

# Overview of Guideline for Supervision of Financial Instruments Firms, etc. for Program Year 2007

## [Understanding of Current Situation]

There is a great need to accelerate the flow of funds from savings to investments, and stimulate the Japanese financial and capital markets and enhance their international competitiveness. Also, the importance of financial institutions' self-help efforts is greater than ever before.

### Making "Qualitative Improvements in Financial Regulation"

## [Qualitative Improvements in Financial Regulation (Better Regulation)]

- (1) Optimal combination of rules-based and principles-based supervision approaches
- (2) Responding to high-priority issues through the effective use of regulatory resources
- (3) Placing greater emphasis on incentives for financial instruments firms, etc.
- (4) Enhancing the transparency of regulatory actions

## [Key Areas]

### Supervision of Financial Instruments Firms

#### 1. Ensuring Appropriate Business Operation System and Staffing

- Smooth and strict performance of registration tasks
  - Check staffing
  - Check whether the dealer is a member of a self-regulatory organization
- Development of systems, etc.
  - Consistently ensure an appropriate business operation system and staffing under principle of self-responsibility

#### 2. Development of Advanced and Robust Compliance System and Risk Management System

- Compliance system
- Risk management system
- Internal audit department verification

#### 3. Customer Protection

- Ensure proper solicitation and explanation
  - Proper screening of specific investors and general investors, suitability rule
  - Advertising regulations
- Development of systems, etc.
  - System for screening specific investors and general investors and ex-post-facto verification system
  - Customer management system to observe suitability rule, advertisement screening system, complaints processing system
  - Verify the development of systems while respecting voluntary efforts

#### 4. Customer Information Management

- Existence of leakage, loss or impairment of information and improper sharing of information
- Customer information management system, etc.

#### 5. Governance of Financial Conglomerates

### Supervision by Business Type

#### 1. The First Financial Instruments Business

- Ensuring appropriateness of operations
  - Advertising regulations, prohibition of unsolicited calls
  - Accurate calculation of capital adequacy ratio
- Development of systems, etc.
  - Proper demonstration of market intermediation functions of securities companies, etc.
  - Prevention of conflict of interest when conducting investment banking or principal investment business

#### 2. The Second Financial Instruments Business

- Verification of explanation status of collective investment schemes (funds)

#### 3. Investment Management Business

- Business execution system
- Advertising regulations
- Due diligence system, system of preventing conflict of interest for real estate fund investment businesses
  - \* Measure to demonstrate appropriate pricing function. Not intended to affect individual real estate prices, etc.

#### 4. Investment Advisory and Agency Businesses

- Advertising regulations, etc.

### Supervision of Registered Financial Institutions

#### 1. Prevention of Abuse of Dominant Position

- Prevention of abuse of dominant position
- Development of system for registered financial institutions, etc.

#### 2. Matters requiring Attention in Sales of Investment Trusts, etc

- Prevention of investment trusts from being misconstrued as deposits, etc.
- Dealing with customers in a sincere and fair manner in the event of any mishaps

#### 3. Information Management System

- Information management between department handling credit derivatives transactions and loans department, system to prevent conflict of interest.

### Matters requiring Attention for Funds

While funds are expected to help internationalize Japanese financial and capital markets, they are also deemed to be exposed to specific potential risks. Therefore, it is necessary to endeavor to identify their actual state according to various investment structures in consideration of discussions at summits, etc., promptly determine the whereabouts of risks and allocate supervisory resources. Encourage dialogues, identify the actual state of funds and conduct an investigation and analysis through monitoring surveys pursuant to the supervision guidelines.

### Response to Unregistered/Unlicensed Entities

Warn such entities in writing, etc. and encourage them to apply for registration or file a notice. If they operate intentionally, etc., contact the law enforcement authorities, etc. of the countries in question so as to prevent the damage from occurring/spreading.

## [Supervision Method]

### 1. Ensuring Proper Cooperation with Inspection and Oversight Departments/Bureaus

#### 2. Cooperation with Self-regulatory Organizations, etc.

- Follow-up and cooperation for *Summary of Issues produced by the Round Table Conference on the Financial Market Intermediation Function of Securities Companies*
- Follow-up on actions in consideration of *Interim Summary of Issues on the Status of Financial Instruments Firms Association*
- Cooperation to eliminate organized crime groups, etc. through the **Securities Safeguard Liaison Council**, proper accreditation of accredited investment protection organizations

### 3. Relationship with Financial Instruments Firms, etc.

- Improve the transparency and predictability of FSA's responses by encouraging active dialogue
- As it is possible to issue orders such as to modify business methods in cases where it is deemed necessary and appropriate in the interest of the public or for the purpose of protecting investors, even if laws and regulations, etc. have not necessarily been violated, it is necessary to maintain appropriate internal control in consideration of the fundamental approach underpinning the laws and regulations and the principle and objective of the regulations. Accordingly, ensure that sufficient exchange opinions with management takes place.

### 4. Enhancement of Cooperation with Foreign Supervisory Authorities, etc.