a financial instruments transactions contract, a registered financial institution suggests to suspend transactions related to loan, etc. other business engagement or to treat unfavorably for such business and effectively forces the customer to enter into a financial instruments transactions contract.
- ② Whether a registered financial institution requests to enter into a financial instruments transactions contract in conducting transactions related to other business engagement with a customer, and effectively forces the customer to follow the request.
- ③ Whether, if a customer enters into a financial instruments transactions contract with a competitor (a competitor for business conducted as a registered financial institution), the registered financial institution suggests the customer to suspend transactions of other business engagement or treat unfavorably regarding such business and disturbs entering into a contract with the competitor.
- ④ Whether a registered financial institution requests a customer not to enter into a financial instruments transactions contract with a competitor in conducting transactions of other business engagement with the customer, and effectively forces the customer to follow the request.

(2) Remarks on prevention of abuse of dominant bargaining position

The authority shall verify the system implementation to prevent the abuse of the dominant bargaining position with the following remarks.

- ① Whether a registered financial institution establishes a division, or appoints a person, responsible for taking measures to prevent such act and implements the internal control system to verify whether appropriate measures to prevent such act are taken by such divisions or person.
- ② Whether trainings are made by a person with knowledge of business operations and work experience of a registered financial institution periodically and when needed in order to prevent such act.
- ③ Whether a registered financial institution implements a system to respond to grievances such as the clarification of a contact place for grievances from customers for such acts, the establishment of a grievances settlement division and the implementation of grievances settlement procedures.

(3) Supervisory method and response

With respect to the issues of the abuse of the dominant bargaining position in respect of other business engagement of a registered financial institution found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of a registered financial institution through holding hearings in depth or collection of reports under Article 56-2.1 of the F.I. Act when needed.

Further, if a gross problem in the public interest or to protect investors has been found, the authority shall make responses such as the issuance of an order to improve business management under Article 51-2 of the F.I. Act, and if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to suspend business under Article 52.1 of the F.I. Act.

VIII-1-3 Remarks on supervision over registered financial institutions which are not members of association, etc.

- (1) Main focus points
 - ① Whether a registered financial institution which is not a member of a financial instruments firms association or a member or trading participant of a financial instruments exchange (hereinafter, referred to as "registered financial institution which is not a member of an association, etc.") implements internal rules appropriately considering the association, etc. rules.
 - ② Whether a registered financial institution which is not a member of an association, etc. ensure to implement a system to ensure appropriate compliance with internal rules (such as informing all officers and employees or verification of their compliance with internal rules).
 - ③ Whether it is ruled that, when there has been an amendment, etc. to association, etc. rules, a registered financial institution which is not a member of an association, etc. reviews the internal rules immediately after, and according to, the amendment, etc.
- (2) Supervisory method and response
 - ① If a registered financial institution which is not a member of an association, etc. fails to prepare, and is not expected to prepare internal rules voluntarily, internal rules for which association, etc. rules have been taken into consideration, the authority shall order the firm to prepare appropriate internal rules under Article 56-4.2 of the F.I. Act. In this case, the authority shall, when there has been an amendment, etc. to association, etc. rules, require the firm to review the internal rules immediately after, and according to, the amendment, etc. together.
 - ② If reviewing internal rules of a registered financial institution is not a member of an association, etc. is needed in light of association, etc. rules and the registered financial institution is not expected to review voluntarily, the authority shall order the firm to make an amendment to internal rules under Article 56-4.2 of the F.I. Act.
 - ③ If it is determined that there is a problem for the preparation of, amendment to and compliance with internal rules of a registered financial institution which is not a member of an association, etc., the authority shall make an effort to recognize the real state through holding hearings in depth and collection of reports under Article 56-2.1 of the F.I. Act. Further, the authority shall make appropriate supervision considering association, etc. rules under Article 56-4.1 of the F.I. Act such as the issuance of an order to improve business management under Article 51-2 of the F.I. Act when needed and the issuance of an order to suspend business under Article 52-2.1 of the F.I. Act.

VIII-2 Procedures (registered financial institution)

VIII-2-1 Registration

The authority shall treat an application for registration filed by a registered financial institution in accordance with III-3-1 (excluding (2) and (4)), VI-3-1 and VII-3-1, and remarks shall be made on the followings. The text shall be amended in reading in the case of Forms accordingly.

- (1) Treatment of registration number

A registration number to be stated in a financial institution registry shall be:
Example) The Director-General of ○○ Finance Bureau No. ○○
- (2) Items of examination of system

In examining whether the applicant is a corporation having personnel resources insufficient to carry out registered financial institution business accurately as provided in Article 33-5.1 (3) of the F.I. Act, the authority shall refer to the application for registration and the attachments and hold a hearing to confirm the followings.
- ① Whether the applicant ensures the organizational system and personnel structure that personnel necessary for accurately carrying out the proposed business is allocated to each

division, and persons responsible for internal control, etc. are allocated properly:

- ② Whether the applicant ensures the employment of personnel required for the following system implementation for the proposed business:
 - (a) preparation and retention of books and records, reports, etc.;
 - (b) disclosure;
 - (c) segregation of customer funds;
 - (d) risk control;
 - (e) computer system control;
 - (f) trades control, customer control;
 - (g) settlement of grievances and troubles; and
 - (h) internal audit.
- ③ Whether the applicant ensures the employment of more than one person with at least three years experience of securities related business among full-time officers and employees. *Provided*, That, in the case of a financial institution wishing to engage in only national government bond counter sale business without underwriting activities or clearing brokerage business, the financial institution is deemed to meet such criteria if it ensures the employment of more than one person who is determined to have knowledge, experience, etc. necessary for accurate carrying out such business. Such conditions shall be confirmed again when the financial institution began securities related business other than such business after the registration.
- ④ Whether, in a business office, etc. of a financial institution carrying out any of, or more than one, overall dealing business of national government bonds, etc., overall business of purchase or sale, etc. of short-term securities or overall business of purchase or sale, etc. of assets finance type securities, organization, division of business operations and authorization of a division in charge of such business is clearly separated and independent from purchase or sale operation, etc. for the investment purpose of securities related to such business and loan business. Whether employees in charge of such business engages in purchase or sale operation for the investment purpose and loan business.
- ⑤ With respect to a financial institution carrying out futures brokerage business
 - (a) Whether the financial institution prevents information of securities futures transaction, etc. of national government bonds, etc. conducted by a customer from being sent to a division of trading for house account and used inappropriately. In this case, the organization, division of business operations and the authorization of a division in charge of overall futures brokerage business, etc. is in principle separated and independent from other business (including registered financial institution business other than business under (2) and (3) of Article 2.8 of the F.I. Act) in a business office, etc. carrying out overall futures brokerage business, etc.
 - (b) It is necessary to prevent solicitation with agreeing to give special facilities such as loan or guarantee to customers in a business office, etc. carrying out futures brokerage business, etc. Whether the financial institution considers that an organization is formed to carry out such business in line with such purpose.
- ⑥ Whether a financial institution carrying out financial instruments intermediary business blocks receipt or giving of undisclosed loan, etc. information of a customer which is the issuer of securities between a person engaged in financial instruments intermediary business and a person engaged in loan business. Whether, for example, a financial institution makes an effort to ensure the effectiveness concerning blocking of receipt and giving of undisclosed loan, etc. information by means such as the implementation of internal rules for the separation of financial instruments intermediary business and loan business and clarification of employees in charge or measures equivalent thereto.
- ⑦ Whether a financial institution which is not a member of a financial instruments firms association implements internal rules to carry out business appropriately after the consideration of the articles of incorporation and rules of a financial instruments firms association according to the type of the proposed business.
- ⑧ III-3-1 (9) ② shall apply to a notification of a change of the total amount of capital contributions of a credit cooperative, etc.
- (3) Remarks on registered financial institutions which have no plan to become a member of a financial instruments firms association or which have no plan to become a member or trading participant of a financial instruments exchange.

The authority shall give the following notices to a registered financial institution which has no plan to become a member of a financial instruments firms association or which has no plan to become a member or trading participant of a financial instruments exchange at the time of an

application for registration and require such financial institution to make an appropriate responses.

- ① If it is determined that there is no appropriate internal rules for which association, etc. rules have been taken into consideration, such registered financial institution shall be ordered to prepare internal rules immediately after the registration in principle.
- ② A registered financial institution which is not a member of an association, etc. may be ordered to amend internal rules for which association, etc. rules have been taken into consideration.
- ③ A registered financial institution which is not a member of an association, etc. shall, when ordered to prepare or amend internal rules, etc., prepare or amend internal rules within 30 days and obtain an approval from the Prime Minister.
- ④ A registered financial institution which is not a member of an association, etc. shall, when it wishes to amend or abolish internal rules approved under ③, obtain an approval from the Prime Minister.
- ⑤ The authority shall make an appropriate supervision over business of a financial institution which is not a member of an association, etc. considering association, etc. rules not to harm the public interests or constitute a failure of the investor protection.

VIII-2-2 Approval and notification, etc.

III-3-2 and IV-4-2-4, IV-4-3 and VI-3-2 shall apply.

VIII-2-3 Books and records of business operations

III-3-3 shall apply to handling preparation and retention of books and records of business operation. A system or format used by a commissioning financial instruments firm may be used to prepare books and records regarding financial instruments intermediary business referred to in Article 184.1 (3) of the F.I. Business Ordinance. A financial institution may commission a commissioning financial instruments firm to construct a system or format for such preparation. It shall be noted that such registered financial institution shall have obligation of preparation and retention.

VIII-2-4 Registration of sales representative

IV-4-3 and V-3-2 shall apply.

VIII-2-5 Interpretation of provisions of Article 33 of the F.I. Act

- (1) Interpretation of the provisions of the main text of Article 33.1 of the F.I. Act
 - ① An act prohibited under Article 33.1 of the F.I. Act shall not apply to the following businesses carried out by a bank, cooperative organization financial institution or other financial institution provided in Article 1-9 of the F.I. Act Enforcement Order (hereinafter in VIII-2-4, referred to as "bank, etc."):
 - (a) business to give a business counterparty corporation an advice of the offering of stock to the public, or introduce a business counterparty corporation eligible for offering of stock to the public to an underwriting financial instruments firm; or
 - (b) business to introduce a customer to a financial instruments firm without solicitation.
 - ② "Introduce" under the above ① (b) includes the following acts:
 - (a) A financial instruments firm puts or posts an advertisement media to introduce itself at a business office of such bank, etc.;
 - (b) Explanation of the relationship between such bank, etc. and a financial instruments firm or the business of such financial instruments firm.
- (2) Interpretation of the provisions of Article 33.2 of the F.I. Act

Remarks shall be made on the followings for a written statement brokerage act provided in Article 33.2 of the F.I. Act.

 - ① A bank, etc. shall not solicit a customer to conduct purchase or sale or other type of transactions of securities in carrying out such business: *Provided*, That the following acts shall not be regarded as soliciting act:
 - (a) explanation of the details of such business to a customer;
 - (b) introduction of the details of such business by means such as newspaper, magazine,

- documents, direct mail, home page of the Internet, broadcasting and movie;
- (c) putting an order form related to such business and documents provided in (b) in a business office of such bank, etc or sending them to a customer, or posting such documents in a business office.
- ② A bank, etc. shall receive directions from a customer for the distinction of purchase or sale, issue name, number and price for each transaction for a customer account in the case of an order in writing received by a bank, etc.
- Such order in writing shall include orders received in a lump for continuous transaction on a date fixed in advance.

VIII-2-6 Others

(1) Remarks on segregation

It shall be noted that, in the case where a registered financial institution (limited to a deposit taking registered financial institution) accepts the deposit, etc. of money from customers arising from transactions in the course of securities related business as a deposit for primary business of such registered financial institution, such money shall not be subject to segregation.

(2) Remarks on implementation of internal rules

A registered financial institution which is not a member of a financial instruments firms association implements internal rules to carry out business appropriately after the consideration of the articles of incorporation and rules of a financial instruments firms association according to the type of registered financial institution business.

It shall be noted that a registered financial institution shall carry out appropriate business management such as reviewing internal rules each time when relevant laws or regulations and various rules are amended or periodically.

IX Supervisory Valuation Items and Procedures (Eligible Institutional Investors, etc. Subject to Special Provisions Business, etc.)

IX-1 Appropriateness of business related to eligible institutional investors, etc. subject to special provisions business, etc.

The authority shall verify the appropriateness of business of eligible institutional investors, etc. subject to special provisions firm (which means a person carrying out business provided in the items of Article 63.1 of the F.I. Act; hereinafter the same) with the following remarks.

IX-1-1 Solicitation and explanatory system

(1) Main focus points

- ① Whether an eligible institutional investors, etc. subject to special provisions firm makes false representation or explanation that no remuneration is charged or remuneration is extremely smaller than the actual amount.
- ② Whether an eligible institutional investors, etc. subject to special provisions firm makes false representation or explanation that the yield will be guaranteed or the whole or part of losses will be compensated or false representation or explanation that such guarantee or compensation are currently available.
- ③ Whether an eligible institutional investors, etc. subject to special provisions firm makes false representation or explanation that no loss will arise from transactions or no demerit in respect of risks, etc. is involved in transactions.
- ④ Whether an eligible institutional investors, etc. subject to special provisions firm makes false representation or explanation in respect of other details of products (such as fundamental merchantability, risks, types or reason of movement).

(2) Supervisory methods and responses

If there is a doubt through daily supervisory operations, etc. that an eligible institutional investors, etc. subject to special provisions firm performs an act to give false information to investors regarding solicitation, etc., the authority shall take necessary responses such as the collection of report for the purpose of confirming the state of business provided in Article 63.7 of the F.I. Act and warning in writing.

IX-1-2 Recognition of real state

The authority shall collect a monitoring survey sheet for the following matters pursuant to Article 63.7 of the F.I. Act or Article 48.3 of Amended Law Supplementary Provisions in order to recognize appropriately the real state of business of an eligible institutional investors, etc. subject to special provisions firm, etc. (which means an eligible institutional investors, etc. subject to special provisions firm or investment management firm subject to special provisions (which means a person carrying out businesses provided in Article 48.1 of the Amended Law Supplementary Provisions; hereinafter the same); hereinafter the same).

[Monitoring a person carrying out business provided in Article 63.1 (1) of the F.I. Act who resides in Japan (for each fund)]

- ① the name of fund;
- ② the classification of the firm;
- ③ business to be carried out;
- ④ the legal form of interest in fund;
- ⑤ matters regarding the investment management period (the date of establishment and the date of terminating investment management);
- ⑥ the type of sales method;
- ⑦ matters regarding interest holder;
- ⑧ the amount of public offer, etc. during the latest one year;
- ⑨ matters regarding the amount of properties under investment management;
- ⑩ matters regarding the amount of net assets;
- ⑪ matters regarding the types of products;
- ⑫ matters regarding the products to be invested in.

[Monitoring of a person carrying out business provided in Article 63.1 (2) of the F.I. Act and an investment management firm subject to special provisions who resides in Japan (for each fund)]

- ① the name of the fund;
- ② the classification of the firm;
- ③ business to be carried out;
- ④ the legal form of interest in fund;
- ⑤ matters regarding the investment management period (the date of establishment and the date of terminating investment management);
- ⑥ matters regarding interest holders;
- ⑦ matters regarding the amount of properties under investment management;
- ⑧ matters regarding the amount of net assets;
- ⑨ matters regarding types of products;
- ⑫ matters regarding products to be invested in.

IX-1-3 Identification, notification obligation of doubtful transactions

III-2-6 shall apply to identification, notification of doubtful transactions of an eligible institutional investor, etc. subject to special provisions firm.

IX-2 Procedures

IX-2-1 Preparation, publication, renewal, etc. of Notifying firm list

The authority shall publish a list of the name, trade name, notification date, competent local finance bureau and notification grounds (the distinction of an eligible institutional investor, etc. subject to special provisions firm and an investment management firm subject to special provisions) of an eligible institutional investor, etc. subject to special provisions firm, etc. in order to facilitate investors to recognize information of the particulars of each firm (the distinction of registered firm and notified firm) (hereinafter referred to as "notified firms list").

A local finance bureau shall make a report of the state of the acceptance of notifications under Article 63.2, 63.3, 63.6, 63-2, 63-3.1 or 63-3.2 of the F.I. Act or Article 48.3 of the Amended Law Supplementary Provisions each month. The Financial Services Agency shall prepare and renew the notified firms list based on such reports, etc. and post it on the website of the Financial Services Agency.

If there is an eligible institutional investor, etc. subject to special provisions firm, etc. which has a problem such as the failure of the submission of a monitoring survey sheet under IX-1-2 above, the authority shall put the fact in the notified firms list. If there is an eligible institutional investor, etc. subject to special provisions firm, etc. which cannot be reached from the supervisory authority and the business office of which cannot be confirmed through daily supervisory operations, etc., the authority shall put such fact in the notified firms list. If such eligible institutional investor, etc. subject to special provisions firm, etc. fails to request after three months have passed since the day of such posting, the authority shall in principle delete the information of such eligible institutional investor, etc. subject to special provisions firm, etc. from the notified firms list.

IX-2-2 Remarks on unnotified firm

If the authority found a firm carrying out eligible institutional investor, etc. subject to special provisions business without notification under Article 63.2 of the F.I. Act through grievances from investors, enquiry from the investigative authority, information from a financial instruments firm or financial instruments firms association, etc. or newspaper advertisement, the authority shall warn the firm to suspend the act immediately or to notify immediately in writing.

IX-2-3 Remarks in the case where there is doubt of failure of meeting criteria for eligible institutional investor, etc. subject to special provisions firm, etc.

If businesses carried out by an eligible institutional investor, etc. subject to special provisions firm, etc. fails to meet criteria for eligible institutional investor, etc. subject to special provisions business (Article 63.2 of the F.I. Act) or investment management subject to special provisions business (Article 48.1 of the Amended Law Supplementary Provisions), the authority shall make an effort to inform the public that such firm must register under Article 29 of the F.I. Act.

If a doubt that an eligible institutional investor, etc. subject to special provisions firm, etc. fails to meet the above criteria has been found through daily supervisory operations, etc., the authority shall collect reports in order to confirm the state of business provided in Article 63.7 of the F.I. Act or Article 48.3 of the Amended Law Supplementary Provisions and, if necessary as a result thereof, the authority shall take responses equivalent to responses to unregistered firms under II-1-1 (7).

IX-2-4 Remarks in the case where an eligible institutional investor, etc. subject to special provisions firm is not applicable

If a person carrying out eligible institutional investor, etc. subject to special provisions business fails to meet the criteria because of a change of attributes of a fund contributor or withdrawal from investment by an eligible institutional investor or increase of retail investors, the authority shall take the following responses in order to protect investors.

(1) Issuance of order under Article 63.5 of the F.I. Act.

"If a filing person carrying out business subject to special provisions has commenced a business of performing an act referred to in Article 63.1 (2) as eligible institutional investors, etc. business subject to special provisions and eligible institutional investors, etc. business subject to special provisions has become not applicable to the first-mentioned business" under Article 63.5 of the F.I. Act is provided assuming that the fund contributor met the criteria for "eligible institutional investor, etc." under Article 63.1 (1) of the F.I. Act at the time of the commencement of business subject to special provisions, but failed to meet such criteria for some reason not attributable to a filing person carrying out business subject to special provisions. In this case, the authority shall issue an order to take measures such as transferring business of the filing person carrying out business subject to special provisions to an other financial instruments firm.

(2) Case other than the above (1)

If the number of persons other than eligible institutional investors exceeds 49, the special provisions under Article 63 of the F.I. Act are not applicable, and the filing person carrying out business subject to special provisions carries out investment management business without registration under the F.I. Act. The authority shall therefore take responses equivalent to responses to unregistered firms under II-1-1 (7) to such filing person carrying out business subject to special provisions.

X Supervisory Valuation Items and Procedures (Foreign Securities Firm)

X-1 Fundamental concept for foreign securities firm

X-1-1 Fundamental concept under laws and regulations for foreign securities firm

No foreign securities firm shall perform any of the acts referred to in the items of Article 28.8 of the F.I. Act (hereinafter referred to as "act related to securities related business") with a person in Japan as a counterparty unless registered in respect of the principal business office or other type of office established as the headquarter for securities related business in Japan.

On the other hand, an unregistered foreign securities firm without having an office in Japan is allowed to perform an act related to securities related business from a foreign jurisdiction with a person in Japan, as a counterparty, from whom such foreign securities firm accepts an order by means that a financial instruments firm (limited to a first-type financial instruments business) act as an agent or intermediary without solicitation for an act related to securities related business.

Further, a foreign securities firm is allowed to trade on a financial instruments exchange in Japan as a business with a permission from the authority under Article 60.1 of the F.I. Act. The authority shall supervise such firm based on remarks shown in X-2.

X-1-2. Cross-boarder transactions using Internet, etc. by foreign securities firm

An act to put advertisement, etc. regarding an act related to securities related business on the website, etc. of a foreign securities firm shall be regarded as "solicitation" in principle.

Provided, That, if reasonable measures are taken to prevent an act related to securities related business with investors in Japan, such advertisement, etc. is not regarded as "solicitation" targeting investors in Japan including the following measures:

(1) Securing wording

There is a clear wording to the effect that investors in Japan will not be served. Remarks shall be made on the followings when the authority judges whether the above measures are taken fully:

- ① such securing wording can be read by browsing the advertisement, etc. and does not require special or additional operation; and
- ② such securing wording is stated in languages that investors in Japan using such site can read reasonably.

(2) Measure to prevent transactions, etc.

Measures to prevent an act related to securities related business with investors in Japan are taken.

Remarks shall be made on the followings when the authority judges whether the above measures are taken fully:

- ① procedures to confirm the place of residence shall be taken by requiring an investor to show the address, mailing address, e-mail address, method of payment or other information at the time of trading;
- ② if it could be reasonably believed that an act related to securities related business are performed by an investor in Japan, the foreign securities firm shall take care not to accept orders from such investor in Japan; and
- ③ the foreign securities firm shall take care not to encourage investors in Japan to perform an act related to securities related business by means of, for example, establishing a call center for customers, etc. in Japan or establishing a link on the website, etc. for investors in Japan.

The above measures are just examples and, if equivalent or stricter measures are taken, such advertisement, etc. shall not be regarded as "solicitation" targeting investors in Japan.

(3) If such reasonable measures as the above are not taken, "solicitation" targeting investors in Japan is very likely applicable to such advertisement, etc., and therefore such foreign securities firm shall certify that it is not performing an actual act related to securities related business involving solicitation of investors in Japan.

X-2 Appropriateness of business (on-exchange trading permit firm)

- (1) The authority shall verify the appropriateness of business of a foreign securities firm carrying

out on-exchange trading business (which means a business as defined in Article 60.1 of the F.I. Act; hereinafter the same) (hereinafter referred to as "on-exchange trading permit firm") with a permission from the authority in accordance with III-2-1 (excluding (1) ⑤), III-2-5, III-2-7, III-2-8, III-2-9, IV-3-1-1, IV-3-1-5, IV-3-2 (excluding IV-3-2-2, IV-3-2-3 (2) (3), IV-3-2-4, IV-3-2-5). Considering that an on-exchange trading permit firm is under the supervision of the overseas authority in principle, it shall be noted that concrete methods of business management shall not be subject to requirements if it is determined that the on-exchange trading permit firm carries out business management equivalent to those effectively required in Japan.

(2) Supervisory responses to accident, etc.

Supervisory responses to an accident, etc. (which means an act in violation of the laws or regulations provided in Article 223 (10) of the F.I. Business Ordinance; hereinafter the same) shall be dealt as follows.

① When an on-exchange trading permit firm has filed a notification of an accident, etc., the authority shall confirm the followings:

- (a) Whether a quick report has been made to the internal control division and the internal audit division in accordance with the compliance rules, etc. and to the board of directors, etc.;
- (b) Whether the investigation or clarification of the accident, etc. has been made by a division (such as internal audit division, etc.) independent from the division where the accident, etc. has occurred.

② The authority shall verify the relationship between the accident, etc. and the appropriateness of business of the on-exchange trading permit firm based on the following focus points.

- (a) Whether any of officers was involved or the involvement was organized.
- (b) How such accident, etc. influences on financial instruments markets in Japan.
- (c) Whether the internal mutual checking system works properly.
- (d) Whether the preparation of improvement measures for recurrence prevention or implementation of self-cleansing function are sufficient, and the responsibility of persons concerned are clearly pursued.
- (e) Whether the response after the finding of such accident, etc. was appropriate.

(3) Supervisory method and response

With respect to the business and financial issues of an on-exchange trading permit firm found through the daily supervisory operations or notification of accident, etc., the authority shall recognize voluntary improvement of business management of an on-exchange trading permit firm through holding hearings in depth from the representative in Japan or collection of reports under Article 60-11 of the F.I. Act when needed.

Further, the authority shall make daily efforts to recognize and solve at an early stage the issues of an on-exchange trading permit firm through active information sharing with a financial instruments exchange of which the on-exchange trading permit firm is a member and an overseas authority with which information sharing agreements have been entered into, and if a violation of laws or regulations of a particularly grave nature has been found, the authority shall consider necessary responses such as the issuance of an order to improve business management or an order to suspend business under Article 60-8.1 of the F.I. Act.

X-3 Procedures (on-exchange trading permit firm)

X-3-1 Permit

The authority shall handle an application for permit pursuant to Article 60-2 of the F.I. Act in accordance with III-3-1, and remarks shall be made on the followings.

(1) Permission procedures

① Seal on application for registration

The case where the seal may be replaced with signature as stated in the remarks on entries shall apply to the case of the representative who is a foreigner and has no custom to use a seal.

② Attachments to application for registration

- (a) An abridged copy of the resident's card shall state the followings:
 - a. the address;
 - b. the name;
 - c. the date of birth.
- (b) A copy of the foreign resident's registration card or foreign resident's registered certificate submitted by a foreigner who resides in Japan and a copy of resident's card in the home country submitted by a foreigner who does not reside in Japan or a written statement

equivalent thereto (in the case where it is written in a foreign language such as English, together with Japanese translation) shall be regarded as "a written statement equivalent thereto" as provided in Article 221 (6) of the F.I. Business Ordinance.

③ Remarks on the period until permission

- (a) The authority shall remind an applicant for permission not to carry out on-exchange trading business until permitted.
- (b) In the case where an applicant for permission carries out other business related to the laws or regulations over which the Financial Services Agency has the jurisdiction and administrative disposition for such other business has been made, the authority shall confirm the details thereof and confirm the state of measures for improvement through hearings, etc. when needed.

If such administrative dispositions relate to a compliance system, the authority shall confirm with remarks on III-2-1 which is applied *mutatis mutandis* under X-2.

④ Notice to applicant for permission

Upon granting a permission under Article 60.1 of the F.I. Act, the authority shall furnish the applicant for permission with a notice of permission.

⑤ Conditions for permission

With respect to a foreign securities firm which applies a permission under Article 60.1 of the F.I. Act for the sole purpose of trading for house account, the authority shall examine whether the applicant carries out business so applied appropriately. If such foreign securities firm wishes to carry out brokerage business for an order of an overseas customer newly after obtaining such permission, the authority shall examine again whether the foreign securities firm can carry out such business appropriately. In granting a permission to a foreign securities firm carrying out only on-exchange trading business for house account therefore, the authority shall impose conditions that, if the applicant wishes to carry out business other than business applied at the time of the application for permission, the applicant is required to obtain an approval from the authority in advance.

⑥ Refusal of registration

- (a) In refusing permission, the authority shall furnish the applicant for permission with a registration refusal notice stating the reasons for such refusal and the applicant's right to file a petition for appeal to the Commissioner of the Financial Services Agency for objection.
- (b) The authority shall clarify, in a registration refusal notice, an item applicable to the reason for the refusal under Article 60-3.1 of the F.I. Act or a false statement on important matters or omission of important fact in the application for registration and attachments clearly.

(2) Matters to be examined

① Items of corporate form

In examining whether an applicant is the same type of corporation as a corporation maintaining the board of directors as provided in Article 60-3.1 (1) (a) of the F.I. Act, the authority shall refer to the application for registration and the attachments and hold a hearing to confirm the followings.

- (a) Whether the applicant establishes a collegial body composed of more than one officer or employee as a decision making body;
- (b) Whether mutual checking by participants work in the decision making body and the foreign securities firm takes care that its business management is not influenced by a specific officer.
- (c) Whether the representative is appointed based on mutual agreement, etc. of more than one officer and employee.
- (d) Whether a system that an internal control division checks sales divisions, etc. appropriately is implemented.
- (e) Whether a system that auditing is made effectively by an independent internal audit division or external auditor, etc. is implemented.

② Items of system examination

In examining whether an applicant is a person having personnel resources insufficient to carry on on-exchange trading business in an accurate manner as provided in Article 60-3.1 (1) (k) of the F.I. Act, the authority shall refer to an application for permission and its attachments and hold a hearing to confirm the followings:

- (a) Whether it is determined that the applicant ensures the employment of officers and employees having sufficient knowledge and experience of the business and has organization and the applicant is able to carry out such business appropriately in light of the followings.
 - a. The management and full-time officer is qualified to carry out the on-exchange trading

- business in a fair and accurate manner in light of the career, ability, etc.
- b. Ensuring that a full-time officer and employee has knowledge and experience sufficient to understand and perform focus points of the appropriateness of business management provided in various regulations such as the Financial Instruments and Exchange Act and the Supervisory Guidelines, and has sufficient knowledge and experience of compliance and risk control necessary for fair and accurate carrying out on-exchange trading business.
 - c. Having organizational and personnel structure to carry out business appropriately such as allocation of personnel necessary for carrying out on-exchange trading business accurately to each appropriate division, and allocation of persons responsible for internal control, etc. independently from sales divisions.
 - d. There is more than one full-time officer or employee with at least three years experience of the business for the same type of trading as on-exchange trading at each on-exchange trading office (which means a business office or other type of office carrying out on-exchange trading business provided in Article 60-2.1 (3) of the F.I. Act; hereinafter the same).
 - e. The employment of personnel required for the following system implementations is ensured in respect of on-exchange trading business:
 - i). preparation and retention of books and records, reports, etc.;
 - ii) computer system control;
 - iii) trade control;
 - iii) settlement of grievances and troubles;
 - iv) internal audit;
 - v) training.
 - f. If the applicant wishes to conduct transactions for customer account, the applicant implements an order control and trade examination system to prevent unfair transactions such as insider transactions or manipulation, etc.
 - g. A system to take the measures referred to in X-1-2 (2) is implemented in order to prevent an act related to securities related business with an investor in Japan.
 - h. A person who can coordinate appropriately with an on-exchange trading office or the principal business office and respond accurately to the collection of reports, etc. by the supervisory authority is appointed as the representative in Japan.
- (b) Whether it is determined as a result of comprehensive consideration of the following matters that the applicant has a person with inappropriate qualification for business management of on-exchange trading business among officers and employees engaging in on-exchange trading business, which will likely result in the downfall of the credit of an on-exchange trading permit firm.
- a. The applicant has an experience of the violation of the laws or regulations related to finance in Japan such as the F.I. Act or the laws or regulations in a foreign jurisdiction analogous thereto and being fined (including a criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto).
 - b. The applicant has an experience of being punished by a criminal penalty of imprisonment or severer (including criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto) (particularly, the case of crimes under Articles 246 to 250 of the Criminal Code (fraudulence, fraudulence using a computer, breach of trust, quasi-fraudulence, threat, attempted crime) shall be noted).
- ③ Others
- (a) The authority shall confirm the implementation of measures to prevent insider transactions, measures to limit orders, and, in the case of conducting transactions for customer account, an order control and trade control system to prevent unfair transactions by "a written statement describing the measures taken to prevent unfair trading" provided in Article 221 (9) of the F.I. Business Ordinance.
 - (b) In examining under Article 60-3.1 (1) (b) of the F.I. Act, the authority shall confirm the registration, etc. in all of the jurisdictions where the principal business office or on-exchange trading office exists using attachments and, when needed, agreements regarding information sharing with an overseas authority.
 - (c) In examining under Article 60-3.1 (2) of the F.I. Act, the authority shall confirm the effectiveness of guarantee by an overseas authority that the overseas authority will respond to the request for cooperation of investigation made by Japan through communication with the overseas authority.
 - (d) In examining under Article 60-3.1 (3) of the F.I. Act, the authority shall require a financial instruments exchange in Japan to confirm the effectiveness of an agreement regarding

information sharing entered into with a foreign financial instruments market operator.

It shall be noted that such "agreement regarding information sharing" is not limited to an agreement between individual exchanges, but a framework of information sharing between multiple exchanges could be approved if information is shared appropriately between inter-market surveillance group (ISG) and other exchanges.

X-3-2 Notification

Notification of an on-exchange trading permit firm shall be filed in accordance with III-3-2 (2), and remarks shall be made on the followings.

(1) Remarks on notification of change, etc.

Upon accepting a notification pursuant to Articles 60-5.1 and 60-5.2 of the F.I. Act from an on-exchange trading permit firm, the authority shall recognize and confirm its details and appropriateness in respect of the permit foreign securities firm through holding hearings in depth from the representative in Japan or collection of reports under Article 60-11 of the F.I. Act when needed. Further, if a violation of laws or regulations of a particularly grave nature has been found, consider necessary responses such as the issuance of an order to revoke the permission or suspend business under Article 60-8.1 of the F.I. Act.

(2) Remarks on notification of addition, etc. of on-exchange trading office

In the case of accepting a notification of the addition of an on-exchange trading office or the addition of a financial instruments exchange of which an on-exchange trading permit firm becomes a trading participant from the on-exchange trading permit firm pursuant to Articles 60-5.1 of the F.I. Act, the authority shall confirm non-existence of causes for the refusal of permission under the items of Article 60-3.1 of the F.I. Act in respect of personnel structure and appropriateness of business of the on-exchange trading office.

X-3-3 Books and records on business

Books and records on business shall be prepared and kept in accordance with III-3-3. "Branch office" in III-3-3 shall be read as "on-exchange trading office."

XI Supervisory Valuation Items and Procedures (Financial Instruments Intermediary Firm)

XI-1 Appropriateness of business (financial instruments intermediary firm)

The authority shall verify the appropriateness of business of a financial instruments intermediary firm in accordance with III-2 (excluding III-2-6 (1) ②), IV-3-1 (excluding IV-3-1-2 (2), IV-3-1-3 (1) and (2) and IV-3-1-6) and (3) and (6) of IV-3-3-2 (limited to the part related to the sale of complex structured debt securities and investment trust similar to over-the-counter derivatives transactions), and explanatory documents provided in Article 66-18 of the F.I. Act with the following remarks.

Debt securities under IV-3-1-2 (4) means securities provided in Article 281 (7) of the F.I. Business Ordinance, and the theoretical price and internal rules computed and prepared respectively by a commissioning financial instruments firm, etc. may be used as the theoretical price under (a) and (b) of IV-3-1-2 (4) and internal rules under (b) and (d) of IV-3-1-2 (4).

(1) The authority shall instruct a financial instruments intermediary firm to make them available for inspection any time when a customer requests.

(2) The authority shall confirm the date when each financial instruments intermediary firm put them at business offices, when needed.

XI-2 Procedures (financial instruments intermediary firm)

XI-2-1 Registration

An application for registration pursuant to Article 66-2 of the F.I. Act shall be handled in accordance with III-3-1 (excluding (2) and (9) ③), and remarks shall be made on the followings. The text shall be amended in reading in the case of Forms accordingly.

(1) Procedures for registration

① Handling of registration number

Registration numbers to be stated on the financial instruments intermediary firms registry

shall be:

Example) Director-General of ○○ Finance Bureau (Financial Instruments) ○○

② Proxy application for registration application

With respect to an application for registration in respect of a financial instruments intermediary firm, it shall be noted that a proxy application can be made after a belonging financial instruments firm, etc. investigates closely the details of an application for the purpose of ensuring convenience of the applicant and belonging financial instruments firm, etc., efficiency of application procedures by a belonging financial instruments firm, etc., and further, ensuring the accuracy of the contents of an application for registration, acceleration of proceedings, etc.

When a proxy has filed an application, the authority shall confirm the existence of authorization and the scope of authorization by a letter of proxy, etc. If the scope of authorization covers a request for the correction of an application, sending of a notice of the completion of registration, it shall be noted that such request or sending a notice, etc. may be made to the proxy.

(2) Matters to be examined

① In examining whether the name or trade name of a belonging financial instruments firm, etc. to compensate, in respect of an accident of the applicant for registration, the applicant for registration for losses when there is more than one belonging financial instruments firm, etc. as provided in Article 258 (3) of the F.I. Business Ordinance, the authority shall confirm that the followings are satisfied.

(a) Whether the state of the occurrence of the accident, etc. is classified into each type and the name or trade name of a belonging financial instruments firm, etc. to compensate such losses is specified clearly for all of such types.

(b) Whether, if none of the types is applicable or it is not clear which type is applicable, the name or trade name of a belonging financial instruments firm, etc. to compensate losses from such accident is specified.

② The authority shall confirm whether the following matters are stated as the types of business and manner of operation as provided in Article 259 of the F.I. Act:

(a) business area;

(b) types of business (such as face-to-face, use of computer connecting with an electronic communication line, existence of an employee carrying out financial instruments intermediary business in the case where the applicant is an individual);

(c) types of business offices (such as attended business office or unattended business office);

(d) types of securities to be handled;

(e) types of transactions for which the applicant acts as an intermediary among market derivatives transactions or foreign market derivatives transactions (according to the classification of the transactions referred to in the items of Article 2.21 of the F.I. Act and transactions provided in Article 2.23 of the F.I. Act);

(f) In the case of wishing to act as an intermediary for entering into an investment advisory contract or discretionary investment contract, such fact.

(3) Others

In examining whether an applicant is a person without knowledge and experience to carry out financial instruments intermediary business accurately provided in Article 66-4 (4) of the F.I. Act, the authority shall confirm the followings referring to an application for registration and its attachments, etc. If an applicant is a foreign juridical person, the authority shall confirm the state of officers and employees stationed in Japan for ①, and confirm the state in Japan for ② and ③.

① A person carrying out financial instruments intermediary business (such as an officer carrying out financial instruments intermediary business and a person, etc. responsible for internal control) has passed a securities representative qualification examination conducted by the Japan Securities Dealers Association, and have a certain level of knowledge of the laws and regulations.

② Whether, if an applicant is a jurisdiction or an individual having an employee carrying out financial instruments intermediary business, the applicant has an organization and personnel structure that personnel necessary for accurate carrying out the proposed business is allocated and a person responsible for internal control, etc. is allocated appropriately according to the type and scale of the business.

③ Whether, if an applicant is a juridical person or an individual having an employee carrying out financial instruments intermediary business, the following systems are implemented

according to the type and scale of the business. (In the case of (a) and (b), it is possible to commission a belonging financial instruments firm, etc. operations to prepare sheets and to be controlled by the intermediary firm. Items, among (c) to (e), for which a system to carry out appropriately by a belonging financial instruments firm, etc. is ensured are excluded.):

- (a) preparation and retention of books and records, reports, etc.;
- (b) customer control;
- (c) computer system control;
- (d) settlement of grievances and troubles;
- (e) internal audit.

XI-2-2 Notification

A notification of a financial instruments intermediary firm shall be filed in accordance with III-3-2 (1), and it shall be noted that the authority shall confirm non-existence of a reason for revocation of registration under Article 66-20.1 of the F.I. Act through hearings when needed from the financial instruments intermediary firm when the authority accepts a notification for the cessation of business, etc. filed pursuant to Article 66-19.1 of the F.I. Act from the financial instruments intermediary firm.

XI-2-3 Books and records of business operations

III-3-3 (excluding (4) and (5) of III-3-3) shall apply to handling preparation and retention of books and records of business operation. A system or format used by a belonging financial instruments firm, etc. may be used to prepare books and records regarding financial instruments intermediary business referred to in Article 282 of the F.I. Business Ordinance or a financial instruments intermediary firm may commission a belonging financial instruments firm to construct a system or formation for such preparation with remarks that such financial instruments intermediary firm shall have the obligation of preparation and retention.

XI-2-4 Registration of sales representative

IV-4-3 and V-3-2 shall apply.

XII. Supervisory Valuation Items and Procedures (Securities Finance Company)

XII-1 Business control (securities finance company)

III-1 (excluding (1) ② (f)) shall apply to business control of a securities finance company. IV-1-2 shall apply to personnel structure sufficiently eligible to carry out business as a securities finance company.

XII-2 Appropriateness of business (securities finance company)

III-2 (excluding III-2-3-1, III-2-3-3, III-2-3-4, III-2-4 (1) ③ and ④ and III-2-7 (2) ① (f)), IV-3-1-6 and IV-3-1-7 shall apply to the appropriateness of business of a securities finance company, and remarks shall be made on the followings for entries in "3 State of measures taken for protection of information of individuals" in a business report provided in Article 3-4.1 of the Cabinet Office Ordinance on Securities Finance Company (hereinafter referred to as "Finance Company Office Ordinance").

(1) State of performance of security control measures

With respect to the security control and supervision over an employee in respect of customer information who is an individual handled by a securities finance company and supervision over outsourcee in the case of outsourcing such handling of information, the authority shall collect reports for the following measures as measures necessary and appropriate to prevent leakage, loss or damage of such information:

(Measures necessary and appropriate for security control)

- ① measures pursuant to Article 10 of the Protection Law Guidelines;
- ② measures pursuant to the Operational Guidelines I and Attachment 2;

(Measures necessary and appropriate for supervision over employee)

- ① measures pursuant to Article 11 of the Protection Law Guidelines;

- ② measures pursuant to the Operational Guidelines II;
(Measures necessary and appropriate for supervision over outsourcee)
- ① measures pursuant to Article 12 of the Protection Law Guidelines;
- ② measures pursuant to the Operational Guidelines III;
- (2) State of performance of measures to prevent use for purpose other than the purpose of special undisclosed information
"Other special undisclosed information" under 3 (2) of Remarks on entries shall mean information regarding participation to a labor union, race or sex life, and "to ensure appropriate business management or other purpose determined to be necessary" shall mean the cases provided in the items of Article 6.1 of the Protection Law Guidelines:

XII-3 Procedures (securities finance company)

XII-3-1 Examination criteria for license

- (1) Personnel structure
The authority shall judge the eligibility for the personnel structure provided in Article 156-25.1 of the F.I. Act considering the following matters.
 - ① Whether the applicant ensures personnel allocation to each division necessary to carry out business referred to in Article 156-24.1 of the F.I. Act (hereinafter referred to as "margin transaction business");
 - ② Whether the applicant ensures the employment of a person with at least three years experience of securities related business among officers and employees and the employment of a person who is familiar with the system of margin transactions;
 - ③ Whether the applicant ensures the employment of officers and employees having sufficient knowledge and experience of the proposed business and it is determined that the applicant is able to carry out such business appropriately and efficiently in light of the followings:
 - (a) a full-time officer understands, and has knowledge and experience sufficient to perform, focus points of business management provided in relevant various regulations such as the F.I. Act and the Supervisory Guidelines, and has sufficient knowledge and experience of the compliance and the risk control necessary for fair and accurate carrying out the financial instruments business;
 - ④ Whether the applicant has a person with inappropriate qualification for business management among officers and employees as a result of comprehensive consideration of the following matters as a relationship with a member of a crime group or other circumstances, which will likely result in the downfall of social credit of a securities finance company.
 - (a). the person concerned is a member of a crime group (including a person who was a member of a crime group in the past);
 - (b) the person concerned has a close relationship with a crime group;
 - (c) the person concerned has an experience of the violation of the laws or regulations related to finance in Japan such as the F.I. Act or the laws or regulations in a foreign jurisdiction analogous thereto and being fined (including a criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto);
 - (d) the person concerned has an experience of the violation of the provisions of the Law on Prevention of Improper Act by Member of Crime Group (excluding the provisions of Article 32-2.7 of said Law) or the provisions under the laws or regulations analogous thereto in a foreign jurisdiction, or commitment of crimes under the Criminal Code or the Law on Violence, etc. Punishment and being fined (including a criminal penalty under the laws or regulations analogous thereto);
 - (e) the applicant has an experience of being punished by a criminal penalty of imprisonment or severer (including criminal penalty under the laws or regulations in a foreign jurisdiction analogous thereto) (particularly, the case of crimes under Articles 246 to 250 of the Criminal Code (fraudulence, fraudulence using a computer, breach of trust, quasi-fraudulence, threat, attempted crime thereto) shall be noted).;
- (2) Credit standing and financing ability
The authority shall judge the eligibility for credit standing and ability to raise funds provided in Article 156-25.1 of the F.I. Act with the following matters.
 - ① Whether the applicant is determined to have an ability to procure shares of stock and ability to raise funds sufficient to carry out margin transactions business objectively.
 - ② Whether the applicant implements a system to acquire information of margin transactions on

an on-exchange financial instruments market or over-the-counter traded securities market any time, and implements a procurement system and settlement system, which can be judged as a system that immediate response is possible, with a financial instruments firm and a counterparty, etc.

XII-3-2 Notification

A change in the types of business and manners of operation provided in Article 1-2.2 (2) of the Finance Company Office Ordinance means a change in the types of business or manners of operation, other than conditions of transactions, involving in internal rules, etc, and a matter necessary to inform all counterparties.

XII-3-3 Approval

Remarks shall be made on the followings for approving under Article 156-27.3 of the F.I. Act.

- (1) The authority shall not approve if it is determined that business for which an approval is applied is inconsistent with the public interest or holding of securities, etc. will likely cause significant price movement risk, etc.
- (2) Whether a written statement projecting the revenue and expense provided in Article 2.1 (1) of the Finance Company Office Ordinance shows that the balance of revenue and expense is expected to be surplus within three years after the commencement of such business and such revenue and expense plan can be achieved objectively.

XII-3-4 Approval

- (1) Change in types of business and manner of operations

Remarks shall be made on the followings when an application for an approval for a change in the type of business or manner of operation provided in Article 156-28.1 of the F.I. Act has been filed.

- ① Whether the change will not cause interference on smooth carrying out of margin transactions business.
- ② Whether the change will be informed to all parties thoroughly and immediately.

- (2) Decrease in the amount of capital

Remarks shall be made on the followings when an application for approval for decrease in the amount of capital provided in Article 156-28.1 of the F.I. Act has been filed.

- ① Whether the amount of capital after the capital decrease is not smaller than the amount provided in Article 156-23 of the F.I. Act.
- ② Whether the capital decrease will not cause interference on smooth carrying out of margin transactions business.
- ③ Whether it is determined that the capital decrease is made in order to clear deficit or other unavoidable reason to maintain business.

- (3) Cessation of business or resolution of dissolution

Remarks shall be made on the followings when an application for an approval for cessation of business or resolution of dissolution provided in Article 156-36 (1) of the F.I. Act has been filed.

- ① Whether the cause to revoke a license provided in Article 156-32. 1 of the F.I. Act does not exist.
- ② Whether the assets exceeds liabilities and clearing business can be carried out smoothly.
- ③ Whether responses are arranged in view of a system and physically not to cause interference on margin transactions on an on-exchange financial instruments market or over-the-counter traded securities market after the cessation of business or dissolution.

- (4) Merger or Assignment of business or acquisition of business by assignment

Remarks shall be made on the followings when an application for an approval for merger or assignment of business or acquisition of business by assignment provided in Article 156-36 (2) of the F.I. Act has been filed.

- ① Whether the cause to revoke a license provided in Article 156-32. 1 of the F.I. Act does not exist in a company extinguished as a result of merger or business assignment.
- ② Whether responses are arranged in view of a system and physically not to cause interference on margin transactions on an on-exchange financial instruments market or over-the-counter traded securities market as a result of merger or business assignment.

Forms
Translation omitted.