

Outline of the Interim Report of the First Subcommittee of the Financial System Council

Purpose

It is appropriate to enact the “Investment Services Law (provisional title)” to establish a framework of comprehensive and cross-sectional protection of users of a wide range of financial products, and to allow market functions to work to the fullest potential.

I. Scope

(1) In order to achieve appropriate protection of users and improve user convenience by enlarging a scope of products and services of the institutions, the Investment Services Law will establish a comprehensive and cross-sectional legal system as a general law, that will regulate sales, asset management and other activities of financial businesses. Moreover, the integration of sales and solicitation rules for deposits and insurance, and the rules for investment services will be continuously discussed with a view to establishing the Financial Services and Markets Law.

(2) The following activities will be regulated as investment services businesses:

- (i) sales and solicitations;
- (ii) asset management and investment advise; and
- (iii) administration of investment products.

II. Regulations

(1) The new legal system will be based on the framework of the current Securities and Exchange Law and Securities Investment Advisor Law and have flexible structures that:

- (i) incorporate regulations of other laws and rearrange them by their functions in a cross-sectional manner;
- (ii) promote deregulation of sales and solicitation rules of investment products for professional investors such as institutional investors; and
- (iii) ensure appropriate protection of investors for the sales and solicitation of investment products for non-professional investors such as retail investors.

(2) With the enlargement of the scope of ancillary and side businesses, a firm will be required to register in principle for entry to the market, and different criteria for registration, depending on the nature of its businesses, will be applied, such as (i) requirements equivalent to the current requirements for a securities company, (ii) requirements equivalent to the current requirements for a securities-introducing agent, and (iii) requirements that fall between (i) and (ii) above.

(3) In terms of a rule of conduct, fiduciary duty will be prescribed in a cross-sectional manner. In addition, duties, such as the duty to provide documents and explain such matters as disclosure of fees and commissions, principles of suitability, rules of advertisement, and prohibited acts will be required in a cross-sectional manner in accordance with the natures of financial products such as a degree of risks

III. Collective Investment Schemes

(1) The scope of the Investment Services Law will cover sales and solicitations of all kinds of funds and apply minimum regulations to the funds, such as (i) notification or registration, of funds, (ii) administration of customers' assets, (iii) requirements for a fund manager, (iv) fiduciary duty and prevention of conflict of interests, and (v) investment performance reports.

(2) Except for rules such as the arrangement of a scheme that needs to be prescribed as a special law, the current laws for regulating funds will be preferably rearranged in a functional and cross-sectional manner depending on the natures of the regulations.

IV. Markets Regulation

(1) A broad range of products, in addition to the investment products such as securities and financial futures, should be traded on exchanges.

(2) Improvement of examination and oversight of listings conducted by exchanges and revision of the listing criteria will be desirable. The role of the exchanges as self-regulatory organizations (SROs) for the governance of listed companies should be reviewed.

(3) Disclosure requirements tailored to the natures of the investment products, definition of qualified institutional investors, quarterly disclosure system and internal control over financial reporting should be continuously reviewed.

(4) Rules on takeover bids and reporting system of large shareholdings need to be reviewed.

V. Enforcement

(1) The administration of capital markets needs to be substantially strengthened. In line with the globalization of financial and capital markets, international cooperation, improvement of the enforcement structure and frameworks of exchange of information in the securities area (securities MOU) should be established as early as possible.

(2) The administrative civil money penalty system and provision of investors' rights to demand compensation for damage will be continuously discussed.

(3) By strengthening the functions of SROs, mandatory membership, the linkage among SROs regarding handling of complaints and mediation of disputes, and role of SROs in accordance with the international trend should be continuously considered.

(4) It is appropriate to take measures that enable a regulatory authority to make inquiries and take administrative actions on persons to whom the company conducting an illegal activity has assigned or outsourced its business.

(5) The role of financial education should be discussed.