

## **Basic Policy for Financial Inspections in Program Year 2010**

### **I. Foreword**

The Financial Services Agency (FSA) is not only making efforts to ensure the stability of the financial system, the facilitation of financing and the protection of users, but is also engaging in vigorous activities to strengthen the competitiveness of the Japanese financial and capital markets, and the financial system that supports economic growth, while working hard to establish reliable and transparent financial regulations.

In its financial inspections, the FSA is examining necessary items based on the Japanese financial and economic situation. In the previous program year, the FSA focused on the examination of how the financial institutions exercise the financial intermediary function as well as develop robust risk management systems in response to the financial market turmoil stemming from the sub-prime problem.

Although the Japanese economy has been steadily recovering, it is still in a severe situation. There are risk factors, such as a possible downturn of the world economy, changes in the financial and capital markets, and the influence of deflation. Under such circumstances, although it is necessary to keep in mind that risk faced by financial institutions may grow, they are expected to function as a backup supporter of the real economy and firms.

In view of such situations, the basic objectives of financial inspections in the current program year should be (i) to examine whether financial institutions have developed procedures and arrangements to play a role in smooth and appropriate financing to borrowers and to provide good-quality financial products and services to users, and also (ii) to examine whether financial institutions have developed a sufficient financial base to play such a role and a robust and comprehensive risk management system.

It should be noted that this basic policy for financial inspection was drawn up in light of the circumstances that surrounded financial institutions as of August 2010, and may be subject to review as necessary.

### **II. Basic Policy for the Conduct of Inspections**

#### **1. Promoting the Implementation of the Five Principles Prescribed in the Preamble of the Inspection Manual**

When conducting inspection activities, it is necessary for the FSA to anticipate problems while enhancing its sensitivity to risk, and share the recognition of the problems with financial

institutions through in-depth dialogue so that they can make voluntary management improvement. Therefore, the FSA places the Better Regulation initiative as a guideline on financial administration and will continue to proceed with its implementation.

To be specific, the FSA will conduct more in-depth inspections through dialogue with financial institutions, based on the following five principles mentioned in the preamble of the Inspection Manual, namely, (i) Inspection focusing on important risks, (ii) In-depth analysis and clarification of causes of problems necessary for fundamental improvement, (iii) Identification of problems, evaluation of appropriate improvement efforts, and examination of static and dynamic aspects, (iv) Explanation of the basis for ratings and pointing out problems, and clarification of items to be considered for improvement, and (v) Accurate understanding of examination findings (“Sense of Satisfaction”).

## 2. Activities to Develop the Better Regulation Initiative

### (1) Implementation of the comprehensive action plan (Action Plan II)

The FSA will implement a comprehensive action plan (Action Plan II; (i) implementing and strengthening the Better Regulation initiative, (ii) enhancing dialogue with financial institutions and strengthening the dissemination of information, (iii) improving the inspection capability, and (iv) enhancing human resource development and increasing the staff, see the attachment) adopted to conduct inspections that contribute more to voluntary improvement efforts by financial institutions in a consistent and systematic manner.

### (2) Enhancement of the coordination with related institutions

From the viewpoint of improving the effectiveness and efficiency of financial inspections, the FSA will further enhance its coordination with the Bank of Japan and overseas authorities, including the sharing of information and awareness of issues about financial institutions/systems.

### (3) Enhancement of the coordination with auditors

In view of the increasing importance of external audits as the function that supports the effectiveness of the internal control systems of financial institutions, including the introduction of internal control audit systems, etc., the FSA will further strengthen the coordination with auditors who conduct accounting audits and internal control audits of financial institutions.

### (4) Reduction of the workload on financial institutions

Regarding the workload on financial institutions, required investigations were done in the previous program year while considering the situation of implementation of financial inspections and opinions from industry groups, and a policy was created for reducing the

materials to be submitted in advance. In the current program year, the FSA is working on the solid execution of that policy, to reduce the workload imposed on financial institutions by financial inspections.

### III. Basic Framework for Inspections

In the current program year, the FSA will seek the following basic frameworks for inspections so as to further improve the effectiveness of financial inspections and reduce the workload imposed by inspections of financial institutions.

#### 1. Enhancement of the integration of on-site and off-site monitoring

In order to effectively and efficiently perform financial inspections that are fully focused on the risk characteristics of financial institutions, the FSA needs to further enhance the integration of on-site and off-site monitoring. To do this, the FSA will promote more focused financial inspections, while working to reduce the workload on financial institutions, by integrating the Inspection Bureau's on-site data collection and analysis function with the Supervisory Bureau's off-site monitoring data collection and analysis function at the beginning of this current program year, and enhancing seamless on-site and off-site monitoring.

The Inspection Bureau will analyze the information obtained from the financial inspection of each individual financial institution in order to identify and grasp common risks inherent in all business categories and risks underlying the entire financial system, while sharing the analysis results with the Supervisory Bureau. Furthermore, the information conducive to the planning and drafting of financial regulations, which is obtained from the analysis results, will be shared with the Planning and Coordination Bureau as necessary.

#### 2. Inspections of Financial Institutions, etc.

##### (1) Major banks

When conducting financial inspections, chief inspectors in charge on a multi-year basis (a Japanese equivalent to the "Examiner-in-Charge"; hereinafter referred to as "EiC") conduct in-depth analyses in advance, together with the assistants to the EiC to specify the risk of the banks.

The FSA will inspect major banks basically through targeted inspections that narrow down the areas examined, and conduct theme-specific horizontal inspections as necessary.

##### (2) Regional financial institutions

The FSA will deepen the pre-inspection analysis by Local Finance Bureaus and conduct more focused financial inspections based on the size and characteristics of businesses, actively executing targeted inspections and simple inspections, in order to enhance the

effectiveness and efficiency of financial inspections as well as to reduce the workload of regional financial institutions.

(3) Foreign banks

The FSA will conduct more focused financial inspections based on the size and characteristics of businesses, actively executing targeted inspections and simple inspections, in order to reduce the workload on foreign banks as well as to enhance the effectiveness and efficiency of financial inspections.

The Inspection Bureau will conduct off-site hearings in cooperation with the Supervisory Bureau in order to grasp the actual circumstances of foreign banks.

(4) Insurance companies

The FSA will soon make a complete revision of the Inspection Manual for Insurance Companies.

The Inspection Bureau will conduct off-site hearings in cooperation with the Supervisory Bureau in order to gain a clearer picture of the actual state of insurance companies.

(5) Financial companies, etc.

The FSA will conduct financial inspections in response to the full enforcement of the revised Money Lending Business Act and the enforcement of the Payment Services Act. As for the money lenders registered by Local Finance Bureaus, the FSA will examine the status of various systems required by the full enforcement of the revised Money Lending Business Act referring to the contents of the Comprehensive Guidelines for Supervision of Money Lenders. Regarding financial inspections of financial companies, etc., the FSA strengthens the Inspection Bureau's function of instructions to the Local Finance Bureaus which conduct financial inspections of them.

(6) Inspections of large financial groups

(i) Inspections of financial conglomerates

The FSA will inspect the governance and risk management systems of financial institutions on a group basis, as well as their internal control systems with respect to the management of conflicts of interest and the handling of customer information in coordination with the Securities and Exchange Surveillance Commission as necessary.

(ii) Response to global business expansion

The FSA will conduct inspections of the Japanese financial groups (including insurance companies) that engage in international business activities and Japanese establishments of large foreign financial institutions (including insurance companies) with due attention to the

situation of international finance, while coordinating with foreign authorities. When the Securities and Exchange Surveillance Commission conducts inspections of securities companies that engage in international business activities (including securities companies that do not own banks in their group), the FSA will send experts from the Inspection Bureau as necessary.

The FSA will attempt to identify global risks at an early stage, including those of emerging countries, by dispatching staff at the Inspection Bureau and making strategic use of resident examiners abroad.

#### (7) Inspections of entrusted companies and agents

With the progress of outsourcing of financial institutions' business (especially that related to computer systems) and agency business (especially that related to insurance), in addition to inspecting the financial institutions' management of such companies, the FSA will also actively conduct financial inspections of outsourcing contractors and agents.

#### (8) Inspections of clearing organizations, etc.

The FSA will conduct inspections of clearing organizations, etc., which are granted a license, etc. pursuant to the stipulations in the Payment Services Act, which went into effect on April 1, 2010, focusing on their information technology risks concerning safety.

### IV. Priority Inspection Items

#### 1. Development of Governance System

The leadership and commitment of management based on proper business management is critically important, in order to exercise the financial intermediary function, thorough legal compliance and protection of customers, and accurate management of various risks. Therefore, when conducting financial inspections, the FSA will focus on examining the following points not only through dialogues with the management, but also through examinations of some branches as necessary.

- Whether the financial institution adequately analyzes and deliberates strategic objectives (earnings, costs, capital policy, etc.) based on its management policy in light of the medium-term business outlook and from the viewpoint of their rationality and sustainability.
- Whether the strategic objectives set for individual businesses based on the strategic objectives for the financial institution as a whole are consistent with risk management policies concerning various risks.
- Whether the strategic objectives and the management policy of various risks have solidly penetrated through the entire organization, including sales offices, and have been implemented.

- Whether the financial institution has developed a robust governance system regarding risk taking, risk management, legal compliance and the protection of customers in the whole group, including at foreign establishments, and whether the system is functioning properly.
- Whether the effectiveness of internal audits (whether the audits are based on a risk-focused, forward-looking approach and whether their coverage and depth are adequate) is ensured and whether the checking and monitoring function of the audits is used to improve management.

In addition, the FSA will examine whether directors and auditors etc. are holding substantive discussions at meetings of the board of directors, etc., and whether directors and auditors, etc. are performing the duties of executing and supervising business.

## 2. Further Promotion to Facilitate Financing

It is expected that financial institutions will, with due attention to ensuring their sound and appropriate business operations, promote the facilitation of financing, while providing proactive support toward improved management of debtors. In program years 2008 and 2009, the FSA focused on examining whether financial institutions have developed procedures and arrangements that enable them to smoothly and actively exercise the financial intermediary function based on appropriate risk management while taking into consideration the actual circumstances of SMEs and individuals. In the current program year, in addition to such consideration, the FSA will continue to focus on examining whether financial institutions have developed procedures and arrangements to be able to demonstrate a smooth and active financial intermediary function, while sufficiently fulfilling their consulting function.

(1) Ensuring that financial institutions perform the financial intermediary function for SMEs, individuals (housing loans), etc.

(i) Loans to SMEs

- The FSA will focus on examining whether financial institutions have developed procedures and arrangements for providing loans that ensures the smooth exercise of the financial intermediary function in line with the purposes of the Supplement to the Financial Inspection Manual (the borrowing company should be evaluated with due consideration of unquantifiable factors such as technological capability and the abilities of managers, rather than based merely on formal facts, such as incurring losses and being in a state of negative net worth) while making conscientious efforts to grasp the actual circumstances of the debtors.
- The FSA will focus on examining whether financial institutions have developed procedures and arrangements for taking required measures as stipulated in Article 6 of the Act for Financial Support for Small and Medium-sized Companies, in response to requests

- The FSA will focus on examining whether financial institutions have developed procedures and arrangements, such as appropriate screening, for proper response to requests from and consultations with customers for new loans (including funding after making changes in loan terms), and for proper customer explanations when rejecting requests.

(ii) Housing loans

- The FSA will focus on examining whether financial institutions have developed procedures and arrangements for taking required measures as stipulated in Article 6 of the Act for Financial Support for Small and Medium-sized Companies, in response to requests from debtors for changes in loan terms, etc.
- The FSA will also focus on examining whether financial institutions have developed procedures and arrangements, such as appropriate screening, for proper response to requests from or consultations with customers for new loans (including funding after making changes in loan terms), and for proper customer explanations when rejecting requests.
- In the case of housing loans insured by group guarantee companies (including the cases in which the guarantee company, etc. obtained housing loans through subrogation), the FSA will focus on examining whether financial institutions are giving guidance to, having dialogues with and making requests of such companies as efforts to properly deal with the facilitation of financing.

(2) Securing support regarding management consultation, management guidance and management improvement for SMEs

The FSA will examine whether financial institutions have developed procedures and arrangements for actively engaging in steady efforts on a daily basis, such as management consultations by visiting their customers, and for providing conscientious management consultations and guidance to SMEs, and supporting their creation of management improvement plans at each stage of their lifecycle (support of start ups and new business, support of management improvement, business rehabilitation, and succession of business). Especially, based on the size and characteristics of financial institutions, the FSA will focus on examining:

- Whether financial institutions have developed procedures and arrangements for providing adequate support to the SME debtors, whose business has deteriorated, including helping to create management improvement plans and coordinating with other financial institutions and business rehabilitation support organizations as necessary, upon assessing the feasibility of their business rehabilitation.
- During the implementation period of the management improvement plan, whether financial institutions have developed procedures and arrangements for reaching out to SMEs

- Furthermore, if superior initiatives and innovative ideas are recognized in management consultation, management guidance and management improvement, the FSA will evaluate them positively in financial inspections and clearly reflect the results in financial inspection ratings, etc. and will make them widely known by describing them in Collection of Reference Cases identified in inspections.

### 3. Development of Risk Management System

#### (1) Comprehensive risk management

As transactions made between financial institutions are becoming more and more advanced and complex due to the evolution of financial engineering, financial institutions need to develop a risk management system while taking into consideration the possibility that risks that do not fit any conventional risk category will arise and that risks will amplify and spread in a chain reaction as a result of stress events in the financial and capital markets. Financial institutions also need to recognize the limits of statistical risk measurement techniques and develop appropriate risk management systems commensurate with the size, characteristics and risk profile of their businesses by conducting stress tests based on forward-looking scenarios and using the test results in management judgment. Especially, regarding risk management concerning financial products which involve various risks, financial institutions need to take into consideration those risks in a comprehensive manner. In addition, it is also necessary to develop an appropriate management system with respect to the main risks (interest rate risk in bank accounts, etc.) that need to be considered in Basel II/the second pillar.

Accordingly, in the current program year, the FSA will focus on examining whether financial institutions have developed comprehensive risk management systems commensurate with the size, characteristics and risk profile of their business.

#### (2) Credit risk management

In light of the importance of credit risk management by financial institutions, the FSA will focus on examining whether financial institutions have developed a credit risk management system with due consideration of their management strategies as well as their size and characteristics, whether they adequately grasp the actual state and risk profiles of schemes related to large-lot credit exposure, complex forms of credit exposure and loans to overseas clients, etc., and properly conduct screening and manage credit exposure in a manner suited to their own circumstances.

In addition, the FSA will examine whether the credit management division of a financial institution is properly revising debtors' credit ratings based on the timely and appropriate analysis of the actual state of the debtors, and make efforts to exercise predictive control



regarding such debtors appropriately.

Furthermore, regarding banks that adopt the Internal Ratings-Based approach under Basel II, the FSA will examine whether they properly operate their internal ratings system and whether they properly verify parameter estimates.

### (3) Group-wide risk management

With the growing potential impact that large financial groups could have on the financial system, it is becoming difficult for such groups to identify group-wide risks because of the enormous size, the compartmentalization of their organizations and the globalization of financial trade.

On the other hand, even in the areas of overseas activities of Japanese companies and overseas projects, financial institutions are now expected to provide growth funds that are suitable for investment and lending as well as appropriate for the size and characteristics of the companies and projects. In order to respond to requests for such funds and to strengthen their earnings base, financial institutions, mainly major banks and insurance companies, are actively promoting overseas business. Establishing a robust risk management system for a whole group in order to support such activities is expected to contribute to the enhancement of the international competitiveness of the Japanese financial institutions.

Consequently, when conducting financial inspections of large financial groups, the FSA will focus on examining whether an inclusive risk management system has been developed on a group basis. In doing so, the FSA will pay special attention to whether they have developed a management system on a global basis for timely and properly: 1) funding liquidity (especially the liquidity of foreign currencies at major banks, and the liquidity of the Japanese yen at foreign banks and foreign securities companies); 2) collateral with respect to OTC derivative transactions, etc.; and 3) credit exposure.

### (4) Risk management system at insurance companies

The FSA will focus on examining whether insurance companies have developed asset management risk, insurance underwriting risk and policy reserves management systems in light of the significant changes occurring in the domestic and foreign economic and financial environments surrounding insurance companies. It will also examine whether insurance companies are making efforts to develop a comprehensive risk management system and whether they are conducting stress tests and using the test results in the management of their companies.

### (5) Information Technology risk management

Financial institutions' computer systems constitute the infrastructure of their business operations. In line with the increase in sophistication and complexity of the systems, the

potential impact of system failures on transactions with customers is increasing. Therefore, in the current program year, the FSA will focus on examining the following points:

- Whether the management is adequately committed to information technology risk management, rather than leaving it to experts.
- Whether the financial institution is giving consideration to strategically using IT systems as an important business infrastructure.
- Whether the financial institution has developed management systems required as a result of joint operation of a computer system or outsourcing of computer system operation, such as a system for managing the outsourcing contractor.
- Whether risks related to the upgrading of a computer system and the integration of computer systems are properly recognized at the management level and project management is properly conducted.
- Whether the financial institution has identified all risk events that could have a significant impact on or cause a significant problem for customers or settlement systems and has taken measures to deal with such events.
- Whether the financial institution has formulated an effective contingency plan in preparation for a possible computer system failure.

Regarding financial institutions that plan to upgrade or integrate their computer systems, the FSA will conduct inspections of system integration risk as necessary, in light of their progress, the current situation of the project management and the possible impact of system failures.

Furthermore, the FSA will actively conduct financial inspections of contractors entrusted with outsourced system management, while considering the workload on inspected institutions, such as joint centers of regional financial institutions in light of the progress made in the outsourcing of computer system management and in the joint operation of computer systems.

#### 4. Protection of Customers and Improvement of Users' Convenience

The protection of customers and the improvement of users' convenience by financial institutions contribute not only to the sound development of the national economy but also to the stability of the financial system by increasing the trust of the people in them. It is important that financial institutions enhance their competitiveness by providing financial products and services using innovative ideas based on the principle of ensuring a sense of security and trust through the implementation of measures to thoroughly protect customers. Therefore, in the current program year, the FSA will focus on examining financial institutions' following activities related to the protection of customers and the improvement of users' convenience.

In addition, it will cooperate, as necessary, with the Consumer Affairs Agency, which is expected to exercise central control over the conduct of consumer-related administration.

(1) Protection of customers

(i) Thorough management of information on customers, etc.

As customer information forms a base for financial transactions, and in light of personal information protection, it is necessary to strictly manage such information. It is also necessary to strengthen the management of corporate-related information in order to enhance reliance on market transparency and fairness. In view of these points, the FSA will focus on examining whether financial institutions have developed internal control systems for the management of information on customers, etc., including the prevention of employee and officer misconduct (such as leakage of internal information and insider trading).

(ii) Ensuring appropriate and safe financial transactions

Ensuring safe financial transactions is essential for the protection of customers. From this viewpoint, the FSA will focus on examining whether financial institutions have taken measures necessary for the prevention of financial damage that may be caused by illegal uses of deposit accounts, including “furikome” billing fraud, whether they have made preparations such as creating internal rules for proper handling of the procedures stipulated in the Furikome Billing Fraud Payments Act, whether they provide needed information and have taken other proper measures for people whom are suspected to have suffered damages, etc.

The FSA will also focus on whether they have made preparations for enhancing information security measures, including measures to protect information used for identity verification, in light of the high incidence of crimes using forged or stolen cash cards and crimes related to Internet banking in recent years.

In addition, the FSA will focus on whether financial institutions, as part of the anti-money laundering initiative, have developed procedures and arrangements for preventing transactions involving anti-social forces by gathering and analyzing information concerning such forces in close cooperation with relevant organizations.

(iii) Appropriate responses to consultation requests and complaints

In order to gain the trust of customers and reflect their needs in business operations, it is very important for financial institutions to proactively make timely and appropriate responses to consultation requests and complaints from customers. From this viewpoint, the FSA will focus on examining whether financial institutions are meeting customers’ consultation requests and dealing with their complaints properly. To be more specific, the FSA will examine whether financial institutions properly analyze the causes of such complaints, adopt measures to prevent their recurrence, raise institution-wide awareness about the measures and follow up on their implementation.

In addition, as for the financial ADR system, in light of the application of conduct regulations on each financial institution from October 1, 2010, the FSA will especially focus

on examining whether each financial institution has properly developed alternative measures in case of an absence of designated dispute resolution organizations.

(iv) Appropriate explanations to customers

Amid the increasing complexity and diversity of financial products and services, users expect and demand higher standards from financial institutions as well as from financial products and services. When financial institutions sell insurance products and risky products, they need to provide accurate explanations concerning the characteristics of the products and where risks reside while taking into consideration customers' actual needs. In the current program year, the FSA will continue to focus on examining substantially whether financial institutions act appropriately and flexibly in dealing with customers while sufficiently considering each customer's knowledge, experience and understanding of risk, etc., in accordance with the purpose of relevant laws and regulations. In addition, the FSA will pay adequate attention to whether financial institutions are not imposing an excessive workload on customers in terms of time and procedures.

In view of the recent trend toward greater business size and a broader scope of insurance products handled by insurance agents (life insurance sales agents and non-life insurance agents), the FSA will conduct financial inspections of the insurance agents, as necessary, in order to examine whether appropriate Sales Management Systems have been developed as well as examine whether insurance companies are properly managing their agents.

(2) Improvement of convenience for users

In light of the increasingly high standards that the people expect and demand from financial institutions, financial institutions need to make further efforts to improve convenience for users by developing new products and services if they are to obtain the support and trust of customers and maintain their business foundation. Therefore, in the current program year, the FSA will continue to positively evaluate excellent financial institutions' activities to improve convenience for users.

(End)

# Measures to Promote the Better Regulation Initiative in Inspections (Action Plan II)

## 1. Implementation and Enhancement of the Better Regulation Initiative

- (1) Inspections focusing on important matters ((1) and (2) of the five principles of the inspection manual)
  - (i) Holding dialogue between the chief inspector and the management at an early stage and enhancing such effective dialogue (continued measure)
  - (ii) Establishing inspection teams in charge of major banks and management inspections in line with the introduction of the Examiner-in-Charge (hereinafter referred to as the “EiC”) system (increasing the frequency of monitoring, strengthening cooperation between the inspection and supervisory departments, conducting comprehensive/partial inspections and theme-specific, sector-wide inspection and enhancing the staff supporting the EiC) (continued and strengthened measure)
  - (iii) Considering appointing EiCs at Local Finance Bureaus (strengthening the information-collecting function through the appointment of EiCs at Local Finance Bureaus, strengthening cooperation with supervisory departments and the FSA, and fostering core personnel) (continued and strengthened measure)
  - (iv) Promoting partial inspections of regional banks (continued measure)
  - (v) Promoting simplified inspections of credit associations serving customers engaging in particular occupations or those working in particular business sectors and foreign financial institutions whose Japanese operations are small, as well as making more efficient use of manpower (continued measure)
  - (vi) Improving and enhancing the use of interim reports (continued and strengthened measure)
- (2) Inspections that lead to voluntary management improvement efforts by financial institutions ((3) and (4) of the five principles of the inspection manual)
  - (i) Clarifying the notification of inspection results (indicating the degree of importance of a problem in terms of risk category and the direction of improvement) (continued and strengthened measure)
  - (ii) Considering how the Financial Inspection Rating System should be operated (clarifying the criteria for the “B” and “C” ratings, taking into consideration the dynamic aspect of financial institutions’ improvement efforts and adopting an evaluation yardstick that takes account of the size and characteristics of financial institutions) (new measure)
  - (iii) Providing information concerning excellent cases of activities (new measure)
- (3) Inspections that provide a high sense of satisfaction ((5) of the five principles of the inspection manual)
  - (i) Fully implementing on-site and off-site monitoring of inspection (including cross monitoring) (continued measure)
  - (ii) Enhancing the opinion submission system (increasing the number of outside expert members (to 10 members) and extending the deadline for submitting opinions (to within two weeks) (new measure)
- (4) Establishment of the headquarters for the promotion of the Better Regulation initiative and enhancement of external assessment
  - (i) Ensuring that the progress in the Better Regulation initiative is presented and debated at meetings of the Directors-General of Local Finance Bureaus and meetings of the directors of financial departments and inspection supervisors (continued measure)
  - (ii) Considering the establishment of a committee of external experts on the assessment of the implementation of the Better Regulation initiative (new measure)

## 2. Enhancement of Dialogue with Financial Institutions and Dissemination of Information

- (i) Enhancing collections of example cases of issues pointed out in inspections and example cases of issues related to financial ratings (establishing “Facilitation of Financing for Small and Medium-Size Enterprises” as an independent category, increasing the number of example cases and publishing collections of example cases twice a year) (continued and strengthened measure)
- (ii) Visiting regional banks and holding hearings with top managers (as part of the risk-focused, forward-looking approach to identify management tasks) (continued and strengthened measure)

- (iii) Strengthening networks between Local Finance Bureaus and financial industry organizations and holding meetings for exchanges of opinions (particularly with Shinkin banks and Credit cooperatives and at the working level) (continued and strengthened measure)
- (iv) Holding meetings for exchanges of opinions with associations of foreign financial institutions (considering holding such meetings periodically) (continued measure)
- (v) Holding meetings for exchanges of opinions with the Japanese Institute of Certified Public Accountants and the four major accounting firms (considering holding such meetings periodically) (continued measure)
- (vi) Holding briefings on the Supplement to the Financial Inspection Manual “Financing for Small and Medium-Size Enterprises” (continued measure)
- (vii) Disseminating inspection-related information through Chambers of Commerce and Industry, and strengthening efforts to collect information concerning inappropriate curbs on new loans and forcible withdrawals of outstanding loans (continued measure)

## 3. Enhancement of Inspection Capability: Central Point of Tasks in 2nd Stage

- (1) Enhancement of pre-inspection analysis
  - (i) Enhancing and strengthening pre-inspection analysis and increasing checkpoints of back-office operations (concerning major banks’ foreign establishments, insurance companies and foreign financial institutions) (continued and strengthened measure)
  - (ii) Reducing analysis materials conducted by FSA for Local Finance Bureaus in order to inspection of regional banks (continued and strengthened measure)
  - (iii) Considering holding periodic hearings with insurance companies and foreign financial institutions (in cooperation with the Supervisory Bureau) (new measure)
  - (iv) Strengthening the Office for Instruction on Inspection of Information Technology Risk (collecting information concerning computer system integration and drawing up multi-year inspection plans) (new measure)
- (2) Building a database of inspection know-how (accumulation, sharing and utilization of information and compilation of training materials) (considering new measures to be taken in relation to the start of the operation of a new computer system scheduled for 2012 and temporary measures to be in place until then) (new measure)
- (3) Establishment of new inspection ways and new inspection systems
  - (i) Enhancing an inspection technique concerning the smooth of financing to Small and Medium-Size Enterprises (new measure)
  - (ii) Enhancing an inspection technique concerning restructured loans (new measure)
  - (iii) Developing and enhancing a technique for analyzing information related to market risk management and comprehensive risk management by small financial institutions (continued and strengthened measure)
  - (iv) Considering having an expert inspection team conduct sector-wide inspections (considering and conducting theme-specific inspections covering financial institutions in a particular sector or of a particular type (mainly major banks) (new measure)
  - (v) Considering conducting principles-based inspections (new measure)
  - (vi) Considering revising the Inspection Manual for Insurance Companies and the Inspection Manual for Trust Banking Companies (new measure)
  - (vii) Considering how inspections should be conducted in light of financial regulatory reforms implemented abroad (new measure)
- (4) Enhancement and strengthening of instruction on inspections

- (i) Enhancing support for inspections and holding cross inspections (continued measure)
- (5) Strengthening cooperation with supervisory departments and relevant organizations
  - (i) Strengthening cooperation with the Supervisory Bureau (strengthening cooperation between the Inspection Bureau's Planning and Data Analysis Office and the Supervisory Bureau's Office for Supervisory Policy, Financial Market & Risk Analysis [joint implementation of risk assessment and joint collection and sharing of information concerning financial institutions subject to supervisory college]) (new measure)
  - (ii) Strengthening cooperation with the Securities and Exchange Surveillance Commission (SESC) (discussing with the SESC how to cooperate in inspections [inspections of financial conglomerates, major Japanese securities companies, etc.] and implementing such cooperation) (new measure)
  - (iii) Cooperation with the Bank of Japan (continued measure)
  - (iv) Strengthening cooperation with foreign authorities (enhancing channels of communication with foreign authorities, such as the FRB (Federal Reserve Board), the OCC (Office of the Comptroller of the Currency), the UKFSA (UK Financial Services Authority) and the HKMA (Hong Kong Monetary Authority) and implementing cooperation by dispatching inspectors to foreign establishments of Japanese financial institutions and resident examiner in abroad) (new measure)

#### 4. Enhancement of Personnel Training: Central Point of Tasks in 2nd Stage

- (1) Enhancement of practical training
  - (i) Collecting example cases of excellent inspections and communicating them through training (continued measures)
  - (ii) Expanding practical training based on example cases of issues pointed out in inspections (continued measure)
  - (iii) Enhancing training for personnel in departments related to the insurance business and foreign financial institutions (new measure)
  - (iv) Considering conducting joint training with the SESC (new measure)
  - (v) Having personnel receive external expert training (training related to computer systems and risk management) and lessons in general-interest matters (continued and strengthened measure)
  - (vi) Conducting joint training of personnel of the FSA and Local Finance Bureaus (continued and strengthened measure)
  - (vii) Increasing the number of trainees accepted from Local Finance Bureaus (for training related to computer systems and market risk) (continued measure)
  - (viii) Diversifying and advancing the contents of training materials, preparing training materials in-house, simplifying and integrating training materials (continued and strengthened measure)
- (2) Securing and fostering personnel
  - (i) Fostering inspectors in charge of loans (new measure)
  - (ii) Fostering and assigning personnel so as to strengthen inspections of insurance companies and foreign financial institutions (e.g. employing people with the experience of working for private insurance companies or engaging in financial business abroad) (new measure)
  - (iii) Extending the period of personnel assignment and the interval between rotations (e.g. considering career paths from a long-term perspective, extending the interval between rotations and actively employing experts) (continued and strengthened measure)
  - (iv) Securing personnel with expert knowledge and skills (e.g. experts in computer systems and market risk, actuaries, lawyers and accountants) (continued measure)
  - (v) Exchanging personnel with the SESC (new measure)
- (3) Appropriate evaluation of personnel and enhancement of motivation

- (i) Commending personnel for excellent inspections, making such inspections well-known, and reflecting the commendations in personnel performance evaluation (continued and strengthened measure)
- (ii) Reflecting the progress in the implementation of the Better Regulation in personnel performance evaluation and assignment (continued and strengthened measure)

## Basic Plan for Financial Inspections for PY2010

		Number of institutions to be inspected	The previous program year (PY 2009)	
			Number of institutions to be inspected	Actual number of inspected institutions
	Banks	105	100	85
	Shinkin banks Credit cooperatives	260	170	199
	Labor banks (Rokin) Federation of agricultural co-operatives associations and Federation of fishery co- operative associations	5	15	6
Total of deposit-taking financial institutions		370	285	290
Insurance companies		20	20	17
	Non-banking money lenders	90	100	101
	Issuer of prepaid payment instruments	145	165	183
	Others	20	25	30
Total of other financial institutions		255	290	314

Note:

(1) These inspection numbers may be changed as necessary.

(2) The figure on "Banks" is the aggregated number of banks and bank holding companies. That of "Insurance companies" is the aggregated number of insurance companies and insurance holding companies.