



Minister Watanabe took over the post from former Minister Yamamoto (August 28)

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Revision of Inspection Manual for Financial Holding Companies

1. Introduction

The Financial Services Agency (FSA) on July 9, 2007, revised the Inspection Manual for Financial Holding Companies and issued a notification to this effect in the name of the Director-General of the Inspection Bureau (notification No. 272, July 7, 2007).

The outline of the revised Inspection Manual for Financial Holding Companies is as shown below.

2. Background to Revision of Inspection Manual for Financial Holding Companies

The Inspection Manual for Financial Holding Companies (formulated in July 2003) is intended for use by inspectors when inspecting financial holding companies. The contents of this manual are based on the Inspection Manual for Deposit-Taking Institutions (hereinafter referred to as the Financial Inspection Manual"), the Inspection Manual for Insurance Companies and the Inspection Manual for Securities Companies, and it lists check items for each of the lines of business covered by financial conglomerates in a structure similar to the manuals used as references. However, as the Inspection Manual for Insurance Companies and the Financial Inspection Manual underwent sweeping revisions in June 2006 and February 2007, respectively, the FSA revised the Inspection Manual for Financial Holding Companies mainly regarding the Checklist Concerning Bank Holding Companies and the Checklist Concerning Insurance Holding Companies. The FSA announced the revised Inspection Manual for Financial Holding Companies on July 9, 2007, after subjecting the draft thereof to the public comment process.

The revised manual is to be applicable starting with inspections conducted in Program Year 2007 (in July and thereafter).

Note: Regarding the Checklist Concerning Securities Holding Companies, the FSA made no revision considering the fact that the Securities and Exchange Surveillance Commission was in the process of formulating the Inspection Manual for Financial Instruments Business Operators.

3. Structure of Revised Manual for Financial Holding Companies

The revised manual is comprised of chapters entitled "Basic Concept" concerning the inspection of financial holding companies, "Checklist for Group Business Management (Governance) System", "Checklist for Group Capital Management System" and "Checklist for Group Comprehensive Risk Management System. "

4. Outlines of Checklists

1) Checklist for Group Business Management (Governance) System

In order to ensure the soundness and appropriateness of the businesses of financial institutions that are subsidiaries of the financial holding company inspected, this checklist seeks to examine whether the holding company's group business management (governance) system is functioning effectively with a focus on whether the holding company is appropriately handling specific issues that require special

attention in its group organization such as a) the formulation of group management policies, b) improvement and establishment of the system for managing intra-group companies, c) monitoring and review and d) management of intra-group transactions.

2) Checklist for Group Capital Management System

This checklist seeks to examine whether the capital management system of the inspected financial holding company is functioning effectively with a focus on whether the holding company is appropriately implementing a) measures concerning the buildup of the group's capital, b) evaluation of the level of the group's capital buildup and c) calculation of the capital adequacy ratio on a consolidated basis (This item concerns only bank holding companies.).

3) Checklist for Group Comprehensive Risk Management System

This checklist seeks to examine whether the comprehensive risk management system of the inspected financial holding company is functioning effectively with a focus on whether the holding company oversees a variety of risks faced by intra-group companies, grasps in a comprehensive manner risks specific to the group organization that cannot be handled by individual intra-group companies, such as the possibility of spillover of risks throughout the group, and appropriately compares such risks with the group's management strength (capital).

Note: When examining the above-mentioned management systems, the inspector shall refer to the relevant sections of the Financial Inspection Manual and the Inspection Manual for Insurance Companies as necessary, in addition to the Inspection Manual for Financial Holding Companies, in light of the roles and responsibilities of the financial holding company inspected.

5. Conclusion

The Inspection Manual for Financial Holding Companies was formulated in light of the actual status of financial holding companies in ways to enable inspectors to deal with a variety of cases, and financial holding companies and their group companies do not necessarily have to meet all of the requirements of this checklist. The FSA hopes that financial holding companies will implement measures in a manner suited to the size and characteristics of their businesses under the principle of self-responsibility in light of this manual by fully exploiting their resourcefulness and creativity.

Outline of the Revision of the Trust Business Act Pertaining to the Revision of the Trust Act

On December 8, 2006, the Trust Act (Act No. 108 of 2006) and the Act on Coordination, etc. of Related Acts Pertaining to Enforcement of the Trust Act (Act No. 109 of 2006) (hereinafter referred to as the “Coordination Act”) were approved and enacted at the 165th session of the Diet, and were promulgated on December 15, 2006. In order to provide appropriately for matters pertaining to the revision of the Trust Act, the Trust Business Act was revised by the Coordination Act, which was submitted by the Ministry of Justice and which made various revisions of Acts that had become necessary as a result of the revision of the Trust Act.

In line with this, the Financial Services Agency (FSA) invited public comments on the Cabinet Order on

Coordination of FSA Related Cabinet Orders Pertaining to the Enforcement of the Trust Act and the Act on Coordination, etc. of Related Acts Pertaining to Enforcement of the Trust Act (Draft) and the Cabinet Ordinances, etc. for Partial Revision of the Ordinance for Enforcement of the Trust Business Act, etc. (Draft) on April 4, 2007 and published the results thereof on July 13, 2007.

The day of the enforcement of these Acts, Cabinet Orders and Cabinet Ordinances is September 30, 2007, which is the day of the enforcement of the Trust Act (Act No. 108 of 2006).

The revisions of the Trust Business Act and the related Cabinet Order and Cabinet Ordinance pertaining to the revision of the Trust Act are outlined below.

1. Basic Concept

In line with the revision of the Trust Act, discussions were also held on the revision of the Trust Business Act at the sessions of a joint meeting between the Second Subcommittee, Sectional Committee on Financial System, Financial System Council and the Trust Working Group which started on November 16, 2005. On January 26, 2006, the joint meeting compiled a report entitled "Review of the Trust Business Act Pertaining to the Revision of the Trust Act." In this report, the joint meeting indicated the following concept with regard to the revision of the Trust Business Act pertaining to the revision of the Trust Act:

- (1) The framework of the Trust Business Act prior to revision shall be maintained in principle regarding the need for protection of settlors and beneficiaries and how trust business should be regulated.
- (2) Protection of beneficiaries shall be ensured by establishing the appropriate requirements for the market entry of businesses handling new categories of trust and having such businesses assume the same obligations of trustees as those of trust companies.
- (3) Provisions on the obligations of trustees shall be established for parts of the Act that are practically causing inconvenience, while taking into consideration the demand for protection of beneficiaries.

The work to revise the Trust Business Act was carried out based on this concept.

2. Obligations of Trustees Related to Management and Administration

Under the new Trust Act, the provisions on the due care of a prudent manager and duty of loyalty regarding trustees have been changed into discretionary provisions, allowing for a reduction of such obligations through a contract between the parties concerned. Under the Trust Business Act, however, the due care of a prudent manager and duty of loyalty continue to be imposed on trust companies as mandatory provisions. This is because, if the level of the due care of a prudent manager is to be left to a contract between the parties concerned, the contract would be excessively advantageous for the trust company due to a gap in access to information between the trust company and the customer, and would put customer protection at risk. Another reason is that there is a need to prevent trustees from abusing their authority or causing conflicts of interest and to ensure that they perform their obligations fully.

With regard to the prohibition of acts that cause conflicts of interest, such as self-dealing, the cases in which such acts are considered not to hinder beneficiary protection have been specified in the Ordinance for Enforcement of the Trust Business Act so as to clarify the permissible categories of trade, in order to define clearly the requirements for cancellation of the prohibition. In addition, the scope of interested persons with whom trade is restricted has been reviewed by referring to the scope of persons having a specified relationship under the Banking Act.

As for the entrustment of trust businesses to a third party, the new Trust Act provides that a trustee may, in principle, entrust trust affairs to a third party based on the due care of a prudent manager even when such entrustment is not prescribed in the deed of trust. On the other hand, the Trust Business Act maintains the conventional framework in which a trust company cannot, in principle, entrust trust businesses to a third party unless such entrustment is prescribed in the deed of trust and the same due care of a prudent manager and duty of loyalty as those of the trust company are imposed on the entrusted party.

However, it was provided that entrustment is possible, even when such entrustment is not prescribed in the deed of trust, to the extent that it is not problematic in terms of beneficiary protection with regard to certain acts that are specified by the Ordinance for Enforcement of the Trust Business Act including the following: (1) businesses pertaining to the preservation of trust property; (2) businesses aimed at using or improving trust property to the extent that the nature thereof does not change; and (3) acts that are ancillary to the performance of businesses of the trust company. When the entrusted party is not considered to have the same function as the trust company, there would be no need to impose the same obligations on the entrusted party, so the scope of the obligations to be imposed on the entrusted party is to be limited in such a case.

3. Regulations on New Trust Categories under the Trust Business Act

Under the new Trust Act, the following four new categories of trust were introduced: a trust issuing a beneficiary certificate, a trust created by the method set forth in Article 3(iii) of the Trust Act (a declaration of trust), a trust that does not specify the beneficiary (a purpose trust), and a limited liability trust.

Among these, the conventional regulations on market entry and acts for trustees of ordinary trusts are imposed, in principle, on trustees of a trust issuing beneficiary certificates, a limited liability trust and a purpose trust, while additionally imposing the duty to explain and/or other obligations that would be necessary according to the trust category. For example, since a purpose trust does not specify the beneficiary, there is no need to consider beneficiary protection. A trustee is to assume the duty to explain and the duty to deliver documents to the settlor. Meanwhile, unlike an ordinary trust, a limited liability trust is subject to property distribution regulation. Therefore, a trustee of a limited liability trust is to assume the ordinary duty to explain as well as the duty to explain property distribution regulation to the settlor.

On the other hand, new rules were created for the declaration of trust based on an idea that it should be regulated by rules separate from those for a trust business. Even if an entity executes a declaration of trust for a business purpose, it would not correspond to a trust business, but when it executes a declaration of trust for a large number of beneficiaries, it needs to obtain the registration set forth in Article 50-2(1) of the revised Trust Business Act. The details of a case that corresponds to the case of executing a declaration of trust for a large number of beneficiaries are prescribed in concrete terms in the Order for Enforcement of the Trust Business Act; a large number of beneficiaries is regarded as being 50 beneficiaries or more.

An entity that executes a declaration of trust assumes the same obligations of a trustee related to management and administration as those of an ordinary trust company, in principle. However, the requirements for registration of a declaration of trust differ from those for the license/registration of a trust company, although they have many points in common. For example, the minimum amount of stated capital required for registration of a declaration of trust is 30 million yen, and an entity that is not a stock company can also obtain the registration as long as it is a company that has been established under the Companies Act. The entity is not required to be dedicated to such business alone, but it is required to secure the soundness of its other businesses

objectively in terms of ordinary profit and loss and amount of net assets. Furthermore, in the case of a declaration of trust, an entity must assume an additional legal obligation of investigation by a third party such as a lawyer or a certified public accountant regarding the status of the property to be placed in trust, in order to prevent the sale of beneficial interest in a dummy property or an overvalued property to a large number of investors. The detailed contents of the regulation on engagement in additional business and the actual matters for investigation concerning a third-party investigation are specified by the Ordinance for Enforcement of the Trust Business Act.

The provisions of the Trust Act concerning a declaration of trust shall not be applied until the day on which one year has elapsed from the day of the enforcement of the Trust Act. Likewise, the provisions of the Trust Business Act concerning a declaration of trust shall not be applied until then.

4. Exclusion from Trust Business

A trust business is defined as an “operation accepting trusts.” However, apart from the case of simply concluding trust contracts, sometimes there are cases where a trust is created in a manner that is not expected by the parties concerned when depositing money in accordance with another contract. Since it is not reasonable to apply the Trust Business Act to such unexpected cases, the following acts have been specified by the Order of Enforcement of the Trust Business Act as acts that are excluded from a trust business: (1) the receipt of a deposit of money by a lawyer, etc. for the purpose of using it for the expenses necessary for the services of the lawyer or any other receipt of a deposit of money by a mandatary under a mandate contract for the purpose of using it for the expenses necessary for the mandated affairs; and (2) the receipt of a deposit of money by a contractor for the purpose of using it for the expenses necessary for his/her work.

The only types of acts excluded from a trust business under the Trust Business Act are those where a trust is created in a manner that is unexpected even by the parties concerned as a result of concluding another contract. It should be noted that the excluded act is not the act of concluding the trust contract itself.

Similarly, with regard to a declaration of trust, certain cases, where the declaration is considered not to hinder beneficiary protection (such as cases where a servicer declares a trust over money, etc. it has collected from debtors), have been specified by the Order/Ordinance for Enforcement of the Trust Business Act as exceptions to the registration of a declaration of trust.

The revisions of the Trust Business Act and the related Cabinet Order and Cabinet Ordinance pertaining to the revision of the Trust Act have been briefly outlined above. In addition to the matters already mentioned, many other necessary revisions have been made pertaining to the revision of the Trust Act. For further details, access “Results of Public Comments on the Cabinet Order on Coordination of FSA Related Cabinet Orders Pertaining to the Enforcement of the Trust Act and the Act on Coordination, etc. of Related Acts Pertaining to Enforcement of the Trust Act (Draft) and the Cabinet Ordinances, etc. for Partial Revision of the Ordinance for Enforcement of the Trust Business Act, etc.

Basic Policy and Plan for Securities Inspections in Program Year 2007

The Securities and Exchange Surveillance Commission (SESC) on July 27 announced the “Basic Policy and Plan for Securities Inspections in Program Year 2007,” thus clarifying its implementation policy concerning the

inspections of securities companies and the number of companies to be inspected. The outline of the Basic Policy and Plan for Securities Inspections is as explained below.

In accordance with its basic mission of securing the fairness of transactions and maintaining investors' confidence in the market, the SESC aims to establish a fair and highly transparent market for financial instruments and enhance investors' confidence in the market, with particular emphasis on the protection of individual investors.

In this context, the SESC intends to take a flexible approach to inspections based on the basic policy stated below while paying constant attention to market conditions from a broad perspective. At the same time, it will endeavor to conduct inspections in an effective and efficient manner so as to identify the essential nature of problems at the companies inspected with a view to enabling voluntary activities of the companies such as internal control to function appropriately and encouraging the companies to deal with customers and the market sincerely.

Furthermore, based on the results of the inspections, the SESC intends to recommend administrative actions by the Financial Services Agency as necessary and pay attention to and take appropriate actions, such as presenting proposals, regarding the establishment of new market rules.

1. Priority Matters in Administrative Operations for Ensuring Efficient Inspections

The SESC will formulate inspection plans in accordance with risks faced by the companies inspected by taking account of a variety of information and documents, concerning matters such as the position of the companies in the market and their problems, in a comprehensive manner. In addition, it will conduct special inspections as necessary based on specific information or cross-sectoral themes.

Furthermore, the SESC will collaborate with the inspection section of the Ministry of Finance's local finance bureaus, inspect financial conglomerates concurrently with the Financial Services Agency's Inspection Bureau, and exchange information with self-regulatory organizations, supervisory bureaus and foreign securities industry regulatory authorities regularly or on an as-needed basis.

It should be noted that by the time the Financial Instruments and Exchange Act comes into force, the Basic Policy for Securities Inspection and the Securities Inspection Manual will be revised.

2. Priority Matters in Implementation of Inspection for Ensuring In-Depth and Effective Inspections

The SESC will conduct comprehensive analysis of the relationship among various information and documents so as to ensure in-depth inspections. Regarding companies that are not familiar with regulations on financial instruments business, including companies inspected for the first time, the FSA will focus its inspection on their institutional culture.

In addition, the SESC will not only examine activities that could prevent fair pricing but also look closely into the transaction management system of the companies inspected. Furthermore, it will conduct in-depth examination of internal control, since the status of internal control is a key factor for judging the attitude of the companies inspected.

It should be noted that the SESC will continue to focus its inspection of investment management business operators on the status of compliance with legal requirements such as duty of loyalty and duty of prudence.

Under the Basic Plan for Securities Inspection in the current program year, a total of 135 Type I financial

instruments business operators (including 115 to be inspected by local finance bureaus, etc.) and 60 companies engaging in investment management business and in investment advisory/agent business (including 30 to be inspected by local finance bureaus, etc.) will be inspected. In addition, self-regulatory organizations and Type II financial instruments business operators, which are included in the list of companies subject to inspection for the first time, will be inspected as necessary.

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Regarding Comprehensive Guideline for Supervision of Financial Instruments Business Operators

Guidelines for supervision are formulated and published so as to ensure the consistency of the activities of regulatory authorities such as the Financial Services Agency (FSA) and local finance bureaus of the Ministry of Finance and enhance transparency over administrative actions and foreseeability for business operators. On Sept. 30 this year, the Financial Instruments and Exchange Act, which seeks to ensure full compliance with rules concerning investor protection across various business sectors and promote financial innovation, took effect. In this context, the FSA has systematically sorted out various guidelines for supervision applicable to individual business sectors under a traditional legal framework as well as the guideline for administrative processes. In addition, the FSA established a cross-sectoral and comprehensive approach to supervision, necessary viewpoints and a suitable method of supervision in accordance with regulations specified by this act for the first time in relation to businesses and activities. The Comprehensive Guideline for Supervision of Financial Instruments Business Operators was decided and announced on July 31, after undergoing the public comment process starting in April 2007. The outline of this guideline is as explained below.

1. Sorting-out and Unification of Guidelines of Supervision

Currently, the supervisory authorities are dealing with securities companies, registered financial institutions, financial futures trading firms, investment trust management firms, and investment advisory firms based on individual laws applicable thereto and individual guidelines such as the Comprehensive Guideline for Supervision of Securities Companies, the Comprehensive Guideline for Supervision of Financial Futures Trading Firms and the Guideline for Administrative Processes (concerning points of attention in the supervision of investment trust management firms and investment corporations as well as securities investment advisory firms). Following the effectuation of the Financial Instruments and Exchange Law, these firms will be grouped together in the category of financial instruments business operators and will be, in principle, subject to uniform regulations on businesses and activities. Accordingly, the FSA has decided to sort out guidelines for supervision systematically.

First, the FSA sorted out and unified supervisory viewpoints and methods concerning these firms by formulating the Comprehensive Guideline for Financial Instruments Business Operators (hereinafter referred to as the “New Guideline”). Furthermore, the FSA decided to make the new guideline a comprehensive one applicable across various sectors by including in it viewpoints related to firms to be subjected to supervision for the first time, such as companies engaging in fund business as well as companies that have until now been supervised based on different laws and guidelines for supervision, such as companies engaging in the sale of

trust beneficiary interests and commodity fund business.

2. Basic Concept

In order to ensure that the Japanese economy will maintain sustainable development, it is important to redress its excessive dependence on indirect finance and promote a shift to direct finance and market-based indirect finance. In other words, it is important to accelerate the flow of funds from savings to investment. Such a shift is expected to contribute to the realization of a market attractive for market participants, the growth of companies and the development of the economy by bringing the following four benefits.

- 1) To realize a solid and advanced financial system that provides risk-sharing capability by promoting structural change in ways to enable a number of market participants to bear risks according to their respective capacity, thereby spreading the risks wide (prevention of a weakening of the financial system that may be caused by the concentration of risks in indirect finance).
- 2) To promote corporate innovation by ensuring smooth supply of risk money.
- 3) To improve the profitability of Japanese companies by realizing a market with sufficient depth for the monitoring of business managers through a shift of funds from savings to investment and thus enhancing the efficiency of capital.
- 4) To realize a diverse and wealthy society amid the decline of the birthrate and the aging of society by providing investors with a variety of means for asset management.

In order to achieve the above benefits, it is necessary to ensure not only that financial instruments business operators, which act as intermediaries, win the trust of people but also that financial regulators engage in appropriate institutional designing and implement adequate measures to motivate financial instruments business operators to strengthen governance with due consideration of customer protection and risk management.

3. Points of Attention in Administrative Processes Related to Supervision

(1) Policy for supervision in the early part of the program year and hearings

In the early part of each program year, the FSA will formulate and announce a guideline for supervision for the year in order to clarify priority matters concerning supervision in the year. In addition, the FSA will hold hearings focusing on earnings and comprehensive hearings covering a broad range of issues on a regular or as-needed basis.

(2) Implementation of monitoring surveys on funds

The FSA will continue the monitoring surveys concerning information related to the capital regulation ratio that it has until now been conducting on securities companies, etc. In addition, it will conduct similar surveys on investment management business operators in order to identify 1) the fund name, 2) the fund type and 3) the total amount of assets managed. These surveys will also be conducted on management firms subject to the notification requirement (A provision to this effect is included in Chapter IX. "Evaluation Items and Procedures Concerning Supervision (special businesses for eligible institutional investors)" of the guideline).

The purpose of the above-mentioned monitoring surveys is to grasp the actual status of funds managed in Japan. We assume that in light of the need to promote financial innovation and the global trend of supervision,

some fund management firms should not necessarily be subjected to direct and rigorous supervision. On the other hand, we believe it is useful in terms of financial supervision to get a rough picture of the types and amount of funds managed in Japan, including funds managed by the aforesaid fund management firms, and to use data thus collected to promote dialogue.

(3) Warning against non-registered firms

In recent years, there have been many cases in which investors incurred financial damage after investing in unlisted stocks in response to solicitation by non-registered firms. When the FSA finds inappropriate activities by non-registered firms after receiving complaints from investors and inquiries from the investigative authorities, it is ready to warn the firms concerned in writing and take necessary actions in collaboration with police, local consumer centers, etc.

(4) Points of attention in the implementation of administrative actions

When examining the implementation of administrative actions such as the issuance of a business improvement order, a business suspension order, an order for the revocation of registration and a license in relation to an inappropriate act by a financial instruments business operator, the FSA will take account of 1) the seriousness and malicious nature of the relevant act, 2) the business management system under which the relevant act occurred and the appropriateness of the operational system and 3) attenuation factors, in order to make a final decision as to the following matters:

- whether it is appropriate to leave the implementation of improvement measures to the discretion of the financial instruments business operator concerned.
- whether it is necessary to require the firm to concentrate on improving its business for a certain period of time.
- whether it is appropriate to allow the firm to continue its business.

4. Evaluation Items and Various Procedures Concerning Supervision (general)

(1) Specification of viewpoints concerning regulations on advertisements

Regarding the business management system and the legal compliance system, the comprehensive guideline includes viewpoints related to the establishment of appropriate systems, as it previously did with regard to securities companies.

Regarding solicitation and explanations, the comprehensive guideline provides detailed viewpoints related to regulations on advertisements, concerning which the Securities and Exchange Law had no particular provision. The guideline makes it clear that the scope of regulated advertisements covers materials for solicitation, web sites, postal mail, correspondence letters, facsimile documents, e-mail, fliers and pamphlets.

In addition, the guideline calls for attention to be paid, concerning the contents of advertisements, to 1) whether important items (fees, the risk of principal loss and the risk of loss exceeding the principal) are specified, 2) the risk of principal loss and the risk of loss exceeding the principal are indicated in a clear and precise manner, with the indication made in characters with a size not significantly smaller than the largest characters in the relevant advertisement, 3) whether there is not any representation that may unduly encourage investment or mislead investors about the yield level and the loss compensation guarantee, or any exaggerated

expression, and 4) whether an appropriate system is in place for screening advertisements.

Regarding the identity verification and the obligation for reporting suspicious transactions, the guideline specifies in detail matters concerning the establishment of a desirable system.

(2) Specification of viewpoints concerning eligibility of officers and employees

Regarding criteria for the eligibility of officers and employees (so-called “fit and proper principles”), there is a requirement that the authorities should refuse registration of an applicant who “does not have a personnel structure sufficient to conduct financial instruments business.” As criteria for refusing registration, a Cabinet Office Ordinance stipulates that 1) the applicant should be deemed to be incapable of executing the relevant business appropriately in light of the status of securing officers and employees with sufficient knowledge and experiences and the organizational structure and 2) the applicant should be deemed to pose the risk of undermining the credibility of the financial instruments business because of the inclusion among its officers and employees of personnel whose qualifications are inappropriate in light of their backgrounds and circumstances such as their relations with organized crime groups or with members of such groups. These criteria shall be applied to companies engaging in financial instruments business excluding those engaging in investment advisory and agency business.

With due consideration of the above-mentioned rules, the new guideline for supervision specifies what kind of viewpoints and methods should be adopted when supervision of financial instruments business operators is conducted in practice.

First, the guideline calls attention to whether officers and employees of the supervised financial instrument firms have sufficient knowledge and experience concerning governance and compliance and also points to the need to make sure that officers and employees are not members (or former members) of organized crime groups, do not have close relations with organized crime groups, and do not have experience of being imposed a fine or sentenced to imprisonment or higher punishment by violating laws governing financial institutions such as the Financial Instruments and Exchange Act (Special attention should be paid to records on fraud charges.).

The supervisory authorities are required to not only check the above-mentioned points when registration is made but also, after registration, to examine whether or not there is any problem regarding these points and take administrative actions against registered firms if need be.

5. Evaluation Items and Various Procedures on Sector-by-Sector Basis

(1) Type I financial instruments business

Concerning the “soundness of financial conditions,” the guideline specifies points of attention with regard to the capital regulation ratio.

Concerning the “appropriateness of business,” the guideline specifies points of attention separately for companies engaging in securities-related business and for companies engaging in over-the-counter derivatives business. Basically, the points specified for companies engaging in securities-related business include those specified by the guideline for the supervision of securities companies plus new viewpoints that have emerged in recent years in relation to supervision and the points specified for companies engaging in over-the-counter derivatives business include those specified by the guideline for the supervision of financial futures trading firms plus some new viewpoints.

Concerning “the exercise of an appropriate market intermediary function,” the new comprehensive guideline

provides viewpoints for supervision in relation to four themes--1) improvement in the credibility of the operations as market intermediaries, 2) the exercise of the function of checking issuers, 3) the exercise of the function of checking investors and 4) the maintenance of self-discipline as market players--in light of deliberations conducted at a consultation forum concerning the market intermediary function, etc. of securities companies” that was held last year by the Supervisory Bureau, a summary report thereof and the measures implemented by self-regulatory organizations such as the Japan Securities Dealers Association in line with the summary report.

(2) Type II financial instruments business

With regard to second financial instruments business, the guideline specifies rules concerning persons engaging in the sale, solicitation, public offering or private placement of interests in collective investment schemes as defined comprehensively by the Financial Instruments and Exchange Act. We assume such persons include those who were not subject to supervision by the authorities before the enforcement of this act and those who deal in funds with low transparency and liquidity regarding which it is extremely difficult for investors to grasp the actual status and conduct evaluation.

Therefore, the guideline calls attention to whether financial instruments business operators, when dealing in the aforesaid interests, provide investors with sufficient explanations regarding the outline of association contracts, etc., the outline of the business actually conducted by the relevant fund, and risks involved in interests under the relevant contract.

In particular, the guideline requires that the authorities take necessary actions in collaboration with the National Police Agency and other organizations concerned in the case where the relevant fund actually engages in pyramid selling and the like or constitutes a pyramid investment scheme or an endless money chain.

(3) Investment management business

With regard to investment management business, the guideline specifies points of attention concerning discretionary investment business, investment trust management business and fund management business. As items to be added to the “general” category, it also specifies points of attention concerning the management and administration of assets in relation to the business execution system and points of attention concerning the prohibition of exaggerated expressions in advertisements in relation to the system for solicitation and explanations.

In addition, as points of particular attention regarding companies engaging in the management of real estate-related funds, the guideline specifies evaluation items concerning two important matters--the system for ensuring due diligence on the occasion of the acquisition and sale of real estate and the system for preventing conflicts of interest. Companies engaging in the management of real estate-related funds include various types of firms such as anonymous associations and REITs (real estate investment funds). The guideline provides common points of attention useful in the case of investment in real estate as a specific resource.

(4) Investment advisory and agency business

With regard to investment advisory and agency business, the guideline specifies additional rules concerning exaggerated expressions in advertisements.

Regarding Announcement of Partial Revision of Guideline for Financial Conglomerates Supervision

The Financial Services Agency (FSA) on July 31, 2007 made necessary revisions to the Guideline for Financial Conglomerates Supervision and decided to apply it from September 30, 2007, when the Financial Instruments and Exchange Act was to take effect. The outline of the revision is as shown below.

1. Background to Revision

In line with the enforcement of the Financial Instruments and Exchange Act (hereinafter referred to as the "New Act"), the FSA partially revised the definition of a financial conglomerate based on the concept of the New Act and made necessary wording changes.

2. Contents of Revision

Previously, a financial conglomerate was defined as a financial group that includes two or more of the following categories of entities: 1) an entity engaging in banking business. 2) an entity engaging in insurance business and 3) an entity engaging in securities business, etc. The "entity engaging in securities business, etc." referred to an entity engaging in securities business, investment trust management business or investment advisory business. As the enforcement of the New Act makes it necessary to revise the definition of the "entity engaging in securities business, etc.," the FSA decided to revise the definition of a financial conglomerate as follows, too.

First, an entity engaging in securities business, etc. as defined previously is now defined as a "Type I financial instruments business operator engaging in securities-related business." In line with the fact that fund management companies, in addition to investment trust management companies and investment advisory companies engaging in business related to discretionary investment contracts, are subject to supervision by the FSA under the New Act, said companies are categorized together under the definition of "investment management business operators." It should be noted that under the New Act, an investment advisory company as defined previously is redefined as an "entity engaging in investment advisory and agency business" and treated separately from an entity engaging in business related to discretionary investment contracts. However, since most of the investment advisory companies that formed part of financial conglomerates as defined previously were concurrently engaging in investment trust management business, investment advisory companies are excluded as an element of the definition of a financial conglomerate in the latest revision.

Following the effectuation of the New Act, a corporate group that includes two or more of the three categories of entities--1) "Type I financial instruments business operators engaging in securities-related business" and an "entity engaging in investment advisory and agency business," 2) an entity engaging in banking business and 3) an entity engaging in insurance business-- is defined as a financial conglomerate.