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Kaoru Yosano (Minister of State for Economic & Fiscal Policy and Financial Services) making an address at the 18th Round Table Conference on Money-lending Business on July 27

Yoshitaka Sakurada (Senior Vice Minister for Financial Services) meets with Mr. David Knott, Chief Executive of the Dubai Financial Services Authority (DFSA) on July 23

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【Topics】

Quality Control of Audits of the Four Largest Japanese Audit Firms

1. Introduction

The Certified Public Accountants and Auditing Oversight Board (CPAAOB) examines and as necessary, conducts inspections in response to reports from the Japanese Institute of Certified Public Accountants (hereinafter referred to as "JICPA") about fact-finding surveys on audit engagements (hereinafter referred to as "quality control review") pursuant to the Certified Public Accountant Law.

(Reference) "Quality control review" involves "reviewing the status of quality control of audits conducted by Certified Public Accountants (CPAs) or audit firms as entities in charge of conducting audits, notifying the results, recommending improvements as necessary, and receiving reports on the status of improvements based on such recommendations" (Article 87 (1) of JICPA Rules) in consideration of the public benefits of audit work. It has been implemented by JICPA as a self-imposed regulation since April 1999 with the aim of maintaining and ensuring the quality level of audit engagements performed by CPAs.

2. Measures including Prompt Inspection, etc. of Big Four Firms

Under these circumstances, with respect to the Big Four firms (KPMG AZSA & Co., Deloitte Touche Tohmatsu, Ernst & Young ShinNihon and ChuoAoyama Pricewaterhouse Coopers), CPAAOB published a document entitled "Measures to Conduct Prompt Inspections, etc. targeting the Big Four Firms" on October 25, 2005 in the interest of the public and for the purpose of investor protection, in consideration of the recent events involving financial audits and the trends in the supervision and oversight of international auditing firms. In view of the quality control of audits, CPAAOB steadily examinend and inspected the quality control reviews performed by JICPA.

3. Quality Control of Audits of the Four Largest Japanese Audit Firms

CPAAOB summarized the results of the inspections of the Big Four firms based on the inspection results, and published it under the title "Quality Control of Audits of the Four Largest Japanese Audits Firms" on June 30, 2006. To the extent of these inspections, the CPAAOB found that all of the Big Four firms were insufficient concerning quality control as a firm, specifically in the systematic management of audit engagements that ensures quality control of audits. In particular, deficiencies were identified in the overall management of audit engagements, independence, acceptance of new clients and client retention, performance of audit work, working papers, internal review of engagements, management of the quality control system, joint audits, and systematic audits, etc. Concerning the quality control of individual audit engagements, deficiencies were identified regarding compliance with generally accepted audit standards ("GAAS").

4. Recommendations based on Results of Inspection of Big Four Firms

As systematic management of audit engagements that ensures quality control of audits were found to be insufficient at the Big Four firms based on the inspection results, CPAAOB recommended the Commissioner of the Financial Services Agency that they be instructed to improve their operations.

5. Conclusion

CPAAOB will implement follow-up inspections to review the progress of improvements by the Big Four firms. CPAAOB will also inspect medium-sized audit firms as necessary after having examined the quality control review report of JICPA, while heeding their characteristics according to the size and other factors, in consideration of international trends and the recent events involving financial audits.

Furthermore, as more than a year has passed since recommendations were made to JICPA for improvements in quality control reviews in February 2005, CPAAOB will verify the status of improvements.

Basic Policy and Plan for Financial Inspections in Program Year 2006

The Financial Services Agency (FSA) recently (July 27) released to the public a document entitled "Basic Policy and Plan for Financial Inspections in Program Year[1] (PY) 2006," which reveals its inspection implementation policies for PY2006 and the scheduled number of inspections. An overview of the Basic Policy and Plan for Financial Inspections is as follows.

The FSA is aiming to realize an internationally reputable financial system with a high level of user satisfaction in accordance with the Program for Further Financial Reform. The FSA is striving to familiarize financial institutions with the Financial Inspection Rating System (FIRST), in addition to conducting inspections focusing on dialogues between financial institutions and inspectors by such means as implementing the Financial Inspection Basic Policy (FIBP).

In these circumstances, the FSA will endeavor to conduct inspections both properly and effectively in PY2006 based on the following basic policies, to ensure that financial institutions run their business operations in a sound and appropriate manner, while paying attention to changes in the environment currently surrounding them, such as the need to strictly enforce customer protection and the implementation of New Basel Capital Accord (the new capital adequacy framework).

1) Strict Enforcement of User Protection

In conjunction with the enactment of the Financial Instruments and Exchange Law, the FSA will examine financial institutions' efforts to protect customers with a focus on customer protection management systems, etc., in order to strictly enforce user protection in financial transactions. In inspections, the FSA will continue to actively use information received by the Counseling Office for Financial Services Users established in July 2005, as well as information received by the Inspection Information Desk.

2) Examination of Diversification of Risks and Sophistication of Risk Management

The FSA will conduct proper inspections with respect to the diversification of risks due to the widening range of asset management and operations of financial institutions and the sophistication of risk management by financial institutions.

3) Examination in View of Globalization of and Structural Changes in Financial Services

The FSA will properly respond to the globalization of and structural changes in financial services, increased outsourcing of operations and new market entrants.

4) Examination of Small Business Financing

In order to help revive small and medium-sized enterprise (SME) businesses and revitalize regional economies through the enhancement of financial functions, the FSA will promote inspections in tune with the actual business status, etc. of SMEs, including examining the SME business revitalization efforts of regional financial institutions (RFIs), in consideration of the extent to which financial institutions have identified the actual state of SMEs.

The FSA will continue to thoroughly examine RFIs in regards to their SME business revitalization efforts in consideration of The Supplement to the Financial Inspection Manual, etc.

Furthermore, under the Basic Plan for Financial Inspections in PY2006, the FSA is planning to inspect 300 deposit-taking financial institutions, 15 insurance companies, 10 securities companies, etc. and 385 other financial institutions including non-bank money lenders, as well as six other institutions consisting of governmental financial agencies and Japan Post.

[1] July 2006 - June 2007

Amendment of Comprehensive Guideline for Supervision of Trust Companies

1. Introduction

The Financial Services Agency (FSA) revised the Comprehensive Guideline for Supervision of Trust Companies, etc., (hereinafter referred to as "Supervisory Guideline") on July 19, 2006, to develop a screening system for trust acceptance for the purpose of protecting trustors and beneficiaries and for other such purposes. This article explains the background of and the outline of the revision of the Supervisory Guideline.

2. Background of Revision of Supervisory Guideline

As there has been a steady increase in new market entrants, including trust companies, trust banking agents and trust beneficial interests distributor, etc., since the enforcement of the amended Trust Business Law on December 30, 2004, the FSA revised the Supervisory Guideline on April 28, 2006 (enforcement date: May 1, 2006), in consideration of queries about the Supervisory Guideline and deregulation requests made by the industry. In regards to the screening of trust companies, etc., upon their market entry and the "development of a screening system for trust acceptance", which had to be clearly defined as the highlight of supervision after market entry, the latest revision of the Supervisory Guideline was performed based on the decision to reexamine the content to make it more appropriate as the highlight of supervision, in consideration of the approach of the new trust inspection manual to be formulated by the Inspection Bureau as well as the problems and cases identified in the course of inspecting some trust banks.

The Supervisory Guideline was revised and released to the public on July 19 based on the comments received from the general public between June 6 and July 6, and came into force on the same day.

3. Overview of Revision

(1) Highlights of Screening upon New Market Entry

1) Development of Screening System for Trust Acceptance

The FSA explicitly stated that for the purpose of protecting trustors and beneficiaries and for other such purposes, matters to be highlighted when screening asset management trust companies and financial institutions engaged in trust business upon their entry into the market are: whether or not they have developed internal regulations for a screening system for trust acceptance that enables the proper execution of trust operations under laws and regulations and trust agreements; and whether or not they have developed a framework to ensure proper screening of trust acceptance under such regulations. Examples of matters to be stated in such regulations were also provided.

2) Highlights of Supervision after Market Entry

1) Points to Consider in Evaluation of Operational Status

As points to consider when evaluating the operational status of trust companies, financial institutions engaged in trust business, etc. in cases where they are asked to report and improve their operational status, the FSA explicitly stated that it will examine: whether or not they have developed a system to properly execute trust operations, including providing an explanation of the terms and conditions of the agreement to trustors, conducting screening of trust acceptance before concluding an agreement, and managing and investing trust assets after the acceptance of trusteeship; and whether or not they have ensured a proper internal control system for such trust operations.

2) Points to Consider in Evaluation of Status of Fulfillment of Duty of Care

As points to consider when evaluating the extent to which trust companies, financial institutions engaged in trust business, etc. are fulfilling their duty of care of a good manager, the FSA explicitly stated their need to properly perform investigation, screening and management for the acceptance of trusteeship so as to sufficiently fulfill their duty of care as a trustee, and provided examples of points to consider when examining the status of such investigation, etc.

Inspection Manual for Trust and Banking Companies (Supplement to the Financial Inspection Manual for Trust Services Business)

On July 13, 2006, the Financial Services Agency (FSA) produced a manual to be used by inspectors upon inspecting the trust operations of financial institutions engaged in trust business (trust banks, city banks and regional banks running trust operations, etc.) entitled "Trust Inspection Manual (the Supplement to the Financial Inspection Manual: for Trust Operations)" and issued it in the form of an official notice from the Director-General of the Inspection Bureau.
This article provides an overview of the Trust Inspection Manual.

1. Overview of Trust Inspection Manual

(1) Purpose of Producing Trust Inspection Manual

The FSA has steadily developed the inspection framework by producing financial inspection manuals, etc., since 1999. As part of such efforts, the FSA has recently produced an inspection manual for trust operations of financial institutions engaged in trust business.
The role of trust operations of financial institutions engaged in trust business is becoming increasingly important, considering the advances in financial technologies and market trends, as exemplified by the increasing number of cases in which trusts are utilized as a vehicle of asset liquidation and securitization in recent years. The FSA believes it was the right time to produce the Trust Inspection Manual at this point.

(2) Background to Publication of Trust Inspection Manual

In April 2006, a study group including experts and professionals in the private sector was established within the Inspection Bureau of the FSA. The study group began looking into preparing the Trust Inspection Manual from a specialized and technical viewpoint, and held discussions from various angles.
A draft of the Trust Inspection Manual was put together based on its studies, and opinions were sought broadly from the general public. The draft was examined based on the opinions and comments received, and the final draft of the Trust Inspection Manual was compiled and issued in the form of an official notice from the Director-General of the Inspection Bureau.
The Trust Inspection Manual will be applied to inspections conducted in Program Year 2006 (July 2006) and thereafter.

(3) Application of Trust Inspection Manual

Banking operations and trust operations will be clearly distinguished from each other in inspections targeted at financial institutions engaged in trust business: inspections will based on the Trust Inspection Manual in relation to trust operations and problems unique to financial institutions engaged in trust business, and on Financial Inspection Manuals in relation to banking operations.
Moreover, as trust products handled by financial institutions engaged in trust business vary widely and are diverse in features, the Trust Inspection Manual explicitly states that when applying the Manual, inspectors should give due consideration to the features of trust products, in addition to the size and characteristics of the financial institution, so that it would not be implemented in a mechanical/monotonous manner.

2. Focus of Each Checklist

(1) Trust Operations Management Systems Checklist

The Trust Operations Management Systems Checklist consists of four check items relating to internal control systems for properly managing trust operations in general: *I. Management in General; II. Compliance with Laws and Regulations; III. Risk Management*; and *IV. Internal Audit*.

Check items in *I. Management in General* include: (1) whether or not management policies for trust operations have been clearly defined; (2) whether or not management policies for trust operations address the fulfillment of the duty of care of a good manager, duty of loyalty, duty of segregated custody, etc.; and (3) whether or not management policies for trust operations address the development of a system to prevent conflict of interest.
Check items in *II. Compliance with Laws and Regulations, III. Risk Management* and *IV. Internal Audit*

include whether or not staff with sufficient knowledge and experience of trust business are assigned.

(2) Management Systems for Trust Acceptance Checklist

When concluding a trust agreement, a financial institution engaged in trust business needs to accept trust with a proper explanation of the terms and conditions of the agreement, etc.

Accordingly, this checklist is designed to examine the development status of the management system for trust acceptance and the fulfillment status of its functions, and consists of such check items as: (1) whether or not the financial institution identifies the attributes of the trustor (knowledge, objectives, experience, asset position, etc.) and confirms that there are no problems in the individual solicitation activities in view of suitability; (2) whether or not the financial institution is fulfilling its duty to provide an explanation as a trustee such as providing an explanation of risks to trustors as obliged by laws and regulations and information on matters required for making an investment decision; and (3) whether or not the financial institution is performing any acts prohibited by laws and regulations in relation to the trust acceptance under a trust agreement, such as making false statements and making assertions in view of trustor protection.

(3) Screening Systems for Trust Acceptance Checklist

It is important that a financial institution engaged in trust business ensures a system to only accept trusts that enable the execution of operations concerning trust business under laws and regulations and trust agreements by properly screening the trustor's objectives, trust assets, etc., before concluding a trust agreement, in view of: (1) whether or not the duty of care of a good manager and other such duties as a trustee can be fulfilled; (2) whether or not the responsibilities as a legal owner can be fulfilled; and (3) whether or not it would result in taking part in illegal acts, etc., by the trustor.

Accordingly, it is necessary to conduct appropriate screening for trust acceptance by developing a system to properly screen new products, new schemes, etc., in advance and conduct screening for acceptance.

For this purpose, this checklist is designed to examine the development status of the screening system for trust acceptance and the fulfillment status of its functions, and consists of such check items as: (1) whether or not the terms and conditions or the scheme of the trust agreement are aimed at evasion of laws or prohibited by laws and regulations such as money laundering; (2) whether or not the financial institution confirms and examines in detail the terms and conditions of the trust agreement are not based on the trustor's inappropriate objectives (such as concealment of losses, avoidance of disclosure and tax avoidance); (3) whether or not the financial institution confirms and examines off-balance-sheet liquidation transactions are acceptable as off-balance sheet items in accounting terms; (4) whether or not the financial institution confirms and examines the appropriateness of the entrusted amount (amount of trust) so that it does not contribute to the trustor's fraudulent accounting procedures or undermine the beneficiary's interests as a result of overvaluation of trust assets by overestimating the proceeds from trust assets when accepting trust in a liquidation scheme; and (5) whether or not there is a system to confirm the existence of any violations of building-related laws and regulations in cases where the trust asset is real estate, and if there are violations, examine whether it is possible to fulfill the owner's responsibility as a trustee by such means as identifying the actual situation, etc., and restoring it to a legal state within a reasonable restoration period.

(4) Trust Asset Management Systems Checklist

Financial institutions engaged in trust business are required to manage trust assets by exercising care of a good manager, including the segregated custody of trust assets and the protection of trustors' rights without fail.

For this purpose, this checklist is designed to examine the development status of the trust asset management system and the fulfillment status of its functions, and consists of such check items as: (1) whether or not the financial institution engaged in trust business has a system for segregated custody of trust assets to clearly distinguish between the accepted trust assets and its own assets and other trust assets and properly determine the respective beneficiaries of the trust assets; (2) whether or not the financial institution properly performs cross-checks with covenants and delivery settlement in cases where trust assets are invested in securities according to the orders of the person who has the right to give investment orders such as the trustor; (3) whether or not the financial institution promptly collects accurate information on

allotment to shareholders, mergers, demergers and other corporation actions, etc., that give rise to changes in the value of shares and corporate bonds, and properly protects the rights so that the trust assets would not incur losses; (4) whether or not the financial institution observes the clauses of the trust agreement regarding the management of trust assets in the form of real estate such as land and buildings, and if a real estate with such problems as environmental risks are accepted, whether or not it takes such measures as monitoring aimed at identifying changes in the situation regarding the problems and solving the problems in light of owner responsibility and trustee responsibility.

(5) Trust Asset Investment Management Systems Checklist

A financial institution engaged in trust business needs to invest trust assets in consideration of the duty of care, duty of loyalty, etc.

Accordingly, this checklist is designed to examine the development status of the trust asset investment management system and the fulfillment status of its functions, and consists of such check items as: (1) whether or not there is a system to observe the trust agreement and operational guidelines, etc., which provide for asset allocation, diversified investment, etc., in order to fulfill the duty of care; (2) whether or not the financial institution has developed a system to execute trading under the best terms for the customer based on the disclosed indicative price and trade terms in cases where trust assets are invested in securities; (3) whether or not there is a system to explain the trust asset investment policies, etc., and report the investment results to the trustor appropriately; and (4) whether or not there is a system to prevent transactions which give rise to conflict of interest in view of the duty of loyalty to the beneficiary.

In particular, (4) is the most important item in trust asset investment management. Financial institutions engaged in trust business operate in a business environment where various activities are prone to give rise to conflict of interest as they invest both their own assets and trust assets. Therefore, it is necessary for the financial institutions to prevent activities that give rise to conflict of interest so that they do not pursue their own interests or interests of a third party, etc., at the expense of the interests of trust accounts.

Furthermore, check items aimed at ensuring the soundness of bank accounts are established in the risk management system item of *V. Trustees' Assets (bank accounts).* As financial institutions engaged in trust business handle deposits, etc., it is important to execute business operations in such a manner that protects both beneficiaries and depositors when running trust operations.

(6) Checklist for Side-business Risk Management Systems

Financial institutions engaged in trust business can engage in side businesses referred to in each item of paragraph 1, Article 1 of the Law Concerning Trust Operations of Financial Institutions, etc. It is necessary to engage in operations with full awareness of the characteristics of the operational risks and system risks arising from such side businesses, as well as the laws and regulations, etc., that must be observed in relation to side businesses.

Accordingly, this checklist is designed to examine the development status of the side-business risk management system and the fulfillment status of its functions, and the consists of check items regarding whether or not a system has been developed to ensure the appropriateness of will executor services, transfer agent services, real-estate-related services and pension plan management services among side-businesses which can be operated by financial institutions engaged in trust business.

3. Conclusion

The Trust Inspection Manual is regarded fundamentally as a handbook to be used by inspectors when inspecting the trust operations of financial institutions engaged in trust business. Financial institutions engaged in trust business are expected to make full use of their creativity and ingenuity in consideration of this Manual, etc., based on the principle of self-responsibility, voluntarily prepare internal regulations and supplementary operational rules according to their size, characteristics and nature of their respective operations, ensure soundness and adequacy of their operations and strive to protect trustors and beneficiaries.

Moreover, it is hoped that sharing the check items in the Trust Inspection Manual with financial institutions engaged in trust business will lead to more efficient and effective inspections through the two-way dialogues between financial institutions and inspectors during inspections, and help improve the transparency of financial administration.

Revision of Inspection Manual for Insurance Companies

1. Introduction

Recently, the Financial Services Agency (FSA) has radically revised the "Inspection Manual for Insurance Companies" prepared in June 2000 (hereinafter referred to as "Insurance Inspection Manual") in order to turn it into an inspection handbook that is more in tune with the actual state of insurance companies. Upon revising the Insurance Inspection Manual, the FSA publicly released the draft and invited the general public to submit opinions, and after making necessary corrections, issued and published it in the form of an official notice from the Director-General of the Inspection Bureau on June 30, 2006. (For the sake of convenience, the Insurance Inspection Manual prior to the revision will be referred to as "the old Manual" and the revised version as "the revised Manual".)

This article provides a brief explanation of the revised Manual.

2. Overview of Revised Manual

In the revised Manual, "internal control system" and "compliance system" are regarded as focuses common to all insurance companies. In consideration of the operations of insurance companies, items to be checked during inspection are sorted by dividing the items into "insurance solicitation", "customer protection, etc.", "financial soundness and actuarial calculations", "product development", "insurance underwriting risks", "asset management risks" and "operational risks, etc." While the revised Manual is written on an operation-by-operation basis unlike the old Manual, various risks subject to verification under the old Manual continue to be treated as check items.

The revision is thoroughgoing, taking into account the formulation of the "Comprehensive Guideline for Supervision of Insurance Companies", the amendment of laws and regulations relating to insurance business and changes in the socioeconomic climate.

The revised Manual will be applied to inspections conducted from inspection year 2006 onwards (July 2006 and thereafter). All insurance companies are within the scope of application, including overseas branches of insurance companies, Japanese branches of foreign insurance companies and specific corporations.

3. Content of Each Checklist

(1) Checklist for Internal Control System

As management discipline needs to function effectively and internal control needs to be exercised properly at insurance companies, the FSA prepared a checklist for the internal control system of insurance companies.

"Internal control system" addresses the role of the board of directors, etc., risk management, internal audit, external audit, and the role of actuaries. For example, the role of directors and the board of directors is to confirm that: (1) corporate ethical standards have been established and a system to secure such standards in concrete terms has been developed; (2) management policies and management plans have been formulated and are made common knowledge; (3) information required for governance is obtained/shared, examined, analyzed and discussed; (4) basic policies have been formulated to establish a framework required for ensuring operational adequacy, etc.; (5) decisions are made regarding the execution of operations, and the execution of operations is supervised; (6) the duty of care of a good manager and the duty of loyalty are fulfilled; (7) divisions in charge of compliance, risk management and internal audits are properly assessed; and (8) an information disclosure framework has been established.

(2) Checklist for Compliance System

This a checklist for confirming the extent to which the compliance system is developed and established in consideration of the importance of insurance companies' compliance with laws and regulations, etc. in all aspects of their operations, based on the view that it is necessary to develop and establish a compliance system on a company-wide scale. "Compliance system" is regarded as a focus common to all insurance companies, as is "internal control system".

This checklist consists of such items as the extent to which the compliance system is developed/established, response to scandals, scope of business, identification, report of suspicious transactions, etc.

(3) Checklist for Insurance Solicitation Management System

The FSA prepared a checklist for insurance solicitation management systems, due to the need to develop and establish appropriate insurance solicitation management systems for the purpose of protecting customers upon the solicitation and conclusion of insurance contracts.

Adequacy of insurance solicitation will be verified on the basis of check items that are distinguished between life insurance policies and non-life insurance policies, as well as newly-established items that are common to life and non-life insurance policies in light of the increase in "third-sector" products and the spread of cross-selling.

(4) Checklist for Management System for Customer Protection, etc.

Insurance contracts need to be managed in an appropriate and speedy manner in view of protecting customers' interests, etc. Moreover, a system to make appropriate judgments and promptly perform clerical processes must be developed to perform work associated with the payment of claims, which is one of the most fundamental and important functions that form the foundation of the operations of insurance companies. In addition, an appropriate management system must be developed and established to deal with customer complaints, etc. and handle customer information. For this reason, the FSA prepared a checklist for management systems for customer protection, etc.

"Management system for customer protection, etc." is a new item group created as part of the latest revision, and consists of such items as an insurance contract management system, claims payment management system, complaints handling system and customer information management system.

Among the above, the checklist addresses the development of a claims payment management system for the purpose of fulfilling the payment of claims in an appropriate manner, in order to protect policyholders, etc. For example, there are check items regarding the extent to which the claims payment management system is developed/established, including the establishment of a claims payment management division, as well as check items relating to the role of the claims payment management division.

(5) Checklist for Financial Soundness and Actuarial Calculations Management System

As the management of financial soundness and actuarial calculations is indispensable for insurance companies to fulfill their responsibilities without fail and to protect policyholders, etc., the FSA prepared a checklist for confirming such a management system.

The checklist addresses the appropriateness of liability reserves, etc. set aside and the adequacy of the solvency margin ratio. Furthermore, the FSA has created a new check item related to the execution of management analysis, considering the importance of conducting stress tests and management analyses such as future cash flow analysis, due to the need for insurance companies to identify the impact of accrual of future liabilities on their financial soundness and to take additional managerial or financial action as necessary.

(6) Checklist for Product Development Management System

Upon product development, insurance companies are required to develop a management system that looks into risk, financial, solicitation, legal and all other aspects based on the principle of self responsibility, in consideration of laws and regulations such as the Insurance Business Law. For insurance products, a more flexible approach is being taken in fields where there are limited problems in terms of protection of policyholders, etc., as exemplified by the gradual shift towards a notification system. Accordingly, it is becoming increasingly important to enhance insurance companies' product development management systems. With this in mind, the FSA has created a specific checklist for insurance product development management systems and product-release follow ups.

(7) Checklist for Insurance Underwriting Risk Management System

As insurance underwriting has a substantial impact on the management of insurance companies in the long run, the FSA has created a checklist for insurance underwriting risk management systems.

Insurance products are peculiar in that the premium is determined when an insurance contract is concluded and security is assured thereafter based on future income and expenditure projections. They are exposed to the risk of the economic climate, incidence of insured events, etc. changing in ways not predicted at the time the premium was decided. The FSA has created this item group in consideration of the importance of managing such risks that are unique to insurance companies.

(8) Checklist for Asset Management Risk Management System

As it is important to engage in asset management in consideration of the whereabouts of risks associated with asset management, the characteristics of liabilities, etc., the FSA has created a checklist for asset management risk management systems.

Market risk management systems, credit risk management systems and real estate risk management systems are brought together under asset management risk management systems. The Credit Risk Assessment Manual is treated as an accompanying document for reference, in consideration of the operations of insurance companies and to ensure user-friendliness for inspectors.

(9) Checklist for Management System for Operational Risks, etc.

The FSA has created a checklist for the management system of operational risks, etc., in consideration of the importance of managing operational risks, information system risks, etc. that exist in all operations.

In addition to check items relating to operational risk management systems, information system risk management systems and liquidity risk management systems, the FSA has created a new check item for crisis management systems, and created an item group named management systems for operational risks, etc. as a whole.

(10) Accompanying Reference Materials

The revised Manual treats the On-Site Business Operation Checklist and Credit Risk Assessment Manual as accompanying reference materials, in order to make it user-friendly for inspectors. The On-Site Business Operation Checklist shows examples to be utilized by inspectors when conducting a site investigation at business establishments, etc. of insurance companies, life insurance agents and non-life insurance agencies.

4. Conclusion

The Insurance Inspection Manual is regarded purely as a handbook to be used by inspectors when inspecting insurance companies. Each insurance company is expected to voluntarily prepare a more detailed manual according to its size and characteristics, ensure soundness and appropriateness of the insurance company's operations and protect customers by fully demonstrating its creativity and ingenuity in accordance with the Insurance Inspection Manual, etc. based on the principle of self-responsibility.

The FSA believes that the development of the Insurance Inspection Manual will contribute to further improvements in its functions to inspect insurance companies. Sharing the check items in the Insurance Inspection Manual with insurance companies should lead to more efficient and effective inspections based on enhanced dialog between insurance companies and inspectors during inspections, and should also help improve the transparency of financial administration.

Final Report on Appropriate Arrangement for Providing Comparable Information that Contributes to Consumers' Choices of Insurance Products Meeting Their Demands

The Study Team on Insurance Product Sales and Solicitation (Chair: Professor Shuya Nomura, CHUO UNIVERSITY Faculty of Law), which is organized under the auspices of the Financial Services Agency (FSA), recently (June 19, 2006) put together and published a document titled "Final Report: Ideal Way of Providing Comparison Information which Helps Consumers Choose Products that Meet Their Needs".

1. Background to Study

In consideration of suggestions that there are still a large number of complaints about sales and solicitation activities in the insurance industry and that product features have become difficult for consumers to understand due to more diversified and complicated insurance product lineups, the Study Team on Insurance Product Sales and Solicitation had been convened, with members including experts and service users, and conducted studies for the purpose of tackling such suggestions in a professional and practice-oriented fashion in order to improve user protection and user convenience.

The Study Team recently compiled a final report as described below, having conducted studies since March 2006 focusing on the ideal way of providing comparison information which would help

consumers choose products that meet their needs.

2. Overview of Final Report

(1) Current Status of Provision of Comparison Information

At present, insurance companies do not necessarily compare products and cannot be deemed to be providing comparison information which helps consumers choose products that meet their needs.

(Note) Laws and regulations only prohibit indications, etc. that have the "risk of causing misunderstanding" with respect to comparisons of the features of insurance policies (paragraph 1 (6) of Article 300 of the Insurance Business Law).

The following may be the reasons why comparison information is not actively provided.

[Point of View based on Existing Regulations]

- It is not exactly clear as to what exactly constitutes a comparison of features of insurance policies that has no "risk of causing misunderstanding".

[Practical Point of View]

- If an insurance company, etc. tries to compare products it deals in ("its products") with products that it does not deal in ("other products"), it is difficult to obtain accurate information on other products.
- Insurance companies have no incentive to compare its products with other products.
- When an independent agent, etc. prepares insurance solicitation documents including comparison tables, insurance companies request that they be screened and obtain their approval in practice. Insurance companies might not approve them due to the fear of infringing laws and regulations, etc.

(2) Approach to Study

The Study Team expressed its view that it is necessary to keep the following two points in mind when examining the ideal way of providing comparison information:

1) Promotion of provision of comparison information will help improve convenience for consumers.

2) In the event that comparison information with the "risk of causing misunderstanding" is provided, there is a risk that consumers might not be able to choose insurance products that meet their needs due to misunderstanding.

(3) Issues involved in providing Comparison Information

Comparison information required by consumers are deemed to be wide-ranging, spanning from information on features of insurance policies such as coverage and premiums, to information on ancillary services of the insurance product, and even information on the creditworthiness of the insurance company. The Study Team broadly divided such comparison information required by consumers into the following categories, and then examined the issues involved in providing each type of comparison information.

1) Information on the insurance product, such as the terms and conditions of the insurance contract ("product selection information")

2) Basic information on the insurance company such as its financial position ("company selection information")

A. Product Selection Information

Entities which provide product selection information are presumably (1) insurance companies, (2) exclusive agents, (3) independent agents, (4) insurance brokers, and (5) third parties. As described below, the Study Team examined matters to be considered by these entities when providing comparison information on the terms and conditions of insurance contracts, etc.

[Subject of Comparison]

For example, in the comparison of products with different insurance periods as in the case of life insurance and term insurance, or in the comparison of products that are distinguished by the existence of dividends as in the case of participating insurance and nonparticipating insurance, the Study Team expressed its view that it is necessary to make carefully thought-out statements so that consumers would not confuse the product with similar types of insurance, including providing a clear description of the differences in product features.

[Method of Comparison]

The following two methods of comparison may be considered.

1) Comparison by displaying the information prepared by insurance companies side-by-side (i.e., side-by-side comparison of insurance policy overview)
2) Comparison by using information provided by insurance companies processed into a comparable format (i.e., comparison at a glance based on comparison tables, etc.)

The Study Team expressed its view that the following information should be explicitly stated when providing comparison information due to its importance for consumers:
1) Description of the provider of comparison information;
2) Whether or not the provider has any special stake in the insurance companies, etc. which might undermine the impartiality and fairness of comparison information; and
3) The type of information used as the source of comparison information provided.

[Comparison Items]

(a) Acceptability of Partial Comparison

Comparison of some of the features of insurance policies ("partial comparison") is not prohibited by the Insurance Business Law; partial comparison that has no "risk of causing misunderstanding" among consumers is permitted. That said, the fewer items there are in comparison information, consumers can compare insurance products more easily, but the risk of misleading consumers increases as only some of the information is stated. With this in mind, the Study Team examined cases in which partial comparison would be permissible and expressed its views as follows.

(i) Comparison information using the insurance policy overview itself (including those in table format)
⇒ In principle, it has no "risk of causing misunderstanding".

(ii) Simplified comparison information with less information volume than (i)
⇒ In principle, it has no "risk of causing misunderstanding" provided that all of the following requirements are met.

1) The insurance policy overview is provided at the same time as the comparison table for all insurance products covered in the comparison table.
2) The comparison table neither blatantly emphasizes only the merits of insurance products, nor makes the product look as if it is superior on the whole due to information that is an integral part of the merits not being made recognizable together with the presented merits.
3) The comparison table has the following cautionary statement.
- The comparison table does not show all the features of insurance products, and needs to be used purely as reference.
- The features of insurance products shown in the comparison table needs to be confirmed broadly and in detail in the insurance policy overview, etc. without fail.

(Note) The requirement referred to in 1) above is deemed to have been met even in cases where a framework has been developed to enable consumers to obtain an insurance policy overview promptly upon request (such as enabling the issuance of an insurance policy overview by post, etc. without delay upon a consumer's request) and is made common knowledge among consumers.

(b) Comparison of Premiums

Comparison of premiums has the risk of making consumers focus solely on the expensiveness/cheapness of premiums, resulting in the selection of a product without fully looking into other important factors such as coverage. Accordingly, the Study Team examined ideal ways to compare premiums without the "risk of causing misunderstanding" and expressed its views as follows.

(i) If indications excessively highlight premiums

1) Due consideration needs to be given so that indications do not induce consumers to pay too much attention to premiums and overlook other important factors such as coverage.
2) At least, there must be an accompanying statement of the assumptions which affect the premium such as the terms and conditions of the insurance contract and the outline of the coverage.
3) If the premium substantially varies with the assumptions such as age, it would be appropriate to make a cautionary statement that it is necessary to inquire the insurance company, etc. about the actual premium applied before choosing the product.

(ii) If indications of comparison include premiums except in cases referred to in (i)

It is necessary to make creative efforts in the layout of the comparison table, the presentation method, etc. to avoid misleading consumers, including inserting an accompanying cautionary statement that consumers must compare and examine the products in consideration of not only premiums but also other factors such as coverage, in order to prevent consumers from paying attention only to premiums.

B. Company Selection Information

Company selection information is deemed to be useful information for consumers when examining a company's solvency. Accordingly, the Study Team expressed its view that it would be appropriate to make an entity in an impartial and fair position to provide the following basic corporate information such as the insurance company's financial position, assuming that an explanation is provided to consumers at the same time so that there is no misunderstanding.

1) Solvency margin ratio
2) Information on core profit, insurance underwriting margin, etc.
3) Sales offices and other basic information on insurance company

(Note) In the United States, the National Association of Insurance Commissioners (NAIC) publishes company selection information such as financial data of insurance companies on its website so that consumers can obtain such information easily.

(4) Concrete Measures to Develop a Framework to Encourage Provision of Comparison Information

The Study Team recommended that the following concrete measures be considered in light of the issues involved in providing comparison information as referred to in (3) above, in order to develop a framework for encouraging the provision of comparison information that would help consumers choose insurance products that meet their needs.

1) Amendment of Supervisory Guidelines

Matters to be considered when providing comparison information relating to the aforementioned partial comparison, comparison of premiums, etc. should be clarified in the Supervisory Guidelines.

2) Disclosure of Information on Policy Overview by Insurance Companies

Insurance companies should disclose information as follows on their respective websites, etc. to enable consumers to compare insurance products themselves and make it easier to prepare an accurate comparison table.

- Disclosure of model examples of policy overview by insurance companies
- Disclosure of a "policy overview for comparison information" which narrows down the items and information shown and standardizes the format.
- Disclosure of a policy overview of the product demanded by a consumer that shows the premium, amount insured and other individual items, which is made available to consumers, agents, etc. if specific information on the consumer is entered.

3) Third-party Comparison Information Service

Consumer groups, nonprofit organizations (NPOs) and other third parties should provide comparison information such as comparison tables in consideration of impartiality and fairness.

4) Establishment of Council to Develop a Framework to Encourage Provision of Comparison Information

A voluntary council consisting of third parties who offer comparison information services, consumers, experts, the insurance industry and administrative authorities should be established, for the purpose of developing a framework for encouraging the provision of comparison information. The council is expected to fulfill the following roles.

- The council will put together a collection of specific examples of comparison information, conduct a study on what kind of comparison information would be appropriate and publish the study findings in some way.
- The council will inform and warn consumers about cases in which there is an extremely high possibility of consumers being victimized. It is also expected to play the following roles in the

future.
- Consider categorizing comparison information that has no “risk of causing misunderstanding” in each product field.
- Examine items, format, etc. of “policy overview for comparison information”.

5) Provision of Basic Corporate Information

For example, financial data (solvency margin ratio, core profit, etc.) and basic corporate information (sales offices, etc.) should be published on FSA’s website, in an effort to develop a framework that enables consumers to obtain such information easily.

6) Consumer Enlightenment Activities

The Insurance Buyers’ Guide (handbook for buyers) should state matters to be considered when comparing insurance products to make them common knowledge among consumers.

7) Monitoring of Inappropriate Comparison Information

Supervisory authorities should continually verify whether insurance companies have developed an insurance solicitation management system to give appropriate indications and should monitor comparative indications based on the recently-revised Supervisory Guidelines, in order to further enhance the framework for screening insurance companies’ advertisements.
- Among the measures mentioned above, it is hoped that the revision of the Supervisory Guidelines, the disclosure of model examples of insurance policy overview, the provision of basic corporate information, the revision of the Insurance Buyers’ Guide as part of consumer enlightenment activities and the monitoring of inappropriate comparison information will be implemented promptly.
- The aforementioned council should examine the items, format, etc. of the “policy overview for comparison information” with respect to each product field.
- The disclosure of individual items based on entry of consumer information should be left to voluntary, creative efforts of insurance companies.

(5) Medium-term Challenges

This is the final report by the Study Team on Insurance Product Sales and Solicitation. The following issues have been pointed out as medium-term challenges.

1) Standardize terminology, formulate rules on providing explanations, etc.
2) Rewrite insurance clauses in plain language and simplify them in view of consumer convenience and consumer protection;
3) Improve the quality of insurance agents.

Results of Offsite Monitoring of Inspection: Questionnaire Survey to Financial Institutions

Overview

The Financial Services Agency (FSA) is currently putting together the Financial Inspection Basic Guidelines (FIBG) to help conduct accurate and effective inspections, etc. by taking the viewpoint of ordinary users, such as depositors, and the national economy in regards to financial inspections.

In order to ensure the proper implementation of FIBG and to prevent the mechanical/uniform implementation of inspection manuals, the FSA is performing inspection monitoring and making use of the findings as references for future inspections.

The FSA performs two types of inspection monitoring: onsite monitoring, in which a senior officer of the Inspection Bureau or the Regional Financial Bureau visits an inspected financial institution and directly asks its opinions on the implementation status of inspection and other matters; and offsite monitoring, in which the financial institution is asked to respond in writing after an inspection is completed.

Since the introduction of a questionnaire system for document-based offsite monitoring in July 2005, the FSA has received many responses and opinions and would like to express its deep gratitude to the parties concerned for their cooperation.

The results of the questionnaire-based offsite inspection monitoring were compiled and published on July

27, 2006.

Procedures of Questionnaire Survey

In the questionnaire survey, the inspected financial institutions were basically asked to answer 25 multiple-choice questions, including those relating to the execution status of inspections conducted by the FSA and Regional Financial Bureaus, by selecting one option from among the following four: “1. Reasonable”, “2. More or less reasonable”, “3. Somewhat unreasonable” and “4. Unreasonable”.

◇ **Targeted Financial Institutions**

177 financial institutions inspected in accordance with inspection manuals in July 2005 or later and notified of the inspection results no later than May 10, 2006.

◇ **Collection Period**

From July 2005 to May 2006

◇ **Number of Respondents (Response Rate)**

110 financial institutions (62%)

Results of Questionnaire Survey

The results of the questionnaire survey revealed that financial institutions that chose options “1” and “2” accounted for 58% and 35%, respectively, of all respondents.

In some questions, however, financial institutions that chose option “1” accounted for only about 40%, while quite a few financial institutions chose “3” in each question.

The following is a review of the comments written in response to questions in which option “3” was chosen, as well as the results of a study conducted by the FSA.

“Inspection Management”

Overall, financial institutions that chose either option “1” or “2” accounted for 93% of all respondents.

◇ **“Inspection Period” and “Timing of Inspection”**

Financial institutions that chose option “3” accounted for 9% of all respondents in each of these questions. Their written comments included: “the burden is heavy when the inspection period clashes with busy times such as the end of the financial year” and “the inspection period should be shortened as it affects the execution of operations depending on the size and other factors of financial institutions”.

In response to such comments, the FSA will continue to be mindful of lightening the burden on financial institutions, but please understand that there are limits to what can be done due to the need of inspections as well as problems including the current staffing regime.

◇ **“Consideration given to Business Hours”**

Financial institutions that chose option “3” accounted for 10% of all respondents. Their written comments included “the inspector left late on some days” and “please give us a rough idea of the finishing time in advance”.

In response to such comments, the FSA will make sure the chief inspector exercises sufficient control and will continue to make efforts in giving guidance to inspectors in training programs and at other such opportunities in the future, as consideration needs to be given to the burden on financial institutions. And if interviews, etc. are to be conducted outside office hours, the financial institutions’ understanding will be required.

“Submission of Data”

On the whole, financial institutions that chose either option “1” or “2” accounted for 98% of all respondents.

However, for the question on “setting of submission deadline”, financial institutions that chose option “3” accounted for 5%. Their written comments included “the deadline was too soon and the paperwork was burdensome.”

In response to such comments, the FSA will make sure the chief inspector exercises sufficient control and will continue to make efforts in giving guidance to inspectors in training programs and at other such

opportunities in the future.

“Execution Status of Inspections, etc.”

On the whole, financial institutions that chose either option “1” or “2” accounted for 89% of all respondents.

However, for the question on “dialogue upon verification”, financial institutions that chose option “3” accounted for 5%. Their written comments included “it is questionable that the dialogues were fruitful and adequate.”

In response to such comments, the FSA will continue to give instructions to ensure that the chief inspector gives guidance to inspectors and strictly enforce dialogues among inspectors in training programs and at other such opportunities in the future, as there is a risk that it might lead to the mechanical/uniform implementation of the manuals.

Furthermore, for the question on “inspectors’ attitude”, financial institutions that chose option “3” accounted for 4% of all respondents. Complaints have been received regarding the language and behavior of some inspectors. With respect to this issue, the FSA will give instructions to make sure that the chief inspector gives guidance to inspectors, and strictly enforce a calm and levelheaded attitude among inspectors during inspections in training programs and at other such opportunities.

“Inspection Results Notice”

On the whole, financial institutions that chose either option “1” or “2” accounted for 98% of all respondents, and those that chose option “1” accounted for 73%.

However, for the question on “time taken to issue notice”, financial institutions that chose option “3” accounted for 3%, and requests for a shorter waiting period for the notice were received.

In response to such comments, the FSA believes that it is important to issue inspection results notices as quickly as possible, and has established its basic policy to issue a notice roughly within three months of completing the inspection as a general rule and is striving to issue notices as soon as possible.

“Inspection Monitoring”

◇ None of the comments received were against the implementation of onsite monitoring. The need for the onsite monitoring system itself seems to have been acknowledged.

◇ As some financial institutions commented that the questions in the questionnaire survey for offsite monitoring were hard to understand, the FSA is currently reviewing the questions. Especially with respect to the question on “comparison with previous inspection”, financial institutions that responded “inspection was conducted from a new angle in some areas” accounted for 30% of all respondents. As this is deemed to be attributable to the introduction of the rating system, the FSA will review the questioning method.

◇ The FSA is committed to conducting inspections in a more appropriate manner, in consideration of the various comments received in inspection monitoring and on other occasions. Financial institutions’ understanding of and cooperation in inspection monitoring will be highly appreciated in the future.

Summary of Issues by the Round Table Conference on the Financial Market Intermediation Function of Securities Companies

The Council on Securities Companies' Financial Intermediation Functions established under the Supervisory Bureau of the Financial Services Agency (FSA) compiled and published a summary of issues on June 30, based on discussions held since March 2006.

It appears that the securities market faces many challenges, as exemplified by the unfair trading by investors and misconduct by issuers of late, as well as the erroneous buy/sell orders placed in the stock market since last year.
In order to deal with such challenges, it is deemed necessary for securities companies[(note)], which have strong public characteristics as market intermediaries, to properly demonstrate their functions by maintaining self-discipline, in conjunction with legislation and enforcement (law enforcement system) including the recently-enacted Financial Instruments and Exchange Law.

[(Note)] Role of Securities Companies

In the securities market, there are a wide range of investors such as institutional investors, ordinary individual investors and funds, and there are various issuers such as listed companies. Access to the securities market by any entity requires intermediation by securities companies. Securities companies which serve as market intermediaries in this context are required to demonstrate their market intermediation functions in an efficient and stable manner, as well as functions to check unfair trading, etc. by investors and issuers.
Furthermore, securities companies trade securities themselves as market players. When doing so, they are required to carry out business operations in a sound and appropriate manner based on strict self-discipline [Figure 1].
As concrete measures to achieve this, it is deemed necessary to utilize the self-regulation functions of the Japan Securities Dealers Association (JSDA), etc. and develop rules to enhance self-discipline among securities companies.

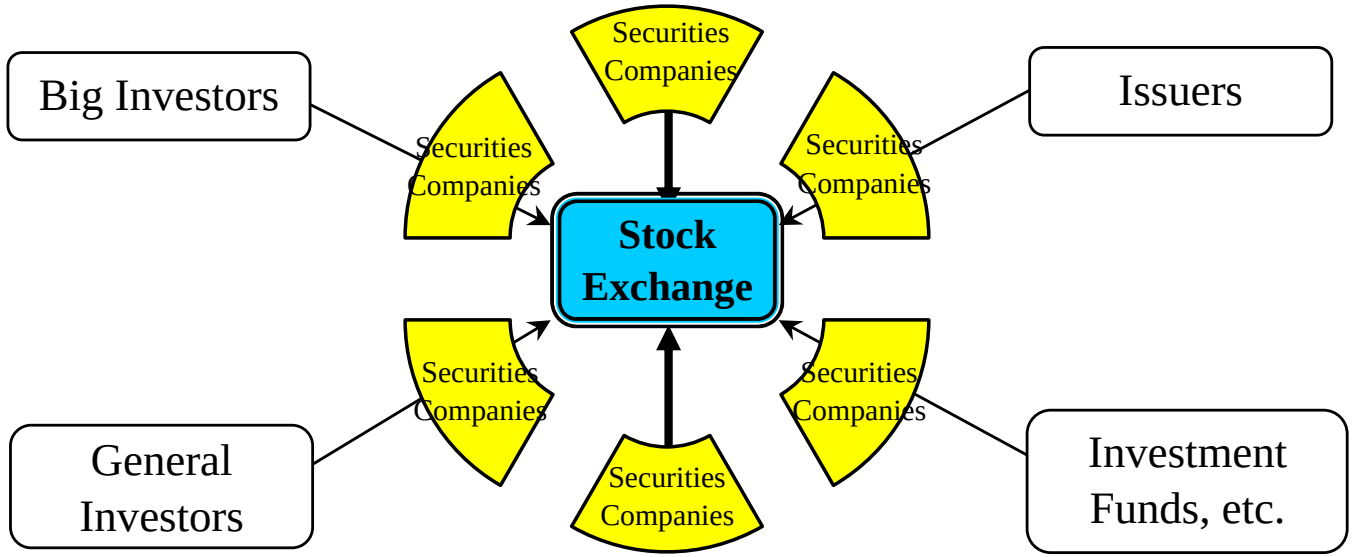
The Council has conducted studies with a critical awareness of these matters, in view of the following four themes:

I) Improve reliability of operations as market intermediaries;
II) Demonstrate securities companies' functions to check issuers;
III) Demonstrate securities companies' functions to check investors; and
IV) Maintain self-discipline of securities companies as market players.

As part of the Council's efforts to summarize the issues, issues that should be tackled by securities companies are being selected and identified from among various issues currently facing the securities companies. The Council is presenting a future approach to issues that have been identified, and demanding that the JSDA, stock exchanges and other interested parties look into the code of ethics, self-imposed regulations, etc. implemented by the industry itself [Figure 2].

JSDA has already taken certain actions, such as establishing self-imposed regulations aimed at preventing erroneous buy/sell orders. Moreover, JSDA has established a working group and a subcommittee on the issue regarding the screening of insurance underwriting, in which discussions are actively being held. It is hoped that the interested parties will continue to make proactive efforts in accordance with the approach presented by the Council. The FSA intends to make contributions and provide assistance in an appropriate fashion with respect to such efforts.

Role of Securities Companies



○ Trustworthiness of Securities Companies is Indispensable for the Credibility of the Market as a Whole

(1) Securities Company as a Market Intermediary

[Required Role]

・Demonstrate market intermediation functions in an efficient and stable manner

・Functions to check unfair trading, etc. by investors and issuers

(2) Securities Company as a Market Player

[Required Role]

・Sound and appropriate business operations based on strict self-discipline with the view of preventing conflict of interest, etc.

Main Issues regarding Securities Companies' Market Intermediation Functions, etc.

(1) Improve Reliability of Operations as Market Intermediary

Prevent Recurrence of Erroneous Buy/Sell Orders

Large erroneous order placed by securities company last December

[Japan Securities Dealers Association (JSDA)]

○ Established self-imposed regulations on order management framework (April 18)

≫ Developed framework for checking received orders

≫ Established and systemized restrictions on orders exceeding a certain amount through:

- Banning of order placement (hard limit)
- Approval by administrator (soft limit)

≫ Appointed administrator, etc. in charge of approval of lifting ban

○ Examining possibility of standardizing trading unit, etc.

[Stock Exchanges]

○ Support system such as selection of abnormal orders

Collateral Margin for Margin Trading

Zero margin for stock related to a company raided last January

[JSDA]

○ Established self-imposed regulations (April 18)

≫ Explain to customers in advance and make it widely known

≫ Notify customers upon change in margin

(2) Demonstrate Securities Companies' Functions to Check Issuers

Enhance Screening of Underwriting, etc.

Cases in which there are problems in financial position, etc. of recently-listed company

[JSDA]

○ Look into reviewing items and content of screening of insurance underwriting in self-imposed regulations

(a) Corporate governance status

(b) Growth potential of company

(c) Appropriateness of purpose of funds

(d) Develop framework for timely disclosure, etc.

Increase in equity financing through dilution, etc. which undermines shareholders' interests

○ Look into clarifying matters to be considered upon underwriting, purchasing, etc. of so-called CB (including MSCB)

Disparity between securities companies in screening ability

○ Look into formulating specific standards for framework of screening of insurance underwriting

(a) Ensure independence of screening of insurance underwriting

(b) Develop an in-house manual for screening of insurance underwriting

(c) Develop a framework to check appropriateness of screening of insurance underwriting by internal audit division, etc.

(3) Demonstrate Securities Companies' Functions to Check Investors

Price Manipulation

Endless unfair trading by investors

[JSDA]

○ Enforced self-imposed regulations on trading management framework (June 1)

≫ Trading items that should at least be screened

- Select the following customers as subjects of trading screening with respect to specific shares:

1) Customers deeply involved in trading;

2) Customers whose trades are concentrated in a certain timeframe;

3) Customers who placed calls and made orders at the same time and price; and

4) Customers who cancelled an order exceeding a certain amount, etc.

≫ If it might lead to unfair trading, the customer will be warned and acceptance of orders will be suspended.

[JSDA & Stock Exchanges]

○ Look into building WAN, etc. to promptly and smoothly exchange information between market participants including FSA

Insider Trading

Difficult to get accurate information on insiders who can obtain insider information

[JSDA, Stock Exchanges, Listed Companies, etc.]

○ Review the insider registration system currently implemented by securities companies and look into measures to improve its effectiveness

(4) Maintain Self-discipline by Securities Companies as Market Players

Increase in cases involving problems such as (potential) conflict of interest

[JSDA]

○ Look into code of ethics that would serve as a standard for securities companies, officers and employees

○ Look into self-imposed regulations which require securities companies to do the following to prevent problems arising from conflict of interest

(a) Formulate internal policies and rules

- Identify transactions with increased legal risks, substantial rumor risks, etc.
- Split and separate internal organizations
- Build a preliminary screening system independent of the sales division
- Enhance explanations and disclosure to customers and investors

(b) Build an internal control system based on (a).

Summary of Issues in Joint Study by Ministry of Finance, Bank of Japan and Financial Services Agency on Development of Financial and Capital Markets in Asia and Japanese Market

With the increase of interdependency among Asian countries and Japan, a sound development of Asian financial and capital markets has become indispensable for sustainable economic growth of Asia including Japan. Under this circumstance, financial institutions and markets of Japan are required to play an even greater role in the development of the Asian financial sector.

Against this background, this joint study was conducted with the cooperation of the Ministry of Finance and the Bank of Japan. In the Study, interview surveys with financial institutions were conducted and in addition to that, an advisory panel consisting of experts from the private sector and academics (chaired by Prof. Naoyuki Yoshino, Keio University) was established in January 2006. In the panel meetings, held three times in total, members discussed the present state of the financial and capital markets in Asia and the challenges they face, as well as the Japanese market as their mainstay. A paper, titled 'Summary of Issues in Joint Study on Development of Financial and Capital Markets in Asia and Japanese Market', compiled by the secretariat of the joint study[2] and issued June 30th, summarizes the current situation identified and the issues discussed by the joint study group mainly through panel meetings and interview surveys.

The followings are brief summaries of the paper.

I. Outline of 'Summary of Issues in Joint Study on Development of Financial and Capital Markets in Asia and Japanese Market'

1. Overview of Financial and Capital Markets in Asia and Japan's Challenges

● Overview of Financial and Capital Markets in Asia

Since the recovery from the Asian currency crisis, Asia has become increasingly important as a financial services market, while it has experienced such changes as (i) the growing presence of American and European financial institutions and (ii) the expansion of the retail market driven by economic growth and the growing middle class, etc. However, its capital markets remain underdeveloped and the intra-regional flow of funds is still limited, despite the efforts that have been made by countries within the region to foster the markets.

Furthermore, while Asian countries have taken actions to liberalize their financial markets and open them up, they vary widely in terms of content and strictness of their respective financial services regulations, tax systems, foreign exchange regulations, etc. Moreover, despite their progress on the financial infrastructure front such as legal framework, it has been pointed out that their challenges remain in ensuring the effectiveness of such infrastructure. One such example may be the framework for disclosure of corporate information aimed at improving the transparency and credibility of corporate financial data that was developed recently as part of the corporate governance reform carried out rapidly in each country throughout the late 1990s.

●Japanese Financial Institutions' Operations in Asia

Since the mid-1990s, Japanese financial institutions either curtailed or withdrew their overseas operations in response to the series of international financial crises, such as the Asian currency crisis, and the non-performing loans problem in Japan. Meanwhile, American and European financial institutions have strengthened their presence and increased the ratio of earnings from Asia through such operations as investment banking in conjunction with corporate restructuring after the currency crisis, the acquisition of local financial institutions and the expansion of retail banking taking advantage of brand value. On the other hand, the financial services needs of Japanese companies—who have traditionally been the principal clients of Japanese financial institutions' operations in Asia—have become more sophisticated and diversified reflecting changes in their business activities associated with the enhancement of internal financial functions of these companies, and the establishment of production and sales networks in Asia.

However, Japanese financial institutions have recently started expanding into Asia again, as exemplified by the rapid increase in loans made by Japanese banks to local subsidiaries of Japanese companies, and are

[2] Office of International Affairs of the General Coordination Division of the Planning and Coordination Bureau at the Financial Services Agency

deemed to continue securing earnings in the future from operations targeted at Japanese companies by capitalizing on the breadth and depth of Japanese companies' reach in Asia. To achieve this, Japanese financial institutions need to further improve their local-currency operations, M&A and related advisory operations, cash management services, receivables liquidation operations, etc., to meet Japanese companies' diversifying needs for financial services.
Moreover, in building business relations with local (non-Japanese) companies, Japanese financial institutions need to improve their ability to develop products and propose solutions and broaden the investor base, in addition to localizing business systems such as making full use of local staff who have advantages in such areas as collecting information on local business practices, credit risks, etc.

● **Approach of Japanese Authorities**

In regards to the approach of Japanese authorities concerned with developing financial and capital markets in Asia, the following have been identified as important: enhancing collaboration among financial supervisory authorities aimed at conducting proper inspections and supervision of financial institutions, engaging in negotiations for further deregulation of financial services, providing technical assistance to improve the financial infrastructure and to ensure their effectiveness. In particular, for the development of financial and capital markets in Asia, it is necessary to make qualitative improvements in disclosure and audits that would alleviate the asymmetry of information and enable investors to make investment decisions based on appropriate information; hence, it is necessary to promote information sharing on policies and practices among authorities and cooperation in enhancing the capacity, including human resource development of Asian authorities.
As indirect financing continues to play a prominent role and is deemed to serve as the principal means of financing in Asia, banking sector's governance and its monitoring of corporate governance of borrowing companies as part of efforts to manage its credit risks will be of great importance, from the viewpoint of making qualitative improvements in disclosure and audits. As supervision of banks is significant for banking sectors to also fulfill such functions, technical cooperation is important on supervisory authorities in each Asian country in this regard.

2. Regional Financial Cooperation

From the point of regional financial cooperation, namely the Asian Bond Markets Initiative (ABMI), markets in Asia will continue to face common challenges, such as to increase the number of both issuers and investors, foster the corporate bonds market which is underdeveloped compared to the government bonds market, clarify the market rules, and further develop the market infrastructure for disclosure, rating, etc. The public and private sectors need to continue coherent efforts in tackling these challenges in the future.

3. Role of Japanese Market in Flow of Funds in Asia

While deregulation of the Japanese market has largely been achieved by the "financial big bang", progress has not necessarily been sufficient in terms of internationalization of market partly due to flagging transactions associated with the stagnation of the Japanese economy in recent years. In order for the Japanese financial capital market to play a crucial part as a financing market for Asian countries against the background of its abundant financial assets, it is necessary to examine measures to further improve the convenience of the market as well as encouraging foreign companies' listing on Japanese stock exchanges by utilizing, for instance, such schemes as Japanese Depositary Receipts (JDR). In addition, in order for Japanese markets to function as one of the central financial markets in Asia, it is also important that the cross-border yen-denominated syndicated loan market in Japan is developed and efforts are made towards its development.

II. FSA's Response

The FSA will use the paper as a reference in its administration and hopes private financial institutions will do so when considering their respective Asian business.

Consultation Requests Received by Counseling Office for Financial Services Users

The number of consultation requests received by the Counseling Office for Financial Services Users (hereinafter referred to as "Counseling Office") , the gist of major consultation cases and other such information are released to the public on a quarterly basis. The consultation requests, etc. received, their characteristics and other related information for the quarter commencing April 1, 2006 and ending June 30, 2006 are as follows.

(1) We received a total of 13,938 consultation requests, etc. between April 1, 2006 and June 30, 2006. The average number of consultation requests, etc. received per day was 225 and greatly increased compared to the level in the previous period from January 1, 2006 to March 31, 2006 (158 requests).
(2) By subject, the number of consultation requests, etc. related to depositing, financing, etc. totaled 3,527 (25%), insurance products, etc. totaled 3,882 (28%), investment products, etc. totaled 3,053 (22%), cash loans, etc. totaled 1,915 (14%) and financial administration in general and other issues totaled 1,561 (11%).
(3) The following characteristics, etc. were identified with respect to each subject area.

a. Depositing, financing, etc.: With respect to financing services, we received consultation requests concerning the execution and repayment of loans, etc. With respect to depositing services, we received consultation requests relating to the deposit-making structure, such as personal identification procedures.
b. Insurance products, etc: We received consultation requests, etc. concerning insurance payments, insurance companies' responses to insurance claims, etc.
c. Investment products, etc.: We received consultation requests, etc. relating to unlisted shares, securities companies, securities reports, foreign exchange margin trading businesses, etc.
d. Cash loans, etc.: We received consultation requests, etc. relating to inquiries about the existence of moneylender registration, requests for administration, individual transactions, contract results, etc.

(4) Consultation requests, etc. received by the Counseling Office included information that would be useful for inspection and supervision purposes. For the purpose of protecting users in general and improving user convenience, we make use of such valuable information in financial administration, when conducting verification as part of an inspection, conducting interviews for supervision, issuing reporting orders and taking administrative action with respect to the financial institution concerned:

a. Information on credit crunch and oppressive debt collection;
b. Information on the sale of financial products to a borrower by a financial institution exploiting its dominant position;
c. Information on improper conduct by salespersons, etc. of an insurance company (such as abetting non-disclosure, paying insurance premiums on behalf of the policyholder, producing a contract without authorization and borrowing someone else's name)

【Featured】

Overview of "Financial Instruments and Exchange Law" (Part 1)

The law for amending the Securities and Exchange Law and other financial laws (2006 Law No.65) and the law for abolishing and amending the related laws to implement the law for amending the Securities and Exchange Law and other financial laws (2006 Law No.66) were promulgated on June 14, following the approval and passage of the respective bills at the 164th Diet session held on June 7, 2006.

The said Laws consist of legislations including reorganizing the Securities and Exchange Law into the Financial Instruments and Exchange Law (so-called "Investment Services Law") in response to the report titled "Legislation for the Investment Services Law (provisional title)" released by the First Subcommittee of the Sectional Committee on Financial System of the Financial System Council on December 22, 2005, which was featured in the February edition of the FSA Newsletter. Their aim is to adapt to changes in the environment surrounding financial and capital markets, strictly enforce rules on user protection, improve user convenience, secure market functions to shift funds from savings to investments, and adapt to the globalization of financial and capital markets.

More specifically, the legislations can broadly be divided into the following four basic elements:

(1) Development of a cross-sectoral legal system to protect investors regarding financial instruments with strong investment characteristics (legal system based on so-called "Investment Services Law");

(2) Enhancement of the disclosure system;

(3) Reinforcement of self-regulatory functions of stock exchanges; and

(4) Strict approach to unfair trading, etc.

The key adjectives here are "comprehensive and cross-sectoral", "flexible (increased structural flexibility)", "fair and transparent" and "strict".

This is the first of the three-part series featuring the latest set of legislations.

Provisions regarding the enhancement of punitive clauses in disclosure documents and unfair trading, including fictitious orders, in the law for amending the Securities and Exchange Law and other financial laws came into force on July 4, 2006 (20 days after the promulgation date). In conjunction with the enforcement of these provisions, the Cabinet Order for implementing the Securities and Exchange Law (1965 Ordinance No.321) was amended.

1. Building a Cross-sectoral Legal System to Protect Investors regarding Financial Instruments with Strong Investment Characteristics (Legislation for "the Investment Services Law")

1) Transition from Securities and Exchange Law to Financial Instruments and Exchange Law

- The latest legislations involved abolishing four laws, including the Financial Futures Trading Law, and consolidating them into the Securities and Exchange Law, in view of reviewing the existing sectional business laws. Furthermore, they involved amending 89 laws, including the Law Concerning Investment Trusts and Investment Corporations, and consolidating some of the amended provisions into the Securities and Exchange Law.
- As a result, the Securities and Exchange Law covers a wider scope of financial instruments than before. Accordingly, it is renamed "Financial Instruments and Exchange Law".

  (Note*) The Securities and Exchange Law and the Financial Instruments and Exchange Law are hereinafter referred to as "SEL" and "FIEL", respectively.
- In conjunction with this, regulated businesses are now legally referred to as "financial instruments firms" instead of "securities companies", and exchanges are now legally referred to as "financial instruments exchanges" instead of "securities exchanges". (However, these are just legal names so securities companies and securities exchanges can continue using their existing names.)

2) Expansion of Scope of Regulated Products

In recent years, financial instruments that are not regulated by SEL and other user-protection laws have started to appear on the back of the progress in financial technology, etc., and users have been

victimized in some cases. FIEL has expanded the scope of regulated products as follows, in order to close the loopholes in the existing legal system for user protection.

a) Expansion of Definition of Securities

The definition of "securities" as products regulated by the existing SEL has been expanded. For example, interests in trusts in general are regarded as securities (paragraph 2 (1) and (2) of Article 2 of FIEL) and holdings of so-called collective investment schemes (funds) are comprehensively regarded as securities (paragraphs 5 and 6 of Article 2 of FIEL).

b) Expansion of Definition of Regulated Derivative Transactions

Under the existing SEL, only "derivative transactions" related to securities are regulated. Under FIEL, transactions relating to a wide range of underlining assets and indexes and various types of transactions are regulated, including transactions subject to the Financial Futures Trading Law under the existing system (such as foreign exchange margin trading). So-called currency swaps, interest rate swaps, weather derivative and credit derivative transactions are also regulated. (Paragraphs 20 through 25 of Article 2 of FIEL).

Products regulated by Existing Securities and Exchange Law		**Products regulated by Financial Instruments and Exchange Law**
- Japanese government bonds - Local government bonds - Corporate bonds - Shares - Investment trusts - Securities-related derivative transactions, etc. (limited listing)	⇒	- Japanese government bonds - Local government bonds - Corporate bonds - Shares - Investment trusts - Interests in trust in general - Holdings of collective investment schemes (comprehensive definition) - Various derivative transactions (Examples: Foreign exchange margin trading, currency and interest rate swaps, weather derivative transactions, credit derivatives transactions), etc.

(Reference) Comprehensive Definition of Collective Investment Schemes

Holdings of arrangements (collective investment schemes) with the following characteristics are regarded as securities under the Financial Instruments and Exchange Law:

i) Receives investment (contribution) of money, etc. from other parties;
ii) Runs a business by using those assets; and
iii) Distributes proceeds, etc. from the business to the investors, etc.

It is a comprehensive definition in that it does not matter whether it is a partnership contract under the Japanese civil code or in any other legal format, or what kind of business is operated by using the invested money, etc.

(Assuming the above, certain schemes in which all investors participate in the business are excluded from the definition of securities.)

3) Regulated Cross-sectoral Operations

Under the existing SEL, "sales and solicitation" operations relating to securities and derivative transactions are regarded as "securities businesses", and are basically regulated through a registration system. Under FIEL, the existing sectional business laws have been reviewed, and a wide range of operations including conventional securities businesses are regarded as "financial instruments businesses" and regulated across sectors through a registration system (paragraph 8 of Article 2 and Article 29 of FIEL).

a) "Sales and Solicitation" Operations

- Under FIEL, the scope of regulated operations (financial instruments businesses) has been expanded in conjunction with the expanded definition of securities and derivative transactions as

referred to in 2) above: an example is the consolidation of financial futures trading business regulated by the Financial Futures Trading Law under the current system.

- Furthermore, in contrast with SEL, which does not regulate "sales and solicitation" by the securities issuers themselves (so-called own offering), FIEL treats own offering such as holdings of collective investment schemes as newly-regulated operations (paragraph 8 (7) of Article 2 of FIEL).

b) "Investment Advisory", "Investment Management" and "Customer Asset Administration" Operations

- In addition to "sales and solicitation" relating to securities and derivative transactions, FIEL regulates "investment advisory", "investment management" and "customer asset administration" operations as core operations.
- FIEL also clearly states that operations in which assets of collective investment schemes are invested mainly in securities or derivative transactions (so-called investment on own account) are also subject to regulation (paragraph 8 (15) of Article 2 of FIEL).

	(Operations Regulated by Existing Business Laws)			**(Financial Instruments & Exchange Law)**
Sales & Solicitation	Securities and Exchange Law	Securities business (Registration system)	⇒	Financial instruments businesses (Registration system)
	Financial Futures Trading Law	Financial futures trading business (Registration system)		
	Trust Business Law	Trust beneficiary certificate sales business (Registration system)		
	Law Regarding Regulation of Business Concerning Commodities Investment	Commodities investment sales business (Permission system)		
	———	Business relating to own offering of holdings of collective investment schemes		
Advisory	Law Concerning the Regulation of Investment Advisory Service Relating to Securities	Investment advisory business (Registration system)		
Investment	Law Concerning the Regulation of Investment Advisory Services Relating to Securities	Business relating to discretionary investment agreements (License system)		
	Law Concerning Investment Trusts and Investment Corporations	Investment trust business, investment corporation asset management business (License system)		
	———	Investment of assets of collective investment schemes on own account		
Administration	(Securities companies' ancillary operations)	Custody of securities		

4) Flexible Requirements on Market Entry according to Nature of Operations

FIEL regulates financial instruments businesses based on a registration system across sectors as referred to in 3) above. On the other hand, it categorizes financial instruments businesses according to the scope of their operations, and by category, sets forth requirements on market entry (criteria for rejection of registration), including the acceptability of entry by individuals and basic financial requirements

(paragraph 4 of Article 29 of FIEL).
If a financial instruments dealer wishes to launch operations in a category that is different from the one it is engaged in, the dealer must go through procedures to modify the registration (paragraph 4 of Article 31 of FIEL).

Financial instruments business	"the first financial instruments business"	All financial instruments business dealing with all securities and derivatives
	"the second financial instruments business"	Sales and solicitation of securities with lower liquidity and market derivatives
	"investment management business"	Investment management
	"investment advisory and agency business"	Investment advice

The next edition will review the development of codes of conduct that should be observed by businesses in "1. Building a System based on the Legislation for the Investment Services Law" focusing on:
5) Relaxation of codes of conduct, etc. according to customer categories;
6) Treatment of deposits, insurance, etc. with strong investment characteristics; and
7) Development of other systems for user protection.

【Primer on Financial Literacy】

Hostile Corporate Takeover Bids

The takeover bid (TOB) disclosure system is a system designed to ensure transparency and fairness in securities transactions that might affect the controlling stake in a company. Specifically, in cases where shares are to be purchased in large volumes by non-exchange trade, the bidder is obliged to disclose the TOB period, bidding volume, TOB price, etc. in advance and give a fair opportunity to the shareholders of the targeted company to sell their shares.

There has been a rapid increase in the number of corporate mergers and acquisitions in Japan lately, and the number of cases of TOB as one of the measures of acquiring a company is on the increase as well. TOBs are also diversifying in form, as exemplified by the emergence of cases involving so-called **hostile TOB**, in which TOB is carried out without the consent of the management of the targeted company.

It is therefore indispensable to have a framework that enables shareholders and investors to receive sufficient information from both the bidder and the targeted company and properly determine whether or not to sell their shares after giving careful thought. For this reason, the TOB disclosure system was revised under the Law for the Partial Amendment of Securities and Exchange Law, etc. established in June 2006. The specifics of the revision are described below.

1) Response to Law-evading Types of Transactions
Cases in which the bidder has acquired more than one-third of all outstanding shares after rapidly purchasing the shares based on a combination of trades including purchase at on-exchange and non-exchange markets were clarified as the type of transactions subject to TOB regulations.

2) Enhancement of Provision of Information to Investors
In order to provide shareholders and investors with sufficient information so that they can decide whether or not to accept the TOB after giving careful thought, measures were taken including obliging the targeted company to declare its opinion on the TOB, giving the targeted company the opportunity to ask questions to the bidder, and allowing the targeted company to request an extension of the TOB period.

3) Flexible Approach to Withdrawal of TOB, etc.
In order to prevent the bidder from being put in an extremely unreasonable position, rules on withdrawal of the TOB and changes in the terms of the TOB became more flexible in cases where the so-called anti-takeover measure is launched by the targeted company.

4) Partial Introduction of Obligation to Purchase All Shares
For the purpose of ensuring fairness between shareholders and investors, purchasing *pro-rate* became a narrower option and acquiring all the shares responding to the TOB became mandatory in cases where the post-TOB shareholding ratio exceeds a certain percentage.

5) Ensuring Fairness between Bidders
In cases where another shareholder who holds more than one-third of all outstanding shares of the targeted company rapidly accumulates certain shares while a bidder is executing a TOB, TOB became mandatory for such shareholders.

Further improvements in the transparency and fairness of the procedures are expected to be made in cases of so-called hostile TOB, relying upon due consideration given by the parties concerned with respect to the objective of the TOB system.

【Hot Picks from the Financial World】

* We deliver the hottest information of the times in this section, selected from among questions and answers given at the Minister's press conferences, etc. If you wish to find out more, we invite you to visit the "Press Conferences" section of Financial Services Agency's website.

Q. At the round-table conference held last Friday, Mr. Taizo Nishimuro, the President & CEO of the Tokyo Stock Exchange (TSE), reinstated TSE's policy to go public, which had been put on hold. What is your perception of TSE's policy to go public at this stage?

A. In theory, there is no problem whatsoever in floating the TSE, but the fact is that the TSE itself has extremely strong public characteristics. The float of the TSE based on such characteristics requires that a series of issues be addressed properly, including regulations on major shareholders and what to do with foreign investors.
Considering that the TSE has the authority to establish regulations as enforceable provisions, the crucial issue after becoming a listed company will be how to balance its function as a joint-stock corporation and its authority to establish regulations.

(from the press conference following a cabinet meeting on Tuesday, July 4, 2006)

Q. The subcommittee of the Research Commission on the Finance and Banking Systems of the Liberal Democratic Party (LDP) largely agreed to reduce the interest rate cap for the money-lending industry to the level set forth in the Interest Payment Restriction Law. What are your views on this, in consideration of the revision of relevant bills in the future?

A. There are three laws which relate to this matter, namely, the Law Concerning the Regulation of Receiving of Capital Subscription, Deposits and Interest on Deposits, the Interest Payment Restriction Law and the Moneylending Control Law. The Law Concerning the Regulation of Receiving of Capital Subscription, Deposits and Interest on Deposits and the Interest Payment Restriction Law are both under the jurisdiction of the Ministry of Justice, whereas the Moneylending Control Law is under the jurisdiction of the Financial Services Agency (FSA). Both the LDP and the New Komeito have determined their policies to a certain extent. As some members are requesting that a feasibility study be conducted for this, the FSA will properly research and examine the best way to reflect the ruling parties' intentions in the laws with the cooperation of the Ministry of Justice.
As there are a couple of options available in regards to the ways it can be done, we need to look into the respective merits and demerits of the options.
In any case, the LDP reached an interim conclusion three weeks earlier than we expected, so we intend to accelerate the pace of our work.

(from the press conference following a cabinet meeting on Friday, July 7, 2006)

Q. How do you expect financial institutions to behave at a time when positive interest rates have been restored?

A. The biggest mission of financial institutions is to properly allocate a resource called money in society through financial intermediation and thereby create an efficient society. It was dubious to claim the act of borrowing money while being charged next to nothing and then lending it to people as financial intermediation. So a certain amount of money will be allocated to lenders in the form of interest, and borrowers will pay for the cost of the resource called money. In that sense, the termination of the zero interest rate policy indicates that the finance sector has made its first step toward returning a normal state, and it is healthy for the interest rate for ordinary savings accounts to return from less than 0.01% to 0.1% or 0.2%.

(from the press conference following a cabinet meeting on Tuesday, July 18, 2006)

Q. The results of a survey conducted by the Financial Services Agency (FSA) and the Japanese Bankers Association revealed that the amount retained and not paid back by banks nationwide to fraud victims totaled $5.9 billion. What is your opinion on this, and what are your thoughts on actions to be taken by the FSA so that the amount will be paid back smoothly to victims?

A. This has been a social problem for some time: individuals who remitted money to the holder of a bank account purchased from someone else for the purpose of bank transfer fraud demanded the banks to pay back the money, but the banks are reluctant to pay it back due to their fear of incurring civil liability in the future. While I understand the banks' position, I also understand the feelings of bank transfer fraud victims who want their payback request to be met quickly. We need to have extensive discussions with financial institutions—the financial institutions must hold extensive discussions with each other as well—and work closely with the law enforcement authorities, and in the meantime, top priority must be given to the relief of victims as a matter of course.

While due consideration will be given in the process to make sure that the banks which received the money will not in turn be unexpectedly victimized, the FSA, the banks and the police basically need to think about providing relief to victims.

(from the press conference following a cabinet meeting on Tuesday, July 21, 2006)

Q. The minimum amount of cash transfers requiring identification will be reduced to ¥100,000 from next year onwards, giving rise to concerns over swamped bank tellers and burdens on fees and user convenience. How should financial institutions respond to this?

A. Japan's ATM system differs from those of the rest of the world in that Japan is probably the only developed country in which ATMs allow remittance, in contrast with ATMs in major countries, which only allow withdrawals. Under these circumstances, remittance of money in cash exceeding a certain amount will have to be done through tellers instead of ATMs in order to prevent money laundering as an international requirement. While it certainly may increase the clerical burden to some extent, it should not have a severe impact on banks' operations on the whole.

(from the press conference following a cabinet meeting on Friday, August 4, 2006)

Q. In regards to the revision of the interest rate cap under the Moneylending Control Law, some news articles today reported that the Financial Services Agency (FSA) had starting looking into making an exception for short-term loans in small amounts. What are your thoughts on this?

A. Some members of the Liberal Democratic Party (LDP) are suggesting that short-term loans in small amounts be treated as exceptions. One of the problems is how to define "small amount" and "short-term".

Another problem is that if a person borrows money from more than one moneylender, it will give rise to multiple debts. There is also the question of whether it is possible to technically prevent people from borrowing money from more than one moneylender. A massive system might be needed.

Furthermore, opinions are divided over the issue of whether such exceptional treatment should be implemented as a permanent measure, or whether exceptions should be allowed as a provisional, interim measure in consideration of radical changes. Our plan is to compile a summary of various approaches to this issue by the end of this month and pass it on to the LDP, so that it can be discussed within the LDP as well. The FSA has not reached any conclusion yet.

(from the press conference following a cabinet meeting on Tuesday, August 15, 2006)

Q. Mizuho Securities is claiming damages against the Tokyo Stock Exchange (TSE) for the erroneous order of J-Com shares. Some people have stated that it could be a huge blow to TSE, in consideration of its financial position. What are your thoughts on this?

A. It will undoubtedly be a blow if TSE really has to pay ¥40 billion. Both parties initially had the intention to resolve the issue by negotiation, but it is more transparent and objective to settle the matter in a court of law through public trial than by negotiation. I believe their aim is to resolve the issue in an open court based on the view that they could fulfill their accountability by doing so, rather than settling by negotiation, which would be nontransparent and involve difficulties in providing an explanation in the subsequent process. I have no idea what kind of outcome will be reached, but naturally, this is one of the key approaches to resolving the issue.

(from the press conference following a cabinet meeting on Friday, August 25, 2006)