

(Provisional translation)

Summary of Issues for the Improved Operations of
EDINET

February 2008

Working Group for the Improved Operations of EDINET

1. Basic concept

EDINET (Electronic Disclosure for Investors' Network) started its operations in June 2001. It is an online system wherein a series of procedures pertaining to the submission, receipt, and public viewing of annual security reports and other disclosure documents are carried out online¹. Prior to the introduction of EDINET, these procedures had been implemented on paper.

EDINET serves as a platform for information disclosure, enabling the prompt disclosure of critical information for investors and issuers, etc., and helping the general public to instantly access information furnished via the Internet by the submitters, who are responsible for the content of the information. One can say that EDINET is an essential part of the infrastructure of Japan's financial and capital markets.

Recently, however, false statements with respect to the contents of large shareholding reports were posted on EDINET. This constitutes an extremely serious issue in the context of the large shareholding reporting system that is intended to enhance the fairness and transparency of markets through prompt disclosure of information on large shareholdings of listed companies.

Considering the incident as a lesson, we have examined what needs to be done to prevent the recurrence of such incidents and to develop a contingency management plan, mainly from practical perspectives.

The purpose of the large shareholding report system is to improve market fairness and transparency and to protect investors by promptly providing investors and issuers with information on large shareholdings of listed companies, which is crucial for their investment decisions in terms of the influence it can have on company management and of market supply and demand.

The significant feature of the system is its swiftness. Since the demand for swiftness is on the increase², introduction of a screening by the authorities prior to posting on EDINET that can reduce swiftness should be discouraged.

Based on this idea, it is necessary to give sufficient consideration so as not to reduce the

¹ The disclosure of documents such as the annual security report, security registration statement, and tender offer registration form on EDINET has been required since June 2004 and that of the large shareholding report, since April 2007.

² Regarding the large shareholding reporting system, there has been an increase in the incidence of cases of holding a large volume of the stocks of listed companies within a short period. Owing to an increasing demand for swiftness in relation to anti-takeover defense, etc., efforts were made to shorten the reporting period and frequency of the special reporting system in December 2006.

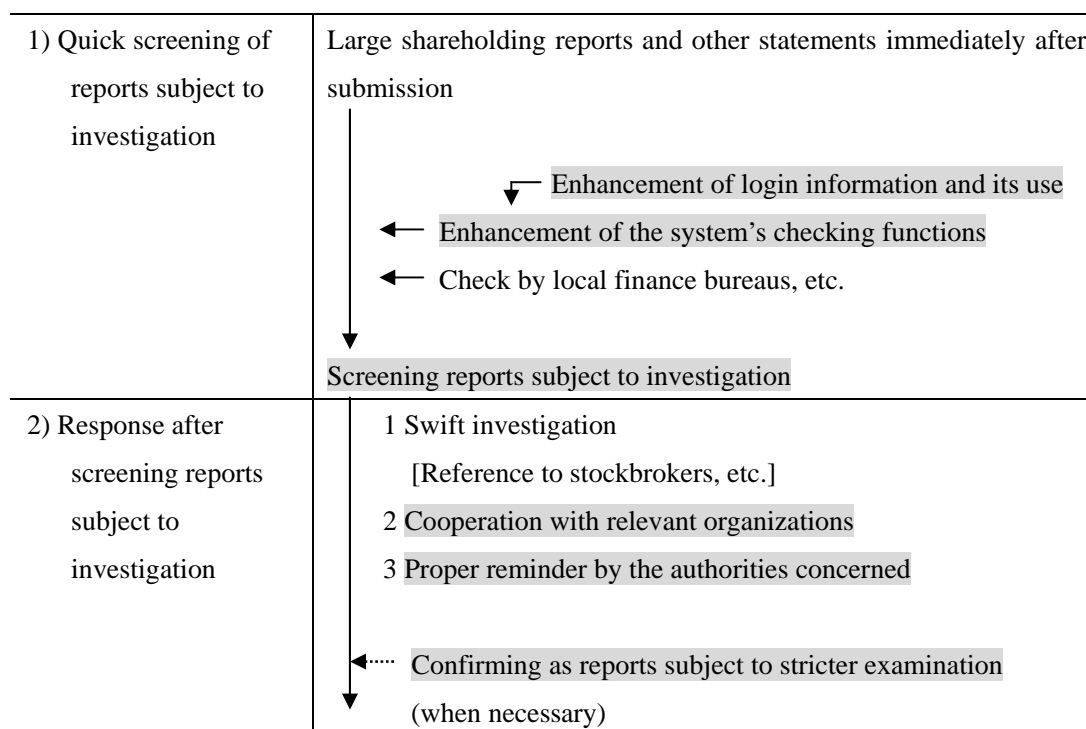
convenience associated with the current framework; further, it is also important to avoid the imposition of excessive costs on investors when measures to prevent the recurrence of such cases and to develop a contingency management plan are considered.

2. Consideration of measures to prevent recurrence and to develop a contingency management plan

Based on the basic concept described earlier, we need to examine our course of action with regard to large shareholding reports and other statements that are submitted. In formulating measures to prevent the recurrence of such cases and in developing a contingency management plan, consideration should be given from the following standpoints:

- 1) How can the authorities promptly and efficiently locate the reports suspected of containing false statements?
- 2) How can the authorities quickly investigate into such reports, and then issue reminders externally?
- 3) What are the effective administrative measures to be taken after the investigation of the reports that have been identified as containing false statements?

We examined the measures that were mainly related to the operations and the system, and believe that it is appropriate to adopt measures for improvement in phases 1–3, as follows.



3) Swift administrative response	Implementation of effective administrative measures
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(Note) The following classification is used for large shareholding reports in accordance with the stages of investigation and check outlined in this report.

- ❑ Reports subject to investigation These are identified for investigation by virtue of being suspected of containing false statements after the check by the local finance bureaus, etc., including with the IT system support.
- ❑ Reports subject to stricter examination These have a high probability of containing false statements; the local finance bureau, etc. concerned cannot conclude that the information contained in the reports is accurate even after the investigation on their own. Therefore, such reports require stricter examination.

1) Quick screening of reports subject to investigation

【 enhancement in the checking functions with the IT system 】

In order to examine at local financial bureaus, etc. as many as 20,000 large shareholding reports per year in a quick and efficient manner, it is necessary to quickly find the reports that need to be investigated, in accordance with the types of submitters and features of the contents.

We believe that it is necessary to enhance the checking functions with the IT system so as to automatically classify submitted reports and prioritize them in order to check whether or not they should be investigated. This will ensure that a smooth and swift system is in place.

Since the current system does not have such a feature, the introduction of a new system such as the one given below should be considered.

《 Examples of specific measures 》

◆ Transition to a method that enables selection through the IT system

Transition from the current text-based method to a method that uses logical checking to enable selection of reports to be examined through the IT system (e.g., fill-in-form method)

《Expected effects of improvement of the method》

The improvement of the method will enable the following:

- An effective combination of analytical indicators such as the types of submitters, holding ratios of concerned share certificates, frequency of submissions, and features mentioned in the submitted reports will enable the selection of reports that should be given priority in examination.
- It is important to flexibly decide on the analytical indicators to be used in accordance with operational demands and changes in the trend of submitted reports. It is necessary to design an IT system that provides such flexibilities.
- In addition to the introduction of the new method, the format checking function to check whether or not there is any missing information may be enhanced to enable automatic finding of, for example, serious inconsistency among the information provided in the reports.
- How to handle frequent submitters of large shareholding reports should be examined.

◆ Quick notification of results of selection with IT system

For the effective use of the results of the IT system check in the examination of the

local finance bureaus, etc., an examination system should be enhanced, for instance, by introducing a function to promptly notify the local finance bureaus' staff in charge of the result (e.g., by pop-up notifications).

※ In order to enhance the checking functions through the IT system, the following measures regarding the login information (ID and password)—which submitters obtain when they submit registration forms³ and attached documents⁴ in advance of the use of EDINET—can contribute to a better understanding of the information on submitters.

< Examples of specific measures >

A. Improvement and enhancement in understanding the information on submitters

- ◆ The corporation's certified copy of the commercial register and other documents may be added to the articles of incorporation in the case of the corporations; this is to confirm the existence of the said corporations.
- ◆ Substantive information such as the submitters' purpose of obtaining the login information may be added to the current information in order to check the submitters' existence (this information can be required in the registration form).

B. Introduction of a measure for the periodic reconfirmation of login information

- ◆ Introduce a measure for periodic reconfirmation (e.g., once every three years) of login information. The Financial Services Agency should consider the possibility of a flexible treatment of banks and stockbrokers who are subject to the supervision of the Financial Service Agency or the local finance bureaus, etc., in accordance with laws and regulations.

※ The possibility of introducing an Extensible Business Reporting Language (xBRL) for large shareholding reports in the future also needs to be examined.

The introduction of such new measures is considered to be effective because it will reduce the workload at the local finance bureaus, etc. that is required to deal with errors in the forms, and ensures efficient allocation of human resources for more substantive examinations.

【 Provision of information by target issuers 】

³ The items on the registration form are limited to the submitter's name, title and name of the representative, location or address of the head office, and contact details (phone number and email address, etc.).

⁴ Attached documents are articles of incorporation or equivalent documents for corporations and a copy of the residence certificate or equivalent documents for individuals.

As soon as large shareholding reports are posted on EDINET, the concerned issuers (listed companies) (hereinafter referred to as “target issuers”) will receive notifications about relevant information via e-mail (automatic notification) from EDINET; this is effective from March 2008⁵.

This will enable the following:

1. The target issuers that receive an e-mail will be able to check the contents of the relevant large shareholding reports on EDINET.
2. The target issuers will be able to provide information to the local finance bureaus, etc., via e-mail or other means when they come across unusual information.
3. The local finance bureaus, etc., will be able to confirm and find reports subject to investigation, in response to the information provided by target issuers.

It will be necessary to raise the awareness of target issuers and establish a communication network between the local finance bureaus, etc., and the target issuers in order to secure the effectiveness of the abovementioned efforts.

2) Response after finding the reports subject to investigation

【 improvement in investigation system, establishment of network for cooperation with relevant organizations, and creation of new reminder system 】

It is necessary for the local finance bureaus, etc., to promptly investigate the facts associated with the information in the reports in collaboration with the relevant organizations; inform these organizations; and issue reminders to investors and target issuers upon the finding of reports subject to investigation.

It will be also necessary for the Financial Service Agency and the local finance bureaus, etc., to adopt necessary measures for the correction of large shareholding reports upon the confirmation of false statements as a result of the examination. They will also need to take appropriate measures in relation to disclosed information on EDINET in order to prevent misunderstanding among investors and issuers.

2)-1. Swift investigation

⁵ EDINET notifications (automatic notifications) are aimed at strengthening its functionality. Note that this does not eliminate the requirement for submitters to send a copy of large shareholding reports to target issuers (Paragraph 27 of Article 27 of the Financial Instruments and Exchange Act).

Upon the detection of the reports subject to investigation, the local finance bureau, etc. concerned will promptly check the facts through, *inter alia*, referring to relevant organizations. One of the most effective means at an early stage of investigation is to refer the submitters' shareholdings to the concerned stockbrokers, trust banks, etc.

From this perspective, it is necessary to introduce a framework that facilitates early recognition of the concerned stockbrokers at the local finance bureaus, etc. It is also required to strengthen cooperation with the Japan Securities Depository Center, Inc. (JASDEC) after the introduction of new book-entry transfer system of stock certificates, i.e., the dematerialization of stock certificates (planned for January 2009).

《 Examples of specific measures 》

- ◆ The names of the stockbrokers and/or trust banks concerned may be included as a required item in large shareholding reports or attached to them. (These names shall not be made public.) When the submitters are banks and financial instruments dealers under the supervision of the Financial Service Agency and/or the local finance bureaus, etc., in accordance with laws and regulations, flexible treatment is permissible on the grounds that they can immediately respond to enquiries from the local finance bureaus, etc.
- ◆ After the dematerialization of stock certificates, the JASDEC will, in principle, hold data related to the names of account management institutions for particular shareholders with regard to all share certificates. This will increase the avenues of the local finance bureaus, etc. conducting the investigation to recognize the names of the account management institutions and to check shareholding of the submitters. In particular, the following occurs:
 1. The local finance bureaus, etc., can refer to the JASDEC the account management institutions for the submitters of large shareholding reports and then request the account management institutions concerned for information about the submitters' shareholdings.
 2. The local finance bureaus, etc., can refer the submitters' shareholdings to the target issuers. (A system exists wherein the referred target issuers can receive information from the account management institutions through the JASDEC.)

In addition, it is possible to consider the introduction of a system wherein the local finance bureaus, etc., directly refer the submitters' shareholdings to the JASDEC.

However, it should be noted that the scope of securities handled by the JASDEC differs from that of the share certificates under the large shareholding reporting system. Furthermore, differences exist between the information provided under the large shareholding reporting system, which focuses on the actual shareholding, and the information of the JASDEC, which contains the record of the whereabouts of physical rights.

2)-2. Establishment of a network for cooperation with relevant organizations

When the local finance bureaus, etc., find suspicious large shareholding reports, it is important to properly communicate and cooperate with stock exchanges, the Japan Securities Dealers Association and, if necessary, overseas authorities and foreign stock exchanges, by promptly providing them with information in the course of the stages of investigation and confirmation.

Such communication and cooperation is necessary at each of the following junctures:

- a. When reports are found subject to investigation;
- b. When the existence of a false statement is confirmed and necessary measures are taken (issuance of an order to submit correction reports); and
- c. When necessary corrections are made (at the time of the submission of correction reports)

Thus far, since there had been no actual cases requiring swift action, communication, and cooperation, a network has not yet been established with these relevant organizations. The creation of such a network should be initiated in order to handle the abovementioned scenarios promptly and systematically and to raise the awareness of the relevant organizations.

《 An example of specific measures 》

⇒ Attachment 【 System of receipt and examination of large shareholding reports and network of cooperation with relevant organizations 】

In particular, close information exchanges and cooperation with stock exchanges are considered necessary; this is because the stock exchanges may adopt measures to suspend their dealings whenever necessary, after they receive information from the local finance bureaus, etc. that have found reports subject to investigation.

2)-3. Creation of a new reminder system by the authorities

When the Financial Service Agency and/or the local finance bureaus, etc., find large shareholding reports of a suspicious nature, they need to promptly issue reminders to the securities market in order to prevent any misunderstanding and confusion among investors and target issuers.

There is currently no specific reminder system in place because the recent incident represented the first case. In order to provide information to investors at the earliest, it will be necessary to create a reminder system when the local finance bureaus, etc., find the reports subject to investigation and when they begin checking the facts with the stockbrokers.

《 Examples of specific measures 》

When issuing a reminder

- ◆ Reminder by the authorities can be provided in each of the following stages:
 - a. When reports are found, subject to investigation; and
 - c. When an order to submit a correction report is issued

When a certain amount of time is necessary to confirm false statements, reminders can be provided in the event of a high probability of false statements (b. when the report is subjected to a stricter examination). This should occur in cases wherein no conclusion can be drawn about the veracity of the information after the investigation has been underway.

How to issue a reminder

- ◆ A possible way to issue a reminder is to post the names of the relevant large shareholding reports and their submitters on the front page of EDINET. Herein, it should be clarified as to which stage—a, b, or c—applies to a particular case. When issuing reminders in stage a or b, i.e., before the confirmation of false statements, it is necessary to adopt a cautious approach in order to prevent misunderstanding among investors and target issuers by notifying them, in advance, that the existence of false information is yet to be confirmed.
- ◆ Reminders may be attached to other disclosed documents provided by the submitters of large shareholding reports that come under the purview of the reminders (at the names of submitters on EDINET) to remind investors and target issuers.

III. Swift administrative action

Withholding of submitted reports from public viewing

Under the current Financial Instruments and Exchange Act, even when there are false statements in disclosed documents, including large shareholding reports, the documents are not removed from the list for public viewing. Making the disclosure documents with false statements available to the public along with the correction reports that clarify where the correction is made will serve as reminders for investors who might have made investment judgments after viewing the documents.

However, when an order to submit correction reports is issued, even after the authorities concerned issue reminders (see 2)-3.), the provision of disclosure documents with false statements subject to correction for public viewing can be problematic in light of public interest and the protection of investors.

Given such circumstances, it is desirable to examine the various possibilities, including rule changes, in order to enable the following measures. This will contribute to the public interest and protection of investors in order to avoid misunderstanding and confusion among the investors and target issuers with regard to the documents with false statements.

1. Attaching important reference information to the disclosed documents on EDINET, for instance, that an order to submit corrected reports has been issued.
2. Allowing the authorities concerned to withhold the submitted reports from public viewing, in whole or in part, as an exceptional measure, when an order to submit correction reports is issued⁶.

Imposing administrative monetary penalties

Under the current system, an order of submission of correction reports⁷ is designed as an administrative measure against disclosed documents with false statements. False statements and an infringement of the order of submission are subject to criminal penalty.

⁶ The concerned measure is adopted only in a limited array of cases, i.e., in cases wherein a submitter does not follow the order for correction. When this measure is taken, there should be an indication that the document is not provided for public viewing.

⁷ The Prime Minister can order the submission of correction reports when (1) it is considered that there is insufficient information in the form in the document or the document does not contain enough information on material matters or (2) it is discovered that there are false statements on material matters, or that information on material matters or information that prevents misunderstanding is missing (Paragraph 29 of Article 27 of the Financial Instruments and Exchange Act.)

The Financial Service Agency and the local finance bureaus, etc., are expected to continuously take strict action against infringements, i.e., false statements, under the current framework.

The report issued by the Legal System Working Group of the First Subcommittee of the Sectional Committee on Financial System of the Financial System Council (December 18, 2007) states that false statements in the tender offer registration forms and large shareholding reports and non-submission of those forms/reports should be subject to administrative monetary penalties. It is desirable that work to increase the variety of such deterrent measures will continue steadily so as to adequately prevent the violations witnessed in the recent incident.

System of receipt and examination of large shareholding reports and the cooperation with the relevant organizations

