

## 4. Recommendations

### 1) Outline

Based on the results of the inspections or the investigations of criminal offenses, the SESC may, if deemed necessary, present recommendations to the Prime Minister and the FSA Commissioner on administrative disciplinary actions and other necessary measures intended to ensure fairness in securities transactions (Article 20, Paragraph 1 of the FSA Establishment Law).

Specifically, recommendations by the SESC include proposing that administrative disciplinary measures be taken against securities companies and other entities if they are found to be violating laws and proposing that self-regulatory organizations take punitive measures against executives or employees of securities companies for such violation.

The SESC can ask the Prime Minister and the FSA Commissioner for a report on the measures taken based on the SESC's recommendations (Article 20, Paragraph 2 of the FSA Establishment Law).

Following the receipt of the recommendations by the SESC, the Prime Minister or the FSA Commissioner will hear from the securities companies concerned on the transactions in question, based on the results of the SESC inspections. If deemed necessary, the Prime Minister or the FSA Commissioner will take administrative disciplinary measures against the securities companies, including depriving the securities companies of their business registration license and ordering the suspension of their business operations.

Disciplinary measures against the registered securities traders of the securities companies are to be taken by the Japan Securities Dealers Association, which is entrusted by the Prime Minister to do clerical work on such measures (Article 64-7, Paragraph 1 of the SEL). The Japan Securities Dealers Association will hear from the registered securities traders concerned on the transactions in question, based on the results of the SESC inspections. If deemed necessary, the association will deprive the registered traders of their business registration license or order the suspension of their business activities.

Upon receipt of a recommendation for an order to pay penalties, the Prime Minister and the Commissioner of the FSA decide to initiate a hearing procedure. A hearing examiner drafts a decision on the case, following the hearing procedure. The Commissioner of the FSA (with delegation by the Prime Minister) makes a decision to order payment of a penalty, based on the draft decision.

### 2) Recommendations and measures taken based on recommendations

Based on the results of the inspections of securities companies and registered financial institutions, as well as those of the investigations of criminal offenses, the SESC made recommendations to the Prime Minister and the FSA Commissioner for administrative disciplinary measures against 17 companies that were found to have violated laws or regulations. (These included 12 cases that were revealed by inspections conducted by the chief of the Local Finance Bureau.)

13 recommendations were in 12 companies to take administrative disciplinary measures against securities companies. Two recommendation in one institution were against registered financial institution, and 18 recommendation for 32 people were against executives or

employees of securities companies or registered financial institutions.

Note: In 12 of these cases, administrative disciplinary measures were sought against both securities companies and their executives or employees. In one other case, administrative disciplinary measure was sought against both a registered financial institution and its executives or employees. Furthermore, there were cases in which multiple violations were pointed out against one company. As a result, the total number of cases are not consistent with the number of recommendations, which is 17.

## 1. Violations of laws and regulations by securities companies

(1) A Senior Vice President & Manager and an employee of Japanese Government Bonds division of Cantor Fitzgerald Shoken Kaisha Ltd, from May 2002 to July 2003 and from July 2002 to August 2002, respectively, had, in the course of business, executed several customers' orders by acting as a broker and at the same time as a principal for several times.

The aforementioned act of the two persons mentioned above is acknowledged to fall under the act of "acting as a principal and at the same time as a broker of the other party in consummating sale or purchase of securities" prescribed in Article 39 of the Securities and Exchange Law, which is applied to Paragraph 1 of Article 14 of the Law on Foreign Securities Firms.

Six other employees had, in pursuing their business, also executed customers' orders with their own accounts. The act of eight persons in total is considered to be that of the company, thus, Cantor Fitzgerald as a company is also acknowledged to amount to the violation of Paragraph 1 of Article 14 of the Law on Foreign Securities Firms.

- Date of Recommendation: September 10, 2004

- Administrative Disciplinary Action: A business improvement order.

\* The recommendation also sought disciplinary measures against two registered representatives.

(2) The Act of Concluding Contracts for Discretionary-Account Trading [Violation of Item 5, Paragraph 1, Article 42 of the SEL]

- The assistant manager of the Sales Department at the head office and another employee of **Chuo Securities Co., Ltd.** concluded discretionary-account trading contracts with their respective clients in the course of their business operations. These contracts gave them full authority over the execution of stock trading on behalf of their clients with complete discretion as to whether to sell or buy, and which stocks to trade, as well as how many shares and at what prices to trade, without the clients' consent on individual transactions. They then accepted orders and executed transactions.

- Date of Recommendation: November 16, 2004

- Administrative Disciplinary Measures: Suspension of stock brokerage services of the Sales Department at the head office for two days, and an order for business improvement.

\* The recommendation also sought disciplinary measures against one registered securities representatives.

Note: The disciplinary measures described above include disciplinary measures relating to the prohibited Act of representing Misleading Statements about Material matters in Connection with Securities Trading and Other Transactions described under 3), which was subjected to recommendations along with the violation described above.

- A director of **Iizuka Nakagawa Securities Co., Ltd.** concluded discretionary-account trading contracts with his clients in the course of the company's business operation. These contracts gave the director full authority over the execution of stock trading on behalf of his clients with complete discretion as to whether to sell or buy, and which stocks to trade, as well as how many shares and at what prices to trade, without the clients' consent on individual transactions. He then accepted the orders and executed transactions.

- **Date of Recommendation: February 23, 2005**

- **Administrative Disciplinary Measures: Suspension of stock and bond brokerage services of Sales Department at the head office for one day, and an order for business improvement.**

\* The recommendation also sought disciplinary measures against one registered representative.

- The (then) head of the Oyama branch of **Meiwa Securities Co., Ltd.** concluded discretionary-account trading contracts with his clients in the course of the company's business operation. These contracts gave the branch manager full authority over the execution of stock trading on behalf of his clients with complete discretion as to whether to sell or buy, and which stocks to trade, as well as how many shares and at what prices to trade, without the clients' consent on individual transactions. He then accepted orders and executed transactions.

- **Date of Recommendation: June 3, 2005**

- **Administrative Disciplinary Measures: Suspension of stock brokerage services at Oyama Branch for four days, and an order for business improvement.**

\* The recommendation also sought disciplinary measures against one registered representative.

- The (then) managing executive officer and manager of Corporate Department and other fourteen employees of **Maruhachi Securities Co., Ltd.** concluded discretionary-account trading contracts with their clients in the course of the company's business operations. These contracts gave them authority over the execution of stock trading on behalf of their clients with complete or partial discretion as to whether to sell or buy, and which stocks to trade, as well as how many shares and at what prices to trade, without the clients' consent on individual transactions. He then accepted and executed transactions.

- **Date of Recommendation: June 21, 2005**

- **Administrative Disciplinary Measures: Suspension of stock brokerage services for two days, and an order for business improvement.**

\* The recommendation also sought disciplinary measures against eight registered representatives.

(3) The Act of Representation of False, or Misleading Statements with Respect to Material Facts, in Connection with Securities Trading and Other Transactions [Violation of Item 1, Article 4 of the Ordinance of Cabinet Office concerning Regulations, etc. of Conducts of Securities Company, based on Item 9, Paragraph 1, Article 42 of the SEL prior to its amendment by Law No. 97 of 2004]

- Between January 1989 and August 2004, the president and another employee of **Niigata Securities Co., Ltd.** represented a false statement to a number of clients regarding trading of discount bank debentures in the course of their business operations. They informed the clients that they intended to have the clients acquire such debentures when in fact they had no such intentions. Furthermore, they made a false representation when they furnished trade reports and securities receipts containing false information when in fact there was no acquisition made.

- Date of Recommendation: December 22, 2004

- Administrative Disciplinary Measures: Suspension of the entire securities operations for one month, and an order for business improvement.

\* The recommendation also sought disciplinary measures against one registered representatives.

Note: The disciplinary measures described above include disciplinary measures pertaining to violations of laws and regulations that were revealed by an inspection by the Commissioner of the FSA.

- While soliciting a number of customers to purchase shares of multiple stocks between August 31, 2001 and March 12, 2003, the (then) manager of the Head Office Sales Planning Department, the (then) head of Narita branch, and the (then) head of Toshin branch of **Chuo Securities Co., Ltd.** made a representation that can mislead the clients to believe that they would receive a fixed amount of dividends yearly in the future in an advertisement that stressed such shareholder benefits as dividends and preferential treatment of shareholders.

- Date of Recommendation: November 16, 2004

- Administrative Disciplinary Measures: Suspension of stock brokerage services of the Sales Department at the head office for two days, and an order for business improvement.

\* The recommendation also sought disciplinary measures against three registered representatives.

Note: The disciplinary measures described above include disciplinary measures relating to the Act of Concluding Contracts for Discretionary-Account Trading that are described under 2) and were subjected to recommendations along with the violation described above.

(4) The Act of Making a Series of Securities Transactions to Create an Artificial Market that Does Not Reflect the Actual Market or the Act of Accepting a Series of Securities Brokerage Orders Knowing that Tradings Would Create an Artificial Market That Does Not Reflect the Actual [Violation of Item 3, Article 4 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Item 9, Paragraph 1, Article 42 of the SEL prior to its amendment by Law No. 97 of 2004]

- Between March and September 2003, in the course of business operations, a senior dealer of the Second Dealing Team of **Jujiya Securities Co., Ltd.** carried out a series of transactions in connection with shares of multiple listed stocks with the intention of moving the prices of the stocks in his favor. He did this by driving up the prices of the stocks by buying shares of the stocks, using either market or limit orders, followed by orders to buy at the best bid or a price below the best bid.
- Date of Recommendation: October 8, 2004
  - Administrative Disciplinary Measures: Suspension of stock dealing operations for 15 days, and an order for business improvement.
  - \* The recommendation also sought disciplinary measures against one registered representatives.
- Between, April and October 2003, in the course of business operations, a dealer of Dealing Department of **Aizawa Securities Co., Ltd.** placed a series of limit orders to buy shares of a number of stocks with the intention of moving the prices of the stocks in his favor by inducing orders from other market participants even though he had no intention of actually having his orders executed.
  - Between July and August 2002, in the course of business operations, the (then) head of Mishima branch and the assistant sales manager at the same branch of **Aizawa Securities Co., Ltd.** accepted and executed a series of client's buying orders for shares of certain listed stocks even though they were aware that their client was carrying out a series of securities buying and selling transactions by using limit orders, etc. with the intention of driving up the prices of the stocks.
- Date of Recommendation: February 23, 2005
  - Administrative Disciplinary Measures: Suspension of dealing in stocks for ten days, suspension of stock brokerage by Mishima Branch for five days, and an order for business improvement.
  - \* The recommendation also sought disciplinary measures against three registered representatives.
- (5) The Act of Engaging in Business Operations that Create a Situation in Which Explanations are Not Provided to Clients with Respect to Material Facts Relating to Switching Investment Trust Beneficiary Securities when Soliciting Clients to Switching Investment Trust Beneficiary Securities [Violation of Paragraph 8, Article 10 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Paragraph 2, Article 43 of the SEL]
- The executive director and another individual of **Ichiyoshi Securities Co., Ltd.** failed to provide proper guidance to the company's sales people in the course of the company's business operations, and as a result created a situation in which the company's sales people failed to explain to customers about a redemption switch preferential treatment program, a material fact concerning such switches, when they solicited their customers to switch their investment trust beneficiary certificates that are redeemed prematurely. In addition, the two failed to construct an internal control system to ensure that internal records of such explanations are created and retained, and that the status of such explanations is monitored. As a result, they carried out their operations without their customers being provided

with explanations of certain material facts relating to the switches when they solicited the customers to switch their investment trust beneficiary certificates.

- Date of Recommendation: June 3, 2005

- Administrative Disciplinary Measure: A business improvement order.

\* The recommendation also sought disciplinary measures against one registered representative.

- The manager-director of Sales Division and the (then) managing director of **World Nichiei Frontier Securities Co., Ltd.** failed to provide proper guidance to the company's sales people in the course of business operations, and as a result created a situation in which the company's sales people failed to explain to customers about a redemption rollover preferential treatment program, a material fact concerning such rollovers, when they solicited their customers to roll over their investment trust beneficiary certificates that are redeemed prematurely. In addition, by failing to make the company's internal control system to function effectively to ensure that internal records of such explanations were created and retained and that the status of such explanations was monitored, the individuals let their business operations to go on without their customers being provided with explanations of certain material facts relating to the rollovers when they solicited the customers to roll over their investment trust beneficiary certificates.

- Date of Recommendation: June 23, 2005

- Administrative Disciplinary Measure: A business improvement order.

\* The recommendation also sought disciplinary measures against two registered representatives.

(6) Prohibition of market manipulative [Violation of Items 4 and 5, Paragraph 1, Article 159 of the SEL]

- Between 4 and 20 June 2001, **UFJ Tsubasa Securities Co., Ltd.** colluded with another party to engage in collusion to trade a total of 355 thousand shares of Cats Corporation over a period of 12 business days on the Tokyo Stock Exchange. UFJ Tsubasa Securities Co., Ltd. made an arrangement in advance to have the other party simultaneously buy or sell the shares that UFJ Tsubasa sold or bought at the same price, and executed the collusion sales and purchases of the stock.

- Date of Recommendation: January 7, 2005

- Administrative Disciplinary Measures: Suspension of dealing in stocks for ten days, and an order for business improvement.

(7) The Act of Failing to Perform Personal Identity Confirmation when Trading or Brokering Securities, and the Act of Failing to Create Records of Personal Identity Confirmation [Violation of Paragraphs 1 and 2, Article 3 and that of Paragraph 1, Article 4 of the LCIRR]

- Between February 26, 2003 and January 21, 2005, a director and another individual of **Credit Agricole Indosuez Securities (Japan) Ltd.** let some corporate clients open accounts either without performing the required confirmation of the identity of such corporate clients or that of the natural persons who were engaged in such

transactions or without creating any records of such identity confirmation in the course of the company's business operations.

- Date of Recommendation: June 17, 2005

- Administrative Disciplinary Measure: An order for remedial measures.

\* The recommendation also sought disciplinary measures against one registered representative.

## **2. Violations of laws or regulations by executives and other employees of securities companies**

The following types of violations of laws or regulations were found to have been committed by executives and other employees (registered representative) of securities firms. (The descriptions contain only the disciplinary actions that are recommended strictly against executives and employees. Violations that involved concurrent recommendations of disciplinary actions against corporations are excluded.)

(1) The Acts of Concluding into Contracts for Discretionary-Account Trading [Violation of Item 5, Paragraph 1, Article 42 of the SEL]  
(Recommendations were issued against four individuals at four corporations)

(2) Securities Trading Intended for Executives and Other Employees of Securities Companies to Pursue Speculative Profits [Violation of Item 5, Article 4 of the Ordinance of Cabinet Office Concerning Regulation, etc. of Conducts of Securities Company, based on Item 10, Paragraph 1, Article 42 of the SEL (or Item 9, Paragraph 1, Article 42 of the SEL prior to its amendment by Law No. 97 of 2004 for acts committed on or prior to March 31, 2005)]  
(Recommendations were issued against one individual at one corporation.)

## **3. Violations of laws or regulations by Registered Financial Institutions**

(1) The Act of Presenting Misleading Statements with Respect to Material Facts in Connection with the Handling of Private Placement of Securities [Violation of Item 1, Article 21 of the Ordinance of Cabinet Office concerning Securities Operations of Financial Institutions, based on Item 9, Paragraph 1, Article 42 of the SEL prior to its amendment by Law No. 97 of 2004. Provisions of Paragraph 5, Article 65-2 of the SEL are relied upon.]

- In connection with private placement of structured bonds (which are bonds issued with various conditions attached to meet the investment objectives of individual clients) in the course of their business operations, two vice presidents of the Second Sales Dept. at the **Marunouchi Branch of Citibank, N.A.** made statements that are bound to mislead investors with respect to certain material facts by distributing to multiple clients certain solicitation materials that do not properly describe the product features of the notes.

- Date of Recommendation: September 14, 2004

- Administrative Disciplinary Measure: A business improvement order.

\* The recommendation also sought disciplinary measures against two registered securities traders.

Note: The disciplinary measure described above includes disciplinary measures relating to the **Act of Handling Private**