

Basic Securities Inspection Policy and Program for 2011¹ (Summary)

I. Basic Securities Inspection Policy

The regulatory environment has been changing dramatically:

- *Expansion of the scope of, and increase in the number of, financial firms subject to inspection
- *Innovations in financial instruments and transaction
- *Cross-border transactions and international activities of market participants have become common
- *Experience of global financial crisis (bankruptcy of a global and large-scale investment bank)
- *Spread of the use of IT systems in financial instruments transactions
- *Damage by non-registered firms has become a social problem
- *Impacts of the Great East Japan Earthquake

⇒ SESC shall adapt to the changes by implementing **efficient and effective inspection** through **risk-based inspection programs, inspection with prior notice, the enhancement of cooperation with the supervisory department's off-site monitoring and the examination of risk control systems**, and employing **applications for emergency court injunctions against violations of the Financial Instruments and Exchange Act**.

⇒ Also, to ensure fairness and transparency of capital markets and protect investors, the SESC shall continue to focus on **the examination of violations of laws and regulations**, as well as on **the verification of internal control systems behind individual problems**.

Inspection Implementation Policy

(1) Towards efficient and effective inspection

1) Risk-based inspection

2) Implementation of effective inspection

Inspection with prior notice, verification of the appropriateness of internal control systems and enhancement of interactive dialogue

3) Enhancement of cooperation with relevant departments/organizations

Supervisory, inspection, and disclosure oversight departments of FSA and Local Finance Bureaus, SROs, overseas regulators, and investigative authorities

4) Revision of the inspection manual

(2) Focuses of inspection

1) Verification of the exercise of gatekeeper functions

Market intermediary functions, including customer management, surveillance of transactions and underwriting examination, management of undisclosed corporate information, and conduct that may hinder fair price formation

2) Examination of internal control systems

Examination of the appropriateness of internal control and risk management systems and management of IT system risk

3) Examination from the viewpoint of investor protection

Examination of solicitation for investment, the appropriateness of asset management business, compliance with laws and regulations by fund business operators and investment advisories/agencies, and response to non-registered firms

4) Others

Functions of SROs, business management of credit rating agencies, and response to inappropriate transactions and legal violations taking advantage of disasters

¹ Corresponds to government's fiscal year 2011 (from April 1, 2011, to March 31, 2012).

2. Basic Securities Inspection Program

1. Basic Concept

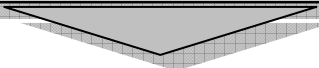
(1) Principles

The SESC shall formulate an inspection program based on the following principles, while there can be some exceptions in response to a change in market environment, impacts of disasters, factors related to specific firms.

- 1) Firms that underwrite, trade or solicit liquid financial instruments, such as listed securities, and firms that manage assets on commission from investors for their interests
 ⇒ In principle, the SESC shall examine their business operations and financial soundness on an ongoing basis.
 Credit rating agencies that assign credit ratings that greatly affect investment decisions of investors
 ⇒ In principle, the SESC shall examine their business operations on an ongoing basis.
- 2) Firms other than those specified in 1) above (e.g., firms that deal with illiquid financial instruments or firms that only conduct investment advisory business)
 ⇒ The SESC shall judge inspection priority based on information from supervisory departments in light of the huge number of firms subject to inspection.
- 3) Serious violations of the Financial Instruments and Exchange Act by non-registered firms
 ⇒ The SESC shall appropriately execute investigations for applications for emergency court injunctions, based on information from supervisory departments.

(2) Cooperation with securities and exchange surveillance departments of Local Finance Bureaus

- *The SESC shall work with securities and exchange surveillance departments of the Local Finance Bureaus to conduct efficient and effective inspection through active use of joint inspections and the exchange of inspectors.
- *The SESC shall support the securities and exchange surveillance departments through sharing inspection techniques and information, and thereby shall conduct inspections in an integrated manner.



2. Basic Securities Inspection Program

Type I Financial Instruments Businesses Operators (including Registered Financial Institutions), Asset Management Firms, and Credit Rating Agencies	To be inspected on an on-going basis (Note)
Type II Financial Instruments Businesses Operators, Investment Advisories/Agencies, Specially Permitted Business Notifying Firms for Qualified Institutional Investors, and Financial Instruments Intermediaries	To be inspected on an on-going basis
SROs	To be inspected as necessary
Non-registered firms	To be inspected on an on-going basis

(Note) The number of firms to be inspected is shown in normal years, but due to the impacts of the Great East Japan Earthquake, it is difficult to show it at the current moment.