(Provisional translation)

Comprehensive Guidelines for Supervision of Financial Instruments Business Operators, etc

April 2008
Securities Business Division, Supervisory Bureau,
Financial Service Agency

Comprehensive Guidelines for Supervision of Financial Instruments Business Operators, etc

I. Basic Concept

I-1 Basic Concept for Supervision of Financial Instruments Business Operators, etc.

I-1-1 Purpose of Supervision of Financial Instruments Business Operators, etc., and Role of Supervisory Departments

The primary preconditions for investors to actively make investments and for companies to smoothly raise funds in the financial instruments market are that the market be fair and efficient, and that Financial Instruments Business Operators, etc., ("Financial Instruments Business Operators, etc." refers to Financial Business Operators and Registered Financial Institutions. The same shall apply hereinafter.) play an important role as market intermediaries.

The purpose of the supervision of Financial Instruments Business Operators, etc., is to secure sound and appropriate business operations of persons who conduct Financial Instruments Business, to ensure fairness in the issuance of securities and transactions of financial instruments, to facilitate the smooth distribution of securities and to realize fair price formation of financial instruments by fully utilizing the functions of the capital market through the appropriate exercise of their own market intermediary function, thereby contributing to the sound development of the national economy and the protection of investors.

In order to conduct administrative supervision in an effective manner, it is necessary to properly combine the "onsite" monitoring technique used by inspection departments ("Inspection departments" include the Executive Bureau of the Securities and Exchange Surveillance Commission and the Inspection Bureau of the Financial Services Agency (FSA). The same shall apply hereinafter.) and the off-site monitoring technique used by supervisory departments. In addition, in order to enhance the effectiveness of supervision, inspection and supervisory departments need to exercise their respective functions properly while maintaining appropriate cooperation.

The role of supervisory departments under this framework of supervision is to continuously collect and analyze information during intervals between inspections and quickly identify problems that may affect the soundness and appropriateness of the business operations of Financial Instruments Business Operators, etc., while taking supervisory measures, including administrative actions, as necessary, thereby encouraging the correction of problems before they become serious.

To be more specific, it is important to ensure that Financial Instruments Business Operators, etc., fully comply with various laws and regulations, including those intended to protect investors, precisely grasp the state of their business operations through periodic and continuous exchanges of opinions and other means, accumulate and analyze various data and information provided by them and encourage them to make voluntary improvement efforts in order to ensure the soundness of their business managements.

In particular, since supervisory authorities are in a position to know the condition of Financial Instruments Business Operators, etc., as a whole, as well as the condition of individual business operators, it is important that they precisely grasp the position of individual Financial Instruments Business Operators, etc., within the whole industry through comparative analysis, and ensure that they make efforts to correct problems by providing feedback of the analysis results to them or by holding hearings with them.

I-1-2 Basic Concept Concerning Supervision of Financial Instruments Business Operators, etc.

In light of the above, the basic concept for the supervision of Financial Instruments Business Operators, etc., can be described as follows:

(1) Securing Appropriate Cooperation with Inspection Departments

It is important for supervisory and inspection departments to properly cooperate with each other while respecting each other's independence, and to achieve highly effective supervision of Financial Instruments Business Operators, etc., by properly combining both onsite and offsite monitoring techniques. To this end, supervisory departments shall pay due consideration to the following points regarding cooperation with inspection departments.

(i) Supervisory departments shall conduct follow-up monitoring of improvements concerning the problems identified by inspections and strive to ensure that the problems are corrected. They shall take strict supervisory measures, including administrative actions, when necessary.

(ii) The problems identified by supervisory departments through offsite monitoring shall be notified to inspection departments as feedback for use in the next inspection.

(2) Securing Sufficient Communications with Financial Instruments Business Operators, etc.

In the supervision of Financial Instruments Business Operators, etc., it is important to precisely grasp and analyze information concerning their business management and use the analysis results for supervisory activities as necessary in an appropriate and timely manner. Therefore, rather than merely waiting for reports from Financial Instruments Business Operators, etc., supervisory departments need to proactively gather information by engaging in communications with them on a daily basis. To be more specific, supervisory departments should ensure daily communications with Financial Instruments Business Operators, etc., through periodic exchanges of opinions so as to grasp information not only concerning their financial conditions, but also various business management matters.

(3) Respect of Voluntary Efforts by Financial Instruments Business Operators, etc.

The standpoint of supervisory departments is to examine, in the light of laws and regulations, management decisions made by Financial Instruments Business Operators, etc., in their capacity as private companies, based on the principle of self-responsibility and to encourage correction of problems. With due consideration of this standpoint, supervisory departments must respect the voluntary efforts of Financial Instruments Business Operators, etc., regarding business operations when supervising them.

(4) Securing Efficient and Effective Supervisory Processes

In order to make effective use of the limited resources of the supervisory authorities as well as those of Financial Instruments Business Operators, etc., it is necessary to implement supervisory processes in an efficient and effective manner. Therefore, when requiring Financial Instruments Business Operators, etc., to submit reports and other materials, supervisory departments must make sure to limit the volume of the required reports and

materials to the minimum necessary for the supervisory purpose and strive to improve the efficiency of supervision by, for example, constantly reviewing the necessity of existing supervisory processes and the method of implementing them and by making improvements as necessary.

It is also necessary to strive to implement supervisory processes in a manner suited to the increasingly diverse businesses of Financial Instruments Business Operators, etc. Regarding Financial Instruments Business Groups with international operations (as defined in IV-2-6) in particular, it is necessary to implement supervisory processes with due consideration of the viewpoints specified in the Guideline for Financial Conglomerates Supervision as well as the viewpoints necessary for the supervision of individual Financial Instruments Business Operators, etc.

Furthermore, the supervisory authorities need to maintain close cooperation with Financial Instruments Firms Associations (which refer to the Authorized Financial Instruments Firms Association and Public Interest Corporation-Type Financial Instruments Firms. The same shall apply hereinafter.), which are self-regulatory organizations as specified by the Financial Instruments and Exchange Act (hereinafter referred to as "FIEA"), as well as financial instruments exchanges, since they, in their capacity as entities familiar with the circumstances of the market, are responsible for exercising the function of self-regulation that is intended to secure investors' confidence in Financial Instruments Business Operators, etc.

I-2 Purpose of Establishment of Guideline for Supervision

I-2-1 Purpose of Establishment of Guideline for Supervision

In order to enable the Japanese economy to achieve sustainable development, it is important to accelerate a shift of funds "from savings to investment," which means a shift in emphasis from indirect financing to direct financing and market-based indirect financing. This shift is expected to contribute to the stability of Japan's financial system, the creation of an attractive market for both domestic and foreign market participants as well as corporate growth and economic development, by bringing about the following four benefits:

(i) Creating a robust financial system with an advanced risk-dispersion capability by moving to a market structure in which a wide range of market participants share risks according to their own capabilities (avoiding vulnerability of the financial system that may result from concentration of risks on indirect finance).

(ii) Promoting corporate innovation by facilitating smooth provision of risk money.

(iii) Improving the efficiency of capital and the profitability of Japanese companies by promoting a shift of funds from savings to investment, thereby creating a market with sufficient depth to keep a watchful eye on business managers.

(iv) Creating an affluent and colorful society by providing investors with a diverse range of means to manage assets amid the declining birth rate and the aging of society.

In order to promote the shift of funds from savings to investment, it is essential not only that Financial Instruments Business Operators, etc., which act as market intermediaries, gain and maintain public confidence, but also that financial authorities design appropriate institutional frameworks and properly motivate Financial Instruments Business Operators, etc., to strengthen governance while bearing in mind the protection of investors and appropriate risk management.

Since the financial system reform of 1998, which was carried out under the banner of "a free, fair and global market," Japan has implemented a variety of measures, including making it easier for securities companies to advance into new businesses, liberalizing their business operations and diversifying the range of institutions allowed to undertake securities business, in order to invigorate the securities market. These measures gradually produced benefits in the form of the diversification of financial instruments and sales channels, thereby bringing about changes in the environment for securities business and promoting the globalization of the financial and capital markets.

Even as the reform described above proceeded, protecting investors, improving convenience for them and ensuring the reliability of Japan's markets remained as major challenges. Regarding cases of financial damage to ordinary customers, such as losses caused by fraudulent sales of unregulated financial instruments, Japan reformed the institutional framework for the protection of investors by strengthening relevant measures on a case-by-case basis, an example of which was the introduction of regulation on foreign exchange margin trading (put into effect in July 2005) through a revision of the Financial Futures Trading Act.

The revamping of the Securities and Exchange Act as the FIEA (put into effect on September 30, 2007), is

intended to promote financial innovation, in order to reap further benefits from the reform measures already implemented and to ensure appropriate protection of users through the establishment of comprehensive and cross-sectoral rules concerning the protection of investors. In order to accelerate the shift of funds “from savings to investment,” the supervisory authorities will need to take advantage of the results of the past reform measures while dealing with Financial Instruments Business Operators, etc., in an appropriate manner under the cross-sectoral legal framework, as their businesses are becoming increasingly diverse.

In order to conduct daily supervisory processes under these circumstances, we decided to systematically sort out the contents of sector-by-sector guidelines for supervision and administrative processes, and work out concepts concerning supervision, supervisory viewpoints and methods of supervision in a comprehensive manner on a cross-sectoral basis.

This Guideline was compiled with due consideration of the actual state of Financial Instruments Business Operators, etc., so that it can be applied to various cases, and the requirements of the supervisory evaluation points specified in the Guideline shall not be uniformly applied to all Financial Instruments Business Operators, etc.

Accordingly, when applying this Guideline, it is necessary to bear in mind that even if a Financial Instruments Business Operator does not literally meet the requirements of all evaluation points, the case shall not be judged inappropriate insofar as there is no problem from the viewpoint of protecting public interests and investors; it is necessary to avoid applying the Guideline in a mechanical and uniform fashion. On the other hand, it should also be borne in mind that even if a Financial Instruments Business Operators etc. formally fulfills all the functions concerning evaluation points, the case could be deemed to be inappropriate from the viewpoint of protecting public interests and investors.

Local Finance Bureaus (including the Fukuoka Local Finance Branch and the Okinawa General Bureau. The same shall apply hereinafter), as well as relevant divisions of the FSA, shall implement supervisory processes regarding Financial Instruments Business Operators, etc., that operate in their districts of jurisdiction based on this Guideline. Following the establishment of this Guideline, we abolished “the Comprehensive Guideline for Supervision of Securities Companies,” “Comprehensive Guideline for Supervision of Financial Futures Traders,” “Guideline for Administrative Processes (points of attention regarding the supervision of investment trust management companies, investment corporations and securities investment advisory companies)” and Section 10 “Trust Beneficiary Rights Sales Business” of the “Comprehensive Guideline for Supervision of Trust Companies, etc.” and Section 6 “Commodity Fund Business” of the “Points of Attention in Financial Supervision, etc. (Guideline for Administrative Processes) Vol. 3: Financial Companies.”

I-2-2 Structure of This Guideline

This Guideline was compiled as a comprehensive one applicable to the supervision of a diverse range of Financial Instruments Business Operators, etc., with a view to limiting overlapping descriptions to a minimum.

Accordingly, the contents of Section I “Basic Concept” and Section II “Points of Attention in the Conduct of Administrative Processes Regarding the Supervision of Financial Instruments Business Operators, etc.,” although

basically covering persons engaging in Financial Instruments Business (Type I Financial Instruments Business, Type II Financial Instruments Business, Investment Management Business and Investment Advisory and Agency Business), also consider the supervision of persons engaging in businesses specially permitted for qualified institutional investors, foreign securities companies, financial instruments intermediary service providers, securities finance companies, investment corporations and commodities investment sales companies.

Sections I and II are followed by "Supervisory Evaluation Points and Various Administrative Procedures," which comprises Sections III to VII. Section III sets forth general supervisory viewpoints and procedures that are common to all types of Financial Instruments Business Operators, etc., while Sections IV to VII set forth additional supervisory viewpoints that are specific to individual types of Financial Instruments Business Operators, etc.

Therefore, supervisors of Financial Instruments Business Operators, etc., shall first refer to Section III and then to either of Sections IV to VII according to the attributes of the businesses they supervise.

Section VIII and the following sections set forth supervisory viewpoints and various administrative procedures regarding registered financial institutions, qualified institutional investors engaging in specially permitted businesses, foreign securities companies, financial instruments intermediary service providers and securities finance companies, selecting suitable points of attention and procedures from among those specified in the preceding sections and applying them mutatis mutandis, so supervisors should refer to them when necessary.

(Reference)

Application Table for the Comprehensive Guidelines for Supervision of Financial Instruments Business Operators, etc

Sections of the Guideline \ Businesses Covered	Financial Instruments Business Operators				Registered Financial Institutions	Specially Permitted Businesses for Qualified Institutional Investor	Foreign Securities Company	Financial Instruments Intermediary Service Provider	Securities Finance Company
	Type I Financial Instruments Business	Type II Financial Instruments Business	Investment Management Business	Investment Advisory and Agency Business					
I. Basic Concept	○	○	○	○	○	○	○	○	○
II. Points of Attention in the Conduct of Administrative Processes Regarding the Supervision of Financial Instruments Business Operators, etc.	○	○	○	○	○	○	○	○	○
III. Supervisory Evaluation Points and Various Administrative Procedures (General)									
Evaluation points (general)	○	○	○	○					
Various administrative procedures (general)	○	○	○	○					
IV. Supervisory Evaluation Points and Various Administrative Procedures (Type I Financial Instruments Business)									
Evaluation points (Type I Financial Instruments Business)	○								
Various administrative procedures (Type I Financial Instruments Business)	○								
V. Supervisory Evaluation Points and Various Administrative Procedures (Type II Financial Instruments Business)									
Evaluation points (Type II Financial Instruments Business)		○							
Various administrative procedures (Type II Financial Instruments Business)		○							
VI. Supervisory Evaluation Points and Various Administrative Procedures (Investment Management Business)									
Evaluation points (Investment Management Business)			○						
Various administrative procedures (Investment Management Business)			○						
VII. Supervisory Evaluation Points and Various Administrative Procedures (Investment Advisory and Agency Business)									
Evaluation points (Investment Advisory and Agency Business)				○					
Various administrative procedures (Investment Advisory and Agency Business)				○					
VIII. Supervisory Evaluation Points and Various Administrative Procedures (Registered Financial Institutions)									
Evaluation points (Registered Financial Institutions)					○				
Various administrative procedures (Registered Financial Institutions)					○				
IX. Supervisory Evaluation Points and Various Administrative Procedures (Specially Permitted Businesses for Qualified Institutional Investor, etc.)									
Evaluation points (Specially Permitted Businesses for Qualified Institutional Investor, etc.)						○			
Various administrative procedures (Specially Permitted Businesses for Qualified Institutional Investor, etc.)						○			
X. Supervisory Evaluation Points and Various Administrative Procedures (Foreign Securities Company)									
Evaluation points (Foreign Securities Company)							○		
Various administrative procedures (Foreign Securities Company)							○		
XI. Supervisory Evaluation Points and Various Administrative Procedures (Financial Instruments Intermediary Service Provider)									
Evaluation points (Financial Instruments Intermediary Service Provider)								○	
Various administrative procedures (Financial Instruments Intermediary Service Provider)								○	
XII. Supervisory Evaluation Points and Various Administrative Procedures (Securities Finance Company)									
Evaluation points (Securities Finance Company)									○
Various administrative procedures (Securities Finance Company)									○

II. Points of Attention in the Conduct of Administrative Processes Regarding the Supervision of Financial Instruments Business Operators, etc.

II-1 Conduct of General Administrative Processes, etc.

II-1-1 General Supervisory Processes

(1) Formulation and Announcement of Priority Items for Supervision in the Current Program Year

In order to clarify priority items for supervision, supervisors shall formulate and announce an annual policy on supervision at the beginning of each program year.

(2) Periodic Hearings

As part of off-site monitoring activities, supervisors shall hold periodic hearings with Financial Instruments Business Operators as follows.

It should be noted that since some types of business may not necessarily be suited to periodic hearings from the viewpoint of supervisory necessity and efficient implementation of supervisory processes, supervisors shall strive to ensure efficient and effective monitoring with the use of resourceful and creative ideas and approaches in such cases.

(i) Hearings Regarding Financial Results

Supervisors shall hold hearings regarding the financial results of Financial Instruments Business Operators as well as problems with their financial positions on a semiannual or quarterly basis. In conducting hearings, they shall strive to ensure efficiency by, for example, selecting the targets of hearings in light of Financial Instruments Business Operators' financial positions and the nature of their business operations.

(ii) Comprehensive Hearings

Supervisors shall hold hearings regarding Financial Instruments Business Operators' management strategies, policies for business expansion, management of various risks, profit management, establishment of governance systems and so on in light of their financial results, among other factors. In addition, senior officials of supervisory departments shall hold hearings with top managers of Financial Instruments Business Operators as necessary.

(3) Hearings on an As-Necessary Basis

As part of off-site monitoring activities, supervisors shall hold hearings with Financial Instruments Business Operators, including with top managers, when it is deemed necessary to do so from the supervisory viewpoint due to factors such as unfavorable economic developments, including fluctuations in interest rates and asset prices, problems regarding the protection of investors and incidents that could undermine the sound and appropriate management of Financial Instruments Business Operators.

(4) Submission of Monitoring Survey Reports

The directors-general of Local Finance Bureaus (including the directors-general of the Fukuoka Local Finance Branch and the Okinawa General Bureau. The same shall apply hereinafter.) shall conduct administrative processes regarding offsite monitoring reports, in accordance with a guideline issued by the FSA Commissioner, when they have received monitoring survey reports regarding the following matters that are submitted in accordance with Article 56-2(1) of the FIEA. In conducting administrative processes, relevant sections of Local Finance Bureaus shall cooperate sufficiently with the FSA divisions concerned.

[Monitoring of Financial Instruments Business Operators (Type I Financial Instruments Business Operators)]

(i) Capital Adequacy Ratio
(ii) Status of business operations and accounting
(iii) Status of segregated management of customer assets
(iv) Market risk
(v) Counterparty risk
(vi) Operational risk
(vii) Liquidity risk

[Monitoring of Financial Instruments Business Operators (Operators Engaging in Investment Management Business)]

(i) Fund name
(ii) Fund type
(iii) Overall amount of assets under management

(5) Points of Attention Regarding Public Notice of Administrative Dispositions

A public notice of an administrative disposition based on Article 54-2 of the FIEA shall specify the following items:

(i) Name of the financial instruments business operations and individuals concerned
(ii) Location of the head office, etc.
(Note) The "head office, etc." refers to the head office, or the principal office engaging in sales and administrative work (the principal office in Japan in the case of foreign corporations or individuals). The same shall apply hereinafter.
(iii) Registration number
(iv) Registration date
(v) Date of the administrative disposition
(vi) Contents of the administrative disposition

(6) Grasp of the Actual State of Unregistered Business Operators and Operators Using Similar Trade Names

When supervisors have recognized the existence of operators engaging in financial instruments business without registration, or operators' names that may be confused with other operators that are registered, based on complaints from investors, inquiries from investigative authorities, information provided by Financial Instruments Firms' Associations, advertisements carried by newspapers, etc., they shall make active efforts to grasp the actual

state of such operators through means such as inquiring with police, local consumer centers, etc., about the operators and directly contacting the operators via telephone.

When they have received complaints from consumers and inquiries from investigative authorities in particular, supervisors shall take sufficient care to do more than merely respond to the complaints and inquiries.

(7) Handling of Unregistered Business Operators and Other Questionable Operators

When supervisors have received information regarding unregistered business operators and other questionable operators, they shall take the following measures in order to prevent financial damage to customers from spreading.

It should be kept in mind that the cases of business operators engaging in businesses specially permitted for qualified institutional investors without notification shall be handled likewise.

(i) Receipt of Complaints

When supervisors have received information from investors and other persons with regard to business operators engaging in financial instruments business without registration, they shall take the following measures after collecting information as detailed as possible (e.g. the corporate name, location, telephone number, the state of sales activities of the said business operators and the names of the operators' representatives, the names of the information providers and whether the information providers agree to have their information communicated to the investigative authorities).

A. When a Local Finance Bureau has received information regarding an unregistered business operator based in a region under the jurisdiction of another Local Finance Bureau, it shall communicate the information to the competent bureau. (The competent Local Finance Bureau shall handle the case thereafter, in principle.)

B. Regarding business operators who cannot be contacted, supervisors shall strive to collect more information.

C. When the information provider asks supervisors to refrain from contacting the business operator concerned or other organizations, supervisors shall make sure to prevent his/her interests from being damaged.

D. Regarding information related to a business operator suspected of conducting business without registration, supervisors shall encourage the information provider to provide information directly to investigative authorities.

E. A registry book (the format is specified in the Attached List of Formats II-6 of the Guideline for Supervision) shall be compiled to systematically record complaints and inquiries from investors, guidance given by the authorities to business operators, and the operators' responses thereto.

(ii) Measures to Be Taken against Unregistered Operators

Regarding a questionable business operator whose name and contact details have been identified through information received directly or via the FSA or other bureaus, and whose actual state of sales activity has become known to a certain extent, supervisors shall strive to grasp the actual state by directly contacting the said business operator by telephone or through other means. If the operator is found to be conducting business without registration, the following measures shall be taken:

A. If the business operator is found to be unintentionally operating without registration and with no malicious intent and to have no problem from the viewpoint of investor protection, it shall be immediately required to be registered.

B. If the business operator is found to be intentionally operating without registration and with malicious intent or to have other problems from the viewpoint of investor protection, the investigative authorities shall be notified and the business operator shall be warned in writing, in the format specified in the Attached List of Formats II-4 and II-5 of the Guideline for Supervision, to stop conducting business immediately.

(iii) Suspected but Undetermined Cases of Unregistered Business Operators

Business operators who are suspected of conducting business without registration although they have not been conclusively found to be doing so shall be warned in writing, in the format specified in the Attached List of Formats II-5 of the Guideline for Supervision (excluding cases where the issuance of such a warning could impede investigation by the investigative authorities).

(iv) Cases Where Correction Is Not Made In Response to a Warning

Regarding business operators who refuse to take corrective action in response to warnings, complaints shall be filed with the investigative authorities as necessary.

(v) Reporting to the FSA

Regarding cases where a warning has been issued against a business operator or a complaint has been filed with the investigative authorities, a set of copies of the relevant section of the aforesaid registry book, the written warning and other relevant documents shall be immediately sent to the FSA Commissioner.

(8) Handling of Business Operators Using Similar Trade Names

(i) A business operator whose trade name is deemed to be undoubtedly similar to an existing trade name (e.g. “XXX Securities Company,” “Type X Financial Business Operator” and “XXX Investment Corporation”) shall be warned in writing, in the format specified in the Attached List of Formats II-1, and ordered, through direct contact such as telephone conversations or face-to-face interviews, to take corrective action. In addition, such cases shall be notified to the investigative authorities and the exchange of information with the authorities shall be maintained.

(ii) A business operator using a trade name that could be confused with that of a Financial Instruments Business Operator (refer to Note) shall be warned in writing, in the format specified in the Attached List of Formats II-2. In addition, the details of the business operators’ business shall be investigated through means such as inquiring with police, local consumer centers and other entities about the operators and directly contacting them via telephone.

Unless the business operator is found as a result of the investigation to be engaging in a business that is obviously different from Financial Instruments Business, it shall be warned in writing again, this time in the format specified in the Attached List of Formats II-3 and ordered, through direct contact such as telephone conversations and face-to-face interviews, to take corrective action.

(iii) Regarding a business operator who refuses to take corrective action in response to warnings issued in the formats specified in the Attached List of Formats II-1 and II-3, a complaint shall be filed with the investigative authorities as necessary.

(iv) In cases where the measures (i) to (iii) above have been taken, the Director-General of the competent Local Finance Bureau shall immediately report to the FSA Commissioner the name of the business operator concerned, the name of its representative, the location of its stores and other facilities, the nature and size of its business and so on.

(v) Regarding business operators using similar trade names, and other questionable business operators, the directors-general of Local Finance Bureaus shall compile a registry book (in the format specified in the Attached List of Formats II-6) to systematically record complaints and inquiries from investors, guidance given by the authorities to the business operators, and the business operators' response thereto.

(Note) "Examples of Trade Names Which Could be Confused with Those of Financial Instruments Business Operators"

Of Financial Instruments Business Operators, those who were registered under Article 28 of the former Securities and Exchange Act at the time when the FIEA was put into force, and those who started engaging in securities-related businesses after the FIEA was put into force are entitled to include the word "Securities" in their trade names. Judgment on the appropriateness of trade names that could be confused with the names of these business operators (hereinafter referred to as "Specified Securities Companies, etc.") shall be made on a case-by-case basis in light of the degree of the risk of such confusion. The following are examples of names that could cause confusion:

(a) Trade names which could be confused with those of specified securities companies although they combine "Securities" with words describing other types of businesses.

<Examples>

"XXX Securities Transactions," "XXX Securities Trader," "XXX Securities Broker," "XXX Securities Investment," "XXX Securities Trading Company," "XXX Securities Call Loan," "XXX Securities Entrustment," "XXX Securities Intermediation," "XXX Securities Agency"

However, names that are obviously different from those of specified securities companies, for example, "XXX Securities Printing," shall be excluded.

(b) Trade names which could be confused with those of specified securities companies although not using the word "Securities."

<Examples>

"XXX Stock Entrustment," "XXX Stock Investment," "XXX Stock Brokerage," "XXX Stock Trade," "XXX Stock Transactions," "XXX Stock Agency (Regarding these names, "Stock" may be substituted with "Bond")," "XXX Financial Instrument Trade"

II-1-2 Cooperation between Supervisory Departments

(1) Cooperation between the FSA and Local Finance Bureaus

The FSA and Local Finance Bureaus need to properly maintain the exchange of information deemed

necessary for the supervision of Financial Instruments Business Operators, etc., in order to share the recognition of the location of risks and perspectives on problems. To that end, they shall strive to strengthen their cooperation by providing information to each other in a timely and appropriate manner and actively exchanging views with regard to various matters, including matters other than those that concern consultations related to internal delegation processes. In addition, Local Finance Bureaus shall strive to strengthen cooperation among themselves. For example, when a Local Finance Bureau has detected publicly unknown risks or problems regarding a Financial Instruments Business Operator, etc., under the jurisdiction of the FSA or another Local Finance Bureau, it shall provide relevant information to the FSA or the competent bureau as necessary.

(2) Coordination and Liaison with the Director-General of the Competent Local Finance Bureau

(i) When the FSA Commissioner and the directors-general of Local Finance Bureaus have received a notification of the establishment, relocation, name change, abolition, temporary suspension or resumption of operation of a sales office of a Financial Instruments Business Operator in a region not under their jurisdiction, they shall send a copy thereof to the director-general of the Local Finance Bureau that has jurisdiction over the region where the said sales office is located.

(ii) When the FSA Commissioner and the directors-general of the Local Finance Bureaus have taken an administrative disposition under either of Articles 51 to 54 of the FIEA against a sales office of a Financial Instruments Business Operator, etc., under their jurisdiction that is located in a region not under their jurisdiction, they shall immediately notify the details of the action to the director-general of the Local Finance Bureau that has jurisdiction over the region where the said sales office is located.

(iii) When the director-general of a Local Finance Bureau has received a notification submitted under Article 32 of the FIEA by a major shareholder in a Financial Instruments Business Operator under the jurisdiction of the FSA Commissioner or the director-general of another Local Finance Bureau, he/she shall immediately send the original of the notification to the FSA Commissioner or the director-general of the competent Local Finance Bureau.

(iv) When the FSA Commissioner and the directors-general of the Local Finance Bureaus have issued an order based on Article 32-2 of the FIEA to a major shareholder in a Financial Instruments Business Operator under their jurisdiction, they shall notify the details of the order to the director-general of the Local Finance Bureau (to the director-general of the Kanto Local Finance Bureau in cases where the shareholder is a nonresident) that has jurisdiction over the region where the head office or principal office of the said major shareholder (the residence of the shareholder in cases where the shareholder is an individual) is located.

(v) The FSA Commissioner and the directors-general of Local Finance Bureaus, when a Financial Instruments Business Operator, etc., under their jurisdiction entrusts business operations to a financial instruments intermediary service provider located in a region not under their jurisdiction, shall cooperate with the director-general of the Local Finance Bureau that has jurisdiction over the said financial instruments intermediary service provider by, for example, providing the information necessary for the supervision thereof.

II-1-3 Cooperation with Inspection Departments

It is important for supervisory and inspection departments to properly cooperate with each other while respecting each other's independence, and to achieve highly effective supervision by properly combining both on-site and off-site monitoring techniques. To this end, supervisory departments shall pay due consideration to the following points regarding cooperation with inspection departments.

(1) Feedback of Information Regarding Problems and Issues Identified through Off-site Monitoring to Inspection Departments

Problems and issues identified by supervisory departments through off-site monitoring shall be notified to inspection departments as feedback information for use in the next inspection.

Specifically, supervisory departments shall provide inspection departments with explanations concerning the current state of Financial Instruments Business Operators, etc., with regard to the following matters, for example:

(i) Major moves made by Financial Instruments Business Operators, etc., since the previous inspection (e.g. business alliances with other companies, capital increases, management reshuffles)

(ii) The schedule of business restructuring in the case of Financial Instruments Business Operators, etc., planning a system integration or other measures in line with management restructuring moves such as a merger

(iii) Results of the analysis of the most recent financial results

(iv) Results of the analysis of risk-related information identified through offsite monitoring

(v) Results of comprehensive hearings

(vi) Status of the implementation of supervisory measures (e.g. requirements for the submission of reports and administrative dispositions) and follow-up thereon

(vii) Matters which supervisory departments believe are important.

(viii) Other matters

(2) Supervisory Response to Problems and Issues Identified through Inspections

Regarding problems and issues identified through inspections, supervisory departments shall consider taking administrative dispositions based on II-5 in order to properly reflect the inspection results in supervisory processes.

(3) Holding of Meetings for Facilitating Cooperation between Inspectors and Supervisors

(i) Supervisory and inspection departments shall hold meetings aimed at ensuring their appropriate cooperation. The meetings should be held, in principle, at the beginning of each program year, and at other times as necessary.

(ii) At the said meeting, supervisory and inspection departments shall exchange views about important matters regarding the inspection and supervision of Financial Instruments Business Operators, etc., in the current program year.

II-1-4 Cooperation with Self-Regulatory Organizations

It should be kept in mind that in the supervision of Financial Instruments Business Operators, etc., it is

necessary to attach importance to rules set by relevant self-regulatory organizations as well as to laws and regulations. In addition, supervisors shall maintain the appropriate exchange of information necessary for supervision with self-regulatory organizations, to the extent necessary for the purpose of ensuring the fairness of transactions and protecting investors. It is also essential that supervisors strive to share the recognition of the location of risks and perspectives on problems with self-regulatory organizations. Furthermore, they shall provide active support to self-regulatory organizations' efforts to exercise cross-sectoral self-regulatory functions through participation in meetings aimed at facilitating liaison and coordination between self-regulatory organizations.

Also, in order to exclude crime syndicates and other illegal organizations from financial instruments business, supervisors shall maintain appropriate cooperation with relevant organizations through the securities security liaison group.

II-1-5 Internal Delegation

(1) Consultations with the FSA Commissioner

The directors-general of Local Finance Bureaus shall hold prior consultations with the FSA Commissioner with regard to the following matters when they conduct delegated supervisory processes concerning Financial Instruments Business Operators, etc.

In addition, directors-general shall report the results of the deliberations made by their bureaus and express the opinions thereof in the consultations.

(i) Refusal of registration under Article 29-4(1) and Article 33-5 of the FIEA
(ii) Granting of authorization of the conduct of business under Article 30(1) of the FIEA
(iii) Administrative disposition against a major shareholder under Article 32-2 of the FIEA (including cases where the provision of Article 32-4 of the FIEA is applied mutatis mutandis)
(iv) Approval of other businesses under Article 35(4) of the FIEA (limited to the first approval to be granted in the region under the jurisdiction of the relevant Local Finance Bureau)
(v) Approval of exclusion from application regarding preventive measures against internal collusion under the proviso of Article 44-3(1) and (2) of the FIEA
(vi) Administrative dispositions, including orders to improve or suspend business operation and rescission of registration and authorization under Article 51, Article 51-2, Article 52 (1) and Article 52-2(1) of the FIEA
(vii) Dismissal of officers of Financial Instruments Business Operators (limited to officers stationed at sales and other offices in Japan or representative persons in Japan in the case of foreign securities companies) under Article 52(2) and Article 52-2(2) of the FIEA
(viii) Administrative dispositions, including business improvement orders in relation to the Capital Adequacy Ratio under Article 53 of the FIEA
(ix) Rescission of registration of Financial Instruments Business Operators, etc., who have suspended their business operations for an extended period of time under Article 54 of the FIEA
(x) Orders for Financial Instruments Business Operators, etc., who have not joined an association, to compile or change internal rules under Article 56-4(2) of the FIEA

(xi) Approval of the compilation, change or abolition of internal rules by Financial Instruments Business Operators, etc., who have not joined an association under Article 56-4(3) and (4) of the FIEA

(xii) Dispositions necessary for investigation under Article 187 of the FIEA

(xiii) Approval of the use of the interest rate sensitivity analysis under Article 8(1) of the Notice of the Establishment of Criteria for the Calculation of Financial Instruments Business' Market Risk Equivalent, Counterparty Risk Equivalent and Basic Risk Equivalent (hereinafter referred to as the "Capital Adequacy Notice")

(xiv) Approval of the use of an internal control model under Article 12 of the Capital Adequacy Notice

(xv) Rescission of approval under Article 15(4) of the Capital Adequacy Notice

(2) Reporting to the FSA Commissioner

When the directors-general of Local Finance Bureaus conduct delegated supervisory processes regarding Financial Instruments Business Operators, etc., they shall complete the relevant processes and then report to the FSA Commissioner on the following matters:

(i) When a Financial Instruments Business Operator, etc., under the jurisdiction of the FSA has obtained registration from a Local Finance Bureau under Article 29-3(1) or Article 33-4(1) of the FIEA, the director-general of the said bureau shall immediately send the original of the registration application and attached documents to the FSA Commissioner.

(ii) The directors-general of Local Finance Bureaus shall report on the conditions of Financial Instruments Business Operators, etc., as of the end of each financial quarter to the FSA Commissioner by the 20th day of the month following the end of the quarter, in the format specified in the Attached List of Formats II-7 (the Attached List of Formats II-8 in the case of Registered Financial Institutions and the Attached List of Formats II-9 in the case of Financial Instruments Intermediary Service Providers).

(iii) The directors-general of Local Finance Bureaus shall report on the conditions of major shareholders (major shareholders as specified under Article 29-4(2) of the FIEA) as of the end of each financial quarter to the FSA Commissioner by the 20th day of the month following the end of the quarter, in the format specified in the Attached List of Formats II-10.

(iv) The directors-general of Local Finance Bureaus shall compile a report regarding administrative processes concerning the confirmation of problems (as specified in the proviso of Article 39(3) of the FIEA) on a half-yearly basis, in the format specified in the Attached List of Formats II-11 (Report on the Status of the Conduct of Administrative Processes concerning Confirmation), and submit the report to the FSA Commissioner by the 15th day of the month following the end of each six-month period.

(v) When the directors-general of Local Finance Bureaus have received the following documents, they shall immediately send a copy thereof to the FSA Commissioner.

A. Reports regarding international businesses (Article 173 (2) of the Cabinet Office Ordinance regarding Financial Instruments Business, etc. (hereinafter referred to as the "FIB Cabinet Office Ordinance")

B. Reports regarding the establishment or abolition of representative offices of foreign securities companies (Article 199 (11) H of the FIB Cabinet Office Ordinance)

(vi) When the directors-general of Local Finance Bureaus have received reports based on Article 50-2(1)

and (7) of the FIEA, they shall immediately send a copy thereof to the FSA Commissioner.

(vii) When the directors-general of Local Finance Bureaus have issued a notice based on Article 57(3) of the FIEA (limited to cases where a notice to the Minister of Finance based on Article 194-4(1) of the FIEA is required), they shall immediately send a copy thereof to the FSA Commissioner.

(viii) When the directors-general of Local Finance Bureaus have received reports based on Article 15(1) and (2) of the Capital Adequacy Notice, they shall immediately send a copy thereof to the FSA Commissioner.

(ix) The directors-general of Local Finance Bureaus shall examine the status of the payment, for the previous business year, of the Registration and License Tax (the registration license tax as specified under Article 2 of the Registration and License Tax Act) by Financial Instruments Business Operators, etc., under their jurisdiction, and report the findings to the FSA Commissioner by April 30 every year.

(3) Re-delegation to Director-General of Local Finance Offices, etc.

Of the processes delegated to the directors-general of Local Finance Bureaus under Article 42 of the Order for the Enforcement of the Financial Instruments and Exchange Act (hereinafter referred to as the "FIEA Enforcement Order"), the directors-general may re-delegate the following processes to the director-general of local Finance Offices that have jurisdiction over the regions where the head offices of the applicants and Financial Instruments Business Operators, etc., are located as well as to the heads of the Otaru and Kitami Branch Offices.

(i) Administrative processes regarding the receipt of applications for registration as specified under Article 29-2 (1) and Article 33-3(1) of the FIEA

(ii) Administrative processes regarding the receipt of applications for authorization specified under Article 30-3(1) of the FIEA

(iii) Administrative processes regarding the receipt of applications for approval as specified under Article 35(4) of the FIEA

(iv) Administrative processes regarding the receipt of notifications based on Article 31(1) and (3), Article 33-6(1) and (3), Article 31-2(5) and (8), Article 31-4(4), Article 35(3) and (6), Article 46-6(1), Article 50(1), Article 50-2(1) and (7) of the FIEA

(v) Administrative processes regarding the receipt of notifications based on Article 32(1), Article 32-3 and Article 32-4 of the FIEA

(vi) Administrative processes regarding the receipt of documents submitted under Article 46-3(1) and (2), Article 47-2, Article 48-2(1) and (2) and Article 49-3(1) and (2)

(4) Points of Attention

The provisions of (ii) to (iv), (viii) and (xiii) to (xv) of II-1-5(1), (iii), (v) and (viii) of II-1-5(2) and (ii), (iii) and (v) of II-1-5(3) shall not be applicable to the conduct of administrative processes concerning the supervision of registered financial institutions.

II-2 Handling of Complaints, Provision of Information, etc.

(1) Response to Complaints, etc.

At the FSA, the Counseling Office for Financial Services Users is primarily responsible for handling complaints regarding Financial Instruments Business Operators, etc., and financial instruments transactions. At Local Finance Bureaus, relevant divisions primarily handle such complaints. It is necessary to make it clear to persons who lodge complaints that the FSA and Local Finance Bureaus are not in a position to act as an arbitrator regarding specific transactions and that their task is to ensure the soundness of the management of Financial Instruments Business Operators, etc., based on laws and regulations. In addition, the FSA and Local Finance Bureaus shall introduce the said persons to Financial Instruments Firms' Associations and Certified Investor Protection Organizations, which handle complaints and settle disputes based on the FIEA.

(2) Accumulation of Information

Complaints and information regarding Financial Instruments Business Operators, etc., deemed to be useful for ensuring the soundness of the management of such operators shall be recorded (in the format specified in the Attached list of Formats II-12). Information deemed to be particularly important shall be immediately reported to the relevant FSA divisions.

II-3 Response to External Inquiries about Interpretations of Laws and Regulations, etc.

II-3-1 Inquiries about Laws and Regulations

(1) Scope of Laws and Regulations Regarding Which Inquiries May be Processed

Inquiries may be processed only regarding the FIEA and related laws and regulations that are under the FSA's jurisdiction. Comments shall never be made in response to inquiries regarding laws and regulations outside the FSA's jurisdiction.

(2) Method of Response to Inquiries

(i) Regarding an inquiry to which a reply can be made based on existing documents and reference materials, such as this Guideline for Supervision and reports compiled by advisory councils, the reply shall be provided promptly.

(ii) When Local Finance Bureaus have received an inquiry to which they find it difficult to reply on their own, they shall compile an inquiry mail in the format specified in the Attached List of Formats II-13 and consult with the relevant FSA division via e-mail, fax or through other means (hereinafter referred to as "e-mail, etc").

(iii) When business operators to which the laws and regulations under the FSA's jurisdiction are directly applicable or business associations comprising such business operators have made a general inquiry that meets the requirements specified in the following A and B with regard to the said laws and regulations, the head of the relevant FSA division shall provide a written reply and make it public if it is deemed to be appropriate to do so from the viewpoint of improving the predictability of the application of laws and regulations.

(Note) A "business association" refers to a group formed by a substantial number of business operators engaging in the same type of business to which the laws and regulations under the FSA's jurisdiction are directly applicable in order to promote their common interests, or a federation of such groups (limited to the top-tier organization in the case of business sectors where there are layers of associations and federations).

A. Scope of Inquiries for Which the Reply may be Published

An inquiry must meet all of the following requirements if the written reply thereto is to be made public:

a. Must not ask whether a law or regulation is applicable to a specific transaction involving a specific business operator, but rather ask about the general interpretation of the law or regulation. (Not eligible for the application of the Prior Confirmation Procedures on the Application of Laws and Regulations by Administrative Agencies ("no action letter" system).)

b. Must not seek factual recognition.

c. Must relate to transactions and other matters common to business operators to which the laws and regulations under the FSA's jurisdiction are directly applicable (in cases where the inquirer is an association of business operators, the inquiry must concern transactions and other matters

common to business operators constituting the association) and must be regarding matters that a number of business operators are expected to make an inquiry into.

d. Must not ask about points that are clear in light of the Guideline for Administrative Processes and other documents and materials that have been made public in the past.

B. Written Inquiry Forms (including Electronic Forms)

The inquirer shall submit a written inquiry that specifies the following items. In addition to the written inquiry, the inquirer may be asked to submit additional or corrected documents, if necessary, in order to judge the contents of the inquiry and whether it meets the criteria specified in "A" above.

a. The legal provision which the inquiry concerns and specific points of issue
b. The inquirer's opinion concerning the inquired points of issue and the basis thereof
c. A statement from the inquirer agreeing to have the contents of the inquiry and the response thereto made public.

C. Contact Point for Inquiry

A written inquiry shall be submitted to the FSA division with jurisdiction over the law or regulation in question or the relevant section of the Local Finance Bureau that has jurisdiction over the inquirer. When a Local Finance Bureau section has received an inquiry, it shall immediately forward it via e-mail, etc., to the relevant FSA division.

D. Reply

a. The head of the relevant FSA division shall strive to reply to the inquirer within two months in principle of the arrival of a written inquiry at the contact point. In cases where it is not possible to reply within two months, it is necessary to provide the reason for the delay and the expected date of reply to the inquirer.
b. Written replies shall contain the following disclaimer:

"This reply expresses a general view regarding the law or regulation in question that the FSA formed at this time exclusively on the basis of information contained in the written inquiry, in its capacity as the entity that has jurisdiction over the said law or regulation. Therefore, the reply does not provide judgment regarding the application of the said law or regulation to a specific case or have binding power on the judgment of the investigative or judicial authorities."

c. When the relevant FSA division decides not to reply to the inquiry through said process, it shall notify the inquirer with the decision and provide the basis thereof.

E. Publication

When the FSA has provided a reply according to the procedures prescribed in "D" above, it shall immediately publish the inquiry and the reply on its web site.

(iv) Regarding inquires which do not fit the description of (iii) above but are made frequently, a reference circular that describes the reply to the inquiry (in the format specified in the Attached List of Formats II-14) shall be compiled, distributed to the relevant departments and stored at the planning sections of the relevant departments of the FSA and the Local Finance Bureaus.

(v) In cases where the inquirer seeks a written reply from the FSA and where the Prior Confirmation Procedures on the Application of Laws and Regulations by Administrative Agencies ("no action letter" system) are applicable in light of II-3-2(2), the inquirer shall be asked to apply for the said procedures.

II-3-2 Prior Confirmation Procedures on the Application of Laws and Regulations by Administrative Agencies ("No Action Letter" System)

Under the Prior Confirmation Procedures on the Application of Laws and Regulations by Administrative Agencies (hereinafter referred to as the "No Action Letter System"), private companies seek prior confirmation as to whether specific practices related to their planned business activities are subject to specific laws and regulations, and the said organizations make the replies they receive public. The FSA has established detailed rules concerning the No Action Letter System. This section only specifies the administrative procedures concerning the No Action Letter System, so supervisors shall make sure to refer to "Detailed Rules concerning the Prior Confirmation Procedures on the Application of Laws and Regulations by Administrative Agencies" when using the No Action Letter System.

(1) Contact Point for Inquiry

Inquiries shall be submitted to the Coordination Division of the Supervisory Bureau. The Coordination Division shall immediately process the inquiry if it meets the requirements specified in (2) (iii) below and forward it to the division that has jurisdiction over the law or regulation in question. Financial institutions under the jurisdiction of Local Finance Bureaus shall submit an inquiry to the relevant bureaus, which shall in turn immediately forward the written inquiry to the Coordination Division of the Supervisory Bureau via e-mail, etc.

(Note) In principle, the local Finance Bureau forwarding the written inquiry to the Coordination Division of the Supervisory Bureau shall attach its own opinion thereto.

(2) Flow of Processes after Receipt of a Written Inquiry

The relevant division that has received the inquiry shall check whether it is appropriate to reply thereto in light of (i) and (iii) below in particular. In cases where the inquiry is not eligible for the No Action Letter System, the inquirer shall be notified of the ineligibility. In cases where it is deemed to be necessary for the inquirer to submit additional or corrected documents, the inquirer may be asked to do so. However, it is important to avoid imposing an excessive burden on the inquirer, by minimizing the volume of requested additional or corrected documents.

(i) Scope of Matters Subject to Inquiry

Whether the inquiry has been submitted by a private company planning to engage in a new business or transaction in order to inquire about the following matters, in relation to the laws and ordinances listed on the FSA's web site as subject to the No Action Letter System (hereinafter referred to as "Relevant Laws and Regulations (Provisions)" and government orders based thereon.

A. Whether engaging in the business or transaction in question amounts to operating without authorization.

B. Whether engaging in the business or transaction in question amounts to operating without notification.

C. Whether engaging in the business or transaction in question leads to the suspension of business

operation or rescission of a license (adverse dispositions).

D. Whether engaging in the business or transaction in question leads to the direct imposition of a certain obligation or limitation of rights.

(ii) Scope of Eligible Inquirers

Whether the inquirer is an individual or a legal person planning to start a new business and wishing to inquire about the applicability of the Relevant Laws and Regulations (Provisions), or a lawyer or the like employed by the said individual or legal person. Whether the inquirer has submitted a written inquiry that meets the criteria specified in (iii) below and agreed to have the content of the inquiry and the reply thereto made public.

(iii) Inquiry Content

An inquiry must meet the following criteria:

A. Describing specific and concrete facts relating to planned business activity.

B. Containing specific indication of the provisions of the relevant laws and regulations (Provisions) regarding which the inquirer wishes to check the applicability to the planned activity.

C. Containing a statement from the inquirer agreeing to have the contents of the inquiry and the reply thereto made public.

D. Clarifying the inquirer's opinion concerning the applicability of the provisions of the laws and regulations in "B" above and the basis thereof.

(iv) Response Timeframe

In principle, the head of the division that has received the inquiry shall reply to the inquirer within 30 days from the arrival at the contact point of a written inquiry from the inquirer. However, in the following cases, the response timeframe shall be set as follows. In any case, the FSA shall strive to ensure that the response time, including the time needed for submitting additional or corrected documents, is made as short as possible.

A. In cases where the inquiry concerns advanced financial techniques or technologies, thus requiring a careful judgment, the FSA shall make a reply within 60 days in principle from the receipt of the inquiry.

B. In cases where the relevant section's conduct of administrative processes may be impeded significantly by an excessive volume of inquiries, a reply may be delayed till 30 days from the initial receipt of the inquiry or later but must be made within a reasonable period of time.

C. In cases where the law or regulation in question is under the joint jurisdiction of the FSA and another government agency, a reply shall be made within 60 days in principle from the receipt of the inquiry.

In cases where the inquirer has been asked to submit corrected or additional information, the days involved in gathering the said information shall not be counted in the 30-day period. If it is not possible to make a reply within 30 days, the FSA shall provide the reason for the delay and the expected date of reply to the inquirer.

(v) Publication of Inquiries and Replies

As a general rule, the contents of inquiries and the replies thereto shall be posted on the FSA's web site in their entirety within 30 days from the issuance of the reply.

However, in cases where the inquirer requests a delay in the publication of the inquiry and the reply thereto, and provides a rational reason for the delay and specifies the time when publication may be made, the FSA may delay the publication of the inquiry and the reply. In such cases, the publication may not necessarily be delayed until the date requested by the inquirer. When the reason for the requested delay has ceased to be valid, the FSA may make the inquiry and the reply thereto public after giving prior notice to the inquirer. In cases where an inquiry or the reply thereto contains information that falls under the category of matters of non-disclosure, as specified under the provisions of Article 5 of the Act Concerning the Disclosure of Information Retained by Administrative Agencies, the FSA may, as necessary, withhold such information from disclosure.

II-4 Points of Attention in Providing Administrative Guidance, etc.

II-4-1 Points of Attention in Providing Administrative Guidance, etc.

When providing administrative guidance, etc., ("Administrative guidance, etc.," includes administrative guidance as specified under Article 2(vi) of the Administrative Procedure Act as well as the advice and other acts that cannot be clearly distinguished from administrative guidance) to Financial Instruments Business Operators, etc., supervisors shall abide by the Administrative Procedure Act and other relevant laws and regulations. The following points shall be taken into consideration.

(1) General Principles (Article 32 of the Administrative Procedure Act)

(i) Whether the administrative guidance, etc., is followed entirely on the basis of voluntary cooperation of the supervised business operator. For example, the following points shall be taken into consideration:

A. Whether the supervisor has obtained the understanding of the supervised business operator on the contents and application of the administrative guidance, etc., and the conduct of the official in charge.

B. Whether the administrative guidance has been continued despite the supervised business operator's expression of an unwillingness to cooperate.

(ii) Whether the supervisor has given unfavorable treatment to a business operator for failing to follow administrative guidance, etc.

A. It should be kept in mind that disclosing a failure to follow administrative guidance, etc., without due legal grounds could amount to "unfavorable treatment" in a situation where such disclosure would serve as a social punishment by causing economic losses, for example.

B. In cases where the authority to take administrative dispositions may be exercised depending on the circumstances following the provision of administrative guidance, etc., the supervisor may provide the administrative guidance, etc., while indicating the possibility of the exercise of the said authority.

(2) Administrative Guidance, etc. Related to Applications (Article 33 of the Administrative Procedure Act)

Whether the supervisor has prevented the applicant's exercise of its rights by continuing administrative guidance, etc., despite the applicant's expression of an intention not to follow the said administrative guidance, etc.

(i) Even if the applicant has not clearly expressed an intention not to follow administrative guidance, etc., the supervisor shall consider whether the applicant has no intention to do so by taking into consideration the background to the administrative guidance etc., and changes in the objective circumstances, etc.

(ii) It should be kept in mind that even if the applicant is following administrative guidance etc., this does not necessarily constitute voluntary consent to the supervisor's possible suspension of the screening and response processes regarding the application.

(iii) The following points shall be taken into consideration, for example:

A. Whether the supervisor has prevented the applicant's exercise of its rights by putting the applicant in a situation in which it is impossible not to follow administrative guidance, etc.

B. In cases where the applicant has not clearly expressed an intention to not follow administrative

guidance, etc., whether the supervisor has not suspended the screening and response processes regarding the application on the grounds that the applicant is receiving administrative guidance, etc.

C. In cases where the applicant has expressed an intention to not follow administrative guidance, etc., whether the supervisor has ceased the said administrative guidance, etc., and processed the application in a prompt and appropriate manner.

(3) Administrative Guidance, etc., Concerning Authority over Granting of License and Approval (Article 34 of the Administrative Procedure Act)

In cases where the supervisor does not have the authority to grant a license or approval or take administrative dispositions based thereon, or where the supervisor has no intention to exercise such authority, whether the supervisor is forcing a business operator to follow administrative guidance, etc., by making an ostensible show of the possibility of exercising the authority.

For example, the following points shall be taken into consideration:

(i) Whether the supervisor is requiring a business operator to engage in or refrain from engaging in a particular act by pretending to have the authority to deny a license or approval in cases where the supervisor does not in reality have such authority.

(ii) Whether the supervisor is forcing a business operator to follow administrative guidance, etc., by indicating the possibility of exercising the authority regarding licensing and approval at any time unless the administrative guidance, etc., is followed, or by implying that some kind of unfavorable treatment would be given.

(4) Method of Administrative Guidance (Article 35 of the Administrative Procedure Act)

(i) When providing administrative guidance, etc., whether the supervisor clarifies to the supervised business operator what the purpose and contents of the said guidance, etc., are and who the officer in charge is.

The following points shall be taken into consideration, for example:

A. Whether the supervisor clarifies what act the supervised business operator should engage in or refrain from engaging in.

B. Whether the supervisor indicates which officer is responsible for the provision of relevant administrative guidance, etc.

C. In cases where administrative guidance, etc., is provided based on a specific law, whether the supervisor indicates the legal provision used as the basis.

D. In cases where the provided administrative guidance, etc., is not based on a specific law, whether the supervisor gains the business operators understanding of the necessity of the said guidance by explaining the purpose thereof.

(ii) In cases where the supervised business operator requests the provision of a document that specifies the officer in charge and the purpose and contents of administrative guidance, etc., whether the supervisor meets the request in principle, unless there is any particular problem from the viewpoint of the conduct of administration (excluding cases that fit the description of either item of Article 35 (3)).

A. In cases where the provision of a written document is requested, it is necessary to meet the request as soon as possible.

B. A "particular problem from the viewpoint of the conduct of administration" that justifies a refusal to provide the requested document refers to the case in which a significant impediment could be caused to the conduct of administration by the indication in writing of the officer in charge and the purpose and contents of administrative guidance, etc. For example, if the document specifying those matters is utilized or interpreted regardless of the intention of the person who compiled it, achieving a certain administrative objective could become impossible.

C. It should be kept in mind that a large backlog of work to be conducted or a need to conduct work in a short period of time alone would not constitute a "particular problem from the viewpoint of the conduct of administration."

II-4-2 Points of Attention in Holding Interviews, etc.

When FSA employees hold interviews, etc., ("Interviews, etc.," include face-to-face interviews, telephone conversations and e-mail exchanges) with management and employees of Financial Instruments Business Operators, etc., they shall take the following points into consideration:

(i) Whether the FSA employees who participate in interviews, etc., always maintain discipline and decorum as well as a calm and composed attitude.

(ii) Whether FSA employees confirm the purpose of interviews, etc., and the names and affiliation of the interviewees.

(iii) Whether FSA employees ensure that the place and time of their interviews, etc., as well as the composition of participants from the FSA side and the interviewed business operator are appropriate in light of the purpose and contents thereof.

(iv) Whether FSA officials make sure, as necessary, to have both sides share the recognition of the contents and results of interviews, etc. In particular, when the contents and results of an interview, etc., are subject to a confidentiality obligation, whether it is ensured that the need for confidentiality is made clear to both sides.

(v) In cases where FSA officials face a need to consult their superiors with regard to the contents of interviews, etc., whether they seek the superiors' judgment in advance or make a report to the superiors immediately after the interviews, etc., depending on the circumstances. Furthermore, when they hold interviews with two or more business operators regarding matters that require consultations with their superiors, whether FSA officials take care to ensure the consistency and transparency of the conduct of administration.

II-4-3 Procedures for Communications and Consultations

When supervisors find it difficult to make judgment in light of the Administrative Procedure Act as to the appropriateness of the administrative guidance, etc., that they plan to provide through interviews, etc., they shall contact the relevant FSA division and hold consultations as necessary about what to do.

II-5 Points of Attention in Taking Administrative Dispositions

II-5-1 Response to Inspection Results, etc.

(1) Response to Inspection Results

Supervisory departments shall properly reflect the results of inspections of Financial Instruments Business Operators, etc., conducted by inspection departments in supervisory processes as follows:

(i) Regarding violation of laws pointed out in inspection reports, and acts and situations that are related to Financial Instruments Business Operators' business operations and assets and registered financial institutions' business operations, and that are problematic from the viewpoint of protecting public interests and investors, as well as important matters pointed out in the previous inspection regarding which improvement is not sufficient, supervisors shall order, under Article 56-2(1) of the FIEA, the submission within one month (the deadline for the submission may be shortened on an item-by-item basis) of a report on factual confirmation, the analysis of causes, and improvement and corrective measures, when they deem it necessary and appropriate to do so.

In addition, regarding a Financial Instruments Business Operator, etc., that is planning a system integration as part of a merger or another similar business restructuring move, and regarding which a problem has been pointed out with regard to the internal control environment for managing system integration risk, the supervisor shall order the submission of a report under the same legal provision on the policy for implementing its system integration plan precisely and on the internal control environment regarding the system risk (including internal audits), among other matters, when they deem it necessary and appropriate to do so.

Orders for the submission of the above reports shall be issued in the format specified in the Attached List of Formats II-15.

(ii) When receiving the above reports, the supervisor shall hold sufficient hearings with the Financial Instruments Business Operator, etc. When holding the hearings, the supervisor shall maintain close cooperation with inspection departments.

(iii) In cases where a certain period of time is deemed to be necessary in order to implement improvement and corrective measures specified in the reports and to make improvement regarding the matters pointed out in the inspection, the supervisor shall strive to ensure appropriate follow-up through periodic hearings, for example.

(iv) In cases where the Securities and Exchange Surveillance Commission has issued a recommendation regarding administrative dispositions and other measures to be taken based on Article 20 (1) of the Act for Establishment of the Financial Services Agency, supervisory authorities shall consider issuing an order for the submission of reports based on Article 56-2(1) of the FIEA and taking administrative dispositions based on Articles 51 to 52-2 of the FIEA and other appropriate measures after examining the contents of the recommendation.

(2) Requirement for the Submission of Reports Based on Off-site Monitoring

(i) In cases where a Financial Instruments Business Operator, etc., is deemed to have a problem in its control environment for risk management, legal compliance and governance, etc., the supervisor shall require the submission of a report, based on Article 56-2(1) of the FIEA, on factual recognition regarding the problem, the analysis of the cause, improvement and corrective measures and other necessary matters.

(ii) In cases where it is deemed necessary to conduct more detailed investigation as a result of verifying the report, the supervisor shall require the submission of an additional report based on Article 56-2(1) of the FIEA.

(iii) In cases where any serious problem from the viewpoint of protecting public interests and investors has not been detected as a result of the examination of the above reports, and where it is deemed possible for the Financial Instruments Business Operator, etc., to make voluntary improvement efforts, the supervisor shall follow up on the reported improvement and corrective measures through voluntary hearings and other means.

(iv) When necessary, the supervisor shall require the submission of periodic reports based on Article 56-2(1) of the FIEA and follow up thereon.

II-5-2 Administrative Dispositions Based on Articles 51 to 52-2 (1) (Business Improvement Orders, Business Suspension Orders, etc.)

In cases where a serious problem from the viewpoint of protecting public interests and investors has been detected as a result of the examination of the contents of reports submitted by Financial Instruments Business Operators, etc., or the contents of recommendations issued by the Securities and Exchange Surveillance Commission in light of the evaluation items specified in this Guideline for Supervision, the supervisory departments shall decide which administrative dispositions to take with due consideration of the factors described in (1) to (3) below after considering, among other factors, the following points:

- Whether it is appropriate to leave it to the Financial Instruments Operator, etc., to make improvement efforts on a voluntary basis.
- Whether substantial improvement is required and it is necessary to have the Financial Instruments Business Operator, etc. concentrate on business improvement for a certain period of time.
- Whether it is appropriate to allow the Financial Instruments Business Operator, etc., to continue business operations.

(1) Seriousness and Maliciousness of Acts

(i) Degree of Damage to Public Interests

Whether the Financial Instruments Business Operator, etc., is undermining public interests significantly by, for example, originating and providing products markedly inappropriate from the viewpoint of appropriate disclosure of financial conditions to customers, thereby damaging confidence in the financial markets?

(ii) Extent of Damage to Users

Whether a number of users across wide regions have suffered damage. How serious the damage done to individual users is.

(iii) Maliciousness of Acts

Whether the Financial Instruments Business Operator, etc., has acted in a malicious way, such as by continuing to sell similar products despite receiving numerous complaints from users.

(iv) Duration and Repetitive Nature of Acts

Whether the act in question committed by a Financial Instruments Business Operator, etc., has been committed for a long period of time. Whether the act has been committed repeatedly and continuously or only once. Whether the Financial Instruments Business Operator, etc., committed a similar illegal act in the past.

(v) Intentionality

Whether the Financial Instruments Business Operator, etc., has committed the illegal/inappropriate act intentionally while recognizing the illegality and inappropriateness, or has done so through negligence.

(vi) Institutional Involvement

Whether the act has been committed based on an individual employee's judgment or a manager has been involved. Whether the management team has been involved.

(vii) Presence or Absence of Cover-Up Actions

Whether an attempt to cover up the act has been made after its illegality was recognized. Whether a cover-up, if one exists, was an institutional act.

(viii) Involvement of Anti-Social Forces

Whether any anti-social forces have been involved. How much involvement, if any.

(2) Appropriateness of Control Environment for Governance and Business Operation

(i) Whether the representative director and the board of directors are fully aware of the importance of legal compliance and make sufficient efforts to ensure compliance.

(ii) Whether the internal audit section is adequately staffed and equipped to conduct audits and whether the division is functioning properly.

(iii) Whether the compliance and risk management divisions are adequately staffed and equipped to perform their tasks and whether they are functioning properly.

(iv) Whether employees engaging in business are fully aware of the importance of legal compliance and whether sufficient internal training is provided.

(3) Attenuation Factors

Whether there are attenuation factors, such as the implementation of voluntary efforts by the Financial Instruments Business Operator, etc., to protect investors before the administrative response.

II-5-3 Points of Attention Regarding Administrative Dispositions against Registered Financial Institutions

In cases where inappropriate practices have been recognized with regard to securities-related businesses conducted by registered financial institutions, supervisory departments shall require the submission of reports and issue orders for business improvement, etc., as necessary in cooperation with the divisions in charge of the supervision of banks, from the viewpoint of not only protecting investors under the FIEA but also ensuring the

soundness of the management under the Banking Act and other relevant laws.

II-5-4 Standard Processing Period Regarding Supervisory Actions Based on Inspection Results

In cases where supervisory actions are to be issued based on Articles 51 to 52-2 of the FIEA, the following procedures shall be followed:

(i) The supervisor shall determine supervisory actions within one month from the receipt of letters of recommendations or inspection reports (copies) (within two months in cases where the chief of the relevant Local Finance Bureau needs to consult the FSA Commissioner and in cases where the actions are based on laws that are under the joint jurisdiction of the FSA and other ministries and agencies).

(ii) In cases where the Financial Instruments Business Operators, etc., and other business operators are required to submit reports, regarding the matters pointed out in the said letters of recommendations and inspection reports, for factual confirmation or other purposes, the said orders shall be issued within one month from the receipt of the reports (within two months in cases where the chief of the relevant Local Finance Bureau needs to consult the FSA Commissioner and in cases where the orders are based on laws that are under the joint jurisdiction of the FSA and other ministries and agencies).

(Note 1) In determining the timing of the "receipt of a report," the following points shall be taken into consideration:

(a) In cases where the submission of a report based on Article 56-2(1) of the FIEA is required twice or more (limited to cases where the submission of an additional report is required within the prescribed period from the receipt of the most recent report), the receipt of the last report shall be the starting point of the counting of the standard processing period.

(b) In cases where the submission of corrected or additional documents (excluding those concerning minor corrections and additions) is required, the receipt of the said documents shall be the starting point of the counting of the standard processing period.

(Note 2) The time necessary for legal explanations and hearings shall not be included in the counting of the standard processing period.

(Note 3) The standard processing period shall be applied on the basis of each item of information used as the basis for determining what supervisory action to take.

II-5-5 Removal of the Requirement for the Submission of Reports on Compliance with Business Improvement Orders under Articles 51 and 51-2 of the FIEA

In cases where business improvement orders are issued against Financial Instruments Business Operators, etc., based on Articles 51 and 51-2 of the FIEA, the supervisor shall follow up on their business improvement efforts and, in principle, require the submission of reports on the implementation of business improvement plans so as to promote such efforts. Regarding the follow-up and the requirement for the submission of reports, the following points shall be taken into consideration:

(1) In cases where Financial Instruments Business Operators, etc., who have received business improvement orders based on Article 51 and 51-2 of the FIEA are required to submit reports on the implementation of their

business improvement plans for a specified period of time, the requirement shall be removed upon the arrival of the end of the said period.

(2) In cases where Financial Instruments Business Operators, etc., who have received business improvement orders based on Article 51 and 51-2 of the FIEA are required to submit reports on the implementation of their business improvement plans continuously without any set timeframe, the requirement shall be removed when it is recognized that sufficient improvement measures have been taken in line with their business improvement plans with regard to the problems that constituted the basis of the issuance of the orders. A decision on whether to remove the requirement shall be made in light of the implementation of improvement efforts as identified through the submitted reports and other means.

II-5-6 Relation to the Administrative Procedure Act and Other Laws

(1) Relation to the Administrative Procedure Act

It should be kept in mind that in cases where supervisors intend to take adverse dispositions, including issuing orders for business improvement and business suspension and rescinding registration and licenses, they must hold legal hearings based on Article 57(2) of the FIEA.

It should also be kept in mind that in the case of any of the adverse dispositions, supervisors must indicate the reason for the action based on Article 14 of the Administrative Procedure Act.

(2) Relation to the Administrative Appeals Act

It should be kept in mind that in cases where supervisors intend to issue orders for business improvement and business suspension or rescind registration and licenses, the relevant Financial Instruments Business Operators, etc., must be advised in writing that they are entitled to lodge complaints, based on Article 5 of the Administrative Appeals Act if they are under the jurisdiction of Local Finance Bureaus and based on Article 6 of the same act if they are under the jurisdiction of the FSA.

(3) Relation to the Administrative Case Litigation Act

It should be kept in mind that in cases where supervisors intend to require the submission of reports, issue business improvement or business suspension orders, and rescind registration or licenses, the relevant Financial Instruments Business Operators, etc., must be advised in writing that they are entitled to file suits to seek the rescission of the said administrative dispositions based on Article 8 of the Administrative Case Litigation Act.

II-5-7 System for Exchange of Opinions

In cases where adverse dispositions are to be taken, it may be useful for supervisors to exchange opinions with the relevant Financial Instruments Business Operators, etc., at several levels upon their request, in addition to holding legal hearings and granting opportunities for making explanations based on the Administrative Procedure Act, in order to share the recognition of the facts that constitute the basis of the administrative dispositions and their seriousness.

In cases where a Financial Instruments Business Operator, etc., who has recognized the likelihood of becoming the target of an adverse disposition during the hearing process concerning the requirement for the submission of a report, requests that an opportunity be provided for an exchange of opinions (refer to Note 1) between senior supervisors (refer to Note 2) and senior officials of the business operator, and where the supervisory authorities intend to take adverse disposition that involves opportunities for hearings or explanations, an opportunity for an exchange of opinions about the facts that constitute the basis of the adverse disposition and their seriousness shall be granted before the notification of the said opportunity for hearings and explanations, unless it is necessary to take the said administrative disposition urgently.

(Note 1) Requests from Financial Instruments Business Operators, etc., for an opportunity for an exchange of opinions shall be met only if they are made between the receipt of reports on the facts that constitute the basis of the relevant adverse dispositions that have been submitted based on Article 56-2(1) of the FIEA and the notification of opportunities for hearings and explanations.

(Note 2) "Senior supervisors" include the directors-general of the relevant divisions of the FSA and Local Finance Bureaus.

II-5-8 Notification to Relevant Authorities, including Overseas Supervisory Authorities

In cases where supervisors intend to take adverse dispositions, including issuing orders for business improvement and business suspension and rescinding registration and licenses, they shall, as necessary, notify other relevant authorities, including overseas supervisory authorities

II-5-9 Concept on the Publication of Adverse Dispositions

(1) It should be kept in mind that when supervisors have issued orders for business suspension and rescinded registration and licenses, they must publish the administrative dispositions in official gazettes.

(2) It should be kept in mind that regarding the publication of matters other than those specified in (1) above, the concept specified in 1-5 (Transparency) of "Principles of Financial Supervision and Guidelines of Actions for Supervisory Department Employees (Code of Conduct)" shall be used as a reference for making judgment.

This means that the facts that constitute the basis of adverse dispositions, such as the issuance of orders for business improvement and the contents of the dispositions, should be published, except for cases where the publication of those matters could undermine efforts to improve the management of the relevant Financial Instruments Business Operators, etc. The purpose of this publication is to make it easier for financial institutions in general to predict what administrative dispositions will be taken under what circumstances, thereby reducing the possibility of similar inappropriate incidents arising in the future

II-6 Application Mutatis Mutandis

(1) Application Mutatis Mutandis to Persons Engaging in Businesses Specially Permitted for Qualified Institutional Investors

The provisions of II-2, II-3, II-4 and II-5 shall be applied mutatis mutandis to administrative processes regarding persons engaging in businesses specially permitted for qualified institutional investors. It should be noted that words and sentences in the relevant format specified in the Attached List of Formats shall be replaced as necessary.

(2) Application Mutatis Mutandis to Financial Instruments Intermediary Service Providers

The provisions of II-1-1(6) and (7) (limited to (iii) to (vi)), II-1-3, II-1-5, II-2, II-3, II-4 and II-5 shall be applied mutatis mutandis to administrative processes regarding financial instruments intermediary service providers. In addition, the following points shall be taken into account. It should be noted that words and sentences in the relevant format specified in the Attached List of Formats shall be replaced as necessary.

(i) Coordination and Liaison with Competent Directors-General of Local Finance Bureaus

The directors-general of Local Finance Bureaus shall apply mutatis mutandis the provisions of II-1-2 (2) (i) and (ii) to their coordination and liaison with the competent directors-general of Local Finance Bureaus regarding supervisory processes related to financial instruments intermediary service providers and take the following points into consideration:

A. When the directors-general of Local Finance Bureaus supervise financial instruments intermediary service providers who handle financial products on behalf of Financial Instruments Business Operators, etc., under the jurisdiction of the FSA Commissioner or the directors-general of other Local Finance Bureaus, they shall strive to cooperate therewith by, for example, providing information necessary for supervising the said Financial Instruments Business Operators, etc.

B. The directors-general of Local Finance Bureaus, when sales offices or other facilities of financial instruments intermediary service providers under the jurisdiction of the directors-general of other Local Finance Bureaus are located in their areas of jurisdiction, shall strive to cooperate with those Local Finance Bureau directors-general by, for example, providing information necessary for the supervision of the said financial instruments intermediary service providers.

(3) Application Mutatis Mutandis to Securities Finance Companies

The provisions of II-1-3, II-2, II-3, II-4 and II-5 shall be applied mutatis mutandis to administrative processes regarding securities finance companies.

(4) Application Mutatis Mutandis to Investment Corporations

The provisions of II-1-1(6) and (7), II-1-3, II-2, II-3, II-4 and II-5 shall be applied mutatis mutandis to administrative processes regarding investment corporations. It should be noted that words and sentences in the relevant format specified in the Attached List of Formats shall be replaced as necessary.

(5) Application Mutatis Mutandis to Commodities Investment Sales Companies

The provisions of II-1-2(1) and (2)(ii), 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 be applied mutatis mutandis to administrative processes regarding commodities investment sales companies, based on the Act on Regulation on Commodities Investment-Related Business. It should be noted that words and sentences in the relevant format specified in the attached list of formats shall be replaced as necessary.

III. Supervisory Evaluation Points and Various Administrative Procedures (General)

III-1 Governance (General)

In order to realize the sound development of the securities market, it is important for Financial Instruments Business Operators themselves to endeavor to develop their control environment for legal compliance and conduct management in a manner to ensure full customer protection. In conducting daily supervisory administrative processes, it is necessary to examine what the desirable status of governance by a Financial Instruments Business Operator is, from the viewpoint of whether its management team's checking of the execution of the business operators' business is conducted effectively and whether the monitoring and control of the management team is conducted effectively.

(1) Major Supervisory Viewpoints

In order to ensure that governance by a Financial Instruments Business Operator functions effectively, all officers and employees need to recognize that the business operator bears important social responsibilities as an intermediary of the financial instruments market, and need to be involved in business operations based on a full understanding of the roles assigned to them. In particular, the representative director, individual directors and the board of directors, individual auditors and the board of auditors, and the internal audit section bear important responsibilities.

Naturally, the representative director, as the director empowered to represent the Financial Instruments Business Operator, bears the greatest responsibility for the management thereof. The board of directors, as the highest decision-making body of the Financial Instruments Business Operator, is not only empowered to make specific decisions regarding the execution of business, but also has the functions of monitoring the execution of business by the representative director and the director in charge, and preventing autocratic management. Auditors and the board of auditors are granted broad and strong authority so as to audit the execution of business by directors, etc., who bear important responsibilities for the management of the Financial Instruments Business Operator as stated above, thereby bearing important responsibilities for the task of monitoring governance.

It is necessary to examine whether the representative director, directors/the board of directors and auditors/the board of auditors are fully performing their important responsibilities for the management of the Financial Instruments Business Operator, by paying attention to the following points, for example:

(Note) In the case of Financial Instruments Business Operators that have established committees based on the Companies Act, it is necessary to examine whether the board of directors, committees, executive officers, etc., exercise their respective authority appropriately. In this case, examination should be conducted with due consideration of the actual status of management based on the purpose of this Guideline.

(i) Representative Director

A. Whether the representative director counts matters concerning the execution of business as well as those concerning the development and establishment of legal compliance and internal control environment among the most important management issues. Also, whether the director is sincerely leading efforts to formulate a specific policy for implementing compliance and is ensuring full

compliance.

B. Whether the representative director fully recognizes that disregard of the risk management division may have a serious impact on corporate earnings and attaches importance to the said division.

C. Whether the representative director, based on the recognition of the importance of internal audits, sets appropriate objectives of internal audits and establishes arrangements for enabling the internal audit section to fully perform its functions (including securing the independence of the internal audit section), and periodically checks the performance of the functions. Whether the representative director approves basic matters concerning internal audit plans, including an audit policy and priority items, in light of the risk management status, etc., of divisions subject to audits, and implements appropriate measures based on the results of internal audits.

D. Whether the representative director fully understands that banning any relations with anti-social forces and firmly excluding such forces is vital for maintaining public confidence in the Financial Instruments Business Operator and securing the appropriateness and soundness of its business. In addition, based on this understanding, whether the representative director has made clear, both throughout the company and to the outside, a basic policy decided by the board of directors with due consideration of the "Guideline for Prevention of Damages from Anti-Social Forces in Industry" (agreed upon at a meeting on June 19, 2007 of cabinet ministers responsible for anti-crime measures; referred to as the "Government Guideline" hereinafter in III-1).

(ii) Directors/Board of Directors

A. Whether directors check and prevent autocratic management by the representative director and other officers who are responsible for business execution, and are actively involved in the board of directors' decision-making and checking process concerning business execution.

B. Whether the Board of Directors has specified a management policy based on the overall vision of the desirable status of the Financial Instruments Business Operator. Whether it has established management plans in line with the management policy and communicated the plans throughout the company. Whether it regularly reviews and revises the progress status thereof.

C. Whether the board of directors counts not only matters concerning the execution of business, but also those concerning the development and establishment of legal compliance and internal control environment among the most important management issues, and is sincerely leading efforts to formulate a specific policy for implementing compliance and ensuring full compliance. Whether it makes sure to communicate the said policy throughout the company. In addition, whether the board of directors has decided a basic policy based on the Government Guideline, established a framework for implementing it and clearly positioned the prevention of damage that could be inflicted by anti-social forces as a matter of legal compliance and risk management by, for example, periodically examining the effectiveness thereof.

D. Whether the board of directors fully recognizes that disregarding the risk management division may have a serious impact on corporate earnings, and attaches importance to the said division. In particular, whether the director in charge has in-depth knowledge and understanding concerning the methods of measuring, monitoring and managing risks, in addition to an understanding of where risks reside and

what kind of risks they are.

E. Whether the board of directors has set up a policy for managing various risks based on strategic objectives. Whether it reviews and revises the risk management policy on a periodic or as-needed basis so as to adapt the policy to changes in strategic objectives, and the development of risk management techniques, etc. In addition, whether the board of directors makes use of risk-related information in the execution of business and the development of risk management systems by, for example, making necessary decisions based on risk-related information reported periodically.

F. Whether the board of directors recognizes the importance of segregated custody of customer assets based on their understanding that it contributes to investor protection and the sound development of the financial instruments market. In addition, whether the board of directors makes use of information related to the status of the segregated custody of customer assets when developing systems for ensuring appropriate segregated custody by, for example, receiving status reports on a periodic or as-needed basis.

G. Whether the board of directors has set appropriate objectives of internal audits and established arrangements for enabling the internal audit section to fully perform its functions based on the recognition of the importance of internal audits (including securing the independence of the internal audit section), and periodically checks the performance of the function. Whether the board of directors approves basic matters concerning internal audit plans, including an audit policy and priority items, in light of the risk management status, etc., of divisions subject to audits, and implements appropriate measures based on the results of internal audits.

(iii) Auditors/Board of Auditors

A. Whether the independence of the board of auditors is ensured in accordance with the purpose of the board of auditors system.

B. Whether the board of auditors properly exercises the broad authority granted thereto and conducts audits of business operations in addition to audits of accounting affairs

C. Whether individual auditors recognize the importance of their own independence within the board of auditors and actively take the initiative to conduct audits.

D. Whether the board of auditors strives to ensure the effectiveness of its audits by, for example, receiving reports on the results of external audits, depending on the contents thereof.

(iv) Internal Audit Section

Internal audits are conducted by entities independent from audited divisions, in order to examine and evaluate the status of business execution and the appropriateness, effectiveness and reasonableness of internal management and control, and to provide advice and make recommendations to the management based thereon, with a view to contributing to the achievement of the management goals of Financial Instruments Business Operators. Therefore, internal audits constitute one of the most important corporate activities for Financial Instruments Business Operators if they are to secure autonomous corporate management. In light of the importance of internal audits, it is necessary to examine whether the function of internal audits is working effectively at Financial Instruments Business Operators, by paying attention to the following points, for example.

A. Whether the internal audit section has been established as an organization that is independent from divisions subject to audit so as to fully check the actions thereof, and is sufficiently staffed and equipped to conduct effective internal audits.

B. Whether the internal audit section formulates internal audit plans based on its understanding of the status of risk management by divisions subject to audits and the types of risks faced thereby with regard to all businesses conducted by the Financial Instruments Business Operator.

C. Whether the internal audit section audits divisions subject to audits in an efficient and effective manner based on internal audit plans.

D. Whether the internal audit section reports important issues identified and pointed out in internal audits without any delay to the representative director and the board of directors.

E. Whether the internal audit section appropriately oversees the improvement status of divisions subject to audits, with regard to matters pointed out in internal audits and reflects it in future internal audit plans.

(v) Use of External Audits

This Guideline does not obligate Financial Instruments Business Operators to undergo external audits of their business operations by external auditors (including audits by the head offices and group companies) in addition to mandatory audits of financial statements, etc., by accounting auditors. However, in order to acquire the profits and secure the effectiveness of the risk management and internal control environment, it is desirable to ensure effective use of external audits by accounting auditors and others, as well as internal audits by Financial Instruments Business Operators themselves. Therefore, examination of the status of external audits should be conducted by paying attention to the following points, for example.

A. Whether important issues identified and pointed out in external audits are reported without any delay to the board of directors or to the board of auditors.

B. Whether divisions subject to audits make improvements with regard to matters pointed out in external audits within a certain time period. In addition, whether the internal audit section appropriately identifies and examines the improvement status.

(2) Supervisory Method and Actions

Supervisors shall examine the status of governance through the following hearings and daily supervisory administrative processes.

(i) Comprehensive Hearings (See II-1-1 (2))

Supervisors shall hold hearings regarding Financial Instruments Business Operators' management challenges, strategies and the status of risk management and governance, among other matters. In addition, senior supervisors shall directly hold hearings with top managers of Financial Instruments Business Operators as necessary.

(ii) Hearings Regarding Internal Audits

Supervisors shall hold hearings with the internal audit sections of Financial Instruments Business Operators as necessary, with regard to their control environment for internal audits, the status of the implementation of internal audits and the correction of problems, from the viewpoint of identifying the

status of the divisions' exercise of their functions.

In addition, supervisors shall hold hearings with Financial Instruments Business Operators' auditors and outside directors when a particular need to do so is recognized.

(iii) Examination of Governance through Daily Supervisory Administrative Processes

Supervisors shall examine the effectiveness of governance not only through the hearings described above but also through daily supervisory administrative processes, such as receiving reports on problematic conduct in financial instruments business.

(iv) Recording of Monitoring Results

Supervisors shall compile and store records on matters of particular note based on the results of monitoring conducted through procedures described above, and make effective use thereof in future supervisory administrative processes.

(v) Supervisory Method and Actions

In cases where doubt has arisen about the effectiveness of a Financial Instruments Business Operator's governance, the supervisor shall monitor voluntary business improvement made by the business operator, by holding an in-depth hearing regarding the cause of problems and improvement measures and, when necessary, requiring the submission of a report based on Article 56-2(1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisor shall take actions such as issuing a business improvement order based on Article 51 of the FIEA. When the business operator is deemed to have committed a serious and malicious illegal act, the supervisor shall consider necessary actions, including issuing an order for business suspension based on Article 52(1) of the FIEA.

III-2 Appropriateness of Businesses (General)

III-2-1 Control Environment for Legal Compliance

(1) Development of Control Environment for Legal Compliance

In order to ensure the development of the Japanese financial market as well as the economy, it is necessary to provide financial instruments and services in an appropriate manner in a fair and transparent securities market, and the confidence of users in Financial Instruments Business Operators is one of the important elements thereof. Financial instruments business operators must make sure to strictly comply with laws and regulations as well as business rules and maintain sound and appropriate business operations. The development of the control environment for legal compliance by Financial Instruments Business Operators shall be examined in light of their business profile with due consideration of the following points, for example.

(i) Whether the Financial Instruments Business Operator has counted compliance as one of the most important management issues and formulated a basic policy concerning the implementation of compliance, a comprehensive implementation plan (compliance program) and a code of conduct (rules concerning ethics and a compliance manual, etc.). In addition, whether it has informed all officers and employees of the existence and contents of the implementation policy, etc., and ensured a full understanding thereof and the implementation of compliance in daily business operations.

(ii) Whether the Financial Instruments Business Operator conducts evaluation and a follow-up regarding the implementation policy and the code of conduct on a periodic or as-needed basis. Whether it reviews and revises the contents thereof.

(iii) Whether the Financial Instruments Business Operator has established a system for ensuring appropriate communications and reporting of compliance-related information among divisions in charge of sales (which refer to all divisions engaged mainly in profit-generating business operations. Hereinafter referred to as "sales divisions."), the division/manager in charge of compliance and the management team.

(iv) Whether the Financial Instruments Business Operator has established robust systems for training and educating officers and employees on compliance and strives to foster and enhance a sense of compliance among officers and employees. In addition, whether it strives to ensure the effectiveness of training by, for example, conducting evaluation and follow-up in a timely manner and by reviewing and revising the contents thereof.

(v) Whether the Financial Instruments Business Operator has established a system for enabling the person in charge of supervising the status of compliance with laws, regulations, rules, etc., (the person specified by Article 15-4(i) of the FIEA Enforcement Order) to perform his or her functions fully so as to enhance the internal control environment and contribute to appropriate business execution. Whether it conducts an evaluation and follow-up regarding the status of performance of the function of the manager in charge of internal control, etc.

(2) Supervisory Method and Actions

Regarding issues of supervisory concern identified through daily supervisory administration and the reporting

of problematic conduct in relation to a Financial Instruments Business Operator's control environment for legal compliance, the supervisor shall keep track of the status of voluntary business improvement made by the business operator by holding an in-depth hearing and, when necessary, requiring the submission of a report based on Article 56-2(1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem, from the viewpoint of protecting public interests and investors, the supervisor shall take actions, including issuing a business improvement order based on Article 51 of the FIEA. When the business operator is deemed to have committed a serious and malicious illegal act, the supervisor shall consider necessary actions, including issuing an order for business suspension based on Article 52(1) of the FIEA.

III-2-2 Supervisory Response to Problematic Conduct in Financial Instruments Business

Supervisory response to problematic conduct in financial instruments business, etc., (refer to Note) shall be made as follows.

(Note) A "problematic conduct in financial instruments business, etc." refers to either of the following cases:

(a) An act that constitutes a violation of the provisions of Article 199 (vii) of the FIB Cabinet Office Ordinance

(b) An indictment of a Financial Instruments Business Operator or officers and employees thereof

(c) Other acts which could undermine the soundness and appropriateness of a Financial Instruments Business Operator's business operations and which are similar to the acts described in (a) and (b).

(1) Major Supervisory Viewpoints

(i) Initial Notification of Problematic Conduct in Financial Instruments Business, etc.

Supervisors shall check the following points upon the receipt of an initial notification of problematic conduct in a financial instruments business, etc., at a Financial Instruments Business Operator. It should be noted that cases in which a written report is submitted without an initial notification shall be handled likewise.

A. Whether the Financial Instruments Business Operator has promptly reported to the internal control and internal audit section as well as to the board of directors, etc., in accordance with compliance rules.

B. In cases where the conduct could constitute a criminal offense, whether the Financial Instruments Business Operator has reported to the police and other relevant organizations.

C. Whether a division independent of the division involved in the conduct (e.g., the internal audit section) investigates the conduct.

(ii) Examination of Appropriateness of Business Operations

Supervisors shall examine the appropriateness of a Financial Instruments Business Operator's business operations in relation to problematic conduct in a financial instruments business, etc., based on the following viewpoints:

A. Whether an executive has been involved in the conduct and whether there has been an institutional involvement.

B. What impacts the conduct is expected to have on the management of the Financial Instruments

Business Operator and on customers and the financial instruments market.

C. Whether the internal checks and balances function is properly functioning.

D. Whether the Financial Instruments Business Operator has formulated improvement measures intended to prevent the recurrence of the conduct, is equipped with a sufficient self-purification function and has clarified the allocation of responsibilities.

E. Whether the Financial Instruments Business Operator acted appropriately immediately after the conduct came to light.

F. In cases where the Financial Instruments Business Operator provides profits from its assets in order to compensate for the losses caused by the conduct, whether the business operator compiles records on the provided profits and the basis of the compensation calculation. In addition, whether the Financial Instruments Business Operator has established arrangements and procedures for enabling a division independent from the sales division, such as the internal control division, to check the status of the compilation of the said records.

(2) Supervisory Method and Actions

In cases where supervisors have recognized the occurrence of problematic conduct in financial instruments business, etc., through reports and notification by Financial Instruments Business Operators, they shall identify and monitor voluntary business improvement made by the business operators by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the Financial Instruments Business Operators are deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing a business improvement order based on Article 51 of the FIEA. When the business operator is deemed to have committed a serious and malicious illegal act, the supervisors shall consider necessary actions, including issuing an order for business suspension based on Article 52(1) of the FIEA.

III-2-3 Control Environment for Customer Solicitation and Explanations

III-2-3-1 Principle of Suitability

In accordance with Article 40 of the FIEA, Financial Instruments Business Operators must ensure that investment solicitation is conducted in an appropriate manner suited to their customer’s attributes, etc., by offering transactions with terms and contents that are commensurate with the customer’s knowledge, experience, asset status and investment purpose as well as his/her ability to make judgment regarding risk management. To this end, it is important to establish a control environment for customer management that enables a precise identification of the customer's attributes and the actual status of transactions, and the supervisor should pay attention to the following issues, for example. (Careful attention should be paid to Internet transactions in particular in light of the absence of face-to-face contact therein.)

(1) Major Supervisory Viewpoints

(i) Efforts for Securing of an Appropriate Identification of Customer Attributes and Appropriate Management

of Customer Information

A. Whether the Financial Instruments Business Operator strives to identify customer attributes such as investment intention and experiences in a timely manner, while properly compiling and managing documented customer information and making sure that all directors, officers and employees recognize the need to strive to conduct investment solicitation in an appropriate manner suited to the customer attributes.

B. Whether the internal control division strives to keep track of how customer attributes are identified and how customer information is managed, and establish an internal control environment that ensures the effectiveness of customer information management by, for example, checking whether solicitation is conducted in an appropriate manner suited to the customer attributes and revising the method of customer information management when necessary.

(ii) Precise Identification of the Actual Status of Customers' Transactions and Effective Use of Acquired Information

A. Whether the Financial Instruments Business Operator examines the transaction conditions, such as trading losses, evaluation losses, the frequency of transactions and the status of fee payment with regard to each customer account, for example, as part of its effort to identify the actual status of transactions conducted by customers.

B. Regarding customers who are deemed to require direct contact in order to check the contents of their transactions, whether the Financial Instruments Business Operator strives to identify the actual transaction status by appropriately, for example, having a sales division manager (this should be a person other than the employee in charge of handling the said customers but may be the manager in charge of internal control or the head of a division, a branch office or a person with a similar status; the same shall apply hereafter) conduct an interview with the said customers in a timely and appropriate manner.

C. Whether the internal control division strives to develop a control environment that ensures the effectiveness of interviews to be conducted by sales division managers with customers by, for example, prescribing a specific interview method, communicating the method to all directors, officers and employees and revising the method as necessary after examining how interviews have been conducted.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's control environment related to the principle of suitability, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the

supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-3-2 Control Environment for Managing Sales Staff

From the viewpoint of ensuring that Financial Instruments Business Operators solicit customers in an appropriate manner suited to the customer attributes, it is important to identify and keep track of the actual state of customer solicitation conducted by the business operators' sales staff. To this end, particular attention shall be paid to the following points:

(1) Major Supervisory Viewpoints

(i) Identification of the Actual State of Customer Solicitation by Sales Staff and Efforts to Ensure Appropriate Solicitation

A. Whether the manager of each sales division, for example, strives to identify and keep track of the actual state of customer solicitation by directly holding interviews with customers, and takes appropriate measures when necessary.

B. Whether the internal control division has developed a specific method of identifying and keeping track of the actual state of customer solicitation and communicated it to all officers and employees, and is striving to establish a control environment that ensures the effectiveness of the method by identifying and examining the status of solicitation and is reviewing and revising the method when necessary.

(ii) Efforts to Foster and Maintain Sense of Compliance among All Officers and Employees

A. Whether the Financial Instruments Business Operator provides case study training, external training and other types of training with a view to enhancing the sense of compliance among all officers and employees.

B. Whether the internal control division implements measures to enhance the effectiveness of training, such as identifying and examining the contents of training programs and the implementation thereof and reviewing and revising the contents of the programs when necessary.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's control environment for managing sales staff, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-3-3 Regulation on Advertisements, etc.

The representations in advertisements, etc., of Financial Instruments Business Operators (advertising as specified under Article 73(1) of the FIB Cabinet Office Ordinance; the same shall apply hereinafter) are the starting points of their solicitation for customers to make investments, and the most important thing about the said representations is that they provide clear and precise information. To ensure this, particular attention shall be paid to the following points.

(Note) "Advertisements etc." includes written materials for customer solicitation, Web pages, postal mail, letters, fax messages, e-mails, fliers and pamphlets and other media materials that provide information to a large number of people. However, judgment as to whether specific media materials are actually advertisements etc., shall be made not on the basis of the appearance or form of the materials or the method of providing them, such as an e-mail, etc., exchange, an airing of a commercial message or the provision of a gift, but on the basis of the specific contents of materials in each case.

(1) Major Supervisory Viewpoints

(i) Points of Attention Regarding Important Matters that Could Affect Customers' Judgment

A. Whether the advertisement, etc., contains a representation that could lead customers to erroneously believe that the fees, commissions, other rewards and expenses they must pay are nil or substantially lower than the actual levels.

B. Regarding financial instruments whose value could fall below their principal amount or for which the loss amount could exceed the principal amount, whether the advertisement, etc., clearly indicates such risks.

(ii) Clear and Precise Representation

In cases where the items specified under Article 37 of the FIEA are indicated in an advertisement, etc., supervisors shall judge whether the advertisement, etc., meets the requirement for clear and precise representation as specified under Article 73(1) the FIB Cabinet Office Ordinance, with due consideration of the following points:

A. Whether the letters used in the advertisement, etc., to indicate some items are not too inconspicuous in terms of size, shape and color compared with the letters used for other items.

In particular, whether the letters used to indicate benchmarks whose movements could cause losses, such as interest rates and prices, the risk of losses and the reasons for them, the risk of the loss amount exceeding the principal amount, and the direct cause thereof, are not markedly different in size from the largest letters used in the same advertisement, etc.

B. Whether the advertisement, etc., avoids placing too much emphasis on the advantages of the financial instruments and indicating its disadvantages in an inconspicuous manner.

C. In the case of an advertisement shown on displays of electric devices, whether sufficient display time is secured for users to read and understand all necessary items.

(iii) Points of Attention Regarding Advertisements Using Exaggerated Descriptions

A. Whether the advertisement does not make definitive predictions of the future movements of the prices and other numerical features of securities and other financial instruments as well as rewards they have

to pay, or does not unduly stimulate customers' investment appetites by using descriptions that could lead them to erroneously believe that profits are guaranteed.

B. Whether the advertisement does not use descriptions that could lead customers to erroneously believe that a certain level of yield is guaranteed or that investment losses will be partially or fully compensated for.

C. Whether the advertisement does not use descriptions that could lead users to believe that the application period and the number of applicants to be accepted are limited whereas in reality they are not limited.

D. Whether the advertisement avoids descriptions that could lead customers to erroneously believe that the Financial Instruments Business Operator, because of its registration, is recommended by the Prime Minister, FSA Commissioner or other public officials and organizations, or that the contents of the advertisement are guaranteed thereby.

E. Whether the advertisement avoids descriptions that constitute or could constitute a violation of prefectural ordinances based on the Act Against Unjustifiable Premiums and Misleading Representations, the Outdoor Advertisement Act or other laws and regulations.

F. Whether the advertisement avoids descriptions that could draw public criticism for being excessive.

(iv) Customer-Soliciting Events

A. In cases where a Financial Instruments Business Operator holds seminars, etc. (events inviting customers in general for the solicitation purpose regardless of whether they are nominally represented as lecture speeches, study sessions or briefings), whether the advertisements and invitation fliers clearly indicate that the events are intended to solicit customers to sign contracts for financial instruments transactions.

B. In order to meet the above requirement for "clearly indicating that the events are intended to solicit customers to sign contracts for financial instruments transactions," the financial institution should represent the seminars, etc., with titles that clearly indicate association with financial instruments transactions and also clearly state that the seminars, etc., are held for solicitation purposes.

(v) Advertisement Screening System

Whether the Financial Instruments Business Operator has appointed staff in charge of screening advertisements, etc., and whether appropriate screening is conducted in accordance with the prescribed screening criteria from the viewpoint of ensuring compliance with Article 37 of the FIEA.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding advertisements etc., for a Financial Instruments Business Operator, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is

deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-3-4 Control Environment for Providing Explanations to Customers

Although a fairly high level of expert knowledge is necessary to understand some financial instruments transactions, ordinary customers may not necessarily have sufficient expert knowledge and experiences. As a result, it is necessary for Financial Instruments Business Operators to fulfill their responsibility for providing appropriate explanations by, for example, disclosing correct information that may be used as a basis for investment decisions to customers and others in a fair manner. Therefore, supervisors shall pay attention to the following points when examining the status of a Financial Instruments Business Operator's provision of explanations, etc., to customers.

(Note) It should be kept in mind that "explanations, etc." include explanations provided at seminars etc., that are intended to attract customers in effect for solicitation purposes.

(1) Major Supervisory Viewpoints Regarding Control Environment for Providing Explanations

(i) Development of Control Environment for Providing Explanations Based on Principle of Suitability

Whether the Financial Instruments Business Operator has developed a control environment that ensures appropriate explanations based on the principle of suitability when providing a pre-contract document, by properly selecting the method and extent of explanation necessary for enabling customers to understand the contents of the financial instruments transaction in light of each customer's knowledge, experiences, asset status and the transaction purpose.

(ii) Provision of Appropriate Explanations Regarding Products and Services

A. Whether the Financial Instruments Business Operator avoids placing too much emphasis on the advantages of the transaction and makes sure to sufficiently explain disadvantages, such as the possibility of incurring losses and other risks.

B. Whether the Financial Instruments Business Operator avoids making false statements when promoting products and services or avoids making definitive claims without sufficient grounds when describing products and services.

C. Whether the Financial Instruments Business Operator explains products and transactions in an objective manner and avoids arbitrary and subjective statements.

D. Whether the Financial Instruments Business Operator explains the contents of products and transactions (basic characteristics of products, the nature, types, and variable factors of risks involved, etc.) in a manner that enables the customer to fully understand them.

In particular, whether the Financial Instruments Business Operator strives to prevent the customer from losing interest in understanding the contents, by, for example, first explaining important matters that may affect their investment decisions, in accordance with the purpose of rules concerning the order of items listed in a pre-contract document.

E. Whether the Financial Instruments Business Operator avoids providing explanations that could create misunderstandings regarding the financial instruments transaction. In particular, whether it avoids

providing explanations that could lead customers to erroneously believe that the principal is guaranteed.

F. In cases where the Financial Instruments Business Operator solicits customers with the use of materials (including newspaper articles, analyst reports) containing third-party market forecasts, whether it avoids making arbitrary use of forecasts tinged with a particular bias.

G. Whether the Financial Instruments Business Operator avoids soliciting customers to sign up for products and transactions that impose an undue burden on customers or lack economic rationality, or whether it makes sure to provide sufficient explanations regarding matters important for customers making investment decisions.

(iii) Explanations Regarding Contract Contents

Whether the Financial Instruments Business Operator provides information regarding the contents of the signed contracts (contract date, amount, value, etc.) to the relevant customers in an appropriate manner upon their requests.

(iv) Method of Internet-Based Explanations

Regarding "the explanations provided in a method and to an extent necessary for enabling the customer to understand" specified under Article 117 (1) (i) of the FIB Cabinet Office Ordinance.

In the case of a financial instruments transaction conducted via the Internet, a Financial Instruments Business Operator shall be deemed to have provided "the explanations provided in a method and to an extent necessary for enabling the customer to understand" as specified under Article 117 (1) (i) of the FIB Cabinet Office Ordinance, when the customer has read explanations shown on the computer display and indicated his/her understanding with a click of the button.

(2) Points of Attention Regarding Explanation of Documents

(i) Financial instruments business operators shall be instructed to be ready to allow customers to view the explanation documents as specified under Articles 46-4 and 47-3 of the FIEA (referred to as the "Explanation Documents" in III-2-3-4 (2) and III-3-1 (9)) whenever requested by them to do so.

(ii) Supervisors shall check the date on which each Financial Instruments Business Operator installed the Explanations Documents at its branches.

(iii) Financial instruments business operators may include additional items, other than items specified under law in the Explanation Documents, at their own discretion.

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's control environment for providing explanations to customers, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator by requiring the submission of reports based on Article 56-2 (1) of the FIEA, when necessary, while paying consideration to the above viewpoints. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA.

When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-4 Management of Customer Information

It is extremely important to ensure the appropriate management of customer information, as such information constitutes the basis of financial instruments transactions.

In particular, information regarding individual customers needs to be handled in an appropriate manner in accordance with the Act on the Protection of Personal Information (hereinafter referred to as the "Personal Information Protection Act"), the FIB Cabinet Office Ordinance, and the guideline on the protection of personal information in the financial sector (hereinafter referred to as the "Personal Information Protection Guideline") and the guideline for practical affairs regarding safety control measures specified in the guideline on the protection of personal information in the financial sector (hereinafter referred to as the Practical Guideline).

(1) Major Supervisory Viewpoints

(i) Whether the Financial Instruments Business Operator has formulated a specific standard for the handling of customer information and communicated it to all officers and employees. In particular, whether the Financial Instruments Business Operator has formulated a standard for the provision of customer information to third parties, based on careful deliberations so as to ensure necessary procedures are implemented in accordance with the Personal Information Protection Act, the Personal Information Protection Guideline and the Practical Guideline.

(ii) Whether the Financial Instruments Business Operator has established arrangements and procedures necessary for examining, in a timely and appropriate manner, the status of the management of customer information, including thorough management of access to customer information, measures to prevent the misappropriation of customer information by insiders, and a robust information management system that prevents illegal access from the outside.

(iii) With regard to the safety control of information concerning individual customers and the supervision of employees engaged in the relevant work, whether the Financial Instruments Business Operator has implemented the following necessary and appropriate measures, in accordance with Article 123 (vi) of the FIB Cabinet Office Ordinance, in order to prevent such information from being leaked, lost or damaged.

(Necessary and Appropriate Measures Regarding Safety Control)

A. Measures based on Article 10 of the Personal Information Protection Guideline

B. Measures based on Section I and Attachment 2 of the Practical Guideline

(Necessary and Appropriate Measures Regarding the Supervision of Employees)

C. Measures based on Article 11 of the Personal Information Protection Guideline

D. Measures based on Section II of the Practical Guideline

(iv) Whether the Financial Instruments Business Operator has implemented measures to ensure, in accordance with Article 123 (vii) of the FIB Cabinet Office Ordinance, that information regarding the race, religious belief, family lineage, birthplace, health, and medical and criminal records of individual customers, as well

as other specified non-disclosure information (Note), are not used except for the cases specified in Article 6 (1) of the Personal Information Protection Guideline.

(Note) “Other specified non-disclosure information” includes:

(a) Information regarding labor union membership

(b) Information regarding ethnicity

(c) Information regarding sexual orientation

(v) Whether the Financial Instruments Business Operator has established arrangements and procedures for notifying customers and the public, and reporting to the authorities in a prompt and appropriate manner when customer information has been leaked, so that secondary damage can be prevented.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator’s control environment for managing customer information, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator, by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-5 Control Environment for Processing Complaints

For Financial Instruments Business Operators, responding to complaints and inquiries from customers in a conscientious manner is an important activity from the viewpoint of complementing the fulfillment of their responsibility for providing appropriate explanations to investors. Therefore, supervisors shall pay attention to the following points, for example, when examining a Financial Instruments Business Operator’s control environment for processing complaints.

(1) Major Supervisory Viewpoints

(i) Business Operator’s Response to Complaints

Whether the board of directors has implemented appropriate measures based on the recognition of the possibility that complaints from customers could cause disadvantages, such as a loss of public confidence, on the Financial Instruments Business Operator.

(ii) Development of Arrangements and Procedures for Handling Complaints

Whether the Financial Instruments Business Operator has clearly designated a division in charge of processing customer complaints and set specific procedures for performing that task so as to ensure that complaints are processed and a response is made in a prompt and appropriate manner. Whether there are arrangements and procedures for ensuring that the contents of complaints are shared among relevant

officials and divisions on a case-by-case basis; for example, whether the contents of complaints that could have material effects on the management of the Financial Instruments Business Operator are reported to the internal audit section and the board of directors.

(iii) Fulfillment of Responsibility to Provide Explanation

Whether the Financial Instruments Business Operator provides sufficient explanations regarding matters about which customers have complained. Whether it makes sure to properly follow up on the status of response to complaints.

In cases where customers have requested the disclosure of information regarding the status of their own transactions, whether the Financial Instruments Business Operator makes appropriate disclosure in accordance with the Personal Information Protection Act.

(iv) Feedback

Whether the Financial Instruments Business Operator makes full use of complaints as a source of feedback information useful for improving its control environment for the solicitation of customers and the conduct of administrative processes, by properly recording and storing the contents of complaints, building a database and analyzing the accumulated data.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's control environment for processing complaints, through daily supervisory administration, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-6 Obligation for Customer Identification and Reporting of Suspicious Transactions

Financial instruments business operators, which play an important role as market intermediaries, should never be involved or exploited in cases of organized crime such as the provision of profits to corporate extortionists.

In order to prevent Financial Instruments Business Operators from being exploited in cases of organized crime, money laundering, terrorism, or contributing to expanding profits gained from criminal activities, it is necessary to establish an advanced and robust company-wide control environment for legal compliance.

From the viewpoint of preventing abuse of financial services by organized crime groups and maintaining public confidence in Japan's financial and capital markets, it is particularly important to establish an internal control environment for customer identification and the "reporting of suspicious transactions" based on the Act for Prevention of Transfer of Criminal Proceeds (hereinafter referred to as the "Anti-Criminal Proceeds Act").

(1) Major Supervisory Viewpoints

When examining a financial institution's control environment for implementing customer identification and the "reporting of suspicious transactions" based on the Anti-Criminal Proceeds Act, supervisors shall pay attention to the following points:

(i) Whether the Financial Instruments Business Operator has established a control environment for properly implementing customer identification based on the Anti-Criminal Proceeds Act.

A. Whether the Financial Instruments Business Operator has established internal rules that specify internal arrangements and procedures for implementing customer identification. In addition, whether it has fully communicated the rules to all officers and employees and ensured their full understanding thereof.

In particular, the following matters shall be specified:

a. The department and manager in charge of implementing customer identification and the roles thereof

b. The department and manager (including a person who makes a final internal decision concerning the relevant operations) in charge of supervising internal administrative processes regarding customer identification, including judgment as to the appropriateness of the identification implemented by the relevant department, the identification, examination and analysis of the implementation status thereof, and the roles of the department and manager.

c. Reporting systems at the departments referred to in a. and b. above (including arrangements for collaboration with other relevant departments)

d. Timely and appropriate compilation and storage of records concerning customer identification and transactions with customers.

B. When implementing customer identification, whether the Financial Instruments Business Operator verifies the credibility and validity of the identity not only by identifying customer attributes properly, but also by requiring the submission of customer identification documents, for example. Whether it properly responds to and manages a problem identified in relation to a customer.

Regarding identification data obtained from a customer, whether the business operator constantly strives to keep track of up-to-date customer attributes through ongoing monitoring of transactions with the customer, for example.

The following are examples of measures that may be implemented in order to identify and keep track of customer attributes:

a. To periodically consolidate customer accounts with the same telephone number or e-mail address, select from among the accounts those for which different addresses or names are registered and those for which the same password is set and check whether the nominees of the accounts are not fictitious persons by, for example, examining the actual state of transactions involving the nominee and directly contacting the nominee.

b. To periodically remind all customers of the need to notify the business operator when there is a change in their address or other items of data used for identification, thereby grasping any such change in a timely manner.

C. Whether the Financial Instruments Business Operator has properly established internal rules that

specify a policy concerning acceptance of customers. In addition, whether it properly applies the said policy to the customer attributes identified through the procedures for customer identification.

D. Whether the Financial Instruments Business Operator re-checks the customer's identity by requiring the customer to submit customer identification documents again, for example, in cases where doubt has arisen about the credibility and validity of the customer identification information obtained in the past, or where the customer is suspected of impersonating another person under whose name the transaction is being conducted.

E. Whether the Financial Instruments Business Operator takes measures that take account of the specific characteristics of transactions (e.g., transactions conducted over the Internet without any face-to-face contact) when implementing customer identification.

F. When hiring officers and employees, whether the Financial Instruments Business Operator screened candidates from the viewpoint of, at the minimum, properly implementing anti-money laundering measures.

G. Whether the Financial Instruments Business Operator provides officers and employees with training and education concerning customer identification on a periodic and ongoing basis. Whether it evaluates the level of the understanding of the officers and employees receiving training and takes follow-up measures, when necessary, in light of their implementation of customer identification in daily business processes.

H. Whether the Financial Instruments Business Operator ensures the effectiveness of customer identification by identifying and examining the implementation status of the identification through periodic internal reviews and internal audits, and by revising and reviewing the implementation method, for example.

(ii) Whether the Financial Instruments Business Operator has established a control environment for properly implementing the "reporting of suspicious transactions" based on the Anti-Criminal Proceeds Act.

A. Whether the Financial Instruments Business Operator has established internal rules that specify internal arrangements and procedures for the "reporting of suspicious transactions." Also, whether it has fully communicated the rules to all officers and employees and ensured their full understanding thereof.

In particular, the following matters shall be specified:

a. The department and manager in charge of identifying "suspicious transactions" and the roles thereof

b. The department and manager (including a person who makes the final internal decision concerning the relevant reporting) in charge of supervising operations related to the identification of "suspicious transactions" within the institution, including the implementation of judgment as to the appropriateness of "suspicious transactions" identified through the arrangements and procedures mentioned in A. above and the identification, examination, and analysis of the implementation status, and the roles of the department and manager.

c. Reporting systems at the departments mentioned in a. and b. above (including arrangements for collaborating with other relevant departments)

B. Whether the Financial Instruments Business Operator ensures that the supervisory department reports to the authorities promptly when a certain transaction is judged to constitute a "suspicious transaction."

C. In judging whether a certain transaction constitutes a case requiring the "reporting of suspicious transactions," whether the Financial Instruments Business Operator comprehensively takes account of the various specific information that it holds with regard to the relevant transaction, such as customer identification data and the circumstances at the time of the transaction. Whether the business operator properly responds to and manages any problem identified in relation to the relevant transaction.

(Note) Accumulating data regarding matters that may lead to "suspicious transactions" and establishing formal criteria for such transactions may serve as an effective means for Financial Instruments Business Operators to make judgment on whether a certain transaction constitutes a case of suspicious transaction. However, if they are to do so, it is desirable that they make sure to comprehensively take account of the specific characteristics of each transaction and other various factors so as to avoid relying exclusively on the said criteria and relegating the reporting procedure to a matter of formality.

D. When judging whether a certain transaction constitutes a case of "suspicious transaction," whether the Financial Instruments Business Operator takes account of the nature and contents of its own business and customer attributes.

Among customer attributes that should be considered are the customer's nationality (whether the customer's home country falls within the FATF's list of non-cooperative countries and territories), public status (whether the customer is politically exposed) and the nature of business in which the customer is engaging: the specific characteristics of the customer's transaction, such as the value and number thereof and whether it is a foreign or domestic transaction.

E. When hiring officers and employees, whether the Financial Instruments Business Operator screens candidates from the viewpoint of, at the minimum, properly implementing anti-money laundering measures.

F. Whether the Financial Instruments Business Operator provides officers and employees with training and education concerning the "reporting of suspicious transactions" on a periodic and ongoing basis. In order to promote understanding by officers and employees, it may be effective to use as a training material the "List of Referred Cases of Suspicious Transactions" (Refer to the FSA web site), which includes examples that may constitute cases requiring the "reporting of suspicious transactions" and examples of past cases in which Financial Instruments Business Operators actually reported to the authorities.

In addition, whether the business operator evaluates the level of understanding of the officers and employees receiving training and takes follow-up measures when necessary in light of their implementation of reporting in daily business processes.

G. Whether the Financial Instruments Business Operator ensures the effectiveness of the "reporting of suspicious transactions" by identifying and examining the implementation status of the reporting through periodic internal reviews and internal audits and by reviewing and revising the implementation method, for example.

(iii) Whether the Financial Instruments Business Operator has established an integrated and centralized internal control environment for judging whether to implement "the reporting of suspicious transactions," by comprehensively taking account of basic customer information obtained through appropriate implementation of customer identification, the specific characteristics of transactions and other matters based on the full recognition of the co-relation between customer identification and the "reporting of suspicious transactions."

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's internal control environment for implementing customer identification and reporting suspicious transactions, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-7 Control Environment for Managing Administrative Risk

(1) Administrative Risk Management

Administrative risk is the risk of Financial Instruments Business Operators and their customers incurring losses due to their officers and employees failing to conduct administrative work properly, causing accidents or committing illegal acts in the course of the administrative work process. Financial instruments business operators need to strive to ensure their reliability and creditworthiness by properly developing an internal control environment regarding administrative risk and maintaining the soundness and appropriateness of their business operations. Therefore, supervisors shall pay attention to the following points, for example, when examining a Financial Instruments Business Operator's administrative risk management.

(i) Major Supervisory Viewpoints

A. Whether the Financial Instruments Business Operator has developed an appropriate control environment for managing administrative risk based on the understanding that such risk is involved in all business operations.

B. Whether the Financial Instruments Business Operator has implemented specific measures to reduce administrative risk based on the recognition of the importance of reducing such risk.

C. Whether the Financial Instruments Business Operator has established a sufficient system of checks and balances by, for example, ensuring independence of the division in charge of managing administrative risk from divisions in charge of sales operations. Whether the business operator has specified procedures regarding administrative processes and reviews and revises them when

necessary.

D. Whether the internal audit section properly conducts internal audits in order to examine the control environment for managing administrative risk. Whether the division in charge of managing administrative risk has established arrangements and procedures for checking sales divisions' and branches' control environment for managing administrative risk. Whether the administrative risk management division and the sales divisions and branches cooperate when necessary to improve the standard of administrative processes.

(2) Outsourcing of Administrative Processes

As Financial Instruments Business Operators are not exempted from the ultimate responsibility regarding administrative processes outsourced to external contractors, supervisors need to pay attention to the following points, for example, in light of the business operators' business profiles, in order to ensure the protection of customers and the soundness of the business operators' management. It should be kept in mind that the following points are general supervisory viewpoints and that supervisors may need to examine other points, too, depending on the contents of the outsourced business operations and other factors.

(i) Major Supervisory Viewpoints

A. Whether the Financial Instruments Business Operator has specified a policy and procedures for selecting the business operations to be outsourced and the contractors to outsource them to.

B. Whether the Financial Instruments Business Operator has developed a control environment that enables sufficient management of administrative risk regarding outsourced business operations.

C. Whether the Financial Instruments Business Operator has implemented measures to prevent the outsourcing of business operations from impeding the fulfillment of its obligations to the supervisory authorities, such as undergoing inspections, making reports and submitting data.

D. Whether the Financial Instruments Business Operator has made it clear that the outsourcing of business operations does not cause any change in the contractual rights and obligations involving it and its customers, who continue to have the same rights as if the business operations were conducted by the business operator itself.

E. Whether the Financial Instruments Business Operator has developed a control environment that ensures the prevention of inconveniences that may be caused to customers should they not be provided the services guaranteed under their contracts related to outsourced business operations.

F. When the handling of information regarding individual customers is outsourced, whether the Financial Instruments Business Operator implements the following necessary and appropriate measures regarding the supervision of the outsourcing contractor in order to prevent the information from being leaked, lost or damaged.

   a. Measures based on Article 12 of the Personal Information Protection Guideline

   b. Measures based on Section III of Practical Guidelines

G. Whether the Financial Instruments Business Operator has established a system for properly handling complaints and inquiries regarding outsourced business operations by, for example, opening a contact point through which customers can directly consult the business operator.

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's control environment for managing administrative risk or for managing the outsourcing of business operations, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings with the business operator or the outsourcing contractor and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-8 Control Environment for Managing Information Technology Risk

Information technology risk is the risk that customers and Financial Instruments Business Operators will incur losses because of a computer system breakdown, malfunction or other inadequacies, or because of inappropriate or illegal use of computer systems. Information systems used by Financial Instruments Business Operators are becoming increasingly advanced and complex, in line with the integration of systems due to mergers and other management restructuring moves and an expansion of the range of products and services. This, combined with an expansion of computer networks, has increased the risk of important information being illegally accessed or leaked.

As secure and stable operation of computer systems is the overriding prerequisite for ensuring public confidence in the market for financial instruments and in Financial Instruments Business Operators, it is extremely important to enhance the control environment for managing information technology risk.

(1) Major Supervisory Viewpoints

When examining a Financial Instruments Business Operator's control environment for managing information technology risk, supervisors shall pay attention to the following points, for example, in light of the business operator's business profile. (For details of the supervisory viewpoints, refer to the Securities Inspection Manual as necessary.)

(i) Recognition of information technology risk

A. Whether the board of directors has formulated a basic policy for company-wide management of information technology risk based on a full recognition of information technology risk.

B. Whether there are arrangements and procedures for ensuring that information regarding information technology risk is properly reported to the management team.

(ii) Establishment of Appropriate Control Environment for Risk Management

A. Whether the Financial Instruments Business Operator has specified a basic policy for the management of information technology risk and developed a relevant control environment.

B. Whether the Financial Instruments Business Operator has designated the types of risk that should be managed according to specific criteria and has identified the location of the risk.

C. Whether the control environment for managing information technology risk is effective enough to enable the Financial Instruments Business Operator to identify and analyze the actual state of its business operations and system troubles, and minimize the frequency and scale of system troubles in a manner suited to the system environment and other factors, thereby maintaining an appropriate level of computer system quality.

(iii) Computer System Audits

A. Whether an internal audit section that is independent from the computer system division and has auditing staff adept in computer systems conducts periodic audits of the computer system.

B. Whether the audited division accounts for all business operations involving information technology risk.

(iv) Development of Safety Measures

A. Whether the Financial Instruments Business Operator has formulated a basic policy for safety measures

B. Whether the Financial Instruments Business Operator has appointed a safety manager in charge of properly managing safety measures in accordance with the basic policy, standards and procedures specified by the Financial Instruments Business Operator. Whether the safety manager supervises the management of the computer systems, data and networks.

(v) Management of Outsourcing of Business Operations

Whether the Financial Instruments Business Operator properly conducts risk management regarding outsourced business operations related to the computer system.

(vi) Contingency Plan

A. Whether the Financial Instruments Business Operator has formulated a contingency plan and has established arrangements and procedures for dealing with emergencies.

B. Whether the Financial Instruments Business Operator maintains the effectiveness of the contingency plan by constantly reviewing and revising it in light of the actual state of its business operations as well as the system environment and other factors.

(vii) System Integration Risk

A. Whether the Financial Instruments Business Operator has developed a control environment for managing system integration risk by ensuring that its officers and employees fully recognize the risk.

B. Whether the Financial Instruments Business Operator has established arrangements and procedures for conducting tests. Whether its test plan is suited to the nature of the system development necessitated by the system integration.

C. Whether the Financial Instruments Business Operator has established a control environment that enables itself to be proactively involved in the system integration when this task is outsourced.

D. Whether the Financial Instruments Business Operator makes use of third-party evaluation, such as evaluation by a system auditor, when making judgment regarding important matters related to the system integration.

E. Whether the Financial Instruments Business Operator has developed a contingency plan for dealing with an unexpected incident.

(viii) Actions to System Troubles

A. Whether the Financial Instruments Business Operator has implemented appropriate measures to avoid creating unnecessary confusion among customers in the event of system troubles.

B. Whether the Financial Instruments Business Operator, after system troubles have occurred, analyses the cause and implements measures based on the analysis to prevent recurrence.

C. Whether the Financial Instruments Business Operator has established arrangements and procedures for immediately reporting system troubles to the authorities.

(2) Supervisory Method and Actions

(i) At the Time of Problem Recognition

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's control environment for managing information technology risk, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator, by holding in-depth hearings with the business operator and the outsourcing contractor and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement, etc., based on Article 51 and 52(1) of the FIEA.

(ii) At the Time of System Integration

When Financial Instruments Business Operators have announced plans to integrate computer systems as part of planned mergers and other management restructuring moves, they shall be required, as necessary, to submit specific plans for smoothly implementing the system integration, including the schedules and timetables, and documents regarding the internal control environment for managing information technology risk (including internal audits) and other matters, as well as to continue periodically submitting reports based on Article 56-2(1) of the FIEA until the integration is completed.

(3) Actions to System Troubles

(i) Financial instruments business operators shall be required to notify the authorities of the occurrence of any computer system troubles as soon as they have recognized it, and submit a "Report on Problem Occurrence, etc." (in the format specified in Attached List of Formats III-1) to the authorities.

After the computer system operation has been restored to normal and the cause of the problem has been identified, they shall be required to report to the authorities again (It should be kept in mind that they shall be required to report to the authorities on the current state within one month even if the computer system operation has not been restored to normal or the cause of the problem has not been identified within the one-month period.)

It should be noted that when a Local Finance Bureau has received a report from a Financial Instruments Business Operator, it shall immediately notify the FSA division in charge.

(Note) Computer System Trouble Subject to Reporting to the Authorities

Problems that must be reported to the authorities are those which affect systems and equipment (including both hardware and software) used by Financial Instruments Business Operators and contractors undertaking business operations outsourced by Financial Instruments Business Operators, and which could affect the business operators' abilities to identify and keep track of the status of financial instruments transactions, financial settlements, cash deposits and withdrawals, fund-raising and financial conditions, and undermine customer convenience in other ways.

However, the reporting requirement is not applicable to such system troubles in cases where a backup system has started up and effectively prevented adverse effects. (For example, when an order-taking system has broken down in off-market hours but a backup system has quickly started up to take orders in time for the start of market hours, a report is not necessary.)

It should be noted that even if any computer system troubles have not occurred, a report must be made in cases where the probability of the kind of problem described above is deemed to be high, including cases where a Financial Instruments Business Operator has received a warning of a cyber attack on its computer system or where it has detected the possibility of such an attack.

(ii) A Financial Instruments Business Operator who has reported computer system troubles to the authorities shall be required to submit an additional report based on Article 56-2(1) of the FIEA when necessary. When the business operator is deemed to have a serious problem from the viewpoint of protecting public interests and customers, the authorities shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the business operator is deemed to have committed a serious and malicious violation of law, the authorities shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-9 Control Environment for Crisis Management

Given the increased diversity and complexity of risks faced by Financial Instruments Business Operators and changes in the business environment for them in recent years, such as the increasing use of information systems, the possibility cannot be denied that a crisis that cannot be dealt with by ordinary methods of risk management will occur, which means that crisis management has become more important than ever. It is desirable that if risk has materialized at a Financial Instruments Business Operator, the business operator avoids causing unnecessary disruptions to market and social activities by maintaining its functions as much as possible. With this in mind, when supervising a Financial Instruments Business Operator, supervisors shall pay attention to the following points, for example, in light of the business operator's business profile.

(1) Major Supervisory Viewpoints

(i) Preparations to Be Made in Normal Times

A. Whether the Financial Instruments Business Operator recognizes what constitutes an emergency and is striving as much as possible to prevent or guard against any emergency (prepare countermeasures against an emergency that may be unpreventable) by, for example, conducting inspections and anti-crisis practices periodically in normal times.

B. Whether the Financial Instruments Business Operator has formulated a crisis management manual. Whether it has established a control environment that maintains the effectiveness of the crisis management manual by, for example, constantly reviewing and revising it in light of the actual state of its business operations and its risk environment. It should be noted that it is desirable that Financial Instruments Business Operators use objective benchmarks as a basis for the formulation of their crisis management manuals

(Reference) Examples of Conceivable Emergency

- Natural disasters (earthquakes, typhoons, abnormal weather, epidemics of infectious diseases)
- Acts of terrorism and wars (including those that occur outside Japan)
- Accidents (large-scale power failures, computer system breakdowns, etc.)
- Unfounded rumors (word-of mouth rumors, Internet messages, e-mail messages, news articles based on speculation, etc.)
- Crimes committed against Financial Instruments Business Operators (blackmail, intervention by anti-social forces, data theft and abduction of officers or employees)
- Problems involved in business processes (inappropriate response to complaints and inquiries, errors in data entry, etc.)
- Problems related to personnel management affairs (accidents and crimes involving officers and employees, internal disputes, sexual harassment cases, etc.)
- Problems related to labor affairs (cases of whistle-blowing, deaths from excessive workloads, occupational diseases, drain of human resources, etc.)

C. Whether the crisis management manual notes the importance of initial responses, such as accurate identification and objective judgment of the situation and dissemination of information in the period immediately after the occurrence of the emergency.

D. Whether the crisis management manual clarifies the allocation of responsibilities in the event of an emergency and specifies arrangements and procedures for reporting the occurrence of the emergency throughout the institution and to other parties concerned (including the relevant authorities). Whether the crisis management manual specifies arrangements and procedures for reporting the occurrence of an emergency to relevant overseas organizations, including overseas supervisory authorities, depending on the extent of its possible impact abroad as well as its level and type. It is desirable that anti-crisis arrangements and procedures be established under the supervision of the crisis management headquarters that oversees institution-wide response in light of the levels and types of emergencies assumed for each division and branch.

E. Whether the Financial Instruments Business Operator is striving to disseminate and gather information in normal times in a conscientious manner.

(ii) Actions to Emergencies

A. When supervisors have recognized the occurrence of an emergency or the possibility of an emergency occurring, they shall hold hearings periodically and check the situation first-hand so that they can identify and keep track of how the relevant Financial Instruments Business Operator is responding to the emergency, including whether the response (status of the development of a control environment for

crisis management, communications with relevant parties and dissemination of information) is sufficient in light of the level and type of the emergency, until the situation is stabilized. In addition, they shall require the submission of a report based on Article 56-2(1) of the FIEA when necessary.

B. In the above case, supervisors shall make sure to maintain close cooperation with relevant departments and sections, by, for example, immediately reporting to the FSA division in charge.

(iii) Post-Crisis Actions

In cases where supervisors have concluded, after the emergency has been brought under control, that it is necessary to examine the Financial Instruments Business Operator's response to the emergency, they shall require the business operator, under Article 56-2 (1) of the FIEA, to submit a report regarding the outline of the emergency, its response, the analysis of the cause and measures to prevent a recurrence.

(iv) Control Environment for Crisis Management Regarding Reputational Risk

A. Whether the Financial Instruments Business Operator has developed a control environment for managing reputational risk. Whether it has specified how the headquarters, divisions and sales offices should respond to the circulation of unfounded rumors. It is desirable that Financial Instruments Business Operators consider how to respond when unfounded rumors regarding other business operators or their business clients are circulated.

B. Whether the Financial Instruments Business Operator regularly checks whether there are unfounded rumors circulating in each media category (e.g. Internet messages, news articles based on speculation).

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's control environment for crisis management, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-10 Measures to Prevent Violation of Law by Financial Instruments Intermediary Service Providers

(1) Points of Attention Regarding Prevention of Violation of Law by Financial Instruments Intermediary Service Providers

When Financial Instruments Business Operators entrust businesses to financial instruments intermediary service providers, it is important for them to give guidance on the development of a control environment for customer management that enables the intermediary service providers to precisely identify the attributes of customers and the actual state of transactions from the viewpoint of ensuring appropriate investment solicitation

suited to the attributes. It is also important for Financial Instruments Business Operators to identify the actual state of investment solicitation by financial instruments intermediary service providers and urge them to ensure thorough legal compliance. In examining a Financial Instruments Business Operator's control environment for preventing violation of law by financial instruments intermediary service providers, supervisors shall pay attention to the following points in particular:

(i) Precise Identification of Customer Attributes and Thorough Management of Customer Information

A. Whether the Financial Instruments Business Operator shares information regarding the attributes and investment experiences of customers with the entrusted financial instruments intermediary service provider only when it has obtained the customers' consent, and whether it gives the intermediary service provider guidance on how to identify customer attributes as necessary. Whether the Financial Instruments Business Operator has prescribed specific procedures for the intermediary service provider to solicit customers in an appropriate manner suited to the attributes of the customers, has communicated the procedures to the intermediary service provider, and strives to ensure compliance therewith.

B. Whether the Financial Instruments Business Operator has prescribed specific guidelines for the financial intermediary service provider to manage customer information, such as customer attributes, based on careful deliberations made from the viewpoint of the confidentiality obligation, and has communicated the guidelines to the intermediary service provider and strives to ensure compliance therewith.

C. Whether the division in charge of customer due diligence strives to keep track of the Financial Instruments Business Operator's status concerning the identification of customer attributes and the management of customer information, and also establish a control environment that ensures the effectiveness of customer information management by examining, as necessary, whether customer solicitation is conducted in an appropriate manner in light of the attributes of the relevant customers, and by requesting revisions of the method of customer information management, for example.

(ii) Identification of the Actual State of Financial Instruments Intermediary Service Provider's Solicitation for Investment and Efforts to Ensure Appropriate Solicitation

A. Whether the manager of the division in charge of customer due diligence, for example, strives to identify and keep track of the actual state of the entrusted financial instruments intermediary service provider's solicitation for investment by directly holding interviews with customers and taking appropriate measures when necessary.

B. Whether the division in charge of customer due diligence has prescribed a specific method for identifying and keeping track of the actual state of the financial instruments intermediary service provider's solicitation for investment and has communicated the method to them, and is striving to establish a control environment that ensures the effectiveness of the method by identifying and examining the implementation and reviewing and revising the method when necessary.

C. Whether the division in charge of customer due diligence checks whether the entrusted financial instruments intermediary service provider provides appropriate explanations, and requests improvement and takes other measures when necessary.

(iii) Efforts to Foster and Maintain Sense of Compliance at Financial Instruments Intermediary Service Providers

A. Whether the Financial Instruments Business Operator provides case study training, external training and other types of training with a view to enhancing the entrusted financial instruments intermediary service provider's sense of compliance.

B. Whether the division in charge of customer due diligence strives to enhance the effectiveness of training by, for example, identifying and examining the contents of training programs and the implementation thereof and reviewing and revising the contents when necessary.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a Financial Instruments Business Operator's measures to prevent violation of law by an entrusted financial instruments intermediary service provider, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

III-2-11 Prevention of Damage that May be Inflicted by Anti-Social Forces

(1) Significance

Eliminating anti-social forces from society is a task critical to ensuring the order and safety of society, so it is necessary and important for corporations to promote efforts to ban any relations with anti-social forces from the viewpoint of fulfilling their social responsibility. In particular, as Financial Instruments Business Operators have a public nature and play an important economic role, they need to exclude anti-social forces from financial instruments transactions in order to prevent damage from being inflicted not only on their officers and employees but also on their customers and other stakeholders.

Needless to say, if Financial Instruments Business Operators are to retain public confidence and maintain the soundness and appropriateness of their business operations, it is essential that they deal with anti-social forces in accordance with laws and regulations without bowing to pressure from them. Therefore, Financial Instruments Business Operators must strive, on a daily basis, to develop a control environment for banning any relations with anti-social forces in accordance with the purpose of the "Guideline for How Companies Prevent Damage from Anti-Social Forces" (agreed upon at a meeting on June 19, 2007 of cabinet ministers responsible for anti-crime measures).

In particular, anti-social forces have become increasingly sophisticated in their efforts to obtain funds, disguising their dealings as legitimate economic transactions through the use of affiliated companies in order to

develop business relations with ordinary companies. In some cases, the relations thus developed eventually lead to problems. There are also cases in which anti-social forces such as “boryokudan” crime syndicates intervene in the financial instruments market through initial public offering in stock markets for emerging companies and through equity financing deals in markets for listed companies in an attempt to obtain funds. In order to deal with such cases properly, the management teams of Financial Instruments Business Operators need to take a resolute stance and implement specific countermeasures.

It should be noted that if a Financial Instruments Business Operator delays specific actions to resolve a problem involving anti-social forces on the grounds that unexpected situations, such as the safety of employees being threatened, could otherwise arise, the delay could increase the extent of the damage that may be ultimately inflicted on the business operator.

(Reference) “Guideline for How Companies Prevent Damage from Anti-Social Forces” (agreed upon at a meeting on June 19, 2007 of cabinet ministers responsible for anti-crime measures)

(i) Basic principles on Prevention of Damage That May be Inflicted by Anti-Social Forces

- Institutional response
- Cooperation with external expert organizations
- Ban on any relations, including transactions, with anti-social forces
- Legal responses, both civil and criminal, in the event of an emergency
- Prohibition of engagement in secret transactions with and provision of funds to anti-social forces

(ii) Identification of anti-social forces

In judging whether specific groups or individuals constitute “anti-social forces,” which are defined as groups or individuals that pursue economic profits through the use of violence, threats and fraud, it is necessary not only to pay attention to whether they fit the definition in terms of their affiliation, such as whether they constitute or belong to “boryokudan” crime syndicates, “boryokudan” affiliated companies, “sokaiya” racketeer groups, groups engaging in criminal activities under the pretext of conducting social campaigns or political activities and crime groups specialized in intellectual crimes, but also to whether they fit the definition in terms of the nature of their conduct, such as whether they are making unreasonable demands that go beyond the limits of legal liability. (Refer to the “Key Points of Measures against Organized Crime,” a directive issued in the name of the Deputy Commissioner-General of the National Police Agency on October 25, 2004.)

(2) Major Supervisory Viewpoints

In examining a Financial Instruments Business Operator’s control environment for banning any relations with anti-social forces, supervisors shall pay attention to the following points, for example, while also giving consideration to the characteristics of specific transactions.

(i) Whether the Financial Instruments Business Operator has any relations with anti-social forces and whether, with due consideration of the need for the following measures, it makes efforts to ensure that the relations with an anti-social force that it has unwittingly developed can be dissolved as soon as possible after the counterparty has been found to be an anti-social force.

A. Preventing transactions with anti-social forces by, for example, implementing appropriate prior

screening and including in contracts and terms of transactions clauses regarding the exclusion of "boryokudan" crime syndicates.

B. Managing shareholder information properly, through means such as checking the transaction status of own shares and examining information regarding the attributes of shareholders.

C. Avoiding providing funds or engaging in inappropriate or unusual transactions for whatever reason if the counterparty has been found to be an anti-social force.

(ii) Whether the Financial Instruments Business Operator has established a division in charge of supervising responses to unreasonable demands made by anti-social forces (hereinafter referred to as the "anti-social forces response division") so as to develop a centralized control environment for preventing anti-social forces from inflicting damage, and whether this division is properly functioning.

In particular, whether the Financial Instruments Business Operator pays sufficient attention to the following points in developing the centralized control environment.

A. Whether the Financial Instruments Business Operator has established arrangements and procedures for reporting to or consulting with the anti-social forces response division in cases where unreasonable demands are made by anti-social forces. Whether the anti-social forces response division is prepared to ensure the safety of officials who actually deal with anti-social forces and to support the division that deals therewith.

B. Whether the anti-social forces response division has centralized control over the management and accumulation of information regarding anti-social forces, and whether the accumulated information is made available in the form of a database, for example, for use in screening the counterparties of transactions and evaluating the attributes of shareholders of the Financial Instruments Business Operator.

C. Whether the Financial Instruments Business Operator makes sure to maintain the effectiveness of measures to ban any relations with anti-social forces by, for example, having the anti-social forces response division develop a manual for dealing with anti-social forces, provide on-going training, foster cooperative relationships with external expert organizations such as the police, the National Center for the Elimination of Boryokudan and lawyers on an ongoing basis. In particular, whether the Financial Instruments Business Operator is prepared to report to the police immediately when it faces the imminent prospect of being threatened or becoming the target of an act of violence, by maintaining close communications with the police on a daily basis so as to develop a systematic reporting system and build a relationship that facilitates cooperation in the event of a problem.

(iii) Whether the Financial Instruments Business Operator ensures that, when facing unreasonable demands from anti-social forces, the officials or divisions in charge are not left to deal with the situation on their own, but that an institutional response is made with directors and other senior managers properly involved. Whether the response is made with due consideration of the following points:

A. When an unreasonable demand is made by anti-social forces, it must be immediately reported to directors and other senior managers via the anti-social forces response division and a response should be made under the instruction of and with the involvement of the senior managers.

B. It is essential to actively consult external expert organizations such as the police, the National Center

for the Elimination of Boryokudan and lawyers, and respond to the unreasonable demand based on guidelines set by the National Center for the Elimination of Boryokudan and other organizations. In particular, when there is an imminent prospect of a threat being made or an act of violence being committed, it is important to report to the police immediately.

C. It is essential to take every possible civil legal action and to avoid hesitating to seek the initiation of a criminal legal action by proactively reporting damage to the authorities.

(iv) Whether the Financial Instruments Business Operator ensures that the division in charge of handling problematic conduct promptly conducts a fact-finding investigation upon request from the anti-social forces response division, in cases where the unreasonable demand from anti-social forces is based on problematic conduct related to business activity or involving an employee.

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a financial institution's control environment for banning any relations with anti-social forces, through inspection and daily supervisory administration, they shall identify and keep track of the status of voluntary improvement made by the business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the Financial Instruments Business Operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, because its internal control environment is extremely fragile, as shown by, for example, a failure to take appropriate steps toward dissolving relations with anti-social forces despite recognizing the provision of funds thereto and the presence of inappropriate business relations therewith, supervisors shall take actions such as issuing an order for business improvement based on Article 51 of the FIEA. When the Financial Instruments Business Operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider taking strict actions based on Article 52 (1) of the FIEA.

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

(1) Significance

(i) CSR is a concept generally interpreted to include the economic, environmental and social responsibilities a company recognizes in relation to its diverse range of stakeholders, and activities conducted on the basis of those responsibilities. CSR is significant in that the company can enhance its sustainability by fulfilling those responsibilities.

(ii) It should be left to individual Financial Instruments Business Operators to decide, based on the principle of self-responsibility, not only whether to engage in CSR activity but also whether to make information disclosure regarding such activity. Evaluation of a Financial Instruments Business Operator's CSR activity should be made by users and other stakeholders under the principle of market discipline.

(iii) However, if easy-to-understand information disclosure regarding CSR activity is made in a timely and appropriate manner, users are expected to more easily obtain information useful for judging the sustainability of business operators and their financial products and services when deciding which business

operators to make transactions with. From this viewpoint, by clarifying supervisory viewpoints regarding CSR-related information disclosure by Financial Instruments Business Operators as a minimum standard, supervisors shall promote information disclosure that is appropriate and useful for users.

(2) Major Supervisory Viewpoints

Whether the Financial Instruments Business Operator makes information disclosure appropriate from the viewpoints of the following matters in order to enable a diverse range of stakeholders, including users, to properly evaluate its CSR and to contribute to the improvement of the convenience for users.

(i) Suitability with Objective

Whether the Financial Instruments Business Operator's CSR report comprehensively covers the fields of economy, environment and society and whether its contents suit the objective of meeting the needs of a diverse range of stakeholders, including users, by using comprehensive descriptions and reflecting social backgrounds. Whether disclosure is made in a timely and effective manner.

(ii) Reliability

Whether the Financial Instruments Business Operator compiles its CSR report through a transparent process and uses precise and objective data and information, thereby ensuring that the report is highly reliable and widely acceptable.

(iii) Readability

Whether the Financial Instruments Business Operator strives to make its CSR report as easy-to-understand as possible so that a diverse range of stakeholders, including users, can understand it. Whether the Financial Instruments Business Operator pays sufficient attention to the need to enable comparison between recent and past reports by, for example, maintaining consistency.

(3) Supervisory Method and Actions

A Financial Instruments Business Operator's CSR-oriented efforts and information disclosure are voluntary activities made in accordance with management decisions based on the principle of self-responsibility. Therefore, even if the business operator's CSR report fails to take account of the above supervisory viewpoints, supervisors do not need to take supervisory measures.

However, in cases where information disclosure is imprecise or inappropriate, the disclosure practice shall be examined from the viewpoint of the appropriateness of business operations.

III-3 Various Administrative Procedures (General)

III-3-1 Registration

(1) Seal on Application Form for Registration

A signature specified in the instructions for filling-out the form may be used in lieu of a seal if the representative is not accustomed to using a seal.

(2) Trade Name

It shall be confirmed that a trade name given in the application for registration does not infringe Article 25(2) of the Act to Partially Amend the Securities and Exchange Act (hereinafter referred to as the "Amendment Act").

From the viewpoint of preventing misunderstandings by investors, etc., it shall be ensured that the use of the names of securities companies, financial futures transaction companies, investment trust management companies, and investment advisory service companies that existed in the past is avoided as much as possible, except for the case where a business operator, which is allowed to continue the business due to business transfer, etc., uses such a name.

(3) Business Site or Office

The business site or office to be listed in the application for registration shall refer not to representative offices, liaison offices or any other facilities devoted to work other than the financial instruments business, but to a certain facility or utility to be established for the purpose of conducting whole or part of the financial instruments business.

In the case of an unmanned business site or office, the number of stores located within the jurisdiction of each finance bureau and the name of the business site or office that controls such stores shall be entered.

It must be noted that it is necessary to post a sign at unmanned business sites or offices, pursuant to the provision of Article 36-2(1) of the FIEA.

(4) Documents to be Attached to the Application for Registration

(i) The abstract of residence certification to be submitted shall contain the following items:

A. address,

B. name, and

C. date of birth.

(ii) A copy of the foreign registration card or a certificate of foreign registration submitted by a foreign resident living in Japan, and a copy of residence certification of the home country submitted by a foreigner living outside Japan, or any other documents equivalent thereto (a Japanese translation shall be attached to all documents in English, etc.) shall fall under the "documents in lieu thereof" pursuant to the provisions of Article 9(ii)(B) and (iii)(B), and of Article 38(i) of the FIB Cabinet Office Ordinance.

(5) Points to Consider before Granting Registration

(i) Applicants shall be reminded to abstain from conducting any business activities until they are registered in a registry of Financial Instruments Business Operators.

(ii) In the case where an applicant for registration is engaged in another business related to laws and regulations under the supervision of the Financial Services Agency and an administrative reprimand concerning the said business has been issued, the details of such a reprimand shall be confirmed and, when necessary, the progress of improvement measures shall be verified in a hearing session, etc.

In the case where the said disposition is related to legal compliance, attention shall also be paid to III-2-1.

(6) Handling of Registration Numbers

(i) Each registration shall be identified by a serial number (however the following numbers shall not be used, 4, 9, 13, 42, 83, 103, and 893), which is assigned by each local finance bureau, and the registration number to be entered into the registry of Financial Instruments Business Operators shall be subject to the following rules:

e.g., Director General of Finance Bureau …… (Financial instruments business) No. ……

(ii) When a registration is no longer valid, its registration number shall be retired and no new number shall be issued in its place.

(iii) Registration numbers shall be managed by the registration number file of Financial Instruments Business Operators using appended form III-2.

(7) Notification to Applicants for Registration

When registration is made in the registry of Financial Instruments Business Operators, appended form III-3 shall be used to issue notification of registration to the applicant for registration.

(8) Refusal of Registration

(i) When registration is refused, appended form III-4 shall be used to issue notification of refusal of registration to the applicant. The notification shall include the grounds for refusal and state that the applicant is entitled to make a request to the Commissioner of the Financial Services Agency for an examination and file a claim against the government to rescind the decision.

(ii) The Director-General of the Financial Bureau shall enter the corresponding numbers of items set out in Article 29-4(1) of the FIEA as grounds for refusal, or specifically indicate the part of the application for registration or attached documents that lists false information or has important facts missing, in the notification of refusal of registration.

(9) Registry of Financial Instruments Business Operators

(i) The registry of Financial Instruments Business Operators shall be prepared according to the section from page 2 to 12 of the copy of the application for registration.

(ii) When a notification of change in items of application for registration is submitted, the relevant page of the registry for Financial Instruments Business Operators shall be replaced by the revised page of the

application for registration attached to the said notification.

In addition, with respect to the notification of change in the amount of capital due to the issuing of a warrant by a Financial Instruments Business Operator that issues warrants or bonds with warrants, a declaration of the amount of capital at the end of every month shall be submitted by the 15th of the following month and the registry of the relevant Financial Instruments Business Operator shall be revised monthly.

(iii) When Financial Instruments Business Operators under the supervision of the Agency submit notifications of change in the items in the application for registration, the Agency shall compile such notifications every month and send the revised pages of the application forms to the finance bureaus that registered the relevant Financial Instruments Business Operators, by the 20th of the following month.

(iv) The date of inspection of the registry of a Financial Instruments Business Operator shall be a day other than a holiday as specified in Article 1 of the Act on Holidays of Administrative Organs, and the inspection period shall be within the duration designated by the Director-General of the Finance Bureau. However, when it is necessary to organize the registry of financial instruments business operations, etc., the inspection date or time may be changed.

(v) The Inspector of the registry of financial instruments business operations shall use appended form III-5 to enter the necessary items into the inspection book of the registry of Financial Instruments Business Operators.

(vi) The registry of Financial Instruments Business Operators shall not be taken out of the premises designated by the Director-General of the Finance Bureau.

(vii) When any inspector falls under the following category, the inspection may be suspended or refused:

A. Any person who does not follow the items from (iv) to (vi) or the instructions of the bureau.

B. Any person who has defaced or damaged the registry of a Financial Instruments Business Operator, or who may do so.

C. Those who have caused trouble to other inspectors, or who may do so.

(viii) When a request is made for the inspection of a Financial Instruments Business Operator that has been registered by another Director-General of the Finance Bureau, the applicant for inspection shall be informed that such inspection can be supplied by the Finance Bureau that granted the registration, and that explanatory documents are available for public inspection at every business site or office of Financial Instruments Business Operators. However, under unavoidable circumstances, for example, if a business office or office of a Financial Instruments Business Operator is located in a remote area, an inspection shall be carried out by referring the registered items to the Director-General of the relevant Finance Bureau.

III-3-2 Notification

When accepting and processing various notifications prescribed in the FIEA, the following points shall be considered:

(1) Change in the Location of Head Office, etc., to an Area Beyond the Jurisdiction of the Director-General of the Competent Finance Bureau

(i) A Director-General of the Finance Bureau who has received a notification of change in the location of head office, etc., to an area beyond his/her jurisdiction shall send the necessary documents to a Director-General of the Finance Bureau who will process the new registration; such necessary documents include the relevant sections of the notification of change and the registry of Financial Instruments Business Operators prescribed in Article 20(2) of the FIB Cabinet Office Ordinance together with other documents, including the copy of the application for registration, other attached documents, and a report of the most recent inspection.

(ii) A Director-General of the Finance Bureau who has received the above documents shall send a copy of notification of registration to the Director-General of the Finance Bureau who processed the previous registration, after completing the new registration for the Financial Instruments Business Operator concerned.

(iii) A Director-General of the Finance Bureau who processed the previous registration of the said Financial Instruments Business Operator shall delete the previous registration upon receiving a copy of the notification of new registration.

(2) Points for Consideration Concerning Notification of Discontinuation of Business, etc.

(i) When a notification pursuant to Article 50(1)(vii) and Article 50-2(7) of the FIEA and Article 199(v) of the FIB Cabinet Office Ordinance, is received from a Financial Instruments Business Operator, the following points shall be verified by, for example, conducting inspections:

A. There are no grounds for rescission of the registration prescribed in the provision of Article 52(1) of the FIEA.

B. All liabilities to clients are expected to be paid in full.

C. It is confirmed that there are no unlisted liabilities in the form of an outstanding balance of claims/liabilities to clients.

(ii) In the case where a Financial Instruments Business Operator submits a notification prescribed in the provision of Article 199(xi)(g) of the FIB Cabinet Office Ordinance, and when the reason for the termination of entrustment to a financial instruments intermediary services provider is that the said financial instruments intermediary services provider is to discontinue the financial instruments intermediary services, a confirmation shall be made at the time of the submission of the notification that the said Financial Instruments Business Operator has confirmed that there are no grounds for rescission of registration of the said financial instruments intermediary services provider pursuant to the provision of Article 66-20(1) of the FIEA.

III-3-3 Books and Documents Related to Business Activities

The obligation to formulate and retain books and documents related to business activities (hereinafter referred to as “books and documents” [excluding in VI-3-2-4, VI-3-3-4, VII-2-3 and XI-2-3]) is stipulated in laws and regulations in order to contribute to the protection of investors, by means of making books and documents accurately reflect the status of operations and assets of Financial Instruments Business Operators and by examining the appropriateness of business activities and the financial soundness. Based on these principles, the

following points shall be considered when examining books and documents.

(1) Basic Points to Consider

(i) Books and documents may serve as other books and documents within a rational scope, part of the records may be listed in other books, and names other than those prescribed in Article 157 and Article 181 of the FIB Cabinet Office Ordinance, may be used, but only in cases where all the items to be listed are entered in accordance with the type of each business-related document.

(ii) For foreign corporations to which III-3-3 is applicable, the term "head office" shall be replaced with "principal business site or office in Japan" and the term "branch office" shall be replaced with "other business site or office."

(iii) When creating order forms concerning self-transaction, the term "order received" in Article 158 of the FIB Cabinet Office Ordinance, shall be replaced with "order shipped."

(iv) The items directly corresponding to the relevant items among those to be listed in the books and documents shall be replaced with those of the compatible items and those with no applicable items may be omitted.

(v) Among the items to be listed in the books and documents concerning over-the-counter (OTC) derivative transactions, the record of the time may be omitted.

(vi) A copy of the document prescribed in Article 157(1)(i)(A)(4) of the FIB Cabinet Office Ordinance, (a document upon conclusion of the contract prescribed in Article 37-4(1) of the FIEA) shall be prepared by machine concurrently with the said original document, and may be substituted by another book and document which lists all the items to be listed in the said document.

(vii) Individual books and documents may be substituted by the transaction contracts that list all the items to be listed in the respective books and documents, when creating: order forms; transaction records concerning intermediary or agency services; transaction records concerning public offering, secondary distribution or private offering; transaction records concerning the handling of public offering or secondary distribution or the handling of private offering; or transaction records concerning agency or intermediary services for concluding investment advisory contracts or discretionary investment contracts. The said transaction contracts shall be prepared separately.

(viii) Items to be listed in the books and documents may be entered using codes, brevity codes or any other symbols that have been standardized by the said Financial Instruments Business Operator.

(ix) In the cases where part of the items to be listed in books and documents is linked using the transaction contract that lists the appropriate items and the contract number, and they are managed and stored together, this package may be regarded as the relevant books and documents.

(2) Formulation and Storage of Books and Documents on Microfilm

(i) In the cases where books and documents are three or more years-old, and an inspection has been conducted on such books and documents by inspection departments during this period, such documents may be stored on microfilm that is prepared according to the generally accepted standards for formulation.

(ii) Original books and documents may be created and stored on microfilm in the following cases:

A. When the books and documents in question correspond to the items listed in Article 157(1) items (i)(A)(4), (ix), (xi), (xvi) (limited to (B) and (C)), and (xvii) (excluding (A)) of the FIB Cabinet Office Ordinance;
B. When it is possible to prepare written books and documents within a reasonable period of time at each business site for the inspection, etc., by inspection departments; and
C. When personnel in charge of microfilm formulation and storage have been appointed and management procedures have been developed.

(3) Centralized Storage of Books and Documents at the Head Office

(i) In the cases where books and documents are three or more years-old, and an inspection has been conducted on such books and documents by inspection departments during this period, such books and documents may be stored in the head office (including the administrative center, etc., the same shall apply to (ii) below) in an integrated manner.

(ii) Books and documents may be stored in an integrated manner, from the time of their creation, at the companies which are entrusted by a head office or a Financial Instruments Business Operator to create the books and documents, under the condition that the following requirements are met:

A. A system has been established to allow quick response to referrals from clients;
B. A system has been established to enable books and documents to be accessed at a head office within a reasonable period of time; and
C. It does not impede internal audits.

(4) Creation of Forms for Receiving Orders by Direct Entry into a Computer

In the cases where a form for receiving orders is completed by directly entering data into a computer, the following points shall be considered:

(i) Details of orders received shall be entered into a computer when the orders are received (in the case of self-transaction, when orders are shipped).

(ii) The system enables prompt response to referrals from clients.

(iii) Backups of input data are made and stored.

(iv) The system automatically records input time.

(v) The system can track deleted/corrected records, if deletion/correction of input history is made.

(vi) Handwritten forms for receiving orders shall be prepared, as was done previously, in the cases where the order form cannot be made by directly inputting data into a computer at the same time as receiving orders. Examples of such cases are when the details of orders are communicated to executing offices by telephone, where orders for the following day are received after the computer system is shut down for the day, or where computers are not usable due to a disaster, etc. However, a postscript may be omitted if a handwritten form for orders received, which has been created at the same time as orders were received, is stored together with the form for receiving orders that has been prepared by a computer that shows whether all order information agrees if the details of the orders received are input later.

(vii) The system can respond to internal audits.

(5) Formulation of Form for Shipping Orders by Direct Entry into a Computer

In the cases where a form for shipping orders is created by directly entering data into a computer, the following points shall be considered:

(i) Details of shipping orders shall be entered into a computer when orders are shipped.

(ii) Handwritten forms for shipping orders shall be prepared in the cases where order forms cannot be formulated by direct entry of data into a computer at the same time as orders are shipped, such as when computers cannot be used due to a disaster, etc. However, a postscript may be omitted if a handwritten form for shipping orders, which has been created at the same time as orders were shipped are stored together with a form for shipping orders that has been prepared by a computer that shows whether all information agrees if the details of the orders shipped are input later.

(iii) In addition to (i) and (ii) above, the cases corresponding to items (4) (iii) to (v) and (vii) above.

(6) Storage of Books and Documents Using Electronic Media

The following points shall be considered when using electronic media to store books and documents.

(i) Handwritten books and documents shall be saved as image data.

(ii) The electronic media for storage shall have sufficient durability to last for the storage period prescribed in Article 157(2) and Article 181(2) of the FIB Cabinet Office Ordinance.

(iii) One of the electronic media used for data storage shall be designated as “original” and shall be clearly labeled to that effect (judgment on the condition of storage of books and documents shall be made in conformity with this “original”).

(iv) A backup of the “original” mentioned above (iii) shall be created and stored as a “copy.”

(v) The system enables prompt response to client referrals.

(vi) The system allows hard copies of books stored as data to be created within a reasonable period of time

(vii) The system can track deleted/corrected records, if deletion/correction of input history is made;

(viii) The system can accommodate internal audits;

(ix) Personnel in charge of formulation and storage have been appointed and in-house regulations on the said formulation and storage have been developed.

(x) When a handwritten postscript or supplement to a hard copy of a book or document created electronically is made, a copy of the said hard copy shall be made and saved as image data. If it is not stored as image data, the said hard copy shall be stored as the original.

III-3-4 Matters Related to the Special Measure Law for Reviving Industrial Vitality

Matters related to the plans specified in the Special Measure Law for Reviving Industrial Vitality (hereinafter referred to as “Law for Industrial Vitality”) concerning business reconstruction, reorganization of joint projects, reuse of management resources, and introduction of business innovation facilities shall be listed in compliance with the preparation method of financial statements, etc., of Financial Instruments Business Operators, with due consideration to the following points.

(1) Regarding the definition of business innovation in Article 2(2)(ii) of the Law for Industrial Vitality and Article 6, Article 8, and Article 9 of the Guidelines for Enforcement on the Special Measure Law for Reviving Industrial Vitality (hereinafter referred to as "Guidelines for the Law for Industrial Vitality"):

(i) In Article 6 of the Guidelines for the Law for Industrial Vitality, "the case where the total amount of sales from the relevant new services exceeds 1% of the sales from all business activities" shall refer to the case where the total amount of operating revenues from the new services exceeds 1% of the operating revenues from all business activities.

(ii) In Article 8 of the Guidelines for the Law for Industrial Vitality, "the case where selling expenses per unit of the relevant service is reduced by more than 5%" refers to the case, for example, where selling and administrative expenses per unit of operating revenues or operating income is reduced by more than 5%.

(iii) In Article 9 of the Guidelines for the Law for Industrial Vitality, "the case where the percentage growth rate of the amount of sales from the relevant services during business reconstruction exceeds the percentage growth rate of the amount of sales from the business segments related to the said services recorded in the previous three fiscal years by more than 5 percentage points" refers to the case, for example, where the percentage growth rate of operating revenues from the relevant services during business reconstruction exceeds the growth rate of operating revenues from the business segments related to the said services recorded in the previous three business years by more than 5 percentage points.

(2) Regarding the criteria for the authorization of business reconstruction in Article 3(6)(i) of the Law for Industrial Vitality and I(b) of the Basic Guidelines for Industrial Revitalization (hereinafter referred to as the "Basic Guidelines"):

(i) In the Basic Guidelines II(B)(1)(i), "Return on Equity (ROE) after the completion of business reconstruction－ROE before the commencement of business reconstruction≧2" refers, for example, to the case where ROE increases by more than 2 percentage points

(ii) In the Basic Guidelines II(B)(1)(ii), "(Tangible fixed assets turnover after the completion of business reconstruction/Tangible fixed assets turnover before the commencement of business reconstruction) × 100≧105" refers, for example, to the case where the value obtained by dividing operating revenues by the book values of tangible fixed assets increases by more than five percentage points.

(iii) In the Basic Guidelines II(B)(1)(iii), "(Value added per employee after the completion of business reconstruction/Value added per employee before the commencement of business reconstruction × 100≧106" refers, for example, to the case where value added per employee (sum of operating profits, personnel expenses, and depreciation) increases by more than six percentage points.

(3) Definition of objectives concerning improvement in the soundness of finance prescribed in Article 2-2(2)(ii) of the Law for Industrial Vitality and the Basic Guidelines I(C)(2)(iii).

(i) In the Basic Guidelines I(C)(2)(iii)(a), "the total amount of interest-bearing debts" refers, for example, to all the financing instruments with liability characteristics.

(ii) In the Basic Guidelines I(C)(2)(iii)(b), "current revenue" refers, for example, to the total amount of operating revenues and non-operating revenues, while "current expenditure" refers, for example, to the total

amount of operating expenditures and non-operating expenditures.

(4) Regarding the definitions of items related to the standards of business sectors in structural oversupply prescribed in Article 2-2(2)(iii) of the Guidelines for the Law for Industrial Vitality and the Basic Guidelines III(B), in the Basic Guidelines III(B)(3), “amount of sales” refers, for example, to operating revenues.

(5) Regarding the criteria for authorization of reorganization of joint projects prescribed in Article 2-2(2)(iii) and of the Law for Industrial Vitality and the Basic Guidelines III(C), the Basic Guidelines III-3-4(2)(ii) shall apply mutatis mutandis to the Basic Guidelines III(C)(2)(i).

(6) Regarding the criteria for authorization of reuse of management resources prescribed in Article 2-2(2)(iv) of the Law for Industrial Vitality and the Basic Guidelines IV(B), the Basic Guidelines III-3-4(2)(ii) and (iii) shall apply mutatis mutandis to the Basic Guidelines IV(B)(2) and (3), respectively.

IV. Supervisory Evaluation Points and Various Administrative Procedures (Type I Financial Instruments Business)

IV-1 Governance (Type I Financial Instruments Business)

Supervisors shall pay attention to the following points when examining the governance of Financial Instruments Business Operators (limited to Type I Financial Instruments Business Operators; the same shall apply in IV).

It should be noted that in cases where the provisions of III-1 Governance (general) are applied to foreign corporations engaging in Type I financial instruments business, the "representative director" shall be replaced with the "representative in Japan" and "the Board of Directors, etc." with "the highest decision-making organization of a sales branch or business office in Japan."

IV-1-1 Officers of Financial Instruments Business Operators

(1) Major Supervisory Viewpoints

Whether the Financial Instruments Business Operator appropriately takes into consideration the following eligibility requirements in the decision-making process regarding proposals for the appointment of its directors, executive officers and auditors (including the representatives in Japan in the case of foreign corporations; hereinafter referred to as "officers").

(i) A person who does not meet any of the ineligibility criteria (Article 29-4(1)(ii)(a) to (g) of the FIEA) and who did not meet any of them at the time of registration.

(ii) A person who has not violated laws and regulations regarding financial instruments business or related business operations (excluding Article 46-6(2) of the FIEA), or a person who has not been subjected to administrative actions taken based on laws and regulations.

(iii) A person who has not damaged the interests of investors in relation to the conduct of the investment advisory and agency business and the investment management business.

(iv) A person who has not engaged in an illegal or markedly inappropriate act regarding financial instruments business under particularly grave circumstances.

(v) A person who has not violated the conditions attached to authorization under Article 30(1) of the FIEA.

(2) Supervisory Method and Actions

In cases where an officer of a Financial Instruments Business Operator is deemed to meet the ineligibility criteria specified under any of Article 29-4(1)(ii)(a) to (g) of the FIEA, or is found to have done so at the time when the business operator obtained registration under Article 29 of the FIEA, or where an officer of a Financial Instruments Business Operator is deemed to meet the ineligibility criteria specified under any of Article 52 (1)(vi) and (viii) to (x) of the FIEA, supervisors shall consider taking actions such as ordering the dismissal of the said officer based on Article 52(2) of the FIEA.

In addition, they shall hold an in-depth hearing regarding the decision-making process concerning the proposal for the appointment of the said officer and, when necessary, require the submission of a report based on Article

56-2(1) of the FIEA. Furthermore, supervisors shall consider taking actions such as issuing an order for business improvement, if the Financial Instruments Business Operator's control environment for governance is deemed to have a serious problem and the action is deemed to be necessary and appropriate, from the viewpoint of protecting public interests and investors.

IV-1-2 Adequate Staffing for Properly Conducting Financial Instruments Business

(1) Major Supervisory Viewpoints

Supervisors shall examine whether Financial Instruments Business Operators are adequately staffed to properly conduct financial instruments business (limited to Type I financial instruments business; the same shall apply to IV), in light of the following requirements regarding Financial Instruments Business Operators' officers and employees.

(i) Financial instruments business operators should secure officers and employees who understand the viewpoints regarding governance that are specified under the FIEA and other relevant regulations, as well as the supervisory guidelines, and who have the knowledge and experiences necessary for conducting governance, as well as sufficient knowledge and experiences concerning compliance and risk management to ensure the sound and appropriate execution of financial instruments business.

(ii) Officers and employees should not be current or former members of organized crime groups (as specified under Article 2(vi) of the Act on Prevention of Unjust Acts by Organized Crime Group Members; the same shall apply hereinafter).

(iii) Officers and employees should not have close relationships with organized crime groups (as specified under Article 2 (ii) of the Act on Prevention of Unjust Acts by Organized Crime Group Members; the same shall apply hereinafter).

(iv) Officers and employees should not have the experience of being sentenced to a fine for violation of the FIEA or other domestic financial laws and regulations or foreign laws and regulations equivalent thereto.

(v) Officers and employees should not have the experience of being sentenced to imprisonment with work or more severe punishment (including similar punishments imposed under foreign laws or regulations equivalent thereto) (Particular attention should be paid to the case of an officer or employee being accused of committing crimes specified under Articles 246 to 250 of the Penal Code (fraud, fraud using computers, breach of trust, quasi fraud and extortion as well as attempts at these crimes).

(2) Supervisory Method and Actions

The requirements specified in (i) to (v) above are part of a comprehensive set of elements that should be taken into consideration when supervisors examine whether a Financial Instruments Business Operator is adequately staffed to properly conduct financial instruments business. Even if an officer or an employee is deemed to not meet the requirements, it should not automatically lead to the conclusion that the Financial Instruments Business Operator is not adequately staffed. The important thing is, first and foremost, that Financial Instruments Business Operators strive to ensure on their own responsibility that they are adequately staffed, in light of those requirements and other elements.

However, supervisors shall hold in-depth hearings regarding the decision-making process concerning the proposed appointments of officers and employees, in cases where a Financial Instruments Business Operator is deemed to have failed to take those elements into consideration sufficiently in the said decision-making process, and where it is deemed to be necessary and appropriate to hold such hearings. In addition, they shall require the submission of reports based on Article 56-2(1) of the FIEA when necessary.

Supervisors shall consider taking actions such as issuing an order for business improvement under Article 51 of the FIEA, in cases where the Financial Instruments Business Operator's control environment for governance is deemed to have a serious problem as a result of the examination of the submitted report, and where the action is deemed to be necessary and appropriate from the viewpoint of protecting public interests and investors.

Furthermore, when the Financial Instruments Business Operator is deemed to not be adequately staffed to properly conduct financial instruments business, as a result of the examination of the submitted report, supervisors shall consider taking necessary measures, including issuing an order for business suspension based on Article 52(1) of the FIEA.

IV-2 Soundness of Financial Condition (Type I Financial Instruments Business)

With due consideration of the susceptibility of the business of Financial Instruments Business Operators to changes in the market environment, regulation on the capital adequacy ratio aims to ensure the soundness of their financial conditions and the protection of investors, even if the business operators face a decline in their income due to rapid changes in the market conditions or a decline in the value of their asset holdings. Through efforts to maintain an adequate level of capital adequacy ratio, Financial Instruments Business Operators must identify and manage risks involved in their businesses in a comprehensive manner and keep liquid assets (non-fixed capital) in sufficient quantity and quality, to enable them to withstand losses that may be caused by the materialization of various risks. For their part, supervisors need to encourage Financial Instruments Business Operators to make voluntary efforts to maintain the soundness of their financial conditions through their offsite monitoring, which should complement the efforts the business operators make on their own responsibility to maintain an appropriate level of capital adequacy ratio.

IV-2-1 Preciseness of Capital Adequacy Ratio

Supervisors shall examine the preciseness of a Financial Instruments Business Operator's capital adequacy ratio by paying attention to the following points, with due consideration of Article 46-6(1) of the FIEA and the FIB Cabinet Office Ordinance.

(1) Eligibility of Subordinated Debts and Subordinated Bonds

(i) Regarding the notification of the borrowing of a subordinated loan or the issuance of a subordinated bond, whether the terms of the contract give preference to senior creditors in accordance with Article 50(1) of the FIEA (Article 199 (xii) of the FIB Cabinet Office Ordinance.) by including a legal provision stipulating that when a condition for subordination, such as bankruptcy or court-administered corporate rehabilitation, arises, subordinate creditors' claims are voided temporarily and their claims become effective only after all payments to senior creditors have been made.

(ii) Whether the subordinated loan/bond has all of the characteristics described in the individual items of Article 176(2) and (3) of the FIB Cabinet Office Ordinance.

(iii) Whether the contract for the subordinated loan/bond stipulates that contractual revisions disadvantageous to senior creditors and payments made in violation of the special provision for subordination are deemed to be ineffective.

(iv) In the following cases, whether the Financial Instruments Business Operator acknowledges the intentional provision of funds to the subordinated loan lender/the subordinated bond holder as specified under Article 176(4)(iii) of the FIB Cabinet Office Ordinance and accordingly deducts the amount of the said funds from the subordinated loan/bond amount.

A. The Financial Instruments Business Operator has provided a subordinated loan to the subordinated loan lender/the subordinated bond issuer, or holds a subordinate bond issued thereby (excluding cases where the Financial Instruments Business Operator acquired the subordinated bond as its underwriter and the holding period does not exceed six months, and cases where the business operator holds the subordinated bond temporarily for market-making and other similar purposes).

B. The Financial Instruments Business Operator has provided funds to the subordinated loan lender/ subordinated bond issuer for the purpose of supporting business rehabilitation or recapitalization.

C. The Financial Instruments Business Operator has underwritten new stocks and other securities issued by the subordinated loan lender/subordinated bond issuer for the purpose of supporting business rehabilitation or recapitalization (excluding the case where the Financial Instruments Business Operator has purchased the said stocks and securities in the secondary market and holds them purely for the investment purpose or for purposes other than supporting business rehabilitation or recapitalization, with the holding period not exceeding six months, and the case where it holds the stocks and securities temporarily for market-making and other similar purposes).

(2) Collateral Deducted from Deductible Assets

In cases where a Financial Instruments Business Operator has deducted the appraisal value of land and buildings based on Article 177(2) and (3) of the FIB Cabinet Office Ordinance or where it has deducted the appraisal value of funds and assets pledged as collateral based on Article 177(5) of the same act and Article 2(2) of the Capital Regulation Notice, supervisors shall examine whether the deducted value is appropriate by paying attention to the following points:

(i) In cases where the appraisal value of land and buildings is deducted, whether the appraisal value has been calculated in an appropriate manner.

(ii) In cases where the appraisal value of collateral and other assets is deducted, whether the funds and other assets pledged as collateral are eligible as collateral, and whether the appraisal value and the value of the market risk equivalent that should be deducted therefrom have been calculated in an appropriate manner.

(3) Identification of Value of Market Risk Equivalent

Based on Article 178(2) of the FIB Cabinet Office Ordinance supervisors shall check, with due consideration of the following points, whether a Financial Instruments Business Operator identifies and keeps track of the values of the market risk equivalent and the counterparty risk equivalent on a daily basis with a rational method suited to the characteristics of their business.

(i) Whether the Financial Instruments Business Operator properly identifies the market risk equivalent based on the appraisal values of all securities that it holds (the appraisal values verified for objectivity at the end of each month). It should be noted that except for at the end of each month, a rough estimate is permissible with regard to items of little relevance, such as those regarding which the Financial Instruments Business Operator's position is usually small relative to the amount of its non-fixed capital.

(ii) Whether the Financial Instruments Business Operator properly identifies the value of the counterparty risk equivalent based on the total value of the credit equivalent, including all relevant transactions and assets. It should be noted that except for at the end of each month, accounts receivable and accrued income that concerns financial income and those which are booked on the execution dates on a provisional basis (excluding those regarding which the payment was not made on the delivery date) may be excluded.

(iii) Whether the director in charge of risk management keeps track of the values of the market risk equivalent and the counterparty risk equivalent on a daily basis.

In the case of a Financial Instruments Business Operator who accepts margin deposits from customers in amounts corresponding to a certain proportion of the contracted principal amount, and conducts foreign exchange transactions through net settlements (so-called foreign exchange margin transactions) in particular, whether it has developed a risk management and internal control environment that enables the precise and appropriate identification of the impact that rapid movements in the foreign exchange market could have on the soundness of its financial condition and its capital.

(4) Checkpoints Regarding Loaned Securities

Regarding securities lent to other entities, whether the Financial Instruments Business Operator has calculated the value not only of the counterpart risk equivalent but also of the market risk equivalent.

IV-2-2 Supervisory Response to Cases of Financial Instruments Business Operators' Capital Adequacy Ratio Falling Below Prescribed Level

As the "early corrective action" based on the capital adequacy requirement is prescribed under Article 46-6(1) of the FIEA as a means to ensure the soundness of Financial Instruments Business Operators' management, such business operators need to make continuous efforts to improve their management so that they can maintain and enhance the soundness of the management.

Therefore, when a Financial Instruments Business Operator's capital adequacy ratio falls below a legally prescribed level, supervisors shall take the following measures in order to urge the business operator to make improvement quickly.

(1) When supervisors have received a notification based on Article 179(3) of the FIB Cabinet Office Ordinance from a Financial Instruments Business Operator, they shall check the contents of the Plan Regarding Specific Voluntary Measures to Be Taken in Order to Maintain the Capital Adequacy Ratio attached to the notification. In addition, they shall check the future outlook on the business operator's capital adequacy ratio through hearings and urge it to make voluntary improvement efforts.

It should be noted that in cases where the capital adequacy ratio stays below 140% for a long period of time or where the ratio repeatedly falls below 140%, supervisors shall strive to identify and keep track of the Financial Instruments Business Operator's capital adequacy ratio by, for example, requiring the submission of a report based on Article 56-2(1) of the FIEA.

In addition, over the period until a notification based on Article 179(5) of the FIB Cabinet Office Ordinance is submitted, they shall strive to identify and keep track of the Financial Instruments Business Operator's capital adequacy ratio and the status of its management of various risks by, for example, checking a notification regarding the capital adequacy ratio on a daily basis and holding hearings.

(2) When the above notification shows that the Financial Instruments Business Operator's capital adequacy ratio is below 120%, supervisors shall check the contents of the Plan Regarding Specific Voluntary Measures to Be Taken in Order to Improve the Capital Adequacy Ratio" attached to the notification and, when necessary, identify the specific method with which to bring the capital adequacy ratio back above the prescribed level and the

estimated date of the recovery, as well as the status of segregated management of customer assets and fund-raising by, for example, requiring the submission of a report based on Article 56-2(1) of the FIEA.

(3) Regarding the above capital adequacy shortfall, supervisors shall issue an order for the implementation of the following measures, for example, based on Article 53(1) of the FIEA when it is deemed to be necessary and appropriate to do so from the viewpoint of protecting public interests and investors, in light of the Financial Instruments Business Operator's conditions that have been identified through the submitted report and hearings.

(i) To draft and implement measures (including the drafting of specifics and the implementation schedule) to bring the capital adequacy ratio back above the legally prescribed level and maintain the ratio above that level on a permanent basis.

(ii) To implement measures to ensure the protection of investors in preparation for an unexpected event, through appropriate management of securities and cash and careful management of fund-raising.

(iii) To avoid activities that could lead to wasteful use of corporate assets.

(iv) To compile the projections of the balance sheet and fund-raising status on a daily basis and the projection of capital adequacy ratio in ways to reflect the specific measures to be implemented, in order to bring the capital adequacy ratio back above the legally prescribed level.

IV-2-3 Control Environment for Managing Market Risks

Market risks include the risk of a Financial Instruments Business Operator incurring losses due to fluctuations in prices of its asset holdings (including positions related to off-balance transactions) caused by changes in various market-related risk factors, such as prices of securities and other financial instruments, interest rates and exchange rates, as well as credit and other risks associated therewith. It is important for Financial Instruments Business Operators to properly manage market risks.

(1) Major Supervisory Viewpoints

Whether the Financial Instruments Business Operator properly manages market risks by developing a comprehensive control environment for risk management, properly recognizing and evaluating the risks, properly setting and managing position limits and establishing a system of checks and balances based on the clear allocation of roles and responsibilities.

(2) Supervisory Method and Actions

Supervisors shall strive to identify and keep track of the status of a Financial Instruments Business Operator's market risk and its risk management through monthly offsite monitoring reports and hearings based thereon and, when necessary, require it to submit a report based on Article 56-2(1) of the FIEA and urge it to make improvement efforts.

(3) Specific Procedures

(i) Risk Management Regarding Proprietary Trading

When identifying and managing market risks regarding proprietary trading, a Financial Instruments

Business Operator must pay attention to the following points, in addition to identifying the value of the market risk equivalent on a daily basis, based on Article 178(2) of the FIB Cabinet Office Ordinance.

A. Appropriate Risk Management Regarding Proprietary Stock Trading

a. A Financial Instruments Business Operator should set the maximum allowable value of market risks that may be allotted to proprietary stock trading or reasonable limits and risks equivalent thereto (hereinafter referred to as the "allowable market risk value, etc."), based on an appropriate capital adequacy ratio target set with due consideration of its own financial condition and other factors.

b. A Financial Instruments Business Operator should monitor on a daily basis whether its proprietary stock trading operations are conducted properly within the allowable market risk value, etc.

c. From the viewpoint of maintaining the capital adequacy ratio above the target level, a Financial Instruments Business Operator should take necessary measures regarding the allowable market risk value, etc., such as reviewing and revising it in a timely manner, in light of changes in its own financial condition, including profits/losses from proprietary stock trading.

B. Appropriate Management of Proprietary Trade Operations during Daytime

a. A Financial Instruments Business Operator should develop a control environment for managing proprietary stock trading operations so as to keep them within the allowable market risk value, etc.

b. Instead of using the management method described in A. above, a Financial Instruments Business Operator may manage proprietary stock trading operations so as to keep them within the allowable market risk value, etc., during the daytime with similar methods using the position amount, as described below:

i) To make sure that the value obtained by multiplying the total amount of positions at specific points during the daytime with the internally prescribed volatility margin for loss cutting does not exceed the allowable market risk value, etc.

ii) To make sure that the value obtained by multiplying the value of positions accumulated by specific points during the daytime with the internally prescribed volatility margin for loss cutting does not exceed the allowable market risk value, etc.

iii) To allocate position limits set in light of the allowable market risk value, etc., as specified in A. above by trader and unit, and check the status of compliance with the allocated position limits as necessary.

C. A Financial Instruments Business Operator should develop a control environment that ensures the implementation of appropriate measures when it has recognized a situation that could have a significant impact on the soundness of its financial condition.

(ii) Checkpoints regarding Rational Reason for Selecting Calculation Method of Market Risks

In cases where a Financial Instruments Business Operator selects the standard approach or the internal control model-based approach by either risk category or business type for the calculation of the value of the market risk equivalent based on Article 4(4) of the Capital Adequacy Notice, supervisors shall examine

whether there is a rational reason for the selection, by paying attention to the following points:

A. When the calculation method of market risks is selected by risk category

   a. Whether the Financial Instruments Business Operator can better identify market risks by selecting different calculation methods for different risk categories.

   b. Whether the division in charge of comprehensively identifying the overall market risks is independent from other divisions.

B. When the calculation method of market risks is selected by business type

   a. Whether the Financial Instruments Business Operator can better identify market risks by selecting different calculation methods for different business types.

   b. Whether the Financial Instruments Business Operator has developed a control environment that ensures that the division in charge of comprehensively identifying the overall market risks identifies the value of the market equivalent by risk category.

(iii) Representative Stock Price Indexes of Designated Countries

In cases where a Financial Instruments Business Operator calculates the stock risk equivalent based on the standard approach, and has selected stock price indexes other than those listed below as the representative stock price indexes of the designated countries, supervisors shall examine whether the selected indexes are suited to be treated as the representative stock price indexes of the relevant countries, in light of the transaction status and other factors.

A. Japan: Nikkei Stock Average, Nikkei 300 Stock Index, TOPIX Index
B. United States: S&P500
C. Italy: MIB 30
D. Australia: ASX200
E. Netherlands: AEX
F. Canada: S&P Toronto Composite Index
G. United Kingdom: FTSE100
H. Switzerland: SMI
I. Sweden: OMX
J. Spain IBEX35
K. Germany: DAX
L. France: CAC40
M. Belgium: BEL20
N. Hong Kong: Hang Seng

(iv) International Organizations

In cases where a Financial Instruments Business Operator calculates the value of the interest rate risk equivalent based on the standard approach, the following shall be deemed to fall under the category of international organizations:

International Bank for Reconstruction and Development

International Finance Corp.

Asian Development Bank

Inter-American Development Bank
African Development Bank
European Investment Bank
Nordic Investment Bank
European Bank for Reconstruction and Development
Caribbean Development Bank
Social Development Fund of the Council of Europe

(v) Checkpoints Regarding External Audits of Internal Control Model

Regarding a Financial Instruments Business Operator using an internal control model-based approach, supervisors shall annually check the results of external audits of the risk measurement process and the risk measurement model used in the previous year.

(vi) Pre-Auction Trading of Government Bonds

It should be kept in mind that in cases where a Financial Instruments Business Operator engages in pre-auction trading of government bonds, the calculation of the capital adequacy ratio prior to the announcement of the coupon rate and other items should be made according to the following procedures:

A. In calculating the value of the risk equivalent, the Financial Instruments Business Operator should use a coupon rate calculated in a reasonable manner in light of the prevailing rate in the secondary market at the time of the calculation, or use the coupon rate on the most recent government bond with the same maturity and the same issuance format with the relevant government bond (in the case of a government bond whose coupon rate is determined through the formula "standard interest rate – α of the previous bond," "the most recent standard interest rate – α") as a provisional coupon rate, and the same calculation method should continue to be used.

B. After the auction of the relevant government bond has been conducted and the issue name, coupon rate and other details have been announced, the Financial Instruments Business Operator should recalculate the value of the risk equivalent based on the actual coupon rate without any delay, and use it for the calculation of the capital adequacy ratio on and after the announcement date of the said coupon rate.

IV-2-4 Control Environment for Managing Counterparty Risk

Counterparty risk is the risk of a Financial Instruments Business Operator incurring losses due to a failure by the counterparties to its transactions to fulfill their contractual obligations. It is important for Financial Instruments Business Operators to properly manage counterparty risk.

(1) Major Supervisory Viewpoints

Whether the Financial Instruments Business Operator properly manages counterparty risk by developing a comprehensive control environment for risk management, properly recognizing and evaluating the risks, conducting internal screening when a new product or a new business is introduced and establishing a system of checks and balances based on the clear allocation of roles and responsibilities.

(2) Supervisory Method and Actions

Supervisors shall strive to identify and keep track of the status of a Financial Instruments Business Operator's counterparty risk and its risk management, through monthly offsite monitoring reports and hearings based thereon and, when necessary, require it to submit a report based on Article 56-2(1) of the FIEA and urge it to make improvement efforts.

(3) Specific Procedures

(i) Checkpoints Regarding Collateral Deducted from Value of Credit Equivalent

In cases where a Financial Instruments Business Operator has deducted the appraisal value of funds and other assets pledged as collateral based on Article 17(5) and (6) of the Capital Adequacy Notice, supervisors shall examine whether the deducted value is appropriate by paying attention to the following points:

A. Whether the relevant funds and other assets pledged as collateral are eligible as collateral.

B. Whether the appraisal value of the relevant funds and other assets and the value of the market risk equivalent that should be deducted therefrom have been calculated in an appropriate manner.

(ii) Checkpoints Regarding Legally Valid Bilateral Netting Contract

In cases where a Financial Instruments Business Operator calculates the value of the credit equivalent regarding a transaction made under a legally valid bilateral netting contract based on the netted value and uses it for the calculation of the value of the counterparty risk equivalent, supervisors shall check the following points:

A. Whether the Financial Instruments Business Operator has obtained a confirmation, in writing when necessary, of a legal opinion that indicates that if the counterparty to the transaction goes bankrupt or a dispute with the counterparty arises, the rational judgment of the court of jurisdiction or the authorities concerned will be that the business operator's provision of credit should be limited to the netted value under the relevant netting contract in light of the relevant laws.

B. Regarding the relevant laws, whether the Financial Instruments Business Operator has checked, at the minimum, the following ones:

a. The laws of the country that has granted an establishment license or authorization to the counterparty to the transaction and the laws of the countries where the counterparty's overseas sales branches and business offices are located.

b. The laws related to the specific transactions covered by the netting arrangement and the legal basis for the netting

c. The laws related to the contracts necessary for the netting and the legal basis for the netting

(iii) Checkpoints Regarding Commitment to Guarantee

Supervisors shall check whether the Financial Instruments Business Operator recognizes a contract assuring a future conclusion of a loan guarantee contract as a commitment to guarantee, regardless of in what form or name the contract is made, and includes it in the calculation of the value of the counterparty risk. A document made in the name of a "management guidance promise note" (which is submitted by a parent company to a financial institution that provides a loan to its subsidiary in order to acknowledge its responsibility for supervising the subsidiary and providing management guidance) shall be deemed to fall

under the category of commitments to guarantee, if its contents are deemed to have a legal force similar to that of a loan guarantee or a commitment to guarantee, and if it needs to be noted in the balance sheet under Article 58 of the Rules on the Terminology, Formats and Compilation Method of Financial Statements (hereinafter referred to as the "Rules on Financial Statements, etc.").

(iv) Checkpoints Regarding Corporations Deemed to Be Insolvent

A corporation deemed to be insolvent as a result of inspection by an inspection department or through an external audit shall be deemed to fall under the category of the "corporations deemed to be insolvent from an objective standpoint" as specified under Article 17(3)(iii) Table (Note 3)(4) of the Capital Adequacy Notice.

(v) Checkpoints Regarding Consolidated Financial Statement-Submitting Companies

Supervisors shall keep in mind that consolidated subsidiaries for which a consolidated-financial statement-submitting company, as specified under Article 17(3)(iii)(refer to Note 1), is allowed to calculate the value of the counterparty risk equivalent based on a designated rating assigned to itself, are companies which are covered by the said company's consolidated financial results and which are subject to appropriate external audits regarding the relevant consolidated financial results, and supervisors shall check on this point as necessary, based on audit reports. In addition, supervisors shall monitor, as necessary, a consolidated-financial-statement-submitting company's calculation of the values of the credit equivalent and the counterparty risk equivalent related to its transactions with affiliated companies in order to make sure, in reference to contracts, audit reports and other documents and materials, that the calculation is appropriate.

(vi) International Organizations

In cases where a Financial Instruments Business Operator calculates the value of the counterparty risk equivalent based on the standard approach, the following shall be deemed to fall under the category of international organizations:

International Bank for Reconstruction and Development
International Finance Corp.
Asian Development Bank
Inter-American Development Bank
African Development Bank
European Investment Bank
Nordic Investment Bank
European Bank for Reconstruction and Development
Caribbean Development Bank
Social Development Fund of the Council of Europe

IV-2-5 Control Environment for Managing Liquidity Risk

Liquidity risk refers to the risk that because of deterioration in business performance or other factors, a Financial Instruments Business Operator will face a credit crunch as it fails to raise necessary funds, or incurs losses as it is forced to obtain funds at markedly higher interest rates than under normal circumstances (funding risk). It also refers to the risk that a financial institution will incur losses because it is unable to conduct market

transactions or is forced to conduct transactions at far more unfavorable prices than under normal circumstances, because of market turmoil and other emergency market developments (market-liquidity risk). It is important for Financial Instruments Business Operators to properly manage liquidity risks.

(1) Major Supervisory Viewpoints

Whether the Financial Instruments Business Operator properly manages liquidity risk by developing a comprehensive control environment for risk management, properly recognizing and evaluating the risks and establishing a system of checks and balances based on the clear allocation of roles and responsibilities.

(2) Supervisory Method and Actions

Supervisors shall strive to identify and keep track of the status of a Financial Instruments Business Operator's liquidity risk and its risk management through monthly offsite monitoring reports and hearings based thereon and, when necessary, require it to submit a report based on Article 56-2(1) of the FIEA and urge it to make improvement efforts.

IV-2-6 Treatment of Financial Instruments Business Groups with International Operations

Supervision of financial instruments business groups with international operations shall be conducted with due consideration of the viewpoints specified in the Guideline for Financial Conglomerates Supervision. However, instead of the provision of II-2-1(2) ② "Calculation Method" of the said guideline, the "criteria for bank holding companies to judge whether their capital adequacy status is appropriate in light of their own and their subsidiaries' asset holdings, etc." (hereinafter referred to as the "Bank Holding Companies Notice") may be applied mutatis mutandis to the calculation of the combined equity capital and the requisite equity capital (hereinafter referred to as the "combined equity capital, etc.") under Article 52-25 of the Banking Act. (The provisos of this notice shall become applicable after the end of March 2008.)

Capital adequacy as specified by II-2-1 of the said guideline shall be examined with the following points in mind.

A financial instruments business group with international operations is an entity which fits the descriptions of (i) and (ii) or (iii) below.

(i) The financial instruments business group (refer to Note) includes a company which fits the description of (a) (hereinafter referred to as the "Business Management Company") or (b) below and which has an overseas base (not including a representative office) engaging in securities-related business outside Japan.

(ii) The financial instruments business group's financial instruments business affiliate (limited to a company engaging in Type I financial instruments business (limited to securities-related businesses)) that fits the description of (a) or (b) below has capital of more than 200 billion yen after deduction of fixed assets.

(iii) The financial instruments business group is required by the supervisory authorities of the countries where it has business operations to be monitored in Japan for the soundness of its financial condition as a group (on a consolidated basis).

(Note) A financial instruments business group is a group comprised of companies which fit the descriptions of (a) and (b). (If there are companies which fit the descriptions of (c) or (d), they may also be constituents

of the group [excluding cases where the Business Management Company is a bank or a bank holding company].)

(a) A corporation which is a Financial Instruments Business Operator headquartered in Japan or whose subsidiaries (subsidiaries as specified under Article 8(3) of the Rules on Financial Statements, etc.; the same shall apply hereinafter) include a Financial Instruments Business Operator.

(b) A subsidiary of a corporation which fits the description of (a) (Business Management Company).

(c) An affiliate (affiliate as specified under Article 8(5) of the Rules on Financial Statements, etc.) of a corporation which fits the description of (a) (Business Management Company).

(d) A corporation which fits the description of any of (a) to (c) and a company whose internal control-related processes (all or part of processes related to legal compliance, loss-risk management, internal audits and inspections, financial affairs, accounting affairs, tax affairs and the maintenance and management of computer systems) are managed by the same officers and employees with those of a Financial Instruments Business Operator which fits the description of (a) or (b).

(1) In cases where a financial instruments business group calculates the combined equity capital, etc., based on II-2-1(2) ② of the Guideline for Financial Conglomerates Supervision, and where a Financial Instruments Business Operator within the group has obtained approval for the use of the internal control model-based approach based on Article 12 of the Capital Adequacy Notice, the value of the market risk equivalent as part of the group's requisite capital may be calculated with this approach.

(2) In cases where a financial instruments business group calculates the combined equity capital, etc., by applying the Bank Holding Companies Notice mutatis mutandis, the following procedures shall be followed:

(i) Standard I (a standard for the consolidated capital adequacy ratios of banks with overseas sales operations, bank holding companies which have long-term credit banks as subsidiaries, and the subsidiaries) as specified under Article 2 of the Bank Holding Companies Notice shall be applied.

(ii) "Specified transactions as prescribed under Article 13-6-3(2) of the regulation and similar transactions" as specified under Article 4 of the Bank Holding Companies Notice shall be replaced with "transactions related to the trading operations."

(iii) "Other financial institutions" as specified under Articles 6, 8 and 20 of the Bank Holding Companies Notice shall include Financial Instruments Business Operators.

(iv) "Clearing organizations, etc." as specified under Article 10(3) of the Bank Holding Companies Notice shall include securities finance companies, commodities exchanges and clearing organizations for commodities transactions.

(v) The value of the market risk equivalent calculated based on the provisions of Section 3 of the Capital Adequacy Notice may be deemed to be the value of the market risk equivalent. In this case, if the financial instruments business group has obtained approval for the use of the internal control model-based approach under the same notice, this approach may be used to calculate the value of the market risk equivalent.

(vi) In cases where a financial instruments business group uses an internally estimated volatility adjustment rate as specified under Article 73 of the Bank Holding Companies Notice, an exposure volatility estimation

model as specified under Article 83 of the notice, an internal ratings method as specified under Article 118 of the notice, an internal model-based approach regarding exposure to stocks, etc. as specified under Article 217 of the notice, a scenario method as specified under Article 275 of the notice, the standardized approach as specified under Article 283 of the notice or the advanced measurement approach as specified under Article 289 of the notice, the group shall undergo screening based on criteria equivalent to those specified by the notice and be recognized as meeting the criteria, instead of undergoing screening based on the criteria specified by the notice.

(Note) A preliminary calculation of credit risk based on the internal ratings approach shall start when the Bank Holding Companies Notice takes effect, while the application of the internal ratings approach shall start after the end of March 2009.

(3) Supervisors shall strive to identify and keep track of the soundness of a financial instruments business group's financial condition by requiring its business management company and its subsidiaries and affiliates engaging in financial instruments business to submit reports regarding the following items, for example, based on Article 56-2(1) of the FIEA.

In cases where a financial instruments business group is deemed to need to make improvement regarding the soundness of its financial conditions, supervisors shall strive to identify and keep track of the situation by holding in-depth hearings based on the submitted report and urge it to make improvement efforts. In addition, they shall take actions based on Article 51 and other provisions of the FIEA, including issuing an order for business improvement, if the action is deemed to be necessary to ensure improvement.

(i) Companies that constitute the financial instruments business group (If the constituent groups are financial institutions, it should be clarified which supervisory agencies have jurisdiction over them. Any change must be reported immediately.).

(ii) The financial instrument business group's risk management policy (Any change must be reported immediately.).

(iii) The financial instruments business group's capital amount, requisite capital amount and the capital adequacy ratio (The report must be made on a semiannual basis.).

(iv) The financial instruments business group's consolidated financial statements (The report must be made on a quarterly basis.).

(v) The status of the financial instruments business group's major intra-group transactions (The report must be made on a monthly basis.).

(vi) A fall below 120% of the financial instruments business group's capital adequacy ratio (refer to Note). (The report must be made immediately after the ratio falls below 120 %.)

(Note) If the financial instruments business group calculates the consolidated capital-to-asset ratio by applying the Bank Holding Companies Notice mutatis mutandis, it shall immediately report if the ratio falls below 8%.

(4) When applying the provisions of (3) above to a financial instruments business group that calculates the combined equity capital, etc., by applying the Bank Holding Companies Notice mutatis mutandis, supervisors

shall check whether the group identifies the overall quantity of various risks involved in individual business divisions, including risks not reflected in the consolidated capital to asset ratio, such as interest rate risk related to assets and liabilities not included in the calculation of the value of the market risk equivalent and credit risk related to large-lot borrowers, by establishing a comprehensive control environment for group-wide risk management. Supervisors should also check whether the financial instruments business group maintains a sufficient level of capital, in terms of both quality and quantity, in light of the overall risks identified.

IV-2-7 Early Warning System

As a means to maintain the soundness of the management of Financial Instruments Business Operators, the scheme for "prompt corrective actions" has been established under Article 46-6(1) of the FIEA. As well as Financial Instruments Business Operators to which the scheme is applicable, those to which it is not applicable need to make continuous efforts to improve their management so as to maintain and enhance the soundness of the management.

Therefore, in cases where a Financial Instruments Business Operator meets the prescribed criteria regarding changes in the capital adequacy ratio and in prices of securities listed below, supervisors shall strive to quickly identify risks by, for example, holding a hearing and requiring the submission of a report based on the early warning system.

(Note) Although supervisors shall take supervisory actions, including holding hearings, against Financial Instruments Business Operators which meet the said criteria under the early warning system, the management of such business operators should not automatically be deemed to be unsound, or supervisors shall not necessarily urge them to make management improvement efforts.

Also, from the viewpoint of reducing the cost to be imposed on Financial Instruments Business Operators and increasing the efficiency of supervisory processes, the early warning system shall be flexibly operated in a manner suited to the size and the risk profiles of individual business operators.

(1) Change in Capital Adequacy Ratio

Supervisors shall identify the margin and rate of change in Financial Instruments Business Operators' capital adequacy ratios each month, based on offsite monitoring data, and analyze the risks that have materialized.

(2) Change in Prices of Securities

Supervisors shall identify the amount of Financial Instruments Business Operators' securities holdings, based on offsite monitoring data, and analyze market risks through stress testing that assumes a prescribed level of price change.

(3) Impact of Change in Foreign Exchange Rates

Supervisors shall identify the impact of changes in foreign exchange rates on Financial Instruments Business Operators engaging in over-the-counter financial futures transactions, based on offsite monitoring data, and analyze the risk of the business operators' capital being eroded by changes in foreign exchange rates, in light of their method of segregated management, their leverage ratio and the characteristics of their transactions.

(4) Supervisory Method and Actions

In cases where a Financial Instruments Business Operator is deemed to meet the prescribed criteria regarding (1) to (3) above, based on the analysis of the relevant data, supervisors shall strive to quickly identify risks by, for example, holding a hearing with it and requiring it to submit a report under the early warning system.

In addition, supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA, when the action is deemed to be necessary in order to ensure the implementation of improvement measures.

IV-3 Appropriateness of Business Operations (Type I Financial Instruments Business)

IV-3-1 Appropriateness of Business Operations Related to Securities Businesses

IV-3-1-1 Control Environment for Legal Compliance

Securities companies, etc. ("Securities companies, etc." refers to business operators engaging in Type I financial business (limited to securities-related businesses); the same shall apply hereinafter), act as market intermediaries which enable individual investors, institutional investors and securities-issuing companies to make transactions smoothly in the financial instruments market. As their business operations have a highly public nature, securities companies, etc., must exercise their market intermediary function in an efficient and stable manner by executing business operations in a highly reliable way while properly protecting investors. To this end, they must also manage their business operations in a sound and appropriate manner in their capacity as market players, while maintaining a high level of self-discipline.

Their control environment for legal compliance shall basically be examined based on the supervisory viewpoints and method specified in III-2-1. However, it shall also be examined in relation to a broad range of matters, including the status of compliance with voluntary rules adopted from the viewpoint of ensuring an appropriate exercise of the market intermediary function.

IV-3-1-2 Control Environment for Customer Solicitation and Explanations

(1) Points of Attention Regarding Explanation Documents

"The Key Points of the Status of Internal Control" in the Explanation Documents as specified under Article 46-4 of the FIEA (Article 174(iv) of the FIB Cabinet Office Ordinance) shall describe specific arrangements and procedures for handling complaints and inquiries from customers and for conducting internal audits.

(2) Points of Attention Regarding Notification of Necessary Information Related to Delivery of Securities and Other Matters

In cases where a securities company, etc., has failed to properly notify customers of the following items (including cases where the securities company, etc., has failed to notify customers of (iv) below through the method agreed to by the relevant customers), the situation shall be deemed to fall under the category of "situations in which information necessary for customers with regard to the status of delivery and other items regarding the customers' securities transactions is deemed not to have been properly provided," as specified under Article 123(viii) of the FIB Cabinet Office Ordinance.

(i) Items that must be specified in writing when a contract is signed under Article 37-4(1) of the FIEA must be notified to the customer.

(ii) In cases where a customer has made a pre-auction government bond transaction, the issue name and price of the government bond, the transaction amount and items notified in the transaction report at the time of the execution of the relevant transaction (excluding the scheduled redemption date and the contracted yield) must be notified to the customer after the auction of the relevant government bond.

(iii) In cases where a customer has made a pre-auction government bond transaction and where the condition precedent regarding the transaction has not been met, the fact of the condition being unmet and items regarding the execution or non-execution of the relevant transaction (excluding cases where the customer has agreed to these items not being notified) must be notified to the customer.

(iv) In addition to the items described in (i) to (iii) above, items related to the delivery of cash and securities (excluding cases where the transaction does not involve the direct delivery of cash and securities between the customer and the Financial Instruments Business Operator, such as when the delivery of cash is made through a financial institution and when the delivery of securities is made through a transfer settlement.) must be notified to the customer.

(3) Points of Attention Regarding Explanation of Important Items Related to Investment Trust Switching

In cases where a securities company, etc., has failed to provide explanations regarding the following items related to investment trust switching and where it has failed to establish an internal control system for compiling and storing records on their explanations and monitoring explanations, the situation shall be deemed to fall under the category of "situations in which explanations regarding important items related to switching have not been provided to customers in the solicitation for switching of investment trust beneficiary certificates, etc.," as specified under Article 123(ix) of the FIB Cabinet Office Ordinance."

(i) Form and Status (e.g. name, characteristics) of investment trusts and investment corporations (hereinafter referred to as "investment trusts, etc.")

(ii) Status (e.g. rough estimate of profit or loss) of investment trusts, etc., to be cancelled

(iii) Expenses necessary for switching (e.g., cancellation and acquisition fees)

(iv) Items regarding preferential treatment for redemption switching

(v) Other items that could affect customers' investment decisions in light of the characteristics of the relevant investment trust, etc., and the needs of the customers

(4) Points of Attention Regarding Secondary Offering of Bonds

(i) Cases in which a securities company, etc., has failed to provide explanations regarding the following situations when soliciting individual customers (excluding specified investors) to acquire bonds (securities as specified under Article 123(xi) of the FIB Cabinet Office Ordinance.) or selling bonds to them in a secondary offering, under Article 2(8)(viii) or (ix) (excluding the provision regarding private placement of securities) shall be deemed to fall under the category of "cases in which explanations regarding important incidents that have occurred during the application period for the acquisition or purchase of the relevant securities and could affect investment decisions have not been individual customers (excluding specified investors)," as specified under Article 123(xi) of the FIB Cabinet Office Ordinance.

A. When the yield on the relevant bond has become markedly disadvantageous to the customer compared with the yield on a similar bond already issued by the same issuer, the situation must be explained.

B. When the redemption terms of the relevant bond are determined by the market condition and other benchmarks (hereinafter referred to as "benchmarks, etc."), and the condition of benchmarks, etc., regarding the bond at the time when the securities company, etc., is soliciting customers to buy the

bond or selling the bond to them is disadvantageous to the customer compared with the condition of the benchmarks, etc., that were used as a reference when the issuance terms or sales terms were determined, the situation must be explained.

(ii) Regarding (i) A. above, the following points shall be taken into consideration:

A. The "relevant bond" is a bond that falls under the category of corporate bonds, etc., intended for individuals ("corporate bonds, etc.," as specified under "Publication of Information Related to Over-the-Counter Quotations Regarding Bonds Intended for Individuals," which is a resolution adopted by the Japan Securities Dealers Association's Board of Governors; the same shall apply hereinafter).

B. The "similar bond" is a corporate bond intended for individuals which matures in less than six months after the maturity date of the relevant bond (newly issued bond) and whose maturity date is the closest to that of the relevant bond (when there are two or more such bonds, the one that was issued most recently).

C. Whether or not a certain situation should be deemed as a "situation markedly disadvantageous to the customer" shall be judged with due consideration of the interest rate level at the time of the offer (secondary offer) and other circumstances. For example, the value α obtained through the following formula may be used as a basis for the judgment.

α = X (credit spread equivalent of a similar bond) – Y (credit spread equivalent of the relevant bond (newly issued bond))

X = (average (refer to Note) of reported values, as specified under the "System for Publication of Over-the-Counter Quotations Regarding Corporate Bonds, etc., Intended for Individuals" (values published on the day before the offer date) regarding the similar bond) – (average simple yield (the value published on the same day as the offer date), calculated on the basis of reference bond trading statistics published by the Japan Securities Dealers Association, of the government bond whose maturity date is closest to that of the similar bond)

Y = (subscribers' yield (average simple yield) of the relevant bond (newly issued bond)) – (average simple yield (the value published one day after the terms-setting date), calculated on the basis of reference bond trading statistics published by the Japan Securities Dealers Association, of the government bond whose maturity date is closest to that of the relevant bond (newly issued bond))

(Note) The "average of reported values as specified under the 'System for Publication of Over-the-Counter Quotations Regarding Corporate Bonds, etc. Intended for Individuals' regarding the similar bond" shall be a simple average of values (simple yields) that are reported by reporting members to and published by the Japan Securities Dealers Association under this system.

(iii) Regarding (i) B. above, the following points shall be taken into consideration:

A. A "situation disadvantageous to the customer" refers to a case in which the theoretical price of the relevant bond at the time of the solicitation (or the theoretical price based on the closing price of the relevant bond on the previous day) has fallen below the bottom of the range set in advance by the

securities companies, etc., in relation to the offer price (secondary offer price).

B. The theoretical price in A. above shall be calculated through the calculation formula which was used as a basis for determining the issuance (secondary offer) terms of the bond, and the price range shall be determined in light of the levels prescribed under internal rules regarding sales after the offer and secondary offer periods. In addition, records on the calculation formula for the theoretical price shall be organized and recorded, and appropriate arrangements and procedures, including the establishment of internal rules, regarding the handling of such records shall be established.

C. Regarding bonds whose redemption terms depend on the stock market condition, such as bonds exchangeable with stocks of other companies and Nikkei Average-linked bonds with a special redemption provision (hereinafter referred to "EBs, etc."), the definition of a "situation disadvantageous to the customer" may be changed from A. above to "a case in which the price of the relevant stock at the time when the securities companies, etc., solicit customers to acquire or sell EBs, etc., in a secondary offer to them (or the closing price of the stock on the previous day) has fallen more than 7% below the initial price (the price of the relevant stock used as a basis for determining the issuance terms or the price regarded by individual companies as equivalent thereto).(Limited to cases where the use of this definition was decided before the offer (secondary offer) period.)

D. Regardless of which of the above definitions in (A) and (C) is used during the offer/ secondary offer periods, cases in which, after the offer/secondary offer periods, appropriate prices calculated based on internal rules are not offered in the sale of EBs, etc., may be deemed to constitute a violation of Article 117(1)(ii) of the FIB Cabinet Office Ordinance.

(iv) In cases where securities companies, etc., are to conduct solicitation for acquisition under brokerage contracts, they shall provide explanations specified under Article 123(xi) of the FIB Cabinet Office Ordinance.

(5) Points of Attention Regarding Sale of Securitization Products (Assurance of Traceability of Securitization Products)

Some securitization products have a complex structure and involve several parties in the origination to sales processes. Therefore, if the originator of the underlying assets fails to properly provide information regarding the contents of the underlying assets and the risks involved therein to the parties involved in the processes, such as the originator of securitization products, the seller and investors, it may become difficult for investors to identify risks precisely.

As transactions involving securitization products are basically made between professional investors (e.g., securities companies, etc., and qualified institutional investors), they are unlikely to be subject to the legal regulation on disclosure and the legal obligation for explanations. However, regarding the sale of securitization products, supervisors shall pay attention to the following with due consideration of the viewpoint described above.

Even if securities companies, etc., play only a limited role in transactions, such as acting as a sales agent, it is desirable that they provide support where possible, as long as they deal with investors.

(i) Whether before selling securitization products, the securities company, etc., collects information regarding the contents of the underlying assets and the risks involved therein and conducts sufficient

analysis to provide appropriate explanations.

(ii) Whether the securities companies, etc., has established the internal procedures and rules necessary to avoid relying exclusively on credit ratings, and provides information regarding the risks involved in the underlying assets and liquidity risks not reflected in credit ratings when they sell securitization products.

(iii) Whether the securities company, etc., has established the internal procedures and rules necessary for providing information, in ways that enable customers investing in securitization products to trace information regarding the contents of the underlying assets and the risks involved therein, if requested to do so by the investors.

(iv) Whether the securities company, etc., has developed a control environment for evaluating and calculating theoretical prices and quickly informs customers of them, even when it is difficult to determine market prices. Whether the securities company, etc., avoids evaluating and calculating theoretical prices in an arbitrary manner so as to refrain from giving priority to promoting arbitrary use of the information for specific purposes.

(6) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the control environment for customer solicitation and explanations of a securities company, etc., through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the securities company, etc., by requiring the submission of reports based on Article 56-2(1) of the FIEA. When the securities company, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the securities company, etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

IV-3-1-3 Discretionary Trading Contracts

(1) Points of Attention Regarding Discretionary Trading Contracts with Foreign Securities Companies

When supervisors have received a notification regarding the signing of a contract based on Article 16(1)(viii)(b) of the Cabinet Office Ordinance Regarding the Definitions Specified under Article 2 of the FIEA (hereinafter referred to as the "Cabinet Office Ordinance Regarding Definitions"), they shall pay attention to the following points:

(i) Whether the division that executes transactions regarding the said agreement is clearly separated from the divisions that receive and execute orders for other brokerage transactions.

(ii) Whether it is ensured that account books are compiled in ways to enable the identification of transactions related to the said agreement.

(2) Scope of Specified Agreements by Securities Companies, etc.

Specified agreements as prescribed under Article 123(xiii)(b) and (c) of the FIB Cabinet Office Ordinance

include the following agreements:

(i) Agreements regarding prices higher (in the case of sell orders) or lower (in the case of buy orders) than the specified prices (including prices determined with a prescribed method)

(ii) An appropriate range determined with a specified price as a base point

(iii) Agreements regarding the determination of prices at the discretion of securities companies, etc., on the condition that they follow the best execution practice (so-called CD order) in daily trading.

(iv) Targeting of prices determined through a prescribed method such as volume weighted averaging (so-called VWAP target order)

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the transactions specified under Article 123(xiii)(a) to (e) of the FIB Cabinet Office Ordinance through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the securities company, etc., by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the securities company, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the securities company, etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider taking necessary actions, including issuing an order for business suspension based on Article 52(1) of the FIEA.

IV-3-1-4 Measures to Prevent Misrecognition

(1) Points of Attention Regarding Measures to Prevent Securities Companies, etc., from Being Misrecognized as Other Financial Institutions

When examining misrecognition prevention measures to be taken in cases where the headquarters or sales branches of a securities company, etc., conducts business operations in the same building with another financial institution, supervisors shall pay attention to the following points from the viewpoint of preventing customers from misrecognizing the said securities company, etc., as the said financial institution.

(i) Whether the securities company, etc., and the financial institution provide each service over separate counters, and the name of the securities company, etc., is properly displayed, among other appropriate misrecognition prevention measures.

(ii) Whether the securities company, etc., provides sufficient explanations regarding the following matters to customers:

A. The securities company, etc., and the financial institution sharing the building are different corporations.

B. Products and services provided by the securities company, etc., are different from those provided by the said financial institution.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding misrecognition prevention measures taken by a securities company, etc., through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the securities company, etc., by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the securities company, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the securities company, etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including issuing an order for business suspension based on Article 52 (1) of the FIEA.

IV-3-1-5 Business Continuity Management (BCM)

(1) Significance and Response

As securities companies, etc., play an important role as intermediaries in the financial instruments market, it is extremely important for the people's lives and the economy that they act in an appropriate manner in the event of an emergency, by, for example, taking recovery measures quickly and ensuring that the minimum necessary operations and services are maintained. Therefore, securities companies, etc., need to make appropriate preparations in normal times, such as establishing business continuity management (BCM) systems and creating crisis management manuals. From this viewpoint, supervisors shall examine the appropriateness of the BCMs of securities companies, etc., in light of the characteristics of their business, by paying attention to the following points, for example.

(2) Major Supervisory Viewpoints

Whether the business continuity plan (BCP) ensures quick recovery from damage caused by acts of terrorism, large-scale disasters, etc., as well as continuance of the minimum necessary business operations and services for the maintenance of the functions of the financial system. Whether arrangements and procedures are in place for ensuring response coordinated with Financial Instruments Firms' Associations, other securities companies, etc., and relevant organizations based on the results of deliberations conducted at the Securities Market BCP Forum and other forums. Whether the BCP enables the securities company, etc, to deal with international disruptions of business operations in a manner suited to the actual state of its own business operations.

For example, attention shall be paid to:

(i) Whether measures to secure the safety of customer data in the event of disasters, etc., have been taken (storing information printed on paper in electronic media, creating back-ups of electronic data files and programs, etc.).

(ii) Whether measures to secure the safety of computer system centers, etc., have been taken (allocating suitable back-up centers, securing staff and communication lines, etc.).

(iii) Whether the above back-up measures have been taken in ways to avoid geographic concentration.

(iv) Whether a specific target period has been set for the recovery of operations vital for the maintenance of

the lives of customers, economic activities and the functions of the financial instruments markets (e.g., cash withdrawals by customers, cancellation of MRFs and MMFs, sell orders for stocks in custody, orders for the settlement of margin transactions and futures and options transactions and the settlement of executed transactions for which delivery has not been made) through provisional measures such as manual operations and processing by back-up centers.

(v) Whether the securities company, etc., obtains the approval of the board of directors when it adopts the BCM and makes important revisions. Whether the BCM is subjected to examination by independent entities, such as internal and external audits.

(Reference)

"Development of BCM at Financial Institutions" (BOJ, July 2003)

"Basic Principles on Business Continuity" (Joint Forum, August 2006)

In addition, examination of the BCM and BCP shall basically be conducted in reference to III-2-9.

IV-3-1-6 Measures Regarding Financial Services Support in Event of Disasters

(1) Financial Services Support Measures for Disaster-Stricken Areas

The FSA disaster prevention/mitigation plan based on Article 36(1) of the Disaster Countermeasures Basic Act and the FSA plan for the protection of the people based on Article 33(1) and Article 182(2) of the Act on the Protection of the People in Event of Armed Attacks (hereinafter referred to as the "People Protection Act") provides for measures regarding financial services support in the event of disasters and other emergencies. In light of this, when a disaster (including a disaster as specified under Article 2(i) of the Disaster Countermeasures Basic Act, an armed attack specified under Article 2(4) of the People Protection Act and an emergency as specified under Article 183 of the People Protection Act) has occurred or may occur, supervisors shall, while maintaining close contact with relevant organizations, ensure that securities companies, etc., quickly implement the following measures in an appropriate manner within limits deemed necessary, in light of the extent of damage and other circumstances of the affected areas and the demand for funds in such areas.

(i) To provide as much convenience as possible for customers who have lost registered seals.

(ii) To support the re-issuance of lost securities.

(iii) To provide as much convenience as possible for disaster victims who have requested the immediate payment against the sale and cancellation of securities in custody.

(iv) In cases where a securities company, etc., has suspended over-the-counter services, to ensure that all customers know at which branches the said operations have been suspended through means such as notices indicated at branches, newspaper advertisement and notices posted on the Internet.

(v) To take due care in dealing with customers regarding other matters.

(2) Various Financial Services Support Measures in Areas Designated for Enhanced Earthquake Disaster Prevention/Mitigation Measures Related to Tokai Earthquake

When areas for enhanced earthquake disaster prevention/mitigation measures have been designated under the Large-Scale Earthquake Countermeasures Special Act, designated administrative organizations are required to

take preemptive measures to mitigate the damage from earthquakes and prevent secondary disasters.

However, it is difficult to manage administrative processes related to financial instruments business on an area-by-area basis, given the advanced automation and the expansion of networks of unmanned services operations, therefore, regarding the possible Tokai Earthquake, supervisors shall ensure that securities companies, etc., take the following measures in an appropriate manner in light of the fund demand in the affected areas, while maintaining close contact with relevant organizations.

(i) Response to Earthquake Alert by Securities Companies, etc., with Sales Branches and Business Offices in Areas Designated for Enhanced Earthquake Disaster Prevention/Mitigation Measures Regarding Tokai Earthquake

A. In cases where the alert is issued during business hours, supervisors shall request the securities companies, etc., to suspend over-the-counter services.

B. Supervisors shall request the securities companies, etc., to ensure that all customers know at which branches services have been suspended, through means such as notices indicated at branches, newspaper advertisements and notices posted on the Internet.

C. In cases where the alert is issued on a holiday or before or after the business hours of sales branches, supervisors shall request the securities companies, etc., to refrain from resuming over-the-counter services so as to enable the smooth implementation of anti-disaster measures, in case the earthquake actually occurs.

D. Others

a. In cases where the alert is removed, supervisors shall request securities companies, etc., to resume normal operations and services as soon as possible.

b. Supervisors shall request the securities companies, etc., to take appropriate emergency measures based on IV-3-1-6 if the earthquake actually occurs.

(ii) Response to Earthquake Alert by Securities Companies, etc., with Sales Branches and Business Offices in Areas Not Designated for Enhanced Earthquake Disaster Prevention/Mitigation Measures

Even if securities companies, etc., have suspended business operations and services at sales branches and business offices in areas designated for enhanced earthquake disaster prevention/mitigation measures, supervisors shall request them to conduct business and provide services as usual at sales branches and offices in other areas.

(3) Administrative Report

In cases where the above measures have been taken, supervisors shall immediately report them to the Director-General of the Supervisory Bureau.

IV-3-2 Appropriate Exercise of Market Intermediary Function of Securities Companies, etc.

The central role of securities companies, etc., in the financial instruments market is to exercise their market intermediary function, which has a highly public nature. In addition, securities companies, etc., participate in the financial instruments market as market players.

While institutional reforms implemented since the financial “Big Bang” have brought about benefits, a series

of incidents involving problematic conduct occurred, including placement of large-scale erroneous orders in the financial instruments market, system troubles at securities companies, etc., insider trading cases, illegal transactions by investors, such as those aimed at market manipulation, and inappropriate practices by issuer companies, such as including false representations in financial statements. In light of this situation, a study group on securities companies' market intermediary function was established under the FSA's Supervisory Bureau in March 2006, and this group adopted and announced a summary of issues in June of the same year.

The summary included recommendations regarding four issues, namely (1) improvement in the reliability of the operations of securities companies as market intermediaries, (2) securities companies' exercise of the function of acting as a check against issuers, (3) securities companies' exercise of the function of acting as a check against investors and (4) maintenance of the self-discipline of securities companies as market players. Basically, these recommendations should be used as a basis for voluntary rules formulated by self-regulatory organizations, such as the Japan Securities Dealers Association. However, it is also important from the viewpoint of improving the reliability of the financial instruments market through an appropriate exercise of the market intermediary function of securities companies, etc., that the supervisory authorities take necessary actions based on the following viewpoints and with the following supervisory methods, while giving consideration to voluntary rules.

IV-3-2-1 Improvement of Reliability of Operations of Securities Companies, etc., as Market Intermediaries

(1) Points of Attention Regarding Order Management

(i) Whether the securities company, etc., has developed appropriate internal rules based on "Regarding Development of Order Management Systems at Members," which is a resolution adopted by the Japan Securities Dealers Association's Board of Governors, and strives to ensure that all officers and employees are aware of and comply with them,

(ii) Whether the securities company, etc., has implemented sufficient measures regarding computer systems to prevent the placement of erroneous orders, such as incorporating the settings of order limits regarding trading orders, including both hard limits and soft limits, into its systems.

(iii) Whether the securities company, etc., has enhanced the order management system and maintained its functions, for example through periodic inspections, and through an appropriate allocation of personnel, including the appointment of a chief information officer (CIO), who is in charge of supervising the trading system.

(iv) Whether the securities company, etc., has arrangements and procedures for ensuring an appropriate involvement of the relevant manager in the limitation of orders and the removal of alerts against inappropriate orders. In particular, whether appropriate handling of the said matters is ensured in the wholesale division.

(v) Whether the securities company, etc., has developed an emergency response policy for dealing with large-scale erroneous orders and strives to ensure that all officers and employees are aware of and comply with them.

(vi) Whether the securities company, etc., has developed a control environment that ensures the implementation of appropriate measures to prevent failure to meet the settlement deadlines in the event of an

erroneous order.

(2) Points of Attention Regarding Assessment Rates for Substitute Securities Used in Margin Trading

Whether the securities company, etc., in accordance with "Regarding Treatment of Changes in Assessment Rates for Cash Margin Deposit Substitute Securities Related to Margin Trading," a resolution adopted by the Japan Securities Dealers Association's Board of Governors, implements appropriate measures such as the provision of prior explanations regarding incidents which may lead to changes in the assessment rates, so as to ensure that all customers are aware of the changes, the notification of changes, the setting of the notification periods and the establishment of relevant internal rules.

(3) Points of Attention Regarding Computer System Management by Securities Companies, etc.

Cases where the facts that fit the following descriptions are recognized with regard to computer system management by securities companies, etc., shall be deemed to fall under the category of "situations in which computer system management is not adequate" as specified under Article 123 (xiv) of the FIB Cabinet Office Ordinance.

(i) Cases in which the securities company, etc., does not periodically conduct appropriate checks on its computer systems, such as system audits by computer system experts.

(ii) Cases in which the securities company, etc., has failed to take sufficient measures regarding computer systems to prevent the placement of erroneous orders, such as incorporating the settings of order limits regarding trading orders, including both hard limits and soft limits, into their systems.

(iii) Cases in which the securities company, etc., is deemed to have failed to develop an appropriate control environment in light of the viewpoints specified in III-2-8.

IV-3-2-2 Exercise of Checking Function against Issuers

(1) Points of Attention Regarding Screening Related to Underwriting

(i) Whether the securities company, etc., has established appropriate rules regarding the screening of matters used for judgment as to the appropriateness of underwriting, such as the financial condition and business performance of issuers based on Rule 14 "Rule Regarding Securities Underwriting" of the Japan Securities Dealers Association's Fair Practice Rules, and whether it conducts effective screening in an appropriate manner. Whether it has established arrangements and procedures for ensuring the verification of the screening results.

(ii) Whether the securities company, etc., relies on the screening conducted by other securities companies, etc., that act as joint lead underwriters and neglects to conduct its own screening.

(iii) Whether the securities company, etc., has established arrangements and procedures for appropriately conducting screening, such as ensuring the independence of the screening division from the sales divisions, in terms of both function and effect.

(iv) Whether the securities company, etc., has the function of examining and evaluating possible conflicts of interest between the underwriting division and other divisions. Whether it has developed a control

environment for properly preventing conflicts of interest through the exercise of the said function.

(v) Whether the securities company, etc., has established appropriate rules, regarding the calculation of prices based on laws and regulations as well as the Fair Practices Rules, in order to prevent underwriting under terms, such as volume and price, deemed to be markedly inappropriate. Furthermore, whether it has developed a control environment that ensures an appropriate determination of underwriting terms.

(2) Points of Attention Regarding Underwriting and Purchases of Privately Placed CBs

While capital increases through third-party allotment and private placement of convertible bonds (CBs) (including moving-strike CBs (MSCBs)) are seen as effective fund-raising means for corporate rehabilitation and other measures, they involve the risk that the interests of existing shareholders may be undermined through the dilution of the value of their shareholdings, depending on the issuance terms and the usage method. In light of this risk, supervisors shall pay attention to whether securities companies, etc., handling such deals (i) properly design products with due consideration of possible effects on existing shareholders, (ii) provide issuers (senior managers of issuers) with sufficient product explanations suited to their level of understanding and (iii) ensure that issuers make appropriate information disclosure.

(3) Points of Attention Regarding Issuers Affiliated with Anti-Social Forces

From the viewpoint of preventing the listing of stocks issued by antisocial forces or by companies affiliated therewith, it is desirable that securities companies, etc., make sure to properly identify attempts to list such stocks in their screening for underwriting, through cooperation with relevant authorities, the Japan Securities Dealers Association and other organizations. and that they refuse to underwrite such stocks in some cases.

IV-3-2-3 Exercise of Checking Function against Investors

(1) Points of Attention Regarding Trading Management System for Prevention of Illegal Trading

Securities companies, etc., need to exercise the function of acting as a check against investors by preventing the trading of securities on behalf of customers, while understanding that such trading could constitute an illegal activity, such as market manipulation and insider trading. Therefore, in examining the management of trading by securities companies, etc., conducted to prevent illegal trading by customers, supervisors shall pay attention to the following points with due consideration of "Regarding Members' Development of Trading Management System for Prevention of Illegal Trading by Customers," which is a resolution adopted by the Japan Securities Dealers Association's Board of Governors. (Careful attention shall be paid to Internet transactions, in particular, in light of the absence of face-to-face contact therein.)

(i) Precise Identification of Customers' Trading Patterns and Thorough Management

A. Whether the securities company, etc., has established specific procedures for identifying customers' trading patterns as represented by features such as the types of products they trade and the method and characteristics of their trading, and precisely identifies their trading motives by monitoring its trading activity as necessary in accordance with the procedures.

B. Whether the internal control division makes sure that all officers and employees are aware of and

follow the above procedures, and ensures the effectiveness thereof by revising them as necessary, for example.

C. From the viewpoint of ensuring the preciseness of insider registration, whether the securities company, etc., strives to improve the contents of insider registration cards by inquiring with customers about the contents of registration through periodic comprehensive checks and by checking registered information against information available from external information vendors.

D. From the viewpoint of preventing illegal practices such as market manipulation and insider trading, whether the securities company, etc., strives to identify the original customers and the end-investors, with regard to transactions with investment business associations and orders placed from abroad.

E. In cases where the securities company, etc., has recognized the possibility of customers using accounts opened under fictitious names, whether they investigate the true identity of the customers and monitor transactions involving the said accounts with special care.

(ii) Establishment of Trading Screening Criteria and Efficient Utilization Thereof

A. Whether the securities company, etc., has established the criteria for selecting individual issues for screening, in light of factors such as the advancers-to-losers ratio, the own market involvement ratio and the trading status of specified customers, in order to ensure the fairness of customers' transactions and make appropriate selection based on the said criteria.

B. Whether the securities company, etc., conducts appropriate trading management regarding selected issues by, for example, establishing specific screening criteria and taking measures necessary (e.g., inquiries with customers, issuing alerts and suspending trading) for preventing illegal trading practices, such as market manipulation.

C. Whether the internal control division has developed a control environment for examining the consistency of the selection and screening criteria and the implemented measures with the actual status in a timely manner, and is ensuring the effectiveness of the measures and criteria by making revisions as necessary, for example.

(iii) Others

A. Whether the securities company, etc., ensures that all customers are aware of the purpose of restrictions on short-selling by, for example, reminding them that new sell orders for margin trading deemed to have been repeatedly placed by a customer in a short period of time for the purpose of exceeding price limits do not fall under the category of transactions specified by Article 14 (ii) of the cabinet office ordinance regarding regulations on securities transactions.

B. Whether the securities company, etc., conducts appropriate trading management by taking appropriate measures, such as checking the contents of orders in a timely manner, making inquiries to customers, issuing alerts and suspending trading as necessary, in order to avoid taking orders intended to exceed price limits.

C. Whether the securities company, etc., makes sure to immediately report suspected cases of insider trading to the supervisory authorities based on Article 9 of the Anti-Criminal Proceeds Act.

(2) Points of Attention Regarding Pre-Hearing

In cases where a securities company, etc., holds pre-hearings or entrusts third-party entities to do so, whether it makes sure to either implement or entrust third-party entities with the implementation of (i) approval by the legal compliance division, (ii) signing of an agreement with the surveyed entity to not provide information regarding transactions related to the relevant securities and the relevant corporation and (iii) compilation and storage of written records based on the FIB Cabinet Office Ordinance and "Regarding Appropriate Treatment of Pre-Hearings by Members," a resolution adopted by the Japan Securities Dealers Association's Board of Governors.

(3) Points of Attention Regarding Investors Affiliated with Anti-Social Forces

It is desirable that securities companies, etc., conduct sufficient trading management and screening with regard to investors who may be affiliated with antisocial forces, in cooperation with relevant authorities, the Japan Securities Dealers Association and other organizations.

IV-3-2-4 Maintenance of Self-Discipline of Securities Companies, etc., as Market Players

Against the background of the increasing diversity and complexity of the business operations of securities companies, etc., as market players, such as principal investments, M&A advisory services, proposals for fund-raising through complex schemes and trading of securitization products, the number of incidents involving potential conflicts of interest and ethical problems related to their business operations is increasing.

In light of this situation, supervisors shall pay attention to the following points when examining the maintenance of the self-discipline of securities companies, etc., as market players.

(i) Whether the securities company, etc., has formulated internal policies and rules and established an appropriate internal control environment (including a control environment for internal audits) from the viewpoint of preventing conflicts of interest and ensuring compliance with a code of ethics. Whether they have developed an appropriate control environment for legal compliance by ensuring all officers and employees are aware of and comply with those policies and rules through the provision of training, for example.

(ii) Whether the securities company, etc., has identified transactions with a high risk of conflicts of interest.

(iii) Whether the securities company, etc., has established an appropriate control environment for prior screening (for judging whether or not to allow the screened transactions to be made) by a division independent from the sales division, as necessary, from the viewpoint of preventing conflicts of interest.

(iv) Whether the securities company, etc., provides appropriate explanations and makes appropriate disclosure to customers and investors, as necessary, with regard to the status of conflicts of interest.

(Reference) Examples of (Potential) Cases of Conflicts of Interest

- Cases where a securities company, etc., purchases stocks offered for sale through erroneous orders while knowing the orders are erroneous.
- Cases where a securities company, etc., (or companies belonging to the same groups therewith) acts as the lead manager of initial public offerings of stocks in unlisted companies in which it has made investment and where it sell the stocks after the IPO.
- Cases where a securities company, etc., (or companies belonging to the same groups therewith)

originates securitization products based on assets it has acquired as a result of principal investments and sells the products to investors without providing sufficient explanations (transfer of risk).

- Cases in which a securities company, etc., proposes or considers securitization schemes aimed at accounting manipulation and tax evasion, through the use of special-purpose companies, for example.

IV-3-2-5 Supervisory Method and Actions

With due consideration of the above viewpoints, supervisors shall encourage an appropriate exercise of the market intermediary function of securities companies, etc., in cooperation with relevant organizations, including Financial Instruments Firms' Associations. In addition, they shall identify and keep track of the status of voluntary improvement made by securities companies, etc., when it is deemed necessary to do so from the viewpoint of protecting public interests and investors, by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When a securities company, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When a securities company is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including issuing an order for business suspension based on Article 52 (1) of the FIEA.

IV-3-3 Appropriateness of Business Operations Related to Over-the-Counter Derivatives Transactions

IV-3-3-1 Control Environment for Legal Compliance

If over-the-counter derivatives business operators (Type 1 Financial Instruments Business Operators engaging in the business specified under Article 2(8)(iv) of the FIEA; the same shall apply hereinafter) are to gain the trust of investors, it is important that they strive to manage their business operations in an appropriate manner, while strictly complying with laws, regulations and various business rules, and fully recognizing their roles as undertakers of over-the-counter derivatives business.

Basically, supervisors shall examine an over-the-counter derivative business operator's control environment for legal compliance, based on the viewpoints and the supervisory method specified in III-2-1. However, they shall also examine it in relation to a broad range of matters, including the status of compliance with voluntary rules set by self-regulatory organizations.

(1) Points of Attention Regarding Segregated Management

(i) In cases where the over-the-counter derivative business operator entrusts the management of cash margin and other deposits made by customers regarding over-the-counter financial futures transactions (as specified under Article 79(2)(ii) of the FIB Cabinet Office Ordinance) to the counterparty to the cover transactions, as specified under Article 143(1)(iii) of the FIB Cabinet Office Ordinance and where the entrusted margins include those related to proprietary trading, whether the management of margins related to the cover transactions and the management of those related to proprietary trading are clearly segregated.

(ii) In cases where margin calls have been made with regard to margins entrusted to the counterparty to the

cover transactions because of market movements, for example, whether the over-the-counter derivative business operator makes sure to make payment from its own account and prevents margins managed in customers' accounts from being used to make the payment.

IV-3-3-2 Control Environment for Customer Solicitation and Explanations

(1) Points of Attention Regarding Advertisements, etc.

(i) In cases where losses exceeding the amount of cash margin and other deposits may arise due to rapid market movements, despite a contract provision for making automatic settlements through reversing trades in the event of the loss exceeding a prescribed ratio (hereinafter referred to as the "Loss-Cutting Rule"), whether the over-the-counter derivative business operator properly indicates this risk in the advertisement.

(ii) Whether the over-the-counter derivative business operator has forced customers to continue attending seminars and similar events despite their expression of unwillingness to do so (including cases where it has effectively forced them to do so). It should be kept in mind that this kind of practice shall be deemed to meet the provision of Article 38(v) of the FIEA (known as "prohibition of re-solicitation").

(2) Points of Attention Regarding Over-the-Counter Derivative Business Operators' Responsibility for Explanation

"The Key Points of the Status of Internal Control" in the Explanation Documents, as specified under Article 46-4 of the FIEA, shall describe specific arrangements and procedures for handling complaints and inquiries from customers and for conducting internal audits.

(3) Points of Attention Regarding Over-the-Counter Financial Futures Business Operators' Responsibility for Explanation

(i) Offer of Prices Indicated at Time of Transaction

A. Regarding Article 123 (xxi) of the FIB Cabinet Office Ordinance, in cases where an over-the-counter financial futures business operator offers the price of a financial instruments, a financial index or an option concerning over-the-counter financial futures trading to a customer requesting the offer of the price indicated at the time of the transaction, the price offered by the business operator may be either the opening price, the intraday high, the intraday low or the closing price of the relevant transaction date.

B. Over-the-counter financial futures business operators shall record the prices of financial instruments, financial indexes and options indicated at the time of the transaction and store them for at least three years.

(ii) Hedging

A. Whether the over-the-counter financial futures business operator solicits customers to do transactions intended to offset possible losses involved in the transactions made by them (so-called hedging) or engage in similar practices with regard to over-the-counter financial futures business (limited to

transactions involving cash margin and other deposits)

B. Cases where an over-the-counter financial futures business operator confirms the possibility of a customer making hedging transactions, when the customer has expressed willingness to make such transactions or when the customer inquired about the possibility of making such transactions shall not automatically be deemed to fit the provision of Article 117(1)(xxvi) of the FIB Cabinet Office Ordinance. However, if the business operator indicates that possibility without explaining that hedging may lack economic rationality in some cases, as the customer must pay double fees and may incur losses depending on the interest rate differential between currencies (hereinafter referred to as the "Swap Point") and must bear an additional burden regarding the price difference (what is known as "the spread received by over-the-counter financial futures business operators) between the sale and purchase prices with the median price as a base point, the business operator's act shall be deemed to fall under the category of "other similar practices" specified under Article 117(1)(xxvi) of the FIB Cabinet Office Ordinance.

(iii) Transactions with Customers and Counterparties to Cover Transactions

Whether the over-the-counter financial futures business operator provides appropriate explanations regarding the following points when requested to do so by customers:

A. Order placement method of cover transactions
B. Criteria for the execution of cover transactions
C. Response to the occurrence of system troubles in relation to the counterparties to cover transactions

(iv) Response to Rapid Market Movements

Whether the over-the-counter financial futures business operator provides appropriate explanations regarding how it responds to rapid market movements, when requested to do so by customers.

(v) Internal Control Environment for Proprietary Trading

Whether the over-the-counter financial futures business operator provides appropriate explanations regarding whether it engages in proprietary trading and, if it does so, regarding its control environment for risk management, when requested by customers to provide such explanations.

(vi) Status of Segregated Management

In cases where the over-the-counter financial futures business operator entrusts the management of cash margins to the counterparty to cover transactions, whether it provides customers with appropriate explanations, when requested by them to do so, regarding not only information regarding the counterparty to cover transactions, as specified under Article 94(1) of the FIB Cabinet Office Ordinance, but also how accounts are established at the counterparty to cover transactions and how cash margins are managed thereby.

(4) Points of Attention Regarding Provision of Pre-Contract Documents

(i) The "reasons for the possibility of a loss exceeding the principal amount," as specified under Article 82(iv)(b) of the FIB Cabinet Office Ordinance shall include a rapid market movement that could cause a loss exceeding the principal amount despite the Loss-Cutting Rule.

(ii) The "reasons for the termination of the relevant financial instruments transaction contract," as specified

under Article 82 (viii) of the FIB Cabinet Office Ordinance shall include items related to the Loss-Cutting Rule.

(iii) The "types and calculation methods of cash margin and other deposits to be made by customers with regard to the relevant derivatives transactions, etc.," as specified under Article 93(1)(iv) of the FIB Cabinet Office Ordinance shall include items related to the minimum margin deposits and additional margin deposits that must be made when the existing deposits have fallen short of the required level due to market movements, etc. (hereinafter referred to as "margin calls").

(iv) Regarding currency-related transactions, the "major terms and other basic items regarding derivatives trading," as specified under Article 93(1)(vii) of the FIB Cabinet Office Ordinance shall include items related to the method of determining prices of financial instruments, etc., and the Swap Point. In cases where the Swap Point may be either received or paid by customers and where a loss may arise, these possibilities shall be properly indicated.

(v) Regarding the "counterparty to a cover transaction," as specified under Article 94(1)(i) of the FIB Cabinet Office Ordinance all such counterparties shall be indicated when two or more counterparties exist. However, in cases where a participant in the interbank foreign currency market engaging in a cover transaction finds it impossible to identify the counterparty thereto, it shall suffice that an indication to that effect be contained in the Explanation Document.

(vi) Regarding, the "trustee," as specified under Article 94(1)(iv) of the FIB Cabinet Office Ordinance the specific name of the trustee of cash margin and other deposits, as specified under each item of Article 143(1), shall be indicated.

(5) Points of Attention Regarding Provision of Documents Related to Receipt of Cash Margin and Other Deposits

The "date of the receipt of deposits by the relevant Financial Instruments Business Operators, etc.," as specified under Article 114(1)(iv) of the FIB Cabinet Office Ordinance may be either the date on which the deposit is made or a date after that date, depending on the agreement between the business operator and the customer.

(6) Points of Attention Regarding Ban on Uninvited Solicitation

Regarding customer solicitation for over-the-counter derivatives trading, in the past, there were some cases in which solicitation by means of telephone calls and door-to-door visits led customers to engage in such trading without sufficient understanding of the risks and schemes involved and caused disputes, a situation that eventually developed into a social issue. In light of this, a ban has been imposed, under Article 38(iii) of the FIEA, on over-the-counter financial futures business operators and their officers and employees visiting or placing phone calls to customers who have not requested solicitation, in order to solicit them to sign contracts for financial futures transactions (a practice known as "uninvited solicitation").

Meanwhile, Article 116 of the FIB Cabinet Office Ordinance allows over-the-counter financial futures business operators to solicit the customers with whom they have on-going transactions to sign contracts for financial futures transactions, and to solicit corporations engaging in foreign trade and foreign currency transactions to sign such contracts, in order to offset the possibility of losses that may be incurred by the

corporations as a result of exchange rate movements related to their assets and liabilities.

In order to ensure compliance with the above provisions, it is important for over-the-counter financial futures business operators to develop a control environment for customer management so as to precisely identify the status of customers' solicitation requests. Therefore, supervisors shall conduct supervision by paying attention to the following points, for example:

(i) Eligibility for Uninvited Solicitation

A. The "solicitation for signing contracts for financial futures transactions through visits or phone calls," as specified under Article 38(iii) of the FIEA, shall include inquiring with customers as to whether they are willing to accept visits for solicitation.

B. The "persons who have outstanding unsettled over-the-counter financial futures transactions in their accounts," as specified under Article 116(i) of the FIB Cabinet Office Ordinance shall include persons who hold options contracts for which the exercise period has not expired.

C. An inquiry regarding general items submitted via the telephone or through other means to an over-the-counter financial futures business operator from a customer who has seen an advertisement, or a request therefrom for documents regarding the outline of transactions shall not in itself be deemed to constitute a "request for the solicitation for signing contracts for financial futures transactions."

(ii) Identification of Status of Customers' Solicitation Requests

A. Whether the over-the-counter financial futures business operator strives to identify the status of customers' solicitation requests and past transactions in a timely manner, by developing a system of customer cards, for example, and whether it ensures that all officers and employees strive to solicit customers in an appropriate manner in light of the status of their solicitation requests and past transactions.

B. Whether the over-the-counter financial futures business operator has prescribed specific procedures for the management of customer information, such as the status of their solicitation requests and past transactions, and ensures that all officers and employees are aware of and comply therewith. In particular, whether the business operator has prescribed the procedures for managing customer information based on sufficient deliberations made from the viewpoint of the confidentiality obligation.

C. Whether the internal control division strives to grasp how the over-the-counter financial futures business operator identify the status of customers' solicitation requests and past transactions and manage customer information. Furthermore, whether the said division examines, as necessary, if solicitation is conducted in an appropriate manner, and strives to develop a control environment that ensures the effectiveness of the procedures for managing customer information by reviewing and revising them, for example.

(7) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding an over-the-counter derivatives business operator's control environment for customer solicitation and explanations, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary

improvement made by the over-the-counter derivatives business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the over-the-counter derivatives business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the over-the-counter derivatives business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

IV-3-3-3 Discretional Trading Contracts, etc.

(1) Points of Attention Regarding Discretionary Trading Contracts with Foreign Financial Futures Companies

When supervisors receive a notification from an over-the-counter derivatives business operator for the signing of a contract based on Article 16(1)(viii)(b) of the Cabinet Office Ordinance Regarding Definitions, they shall pay attention to the following points:

(i) Whether the division that executes transactions regarding the said contract is clearly separated from the divisions that receive and execute orders for other brokerage transactions.

(ii) Whether it is ensured that account books are compiled in ways to enable the identification of transactions related to the said contract.

(2) Scope of Specified Agreements by Over-the-Counter Derivatives Business Operators

Specified agreements under Article 123(xiii)(b) and (c) of the FIB Cabinet Office Ordinance include the following agreements:

(i) Agreements regarding rewards and contracted values higher or lower than the specified rewards and contracted values (including rewards and contracted values determined with a prescribed method)

(ii) Agreements regarding an appropriate range determined with a specified reward or a contracted value as a base point.

(iii) Agreements regarding the determination of rewards and contracted values at the discretion of over-the-counter derivatives business operators on condition that they follow the best execution practice in daily trading.

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding an over-the-counter derivatives business operator's practices specified under Article 123 (xiii) (a) to (e) of the FIB Cabinet Office Ordinance through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the over-the-counter derivatives business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA, while paying consideration to the above viewpoints. When the over-the-counter derivatives business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the

FIEA. When the over-the-counter derivatives business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

IV-3-3-4 Control Environment for Managing Risk Related to Over-the-Counter Financial Futures Transactions

Regarding currency-related over-the-counter financial futures transactions made with customers, it is important for over-the-counter financial futures business operators to manage their own risks. Therefore, supervisors shall supervise over-the-counter financial futures business operators' control environments for risk management and their execution of business by paying attention to the following points.

(1) Points of Attention Regarding Transactions with Customers and Counterparties to Cover Transactions

(i) In cases where there is the possibility of a timing gap arising between the execution of a transaction with a customer and the execution of a cover transaction, whether the over-the-counter financial futures business operator has developed a control environment for risk management that is well prepared for the risk of a rapid market movement occurring during the intervening period.

(ii) In cases where a cover transaction is made at a specific interval of time or for a specific amount of transactions, or made at the discretion of dealers, rather than being made for each transaction with a customer, whether the over-the-counter financial futures business operator has developed a control environment for risk management that is well prepared for the risk of a rapid market movement occurring between the execution of a transaction with a customer and the execution of a cover transaction, with due consideration of the timing gap.

(iii) In cases where the over-the-counter financial futures business operator makes cover transactions after executing customers' limit orders or loss-cutting orders in light of quotations indicated by information vendors and other factors, whether the business operator has developed a control environment for risk management that is well prepared for the risk of a rapid market movement occurring during the intervening period.

(iv) Basically, handling of information technology risk related to cover transactions made through a computer system shall be examined from the viewpoints regarding the development of the relevant control environment that are specified in III-2-8. However, with due consideration of the possibility of computer system troubles disrupting cover transactions, supervisors shall also examine whether the over-the-counter financial futures business operator has developed a control environment for risk management that is well prepared for the risk of a rapid market movement occurring during the intervening period.

(v) Whether the over-the-counter financial futures business operator fully understands the contents of a contract with the counterparty to cover transactions and has developed a control environment that ensures quick and appropriate response in the event of a dispute.

(2) Points of Attention Regarding Response to Rapid Market Movements

Whether the over-the-counter financial futures business operator has established a specific policy for risk management in preparation for a possible rapid market movement, such as refraining from taking orders from

customers when it has suspended proprietary trading or when it is impossible to make transactions with the counterparty to cover transactions, and whether it has developed a control environment that ensures compliance with the policy.

(3) Points of Attention Regarding Proprietary Trading

In cases where an over-the-counter financial futures business operator engages in proprietary trading in addition to cover transactions related to customers, supervisors shall pay attention to the following points:

(i) Whether the over-the-counter financial futures business operator has established internal rules regarding position limits, stop-loss limits (on daily and monthly bases) and overnight position limits regarding employees engaging in proprietary trading.

(ii) Whether the over-the-counter financial futures business operator has set both soft limits and hard limits regarding order placement by employees engaging in proprietary trading in order to prevent erroneous orders.

(iii) Whether the over-the-counter financial futures business operator has developed a control environment that ensures that the compliance of transactions made by employees engaging in dealing with internal rules is constantly monitored by back-office staff.

(4) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding an over-the-counter financial futures business operator's control environment for risk management, through daily supervisory administration, they shall identify and keep track of the risk management status by conducting in-depth hearings and, when necessary, requiring the submission of a report based on Article 56-2(1) of the FIEA. When the business operator's risk management status is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the business operator is deemed to have the risk of defaulting in light of its business condition or asset status, the FSA shall consider taking necessary actions, such as issuing an order for business suspension under Article 52(1) of the FIEA.

IV-3-4 Points of Attention Regarding Supervision of Non-Affiliated Business Operators

(1) Major Supervisory Viewpoints

(i) In the case of a Financial Instruments Business Operator which does not belong to any Financial Instruments Firms' Association or have membership in or trading participant rights at any financial instruments exchange (referred to as "Non-Affiliated Business Operators" in IV-3-4), whether it has developed internal rules with due consideration of rules set by Financial Instruments Firms' Associations, articles of incorporation set by financial instruments exchanges and other rules and regulations (hereinafter referred to as the "Rules Set by Associations, etc.").

(ii) Whether the Financial Instruments Business Operator has developed a control environment that ensures appropriate compliance with internal rules (e.g., examination of whether all officers and employees are

aware of and comply therewith).

(iii) When the rules set by associations, etc., have been revised, whether the Financial Instruments Business Operator makes sure to quickly review and revise internal rules accordingly.

(2) Supervisory Method and Actions

(i) In cases where a non-affiliated business operator has failed to establish internal rules with due consideration of the rules set by associations, etc., and where it is deemed unlikely to do so on a voluntary basis, supervisors shall order it to establish internal rules based on Article 56-4(2) of the FIEA. In such cases, the non-affiliated business operator shall also be required to revise internal rules immediately in response to any future revision of the rules set by associations, etc.

(ii) In cases where a non-affiliated business operator's internal rules are deemed to need to be revised in light of the rules set by associations, etc., and where the business operator is deemed unlikely to make revision on a voluntary basis, supervisors shall order the business operator to do so based on Article 56-4(2) of the FIEA.

(iii) When supervisors have recognized an issue of supervisory concern regarding the status of a non-affiliated business operator's establishment and revision of internal rules and compliance therewith, they shall strive to identify and keep track of the actual situation, by holding in-depth hearings and requiring the submission of a report based on Article 56-2(1) of the FIEA. In addition, they shall conduct appropriate supervision based on Article 56-4(1) of the FIEA, with due consideration of the rules set by associations, etc., by, for example, issuing an order for business improvement based on Article 51 of the FIEA and an order for business suspension based on Article 52(1), as necessary.

IV-4 Various Administrative Procedures (Type I Financial Instruments Business Operator)

IV-4-1 Registration

(1) Trade Names

A Local Finance Bureau that has received an application from a business operator shall inquire with the FSA and other Local Finance Bureaus, when necessary, to check whether the trade name of the applicant does not violate Article 29-4(1)(vi)(b) of the FIEA.

(2) Items Regarding Examination of System's Appropriateness

When examining whether or not a Financial Instruments Business Operator is sufficiently staffed to properly conduct the financial instruments business as specified under Article 29-4(1)(i)(d) of the FIEA, supervisors shall check the following points based on its application and attachments thereto as well as hearings:

(i) Whether it can be deemed that officers and employees with sufficient knowledge and experience have been secured and a sufficient organization has been established to conduct the relevant financial instruments business in light of the following requirements.

A. Top managers must be sufficiently qualified to conduct financial instruments business in a fair and appropriate manner, in terms of their backgrounds and capabilities.

B. Managing directors must understand the viewpoints regarding governance indicated in the FIEA and various other laws and regulations, and have sufficient knowledge and experience to conduct governance, in addition to sufficient knowledge and experience regarding compliance and risk management to conduct financial instruments business in a fair and appropriate manner.

C. The staff must include two or more permanent officers or employees with more than three years of experience regarding the relevant Type I Financial Instruments Business.

D. The Financial Instruments Business Operator must be staffed and organized so that managers in charge of internal control are appropriately allocated, and personnel necessary for conducting business in an appropriate manner are allocated to individual divisions. (Regarding the conduct of underwriting business in particular, it is necessary to ensure a sufficient control environment and secure staff to conduct the business in a fair and appropriate manner.)

E. The compliance division (staff in charge of compliance) should be independent from the sales division and staffed with personnel who have necessary knowledge and experience.

F. Staff capable of conducting the following processes should be secured, with regard to the relevant business.

a. Compilation and management of account books, reports and other documents.

b. Disclosure

c. Segregated management of customer assets

d. Risk Management

e. Computer system management

f. Trading management, customer management

g. Advertisement screening
h. Customer information management
i. Processing of complaints and disputes
j. Internal audits

(ii) When the qualifications of employees and officers are examined in a comprehensive manner in relation to the following criteria regarding organized crime groups, their members and financial crimes, whether there is the risk that public confidence in the Financial Instruments Business Operator could be damaged because of the inclusion among its staff of officers and employees with inappropriate qualifications.

A. Officers and employees should not be current or former members of organized crime groups.
B. Officers and employees should not have close relationships with organized crime groups.
C. Officers and employees should not have the experience of being sentenced to a fine for violation of the FIEA or other domestic financial laws and regulations or foreign laws and regulations equivalent thereto.
D. Officers and employees should not have the experience of being sentenced to imprisonment with work or more severe punishment (including similar punishments imposed under foreign laws or regulations equivalent thereto). (Particular attention should be paid to the case of an officer or employee being accused of committing crimes specified under Articles 246 to 250 of the Penal Code (fraud, fraud using computers, breach of trust, quasi fraud and extortion as well as attempts at these crimes).

(Note) It should be kept in mind that in cases where it is deemed, as a result of comprehensive examination based on the criteria described in (ii) A to D, that a major shareholder in the Financial Instruments Business Operator could exercise undue influence on it, thereby damaging public confidence in it, the business operator may be deemed to be "not adequately staffed to properly conduct financial instruments business."

(3) Authorization Column of Registry Book of Financial Instruments Business Operators

When authorization has been granted to a financial instruments business, the fact of authorization shall be recorded in the authorization column of the book of registry of the Financial Instruments Business Operator, based on Article 30(1) of the FIEA. Authorization granted by the FSA to Financial Instruments Business Operators under its jurisdiction each month shall be collectively notified by the 15th day of the following month to individual Local Finance Bureaus at which the business operators have been registered.

(4) Points of Attention Regarding Business Operators Not Planning to Join Any Financial Instruments Firms' Association or Obtain Membership in or Participants Rights at Any Financial Instruments Exchange.

Supervisors shall notify the following matters to a business operator that does not plan, at the time of the application, to join any Financial Instruments Firms' Association or to obtain membership in or trade participant rights at any financial instruments exchange, and request them to take appropriate actions.

(i) In cases where the business operator is deemed to lack appropriate internal rules set with due consideration of the rules set by associations, etc., it shall in principle be ordered to immediately establish appropriate internal rules after registration.

(ii) A non-affiliated business operator may be ordered to revise internal rules with due consideration of the rules set by associations, etc.

(iii) In cases where a non-affiliated business operator has been ordered to establish or revise internal rules, they need to do so within 30 days and obtain approval from the Prime Minister.

(iv) In cases where a non-affiliated business operator plans to revise or abolish internal rules established as described in (iii) above, they need to obtain approval from the Prime Minister.

(v) The authorities are to properly supervise non-affiliated business operators' business operations, so as to ensure the full protection of public interests and investors, with due consideration of the rules set by associations, etc.

IV-4-2 Approval and Notification

IV-4-2-1 Authorization

The Proprietary Trading System (PTS) has functions similar to exchanges, and thus the FIEA stipulates that an authorization system shall be maintained for the operations of the PTS, as under the former Securities and Exchange Act. Based on this, business authorization prescribed in Article 2(8)(x) of the FIEA needs to be examined with due consideration to the following points:

(i) The following points shall be considered when deciding whether the relevant operation falls under the PTS category:

A. A system acting as an agent for transactions involving securities in the financial instruments exchange markets or the over-the-counter (OTC) securities markets, or acting as an agent for transactions involving securities for another Financial Instruments Business Operator shall not fall under the category of the PTS or financial instruments exchange market, etc.

B. Some cross trading systems, in which securities are traded with clients, may fall under the category of the PTS or financial instruments exchange market, etc., if the trade is conducted based on bid and offer price indications, bringing together supply and demand for securities on a number of orders.

C. Financial instruments business operators and information vendors, which provide information on stock prices and financial information, may fall under the category of Financial Instruments Business Operators (intermediary) and are required to obtain approval for the PTS operations in the cases where indicative prices presented by several Financial Instruments Business Operators are shown in the list (price competition) and order-matching methods concerning business conditions are provided, including distribution of exclusive terminals and setting up of links, etc., for order placement and negotiation.

(ii) The following points shall be considered when authorizing the operations:

A. Internal control

Whether the following items have been developed regarding the state of internal control of operations:

a. Personnel in charge of management of operations have, in principle, at least five years of experience in securities-related operations, and a division in charge of operations has an

organization and staff necessary for the implementation of the operations

b. A system to verify the identification of clients has been established in operations

c. Methods and measures have been developed to exclude transactions that undermine the fairness of trade, such as insider trading, market manipulation, intentional market making, and short selling, etc. Furthermore, the said items are listed in the content and methods of operations concerning authorization as the "important matters related to the securing of fair trade," prescribed in Article 17(12) of the FIB Cabinet Office Ordinance

d. In-house regulations for operations have been developed in compliance with laws and regulations, such as the FIEA, etc.

B. Accountability to Clients

Whether a system allowing for sufficient explanations concerning the following has been developed, when providing clients with explanations:

a. The method to determine trading prices.

b. Trading rules covering from order placement to confirmation and settlement.

c. The handling of settlement failure.

d. The possibility of a contract at the offered price.

C. Ensuring of Safety and Certainty of System Capacity, etc.

Whether the following items have been developed regarding safety/certainty of system capacity for operations:

a. To rationally estimate the number of orders and contracts, and to ensure system capacity sufficient for the estimation.

b. To perform sufficient tests based on the estimation mentioned above.

c. To prevent the occurrence of excess system capacity and system failure, and to establish a monitoring method and a system for early detection.

d. To have developed a method to handle system failures (including providing explanations to, making contact with clients) and to have developed such a system.

e. To have a dual system (back-up system).

f. To receive third-party evaluation (from an external organization) on the above items and to confirm the safety and certainty of system capacity, etc.

D. Measures for Confidentiality of Trade Information

Whether sufficient measures are taken, including the following items, with respect to confidentiality of clients' trade information:

a. To clearly separate the operators engaged in the operations of the relevant business division from those engaged in other divisions.

b. To prohibit persons engaged in the relevant operations from conducting the operations using information related to other operations, and to prohibit persons engaged in other operations from conducting their operations using information pertaining to the relevant operations.

c. To have accurately taken measures for the prevention of leakage of client information.

d. To have developed in-house regulations in respect to the above measures.

(iii) The following conditions shall be attached to the authorization of the relevant operations:

A. Disclosure of Price Information, etc. (limited to the cases of securities traded in the relevant business (securities specified in the items of Article 14 of the Cabinet Office Ordinance Concerning Financial Instruments Firms' Associations, etc.)).

"To disclose the best quotations/trading prices, etc., of the PTS in such a form which allows comparison with other PTSs and in such a form which allows free access from the outside in real time.

However, information shall be disclosed in such a way which allows free access from the outside until a disclosure format which allows comparison with other PTSs is established."

B. Quantity Standards for Trade Volume

The figures of trade volume of the PTS shall be used for the quantity standards. However, it is necessary to make sure that the figures obtained using the trade volume of a PTS system network to which the said PTS belongs (referring to a network comprising PTSs in the relevant area in the cases where orders of the said PTS are matched with orders of another PTS by using an electronic information processing organization) would not conflict with the quantity standards.

a. In the case of a PTS that handles share certificates and bonds with share options and determines prices by a method other than auctions (limited to those listed in financial instruments exchanges or those registered pursuant to Article 67-11(1) of the FIEA):

"1. In the cases where the ratio of average payments of daily transactions of share certificates or bonds with share options traded on financial instruments exchanges or OTC markets (limited to those listed in financial instruments exchanges and those registered pursuant to Article 67-11 (1) of the FIEA) exceeds 10% of the sum of transaction payments of any security and exceeds 5% of the entire share certificates and bonds with share options of the previous six months, the following measures shall be taken:

A. To expand and develop a system (organization/personnel) for administering trade and inspection in order to ensure trade fairness.

B. To establish a system equivalent to the accumulated reserve for breach of contract losses in the financial instruments exchanges in order to ensure settlement.

C. To establish a periodic monitoring system to ensure the safety and certainty of system capacity, etc.

2. If the said ratio exceeds 20% of any security and 10% of the total share certificates and bonds with share options of the previous six months, a license to establish a financial instruments exchange market shall be obtained.

3. In addition to the above, new criteria shall be introduced within the boundaries of PTSs that trade other debit securities, if, with the expansion in trading volume, etc., the need arises from the viewpoint of public welfare or investor protection."

b. Other cases

"New criteria shall be introduced within the boundaries of PTSs that trade other debit securities, if, with the expansion in trading volume, etc., the need arises from the viewpoint of public welfare or investor protection."

C. Report on the Trade Volume

a. In the case of a PTS that determines prices by the auction method:

"With regard to the ratio, etc., prescribed in Article 1-10(i) and (ii) of the FIEA Enforcement Order, a Financial Instruments Business Operator shall submit a report about end-of-month figures to the Commissioner of the Financial Services Agency or the Director General of the Local Finance Bureau that supervises the said Financial Instruments Business Operator, by the 20th of the following month."

(Note) With regard to the "gross trading volume" concerning the PTS prescribed in Article 1-10(i) and (ii) of the FIEA Enforcement Order, the figures obtained pursuant to the proviso of "B. Quantity standards concerning trade volume" shall also be reported.

b. In the case of a PTS in which prices are determined by a method other than the auction method:

"Regarding the ratio prescribed in a-1 and a-2 of B above, etc., a Financial Instruments Business Operator shall submit a report about the end-of-month figures to the Commissioner of the Financial Services Agency or the Director-General of the Finance Bureau that supervises the said Financial Instruments Business Operator, by the 20th of the following month."

D. "New criteria shall be introduced, within its boundaries, if the need arises from the viewpoint of public welfare or investor protection."

(iv) The following points shall be considered as a supervisory response after authorization is given for the relevant operations:

A. To verify the trading volume, etc., using the reports, etc., in order to judge whether authorization requirements are being met.

B. To verify the progress of implementation of various measures that have been examined at the time of authorization by requesting reports, on an as needed basis.

C. When changes are made to the method used to determine trade prices and the operation methods, including delivery and other settlement methods, after the approval, early submission of an application for change shall be requested.

IV-4-2-2 Approval

IV-4-2-2-1 Approval of Other Businesses

When approving other businesses, based on Article 35(4) of the FIEA, supervisors shall pay attention to the following points:

(1) Whether the business violates applicable laws and regulations.

(2) Whether the calculation of the value of the loss risk equivalent related to the relevant business is appropriate, and whether it is ensured that the calculated value is properly reflected in the applicant Financial Instruments Business Operator's capital adequacy ratio.

(3) Whether the division in charge of calculating and managing the value of the loss risk equivalent related to the

relevant business is independent from the sales division.
(4) In cases where the relevant business involves the signing of contracts, whether the Financial Instruments Business Operator has prescribed the specific procedures necessary for investor protection regarding the signing of contracts with customers.
(5) Whether the Financial Instruments Business Operator has established internal rules regarding the relevant business.
(6) Whether the applicant Financial Instruments Business Operator's capital adequacy ratio is more than 140%.

IV-4-2-2-2 Approval of Exemption From the Preventive Measures Against Adverse Effects

The following shall apply to the approval of exemption from the preventive measures against adverse effects pursuant to the provision of Article 44-3(1) of the FIEA:

(1) Where the Approval is Deemed to be Granted under the Provision of Article44-3 (1) of the FIEA

In the cases where a director or auditor of a Financial Instruments Business Operator (referring to Financial Instruments Business Operators specified in Article 153(vii) of the FIB Cabinet Office Ordinance; hereinafter the same shall apply in IV-4-2-2-2) concurrently holds the position of a board member or auditor of any of the following juridical persons, thus making the said juridical person fall under the category of a parent corporation, etc., of the said Financial Instruments Business Operator, if the said Financial Instruments Business Operator submits a notification pursuant to Article 50(1) of the FIEA, an approval prescribed in the provision of Article 44-3 of the FIEA shall be granted to the said Financial Instruments Business Operator and its director, auditor or employee, exclusively for the activities involving the said juridical person.

(i) Financial Instruments Firms' Associations
(ii) Investor Protection Fund
(iii) Financial Instruments Exchanges

(2) Basic Policies for Implementation of Internal Control Based on the Approval Pursuant to the Provision of Article 44-3 of the FIEA

Operations related to internal control need to be independently and appropriately implemented by each specified person concerned (as prescribed in Article 151 (1) of the FIB Cabinet Office Ordinance; the same shall apply hereinafter), in light of the fact that such operations are important for specified persons concerned, in ensuring the soundness of business. Some operational limitation is imposed by laws and regulations; for instance, Financial Instruments Business Operators are not permitted to engage in the banking business, and banks are not permitted to engage in business related to securities, in principle. Therefore, in the cases where efforts are made to enhance operations concerning internal control within a group, by sharing information when implementing the said operations, the underlying principles are that the adverse effects of information sharing shall be effectively prevented and that operations related to internal control shall be strictly and exclusively implemented by the specified persons concerned. In the cases where these principles are maintained in compliance with laws and regulations, and risk management is strictly enforced, it is deemed that such operations "would not undermine public welfare or investor protection," from the perspective of ensuring prevention of adverse effects, as required

by Article 44-3 of the FIEA.

(3) Points to Consider When Conducting Examinations Prescribed in Article 152 of the FIB Cabinet Office Ordinance for Approval under the Provision of Article 44-3 of the FIEA

The following points shall be considered in each operation concerning internal control listed in items of Article 151(4) of the FIB Cabinet Office Ordinance when conducting examinations prescribed in Article 152 of the FIB Cabinet Office Ordinance for approval under the provision of Article 44-3 of the FIEA.

(i) Operations Related to Legal Compliance

A. Whether a personnel structure and management system have been established to implement operations related to legal compliance fairly and accurately, in light of the following items:

a. It shall be confirmed that a division in charge of operations related to legal compliance in each of the specified persons concerned (hereinafter referred to as the "legal compliance division") is able to take appropriate responses in accordance with the condition of the business, such as the type of products handled by each specified person concerned, the degree of necessity for consideration of legal issues related to the products, and the type of business partners of each specified person concerned.

b. It shall be confirmed that the legal compliance division is able to appropriately settle disputes with clients of each specified person concerned (including the settlement through appropriate instruction to a business division, etc).

c. It shall be confirmed that there would be no obstacles to appropriate responses to investigation or to requests from the competent authority for each specified person concerned to file a report.

d. It shall be confirmed that a legal compliance division has the following roles and authorities and the said roles and authorities are enforced strictly.

i) The authority to investigate facts involved in transactions, recommend chief officers (any person who assumes business and management responsibility (or the general manager of a branch or its equivalent in the case of a foreign Financial Instruments Business Operator or a branch office of foreign banks (hereinafter referred to as "foreign Financial Instruments Business Operators, etc.")); the same shall apply hereinafter) to conduct in-house actions when necessary, and submit reports to the competent authority, when violations of laws and regulations are suspected in the transactions of a business division (referring to the laws and regulations prescribed in Article 151(4) of the FIB Cabinet Office Ordinance.).

ii) The authority to allow appropriate monitoring of the activities of a business division through adequate management of corporate-related information, as prescribed in Article 1(4) (xiv) of the FIB Cabinet Office Ordinance (hereinafter referred to as "corporate-related information"), and the continuous formulation of a list of limited trades and a list of cautions, in order to appropriately prevent illegal acts, such as insider trading, etc.

iii) The authority to be involved in ex-ante examinations and ex-post reviews, from the perspectives of reputational risk (referring to risk of damage to the social reputation and credibility in financial markets of a specified person concerned; the same shall apply hereinafter)

and corporate ethics, in relation to the duties of specified persons concerned.

iv) The authority to require a business division to refer to the legal compliance division for examination and judgment of transactions conducted by the said business division, from the perspective of legal compliance or another legal perspective, such as legal admissibility or legal responsibility, etc. (hereinafter referred to as "legal judgment, etc."). (Except for the cases where there are logical reasons, such as application of a legal judgment, etc., that has already been given).

v) The authority to conduct audits on compliance with pledges, etc., and to promote solid implementation of the results of the audits (except for the cases where a division conducting internal audit and internal inspection (hereinafter referred to as the "internal audit section") performs the said audit.)

e. The legal compliance division shall assume the responsibility to make legal judgments concerning transactions of the business division of a specified person concerned.

f. When taking on a new business, a legal compliance division shall assume the responsibility to urge, in a timely manner, the chief executive officer of the specified person concerned to formulate regulations corresponding to the in-house regulations listed in B below.

g. In the cases where a compliance officer in one of the corporations of a specified person concerned concurrently assumes the role of a compliance officer in another specified party concerned, an individual independent of each of the specified parties concerned, and otherwise suitable for the position, shall be employed as the chief compliance officer.

B. Whether in-house regulations have been developed in order to implement compliance-related operations (limited to the provisions specifying the corporate responsibility concerning the said operations).

Examinations shall be performed to find whether the responsibilities for compliance with the content of A. above, for the operational procedures and all the operations of specified persons concerned (including the assignment of responsibility for compliance to a business division and to a legal compliance division) have been made clear and whether the responsibility to carry out the said operations fairly and accurately has also been clearly stated.

(ii) Operations Related to Risk Management Concerning Loss

A. Whether a personnel structure and management system have been established to fairly and accurately implement operations related to risk management concerning loss, in light of the following items:

a. It shall be confirmed that a division in charge of risk management (hereinafter referred to as "risk management division") related to the individual specified persons concerned (market risk (possible risks arising due to the fluctuation of prices of the securities held; the same shall apply hereinafter), credit risk (possible credit risks accruing from default of contract, such as bankruptcy of a business partner or other reasons; the same shall apply hereinafter), and operational risk (possible risks occurring during the process of daily operations, such as errors in clerical work and inaccurate information processing; the same shall apply hereinafter)) performs risk management appropriately in accordance with the conditions of transactions, such as the type of products handled by each

specified person concerned, the type and magnitude of risks attributed to the said products, and the type of business partners of each specified person concerned.

b. It shall be confirmed that risk management is conducted in the following manner and the risk management operations are strictly implemented:

i) Risks to specified persons concerned are understood not only in an integrated manner, but also individually by each juridical person.

ii) Risks born by a specified person concerned are managed within the bearable range that can explain the rationality as an independent juridical person.

iii) To ensure the financial soundness of specified persons concerned and not abuse the integrated risk management.

iv) The division in charge of operational risk management assumes the responsibility to clearly understand the operational risks recognized by each division in charge of clerical works ranging from the conclusion of contracts to settlement in each specified person concerned, to evaluate the risks quantitatively and qualitatively in accordance with the characteristics and the degree of operational risk, and to urge, in a timely manner, related business divisions to develop procedures and a framework to appropriately manage the operational risk.

v) To clearly understand the quantity and magnitude of the risks and carry out appropriate risk management accordingly, with respect to the market risk, credit risk and operational risk accrued by all the business transactions performed by employees belonging to specified persons concerned.

c. In the cases where an employee in the risk management division of one of the corporations of a specified person concerned concurrently assumes a role in the risk management division of another specified person concerned, an individual independent of each specified person concerned, and otherwise suitable for the position, shall be employed as the chief officer of the risk management division.

d. It shall be confirmed that there would be no obstacle to appropriate responses to investigation or requests from the competent authority for each specified person concerned to file a report.

B. Whether in-house regulations have been developed in order to implement operations related to the risk of loss (limited to the provisions specifying the corporate responsibility concerning the said operations).

Examinations shall be performed to find whether in-house regulations concerning the content of B above and the procedures of risk management operations are clearly and specifically spelled out and the responsibility to carry out the said operations fairly and accurately has been clearly stated.

C. Attention shall be paid to whether examinations are conducted by individual divisions when market risk, credit risk, and operational risk are managed by different divisions. In this case, it is necessary to note that the responsibilities of each risk management division are clearly stipulated.

(iii) Operations Related to Internal Audit and Internal Inspection

A. Whether a personnel structure and management system have been established to fairly and accurately implement operations related to internal audit and internal inspection, in light of the following items:

a. It shall be confirmed that there is a personnel structure and a management system that allow an internal audit section to perform an audit concerning the compliance system and business operation system by an appropriate method and frequency, in accordance with the diversity and size of operations of all divisions of a specified person concerned, to submit a report to the competent authority, and to carry out an audit concerning compliance with pledges, etc. (expect in the cases where audits are conducted by a compliance division).

b. It shall be confirmed that a system is developed that allows solid implementation of appropriate and specified measures for internal control and internal inspection reporting.

c. In the cases where an employee engaged in operations related to internal audit and internal inspection of one of the corporations of a specified person concerned is concurrently engaged in the said operations of another specified person concerned, an individual independent of each specified person concerned, and otherwise suitable for the position, shall be employed as the chief officer of the said operations (provided, however, that this shall not apply to the cases where an internal audit section comes under the direct control (including reporting to a chief officer via the internal audit section, in action, of the head office in the case of foreign Financial Instruments Business Operators, etc.) of a chief officer of a specified person concerned (including a chief officer of the head office or collegial committee that assumes the role of chief officer, or the audit committee in the case of foreign Financial Instruments Business Operators, etc.); hereinafter the same shall apply in (3); however, this is limited to the case where the internal audit follows the control, order and supervision of an internal control administrator (referring to an internal control administrator prescribed in the Fair Business Practice Regulations No.13 of the Japan Security Dealers Association, the "Regulations Concerning Internal Administrators, etc., of Association Members")).

Meanwhile, attention shall be paid to the compliance with the provisions of Article 31-4 of the FIEA and Article 335(2) of the Companies Act (Restriction on Concurrent Holding of Positions by Auditors) with respect to the concurrent holding of positions by executive officers.

d. It shall be confirmed that there would be no obstacle to appropriate responses to investigation or requests from the competent authority for each specified person concerned to file a report.

B. Whether in-house regulations have been developed in order to implement operations related to internal audit and internal inspection (limited to the provisions that specify the in-house responsibilities concerning the operations)

Examinations shall be performed to find whether in-house regulations concerning the content of A. above have been prescribed clearly and specifically and the responsibility to carry out the said operations fairly and accurately has been clearly stated.

(iv) Operations Related to Finance

A. Whether a personnel structure and management system have been established to fairly and accurately implement operations related to finance, in light of the following items:

a. It shall be confirmed that the operations of each specified person concerned are implemented appropriately in accordance with the business size, etc., of the specified person concerned, with respect to the finance division in charge of finance operations (hereinafter referred to as "finance

division"), such as funding, liquidity control, capital policy, and management of surplus funds.

b. It shall be confirmed that the finance division is able to implement appropriate finance control individually in each specified person concerned.

c. In the cases where an employee engaged in operations related to finance in one of the corporations of a specified person concerned is concurrently engaged in the said operations in another specified person concerned, an individual independent of each specified person concerned, and otherwise suitable, shall be employed as the chief officer of the said operations.

d. It shall be confirmed that there would be no obstacle to appropriate responses to investigation or requests from the competent authority for each specified person concerned to file a report.

B. Whether in-house regulations have been developed in order to implement operations related to finance (limited to the provisions that specify the in-house responsibilities concerning the operations).

Examinations shall be conducted to see whether in-house regulations concerning the content of A. above and operations related to finance have been prescribed clearly and specifically and the responsibilities to carry out the said operations fairly and accurately have been clearly stated.

(v) Operations Related to Accounting

A. Whether a personnel structure and management system has been established to implement operations related to accounting fairly and accurately, in light of the following items:

a. It shall be confirmed that the operations of each specified person concerned are implemented appropriately in accordance with the business size, etc., of the specified person concerned, with respect to the accounting division in charge of accounting operations (hereinafter referred to as "accounting division"), such as management of profit and loss, analysis and management of profitability (including capital profitability), management of cost and budget, and formulation of financial statements.

b. It shall be confirmed that the accounting divisions are able to carry out accounting work individually in each specified person concerned.

c. In the cases where an employee engaged in accounting operations of one of the corporations of a specified party concerned is concurrently engaged in the said operations of another specified party concerned, an individual independent of each specified person concerned, and otherwise suitable for the position, shall be employed as the chief officer of the said operations.

d. It shall be confirmed that there would be no obstacle to appropriate responses to investigation or requests from the competent authority for each specified person concerned to file a report.

B. Whether in-house regulations have been developed in order to implement operations related to accounting (limited to the provisions that specify the in-house responsibilities concerning the operations).

Examinations will be conducted to see if in-house regulations concerning the content of A. above and operations related to accounting have been prescribed clearly and specifically and the responsibilities to carry out the said operations fairly and accurately have been clearly stated.

(vi) Operations Related to Tax Practice

A. Whether a personnel structure and management system have been established to fairly and accurately

implement operations related to tax practice, in light of the following items:

a. It shall be confirmed that the operations of the tax division in charge of tax operations (hereinafter referred to as the "tax division") of each specified person concerned are implemented appropriately in accordance with the condition of transactions, such as the type of products handled by the specified person concerned and the tax issues related to the products, etc.

b. The tax division has the capacity to participate in decision-making regarding the tax practice and accounting of the specified person concerned.

c. The tax division makes judgments from the perspective of tax practice and accounting (hereinafter referred to as "tax judgment") and assumes responsibility for the transactions of the specified person concerned.

d. The tax division has the authority to require a business division to refer to the tax division for tax judgment on transactions carried out by the business division (except for the cases where there are logical reasons, such as application of the tax judgment, etc., that has already been given).

e. In the cases where an employee engaged in tax operations of one of the corporations of a specified person concerned is concurrently engaged in the said operations of another specified person concerned, an individual independent of each specified person concerned, and otherwise suitable for the position, shall be employed as the chief officer of the said operations.

f. It shall be confirmed that there would be no obstacle to appropriate responses to investigation or requests from the competent authority for each specified person concerned to file a report.

B. Whether in-house regulations have been developed in order to implement operations related to tax practice (limited to the provisions that specify the in-house responsibilities concerning the operations).

Examinations will be conducted to see if in-house regulations concerning the content of A. above and the operations related to tax practice have been prescribed clearly and specifically and the responsibilities to carry out the said operations fairly and accurately have been clearly stated.

C. In the cases where the said operations are conducted by a legal compliance division or accounting division, examinations listed in (i) or (v) above shall be performed by integrating the criteria listed in (vi).

(vii) Each Division That Conducts Operations Related to Internal Control

A. Whether appropriate measures have been taken to prevent the leakage of nonpublic information (such nonpublic information pertaining to issuers of other specified persons concerned or clients; hereinafter the same shall apply to (7) and (8) below) from each division that conducts operations related to internal control, in light of the following items:

a. To take clear measures to prevent the leakage of nonpublic information, such as the development of in-house regulations, the development of an information management system (including prevention of access to systems), adequate monitoring, and information management measures, by strictly saving and controlling documentations for a sufficient period of time.

b. To take measures to prevent nonpublic information (development of confidential regulations and information management, etc.) from leaking at the time of personnel reshuffles in each division

that conducts operations related to internal control, as well as in the business division.

c. To effectively prevent provision of nonpublic information to other unauthorized divisions that conduct operations related to internal control.

d. Note that provision of nonpublic information for the purpose of internal control to executive officers of a specified person concerned is not deemed to be a leakage of nonpublic information (Note that it is necessary to take preventive measures against leakage of nonpublic information from the executive officers to the business division).

e. To take stringent control measures to prevent corporate information possessed by a specified person concerned from being used by the business division of the specified person concerned.

f. To effectively prevent nonpublic information from being provided to a business division via a division conducting credit scoring.

B. Whether the personnel engaged in operations related to internal control are independent from the business division, in light of the following items:

a. To have an accurate check-and-balance authority; for example, the decision made by personnel engaged in the compliance division on legal judgment, etc., overrides the judgment of sales division.

b. A legal compliance division has independent authority over all departments, etc., regardless of the command and control system, for the recognition of the violation of laws and regulations and for the improvement of measures against illegal conduct.

c. Personnel engaged in risk management have precise check-and-balance authority over the business division.

d. Personnel engaged in operations related to finance have the authority to accurately conduct operations related to finance independently, without being influenced by the business division.

e. Personnel engaged in operations related to accounting have the definite authority to monitor capital allocation and profitability of the business division.

f. Personnel engaged in operations related to tax practice have precise check-and-balance authority: for example, the judgment of personnel engaged in operations related to tax practice overrides that of the business division, without exception.

g. The said personnel are free from the command and control of the business division (except for executive officers).

(viii) Points to be Considered When Examining the Matters Listed from (i) to (vii) Above

A. In the examination of the independence of supervisors of operations related to internal control (supervisors mentioned in (i)-A-g, (ii)-A-c, (iii)-A-c, (iv)-A-c, (v)-A-c, and (vi)-A-e), if one of the supervisors of a specified person concerned (including a supervisor who manages multiple operations) has command and control authority (except for the right to refuse the implementation of trades that may clearly violate laws and regulations or prescribed in-house regulations or trades that may pose a serious concern over risk management) over specific operations of supervisors (including a supervisor who manages multiple operations) of other specific persons concerned, care should be taken so that the independence of other supervisors is not undermined.

B. In the cases where one of the supervisors of operations related to the internal control of a specified person concerned concurrently holds another position as a supervisor of the said operations of another specified person concerned, each specified person concerned must appoint an independent director of the said operations. Attention shall be paid to the fact that it is necessary to clarify the responsibility and authority to allow the said independent director to control operations related to internal control (hereinafter referred to as "director of management division"), to control works of each employee engaged in the said operations, and to ensure accurate implementation of the said operations in each specified person concerned and the effective performance of the check-and-balance function of the said operations against business execution lines.

C. In the cases where a collegial committee attended by executive officers (including those in two or more concurrent positions) is to be set up and when it is not clear that exchange of nonpublic information does not take place in the said collegial committee, attention shall be focused on the possibility that it may constitute the violation of Article 44-3 of the FIEA. In addition, in the cases where executive officers of a Financial Instruments Business Operator or bank (hereinafter referred to as "bank, etc," in IV-4-2-2-2) attend the collegial committee and when it is not clear if the committee aims to manage reputational risk of the said bank, etc., and ensure that laws and corporate ethics are adhered to, attention shall be paid to the fact that holding the said collegial committee may constitute a violation of Article 33 of the FIEA. The Financial Instruments Business Operator which has set up such a collegial committee shall be required, at least, to make proper explanations concerning in-house regulations that specify the objectives of the establishment of the said committee or minutes of the committee meetings, and when necessary, a request for a report shall be made pursuant to Article 56-2 (1) of the FIEA.

However, when an application is filed, pursuant to the provision of Article 44-3 of the FIEA, for the exchange of nonpublic information held by the said collegial committee of a specified person concerned, as part of a meeting which implements operations related to internal control, examinations shall be performed as part of the said operations to be implemented in line with approval requirements concerning the consolidation of said operations.

In this case, the general operations concerned shall first be examined pursuant to the provisions of Article 152 of the FIB Cabinet Office Ordinance. The following points shall be confirmed when performing examinations of the said collegial committee concerning the "operation and management system which enables the fair and accurate implementation of operations related to internal control", as prescribed in Article 152(i) of the said Act:

(i) Whether all of the supervisors (including the director of the management division) (when a supervisor in charge of a legal compliance division of a specified person concerned holds a concurrent position as a legal compliance supervisor of another specified person concerned, the relevant supervisor) of legal compliance divisions in each specified person concerned, which satisfies the requirements listed in (i) above, such as having a sufficient check-and-balance function and assuming compliance responsibility, etc., attend the meeting (in the cases where any supervisor cannot attend the meeting for reasons outside the control of the supervisor, another

employee in the legal compliance division who has a capacity equivalent to the said supervisor in fulfilling the sufficient check-and-balance function and compliance responsibility, and who has been designated in advance by the said supervisor shall attend the meeting without fail). Whether specific measures are taken to prevent the agenda of the said committee from violating laws and regulations.

(ii) It shall be examined whether the said collegial committee aims to manage the reputational risk of a specified person concerned and to ensure that laws and corporate ethics are adhered to.

(iii) It shall be examined whether the establishment of the said collegial committee appears consistent with rationality.

(iv) It shall be examined whether persons in charge or supervisors of individual business divisions or respective transactions/projects (including those in positions assuming responsibility for the management of a specified person concerned (including the director of a branch office in the case of foreign Financial Instruments Business Operators, etc.) and those engaged in actual business activities) participate as committee members, or if only the supervisors of approved operations related to internal control, in addition to executive officers of a specified person concerned (in the case of foreign Financial Instruments Business Operators, the virtual head office shall be requested to submit verification materials of qualification evidence) participate in the collegial committee as members. In addition, it shall be examined whether the above items from (i) to (iv) are ensured and whether in-house regulations have been developed to clarify the shared responsibilities for decisions of the said collegial committee, with respect to the "in-house regulations to implement operations related to internal control," as provided for in (ii) of the said Article.

As for "prevention of leakage of nonpublic information" and "independence from the business-executing divisions," prescribed in (iii) and (iv) of the said Article, examinations shall be conducted to verify if the committee is aimed at refusing any trade transaction that may be in violation of laws and regulations or in clear violation of prescribed in-house regulations, or any trade transaction that may pose a serious threat to risk management. In the cases where executive officers attend the said collegial committee, strict examinations need to be performed on the specific measures taken to prevent information leakage and to secure the independence of supervisors, including whether the said executive officers are actually engaged in business operations.

D. Attention shall be paid to possibility that the case where an employee holds concurrent positions at the relevant Financial Instruments Business Operator and the relevant bank may be a violation of Article 33 of the FIEA (or Article 12 of the Bank Act), except for the cases where approval has been granted pursuant to the provision of Article 44-3 concerning the divisions in charge of operations related to internal control. It may also be in violation of the said act when the said bank is found to make decisions on specific operations of the said Financial Instruments Business Operator (including exercising power over personnel policy for the said purpose), even if there are no employees holding concurrent positions.

E. In the cases where an application for authorization is filed, pursuant to the provision of Article 44-3 of the FIEA, concerning the operations related to the internal control of a holding company, as prescribed in Article 52-2 of the FIEA, a parent juridical person, etc., of a Financial Instruments Business Operator which does not fall under the category of a holding company prescribed in Article 56-2 of the FIEA and which implements governance of the said Financial Instruments Business Operator and its incidental operations (excluding banks, cooperative structured financial institutions, and financial institutions and Financial Instruments Business Operators specified in Article 1-9 of the FIEA Enforcement Order (including cases where a Financial Instruments Business Operator is a foreign juridical person)) or a bank holding company, strict inspections shall be conducted on the measures taken to prevent leakage of nonpublic information obtained from a specified person concerned to the said subsidiary company from the said holding company.

F. Attention shall be paid to the fact that it is necessary to consider the forms of operation implementation when conducting examinations on operations related to compliance management and when the said operations include legal advice, judgment and works, in order to avoid violating the Bar Act and other laws and regulations, as well as when conducting examinations on operations related to tax practice and when the said operations include surveys on finance/accounting, providing advice/judgment on formulation of plans, or finance/accounting, the formulation of and provision of advice/judgment on documents related to tax practice, in order to avoid violating the Certified Tax Accountant Act.

G. In the case where an application is filed for operations other than those related to internal control by a Financial Instruments Business Operator (limited to those engaged in Type I Financial Instruments Business or Investment Management Business) pursuant to the provisions of Article 35(4) of the FIEA, if an activity, which falls under the category prescribed in (vii) or (viii) of Article 153 of the FIB Cabinet Office Ordinance is to be conducted in the process of concurrent implementation of the said operations, the said operations are considered to interfere with public welfare, and thus, approval of concurrent implementation of operations shall not be granted, pursuant to the provision of Article 35(5) of the FIEA. In the meantime, attention shall also be paid to the fact that with respect to operations related to internal control, an approval for exclusion from application of Article 44-3 of the FIEA and an approval of other operations pursuant to Article 35(4) of the FIEA are incompatible with each other, judging from the spirit of the basic principles stipulated in IV-4-2-2-2-2 (2).

H. With respect to the exchange of nonpublic information between divisions that conduct operations related to the internal control of a specified person concerned, attention shall be given to the point that exemption from the obligation to protect client confidentiality shall not be provided by the said approval.

I. In the cases where an application for approval prescribed in the provision of Article 44-3 of the FIEA is filed between the division that examines the underwriting of securities of a Financial Instruments Business Operator (referring to the department that conducts examinations on publicized documents, such as Securities Registration Statements, etc., submitted by an issuer), the legal compliance division, and the division that implements the credit scoring banks, it should be noted that such approval shall not be granted for the purpose of preventing the leakage of nonpublic information to the business

division, in conformity with Article 33 of the FIEA.

J. In the cases where nonpublic information is exchanged upon obtaining the approval of (ii) above by a risk management division of a specified person concerned and where risk assessment and judgment are performed for clients of the specified person concerned, if any division of the specified person concerned conducts business with the said clients under extremely different conditions from ordinary business practices, it should be noted that nonpublic information may have been leaked to the business division.

K. Attention shall be given to the fact that leaks of nonpublic information by a specified person concerned to unauthorized divisions would violate Article 153(vii) or (viii) of the FIB Cabinet Office Ordinance even in the cases where nonpublic information is exchanged between divisions that implement operations related to internal control with the approval of the provision of Article 44-3 of the FIEA.

(4) Interpretation, etc, of Article 153(ix) of the FIB Cabinet Office Ordinance.

Occasions when a Financial Instruments Business Operator visits a client (an individual person) with a parent bank or a subsidiary bank, etc., if sufficient information/explanation with presentation of documents listing the following purports is not provided to the client prior to sales, it may violate the provision of Article 153(ix) of the FIB Cabinet Office Ordinance.

(i) The said Financial Instruments Business Operator and its parent bank, etc./subsidiary bank, etc., are separate juridical persons.

(ii) Products and services concerning financial instruments business operations provided by the said Financial Instruments Business Operator are not those provided by its parent bank, etc./subsidiary bank, etc.

(iii) The said parent bank, etc./subsidiary bank, etc., must not support the conclusion of a contract with a client of a Financial Instruments Business Operator by expressing its own evaluation or opinions on the products or services offered by the Financial Instruments Business Operator, or by emphasizing the credibility or advantage of the products or services in the cases where no request for such conduct is made by the client or such conduct is not necessary for the execution of its own operations, since such conduct may violate the provisions of Article 33(1) of the FIEA.

(5) Interpretation of Article 32 of the FIB Cabinet Office Ordinance

(i) "Operations for the execution of financial instruments business, etc., or financial instruments intermediary services," prescribed in Article 32(i) of the FIB Cabinet Office Ordinance refers to the following operations that do not entail governance decisions in relation to financial instruments operations, etc., or financial instruments intermediary services:

A. Acquisition, possession, lease, maintenance, security and management operations of real estate and facilities, such as sales offices, etc.

B. Management operations of maintenance/operation of automatic teller machines (ATMs).

C. Formulation, organization, storing, issuing and delivery operations of accounts, statements, and slips, etc.

D. Computer-related operations (system development, electronic processing, maintenance/management,

etc.).

E. Calculation operations (including accounting work such as salary calculation and calculation of monthly settlements, etc.).

F. Operations related to the management and organization of securities.

G. Brokerage for name transfer.

H. Requests for the payment of principal and interest of bonds and investment trusts.

I. Delivery and settlement of securities among financial instruments exchanges/Financial Instruments Business Operators, etc.

J. Welfare packages for officers and employees, such as employee counseling and bulk purchase and management of goods and services contributing to clerical work.

K. Supplementary clerical work, such as formulation of personnel-related documents (including operations related to the dispatch of workers to Financial Instruments Business Operators or financial instruments intermediary service providers).

L. Operations related to the education/training of officers and employees.

M. PR and advertisement.

N. Management operations such as use, maintenance and inspection, etc., of vehicles.

O. Formulation of documents for statistical purposes.

P. Providing public information, such as publications.

Q. Printing, binding, issuing and delivery of documents.

(ii) "Operations for the purpose of conducting the business of any of the following persons exclusively," prescribed in Article 32(ii) of the FIB Cabinet Office Ordinance refers to the operations listed in (i) above (except C) that do not entail governance decisions.

In this case, "Computer-related operations (system development, electronic processing, maintenance/management, etc.)" of (i) D and F above shall be replaced with "Operations related to the management and organization of securities (limited to those possessed as the own assets of a parent juridical person, etc., or a subsidiary juridical person, etc.)," (i) G shall be replaced with "Brokerage for name transfer, limited to those possessed as the own assets of a parent juridical person, etc., or a subsidiary juridical person, etc.)," and (i) K shall be replaced with "supplementary clerical work, such as the formulation of personnel-related documents (including operations related to the dispatch of workers to Financial Instruments Business Operators or financial instruments intermediary service providers and a parent juridical person, etc., or a subsidiary juridical person, etc.)."

(iii) The operations listed in (i) C above (excluding issuing and delivery services), data storage and management in (i) D, and those from (i) F to (i) I are closely related for the purpose of implementing the operations of the said Financial Instruments Business Operator, etc., the financial instruments intermediary service provider and the bank, etc. Therefore, it should be noted that the said operations shall not, in principle, be outsourced to any enterprise other than the said Financial Instruments Business Operator, etc., or a parent or subsidiary juridical person of a financial instruments intermediary service provider, or any company prescribed in (i) and (ii) of Article 32 of the FIB Cabinet Office Ordinance and that the process of implementation of the said operations is to be monitored in a timely manner.

In the cases where a Financial Instruments Business Operator (limited to those engaged in Type I Financial Instruments Business or Investment Management Business) is entrusted with the operations listed in (ii) above, it should be noted that the operations listed in (i) A, B, E, and J through Q above need to be approved like the other operations prescribed in Article 35(4) of the FIEA (meanwhile, attention shall be paid to IV-4-2-2-2 (3)(viii)(g)).

(iv) In the cases where the operations listed in (i) and (ii) above are outsourced by the said Financial Instruments Business Operator, etc., or the financial business intermediary service provider, it should be noted that the said Financial Instruments Business Operator, etc., or the financial business intermediary service provider is not exempt from the responsibility to clients for the said operations nor the administrative responsibilities.

IV-4-2-3 Notification

Supervisors shall receive and process notifications specified under the FIEA with due consideration of the following points. When they have received notifications regarding the businesses specified under Article 35(2) of the FIEA in particular, supervisors shall pay attention to whether the procedures legally necessary for regulating the businesses have been implemented. In addition, regarding the businesses listed below, they shall check whether their contents and methods meet the following criteria. In this case, the provision of relevant written documents and the implementation of paper-based procedures may be substituted by electronic means using computer systems and other information technologies, subject to customers' consent. Regarding businesses that do not meet the following criteria, the applicant business operators shall be required to file an application based on Article 35(4) of the FIEA.

(1) Business Related to Trading of Gold Bullion and Intermediary and Brokerage Services

(i) Description of Product

Whether the gold products handled by the Financial Instruments Business Operator are gold bullion, or gold coins, with high levels of purity and market liquidity, for which there is an established global market.

(ii) Procurement

Whether the business operator ensures that it or its affiliated companies do not hold excessive inventories, by including in its purchase contract with the supplier provisions stipulating that (i) the business operator itself does not hold any inventory in principle and (ii) the supplier agrees to buy back the gold product purchased by the business operator when requested to do so. Regarding a sale and buyback contract stipulating that the gold product should be bought back at a specified price (hereinafter referred to as the "Cash Forward Trade"), whether the business operator includes in its contract with the supplier a provision that ensures the execution of a forward contract.

(iii) Customer Services Activities

A. Sales Method

Supervisors shall examine whether the business operator meets the following requirements regarding the sales method:

a. To refrain from offering futures trading and concentrate on physical-delivery transactions.

b. Prior to the sale of gold products through cumulative investments, to provide customers with

sufficient written explanations that describe the scheme of the investment.

B. Solicitation

As gold investment should be made based on investors' own judgments and responsibility, supervisors shall examine whether the business operator meets the following requirements regarding investment solicitation:

a. To refrain from soliciting customers by offering definitive predictions regarding gold price movements.
b. To make appropriate investment solicitation suited to investors' intentions and their knowledge and experience regarding gold investment as well as the size and nature of their investment funds.
c. To refrain from promising loss compensation and soliciting investment by offering special profits.
d. To refrain from soliciting customers to conduct purchases and sales frequently (including frequent switching between securities and gold products) in a short period of time.
e. To refrain from conducting purchases and sales in amounts and at prices determined at its discretion on commission from customers.

C. Provision of Certificates, etc., to Customers

Supervisors shall examine whether the business operator meets the following requirements regarding the provision of certificates of safe custody to customers:

a. Provision of Certificates of Safe Custody to Customers

To provide necessary certificates and other documents necessary for clarifying the contractual rights and obligations and for facilitating transactions, such as the certificate of safe custody (limited to cases of custodial trade), at-delivery statements of account, written demands for purchase (documents which are attached to the gold product delivered in physical-delivery trade and which stipulates that the business operator agrees to buy the gold product), depending on whether the transaction is custodial or physical delivery-based.

However, regarding the Cash Forward Trade, the provision of the certificates of safe custody may be substituted by a statement of trade that describes the contents of transactions and the outstanding balance of gold in custody, if the statement is provided at the time of each delivery. Regarding a trade in which the business operator sells a fixed amount of gold bullion to a customer at a fixed interval of time through a method prescribed under the contract (hereinafter referred to as the "Cumulative Gold Bullion Investment"), the provision of the certificate of safe custody and the at-delivery statement of account may be omitted, if a notice that describes records of gold bullion purchases and the outstanding balance of gold in custody is provided at least once every six months.

b. Provision of a Set of Contract Clauses

To provide a set of contract clauses concerning gold bullion trade that specify items regarding contractual rights and obligations when the customer starts trading and when revisions are made, in both cases of custodial trade and physical delivery-based trade, from the viewpoint of preventing problematic conduct involving gold bullion trade and protecting customers.

D. Determination of Prices

Supervisors shall examine whether the business operator meets the following requirements when determining prices:

a. To set purchase and sale prices in yen terms and take into consideration prices in domestic and overseas markets, foreign exchange rates and other factors in determining prices. In addition, the business operator must purchase gold products from the supplier at market prices in the Cash Forward Trade, and set the resale price and the purchase and sale prices for customers based on market prices.

b. To indicate purchase and sale prices at all branches handling gold products on a daily basis and execute transactions at those prices, and refrain from placing market orders and forward orders.

(iv) Custody

Supervisors shall examine whether the business operator meets the following requirements regarding custody:

A. To refrain from pawning, or transferring to other parties, the certificates of custody issued based on the custody of physical gold products, such as the certificate of safe custody of physical gold products, the certificate of claims thereto and the receipt therefor.

B. When a Financial Instruments Business Operator that handles physical gold products engages in custodial trade, it must procure and store physical products equivalent in amount to the products handled in the custodial trade.

C. To notify customers in writing of the outstanding balance of gold products in custody, at least once every year.

(v) Buyback

Whether the Financial Instruments Business Operator agrees in principle to over-the-counter buyback of gold bullion (including gold bullion in custody) that it has sold to customers, upon their request.

(vi) Agency Business, etc.

Supervisors shall examine whether the Financial Instruments Business Operator limits the agency and intermediary businesses (hereinafter referred to as the "Agency Business, etc.") to those related to the Cash Forward Trade and the Cumulative Gold Bullion Investment as specified below:

A. Commissioned Agency Business, etc. Related to Cash Forward Trade

a. The Agency Business, etc., regarding the Cash Forward Trade shall include brokering between customers and Financial Instruments Business Operators offering gold products, or gold wholesalers (hereinafter referred to as the "Offering Financial Instruments Business Operators, etc.), and implementing all or part of the processes related to the Cash Forward Trade made between the customers and the Inviting Financial Instruments Business Operators, etc. on behalf of the Offering Financial Instruments Business Operators, etc. The Financial Instruments Business Operators engaging in the Agency Business, etc., related to the Cash Forward Trade shall sign contracts regarding the Agency Business etc., with the Offering Financial Instruments Business Operators, etc.

b. Financial instruments business operators engaging in the Agency Business, etc., related to the Cash Forward Trade shall meet the following requirements:

i) Financial instruments business operators engaging in the Agency Business, etc., related to the Cash Forward Trade shall provide customers with sufficient explanations to enable them to understand that the counterparties to their Cash Forward Trades are Offering Financial Instruments Business Operators, etc., and obtain their prior consent regarding this.

ii) Financial instruments business operators engaging in the Agency Business, etc., shall periodically check with Offering Financial Instruments Business Operators, etc., to confirm the contents of the customers' transactions.

B. Commissioned Agency Business, etc., Related to Cumulative Gold Bullion Investment

a. The Agency Business, etc., related to Cumulative Gold Bullion Investment shall include brokering between customers and Offering Financial Instruments Business Operators, etc., and implementing all or part of the processes related to the Cumulative Gold Bullion Investment made between the customers and the Offering Financial Instruments Business Operators, etc., on behalf of the Offering Financial Instruments Business Operators, etc. The Financial Instruments Business Operators engaging in the Agency Service, etc., related to the Cumulative Gold Bullion Investment shall sign contracts regarding the Agency Business etc., with the Offering Financial Instruments Business Operators.

b. Financial instruments business operators engaging in the Agency Business, etc., related to Cumulative Gold Bullion Investment shall meet the following requirements:

i) Financial instruments business operations engaging in the Agency Business, etc., related to Cumulative Gold Bullion Investment shall provide customers with sufficient explanations to enable them to understand that the counterparties to their the Cumulative Gold Bullion Investment transactions are Offering Financial Instruments Business Operators, etc., and obtain their prior consent regarding this.

ii) Financial instruments business operators engaging in the Agency Business, etc., shall periodically check with Offering Financial Instruments Business Operators, etc., to confirm the contents of the customers' transactions.

(2) Businesses Related to Signing of Association Contracts as Specified under Article 667 of the Civil Code and Intermediary, Brokerage and Agency Businesses Therefor and Businesses Related to Signing of Anonymous Association Contracts as Specified under Article 535 of the Commercial Code and Intermediary, Brokerage and Agency Services Therefor (excluding the businesses specified under Article 2(8)(ix) of the FIEA)

When soliciting customers to sign association contracts, whether the Financial Instruments Business Operator and its officers and employees provide sufficient explanations regarding the contents of the contracts and make solicitation in an appropriate manner suited to the customers' intentions, knowledge and experiences regarding the relevant associations, as well as their financial capacity and the nature of their investment funds. At the time of the signing of the contracts, whether they provide the customers with written explanations regarding the contents of the contracts.

(3) Business Related to Signing of Loan Participation Contracts and Intermediary, Brokerage and Agency Services

Therefor.

(i) Description of Business

The loan participation contract is a contract envisaged by "Accounting Treatment and Representation of Loan Participation," a report issued on June 1, 1995 by the Japanese Institute of Certified Public Accountants.

(ii) Conduct of Business.

Supervisors shall examine whether the Financial Instruments Business Operator meets the following requirements regarding the conduct of business:

A. To take due care to protect the original debtors and the transferees in executing business.
B. To provide the transferees with sufficient explanations regarding the nature and contents of the relevant debts.
C. To establish adequate arrangements and procedures for evaluating the relevant debts and ensure appropriate price formation
D. To provide appropriate solicitation in light of the transferees' intentions and experiences as well as their financial capacity.
E. At the time of the signing of the contract, to provide the transferee with written explanations regarding the contents of the contract.

IV-4-2-4 Points to Consider Concerning Cumulative Investment Business

The following points shall be considered concerning the conclusion of a contract for cumulative investment prescribed in Article 35(1) (vii) of the FIEA:

(1) Type of Securities Traded in Cumulative Investment

(i) Government bond certificates
(ii) Local government bond certificates
(iii) Bank debentures and other claims issued by juridical persons pursuant to special laws
(iv) Corporate bond certificates that are deemed to be issued periodically, in substantial amounts, such as corporate bond certificates issued by electricity business operators, etc.
(v) Investment trust beneficiary certificates (excluding listed investment trust beneficiary certificates; hereinafter the same shall apply in IV-4-2-4)
A. Unit type investment trusts
B. Open investment trusts (excluding bond investment trusts; hereinafter the same shall apply in IV-4-2-4)
C. Bond investment trusts
(vi) Foreign ETFs
(vii) Investment certificates of investment juridical persons (excluding listed investment certificates; hereinafter the same shall apply in IV-4-2-4)
(viii) Foreign investment certificates
(ix) Certificates of shares (limited to the certificates of shares listed in financial instruments exchanges or those registered in the registry of OTC traded securities held at the Japan Security Dealers Association, and

those listed in (10); hereinafter the same shall apply in IV-4-2-4)

(x) Listed investment trust beneficiary certificates (limited to those listed in (11); hereinafter the same shall apply in IV-4-2-4)

(xi) Listed investment certificates (limited to those listed in (12); hereinafter the same shall apply in IV-4-2-4)

(2) Method of Purchase of Negotiable Securities in Cumulative Investment

(i) Negotiable securities to be purchased shall be limited to those newly issued (provided, however, that this shall not apply to certificates of shares, listed investment trust beneficiary certificates and listed investment certificates), and the type and the method of appropriation for purchase shall be specified in advance in the contract. However, in the cases where there is no new issuance at the time specified in the contract or where new issuance is not adequately funded, the same type of negotiable securities that have already been issued may be purchased, pursuant to the provisions of the prescribed contract.

(ii) When payment from a client, or securities deposited by a Financial Instruments Business Operator (hereinafter referred to as "paid-up money") accrued from the acceptance of fruits or redemption of investment in negotiable securities deposited by a client (hereinafter referred to as "deposited negotiable securities") has reached the purchase price of negotiable securities to be purchased by the client, the Financial Instruments Business Operator shall purchase the said negotiable securities, without delay. However, the client may instruct the Financial Instruments Business Operator to cancel the purchase of negotiable securities at any time.

(iii) The purchase price of negotiable securities shall be set as follows:

A. The secondary offering price for the government bonds, local government bonds, financial bonds and other bonds and corporate bonds issued by juridical persons pursuant to special laws, however, in the case applicable to the proviso of (i) above, the market value of the financial instruments exchange prescribed in the contract or any other appropriate value;

B. The following prices shall be applied to the following investment trust beneficiary certificates:

a. Unit type investment trust: Public offer price

b. Open investment trust: Net asset value on the purchase date or one day prior to the purchase date (in the case of an open investment trust in which the value of assets retained in the trust is collected at the time of purchase, the amount obtained by adding the said value of assets retained in the trust to the net asset value)

c. Open bond investment trust: net asset value on the purchase date or one day prior to the purchase date

C. Net asset value on one day prior to the purchase date for foreign investment fund beneficiary certificates

D. Value as specified in the bylaws or the equivalent document for investment certificates or foreign investment certificates

E. Market value at the financial instruments exchange prescribed in the contract for certificates of shares (when there are several contract prices at the exchanges of the said stock, their weighted average price)

F. Market value of the financial instruments exchange prescribed in the contract for listed investment trust beneficiary certificates (when there are several contract prices at the exchanges of the said stock, their weighted average price)

G. Market value of the financial instruments exchange prescribed in the contract for listed investment beneficiary certificates (when there are several contract prices at the exchanges of the said stock, their weighted average price)

(3) Payment of Money and Management Method for Deposits in Cumulative Investment

(i) A client may pay, in part or in full, the buying price of negotiable securities as needed, however, this is done in a different way in the cases listed below from (8) to (12)

(ii) Payments received from a client, etc., shall be listed as cumulative deposit, and the maturity of the said deposit, such as interest, shall not be paid to the client.

(4) Timing of Transfer and Delivery of Ownership Right of Securities in Cumulative Investment

In the case of joint purchase, joint possession shall be completed when the trade session and the number of securities purchased by the relevant clients are finalized and the ownership rights of the said securities shall be transferred to the said clients. Fruits of investment in the said securities and the right to the principal of the clients shall come into effect on the said purchase date.

(5) Method of Custody of Securities in Cumulative Investment

(i) Securities purchased in cumulative investment activities shall be in custody in the following manner:

A. Deposit balance in securities based on cumulative investment, new deposit balance and amount of redemption shall be managed separately from other securities

In this case, securities jointly owned by a Financial Instruments Business Operator and its client(s) shall be further separated.

B. The Financial Instruments Business Operator may re-deposit the said securities in its own name in securities finance companies, banks or trust companies, instead of managing the said securities itself.

Here, in the cases where the rights and interests of the clients are deemed to be undamaged, a global certificate may be used for custody or re-deposit, upon obtaining consent from the client.

C. When returning deposited securities in response to the request made by a client, a clause may be included in the contract to the effect that return of securities may be replaced by the return of money obtained by selling the said securities at the market price (including necessary fees).

(ii) Securities purchased not under the cumulative investment contract may be stored as securities based on the cumulative investment contract, when the client requests. However, the said securities shall be limited to the same type of securities as those purchased under the said cumulative investment contract.

(6) Cancellation of a Contract for Cumulative Investment

(i) A contract shall be cancelled when a client requests. A client may request the cancellation at anytime.

(ii) When a client has not paid, in part nor in full, the buying price of securities for a consecutive period of

one year or more, cancellation shall be effective; provided, however, that this shall not apply to contracts prescribed in the provisions of (7) below which allows purchase of negotiable certificates within one year of the date of previous purchase, solely as the consideration of the fruits of investment in securities or deposit in redemption, when the client has deposited securities to a Financial Instruments Business Operator based on a cumulative investment contract.

(iii) Cancellation shall be effective when a Financial Instruments Business Operator can no longer conduct cumulative investment activities.

(iv) In addition to the above, when a client has not paid, in part nor in full, the buying price of securities for a consecutive period of three months or more, a Financial Instruments Business Operator may cancel the contract; provided, however, that this shall not apply to the contract prescribed in the proviso of (ii) above (excluding the cases where all of the following conditions from A through D are met).

A. Reports, etc., to a client have been returned due to the forwarding address being unknown, etc.

B. The address of the said client is unknown despite efforts being made to find it

C. No payment of the buying price or sales have been made for one year or more after the return of a report, etc., mentioned in A. above.

D. The balance is small (less than ¥10,000).

(7) A Financial Instruments Business Operator may conclude a contract to the effect that the Financial Instruments Business Operator shall periodically return part or all of the securities deposited or part or all of the fruits/redemption of investment in the said securities to a client when requested.

(8) The following can be done for joint purchase of government bonds in cumulative investment:

(i) A contract shall be concluded with a client who applies to purchase government bonds jointly with other clients to the effect that a Financial Instruments Business Operator shall buy the said government bonds in the form of cumulative investment. In this case, regardless of (3)-(i) above, an amount less than the minimum amount of payment may be accepted from the second payment and onwards, and when the sum of payments of the client and other clients reaches the purchase value (or an amount equal to the integral multiple of that amount), the Financial Instruments Business Operator shall buy the said government bonds, without delay

(ii) In the case of (i) above, when the total amount of payments from the clients is less than the purchase value of the government bonds, the Financial Instruments Business Operator shall jointly buy the bonds by paying the difference between the purchase value of the minimum unit and the said amount.

(iii) Clients who made a joint purchase (including the Financial Instruments Business Operator in the case of (ii) above) shall acquire ownership rights (co- ownership) in accordance with their respective shares

(iv) A Financial Instruments Business Operator shall set up an account for each client, in order to manage the clients' shares and the receipt of payments on fruits/redemption of the share of the government bonds co-owned by the clients, etc.

(9) The following shall be done for cumulative investment activity (hereinafter referred to as "property accumulation savings") based on the Act on the Promotion of Workers' Property Accumulation (hereinafter

referred to as the "Property Accumulation Act"):

(i) With respect to the purchase value of securities as listed in (1)(v)(B) above among the methods for buying securities, the following shall be used regardless of (2)(iii)(B)(b) above.

A. With respect to purchase under the workers' property accumulation savings contract, prescribed in Article 6(1) of the Property Accumulation Act, net asset value on the date of purchase (in the case of an open investment trust in which the value of assets retained in the trust is collected at the time of purchase, the amount obtained by adding the said value of assets retained in the trust to the net asset value).

B. Net asset value on the date of purchase for a purchase under the workers' property accumulation pension savings contract, prescribed in Article 6, paragraph 2 of the Property Accumulation Act, and under the contract on workers' property accumulation savings for house construction prescribed in paragraph 4 of the said article.

(ii) The following shall be used with respect to payment and management of deposits, regardless of (3)(i) and (ii) above.

A. The amount to be paid for the purchase of securities by clients shall be at least ¥1,000 (however, one yen in the cases listed below from B-b through e)

B. Payment shall be made in the following manner in line with the contract concluded between a business entity and a Financial Instruments Business Operator:

a. Payment by deduction from the said client's salaries

b. Payment by a business operator to the account of the said client for the purpose of encouraging property accumulation savings

c. Payment made from the said client's workers' property accumulation benefit or workers' property accumulation fund

d. In the cases where a client has changed employment, payment from the property accumulation handling organization of the former workplace

e. Payment of savings to be returned to the account of the said client by a business operator prescribed in Article 6(1) of the Property Accumulation Act.

C. Payments, etc., from a client shall be classified as "specified deposit transaction of property accumulation savings" in the accounting book, and the amount equivalent to it shall be deposited in a financial institution in the name of the Financial Instruments Business Operator, separately from other deposits.

D. Payments from a client shall be used for the purchase of negotiable certificates of the said client by adding the equivalent amount of interest to ordinary deposits. However, fruits of deposited securities, such as interest, shall not be paid to the client with respect to deposits generated from the receipt of fruits/redemption of investment in deposited securities.

(iii) A clause may be included to the effect that when the government bonds are bought jointly between a client and another client with respect to property accumulation, and when the total amount of purchase balance and payment of the said government bonds of one client has reached an integral multiple of ¥10,000, the said government bonds may be sold to buy corporate bonds jointly with other clients at integral

multiples of ¥10,000 as a unit/client. In this case, the provisions listed in (8)(ii) through (iv) above shall be applied to the purchase of corporate bonds.

(iv) Deposit balance and the redemption amount of securities based on property accumulation activity shall be managed separately from other securities based on cumulative investment. In this case, the Financial Instruments Business Operator may re-deposit the said securities in its own name in securities finance companies, banks or trust companies instead of storing them themselves.

(v) Cancellation shall be effectuated by the following methods, regardless of (6) above.

A. Contracts concerning property accumulation savings shall be cancelled in the following cases:

a. When a client makes a request. A client may request cancellation at any time

b. When a client no longer meets the requirements of property accumulation savings prescribed in the Property Accumulation Act

c. When a Financial Instruments Business Operator can no longer conduct "property accumulation savings" business.

B. In addition to the above, based on the said contract, the said contract may be cancelled when a client has re-deposited securities in a Financial Instruments Business Operator, etc., and when the client has not paid, in part nor in full, the payment for the purchase of securities for a consecutive period of one year or more following the first payment, after three years have passed under the workers' property accumulation savings contract, or after five years have passed under the workers' property accumulation pension savings contract or the contract on workers' property accumulation savings for house construction.

However, this shall not apply to the cases where a client can purchase securities solely for the consideration of the deposited money from fruits or redemption of investment in the said securities when the client has deposited the securities to a Financial Instruments Business Operator, etc., pursuant to the said contract.

(vi) Report on balance, etc., may be submitted to a client via the employer of the said client.

(10) The following shall be done for joint purchase cumulative investment of stock certificates:

(i) A clause shall be included in a contract to the effect that stock certificates can be jointly purchased with other clients applying for joint purchase in the form of cumulative investment.

In this case, a Financial Instruments Business Operator shall conclude a contract with a client in advance, specifying the name of the purchasing certificates, the amount of payment of the client per payment, and the date of execution of purchase, etc., and shall perform purchase operations in line with the said contract.

(ii) When the sum of payment, etc, of one client and other clients (or its integral multiple) reaches the purchase value of the stock certificates, a Financial Instruments Business Operator shall buy the said stock certificates without delay.

(iii) In the case of (ii) above, when the sum of payments from one client and other clients is not sufficient enough for the purchase value of the stock certificates, a Financial Instruments Business Operator shall keep the said fractional part until the next purchase or shall buy the stock certificates by paying the difference between the purchase value of the minimum unit and the said amount.

(iv) Clients (including a Financial Instruments Business Operator in the case of (iii) above where the Financial Instruments Business Operator has bought stock certificates jointly with a client) shall acquire the ownership (co-ownership) of the purchased stock certificates and hold co-ownership rights in accordance with the proportion of the paid amount (excluding the case in (iii) above where a Financial Instruments Business Operator keeps the fractional part). The name of the stock certificates purchased jointly among the said clients shall be the name of the Financial Instruments Business Operator. However, when a co-owner's share has reached a number of unit shares, the stock certificates shall be divided into share units by the record date prescribed in Article 124(1) of the Companies Act, such as the first end of period of the issuing company of the said stock certificates, and the said units shall be excluded from the application of the cumulative investment contract.

(v) Dividends on the stock certificates co-owned by clients will be distributed according to their respective shares and shall then be re-invested.

(vi) Stock certificates co-owned by clients shall be managed separately from the other shares and the ownership share of the clients and the dividends on their respective shares shall be managed by setting up an account for individual clients.

(11) The following shall be done for joint purchase cumulative investment of listed investment trust beneficiary certificates:

(i) A clause shall be included in a contract to the effect that listed investment trust beneficiary certificates can be jointly purchased with other clients applying for joint purchase in the form of cumulative investment.

In this case, a Financial Instruments Business Operator shall conclude a contract with a client in advance, specifying the name of the purchasing certificates, the amount of payment of the client per payment and date of execution of purchase, etc., and shall perform purchase operations in line with the said contract.

(ii) The minimum amount of payment of a client per payment shall be ¥10,000.

(iii) When the sum of payments, etc, of one client and others (or its integral multiple) reaches the purchase value of the listed investment trust beneficiary certificates, a Financial Instruments Business Operator shall buy the said certificates without delay.

(iv) In the case of (iii) above, when the sum of payments from one client and other clients is not sufficient enough for the purchase value of the listed investment trust beneficiary certificates, a Financial Instruments Business Operator shall keep the said fractional part until the next purchase, or shall buy the stock certificates by paying the difference between the purchase value of the minimum unit and the said amount.

(v) Clients (including a Financial Instruments Business Operator in the case of (iv) above where the Financial Instruments Business Operator has bought listed investment trust beneficiary certificates jointly with a client) shall acquire the ownership (co-ownership) of the purchased listed investment trust beneficiary certificates and hold ownership rights in accordance with the proportion of the paid amount (excluding the case above (iv) where a Financial Instruments Business Operator keeps the fractional part). The name of the listed investment trust beneficiary certificates purchased jointly among the said clients shall be the name of the Financial Instruments Business Operator. However, when a co-owner's share has reached a number of unit shares, the shares shall be divided into share units and the said units shall be excluded from the

application of the cumulative investment contract.

(vi) Dividends on the listed investment trust beneficiary certificates co-owned by clients will be distributed according to their respective shares and shall then be re-invested.

(vii) Listed investment trust beneficiary certificates co-owned by clients shall be managed separately from the other shares, and the ownership share of the clients and the dividends on their respective shares shall be managed by setting up an account for individual clients.

(12) The following shall be done for joint purchase cumulative investment of listed investment certificates:

(i) A clause shall be included in a contract to the effect that listed investment certificates can be jointly purchased with other clients applying for joint purchase in the form of cumulative investment.

In this case, a Financial Instruments Business Operator shall conclude a contract with a client in advance, specifying the name of the purchasing certificates, the amount of payment of the client per payment and date of execution of purchase, etc., and shall perform purchase operations in line with the said contract.

(ii) When the sum of payments, etc, of one client and other clients (or its integral multiple) reaches the purchase value of the listed investment certificates, a Financial Instruments Business Operator shall buy the said certificates without delay.

(iii) In the case of (ii) above, when the sum of payments from one client and other clients is not sufficient enough for the purchase value of the listed investment certificates, a Financial Instruments Business Operator shall keep the said fractional part until the next purchase, or shall buy the stock certificates by paying the difference between the purchase value of the minimum unit and the said amount.

(iv) Clients (including a Financial Instruments Business Operator in the case of (iii) above where the Financial Instruments Business Operator has bought listed investment certificates jointly with a client) shall acquire the ownership (co-ownership) of the purchased listed investment trust beneficiary certificates and hold ownership rights in accordance with the proportion of the paid amount (excluding the case of (iii) above where a Financial Instruments Business Operator keeps the fractional part). The name of the listed investment certificates purchased jointly among the said clients shall be the name of the Financial Instruments Business Operator. However, when a co-owner's share has reached a number of unit shares, the listed investment certificates shall be divided into share units by the record date as provided for in Article 77-3(2) of the Investment Trust and Investment Corporation Act (hereinafter referred to as "Investment Trust Act"), such as the first end of period of the issuing investment corporation of the said listed investment certificates, and the said units shall be excluded from the application of the cumulative investment contract.

(v) Dividends on the listed investment certificates co-owned by clients will be distributed according to their respective shares and shall then be re-invested.

(vi) Listed investment certificates co-owned by clients shall be managed separately from the other shares, and the ownership share of the clients and the dividends on their respective shares shall be managed by setting up an account for individual clients.

IV-4-3 Registration of Sales Representatives

(1) Scope of Registered Sales Representatives

Of Financial Instruments Business Operators' officers and employees engaging in in-branch business operations (including over-the-counter services), those who are in charge of any of the following operations need to be registered in the Registry of Sales Representatives specified under Article 64(1) of the FIEA.

(i) Explanations of the contents of financial instruments transactions for solicitation purposes

(ii) Solicitation for financial instruments transactions

(iii) Order-taking

(iv) Provision of information for solicitation purposes (excluding the provision of information regarding back-office operations and objective information requested by customers)

(v) Activities specified under Article 64(1)(i) and (ii) of the FIEA

(2) Items to be Notified

It should be kept in mind that the case of a sales representative who has ceased to engage in the specified sales representative operations temporarily, due to an intra-company personnel transfer shall not be deemed to fall under the provision of Article 64-4(iii) of the FIEA.

IV-4-4 Financial Instruments Transaction Liability Reserves

It should be kept in mind that a Financial Instruments Business Operator may withdraw funds from the financial instruments transaction liability reserves specified under Article 46-5 of the FIEA, only in cases where the following requirements are met:

(i) An illegal or inappropriate act by an officer or employee of the business operator has been recognized.

(ii) The amount of the withdrawn funds is appropriate and commensurate with the amount necessary to compensate the losses caused by the illegal or inappropriate act.

V. Supervisory Evaluation Points and Various Administrative Procedures (Type II Financial Instruments Business)

V-1 Governance (Type II Financial Instruments Business)

Supervisors shall pay attention to the following points when examining the governance of Financial Instruments Business Operators (limited to Type II Financial Instruments Business Operators; the same shall apply in V).

V-1-1 Officers of Financial Instruments Business Operators

(1) Major Supervisory Viewpoints

Whether the Financial Instruments Business Operator properly takes account of the following eligibility requirements in the decision-making process regarding proposals for the appointment of its officers:

(i) A person who does not meet any of the ineligibility criteria (Article 29-4(1)(ii)(a) to (g) of the FIEA) and who did not meet any of them at the time of registration.

(ii) A person who has not violated laws and regulations of the FIEA regarding financial instruments business or related business operations, or a person who has not been subjected to administrative actions taken based on laws and regulations.

(iii) A person who has not damaged the interests of investors in relation to the conduct of the investment advisory and agency business and the investment management business.

(iv) A person who has not engaged in an illegal or markedly inappropriate act, under particularly grave circumstances, regarding financial instruments business.

(2) Supervisory Method and Actions

In cases where an officer of a Financial Instruments Business Operator is deemed to meet the ineligibility criteria specified under any of Article 29-4(1)(ii)(a) to (g) of the FIEA, or is found to have done so at the time when the business operator obtained registration under Article 29 of the FIEA, or where an officer of a Financial Instruments Business Operator is deemed to meet the ineligibility criteria specified under any of Article 52(1)(vi) and (viii) and (ix) of the FIEA, supervisors shall consider taking actions such as ordering the dismissal of the said officer based on Article 52(2) of the FIEA.

In addition, they shall hold an in-depth hearing regarding the decision-making process concerning the proposal for the appointment of the said officer and, when necessary, require the submission of a report based on Article 56-2(1) of the FIEA. Furthermore, supervisors shall consider taking actions such as issuing an order for business improvement, if the Financial Instruments Business Operator’s control environment for governance is deemed to have a serious problem and the action is deemed to be necessary and appropriate from the viewpoint of protecting public interests and investors.

V-1-2 Adequate Staffing for Properly Conducting Financial Instruments Business

(1) Major Supervisory Viewpoints

Supervisors shall examine whether Financial Instruments Business Operators are adequately staffed to properly conduct financial instruments business (limited to Type II financial instruments business; the same shall apply to V), in light of the following requirements regarding Financial Instruments Business Operators' officers and employees.

(i) Financial instruments business operators should secure officers and employees who understand the viewpoints regarding governance that are specified under the FIEA and other relevant regulations as well as the supervisory guidelines, and who have the knowledge and experiences necessary for conducting governance as well as sufficient knowledge and experiences concerning compliance and risk management, to ensure the sound and appropriate execution of financial instruments business.

(ii) Officers and employees should not be current or former members of organized crime groups.

(iii) Officers and employees should not have close relationships with organized crime groups.

(iv) Officers and employees should not have the experience of being sentenced to a fine for violation of the FIEA or other domestic financial laws and regulations or foreign laws and regulations equivalent thereto.

(v) Officers and employees should not have the experience of being sentenced to imprisonment with work or more severe punishment (including similar punishments imposed under foreign laws or regulations equivalent thereto). (Particular attention should be paid to the case of an officer or employee being accused of committing crimes specified under Articles 246 to 250 of the Penal Code (fraud, fraud using computers, breach of trust, quasi fraud and extortion as well as attempts at these crimes).

(2) Supervisory Method and Actions

The requirements specified in (i) to (v) above are part of a comprehensive set of elements that should be taken into consideration when supervisors examine whether a Financial Instruments Business Operator is adequately staffed to properly conduct financial instruments business. Even if an officer or an employee is deemed to not meet the requirements, it should not automatically lead to the conclusion that the Financial Instruments Business Operator is not adequately staffed. The important thing is, first and foremost, that Financial Instruments Business Operators strive to ensure on their own responsibility that they are adequately staffed in light of those requirements and other elements.

However, supervisors shall hold in-depth hearings regarding the decision-making process concerning the proposed appointments of officers and employees, in cases where a Financial Instruments Business Operator is deemed to have failed to take those elements into consideration sufficiently in the said decision-making process, and where it is deemed to be necessary and appropriate to hold such hearings. In addition, they shall require the submission of reports based on Article 56-2(1) of the FIEA when necessary.

Supervisors shall consider taking actions such as issuing an order for business improvement under Article 51 of the FIEA in cases where the Financial Instruments Business Operator's control environment for governance is deemed to have a serious problem as a result of the examination of the submitted report, and where the action is deemed to be necessary and appropriate from the viewpoint of protecting public interests and investors.

Furthermore, when the Financial Instruments Business Operator is deemed to not be adequately staffed to properly conduct financial instruments business as a result of the examination of the submitted report, supervisors

shall consider taking necessary measures, including issuing an order for business suspension based on Article 52(1) of the FIEA.

It should be noted that if the Financial Instruments Business Operator is an individual person, supervisors shall examine the qualifications of the person from the above viewpoints, in order to judge whether the person is sufficiently qualified, and take necessary supervisory actions.

V-2 Appropriateness of Business Operations (Type II Financial Instruments Business)

V-2-1 Appropriateness of Business Operations Related to Securities Equivalents Sales Business

V-2-1-1 Control Environment for Customer Solicitation and Explanations

(1) Points of Attention Regarding Notification of Necessary Information Related to Delivery of Securities Equivalents and Other Matters

When securities equivalents sellers, etc., (business operators engaging in the activities specified under Article 28(2)(i) of the FIEA (hereinafter referred to as "self-offering companies") and business operators engaging in Article 28(1)(ii) of the FIEA (hereinafter referred to as "securities equivalent sellers") that do not fall under the category of business operators engaging in specially permitted businesses for qualified institutional investors) have failed to properly notify customers of the following items, the situation shall be deemed to fall under the category of "situations in which information necessary for customers with regard to the status of delivery and other matters regarding the customers' securities transactions is deemed not to have been properly provided," as specified under Article 123(viii) of the FIB Cabinet Office Ordinance.

(i) Items that must be specified in writing when a contract is signed under Article 37-4(1) of the FIEA must be notified to customers.

(ii) Items that must be specified in the report on the outstanding balance of transactions as specified under each item of Article 108(1) of the FIB Cabinet Office Ordinance.

(iii) In addition to the items described in (i) and (ii) above, items related to the delivery of cash and securities (excluding cases where the transaction does not involve the direct delivery of cash and securities between the customer and the Financial Instruments Business Operator, such as when the delivery of cash is made through a financial institution and when the delivery of securities is made through a transfer settlement.) must be notified to customers.

(2) Points of Attention Regarding Explanation of Important Items Related to Investment Trust Switching

In cases where a securities equivalents seller, etc., has failed to provide explanations regarding the following items related to investment trust switching, and where it has failed to establish an internal control system for compiling and storing records on its explanations and monitoring explanations, the situation shall be deemed to fall under the category of "situations in which explanations regarding important items related to switching have not been provided to customers in the solicitation for switching of investment trust beneficiary certificates, etc.," as specified under Article 123(ix) of the FIB Cabinet Office Ordinance."

(i) Form and status (e.g., name, characteristics) of investment trusts, etc.

(ii) Status (e.g., rough estimate of profit or loss) of investment trusts, etc., to be cancelled.

(iii) Expenses necessary for switching (e.g., cancellation and acquisition fees).

(iv) Items regarding preferential treatment for redemption switching.

(v) Other items that could affect customers' investment decisions in light of the characteristics of the relevant investment trust, etc., and the needs of the customers.

(3) Points of Attention Regarding Responsibility for Providing Explanations Concerning Funds

Article 2(2)(v) and (vi) comprehensively define collective investment schemes (funds) and the rights to interests therein. Business operators which conduct sales, solicitation, offering and private placement activities related to such rights may include those which were not subject to supervision by the authorities before the enforcement of the FIEA, and those which handle funds that lack sufficient transparency and liquidity to enable investors to identify and evaluate their actual state.

In light of this, in cases where a securities equivalents seller or a self-offering company handles such rights, supervisors shall pay attention to whether it provides investors with sufficient explanations regarding the key points of association contracts, businesses in which relevant funds are involved and risks regarding rights based on the contracts.

In particular, when the actual state of a securities equivalents seller's business fits the description of the Multilevel Marketing activities as specified under Article 33(1) of the Act on Specified Commercial Transactions, supervisors shall pay attention to whether appropriate explanations based on the same act and the FIEA are provided and, when necessary, take appropriate actions in cooperation with the Ministry of Economy, Trade and Industry and other relevant organizations. In addition, the supervisors shall pay attention to whether the case constitutes a violation of the Act on Prevention of Pyramid Schemes, and when a violation is suspected, take appropriate actions, such as providing information to police and other relevant organizations.

(4) Points of Attention Regarding Sale of Securitization Products (Assurance of Traceability of Securitization Products)

Securities equivalents sellers include business operators engaging in the activities specified under Article 28(2)(ii) of the FIEA with regard to the trust beneficiary rights as specified under Article 2(2)(i) and (ii) of the FIEA (hereinafter referred to as "trust beneficiary rights sellers). It is important that regarding securitization products (trust beneficiary rights) handled by trust beneficiary rights sellers, information related to the underlying assets is also properly communicated to investors. With this in mind, supervisors shall pay attention to the following points.

It should be noted that even if trust beneficiary rights sellers play only a limited role in transactions, such as acting as a sales agent, it is desirable that they provide support where possible as long as they deal with investors.

(i) Whether before selling securitization products, the trust beneficiary rights seller collects information regarding the contents of the underlying assets and the risks involved therein and conducts sufficient analysis to provide appropriate explanations.

(ii) Whether the trust beneficiary rights seller has established the internal procedures and rules necessary for providing information regarding the risks involved in the underlying assets and liquidity risks not reflected in credit ratings, rather than relying exclusively on credit ratings, when they sell securitization products.

(iii) Whether the trust beneficiary rights seller has established the internal procedures and rules necessary for providing information in ways that enable customers investing in securitization products to trace information regarding the contents of the underlying assets and the risks involved therein, if requested to do so by the investors.

(iv) Whether the trust beneficiary rights seller has developed a control environment for evaluating and calculating theoretical prices and quickly informing customers of them, even when it is difficult to determine market prices. Whether trust beneficiary rights sellers avoid evaluating and calculating theoretical prices in an arbitrary manner, so as to refrain from giving priority to promoting the arbitrary use of the information for specific purposes.

(5) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the control environment for customer solicitation and explanations of a securities equivalents seller, etc., through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the securities equivalents seller etc., by requiring the submission of reports based on Article 56-2(1) of the FIEA. When the securities equivalents seller, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the securities equivalents seller etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

V-2-1-2 Discretionary Trading Contracts, etc.

(1) Points of Attention Regarding Discretionary Trading Contracts with Foreign Securities Companies

When supervisors have received a notification for the signing of a contract based on Article 16(1)(viii)(b) of the Cabinet Office Ordinance Regarding Definitions, they shall pay attention to the following points:

(i) Whether the division that executes transactions regarding the said agreement is clearly separated from the divisions that receive and execute orders for other brokerage transactions.

(ii) Whether it is ensured that account documents are compiled in ways to enable the identification of transactions related to the said agreement.

(2) Scope of Specified Agreements by Securities Equivalents Sellers, etc.

Specified agreements as prescribed under Article 123(xiii)(b) and (c) of the FIB Cabinet Office Ordinance include the following agreements:

(i) Agreements regarding prices higher (in the case of sell orders) or lower (in the case of buy orders) than the specified prices (including prices determined with a prescribed method).

(ii) An appropriate range determined with a specified price as a base point.

(iii) Agreements regarding the determination of prices at the discretion of securities equivalents sellers, etc., on the condition that they follow the best execution practice (so-called CD order) in daily trading.

(iv) Targeting of prices determined through a prescribed method such as volume weighted averaging (so-called VWAP target order).

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the transactions, as specified under Article 123 (xiii)(a) to (e) of the FIB Cabinet Office Ordinance of a securities equivalents seller, etc., through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the securities equivalents seller, etc., by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the securities equivalents seller, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the securities equivalents seller. etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider taking necessary actions, including issuing an order for business suspension based on Article 52(1) of the FIEA.

V-2-1-3 Measures to Prevent Misrecognition

(1) Points of Attention Regarding Measures to Prevent Securities Equivalents Sellers, etc., from Being Misrecognized as Other Financial Institutions

When examining misrecognition prevention measures to be taken in cases where the headquarters or sales branches of a securities equivalent seller, etc., conducts business operations in the same building with another financial institution, supervisors shall pay attention to the following points, from the viewpoint of preventing customers from misrecognizing the said securities equivalents seller, etc., as the said financial institution.

(i) Whether the counters of the securities equivalents seller, etc., and the financial institution are separated, and the name of the securities equivalents seller, etc., is properly indicated, among other appropriate misrecognition prevention measures.

(ii) Whether the securities equivalents seller, etc., provides sufficient explanations regarding the following matters to customers:

A. The securities equivalents seller, etc., and the financial institution sharing the building are different corporations.

B. Products and services provided by the securities equivalents seller, etc., are different from those provided by the said financial institution.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding misrecognition prevention measures taken by a securities equivalents seller, etc., through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the securities equivalents seller, etc., by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2 (1) of the FIEA. When the securities equivalents seller, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the securities equivalents seller, etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including issuing an order for business suspension based on Article 52 (1) of the

FIEA.

V-2-2 Appropriateness of Business Operations Related to Market Derivatives Business Operators

V-2-2-1 Control Environment for Legal Compliance

If market derivatives business operators (business operators which engage in the activities specified under Article 28(2)(iii) of the FIEA; the same shall apply hereinafter) are to gain the trust of investors, thereby building trust in the derivatives trading market, it is important that they strive to manage their business operations in an appropriate manner while strictly complying with laws, regulations and various business rules, and fully recognizing their roles as derivatives market players.

Market derivatives business operators' control environments for legal compliance shall basically be examined based on the supervisory viewpoints and method specified in III-2-1. However, they shall also be examined in relation to a broad range of matters, including the status of compliance with voluntary regulatory rules established by self-regulatory organizations.

V-2-2-2 Control Environment for Customer Solicitation and Explanations

(1) Points of Attention Regarding Advertisements, etc.

(i) Whether the market derivatives business operator uses descriptions that could cause misunderstandings regarding domestic derivatives markets, for which it can act as a broker, and overseas derivatives markets.

(ii) In cases where losses exceeding the amount of cash margin and other deposits may arise due to rapid market movements despite the Loss-Cutting Rule, whether the market derivatives business operator properly indicates this risk in the advertisement.

(iii) Whether the market derivatives business operator has forced customers to continue attending seminars and similar events despite their expression of unwillingness to do so (including cases where it has effectively forced them to do so). It should be kept in mind that this kind of practice shall be deemed to meet the provision of Article 38(v) of the FIEA (known as "prohibition of re-solicitation").

(2) Points of Attention Regarding Explanation Documents

(i) The Explanation Documents as specified under Article 46-4 of the FIEA shall be kept ready to be made available any time for viewing by customers upon their request.

(ii) "The Key Points of the Status of Internal Control" shall describe specific arrangements and procedures for handling complaints and inquiries from customers and for conducting internal audits.

(iii) Supervisors shall check the date on which each market derivatives business operator installed the Explanations Documents at its branches.

(iv) Market derivatives business operators may, at their own discretion, include other items in addition to the items specified under law, in the Explanation Documents.

(3) Points of Attention Regarding Provision of Pre-Contract Documents

(i) The "reasons for the possibility of a loss exceeding the principal amount," as specified under Article

82(iv)(b) of the FIB Cabinet Office Ordinance shall include a rapid market movement that could cause a loss exceeding the principal amount despite the Loss-Cutting Rule.

(ii) The "reasons for the termination of the relevant financial instruments transaction contract," as specified under Article 82(viii) of the FIB Cabinet Office Ordinance shall include items related to the Loss-Cutting Rule.

(iii) The "types and calculation methods of cash margin and other deposits to be made by customers with regard to the relevant derivatives transactions, etc.," as specified under Article 93(1)(iv) of the FIB Cabinet Office Ordinance shall include items related to minimum margin deposits.

(iv) Regarding currency-related transactions, the "major terms and other basic items regarding derivatives trading," as specified under Article 93(1)(vii) of the FIB Cabinet Office Ordinance shall include items related to the method of determining prices of financial instruments, etc., and the Swap Point. In cases where the Swap Point may be either received or paid by customers and where a loss may arise, these possibilities shall be properly indicated.

(4) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a market derivatives business operator's control environment for customer solicitation and explanations, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the market derivatives business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the market derivatives business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the market derivatives business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

V-2-2-3 Discretionary Trading Contracts, etc.

(1) Points of Attention Regarding Discretionary Trading Contracts with Foreign Financial Futures Companies

When supervisors receive a notification from a market derivatives business operator for the signing of a contract based on Article 16(1)(viii)(b) of the Cabinet Office Ordinance Regarding Definitions, they shall pay attention to the following points:

(i) Whether the division that executes transactions regarding the said contract is clearly separated from the divisions that receive and execute orders for other brokerage transactions.

(ii) Whether it is ensured that account documents are compiled in ways to enable the identification of transactions related to the said contract.

(2) Scope of Specified Agreements by Market Derivatives Business Operators

Specified agreements under Article 123(xiii)(b) and (c) of the FIB Cabinet Office Ordinance include the

following agreements:

(i) Agreements regarding rewards and contracted values higher or lower than the specified rewards and contracted values (including rewards and contracted values determined with a prescribed method)

(ii) Agreements regarding an appropriate range determined with a specified reward or a contracted value as a base point.

(iii) Agreements regarding the determination of rewards and contracted values at the discretion of market derivatives business operators on the condition that they follow the best execution practice in daily trading.

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a market derivatives business operator's practices, as specified under Article 123(xiii)(a) to (e) of the FIB Cabinet Office Ordinance through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the market derivatives business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA, while paying consideration to the above viewpoints. When the market derivatives business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the market derivatives business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

V-3 Various Administrative Procedures (Type II Financial Instruments Business Operator)

V-3-1 Registration

(1) Items Regarding Examination of Staffing Level

When examining whether or not a market derivatives business operator is sufficiently staffed to properly conduct the financial instruments business, as specified under Article 29-4(1)(i)(d) of the FIEA, supervisors shall check the following points based on its application and attachments thereto as well as hearings.

(i) Whether it can be deemed that officers and employees with sufficient knowledge and experience have been secured, and a sufficient organization has been established to conduct the relevant financial instruments business, in light of the following requirements:

A. Top-level managers must be sufficiently qualified to conduct financial instruments business in a fair and appropriate manner, in terms of their backgrounds and capabilities.

B. Managing directors must understand the viewpoints regarding governance indicated in the FIEA and various other laws and regulations, and have sufficient knowledge and experience to conduct governance, and sufficient knowledge and experience regarding compliance and risk management to conduct financial instruments business in a fair and appropriate manner.

C. The market derivatives business operator must be staffed and organized so that personnel necessary for conducting business in an appropriate manner are allocated to individual divisions, and managers in charge of internal control are appropriately allocated.

D. The compliance division (staff in charge of compliance) should be independent from the sales division and staffed with personnel with necessary knowledge and experience.

E. Staff capable of conducting the following processes should be secured, with regard to the relevant business.

a. Compilation and management of account documents, reports and other documents.

b. Disclosure

c. Risk Management

d. Computer system management

e. Trading management, customer management

f. Advertisement screening

g. Customer information management

h. Processing of complaints and resolution of disputes

i. Internal audits

(ii) When the qualifications of employees and officers are examined in a comprehensive manner in relation to the following criteria regarding organized crime groups, their members and financial crimes, whether there is the risk that public confidence in the financial instruments business could be damaged because of the inclusion of officers and employees with inappropriate qualifications among its staff.

A. Officers and employees should not be current or former members of organized crime groups.

B. Officers and employees should not have close relationships with organized crime groups.

C. Officers and employees should not have the experience of being sentenced to a fine for violation of the FIEA or other domestic financial laws and regulations or foreign laws and regulations equivalent thereto.

D. Officers and employees should not have the experience of being sentenced to imprisonment with work or more severe punishment (including similar punishments imposed under foreign laws or regulations equivalent thereto). (Particular attention should be paid to the case of an officer or employee being accused of committing crimes specified under Articles 246 to 250 of the Penal Code (fraud, fraud using computers, breach of trust, quasi fraud and extortion as well as attempts at these crimes).

(Note) If the Financial Instruments Business Operator is an individual, the qualifications of the individual shall be examined in light of the items specified in (i) and (ii) above

V-3-2 Registration of Sales Representatives

(1) Scope of Registered Sales Representatives

Of Financial Instruments Business Operators' (limited to market derivatives business operators; the same shall apply in V-3-2) officers and employees engaging in in-branch business operations, (including over-the-counter services), those who are in charge of any of the following operations need to be registered in the Registry of Sales Representatives specified under Article 64(1) of the FIEA.

(i) Explanations of the contents of financial instruments transactions for solicitation purposes

(ii) Solicitation for financial instruments transactions

(iii) Order-taking

(iv) Provision of information for solicitation purposes (excluding the provision of information regarding back-office operations and objective information requested by customers)

(v) Activities specified under Article 64(1)(iii) of the FIEA

(2) Items to be Notified

It should be kept in mind that the case of a sales representative who has ceased to engage in the specified sales representative operations temporarily, due to an intra-company personnel transfer, shall not be deemed to fall under the provision of Article 64-4(iii) of the FIEA.

V-3-3 Points of Attention Regarding Depositing of Deposits for Operation

(1) When supervisors have received the original of a statement of deposit submitted by a Financial Instruments Business Operator after it has deposited a new deposit for operation in order to replace the existing deposit, they shall implement the procedures for the certification of the return of the original of the statement of deposit in their custody, in accordance with the format specified in the Attached List of Formats V-I and return it the Financial Instruments Business Operator.

(2) When supervisors have received the original of a certificate of receipt submitted by a Financial Instruments

Business Operator after it has submitted a request for substitute deposit/additional deposit in order to substitute redemption funds for deposited securities, they shall provide a certificate of custody in accordance with (5) below and return the original of the statement of deposit already in their custody to the Financial Instruments Business Operator.

(3) When supervisors have received an application for a revision of the contents of a substitute contract for a deposit for operation or for the cancellation of such a contract, they shall grant approval in the approval form regarding deposit contract revision, as specified in the Attached List of Formats V-2, and in the approval form regarding deposit contract cancellation, as specified in the Attached List of Formats V-3, if it is deemed that the revision/cancellation does not lead to insufficient protection of investors.

(4) The public notification of the retrieval of deposits for operation shall be made in the format specified in the Attached List of Formats V-4.

(5) When supervisors have received the original of a statement of deposit, they shall provide a certificate of custody in the format specified in the Attached List of Formats V-5.

(6) Supervisors shall ensure that all applicants for registration are aware of the possibility that in cases where government bonds are deposited as deposits for operation based on Article 31-2(9) of the FIEA, deposits could become invalid after a certain period of time, due to the statute of limitations under the Act Concerning Government Bonds.

VI. Supervisory Evaluation Points and Various Administrative Procedures (Investment Management Business)

VI-1 Governance (Investment Management Business)

Supervisors shall pay attention to the following points when examining the governance of Financial Instruments Business Operators (limited to business operators engaging in investment management business; the same shall apply in VI).

VI-1-1 Officers of Financial Instruments Business Operators

(1) Major Supervisory Viewpoints

Whether the Financial Instruments Business Operator properly takes account of the following eligibility requirements in the decision-making process regarding proposals for the appointment of its officers.

(i) A person who does not meet any of the ineligibility criteria (Article 29-4(1)(ii)(a) to (g) of the FIEA) and who did not meet any of them at the time of registration.

(ii) A person who has not violated laws and regulations regarding financial instruments business or related business operations, or a person who has not been subjected to administrative actions taken based on laws and regulations.

(iii) A person who has not damaged the interests of investors in relation to the conduct of the investment advisory and agency business and the investment management business.

(iv) A person who has not engaged in an illegal or markedly inappropriate act regarding financial instruments business under particularly grave circumstances.

(2) Supervisory Method and Actions

In cases where an officer of a Financial Instruments Business Operator is deemed to meet the ineligibility criteria specified under any of Article 29-4(1)(ii)(a) to (g) of the FIEA or is found to have done so at the time when the business operator obtained registration under Article 29 of the FIEA, or where an officer of a Financial Instruments Business Operator is deemed to meet the ineligibility criteria specified under any of Article 52(1)(vi) and (viii) and (ix) of the FIEA, supervisors shall consider taking actions such as ordering the dismissal of the said officer based on Article 52(2) of the FIEA.

In addition, they shall hold an in-depth hearing regarding the decision-making process concerning the proposal for the appointment of the said officer and, when necessary, require the submission of a report based on Article 56-2(1) of the FIEA. Furthermore, supervisors shall consider taking actions such as issuing an order for business improvement, if the Financial Instruments Business Operator's control environment for governance is deemed to have a serious problem and the action is deemed to be necessary and appropriate from the viewpoint of protecting public interests and investors.

VI-1-2 Adequate Staffing for Properly Conducting Financial Instruments Business

(1) Major Supervisory Viewpoints

Supervisors shall examine whether Financial Instruments Business Operators are adequately staffed to properly conduct financial instruments business (limited to investment management business; the same shall apply to VI) in light of the following requirements regarding Financial Instruments Business Operators' officers and employees.

(i) Financial instruments business operators should secure officers and employees who understand the viewpoints regarding governance that are specified under the FIEA and other relevant regulations as well as the supervisory guidelines, and who have the knowledge and experience necessary for conducting governance as well as sufficient knowledge and experience concerning compliance and risk management to ensure the sound and appropriate execution of financial instruments business.

(ii) Officers and employees should not be current or former members of organized crime groups.

(iii) Officers and employees should not have close relationships with organized crime groups.

(iv) Officers and employees should not have the experience of being sentenced to a fine for violation of the FIEA or other domestic financial laws and regulations, or foreign laws and regulations equivalent thereto.

(v) Officers and employees should not have the experience of being sentenced to imprisonment with work or more severe punishment (including similar punishments imposed under foreign laws or regulations equivalent thereto). (Particular attention should be paid to the case of an officer or employee being accused of committing crimes specified under Articles 246 to 250 of the Penal Code (fraud, fraud using computers, breach of trust, quasi fraud and extortion, as well as attempts at these crimes).)

(2) Supervisory Method and Actions

The requirements specified in (i) to (v) above are part of a comprehensive set of elements that supervisors should take into consideration when examining whether a Financial Instruments Business Operator is adequately staffed to properly conduct financial instruments business. Even if an officer or an employee is deemed to not meet the requirements, it should not automatically lead to the conclusion that the Financial Instruments Business Operator is not adequately staffed. The important thing is, first and foremost, that Financial Instruments Business Operators strive to ensure on their own responsibility that they are adequately staffed in light of these requirements and other elements.

However, supervisors shall hold in-depth hearings regarding the decision-making process concerning the proposed appointments of officers and employees, in cases where a Financial Instruments Business Operator is deemed to have failed to take those elements into consideration sufficiently in the said decision-making process and where it is deemed to be necessary and appropriate to hold such hearings. In addition, they shall require the submission of reports based on Article 56-2(1) of the FIEA when necessary.

Supervisors shall consider taking actions such as issuing an order for business improvement under Article 51 of the FIEA, in cases where the Financial Instruments Business Operator's control environment for governance is deemed to have a serious problem as a result of the examination of the submitted report, and where the action is deemed to be necessary and appropriate from the viewpoint of protecting public interests and investors.

Furthermore, when the Financial Instruments Business Operator is deemed to be not adequately staffed to properly conduct financial instruments business as a result of the examination of the submitted report, supervisors

shall consider taking necessary measures, including issuing an order for business suspension based on Article 52(1) of the FIEA.

VI-2 Appropriateness of Business Operations (Investment Management Business)

VI-2-1 Control Environment for Legal Compliance

Financial instruments business operators, which play an important role in investors' investment management, have fiduciary duty to the investors who entrust investment to them, and are required to fulfill the duty of loyalty, the duty of due care, and the responsibility for ensuring segregated management under the FIEA. In addition, they are required to conduct their business operations as market players in a sound and appropriate manner.

Their control environments for legal compliance shall basically be examined based on the supervisory viewpoints and method specified in III-2-1. However, they shall also be examined in relation to a broad range of matters, including the status of compliance with voluntary regulatory rules.

VI-2-2 Appropriateness of Business Operations Related to Discretionary Investment Business

Supervisors shall examine the appropriateness of the business operations of discretionary investment business operators (business operators engaging in the activities specified under Article 2(8)(xii)(b) of the FIEA under discretional investment contracts (as specified under the same provision; the same shall apply hereinafter); the same shall apply hereinafter) by paying attention to the following points.

VI-2-2-1 Control Environment for Business Execution

(1) Investment and Administration of Investment Assets

Supervisors shall examine whether a discretionary investment business operator is properly investing and administering investment assets, by paying attention to the following points. It should be noted that the following points should be taken into consideration in a comprehensive manner in light of the nature and size of the business operator's business, and that failure to meet some of the criteria should not automatically be deemed to mean that the investment of investment assets is inappropriate.

(i) Whether the discretionary investment business operator has properly specified the matters regarding internal organization that decide its investment policy (including a specific decision-making process).

(ii) Whether the discretionary investment business operator has prescribed a specific investment method for investment of investment assets (as specified under Article 35(1)(xv) of the FIEA; the same shall apply hereinafter) by the investment division.

(iii) Whether the discretionary investment business operator has developed an appropriate control environment for the management of securities transactions between various investment assets and between investment assets and its own assets or third-party assets.

(iv) In cases where the discretionary investment business operator entrusts all or part of the authority over the investment made on behalf of rights holders (as specified under Article 42(1) of the FIEA; the same shall apply hereinafter) to another entity under Article 42-3 of the FIEA (including cases where the entrusted entity entrusts part of the authority to yet another entity), whether the discretionary investment business operator has properly established the criteria for selecting the entity to which the authority is entrusted and the method of communications therewith. Whether the discretionary investment business operator has developed a

control environment for continuously examining the entrusted entity's business execution capability and its compliance with contract provisions. Whether it has specified measures to be taken when a problem is found in the entrusted entity's business execution capability (e.g., providing guidance for business improvement and refusing to renew the entrustment contract).

(v) Regarding the selection of the entities to which orders are placed and business operations are entrusted, whether the discretionary investment business operator has properly specified the matters concerning the entities' transaction execution capability, the control environment for legal compliance, credit risk and trading costs as items that should be taken into consideration.

(vi) Whether the discretionary investment business operator has arrangements and procedures for a division independent from the investment division to periodically examine whether investment assets are properly managed, including whether the investment decision process is appropriate, in accordance with the discretionary investment contract and the investment guideline (including whether records on the investment status are stored).

(2) Execution of Transactions

When discretionary investment business operators execute transactions, they are required to select the transaction form that benefits customers most, by taking into consideration the transaction price and other execution costs in a comprehensive manner. In light of the increasing diversification of the transaction forms due to the advance of financial techniques, supervisors shall examine the status of a discretional investment business operator's transaction execution by paying attention to the following points, for example:

(i) At-Average-Price Transaction (transaction made at the average of prices of various orders of the same transaction and delivery dates, aggregated by issue and order category (sell or purchase))

A. Separation of Divisions

Whether the discretionary investment business operator has separate divisions for making investment divisions and for taking orders. In cases where organizational separation is difficult, whether, at the minimum, different persons are responsible for these two tasks.

B. Examination of Transactions

Whether the discretionary investment business operator has a control environment for ensuring that a relevant management division, for example, examines the whole range of business processes related to at-average-price transactions.

C. Disclosure to Customers and Consent Thereof

Whether the discretionary investment business operator makes at-average-price transactions after making prior disclosure to customers and obtaining their consent. In cases where the discretionary investment business operator places orders involving the proportional allocation of executed transactions with regard to two or more investment asset accounts, whether it provides customers with appropriate explanations regarding the criteria for allocation in the case of the total executed transaction volume falling short of the total order volume.

(ii) Transactions Made via Bulk Orders

In cases where the discretionary investment business operator places a bulk sell or buy order for the

same issue on behalf of two or more investment asset accounts, and allocates executed transactions to each asset account based on the allocation criteria prescribed by the business operator after aggregating the transactions by issue and by buy/sell order, whether it has developed a control environment similar to the one described in (i) above, from the viewpoint of ensuring fairness among customers.

(iii) Transactions Made between Investment Asset Accounts

Whether the discretionary investment business operator has a control environment for ensuring that a relevant management division, for example, properly examines the transactions specified under Article 129(1)(i) of the FIB Cabinet Office Ordinance (non-application of the prohibition of transactions between investment assets accounts).The "case where it is deemed to be necessary and rational," as specified by Article 129(1)(i)(a)(4) of the FIB Cabinet Office Ordinance is a case where because of the need to ensure fairness among customers and fulfill its duties of best execution and loyalty to customers, a discretionary investment business operator seeks to ensure fair price formation, while taking care to exclude arbitrariness regarding transactions between different funds by using the following methods, for example:

A. To have traders execute transactions based on investment decisions made by several fund managers (limited to transactions regarding which there is not the risk of the price formation process being distorted in light of liquidity and other factors related to the relevant issue and, in cases where the transactions are executed by the same trader, transactions of which the trader has no discretion over execution).

B. To place both market buy and sell orders before the market's opening (limited to orders which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

C. To place both buy and sell orders in intraday trading at a reasonable intervals (limited to orders which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

D. To make transactions related to index funds executed through program trading based on contracts and trust contract provisions (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

E. To make VWAP transactions and discretionary transactions, regarding which the decision on the timing of order placement, price and other execution terms related to individual issues are entrusted by the fund management company to a third-party entity (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

F. To make futures transactions, regarding which it is difficult to avoid the placement of orders for the same issue because of the small number of issues available for futures trading (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a discretionary investment

business operator's control environment for business execution, through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the discretionary investment business operator by requiring the submission of reports based on Article 56-2(1) of the FIEA. When the discretionary investment business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the discretionary investment business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

VI-2-2-2 Control Environment for Customer Solicitation and Explanations

(1) Prohibition of Advertisements Using Exaggerated Descriptions

(i) Whether the Financial Instruments Business Operator includes in its advertisements descriptions indicating that the performance, contents and method of its investment are markedly superior to those of other Financial Instruments Business Operators without providing the basis therefor.

(ii) When including investment performance data in its advertisement, whether the Financial Instruments Business Operator uses descriptions that could cause misunderstanding by investors, by putting excessive emphasis on specific parts of the performance. (When investment performance data is included in an advertisement, appropriate and easy-to-understand descriptions must be made, from the viewpoint of protecting investors. For example, it is necessary to examine whether the advertisement specifies the method of investment evaluation and the basis for the use of benchmarks and properly expresses that the investment performance data is an indicator that concerns past results but does not promise future performance.)

(iii) When including investment simulation in its advertisement, whether the Financial Instruments Business Operator uses descriptions that could cause misunderstanding by investors, by setting arbitrary assumptions, for example. (When investment simulation is included in an advertisement, appropriate and easy-to-understand descriptions must be used, from the viewpoint of protecting investors. For example, it is necessary to examine whether the advertisement specifies the basis for the use of assumptions in the simulation and properly indicates that the simulation is based on prescribed assumptions and does not promise future investment performance.)

(2) Points of Attention Regarding Provision of Pre-Contract Documents

(i) In cases where a discretionary investment business operator concurrently undertakes services unrelated to discretionary investment business and where it receives remuneration related to discretionary investment business and fees related to other services collectively under the same contract, the business operator must separately specify the remuneration related to discretionary investment business and the fees related to other services with regard to the "matters concerning fees, remuneration or any other consideration payable by the customer with regard to said Contract for Financial Instruments Transaction," as specified under Article 37-3(1)(iv) of the FIEA.

(ii) The "methods of investment and types of transactions," as specified under Article 96(1)(i) of the FIB

Cabinet Office Ordinance, include specific investment methods (including the individual investment method, the common investment method (under which several customers' assets are invested in the same way with regard to specific securities and the timing of sales and purchases and are administered on a customer-by-customer basis by the same asset administration organization; the same shall apply hereinafter) and the joint investment method (under which several customers' assets are jointly invested and jointly administered; the same shall apply hereinafter)) and also include the following items in the case of common investment and joint investment:

A. In the case of common investment
   a. Items regarding the asset administration organization in charge of common investment assets.
   b. Items regarding the criteria for the allocation of assets acquired through the common investment

B. In the case of joint investment
   a. Customers' attributes and types of customer assets and items regarding the criteria for joint investment
   b. Items regarding the asset administration organization in charge of joint investment assets
   c. Items regarding the criteria for the allocation of assets acquired through the joint investment
   d. Items regarding the evaluation method of joint investment assets and the calculation method of each customer's interests in the assets (including cases where assets are withdrawn from the joint investment prematurely).

(iii) The "items regarding the scope of discretionary investment decisions and the implementation of investment," as specified under Article 96(1)(iii) of the FIB Cabinet Office Ordinance, include the trade names, addresses, the names of the representative of the business operators specified under each item of Article 16-12 of the FIEA Enforcement Order (hereinafter referred to as "re-entrusted entity") as well as the scope of re-entrustment.

(3) Points of Attention Regarding the Provision of Documents at Contract Signing

(i) In the case of joint investment, the "contents and amounts of customers' assets related to discretionary investment contracts," as specified under Article 107(1)(vi) of the FIB Cabinet Office Ordinance, include the total amount of joint investment assets at the time of the start of the joint investment and the shares of the relevant customers' assets in the joint investment assets.

(ii) The "methods of investment and types of transactions," as specified under Article 107(1)(viii) of the FIB Cabinet Office Ordinance, include specific investment methods (including the individual investment method, the common investment method and the joint investment method) and also include the following items in the case of common investment and joint investment:

A. In the case of common investment
   a. Items regarding the asset administration organization in charge of common investment assets
   b. Items regarding the criteria for the allocation of assets acquired through the common investment

B. In the case of joint investment
   a. Items regarding the size of joint investment assets
   b. Customers' attributes and types of customer assets and items regarding the criteria for joint

investment

c. Items regarding the asset administration organization in charge of joint investment assets
d. Items regarding the criteria for the allocation of assets acquired through the joint investment
e. Items regarding the evaluation method of join investment assets and the calculation method of each customer's interests in the assets (including cases where assets are withdrawn from the joint investment prematurely).

(iii) The "methods of investment and types of transactions," as specified under Article 107(1)(viii) of the FIB Cabinet Office Ordinance, include re-entrusted entities' methods of investment and types of transaction.

(4) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a discretionary investment business operator's control environment for customer solicitation and explanations, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the discretionary investment business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the discretionary investment business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the discretionary investment business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-2-3 Duty of Loyalty and Measures to Prevent Internal Collusion

(1) Points of Attention Regarding Discretionary Investment Business Operators Engaging in Two or More Types of Business

When supervisors examine the appropriateness of measures taken by a discretionary investment business operator engaging in two or more types of business (as specified under Article 29-2(1)(v) of the FIEA) to prevent internal collusion, they shall pay attention to the following points, for example, depending on the nature of its business, from the viewpoint of preventing conflicts of interests and ensuring the appropriateness of business operations in other ways.

(i) Whether the discretionary investment business operator has taken appropriate measures to prevent collusion between its different types of business, such as establishing an internal control system and procedures for the prevention of such collusion in a manner suited to the nature of its business.

(ii) Regarding the "non-disclosure information," as specified under Article 147(ii) of the FIB Cabinet Office Ordinance, whether the discretionary investment business operator has put in place information management measures, such as the appointment of the relevant manager and the establishment of management rules, and ensures the effectiveness of information management by, for example, properly identifying and examining the status of the usage of the non-disclosure information and revising the management method as necessary.

(2) Points of Attention Regarding Prevention of Conflicts of Interests in Investment Management Business

Whether appropriate measures have been taken to prevent practices that could promote the interests of specific rights holders at the expense of other rights holders, such as establishing an internal control system and procedures for the prevention of collusion between different types of business in a manner suited to the nature of the business.

(3) Duty of Loyalty to Rights Holders

It should be kept in mind that if a discretionary investment business operator causes financial damage to a beneficiary due to a clerical error involved in the investment of investment assets and fails to compensate for the damage, it could constitute a violation of the duty of loyalty. The same shall apply to cases where the clerical error occurs at an entity to which business operations are entrusted and where the discretionary investment business operator which has the obligation of duty to the beneficiary fails to compensate for the damage.

(4) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a discretionary investment business operator's measures to prevent internal collusion between different types of business, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the discretionary investment business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA, since such an issue could directly undermine the interests of rights holders and, in some cases, lead to legal violations, such as a violation of the duty of loyalty and duty of due care. When the discretionary investment business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the discretionary investment business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-2-4 Measures to Prevent Legal Violations by Agency/Brokerage Service Providers

When discretionary investment business operators entrust business operations to agency/brokerage service providers (business operators engaging in agency/brokerage services (as specified under Article 2(8)(xiii); the same shall apply hereinafter); the same shall apply hereinafter), it is important that they provide the service providers with guidance regarding the establishment of a control environment for customer management, from the viewpoint of ensuring the implementation of appropriate investment solicitation suited to the customers' attributes, and require them to ensure thorough legal compliance based on the examination of the actual status of their investment solicitation. Supervisors shall examine the control environment for the prevention of legal violations by agency/brokerage service providers by paying attention to the following points in particular.

VI-2-2-4-1 Selection of Agency/Brokerage Service Providers

(1) Points of Attention Regarding Selection of Agency/Brokerage Service Providers

(i) When signing contracts for entrusting agency/brokerage services, whether the discretionary investment business operator specifies the significance of the entrustment in relation to governance, identifies the various risks involved therein and conducts sufficient deliberations on the method of risk management.

(ii) Whether the discretionary investment business operator conducts sufficient deliberations on whether the agency/brokerage service providers have sufficient qualifications to conduct the entrusted business operations in a sound and appropriate manner. In cases where the agency/brokerage service providers concurrently engage in other services in particular, whether the discretionary investment business operator not only examines the possibility of the nature of the other services damaging public confidence in the service providers, but also conducts sufficient deliberations in consideration of the primary business operator's reputational risk. (The "primary business operator" refers to discretionary investment business operators which sign discretionary investment contracts through agency/brokerage services provided by agency/brokerage service providers; the same shall apply in VI.)

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the primary business operator's selection of agency/brokerage service providers, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the primary business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the primary business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the primary business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-2-4-2 Measures Taken by Primary Business Operator to Ensure the Appropriateness of Agency/Brokerage Service Providers

(1) Development of Internal Control Environment for Supervising Agency/Brokerage Service Providers

(i) Whether the primary business operator has developed a control environment for ensuring appropriate supervision of agency/brokerage service providers, through actions such as establishing a division responsible for the implementation of measures to ensure the sound and appropriate conduct of business operations related to agency/brokerage services, or appointing a person responsible therefor (including a control environment regarding audits of the business operations of agency/brokerage service providers).

(ii) Whether the primary business operator has developed an internal control environment for examining whether the said division or person has taken proper measures to ensure the appropriateness of the business operations related to the agency/brokerage services.

(2) Points of Attention Regarding Measures to Ensure Necessary and Appropriate Supervision of Agency/Brokerage Service Providers

(i) Whether the primary business operator has taken the following measures in order to ensure the sound and appropriate conduct of business operations related to agency/brokerage services and monitors the status of the conduct of the business operations:

A. To provide guidance regarding business operations related to agency/brokerage services to brokerage service providers and their employees and implement training programs intended to ensure their compliance with laws and regulations regarding the agency/brokerage services.

B. To implement measures to ensure the necessary and appropriate supervision of agency/brokerage service providers, such as examining periodically or as necessary whether the service providers properly conduct the services, including investment solicitation and requiring them to make improvement when necessary.

(ii) Whether the primary business operator has developed a control environment that ensures the results of the above monitoring are examined by the primary business operator's division in charge and reported to the management team when necessary, so that they are reflected in the provision of appropriate guidance by the primary business operator and in the conduct of business operations by agency/brokerage service providers.

(3) Measures to Cancel Contracts for Entrusting Agency/Brokerage Services

Whether the primary business operator has developed a control environment for implementing appropriate measures, such as providing guidance to agency/brokerage service providers and canceling contracts for entrusting agency/brokerage services, when a problem has been found as a result of the monitoring of agency/brokerage service providers. In addition, whether it has developed a control environment for properly protecting customers when canceling the entrustment contracts.

(4) Measures to Process Complaints

Whether the primary business operator has established arrangements and procedures for responding to complaints, such as specifying the contact point for customer complaints regarding agency/brokerage services, establishing a division in charge of processing complaints and prescribing procedures for processing complaints.

(5) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding measures taken by the primary business operator to ensure the appropriateness of agency/brokerage services, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the primary business operator etc., by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the primary business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the primary business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-2-5 Other Points of Attention

(1) Accounts for Settlement of Transactions

(i) It should be kept in mind that regarding transactions made on their own account, discretionary investment business operators must not use an account intended for the settlement of transactions that was made through the activities specified under the proviso of Article 42-5 of the FIEA.

(ii) It should be kept in mind that discretionary investment business operators' use of the said account for placing orders covering both transactions related to investment based on investment decisions commissioned by customers and transactions made on their own account is equivalent to the "use of the relevant account for purposes other than the settlement of the relevant transaction" specified under Article 130(1)(xi) of the FIB Cabinet Office Ordinance.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a discretionary investment business operator's accounts for the settlement of transactions, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the discretionary investment business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the discretionary investment business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the discretionary investment business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

(3) Interpretation of Article 2(8)(xii)(b)

The contracts specified under Article 123(xiii)(b) to (e) of the FIB Cabinet Office Ordinance shall not be deemed to fall under the category of discretionary investment contracts specified under Article 2(8)(xii)(b).

VI-2-3 Appropriateness of Business Operations Related to Investment Trust Management Business, etc.

Supervisors shall examine the appropriateness of the business operations of investment trust management companies, etc. (Financial Instruments Business Operators engaging in the activities specified under Article 2(8)(xii)(a) of the FIEA and based on contracts specified under the same provision and the activities specified in Article 2(8)(xiv); the same shall apply hereinafter) by paying attention to the following points.

VI-2-3-1 Control Environment for Business Execution

(1) Investment and Administration of Investment Assets

Supervisors shall examine whether an investment trust management company, etc., is properly managing and administering investment assets, by paying attention to the following points. It should be noted that the following points should be taken into consideration in a comprehensive manner in light of the nature and size of the

company's business and that failure to meet some of the criteria should not automatically be deemed to mean that the investment and administration of investment assets are inappropriate.

(i) Whether the investment trust management company, etc., has properly specified the matters regarding internal organization that decide its investment policy (including a specific decision-making process).

(ii) Whether the investment trust management company, etc., has prescribed a specific investment method for investment of investment assets by the investment division.

(iii) Whether the investment trust management company, etc., has developed an appropriate control environment regarding the management of securities transactions between various investment assets and between investment assets and its own assets or third-party assets.

(iv) In cases where the investment trust management company entrusts all or part of the authority over the investment made on behalf of rights holders to another entity under Article 42-3 of the FIEA (including cases where the entrusted entity entrusts part of the authority to yet another entity), whether the investment trust management company has properly established the criteria for selecting the entity to which the authority is entrusted and the method of communications therewith. Whether the investment trust management company has established arrangements and procedures for continuously examining the entrusted entity's business execution capability and its compliance with contract provisions. Whether it has specified measures to be taken when a problem is found in the entrusted entity's business execution capability (e.g., providing guidance for business improvement and refusing to renew the entrustment contract).

(v) Regarding the selection of the entities to which orders are placed and business operations are entrusted, whether the investment trust management company, etc., has properly specified the matters concerning the entities' transaction execution capability, control environment for legal compliance, credit risk and trading costs as items that should be taken into consideration.

(vi) Whether the investment trust management company, etc., has arrangements and procedures for a division independent from the investment division to periodically examine whether investment assets are properly invested (including whether records on the investment status are stored), including whether the investment decision process is appropriate, in accordance with investment trust contracts and asset investment contracts and the investment guideline.

(2) Execution of Transactions

When investment trust management companies, etc., execute transactions, they are required to select the transaction form that benefits rights holders most by taking into consideration the transaction price and other execution costs in a comprehensive manner. In light of the increasing diversification of the transaction forms due to the advance of financial techniques, supervisors shall examine the status of the transaction execution of an investment trust management company, etc., by paying attention to the following points, for example:

(i) At-Average-Price Transaction (transaction made at the average of prices of various orders of the same transaction and delivery dates, aggregated by issue and order category (sell or buy))

A. Separation of Divisions

Whether the investment trust management company, etc., has separate divisions for making investment divisions and for taking orders. In cases where organizational separation is difficult,

whether, at the minimum, different persons are responsible for these two tasks.

B. Examination of Transactions

Whether the investment trust management company, etc., has a control environment for ensuring that a relevant management division, for example, examines the whole range of business processes related to at-average-price transactions.

C. Disclosure to Rights Holders and Consent thereof (Limited to Transactions Related to Asset Investment Contracts with Investment Corporations)

Whether the investment trust management company, etc., makes at-average-price transactions after making prior disclosure to rights holders and obtaining their consent. In cases where the investment trust management company, etc., places orders involving proportional allocation of the executed transactions with regard to two or more investment asset accounts, whether it provides rights holders with appropriate explanations regarding the criteria for allocation in the case of the total executed transaction volume falling short of the total order volume.

(ii) Transactions Made via Bulk Orders

In cases where the investment trust management company, etc., places a bulk sell or buy order for the same issue on behalf of two or more investment asset accounts, and allocates the executed transactions to each asset account based on the allocation criteria prescribed by the business operator after aggregating the transactions by issue and by buy/sell order, whether it has developed a control environment similar to the one described in (i) above from the viewpoint of ensuring fairness among various investment assets.

(iii) Transactions Made between Investment Assets Accounts

Whether the investment trust management company, etc., has a control environment for ensuring that a relevant management division, for example, properly examines the transactions specified under Article 129(1)(i) of the FIB Cabinet Office Ordinance (non-application of the prohibition of transactions between investment assets accounts). The “case where it is deemed to be necessary and rational,” as specified by Article 129(1)(i)(a)(4) of the FIB Cabinet Office Ordinance, is a case where because of the need to ensure fairness among customers and fulfill its duties of best execution and loyalty to customers, an investment trust management company, etc., seeks to ensure a fair price formation, while taking care to exclude arbitrariness regarding transactions between different funds with the following methods, for example:

A. To have traders execute transactions based on investment decisions made by several fund managers (limited to transactions regarding which there is not the risk of the price formation process being distorted in light of liquidity and other factors related to the relevant issue and, in cases where the transactions are executed by the same trader, the trader has no discretion over execution).

B. To place both market buy and sell orders before the market’s opening (limited to orders which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

C. To place both buy and sell orders in intraday trading at a reasonable interval (limited to orders which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

D. To make transactions related to index funds executed through program trading based on contracts and

trust contract provisions (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

E. To make VWAP transactions and discretionary transactions, regarding which the decision on the timing of order placement, price and other execution terms related to individual issues are entrusted by the investment trust management company, etc., to a third-party entity (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

F. To make futures transactions, regarding which it is difficult to avoid the placement of orders for the same issue because of the small number of issues available for futures trading (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the control environment for business execution of an investment trust management company, etc., through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the investment trust management company, etc., by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the investment trust management company, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the investment trust management company, etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-3-2 Control Environment for Customer Solicitation and Explanations for Beneficiaries, etc.

(1) Prohibition of Advertisements Using Exaggerated Descriptions

(i) Whether the investment trust management company, etc., includes in its advertisements descriptions indicating that the performance, contents and method of its investment are markedly superior to those of other Financial Instruments Business Operators without providing the basis therefor.

(ii) When including investment performance data in its advertisement, whether the investment trust management company, etc., uses descriptions that could cause misunderstanding by investors, by putting excessive emphasis on specific parts of the performance. (When investment performance data is included in an advertisement, appropriate and easy-to-understand descriptions must be used, from the viewpoint of protecting investors. For example, it is necessary to examine whether the advertisement specifies the method of investment evaluation and the basis for the use of benchmarks and properly expresses that the investment performance data is an indicator that concerns past results but does not promise future performance.)

(iii) When including investment simulation in its advertisement, whether the investment trust management company, etc., uses descriptions that could cause misunderstandings by investors by, for example, setting

arbitrary assumptions. (When investment simulation is included in an advertisement, appropriate and easy-to-understand descriptions must be made, from the viewpoint of protecting investors. For example, it is necessary to examine whether the advertisement specifies the basis for the use of assumptions in the simulation and properly indicates that the simulation is based on prescribed assumptions and does not promise future investment performance.)

(2) Provision of Documents to Beneficiaries, etc., in Potential Cases of Conflicts of Interests

The following are terminology interpretations regarding the provision of documents as specified under Article 13(1) of the Investment Trust Act, and an appropriate response to inquiries shall be made in accordance therewith.

(i) Interpretation of "Same Type of Asset"

The "same type of asset," as specified under Article 13(1)(i) and (ii) of the Investment Trust Act and Article 19(1) of the Order for Enforcement of the Investment Trust Act (hereinafter referred to as the "Enforcement Order of the Investment Trust Act"), does not apply to cases where, because of limits imposed by a relevant investment trust contract or the internal rules of a relevant investment corporation, the contents of a specified asset targeted for investment are different from the contents of a specified asset targeted for investment by another investment trust fund with settlor instructions or by an investment corporation.

(ii) Interpretation of "entrustment of management"

The "entrustment of management," as specified under Article 19(3)(i) of the Enforcement Order of the Investment Trust Act, refers to the entrustment of tenant management operations, such as the renewal of real estate-related rental contracts with tenants and receipts of rents, but does not include the entrustment of the building security and maintenance operations to outside specialist business operators.

(3) Provision of Documents to Investment Corporations, etc., in Potential Cases of Conflicts of Interest

The points of attention described in (2) above shall be applied mutatis mutandis to the provision of documents to investment corporations, etc., as specified under Article 203(2) of the Investment Trust Act.

(4) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the control environment for customer solicitation and explanations to beneficiaries of an investment trust management company, etc., through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the investment trust management company, etc., by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the investment trust management company, etc., is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the investment trust management company, etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-3-3 Duty of Loyalty and Measures to Prevent Internal Collusion

(1) Points of Attention Regarding Investment Trust Management Companies, etc., Engaging in Two or More Types of Business

When supervisors examine the appropriateness of measures taken by an investment trust management company, etc., which is engaging in two or more types of business (as specified under Article 29-2(1)(v) of the FIEA), to prevent internal collusion, they shall pay attention to the following points, for example, depending on the nature of its business, from the viewpoint of preventing conflicts of interests and ensuring the appropriateness of business operations in other ways.

(i) Whether the investment trust management company, etc., has taken appropriate measures to prevent collusion between its different types of business, such as establishing an internal control system and procedures for the prevention of such collusion in a manner suited to the nature of its business.

(ii) Regarding the "non-disclosure information," as specified under Article 147(ii) of the FIB Cabinet Office Ordinance, whether the investment trust management company, etc., has put in place information management measures, such as the appointment of the relevant manager and the establishment of management rules, and ensures the effectiveness of information management by, for example, properly identifying and examining the status of the usage of the non-disclosure information and revising the management method as necessary.

(2) Points of Attention Regarding Prevention of Conflicts of Interest in Investment Management Business

Whether appropriate measures have been taken to prevent practices that could promote the interests of specific rights holders at the expense of other rights holders, such as establishing an internal control system and procedures for the prevention of internal collusion between different types of business in a manner suited to the nature of the business.

(3) Duty of Loyalty to Rights Holders

It should be kept in mind that if an investment trust investment company, etc., causes financial damage to a rights holder due to a clerical error involved in the investment of investment assets and fails to compensate for the damage, it could constitute a violation of the duty of loyalty. The same shall apply to cases where the clerical error occurs at an entity to which business operations are entrusted and where the investment trust management company, etc., which has the obligation of duty to the rights holder fails to compensate for the damage.

(4) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding measures taken by an investment trust investment company, etc., to prevent internal collusion between different types of business, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the investment trust investment company, etc., by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA, since such an issue could directly undermine the interests of rights holders and, in some cases, lead to legal violations, such as a violation of the duty of loyalty and duty of due care. When the investment trust investment company, etc., is

deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the investment trust investment company, etc., is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-4 Appropriateness of Business Operations Related to Fund Management Business

Supervisors shall examine the appropriateness of the business operations of fund management companies (companies engaging in fund management business (financial instruments business involving the activities specified under Article 2(8)(xv) of the FIEA); the same shall apply hereinafter) by paying attention to the following points.

VI-2-4-1 Control Environment for Business Execution

(1) Investment and Administration of Investment Assets

Supervisors shall examine whether a fund management company is properly managing and administering investment assets by paying attention to the following points. It should be noted that the following points should be taken into consideration in a comprehensive manner in light of the nature and size of the fund management company's business, and that failure to meet some of the criteria should not automatically be deemed to mean that the investment and administration of investment assets are inappropriate.

(i) Whether the fund management company has properly specified the matters regarding internal organization that decide its investment policy (including a specific decision-making process).

(ii) Whether the fund management company has prescribed a specific investment method for investment of investment assets by the investment division.

(iii) Whether the fund management company has developed an appropriate control environment regarding the management of securities transactions between various investment assets and between investment assets and its own assets or third-party assets.

(iv) In cases where the fund management company entrusts all or part of the authority over the investment made on behalf of rights holders (as specified under Article 42(1) of the FIEA; the same shall apply hereinafter) to another entity, under Article 42-3 of the FIEA (including cases where the entrusted entity entrusts part of the authority to yet another entity), whether the fund management company has properly established the criteria for selecting the entity to which the authority is entrusted and the method of communications therewith. Whether the investment management company has developed a control environment for continuously examining the entrusted entity's business execution capability and its compliance with contract provisions. Whether it has specified measures to be taken when a problem is found in the entrusted entity's business execution capability (e.g., providing guidance for business improvement and refusing to renew the entrustment contract).

(v) Regarding the selection of the entities to which orders are placed and business operations are entrusted, whether the fund management company has properly specified the matters concerning the entities'

transaction execution capability, control environment for legal compliance, credit risk and trading costs as items that should be taken into consideration.

(vi) Whether the fund management company has arrangements and procedures for a division independent from the investment division to periodically examine whether investment assets are properly invested (including whether records on the investment status are stored), including whether the investment decision process is appropriate, in accordance with the investment guideline or the investment contract specified under Article 2(2)(v) of the FIEA.

(2) Execution of Transactions

When fund management companies execute transactions, they are required to select the transaction form that benefits customers most, by taking into consideration the transaction price and other execution costs in a comprehensive manner. In light of the increasing diversification of the transaction forms due to the advance of financial techniques, supervisors shall examine the status of a fund management company's transaction execution by paying attention to the following points, for example:

(i) At-Average-Price Transaction (transaction made at the average of prices of various orders of the same transaction and delivery dates aggregated by issue and order category (sell or buy))

A. Separation of Divisions

Whether the fund management company has separate divisions for making investment divisions and for taking orders. In cases where organizational separation is difficult, whether, at the minimum, different persons are responsible for these two tasks.

B. Examination of Transactions

Whether the fund management company has a control environment for ensuring that a relevant management division, for example, examines the whole range of business processes related to at-average-price transactions.

C. Disclosure to Customers and Consent Thereof

Whether the fund management company makes at-average-price transactions after making prior disclosure to customers and obtaining their consent. In cases where the fund management company makes orders involving proportional allocation of executed transactions with regard to two or more investment asset accounts, whether it provides customers with appropriate explanations regarding the criteria for allocation, in the case of the total executed transaction volume falling short of the total order volume.

(ii) Transactions Made via Bulk Orders

In cases where the fund management company places a bulk sell or buy order for the same issue on behalf of two or more investment asset accounts, and allocates the executed transactions to each asset account based on the allocation criteria prescribed by the Financial Instruments Business Operator after aggregating the transactions by issue and by buy/sell order, whether it has developed a control environment similar to the one described in (i) above, from the viewpoint of ensuring fairness among customers.

(iii) Transactions Made between Investment Asset Accounts

Whether the fund management company has a control environment for ensuring that a relevant

management division, for example, properly examines the transactions specified under Article 129(1)(i) of the FIB Cabinet Office Ordinance (non-application of the prohibition of transactions between investment assets accounts). The "case where it is deemed to be necessary and rational," as specified by Article 129(1)(i)(a)(4) of the FIB Cabinet Office Ordinance, is a case where because of the need to ensure fairness among customers and fulfill its duties of best execution and loyalty to customers, a fund management company seeks to ensure a fair price formation, while taking care to exclude arbitrariness regarding transactions between different funds by using the following methods, for example:

A. To have traders execute transactions based on investment decisions made by several fund managers (limited to transactions regarding which there is not the risk of the price formation process being distorted in light of liquidity and other factors related to the relevant issue and, in cases where the transactions are executed by the same trader, the trader has no discretion over execution).
B. To place both market buy and sell orders before the market's opening (limited to orders which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).
C. To place both buy and sell orders in intraday trading at a reasonable interval (limited to orders which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).
D. To conduct transactions related to index funds executed through program trading based on contracts and trust contract provisions (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).
E. To make VWAP transactions and discretionary transactions, regarding which the decision on the timing of order placement, price and other execution terms related to individual issues are entrusted by the fund management company to a third-party entity (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).
F. To make futures transactions, regarding which it is difficult to avoid the placement of orders for the same issue because of the small number of issues available for futures trading (limited to transactions which have no risk of distorting the price formation process in light of liquidity and other factors related to the relevant issue).

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a fund management company's control environment for business execution, through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the fund management company by requiring the submission of reports based on Article 56-2(1) of the FIEA. When the fund management company is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the fund management company is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for

business suspension based on Article 52(1) of the FIEA.

VI-2-4-2 Control Environment for Customer Solicitation and Explanations

(1) Prohibition of Advertisements Using Exaggerated Descriptions

(i) Whether the fund management company includes in its advertisements descriptions indicating that the performance, contents and method of its investment are markedly superior to those of other Financial Instruments Business Operators without providing the basis therefor.

(ii) When including investment performance data in its advertisement, whether the fund management company uses descriptions that could cause misunderstanding by investors, by putting excessive emphasis on specific parts of the performance. (When investment performance data is included in an advertisement, appropriate and easy-to-understand descriptions must be used, from the viewpoint of protecting investors. For example, it is necessary to examine whether the advertisement specifies the method of investment evaluation and the basis for the use of benchmarks and properly expresses that the investment performance data is an indicator that concerns past results but does not promise future performance.)

(iii) When including investment simulation in its advertisement, whether the fund management company uses descriptions that could cause misunderstandings by investors by setting arbitrary assumptions, for example. (When investment simulation is included in an advertisement, appropriate and easy-to-understand descriptions must be made, from the viewpoint of protecting investors. For example, it is necessary to examine whether the advertisement specifies the basis for the use of assumptions in the simulation and properly indicates that the simulation is based on prescribed assumptions and does not promise future investment performance.)

(2) Points of Attention Regarding Provision of Pre-Contract Documents

In cases where a fund management company concurrently conducts business unrelated to investment management and where it receives remuneration related to investment management business and fees related to other business collectively under the same contract, the fund management company must separately specify the remuneration related to investment management business and the fees related to other business with regard to the "matters concerning fees, remuneration or any other consideration payable by the customer with regard to said Contract for Financial Instruments Transaction," as specified under Article 37-3(1)(iv) of the FIEA.

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a fund management company's control environment for customer solicitation and explanations, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the fund management company by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the fund management company is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the fund management

company is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-4-3 Duty of Loyalty and Measures to Prevent Internal Collusion

(1) Points of Attention Regarding Fund Management Companies Engaging in Two or More Types of Business

When supervisors examine the appropriateness of measures taken by a fund management company, which is engaging in two or more types of business (as specified under Article 29-2(1)(v) of the FIEA), to prevent internal collusion, they shall pay attention to the following points, for example, depending on the nature of its business, from the viewpoint of preventing conflicts of interests and ensuring the appropriateness of business operations in other ways.

(i) Whether the fund management company has taken appropriate measures to prevent collusion between its different types of business, such as establishing an internal control system and procedures for the prevention of such collusion in a manner suited to the nature of its business.

(ii) Regarding the "non-disclosure information," as specified under Article 147(ii) of the FIB Cabinet Office Ordinance, whether the fund management company has put in place information management measures, such as the appointment of the relevant manager and the establishment of management rules, and ensures the effectiveness of information management by, for example, properly identifying and examining the status of the usage of the non-disclosure information and revising the management method as necessary.

(2) Points of Attention Regarding Prevention of Conflicts of Interests in Investment Management Business

Whether appropriate measures have been taken to prevent practices that could promote the interests of specific rights holders at the expense of other rights holders, such as establishing an internal control system and procedures for the prevention of collusion between different types of business in a manner suited to the nature of the business.

(3) Duty of Loyalty to Rights Holders

It should be kept in mind that if a fund management company causes financial damage to a rights holder due to a clerical error involved in the investment of investment assets and fails to compensate for the damage, it could constitute a violation of the duty of loyalty. The same shall apply to cases where the clerical error occurs at an entity to which business operations are entrusted and where the fund management company that has the obligation of duty to the investor fails to compensate for the damage.

(4) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a fund management company's measures to prevent collusion between different types of business, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the fund management company by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA, since such an issue could directly undermine the interests of rights holders and investment assets and, in some cases, lead to legal violations, such as a violation of the duty of loyalty

and duty of due care. When the fund management company is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the fund management company is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VI-2-5 Points of Attention Regarding Real Estate-Related Fund Management Companies

Real estate investment trusts and other real estate-related funds are financial products based on the investment of funds collected from a broad range of investors, including individual investors, mainly in real estate (including financial products backed by real estate as the underlying assets; the same shall apply in VI). Financial instruments business operators which manage these products are required to ensure the appropriateness of the implementation of due processes, information disclosure and measures to prevent conflicts of interest, which are prerequisites for the exercise of an appropriate price formation function of the real estate market, thereby fulfilling the duties of loyalty and due care to investors.

While the viewpoints and supervisory methods and responses specified in VI-2-2 to VI-2-4 shall be applied to the supervision of real estate-related fund management companies, depending on the investment style, attention also needs to be paid to the following items. In this respect, supervisors shall pay particular consideration to whether real estate-related fund management companies sufficiently identify and understand the characteristics unique to real estate, in comparison with other assets, and the risks involved in the investment therein, as they need to conduct their business in a sound and appropriate manner based on sufficient understanding of these matters. It should be noted that the supervision conducted in this manner is not intended to manipulate specific real estate prices.

VI-2-5-1 Control Environment for Legal Compliance

Real estate-related fund management companies' control environments for legal compliance shall basically be examined based on the supervisory viewpoints and methods specified in III-2-1. However, they shall also be examined in relation to a broad range of matters, including measures to prevent conflicts of interest specific to the real estate-related fund business.

VI-2-5-2 Internal Control Environment

As real estate-related fund management companies are bound to the duties of due care and loyalty, they are required to establish a sufficient control environment for legal compliance and risk management. Their management teams need to formulate various rules that ensure thorough legal compliance and risk management rules that ensure appropriate risk management based on the analysis and evaluation of risks involved in real estate investment, and check the status of compliance therewith.

It should be kept in mind that in doing the above, the management teams need to establish an internal control environment, including a control environment for due diligence that pays due consideration to the unique characteristics of real estate.

VI-2-5-3 Evaluation Items Concerning Operations of Real Estate-related Fund Management Companies

(1) Evaluation Items Concerning Due Diligence Control Environment for Purchase and Sales of Real Estate

Real estate due diligence is an important task for the understanding of the legitimate investment value of real estate, and thus its appropriateness shall be examined with due consideration of the following points.

Meanwhile, the management team must always understand the progress of implementation of measures to ensure the appropriateness of due diligence and the effectiveness of examination functions, while remaining aware of the issues.

(i) Examinations shall be performed to see whether estimates of various costs of repair/renewal are appropriately investigated and reflected in the appraised value of real estate, considering the significance of an impact on cash flows in the future.

(ii) The DCF method is an approach for valuation based on cash flows, and is a major and effective method for the appraisal of real estate. However, there are many preconditions, which may blur details. Thus, the point is whether the following items are verified, and the result of verification is recorded when the DCF method is adopted.

A. Validity of adopted figures (based on the projected estimates, in particular) and basis for judgment
B. Validity of the overall scenario and basis for judgment
C. Comparison and balance between the result of adopting the DCF method and the result of adopting other methods/means.

(iii) The following points shall be considered when entrusting the formulation of engineering reports (ER) and appraisal reports and receiving them:

A. Whether it is ensured that ER writers and real estate appraisers make impartial decisions based on objective standards.
B. Whether necessary information etc., is provided to ER writers and real estate appraisers, when requesting ERs and real estate appraisal. Also, whether such provision of information, etc., is properly managed.
C. Whether the following points are confirmed in addition to necessary examinations on how the information, etc., mentioned in B. above has been reflected in the requested ER:
    a. Whether necessary investigations are conducted and the investigation results are justified by objective grounds when investigating soil contamination and harmful substances.
    b. Whether it is confirmed what kind of repairs are used as the basis for calculations of cost estimates of repairs and renewals of individual parts of a building.
    c. Whether necessary verifications of compliance have been conducted regarding the target property, not only compliance with laws but also with ordinances, such as district plans, etc.
D. When receiving the appraisal report from the appraiser who was requested to perform the evaluation, whether the necessary examination has been conducted to see how the information, etc., listed B. above has been reflected in the report and whether the following points have been verified:
    a. Whether the concept of ER has been considered and reflected. Whether the reasons and grounds for any items not being reflected have been confirmed.

b. In the case of adopting the DCF method, whether estimates of future income and utilization rate, etc., are verified as relevant and based on objective data. Also, whether the level of relevance has been verified in the same way for the estimation of discount rates and terminal rates, which serve as preconditions.

c. Whether necessary examinations have been performed of items that may possibly influence the liquidity of the real estate itself and the cash flows that would be generated by the real estate.

E. In the cases where listed details in the ER and appraisal report are not used when calculating the purchase/sales price based on the result of due diligence, whether the relevance of adopted values, etc., is verified and the basis for such values is recorded and stored.

(2) Control Environment for Preventing Conflict of Interest Transactions

The management team needs to be aware of the potential for risks of conflict of interest transactions to occur, and identify not only interested persons specified in laws, but also possible business partners with which conflicts of interest may arise (hereinafter referred to as "interested persons, etc."), and then to establish an adequate management system concerning the transactions with these persons.

For example, it is desirable to allow compliance personnel to manage negotiations concerning sales and purchases with interested persons, from the perspective of prevention of conflict of interest transactions by constructing a system where property information from interested persons (including the state of negotiations concerning purchase and sales, etc.) can be managed in an integrated manner.

Furthermore, when the "warehousing function" (Refer to Note) of interested persons, etc., is utilized in the cases where an investment corporation is unable to acquire real estate possessed by a third party at the time said party wishes to sell it, the following points shall be considered, for example, to see whether the real estate-related fund has acquired it and is aware that a high risk of conflict of interest exists.

(Note) "Warehousing function" refers to the case when a juridical person acquires and maintains ownership of real estate on a temporary basis until an investment corporation is able to acquire the said real estate from them.

(i) The state of negotiations and sharing of roles with interested persons, etc., when utilizing the warehousing function

(ii) The state of due diligence, including the calculation of the acquisition price when a real estate-related fund makes a purchase.

(3) Points to Consider in the Cases Where Management of Real Estate-related Assets of Several Funds are Entrusted to One Real Estate-related Fund Management Company

In the cases where a real estate-related fund management company is entrusted with the management of real estate from several funds, it shall be considered, at the time when property information is obtained, to see whether measures have been taken to avoid competition over the acquisition among management funds and whether a framework has been established to enable each fund to make decisions independently.

(4) Others

(i) Interpretation of Article 193 (1) (iii) of the Investment Trust Act

"Acquisition of real estate" does not include the development of housing sites or the construction of buildings by an investment corporation itself, but includes cases where the investment corporation concludes an agreement to have others develop housing sites or construct buildings (excluding, however, the case of inadequate investment trust corporations). The following cases shall be considered inadequate with respect to the "case of inadequate investment corporations":

A. When conducting large-scale repair and renovation work, etc., tenants need to be relocated for a certain period of time, and the fluctuations of cash flows will heavily affect the entire portfolio.

B. When an investment corporation purchases undeveloped land and constructs new buildings, various risks will be involved in the development of real estate (development risk, authorization risk, construction completion risk, tenant risk, price fluctuation risk, interest fluctuation risk during development, and large natural disaster risk, etc.), and such risks may greatly affect the entire portfolio because the investment does not generate immediate cash flows.

(ii) Control Environment for Managing the Outsourcing of Business Operations

Real estate-related fund management companies, while exercising investment discretion, outsource part of their businesses to various corporations (ER corporations, appraisal corporations, trust banks, property management corporations, and building management corporations, etc.). Thus, appropriate supervision over the said outsource is essential if they are to exercise loyalty and fulfill their duties. In order to effectuate supervisions, it is necessary to improve various reporting lines from outsourcees (both direct and indirect via trust banks, etc.) upon formulating various regulations/standards, including selection criteria for outsources, thereby implementing effective monitoring periodically. Meanwhile, it should be noted that the appropriate clarification of role sharing between outsourcers and outsourcees is a prerequisite for a control environment for managing the outsourcing of business operations.

(iii) Investment, etc., in Development SPC

Whether analysis and risk management have been appropriately implemented with respect to various risks (development risk, authorization risk, construction completion risk, tenant risk, price fluctuation risk, interest fluctuation risk during development, and large natural disaster risk, etc.). Whether monitoring of project progress has been property conducted. Meanwhile, attention should be taken to ensure that investment in the development SPC by funds other than those specializing in development-style projects does not impose excessive influence on the entire portfolio, considering that the development does not generate immediate cash flows.

(iv) Control Environment for Managing Information

As for the information management of real estate-related fund management companies, which manage listed real estate investment juridical persons, it is necessary to manage information appropriately, by taking measures to ensure confidentiality of information prior to decision making, such as investment decisions based on asset management outsourcing contracts, etc. (decision making, etc., concerning acquisition and sales), as well as confidentiality of information prior to transaction and prior to disclosure.

(5) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the above evaluation points,

through daily supervisory administration and the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the real estate-related fund management company by requiring the submission of reports based on Article 56-2(1) of the FIEA. When the real estate-related fund management company is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the real estate-related fund management company is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52 (1) of the FIEA.

VI-2-6 Appropriateness of Investment Corporations' Business Operations

VI-2-6-1 Items Regarding Investment Corporations' Organizational Management

(1) Points of Attention Regarding Management of Executive Committee Meetings

(i) Whether the investment corporation's executive committee meetings have become a matter of formality. For, example, attention shall be paid to whether decisions are made through the so-called round-robin arrangement, instead of being made at meetings attended by executives in person.

(ii) Whether the investment corporation has received appropriate data and materials and sufficient explanations from the asset investment company in order to ensure the effectiveness of deliberations by the executive committee

(iii) Whether the investment corporation's executive committee clearly categorizes the business operations entrusted to the company undertaking general clerical work and the asset investment company and checks whether the fees paid to them are appropriate and suited to the categories of the business operations entrusted to them.

(2) Role of Executive Officers

Whether executive officers understand the items to be decided by the executive committee and refer all necessary items thereto.

(3) Supervisory Executives

Whether supervisory executives not only attend executive committee meetings, but also supervise the status of business execution by executive officers based on the recognition of their role as the supervisors of executive officers as specified under Article 111(1) of the Investment Trust Act. Whether they require executive officers, the company undertaking general clerical work, the asset investment company and the asset custody company to report to them and conduct necessary investigations, depending on the circumstances.

(4) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding an investment corporation's organizational management, through daily supervisory administration and the reporting of problematic conduct,

they shall identify and keep track of the status of voluntary improvement made by the investment corporation by requiring the submission of reports based on Article 213 of the Investment Trust Act. When the investment corporation is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 214 of the Investment Trust Act. When the investment corporation is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the rescission of registration based on Article 216(1) of the Investment Trust Act.

VI-2-7 Other Points of Attention

VI-2-7-1 Points of Attention Regarding Investment Trust Act and Trust Act

The points of attention regarding the laws and regulations applicable to investment trusts, to which assets were entrusted before the new Trust Act entered into force, are as explained below. It should be noted that the definitions of terms used in VI-2-7-1 are as follows:

(i) "New Trust Act": Trust Act (Act No. 108 of 2006)

(ii) "Act for Establishment of Laws and Regulations Related to the Trust Act": A law for the establishment of laws and regulations necessitated by the entry into force of the Trust Act (Act No. 109 of 2006).

(iii) "New Investment Trust Act": Revised Investment Trust Act specified under Article 5 of the revised law

(iv) "Former Investment Trust Act": Investment Trust Act before the revision as specified under Article 25 of the Act for Establishment of Laws and Regulations Related to the Trust Act

(v) "New Law-Based Trust": Investment trusts to which assets were entrusted after the entry into force of the New Investment Trust Act and New Trust Act

(vi) "Former Law-Based Trust": Investment trusts to which assets were entrusted before the entry into force of the New Investment Trust Act and New Trust Act

The Former Law-Based Trusts may be converted into New Law-Based Trusts under Article 3 or Article 26(1) of the Act for Establishment of Laws and Regulations Related to the Trust Act. Unless the conversion is made, they shall be subject to Article 2 of the Act for Establishment of Laws and Regulations Related to the Trust Act. Therefore, Former Law-Based Trusts are not eligible for the provisions of the New Trust Act nor the Act for Establishment of Laws and Regulations Related to the Trust Act regarding a registry of beneficiary rights, consolidation of trusts and a notice regarding investment trusts by the settlor nor for the provisions of the New Trust Act concerning requests for purchases by beneficiaries who have opposed written resolutions regarding changes in investment trust contract provisions (Articles 4(2)(xvii), 6(7), 16(ii), 17, 18, 20, 25, 49(2)(xviii) and 50(4) of the New Investment Trust Act, Article 16(ii), 17 and 18 of the New Investment Trust Act as applied mutatis mutandis pursuant to Article 54(1) of the same act, Articles 16(ii), 17, 20 and 25 of the New Investment Trust Act as applied mutatis mutandis pursuant to Articles 57 and 59 of the same act, the penalties related to these provisions and relevant FIEA Enforcement Order and cabinet office ordinance). Instead, they are subject to the relevant provisions of the Former Investment Trust Act, the FIEA Enforcement Order and cabinet office ordinance that were effective before the new provisions took effect.

VI-2-7-2 Points of Attention Regarding Investment Trusts without Settlor Instructions

The points of attention specified in VI-2-3-2(2) shall be applied mutatis mutandis to the provision of documents to beneficiaries, etc., based on Article 13(1) of the Investment Trust Act as applied mutatis mutandis pursuant to Article 54(1) of the same act.

VI-2-8 Points of Attention Regarding Supervision of Non-Affiliated Business Operators

(1) Major Supervisory Viewpoints

(i) In the case of a Financial Instruments Business Operator that does not belong to any Financial Instruments Firms' Association nor have membership in or trading participant rights at any financial instruments exchange (referred to as "Non-Affiliated Business Operators" in VI-2-8), whether it has developed internal rules with due consideration of rules set by associations, etc.

(ii) Whether the Financial Instruments Business Operator has developed a control environment that ensures appropriate compliance with internal rules (e.g., examination of whether all officers and employees are aware of and comply therewith).

(iii) When rules set by associations, etc., have been revised, whether the Financial Instruments Business Operator makes sure to quickly review and revise internal rules accordingly.

(2) Supervisory Method and Actions

(i) In cases where a Non-Affiliated Business Operator has failed to establish internal rules with due consideration of the rules set by associations, etc., and where it is deemed unlikely to do so on a voluntary basis, supervisors shall order it to establish internal rules based on Article 56-4(2) of the FIEA. In such cases, the Non-Affiliated Business Operator shall also be required to revise internal rules immediately, in response to any future revision of the rules set by associations, etc.

(ii) In cases where a Non-Affiliated Business Operator's internal rules are deemed to need to be revised in light of the rules set by associations, etc., and where the business operator is deemed unlikely to make revision on a voluntary basis, supervisors shall order the business operator to do so based on Article 56-4(2) of the FIEA.

(iii) When supervisors have recognized an issue of supervisory concern regarding the status of a Non-Affiliated Business Operator's establishment and revision of internal rules and compliance therewith, they shall strive to identify and keep track of the actual situation by holding in-depth hearings and requiring the submission of a report based on Article 56-2(1) of the FIEA. In addition, they shall conduct appropriate supervision based on Article 56-4(1) of the FIEA with due consideration of the rules set by associations, etc., by, for example, issuing an order for business improvement based on Article 51 of the FIEA and an order for business suspension based on Article 52(1) of the FIEA as necessary.

VI-3 Various Administrative Procedures (Investment Management Business)

VI-3-1 Registration

VI-3-1-1 Investment Management Business

(1) Items Regarding Examination of Staffing Level

When supervisors examine whether or not a Financial Instruments Business Operator is sufficiently staffed to properly conduct the financial instruments business, as specified under Article 29-4(1)(i)(d) of the FIEA, they shall check the following points based on its application and attachments thereto as well as hearings.

(i) Whether it can be confirmed that officers and employees with sufficient knowledge and experience have been secured and a sufficient organization has been established to conduct the relevant financial instruments business in light of the following requirements:

A. Top managers must be sufficiently qualified to conduct investment management business in a fair and appropriate manner, in terms of their backgrounds and capabilities.

B. Managing directors must understand the viewpoints regarding governance indicated in the FIEA and various other laws and regulations, and have sufficient knowledge and experience to conduct governance and sufficient knowledge and experience regarding compliance and risk management to conduct financial instruments business in a fair and appropriate manner.

C. Persons with sufficient knowledge and experience regarding investment assets must be secured for the position responsible for making asset investment on behalf of rights holders.

D. The compliance division (staff in charge of compliance) must be independent from the asset investment division and staffed with personnel with sufficient knowledge and experience.

E. In addition to securing the personnel described in C. and D. above, the Financial Instruments Business Operator must be staffed and organized so that personnel necessary for conducting relevant business in an appropriate manner are allocated to individual divisions and managers in charge of internal control are appropriately allocated.

F. Staff capable of conducting the following processes should be secured with regard to the relevant business.

a. Compilation and management of account documents (including the account documents as specified in VI-3-2-4), reports and other documents.

b. Disclosure

c. Segregated management of investment assets

d. Risk management

e. Computer system management

f. Trading management and customer management by relevant management divisions

g. Management of sensitive corporate information

h. Advertisement screening

i. Customer information management

j. Processing of complaints and disputes
k. Execution of asset investment business by the investment division
l. Internal audits
m. Accounting and screening related to investment trust assets in the case of investment of investment trust assets

(ii) When the qualifications of employees and officers are examined in a comprehensive manner in relation to the following criteria regarding organized crime groups, their members and financial crimes, whether there is the risk that public confidence in the financial instruments business could be damaged because of the inclusion of officers and employees with inappropriate qualifications among its staff.

A. Officers and employees should not be current or former members of organized crime groups.
B. Officers and employees should not have close relationships with organized crime groups.
C. Officers and employees should not have the experience of being sentenced to a fine for violation of the FIEA or other domestic financial laws and regulations or foreign laws and regulations equivalent thereto.
D. Officers and employees should not have the experience of being sentenced to imprisonment with work or more severe punishment (including similar punishments imposed under foreign laws or regulations equivalent thereto). (Particular attention should be paid to the case of an officer or employee being accused of committing crimes specified under Articles 246 to 250 of the Penal Code (fraud, fraud using computers, breach of trust, quasi fraud and extortion, as well as attempts at these crimes).)

(Note) It should be kept in mind that in cases where it is deemed as a result of comprehensive examination based on the criteria described in (ii) A. to D. that a major shareholder in the Financial Instruments Business Operator could exercise undue influence on it, thereby damaging public confidence in it, the business operator may be deemed to be "not adequately staffed to properly conduct financial instruments business."

(2) Documents Specifying Contents and Methods of Business Operations

Supervisors shall check whether documents specifying the contents and methods of an investment management business operator's business operations properly specify the following items:

(i) Types of financial instruments transactions which the investment management business operator conducts
(ii) Items specified under Article 8(ix) of the FIB Cabinet Office Ordinance.
(iii) Basic principles on business operations

A. The investment management business operator's basic policy for business operations and principles on the conduct of business operations
B. Items regarding the basic policy for asset investment
C. Types of investment assets
D. Items regarding the entrustment of the authority over investment
E. Items regarding improvement of the investment management business operator's financial condition

(iv) Method of Business Execution

A. Items regarding the investment method

B. Items regarding customer solicitation and contract signing

C. Items regarding the administration of investment assets

(v) Method of the allocation of business operations

Items regarding the investment management business operator's organization

(vi) Arrangements and procedures for dealing with complaints

(vii) Name of the Financial Instruments Firms' Association to which the investment management business operator belongs and items regarding compliance with voluntary regulatory rules set by the association.

(3) Items to Be Specified in Documents Prescribed under Article 9(i) of the FIB Cabinet Office Ordinance. (Documents Specifying Framework for Business Execution Such as Staffing and Organization)

(i) The lineup of officers and employees at the start of the investment management business (including each officer's experiences and knowledge regarding investment instructions and investment assets), an organization chart and the outline of business operations conducted by individual divisions

(ii) Framework for Business Operations Related to Asset Investment

A. Items regarding the internal organization responsible for deciding the investment policy concerning investment assets

B. The asset investment division's arrangements and procedures for asset investment

C. Items regarding the selection of an entity to which asset investment is entrusted (including cases of re-entrustment) and arrangements and procedures for communications therewith

(iii) Knowledge and Experience of Persons in Charge of Asset Investment

The knowledge and experience of each person in charge of asset investment, with regard to investment assets, must be specified.

(iv) Knowledge and Experience of Persons in Charge of Compliance

The knowledge and experience of persons in charge of compliance, with regard to processes for ensuring compliance, must be specified.

(v) Internal Control System and Procedures for Asset Investment and Other Operations

Items regarding rules concerning investment instructions (including investment instructions and investment made by an entity entrusted with asset investment in cases where asset investment is entrusted to an outside entity), rules concerning the division in charge of internal inspection of individual divisions, and arrangements and procedures for clerical processes.

(vi) Arrangements and Procedures for Management of Sensitive Corporate Information

A. The person responsible for the management of sensitive corporate information must be specified, and the person's details must be included, in internal rules.

B. Management arrangements and procedures must be specified in internal rules and a framework for enabling the rules to be effectively enforced must be in place.

(vii) In cases where investment trust assets are invested, the knowledge and experience of persons in charge of accounting work related to investment trust assets must be specified.

A. The knowledge and experience of each person in charge of accounting work related to investment trust

assets, with regard to the relevant work, must be specified.

B. In cases where accounting work related to investment trust assets are entrusted to a third-party entity, the knowledge and experience of the said third-party entity, with regard to the relevant work, must be specified.

(4) Points of Attention Regarding Business Operators Not Planning to Join Any Financial Instruments Firms' Association or Obtain Membership in or Participants Rights at Any Financial Instruments Exchange.

Supervisors shall notify the following matters to a business operator that does not plan, at the time of the application, to join any Financial Instruments Firms' Association or obtain membership in or trade participant rights at any financial instruments exchange, and request them to take appropriate actions.

(i) In cases where the business operator is deemed to lack appropriate internal rules set with due consideration of the rules set by associations, etc., it shall in principle be ordered to immediately establish appropriate internal rules after registration.

(ii) A Non-Affiliated Business Operator may be ordered to revise internal rules with due consideration of the rules set by associations, etc.

(iii) In cases where a Non-Affiliated Business Operator has been ordered to establish or revise internal rules, they need to do so within 30 days and then obtain approval from the Prime Minister.

(iv) In cases where a Non-Affiliated Business Operator plans to revise or abolish internal rules established in the manner described in (iii) above, they need to obtain approval from the Prime Minister.

(v) The authorities are to properly supervise Non-Affiliated Business Operators' business operations, with due consideration of the rules set by associations, etc., so as to ensure the full protection of public interests and investors.

(5) Cases Not Requiring Registration

A corporation is allowed to engage in investment management business irrespective of the provision of Article 29 of the FIEA in cases where it meets the provision of Article 61(2) of the FIEA (cases where a corporation which is established based on foreign laws and regulations and which engages in investment management business abroad seeks to undertake investment management exclusively on behalf of Financial Instruments Business Operators (business operators engaged in investment management business)).

VI-3-1-2 Investment Corporation

(1) Points to Consider When Accepting Notification Concerning the Establishment of Investment Corporations

The following points shall be considered when the director-general of a Local Finance Bureau receives a notification concerning the establishment of an investment corporation (hereinafter referred to as "establishment notification") pursuant to the provisions of Article 69 (1) of the Investment Trust Act:

(i) Points to Consider in Relation to Examinations of Establishment Notification

A. Page 2, section 1 of the establishment notification: Trade name of an investment corporation to be established

The trade name should not lead investors to mistakenly believe that the corporation is a public organization

B. Page 2, section 3 of the establishment notification: (4) Amount of contribution for establishment

Whether the total of issued prices of investment accounts is lower than the total amount of contribution prescribed in Article 57 of the Enforcement Order of the Investment Trust Act

C. Page 2, section 3 of the establishment notification: (7) Outline of asset management of the said investment corporation

Whether assets are mainly to be managed as an investment in specified assets

(ii) Items Related to Examinations of Documents Attached to the Establishment Notification

A document, submitted by a foreigner living outside Japan, which corresponds to the certificate of residence or a document equivalent thereto shall fall under the category of "documents in lieu of these" prescribed in Article 108(2)(v) of the Ordinance for Enforcement of the Investment Trust Act.

(iii) Receipt Procedures, etc., of Establishment Notification

A. Receipt procedures

The director-general of a Local Finance Bureau, upon receiving a notification of establishment of an investment corporation, under Article 69(1) of the Investment Trust Act, shall return a copy of the notification and a set of bylaws using Attached List of Formats VI-1 with a receipt stamp and receipt number to the party making the notification.

B. The director-general of a Local Finance Bureau, upon receiving a notification of establishment of an investment corporation, shall record its details in the register book of the notification of establishment of investment corporations, etc. (Attached List of Formats VI-2).

(2) Points to Consider When Receiving Notification of Failure to Establish Investment Corporations

The director-general of a Local Finance Bureau, upon receiving a notification of failure to establish an investment corporation, under Article 110(1) of the Ordinance for Enforcement of Investment Trust Act, shall perform the following procedures:

(i) Inquire with the project planner about the responses to those who applied for investments and make a record of the merits.

(ii) Enter the date of receipt of the notification of failure to establish an investment corporation into the registry book for notification of establishment of investment corporations, etc., and briefly describe the reasons for failure to establish an investment corporation in the remarks column.

(3) Points to Consider When Receiving Application for Registration of Investment Corporations

The following points shall be considered when the director-general of a Local Finance Bureau receives an application for registration (Ordinance for Enforcement of the Investment Trust Act, Attached List of Formats 9 (hereinafter the same shall apply in (iii)) pursuant to the provision of Article 188(1) of the Investment Trust Act.

(i) Points to Consider Concerning Examinations on Application for Registration

A. Application for Registration Two, page 3, section 2: (5) Minimum net asset to be maintained

Whether the minimum net assets are maintained above the amount prescribed in Article 55 of the Enforcement Order of the Investment Trust Act

B. Application for Registration Two, page 3, section 2: (6) Subject and policy of asset management

Whether assets are mainly to be managed as investments in specified assets

C. Application for Registration Six, page 9: (1) Total contribution

Whether the total contribution at the time of establishment of an investment corporation is above the amount prescribed in Article 57 of the Enforcement Order of the Investment Trust Act

(ii) Points to Consider Concerning the Examinations on Attached Documents to the Application for Registration

A document submitted by a foreigner living outside Japan, which corresponds to the certificate of residence or a document equivalent thereto, shall fall under the category of "documents in lieu of these" prescribed in Article 108(5) of the Ordinance for Enforcement of the Investment Trust Act.

(iii) Other Points to Consider Concerning Receipt of Application for Registration

A. The director-general of a Local Finance Bureau, upon receiving an application for registration of an investment corporation, shall record the date of receipt of the application for registration of an investment corporation in the register book of the notification of establishment of investment corporations, etc.

B. After the offer period of investment to be issued at the time of establishment listed in the notification of the establishment of an investment corporation has elapsed, and after the period usually necessary for the submission of an application for registration for an investment corporation has elapsed, if an application for registration for the relevant investment corporation or the notification of failure to establish investment corporations has not been submitted, the director-general of the Local Finance Bureau shall refer to the project planner who submitted the notification of the establishment of an investment corporation to find out about the circumstances.

(iv) Registration Procedures, etc.

A. Registration number

a. Each registration shall be identified by a serial registration number which is assigned by each local finance bureau (however the following numbers shall not be used: 4, 9, 13, 42, 83, 103, and 893).

b. When a registration is no longer valid, its registration number shall be retired and no new number shall be issued in its place.

c. Registration numbers shall be managed by the registration number file of investment corporations using Attached List of Formats VI-3.

B. Notification to applicants for registration

After the examinations on the application for registration of investment corporations, when it is found that the said application form and the attached documents are complete and there are no grounds for rejecting the application, the director-general of the Local Finance Bureau shall promptly notify the applicant to that effect, using the prepared Attached List of Formats 14 of the Ordinance for Enforcement of Investment Trust Act.

(v) Report to the Commissioner of Financial Services Agency

Every month, registration forms for newly registered investment corporations shall be collectively reported to the Commissioner of the Financial Services Agency, using Attached List of Formats VI-4, by the 15th of the following month.

(vi) Refusal of Registration

The director-general of a Local Finance Bureau shall, when refusing registration, enter the corresponding number among the items listed in Article 190(1) of the Investment Trust Act as grounds for refusal, or shall specifically clarify the part of the application for registration or attached documents that lists false information or is missing important facts, using Attached List of Formats 15 of the Ordinance for Enforcement of the Investment Trust Act.

(vii) Storing of Applications for Registration

Notification of establishment, notification of failure of establishment and their attached documents shall be stored by the director-general of a Local Finance Bureau who has received the said notifications. Application for registration, notification of changes, notification of dissolution and their attached documents shall be stored by the director-general of a Local Finance Bureau who has registered the registered investment corporation.

(viii) Registry of Registered Investment Corporations

A. Registry of registered investment corporations shall be made available for public inspection and an applicant for inspection shall be required to enter necessary items in the application for inspection of the registry of registered investment corporations, using Attached List of Formats VI-5.

B. The date of inspection of the registry of registered investment corporations shall be a day other than a holiday as specified in Article 1 of the Act on Holidays of Administrative Organs, and the inspection period shall be within the duration designated by the director-general of the Local Finance Bureau.

However, when it is necessary to organize registry books or for any other reason, the inspection date or time may be changed or the inspection may be suspended or refused.

C. The registry of registered investment corporations must not be taken out of the place of inspection designated by the director-general of the Local Finance Bureau.

VI-3-2 Approval and Notification

VI-3-2-1 Approval

When approving other businesses based on Article 35(4) of the FIEA, supervisors shall pay attention to the following points.

(i) Whether the relevant business violates relevant laws and regulations.

(ii) Whether there is the risk of the applicant Financial Instruments Business Operator's net asset value falling below 50 million yen.

(iii) In cases where the relevant business involves the signing of contracts with customers, whether the Financial Instruments Business Operator has prescribed specific procedures for the prevention of conflicts of interest, which is necessary for investor protection.

(iv) Whether the Financial Instruments Business Operator has established internal rules regarding the

relevant business.

VI-3-2-2 Notification

Supervisors shall receive and process notifications specified under the FIEA with due consideration of the following points. When they have received notifications regarding the businesses specified under Article 35(2) of the FIEA in particular, supervisors shall pay attention to whether the procedures legally necessary for regulating the businesses have been implemented. In addition, regarding the businesses listed below, they shall check whether their contents and methods meet the following criteria. In this case, the provision of relevant written documents and the implementation of paper-based procedures may be substituted by electronic means — using computer systems and other information technologies — subject to customers' consent. Regarding businesses that do not meet the following criteria, the applicant business operators shall be required to file an application based on Article 35(4) of the FIEA.

(1) Business Related to Trading of Gold Bullion and Intermediary and Brokerage Services

(i) Description of Product

Whether the gold products handled by the Financial Instruments Business Operator are gold bullion or gold coins, with high levels of purity and market liquidity, for which there is an established global market.

(ii) Procurement

Whether the business operator ensures that it or its affiliated companies do not hold excessive inventories, by including in its purchase contract with the supplier provisions stipulating that (i) the business operator itself does not hold any inventory in principle and (ii) the supplier agrees to buy back the gold product purchased by the business operator when requested to do so. Regarding the Cash Forward Trade, whether the business operator includes in its contract with the supplier a provision that ensures the execution of a forward contract.

(iii) Customer Services Activities

A. Sales Method

Supervisors shall examine whether the business operator meets the following requirements regarding the sales method:

a. To refrain from offering futures trading and concentrate on physical-delivery transactions.

b. Prior to the sale of gold products through cumulative investments, to provide customers with sufficient written explanations that describe the scheme of the investment.

B. Solicitation

As gold investment should be made based on investors' own judgments and responsibilities, supervisors shall examine whether the business operator meets the following requirements regarding investment solicitation:

a. To refrain from soliciting customers by offering definitive predictions regarding gold price movements.

b. To make appropriate investment solicitation suited to investors' intention and their knowledge and experience regarding gold investment as well as the size and nature of their investment funds.

c. To refrain from promising loss compensation and soliciting investment by offering special profits.

d. To refrain from soliciting customers to conduct purchases and sales frequently (including frequent switching between securities and gold products) in a short period of time.

e. To refrain from conducting purchases and sales in amounts and at prices determined at its discretion on commission from customers.

C. Provision of Certificates, etc., to Customers

Supervisors shall examine whether the business operator meets the following requirements regarding the provision of certificates of safe custody to customers:

a. Provision of Certificates of Safe Custody to Customers

To provide necessary certificates and other documents necessary for clarifying the contractual rights and obligations and for facilitating transactions, such as certificates of safe custody (limited to cases of custodial trade), at-delivery statements of account, and written demands for purchase (documents which are attached to the gold product delivered in physical-delivery trade and which stipulate that the business operator agrees to buy the gold product), depending on whether the transaction is custodial or physical delivery-based. However, regarding the Cash Forward Trade, the provision of the certificates of safe custody may be substituted by a statement of trade that describes the contents of transactions and the outstanding balance of gold in custody if the statement is provided at the time of each delivery. Regarding the Cumulative Gold Bullion Investment, the provision of the certificate of safe custody and the at-delivery statement of account may be omitted if a notice that describes records of gold bullion purchases and the outstanding balance of gold in custody is provided at least once every six months.

b. Provision of a Set of Contract Clauses

To provide a set of contract clauses regarding gold bullion trade that specify items concerning the contractual rights and obligations when the customer starts trading and when revisions are made, in both cases of custodial trade and physical delivery-based trade, from the viewpoint of preventing problematic conduct involving gold bullion trade and protecting customers.

C. Determination of Prices

Supervisors shall examine whether the business operator meets the following requirements when determining prices:

a. To set purchase and sale prices in yen terms and take into consideration prices in domestic and overseas markets, foreign exchange rates and other factors in determining prices. In addition, the business operator must purchase gold products from the supplier at the market price in the Cash Forward Trade and set the resale price and the purchase and sale prices for customers based on the market price.

b. To indicate purchase and sale prices at all branches handling gold products on a daily basis and execute transactions at those prices, while refraining from placing market orders and forward orders.

(iv) Custody

Supervisors shall examine whether the business operator meets the following requirements regarding

custody:

A. To refrain from transferring to other parties or pawning the certificates of custody issued based on the custody of physical gold products, such as the certificate of safe custody of physical gold products, the certificate of claims thereto and the receipt therefor.

B. When a Financial Instruments Business Operator which handles physical gold products engages in custodial trade, it must procure and store physical products equivalent in amount to the products handled in the custodial trade.

C. To notify customers in writing of the outstanding balance of gold products in custody at least once every year.

(v) Buyback

Whether the Financial Instruments Business Operator agrees, in principle, to over-the-counter purchase of gold bullion (including gold bullion in custody) that it has sold to customers, upon their request.

(vi) Agency Business, etc.

Supervisors shall examine whether the Financial Instruments Business Operator limits the Agency Business, etc., to those related to the Cash Forward Trade and the Cumulative Gold Bullion Investment as specified below.

A. Commissioned Agency Business, etc., Related to Cash Forward Trade

a. The Agency Business, etc., related to the Cash Forward Trade shall include brokering between customers and Offering Financial Instruments Business Operators, etc., and implementing all or part of the processes related to the Cash Forward Trade made between the customers and the Inviting Financial Instruments Business Operators, etc., on behalf of the Offering Financial Instruments Business Operators, etc. A Financial Instruments Business Operator engaging in the Agency Business, etc., related to the Cash Forward Trade shall sign a contract regarding the Agency Business etc., with the Offering Financial Instruments Business Operators, etc.

b. Financial instruments business operators engaging in the Agency Business, etc., related to the Cash Forward Trade shall meet the following requirements:

i) Financial instruments business operators engaging in the Agency Business, etc., related to the Cash Forward Trade shall provide customers with sufficient explanations to enable them to understand that the counterparties to their Cash Forward Trades are Offering Financial Instruments Business Operators, etc., and obtain their prior consent regarding this.

ii) Financial instruments business operators engaging in the Agency Business, etc., shall periodically check with Offering Financial Instruments Business Operators, etc., to confirm the contents of the customers' transactions.

B. Commissioned Agency Business, etc., Related to Cumulative Gold Bullion Investment

a. The Agency Business, etc., related to the Cumulative Gold Bullion Investment shall include brokering between customers and Offering Financial Instruments Business Operators, etc., and implementing all or part of the processes related to the Cumulative Gold Bullion Investment made between the customers and the Offering Financial Instruments Business Operators, etc., on behalf of the Offering Financial Instruments Business Operators, etc. The Financial Instruments Business

Operators engaging in the Agency Service, etc., related to the Cumulative Gold Bullion Investment shall sign a contract regarding the Agency Business, etc., with the Offering Financial Instruments Business Operators.

b. Financial instruments business operators engaging in the Agency Business, etc., related to the Cumulative Gold Bullion Investment shall meet the following requirements:

i) Financial instruments business operators engaging in the Agency Business, etc., related to the Cumulative Gold Bullion Investment shall provide customers with sufficient explanations to enable them to understand that the counterparties to their the Cumulative Gold Bullion Investment transactions are Offering Financial Instruments Business Operators, etc., and obtain their prior consent regarding this.

ii) Financial instruments business operators engaging in the Agency Business, etc., shall periodically check with Offering Financial Instruments Business Operators, etc., to confirm the contents of the customers' transactions.

(2) Businesses Related to Signing of Association Contracts as Specified under Article 667 of the Civil Code and the Corresponding Intermediary, Brokerage and Agency Businesses, and Businesses Related to Signing of Anonymous Association Contracts as Specified under Article 535 of Commercial Code and the Corresponding Intermediary, Brokerage and Agency Services (excluding the businesses specified under Article 2(8)(ix) of the FIEA)

When soliciting customers to sign association contracts, whether Financial Instruments Business Operators and their officers and employees provide sufficient explanations regarding the contents of the contracts and make solicitation in an appropriate manner suited to the customers' intentions and their knowledge and experience regarding the relevant associations, as well as their financial capacity and the nature of their investment funds. At the time of the signing of the contracts, whether they provide the customers with written explanations regarding the contents of the contracts.

(3) Business Related to Signing of Loan Participation Contracts and the Corresponding Intermediary, Brokerage and Agency Services.

(i) Description of Business

The loan participation contract is a contract envisaged by "Accounting Treatment and Representation of Loan Participation," a report issued on June 1, 1995 by the Japanese Institute of Certified Public Accountants.

(ii) Conduct of Business

Supervisors shall examine whether the Financial Instruments Business Operator meets the following requirements regarding the conduct of business:

A. To take due care to protect the original debtors and the transferees when executing business.

B. To provide the transferees with sufficient explanations regarding the nature and contents of the relevant debts.

C. To establish adequate arrangements and procedures for evaluating the relevant debts and ensure

appropriate price formation

D. To provide appropriate solicitation in light of the transferees' intentions, experiences and financial capacity.

E. At the time of the signing of the contract, to provide the transferee with written explanations regarding the contents of the contract.

VI-3-2-3 Investment Report

(1) Items Concerning Discretionary Investment Management Services to be Entered in an Investment Report

(i) With regard to the items to be entered in an investment report prescribed in Article 42-7(1) of the FIEA and in Article 134(1)(ii) of the FIB Cabinet Office Ordinance, they shall include, in the cases where assets of a number of clients are jointly managed, the total amount of assets to be jointly managed, the financial composition, name, number and price of securities, etc., comprising the said assets, as well the said clients' shares of the said assets and values corresponding to their shares.

(ii) Items to be entered, as prescribed in Article 134(1)(iv) of the FIB Cabinet Office Ordinance, shall include details of transaction fees and account management fees when such fees are paid separately from rewards for the discretionary investment contract under an integrated contract of discretionary investment management services and security-related services.

(iii) With respect to details of transactions to be entered, as prescribed in Article 134(1)(vi) of the FIB Cabinet Office Ordinance, it is not necessary to enter the price and quantity of each of the agreed transactions; instead, they can be simplified in light of the purpose and characteristics of transactions. For example, it is sufficient to list the types of mutual transactions of managed assets (requirements, etc., prescribed in each item of Article 129(1) of the FIB Cabinet Office Ordinance).

(2) Details of Items to be Entered in a Report on Investment Trust Asset Management

A management report concerning investment trust assets, in accordance with the provisions of Article 14-1 of the Investment Trust Act, shall be prepared so as to be easily understood by investors, and the following items, which are pursuant to Article 58(1) of the Rules for Calculation of Investment Trust Assets (hereinafter referred to as "Investment Assets Calculation Rules") shall be included. Furthermore, appropriate responses shall be given when referrals are made.

(i) Process of Asset Management During the Calculation of the Said Investment Trust Assets

A. The state of net asset value at the beginning, during and at the end of the period shall be included. In addition, the relationship between the management policy of the investment trust assets of the said investment trust and the "future management policy" described in the investment report of the previous term (examination results on whether investment activities have been in compliance with the management policy) shall be included.

B. The future management policy shall be described specifically, and shall be based on the management policy for investment trust assets of the said investment trust.

C. With respect to dividend from the current term's profits, the grounds for the determination of the

dividend and future management policy for retained earnings shall be included.

(ii) Transition of Management Status

A. In accordance with the categories below, management performance during the corresponding period below shall be included (referring to the performance that allows accurate understanding of the status of investment trust assets, such as net asset value, dividends, rate of fluctuation during the current term, beneficiaries yield, stock price indices, composite ratio of major investment target assets or percentage of outstanding principal, etc.).

a. Unit-type investment trust: from the start of the trust to the end of the current term.

b. Open investment trust (excluding those applicable to c. or d. below): At least five periods prior to the current term (however, at least five formulation periods prior to the current formulation period in the cases where the provision of Article 59(1) of the rules for investment asset calculation applies).

c. Open bond investment trust (excluding those applicable to d. below): At least three periods prior to the current terms (however, at least three formulation periods prior to the current formulation period in the cases where the provision of Article 59(1) of the rules for investment asset calculation applies).

d. Open bond investment trust whose calculation period is one day: at least one formulation period.

B. As a tool for the comparison between net asset value and market conditions during the current term, when the management policy for investment trust assets of the said investment trust adopts the management method that is linked with specific indices, in addition to the ratio of fluctuation of the calculation period of trust, the movement of the said indices shall be included.

(iii) The number of stocks at the end of both the previous and current periods, the aggregate market value by stock at the end of the current period and total transaction volume and total transaction value of stocks during the calculation period of the said investment trust asset.

A. Stocks include warrant. In this case, “the number of stocks” shall be replaced with “number of accounts.”

B. List by currency (in the case of Euro, list by country).

C. List by stock. In the case of domestic stocks (excluding warrants), list by business sector, together with proportion of business sector to the aggregate domestic market value at the end of the current period.

D. With respect to aggregate domestic market value and aggregate domestic market value of warrants at the end of the current period, list each of their proportions to the total value of net investment trust assets.

E. With respect to aggregate foreign market value and aggregate foreign market value of warrants at the end of the current period, list each of their proportions to the total value of net investment trust assets.

F. Transaction volume and transaction value of stocks in the said calculation period shall be listed by sales transaction and by purchase transaction. Changes (increase or decrease) due to capital increase/reduction, stock split, or change in par value shall be listed in the brackets, and a note shall be provided to that effect.

G. List the stock transaction ratio and transaction fees per beneficiary right during the relevant calculation

period

(vi) List by type and name of each bond, aggregate market value at the end of the current period and total transaction value of the relevant investment trust asset during the calculation period.

A. List by type of currency. (In the cases where Article 59(1) of the rule for calculation of investment trust assets applies, the total amount is sufficient, regardless of the type of currency. In the case of Euro, list by country.)

B. Types shall be classified into national bond certificates, local bond certificates, special bond certificates, warrants, and other bond certificates.

C. List by stock name.

D. Total transaction value during the relevant calculation period shall be classified into sales and purchase, and increase/reduction through allocation of bonds with warrants, redemption or exercise of warrants shall be listed in the brackets, and a note is given to that effect.

(v) The items shall be listed by name, as specified in Article 58 (1)(v) of the Rules for Calculation of Investment Trust Assets, with respect to investment trust beneficiary certificates (excluding mother fund beneficiary certificates, hereinafter the same shall apply in (2)), mother fund beneficiary certificates and investment corporation investment certificates

A. List by currency (in the case of Euro, list by country)

B. List the transaction commission fees per mother fund beneficiary certificate for the relevant calculation period. In this case, with respect to transaction commission fees for an investment trust that incorporates the said mother fund beneficiary certificates (hereinafter referred to as “baby fund”), list the part corresponding to the said baby fund of the mother fund.

(vi) In the cases where securities loans are made at the end of the current period, they shall be classified according to total number of stocks or aggregate face value, and type of bond, while the total number of stocks shall be used for stocks and the aggregate face value shall be used for bonds.

(vii) With respect to transactions of securities-related derivatives (referring to the transactions of securities-related derivatives prescribed in Article 2(20) of the FIEA; the same shall apply hereinafter) among transactions of derivatives (referring to the transactions of derivatives prescribed in Article 28(8)(iii) of the FIEA; the same shall apply hereinafter), the outstanding contract balance of the transactions or the transaction balance at the end of the current period and contract transaction value or transaction value during the calculation period of the relevant investment trust asset shall be listed by type.

The outstanding contract balance of the transactions at the end of the current period and contract transaction value or transactions value during the calculation period of the relevant investment trust asset shall be classified and listed by transaction of stocks or by transaction of bonds, etc. (However, in the cases where Article 59(1) of the Investment Assets Calculation Rules applies, it is acceptable to list the balance as of the day prior to the last business day of each month and the total transaction value by sales/purchase during the relevant calculation period, regardless of the above.)

(viii) Rights related to transactions of derivatives, except for transactions of securities-related derivatives, shall be listed by type, including outstanding contract balance as of the end of the current period or trading value and transaction contract value during the calculation period of the relevant investment trust assets.

Asset balance at the end of the current period and management status during the calculation period of the relevant investment trust assets shall be presented in such a way to be easily understood by investors.

(ix) The items listed in Article 58(1)(viii) of the Investment Assets Calculation Rules shall be listed by real estate, leasehold right or surface right of real estate.

Asset balance at the end of the current period and management status during the calculation period of the relevant investment trust assets shall be listed in categories such as real estate, real estate leasehold right or surface right.

(x) The amount of claims as of the end of the current period and aggregate transaction value during the calculation period of the relevant investment trust assets shall be listed for notes prescribed in Article 3(vi) of the Enforcement Order of the Investment Trust Act.

Asset balance at the end of the current period and management status during the calculation period of the relevant investment trust assets shall be presented in such a way to be easily understood by investors.

(xi) With respect to monetary claims prescribed in Article 3(vii) of the Enforcement Order of the Investment Trust Act, the total amount of claims as of the end of the current period shall be listed by type and the aggregate transaction value during the calculation period of the relevant investment trust assets shall be listed by type of claims.

Asset balance at the end of the current period and management status during the calculation period of the relevant investment trust assets shall be presented in such a way to be easily understood by investors.

(xii) With respect to assets prescribed in Article 3(viii) of the Enforcement Order of the Investment Trust Act and assets other than specified assets, major details of assets under management as of the end of the current period shall be listed by type.

Asset balance at the end of the current period and management status during the calculation period of the relevant investment trust assets shall be presented in such a way to be easily understood by investors.

(xiii) With respect to specified assets and other assets listed in item (i) or from item (iii) through item (viii) of Article 3 of the Enforcement Order of the Investment Trust Act as of the end of the current period, the percentage of total value of each asset against the total amount of investment trust assets shall be listed.

The percentage shall be the proportion of the total amount of each asset (by name in the case of mother fund beneficiary certificates) to the total amount of investment assets. Also the percentage of aggregate net assets pertaining to assets in foreign currencies as of the end of the current period against the total amount of investment assets shall be provided in the Note.

(xiv) In the cases where assessment on prices of specified assets has been conducted pursuant to the provision of Article 11(1) of the Investment Trust Act, the name of the person who has conducted the said assessment and the outline of the result and method of the said assessment shall be given.

With respect to the outline of the results and method of the said assessment, type and items of specified assets on which the said assessment was conducted and the qualification, etc., of the assessor shall be included in such a way to be easily understood by investors.

(xv) Status of assets, liabilities, principals and net asset values of beneficiary certificates as of the end of the current period and the status of the profit or loss of the relevant investment trust assets during the calculation period shall be given.

In the cases where there are noted items set forth in the calculation rules for investment trust assets, the said items should be presented in the Note.

(xvi) The status of transactions with an interested person, etc., during the calculation period of the relevant investment trust assets, and the transaction status of the total amount of commission fees paid to the relevant interested person, etc., shall be classified into sales amount and purchase amount by type of security, derivative transaction, and other transaction, and the trading value with interested persons and the percentage against the total amount of each item shall also be included.

(xvii) In the cases where an investment trust management company, etc., is engaged in Type I financial instruments business or Type II financial instruments business, the status of transactions with the said investment trust management company, etc., during the calculation period of the relevant investment trust assets and the total amount of commission fees paid to the said investment trust management company, etc., shall be listed. The trading status shall be grouped into sales amount and purchase amount by type, such as securities and derivative transactions, and the amount of internal transactions and the percentage against the total amount of each item shall be given.

(xviii) In the cases where an investment trust management company, etc., is engaged in real estate business, the status of transactions with the investment trust management company, etc., which is a real estate transaction business operator, during the calculation period of the relevant investment trust assets and the total amount of commission fees paid to the said investment trust management company, etc., shall be listed. The status of transactions shall be classified into sales/purchases, leasing, etc., by type of real estate, and the amount of internal transactions and the percentage against the total amount of each item shall be given.

(xix) In the cases where an investment trust management company, etc., is engaged in specified real estate cooperative business, the status of transactions with the investment trust management company, etc., which is the specified real estate cooperative business operator, during the calculation period of the relevant investment trust, assets shall be listed. The status of transactions shall be classified into sales/purchases, leasing, etc., by type of real estate, and the amount of internal transactions and the percentage against the total amount of each item shall be given.

(xx) In the case of termination of the said trust contract, a summary of investment trust asset management shall be prepared. The outline of the process of management from the start of the said trust to the end of the previous period shall also be included. Meanwhile, when the outline of the process of the said management is given in (i) above, the outline of the process of the said management may be omitted. The term “the status at the end of every calculation period” in Attached List of Formats No. 2 of the Calculation Rules for Investment Trust Assets under the provision of Article 59 (1) of the said rules may be replaced by “the status at the end of every formulation period.”

(3) Items to be Listed in an Investment Report of Investment Trust Fund Without Instruction by Trustor

The criteria for specific items to be included pursuant to each item of Article 58(1) of the Investment Assets Calculation Rules, applied mutatis mutandis pursuant to Article 62 of the said rules, shall be equivalent to (2) above.

(4) Items to be Listed in an Investment Management Report Pertaining to Investment Corporations

An investment management report to be prepared pursuant to the provision of Article 129(2) of the Investment Trust Act shall be prepared in such a way to be easily understood by investors, and the criteria for specific items to be included pursuant to Article 71 of the Calculation Rules for Investment Corporations (hereinafter referred to as the "Investment Corporation Calculation Rules") shall be given pursuant to (2) above; provided, however, that this shall not apply when it may cause difficulty in understanding the status of property or profit/loss of investment trust corporations.

In the cases where an investment trust management company, etc., which has entered into an asset management contract, manages the assets of an investment corporation jointly with another investment trust corporation, the aggregate value of assets under joint management of the said investment trust management company, the type of the said assets, the share of the said investment corporation concerning the said assets, and the amount equivalent to its share shall be entered as items required to clarify the status of management of an investment corporation during the relevant business period, as prescribed in Article 73(1)(xx) of the Investment Corporation Calculation Rules.

VI-3-2-4 Account Documents Regarding Investment Trust Assets

III-3-3(1) (excluding (ii), (iii), (v) to (vii), and (ix)) shall be applied mutatis mutandis to the supervision of account documents regarding investment trust assets compiled and stored based on the Investment Trust Act, and attention shall also be paid to following points:

(1) Of account documents compiled and stored based on the Investment Trust Act, those that may be stored by the electromagnetic method are the account documents as specified under Article 26(1), Article 254(1) and Article 255(1) of the Ordinance for Enforcement of the Investment Trust Act.

(i) Points of Attention Regarding Compilation and Storage of Account Documents in Microfilm Form

A. Microfilm used for storage must have the durability sufficient for the storage periods prescribed for each category of documents as shown below.
   a. Account documents related to investment trust assets: 10 years from the expiry of the accounting period or the trust contract period of relevant investment trusts assets, as specified under Article 26(2) of the Ordinance for Enforcement of the Investment Trust Act.
   b. Account books related to investment corporations: 10 years from the approval of the financial results of relevant investment corporations, as specified under Article 254(2) of the Ordinance for Enforcement of the Investment Trust Act (from the closing of the account book in the case of a commercial account book).
   c. Account documents related to asset custody companies: 10 years from the approval of the financial results of relevant investment corporations as specified under Article 255(2) of the Ordinance for Enforcement of the Investment Trust Act.

B. One of the microfilms used for data storage must be selected and specified as the original.

C. It must be ensured that a back-up of the original as specified in B. above is made and stored as a copy.

D. It must be ensured that account books required for inspection by inspection departments are compiled

within a reasonable period of time.

E. A person in charge of making and storing microfilms must be appointed and procedures for the management of microfilms must be established.

(ii) Points of Attention Regarding Compilation and Storage of Account Documents by Electromagnetic Method

A. The durability of the media used for storage is subject to the requirements specified in (i)A. above.

B. It must be ensured that the computer system used for storage prevents data falsification and mishandling by requiring IDs and passwords for data access and input.

C. In addition to A. and B. above, III-3-3(6)(i), (iii), (iv) and (vi) to (x) shall be applied mutatis mutandis.

VI-3-2-5 Criteria for Items to be Included in Notification of Foreign Investment Fund

The criteria for items to be included in a notification of a foreign investment fund prescribed in each item of Article 58 (1) of the Investment Trust Act and each item of Article 96 (2) of the Ordinance for Enforcement of the Investment Trust Act shall be as follows:

(1) Items Related to Trustors (limited to the cases similar to investment trust fund without instruction by trustor), Trustees, and Beneficiaries

(i) Items Related to Trustors

The name, amount of capital, details of business and outline of operations of a trustor (name of the company that manages the said foreign investment fund, and the management company in the cases of a management company which is entrusted with the management of investment trust assets by a company that manages a foreign investment fund) shall be entered.

(ii) Items Related to Trustees

The name, the amount of capital, details of business and outline of operations of a trustee (custody company) shall be entered.

(iii) Items Related to Beneficiaries

Details of the right to dividend, the right to redemption, the repurchase right, and other rights (including the date of emergence and termination of rights) and procedures for the exercise of rights shall be entered.

(2) Items Related to Beneficiary Certificates

(i) Name of the relevant foreign investment fund

(ii) Form of foreign investment fund

Items regarding registered or bearer form, par-value or no par-value, open end type or closed end type, exchange of registered form and bearer form, transfer of registered beneficiary certificates, and re-issuance of beneficiary certificates shall be entered.

(iii) Number issued (offered)

(iv) Total value of issues (offered)

When submitting notification of a foreign investment fund without entering the “issue price” or “offer price,” the estimated total values as of the date of submission of the said notification shall be entered with a

note to that effect.

(v) Issue (offer) price

When submitting notification of a foreign investment fund without entering the "issue price" or "offer price," a note specifying the scheduled date and method of determining the price shall be given.

(vi) Subscription fee

A. In the cases where subscription fees at each subscription handling office are different, the subscription fee of each office shall be listed. When subscription fees cannot be disclosed due to compelling reasons, a note to that effect shall be given.

B. When fees change, subject to the volume and value of subscription, the fees of the said volume and value at each stage shall be listed.

(vii) Subscription unit

(viii) Subscription period

(ix) Others

A. The method of subscription, interest on deposit for subscription, transfer of deposit of subscription to investment trust assets, and items related to other subscriptions, etc., shall be entered.

B. In the cases where the said subscription, etc., of the said foreign investment fund is handled in areas other than Japan, the number of issues (offered) and total value of issues (offered) shall be entered.

(3) Items Related to Administration and Management of Trust

(i) Administration of Trust

A. Items related to administration of a fund entrusted to a trustee until its redemption

Formulation of management report on investment trust assets, method of treatment of profits, and items related to partial cancellation, etc., shall be entered.

B. Others

Procedures concerning change in the conditions and modification of a contract with related companies, items related to the method of disclosure when changes are made, and other important items shall be entered.

(ii) Management of Trust

A. Basic policy of management

The basic attitude concerning management of investment trust assets shall be described in a detailed manner.

B. Investment target

The type of assets to be invested in, investment criteria, and proportion of planned investment by type or region, if any, etc., shall be given.

C. Investment limit

a. The grounds for all the investment limits prescribed in the laws and regulations or contracts, etc., shall be described.

b. The presence of limits to the underwriting of securities, margin trading, borrowing, concentrated investment, investment in other funds, investment in assets with less liquidity and the grounds and

details of such limits, if any, shall be given.

D. Dividend policy

The dividend policy prescribed in the contracts, etc., shall be listed.

E. Loan of assets

Details of loans of assets acquired from investment trust assets

(4) Items Related to Calculation of Trust and Distribution of Profits

(i) Items Concerning Calculation of Trust

A. Appraisal of assets

Method and frequency of calculation and method, frequency, and place of disclosure of net value of assets per unit of beneficial certificates of foreign investment funds (including evaluation of assets to be invested in) shall be entered.

B. Administration rewards, etc.

Items regarding all rewards and commission fees paid from investment trust assets of a foreign investment fund, the method of calculation, amount of payment, method of payment, and time of payment by each receiver shall be listed.

C. Others

Period of existence of foreign investment fund, calculation period of trust, requirements for limited redemption, etc., in relation to addition and partial cancellation shall be entered.

(ii) Items Related to Distribution of Profits

A. Items related to the calculation of the possible amount of dividend shall be listed.

B. Regarding payment of profits and distribution of payments at the time of redemption, delivery from beneficiary to trustor (limited to those similar to an investment trust fund with instruction by trustor), immunity of trustee, and delivery from trustor (limited to those similar to an investment trust fund with instruction by trustor) to beneficiary, time, place and method shall be entered.

(5) Items related to the transfer of all or part of business (limited to those similar to an investment trust fund with instruction by trustor), procedures for business transfer, method of notification to beneficiaries, and the details of objection if a beneficiary is entitled to oppose the business transfer.

(6) Items Related to Resignation and Removal of Trustee and Appointment of New Trustee

Procedures for resignation and removal of trustee and the appointment of a new trustee shall be described.

(7) When a trustor entrusts another party with power regarding instruction of management (limited to those similar to an investment trust fund with instruction by trustor) or when a trustee entrusts another party with management power (limited to those similar to an investment trust fund without instruction by trustor), details of the entrustment, specific details of entrusted power and the cost of entrustment shall be entered.

(8) Name of Financial Instruments Business Operator Which Handles Subscriptions in Japan

The names of all Financial Instruments Business Operators which handle subscriptions shall be listed.

VI-3-2-6 Criteria for Items to be Entered in an Investment Report on Investment Trust Assets of Foreign Investment Funds

Investment report on investment trust assets prescribed in Article 14 of the Investment Trust Act applied mutatis mutandis to Article 59 of the Investment Trust Act shall be prepared in such as way to be easily understood by investors, and specific operations for items to be included in each item of Article 63(1) of the Investment Assets Calculation Rules shall pay attention to the following points and necessary responses shall be given when referrals are made.

(1) Process of Asset Management During the Calculation Period of Investment Trust Assets Related to the Relevant Foreign Investment Fund

(i) The state of net asset value at the beginning, during, and at the end of the period shall be included. Also, the relationship with the management policy of the investment trust assets of the said foreign investment fund shall be described.

(ii) The future management policy shall be prepared based on the investment report of the said foreign investment fund.

(iii) The amount of dividend per unit, the right to which has been fixed during the current term, shall be entered.

(iv) With regard to an investment report on investment trust assets at the time of termination of trust, the outline of the management process from the acquisition to termination of the said trust shall be given.

(2) Change in Management Status

(i) Management performance (net asset value, dividend, etc.) of the previous ten terms shall be given.

(ii) As a tool for the comparison between net asset value and market conditions during the current term, when the management policy for investment trust assets for the said investment trust adopts a form of management that is linked with specific indices, the movement of the said indices shall be included.

(3) The balance sheet as of the last day of the calculation period of investment trust assets of the relevant foreign investment fund (referred to as “end of current term” in VI-3-2-6) and a statement of income and a statement of retained earnings during the relevant calculation period, and their notes shall be given.

(i) The balance sheet and its notes at the end of the current term shall be included.

(ii) A statement of income and a statement of retained earnings during the relevant calculation period, and their notes shall be included. The amount of loss shall be represented by “△”, “–”, or in the bracket.

(4) Statement of Net Assets at the End of the Current Term

(i) The number of issuance units of the foreign investment fund at the end of the current term shall be specified and the value of net income per unit shall be given, which is to be obtained by dividing aggregate net assets by the number of issuance units.

(ii) When the relevant items are given in the balance sheet of (3) above, the statement of net assets may be replaced by the said balance sheet.

(5) Major Names of Security Certificates to be Invested in

(i) Regarding the top 30 valuations among invested stocks at the end of the current term or on the most recent date as of the formulation of the investment report on investment trust assets, the name of stocks, quantity, monetary value and investment ratio shall be included.

(ii) In lieu of (i) above, monetary value and the investment ratio of securities and the place of issuance of stocks and non-stock securities, at the end of the current term or on the most recent date as of the formulation of the investment report on investment trust assets, shall be given by type of securities, place of issuance or region of listed financial instruments exchange, etc.

(6) Major Types of Real Estate to be Invested in and Real Estate Leasehold Rights or Surface Rights

Asset balance at the end of the current period and the management status during the calculation period of the relevant investment trust assets shall be listed by categories, such as real estate, and real estate leasehold rights or surface rights.

(7) Major Types of Money Claims to be Invested in

Assets outstanding at the end of the current term and the management status during the calculation period of the said investment trust assets shall be presented in such a way to be easily understood by investors.

(8) Major Types of Drafts to be Invested in

Assets outstanding at the end of the current term and the management status during the calculation period of the said investment trust assets shall be presented in such a way to be easily understood by investors.

(9) Assets to be Invested in as Specified in Article 3 (viii) of the Enforcement Order of the Investment Trust Act and Equivalent Thereto

Assets outstanding at the end of the current term and the management status during the calculation period of the said investment trust assets shall be presented in such a way to be easily understood by investors.

(10) Besides those listed in each of the previous items, items to be included in an investment report formulated pursuant to the Japanese laws and regulations under which the relevant foreign investment fund is established (items equivalent to those to be included pursuant to Article 58(1) of the calculation rules for investment assets, in the cases where no specific statute applies to investment reports formulated pursuant to the Japanese laws and regulations under which the relevant foreign investment fund is established).

In the cases under Article 58(1) of the Investment Assets Calculation Rules, items in accordance with VI-3-2-3-(2) shall be entered.

VI-3-2-7 Items to be Included in Notification on Foreign Investment Corporations

The following are the items to be included in a notification of foreign investment funds prescribed in Article 220(1) of the Investment Trust Act and each item of Article 261(2) of the Ordinance for Enforcement of the Investment Trust Act.

(1) Objectives, Trade Name, Address

(i) Objectives

A. The objectives listed in the bylaws of foreign investment corporation or equivalent thereto shall be included.

B. The number of issuances (offer), total value of issue (offer), issue price (offer price), subscription fees, subscription unit, subscription period, etc., shall be listed pursuant to VI-3-2-5 (2).

(ii) Trade Name and Address

The trade name and address (name in the original language shall be attached) shall be listed in the registry of foreign investment corporations or equivalent thereto.

(2) Items Related to Organization and Officers

(i) Items Related to Organization

A. The name and details of the organization of the relevant foreign investment corporation

B. The names and outlines of relevant businesses of corporations concerned (a juridical person equivalent to an asset management company, asset deposit company or equivalent thereto, or a juridical person entrusted with administrative work or equivalent thereto) involved in the management of the said foreign investment corporation shall be included, in addition to those of companies issuing foreign investment certificates for the relevant foreign investment corporation.

(ii) Items Related to Officers

The names, addresses and duties of officers of the foreign investment corporation (details of duties of personnel equivalent to executive officers or supervisory officers of investment corporations) shall be listed.

(3) Items Related to Administration and Management of Assets

(i) Items Related to Administration of Assets

A. Items related to the administration of assets conducted until the dissolution of the relevant foreign investment corporation shall be listed.

B. Others

Changes in the bylaws or the equivalent documents and procedures concerning changes in the contract with concerned companies, items related to the disclosure method of such changes, and other important items shall be included.

(ii) Items Related to Asset Management

A. Basic policy of management

Specific details about the basic attitude toward the management of assets shall be included.

B. Investment target

The type of assets to be invested in, investment criteria, and the proportion of planned investment by type or region, if any, etc., shall be given.

C. Investment limit

a. Grounds for all investment limits prescribed in laws, regulations and bylaws, etc., or other documents equivalent thereto, etc., shall be described.

b. The presence of limits to the underwriting of securities, margin trading, borrowing, concentrated investment, investment in other funds, and investment in assets with less liquidity and grounds for and details of such limits, if any, shall be mentioned.

D. Dividend policy

The dividend policy prescribed in bylaws or other documents equivalent thereto shall be included.

(4) Items Related to Calculation and Distribution of Profits

(i) Items Related to Calculation

A. Asset

The method and frequency of calculation and the method, frequency and place of disclosure of net value of assets per unit of foreign investment certificates (including evaluation of assets to be invested in) shall be entered.

B. Administration rewards, etc.

Regarding all rewards and commission fees paid from the assets of the foreign investment corporation, the method of calculation, amount of payment, method of payment and time of payment classified by each receiver shall be listed.

C. Others

The period of existence of the foreign investment corporation, fiscal year, limits on additional contribution and return of contribution, and conditions for dissolution, etc., shall be entered.

(ii) Items Related to Profit Distribution

Items related to the payment of profits at the time of dissolution or the distribution of profits at the time of each settlement shall include the time, place, method of delivery from an asset custody company to a foreign investment company, immunities of an asset custody company, and delivery from trustor to investor or party equivalent thereto.

(5) Items Related to the Rights Indicated on Foreign Investment Certificates

Details of voting rights, the rights of investors or other persons equivalent thereto, the right to receive dividend, the right to receive settlement (including the date of emergence of termination of rights) and procedures for exercise of rights shall be included.

(6) Items Related to Distribution or Redemption

Details of the claim for distribution or redemption of the relevant foreign investment corporation (including the date of emergence and termination of rights) and the procedures for exercise of rights shall be included.

(7) Items Related to Transfer of All or Part of Business of a Party Equivalent to an Asset Management Company

The procedures of business transfer, the method of notification to investors or parties equivalent thereto, and details of objections if investors or parties equivalent thereto are entitled to oppose the business transfer.

(8) Items Related to Resignation of a Party Equivalent to Asset Custody Company and Appointment of New Asset Deposit Company or a Party Equivalent Thereto

The procedures for resignation of a party equivalent to an asset custody company, and the appointment of a new asset depository company or a party equivalent thereto shall be described.

(9) Details of Entrustment When a Party Equivalent to Asset Custody Company Entrusts the Power to Manage Assets of Another Party

Specific details of entrusted power and the cost of such entrustment shall be listed.

VI-3-3 Points of Attention Regarding Administrative Processes Related to Investment Corporations

VI-3-3-1 Notification of Changes Related to and Dissolution of Registered Investment Corporations

(1) Notification of Changes Related to Registered Investment Corporations

(i) VI-3-1-2(3)(i) and (ii) shall be applied mutatis mutandis to the notification of changes related to registered investment corporations.

(ii) Notifications of changes related to registered investment corporations, based on Article 191(1) of the Investment Trust Act, that are received by the director-general of a Local Finance Bureau (excluding notifications of a relocation of the head office from a region under the jurisdiction of one Local Finance Bureau to a region under the jurisdiction of another) shall be collectively reported each month to the FSA Commissioner by the 15th day of the following month, in the format specified in the Attached List of Formats VI-6.

(iii) In cases where an investment corporation's notification of a change has revealed that a new executive officer meets the provision of any of Article 98(ii) to (v) of the Investment Trust Act, that a new supervisory officer meets the provision of any of the items of Article 100 of the Investment Trust Act, or that a new accounting auditor meets the provision of any of the items of Article 102(3) of the Investment Trust Act, the director-general of the relevant Local Finance Bureau shall immediately instruct the investment corporation to take corrective action. If corrective action is not taken immediately, the registration shall be rescinded based on Article 216(1) of the Investment Trust Act.

(2) Notification of Cross-Jurisdictional Relocation of Head Office

(i) When the director general of a Local Finance Bureau has received notification of a relocation of the head office from a region under the jurisdiction of his/her bureau to a region under the jurisdiction of another bureau, he/she shall send the notification document with an opinion of his/her bureau and the results of the most recent inspection attached thereto, in the format specified in the Attached List of Formats VI-7, to the director-general of the Local Finance Bureau to which the authority over the relevant registered investment

corporation will be transferred, in addition to implementing the procedures specified under Article 275(1) of the Ordinance for Enforcement of the Investment Trust Act.

(ii) When the director-general taking over the authority over the registered business operator has completed registration change procedures based on Article 275(2) of the Ordinance for Enforcement of the Investment Trust Act, he/she shall immediately notify the director-general who previously had the authority via e-mail, etc or through other means.

(iii) The director-general who previously had the authority shall cancel the registration of the relevant investment corporation after being notified, by the director-general who has taken over the authority, of the completion of the registration of the relocation based on Article 275(2) of the Ordinance for Enforcement of the Investment Trust Act.

(iv) Relocations of the head offices registered each month shall be collectively reported to the FSA Commissioner by the directors-general of Local Finance Bureaus who have taken over the authority, by the 15th day of the following month in the format specified in the Attached List of Formats VI-8.

(3) Notifications of Dissolution of Investment Corporations

Notifications of dissolution of investment corporations (the format is as specified in the Attached List of Formats XVII of the Ordinance for Enforcement of the Investment Trust Act) received by the directors-general of Local Finance Bureaus shall be collectively reported each month to the FSA Commissioner by the 15th day of the following month, in the format specified in the Attached List of Formats VI-9.

VI-3-3-2 Business Performance Reports

Procedures to be implemented by the directors-general of Local Finance Bureaus are as follows.

(1) Reports to FSA Commissioner

Business performance reports received by the director-general of a Local Finance Bureau, under Article 212 of the Investment Trust Act, shall be compiled in the business performance summary table as specified in the Attached List of Formats VI-10 for each reporting period (every six months if the reporting period is shorter than six months) and reported to the FSA Commissioner.

VI-3-3-3 Extraordinary Reports

Procedures to be implemented by the directors-general of Local Finance Bureaus are as follows.

(1) The director-general of a Local Finance Bureaus, upon receiving an extraordinary report, based on Article 215(1) of the Investment Trust Act, shall immediately send a copy thereof to the FSA Commissioner.

(2) Notice to Investment Corporations

Directors-general of Local Finance Bureaus shall hold consultations with the FSA before giving notice, based on Article 215(2) of the Investment Trust Act, to an investment corporation.

It should be noted that the directors-general shall report the results of the deliberations made by their bureaus

and express the opinions thereof in the consultations.

VI-3-3-4 Consultations, etc., with FSA about Permissions and Administrative Actions Regarding Investment Corporations, etc

(1) Consultations with FSA about Permissions for Investment Corporations, etc.

(i) The directors-general of Local Finance Bureaus shall hold prior consultations with the FSA with regard to the following permissions and approvals, the authority over which is delegated to them as a matter of supervisory process.

A. Permission based on Article 81(4) of the Companies Act as applied mutatis mutandis pursuant to Article 73(4) of the Investment Trust Act

B. Permission based on Article 82(4) of the Companies Act as applied mutatis mutandis pursuant to Article 73(4) of the Investment Trust Act

C. Permission based on Article 297(4) of the Companies Act as applied mutatis mutandis pursuant to Article 90(3) of the Investment Trust Act

D. Permission based on Article 318(5) of the Companies Act as applied mutatis mutandis pursuant to Article 94(1) of the Investment Trust Act

E. Permission based on Article 371(2) or (4) of the Companies Act as applied mutatis mutandis pursuant to Article 115(1) of the Investment Trust Act (including cases where Article 371(4) of the Companies Act is applied mutatis mutandis pursuant to Article 115(5) of the Investment Trust Act)

F. Permission based on Article 433(3) of the Companies Act as applied mutatis mutandis pursuant to Article 128-3(2) of the Investment Trust Act

G. Permission based on Article 442(4) of the Companies Act as applied mutatis mutandis pursuant to Article 132(2) of the Investment Trust Act

H. Permission based on Article 371(2) or (4) of the Companies Act as applied mutatis mutandis pursuant to Article 154-3(2) of the Investment Trust Act (including cases where Article 371(4) of the Companies Act is applied mutatis mutandis pursuant to Article 154-3(5) of the Investment Trust Act)

I. Permission based on Article 500(2) of the Companies Act as applied mutatis mutandis pursuant to Article 157(3) of the Investment Trust Act

J. Approval based on Article 117(viii) of the Enforcement Order of the Investment Trust Act

(ii) The directors-general of Local Finance Bureaus shall hold prior consultations with the FSA with regard to the exercise of the authority regarding the following matters, the authority over which is delegated to matters of supervisory process concerning investment corporations:

A. Order based on Article 307(1) of the Companies Act as applied mutatis mutandis pursuant to Article 94(1) of the Investment Trust Act

B. Appointment of a person responsible for performing the duties of a temporary officer based on Article 108(2) of Investment Trust Act

C. Order based on Article 359(1) of the Companies Act as applied mutatis mutandis pursuant to Article 110(2) of the Investment Trust Act

D. Order based on Article 162 of the Investment Trust Act

E. Application for a court order of the dissolution of an investment corporation based on Article 824(1) of the Companies Act as applied mutatis mutandis pursuant to Article 144 of the Investment Trust Act

F. Application with a court appointment of an administrator based on Article 825(1) of the Companies Act as applied mutatis mutandis pursuant to Article 144 of the Investment Trust Act

G. Appointment of a liquidator or a liquidation supervisor based on Article 151(3) of the Investment Trust Act

H. Appointment of a liquidator or a liquidation supervisor based on Article 151(4) of the Investment Trust Act

I. Appointment of a liquidator or a liquidation supervisor based on Article 151(5) of the Investment Trust Act

J. Dismissal of a liquidator or a liquidation supervisor based on Article 153(1) of the Investment Trust Act

K. Appointment of a liquidator or a liquidation supervisor based on Article 153(1) of the Investment Trust Act

L. Determination of the amount of remuneration for the liquidator based on Article 154(2) of the Investment Trust Act or determination of remuneration for the liquidation supervisor based on Article 154(2) of the Investment Trust Act as applied mutatis mutandis pursuant to Article 154-2(2) of the same act.

M. Appointment of an appraiser of a debt with an undetermined value based on Article 501(1) of the Companies Act as applied mutatis mutandis pursuant to Article 157(3) of the Investment Trust Act

N. Appointment of a person in charge of the storage of account documents based on Article 508(2) of the Companies Act as applied mutatis mutandis pursuant to Article 161 of the Investment Trust Act

O. Appointment of a person responsible for performing the duties of a temporary liquidator or a temporary liquidation supervisor based on Article 108(2) of the Investment Trust Act as applied mutatis mutandis pursuant to Article 153(2) of the same act

P. Immediate appeal based on Article 872 of the Companies Act as applied mutatis mutandis pursuant to Articles 84(2), 139-9(8), 139-10(2), 141(3), 144, 149-3(4). 149-8(4). 149-13(4), 150 and 163

(iii) When the directors-general of Local Finance Bureaus have decided to grant permissions and approvals regarding the above matters, they shall notify the applicants in the format specified in the Attached List of Formats VI-11. When they have decided not to grant permissions or approvals, the notice shall be made in the format specified in the Attached List of Formats VI-12.

(2) Consultations with FSA about Administrative Actions

(i) The directors-general of Local Finance Bureaus shall hold prior consultations with the FSA with regard to the following matters, the authority over which is delegated to them as a matter of supervisory process concerning investment corporations.

It should be noted that the directors-general shall report the results of the deliberations made by their bureaus and express the opinions thereof in the consultations.

A. Order for business improvement based on Article 214(1) of the Investment Trust Act

B. Rescission of registration based on Article 216 of the Investment Trust Act

(ii) In cases where the director-general of a Local Finance Bureau intends to take an administrative action against a person planning to establish an investment corporation or against an investment corporation, and where the said person or investment corporation, an investment management company to which the investment corporation or said person entrusts asset investment, an entity to which the asset investment is re-entrusted under Article 202(1) of the Investment Trust Act, an asset administration company in charge of the relevant assets, or the company undertaking the relevant general clerical work is located in a region under the jurisdiction of another Local Finance Bureau, the said director-general shall, in principle, solicit the opinion of the director-general of the other Local Finance Bureau before taking said administrative action and later communicate the action taken thereto.

(3) Notice to Heads of Relevant Administrative Organizations

When giving notice to relevant administrative organizations based on Article 132(6) and Article 135(1) of the Enforcement Order of the Investment Trust Act, the directors-general of Local Finance Bureaus shall pay attention to the following points:

(i) Notice regarding a registration application based on Article 187 of the Investment Trust Act must be given to the section in charge of the relevant department of the administrative organization concerned immediately after the receipt of the registration application.

(ii) Regarding a report based on the items of Article 132(3) of the Enforcement Order of the Investment Trust Act, the contents of the report must be quickly notified to the section in charge of the relevant department of the administrative organization concerned, by the end of the month following the month of the receipt of the report at the latest.

(4) Re-delegation to Directors-General of Local Finance Offices

Of the administrative processes delegated to the directors-general of Local Finance Bureaus based on Article 135 of the Enforcement Order of the Investment Trust Act, the directors-general may re-delegate the following processes to the directors-general of local Finance Offices that have jurisdiction over the regions where the applicants and the investment corporations are located, as well as to the heads of the Otaru and Kitami Branch Offices.

(i) Administrative processes regarding the receipt of notification related to the establishment of an investment corporation as specified under Article 69(1) of the Investment Trust Act

(ii) Administrative processes regarding the receipt of a notification based on Article 152(1) of the Investment Trust Act

(iii) Administrative processes regarding the receipt of a registration application as specified under Article 188(1) of the Investment Trust Act

(iv) Administrative processes regarding the receipt of a notification of change as specified under Article 191(1) of the Investment Trust Act

(v) Administrative processes regarding the receipt of a notification based on Article 192(1) of the

VI-3-3-5 Issuance of Certificates

(1) Issuance of Certificates to Trust Companies, etc.

(i) Issuance of Certificates Necessary for Reduction of License Registration Tax Regarding Ownership Transfer

The following procedures should be taken with regard to the issuance of the certificate, as specified under Article 31-7(2) of the enforcement rules for the Act for Special Tax Measures, necessary for the reduction of the license registration tax for trust companies, etc., based on Article 83-3(2) of the said act.

It should be kept in mind that a trust company, etc., seeking to become eligible for the provision of Article 83-3(2) of the Act for Special Tax Measures needs to do so within one year from the acquisition of the relevant real estate.

A. An application from a trust company, etc., for a certificate necessary for the reduction of the license registration tax regarding the transfer of ownership and the certificate to be issued by the FSA Commissioner shall be in accordance with the format specified in the Attached List of Formats VI-13.

B. The applicant shall be required to fill out the necessary items of the application form and attach to it a copy of the relevant real estate transaction contract, in order to confirm the dates of the signing of the contract and the real estate acquisition.

C. After the application for a certificate has been submitted, the certificate shall be issued upon the confirmation, made in reference to the attached documents and other materials, of the following points regarding the items specified in the submitted application.

a. Whether it is specified as an investment policy for the relevant investment trust, under the investment trust contract provisions, that the ratio of the total value of specified real estate assets (as specified under Article 83-3(1) of the act for special tax measures) to the total value of specified assets included in the trusts assets of the said investment trust (hereinafter referred to as the specified real estate asset ratio) should be 75% or higher.

b. In cases where funds are borrowed, whether the borrowed funds have been provided by qualified institutional investors as specified under Article 2(3)(i) of the FIEA and designated under a relevant ordinance of the Ministry of Internal Affairs and Communications.).

c. Whether the specified assets invested by the investment trust meet either of the following criteria:

i) The specified real estate asset ratio is 75% or higher.
(When the submitted asset investment report confirms a specified real estate asset ratio of 75% or higher, this criterion shall be deemed to be met.)

ii) The specified real estate asset ratio is expected to rise to 75% or higher when the applicant trust company, etc., acquires the real estate for which it is filing the application.
(In cases where this criterion is to be met, materials showing the status of the specified assets as of the application date shall be required to be attached to the submitted application in the format specified in the Attached List of Formats VI-14 in order for the status to be confirmed.)

(ii) Issuance of Certificate Necessary for Reduction of Real Estate Acquisition Tax

The following procedures shall be followed with regard to the issuance of the certificate, as specified under Article 7(12) of the supplementary provisions of the enforcement ordinance for the local tax act, necessary for the reduction of the real estate acquisition tax for trust companies, etc., based on Article 11(14) of the supplementary provisions of the local tax act.

A. An application from a trust company, etc., for a certificate for the reduction of the real estate acquisition tax and the certificate to be issued by the FSA Commissioner shall be in accordance with the format specified in the Attached List of Formats VI-15.

B. After the application for a certificate has been submitted, the certificate shall be issued upon the confirmation, made in reference to the attached documents and other materials, of the following points with regard to the items specified in the submitted application.

a. Whether it is specified as an investment policy for the relevant investment trust, under the investment trust contract provisions, that the specified real estate asset ratio should be 75% or higher.

b. In cases where funds are borrowed, whether the borrowed funds have been provided by qualified institutional investors as specified under Article 2(3)(i) of the FIEA and designated under a relevant ordinance of the Ministry of Internal Affairs and Communications.

c. Whether the specified assets invested by the investment trust meet either of the following criteria:

i) The specified real estate asset ratio is at least 75%.
(When the submitted asset investment report confirms a specified real estate asset ratio of 75% or higher, this criterion shall be deemed to be met.)

ii) The specified real estate asset ratio is expected to rise to 75% or higher when the applicant trust company, etc., acquires the real estate for which it is filing the application.
(If this criterion is to be met, materials showing the status of the specified assets as of the application date shall be required to be attached to the submitted application in the format specified in the Attached List of Formats VI-14 in order for the status to be confirmed.)

(2) Issuance of Certificates to Investment Corporations

(i) Issuance of Certificates Necessary for Reduction of License Registration Tax Regarding Ownership Transfer

The following procedures shall be followed with regard to the issuance of the certificate, as specified under Article 31-7(3) of the enforcement rules for the Act for Special Tax Measures, necessary for the reduction of the license registration tax for investment corporations based on Article 83-3(3) of the said act.

An investment corporation seeking to become eligible for the provision of Article 83-3(3) of the act for special tax measures needs to do so within one year from the acquisition of the relevant real estate.

A. An investment corporation's application for a certificate necessary for the reduction of the license registration tax regarding the transfer of ownership and the certificate to be issued by the

directors-general of Local Finance Bureaus shall be in accordance with the format specified in the Attached List of Formats VI-16.

B. The applicant shall be required to fill out the necessary items on the application form and attach to it a copy of the relevant real estate transaction contract, in order for the dates of the signing of the contract and the real estate acquisition to be confirmed.

C. After the application for a certificate has been submitted, the certificate shall be issued upon the confirmation, made in reference to the attached documents and other materials, of the following points regarding the items specified in the submitted application.

a. Whether it is specified as an asset investment policy under the internal rules that the specified real estate asset ratio should be 75% or higher.

b. Whether the applicant is registered under Article 187 of the Investment Trust Act

c. In cases where funds are borrowed, whether the borrowed funds have been provided by qualified institutional investors (limited to those as specified under Article 2(3)(i) of the FIEA and designated under a relevant ordinance of the Ministry of Internal Affairs and Communications.).

d. Whether either of the following criteria is met:

i) The specified real estate asset ratio is 75% or higher.

(When the submitted asset investment report confirms a specified real estate asset ratio of 75% or higher, this criterion shall be deemed to be met.)

ii) The specified real estate asset ratio is expected to rise to 75% or higher when the applicant investment corporation acquires the real estate for which it is filing the application.

(If this criterion is to be met (including in the initial year), materials showing the status of the specified assets as of the application date shall be required to be attached to the submitted application in the format specified in the Attached List of Formats VI-14 in order for the confirm the status to be confirmed.)

(ii) Issuance of Certificates Necessary for Reduction of Real Estate Acquisition Tax

The following procedures shall be followed with regard to the issuance of the certificate, as specified under Article 7(14) of the supplementary provisions of the enforcement ordinance for the local tax act, necessary for the reduction of the real estate acquisition tax for investment corporations, based on Article 11(15) of the supplementary provisions of the said act.

A. An investment corporation's application for a certificate necessary for the reduction of the real estate acquisition tax and the certificate to be issued by the directors-general of Local Finance Bureaus shall be in accordance with the format specified in the Attached List of Formats VI-17.

B. After the application for a certificate has been submitted, the certificate shall be issued upon the confirmation, made in reference to the attached documents and other materials, of the following points regarding the items specified in the submitted application.

a. Whether it is specified as an asset investment policy under the internal rules that the specified real estate asset ratio should be 75% or higher.

b. In cases where funds are borrowed, whether the borrowed funds have been provided by qualified institutional investors as specified under Article 2(3)(i) of the FIEA and designated under a relevant ordinance of the Ministry of Internal Affairs and Communications.

c. Whether the specified assets invested by the investment corporation meet either of the following criteria:

   i) The specified real estate asset ratio is 75% or higher.
   (When the submitted asset investment report confirms a specified real estate asset ratio of 75% or higher, this criterion shall be deemed to be met.)

   ii) The specified real estate asset ratio is expected to rise to 75% or higher when the applicant investment corporation acquires the real estate for which it is filing the application.
   (If this criterion is to be met (including in the initial year), materials showing the status of the specified assets as of the application date shall be required to be attached to the submitted application in the format specified in the Attached List of Formats VI-14 in order for the status to be confirmed.)

VII. Supervisory Evaluation Points and Various Administrative Procedures (Investment Advisory and Agency Business)

VII-1 Governance (Investment Advisory and Agency Business)

Supervisors shall pay attention to the following points when examining the governance of Financial Instruments Business Operators (limited to business operators engaging in investment advisory and agency business; the same shall apply in VII).

VII-1-1 Officers of Financial Instruments Business Operators

(1) Major Supervisory Viewpoints

Whether the Financial Instruments Business Operator properly takes account of the following eligibility requirements in the decision-making process regarding proposals for the appointment of its officers.

(i) A person who does not meet any of the ineligibility criteria (Article 29-4(1)(ii)(a) to (g) of the FIEA) and who did not meet any of them at the time of registration.

(ii) A person who has not violated laws and regulations regarding financial instruments business or related business operations of the FIEA, or a person who has not been subjected to administrative actions taken based on laws and regulations.

(iii) A person who has not damaged the interests of investors in relation to the conduct of the investment advisory and agency business and the investment management business.

(iv) A person who has not engaged in an illegal or markedly inappropriate act, under particularly grave circumstances, regarding financial instruments business.

(2) Supervisory Method and Actions

In cases where an officer of a Financial Instruments Business Operator is deemed to meet the ineligibility criteria specified under any of Article 29-4(1)(ii)(a) to (g) of the FIEA or is found to have done so at the time when the business operator obtained registration under Article 29 of the FIEA, or where an officer of a Financial Instruments Business Operator is deemed to meet the ineligibility criteria specified under any of Article 52 (1)(vi) and (viii) to (x) of the FIEA, supervisors shall consider taking actions such as ordering the dismissal of the said officer based on Article 52(2) of the FIEA. In addition, they shall hold an in-depth hearing regarding the decision-making process concerning the proposal for the appointment of the said officer and, when necessary, require the submission of a report based on Article 56-2(1) of the FIEA. Furthermore, supervisors shall consider taking actions such as issuing an order for business improvement if the Financial Instruments Business Operator's control environment for governance is deemed to have a serious problem and the action is deemed to be necessary and appropriate from the viewpoint of protecting public interests and investors.

VII-2 Appropriateness of Business Operations (Investment Advisory and Agency Business)

Supervisors shall examine the appropriateness of Financial Instruments Business Operators' business operations by paying attention to the following points.

VII-2-1 Appropriateness of Business Operations Related to Investment Advisory Business

VII-2-1-1 Control Environment for Legal Compliance

Investment advisory business operators (Financial Instruments Business Operators engaging in investment advisory business (as specified under Article 2(8)(xi) of the FIEA; the same shall apply in VII); the same shall apply in VII) have the function of contributing to the buildup of customers' assets by providing them with information regarding investment decisions based on the analysis of the values of securities, financial products and other items. Therefore, investment advisory business operators are required to conduct their business in a conscientious manner by putting the top priority on customers' interests and maintaining sound and appropriate business operations with a high level of self-discipline.

Investment advisory business operators' control environments for legal compliance shall basically be examined based on the supervisory viewpoints and methods specified in III-2-1. However, they shall also be examined in relation to a broad range of matters, including the status of compliance with voluntary regulatory rules.

VII-2-1-2 Control Environment for Customer Solicitation and Explanations

(1) Prohibition of Advertisements Using Exaggerated Descriptions

(i) When the investment advisory business operator includes the results of its investment advice regarding specific issues in its advertisements, whether it cites only issues for which results are favorable.

(ii) Whether the investment advisory business operator includes in its advertisements descriptions indicating that the results, contents and method of its investment advice are markedly superior to those of other investment advisory business operators without providing the basis therefor.

(iii) Whether the advertisement does not use descriptions that could mislead users to believe that the customer solicitation period and the number of customers to be accepted are limited whereas in reality they are not limited.

(iv) In cases where the investment advisory business operator has not obtained registration regarding investment management business, whether its advertisements include representations that could lead investors to erroneously believe that it can engage in investment management business.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding an investment advisory business operator's advertisements, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the investment advisory business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article

56-2(1) of the FIEA. When the investment advisory business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the investment advisory business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VII-2-1-3 Cancellation of Investment Advisory Contracts (Cooling-Off Rule)

(1) Points of Attention Regarding Cancellation of Investment Advisory Contracts

(i) The "usual expenses necessary for the signing of an investment advisory contract," as specified under Article 115(1)(i) of the FIB Cabinet Office Ordinance, include the costs of communications using telephone calls, mail and other means, but do not include travel expenses.

(ii) The calculation of the "the number of dates between the receipt of the documents provided at the time of the contract signing and the cancellation date," as specified under Article 115(1)(iii) of the FIB Cabinet Office Ordinance, should include the days on which the documents are received and the cancellation is made.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding an investment advisory business operator's cooling-off rules, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the investment advisory business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the investment advisory business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the investment advisory business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VII-2-1-4 Duty of Loyalty and Measures to Prevent Internal Collusion

(1) Points of Attention Regarding Investment Advisory Business Operators Engaging in Two or More Types of Business

When supervisors examine the appropriateness of measures taken by an investment advisory business operator engaging in two or more types of business (as specified under Article 29-2(1)(v) of the FIEA) to prevent internal collusion, they shall pay attention to the following points, for example, depending on the nature of its business, from the viewpoint of preventing conflicts of interest and ensuring the appropriateness of business operations in other ways.

(i) Whether the investment advisory business operator has taken appropriate measures to prevent collusion

between its different types of business, such as establishing an internal control system and procedures for the prevention of such collusion in a manner suited to the nature of its business.

(ii) Regarding the "non-disclosure information," as specified under Article 147(ii) of the FIB Cabinet Office Ordinance, whether the investment advisory business operator has put in place information management measures, such as the appointment of a relevant manager and the establishment of management rules, and ensures the effectiveness of information management by, for example, properly identifying and examining the status of the usage of the non-disclosure information and revising the management method as necessary.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding measures taken by an investment advisory business operator engaging in two or more types of business to prevent internal collusion, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the investment advisory business operator by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the investment advisory business operator is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the investment advisory business operator is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VII-2-1-5 Measures to Prevent Legal Violations by Agency/Brokerage Service Providers

When investment advisory business operators entrust business operations to agency/brokerage service providers, it is important that they provide the service providers with guidance regarding the establishment of arrangements and procedures for customer due diligence that enable precise identification of the attributes of customers and the actual state of transactions, from the viewpoint of ensuring the implementation of appropriate investment solicitation suited to customer attributes. In addition, they should require the agency/brokerage service providers to ensure thorough legal compliance based on the examination of the actual status of their investment solicitation. Supervisors shall examine an investment advisory business operator's control environment for the prevention of legal violations by agency/brokerage service providers by paying attention to the following points in particular:

(1) Selection of Agency/Brokerage Service Providers

(i) Points of Attention Regarding Selection of Agency/Brokerage Service Providers

A. When signing contracts for entrusting agency/brokerage services, whether the investment advisory business operator specifies the significance of the entrustment in relation to governance, identifies the various risks involved therein and conducts sufficient deliberations on the method of risk management.

B. Whether the investment advisory business operator conducts sufficient deliberations on whether the agency/brokerage service providers have sufficient qualifications to conduct the entrusted business operations in a sound and appropriate manner. In cases where the agency/brokerage service providers

concurrently engage in other services in particular, whether the investment advisory business operator not only examines the possibility of the nature of the other services damaging public confidence in the service providers, but also conducts sufficient deliberations from the viewpoint of reputational risk for the primary business operator. (The "primary business operator" refers to an investment advisory business operator which signs investment advisory contracts through agency/brokerage services provided by agency/brokerage service providers. The same shall apply in VII.)

(2) Measures Taken by Primary Business Operators to Ensure the Appropriateness of Agency/Brokerage Service Providers

(i) Development of Internal Control Environment for Supervising Agency/Brokerage Service Providers

A. Whether the primary business operator has developed a control environment for ensuring appropriate supervision of agency/brokerage service providers through measures such as establishing a division responsible for the implementation of measures to ensure the sound and appropriate conduct of business operations related to agency/brokerage services or appointing a person responsible therefor (including a control environment regarding audits of the business operations of agency/brokerage service providers).

B. Whether the primary business operator has developed an internal control environment for examining whether the said division or person has taken proper measures to ensure the appropriateness of the business operations related to the agency/brokerage services.

(ii) Points of Attention Regarding Measures to Ensure Necessary and Appropriate Supervision of Agency/Brokerage Service Providers

A. Whether the primary business operator has taken the following measures in order to ensure a sound and appropriate conduct of business operations related agency/brokerage services and monitors the status of the conduct of the business operations.

a. To provide guidance regarding business operations related to agency/brokerage services to brokerage service providers and their employees and implement training programs intended to ensure their compliance with laws and regulations regarding the agency/brokerage services.

b. Measures to ensure necessary and appropriate supervision of agency/brokerage service providers, such as examining periodically or as necessary whether the service providers properly conduct the services, including investment solicitation, and requiring them to make improvement when necessary.

B. Whether the primary business operator has developed a control environment that ensures the results of the above monitoring are examined by its division in charge and reported to the management team when necessary, so that they are reflected in the provision of appropriate guidance by the primary business operator and in the conduct of business operations by agency/brokerage service providers.

(iii) Measures to Cancel Contracts for Entrusting Agency/Brokerage Services

Whether the primary business operator has developed a control environment for implementing appropriate measures, such as providing guidance to agency/brokerage service providers and canceling contracts for entrusting agency/brokerage services, when a problem has been found as a result of the

monitoring of agency/brokerage service providers. In addition, whether it has developed a control environment for properly protecting customers when canceling the entrustment contract.

(iv) Whether the primary business operator has established arrangements and procedures for responding to complaints, such as specifying the contact point for customer complaints regarding agency/brokerage services, establishing a division in charge of processing complaints, and prescribing procedures for processing complaints.

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding a primary business operator's selection of agency/brokerage service providers and its measures to ensure the appropriateness of their business operations, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the primary business operator and the service providers by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the primary business operator and the service providers are deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the primary business operator and the service providers are deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VII-2-2 Appropriateness of Business Operations Related to Agency/Brokerage Services

Supervisors shall examine the appropriateness of agency/brokerage service providers with due consideration of the following supervisory viewpoints, for example. It should be noted that the validity of measures to ensure the appropriateness of the business operations of agency/brokerage service providers need to be examined from a comprehensive perspective, in light of the nature and size of their business and their status of concurrent engagement in different types of business, and that failure to meet some of the criteria included in the supervisory evaluation points should not automatically be deemed to mean that their business operations are inappropriate.

VII-2-2-1 Control Environment for Legal Compliance

The establishment of the framework for agency/brokerage services is expected to contribute to securing and improving investors' access to investment services and facilitate efficient use of various sales channels, including Financial Instruments Business Operators. On the other hand, it is essential to maintain the sound and appropriate management of agency/brokerage services in order to prevent illegal transactions that may be made through the abuse of a position as an ordinary business operator.

Therefore, it is important to supervise agency/brokerage service providers in a timely and appropriate manner so as to ensure that their services are steadily conducted in an appropriate manner. In particular, it is necessary for supervisors to make sure to prevent agency/brokerage services providers concurrently engaging in other businesses from using inappropriate practices, such as abuse of a superior bargaining position and misappropriation of customer information.

Agency/brokerage service providers' control environments for legal compliance shall basically be examined based on the supervisory viewpoints and methods specified in III-2-1. However, they shall also be examined in relation to a broad range of matters, including the status of compliance with voluntary regulatory rules.

VII-2-2-2 Development of Control Environment by Agency/Brokerage Service Providers

(1) Major Supervisory Viewpoints

(i) Whether agency/brokerage service providers ensure the conduct of appropriate business operations in compliance with laws and regulations by prescribing specific procedures for customer solicitation, the provision of explanations of the contents of contracts and the provision of documents at the singing of contracts under internal rules.

(ii) Whether agency/brokerage service providers have prescribed specific procedures for properly examining the status of compliance with laws and regulations.

(iii) Whether agency/brokerage service providers have secured an adequate number of personnel with sufficient knowledge regarding its agency/brokerage services.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the development of control environments by agency/brokerage services providers, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the agency/brokerage services providers by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the agency/brokerage services providers are deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the agency/brokerage services providers are deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VII-2-2-3 Provision of Information to Protect Investors

(1) Major Supervisory Viewpoints

(i) Control Environment for Prevention of Explanations That May be Mistaken for Abuse of Superior Bargaining Position

Whether agency/brokerage service providers concurrently engaging in other businesses have developed a control environment that prevents the provision of explanations that could be mistaken as an abuse of a superior bargaining position banned under the Antimonopoly Act in relation to the agency/brokerage services and the businesses in which they concurrently engage.

(ii) Control Environment for Prevention of Misrecognition of Financial Products as Deposits

In cases where banks and other deposit-taking financial institutions engage in agency/brokerage services

for the signing of investment advisory and discretionary investment contracts, whether they have developed a control environment that prevents customers from mistakenly believing these investments to be deposits.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding agency/brokerage service providers' provision of information intended to protect investors, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the agency/brokerage services providers by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the agency/brokerage services providers are deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the agency/brokerage services providers are deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VII-2-2-4 Measures to Be Taken by Agency/Brokerage Service Providers When Undertaking Services for Two or More Primary Business Operators

(1) Explanations to Customers

When an agency/brokerage service provider undertakes services on behalf of two or more primary business operators, whether it explains the following items to customers in advance. Whether the service provider does its utmost to enable customers to understand the items, by using written explanations, for example.

(i) In cases where the amount of fees to be paid by the customer is different from the amount of fees to be paid under a similar contract with another primary business operator, the fact that there is a difference must be explained to the customer.

(ii) In cases where the agency/brokerage service provider acts as an agency/broker for another primary business operator regarding the signing of a contract similar to the one which the customer intends to sign, this fact must be explained to the customer.

(iii) The contents of the similar contract described in (ii) above and other information that could be useful for the customer must be provided upon his/her request.

(iv) The trade name of the primary business operator which is the ultimate counterparty to the customer's transaction must be made clear to the customer.

(2) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding measures taken by agency/brokerage service providers when undertaking agency/brokerage services on behalf of two or more primary business operators, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the agency/brokerage services providers by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article

56-2(1) of the FIEA. When the agency/brokerage services providers are deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51 of the FIEA. When the agency/brokerage services providers are deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52(1) of the FIEA.

VII-3 Various Administrative Procedures (Investment Advisory and Agency Business)

VII-3-1 Registration

When receiving a registration application, supervisors shall pay attention to the following items. It should be noted that judgment as to whether registration is necessary should be made from a comprehensive viewpoint, with the significance of a specific activity to be considered in the context of the full range of activities related to investment advisory and agency businesses. Therefore, it should be kept in mind that it would not be appropriate to conclude that a certain business operator does not need to be registered on the basis of the results of the examination of some parts of the full range of activities.

(1) Cases Not Requiring Registration

(i) Cases to which Article 61-1 of the FIEA Is Applicable

Cases where a corporation which has been established based on foreign laws and regulations and which engages in investment advisory business abroad or an individual person whose residence is located in a foreign country and who engages in investment advisory business abroad seeks to provide investment advisory service exclusively to business operators engaging in investment management business and those designated under the FIEA Enforcement Order.

(ii) Cases to which Article 50-2(3) of the FIEA Is Applicable

Cases where a business operator which is allowed to engage in investment advisory business based on Article 50-2(3) of the FIEA provides investment advisory service for a specified period of time.

(2) Activities Not Deemed to Fall under Category of Investment Advisory and Agency Services

(i) Provision of Investment Decision Information Based on Analysis of Values of Securities and Financial Products (hereinafter referred to as "investment information, etc.") to Unspecified People through Methods that May Be Used Thereby as Necessary

For example, business operators which provide investment information, etc., through the methods described in A to C below are not required to be registered as investment advisory and agency business operators.

However, it should be kept well in mind that in cases where business operators provide investment information, etc., of a specific nature to unspecified people by taking advantage of the Internet and other advanced information technologies and where they allow access to the information only to registered members (not allow one-off access), registration is required.

A. Sales of Newspapers, Magazines, Books, etc.

(Note) Cases where newspapers, magazines and books containing investment information, etc., are displayed in bookstores and other shops for purchase by any person at any time based on the judgment on their contents shall not be deemed to fall under the category of activities regarding investment advisory service. On the other hand, it should be kept in mind that registration may be necessary in cases where a business operator sells reports containing investment information, etc., on a subscription basis.

B. Sales of Investment Analysis Tools and Other Computer Software Products

(Note) Cases where investment analysis tools and other software products are offered through Internet-based downloading sales services for purchase by any person, based on the judgment on the algorithm and other investment analysis functions of the products, shall not be deemed to fall under the category of investment advisory service. On the other hand, it should be kept in mind that registration may be necessary in cases where the use of the software products requires continuous support from the seller, such as the provision of investment information, etc.

C. Provision of advice on the value of financial products

(Note) Providing advice on the value of financial products other than securities, the premium of options, and the trend of indexes without providing advice regarding investment decisions based on the analysis thereof or without signing an agreement on the payment of fees shall not be deemed to fall under the category of investment advisory services.

Providing advice on the average temperature in Japan this winter, for example, shall not be deemed to fall under the category of investment advisory service.

(ii) Activities Not Constituting Brokerage for Signing of Discretionary Investment Contract

In cases where business operators undertake activities which do not constitute a brokerage service, on behalf of investment advisory business operators and discretionary investment business operators, they are not required to be registered as investment advisory/agency business operators.

For example, business operators which undertake only some of the clerical processes related to the activities described in A. to C. below on behalf of investment advisory business operators and discretionary investment business operators may not be required to be registered as investment advisory/agency business operators.

A. Distribution and Provision of Fliers, Pamphlets, Contract application Forms, etc.

(Note) It should be kept in mind that although merely notifying customers of the trade names of investment advisory business operators and discretionary investment business operators and their contacts does not constitute a brokerage service, explaining how to fill out documents distributed and provided to customers may be deemed to constitute a brokerage service.

B. Receipt and Collection of Contract Applications, Attached Documents, etc. (excluding cases where the business operator checks the contents of the documents)

(Note) It should be kept in mind that in cases where the business operator not only points out technical errors in the application form or failure to attach necessary documents when collecting them from customers but also checks the contents of the application form and other documents, the activity may be deemed to constitute a brokerage service.

C. General explanations provided at seminars for financial instruments with regard to the structures, schemes and the utilization methods of financial instruments

VII-3-2 Points of Attention Regarding Depositing of Deposits for Operation

(1) When supervisors have received the original of a statement of deposit submitted by investment

advisory/agency business operators after they have deposited a new deposit for operation in order to replace the existing deposit, the supervisors shall implement the procedures for the certification of the return of the original of the statement of deposit in their custody, in accordance with the format specified in the Attached List of Formats V-I, and return it to the business operators.

(2) When supervisors have received the original of a certificate of receipt submitted by investment advisor/agency business operators after they have submitted a request for substitute deposit/additional deposit in order to substitute redemption funds for deposited securities, the supervisors shall provide a certificate of custody in accordance with (5) below and return the original of the statement of deposit already in their custody to the business operators.

(3) When supervisors have received an application from investment advisory/agency business operators for a revision of the contents of a substitute contract for a deposit for operation or for the cancellation of such a contract, they shall grant approval in the approval form regarding deposit contract revision as specified in the Attached List of Formats V-2 and in the approval form regarding deposit contract cancellation as specified in the Attached List of Formats V-3, if it is deemed that the revision/cancellation does not lead to insufficient protection of investors.

(4) The public notification of the retrieval of deposits for operation shall be made in the format specified in the Attached List of Formats V-4.

(5) When supervisors have received the original of a statement of deposit, they shall provide a certificate of custody in the format specified in the Attached List of Formats V-5.

(6) Supervisors shall ensure that all applicants for registration are aware of the possibility that in cases where government bonds are deposited as deposits for operation based on Article 31-2(9) of the FIEA, deposits could become invalid after a certain period of time due to the statute of limitations under the Act Concerning Government Bonds.

VIII. Supervisory Evaluation Points and Various Administrative Procedures (Registered Financial Institutions)

VIII-1 Appropriateness of Business Operations (Registered Financial Institutions)

III-2 (excluding III-2-3-4(2), III-2-6(1)(ii), III-2-8(3) and III-2-9), IV-3-1 (excluding IV-3-1-2(1) and IV-3-1-4) and IV-3-3 (excluding IV-3-3-1(1), IV-3-3-2(3)(iii) to (vi) and IV-3-3-4; however, the exclusion shall not apply to registered financial institutions engaging in foreign exchange margin trading) shall be applied mutatis mutandis to the examination of the appropriateness of the business operations of registered financial institutions. In addition, attention shall be paid to the following points.

It should be noted that regarding theoretical prices referred to in IV-3-1-2(4)(iii) A. and B. and internal rules referred to in (iii) B. and C. in relation to financial instruments intermediary services,
registered financial institutions may use prices calculated by and rules established by Financial Instruments Business Operators to which their business operations are entrusted.

VIII-1-1 Appropriateness of Individual Operations

(1) Whether registered financial institutions, which conduct dealing operations of government bond certificates, etc., short-term investment securities or asset finance-type investment securities (in the case of accounts other than specified trading accounts conducted by registered financial institutions which have adopted specified trade accounts (accounts similar to the specified trade accounts for a branch of foreign banks; the same shall apply hereinafter)), conduct trading for the purpose of investment of securities related to the said operations in an integrated manner. Also, whether the list of clients has been shared among the concerned parties.

(2) When a registered financial institution conducts any dealing operations in government bond certificates, etc., futures commission business, trading operations of short-term investment securities, or trading operations of asset finance-type investment securities:

(i) Whether the operations and the status of assets are made clear by separating the handling of accounting affairs and dealing with securities associated with the said operations from the handling of accounting affairs and dealing with securities associated with other operations

(ii) Whether the following book transfers between accounts concerning securities handled in the said operations have been conducted:

A. In cases where the registered financial institutions has not adopted specified trading accounts, book transfers between the commodity bond account and other securities accounts in the cases.

B. In the cases where the registered financial institutions has adopted specified trading accounts, book transfers between a trading securities account from among specified trading accounts and other securities accounts or between the derivatives of trading securities from among specified trading accounts and derivatives of other trading securities accounts.

(3) In the case of a registered financial institution conducting option trading, whether it makes efforts to disclose

market indications concerning options trading in government bond certificates with high liquidity to investors through appropriate means, such as store displays, etc.

(4) Whether the registered financial institution compensates for financial instruments losses or offers clients automatic credit for margins (including remargin) in order to conduct financial instruments trading.
(Note) Overdrafts fall under the category of automatic credit grants.

In such cases, the following measures shall be taken, for example:

(i) If the registered financial institution conducts futures commission business, it shall open an account for bond futures transactions and prohibit the said account having an overdraft feature, and automatic transfer from an overdraft account to the account for bond futures transactions of the same account holder shall not be conducted.

(ii) If the registered financial instruments institution conducts financial instruments intermediary services, it shall not conduct financial instruments intermediary activities by providing automatic credit or by promising to do so in order to settle a transaction conducted by a client who failed to settle due to insufficient funds in the securities account opened for the said client in the entrusted Financial Instruments Business Operator.

(5) Regarding registered financial institutions engaged in futures commission business

(i) In the cases where transactions are conducted by using GLOBEX terminals, it shall be made clear whether it has been stipulated to that effect in the company policy for business conduct

(ii) In dealing with payment to the account for bond futures transactions, it shall be made clear whether staff in charge of the relevant client has been appointed in advance, the name of the client (or his/her fund manager) has been registered, and the preliminary consent of the said client shall be obtained by phone each time payment is made.

(6) Whether the department in charge of the overall operations (receiving orders, transactions and transfers) of a registered financial institution that conducts transactions of short-term securities is prepared to take all possible measures to block off the inflow/outflow of so-called subtle information between loan business, etc., and business related to the issuance of and transactions involving commercial papers and short-term corporate bonds, etc. (short-term corporate bonds prescribed in the Act on Transfer of Bonds, etc., short-term corporate bonds prescribed in the Insurance Business Act, specified short-term corporate bonds prescribed in the Act on Securitization of Assets, short-term commercial and industrial bonds prescribed in the Shoko Chukin Bank Act, short-term bonds prescribed in the Shinkin Bank Act, and short-term Norin-chukin Bank bonds prescribed in the Norin-chukin Bank Act).

(7) Whether registered financial institutions that sell securities-related products:

(i) Take necessary measures to avoid misleading clients when soliciting them to sell a set of deposit products and securities-related products

(ii) Explain fully to clients about risks, such as price fluctuations and differing deposits, when selling securities-related products, such as investment trusts, etc.

(8) Regarding registered financial institutions that conduct financial instruments intermediary services.

(i) Whether officers or employees, etc., who control a division which conducts both financial instruments intermediary services and loan business (limited to those handling non-public loan information, etc., of clients, who are the issuers of securities; the same shall apply in (8) and VII-2-1-(2)-(vi)):

A. Provide non-public loan information obtained from a person engaged in loan business to a person engaged in financial instruments intermediary services.

B. Use non-public loan information obtained from a person engaged in financial instruments intermediary services for the purpose of loan business or provide such information to a person engaged in loan business.

(ii) Whether internal administrators (referring to internal administrators prescribed in the "Regulations Concerning Internal Administrators, etc., of Association Members," No.13 of the Japan Securities Dealers Association's Regulations) appropriately control information exchanged among Financial Instruments Business Operators. Such information includes that pertaining to loan business to be given to clients for the purpose of legal compliance of those engaged in financial instruments intermediary services, as well as information for the purpose of conducting financial instruments intermediary services and the purpose of legal compliance of entrusted Financial Instruments Business Operators.

(9) Regarding the department supervising private management and implementation of securities, whether the registered financial institution that handles the private management of securities takes all possible organizational measures to block off the flow of so-called subtle information pertaining to loans and securities to and from the investment division and bond management division; provided, however, that this shall not apply when conducting any activities deemed applicable to the handling of private management of securities prescribed in Article 15, paragraph 3 of the FIEA Enforcement Order.

(10) In the cases where an insurance company acting as a registered financial institution has any employee, as prescribed in each item of Article 15-2(2) of the FIEA Enforcement Order (excluding (iii) (hereinafter referred to as the "representative" in (10)), who conducts the specified financial instruments business prescribed in Article 33-8(2) of the FIEA, the insurance company may entrust the representative office to which the said representative belongs to support for the said specified financial instruments operations.

(11) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding the appropriateness of a registered financial institution's specific business operations, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the registered financial institution by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the registered financial institution is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51-2 of the FIEA. When the registered

financial institution is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52-2(1) of the FIEA.

VIII-1-2 Prevention of Abuse of Superior Bargaining Position

(1) Abuse of Superior Bargaining Position by Business Operators Engaging in Two or More Businesses

Supervision of abuse of a superior bargaining position by business operators concurrently engaging in two or more businesses must be conducted with due consideration of "Regarding Unfair Trading Practices Following Loosening of Financial Institutions' Business Categories and Expansion of Business Scope," a document issued on December 1, 2004 by the Fair Trade Commission. For example, the following practices may constitute an abuse of superior bargaining position by business operators concurrently engaging in two or more businesses, so attention shall be paid thereto.

(i) Whether the registered financial institution effectively forces customers to sign contracts under which they make financial instruments transactions (hereinafter referred to as "financial instruments transaction contracts") by implying that it will suspend loans or transactions related to other businesses it concurrently undertakes, or give unfavorable treatment to them unless they sign the contracts.

(ii) Whether the registered financial institution effectively forces customers to sign financial instruments transaction contracts by requesting them to do so when it makes transactions with them regarding businesses it concurrently undertakes.

(iii) In cases where customers intend to sign contracts with business competitors of the registered financial institution, whether the financial institution tries to prevent the signing of the said contracts by implying it will suspend transactions with them regarding businesses it concurrently undertakes or give unfavorable treatment to them.

(iv) Whether the registered financial institution effectively forces customers to refrain from signing contracts with its competitors by requesting them to do so when it makes transactions with them regarding businesses it concurrently undertakes.

(2) Points of Attention Regarding Abuse of Superior Bargaining Position

Supervisors shall examine a registered financial institution's control environment for the prevention of abuse of a superior bargaining position by paying attention to the following points:

(i) Whether the registered financial institution has established a division responsible for the implementation of measures to prevent the said abuse or appointed a person responsible therefor and developed an internal control environment for examining whether the said division or person is properly implementing the prevention measures.

(ii) Whether the registered financial institution provides training periodically and as necessary, with persons with knowledge and practical experiences regarding its businesses as trainers, in order to prevent the said abuse.

(iii) Whether the registered financial institution has established arrangements and procedures for responding

to complaints, such as specifying the contact point for customer complaints regarding the said abuse, establishing a division in charge of processing complaints and prescribing procedures for processing complaints.

(3) Supervisory Method and Actions

When supervisors have recognized an issue of supervisory concern regarding abuse of a superior position by a registered financial institution concurrently engaging in two or more businesses, through daily supervisory administration or the reporting of problematic conduct, they shall identify and keep track of the status of voluntary improvement made by the registered financial institution by holding in-depth hearings and, when necessary, requiring the submission of reports based on Article 56-2(1) of the FIEA. When the registered financial institution is deemed to have a serious problem from the viewpoint of protecting public interests and investors, the supervisors shall take actions, including issuing an order for business improvement based on Article 51(2) of the FIEA. When the registered financial institution is deemed to have committed a serious and malicious violation of law, the supervisors shall consider necessary actions, including the issuance of an order for business suspension based on Article 52-2(1) of the FIEA.

VIII-1-3 Points of Attention Regarding Supervision of Non-Affiliated Registered Financial Institutions

(1) Major Supervisory Viewpoints

(i) In cases where a registered financial institution does not belong to any Financial Instruments Firms' Association nor have membership in nor trading participant rights at any financial instruments exchange (hereinafter referred to as a "non-affiliated registered financial institution"), whether it has developed internal rules with due consideration of the rules set by associations, etc.

(ii) Whether the non-affiliated registered financial institution has developed a control environment that ensures appropriate compliance with internal rules (e.g., examination of whether all officers and employees are aware of and comply therewith).

(iii) When the rules set by associations, etc., have been revised, whether the non-affiliated registered financial institution makes sure to quickly review and revise internal rules accordingly.

(2) Supervisory Method and Actions

(i) In cases where a non-affiliated registered financial institution has failed to establish internal rules with due consideration of the rules set by associations, etc., and where it is deemed unlikely to do so on a voluntary basis, supervisors shall order it to establish internal rules based on Article 56-4(2) of the FIEA. In such cases, the non-affiliated registered financial institution shall also be required to revise internal rules immediately in response to any future revision of the rules set by associations, etc.

(ii) In cases where a non-affiliated registered financial institution's internal rules are deemed to need to be revised in light of the rules set by associations, etc., and where it is deemed unlikely to make revision on a voluntary basis, supervisors shall order the business operator to do so based on Article 56-4(2) of the FIEA.

(iii) When supervisors have recognized an issue of supervisory concern regarding the status of a

non-affiliated registered financial institution's establishment and revision of internal rules and compliance therewith, they shall strive to identify and keep track of the actual situation by holding in-depth hearings and requiring the submission of a report based on Article 56-2(1) of the FIEA. In addition, they shall conduct appropriate supervision based on Article 56-4(1) of the FIEA with due consideration of the rules set by associations, etc., by, for example, issuing an order for business improvement based on Article 51-2of the FIEA and an order for business suspension based on Article 52-2(1) as necessary.

VIII-2 Various Administrative Procedures (Registered Financial Institutions)

VIII-2-1 Registration

III-3-1 (excluding (2) and (4)), VI-3-1 and VII-3-1 shall be applied mutatis mutandis to the treatment of registration applications from financial institutions, and attention shall also be paid to the following points. It should be noted that terms used in the relevant formats specified in the Attached List of Formats shall be replaced as necessary.

(1) Registration Numbers

The registration numbers to be recorded in a registry of financial institutions shall be specified as follows:

Example) Director-General of XX Local Finance Bureau (Registered Financial Institution) No. XX

(2) Items Regarding Examination of Staffing

When examining whether or not a registered financial institution is sufficiently staffed to properly conduct the business of registered financial institutions as specified under Article 33-5(1)(iii) of the FIEA, supervisors shall check the following points based on the submitted registration application and attachments thereto as well as a hearing.

(i) Whether the registered financial institution is staffed and organized so that personnel necessary for conducting relevant business in an appropriate manner are allocated to individual divisions and managers in charge of internal control are appropriately allocated.

(ii) Whether personnel capable of conducting the following processes have been secured with regard to the relevant business.

A. Compilation and management of account documents and reports.
B. Disclosure
C. Segregated management of customer assets
D. Risk Management
E. Computer system management
F. Trading management, customer management
G. Processing of complaints and disputes
H. Internal audits

(iii) Whether the financial institution's staff includes two or more permanent officers or employees with more than three years of experiences regarding securities-related businesses. Financial institutions which engage in over-the-counter sales of government bonds without undertaking underwriting and those which engage in brokerage for clearing of government bonds without undertaking underwriting shall be deemed to meet this requirement, if their staff include two or more persons with sufficient knowledge and experience to conduct the relevant business operations properly. It should be noted that in cases where a financial institution, after obtaining registration, starts securities-related businesses which it did not initially undertake, compliance with this requirement shall be checked again.

(iv) Whether the financial institution ensures that at sales branches handling any of government bond

dealing operations in general, short-term securities trading operations in general, or asset finance-type securities trading operations in general, the organization, responsibilities and authorities regarding the said operations are clearly separated and independent from those regarding trading of these securities for the investment purpose and loan business, and whether it ensures that at such sales branches, employees handling the said operations do not concurrently engage in loan business or securities trading for the purpose of investment.

(v) Regarding a financial institution engaging in futures brokerage service:

A. Whether the financial institution prevents inappropriate use of information concerning trading of securities futures, such as government bond futures, by the proprietary trading division. In this case, whether the financial institution ensures that at sales branches handling futures brokerage operations in general, the organization, responsibilities and authorities regarding the said operations are in principle clearly separated and independent from those regarding other businesses (including businesses other than those specified under Article 2(8)(ii) and (iii).

B. Whether the financial institution ensures that sales branches engaging in futures brokerage operations are organized in ways to prevent the solicitation of customers through a promise to provide convenience to them in loans and loan guarantees.

(vi) In cases where the financial institution offers financial instruments intermediary services, whether it makes sure to prevent exchanges of non-disclosure information regarding loans and other matters concerning securities-issuing customers between employees engaging in financial instruments intermediary services and those engaging in loan operations. For example, whether the financial institution strives to ensure the effectiveness of the prevention of exchanges of non-disclosure information regarding loans and other matters, by establishing internal rules that provide for the separation of the financial instruments intermediary service operations and loan operations, the clarification of persons in charge of those operations, or other similar arrangements.

(vii) In cases where the financial institution is a non-affiliated registered institution, whether it has established internal rules that ensure appropriate business operations with due consideration of rules set by Financial Instruments Firms' Associations according to the types of business it undertakes.

(viii) III-3-1(9)(ii) shall be applied mutatis mutandis to the notification of a change in the total capital amount of a shinkin bank.

(3) Points of Attention Regarding Registered Financial Institutions Not Planning to Join Any Financial Instruments Firms' Association or Obtain Membership in or Participants Rights at Any Financial Instruments Exchange.

Supervisors shall notify the following points to a registered financial institution which does not have a plan at the time of the application to join any Financial Instruments Firms' Association or to obtain membership in or trade participant rights at any financial instruments exchange and require them to take appropriate actions.

(i) In cases where the registered financial institution is deemed to lack appropriate internal rules set with due consideration of the rules set by associations, etc., it shall in principle be ordered to immediately establish appropriate internal rules after registration.

(ii) A non-affiliated registered financial institution may be ordered to revise internal rules with due consideration of the rules set by associations, etc.

(iii) In cases where a non-affiliated registered financial institution has been ordered to establish or revise internal rules, they need to do so within 30 days and obtain approval from the Prime Minister.

(iv) In cases where a non-affiliated registered financial institution plans to revise or abolish internal rules established as described in (iii) above, they need to obtain approval from the Prime Minister.

(v) The authorities are to properly supervise non-affiliated registered financial institutions' business operations so as to ensure the full protection of public interests and investors with due consideration of the rules set by associations, etc.

VIII-2-2 Approval and Notification

III-3-2, IV-4-2-4, IV-4-3 and VI-3-2 shall be applied mutatis mutandis.

VIII-2-3 Account Documents Related to Business Operations

III-3-3 shall be applied mutatis mutandis to the compilation and storage of account documents related to business operations, and attention shall also be paid to the following points.

(1) Compilation of Account Documents Related to Financial Instruments Intermediary Services

Registered financial institutions may compile the account documents, as specified under Article 184(1)(iii) of the FIB Cabinet Office Ordinance, with the use of computer systems and formats adopted by Financial Instruments Business Operators to which they entrust business operations, or they may entrust the establishment of systems and formats necessary for the compilation of the account documents to the entrusted business operators. However, it should be kept in mind that the registered financial institutions bear the responsibility for the compilation and storage of the account documents.

VIII-2-4 Registration of Sales Representatives

IV-4-3 and V-3-2 shall be applied mutatis mutandis.

VIII-2-5 Interpretation of Article 33 of FIEA

(1) Interpretation of Article 33(1) of FIEA

(i) The following business operations undertaken by banks, cooperative structured financial institutions and other financial institutions as specified under Article 1-9 of the FIEA Enforcement Order (referred to as "banks, etc." in VIII-2-4) shall not be deemed to fall under the category of the prohibited activities as specified under Article 33(1) of the FIEA.

A. Providing client companies with advice useful for initial public offerings, and introducing client companies with potential for initial public offerings to underwriting Financial Instruments Business Operators.

B. Introducing customers to Financial Instruments Business Operators without conducting soliciting

activity

(ii) The act of "introducing" described in (i) B. applies to the following cases:

A. Cases where banks, etc., let Financial Instruments Business Operators display their own advertising media at bank branches.

B. Cases where banks, etc., explain their relationships with Financial Instruments Business Operators and the contents of the business operators' businesses.

(2) Interpretation of Article 33(2)

Regarding the brokerage with written orders as specified under Article 33(2), the following points shall be taken into consideration.

(i) Banks, etc., are prohibited from soliciting customers to sign contracts for securities trading and other financial instruments transactions when engaging in brokerage with written orders. However, the following activities shall not be deemed to fall under the category of solicitation activities:

A. Explaining the specifics of the brokerage with written orders to customers

B. Publicizing the specifics of the brokerage with written orders through media such as newspapers, magazines, documents, direct mail, websites, broadcasting and movies

C. Placing order forms and documents explaining the specifics of the brokerage with written orders at branches of banks, etc., for distribution to customers, sending them to customers, and displaying the documents at branches for perusal by customers.

(ii) When banks, etc., receive written orders, they must take instructions concerning the order category (sell or purchase), the ordered issue, the order volume and price with regard to each transaction.

Written orders to be received by banks, etc., for brokerage include continual orders to be executed at predetermined dates.

VIII-2-6 Others

(1) Points of Attention Regarding Segregated Management

It should be kept in mind that when registered financial institutions (limited to deposit-taking registered financial institutions) treat cash deposits arising from transactions regarding securities-related businesses as deposits in their primary business, the said cash deposits are not subject to segregated management.

(2) Points of Attention Regarding Establishment of Internal Rules

Non-affiliated registered financial institutions must establish internal rules that ensure appropriate business operations, with due consideration of rules set by Financial Instruments Firms' Associations, according to the types of business they undertake.

In addition, they must take care to maintain appropriate business operations by revising internal rules periodically or when relevant laws, regulations and rules are revised.

IX. Supervisory Evaluation Points and Various Administrative Procedures (Businesses Specially Permitted for Qualified Institutional Investors)

IX-1 Appropriateness of Business Operations Related to Businesses Specially Permitted for Qualified Institutional Investors

Supervisors shall examine the appropriateness of the business operations of qualified institutional investors and other business operators engaging in specially permitted businesses (business operators engaging in the businesses specified under each item of Article 63(1) of the FIEA) by paying attention to the following points.

IX-1-1 Control Environment for Customer Solicitation and Explanations

(1) Major Supervisory Viewpoints

Whether qualified institutional investors and other business operators engaging in specially permitted businesses (hereinafter referred to as "qualified institutional investors, etc"):

(i) Provide false representations and explanations that make their products and services appear free of charge or make fees appear markedly lower than the actual levels.

(ii) Provide false representations and explanations to the effect that they guarantee yields or compensate for all or part of losses that may arise.

(iii) Provide false representations and explanations to the effect that their products and services do not involve any risks, including the risk of customers incurring losses from transactions.

(iv) Provide false representations and explanations regarding the contents of products and transactions (basic product features, the types and characteristics of the risks involved and variable factors).

(2) Supervisory Method and Actions

In cases where supervisors have recognized suspected cases of qualified institutional investors, etc., making false statements to customers in soliciting activities, through daily supervisory administration, they shall take necessary actions, such as requiring the submission of a report regarding business operations based on Article 63(7) of the FIEA and issuing a written warning.

IX-1-2 Identification of Actual State of Qualified Institutional Investors, etc.

Supervisors shall require qualified institutional investors, etc., engaging in own-account investment business (as specified under Article 63(1)(ii)) to submit replies to monitoring surveys regarding the following items based on Article 63(7) of the FIEA, in order to properly identify the actual state of their business operations:

(i) Fund name

(ii) Fund type

(iii) Total amount of investment assets

IX-1-3 Obligation for Customer Identification and Reporting of Suspicious Transactions

III-2-6 shall be applied mutatis mutandis to the customer identification and the reporting of suspicious

transactions by qualified institutional investors, etc.

IX-1-4 Points of Attention Regarding Business Operators Which Fail to Make Necessary Reports

When supervisors have recognized cases where a business operator is engaging in business specially permitted for qualified institutional investors without fulfilling the obligation for the reporting of the matters specified under Article 63(2) of the FIEA, as a result of a complaint from customers, an inquiry from investigative authorities, the provision of information by Financial Instruments Business Operators/Financial Instruments Firms' Associations, a newspaper advertisement, etc., they shall warn the business operator in writing to suspend the business or immediately make the necessary report.

IX-1-5 Points of Attention in Cases Where Qualified Institutional Investors, etc., Lose Their Status

In cases where a business operator engaging in businesses specially permitted for qualified institutional investors has become unable to meet the necessary requirements due to reasons such as a change in the attributes of capital providers, withdrawal of qualified institutional investors and an increase in ordinary investors, supervisors shall take the following actions:

(1) Order Based on Article 63(5) of the FIEA

"When a Specially Permitted Business Notifying Person's business commenced under item (ii) of paragraph (1) as a Specially Permitted Businesses for Qualified Institutional Investor, etc., has come to no longer satisfy the requirement to be regarded as a Specially Permitted Businesses for Qualified Institutional Investor, etc.," as specified under Article 63(5) of the FIEA, refers to cases where although the specially permitted business's capital providers included qualified institutional investors when the business was commenced, any qualified institutional investor no longer remains in the business for a reason not attributable to the responsibility of the notifying person. In such cases, supervisors shall order the notifying person to transfer the relevant business operations to another Financial Instruments Business Operator.

(2) Cases Other than (1)

In cases where the number of investors other than qualified institutional investors has exceeded 49, a special clause specified under Article 63 of the FIEA shall not apply, so the notifying person will engage in investment management business without being registered under the FIEA. Therefore, against the said person, supervisors shall take actions similar to those taken against unregistered business operators as prescribed under II-1-1(7).

X. Supervisory Evaluation Points and Various Administrative Procedures (Foreign Securities Companies)

X-1 Foreign Securities Companies' Cross-Border Transactions via the Internet

(1) Basic Concept on Laws and Regulations Regarding Foreign Securities Companies

Foreign securities companies are not allowed to engage in the activities specified under each item of Article 28(8) of the FIEA (hereinafter referred to as "activities concerning securities-related businesses") with persons located in Japan as their transaction counterparts, unless their main Japanese sales branches or main business offices engaging in securities-related businesses are registered.

Meanwhile, unregistered foreign securities companies with no business base in Japan are allowed to engage in activities concerning securities-related businesses with persons in Japan as their transaction counterparts, if they take orders from the said persons without conducting solicitation regarding activities concerning securities-related businesses or take orders through agency and brokerage services provided by Financial Instruments Business Operators (limited to Type I Financial Instruments Business Operators).

(2) Foreign Securities Companies' Cross-Border Transactions Using Internet

The posting by foreign securities companies of advertisements regarding activities concerning securities-related businesses on Web sites shall in principle be deemed to constitute a solicitation.

However, it shall not be deemed to constitute a solicitation aimed at investors in Japan as long as reasonable measures are taken to prevent the advertisement from leading to activities concerning securities-related business with investors in Japan as their transaction counterparts.

(i) Disclaimer

A disclaimer to the effect that the advertised service is not targeted at investors in Japan must be indicated.

In judging whether an adequate disclaimer is properly indicated, attention shall be paid to the following points:

A. Any particular computer operation other than viewing the advertisement should not be necessary for reading and understanding the disclaimer.
B. The disclaimer must be indicated in language reasonably deemed to be readable and understandable for investors in Japan who are accessing the website.

(ii) Measures to Prevent Transactions

Measures to prevent transactions regarding activities concerning securities-related businesses must be in place.

In judging whether adequate measures are in place, attention shall be paid to the following points:

A. When making transactions, the foreign securities company checks the location of the investors by requiring them to provide information regarding their residence location, mail address, e-mail address, payment method and other items.
B. Care must be taken to avoid taking orders from the investors in cases where there is a reasonable reason for believing that the orders obviously concern activities concerning securities-related

businesses involving investors in Japan.

C. Care must be taken to avoid inducing investors in Japan to conduct activities concerning securities-related businesses by, for example, refraining from establishing a call center targeted at customers in Japan and establishing links to web pages targeted at investors in Japan.

The above-mentioned measures are merely examples, so if measures equivalent thereto or more effective measures have been implemented, the posting of advertisements by foreign securities companies shall not be deemed to constitute a solicitation.

(iii) It should be noted that in cases where the above-mentioned reasonable measures are not in place, the said posting of advertisements is highly likely to constitute a solicitation aimed at investors in Japan. Therefore, in such cases, the foreign securities companies should bear the burden of proving that they do not engage in activities concerning securities-related businesses involving solicitation aimed at investors in Japan.

XI. Supervisory Evaluation Points and Various Administrative Procedures (Financial Instruments Intermediary Service Providers)

XI-1 Appropriateness of Business Operations (Financial Instruments Intermediary Service Providers)

III-2 (excluding III-2-6(1)(ii)) and IV-3-1 (excluding IV-3-1-2(2), IV-3-1-3(1) and (2) and IV-3-1-5) shall be applied mutatis mutandis to the examination of the appropriateness of the business operations of financial instruments intermediary service providers, and attention shall also be paid to the following points.

It should be noted that the bonds as referred to in IV-3-1-2(4) are the securities as specified under Article 281(vii) of the FIB Cabinet Office Ordinance and that regarding theoretical prices mentioned in IV-3-1-2(4)(iii) A. and B. and internal rules mentioned in (4) (iii) B. and C. in relation to financial instruments intermediary services, financial instruments service providers may use prices calculated and rules established by Financial Instruments Business Operators to which their business operations are entrusted.

(1) Points of Attention Regarding Explanation Documents

Regarding the Explanation Documents as specified under Article 66-18 of the FIEA, supervisors shall:

(i) Instruct financial instruments intermediary service providers to keep the documents available at any time for perusal by customers upon their request.

(ii) Check the date on which each financial instruments intermediary service provider installed the documents at its branches.

XI-2 Various Administrative Procedures (Financial Instruments Intermediary Service Providers)

XI-2-1 Registration

III-3-1 (excluding (2) and (9)(iii)) shall be applied mutatis mutandis to the treatment of registration applications based on Article 66-2 of the FIEA, and attention shall also be paid to the following points. It should be noted that terms used in the relevant formats specified in the Attached List of Formats shall be replaced as necessary.

(1) Registration Procedures

(i) The registration numbers to be recorded in a registry of financial institutions shall be specified as follows:

(Example) Director-General of XX Local Finance Bureau (Financial Instruments Intermediary Service Providers) No. XX

(ii) Proxy Application for Registration

Regarding registration application concerning financial instruments intermediary service providers, it should be kept in mind that proxy application may be made by the primary Financial Instruments Business Operators and other entities, based on their examination of the applications for the purposes of facilitating the convenience of the applicants and their proxies, streamlining the applicants' clerical work, ensuring the preciseness of the items specified in the application and speeding up the processing of the application.

When supervisors have received a proxy registration, they shall examine the letter of proxy in order to check the validity and scope of the proxy. It should be kept in mind that when the scope of the proxy includes the authority to revise the application and receive the notice of registration, supervisors may request the proxy applicant to make revision and give the notice thereto.

(2) Matters for Screening

(i) Regarding an applicant service provider which undertakes service on behalf of two or more primary Financial Instruments Business Operators under Article 258(iii) of the FIB Cabinet Office Ordinance, supervisors shall check whether the following requirements are met in judging whether the names of the primary Financial Instruments Business Operators responsible for compensating for losses that may arise from problematic conduct are properly indicated.

A. Whether possible problematic conduct is categorized and whether the name of the primary Financial Instruments Business Operator responsible for compensating for losses in the event of each category of problematic conduct is clearly specified.

B. Whether the name of the primary Financial Instruments Business Operator responsible for compensating for losses in the event of problematic conduct that does not fall under any category or that cannot be clearly put into any category is clearly specified.

(ii) Supervisors shall check whether the contents and methods of business operations as specified under Article 259 of the FIB Cabinet Office Ordinance include the following items:

A. Service area

B. Business style (e.g., whether the business involves physical contact with customers, is conducted through a computer system linked to a telecommunications network and, in the case of an applicant who is an individual person, whether the service provider employs persons engaging in financial instruments intermediary service)

C. Types of sales branch (manned branches, unmanned branches)

D. Types of securities handled by the service provider

E. Types of domestic and foreign market derivatives transactions for which the service provider acts as a broker (the types of transactions and as specified under each item of Article 2(21) and Article 23 of the FIEA)

F. In cases where the service provider intends to act as a broker for investment advisory contracts or discretionary investment contracts, the intention must be indicated.

(3) Others

When examining whether officers and employees of a financial instruments intermediary service provider have sufficient knowledge and experience to properly conduct financial instruments intermediary services, supervisors shall check the following points in reference to the submitted applications and documents attached thereto. It should be noted that when the applicant is a foreign corporation, they shall check the status of officers and employees stationed in Japan with regard to (i) below and the corporation's status in Japan with regard to (ii) and (iii).

(i) Whether persons engaging in financial intermediary services (officers and employees engaging in financial intermediary services and managers in charge of internal control and other matters) have passed the securities sales representative qualification examination conducted by the Japan Securities Dealers Association and have a prescribed level of knowledge regarding relevant laws, regulations and rules.

(ii) In cases where the applicant is a corporation or an individual person who employs persons engaging in financial instruments intermediary services, whether the applicant has a staff and an organization that ensure an appropriate allocation of personnel necessary for conducting the relevant service in an appropriate manner and managers in charge of internal control, according to the nature and scale of the relevant service.

(iii) In cases where the applicant is a corporation or an individual person who employs persons engaging in financial instruments intermediary services, whether the applicant has established arrangements and procedures necessary for the following matters. (Regarding A. and B., the intermediary service provider may entrust the compilation of accounts and other documents to the primary Financial Instruments Business Operator while managing the compiled documents itself. C. to E. may be disregarded in cases where the primary Financial Instruments Business Operator has established appropriate arrangements and procedures.)

A. Compilation and management of account documents, reports, etc.
B. Customer due diligence
C. Computer system management
D. Processing complaints and disputes
E. Internal audits

XI-2-2 Notification

III-3-2(1) shall be applied mutatis mutandis to notifications made by financial instruments intermediary service providers, and attention shall also be paid to the following points:

(1) Points of Attention Regarding Notification of Discontinuance of Business

When receiving a notification based on Article 66-19(1) of the FIEA from a financial instruments intermediary service provider, supervisors shall make sure, through a hearing with the service provider, for example, that no reason exists for the rescission of registration as specified under Article 66-20(1) of the FIEA.

XI-2-3 Account Documents Related to Business Operations

III-3-3 (excluding III-3-3(4) and (5)) shall be applied mutatis mutandis to the treatment of the compilation and storage of account documents related to business operations, and attention shall also be paid to the following points:

(1) Compilation of Account Documents Related to Financial Instruments Intermediary Services

Financial instruments intermediary service providers may compile the account documents as specified under Article 282 of the FIB Cabinet Office Ordinance with the use of computer systems and formats adopted by the primary Financial Instruments Business Operators or entrust the establishment of systems and formats necessary for the compilation of the account documents to them. However, it should be kept in mind that the financial

instruments intermediary service providers bear the responsibility for the compilation and storage of the account documents.

XI-2-4 Registration of Sales Representatives

IV-4-3 and V-3-2 shall be applied mutatis mutandis.

XII. Supervisory Evaluation Points and Various Administrative Procedures (Securities Finance Companies)

XII-1 Governance (Securities Finance Companies)

III-1 (excluding (1)(ii) F) shall be applied mutatis mutandis to the examination of the governance of securities finance companies. In addition, IV-1-2 shall be applied mutatis mutandis to the examination of whether officers and employees are sufficiently qualified to conduct securities finance business.

XII-2 Appropriateness of Business Operations (Securities Finance Companies)

III-2 (excluding III-2-3-1, III-2-3-3, III-2-3-4, III-2-4(1)(iii) and (iv) and III-2-7(2)(i)F) shall be applied mutatis mutandis to the examination of the appropriateness of the business operations of securities finance companies.

XII-2-1 Business Reports

Regarding descriptions of "3. Status of Measures Implemented in Relation to Protection of Personal Information," as specified under Article 3-4(1) of the Cabinet Office Ordinance Regarding Securities Finance Companies (hereinafter referred to as the "Finance Companies Cabinet Ordinance"), attention shall be paid to the following points:

(1) Status of Implementation of Safety Control Measures

Regarding a securities finance company's safety control system concerning information related to individual customers, supervision of employees responsible for safety control and, in cases where the safety control is entrusted to an outside entity, supervision of the said entity, supervisors shall require a report regarding the following measures, which are appropriate and necessary from the viewpoint of preventing the said information from being leaked, lost or damaged.

(Necessary and Appropriate Measures Regarding Safety Control)

(i) Measures based on Article 10 of Personal Information Protection Guideline

(ii) Measures based on Section I and Attachment 2 of the Practical Guideline

(Necessary and Appropriate Measures Regarding Supervision of Employees)

(i) Measures based on Article 11 of the Personal Information Protection Guideline

(ii) Measures based on Section II of the Practical Guideline

(Necessary and Appropriate Measures Regarding Supervision of Entrusted Entity)

(i) Measures based on Article 12 of the Personal Information Protection Guideline

(ii) Measures based on Section III of the Practical Guideline

(2) Status of Implementation of Measures to Prevent Use of Specified Non-Disclosure Information for Non-Prescribed Purposes

"Other specified non-disclosure information" as specified in Note 3(2) refers to information regarding labor union membership, ethnicity and sexual orientation, while "assurance of appropriate business operations and other purposes deemed to be necessary" refers to the cases described in each item of Article 6(1) of the Personal

Information Protection Guideline.

XII-3 Various Administrative Procedures (Securities Finance Companies)

XII-3-1 License Screening Criteria

(1) Staffing

The appropriateness of the staffing as specified under Article 156-25(1) shall be judged in light of the following criteria:

(i)Whether the securities finance company has allocated personnel necessary for conducting the business specified under Article 156-24(1) of the FIEA (hereinafter referred to as "debt-credit transaction business") to individual divisions.

(ii) Whether the securities finance company's staff includes officers and employees with three or more years of experience regarding securities-related business as well as those adept in the debt-credit transaction system.

(iii) Whether officers and employees secured by the securities finance company are deemed to have sufficient knowledge and experience to conduct the relevant business in an appropriate and efficient manner in light of the following criteria:

A. Managing directors must understand the viewpoints regarding governance indicated in the FIEA and various other laws and regulations, and have sufficient knowledge and experience to conduct governance and sufficient knowledge and experience regarding compliance and risk management to conduct financial instruments business in a fair and appropriate manner.

(iv) When the qualifications of employees and officers are examined in a comprehensive manner in relation to the following criteria regarding organized crime members and financial crimes, whether there is the risk that public confidence in the securities finance company could be damaged because of the inclusion of officers and employees with inappropriate qualifications among its staff.

A. Officers and employees should not be current or former members of organized crime groups.

B. Officers and employees should not have close relationships with organized crime groups.

C. Officers and employees should not have the experience of being sentenced to a fine for violation of the FIEA or other domestic financial laws and regulations or foreign laws and regulations equivalent thereto.

D. Officers and employees should not have the experience of being sentenced to imprisonment with work or more severe punishment (including similar punishments imposed under foreign laws or regulations equivalent thereto). (Particular attention should be paid to the case of an officer or employee being accused of committing crimes specified under Articles 246 to 250 of the Penal Code (fraud, fraud using computers, breach of trust, quasi fraud and extortion, as well as attempts at these crimes).

(2) Credit Status and Fund-Raising Capability

The appropriateness of a securities finance company's credit status and fund-raising capability shall be judged in light of the following criteria:

(i) Whether the securities finance company can be objectively deemed to have sufficient stock-procurement and fund-raising capabilities for conducting the debt-credit transaction business.

(ii) Whether the securities finance company has established arrangements and procedures for obtaining information regarding credit transactions in the exchange-based financial instruments market and the over-the-counter securities trading market at any time, and procurement and settlement systems which link it with Financial Instruments Business Operators and transactions counterparties, and which are deemed to be capable of responding quickly to procurement and settlement needs.

XII-3-2 Notification

The revisions of the contents and methods of business operations as specified under Article 1-2(2)(ii) of the Finance Companies Cabinet Ordinance refer to those revisions of the contents of methods of business operations, excluding revisions of terms of transactions, which involve revisions of internal rules and which must be communicated to all transaction counterparties.

XII-3-3 Approval

In granting approval based on Article 156-27(3) of the FIEA, supervisors shall pay attention to the following points:

(1) Approval should not be granted in cases where the business for which approval is sought is deemed to undermine public interests or where an excessive amount of securities held by the securities finance company could lead to significant price change risk, for example.

(2) Whether the revenue projection document as specified under Article 2(1)(i) of the Finance Companies Cabinet Ordinance indicates that the business will turn profitable within three years from its commencement and whether the projection can be objectively deemed to be feasible.

XII-3-4 Authorization

(1) Revision of Contents and Methods of Business Operations

When receiving an application for authorization of a revision of the contents or methods of business operations as specified under Article 156-28(1) of the FIEA, supervisors shall pay attention to the following points:

(i)Whether the revision of the contents could undermine the smooth conduct of debt-credit transaction business.

(ii) Whether it is ensured that the revision of the contents is quickly communicated to all necessary parties

(2) Reduction of Capital Amount

When receiving an application for authorization of reduction in the capital amount, supervisors shall pay attention

to the following points:

(i) Whether the capital amount after the reduction will be lower than the minimum level prescribed under Article 156-23 of the FIEA.

(ii) Whether the capital reduction could undermine the smooth conduct of debt-credit transaction business.

(iii) Whether the reason for the capital reduction can be deemed to be one essential to continuing business, such as a need to eliminate a deficit.

(3) Resolution for Discontinuance or Dissolution of Business

When receiving an application for authorization of the resolution for discontinuance or dissolution of business as specified under Article 156-36(i) of the FIEA, supervisors shall pay attention to the following points:

(i)Whether no reason exists for the rescission of a license as specified under Article 156-32(1) of the FIEA.

(ii) Whether the securities finance company has a positive net worth and is ready to proceed with the liquidation process smoothly.

(iii) Whether measures, both institutional and physical, have been taken to avoid causing disruptions to credit transactions in the exchange-based financial instruments market and the over-the-counter securities market after the discontinuance or dissolution of business.

(4) Merger or Transfer or Acceptance of Business

When receiving an application for authorization of the merger or transfer or acceptance of business as specified under Article 156-36(ii) of the FIEA, supervisors shall pay attention to the following points:

(i) Whether no reason exists for the rescission of a license, as specified under Article 156-32(1) of the FIEA, with regard to the company set to be dissolved as a result of the merger or business transfer.

(ii) Whether measures, both institutional and physical, have been taken to prevent the merger or transfer or acceptance of business from causing disruptions to credit transactions in the exchange-based financial instruments market and the over-the-counter securities market.