

Annual Report 2020/2021

(April 2020 – March 2021)

Overview



"for investors, with investors"

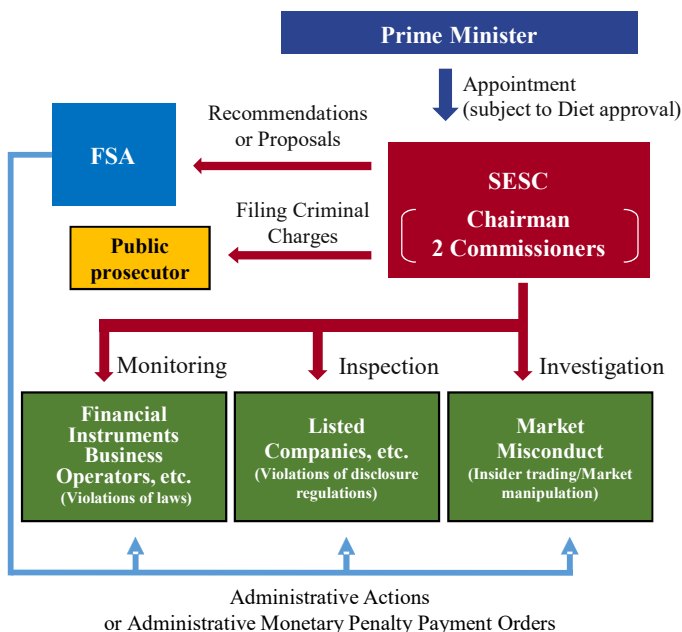
June 2021
Securities and Exchange Surveillance
Commission

1. About the SESC

Activities in 2020/2021

- Timely market surveillance
- On-site monitoring based on thorough risk assessment of financial instrument business operators
 - Published and began implementing “Basic Principles of Securities Business Monitoring” on June 26, 2020
- Swift and efficient investigations taking advantage of the administrative monetary penalty system
- Rigorous enforcement of criminal investigations against serious and malicious market misconduct
- Root-cause analysis and dialogue with stakeholders to prevent and forestall the occurrence and recurrence of violations

Role and Functions of the SESC



Chairman and Commissioners (2020-2022)



**Commissioner
HAMADA Yasushi**

HAMADA Yasushi was appointed as SESC Commissioner in December 2016 (reappointed in 2019). Previously, he served as the Senior Partner and Director of KPMG AZSA LLC, and a professor of Graduate School of Professional Accountancy, Aoyama Gakuin University.

**Chairman
HASEGAWA
Mitsuhiro**

HASEGAWA Mitsuhiro was appointed as SESC Chairman in December 2016 (reappointed in 2019). Previously, he served as the Chief Public Prosecutor of Nagoya District Public Prosecutors Office and the Superintending Public Prosecutor of Hiroshima High Public Prosecutors Office.

**Commissioner
KATO Sayuri**

KATO Sayuri was appointed as SESC Commissioner in December 2019. 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.

Strategy & Policy of the SESC 2020-2022*

- For Trusted and Attractive Capital Markets-

*Published on January 24, 2020

Mission

- Through proper and appropriate market oversight, the SESC
1. Ensures market fairness and transparency, and protects investors
 2. Contributes to the sound development of capital markets
 3. Contributes to sustainable economic growth

SESC's Market Vision

Markets with strong confidence, where market participants share their commitment towards the sound development of capital markets and solid investor protection, fulfill their expected roles and exercise their professionalism^(*)

- * Proper disclosure by listed companies, etc.
 Legal compliance and customer-oriented business administration by market intermediaries
 Self-discipline by market users
 Professional market surveillance

Philosophies and goals

Fairness

Accountability

Forward-looking

Effectiveness and efficiency

Close cooperation

Commitment to excellence

<Based on these philosophies, the SESC aims to achieve the following in terms of market surveillance>

Holistic oversight	Timely oversight	In-depth oversight
<ul style="list-style-type: none"> • Vigilance against new financial products and transactions • Surveillance of multiple markets and cross-market activities • Protecting investors of diverse characteristics • Holistic and comprehensive investigation of cases and cross-sectoral application of findings • Enhanced outreach to stakeholders 	<ul style="list-style-type: none"> • Early detection of market misconduct • Preemptive actions against market misconduct • Effective investigation and inspection, and swift corrective action 	<ul style="list-style-type: none"> • Identifying root causes of problems • Recognizing structural issues of the markets through in-depth and cross-sectoral analysis

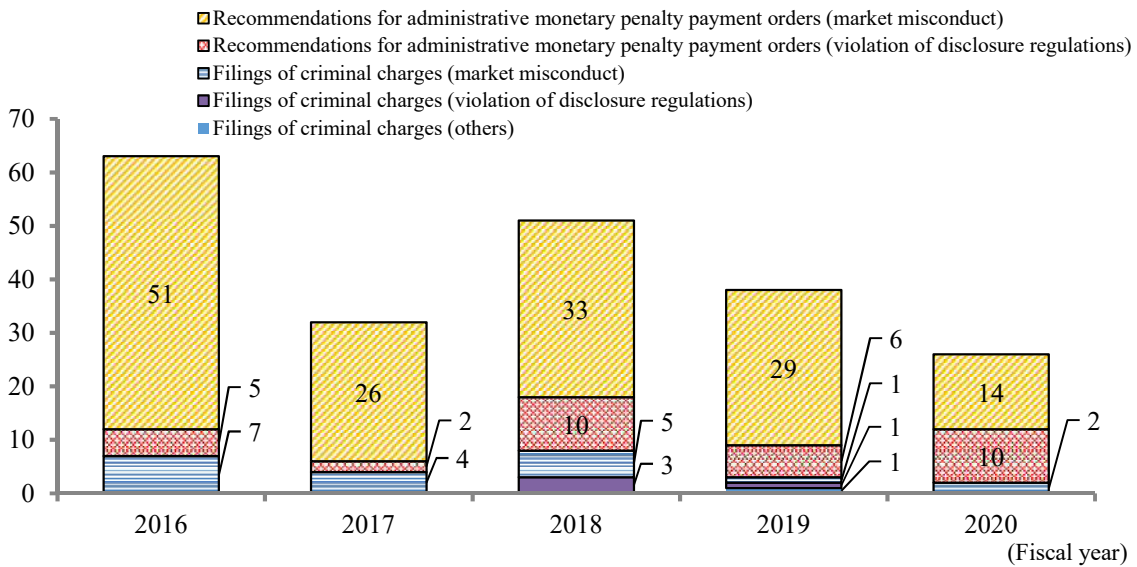


Market Environment & Challenges	Globalization and Integration of Financial Markets	Uncertainty of the Global Economic Outlook	Digitalization	Policy Actions for Stable Asset Building of Household
Mid-term Policy Priorities	(1) Enhanced Intelligence Gathering	<ul style="list-style-type: none"> ➢ Forward-looking surveillance from macroeconomic perspectives ➢ Cross-sectoral surveillance across financial markets ➢ Intelligence gathering through closer cooperation with foreign authorities 	(3) Effective Measures for Strengthened Market Discipline	<ul style="list-style-type: none"> ➢ Multi-dimensional/directional use of outputs from monitoring activities ➢ Enhancement of root-cause analysis and engagement with stakeholders to prevent recurrence of market abuse ➢ Enhanced outreach domestically and globally for pre-emptive measure against market misconduct ➢ Extensive measures for seamless surveillance
	(2) In-depth Analysis and Swift, Effective and Efficient Examination/ Investigation	<ul style="list-style-type: none"> ➢ Multi-directional/dimensional analysis and review ➢ Swift recommendation of administrative penalty ➢ Effective and efficient examination and investigation of cross-border cases ➢ Rigorous enforcement of criminal investigation against market misconduct ➢ Effective and efficient securities business monitoring based on risk approaches ➢ Proactive response to cases where investors are harmed 	(4) Response to Digitalization and Strategic HR Development	<ul style="list-style-type: none"> ➢ Advanced and efficient surveillance with digitalized technologies ➢ Swift response to rapid digitalization in the capital market ➢ Strategic HR development (market abuse, corporate disclosure and securities business monitoring)
			(5) Cooperation with Various Stakeholders	<ul style="list-style-type: none"> ➢ Closer cooperation with SROs ➢ Enhanced cooperation with stakeholders ➢ Enhanced contribution to global market oversight

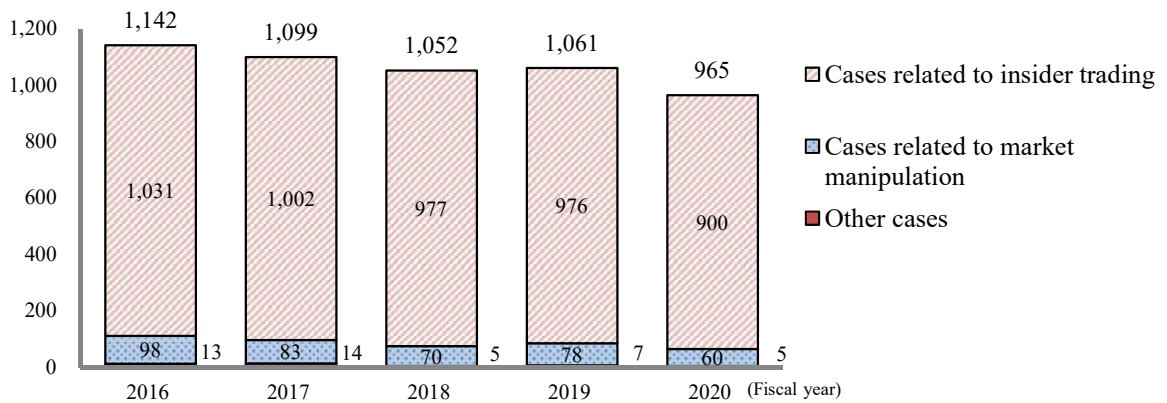
2. Market Misconduct in Numbers

- 14 recommendations for administrative monetary penalty payment orders
 - Insider trading: 8 cases
 - Market manipulation: 6 cases
- 2 filings of criminal charges
 - 1 for insider trading and 1 for market manipulation
- A total of 965 cases were examined

Recommendations and Filings of Criminal Charges



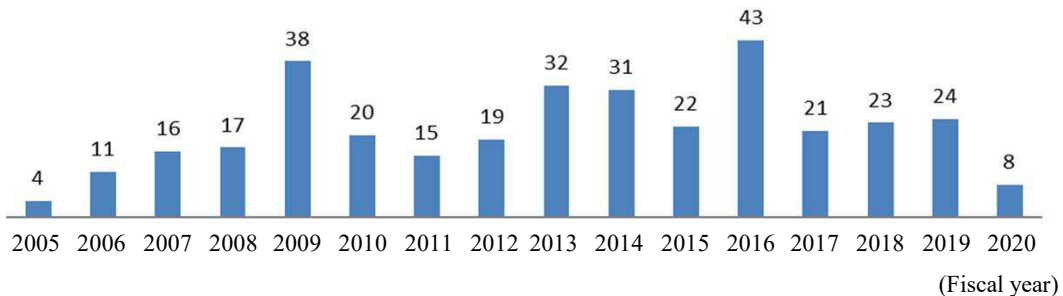
Examined Cases for Market Misconduct



2. Market Misconduct in Numbers (Cont.)

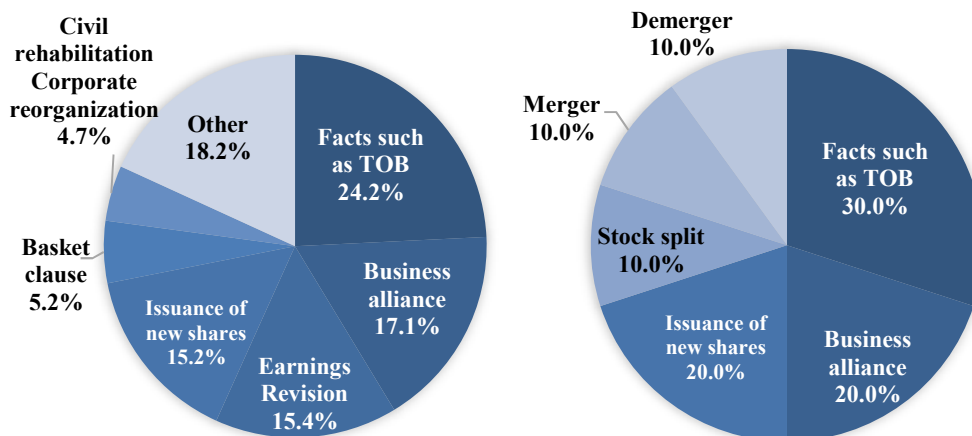
- Insider trading
 - Many cases in which the SESC made recommendations included tender offers, business alliances, and new share issuances as a material fact.
 - A criminal charge solely against a violation of transaction encouragement regulations was filed for the first time.
- Increasingly complicated and sophisticated market manipulation schemes
 - A scheme to artificially raise stock prices of an exchange by purchasing shares at higher prices than the prices of the exchange through a Proprietary Trading System (PTS)
 - A scheme to raise stock prices by repeating minimum-lot purchases after placing multilayered buy orders at lower prices

Number of Cases of Insider Trading



Note: The numbers include cross-border cases.

Breakdown of Cases by Insider Information as a Material Fact



Cumulative numbers between April 2005 and March 2021

FY2020

3. Violation of Disclosure Regulations

- 10 recommendations for administrative monetary penalty payment orders were made, including the following cases:
 - An inappropriate accounting practice case where the cost of sales was understated by long-term reporting of fictitious year-end inventory
 - An inappropriate accounting practice case where the cost of sales by overseas subsidiaries was understated
- To prevent occurrence or recurrence of disclosure regulation violations, the SESC discussed with management of listed companies that had committed violations and shared its view on the backgrounds and root causes of such violations.

Results of the Disclosure Statement Inspections

Number of inspected cases		13cases
(of which)	Recommendations for administrative penalty payment orders	10 cases

Outlines	Background and causes of inappropriate accounting practices
<ul style="list-style-type: none"> • Understating cost of sales by reporting of fictitious year-end inventory • Various types and large amount of inappropriate accounting practices were carried out over a long period of time 	<ul style="list-style-type: none"> • The authority for the accounting of the company was concentrated on one person in charge of accounting. • Their corporate culture of failing to place importance on proper accounting.
<ul style="list-style-type: none"> • Understating cost of sales by overseas subsidiaries • Inappropriate accounting practices prior to listing 	<p>The overseas subsidiary's representative tried to make it appear that they had achieved their performance targets, because the President of the Company, based on an overemphasis on performance, forced officers and employees to achieve overstated performance targets.</p>

4. Monitoring of Financial Instruments Business Operators (FIBOs)

- Risk assessment based on the size and type of business
 - Analyzing operational risks and issues by the size and type of business
- Risk-based on-site monitoring
 - 47 cases of on-site inspection
 - 5 recommendations for administrative actions
- Initiatives to encourage FIBOs to build an effective internal control system
 - Sharing the SESC’s view with the management of FIBOs on issues that have yet to develop into problems but should be improved

Recommendations for administrative actions against FIBOs (5 cases)

Outline of the cases	Securities companies	<ul style="list-style-type: none"> • Significantly false advertising • Illegal failure to confirm customers’ willingness to accept solicitation regarding foreign currency margin transactions and violation of the prohibition of re-solicitation
	Investment management firms	<ul style="list-style-type: none"> • Failure to conduct investment management business for beneficiary owners of an investment trust with the due care of a prudent manager
	Investment advisers/agents	<ul style="list-style-type: none"> • Provision of false information and misleading indication to customers in relation to solicitation for the conclusion of financial contracts • Name-lending to third parties

5. Development of Market Surveillance Infrastructure (Digitalization and Human Resources)

- Enhancing the functions of the trading surveillance system to implement more effective and efficient market surveillance
- Devising a strategic and cross-sectoral plan to further promote digitalization
 - Established the IT Strategy Office
 - Promoting digitalization of an existing administrative process in cooperation with financial institutions and relevant authorities
- Further enhancing Digital Forensic technology and upgrading the Digital Forensic system
- Improving SESC staff members' professional skills and hiring personnel with high expertise

6. International Coordination for Close Market Surveillance

- Proactive participation in the IOSCO discussions on developing internationally recognized securities regulation and enhancing mutual cooperation between regulators
- Active information exchange through IOSCO MMoU for enforcement actions against misconduct in cross-border transactions
- Strengthening the cooperative network and sharing common issues with overseas authorities:
 - Provided on-line seminars for overseas regulators
 - Participated in on-line seminars held by overseas authorities, etc.

Major IOSCO meetings in which the SESC participates

Annual Meeting

An annual conference where various meetings are held, including the Presidents Committee meeting.

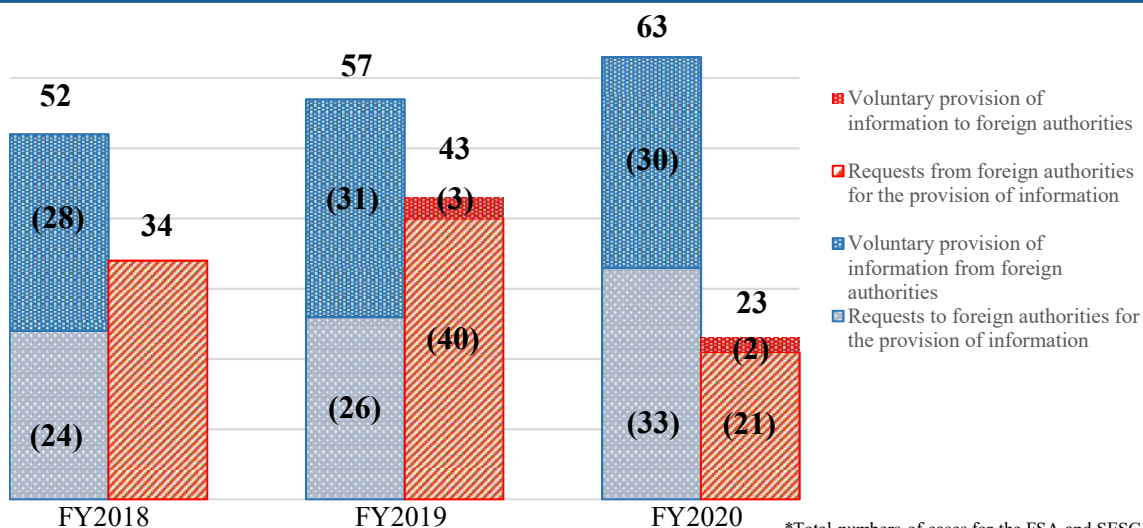
Asia-Pacific Regional Committee

Discussions among Asia-Pacific authorities on region-wide issues

Committee 4

Discussions on information exchange and law enforcement cooperation among authorities

Information Exchange with Foreign Authorities through IOSCO MMoU



7. Cooperation with SROs and Proactive Communication

- Close cooperation with self-regulatory organizations (SROs) in market surveillance
 - Information sharing on a daily basis
 - Periodical discussions to share emerging issues
- Proactive communication on the significance and root causes of the cases with stakeholders
 - Websites, casebooks, articles, lectures, etc.
 - Noteworthy activities in FY2020 described as "Key Topics" (Annual Report 2020/2021)
 - Message to various stakeholders given in the Case Study (Annual Report 2020/2021)

Key Topics

Title

Formulating and publishing “Basic Principles of Securities Business Monitoring”

Case Study

Intended recipients of the message	Title
Market participants	We wouldn't miss any suspicious transactions
Listed companies	Why should related party transactions be disclosed in the notes?
	Is your control over overseas subsidiaries all right?
Investment management firms and investors	Close examination is required responding to financial instruments' features
Investors	Beware of unregistered financial instrument business operators