

Points of Basic Policy for Financial Inspections in Program Year 2012

What is Basic Policy for Financial Inspections? The FSA publishes its Basic Policy for Financial Inspections for every program year (from July to June the next year) with the object of clarifying its basic policy for the conduct of inspections and priority inspection items, etc.

Main New Items Added

II. Basic Policy for the Conduct of Inspections

● Improvement in Quality of Inspection

Promoting the following initiatives for further enhancement of the examination ability

- (i) Research and studies on advanced financial engineering, and utilization of the knowledge obtained through such research and studies
- (ii) Incorporation of advanced inspection methods developed by overseas inspection authorities
- (iii) Efficient examining procedures through active and effective use of information analysis tools
- (iv) Promoting of effective use of information by strengthening information analysis and management
- (v) Hiring of external specialists, and fostering of human resources to gain advanced expertise
- (vi) Enhancing and strengthening of the contents of analysis and examination in the inspection of insurance companies

● Enhancement of Coordination with Auditors and Auditing Committee Members

Enhancing opportunities for dialogue with auditors and auditing committee members of financial institutions

III. Priority Inspection Items

● Development of Governance System

➤ Group governance and risk management of financial holding companies

Actively expanding overseas branch networks by large financial groups

⇒ Global risk management system for the entire group

➤ Business continuity management

Unimaginable events, such as large-scale natural disasters

⇒ Emergency response system to enable prompt collection of accurate information regarding damage caused by natural disasters and system failures, etc.

● Initiatives in Light of the Final Extension of the period of the Act Concerning Temporary Measures to Facilitate Financing for SMEs

With implementing the “exit strategy” from the SME Financing Facilitation Act, expanding the financial institutions’ roles to provide the best possible support for their management improvement and business reconstruction

- ⇒
- Cooperating with external experts and the SME Rehabilitation Support Co-operative, etc.
 - Meeting customers’ needs by utilizing capital type borrowings, ABL, etc.

● Development of Legal Compliance System

➤ Response to anti-social forces and promotion of measures on anti-money laundering and combating the financing of terrorism (AML/CFT)

Enhancing and strengthening initiatives to eliminate organized crime groups at the national and local government levels

- ⇒
- Effectively rejecting relations with anti-social forces
 - Responding to the revised Act on Prevention of Transfer of Criminal Proceeds to be enacted in April 2013

➤ Actions to prevent unfair transactions in financial markets

Revealing unfair practices such as insider trading, and LIBOR manipulation

⇒ Internal control systems for information management, etc. and compliance systems

➤ Legal risk management of wholesale businesses

Different characteristics from retail businesses in terms of handling higher value, more non-routine and complex transactions

⇒ Conducting appropriate legal checks, etc.

● Development of Various Risk Management Systems

➤ Information technology system risk management

Implementing the comprehensive self-inspections of IT system risks, and increasing the use of IT system outsourcing services

⇒ Procedures and arrangements to manage IT system risks and their outsourcing, etc.

➤ Trust business risk management

Recent problem cases related to the entrustment of pension funds

⇒ Management system of customers’ entrusted assets such as from pension funds

➤ Insurance business risk management

Changes in the global economy and large-scale natural disasters

⇒ Insurance underwriting risk management on aggregated risk, etc. including at foreign establishments

IV. Basic Framework for Inspections

● Regional Financial Institutions

Management system of overseas establishments’ business of financial institutions aiming to expand their overseas businesses

● Insurance Companies, etc.

Further enhancing and reinforcing the inspection system for insurance companies, making efforts to shorten the inspection cycle, and promoting the Insurance Inspection Rating System, the trial application of which started in April 2012.

● Agricultural Cooperatives

Making efforts to increase the frequency of inspections, based on the discussion at the sub-committee for Reforms of Regulations and Systems of the Government Revitalization Unit

Reference: Composition of Basic Policy for Financial Inspections

I. Introduction

In light of the current economic and social situation in Japan, the FSA will examine whether the systems are well-established to play a role to provide smooth and appropriate financing to borrowers and providing good-quality financial products and services to users. Development of a sound financial base, and a robust and comprehensive risk management system is also examined.

II. Basic Policy for the Conduct of Inspection

- | | |
|---|--|
| 1. Improvement in quality of inspection and strengthening of information delivery ability, etc. | 3. Enhancement of the coordination with auditors, auditing committee members and external auditors |
| 2. Enhancement of the coordination with related institutions | 4. Reduction of the workload on financial institutions |
| | 5. Response for earthquake recovery and electricity conservation |

III. Priority Inspection Items

1. Development of Governance System

- Appropriate governance
- Group governance and risk management of financial holding companies, etc.
- Business continuity management

2. Further Promotion to Facilitate Financing

- Loans to SMEs
 - Initiatives in light of the last extension of the Act Concerning Temporary Measures to Facilitate Financing for SMEs
 - Initiatives reflecting actual business conditions of SMEs
- Housing loans

3. Development of Legal Compliance System

- Response to anti-social forces and promotion of measures on anti-money laundering and combating the financing of terrorism
- Actions to prevent unfair transactions in financial markets
- Actions to prevent inappropriate new business, etc.
- Legal risk management related to wholesale businesses

4. Protection of Customers and Improvement of User Convenience

- Protection of customers, etc.
 - Thorough management of information on customers
 - Ensuring appropriate and safe financial transactions
 - Active responses to consultations and complaints (including handling of financial ADR system)
 - Appropriate explanations to customers
- Increasing of user convenience

5. Development of Risk Management System

- Enterprise risk management
- Credit risk management
- Market risk management
- Liquidity risk management
- Information technology system risk management
 - Examinations based on the results of comprehensive self-inspections of IT system risks
 - Response to the expansion of operations and updating or integrating IT systems, etc.
 - Management of outsourcing contractors for IT system, etc.
- Trust business risk management
 - Management of trust business
 - Management of outsourcing of trust business
- Insurance business risk management

IV. Basic Framework for Various Inspections

➤ **Major banks**

- Examiner in Charge conducts in-depth analysis

➤ **Regional financial institutions**

- A management system for their overseas establishments' business for those aiming to expand overseas

➤ **Newcoming banks**

- Conducting inspection at an appropriate time

➤ **Financial institutions which also engage in trust business and trust banks**

- With considering recent problem cases, conducting inspections based on the Inspection Manual for Trust and Banking Companies

➤ **Insurance companies, etc.**

- Further enhancing and strengthening the inspection system
- Shortening of inspection cycle, and evaluating inspection results by the Insurance Inspection Rating System

➤ **Large financial groups**

- Coordination with the SESC for financial conglomerates inspection as necessary
- Responds to the global business expansion

➤ **Foreign banks and foreign insurance companies**

- Dialogues with the management of their head offices, authorities in their home countries, etc.

➤ **Financial companies, etc.**

- Examining the development of management systems in response to the revised Money Lending Business Act, the Act on Settlement of Funds and the Credit Guarantee Corporations Act

➤ **Designated dispute resolution institutions**

- Examining the development of management systems in consideration of the increase of cases they handle

➤ **Outsourcing contractors and agents**

- Conducting inspections proactively

➤ **Policy-based financial institutions**

- Enhancing dialogues with the competent government authorities

➤ **Agricultural cooperatives**

- Making efforts to increase the number of inspections