

# Summary of Monitoring Priorities for Securities Businesses (July 2019-June 2020)

## Basic monitoring policy

- The SESC will continue to select the businesses subject to on-site monitoring based on the off-site risk assessment of all securities businesses. The SESC will carry out off-site risk assessment in collaboration with the relevant bureaus of the JFSA and conduct assessment including an analysis of the business environment covering economic and industrial trends and an business model of each securities business.
- Through its on-site monitoring, the SESC will analyze the whole picture and root cause of problems identified to develop effective recurrence prevention measures. Also, the SESC will urge securities businesses to improve business operations if they have potential issues which may not necessarily have become materialized problems.

## Activity policy for the current business year

- Bearing in mind that excessive sales targets and significant burdens beyond the front-line resources can cause inappropriate conducts against investors, the SESC will assess risks focusing on the status of establishment of necessary internal control environments, management's intentions which lurk in the background of such issues, and insufficient distribution of managerial resources.
- The SESC will continue to proactively conduct on-site monitoring for in-depth examinations particularly in any of the following situations:
  - a relevant law and/or regulation is breached or there is a deficiency in business operations that requires a prompt in-depth examination;
  - a financial instrument is offered with an unclear risk profile, necessitating an examination of its solicitation activities;
  - the actual situation of business operations is not fully comprehended from an information analysis based on off-site monitoring (including where there is a long period between examinations); or
  - there is a possible serious problem concerning investor protection (e.g. inappropriate segregated management of customer assets).
- The SESC will conduct mainly off-site monitoring of the governance of regional securities firms, the sustainability of business models (including customer-oriented business conduct), and the roles of regional operators of direct finance, in particular.
- In addition to the above, the SESC will actively collect and analyze information on unregistered FIBOs, conduct investigations in collaboration with relevant agencies, and seek court injunctions to cease and suspend the violations.

- ◎ Efforts to enhance AML/CFT (Anti-Money Laundering/Combating the Financing of Terrorism) measures
- ◎ Sufficiency of cyber security measures, implementation of system risk management that suits business model
- ◎ Measures to implement customer-oriented business conduct
- ◎ Implementation of measures to improve or prevent the recurrence of matters pointed out in results of internal audits or examinations by self-regulatory organizations

《Monitoring strategies for various FIBO business models》

Major securities business groups	<ul style="list-style-type: none"> <li>• Development of governance/risk control environments that support domestic and overseas business operations and efforts to establish a sustainable business model</li> <li>• Efforts to establish an effective and principle-based compliance environment that is beyond mere compliance with formal rules</li> <li>• Efforts to instill and establish customer-oriented business conduct and enhance AML/ CFT (Swiftly conduct on-site monitoring where it is necessary to confirm actual practices at sales offices.)</li> <li>• Control environments for conflict of interest management for banking/securities collaboration (securities businesses under the three mega banking groups)</li> </ul>
Foreign securities firms	<ul style="list-style-type: none"> <li>• Progress of overseas outsourcing of back office operations and development of internal control environments that respond to structural changes in business models</li> <li>• Trends of products sold to Japanese financial institutions and the risks of these products</li> <li>• Situation of investment banking business, such as M&amp;A and underwriting operations in bond issuance</li> </ul>
Online securities firms	<ul style="list-style-type: none"> <li>• Understand the group-wide strategies and operation policies, including earnings, of non-financial entities that are rapidly entering the market.</li> <li>• Status of system risks including cyber security</li> <li>• Development of internal control environments in preparation for increases in products offered, and launch and expansion of face-to-face sales activities</li> </ul>
Semi-major/regional securities firms	<ul style="list-style-type: none"> <li>• Inappropriate solicitation and other conducts that are inappropriate from the viewpoint of investor protection</li> <li>• Business operations of securities firms whose major shareholders and management structure changed due to participation of new investors, and securities firms that participate in funding by companies with financial trouble</li> <li>• Conduct mainly off-site monitoring on governance, sustainability of business models (including customer-oriented business conduct), and the roles of regional operators of direct finance (regional securities firms)</li> </ul>
Foreign currency margin transactions business operators	<ul style="list-style-type: none"> <li>• Efforts based on the revision to the Cabinet Office Ordinance, etc. for strengthening settlement risk management, etc., such as disclosure of risk information, appropriateness of stress tests, and appropriate reflection of stress test results to capital</li> </ul>
Investment management business operators	<ul style="list-style-type: none"> <li>• Control environments for management of conflicts of interests and for outsourced investment management</li> <li>• Assess the actual situation of operators that manage real estate-related funds such as private REITs and the current situation of investment in alternative assets.</li> </ul>
Investment advisors/agencies	<ul style="list-style-type: none"> <li>• Misleading advertisements, solicitation activities using false explanations</li> </ul>
Type II FIBOs/QII business operators, and others	<ul style="list-style-type: none"> <li>• Funds advertising high returns and actual existence of business project to be invested</li> <li>• Risk-based securities monitoring in light of the firm’s particular business types (securities finance companies, credit rating agencies, registered financial institutions, self-regulatory organizations, etc.)</li> </ul>
Unregistered business operators	<ul style="list-style-type: none"> <li>• Proactively exercise the investigative authority to seek court injunctions to cease and suspend activities that violate the FIEA.</li> <li>• Publicly disclose the name, name of representative, nature of illegal conduct, etc. of unregistered business operators as needed.</li> </ul>

《Collaboration with relevant agencies, and dissemination of monitoring results》

- ◎ The SESC will collaborate closely with Local Finance Bureaus (LFBs) from the planning stage of both off-site and on-site monitoring, and conduct joint examinations if needed. In addition, the SESC will collect and share information with LFBs, consider appropriate monitoring methods, and focus on training that LFBs require.
- ◎ The SESC will continue collaborating closely with self-regulatory organizations and other relevant organizations, and share information and findings with them on a timely basis. By doing so, the SESC will work out to effectively improve and prevent recurrences of problems identified in the securities monitoring.
- ◎ The SESC will encourage FIBOs to make voluntary improvement by sharing the monitoring results and other information to their auditors when necessary.