

The main issues raised by the FSA at opinion exchange meetings with trade associations

[held on July 19, 2022, with the Japan Securities Dealers Association]

1. Policies for the 2022 business year

- We are planning to reflect the direction of financial policies for the 2022 business year in the JFSA Priorities for July 2022- June 2023 and publish it by around mid-August as usual. In order to achieve Prime Minister Kishida's "a New Form of Capitalism," which aims to create a virtuous cycle of growth and distribution, the FSA will carry out related measures. Securities companies are expected to support fund procurement of companies with growth potential and contribute to asset building of households by exercising their financial intermediary function.

2. For formulating a "Doubling Asset-based Incomes Plan"

- The Grand Design and Action Plan for a New Form of Capitalism, which was decided by the Cabinet in June, states that the government will formulate the comprehensive "Doubling Asset-based Incomes Plan" by the end of 2022 with the aim of further accelerating the shift of personal financial assets from savings to investment.
- The FSA has been deliberating measures concretely from a broad perspective. We understand that you are also considering proposals concerning specific measures. We would like to continue opinion exchanges with you and other related parties.

3. Customer-oriented business conduct

- In order to facilitate the shift of personal financial assets from savings to investment, efforts by securities companies and other financial institutions to ensure customers' trust are indispensable, in addition to the government's institutional measures. Also,

from the perspective of the sustainability of the securities companies, it is important to further deepen their initiatives for customer-oriented business conduct under strong leadership of the top management.

- Regarding structured bonds, in particular, the FSA has pointed out problems repeatedly on occasions including the opinion exchange meetings.

We hear that based on the awareness that complicated structured bonds are not stable investment products, some securities companies have further limited the targeted customers or have internally and externally clarified their policies not to deal with structured bonds or other products that are not suited for medium-to long-term asset building.

- The FSA considers it important that the top management of securities companies repeatedly discuss the true meaning of customer-oriented business conduct and optimal support for asset building for customers based on their management principles. The FSA would like to continue dialogues regarding efforts being made by related parties.

4. Promoting sustainable finance

- Initiatives for achieving carbon neutrality by 2050 are also the top priorities for the national government, and we have conducted deliberations for promoting sustainable finance with the participation of the Japan Securities Dealers Association.

The FSA intends to attract ESG funds to Japan from all over the world, thereby making Japan a capital market base open to the whole world, or a Green International Financial Center, in the field of sustainable finance, including social bonds, not only for achieving decarbonization but also for solving various other social problems. We would appreciate your continued cooperation for facilitating this move.

5. Financial education

- In order to promote asset building of households, the FSA has endeavored to enhance

people's financial literacy. Accompanying the lowering of the legal age of adulthood to 18 in April 2022, lessons on asset building came to be incorporated in the high school homemaking curriculum. We appreciate your efforts, such as signing the Memorandum of Understanding on financial education with the Japanese Bankers Association at the end of 2021, and we have high expectation for your future initiatives.

6. Human investment

- For achieving a new form of capitalism, human investment is also important. Personnel expenses should be considered as human investment, not merely as cost, and companies should be aware of the fact that human investment will make a base for creating sustainable value. Securities companies have also considered human capital to serve as a base for appropriately fulfilling their financial intermediary function, including customer-oriented business conduct. We would like to have talks with securities companies regarding their efforts for human investment and human resources development, including wage increases.

7. Financial measures in response to the disaster, etc. caused by the heavy rain from July 14, 2022

- We express our condolences and sympathies to victims of the disaster, etc. caused by the heavy rain from July 14, 2022.
- The Disaster Relief Act is applied to Miyagi Prefecture in relation to the latest disaster, and the Tohoku Local Finance Bureau issued a notice requesting financial measures to relevant financial institutions, etc. on July 19.
- Financial institutions in disaster-affected areas are requested to ascertain disaster victims' opinions and needs and offer support meticulously from their standpoints based on the issued requests.
- Additionally, as the heavy rain from July 18 also caused damage mainly in the

Kyushu region, financial institutions in relevant areas are requested to offer support depending on the circumstances of individual areas.

8. Monitoring of securities business for the 2022 business year

- We understand that securities companies are playing significant roles as gatekeepers in the market and actively contribute to securing the fairness in the market, and at the same time, sufficiently fulfill their financial intermediary function and support stable asset building of households and fund procurement of companies with growth potential.
- In order to properly exercise these functions, it is important for securities companies to develop better compliance systems and ensure good governance, and make constant efforts to ascertain customers' real needs by deepening their initiatives for customer-oriented business conduct, in light of their own business size and characteristics, under strong leadership of the top management.
- The FSA maintains the basic policy for monitoring in the 2022 business year as well and will continue deepened dialogues on securities companies' initiatives for these challenges, while taking into account changes in business environments surrounding individual companies.
- Concrete issues include the following.
 - Regarding customer-oriented business conduct, the FSA will continuously conduct monitoring from such perspectives as whether customers really understand risks and whether companies make recommendations that serve customers' best interests upon selling risk-involving products.

With regard to complicated structured bonds, in particular, the FSA will continue dialogues carefully with individual securities companies as to whether actual solicitation activities are consistent with their management principles and sales strategies in light of the characteristics and risk levels of those products and the actual status of solicitations that involve methods such as selling similar products

continuously through earlier reimbursements.

Recently, cases of selling structured bonds and other complicated risk-involving products through IFAs, etc. under outsourcing agreements are increasing. In monitoring, the FSA will also pay attention to whether securities companies are managing outsourcees' business operations properly.

- Regarding compliance systems, the FSA will continuously monitor whether securities companies have developed an effective, functional system and corporate culture, and not just check individual cases. Additionally, the FSA will monitor the status of their compliance to the measures to prevent adverse effects in consideration of the reviewed firewall regulations separating banks and securities companies and whether information relating to customers, etc. in general is thoroughly managed on a need-to-know basis.
- Regarding system risk management systems, the FSA will continuously monitor the status of measures taken by securities companies for unauthorized accesses in light of the details of past related cases, and the status of the development and operation of relevant systems, such as those for substantially managing the business processes as a whole, including those of outsourcees, and for securing toughness in business operations. Based on the monitoring results, the FSA will request individual companies to take required measures as necessary.
- Furthermore, based on the Comprehensive Guidelines for Supervision, which was revised on June 22, the FSA will also conduct the following.
 - (i) When acquisition, etc. of financial institutions caused material changes in the composition of officers, management policies or the like of any financial institution, the FSA will verify the content of its business and the appropriateness of its business execution system in detail at a similar level as in the case of registration screening.
 - (ii) With regard to financial institutions that have been suspending business for a long time or those that have not commenced business for a long time after being registered, when any problem is found in the process of ascertaining and verifying the legitimacy of the reasons therefor, the FSA will take required supervisory actions.

- In addition to these issues found across business categories, the FSA will continue deepened dialogues depending on individual companies' characteristics, sometimes in collaboration with foreign authorities, with regard to how globally operating securities companies have developed their governance and business management systems and risk management systems that support their global businesses and their measures against emergencies, while referring to a letter compiling supervisory focus points issued in April 2022.

9. Review of use of papers, seals, and face-to-face procedures in the financial industry

- The "Study Group on Review of Use of Papers, Seals, and Face-to-Face Procedures in the Financial Industry" has continuously been held also in the business year 2021 to follow up the progress of the review, concrete examples and remaining challenges in the financial industry. The outline of the follow-up results was published on June 24.
- Apart from procedures based on legal regulations, active responses of the industry as a whole and ongoing efforts of individual financial institutions exercising ingenuity are indispensable for the revision of industry practices predicated on the use of papers, seals, and face-to-face procedures.
- The Japan Securities Dealers Association is expected to have such awareness and establish matters to be addressed in the revision of industry practices predicated on the use of papers, seals, and face-to-face procedures by setting a specific period, and periodically check concrete progress to promote steady implementation of the review.
- When establishing matters to be addressed, the key points for the future follow-ups shown in the outline of the results should be referred to, including the following.
 - Deliberations for increasing the utilization rate of online procedures based on the ascertaining and analysis of the current status of utilization
 - Substantial sharing of problems and concrete examples among individual companies

- Promotion of further computerization of various types of procedures, including the utilization of a public identity verification service in online procedures.

10. G20 Finance Ministers and Central Bank Governors Meeting in July

- The G20 Finance Ministers and Central Bank Governors Meeting was held from July 15 to July 16, and matters concerning the global economy and the financial sector were discussed. The next Finance Ministers and Central Bank Governors Meeting will be held in October, and the Leaders' Summit is also scheduled in November.
- After the G20 Finance Ministers and Central Bank Governors Meeting, Indonesia, which holds the presidency, published the Chair's Summary compiling member countries' opinions and the details broadly supported. Key points of the summary are as follows.
 - Member countries welcomed the progress of discussions on sustainable finance mainly at the G20 Sustainable Finance Working Group (SFWG). The SFWG has been working on a high-level transition finance framework and the improvement of the reliability of financial institutions' commitments towards net-zero emissions. A report will be made at the Finance Ministers and Central Bank Governors Meeting in October.
 - Regarding financial regulations and systems, the work being conducted by the Financial Stability Board (FSB) for strictly regulating and supervising crypto-assets is welcomed. The results of the work will be reported at the Finance Ministers and Central Bank Governors Meeting in October. Member countries also support the effective implementation of standards regarding crypto-assets established by the Financial Action Task Force (FATF), or the Travel Rule in particular.

11. Recent activities of the IOSCO

<< Non-bank financial intermediation (NBFIs) >>

- The Financial Stability Board (FSB) and the International Organization of Securities Commissions (IOSCO) have continuously been prioritizing works concerning non-bank financial intermediation (NBFi).
- Regarding measures for money market funds (MMFs), the FSA has had discussions with related parties based on international discussions. We hope to receive the continued cooperation of related parties for materializing measures for Japanese money reserve funds (MRFs), etc.
- Works have also been underway concerning a wide range of topics on non-bank financial intermediation other than MMFs. With regard to the project to analyze liquidity risk management of open-end funds (OEFs) amid the COVID-19 pandemic, a report will be compiled by the end of 2022.
- With regard to the project to analyze practices concerning deposits amid the COVID-19 pandemic, the final report will be compiled by around the end of September 2022 based on comments received through the consultative discussions on the analysis results.
- The FSB plans to deliberate about systemic measures for NBFi based on these works and report its major achievements and future policies to G20.

<< Sustainable finance >>

- The Sustainable Finance Task Force consists of three working groups (under themes of issuers' sustainability-related disclosures, promotion of good practices in the industry and in conducting supervision, and the carbon market) based on the new work plan approved at the IOSCO's representative directors meeting in March 2022. Under Working Group I (issuers' sustainability-related disclosures), the ISSB Standards Endorsement WG and the Guarantee WG have been established, and the Head of the International Accounting Adjustment Office, SONODA, of the FSA serves as a co-leader of the latter WG.
- As international discussions on sustainability are expected to become more and more

active, we would like to continue opinion and information exchange closely with related parties.

<< FinTech >>

- The IOSCO established the FinTech Task Force in March 2022 with the aim of accelerating the analysis of the latest trends on FinTech, such as crypto-assets, and its Roadmap was approved at the representative directors meeting in June. FinTech covers a wide range of areas. However, for 2022 and 2023, problems and countermeasures mainly focusing on crypto-assets, stable coins, and DeFi will be discussed from the perspective of protecting investors and ensuring the fairness of the market.

12. Trends at the FATF

- In June 2022, the Director for International Policies, HABUCHI, of the FSA was appointed as the co-chair of the working group in charge of the revision of the FATF standards. The accession to office of co-chair is significant from the perspective of [i] reflecting the circumstances and ideas of Japan in international discussions and [ii] enhancing Japan's anti-money laundering and terrorist financing measures based on international discussions. We would like to maintain close collaboration with financial institutions.

13. Revision of the "Frequently Asked Questions Regarding the Guidelines for Anti-Money Laundering and Combating the Financing of Terrorism (FAQ)"

- The FSA have received various opinions and questions concerning the "Frequently Asked Questions Regarding the Guidelines for Anti-Money Laundering and Combating the Financing of Terrorism (FAQ)." In order to clarify the ideas which attracted many questions in particular, the FSA prepared a draft revision of the FAQ and sent it to the financial business associations in May to seek opinions and

comments.

- The FSA appreciates that many valuable opinions and comments were submitted through the associations.
- The FSA are now carefully reviewing the opinions and comments received and will respond to the opinions and comments later. The FSA will review the draft with your opinions and publish revised FAQ in coming weeks.

14. Publication of the "Results of Monitoring Customer-Oriented Business Conduct of Investment Trust Distributors"

- The FSA published the "Results of Monitoring Customer-Oriented Business Conduct of Investment Trust Distributors" on June 30.
- The document points out the following.
 - Thanks to efforts to exercise ingenuity of some distributors, a mechanism to allow customers to select distributors is found to have been established.
 - However, many of the distributors still have problems in customer-oriented business conduct in terms of their sales systems and in visualization of their related policies, and they may have failed to take this issue seriously as a business challenge.
 - The document cites problems of structured bonds regarding their characteristics and distributors' sales systems, and mentions the necessity of discussions on those problems at the level of the top management if distributors continue dealing with such products.
- Major perspectives for future monitoring are to be the following.
 - Whether the top management considers sustainable business strategies on a long-term basis and has clarified and materialized the content thereof in their policies for achieving the Principles for Customer-Oriented Business Conduct
 - Whether those policies have been firmly rooted among front-line sales personnel

and have borne fruit

- Please continue efforts for achieving customer-oriented business conduct.

15. Publication of the "Second Report of the FSA's Expert Panel on Sustainable Finance"

- While the approaches to achieve decarbonization and a new form of capitalism are being discussed as significant challenges, it has become indispensable to promote finance to facilitate the shift to a new industrial and social structure and achieve a sustainable society (sustainable finance). The FSA has also been promoting relevant measures as significant themes.
- On July 13, the FSA published the Second Report of the Expert Panel on Sustainable Finance, which compiles the progress of the measures for promoting sustainable finance for the last one year period, challenges further identified and the direction for responding thereto.
- The Second Report contains the following statements.
 - Regarding the "**enhancement of corporate disclosure**," the Working Group on Corporate Disclosure of the Financial System Council recommended in June to create a column for sustainability-related disclosure in an annual securities report. Relevant Cabinet Office Order and other laws and regulations need to be developed promptly.
 - Targeting ESG evaluation and data providers that evaluate companies' ESG-related efforts, the FSA published a draft Code of Conduct for ESG Evaluation and Data Providers on July 12 in order to ensure fairness in evaluation as a result of the deliberations on the theme of the "**demonstration of capital market functions**." The FSA should request approval of ESG evaluation and data providers and encourage them to follow the code of conduct.
 - Regarding the "**financial institutions' support for borrowers and risk management**," the FSA formulated and published the guidance for climate

change measures for financial institutions on July 12. It will become further more important for financial institutions to deepen their efforts for risk management and have talks with customer companies.

- Securities companies, which have contact both with issuers and investors through the underwriting and sale of securities, are expected to check to what extent individual companies and investment products contribute to solving environmental and social problems, including decarbonization, and provide information appropriately to customers and market players. Such conduct is significant also from the perspective of ensuring the sound fulfilment of market functions.
- We understand that you are promoting various initiatives that include:
 - To hold briefing sessions concerning a roadmap for each industry for achieving carbon neutrality by 2050 four times in and after this April, targeting securities companies, institutional investors, issuers, etc.
 - To add matters concerning sustainable finance to the scope of the qualification examination for sales representatives from July 2022
 - To provide information on bonds to the JPX's Information Platform, which will be launched this month

Please continue efforts to foster specialists and expand the market.