

## Chapter 7: Self-Regulatory Organizations

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### Section 1. Relationship between the Securities and Exchange Surveillance Commission and Self-Regulatory Organizations

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SROs (the JSDA, stock exchanges, the FFA, and the TIFFE) make self-regulatory rules and conduct surveillance activities of their members concerning whether member companies operate appropriately in accordance with laws, regulations, and self-regulatory rules in order to ensure fairness in and the transparency of the markets. When conducting surveillance, SROs operate in close cooperation with the SESC (see Diagram 4 on page 55).

The SESC is also in a position to make inspections to judge whether SROs are conducting surveillance in the appropriate manner and whether they are taking proper actions against members who violate laws, regulations, and self-regulatory rules. Having market intermediaries as members, SROs establish frameworks for acceptable conduct and demand that their members comply with regulations, and are thus in a position to enhance investors' confidence in markets and intermediaries. Through their efforts, SROs bring greater benefits to market intermediaries in the long run. Along with the progress of the Financial System Reform, the role of SROs backed by the law is becoming increasingly important, and they are expected to intensify their efforts.

The SESC maintains a close interactive relationship with SROs and holds hearings with them on such matters as their surveillance.

The following are the activities of SROs from April 2000 to March 2001.

### Section 2. Activities of the Japan Securities Dealers Association

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#### 1. Inspection of members

The JSDA inspected its regular members with emphases placed on ① compliance with laws and regulations from the standpoint of ensuring fair transactions by members, ② the segregation of customers' assets from their own assets, ③ compliance with suitability from the standpoint of

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further promoting proper investment solicitations by members, ④ internal control systems from the standpoint of further promoting the improvement and strength of members' internal control systems, and ⑤ the registration of sales representatives following the expansion of the scope of registration.

*Note: Members are classified into two categories, according to their rights and duties, as follows:*

- ① *Regular members: domestic and foreign securities companies*
- ② *Special members: registered financial institutions*

The JSDA inspected its special members, emphasizing ① compliance with rules and regulations concerning the securities business from the standpoint of ensuring fair transactions in securities businesses, such as the registration of special members, ② compliance with suitability in the retail business from the standpoint of further promoting proper investment solicitations by special members, and ③ internal control systems from the standpoint of strengthening and completing their customer management systems.

The inspection of special members is conducted primarily by six associations organized by special members, such as the Japanese Bankers Association, under the delegation of operation by the JSDA. These associations implement inspections, working with personnel designated by the JSDA.

## **2. Surveillance of securities market**

The JSDA's OTC Stock Surveillance Division, which is responsible for market surveillance, collects market information related to registered OTC stocks and monitors stock prices and the trading volume of certain stocks as well as the involvement of members in transactions of those stocks. The division conducts investigations into certain stocks when it observes irregularities in the transactions of those stocks. In addition, when the Securities Business Division reports violations of

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laws or the occurrence of incidents related to OTC-registered companies and having a considerable influence on investors' judgments, the Surveillance Division also conducts investigations and, when deemed necessary, further detailed surveillance.

The Surveillance Division maintains close relationships with relevant divisions when conducting market surveillance and, if necessary, requests audits by the Audit Division.

When inappropriate securities transactions are uncovered through surveillance, the JSDA takes appropriate measures in accordance with its Articles of Association against the members involved to prevent such transactions from recurring. In addition, when inappropriate securities transactions are suspected but cannot be proven, the JSDA cautions the members involved.

### **Section 3. Activities of stock exchanges**

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#### **1. Inspections of members and special participants**

Inspections of stock exchange members and special participants are conducted on their compliance with laws and rules laid down by stock exchanges. In the TSE, members and special participants are mainly inspected with regard to ① inspecting members effectively and profoundly for their compliance with regulations and TSE rules, especially regarding their activities from consignment to settlement, and strong measures are taken when violations are uncovered, ② extending the scope of the inspections to verify capital adequacy regulation, which is disclosed for investors as a basic index to check a member's financial sustainability, ③ understanding the cause of rule violations and the problems in internal management accurately and directing appropriate internal management, and ④ cooperation with other SROs to make its inspections more efficient.

*Note: "Special participants" are financial institutions other than members that are certified to participate directly in the transactions of listed financial futures.*

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## **2. Market surveillance**

Taking the TSE as an example, the Department of Market Surveillance and Compliance conducts investigations and surveys of stocks selected by examining collected market information, stocks notified by the Stock Market Department and Bond Market Department as unusual in their trading, and stocks about which the Office of Listings Supervision reported the occurrence of information that could influence investment decisions. Thus, the Department of Market Surveillance and Compliance conducts market surveillance in close cooperation with these departments.

When inappropriate transactions are uncovered through market surveillance, stock exchanges impose sanctions or take other actions against the members or special participants involved in order to prevent recurrence.

In addition, when securities transactions are suspected of being inappropriate but cannot be proven, stock exchanges caution the members involved to be prudent in transactions in the future in order to prevent unfair transactions from occurring.

## **Section 4. Activities of the FFA**

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The FFA inspected the activities of its members with respect to the management of financial futures transaction orders, the management of customers' margin deposits, and compliance with rules regulating financial futures transactions.

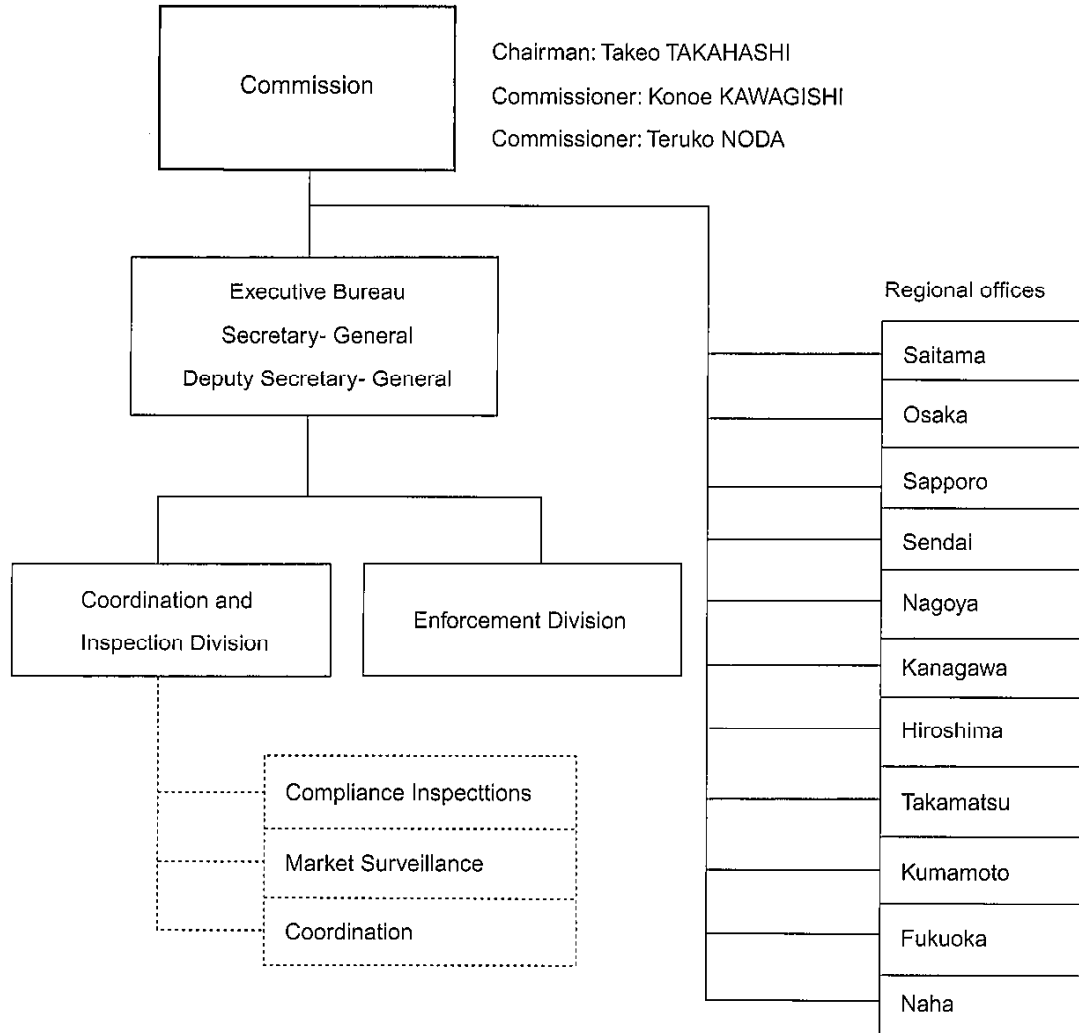
## **Section 5. Activities of the TIFFE**

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The TIFFE inspected the activities of its members with regard to compliance with rules related to the management of the acceptance of financial futures transaction orders, the management of international control systems, and prohibited acts concerning financial futures transactions.

Diagram 1

## Securities and Exchange Surveillance Commission Organization Chart



Note: Regional offices were established under the Regional Finance Bureaus of the Ministry of Finance to carry out SESC surveillance activities. The directors general of Regional Finance Bureaus conduct inspections and market surveillance under the authority delegated by the SESC and investigations of criminal offenses under the direction and supervision of the SESC (see Diagram 3).

Surveillance Framework

(After January 6, 2001)

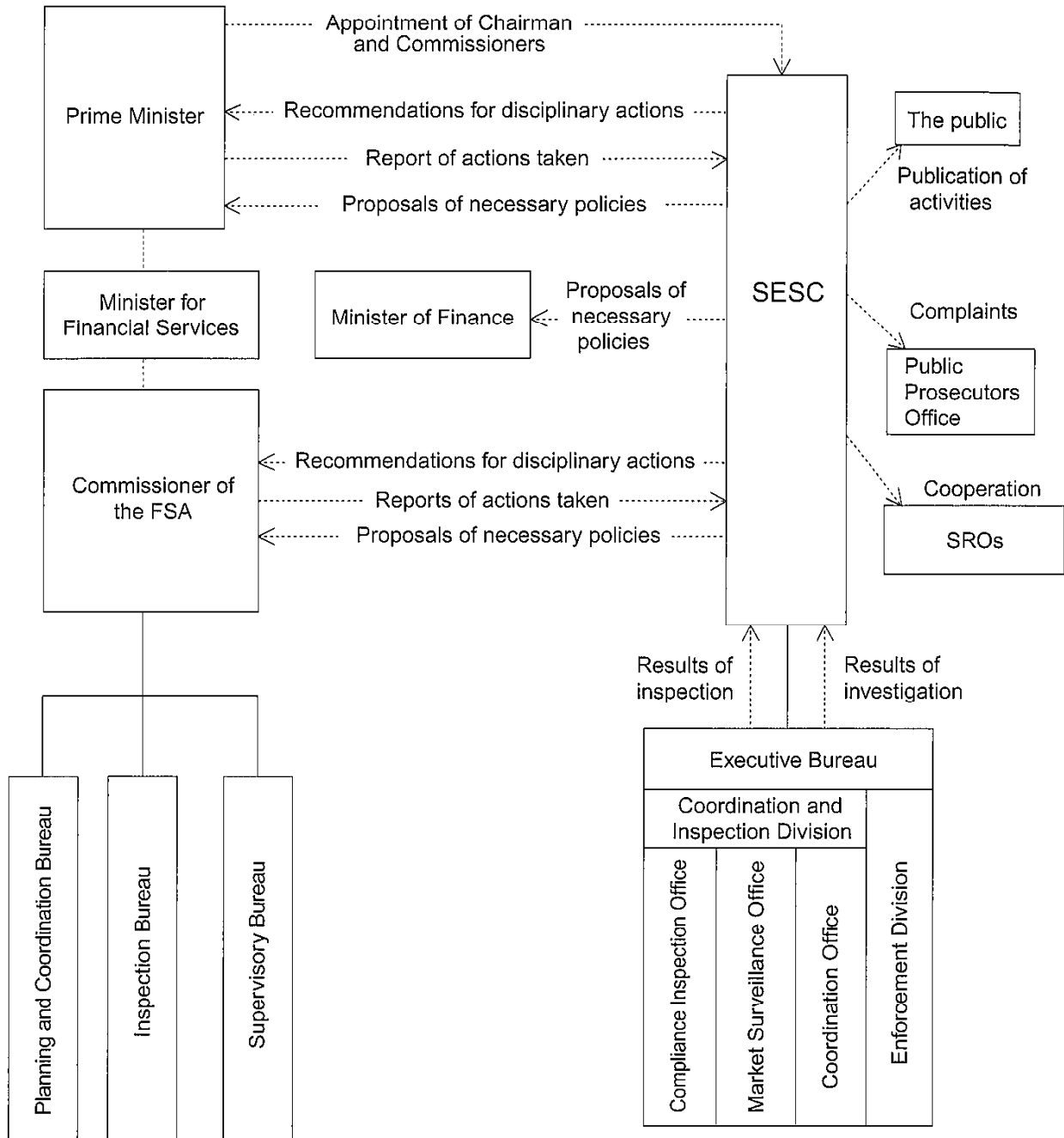
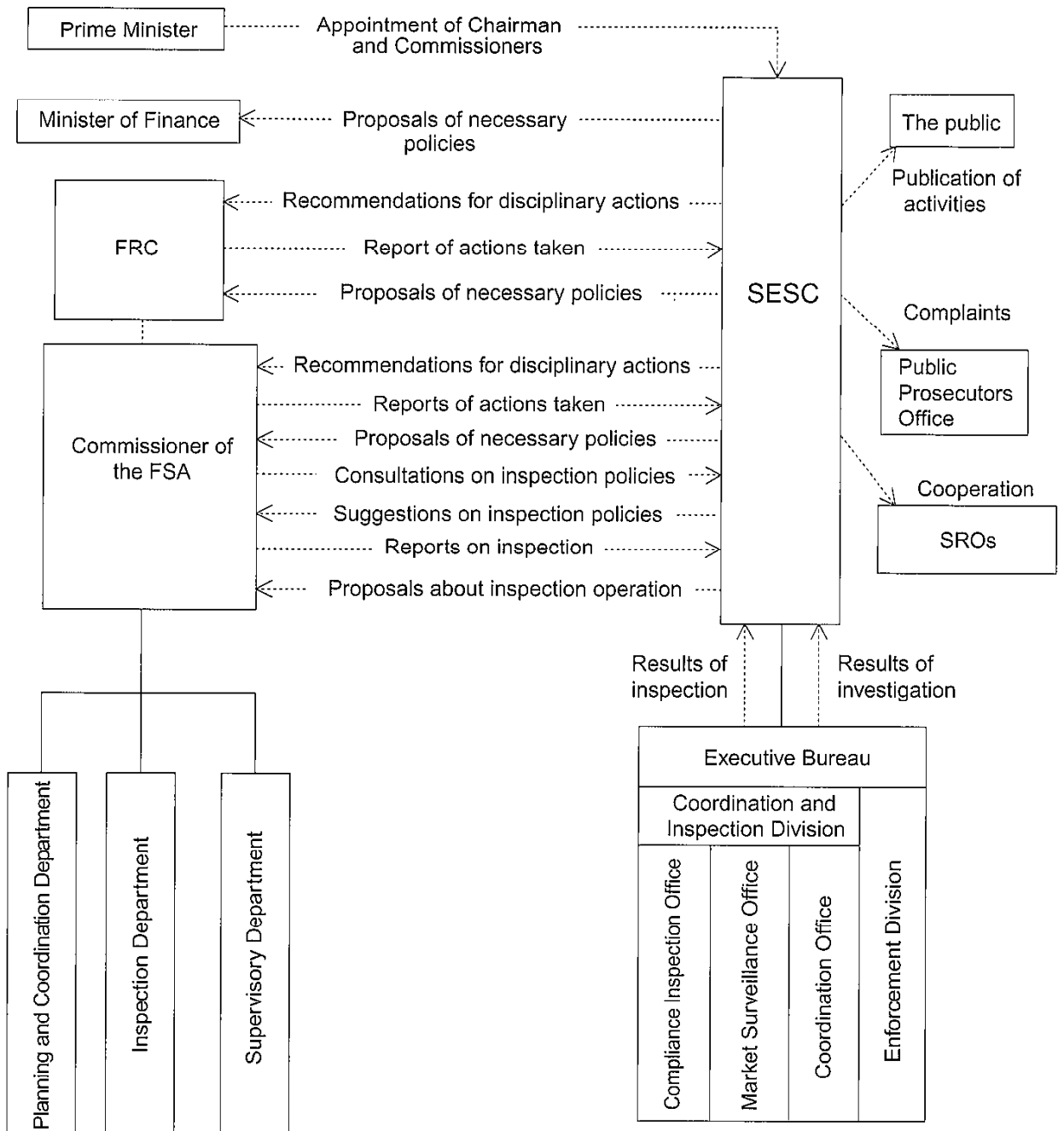


Diagram 2-2

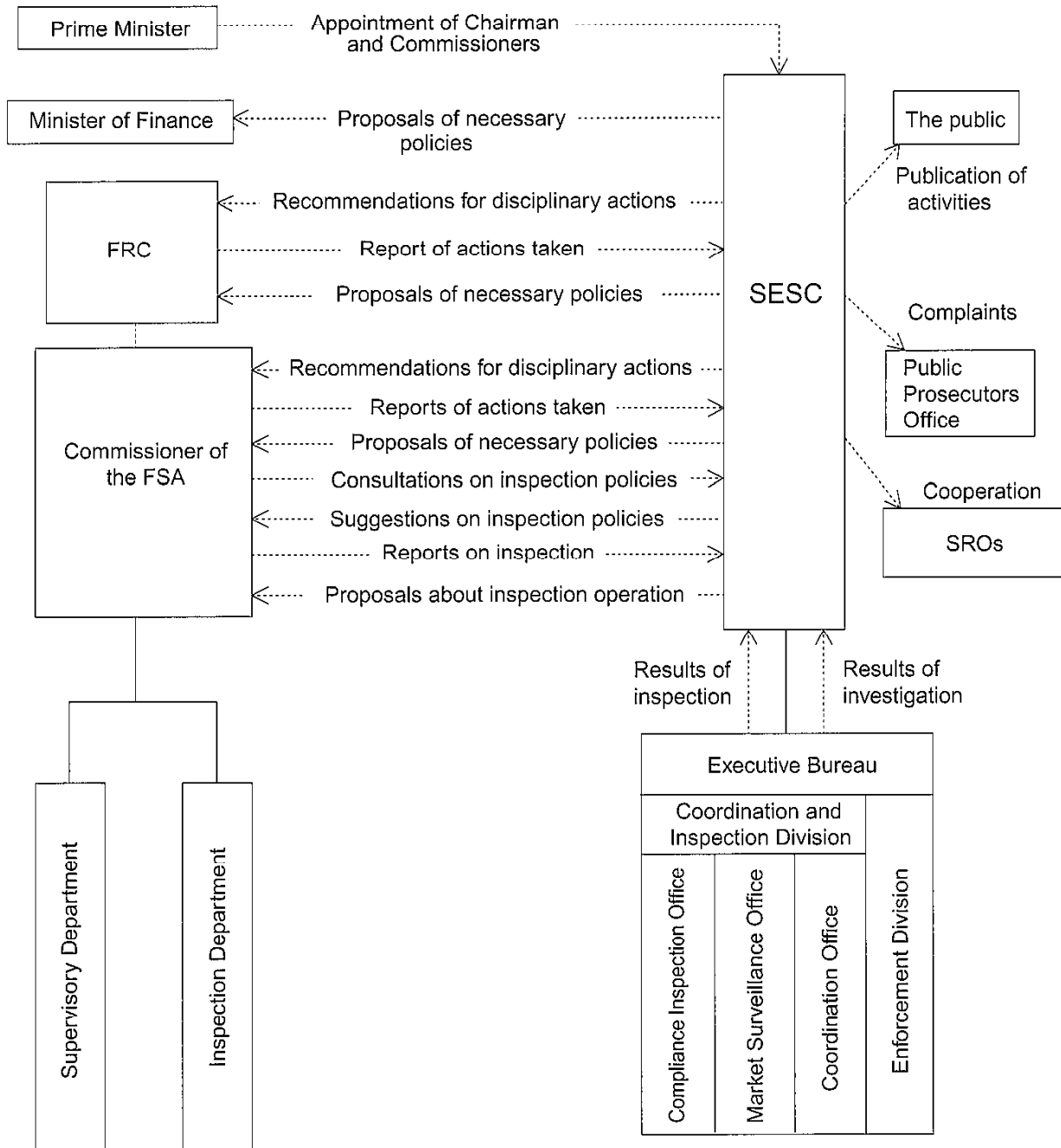
**Surveillance Framework**

(July 1, 2000, to January 5, 2001)



Surveillance Framework

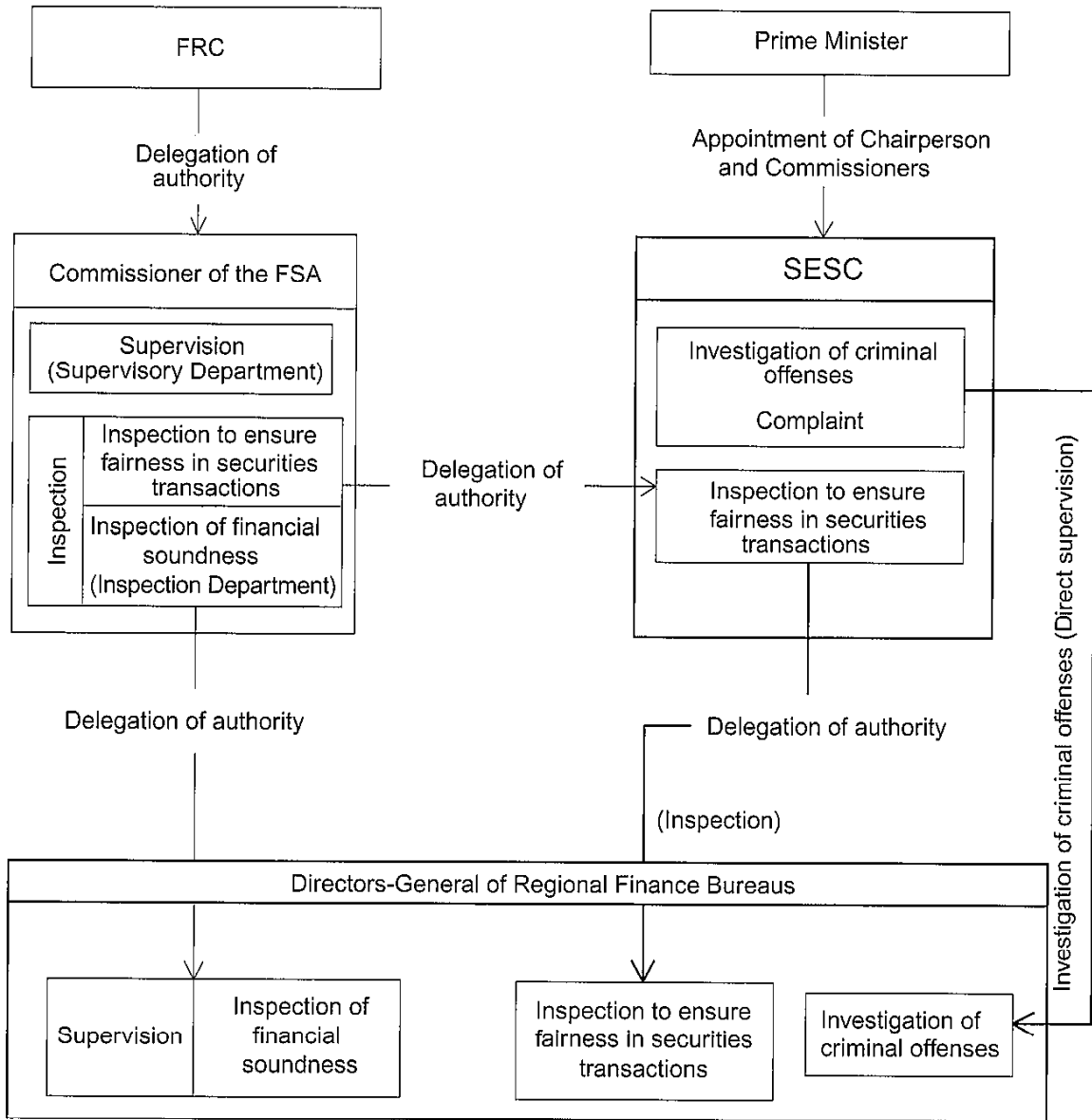
(July 1, 1999, to June 30, 2000)





**Diagram 3**

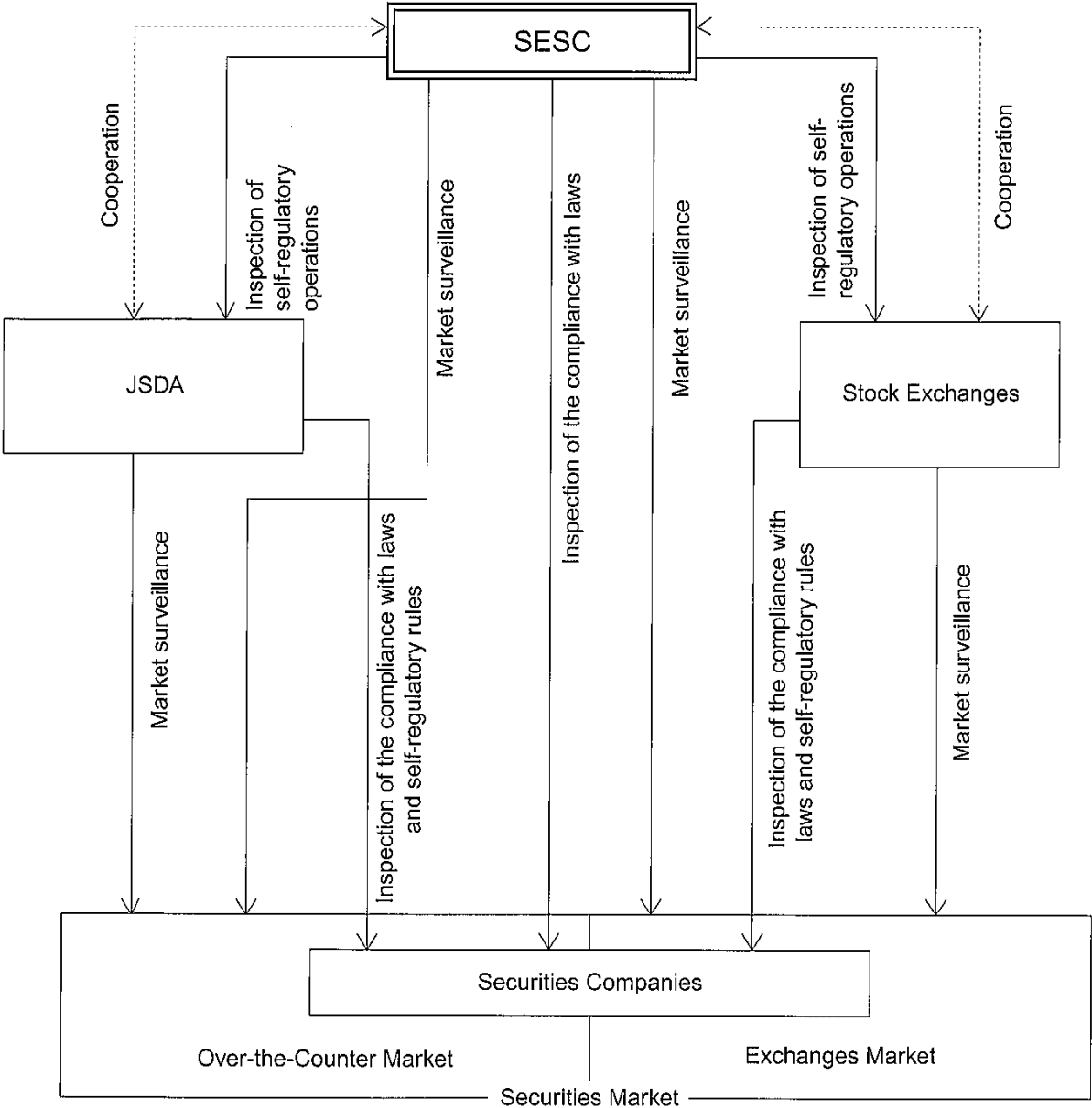
**Relationship among the Prime Minister, the Financial Reconstruction Commission, the Commissioner of the Financial Supervisory Agency, and the Securities and Exchange Surveillance Commission**



Note: Investigation of criminal offenses is carried out by the SESC staff under their peculiar authority.

- Authority of non-compulsory investigation (Article 210 of the SEL, Article 53 of the LFSF, and Article 106 of the FFTL)
- Authority of compulsory investigation (Article 211 of the SEL, Article 53 of LFSF, and Article 107 of the FFTL)

# Relationship between the Securities and Exchange Surveillance Commission and Self-Regulatory Organizations



Note: The same system applies to financial futures.

## Chairman and Commissioners Profiles

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**Chairman**  
**Takeo TAKAHASHI**

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Before his appointment as commissioner of the SESC(1998), Mr.Takahashi served as chief prosecutor of the Tokyo District Public Prosecutors Office(1995-1997)and superintending public prosecutor of the Fukuoka High Public Prosecutors Office(1997-1998).in July 2001, he was appointed chairman of the SESC



**Commissioner**  
**Konoe KAWAGISHI**

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Mr.kawagishi was appointed commissioner of the SESC in july 1998.Before being appointed to the commission, he served as deputy chief of the Editorial Board of the yomiuri shimbun(a japanese newspaper company).



**Commissioner**  
**Teruko NODA**

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Ms.Noda was appointed commissioner of the SESC in July 2001.Before being appointed to the commission,she served as a partner of Chuo Audit Corporation(now Chuo-Aoyama Audit Corporation).

## List of Abbreviations

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EB	Exchangeable bond
FFA	Financial Futures Association of Japan
FFTL	Financial Futures Trading Law
FRC	Financial Reconstruction Commission
FSA	Financial Supervisory Agency Financial Services Agency
FSAEL	Financial Services Agency Establishment Law
IOSCO	International Organization of Securities Commissions
IPS	Internet Patrol System
JSDA	Japan Securities Dealers Association
LFSF	Law on Foreign Securities Firms
MOU	Memorandum of Understanding
OSE	Osaka Securities Exchange
PTS	Proprietary Trading System
SCAN-System	Securities Comprehensive Analyzing System
SEL	Securities and Exchange Law
SRO	Self-Regulatory Organization
STAF	Surveillance by Technical Analysis of corporation Finance
TIFFE	Tokyo International Financial Futures Exchange
TSE	Tokyo Stock Exchange