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Access FSA

Provisional Translation

Contents

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Financial Services Agency

Appointment of New State Minister and Parliamentary Vice-Minister

On August 10, 2022, Prime Minister KISHIDA Fumio reshuffled the cabinet, with SUZUKI Shunichi being reappointed as the Minister of State for Financial Services. In addition, at an extraordinary cabinet meeting on August 12, FUJIMARU Satoshi and SUZUKI Eikei were appointed as the State Minister and the Parliamentary Vice-Minister, respectively.

On August 15, State Minister FUJIMARU and Parliamentary Vice-Minister SUZUKI attended office for the first time and delivered speeches to the staff of the Financial Services Agency (FSA).

Inaugural speach to FSA staff

Photo:
State Minister FUJIMARU (above) and Parliamentary Vice-Minister SUZUKI (left)

Establishment of the "Human Capital Management Consortium"

It is essential to sustainable growth in corporate value that the management team exercise leadership in developing and executing a human capital strategy that contributes to the medium- and long-term growth of their company and also explain it to stakeholders in dialogue with investors and in integrated reports. Therefore, the Human Capital Management Consortium, which is led by the private sector, has been established as a forum for sharing best practices of human capital management, discussing inter-company collaboration, and deliberating on effective information disclosure.*

Photo: Photo sessions of member companies

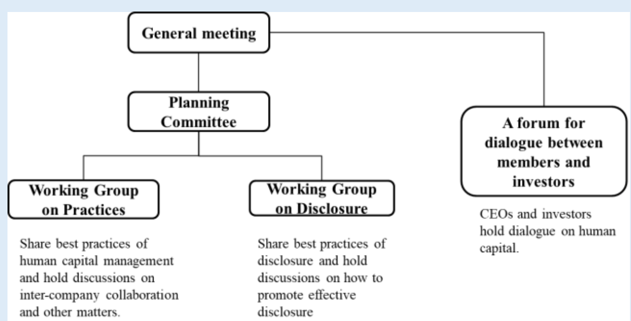
On August 25, 2022, at the Otemachi Place Conference Center, an inaugural general meeting of the Human Capital Management Consortium was held. State Minister FUJIMARU, representing the FSA, made a speech, in which he expressed expectations for the consortium as follows: "I believe that the establishment of the Human Capital Management Consortium is very useful for exploring a human capital strategy linked to a management strategy and an ideal disclosure regarding human capital.“

He also stated that international discussions on disclosure regarding human capital that are about to start may provide an opportunity for Japan to play a leading role and that in those discussions, which will be led by the International Sustainability Standards Board (ISSB), it is important for Japan to express opinions so that the country's active efforts concerning human capital will be reflected in the ISSB's agenda. He voiced hopes that the results of discussion at the consortium will lead to expression of opinions from Japan to other countries.

Photo: State Minister FUJIMARU

As for the specifics of the consortium's activity, in line with the policy for activity deliberated on by the Planning Committee, best practices of human capital management will be shared and inter-company collaboration will be discussed at the Working Group on Practices, while best practices of disclosure will be shared and how to promote effective disclosure will be discussed at the Working Group on Disclosure. In addition, top officials of member companies are scheduled to hold dialogue with investors on human capital.

Figure: Organization chart of the Human Capital Management Consortium



The FSA will provide support to the consortium in terms of management by attending its meetings as an observer, for example.

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* Published on July 25: "Human Capital Management Consortium to Be Established"
https://www.meti.go.jp/english/press/2022/0725_004.html

The JFSA Strategic Priorities July 2022-June 2023

– Overcoming Challenges Confronting the Financial System and Building Foundation for Sustainable Growth –

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Upon the publication of the JFSA Strategic Priorities July 2022-June 2023

On August 31, 2022, the JFSA published "The JFSA Strategic Priorities July 2022-June 2023 (Overcoming Challenges Confronting the Financial System and Building Foundation for Sustainable Growth)".* This clarifies the goal of financial administration and shows policies to be taken by financial administration to achieve those goal. The JFSA expects that this publication will further enhance transparency and contribute to achieving better financial administration by facilitating awareness sharing and constructive dialogues among the JFSA, financial service users, financial institutions, and market players, etc.

The JFSA accepts comments on the JFSA Strategic Priorities on an ongoing basis. Your comments will be used as reference in the future. Please send your comments to our website contact (https://www.fsa.go.jp/opinion/) (Available in Japanese).

This business year's JFSA Strategic Priorities July 2022-June 2023 was compiled based on broad opinions, including those from young JFSA officials and officials of Local Finance Bureaus nationwide, in addition to major administrative challenges ascertained in the last business year, through repeated discussions among executive officials and with the participation of many others. Through these activities, we will develop an organizational culture wherein all staff members voluntarily plan, formulate and implement policies, and will pursue further collaboration with Local Finance Bureaus.

Priorities for business year 2022

The JFSA Strategic Priorities July 2022-June 2023 focuses on the following three areas:

I. Support the Economy and People's Lives for Future Growth

II. Build the Financial System in which Economic Growth is Achieved by Resolving Social Issues and is Shared with Individuals

III. Evolve JFSA's Financial Administration Further

First, with future prospects remaining uncertain due to the COVID-19 pandemic and the Russian's invasion into Ukraine, the JFSA will proceed with measures required to support the stability of Japan's economy and national life for future growth.

Second, the JFSA will financially develop an environment to resolve various social issues and achieve new economic growth and will promote the shift of individual's financial assets from savings to investment and realize a virtuous cycle in which the fruits of growth are widely shared with individuals.

Third, amid significant changes in the domestic and international environment, the JFSA will enhance its capabilities as a financial administration organization to make further contributions to Japan's sustainable growth.

(Front cover of the JFSA Strategic Priorities July 2022-June 2023)

1. Support the Economy and People's Lives for Future Growth

First of all, it is important for the JFSA to financially support the stability of Japan's economy and national life for future growth by responding accurately to rapid structural environmental changes that have emerged as uncertainties about future domestic and foreign economies have grown under the impact of the COVID-19 pandemic and Russia's invasion of Ukraine. To this end, the JFSA will take all possible measures to ensure financial institutions' support for companies and will back up financial institutions' initiatives to support the powerful growth of Japan's national and regional economies and their later sustainable growth. The JFSA will also develop its dialogues with financial institutions to enhance their business infrastructure, secure their financial soundness, and build their sustainable business models based on their customers' perspectives.

* Published on September 26, 2022: Publication of the summary from "The JFSA Strategic Priorities July 2022-June 2023"
https://www.fsa.go.jp/en/news/2022/20220926.html

II. Build the Financial System in which Economic Growth is Achieved by Resolving Social Issues and is Shared with Individuals

As the second pillar, while Japan needs to deal with various social issues, including climate change, digital society realization, and startup support, the JFSA will financially develop and environment to have such social issue resolution bring about new economic growth and achieve a "virtuous cycle of growth and distribution" in which the fruit of growth will be passed on to people widely and lead to people' asset formation and a further increase in consumption and investment.

For instance, the JFSA will endeavor to enhance the financial literacy and ensure customer-oriented business conduct by financial institutions to promote people’s stable asset formation, and encourage asset owners and asset management firms to sophisticate their asset management for stable higher investment returns. In order to facilitate smooth funds supply to startups and other growth company, the JFSA will take measures to strengthen the functions of capital markets and enhance companies' disclosure of non-financial information, such as that on human capital, which serves as the basis for their sustainable value creation. Furthermore, the JFSA will proceed with the environment to promote sustainable finance to facilitate a transition to new industrial and social structures and to realize a sustainable society. The JFSA will also strengthen support for businesses so that financial services using new technologies will develop, without undermining customer protection and the safety of the financial system. Towards the development of the international financial center, the JFSA will improve an environment and promote the detailed information and funds to foreign asset management firms.

III. Evolve JFSA's Financial Administration Further

Thirdly, the JFSA, with a view to evolving financial administration further, will attempt to improve all its staff members' capacity, quality and motivation, and upgrade data utilization and enhance capabilities to advocate its policies at home and abroad.

For instance, the JFSA will improve its staff members' capacity and quality by providing them with training programs in accordance with their desired fields to enhance their expertise. The JFSA will also develop a workplace where all staff members can engage in free and vigorous discussion and work actively to maximize performance, while placing priority on their independence and autonomy. To accurately identify financial institutions' business conditions and the entire financial system, the JFSA will sophisticate data utilization for multifaceted understanding of realities and will use data for considering how financial institutions should support companies and how the monitoring of financial institutions should be sophisticated. Furthermore, the JFSA will enhance its ability to advocate its policies and appropriately communicate its initiatives at home and abroad to deepen public interest in and understanding of Japan's financial administration.

Ⅰ. Support the Economy and People’s Lives for Future Growth

With future prospects remaining uncertain due to the COVID-19 pandemic and the Russian invasion of Ukraine, the JFSA will support the economy and people's lives from the financial aspect and lead the economy to growth. The JFSA will also encourage financial institutions to support their clients’ business and to strengthen their business bases.

Ⅱ. Build the Financial System in which Economic Growth is Achieved by Resolving Social Issues and is Shared with Individuals

The JFSA will improve the financial system in order to facilitate firms to address social issues such as climate change, realizing the digital society and support for start-ups, which would lead the economy to growth. At the same time, the JFSA will promote the shift of individual’s financial assets from savings to investment and realize a virtuous cycle in which the fruits of economic growth are widely shared with individuals.

Ⅲ. Evolve JFSA’s Financial Administration Further

Amid significant changes in the domestic and international environment, the JFSA will improve the competence of the staff, enhance data analysis, and strengthen policy communications both domestically and internationally.

Actions Required of Financial Institutions, etc. in Light of the FATF's Fourth Mutual Evaluation of Japan

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1. Introduction

On August 30, 2021, the Financial Action Task Force (hereinafter referred to as the "FATF") published the FATF "Anti-money laundering and counter-terrorist financing measures Japan Mutual Evaluation Report" (hereinafter referred to as the "Report") as a result of the fourth mutual evaluation of Japan (hereinafter referred to as the Fourth Mutual Evaluation"). On the same day, the government published the "AML/CFT/CPF Action Plan" (hereinafter referred to as the "Action Plan"), which is intended to address the issues pointed out on the Fourth Mutual Evaluation.*1

Of the issues pointed out on the Fourth Mutual Evaluation, the main issues related to financial institutions, etc. were the following: (i) that financial institutions, etc. excluding large-size banks and some fund transfer service providers have a limited understanding of the risks related to money laundering, terrorist financing and proliferation financing (hereinafter referred to as "money laundering, etc.") and obligations related to anti-money laundering, etc. measures (e.g., 335th paragraph of the Report); (ii) that collaboration between customer due diligence and transaction monitoring is inadequate (e.g., 360th paragraph of the Report) due to financial institutions, etc.'s failure to update customer information (e.g., 363rd paragraph of the Report), and (iii) that the false-positive ratios regarding transaction monitoring and filtering are high (e.g., 339th paragraph of the Report).

Below, explanations will be provided about some of the important points of attention for financial institutions, etc. in light of the issues pointed out on the Fourth Mutual Evaluation while references are also made to the specifics of the revisions of the "Frequently Asked Questions Regarding Guidelines for Anti-Money Laundering and Combating the Financing of Terrorism (FAQ)" (hereinafter referred to as the "FAQ") that were made in March 30 and August 5, 2022 (hereinafter, those revisions are referred to as the "March revision" and the "August revision," respectively).*2

The cover of the FATF fourth Mutual Evaluation Report of Japan.

2. Challenges for financial institutions, etc. and the direction of future enhancement

(1) Understanding of risks

Techniques of money laundering, etc. and the environment surrounding financial institutions, etc. are changing from day to day. Therefore, the Guidelines for Anti-Money Laundering and Combating the Financing of Terrorism (hereinafter referred to as the "GL") requires financial institutions, etc. to take anti-money laundering, etc. measures under a risk-based approach. Financial institutions, etc. must identify and evaluate the money-laundering, etc. risks that they face and take mitigation measures in accordance with the risks evaluated.

Financial institutions, etc. are expected to be able to enhance their understanding of risks by carefully identifying and evaluating risks in light of the GL and the FAQ.

*1 FATF Anti-money laundering and counter-terrorist financing measures Japan Mutual Evaluation Report and "AML/CFT/CPF Action Plan," published on August 30, 2021: https://www.fsa.go.jp/inter/etc/20210830/20210830.html (Available in Japanese)

*2 Frequently Asked Questions Regarding "Guidelines for Anti-Money Laundering and Combating the Financing of Terrorism (FAQ)"
March 30, 2022 revision: https://www.fsa.go.jp/news/r3/202203_amlcft_faq/202203_amlcft_faq.html (Available in Japanese)
August 5, 2022 revision: https://www.fsa.go.jp/news/r4/202208_amlcft_faq/202208_amlcft_faq.html (Available in Japanese)

When identifying risks, it is necessary that employees in the first and second lines of defense cooperate with each other (GL, II-2(1) [Required actions for a financial institution] (v)). That is because, in order to identify risks during the course of practical work, it is necessary for financial institutions, etc. to use sufficient information regarding their own products, services and customers. As a concrete example of cooperation between the first and second lines of defense, the August revision cited a case in which the first line replies to the second line in response to an inquiry from the latter about information necessary for identifying the risks (FAQ, pp. 28-29).

When evaluating risks, it is necessary to evaluate the levels of the identified risks while taking into consideration factors such as the volume of transactions, and the incidence rate and scale of the impact (tangible and intangible losses) (FAQ, p. 29).

(2) Updating of customer information, etc.

When conducting transactions with customers, financial institutions, etc. must appropriately check basic information regarding customers, including customer attributes and the transaction purpose, and decide on and implement necessary mitigation measures. Under the GL, this sequence of processes is referred to as "customer due diligence.“

In the Fourth Mutual Evaluation, it was pointed out that the updating of customer information in particular is inadequate.

When updating customer information, it is necessary to implement at least the following procedures: (i) identifying the scope of customer information that should be updated; (ii) determining the method of updating customer information and finalizing the scope of customer information that should be updated; and (iii) clarifying the actions that should be taken when customers refuse to cooperate with the updating of customer information.

Regarding (i), the March revision has made it easier to select customers for whom proactive actions, such as sending direct mail (DM)[*3] and updating customer information, are reserved by revising the description of the points of attention for the selection of such customers (FAQ, pp. 61-62).

Regarding (ii), the March revision has made it clear that methods other than DM that can achieve the purpose of updating customer information should also be used and that information essential to risk management should be updated (FAQ, pp. 65-66).

Regarding (iii), the August revision has indicated the view that when customers do not cooperate with the updating of information by financial institutions, etc., one possible option is to review customer risk assessment in light of the refusal of cooperation and data on past transactions, among other factors (FAQ, p. 70). In addition, regarding the elimination of risks in cases where necessary information cannot be obtained, the August revision explicitly stated that the methods of risk elimination should be considered in accordance with the sort of information that cannot be collected and that the procedures for risk elimination should be appropriately prescribed under internal regulations (FAQ, pp.72-73).

Financial institutions, etc. need to review customer risk assessment in light of updated information and set the risk detection criteria in light of the customer risk assessment.

(3) High false-positive ratios regarding transaction monitoring and filtering

Transaction monitoring refers to a method of detecting suspicious transactions through ex-post verification of transactions. Transaction filtering refers to a method of mitigating risks by preventing transactions by persons and entities subject to economic sanctions through cross-checking of customers against lists of those persons and entities.

When the false-positive ratio is high, it is important to lower the ratio because in that case, it becomes necessary to allocate many resources to processing alerts, resulting in the reduction of resources that can be allocated to other measures.

On the other hand, it is also necessary to prevent failure to detect suspicious transactions and appropriately implement suspicious transaction reporting.

Financial institutions, etc. need to appropriately adjust detection volume through verification of the effectiveness of the method of transaction monitoring.

3. Conclusion

The issues pointed out in the Fourth Mutual Evaluation with respect to financial institutions, etc. can be resolved by enhancing the preparedness to address money laundering, etc. in light of the GL and FAQ.[*4]

The FSA will continue to verify the development of preparedness by financial institutions, etc. through risk-based inspection and supervision, and take measures to enhance their preparedness, including taking administration actions as necessary.

[*3] At present, many financial institutions update customer information after receiving replies to direct mail (DM), etc. sent to customers asking for new information, for example.

[*4] The FSA requires all financial institutions, etc. to complete by the end of March 2024 the actions based on [Required actions for a financial institution] under the GL ("Setting of the Deadline for Developing Preparedness Related to AML/CFT Measures" [https://www.fsa.go.jp/news/r2/20210531_amlcft/2021_amlcft_yousei.html]) (Available in Japanese)

Overview of the "Supervisory Guidance on Climate-related Risk Management and Client Engagement"

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In July 2022, the FSA published the "Supervisory Guidance on Climate-related Risk Management and Client Engagement" (hereinafter referred to as the "Guidance"), which presents the FSA's approach for supervision and inspection with respect to climate change for the first time. Below, an overview of the Guidance will be provided.

1. Background to and characteristics of the Guidance

With respect to climate change, as initiatives toward achieving carbon neutrality steadily proceed, interest in climate change continues to grow. Companies are facing various challenges in the surrounding environment due to technological innovations to mitigate climate change, changes in national policies and regulations, and changing values among consumers and investors.

Those changes related to climate change could become either opportunities or risks for companies, depending on how they respond. The changes could also turn into opportunities or risks for financial institutions through their effects on loans, for example. It may be said that by mitigating client companies' climate change-related risks, financial institutions will be able to acquire opportunities for themselves and reduce their own climate change-related risks (Figure 1).

The FSA believes that it is important for financial institutions to establish a business foundation that is resilient to the changes and to ensure business sustainability through supporting their clients' efforts to address climate change. From the viewpoint of supporting such efforts of financial institutions, the Guidance (for the main structure, see Figure 2) documents viewpoints of supervisory dialogues regarding financial institutions' climate-related risk management in order to evaluate the effects of climate change on their clients and themselves and appropriately respond (Chapter III), and it also illustrates approaches and case example of client engagement, which should serve as references for financial institutions to take actions (Chapter IV).

Figure 1: Relationship between client firms and financial institutions' opportunities and risk

2. Characteristics of climate-related effects and financial institutions' climate-related risk management

Chapter III of the Guidance indicates viewpoints of supervisory dialogues regarding financial institutions' climate-related risk management.

Among the characteristics of climate-related effects are the following: the effects would materialize in a long-term horizon; high uncertainty remains around how they would materialize and how significant their impacts are; and the effects affect financial institutions through various channels.

Figure 2: Main structure of the Guidance

II. Discussions and background on climate change	・Japanese and global initiatives toward realizing carbon neutrality ・Economic, industrial and social changes ・Effects on financial and capital markets and financial institutions ・International discussions on financial institutions' response to climate change
III. Viewpoints of Dialogue on Financial Institutions' Responses to Climate Change	1. Strategies and governance related to climate change 2. Recognition and assessment of opportunities and risks related to climate change 3. Addressing opportunities and risks related to climate change 4. Communication with Stakeholders
IV. Approaches to support clients in responding to climate change	1. Assessing the impact on clients 2. Development of appropriate support measures for clients

It is important for financial institutions to understand those characteristics and the transmission channels of the effects, and develop strategies from a medium to long-term perspective including how to support customers' responses to climate change and how to stabilize their own businesses through such assistance. The Guidance presents the strategies and internal control framework that financial institutions should develop to that end.*

The FSA hopes that the Guidance will encourage financial institutions to hold active discussions once again on how climate change may affect their businesses and how to respond.

3. Approaches to support clients

Chapter IV of the Guidance describes three perspectives for identifying opportunities and risks for client companies (technical perspective, industrial perspective and perspective on changes in the natural environment [Figure 3]), and examples of support measures such as the provision of consulting and solutions, the provision of funding for growth, area-wide support for companies and strengthening cooperation among relevant parties. As the Guidance also illustrates many case examples in a "BOX" column, which serve as references for financial institutions to take actions.

4. Current situation of financial institutions and the FSA's future activities

The FSA recognizes that in many cases, financial institutions are engaging in activities to respond to climate change. On the other hand, practices and methodologies for responding to climate change are still evolving although there are ongoing discussions on various topics, including disclosure and auditing, private capital mobilization, enhancement of capital market mechanisms, and climate-related risk management. Financial institutions need to deal with various challenges in light of the international discussions, but the FSA believes that the first step toward responding to climate change is to have a common understanding with stakeholders, including customers. The FSA hopes that the Guidance will serve an opportunity for such dialogue.

The FSA will make efforts to understand how each financial institution is trying to address climate change through dialogue, identify challenges for financial institutions to advance their efforts. Then, the FSA will encourage financial institutions to strengthen their efforts by providing information and sharing know-how on risk management and client engagement.

Figure 3: Identification of the effects on client companies

Viewpoints	Relevant information
Technical perspective	Information related to technologies owned by client companies ・Whether they contribute to the efficient use of energy and reduction of greenhouse gas emissions ・What extent they can be implemented as products
Industrial perspective	High-level view of the entire industry such as; ・Strategic changes at their primary contractors ・Procurement and production processes that are bottlenecks in reducing emissions throughout the supply chain ・Whether or not alternative raw materials and technologies can be introduced ・mitigation measures such as shifting procurement energy sources
Viewpoints related to changes in the natural environment	・Information on the meteorological conditions and geographical environment of each region ・The vulnerable regions and projects and the extent of their impacts

Figure 4: Approaches and case example of client engagement

Providing Consulting and Solution-delivery Services

Examples
- Supporting clients in making their greenhouse gas emissions "transparent"
- Establishing a link between clients who do not have energy-efficient technologies and those who do (client-client matching)

Supplying Funding for Growth

Examples
- Providing financing to support decarbonization programs tailored to the specific needs of clients (e.g., transition loans and green loans)
- Providing financing via growth-targeted investment funds that leads to fostering new technologies and industries in response to climate change

Providing Area-wide Support / Improving Cooperation among Stakeholders

Examples
- Providing area-wide support, such as mapping out a strategy for a group of linked suppliers in a certain region, taking into account the strategies of core manufacturers
- Supporting community-wide initiatives toward decarbonization and resource utilization in collaboration with local governments and research institutes

* It should be noted that the Guidance considers scenario analysis to be an effective means of evaluating climate change-related opportunities and risks. The FSA and the Bank of Japan, in cooperation with the three megabanks and the three major non-life insurance groups, implemented the Pilot Scenario Analysis Exercise Based on Climate-Related Common Scenarios and published a summary of the results on August 26, 2022. ("Pilot Scenario Analysis Exercise on Climate-Related Risks Based on Common Scenarios": https://www.fsa.go.jp/en/news/2022/20220826.html)

Tentative decisions on the fundamental elements of the Economic Value-Based Solvency Regulation

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On June 30, 2022, the "Tentative Decisions on the fundamental elements of the Economic Value-Based Solvency Regulation"[*1] which concerns the insurance business, was published. Below, the background to and the key points of that will be described.

1. Solvency margin regulation concerning insurance companies

Insurance is a scheme to prepare for various risks that may arise in everyday life. As providers of such insurance, insurance companies are required to have a sufficient payment ability to fulfill insurance obligations even when a risk that is beyond normal predictability, such as a major disaster that only occurs once every dozens of years, has materialized, for example.

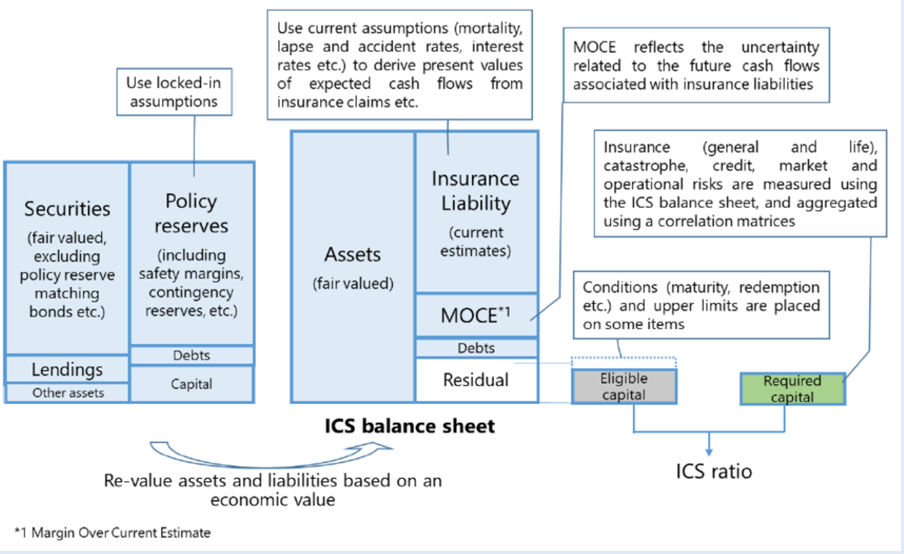
The solvency margin regulation, which is intended to ensure that insurance companies have a sufficient payment ability, has played an important role in regulatory administration over insurance and in the insurance market since its introduction following the amendment of the Insurance Business Act in April 1996.

However, amid the significant changes in the risks surrounding insurance companies, exemplified by the progress in the aging of society with a low birth rate, changes and diversification of consumers' needs, the continuation of the low-interest-rate environment, a rise in the volatility of domestic and foreign economies and markets, increased climate change risk, including the increased frequency and severity of natural disasters, and the emergence of cyber risks, it has been pointed out that the current solvency margin regulation may be unable to adequately reflect medium and long-term risks faced by insurance companies and may be failing to promote proactive enhancement of governance and risk management by insurance companies.

2. Economic value-based solvency assessment

Discussions have been held on "economic value-based" assessment of assets and liabilities as a measure to deal with those challenges. "Economic value-based" refers to the approach of assessing all assets and liabilities at market value (fair value). Insurance liabilities are evaluated based on a “market consistent approach” by using discount rates consistent with the financial market and expected accident rates[*2] (see Figure 1).

(Figure 1) Overview of the ICS



[*1] "Publication of the 'Tentative decision on the Basics of Economic Value-Based Solvency Regulation, etc.,'" published on June 30: https://www.fsa.go.jp/news/r3/hoken/20220630_2.html (Available in Japanese)

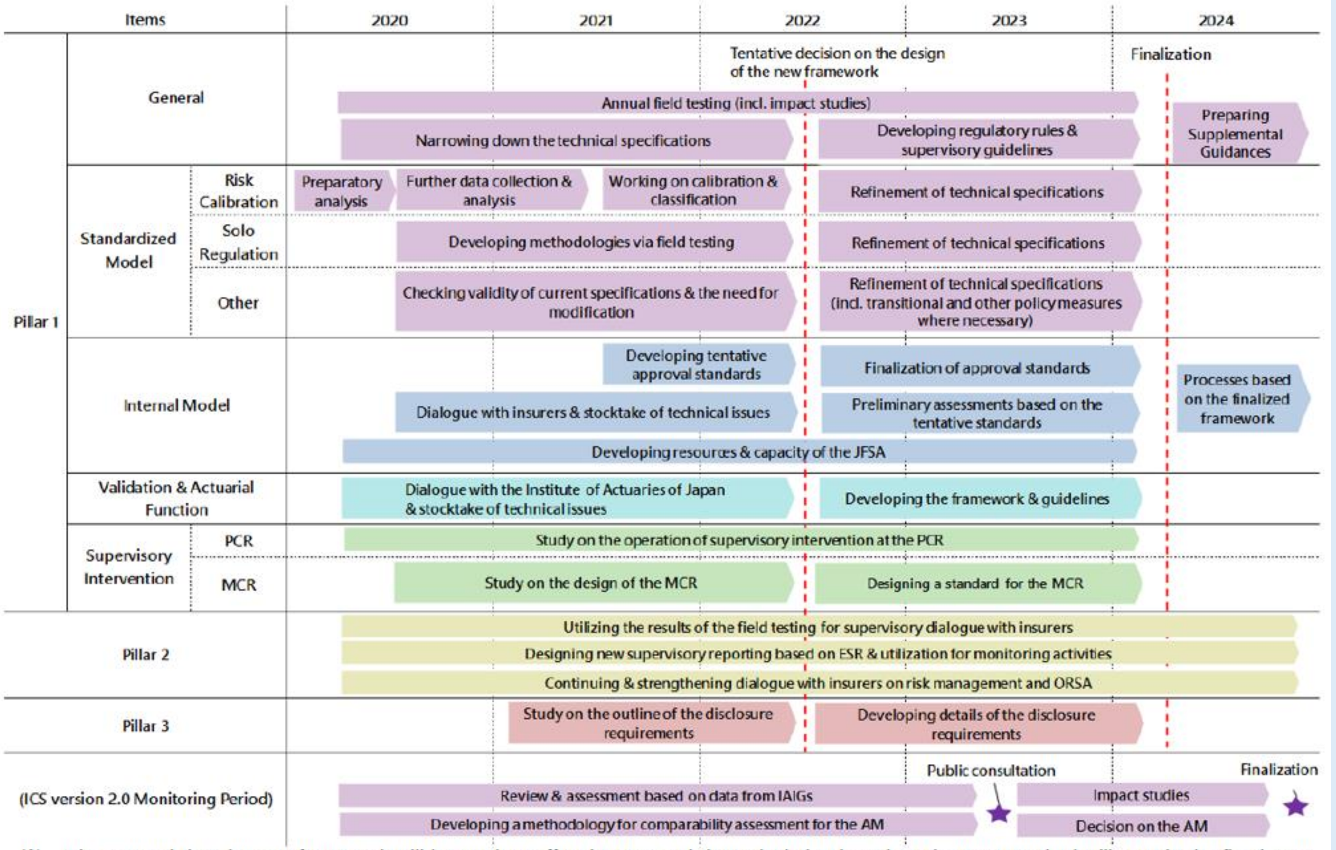
[*2]. An approach similar to market price assessment. Insurance liabilities (unlike many other asset items) do not have market prices, and therefore, they are assessed through a "market-consistent" method (e.g., using a discount rate based on a market interest rate, or an expected future accident rate). The current solvency margin ratio (SMR) is calculated under the lock-in method of assessing liabilities (which fixes the discount rate, the occurrence rate, etc. at the levels as of the time of contract).

The FSA is considering how to introduce into Japan an "economic value-based solvency regulation" that represents a new prudence policy based on economic value, because it has the merit of making it possible to identify insurance companies' assets and liabilities in a way that better reflects the actual economic environment. Among Japanese insurance companies, there are also moves to use an economic value-based approach for the purposes of internal control and voluntary disclosure. In addition, the International Association of Insurance Supervisors (IAIS), which is comprised of national insurance supervisory authorities, is developing the Insurance Capital Standard (ICS), which has incorporated an economic value-based approach.

In the meantime, with regard to a new framework of solvency regulation, the "Report by the Advisory Council on the Economic Value-based Solvency Framework"[*3] (hereinafter referred to as the "Advisory Council Report"), which was published on June 26, 2020, recommended that the FSA should aim to make a tentative decision on the basics of the framework by around 2022 while bearing in mind the timeline, including finalizing the standard by around the spring of 2024 and also taking into consideration analyses using domestic field tests (FTs) and international developments (see Figure 2).

Afterwards, the FSA published the status of deliberation on the points of discussion regarding the design of the framework as of June 2021 in the form of "Status of Deliberation on Economic Value-Based Solvency Margin"[*4] (hereinafter referred to as the "Deliberation Status") and held concrete discussions with a view to making a tentative decision in 2022 by analyzing the results of FTs conducted in the second half of 2021 and by engaging in dialogue with insurance companies and other relevant parties.

(Figure 2) Proposed timeline towards the introduction of the new framework



※ It is assumed that the new framework will be put into effect in 2025 and that calculation based on the new standard will start in the fiscal year ending March 31, 2026.

*3 "Publication of the 'Report by the Advisory Council on the Economic Value-based Solvency Framework,'" published on June 26, 2020: https://www.fsa.go.jp/news/r1/sonota/20200626.html (Available in Japanese)

*4 "Status of Deliberation on Economic Value-Based Solvency Regulation, etc.," published on June 30, 2021: https://www.fsa.go.jp/policy/economic_value-based_solvency/index.html#esr (Available in Japanese)

3. Key points of the tentative decision

The tentative decision announced at this time offers a provisional conclusion concerning the basics of the regulation and the basic direction of future deliberations in light of the results of the deliberations so far conducted and international developments. By making the tentative decision on the basics before introducing the new regulation, the FSA aims to encourage insurance companies to take steps to develop their preparedness, including by making investment in computer systems.

The details of the tentative decision conform with "Pillars 1 to 3" that were indicated in the Advisory Council Report. Because of the abovementioned purpose, the tentative decision focuses mainly on the standard model approach and the validation framework concerning the economic value-based solvency ratio (ESR) under the first pillar. With respect to ideal supervisory intervention under the first pillar and the points of discussion related to the second and third pillars, the tentative decision indicates the currently conceivable main points of discussions and the direction of future deliberation.

(1) Pillar 1 (the standard model approach, the framework of verification concerning ESR

Pillar 1, which corresponds to the "solvency regulation" as narrowly defined, which is usually used, lays down the basic benchmark (standard model) for solvency evaluation and prescribes the framework for supervisory intervention intended to protect policyholders.

Regarding the timeline toward the introduction of the new regulation, the tentative decision requires that steady preparations and deliberations proceed on the premise of introducing the new regulation in 2025 in light of the results of FTs continuously implemented, deliberations conducted through dialogue with insurance companies and international developments. As for the standard model under the new regulation, the tentative decision states that deliberations should be conducted with respect to unique points of discussions so as to ensure that the model is suited to domestic regulation while it shares the basic structure with the ICS and that revisions should be made within the reasonable limits in light of the risk profiles of Japanese insurance companies. Regarding the current estimation of economic value-based insurance liabilities, from the viewpoint of securing the validity of estimated values and some degree of comparability, the tentative decision also requires the introduction of guidelines as something that complements the legally prescribed basic criteria concerning the evaluation and verification of insurance liabilities. In addition, it offers provisional conclusions and the future direction of deliberation on the points of discussions related to the standard model, such as the methods of calculating the various risks and states that deliberations should continue. With respect to ESR, since much is left to the reasonable judgment of insurance companies during the calculation process, the governance system that ensures the validity of the judgment is very important. Therefore, the tentative decision defines the establishment of a validation framework, including the development of internal verification systems by insurance companies and the use of outside experts, as the basic direction of deliberation and states that deliberation on the details should be conducted from now on.

(2) Supervisory intervention based on ESR and Pillars 2 and 3

In order for prudence policy to function effectively, it is important that the authorities implement appropriate supervisory intervention in a timely manner based on insurance companies' prudence benchmarks. The tentative decision states that it is desirable to hold in-depth deliberations on the details of supervisory interventions and measures and to make clear their directions as early as possible.

Pillar 2, which is characterized as a framework for the supervisory authorities to verify insurance companies' internal control based on the premise of the companies' voluntary internal control, is intended to capture risks that cannot be detected under Pillar 1 and to verify and promote the enhancement of insurance companies' internal control.

The tentative decision clarifies the direction of deliberation on the currently conceivable main points of discussion related to Pillar 2, such as the ideal visions of insurance companies' internal control and monitoring by the authorities, and states that deliberations should start in earnest from now on.

Pillar 3 is intended to encourage dialogue between insurance companies and outside stakeholders (e.g., investors) and to enhance governance and discipline over insurance companies through their information disclosure.

Regarding the disclosure requirements intended to encourage dialogue with outside stakeholders and the framework for ensuring comparability of disclosure under the new regulation, the tentative decision sets forth the basic approaches and states that more detailed deliberations should be conducted from now on.

4. Future proceedings, etc.

In light of the points of discussion and the direction of future deliberation described in the tentative decision, the FSA will steadily conduct deliberations with a view to smoothly introducing the new framework in 2025 while providing information concerning the status and direction of deliberation through analysis through its analysis based on FTs and dialogue with a broad range of relevant parities, including insurance companies.

Message to the Market (explanations of an administrative monetary penalty order case)

The Securities and Exchange Surveillance Commission (SESC) posts explanations on recommendations it has given on its website as an article titled "Message to the Market."

The "Message to the Market" posted on August 31, 2022, is summarized below.

* The whole Japanese text is available on the SESC website:
https://www.fsa.go.jp/sesc/message/20220831.html

"for investors, with investors"

Recommendation of an administrative monetary penalty order for false statements in annual securities report, etc. by Asia Development Capital Co. Ltd.

The SESC examined the suspected violation of the disclosure regulations under the Financial Instruments and Exchange Act by Asia Development Capital Co. Ltd. (hereinafter referred to as "the Company") and found the fact of legal violation as follows. Accordingly, the SESC recommended the Prime Minister and the Commissioner of the FSA to issue an administrative monetary penalty payment order on June 17, 2022.*

[Details of the legal violation]

The Company overstated the sales amount through inappropriate accounting processing and submitted the following disclosure documents, which contained false statements regarding material particulars, to the Director-General of the Kanto Local Finance Bureau.

・A total of six sets of documents, including the annual securities report for the business year that ended in March 2018 (submitted on June 28, 2018).

[Inappropriate accounting processing]

A subsidiary of the Company participated in multiple chains of transactions based on the understanding that it was participating in chains of sales from manufacturers of storage batteries to final sales destinations via several intermediary companies. However, those activities represented fictitious transactions under which storage batteries that were supposed to be traded did not exist. Funds related to sales and procurement in those chains of transactions merely flowed back and forth between the parties concerned without actual transactions.

As a result, the Company overstated its sales amount and sales cost.

The SESC will continuously take strict actions against violations of disclosure regulations, such as false statements in annual securities reports, etc., as seen in this case.

* "Recommendation for an administrative monetary penalty payment order against Asia Development Capital Co. Ltd. for making false statements in its disclosure documents," published on June 17, 2022. (https://www.fsa.go.jp/sesc/news/c_2022/2022/20220617-1.html) (Available in Japanese)

Children‘s Visit to Kasumigaseki (Government District)

On August 3 and 4, 2022, the "Children's Visit to Kasumigaseki" was held. The event is aimed at deepening the contact between parents and children and letting children have a taste of society on a broad basis through experimental activities. Government ministries and agencies including the Financial Services Agency participate in the event, led by the Ministry of Education, Culture, Sports, Science and Technology.

The FSA devised the online program "Let's Start!— Financial Education" and the practical experience program "Let's Go to FSA!!" in order to help children easily understand the role and importance of money through first-hand experience.

1. Online program "Let's Start! — Financial Education"

➢ **August 3 session: "Let's Enjoy Cashless Payment!"**

In this session, the children learned about the types and mechanism of cashless payment while considering which circumstances are suited for cashless payment and how cashless payment should be used. They actively participated in the session via chat and video.

➢ **August 4 session: "Basics for Investment Beginners"**

In this session, the children learned about a broad range of matters, from basic investment terms such as stocks, interest and risk to the meaning of investing in companies. They eagerly listened to the session while taking notes. They appeared to enjoy learning about investment. For example, the children were absorbed in watching a skit played by an instructor impersonating the president of an investee company to explain the meaning of investing in companies, and they also participated in games and quiz competition.

Photo: Children participating in the online program

2. Practical experience program "Let's Go to FSA!!"

On August 4, the practical experience program "Let's Go to FSA!!" was held. Children were invited to the FSA, and an FSA employee explained the FSA's operations in an interview format and delivered a lecture speech on financial and economic education entitled "Money Lesson."

When the FSA employee asked questions and gave quizzes, many children gave replies.

Photo: A scene from the "Money Lesson" lecture speech on financial and economic education

In a tour of the FSA, the children were shown into the Minister's office and the FSA courtroom. In the Minister's office, not only children but also parents appeared to enjoy themselves as they sat in the Minister's chair and posed for a commemorative photo.

Photo: Participants taking a commemorative photo

FSA's symbol mark

Starting with this month's issue, we introduced a new section called "FSA Plus."

In this section, we will provide tidbits of trivia related to the FSA on an irregular basis so that readers can get to know the agency better.

We will try to offer topics of casual conversation.

The first topic of the new section is FSA's symbol mark.

The FSA symbol mark was established and announced on December 25, 2000, as part of an effort to promote the understanding of the FSA's missions widely among the general public and has been used since January 6, 2001, when the ministries and agencies were reorganized.

At that time, the symbol mark had the following three design concepts:

(1) The symbol mark was intended to represent a stylization of the letters "F," "S," and "A," the initials of the Financial Services Agency.

(2) The shape of the letter "S" in the middle was intended to express a smooth flow of finance, while the letters at both ends were designed so as to create an impression of guarding that flow.

(3) The color of the symbol mark, light blue, was intended to express a smooth flow of finance and the transparency of the FSA's regulatory administration.

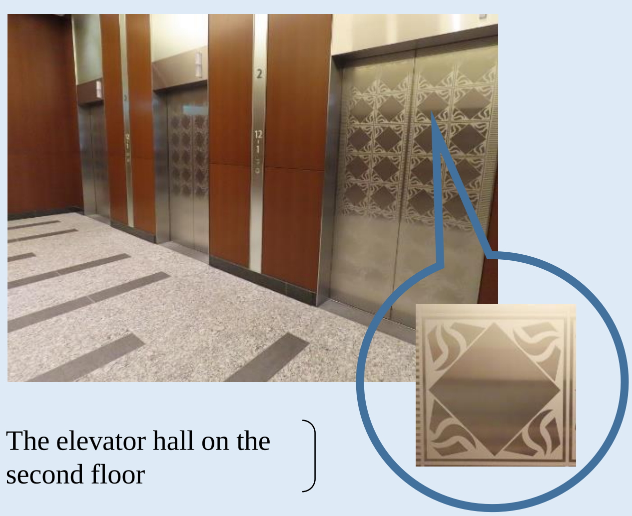
FSA's symbol mark is also used in the FSA's logo design (lower left: the Japanese logo; lower right: the English logo).

Even now, nearly 22 years since then, we believe that the symbol mark expresses the ideal vision of the FSA.

The symbol mark is widely used at the FSA, for example on the FSA's official envelopes and employees' name cards, as well as on the covers of documents prepared by the FSA for government meetings and in the profile image on the FSA Twitter account.

The symbol mark is printed not only on the FSA's envelopes and name cards but also on a wide range of items handed out for publicity, including pamphlets and clear files.

The symbol mark is also featured at the front of the vehicle entranceway for the FSA on the first basement floor, the front of the entrance to the FSA on the second floor, and the elevator doors on the 17th floor, where the offices of the Minister, the State Minister and the Parliamentary Vice-Minister, as well as Commissioner are located. A surprising large number of people have not noticed the symbol used in those places. If you ever visit the FSA, be sure to look for the symbol mark.



The elevator hall on the second floor

JFSA's Major Activities in August (August 1 to August 31, 2022)

- Public Consultation on Partial Amendment for Regulatory Notice Specifying the Documents Based on Article 2 (1) of the Cabinet Office Order on Financial Instruments Business, etc. (August 31, 2022)
- The FSA publishes the status of loans held by all banks as of the end of March 2022, based on the Financial Reconstruction Act (August 26, 2022)
- Release of “Pilot Scenario Analysis Exercise on Climate-Related Risks Based on Common Scenarios” (August 26, 2022)
- Stewardship Code : 322 institutional investors have signed up to the Principles for Responsible Institutional Investors as of July 31, 2022 (August 10, 2022)
- Updated : Guidebook for Registration of Investment Management Business and Other Financial Instruments Businesses (August 9, 2022)
- Sustainable finance (August 4, 2022)
- Updated : Financial Services Agency’s Efforts to Promote Innovation (August 3, 2022)

- JFSA's official English Twitter account
  https://twitter.com/JFSA_en

We are promoting information dissemination using Twitter!

- Please send your opinions using the following email address to the Public Relations Office's personnel in charge of Access FSA.

  E-mail : fsa_kouhou@fsa.go.jp

Editorial Postscript

As a result of the cabinet reshuffle last month, State Minister FUJIMARU Satoshi and Parliamentary Vice-Minister SUZUKI Eikei took office.

Under the new leadership, the FSA submitted budget and personnel requests for the next fiscal year as well as requests for tax system reform and also published “The JFSA Strategic Priorities July 2022-June 2023” at the end of last month.

From this month onward, we expect that there will be various moves toward executing policy measures on which deliberations have been so far conducted.

Access FSA will strive to provide full information on such moves. We hope that readers will also take a look at the new section called "FSA Plus."

We appreciate your continued readership of Access FSA.

MORIYA Takayuki, Director,
Public Relations Office, FSA

(*The opinions expressed in this report are the personal views of the author and do not necessarily reflect the organization with which the author is affiliated.)