

- orders from the beginning. Instead, they tried to settle the issue by seeking the customers' approval on what they had already done while offering an apology.
- (2) Some financial institutions showed ads containing the content of specific investment trust products to many customers as a way to solicit business from them even though the ads did not undergo checks by in-house officials in charge of screening such ads.

5. Outline of financial futures trader inspection results

In the 2003 SESC year, the Kanto Local Finance Bureau conducted an inspection on a firm mainly engaging in financial futures trading and found problems with its trading as explained below. In June 2004, the bureau chief notifies the firm of the inspection results, and the SESC made a recommendation to the Prime Minister and the FSA Commissioner.

- (1) Business solicitation accompanied by pledges to generate profit, conclusion of contracts for discretionary-account trading, reimbursement of investment losses and the act of providing benefits to customers to increase their fortune
- (2) Conduct that is recognized as significantly inappropriate for financial futures trading

In the 2003 SESC year, the SESC conducted inspections of firms which were authorized to conduct financial futures trading business to check if they were complying with market rules and how they were soliciting business from customers. However, no problems with financial futures trading by them were found in the inspections.

6. Outline of self-regulatory organization inspection results

The SESC conducts inspections of self-regulatory organizations, jointly with the Inspection Bureau of the FSA as a general rule, to make a comprehensive examination of operations of securities exchanges and their financial conditions amid increasing moves by securities exchanges to become stock companies and an increase in roles to be played by the exchanges as self-regulatory organizations.

The SESC launched inspections of trading at the Osaka Securities Exchange (OSE) in May 2002 and informed the OSE of the results in August 2003. In addition, the SESC conducted special inspections of the OSE in February 2004, and later informed the OSE of the results.

In May 2004, the SESC conducted inspections of the Nagoya Stock Exchange (NSE) and informed the NSE of the results in July 2004.

3. Recommendations

1) Outline

Based on the results of the inspections or the investigations of criminal offenses, the SESC may, if deemed necessary, present recommendations to the Prime Minister and the FSA Commissioner on administrative disciplinary actions and other necessary measures intended to ensure fairness in securities transactions (Article 20, Paragraph 1 of the FSA Establishment Law).

Specifically, recommendations by the SESC include proposing that administrative disciplinary measures be taken against securities companies and other entities if they are found to be violating laws and proposing that self-regulatory organizations take punitive measures against executives or employees of securities companies for such violation.

The SESC can ask the Prime Minister and the FSA Commissioner for a report on the measures taken based on the SESC's recommendations (Article 20, Paragraph 2 of the FSA Establishment Law).

Following the receipt of the recommendations by the SESC, the Prime Minister or the FSA Commissioner will hear from the securities companies concerned on the transactions in question, based on the results of the SESC inspections. If deemed necessary, the Prime Minister or the FSA Commissioner will take administrative disciplinary measures against the securities companies, including depriving the securities companies of their business registration license and ordering the suspension of their business operations.

Disciplinary measures against the registered securities traders of the securities companies are to be taken by the Japan Securities Dealers Association, which is entrusted by the Prime Minister to do clerical work on such measures (Article 64-7, Paragraph 1 of the SEL). The Japan Securities Dealers Association will hear from the registered securities traders concerned on the transactions in question, based on the results of the SESC inspections. If deemed necessary, the association will deprive the registered traders of their business registration license or order the suspension of their business activities.

2) Recommendations and measures taken based on recommendations

Based on the results of the inspections of securities companies and investigations of criminal offenses, the SESC issued 26 recommendations (16 cases of which were based on inspections by Local Finance Bureau chiefs) to the Prime Minister and the FSA Commissioner in the 2003 SESC year, calling for administrative disciplinary measures to be taken against securities companies and their executives and employees (registered securities traders) who was judged to have violated laws or regulations. Of these, 14 were administrative disciplinary measures against an identical number of securities companies, and one each was against a financial futures trader and a self-regulatory organization. In addition, 18 cases were against 28 executives and employees of securities companies.

(Note) Eight cases involved administrative disciplinary measures against both securities companies and their executives and employees, so the total number of cases does not coincide with the number of recommendations.

The following are specific cases of violations that led to the SESC's recommendations, which are explained in terms of who have violated the law, which law they have violated and what kind of administrative disciplinary measures have been taken by the FSA Commissioner.

1. Violations of laws by securities companies

1) Act of concluding contracts for discretionary-account trading (violation of Article 42, Paragraph 1, item 5 of the SEL)

- An employee working under a performance-based pay system at the investment service division of the head office of **Okachi Securities Co.** concluded discretionary-account trading contracts with the employee's clients, in which the clients agreed to enable the employee to trade stocks on behalf of the clients without their consent on all aspects of trading, whether buy or sell orders were to be placed, which stocks were to be traded, in what amount and at what price. Based on the contracts, the employee in question accepted orders from the clients and executed transactions without prior consent of each transaction.

The securities company had been found to have engaged in discretionary-account trading in previous inspections.

- Recommendation date: June 8, 2004
- Administrative disciplinary measures: One-day suspension of stock brokerage services and business improvement order

(Note) The recommendation called for disciplinary measures against the employee as well.

2) **Act of making false statements, or misleading statements about important matters, in securities and other financial transactions** (violation of Article 4, item 1 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Article 42, Paragraph 1, item 9 of the SEL)

- The general manager of the sales department at the head office of **Mizuho Investors Securities Co.** prepared a document to publicize an investment technique combining the trading of exchange-traded funds (ETFs) and stock index options that would boast an annual yield of 27% on a simulation basis without showing any investment preconditions, although such a high return of profit was least likely to be achieved. The general manager also compiled a customer-by-customer list of investment achievements that did not accurately reflect actual trading results because the list did not take into account each customer's latent profits or losses on ETF holdings. The manager then distributed or presented the document between July 2001 and January 2003 to a large number of individual investors who had little experience with options trading, which amounted to the act of making misleading statements about important matters in trading.

- Recommendation date: August 19, 2003

- Administrative disciplinary measures: Business improvement order

(Note) The recommendation called for disciplinary measures against the general manager as well.

3) **Act of soliciting business with promises to provide special benefits** (violation of Article 4, item 2 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Article 42, Paragraph 1, item 9 of the SEL, Article 14, Paragraph 1 of the LFSF applied)

- In January 1997 and January 1998, **HSBC Securities (Japan) Ltd.** solicited securities transactions from an investment advisory company, which had contracts concluded with customers for discretionary investment, with a promise to pay money to the investment advisory company under the pretext of investment consulting fees in return for receiving trading orders from the advisory company.

- Recommendation date: July 17, 2003

- Administrative disciplinary measures: Three-day suspension of stock brokerage services and business improvement order

4) **Act of making a series of securities transactions to create an artificial market that does not reflect the actual state of the market or the act of receiving a series of securities brokerage orders with knowledge that doing so would help create an artificial market that does not reflect the actual state of the market** (violation of Article 4, item 3 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Article 42, Paragraph 1, item 9 of the SEL, Article 14, Paragraph 1 of the LFSF applied)

- In connection with corporate bonds with a clause to exchange them for shares of a listed company other than the bond-issuing firm, or exchangeable bonds (hereinafter referred to as "EB"), a (then) trader at the Japanese equity derivatives department of **Societe Generale Securities (North Pacific) Ltd.** placed a series of large limit orders to sell the reference shares at ¥782, a lower price than the EB's strike price (¥783). This created a situation in which the closing price of the reference shares would not equal or exceed the strike price unless all the orders

were consummated during the last minute of trading for the day, from 14:58 until the day's closing, on November 14, 2001, which was the valuation date when the EB redemption method, as to whether by payment of cash equal to the EB's principal amount or by delivery of the reference shares, was to be decided upon the day's closing price of the reference shares. This was intended to make the reference price lower than the strike price so that the EB would be redeemed by the delivery of the shares so as to enable Societe Generale Securities' parent company to avoid risks that might have arisen in the event of the EB's redemption by cash payment from its status as a holder of the reference shares that had been held in preparation for the stock redemption.

As a result of this, the price of the reference shares dropped from ¥783 in the immediate past to close at ¥781, making the EB redeemable by the delivery of the shares. The parent company therefore succeeded in avoiding risks that might have arisen from its status as a holder of the reference shares.

- Recommendation date: November 28, 2003
 - Administrative disciplinary measures: Ten-day suspension of own-account stock trading and business improvement order
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- On February 4, 2003, an executive staff of the dealing group of the equity department of **Mizuho Investors Securities Co.** placed a series of buy orders for shares of a certain listed stock on the company's own account to absorb sell orders placed by its customer, at a price lower than the ¥275 quoted in the immediate past, with the aim of causing the price of the listed stock to drop by ensuring that the buy and sell orders could be executed immediately. The executive staff engaged in the dealing in a manner that would not cause the stock exchange to temporarily suspend trading in the shares of the listed stock that would have happened if a special sell quote had been indicated for the stock. As a result, the executive staff succeeded in pushing down the stock price in favor of Mizuho Investors Securities.
 - Recommendation date: January 8, 2004
 - Administrative disciplinary measures: Ten-day suspension of own-account stock trading and business improvement order(Note) The recommendation called for disciplinary measures against the executive staff as well.
-
- The President of **Get Securities Co.**, the (then) executive manager of the company's first marketing division, the (then) deputy manager of the first marketing division and the manager of the marketing department received buy and sell orders from a customer for shares of Cats Inc. and executed the orders between June 5, 2001 and October 28, 2002 despite their knowledge that the customer (who was later accused and indicted on the charge of manipulating Cats shares in violation of the SEL) was placing successive limit buy orders at high prices for the stock with the aim of pushing up its prices.
 - Recommendation date: June 30, 2004
 - Administrative disciplinary measures: Three-day suspension of all securities services, five-day suspension of stock brokerage service and business improvement order(Note) The recommendation called for disciplinary measures against the four officials of Get Securities as well.

- **Marusan Securities Co.** received buy and sell orders from a customer for shares of Cats Inc. and executed the orders between June 8, 2001 and July 10, 2001 despite its knowledge that the customer (who was later accused and indicted on the charge of manipulating Cats shares in violation of the SEL) was placing successive limit buy orders at high prices for the stock with the aim of pushing up its prices.
 - Recommendation date: June 30, 2004
 - Administrative disciplinary measures: Three-day suspension of stock brokerage service and business improvement order
- 5) **Act of soliciting business by providing undisclosed corporate-related information** (violation of Article 4, item 9 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Article 42, Paragraph 1, item 9 of the SEL)
- The three executives mentioned below and four other employees of **Iida Securities Co.** solicited orders for buying over-the-counter securities by providing undisclosed corporate-related information.
 - (1) The executive manager of the marketing department received undisclosed corporate-related information on stock-split plans by several issuers of securities registered for over-the-counter trading from a manager of the Nagoya corporate finance department of Tokai Tokyo Securities Co. on January 27, 2004. The executive manager solicited buying orders for the over-the-counter securities from a large number of customers between January 28, 2004 and February 16, 2004 by providing the undisclosed corporate-related information.
 - (2) The President of the securities company received the undisclosed corporate-related information above mentioned from the executive manager of the company's marketing department, and solicited buying orders for the over-the-counter securities from several customers between February 2, 2004 and February 13, 2004 by providing the undisclosed corporate-related information.
 - (3) The executive manager in charge of overall operations at the company's head office received the undisclosed corporate-related information above mentioned from the executive manager of the marketing department, and solicited buying orders for the over-the-counter securities from a customer between February 2, 2004 and February 9, 2004 by providing the undisclosed corporate-related information.
 - Recommendation date: June 30, 2004
 - Administrative disciplinary measures: Two-day suspension of all securities services at all outlets and business improvement order
 (Note) The recommendation called for disciplinary measures against the three executives as well.
- 6) **Act of engaging in business operations that create a situation in which a brokerage firm fails to protect the interest of investors in its securities options brokerage service by soliciting business deemed inappropriate in light of the customers' knowledge of the financial instruments, their experience with trading and their financial state or a situation in which a brokerage firm is likely to fail to protect the interest of investors for a similar reason** (violation of Article 43, item 1 of the SEL)
- **Izumi Securities Co.** worked out a plan to launch a campaign for options trading linked with the 225-issue Nikkei Stock Average (referred to as "options trading")

for this case) at all its outlets, and started to actively solicit business for the financial product from customers in April 2003 under the leadership of the management, including the President. Meanwhile, the securities company failed to provide sufficient in-house education to its salespersons over the mechanism of options trading even though a large number of them kept soliciting business for the trading while lacking knowledge about such trading. The situation indicated that the securities company failed to establish a sufficient system to prevent salespeople from engaging in inappropriate business solicitation unsuitable for customers' investment situations.

Under these circumstances, several salespeople solicited business from customers who mainly lived on pension revenues and who had primarily traded in investment trusts and bonds in the past but had no experience in trading in stock margin trading or options trading and had no knowledge about the basic trading mechanism of options trading until they were approached by the salespeople for the options trading in question. Without having the basic mechanism of options trading and its investment risks well understood by these customers, the salespeople offered investment proposals to the customers, with every aspect of trading decisions-options to be traded, the amount to be invested and whether sell or buy orders were to be placed-decided by the salespeople. As the customers were led to unconditionally accept these proposals, the salespeople repeatedly placed sell orders for the options during a short period of time, with the trading amount well exceeding the total value of the financial assets held by the customers. As a result, the customers suffered a large amount of losses.

- Recommendation date: March 5, 2004
- Administrative disciplinary measures: One-day suspension of all securities services at all outlets, two-day suspension of brokerage service for stock index options at all outlets and business improvement order

7) Act of engaging in business operations that create a situation in which a securities company's control of undisclosed corporate-related information it has obtained is deemed insufficient from the viewpoint of preventing unfair trading making use of such information (violation of Article 10, item 4 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Article 43, item 2 of the SEL, Article 14, Paragraph 1 of the LFSF applied)

- Due to a failure by **UBS Securities Japan Ltd.** to take adequate steps over the control of undisclosed corporate-related information, analysts at the securities company's stock research department listed information on a particular listed firm obtained from that listed firm, including the firm's own stock-buying plan and its downward earnings revision plan, on their report with no knowledge that such information was classified as undisclosed corporate-related information as defined under the SEL.

The stock research department's division in charge of screening analysts' reports overlooked the inclusion of the undisclosed corporate-related information in the report, and posted the report on the securities company's Web site in April 2003. The screening division then explained the report at in-house meetings and distributed the report to a large number of client investors via e-mail. The situation indicated that the securities company conducted business even though they failed to take sufficient steps to prevent unfair trading in connection with the handling of undisclosed corporate-related information.

- Recommendation date: May 21, 2004

- Administrative disciplinary measures: Business improvement order
- **Tokai Tokyo Securities Co.**'s trade-screening room failed to take adequate steps to control undisclosed corporate-related information on stock-split plans by several issuers of securities registered for over-the-counter trading as the room did not receive any report on the plans from relevant personnel of the company, including the manager of the Nagoya corporate finance department of Tokai Tokyo Securities. In addition, the manager of the Nagoya corporate finance department leaked this information and other undisclosed corporate-related information held by the securities company regarding stock-split plans by other issuers of over-the-counter securities to the executive manager of Iida Securities Co.'s marketing department. This indicated that Tokai Tokyo Securities was engaging in business operations in a situation in which its control of undisclosed corporate-related information was deemed insufficient from the viewpoint of preventing unfair trading making use of such information.
 - Recommendation date: June 30, 2004
 - Administrative disciplinary measures: Business improvement order

(Note) The recommendation called for disciplinary measures against the manager of the Nagoya corporate finance department as well because the manager's act of leaking the undisclosed corporate-related information to another company amounted to an act of leaking confidential information that brokerage officials have obtained in the course of implementing their business duty to third parties as defined under Article 9, Paragraph 3, item 18 of the Regulation Concerning Employees of the Securities Industry (Fair Business Practice Regulation 8) set by the Japan Securities Dealers Association. Disciplinary measures were also sought against the manager as the manager's act could be classified as "significantly inappropriate conduct" by registered securities traders prescribed under Article 64-5, Paragraph 1, item 2 of the SEL.
- The President of **Iida Securities Co.** received undisclosed corporate-related information on stock-split plans by several issuers of securities registered for over-the-counter trading from the executive manager of the securities company's marketing department, and solicited buying orders for the over-the-counter securities from several customers between February 2, 2004 and February 13, 2004 by providing the undisclosed corporate-related information. In addition, the President convened marketing meetings and encouraged other executives of Iida Securities to follow him in soliciting business using this information. This indicated that Iida Securities was engaging in business operations in a situation in which its control of undisclosed corporate-related information was deemed insufficient from the viewpoint of preventing unfair trading taking advantage of such information.
 - Recommendation date: June 30, 2004
 - Administrative disciplinary measures: Two-day suspension of all securities services and business improvement order

(Note) The recommendation called for disciplinary measures against the President as well.

8) Act of failing to verify the identity of customers who are suspected of engaging in trading by pretending to be other persons whose names are registered for the trading (violation of Article 3, Paragraph 1 of the Personal Identity Verification Law)

- When receiving orders for securities trading from several customers at least between April 1, 2003 and March 31, 2004, **Monex Securities Co.** suspected that

the customers who had placed these orders were pretending to be other persons whose names were registered for the trading in question. Nevertheless, Monex accepted the orders and executed them without verifying the customers' real identity.

- Recommendation date: June 17, 2004
- Administrative disciplinary measures: Order for remedial measures

- The (then) executive manager of the Tokyo branch of **Angel Securities Co.** received a request from a customer for the securities company to open accounts for several corporate clients without verifying the identity of the customer and the corporate clients. The branch manager then instructed his subordinates to open the accounts in line with the request. The subordinates opened the accounts as requested, accepted stock trading orders from the customer and executed the orders on April 10, 2003 and later.

- Recommendation date: June 22, 2004
- Administrative disciplinary measures: Yet to be determined

(Note) The recommendation called for disciplinary measures against the branch manager as well because his conduct amounted to a "significantly inappropriate conduct" by registered securities traders prescribed under Article 64-5, Paragraph 1, item 2 of the SEL.

- The manager of the marketing department of **Get Securities Co.** gained knowledge that a customer (who was later accused and indicted on the charge of manipulating prices of Cats Inc. shares) was engaging in trading under several corporate accounts whose registered names were different from the name of the customer. Nevertheless, the marketing department manager accepted trading orders from the real customer and executed them without verifying the real identity of the customer.

- Recommendation date: June 30, 2004
- Administrative disciplinary measures: Three-day suspension of all securities services, five-day suspension of stock brokerage services, and business improvement order

(Note) The recommendation called for disciplinary measures against four registered securities traders at Get Securities.

9) **Prohibition of act deemed as manipulating securities prices** (violation of Article 159, Paragraph 1, items 3 and 8 of the SEL)

- The President of **Japan Electronic Securities Co.** engaged in fictitious trading for stock options listed on the options market established by the Osaka Securities Exchange in order to make trading in the stock options in question look more active than it really was.

- Recommendation date: August 5, 2003
- Administrative disciplinary measures: Five-day suspension of all securities services at all outlets, two-month suspension of options trading services and business improvement order

2. **Violations of laws or regulations by executives and other employees of securities companies**

The following are types of violations of laws or regulations committed by executives and other employees (registered securities traders) of securities companies for which the SESC

issued recommendations. (Listed below are violations involving recommendations made only for executives and other employees of securities companies. Violations also involving recommendations made for securities companies are excluded.)

- 1) **Act of concluding contracts for discretionary-account trading** (violation of Article 42, Paragraph 1, item 5 of the SEL)
(Recommendations issued against 11 individuals at eight companies)
- 2) **Act of soliciting business with promises to provide special benefits** (violation of Article 4, item 2 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Article 42, Paragraph 1, item 9 of the SEL)
(Recommendation issued against one individual at one company)
- 3) **Securities trading intended for executives and other employees of securities companies to pursue speculative profits** (violation of Article 4, item 5 of the Cabinet Office directives, based on Article 42, Paragraph 1, item 9 of the SEL)
(Recommendation issued against one individual at one company)
- 4) **Securities trading based on non-disclosed information obtained in the course of business operations** (violation of Article 4, item 5 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Article 42, Paragraph 1, item 9 of the SEL)
(Recommendation issued against one individual at one company)

3. Violations of laws or regulations by financial futures traders

- 1) **Business solicitation with promises to guarantee profits, conclusion of contracts for discretionary-account trading, reimbursement of investment losses and the act of providing benefits to customers to help increase their fortune** (violation of Article 25, item 3 of the FFTL Enforcement Order, based on Article 74, items 2, 3 and 7 of the FFTL)

- The chairman of **A.C.E. International Inc.** was involved in the following acts.
 - (1) Concluding contracts with a large number of customers from March 2001 to September 2003 on overseas currency futures options trading. In concluding the contracts, the chairman promised the customers to reimburse all or part of their losses incurred on such investments or guaranteed that they would receive a profit on the investments to solicit business from the customers. The chairman then received the customers' agreement that he could decide on all investment conditions set under each item of Article 24 of the FFTL Enforcement Order-specific financial instruments to be traded, types of currency subject to options trading, whether to place buy or sell orders and trading prices-without the customers' prior consent. Based on the contracts, the chairman accepted orders from the customers and executed them from April 2, 2001 to September 18, 2003.
 - (2) Providing benefits to a large number of customers and helped increase their fortune from June 2001 to December 2003 by reimbursing all or part of the losses his customers incurred on investment in overseas currency futures options trading, transferring investment losses suffered by customers to the company's account and shifting profits earned by the company from the company's account to customers' accounts.
 - Recommendation date: June 30, 2004
 - Administrative disciplinary measures: Yet to be determined

- 2) **Conduct deemed significantly inappropriate for trading by financial futures traders**
The conduct described in this section is deemed the conduct aimed at soliciting business

from customers in financial futures trading in excess of their financial standing in light of their financial conditions that has come to the knowledge of financial futures traders through customer application forms, such as funds earmarked for investment. Such conduct is prescribed under Article 4, item 6 of codes of conduct for employees engaging in financial futures trading that are set by the Financial Futures Association of Japan.

The conduct explained below resulted from a financial futures trader's lack of an in-house customer management system. The trader in question was involved in the illicit practice in a systemic manner. The conduct can be described as significantly inappropriate for the financial futures trader as it undermined the fairness of trading and the interest of customers.

- **A.C.E. International** actively solicited business from customers in overseas currency futures options trading (referred to as "options trading" for this case) while the company failed to establish an in-house customer management system, including the daily monitoring of customers' financial transactions, independent from the company's marketing division. In addition, the face to face survey system at the company had become a system in name only. Meanwhile, the President of the company drummed up a business solicitation campaign by instructing salespeople to ease in-house rules on options trading and asked for short-term efforts to increase the number of buying orders.

In response to these instructions, many salesclerks encouraged their customers to buy or sell a large number of options soon after they had opened their accounts even though they did not have sufficient ability for investment judgment. Such transactions were apparently deemed excessively speculative in light of the customers' financial conditions and the level of their investment ability. As a result, the customers suffered large capital losses. In accepting brokerage orders for overseas financial futures trading, the company failed to address the "prevention of excessively speculative transactions" as prescribed under 9-2-4 (2) of a guideline for supervision set by the FSA.

- Recommendation date: June 30, 2004
- Administrative disciplinary measures: Yet to be determined

4. Violations of law by self-regulatory organizations

(1) Violations of laws unearthed through investigations of criminal offenses (Article 159, Paragraph 1, items 3 and 8)

The Vice President of the **Osaka Securities Exchange (OSE)** conducted fictitious trading on stock options listed on the securities options market run by the OSE in order to make option trading on the OSE look more active than it really was.

(Note) The SESC filed a criminal accusation on the case on July 25, 2003. Refer to "(2) OSE Case" in "2. Filing of complaints" of "2) Investigations of criminal offenses and filing of complaints" under "1. Investigations of Criminal Offenses and Filing of Complaints."

(2) Problems found at the OSE regarding its business as a self-regulatory organization

As of the benchmark inspection date of May 8, 2002, the following problems were found at the OSE regarding its business as a self-regulatory organization.

1) Inspection business

The OSE failed to devise long-term plans to foster the ability of its officers in charge of inspections on its member securities companies. In addition, no systemic or sufficient efforts were made to compile inspection plans.

The OSE failed to consider elements other than the length of interval from the latest inspections in selecting OSE member companies subject to inspection, including

transaction records at the OSE and information obtained by relevant divisions of the OSE.

2) Measures taken based on inspections

The OSE failed to clarify standards used to decide what measures to take based on inspections. The OSE also did not make efforts to establish such standards in a systemic manner while continuing to take actions against member companies.

3) Market administration business

The OSE failed to devise long-term plans to foster the ability of its officers in charge of market administration. The OSE also did not act to improve its ineffective system of taking out samples of transactions for the detecting of illicit trading practices. Standards currently used by the OSE in extracting such samples do not accurately reflect the actual state of the market, resulting in the number of samples taken becoming excessive-sometimes enormous and other times zero. The OSE did not take measures to review these standards.

Even though the OSE took out trading samples for the detecting of illicit trading practices, such as fictitious trading and coordinated trading, the exchange did not look into records of own-account transactions in question made by securities companies involved in cross-trade transactions relationship with transaction counterpart of customers identified.

4) Cooperation between relevant sections

The OSE failed to make efforts to promote in-house cooperation and information-sharing among relevant sections. Due to the lack of this in-house cooperation, information obtained separately by different sections was not used effectively in the OSE's overall inspection and market administration business.

- Recommendation date: August 5, 2003
- Administrative disciplinary measures: Three-month suspension of business related to the listing of stocks on the OSE securities market, three-month suspension of business related to the new listing of stock options on the OSE securities market, business improvement order, submission of a report on the implementation of measures under the business improvement order and checks of the implementation

4. Policy Proposals

1) Outline

Based on the results of inspections or investigations of criminal offenses, the SESC may, if necessary, present policy proposals to the Prime Minister, the FSA Commissioner or the Minister of Finance in order to ensure fairness in securities transactions (Article 21 of the FSA Establishment Law).

Policy proposals are put forward by the SESC after its comprehensive analysis of the results it obtained through the inspections and investigations. Such proposals are intended to clarify the SESC's view on laws, regulations and self-regulatory trading rules and have it reflected in policy measures being taken by other government agencies and self-regulatory organizations. Proposals by the SESC serve as important yardsticks for relevant government authorities in formulating certain policies.

The SESC has proposed reviewing or revising existing laws or regulations on securities trading and related matters, and self-regulatory rules, when such rules and laws are found unfit to deal with issues found in actual transactions. The SESC has also pointed out problems inherent in the current legal framework for securities transactions and specific areas