



The roles of IBA members in promoting Leading Asset Management Center

IBA Japan, Executive Committee meeting

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*Any views expressed in this presentation are those of the presenter and are not necessarily the official views of the SESC/FSA.

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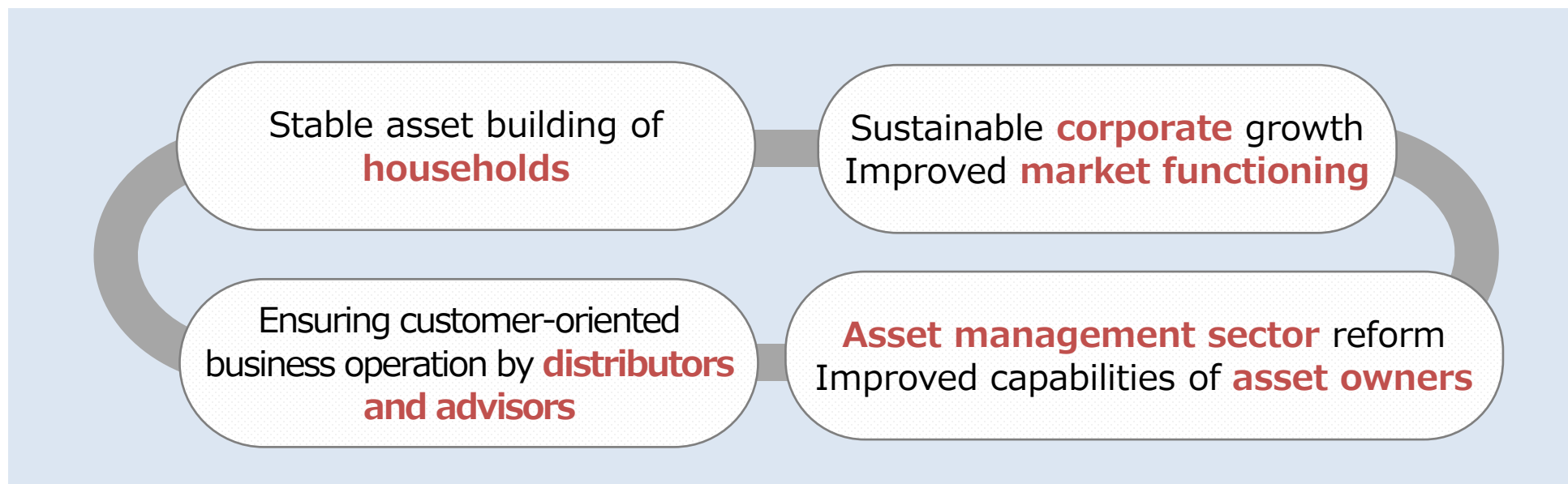
I. The roles of IBA members in promoting Leading Asset Management Center



1. Overview of “Policy Plan for Promoting Japan as a Leading Asset Management Center”

Overview of “Policy Plan for Promoting Japan as a Leading Asset Management Center”

- For the growth of Japan’s economy and Japanese people’s asset income, the Japanese government has been undertaking policy initiatives to achieve a **“virtuous cycle of growth and distribution”**, including through an increased flow of Japan's household savings into productive investment.
- The government has been engaging with **various stakeholders in the investment chain** to encourage this move, including through:
 - I. Doubling Asset-based Income Plan**
 - II. Corporate governance reforms**
 - III. Reform of Asset Management Sector and Asset Ownership**



Stable Asset Formation of Household

- ✓ Complete Revamp of NISA (Jan. 2024)
- Reform of iDeCo
- ✓ Establishment of J-FLEC (in full operation from Aug. 2024)
- ✓ The legal obligation to operate in the best interests of customers (Nov. 2023)

Corporate Governance Reform

- ✓ Request by TSE to encourage effective management of listed companies (Mar. 2023)
- ✓ Reform of the Quarterly Securities Reporting system (Apr. 2024)
- ✓ Obligation for listed companies to disclose key information in English (Apr. 2025)
- ✓ "Action Program for Corporate Governance Reform 2024: Principles into Practice" (Jun. 2024)
- Acceleration of Corporate Governance Reform (ongoing)

Reforming the Asset Management Sector and Asset Ownership

- ✓ Plan for Major financial groups to enhance asset management businesses (Jan. 2024-)
- ✓ Policy Package to Achieve Special Zones for Asset Management Businesses (Jun. 2024)
- ✓ A new program to assist new entrants (Emerging Manager Program) (Jan. 2024-)
- ✓ Asset Owner Principles (Aug. 2024)
- Reform of occupational pension funds



2. Fulfilling the role as gate-keeper regardless of market conditions



- The FSA has published a detailed [analysis](#) of **the supply-demand and liquidity conditions of the Japanese stock market to examine the background of sharp swings on August 5, 2024.**
- While the analysis does not cover inter-market connectedness due to lack of data availability, **use of granular order/transaction level data** on the Nikkei 225 Futures and associated several indicators have provided a new insight into the background and mechanism of the market turbulence.

Figure 1: Stock Price Movement on August 5

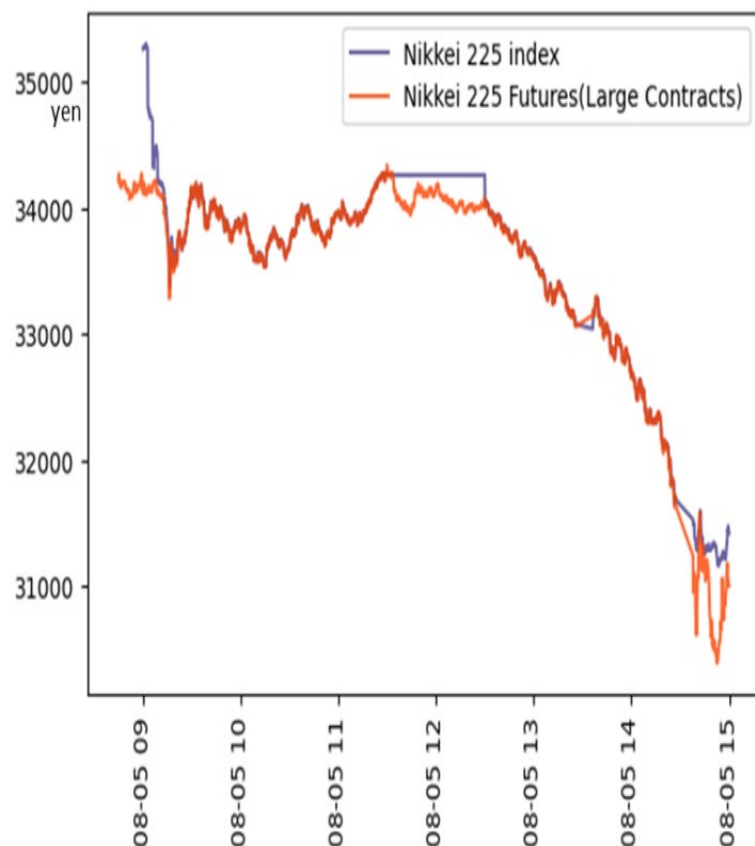
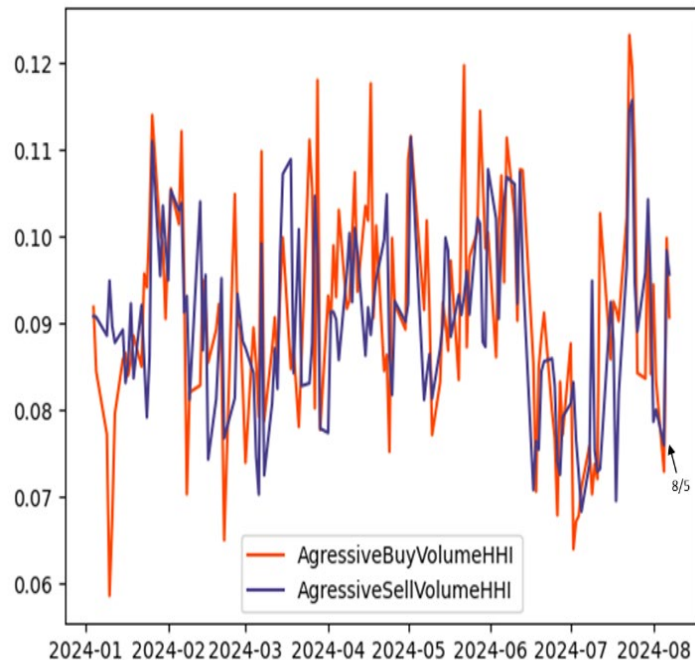


Figure 2: Summary of list of indicators

| Indicator | Overview |
|--|---|
| Aggressive Buy Volume Ratio | Imbalance between supply and demand (i.e., whether buyers dominate or not) |
| Aggressive Buy(Sell) Volume HHI | Degree of concentration of execution amounts of take orders by buying(selling) entities (i.e., to what extent transactions by specific entities were concentrated) |
| Range of scale up(down) HHI | Concentration of price fluctuations by buying(selling) entities (i.e., to what extent price increases/decreases were concentrated in transactions by specific entities) |
| Buy(Sell) Price Impact Ratio | Likelihood of price movements due to buy(sell) orders (i.e., the extent to which prices moved per contract amount) |
| Number of quotations indicated within five ticks around the best quote price for each transaction | Liquidity around the best quote (i.e., whether there were a lot of orders around the best quote prices) |

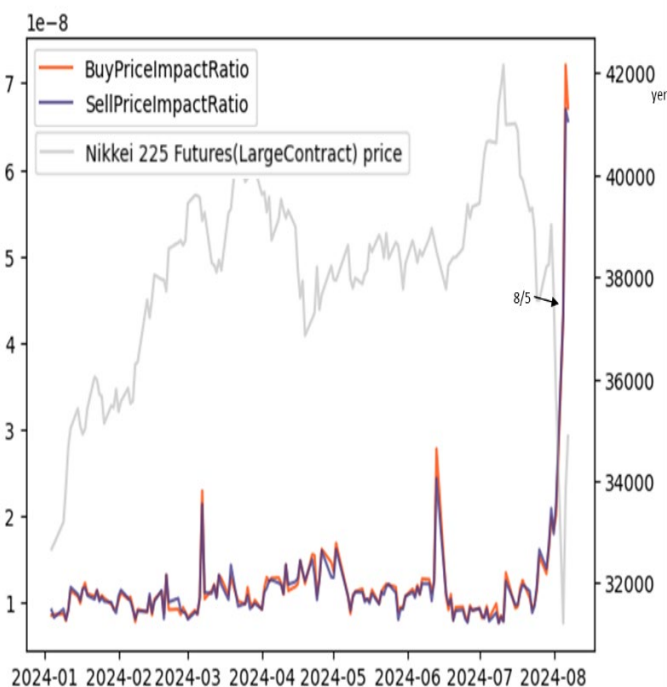
- The orders were not concentrated by specific trading entities on August 5, compared to normal times*.
- However, the indicators suggests that, **in early August, the market was prone to large price fluctuations** against a small imbalance between supply and demand, exacerbated by **sharply-declining depth of orders**.

Figure 1: The degree of concentration



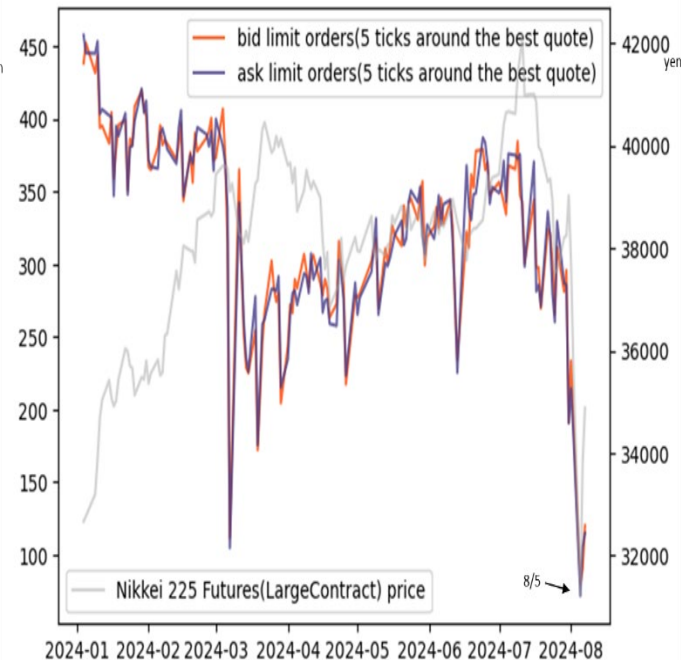
| | YTD Average* | August 5 |
|--------|--------------|----------|
| Buyer | 0.091 | 0.072 |
| Seller | 0.089 | 0.075 |

Figure 2: Likelihood of price movements



| | YTD Average* | August 5 |
|--------|-----------------------|-----------------------|
| Buyer | 1.21×10^{-8} | 4.29×10^{-8} |
| Seller | 1.20×10^{-8} | 4.34×10^{-8} |

Figure 3: Order volume around best quote



| | YTD Average* | August 5 |
|-----|--------------|----------|
| Bid | 322.20 | 79.55 |
| Ask | 322.28 | 71.80 |

* Analysis period is from January 2024 to August 7, 2024.

- Several intraday indicators on August 5 confirmed that **market liquidity had rapidly subsided toward the afternoon session, which may have induced the market turbulence.**
 - The take order was biased toward sellers from around the lunch break in the cash equity market (11:30 to 12:30) to around 14:00, where a sharp fall of stock prices occurred. From 12:30 onwards, the order book got thinner, and prices moved more easily.

Figure 1: Imbalance between supply and demand

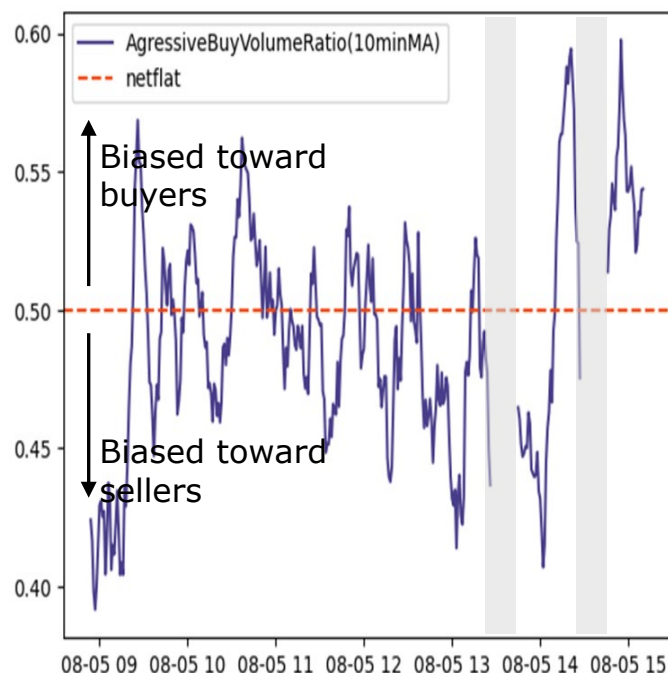


Figure 2: Concentration of price fluctuations by buying/selling entities

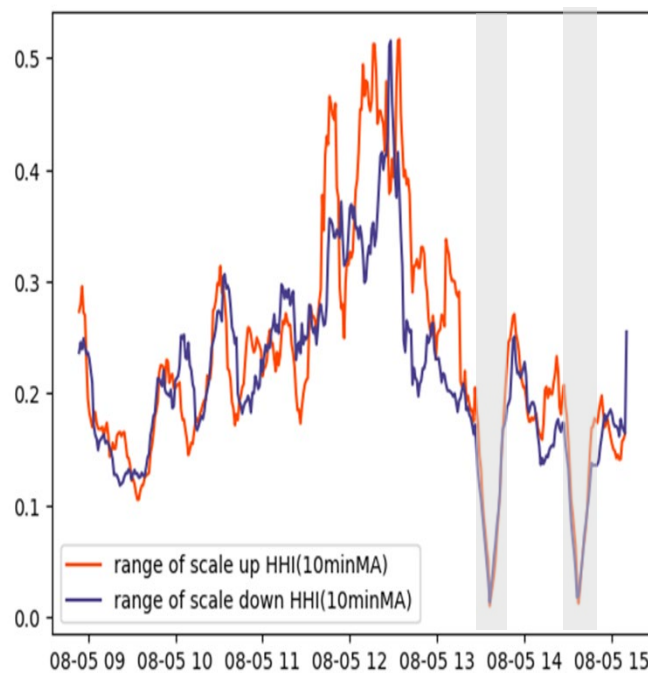
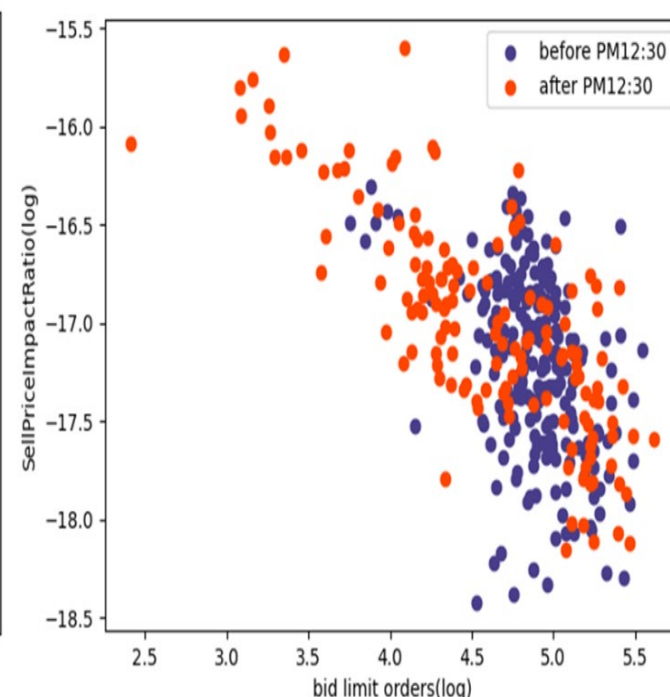


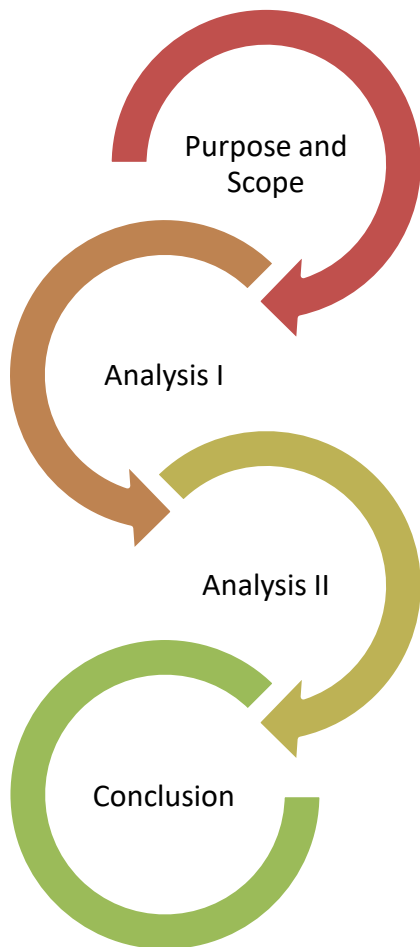
Figure 3: Scatter plot of Sell Price Impact Ratio and bid limit order volume



* The time zones colored in gray show the periods that the circuit breaker was activated (i.e. 13:26-13:36 and 14:27-14:37). To see more on the Circuit Breaker Rule, see [JPX website](#).

** Calculation are made for a one-minute period. For Figures 1 and 2, indicators calculated every minute are leveled using a 10-minute moving average (MA) for the purpose of making it easier to understand the trends.

Key Takeaways and Next Steps



- [The paper](#) presents a detailed analysis of the sharp swings that occurred in the Japanese stock market on August 5, 2024, using granular data and indicators.



The analysis is obliged to focus on the Japanese stock market. While other domestic and overseas market (e.g. bond, forex and derivatives) should be analyzed all together, it was not possible due to the lack of data availability.

1) Year-to-date (until early August) Analysis

- On a daily basis from mid-July to early August, excessive imbalances were not observed but the market liquidity was markedly declining, making prices more susceptible to fluctuations.

2) August 5 Intraday Analysis

- Market liquidity subsided rapidly toward afternoon session. At these hours, take orders were found to be concentrated on the seller side.
- This suggests that the imbalance between supply and demand on the seller side was amplified by a shortage of market liquidity, which may be one of the factors of the rapid market turbulence.

One implication: Amid a decline in the market liquidity, a large amount of selling demand that occurred at a specific period caused a shortage of market liquidity provided by buyers, resulting in rapid market turbulence in which sell orders call sell orders.

- ✓ Evaluating the impact of market fluctuations on financial stability is an important issue on the regulatory agenda.
- ✓ [The FSA will continue to analyze the mechanism of sharp market turbulence and its impact on financial stability by enhancing analytical capabilities and expanding of its analysis.](#)

IOSCO Consultation Report on Liquidity Risk Management for CIS (November 2024)

- IOSCO published a Consultation Report on its revised recommendations for Liquidity Risk Management for Collective Investment Schemes ("CIS") (the 'Revised LRM Recommendations'), especially for open-ended funds on 11 November 2024. IOSCO also consulted on complementary Guidance for the Effective Implementation of the Recommendations for Liquidity Risk Management ('Implementation Guidance').
- The Revised LRM Recommendations take into consideration the FSB's revised Recommendations to Address Structural Vulnerabilities from Liquidity Mismatch in Open-Ended Funds ('Revised FSB Recommendations') from December 2023, as well as recent market events such as the COVID-induced market volatility and those following the war in Ukraine.
- The accompanying Implementation Guidance sets out technical elements focusing on open-ended funds, such as determination of asset and portfolio liquidity and considerations relating to the calibration and activation of LMTs and other liquidity management measures.
- The Revised LRM Recommendations and the Implementation Guidance incorporate IOSCO's Anti-dilution Liquidity Management Tools – Guidance for Effective Implementation of the Recommendations for Liquidity Risk Management for Collective Investment Schemes ('IOSCO ADT Guidance') published in 2023 and should be read in conjunction with each other for completeness.

Proposed changes

- **Categorizing open-ended funds (OEFs) based on the liquidity of their assets.**
- **Encouraging investments managers to implement a broad set of liquidity management tools (LMTs) and other liquidity management measures.**
- **Emphasizing the importance of anti-dilution LMTs to mitigate material investor dilution and potential first-mover advantage arising from structural liquidity mismatch in OEFs.**
- **Incorporating new guidance on quantity-based LMTs and other liquidity management measures.**

IOSCO Consultation Report on Liquidity Risk Management for CIS (November 2024)

The Revised LRM Recommendations

1. The responsible entity should draw up an effective liquidity risk management process, compliant with local jurisdictional liquidity requirements.

2. The responsible entity should set appropriate liquidity thresholds which are proportionate to the redemption obligations and other liabilities of the CIS.

3. The responsible entity should ensure that the OEF's investment strategy and the liquidity of its assets should be consistent with the terms and conditions governing fund unit subscriptions and redemptions both at the time of designing an OEF and on an ongoing basis. The redemption terms that the OEF offers to investors should be based on the liquidity of its asset holdings in normal and stressed market conditions. To this end, when structuring an OEF that allocates a significant proportion of its assets under management to illiquid assets, responsible entities should consider low redemption frequency and/or implementing long notice or settlement periods.

4. The responsible entity should consider liquidity aspects related to its proposed distribution channels.

5. The responsible entity should ensure that it will have access to, or can effectively estimate, relevant information for liquidity management.

6. The responsible entity should consider and implement a broad set of liquidity management tools and measures to the extent allowed by local law and regulation for each OEF under its management, for both normal and stressed market conditions as part of robust liquidity management practices.

7. The responsible entity should consider and use anti-dilution LMTs to mitigate material investor dilution and potential first-mover advantage arising from structural liquidity mismatch in OEFs it manages, to ensure that investors bear the costs of liquidity associated with fund subscriptions and redemptions, and to arrive at a more consistent approach to the use of anti-dilution LMTs. Such tools should impose on subscribing and redeeming investors the explicit and implicit costs of subscriptions and redemptions, including any significant market impact of asset sales to meet those redemptions

8. The responsible entity should regularly assess the liquidity of the assets held in the portfolio.

9. The responsible entity should integrate liquidity management in investment decisions.

10. The liquidity risk management process should facilitate the ability of the responsible entity to identify an emerging liquidity shortage before it occurs.

11. The responsible entity should be able to incorporate relevant data and factors into its liquidity risk management process in order to create a robust and holistic view of the possible risks.

12. The responsible entity should conduct ongoing liquidity assessments in different scenarios, which could include fund level stress testing, in line with regulatory guidance.

13. Responsible entities should have adequate and appropriate governance arrangements in place for their liquidity risk management processes, including clear decision-making processes for the use of liquidity management tools and other liquidity management measures in normal and stressed market conditions.

14. The responsible entity should put in place and periodically test contingency plans with an aim to ensure that any applicable liquidity management tools and liquidity management measures can be used where necessary, and if being activated, can be exercised in a prompt and orderly manner.

15. The responsible entity should ensure appropriate records are kept, and relevant disclosures made, relating to the performance of its liquidity risk management process.

16. The responsible entity should ensure that liquidity risk of CIS it manages and its liquidity risk management process, including the availability and use of liquidity management tools and liquidity management measures, are effectively disclosed to investors and prospective investors.

17. The responsible entity should publish clear disclosures of the objectives and operation (including design and use) of anti-dilution LMTs, quantity-based LMTs and other liquidity management measures to improve awareness among investors and enable them to better incorporate their potential use and the cost of liquidity into their investment decisions and mitigate potential adverse trigger effects.

: Changes made with reference to Revised FSB Recommendations or IOSCO ADT Guidance.

IOSCO Consultation Report on Liquidity Risk Management for CIS (November 2024)



Implementation Guidance

1. Responsible entities should holistically consider quantitative and qualitative factors to determine the liquidity of an OEF's assets and of the OEF's overall portfolio, both at the time of designing an OEF and on an ongoing basis.

2. Responsible entities should ensure that an OEF's redemption terms are consistent with its portfolio liquidity on an ongoing basis to reduce potential structural liquidity mismatches and consequently mitigate material investor dilution and any potential first mover advantage. Responsible entities should ensure the OEF is able to maintain the initial promise of liquidity disclosed to investors in normal and stressed conditions, taking into account the liquidity of underlying assets and overall portfolio, the investor base, and the effectiveness of liquidity management tools implemented by the OEFs.

3. Responsible entities should have appropriate internal systems, procedures and controls in place at all times in compliance with applicable regulatory requirements for the design and use of anti-dilution LMTs, quantity-based LMTs and other liquidity risk management measures, as part of the everyday liquidity risk management of their OEFs to mitigate material investor dilution and potential firstmover advantage arising from structural liquidity mismatch in OEFs

4. As part of their liquidity risk management framework, responsible entities should consider and use appropriate anti-dilution LMTs for OEFs under management (where appropriate as per the explanatory text set out below) to mitigate material investor dilution and potential first-mover advantage arising from structural liquidity mismatch in the OEFs they manage.

5. Anti-dilution LMTs used by responsible entities should impose on subscribing and redeeming investors the estimated cost of liquidity, i.e., explicit and implicit transaction costs of subscriptions or redemptions, including any significant market impact of asset purchases or sales to meet those subscriptions or redemptions. Independently of the anti-dilution LMT used, responsible entities should be able to demonstrate to authorities (in line with the authorities' supervisory approaches) that the calibration of the tool is appropriate and prudent for both normal and stressed market conditions.

6. If responsible entities set thresholds for the activation of anti-dilution LMTs, those thresholds should be appropriate and sufficiently prudent so as not to result in any material dilution impact on the fund.

7. As part of their liquidity risk management framework, responsible entities should consider and implement a broad range of quantity-based LMTs or other liquidity management measures for OEFs under management as part of their liquidity risk management.

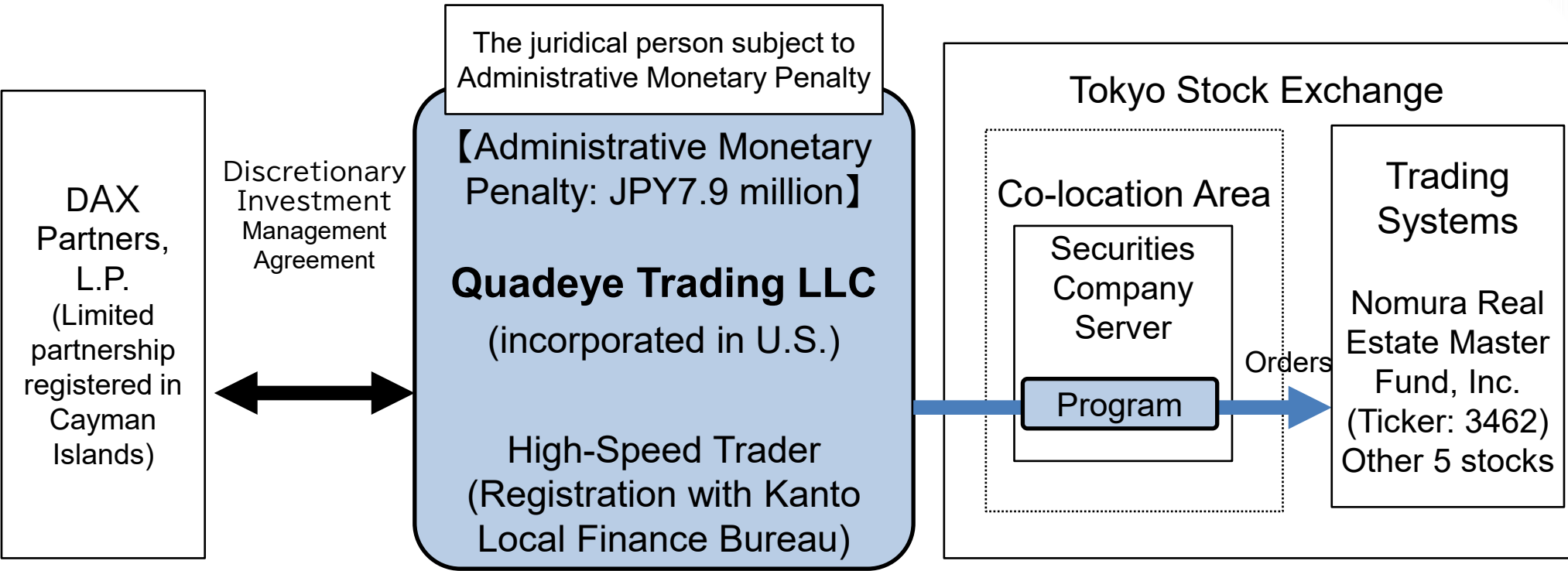
8. Responsible entities should have a clear decision-making process for the use of quantity-based LMTs and other liquidity management measures in the best interests of investors. In particular, the thresholds or criteria set (if any) for the activation of such tools and measures should be appropriate, objective and sufficiently prudent. Responsible entities should also regularly review the tools and measures currently in use and take all necessary steps to resume normal operations as soon as practicable.

9. Stress testing is an important component of a responsible entity's liquidity risk management process for an OEF. Responsible entity should appropriately design stress testing arrangements as set out in this section, taking into account the size, investment strategy, underlying assets, and investor profile of the OEF; the current and expected market conditions and other relevant market and regulatory factors.

: Guidance 4 to 6 are not open to consultation as they are carried forward from IOSCO ADT Guidance.

Recommendation for Administrative Monetary Penalty Payment Order for Use of Fraudulent Means with High Speed Trading by Quadeye Trading LLC

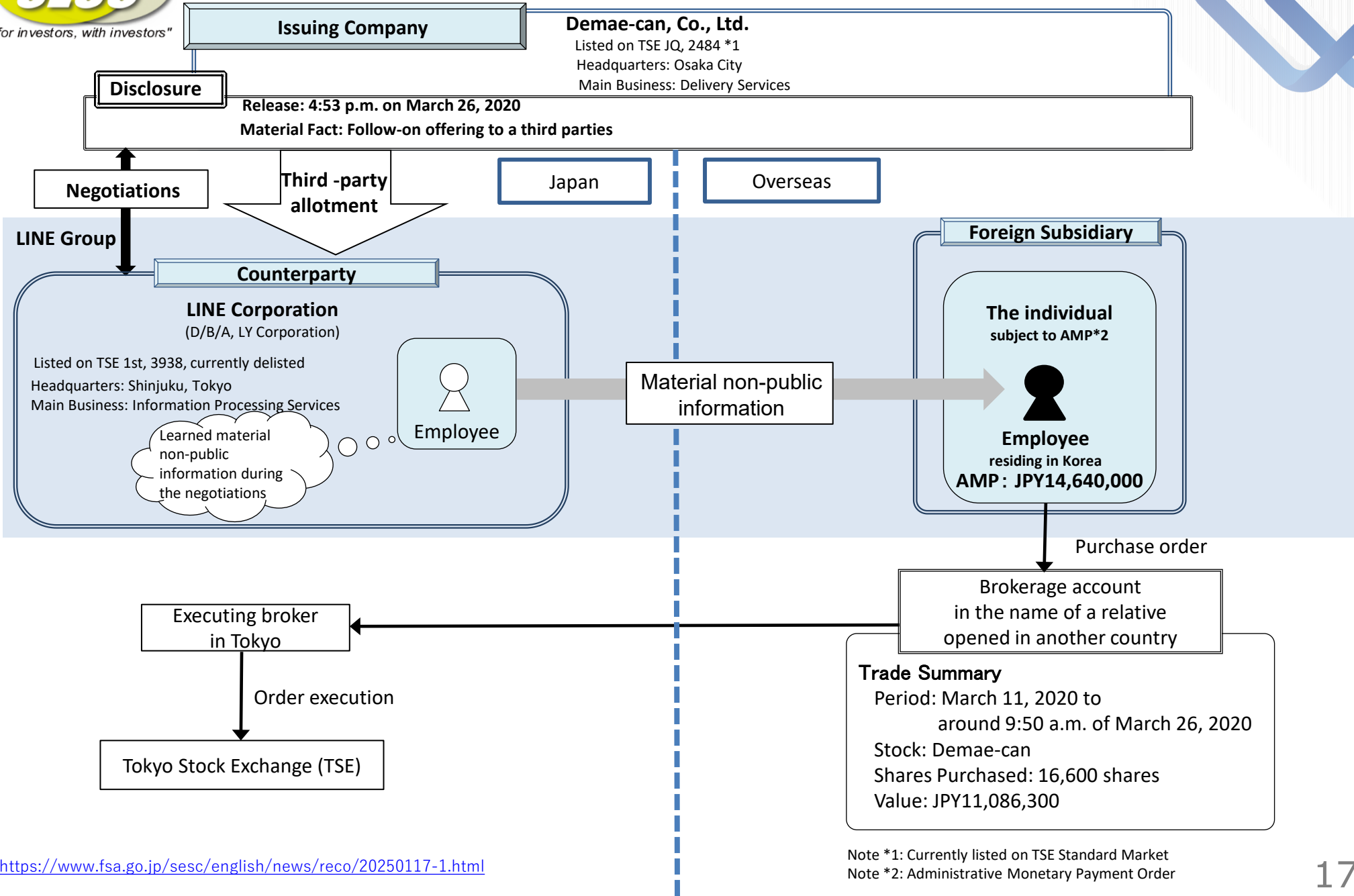
Summary of Misconduct





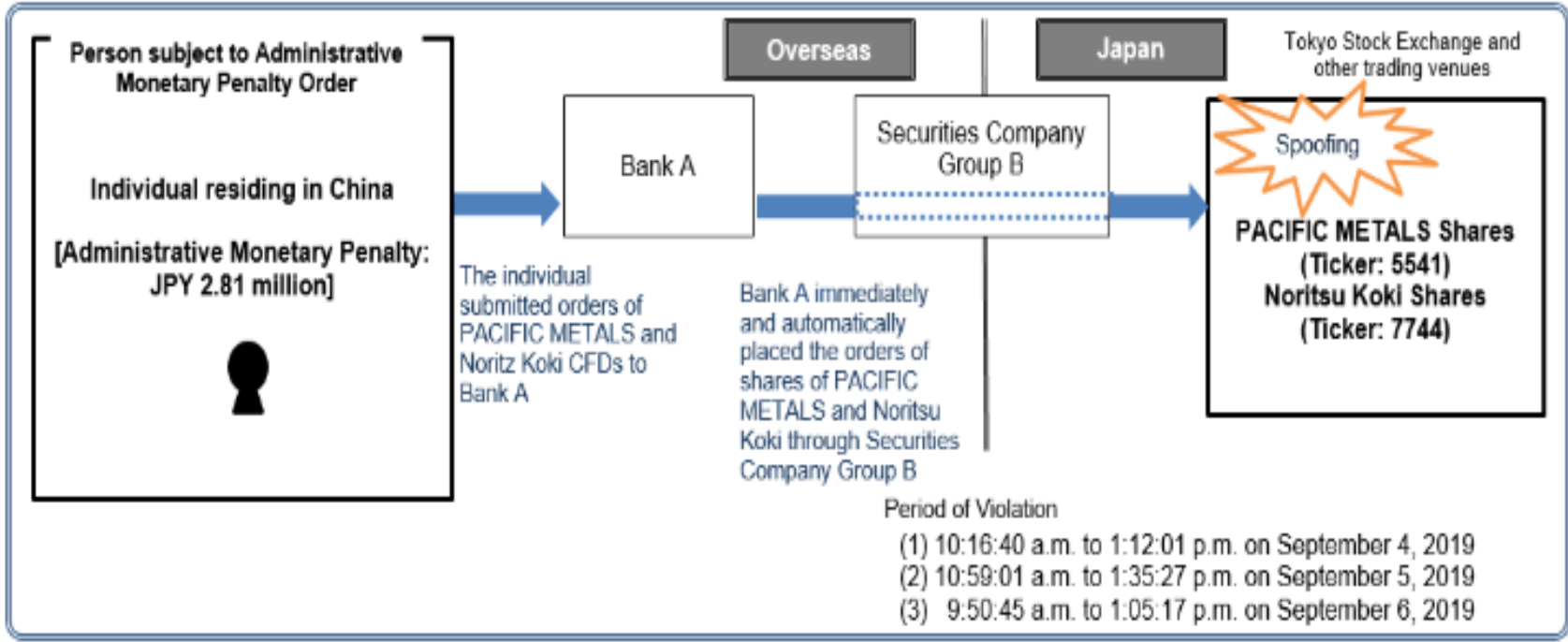
3. Conducting thorough monitoring to tackle cross-border market misconduct

Recommendation for Administrative Monetary Penalty Payment Order for Insider Trading
in Shares of Demae-can Co., Ltd. by an Individual Residing Abroad



Note *1: Currently listed on TSE Standard Market
Note *2: Administrative Monetary Payment Order

Recommendation for Administrative Monetary Penalty Payment Order for Market Manipulation in Shares of PACIFIC METALS CO., LTD. and Other Securities by an Individual Residing Abroad

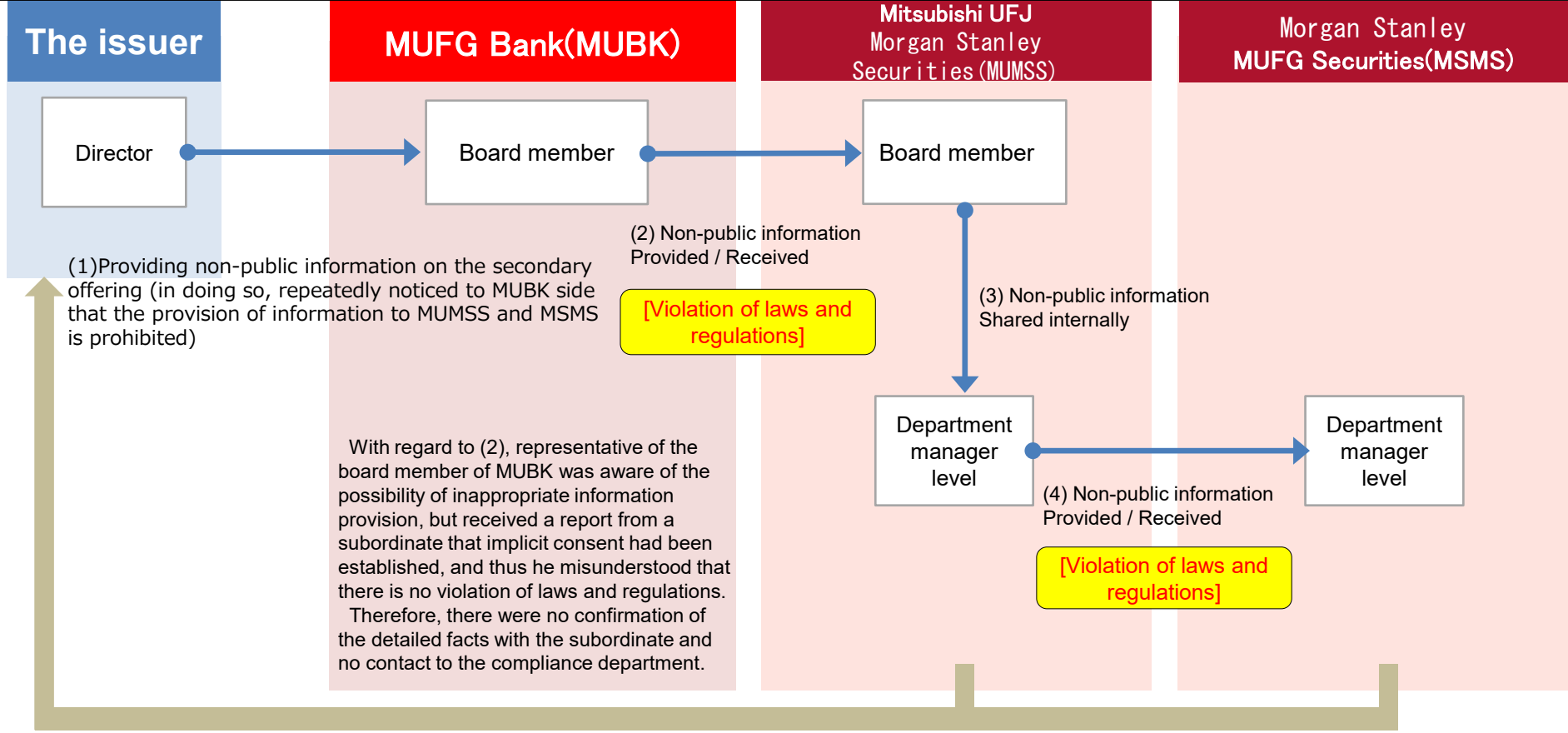




4. Solidifying substantive measures of compliance

Recommendation for Administrative Disciplinary Action against Inappropriate sharing of customer information

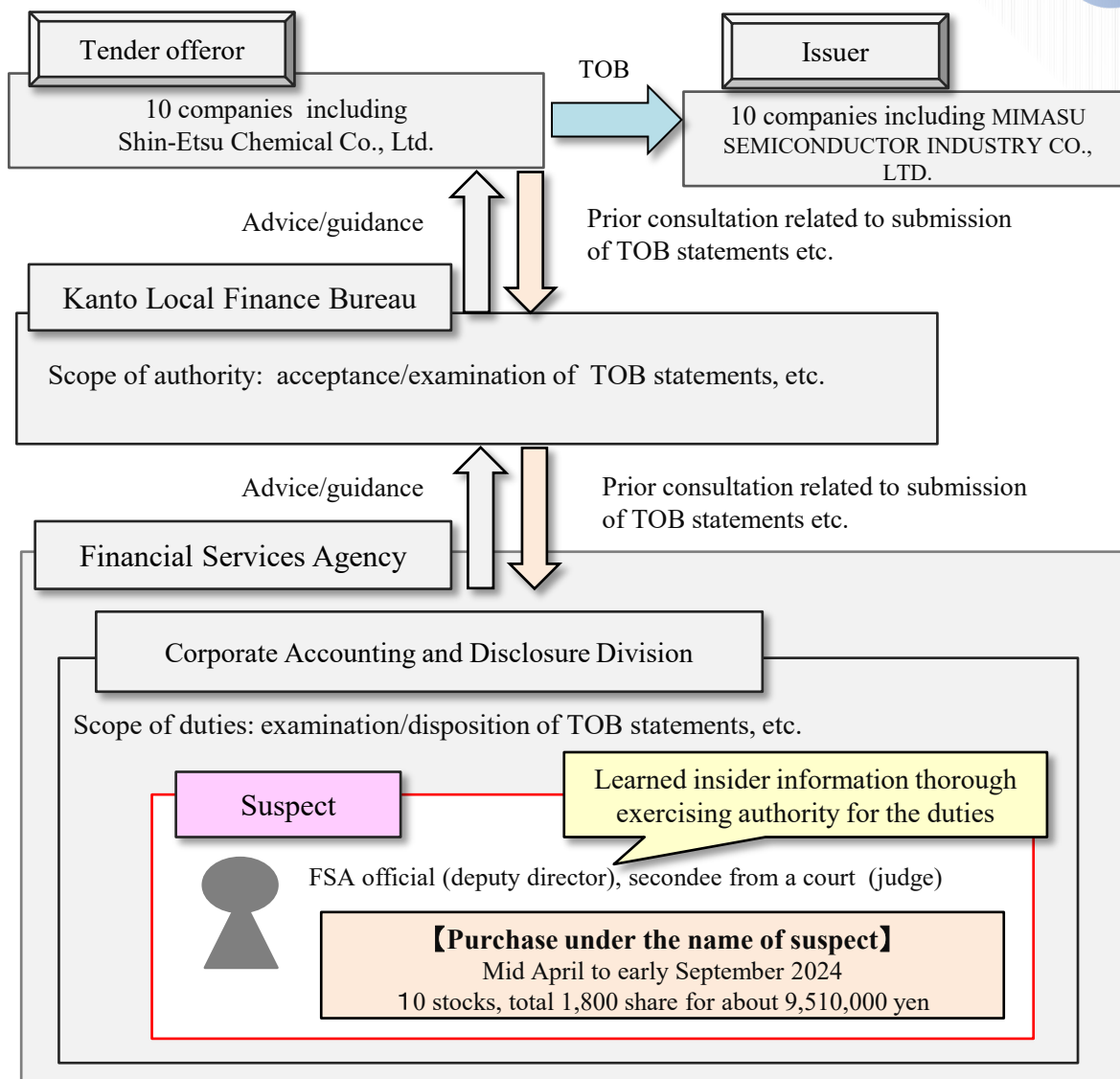
- The Financial Instruments and Exchange Act prohibits a Financial Instruments Business Operator from providing and/or receiving non-public client information among financial firms within the same group, without the consent of the client.
- Nevertheless, three firms (MUBK, MUMSS, MSMS) repeatedly exchanged non-public client information knowing that the clients had refused to share their information with other group firms, and some of the information contained material information that would impact investment decisions.
- These findings led to the conclusion that the three firms had deficiencies in control environment for the management of information, and the information received was used to solicit the client.





Summary of the case

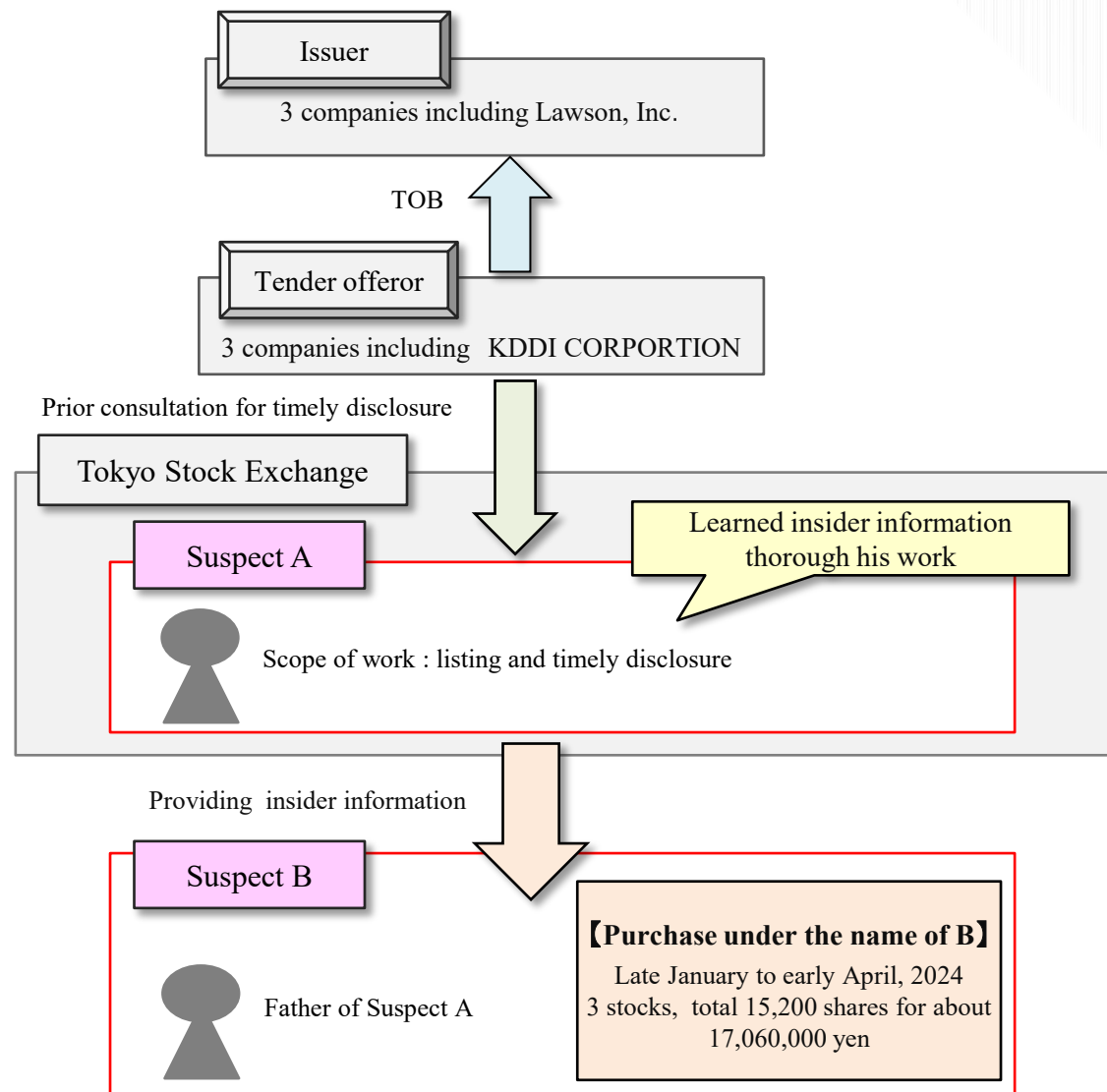
- On December 23, 2024, SESC filed a criminal charge against Financial Services Agency Official, who was a judge seconded from a court, for insider trading.
- The suspect was engaged in examination and disposition of TOB statements at FSA and learned the launch of 10 companies' TOB (insider information) through exercising authority for the duties.
- The suspect purchased the companies' stocks under the name of the suspect prior to the announcement of the information, despite of no applicable exemption clause under the FIEA.





Summary of the case

- On December 23, 2024, SESC filed criminal charges against Tokyo Stock Exchange (TSE) staff (suspect A) and his father (suspect B)
- Suspect A's scope of work at TSE was issues related to listing and timely disclosure, and through his work he learned the launch of three companies' TOB (insider information).
- Prior to the announcement of the information, Suspect A provided the information to Suspect B with an intent to have Suspect B gain profits by having Suspect B purchase the stocks.
- By receiving the information from Suspect A, Suspect B purchased the companies' stocks under the name of Suspect B prior to the announcement of the information, despite of no applicable exception clause under the FIEA.





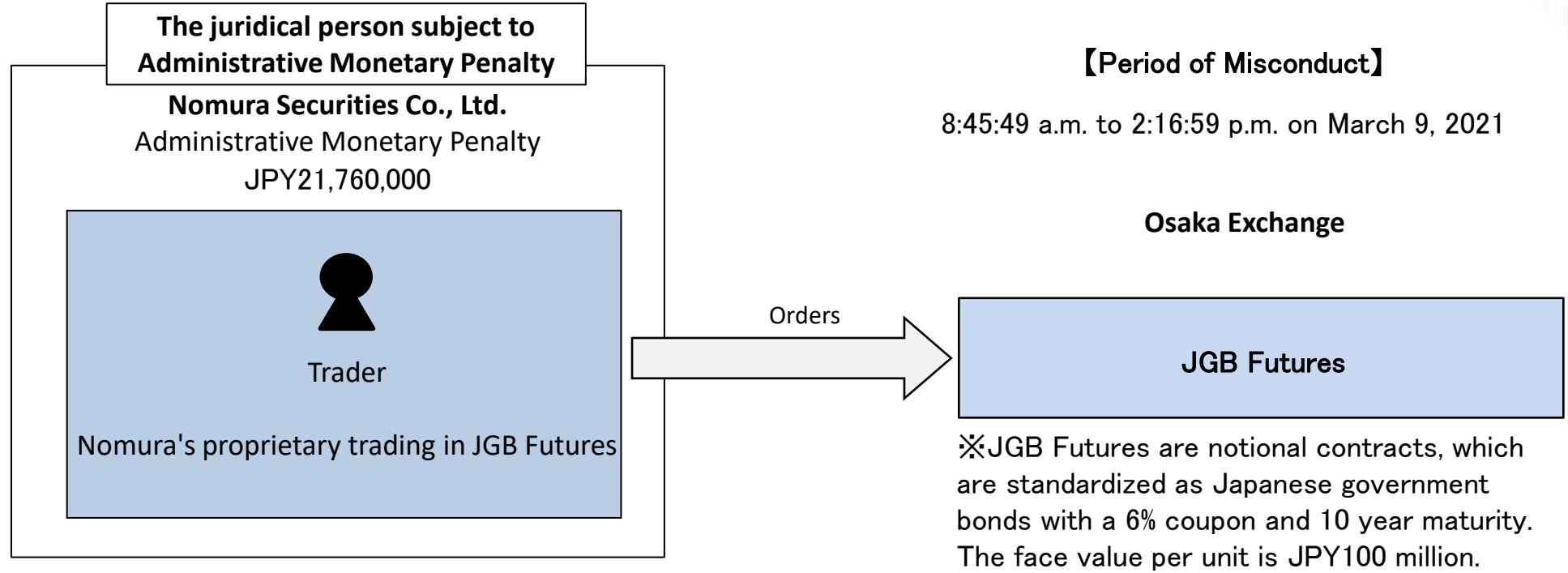
5.Securing market fairness and transparency of professional market

Recommendation for Administrative Monetary Penalty Payment Order for Market Manipulation in JGB Futures by Nomura Securities Co., Ltd.



(1)

Summary of Misconduct



Characteristics

- Cancellation ratio of layered orders: 98%
- Occupancy ratio of layered orders within the best 5 ticks: Maximum 74% on the bid and 70% on the offer; Average 47%

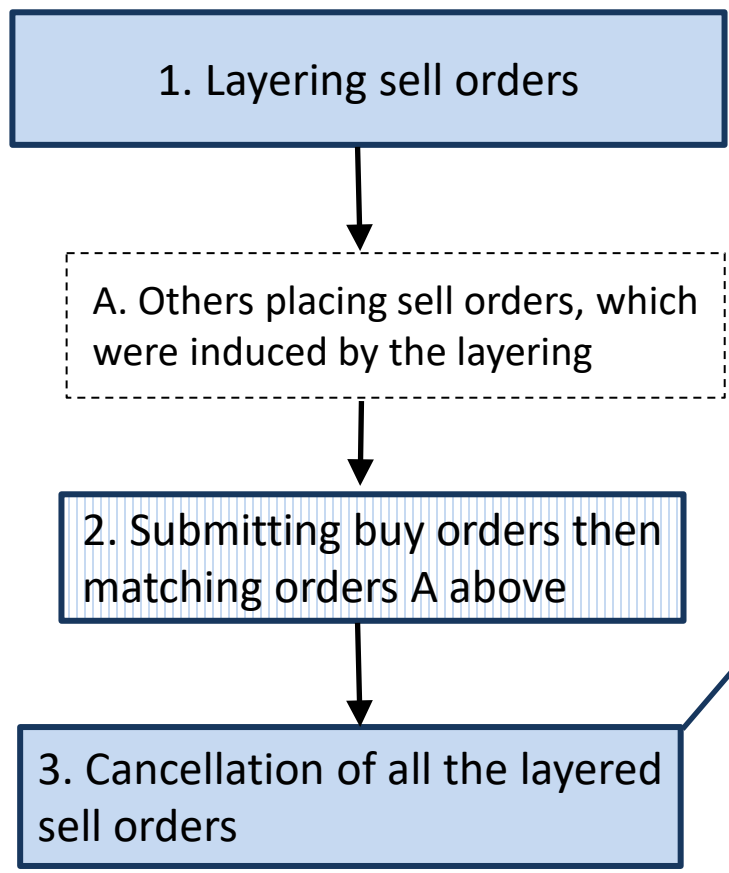


(2)

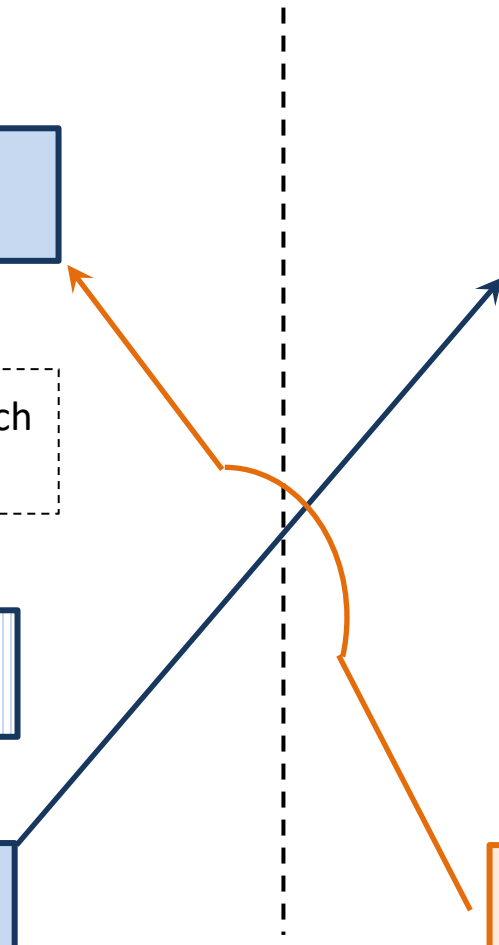
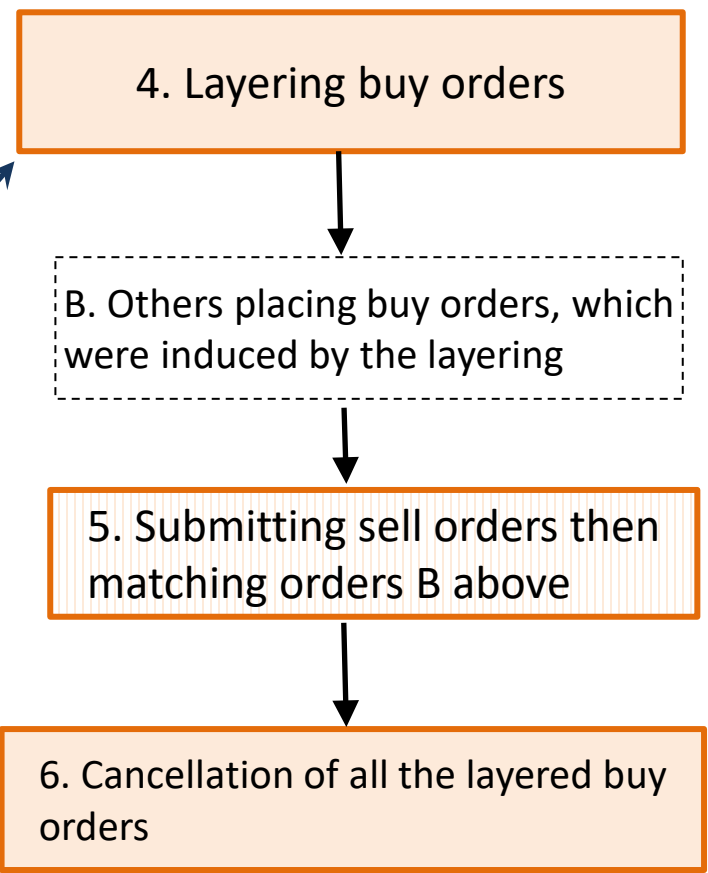
Summary of Misconduct

Example of Trading Behavior

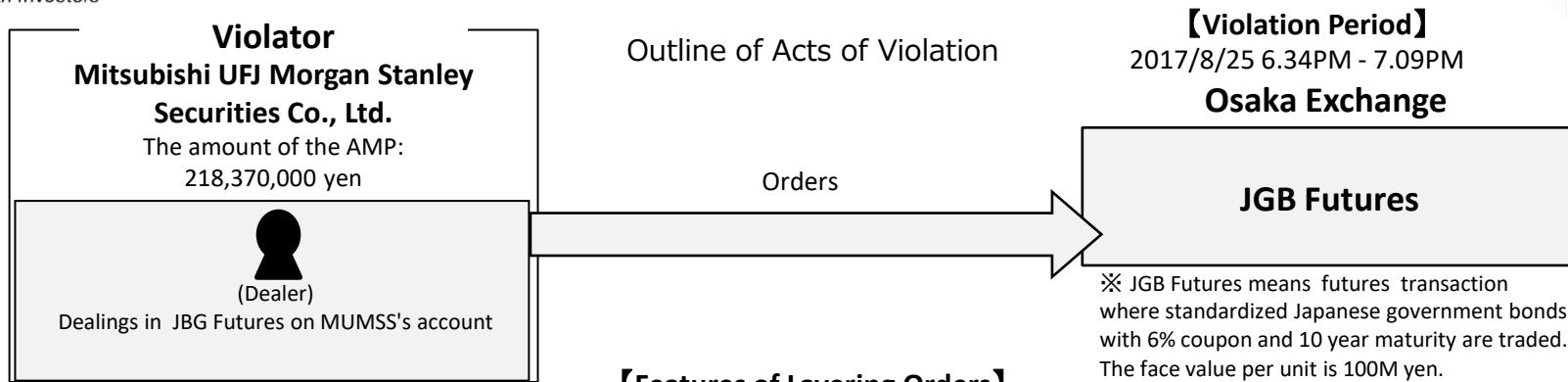
Buying at a lower Price



Selling at a higher price



The market manipulation by securities company's dealer of JGB Futures by the use of layering

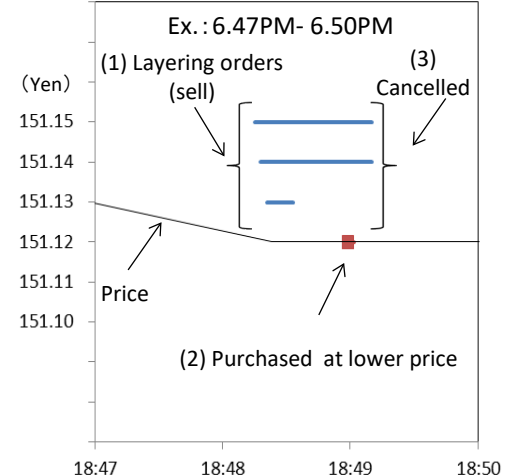
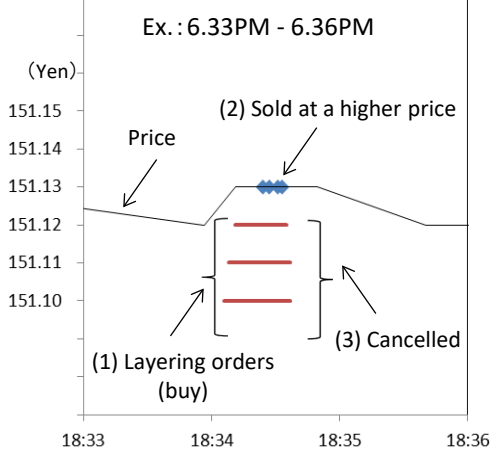


- 【Features of Layering Orders】**
- Execution rate of layering orders: 0 % (buy, sell)
 - Occupancy rate (within 5 ticks): max. approx. 64 % (buy), max. approx. 57 % (sell), avg. 48 % (buy, sell)
 - Scale of layering orders (one cycle) : 200 - 850 units (buy), 100 - 600 units (sell)

【A Method of Layering Orders】

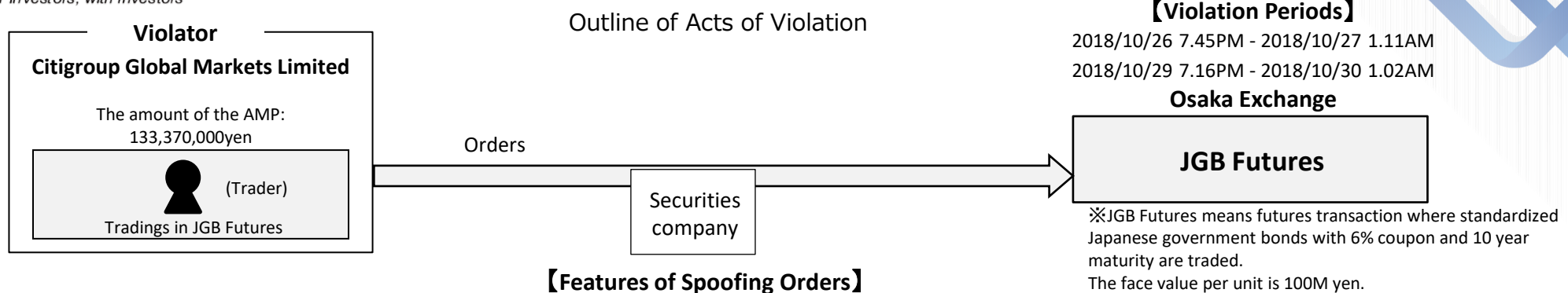
- | A series of layering orders (buy) | A series of layering orders (sell) |
|---|--|
| (1) Placed layering orders on the buy side (→other investors were misled to place buy orders at higher prices) | (1) Placed layering orders on the sell side (→other investors were misled to place sell orders at lower prices) |
| (2) Placed sell orders and had the orders executed with the misled other investors' buy orders | (2) Placed buy orders and had the orders executed with the misled other investor's sell orders |
| (3) Cancelled above (1) orders within few seconds after the above (2) execution | (3) Cancelled above (1) orders within few seconds after the above (2) execution |

Images of layering orders and transition of prices (※)



(※) The images were extracted and simplified.

Market manipulation by foreign financial institution's trader of JGB Futures by use of spoofing



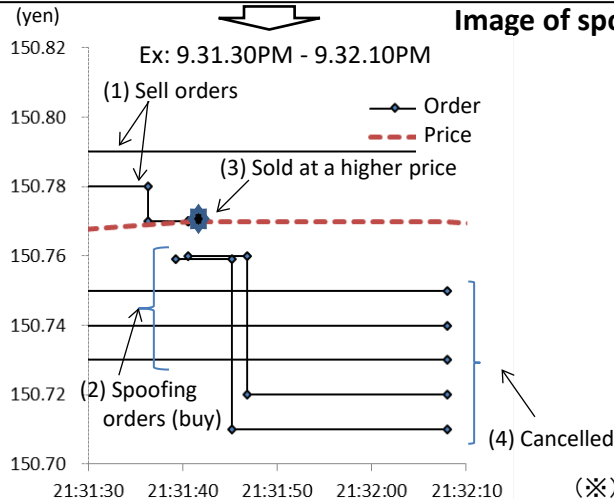
【Features of Spoofing Orders】

- Execution rate of spoofing orders: 0.08% (buy, sell)
- Occupancy rate (within 5 ticks): max. approx.69%(buy), max. approx.66% (sell), avg. 48%(buy, sell)
- Scale of spoofing orders (one cycle): 150~1,625 units (buy), 100~950 units (sell)

【A Method of Spoofing Orders】

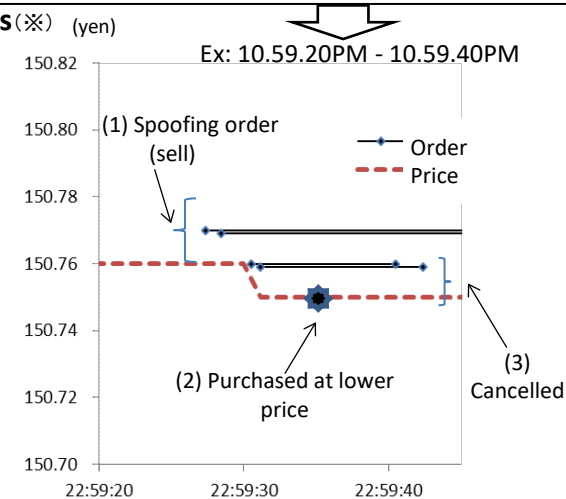
A series of spoofing orders (buy)

- (1) Placed small sell orders
- (2) Placed spoofing orders on the buy side
(→other investors were misled to place buy orders at higher prices)
- (3) Sell orders (1) above were executed with the misled other investors' buy orders
- (4) Cancelled above (2) orders within a few seconds after the above (3) execution

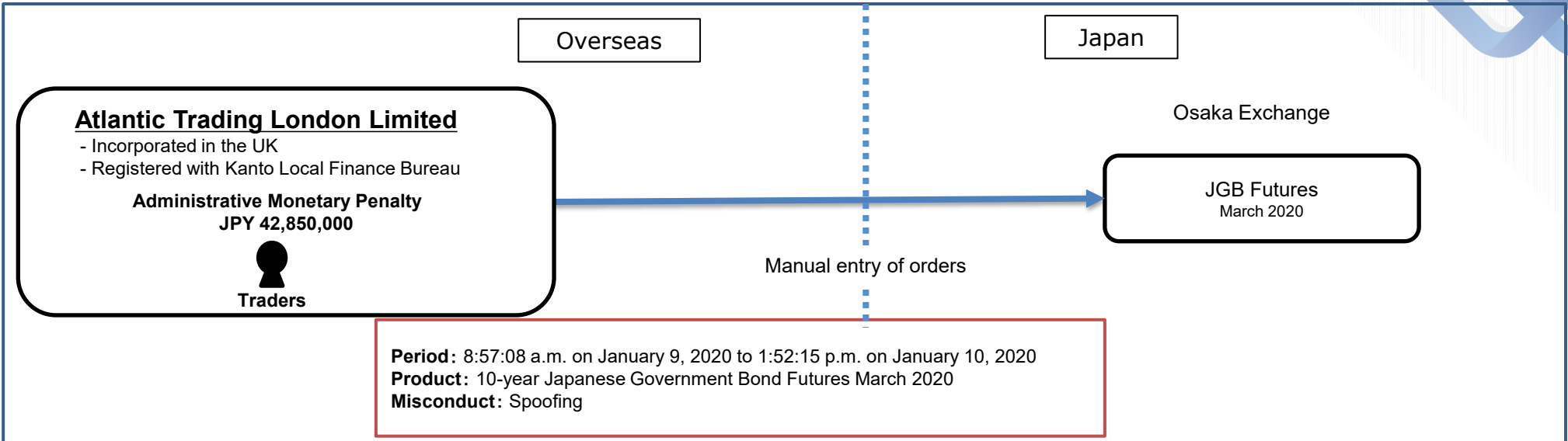


A series of spoofing orders (sell)

- (1) Placed spoofing orders on the sell side
(→other investors were misled to place sell orders at lower prices)
- (2) Placed buy orders and had the orders executed with the misled other investor's sell orders
- (3) Cancelled above (1) orders within a few seconds after the above (2) execution



Summary of Misconduct



1. Characteristics of Spoofing

- Limit price: typically at one tick inferior to the best bid/offer ("one tick away")
- Volume: a total of 100 or more contracts by placing multiples of 20 or more per order
- Order book share: typically dominated in half of bid/offer by the depth within one tick away
- Order life time: typically 2 seconds
- Execution ratio: zero

2. Behavior

1. Small orders: Placement of bona fide small orders at the best bid/offer
2. Large orders: Placement of large orders, a total of 100 or more contracts typically at one tick away on the opposite side
3. Execution of small orders: Execution of the small orders, which were crossed by others induced
4. Cancellation of large orders: Cancellation of all the large orders

- Pre-hedging is used by dealers to manage risks associated with anticipated wholesale principal orders in relation to primary market offerings and secondary market transactions. This can occur across various markets, including securities and derivatives, on trading venues and over the counter (OTC) markets. It encompasses a range of asset classes such as equities, fixed income, currencies and commodities.
- The Consultation Report offers a definition of pre-hedging and proposes a set of recommendations to guide regulators in determining acceptable pre-hedging practices and managing the associated conduct risks effectively.

Proposed definition

“trading undertaken by a dealer, in compliance with applicable laws and rules, including those governing frontrunning, trading on material non-public information/insider dealing, and/or manipulative trading where:

- (i) the dealer is dealing on its own account in a principal capacity;
- (ii) the trades are executed after the receipt of information about an anticipated client transaction and before the client (or an intermediary on the client’s behalf) has agreed on the terms of the transaction and/or irrevocably accepted an executable quote; and
- (iii) the trades are executed to manage the risk related to the anticipated client transaction.”

A. Cumulative recommendations for circumstances when pre-hedging is acceptable

Consistent with any existing jurisdictional obligations:

- **A1:** Dealers should undertake pre-hedging only for a genuine risk management purpose.
- **A2:** Dealers should (i) act fairly and honestly to clients and (ii) undertake pre-hedging only with the intention to benefit the client.
- **A3:** Dealers should (i) minimise market impact and (ii) maintain market integrity when pre-hedging.

B. Recommendations for managing conduct risk from pre-hedging

Consistent with any existing jurisdictional obligations:

- **B1:** The dealer should document and implement appropriate policies and procedures for pre-hedging.
- **B2:** The dealer should provide clear disclosure to clients of the dealer’s pre-hedging practices.
- **B3:** The dealer should obtain prior consent from the client.
- **B4:** The dealer should implement appropriate compliance and supervisory arrangements for pre-hedging including: i. Supervisory systems and reviews; and ii. Trade and communications monitoring and surveillance.
- **B5:** Dealers should appropriately manage access to and prohibit misuse of confidential client information and adequately manage any conflicts of interest that may arise in relation to pre-hedging. Dealers should consider establishing, monitoring, and regularly reviewing appropriate physical and electronic information controls to align with changes to the dealer’s business risk profile.
- **B6:** The dealer should maintain adequate records of pre-hedging to facilitate supervisory oversight, monitoring and surveillance.



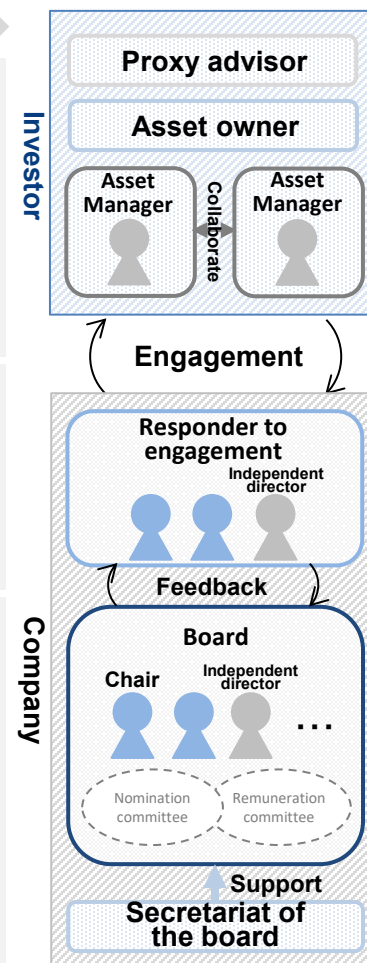
6. Promoting dialogues between investors and companies and ensuring the effective implementation of the Large Shareholder Reporting rule

Action Program for Corporate Governance Reform 2024: Principles into Practice

"for investors, with investors"

- Various initiatives are taken based on the "Action Program for Accelerating Corporate Governance Reform" established in April 2023. It is necessary to follow-up on the progress of each measure and consider the future initiatives continuously.
- Going back to the spirit of the Codes, which is to ensure **sustainable corporate growth and increased corporate value over the mid- to long- term**, the following initiatives should be undertaken for putting corporate governance reform **"into practice"** based on self-motivated changes in the mindsets of companies and investors through examining and sharing specific measures.

| Issues | Follow up | Future Initiatives |
|--|---|--|
| Effective implementation of stewardship activities | <ul style="list-style-type: none"> ✓ The law to amend the Financial Instruments and Exchange Act, including clarification of the scope of "joint holders" in the large shareholding reporting rule, was enacted (in May 2024). | <ul style="list-style-type: none"> ✓ Consider the revision of the Stewardship Code with the aim of promoting collective/collaborative engagements that contribute to constructive and purposeful dialogues and ensure the transparency of beneficial shareholders. ✓ Assess compliance with the Stewardship Code by investors (asset managers, asset owners, proxy advisors, etc.) |
| Improvement of the effectiveness of the board | <ul style="list-style-type: none"> ✓ Published "The Basics of Being an Independent Director" to ensure and improve the quality of independent directors (in January 2024). ✓ The private sector continues to conduct educational activities for directors. | <ul style="list-style-type: none"> ✓ Share specific examples of efforts, such as dialogues between independent directors and investors and encouragement for substantive discussions by the secretariats of boards, in order to promote the implementation of efforts to improve the effectiveness of boards. |
| Encouraging the management with an awareness of profit-making and growth | <ul style="list-style-type: none"> ✓ "Visualized" companies that make efforts in order to implement management that is conscious of the cost of capital and stock prices, including PBR, based on the request from the TSE (from January 2024). | <ul style="list-style-type: none"> ✓ Follow up on the status of each company's initiatives continuously to encourage them to take substantial measures. In doing so, focus on whether boards are committed to the initiatives proactively and actively, whether specific discussions are conducted during dialogues with investors and whether analyses and evaluations are conducted with an awareness of specific outcomes from the perspective of increasing corporate value over the mid- to long-term occur. |





| Issues | Follow up | Future Initiatives |
|---|--|---|
| Enhancing the quality of disclosure and promoting dialogues with global investors | <ul style="list-style-type: none"> ✓ Requested to disclose information about dialogues with investors, and published sufficient and insufficient cases of explanations (in March 2023). ✓ Revised the TSE's Listing Rules toward mandatory English disclosures (financial results and timely disclosure information) from April 2025 (in May 2024). | <ul style="list-style-type: none"> ✓ Examine actual situations and advance discussions on the development of an environment, including enhancing the efficiency of disclosures of duplicate information in Annual Securities Reports and Business Reports, that will lead companies to disclose Annual Securities Reports before general shareholder meetings, in addition to enhancing timely disclosures. ✓ Publish a specific list in order to "visualize" the group of companies that willingly and actively respond to the expectations of global investors. |
| Resolving market environment issues | <ul style="list-style-type: none"> ✓ Requested the enhancement of information disclosures of quasi-controlled listed companies (in December 2023). ✓ Published issues and good practices regarding disclosures of cross-shareholdings (in March 2024). | <ul style="list-style-type: none"> ✓ Encourage companies to examine their rationale of cross-shareholdings in light of the Corporate Governance Code (e.g. whether appropriate disclosures based on actual situations be made in the Annual Securities Reports) to avoid a formalistic response. |
| Encouraging the management with an awareness of sustainability issues | <ul style="list-style-type: none"> ✓ Added metrics on diversity such as the ratio of women in managerial positions and the gender pay gap in Annual Securities Reports (from the fiscal year ended March 31, 2023). ✓ Published a booklet of companies' good disclosure practices on sustainability issues such as human capital (in December 2023). ✓ Amended the TSE's Listing Rules to set numerical targets for the ratio of female executives at companies (at least 30% by 2030) (in October 2023). | <ul style="list-style-type: none"> ✓ Discuss disclosures and assurances of the sustainability-related information while ensuring international comparability. ✓ Share specific good examples such as the awareness of the outcome of increasing corporate value as well as management and dialogues with an awareness of corporate culture. |

(The image of a list)
The status of JPX Prime 150 Index
Constituent Stocks

| Company name | Status of various indicators | | Governance items expected by global investors | |
|--------------|------------------------------|-----|---|--------------------------------|
| | PBR (times) | | Ratio of Independent Directors (%) | Ratio of female executives (%) |
| A | 2.5 | | 37.5 | 18.2 |
| B | 1.1 | | 41.7 | 8.3 |
| C | 1.2 | | 44.4 | 23.1 |
| D | 1.2 | ... | 44.4 | 22.2 |
| E | 5.3 | | 33.3 | 13.3 |
| F | 5.8 | | 66.7 | 22.2 |
| G | 1.8 | | 60.0 | 20.0 |
| H | 6.7 | | 40.0 | 13.3 |
| I | 15.8 | | 37.5 | 16.7 |

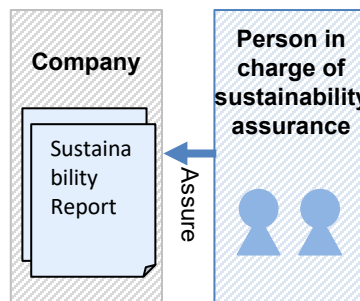
Annual Securities Report

Part 1: Company Information

...

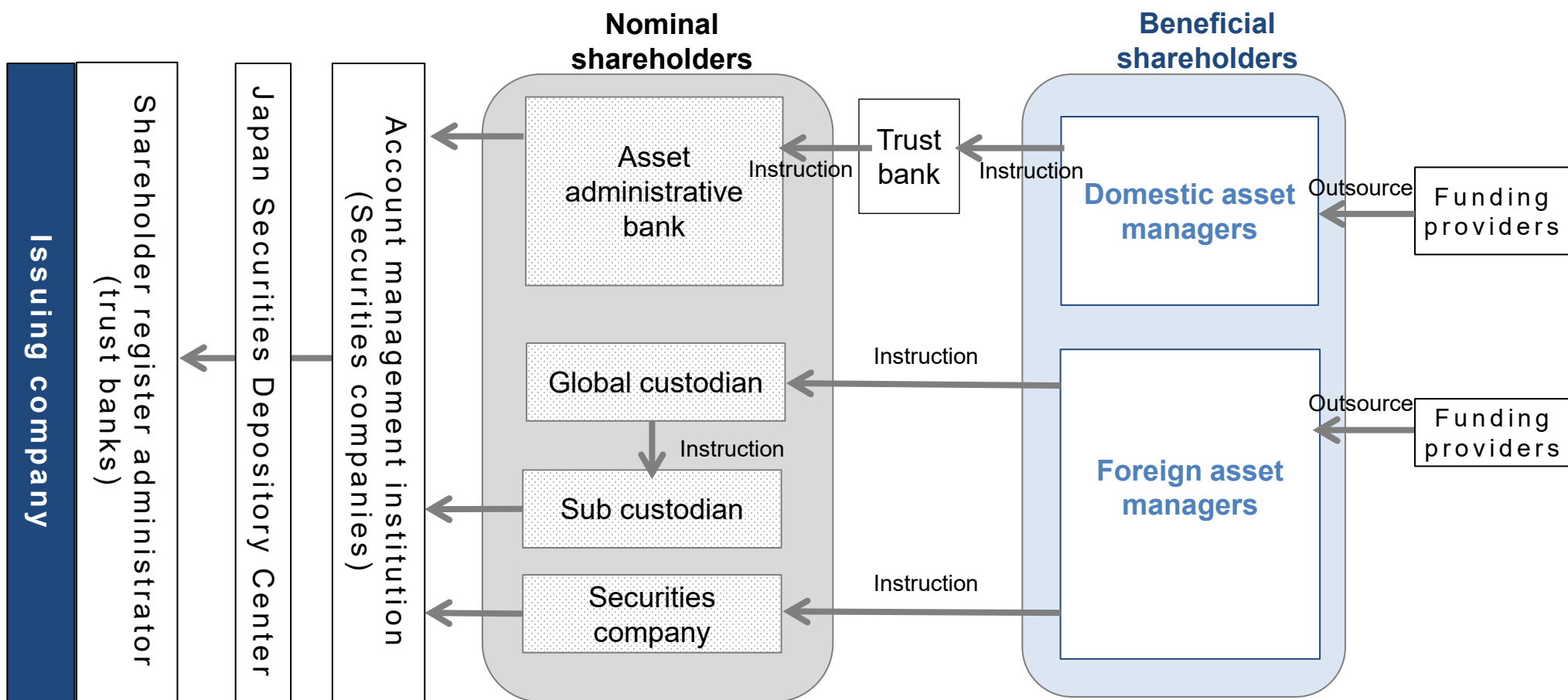
IV. Information on the Company Submitting Financial Reports

The purpose of holding each issue of cross-shareholdings is not stated specifically.



Stakeholders on the shareholder registration

- Shareholder registration involves a number of stakeholders. In cases where shares are held by financial institutions (e.g., banks as well as life and non-life insurance companies), business companies and individuals, shareholders on the register are equated to beneficial shareholders (i.e., a person who has the authority to direct voting rights and invest). In other cases, however, the names of institutional investors who are beneficial shareholders do not appear on the shareholder register.
- Many companies outsource the survey of domestic and overseas shareholder identification.



- ❑ To promote constructive dialogue from a mid- to long-term perspective, the scope of “joint holders” is to be clarified

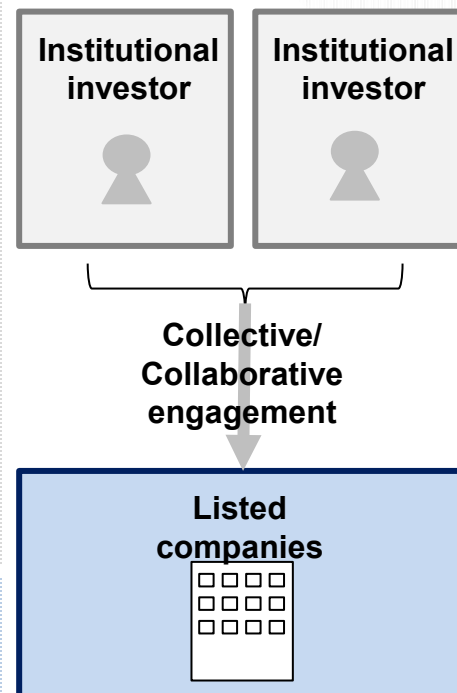
Issues and policy measures

Issues

- As investors are expected to engage in dialogue with companies based on their in-depth understanding of individual companies, it is important to compensate for the lack of investors’ qualitative and quantitative resources and increase the effectiveness of dialogue by means of collective or collaborative engagement.*
 - * Refers to the effort to engage in dialogue with individual companies in collaboration with other institutional investors about specific topics
- However, it is pointed out that joint holders as defined under the large shareholding reporting rule may have room for legal ambiguity and hinder collective or collaborative engagement.
 - ※ If two or more investors (Investor A:X%, Investor B:Y%) fall under the category of “joint holders” (i.e. persons who have agreed to jointly exercise voting rights and other rights as shareholders) and the combined ownership ratio (X%+Y%) exceeds 5%, they will be required to submit a large shareholding report.

Policies

- In light of promoting constructive dialogue from a mid- to long-term perspective, the scope of “joint holders” is to be clarified at the level of acts.



Law revision

Clarifying “joint holders” in relation to the Large Shareholding Reporting Rule

- **Unless two or more investors reach an agreement which would have a material impact on a company’s management,* they should not be required to aggregate their ownership ratio as “joint holders”**

* Assuming a case where two or more investors jointly make a proposal that is not directly related to corporate control, such as a change in dividend policies or capital policies

(Ref.) On the other hand, in order to appropriately respond to cases that may threaten the fairness of the capital market, such as cases in which two or more investors stealthily failed to submit reports, a cabinet order is to be revised to deem a joint holder when there are certain external facts, such as an officer concurrent position relationship and a funding relationship.



- It has been pointed out that the effective implementation of the large shareholding reporting rule has not been ensured.

Comments on the Current Rule

- With the amendment of the Financial Instruments and Exchange Act in 2008, non-submission of the large shareholding report and false statements were subject to the administrative monetary penalty rule from the viewpoint of deterring violations of the large shareholding reporting rule.
- However, there has been a number of cases in which the submission of reports has been delayed, and it has been pointed out that the effective implementation of the large shareholding reporting rule has not been ensured.

Submission of the large shareholding report

| | |
|---|-------------------------------|
| Number of submissions of the large shareholding report (Note 1) | Approx. 14,000 cases per year |
| Number of late submissions (Note 2) | Approx. 1,500 cases per year |
| Number of administrative monetary penalty payment orders (Note 3) | Total 8 cases |

Main reasons for late submission (Note 4)

- Ignorance and insufficient understanding of laws and regulations
- Not familiar with EDINET operation
- Delay in fact-finding

(Note 1) Average from 2019 to 2022.
 (Note 2) Average number of reports submitted after the due date from 2019 to 2022.
 (Note 3) Number of cases from 2008 to 2022.
 (Note 4) Based on interviews conducted by local finance bureaus with persons whose submission of a report was delayed.

Enforcement of Large Shareholder Reporting(1)



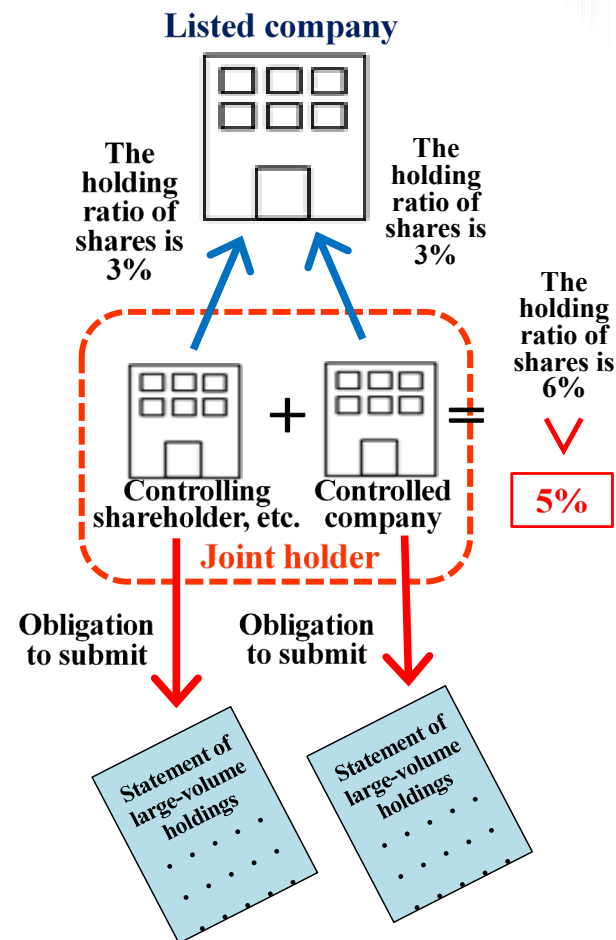
- Do you properly submit statements of large-volume holdings and statements of changes?

A holder whose holding ratio of share certificates, etc. issued by a listed company has exceeded 5% must submit a statement of large-volume holdings, in principle within five business days.

Thereafter, the holder whose holding ratio has changed by 1% or more must submit a statement of changes, in principle within five business days.

The holding ratio of share certificates, etc. must be calculated by the sum of the number of share certificates, etc. that are held by the holder and the joint holder(s).

A joint holder is a person who has agreed to jointly acquire or transfer the share certificates, etc., or to jointly exercise voting rights or other rights as the issuer's shareholders with other holders. Even if such agreement has not been made, joint holders include a company that holds the majority of voting rights in a company and that company, and companies that have the same controlling shareholder, etc.



Enforcement of Large Shareholder Reporting(2)

- **Violation of the large-volume holding reporting system is subject to penalty, including non-residents.**

SESC has made the following recommendations for administrative monetary penalty payment orders against a person that has violated the large-volume holding reporting system.

- Recommendation for Administrative Monetary Penalty Payment Order for Violation of Disclosure Requirements by Large-Volume Holders of Shares of MITSUBOSHI CO., LTD. (June 28, 2024)
<https://www.fsa.go.jp/sesc/english/topics/20240807.html#topics04>
- Recommendation for Administrative Monetary Penalty Payment Order for Violation of Disclosure Requirements by Large-Volume Holders of Shares of SAKAI Holdings CO.,LTD (September 10, 2024)
<https://www.fsa.go.jp/sesc/english/topics/20241017.html#topics02>

In addition, **the SESC announced that will also take proactive actions against non-traditional and new types of violations** that may threaten market fairness (such as legally-evasive large volume holding) in its Strategy & Policy 2023-2025 (published in January 2023). The SESC will conduct disclosure inspections for violations of disclosure regulations, including the large-volume holding reporting system, to ensure appropriate disclosure.



II. Reference

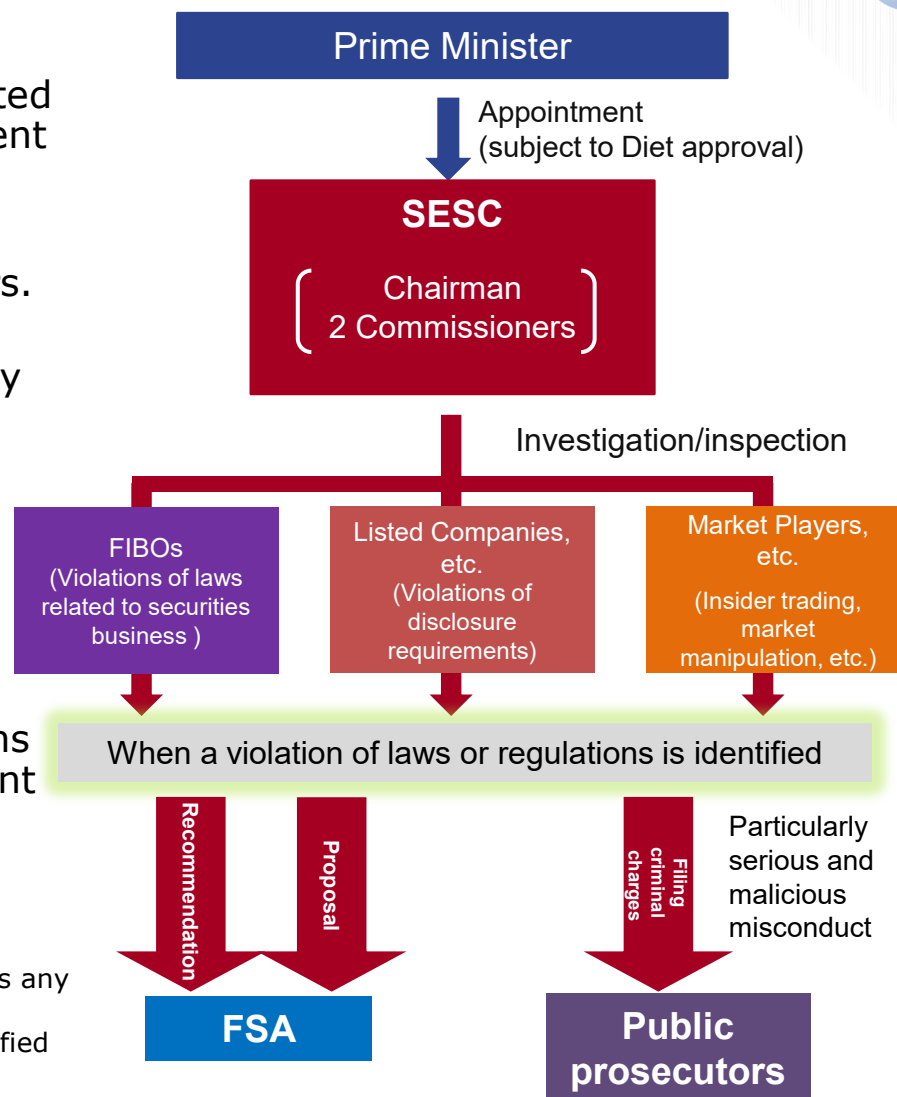


1.Basic information of SESC

Objectives of the SESC

- ◆ The SESC is a collegiate organization within the FSA, founded in 1992.
- ◆ A Chairman and two Commissioners are appointed by the Prime Minister and function as independent agents. (Term of office: 3 years)
- ◆ The SESC aims to ensure the fairness and transparency of markets and to protect investors.
 - Inspections of violations of laws and regulations related to securities business by Financial Instruments Business Operators (FIBOs)*
 - Investigations of market misconduct, including insider trading and market manipulation
 - Inspections of violations in disclosure requirements by listed companies
 - Recommendations for administrative actions or administrative monetary penalty payment orders, policy proposal, or filing criminal charges based on the results of the above investigations or inspections

* "FIBOs" stands for Financial Instruments Business Operators and includes any business operator subject to inspections, such as registered financial institutions, financial instruments intermediary service providers, and qualified institutional investors



Chairman and Commissioners of the SESC



**Commissioner
KATO Sayuri**

KATO Sayuri was appointed as SESC Commissioner in December 2019 (reappointed in 2022). Previously, she served as Director of the Consumer Affairs Agency, Vice-Governor of Nagano Prefecture, and Executive Vice President of the National Consumer Affairs Center of Japan.

**Chairman
NAKAHARA Ryoichi**

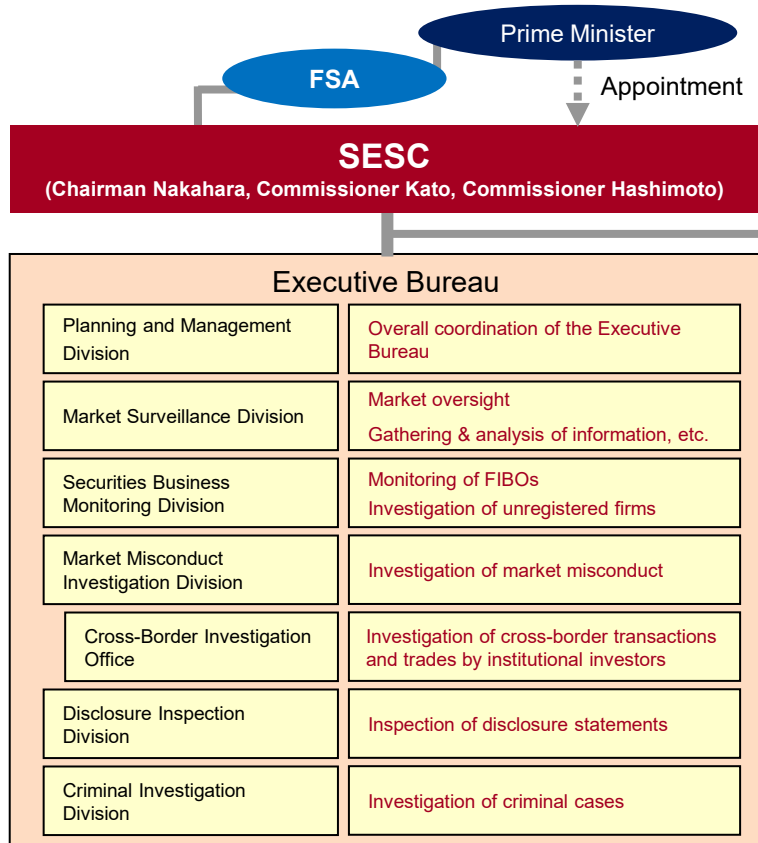
NAKAHARA Ryoichi was appointed as SESC Chairman in December 2022. Previously, he served as the Chief Public Prosecutor of the Hiroshima and Fukuoka High Public Prosecutors Offices.

**Commissioner
HASHIMOTO Takashi**

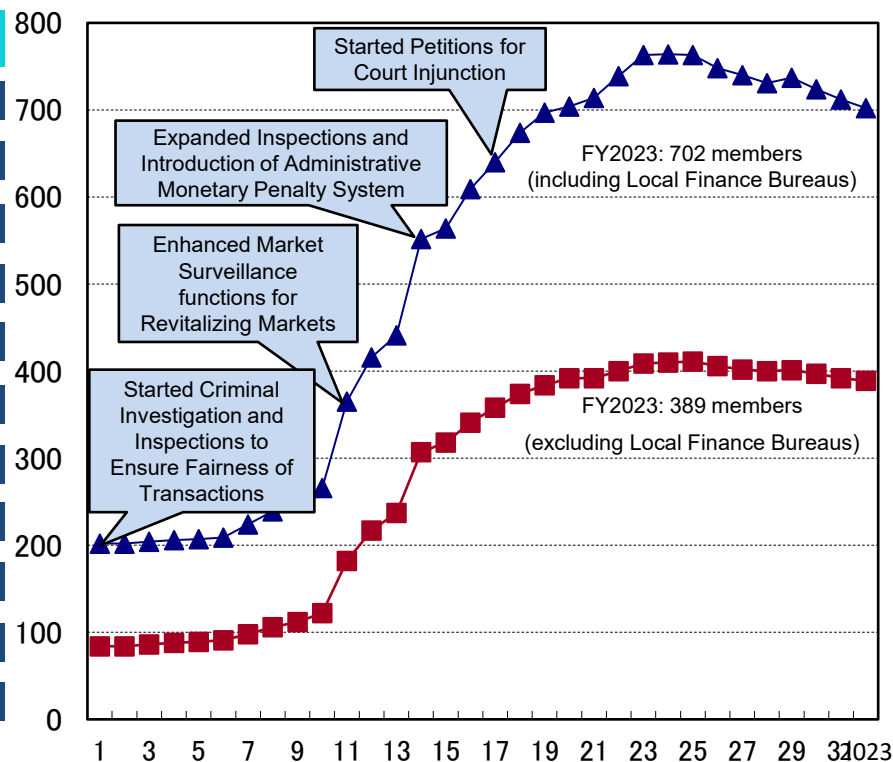
HASHIMOTO Takashi was appointed as SESC Commissioner in December 2022. Previously, he served as a professor at Nihon University College of Commerce and at Aoyama Gakuin University Graduate School of Professional Accountancy.

Organizational Structure and Resources of the SESC

- ◆ The Executive Bureau is composed of the following six divisions: Planning and Management Division, Market Surveillance Division, Securities Business Monitoring Division, Market Misconduct Investigation Division, Disclosure Inspection Division, and Criminal Investigation Division.
- ◆ In addition to the Executive Bureau in Tokyo, the SESC has staff members at the Local Finance Bureaus, which perform mainly inspections of FIBOs located in respective areas.
- ◆ There are 702 staff members in total (389 of which work for the Executive Bureau) as of March 31, 2024, the end of fiscal year 2023.



Staff Number



History of the SESC

Since its establishment in 1992, the SESC has expanded its administrative investigations beyond its investigation of criminal cases to strengthen its functions as a market surveillance organization

Jul. 1992

SESC established within the Ministry of Finance, consisting of two divisions: the Coordination and Inspection Division and the Criminal Investigation Division

Jun. 1998

SESC moved to the Financial Supervisory Agency

Jan. 2001

SESC moved to the FSA

in reorganization of Japanese central government ministries

Apr. and Jul. 2005

Introduction of administrative monetary penalty system

Addition of authority to inspect disclosure statements and to conduct investigations to impose administrative monetary penalties to the SESC

Sept. 2007

Addition of authority to conduct inspections on investment funds

Dec. 2008

Addition of authority to file petitions for court injunctions against violations by unregistered business operators

Jul. 2011

SESC reorganized to its current structure of six divisions:
Planning and Management, Market Surveillance,
Securities Business Monitoring, Market Misconduct Investigation,
Disclosure Inspection, and Criminal Investigation

Aug. 2011

Cross-Border Investigation Office was established within the Market Misconduct Investigation Division to respond to market misconduct involving cross-border and transactions by institutional investors

Apr. 2014

Introduction of insider trading regulations for encouragement of transactions

Apr. 2015

Digital Forensic Solutions Office was established to preserve evidence on electromagnetic records (digital forensics)

Apr. 2018

Addition of authority to conduct inspections on high speed trading business operators

Nov. 2021

Addition of authority to conduct inspections on financial service intermediaries that provide securities intermediary services

Apr. 2022

Foreign Securities Business Monitoring Office was established as part of the environmental improvement accompanying the establishment of international financial markets

Jul. 2024

Global Market Research and Analysis Office was established to promote cooperation with overseas authorities and to collect and analyze information on international transactions

Activities in Figures

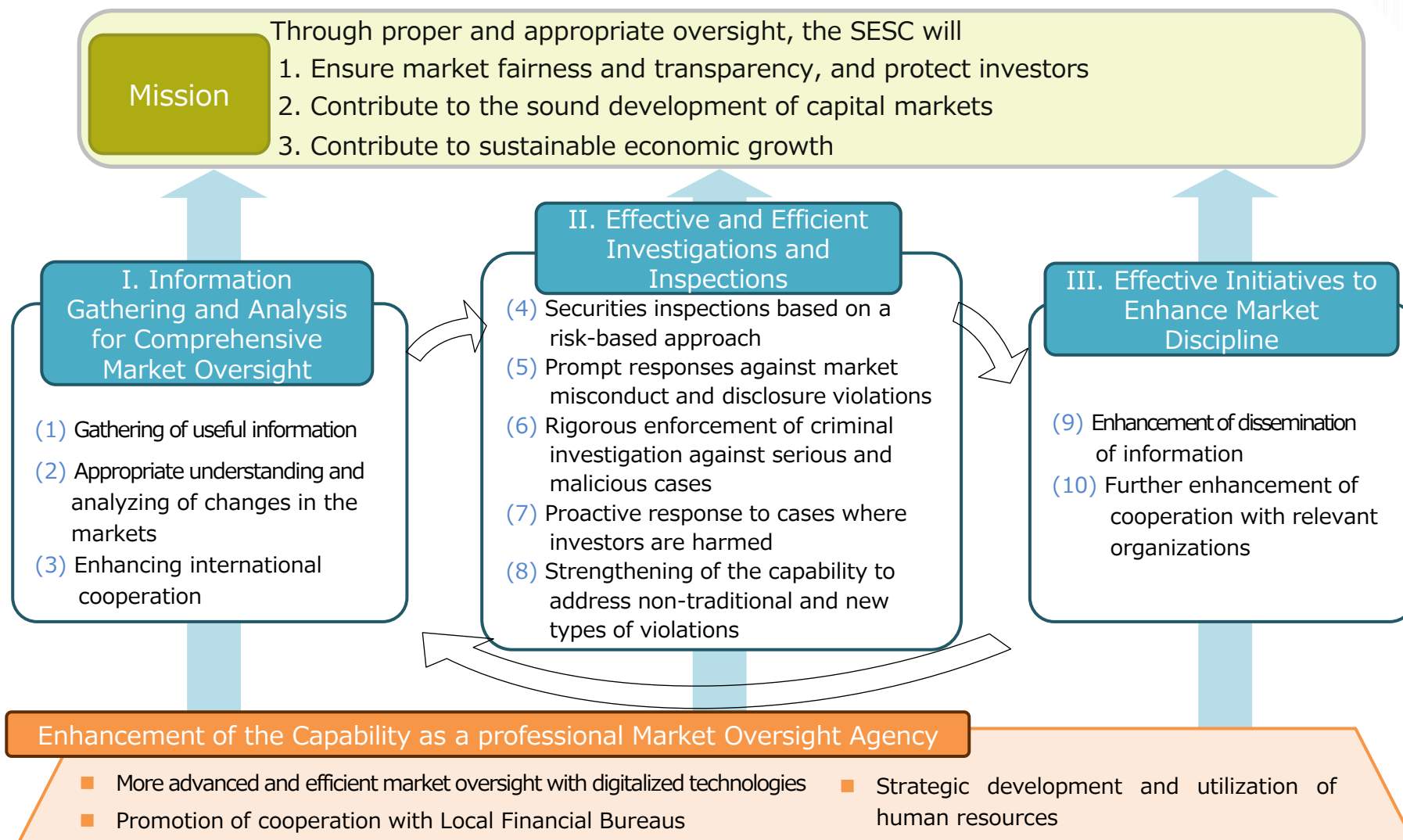
| Category | Fiscal Year | 1992 to 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | Total |
|---|-------------|--------------|------|------|------|------|------|--------------|
| Filed Criminal Charges | | 200 | 3 | 2 | 8 | 8 | 4 | 225 |
| Recommendations: | | 1,082 | 49 | 29 | 20 | 26 | 33 | 1,239 |
| To Take Administrative Actions Against Operators (*1) | | 570 | 14 | 5 | 2 | 5 | 8 | 604 |
| To Issue Orders to Pay Administrative Monetary Penalties: Market Misconduct (*2) | | 397 | 29 | 14 | 12 | 14 | 17 | 483 |
| To Issue Orders to Pay Administrative Monetary Penalties: Disclosure Containing False Statements | | 111 | 6 | 10 | 5 | 7 | 8 | 147 |
| For Order to Submit Revised Report, etc. | | 4 | 0 | 0 | 1 | 0 | 0 | 5 |
| Announcements of Inspection Results of QII Business Operators | | 86 | 2 | 0 | 0 | 1 | 0 | 89 |
| Petitions for Prohibition and Stay Order | | 22 | 3 | 1 | 1 | 2 | 1 | 30 |
| Policy Proposals | | 26 | 0 | 0 | 0 | 1 | 0 | 27 |

*1: In line with the revision of the FIEA (enforced in Mar. 2016), the SESC began to make recommendations to take administrative actions against business operators, etc. engaging in specially permitted businesses for qualified institutional investors, etc. ("QII Business Operators") as well from FY2016.

*2: Market misconduct - "Market Manipulation," "Insider Trading" and "Use of Fraudulent Means" - counts persons subject to orders to pay administrative monetary penalties.

Strategy & Policy of the SESC 2023-2025

- For Trusted, Fair and Transparent Markets in Response to the Changing Times -





2. Monitoring Priorities for Securities Businesses (July 2024 - June 2025)

Summary of Monitoring Priorities for Securities Businesses (July 2024-June 2025)

Environment surrounding FIBOs (Financial Instruments Business Operators), etc.

1. Environment surrounding FIBOs
 - Requirement for customer-oriented business conduct, sharp increase in the number of victims of fraudulent investment solicitation, building a sustainable business model, etc.
2. Changes to regulatory frameworks for FIBOs
 - (i) Measures for ensuring customer-oriented business conduct; (ii) Response to the progress in digitalization, etc.; (iii) Sophistication and diversification of asset management; (iv) Clarification regarding control environments for preventing conflicts of interest of real estate-related fund management companies, etc.
3. Findings through the securities business monitoring over the past business year
 - Type I FIBOs: Violation of the principle of suitability, violation of the firewall regulations between banks and securities firms, acceptance of orders for fictitious market formation, implementation of stress tests using falsified data
 - Investment management business operators: Deficiencies in conflict-of-interest control systems, and deficiencies in the decision-making process concerning investment policy
 - Investment advisors: False notification, misleading representation
 - Type II FIBOs: Deficiency in requirements for acts of managing specified securities
 - Unregistered business operators: Financial instruments business operations without Type II FIBOs registration (public offering or private placement of collective investment schemes under foreign laws and regulations)

Industry-wide monitoring priorities

1. Development of internal control environments with a focus on appropriate investment solicitation based on the principle of suitability, and appropriate sales operations based on customer-oriented business conduct (Sale of complex or high-risk products, unreasonable, short-term solicitation for switching, sale and solicitation by bank-securities collaborative business)
2. Business model changes along with progress in digitalization, etc., and the development of internal control environments in response to such changes
3. Sufficiency of cybersecurity measures (including countermeasures against unauthorized access in online trading), and system risk management (including management of system development and operation and management of trustees) in response to progress in digitalization
4. Firm establishment of internal control environments for AML/CFT (Anti-Money Laundering and Combating the Financing of Terrorism)
5. Implementation of measures to improve or prevent the recurrence of matters pointed out in internal audits or self-regulatory organization examinations

In addition to the above, the SESC (Securities and Exchange Surveillance Commission) will also examine other matters in a timely manner in response to changes in the environment surrounding FIBOs.

Summary of Monitoring Priorities for Securities Businesses (July 2024-June 2025)



Monitoring priorities by FIBOs' size and business type

| | | |
|---|---|--|
| Type I FIBOs | Major securities business groups | <ul style="list-style-type: none"> Development of control environments for governance and risk management that support global business operations Efforts to build sustainable business models Development of internal control environments, including those for detecting and preventing market misconduct. If necessary, the SESC will swiftly inspect relevant sales offices to examine actual sales practices there. |
| | Foreign securities firms | <ul style="list-style-type: none"> Development of internal control environments in response to the overseas outsourcing of back-office operations and control environments for system risk management Development of control environments for managing sales of financial instruments to Japanese financial institutions and other investors |
| | Online securities firms | <ul style="list-style-type: none"> Development of control environments for system risk management, including cybersecurity measures Development of control environments for outsources in response to the expansion of face-to-face sales utilizing Financial Instruments Intermediary Service Providers, and business operation environments in light of business models changes such as provision of new products and services. As the new NISA (Nippon Individual Savings Account) has been launched, development of internal control environments, including an effective trade management environment suited to the increasing number of new accounts opened and trading volume. |
| | Semi-major/ regional securities firms, etc. | <ul style="list-style-type: none"> Efforts to build sustainable business models, and compliance with the principle of suitability. Development of internal control environments at those securities firms whose major shareholders or business management systems have changed, from the viewpoint of their business models or governance. |
| | Foreign currency margin transactions business operators | <ul style="list-style-type: none"> Development of control environments for system risk management, including cybersecurity measures Development of adequate internal control environments for relevant advertising and sales/solicitation regulations Settlement risk management, including implementation of stress testing. |
| Investment management business operators | | <ul style="list-style-type: none"> Actual investment practices, development of control environments for managing investment (including those outsourced) and conflicts of interest (including whether there is a system in place under which the appropriateness of transactions can be examined ex-post facto), etc. |
| Investment advisors/agencies | | <ul style="list-style-type: none"> Misleading advertisement, solicitation through false explanation, breach of fiduciary duty, development of internal control environments at those securities firms whose major shareholders or business management systems have changed, etc. |
| Registered financial institutions | | <ul style="list-style-type: none"> Development of internal control environments regarding appropriate investment solicitation and the principle of suitability |
| Type II FIBOs, QII business operators, Financial instruments intermediary service providers, etc. | | <ul style="list-style-type: none"> Funds claiming high returns and existence of investment projects, development of internal control environments at those securities firms whose major shareholders or business management systems have changed. [Type II FIBOs, QII business operators] Appropriateness of their investment solicitation and sufficiency of management by their entrusting FIBOs [Financial instruments intermediary service providers] |
| Unregistered business operators | | <ul style="list-style-type: none"> Exercising investigative authority proactively to file a petition with the court for a prohibition and stay order against their illegal conduct Further strengthen information dissemination, including warnings and public disclosure of their representatives' names and illegal conduct, etc. Coordinating more proactively with relevant JFSA (Financial Services Agency, Japan) divisions, Local Finance Bureaus, investigative authorities and the Consumer Affairs Agency. |

*The SESC will also examine FIBOs' response to the changes in regulatory frameworks.

On the SESC's website, you can find press releases, case studies by category and messages to the market participants and other stakeholders.

[URL] <https://www.fsa.go.jp/sesc/english/index.html>



SESC X (formerly Twitter) account

✕@SESC_JAPAN



This X account is not intended to receive information from the public.

Case Studies by Category

Casebooks introduce the SESC's recent recommendations for administrative monetary penalty payment orders, and illustrate issues identified through the SESC's securities monitoring.

- Casebook of Administrative Monetary Penalties (Market Misconduct) and Casebook of Inspection of Disclosure Statements :

[URL] <https://www.fsa.go.jp/sesc/jirei/index.html> (Japanese Version Only)

- Securities Monitoring Overview and Case Studies:

[URL] <https://www.fsa.go.jp/sesc/kensa/shitekijirei.html> (Japanese Version Only)



令和5年度
金融商品取引法における
課徴金事例集～不正取引編～

令和5年9月
証券取引等監視委員会事務局

Casebook of Administrative
Monetary Penalties (Market
Misconduct)

令和5事務年度
開示検査事例集

令和5年9月
証券取引等監視委員会事務局

Casebook of Inspection of
Disclosure Statements

令和5事務年度
証券モニタリング概要・事例集

令和5年9月
証券取引等監視委員会事務局

Securities Monitoring
Overview and Case Studies

Monitoring Priorities for Securities Businesses

Basic policy and monitoring priorities
for financial instruments business operators

[URL] https://www.fsa.go.jp/sesc/news/c_2023/2023/20230801-2/01-en.pdf

https://www.fsa.go.jp/sesc/news/c_2023/2023/20230801-2/02-en.pdf



Annual Report

Summary of the SESC's activities over the year (annual
publication under Article 22 of the Act for Establishment of the
Financial Services Agency)

[URL] <https://www.fsa.go.jp/sesc/english/reports/reports.html>

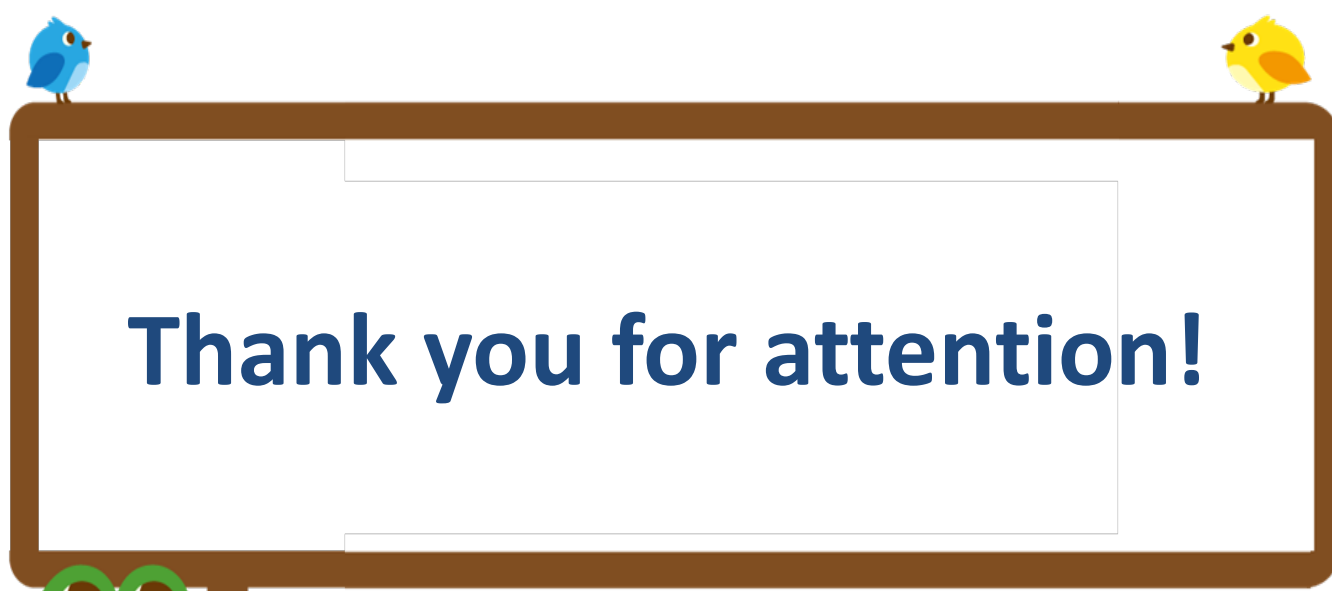


SESC Latest Topics

Quick summary of latest cases of recommendations
and criminal charges (updated about once a month)

[URL] <https://www.fsa.go.jp/sesc/english/topics/index.html>





Thank you for attention!

