

Summary of Monitoring Priorities for Securities Businesses (July 2021-June 2022)

Environment surrounding FIBOs

1. Environment surrounding FIBOs

- The declining birthrate and aging population, an intensifying race to cut brokerage commissions, expanding impact of COVID-19
- Progress in digitalization
- International interest in Anti-Money Laundering/Countering the Financing of Terrorism (AML/CFT) measures

2. Changes to regulatory frameworks for FIBOs

- New measures to further promote customer-oriented business conduct, reviewing financial services in the super-aged society
- Establishing guidelines for preventing illegal access in Internet transactions
- Measures to improve transparency in dark pool trading
- Measures accompanying the realization of the Integrated Exchange
- Establishing a notification system for financial service intermediary businesses and investment management businesses for foreign investors in Japan

3. Findings through monitoring of securities businesses in the previous business year

- (Type I FIBOs) Inadequate salesperson-led investment solicitation, illegal withdrawals of customers' money through illegal access, etc.
- (Investment management business operators) Breach of duty of due care of a prudent manager, including failure to grasp the actual state of managing investment assets
- (Type II FIBOs) Using false indications and misleading indications regarding important matters to solicit customers to acquire shares of a loan-type fund
- Without being registered as a FIBO, a business operator was soliciting customers to acquire financial instruments

Industry-wide monitoring strategies

1. Customer services under the impact of COVID-19
2. Developing internal control environments focusing on appropriate investment solicitation based on the clarification of the principle of suitability and establishing customer-oriented business conduct
3. Business model and market changes under the falling birthrate and aging population, progress in digitalization, etc. and the development of internal control environments responding to such changes
4. Sufficiency of cybersecurity measures and the status of risk management in system amid progress in digitalization
5. Firm establishment of internal control environments for AML/CFT
6. Implementation of measures to improve or prevent the recurrence of matters pointed out in results of internal audits or examinations by self-regulatory organizations

In addition to the above, the SESC will flexibly examine FIBOs on other themes in response to changes in the environment surrounding them.

The SESC will also cooperate with relevant parties in considering monitoring approach in line with the revision of regulations regarding the firewall between banking and securities businesses.

Monitoring strategies for various FIBO business models

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 If it is necessary to confirm actual sales practices at sales offices, the SESC will swiftly inspect relevant sales offices. Control environments for conflict-of-interest management regarding cooperation between banking and securities businesses [3 mega banking groups]
	Foreign securities firms	<ul style="list-style-type: none"> Development of internal control environments responding 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 internal control environments in line with their business model changes, such as initiatives to eliminate brokerage commissions, increases in products and launch and expansion of face-to-face sales activities in collaboration with independent financial advisors
	Semi-major/ regional securities firms	<ul style="list-style-type: none"> Inappropriate solicitation and other problems regarding investor protection, including steps taken to conform to the principle of suitability Effectiveness of internal control environments from the viewpoint of business models or governance at securities firms where major shareholders or business management systems have changed.
	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 regarding advertising and sales/solicitation regulations Disclosure of risk information, reflection of stress test results to capital and development of transaction data storage and reporting arrangements
Investment management business operators	<ul style="list-style-type: none"> Grasp of investment status, development of control environments for investment management (including those outsourced) and conflict-of-interest management, etc. 	
Investment advisors/agencies	<ul style="list-style-type: none"> Misleading advertisement, solicitation through false explanation, etc. 	
Type II FIBOs, QII business operators, independent financial advisors, and others	<ul style="list-style-type: none"> Funds advertising high returns and substantiality of investment target projects, etc. [Type II FIBOs, business operators, etc., engaging in specially permitted businesses for qualified institutional investors (QII business operators)] Adequacy of their investment solicitation, sufficiency of control by entrusting FIBOs [Independent financial advisors] Risk-based securities businesses monitoring in light of the firm's particular business types [registered financial institutions, credit rating agencies, securities finance companies, self-regulatory organizations, etc.] 	
Unregistered business operators	<ul style="list-style-type: none"> Exercising investigative authority proactively to seek court injunctions on illegal conduct Enhancing information dissemination, including the public disclosure of unregistered business operators' names, their representatives' names and their illegal conduct, etc. Collaborating proactively with relevant JFSA divisions, Local Finance Bureaus, investigative authorities and the Consumer Affairs Agency. 	

*The SESC will also verify FIBOs' responses to changes in regulatory frameworks.

Approach to monitoring securities businesses

- The SESC will select FIBOs for inspection based on risk assessment from various viewpoints, including business models, in cooperation with relevant JFSA divisions. Inspection will be mainly conducted in cases where it is necessary to comprehend further details, such as:
 - ① a relevant law and/or regulation is breached or there is a deficiency in business operations that requires a prompt in-depth examination;
 - ② a financial instruments is offered with an unclear risk profile, necessitating an examination of its solicitation activities;
 - ③ the actual situation of business operation is not fully comprehended from an information analysis based on monitoring (including where there is a long period between examinations);
 - ④ There is a possible serious problem concerning investor protection, including the inappropriate segregated management of customer assets
- Through its inspection, the SESC aims not only to point out problems and take actions, such as making recommendation for administrative disciplinary actions, but also to analyze the whole picture of the problems to identify their root causes, so that effective measures to prevent problems will be developed. Furthermore, if the need to improve business operations is identified before any potential issues materialize, the SESC will describe it as “Items to be noted” in the notification of completion of inspection to share the awareness with the inspected businesses and urge them to build effective internal control environments or take other actions to address the issues.
- To prevent the spread of COVID-19 infections, the SESC will, for the time being, conduct inspection with the utmost care for the inspection targets’ COVID-19 infection prevention measures, including through using remote conference systems.

Cooperation with relevant organizations and dissemination of inspection results

- The SESC and Local Finance Bureaus will work closely from the planning stage of monitoring and inspection and conduct joint inspection as needed. In addition, The SESC will collect and share information with Local Finance Bureaus, consider appropriate monitoring methods and focus on training required for them.
- The SESC will continue collaborating closely with self-regulatory organizations, sharing information with them in a timely manner to promote securities businesses monitoring effectively and efficiently.
- The SESC will share inspection results with inspected FIBOs’ audit-related officials and outside directors, encouraging these FIBOs to voluntarily improve practices.