

ASEAN+3 BOND MARKET GUIDE 2016 JAPAN

ASEAN+3 BOND MARKET GUIDE 2016 JAPAN



Creative Commons Attribution 3.0 IGO license (CC BY 3.0 IGO)

© 2016 Asian Development Bank
6 ADB Avenue, Mandaluyong City, 1550 Metro Manila, Philippines
Tel +63 2 632 4444; Fax +63 2 636 2444
www.adb.org

Some rights reserved. Published in 2016.
Printed in the Philippines.

ISBN 978-92-9257-501-4 (Print), 978-92-9257-502-1 (e-ISBN)
Publication Stock No. RPT168186-2

Cataloging-In-Publication Data

Asian Development Bank.
ASEAN+3 bond market guide 2016 Japan
Mandaluyong City, Philippines: Asian Development Bank, 2016.

1. Regional cooperation. 2. Regional integration. 3. ASEAN+3. 4. Bond market I. Asian Development Bank.

The views expressed in this publication are those of the authors and do not necessarily reflect the views and policies of the Asian Development Bank (ADB) or its Board of Governors or the governments they represent.

ADB does not guarantee the accuracy of the data included in this publication and accepts no responsibility for any consequence of their use. The mention of specific companies or products of manufacturers does not imply that they are endorsed or recommended by ADB in preference to others of a similar nature that are not mentioned.

By making any designation of or reference to a particular territory or geographic area, or by using the term “country” in this document, ADB does not intend to make any judgments as to the legal or other status of any territory or area.

This work is available under the Creative Commons Attribution 3.0 IGO license (CC BY 3.0 IGO)
<https://creativecommons.org/licenses/by/3.0/igo/>. By using the content of this publication, you agree to be bound by the terms of this license.

This CC license does not apply to non-ADB copyright materials in this publication. If the material is attributed to another source, please contact the copyright owner or publisher of that source for permission to reproduce it. ADB cannot be held liable for any claims that arise as a result of your use of the material.

Attribution—In acknowledging ADB as the source, please be sure to include all of the following information:

Author. Year of publication. Title of the material. © Asian Development Bank [and/or Publisher].
URL. Available under a CC BY 3.0 IGO license.

Translations—Any translations you create should carry the following disclaimer:

Originally published by the Asian Development Bank in English under the title [title] © [Year of publication]
Asian Development Bank. All rights reserved. The quality of this translation and its coherence with the original text is the sole responsibility of the [translator]. The English original of this work is the only official version.

Adaptations—Any adaptations you create should carry the following disclaimer:

This is an adaptation of an original Work © Asian Development Bank [Year]. The views expressed here are those of the authors and do not necessarily reflect the views and policies of ADB or its Board of Governors or the governments they represent. ADB does not endorse this work or guarantee the accuracy of the data included in this publication and accepts no responsibility for any consequence of their use.

Please contact publications@adb.org if you have questions or comments with respect to content, or if you wish to obtain copyright permission for your intended use that does not fall within these terms, or for permission to use the ADB logo.

Note:

Corrigenda to ADB publications may be found at <http://www.adb.org/publications/corrigenda>

Contents

Figures and Tables	vi
Foreword	viii
Acknowledgments	ix
Abbreviations	x
I. Overview	1
A. Introduction	1
B. Liquidity-Enhancing Measures in the Japanese Government Bond Market	5
C. Secondary Market Overview	6
D. Japanese Government Bond Market	7
E. Liberalization of the Japanese Yen and the Corporate Bond Market	8
F. Tide for Change in the Corporate Bond Market	10
II. Legal and Regulatory Framework	17
A. Legal Tradition	17
B. English Translation of the Law	17
C. Legislative Structure—Bond Market	17
D. Japan Bond Market Regulatory Structure	18
E. Self-Regulatory Organizations and their Roles in the Japan Bond Market	20
F. Legal Framework of Public Offering and Private Placement	24
G. Securities Issuance Regulatory Processes	32
H. Disclosure Requirements for the Public Offering of Securities	34
I. Establishment of the TOKYO PRO-BOND Market	39
J. Participation of Nonresidents in the Japan Bond Market	43
K. Regulations on Credit Rating Agencies	46
III. Characteristics of the Japan Bond Market	50
A. Definition of Corporate Bond	50
B. Types of Bonds and Notes	50
C. Money Market Instruments	57
D. Segmentation of the Market (Except for Japanese Government Bonds)	59
E. Methods of Issuing Bonds (Primary Market)	65
F. Governing Law and Jurisdiction (Bond and Note Issuance)	74
G. Language of Documentation and Disclosure Items	75
H. Listing on the TOKYO PRO-BOND Market	76
I. Bond and Note Pricing	85
J. Transfer of Interests in Bonds and Notes	86
K. Definition of Professional Investor and Related Classifications	87
L. Credit Rating Requirements	90

M. Commissioned Company for Bondholders (Bond Managers)	91
N. Securitized Products Market	94
O. Bankruptcy Procedures	98
P. Event of Default	99
IV. Trading and Transactions of Bonds and Notes, and Trading Market Infrastructure	101
A. Participants in the Secondary Bond Market	101
B. Trading of Bonds and Notes on Exchange	104
C. Over-the-Counter Trading of Bonds and Notes	104
D. Proprietary Trading System for Fixed-Income Securities	104
E. Publication of Reference Statistical Prices for Over-the-Counter Bond Trading	107
F. Secondary Market Yields and Bond Indexes	110
G. Repurchase (<i>Gensaki</i>) Market for Bonds	112
H. Bond Borrowing and Lending	116
I. Bond Market-Related Derivatives	117
V. Description of the Securities Settlement System	121
VI. Bond Market-Related Costs and Taxation	122
A. Costs Associated with Bond and Note Issuance	122
B. Ongoing Costs (Agent Fees) for Issuers of Corporate Bonds and Notes, and Commercial Paper	124
C. Costs Associated with Deposit, Withdrawal, Settlement (Set-Up, Book-Entry, and Transfer Fees) for Japan Securities Depository Center Account Holders	124
D. Other Fees and Costs	130
E. Taxation (Withholding Tax on Interest Income, Etc.)	130
F. Taxation for Resident Japanese Investors (Integration of Taxation on Financial Income and Gains)	135
VII. Market Size and Statistics	138
VIII. Islamic Finance in Japan	139
A. Background on Introducing Islamic Finance in Japan	139
B. Regulatory Framework for Islamic Finance in General	140
C. Regulatory and Legal Framework for Islamic Bonds (<i>J-Sukuk</i>)	140
D. Type of Instruments Available, Segments, and Tenure	143
E. Tax-Related Issues	143
F. Impediments for Structuring <i>Sukuk</i>	144
G. Significance of the Islamic Finance and Islamic Bonds (<i>Sukuk</i>) Market	145
IX. Bond Market Challenges and Opportunities	146
A. Corporate Bond Market Characteristics and Issues	146
B. Reducing the Blackout Period and Expanding Funding Sources	149
C. Inconvenience of the Current Disclosure System for Public Offering	149
D. Underwriting Examination (Due Diligence) by Securities Companies	149
E. Determination Process for Corporate Bond Issuance Conditions	154
F. Measures to Cope with Default Risk	155
G. Bond Investment Education and Bond Investor Relations	159
H. Opportunities for the Japanese Market and Its Participants	160

X.	Recent Developments and Future Direction	161
A.	Recent Major Developments	161
B.	Future Direction	163

Appendixes

1	Group of Thirty Compliance	165
2	Group of Experts Report—Market Barriers Assessment	166
3	List of Bond Market-Related Legislation and Rules	168
4	Practical References	178
5	Recommended Expression of Related Translations	180
6	Glossary of Technical Terms	183

Tables and Figures

Tables

1	Publicly Offered Bonds Outstanding	2
2	Issuance of Publicly Offered Bonds	3
3	Trading Volume of Publicly Offered Bonds	7
4	Liberalization of the Japanese Yen and the Corporate Bond Market	9
5	Publicly Offered Corporate Bonds Outstanding	11
6	Publicly Offered Corporate Bond Issuance Volumes	11
7	Corporate Bond Issuing Entities by Structure	14
8	Corporate Bond Holdings by Structure	15
9	Coverage of the Three Self-Regulatory Organizations in the Japan Bond Market	23
10	Regulatory Framework Matrix in the Corporate Bond Market in Japan	25
11	Comparison of Financial Instruments Exchange Act Terms with Market Practice Terms	42
12	Overview of Types of Bonds and Notes Issued in Japan	50
13	Japanese Government Bonds Outstanding	53
14	Trading Volume of Japanese Government Bonds by Category	54
15	Local Government Bonds Outstanding by Type	54
16	Government Agency Bonds Outstanding by Type	55
17	Corporate Bonds Outstanding by Type	56
18	Bank Debentures Outstanding	56
19	Nonresident Bonds Outstanding by Type	56
20	Commercial Paper Outstanding	58
21	Commercial Paper Outstanding by Issuer	59
22	Bonds, Notes, and Commercial Paper Outstanding by Type (JPY trillion)	60
23	Bonds, Notes, and Commercial Paper Outstanding by Type (number of issues)	61
24	Public Sector Bonds Outstanding by Type (JPY trillion)	64
25	Corporate Bonds, Notes, Commercial Paper Outstanding by Type	64
26	Methods of Japanese Government Bond Issuance	65
27	Sample Wording of the Transfer Restrictions in the Terms and Conditions of Notes	84
28	Classification and the Change of Status of Investors in Japan	90
29	Change in Number and Value of Securitized Product Issuance Market	96
30	Summary of the Enactment of Securitization-Related Laws	97
31	Bond Market Transactions by Type and Party	102
32	Bond Lending Balances	118
33	Bond Market-Related Derivatives Products on the Osaka Exchange	118
34	Standard Underwriting Fee Schedule for a Public Offering of Bonds	123
35	Standard Fiscal Agent Fee for a Public Offering of Corporate Bonds	123
36	Standard Fee Rates for Applicable Agent Services	124
37	Short-Term Corporate Bonds—Participation in the Book-Entry System	125
38	Short-Term Corporate Bonds—Book-Entry-Related Fees	126
39	Corporate Bonds—Participation in the Book-Entry System	127

40	Corporate Bonds Book-Entry-Related Fees	128
41	Other Typical Fees and Costs in the Context of Corporate Bond Issuance	130
42	Taxation Treatment for Nonresident Investors (Foreign Juridical Persons)	130
43	Taxation Treatment for Resident Japanese Investors	130
44	Summary of Taxation System for Financial Products for Japanese Resident Individuals before and after Reform	137
45	Japanese Organizations in the Islamic Financial Services Board	139
46	Excerpt of Underwriting Examination Items from the Rules and Detailed Rules Concerning Underwriting, Etc. of Securities	150
A1	Group of Thirty Compliance for Japan	165
A2	Summary of the Group of Experts Market Barriers Assessment	166
A3.1	Examples of Bond Market-Related Legislation in Each Legislative Tier	168
A3.2	Japan Securities Dealers Association Self-Regulatory Rules, Etc. for Bond Transactions	173
A3.3	Japan Securities Dealers Association Recent Guidelines Related to the Bond Market	175
A3.4	List of the Tokyo Stock Exchange Rules and Regulations Related to the TOKYO PRO-BOND Market	176

Figures

1	Publicly Offered Bonds Outstanding	2
2	Issuance of Publicly Offered Bonds	3
3	Local Currency Bonds Outstanding—US Dollars versus Japanese Yen	4
4	Japanese Yen–US Dollar Exchange Rate	5
5	Trading Volume of Publicly Offered Bonds	6
6	Publicly Offered Corporate Bonds Outstanding	10
7	Publicly Offered Corporate Bond Issuance Volumes	11
8	Corporate Bond Issuing Entities by Structure	13
9	Corporate Bond Holdings by Structure	15
10	Regulatory Process Map—Public Offering	33
11	Regulatory Process Map—Private Placement	33
12	Regulatory Process Map—Listing on the TOKYO PRO-BOND Market	34
13	Creation of a Market for Professional Investors	41
14	Introduction of Regulation for Credit Rating Agencies	48
15	Summary of Guidelines for Supervision of Credit Rating Agencies	49
16	Trading Volume of Japanese Government Bonds by Category	53
17	Commercial Paper Outstanding by Issuer	58
18	Bonds, Notes, and Commercial Paper Outstanding by Type (JPY trillion)	59
19	Bonds, Notes, and Commercial Paper Outstanding by Type (number of issues)	61
20	Public Sector Bonds Outstanding by Type	63
21	Corporate Bonds, Notes, and Commercial Paper Outstanding by Type	63
22	New System to Disseminate Bond Trading Prices for Corporate Bonds	110
23	Japanese Government Bond Yield Curve for Selected Periods on <i>AsianBondsOnline</i>	111
24	Nikkei Japanese Government Bond Index	112
25	End-of-Month Balances of Bond Transactions with Repurchase Agreements	116
26	<i>Sukuk</i> Issuance Scheme in Japan	141
27	New Taxation Measures on <i>Sukuk</i> in Japan	144
28	Japan Exchange Group Announcement of Listing of ASEAN+3 Multi-Currency Bond Issuance Framework Pilot Issue	162

Foreword

The Asian Development Bank (ADB) is working closely with the Association of Southeast Asian Nations (ASEAN) and the People's Republic of China (PRC), Japan, and the Republic of Korea—collectively known as ASEAN+3—to develop local currency bond markets and facilitate regional bond market integration under the Asian Bond Markets Initiative (ABMI) in order to strengthen the resilience of the region's financial systems.

Thanks to the efforts of the concerned governments, the local currency bond markets in the region have grown rapidly, with the amount of outstanding bonds reaching more than USD8 trillion in 2015. However, financial markets in the region are still not as integrated as the region's trade linkages and supply chain networks. If efforts toward harmonization and integration succeed, financial markets will be able to increase efficiencies and benefit from much larger economies of scale; hence, the region's vast savings can be better utilized to meet its enormous investment needs. Bond market development should proceed from an early stage with a common understanding of what should be harmonized and integrated.

The ASEAN+3 Bond Market Forum (ABMF) was established with the endorsement of the ASEAN+3 Finance Ministers in 2010 as a common platform to foster standardization of market practices and harmonization of regulations relating to cross-border bond transactions in the region. As the first step, ABMF published the ASEAN+3 Bond Market Guide in 2012, which was welcomed as the first official document to comprehensively explain the structure and operations of bond markets in the region. Since its publication, ASEAN+3 bond markets have continued to develop and ABMF recognizes the need to reflect these changes in a revised publication, though it is not an easy task to keep up with rapid changes in the markets.

This report is an outcome of strong support and kind contributions from ABMF members and experts, particularly those in Japan. The report should be recognized as a collective good to support market development by ABMF members and experts. It is our hope that the revised bond market guide will facilitate further development of the market and contribute to more active intraregional bond transactions.



Ma. Carmela D. Locsin
Director General
Sustainable Development and Climate Change Department (SDCC)

Acknowledgments

The Japan Bond Market Guide was first published in 2012 as the initial output of Phase 1 of the ASEAN+3 Bond Market Forum (ABMF).¹ Since then, the region's domestic bond markets have experienced tremendous developments. Now in Phase 3, ABMF would like to share information on these developments in the public domain by publishing an update to the Japan Bond Market Guide. Therefore, Chapters I–III have been updated and rewritten for the 2016 Japan Bond Market Guide.

The ABMF Sub-Forum 1 Team, comprising Satoru Yamadera (principal financial sector specialist, Sustainable Development and Climate Change Department, Asian Development Bank [ADB]); Shigehito Inukai (ADB consultant and Waseda University); and Matthias Schmidt (ADB consultant), would like to express their sincere gratitude to ABMF national and international members and expert institutions including the Ministry of Finance Japan; Financial Services Agency; Bank of Japan; Tokyo Stock Exchange; Japan Securities Dealers Association; JASDEC; Nomura Securities; Daiwa Securities Capital Markets; Nikko SMBC; Sumitomo Mitsui Banking Corporation; Mizuho Bank; Mizuho Securities; Bank of Tokyo–Mitsubishi UFJ; Mitsubishi UFJ Trust; Mitsubishi UFJ Morgan Stanley Securities; Morgan Stanley; Barclays; JP Morgan; CITI; HSBC; Bank of America Merrill Lynch; Mori Hamada & Matsumoto; Nagashima Ohno & Tsunematsu; and other supporters including NTT Data Corporation, Rating and Investment Information (R&I), JCR, and Waseda University. They kindly provided answers to the questionnaires prepared by the ABMF Sub-Forum 1 Team, thoroughly reviewed the draft of the Japan Bond Market Guide, and offered valuable comments.

The creation and ongoing activities of the ABMF–Japan Group, also known as the Waseda Asia PRO-BOND Research Committee, comprising the abovementioned members, experts, and other volunteer supporters, is a major achievement. It can serve as an excellent model for other market associations given the commitment and efforts of members have been substantial. The ABMF Sub-Forum 1 Team also would like to express special thanks to the Japan Securities Research Institute for providing information from its market guides and other relevant publications, as well as valuable research expertise. Because of the Japan Securities Research Institute's cooperation and contributions, the ABMF Sub-Forum 1 Team was able to start its own research efforts on solid ground. Last but not least, we would like to thank everyone who gave their opinions and/or comments in response to questions posed over the course of several rounds of market consultations.

This report does not represent the official views or opinions of any institution that participated in this activity as an ABMF member or expert. The ABMF Sub-Forum 1 Team bears sole responsibility for the contents of this report.

May 2016

ASEAN+3 Bond Market Forum (ABMF) Sub-Forum 1

¹ ASEAN+3 refers to the 10 members of the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China, Japan, and the Republic of Korea.

Abbreviations

ABMF	ASEAN+3 Bond Market Forum (http://www.asean3abmf.adb.org)	PSD	Private Secondary Distribution
ABS	asset-backed securities	PTS	proprietary trading system
ADB	Asian Development Bank (http://www.adb.org)	QII	Qualified Institutional Investor
AI	Accredited Investors	QII-PP	Qualified Institutional Investor-Private Placement
AMBIF	ASEAN+3 Multi-Currency Bond Issuance Framework	QII-PSD	Qualified Institutional Investor-Private Secondary Distribution
ASEAN	Association of Southeast Asian Nations (http://www.asean.org)	R&I	Rating and Investment Information (https://www.r-i.co.jp/eng/)
ASEAN+3	Association of Southeast Asian Nations plus the People's Republic of China, Japan, and the Republic of Korea	SESC	Securities and Exchange Surveillance Commission
BOJ	Bank of Japan	SF1	Sub-Forum 1 of ASEAN+3 Bond Market Forum (ABMF)
CRA	credit rating agency	SN	Securities Notice
CSD	central securities depository	SN-PP	Small Number-Private Placement
DVP	delivery versus payment	SN-PSD	Small Number-Private Secondary Distribution
EDINET	Electronic Disclosure for Investors' Network	SPV	special purpose vehicle
FIEA	Financial Instruments and Exchange Act	SR	Shelf Registration
FSA	Financial Services Agency	SRO	self-regulatory organization
FX	foreign exchange	SRS	Securities Registration Statement
IDB	inter-dealer broker	SSF	Single Submission Form (used in conjunction with AMBIF)
IOSCO	International Organization of Securities Commissions (www.iosco.org/about)	SSI	Specified Securities Information
JASDEC	Japan Securities Depository Center	TPBM	TOKYO PRO-BOND Market
JGB	Japanese Government Bond	TSE	Tokyo Stock Exchange (part of JPX)
JPY	Japanese yen	USD	Unites States dollar
JPX	Japan Exchange Group (TSE is a part of JPX)		
JPX-R	Japan Exchange Regulation		
JSDA	Japan Securities Dealers Association		
MBS	mortgage-backed securities		
MOF	Ministry of Finance Japan		
MOU	memorandum of understanding		
MTN	medium-term note		
MYR	Malaysian ringgit		
OTC	over-the-counter		
PI	Professional Investor		
PP	Private Placement		

USD1 = JPY120.42 as of 30 December 2015
(Bank of Japan spot rate)
http://www.stat-search.boj.or.jp/ssi/mtshtml/m_en.html

Overview

A. Introduction

The Government of Japan raises significant amounts from domestic capital markets to finance government expenditures, mainly through the issuance of Japanese Government Bonds (JGBs) and Treasury Discount Bills (Treasury Bills and Financial Bills, collectively T-Bill). These funding activities have been supported by a large and diverse community of domestic and overseas investors and intermediaries.

Japan offers a wide range of financial tools to meet a range of issuer and investor requirements. Aside from traditional bank instruments (e.g., loans), corporate bonds, commercial paper, and securitized products are also available in Japan's credit market. Securities lending and securities financing are also established. Various credit risks are pooled through securitized products, with the value of the underlying assets exceeding the risks taken by investors.

Among the major market participants in Japan's bond market are domestic and foreign securities companies that serve as dealers, brokers, traders, and underwriters in the primary and secondary markets. Local governments, government agencies, and local public corporations are the largest issuers of government bonds in the market excluding JGBs. The majority of JGB holders are from the public sector, commercial banks, and insurance companies.

The amount of outstanding bonds in the government bond sector has expanded enormously over the past 2 decades (Figure 1 and Table 1).

During the period 2005–2008, JGB issuance was on the decline as the central government's financial position improved. However, the economic slump that followed the Lehman shock in September 2008 led to a deterioration in the government's finances and an increase in issuance (Figure 2 and Table 2).

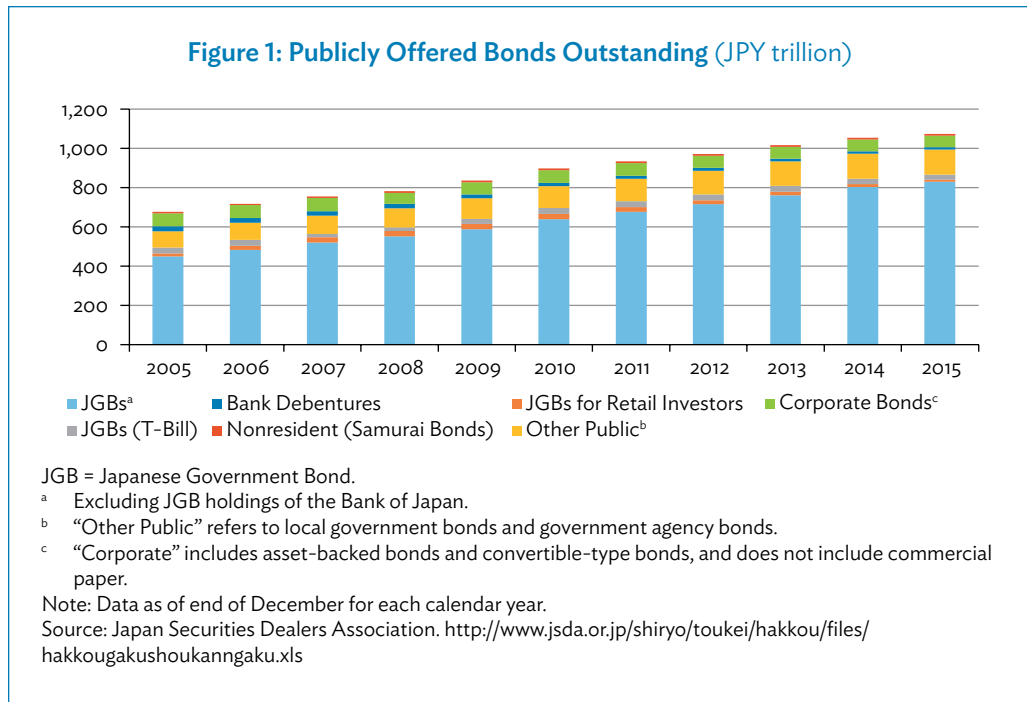


Table 1: Publicly Offered Bonds Outstanding (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
JGBs ^a	448.8	482.2	520.1	551.7	587.3	638.6	676.9	715.3	760.7	802.7	830.0
JGBs for Retail Investors	15.3	22.0	26.5	27.5	27.7	27.2	23.4	20.3	17.8	14.9	11.2
JGBs (T-Bill)	30.3	29.0	16.8	17.1	25.4	30.0	30.0	30.0	30.0	28.1	25.7
Other Public ^b	82.9	88.1	94.4	99.1	105.8	111.5	115.3	121.1	126.0	127.8	128.0
Bank Debentures	25.8	23.4	22.2	21.3	19.4	17.2	15.2	14.0	12.5	11.8	11.4
Corporate Bonds ^c	66.5	66.6	67.8	56.9	61.4	63.8	63.6	62.4	61.5	60.4	58.4
Nonresident (Samurai Bonds)	6.9	6.4	7.6	9.1	8.9	9.3	9.8	9.3	8.8	9.2	9.1
Total ^d	676.4	717.7	755.4	782.7	835.9	897.6	934.2	972.3	1,017.3	1,054.9	1,073.8
JGB Holdings of the BOJ ^a	180.0	161.4	138.6	109.7	88.2	81.0	66.6	59.2	52.3	34.4	27.6

BOJ = Bank of Japan, JGB = Japanese Government Bond.

^a Excluding JGB holdings of the BOJ.

^b “Other Public” refers to local government bonds and government agency bonds.

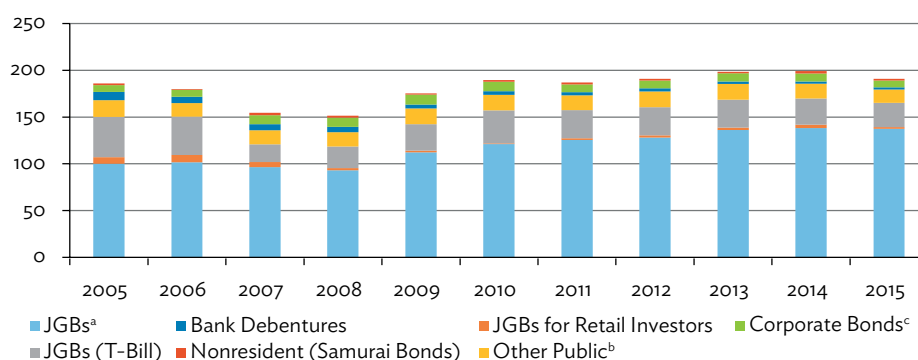
^c “Corporate” includes asset-backed bonds and convertible-type bonds, and does not include commercial paper.

^d Outstanding value of privately offered bonds and notes may not be included.

Note: Data as of end of December for each calendar year.

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryotoukei/hakkou/files/hakkougakushoukannagaku.xls>

Figure 2: Issuance of Publicly Offered Bonds (JPY trillion)



JGB = Japanese Government Bond.

^a Excluding JGB holdings of the Bank of Japan.

^b “Other Public” refers to local government bonds and government agency bonds.

^c “Corporate” includes asset-backed bonds and convertible-type bonds, and does not include commercial paper.

Note: Data as of end of December for each calendar year.

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryō/toukei/hakkou/files/hakkougakushoukannangu.xls>

Table 2: Issuance of Publicly Offered Bonds (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
JGBs ^a	100.1	101.8	96.4	93.2	112.4	121.1	125.5	128.2	136.3	138.3	137.4
JGBs for Retail Investors	7.1	7.6	5.6	2.3	1.6	0.9	1.9	2.4	2.4	3.5	1.9
JGBs (T-Bill)	42.9	41.0	18.8	23.1	28.4	35.0	30.0	30.0	30.0	28.1	25.7
Other Public ^b	17.9	14.6	15.0	15.3	16.8	16.7	15.7	16.9	16.8	15.6	14.3
Bank Debentures	8.8	6.7	6.5	5.5	4.2	3.8	3.4	3.2	2.6	2.5	2.5
Corporate Bonds ^c	7.4	7.5	9.6	9.9	10.6	10.1	8.5	8.4	8.8	8.5	7.1
Nonresident (Samurai Bonds)	1.6	0.8	2.6	2.1	1.2	1.9	2.0	1.7	1.6	2.5	1.9
Total ^d	177.6	168.1	152.9	147.0	178.1	183.7	185.1	190.8	198.4	199.0	190.8
JGB Holdings of the BOJ ^a	44.3	31.7	23.5	11.1	10.6	9.8	10.4	14.1	14.8	9.5	11.4

BOJ = Bank of Japan, JGB = Japanese Government Bond.

^a Excluding JGB holdings of the BOJ.

^b “Other Public” refers to local government bonds and government agency bonds.

^c “Corporate” includes asset-backed bonds and convertible-type bonds, and does not include commercial paper.

^d Outstanding value of privately offered bonds and notes may not be included.

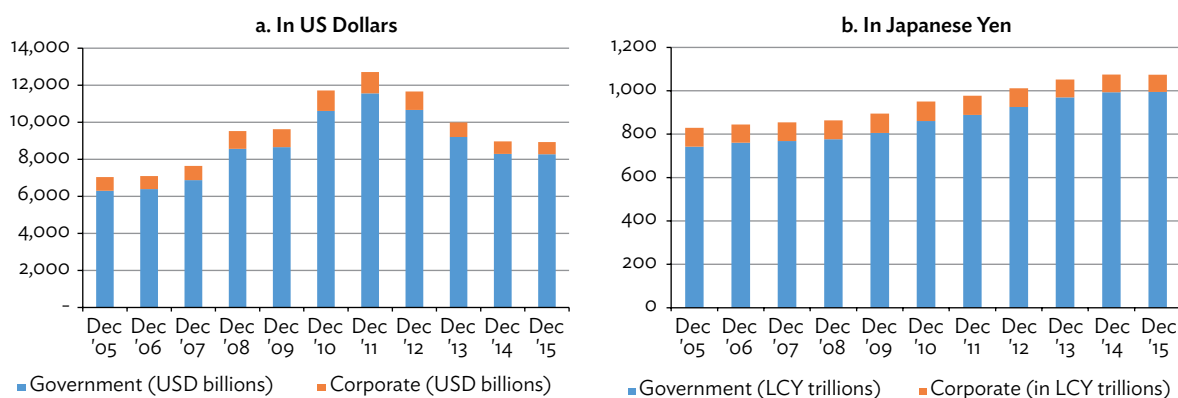
Note: Data shown for each calendar year

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryō/toukei/hakkou/files/hakkougakushoukannangu.xls>

The amount of bank debentures issued in 2015 stood at JPY2.5 trillion, down from JPY21.0 trillion in 2000. This decline suggests that Japanese industry's dependency on long-term credit from banks as a source of long-term capital came to an end in the first half of the 2000s, and also points to the weakness in financing for the private sector as a whole during the review period.

The total volume of publicly offered corporate bonds excluding commercial paper amounted to JPY7.1 trillion in 2015, remaining below the JPY10 trillion level for the fifth consecutive year and comprising less than 4% of total publicly offered bonds. Meanwhile, after being depressed in the aftermath of the Argentine government's default in 2002, the issuance of JPY-denominated foreign bonds (Samurai Bonds issued by nonresidents) has been steadily recovering. Today, JPY-denominated foreign bonds are once again used as an important financing source for foreign issuers due to their need to diversify currency risks.

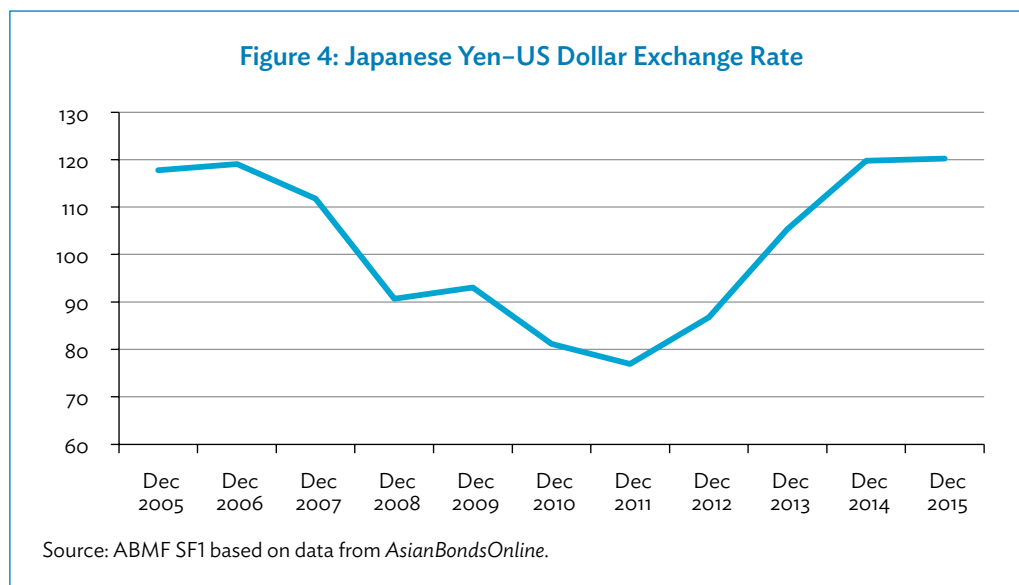
Figures 3: Local Currency Bonds Outstanding—US Dollars versus Japanese Yen



LCY = local currency.
Source: *AsianBondsOnline*.

Influence of Fluctuations in the JPY–USD Exchange Rate

According to data available on *AsianBondsOnline*, the total amount of local currency (LCY) bonds outstanding in the Japanese bond market was JPY1,074 trillion (USD8,931 billion) at the end of December 2015. Figure 3 shows total outstanding amounts denominated in US dollars and Japanese yen, respectively, between December 2005 and December 2015. It is significant that these graphs are based on the same LCY bond volumes, yet they have entirely different shapes due to the influence of fluctuations in the JPY–USD exchange rate (Figure 4).



B. Liquidity-Enhancing Measures in the Japanese Government Bond Market¹

In realizing the basic objectives of the Debt Management Policy—ensuring stable and smooth issuance of JGBs and minimizing medium-to-long-term financing costs—the issuing authorities have a keen interest in whether the JGB market has sufficient liquidity to enable transactions to be conducted freely in accordance with market participants’ interest rate forecasts and investment strategies.

The JGB secondary market consists of brokers such as JGB Market Special Participants, who are also known as Primary Dealers, and investors. Basically, the maintenance and enhancement of liquidity should be achieved by the autonomous functioning of the market, which is stimulated by active transactions among such market participants. Consequently, the Ministry of Finance Japan’s (MOF) Debt Management Office should support this autonomous functioning by arranging the appropriate amounts and maturities for auctions, and reopening issues in the primary market as needed.

In March 2001, the immediate reopening rule was introduced to principally treat a new JGB issue as an addition to an outstanding issue immediately from the issuance day if the principal and interest payment dates and coupon rate for the new issue are the same as those for the outstanding issue. In line with the immediate reopening rule, accrued interest emerges on new JGB issues. Accrued interest is a distinct practice in the trading of coupon bonds, and represents the interest accumulated since the last coupon payment date. When buying JGBs, investors pay the accrued interest for the period since the last coupon payment to sellers.

Under the JGB Issuance Plan for fiscal year (FY) 2014 (1 April–31 March), the central government increased the monthly size of JGB issuance through Auctions for Enhanced Liquidity by JPY100 billion and the overall JGB issuance through such auctions by

¹ Excerpts from the Ministry of Finance Japan’s FY2014 debt management policies are available at https://www.mof.go.jp/english/jgbs/publication/debt_management_report/2014/saimu1-1-1.pdf

JPY1.2 trillion–JPY8.4 trillion. The coverage of such auctions is expanded to include all issues maturing in more than 5 years, other than on-the-run issues. Furthermore, JGB Market Special Participants are each required to make a bid for 3% or more of a planned issuance amount.

In FY2014, the government subjected 20-, 30-, and 40-year JGB issues to reopening in principle to secure market liquidity for each issue. As for 10-year JGBs, the government decided to adopt reopen issuances in April and May in cases where the spread between the coupon rate of the new bond being issued and the market JGB yield as of the auction date was less than 20 basis points.

C. Secondary Market Overview

Most Japanese domestic investors tend to hold bonds and notes until maturity. The selling of bonds and notes for switching, profit-taking, and loss-cutting is generally undertaken by institutional investors. With the exception of the impact of the global financial crisis, recent years have seen bond trading volumes in the secondary market continuously increase (Figure 5 and Table 3).

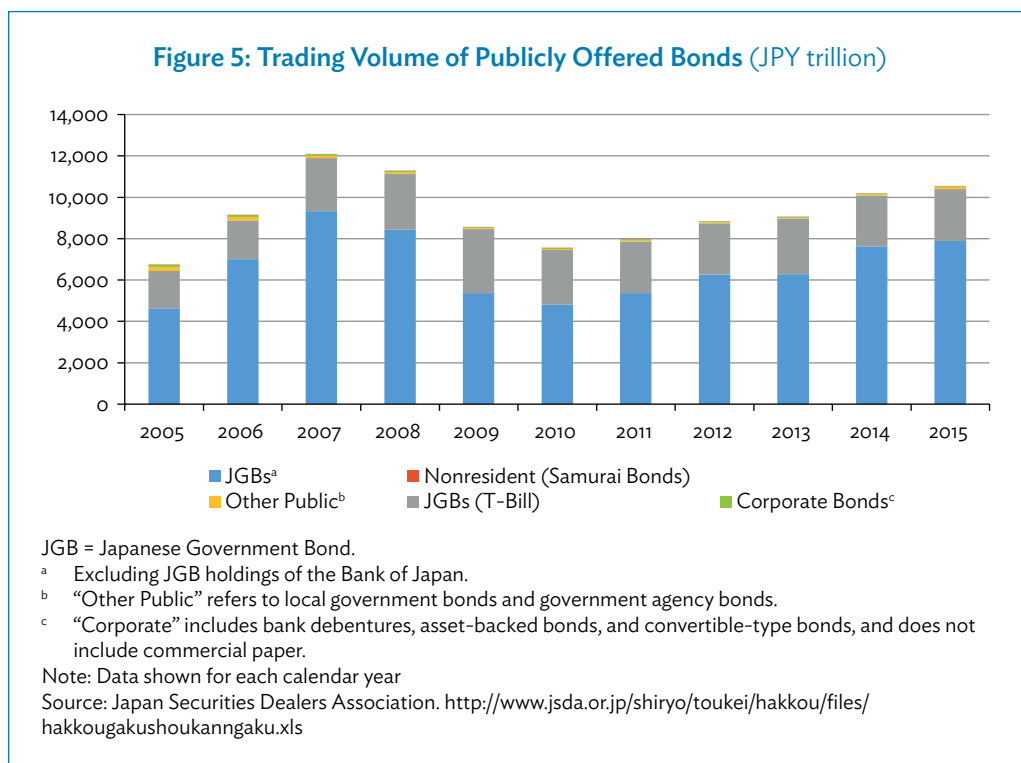


Table 3: Trading Volume of Publicly Offered Bonds (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
JGBs ^a	4,611	7,010	9,335	8,438	5,374	4,806	5,362	6,263	6,275	7,626	7,894
JGBs (T-Bill)	1,818	1,872	2,555	2,681	3,084	2,647	2,498	2,476	2,694	2,449	2,500
Other Public ^b	193	163	127	89	50	49	50	48	41	51	107
Corporate Bonds ^c	122	98	73	73	49	47	50	54	45	49	31
Nonresident (Samurai Bonds)	15	10	7	7	6	5	4	3	3	6	6
Total ^d	6,758	9,153	12,097	11,288	8,563	7,553	7,964	8,844	9,058	10,182	10,536

JGB = Japanese Government Bond.

^a Excluding JGB holdings of the Bank of Japan.

^b “Other Public” refers to local government bonds and government agency bonds.

^c “Corporate” includes bank debentures, asset-backed bonds, and convertible-type bonds, and does not include commercial paper.

^d Outstanding value of privately offered bonds and notes may not be included.

Note: Data shown for each calendar year.

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryo/toukei/hakkou/files/hakkougakushoukanngaku.xls>

The increase in the trading volume of JGBs during the period 2005–2015 can be explained by a number of factors. Firstly, the government continued to issue massive amounts of JGBs during the review period, resulting in a large increase in the size of the JGB market. Secondly, brokers, dealers, and other financial institutions such as banks actively dealt in bonds and notes for trading gains. Thirdly, the government started to auction T-Bill, which are now actively traded by market participants with short-term cash management needs. “T-Bill” is the sum of “Treasury Bills (TBs)” and “Financial Bills (FBs)” with a maturity of 1 year or less and TBs and FBs have been jointly issued since February 2009. Fourthly, the growing so-called flight-to-quality trend among domestic and foreign investors has also played a significant part. Over the past several years, the movement into the JGB trading market was prompted by a worsening in the worldwide investment environment against the backdrop of prolonged economic stagnation and recurring turmoil in global financial markets.

Additionally, government securities significantly outweigh other categories of bonds in overall fixed-income trading volume. The dominance of government debt stems mostly from the difference in liquidity, which in turn is because the major market participants are Japanese banks with tremendous excess cash and a preference for outstanding liquidity given the Bank for International Settlement’s zero-risk weighting of Japanese government debt.

D. Japanese Government Bond Market

Amid the continued massive issuance volumes of JGBs, the proportion of bond issuance made through public auctions that more closely reflect market conditions has steadily increased under a market-oriented national debt management policy. This replaced the previous emphasis on noncompetitive, syndicated underwriting, where issue terms were based on the official discount rate or other benchmarks.

As far as the 10-year JGB is concerned, the syndicated underwriting system, which is a noncompetitive (conventional) system, was maintained until the syndicated underwriting system was abolished in 2006. In contrast, for government bonds of other terms, over a

substantial length of time prior to 2006 they were issued as determined by the tender or auction conditions known as the partial price competitive tendering system.

For years, market participants and government officials have made efforts to realize fair market price formation. Currently, in principle, all government bonds are issued through auctions as the syndicated underwriting program for JGBs was discontinued in March 2006. The market-oriented transition of bond issuance has also been witnessed in pricing spreads among bonds with different credit qualities. For example, yields at the issue of government-guaranteed bonds and local government bonds were determined in reference to the yield at the issue of 10-year JGBs earlier in the month. From time to time, the spreads for issues among these three classes of bonds have deviated from market spreads. In recent years, however, as investors started to focus more on differences in credit quality, the spreads for issues among the three classes have increasingly tended to move more in line with credit spreads prevailing in the market.

Another case in point that demonstrates the increased market orientation in bond issuance is the growing portion of government-guaranteed bonds being issued through a competitive bidding process (as individual issues). Investors are also showing an increasing tendency to differentiate corporate bonds based on credit ratings by rating agencies and other factors. In response, many issuers go through a premarketing process to identify and estimate investor demands and determine the terms of issuance accordingly.

E. Liberalization of the Japanese Yen and the Corporate Bond Market

There is a need to identify in Japan a market that can serve as a good model for the development of corporate bond markets in emerging economies, particularly in Asia. Additionally, there has been a need to fully open the Japanese corporate bond market to global participants by making it easy to use for both domestic and overseas issuers and investors.

Formerly, there were a number of different regulations on the issuance of corporate bonds in Japan. The issue terms were uniformly determined according to a set formula, and issuance volumes were constrained as well. This rigid issuance mechanism was subsequently modified to allow issue terms and conditions to be determined in accordance with actual market practices and conditions, in line with other deregulation measures. A selection of significant steps undertaken in the liberalization of the Japanese yen and the corporate bond market is listed in Table 4.

Table 4: Liberalization of the Japanese Yen and the Corporate Bond Market

Year	Event
1970	The Tokyo capital market is inaugurated, the Japanese yen is internationalized, and the Asian Development Bank issues its first bonds in the Japanese market, effectively creating the first Samurai Bond.
1971	Nixon shock: Dollar–gold convertibility is suspended, followed by a shifting of the Japanese yen to a floating-rate system in 1973.
1972	GTE public stock offering in Japan (first foreign stock)
1973	Australian government bonds offered in Japan (first Samurai Bonds)
1974	First German deutschemark public offering of corporate bonds (Mitsubishi Heavy Industries)
1975	First Swiss franc public offering of corporate bonds (Mitsubishi Chemical)
1977	Expansion of foreign exchange reserves, yen interest rates fall due to a decline in private sector funding demand, record issuance of Samurai Bonds Lifting of the ban on the issue of Euroyen bonds by nonresidents; first issue by the European Investment Bank
1984	Japan–US Yen–Dollar Committee (Japan–US financial market friction prompts further internationalization of the Japanese yen) Substantial easing of issuer qualifications for nonresident Euroyen bonds Lifting of the ban on the issue of Euroyen bonds by residents; first such issuance by Mitsubishi Heavy Industries (Euroyen Convertible Bonds worth JPY30 billion, which included a 180-day restriction on the recycling of Euroyen bonds in Japan)
1985	Plaza Agreement (major industrialized countries’ coordinated response to rising US dollar interest rates due to US trade and fiscal deficits); managed floating exchange rate system is implemented
1990	Weakening of the Japanese yen following the collapse of the bubble economy in Japan
1991	Issuance eligibility criteria are amended to abolish quantitative requirements and credit rating criteria became fully adopted.
1993	Abolishment of regulations on corporate bonds issuance ceiling limits and revision of the trustee company system
1994	Abolition of recycling restrictions on sovereign Euroyen bonds; first Alpine bonds issued ^a
1996	Foreign exchange controls are abolished under the “Tokyo Big Bang” by the Hashimoto Cabinet, including the abolition of recycling restrictions on Euroyen bonds issued by residents.
1996	Eligibility criteria for corporate bond issuance are abolished and bond covenants are deregulated. Eligibility criteria for issuing unsecured bonds and the duty to establish a debt restriction clause were also abolished.
1997	Onset of the Asian financial crisis; failure of Sanyo Securities, Hokkaido Shokutaku Bank, and Yamaichi Securities
1999	Appreciation of the Japanese yen in the wake of the bursting of the US information technology bubble; ban on the issuance of straight bonds by commercial banks lifted
2006	Electronic registration of corporate bonds certificates launched (complete dematerialization)
2010	Announcement of the commencement of the TOKYO PRO-BOND Market

US = United States.

^a Alpine bonds refer to foreign-currency-denominated bonds issued in Switzerland by non-Swiss residents (e.g., Japanese domestic corporation).

Source: ABMF SF1.

F. Tide for Change in the Corporate Bond Market

1. Liberalization and Influences

Fortunately, over the past 2 decades, the impediments that had isolated domestic Japanese markets from foreign international markets were removed through the significant efforts of policy makers and market participants. In 2008, the Financial Services Agency (FSA) revised the Financial Instruments and Exchange Act, 2006 (FIEA) as part of its plan to enhance the competitiveness of Japan's financial and capital markets, thereby establishing the legal framework for markets oriented toward Professional Investors; that is, a private offering system for designated investors and financial instruments exchange markets. This provided the legal framework for the establishment of a new securities market for Professional Investors that was not predicated on full legal disclosure requirements.

In addition, the taxation system was reformed in FY2010 to reduce the tax to 0 on revenues from domestic corporate bonds held by nonresidents. This was seen as a particularly useful opportunity to put an end to the state of isolation of Japan's domestic markets.

Having undergone various systemic reforms, the corporate bond market in Japan has developed into a free and efficient market that plays an important role in corporate financing. Notwithstanding the global financial crisis, which generated a downward trend in the second half of 2008, the corporate bond market has generally demonstrated a record of recovery and expansion. In addition, the bond market's performance was significantly affected in the first half of 2011 by the tragic earthquake and tsunami on 11 March. Since then, amid a recovery of the overall Japanese economy, the corporate bond market has been poised for recovery as well, signs of which can be seen in the professional bond market, the TOKYO PRO-BOND Market (TPBM), and the nonresident bond market (Figures 6 and 7, and Tables 5 and 6).

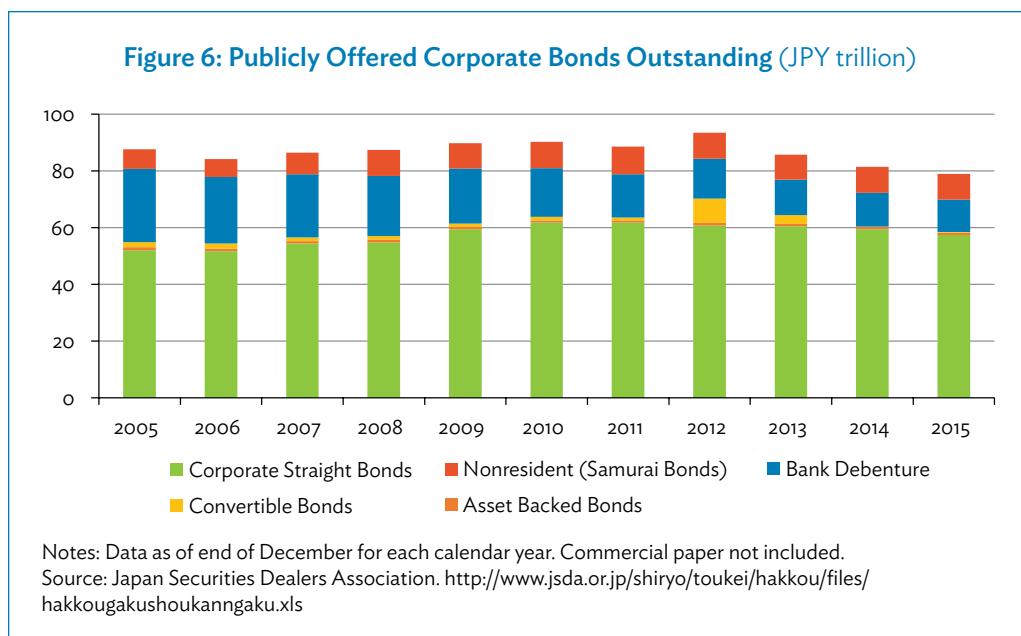


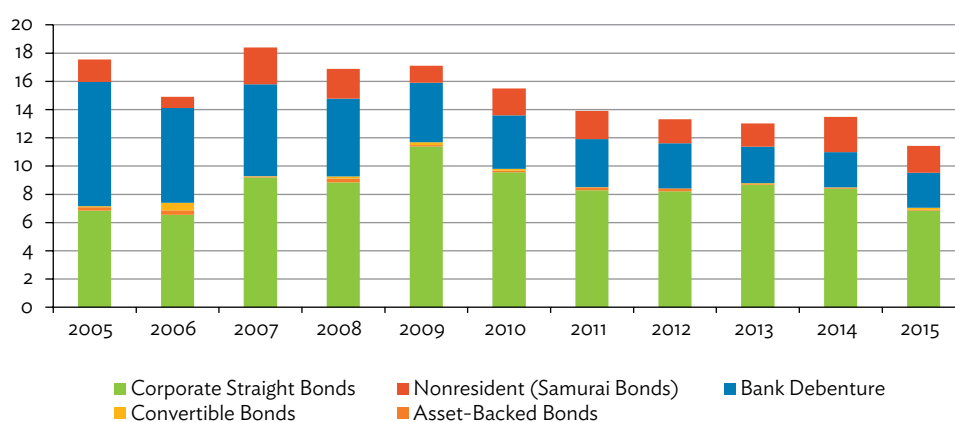
Table 5: Publicly Offered Corporate Bonds Outstanding (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Corporate Straight Bonds	52.0	51.6	54.4	54.8	59.4	61.8	61.7	60.7	60.4	59.3	57.4
Asset-Backed Bonds	1.0	1.0	0.8	0.9	0.8	0.7	0.8	0.9	0.8	0.8	0.7
Convertible Bonds	1.8	1.7	1.4	1.3	1.2	1.2	1.0	8.6	3.1	0.2	0.3
Bank Debenture	25.8	23.4	22.2	21.3	19.4	17.2	15.2	14.0	12.5	11.8	11.4
Nonresident (Samurai Bonds)	6.9	6.4	7.6	9.1	8.9	9.3	9.8	9.3	8.8	9.2	9.1
Corporate Bonds Total	87.6	84.2	86.4	87.3	89.7	90.3	88.6	93.5	85.7	81.4	78.9

Note: Data as of end of December for each calendar year.

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryotoukei/hakkou/files/hakkougakushoukanngaku.xls>

Figure 7: Publicly Offered Corporate Bond Issuance Volumes (JPY trillion)



Notes: Data shown for each calendar year. Commercial paper not included.

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryotoukei/hakkou/files/hakkougakushoukanngaku.xls>

Table 6: Publicly Offered Corporate Bond Issuance Volumes (JPY trillion)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Corporate Straight Bonds	6.9	6.5	9.2	8.8	11.4	9.6	8.3	8.2	8.7	8.4	6.8
Asset-Backed Bonds	0.2	0.3	0.1	0.3	0.1	0.1	0.2	0.2	0.1	0.1	0.1
Convertible Bonds	0.1	0.6	0.0	0.2	0.2	0.1	0.0	0.0	0.1	0.0	0.2
Bank Debenture	8.8	6.7	6.5	5.5	4.2	3.8	3.4	3.2	2.6	2.5	2.5
Nonresident (Samurai Bond)	1.6	0.8	2.6	2.1	1.2	1.9	2.0	1.7	1.6	2.5	1.9
Corporate Bonds Total	17.6	14.9	18.4	16.9	17.1	15.5	13.9	13.3	13.0	13.5	11.4

Notes: Data shown for each calendar year. Commercial paper not included. The outstanding values of privately placed bonds and notes may not be included.

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryotoukei/hakkou/files/hakkougakushoukanngaku.xls>

2. Developments in Issuance Methods and Price Discovery

The process for determining the method of the issuing condition has developed in the corporate bond market over the past 2 decades.

a. Proposal Method

In the corporate bond market, the proposal method was launched in 1988 based on the recommendation of the Securities and Exchange Committee of the MOF to abolish permanent fixed-member syndicates under a pre-agreed pricing matrix set by commissioned banks and introduce free competition among securities firms. Despite naming it the proposal method, the new measure was in fact a competitive bidding system. Since the issuer previously had no freedom to hold competitive bidding, the new method was welcomed by the users of the debt capital market in Japan.

The proposal method, however, soon collapsed because it was premature, given prevailing conditions in the Japanese domestic market, to expect the method to guide fair pricing. It created pricing that was too tight due to intensified competition among securities firms to win the lead manager position and neither issuers nor investors could confirm fair pricing due to undeveloped and illiquid secondary market conditions. Confidence in the pricing being offered by potential lead managers was often lacking. Consequently, new issue pricing under the proposal method was unable to perform its intended function because the majority of domestic investors did not trust the new issue price to be a fair price.

b. Negotiated Method

In 1991, Nippon Telegram and Telephone dropped the proposal method and introduced a new method to appoint lead manager(s). Even in the immature and undeveloped bond market, and amid declining liquidity in the secondary bond market, it was necessary to emphasize the determining of fair pricing in the market. In order to achieve fair pricing, the “JGB spread pricing new issue” under the negotiated method plus the fixed price reoffer with syndicate break for launching method (released to the syndicate selling group with the uniform fixed reoffering price) were developed and introduced in the corporate bond primary market.

Under the new negotiated method, Nippon Telegram and Telephone no longer requested pricing indication from securities firms. Instead, they put weight on the new issuance strategy proposal and commitment to secondary market maintenance in the selection of lead manager(s). As for new issue pricing, Nippon Telegram and Telephone emphasized discrete price discovery and a solid book-building process by the appointed or selected lead manager(s).

This new scheme aimed for fair pricing to reflect investor demand accurately under the prevailing market. For that purpose, the price talk with investors based on the JGB spread was introduced to find out the appropriate price as the benchmark to clear target issue amounts. As a result, the issuance of corporate bonds shifted to a flat sales price system. After several years, utilities companies, general business corporations, and some public sector entities adopted a similar concept.

This method is not applicable to discount sales since the sales price needs to reflect the prevailing market conditions. Since then, many issuers have tried various methods to realize fairer market pricing.

3. Corporate Bond Issuers and Holding Structure

The Japanese corporate bond market remains a small market compared with the United States (US) and Eurobond markets. Although different types of companies have actively issued corporate bonds in the US and Europe (Eurobond market), the issuance of corporate bonds in Japan is still limited largely to

- (i) fairly high-rated companies in specific sectors, including banks, electric power, telecommunications carriers, Japan Railways Group companies, and leasing and finance companies; and
- (ii) small and medium-sized enterprise (SME) bonds that are issued and underwritten by bank(s) while utilizing the legal scheme known as Private Placement to Qualified Institutional Investors. (Significant numbers of small issuances have been made by SMEs.)

For a detailed look at the segmentation of the market, including the breakdown by type of bond or note available in Japan, please refer to Chapter III.D (Figures 19 and 21).

The breakdown of the corporate bonds at the end of March 2015 by issuing entities is displayed in Figure 8 and listed in Table 7.

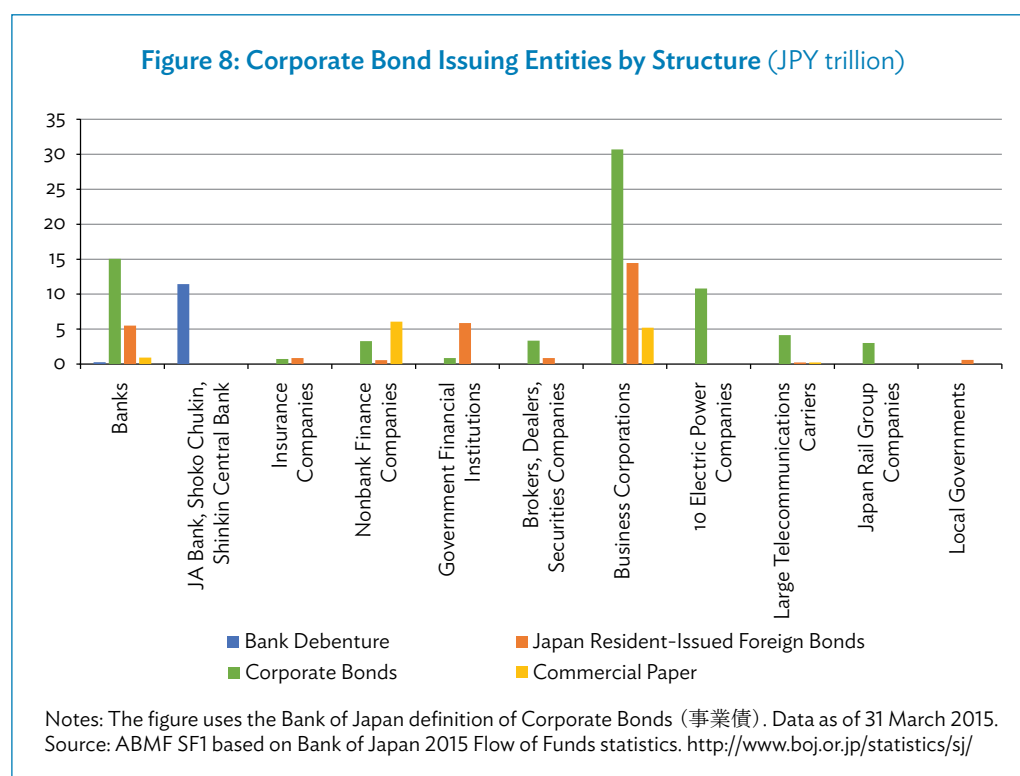


Table 7: Corporate Bond Issuing Entities by Structure (JPY trillion)

	Banks	JA Bank, Shoko Chukin, Shinkin Central Bank	Insurance Companies	Nonbank Financial Companies	Government Financial Institutions	Brokers, Dealers, Securities Companies
Bank Debenture	0.3	11.4	–	–	0.0	0.0
Corporate Bonds	15.0	0.0	0.7	3.3	0.9	3.4
Japan Resident-Issued Foreign Bonds	5.5	0.0	0.9	0.6	5.9	0.9
Commercial Paper	0.9	0.0	–	6.1	0.0	0.0

	Business Corporations	10 Electric Power Companies	Large Telecommunications Carriers	Japan Rail Group Companies	Local Governments	Total
Bank Debenture	–	–	–	–	–	11.7
Corporate Bonds	30.7	10.8	4.1	3.0	–	71.9
Japan Resident-Issued Foreign Bonds	14.5	0.0	0.2	0.0	0.6	29.0
Commercial Paper	5.2	0.0	0.2	0.0	–	12.4

Notes:

1. Data as of 31 March 2015.
2. The Bank of Japan's definition of "Corporate Bonds" for flow of funds statistics includes industrial securities (jigyousai: 事業債). Corporate bonds other than bank debentures issued by financial institutions are included in Industrial securities or Japan resident-issued foreign bonds (external securities issued by residents). Industrial securities are bonds issued domestically by joint-stock corporations. They correspond to secured or unsecured bonds under the Financial Instruments and Exchange Act and include (i) straight bonds (e.g., electric power bonds, Japan Rail bonds, large telecommunications carrier bonds such as NTT bonds, and ordinary business corporations bonds); and (ii) bonds with warrants.
3. "Business Corporations" indicate ordinary business corporations other than the three commercial issuer types stated separately.
4. '–' indicates no issuances under this categorization.

Source: ABMF SF1 based on the Bank of Japan Guide to Japan's Flow of Funds Accounts. <http://www.boj.or.jp/en/statistics/outline/exp/data/exsj01.pdf>

The main holders of corporate bonds in Japan are banks—including as securities custodians on behalf of individual investors—insurance companies, and pension funds, with the remaining types of investors being relatively minor players (Figure 9 and Table 8).

The investor base in Japan for foreign bonds, which comprise corporate bonds issued in the US and Europe (Eurobonds) that are aimed at Japanese residents—is very narrow in comparison to the investor base for corporate bonds issued in Japan by resident issuers.

4. Low Liquidity and Vitalization in the Corporate Bond Market

There are many complex factors behind the small size of the corporate bond market in Japan. For starters, many investors hold corporate bonds until redemption, which limits liquidity in the corporate bond market and restricts the size of the secondary market.

It is believed that a vitalization of the corporate bond market is needed to promote the diversification and decentralization of financing methods used by private companies, as well

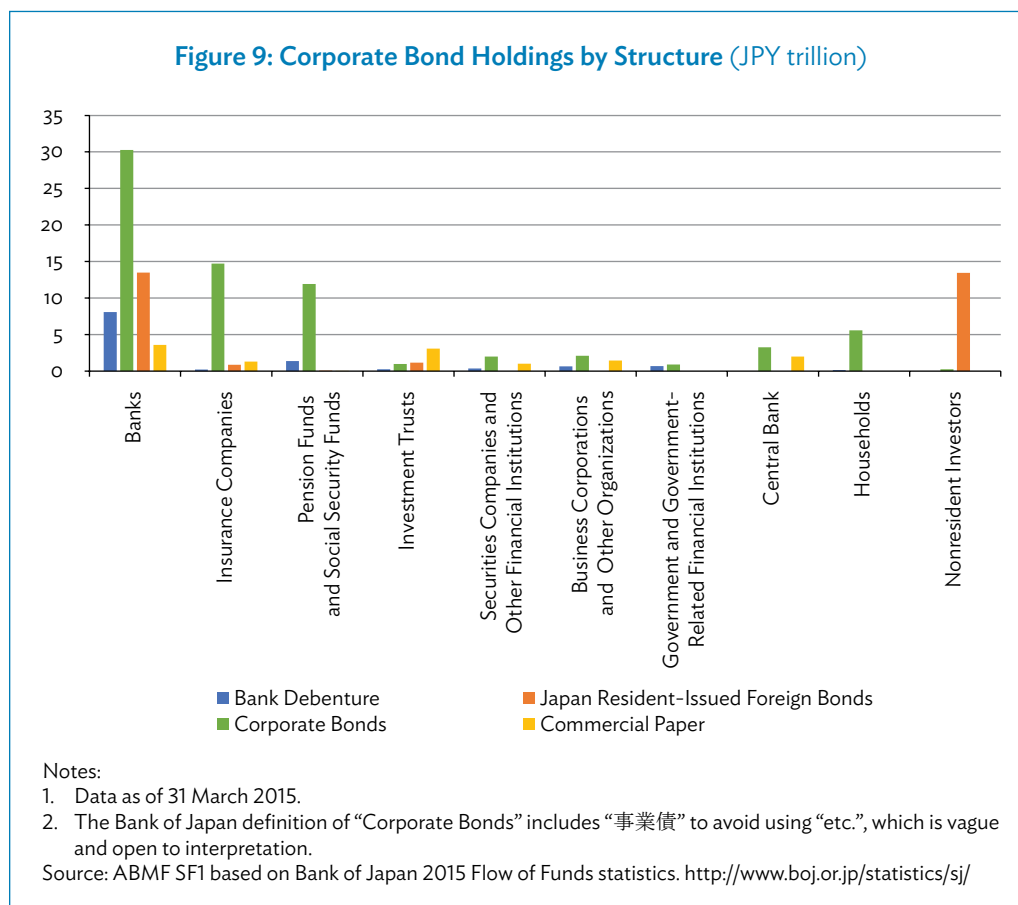


Table 8: Corporate Bond Holdings by Structure (JPY trillion)

	Banks	Insurance Companies	Pension Funds and Social Security Funds	Investment Trusts	Securities Companies and Other Financial Institutions	Business Corporations and Other Organizations
Bank Debenture	8.1	0.2	1.4	0.2	0.4	0.6
Corporate Bonds	30.3	14.7	11.9	1.0	2.0	2.1
Japan Resident-Issued Foreign Bonds	13.5	0.8	0.1	1.1	0.0	0.0
Commercial Paper	3.6	1.3	0.0	3.1	1.0	1.5

continued on next page

Table 8 continued

	Business Corporations and Other Organizations	Government and Government-Related Financial Institutions	Central Bank	Households	Nonresident Investors	Total
Bank Debenture	0.6	0.7	0.0	0.1	0.0	11.7
Corporate Bonds	2.1	0.9	3.2	5.6	0.2	71.9
Japan Resident-Issued Foreign Bonds	0.0	0.0	0.0	0.0	13.4	29.0
Commercial Paper	1.5	0.0	2.0	0.0	0.0	12.4

Notes: Data as of 31 March 2015. The table uses the Bank of Japan definition of Corporate Bonds (事業債).
Source: ABMF SF1 based on Bank of Japan 2015 Flow of Funds statistics. <http://www.boj.or.jp/statistics/sj/>

as the expansion of asset management opportunities for investors, leading to a strengthening of the financial and capital markets. This, in turn, will result in the steady development of the Japanese economy. To this end, market participants need to take measures to vitalize the corporate bond market in their daily business activities to establish a sound and liquid market.

Since the global financial crisis, the vitalization of the corporate bond market has become a particularly important issue. At the onset of the crisis, liquidity in the short-term money market became extremely tight and many companies shifted to bank loans. In some cases, it was difficult to borrow from banks, and new and rollover issuance conditions were very unfavorable in the corporate bond market. In light of these circumstances, private corporations recognized the need to diversify their financing methods and sources of funds. Similarly, it has become increasingly essential to develop a corporate bond market with high degrees of transparency and liquidity to enable the steady financing of large amounts of money on a long-term basis.

Because strengthening the equity capital of banks and other financial institutions has become a major issue of global financial regulatory reform following the financial crisis, it is believed that banks' loan activities will change accordingly. It is expected that improving corporate bond market functions within a new regulatory environment will result in the proper development of financing mechanisms, including bank loans, and contribute to the advancement, enhancement, and stability of Japan's financial and capital markets. The development of the TPBM was in line with this approach.

Furthermore, developing the infrastructure of the corporate bond market in Japan and creating a more efficient market with higher levels of transparency and liquidity will increase the participation of foreign issuing corporations and investors, including those from Asia. It will also help the Japanese financial and capital markets play a role more suitable for the economic scale of Japan in global markets.

Building a market that meets the needs of Professional Investors such as institutional investors will contribute to improving the diversity of corporate bond issuers, market usability, and the diversification of asset management methods for investors, as well as enable Japanese market participants to utilize the human resources and information-analysis skills held by Japanese financial institutions. Strengthening the corporate bond market will also assist the Japanese capital market in playing an important role as a primary regional market within Asia.

Legal and Regulatory Framework

A. Legal Tradition

Japan is a market with civil law tradition. To some extent, it has also been influenced by English law, European Union law, and US law.

B. English Translation of the Law

1. Japanese Law Translation Database System

As far as the translation of the laws and regulations in Japan are concerned, the Ministry of Justice hosts a database of translated Japanese laws.²

2. Recommended English Expression

Separate from the above translations, examples of the Recommended English Expressions of Related Translations are included in Appendix 5.

C. Legislative Structure—Bond Market

Japan features a multitiered legislative structure to govern the financial and capital markets.

[1st tier] Constitution

[2nd tier] Statutes and acts (key legislation for the market and market participants)

[3rd tier] Subordinate legislation (Cabinet Order or Ministerial Ordinance)

[4th tier] Self-regulatory organization (SRO) rules (e.g., Japan Securities Dealers Association [JSDA], Tokyo Stock Exchange [TSE])

² All of the translations contained in this system are unofficial. Only the original Japanese texts of the laws and regulations have legal effect, and the translations are to be used solely as reference materials to aid in the understanding of Japanese laws and regulations. The Government of Japan is not responsible for the accuracy, reliability, or currency of the legislative materials provided, or for any consequences resulting from use of the information on the website hosted by the Ministry of Justice. For purposes of interpreting and applying a law to any legal issue, users should consult the original Japanese text published in the Official Gazette. Furthermore, any translation in which the title of a law indicates it to be a tentative translation has not yet been proofread or corrected by a native English speaker or legal translation expert; these translations may be revised in the future. Japanese Law Translation Database System by the Ministry of Justice. <http://www.japaneselawtranslation.go.jp/?re=02>

Statutes and acts, in the context of the bond market, refer to legislation specifically aimed at the securities market or capital market. These laws establish and govern securities markets or market segments, including the bond market, and related institutions and participants, and define instruments and their basic issuance requirements. These laws are passed by the National Diet of Japan (Parliament) and need to be promulgated in the Official Gazette within 30 days of the Cabinet sending them to the Emperor for assent. Laws generally state in their text when they take effect. The Companies Act and the FIEA effectively represent the key legislation relevant for the Japanese bond market. The FIEA is the fundamental law governing the domestic financial and capital markets, as well as securities and other financial instruments in Japan.

Subordinate legislation is issued in the form of a Cabinet Order or Ministerial Ordinance by the Government of Japan or the MOF as the government body administering the legislation for the financial and capital markets in Japan. This subordinate legislation renders statutes and acts effective and interprets aspects from key legislation for practical application in the markets.

In turn, the rules of the SROs, which have been charged with governing the market and its participants on a day-to-day basis, play a very important part in defining the roles and responsibilities of market institutions and their participants, and the actions they may take. These rules contain descriptions on how regulations should be applied and specific market activities carried out.

Table A3.1 in Appendix 3 contains a list of examples of significant legislation related to the bond market and applicable rules for each of the tiers of the legislative structure explained above.

D. Japan Bond Market Regulatory Structure

The capital market and various aspects of the bond market in Japan are governed by regulations issued and enforced by the MOF, Bank of Japan (BOJ), and FSA. In addition, the bond market is administered by three SROs: JSDA, the Japan Exchange Regulation (JPX-R), and TSE. The latter two are part of the Japan Exchange Group (JPX), which organizes their membership and market participation, and issues rules for market conduct and practices.

Market regulatory authorities involved in the bond and note issuance approval processes—in effect for corporate bonds, notes, and commercial paper—include the FSA and TSE.

1. Financial Services Agency

The financial and capital market of Japan is supervised solely by the FSA, which is part of the Cabinet Office. The FSA is the preeminent regulator for the Japanese financial industry and the domestic financial and capital markets. The Securities and Exchange Surveillance Commission is the FSA's enforcement arm for the securities market.

Pursuant to the FIEA, JPX-R and JSDA are SROs that oversee and inspect day-to-day securities trading. Market surveillance is a shared responsibility of the Securities and Exchange Surveillance Commission and these SROs.

2. Ministry of Finance Japan

The Financial Bureau of the MOF is responsible, among others, for matters concerning treasury systems, government debt management, local bonds, issuance of coins, the Fiscal Investment and Loan Program (FILP), national property, the tobacco industry, the salt industry, and ensuring proper management of BOJ operations and organization. In relation to JGBs, the MOF is responsible for maintaining balance in tenures or interest rates, among JGBs, announcing upcoming JGB issues, and providing relevant tax policies. The International Bureau of the MOF is responsible for the investigation, planning, and drafting of matters concerning foreign exchange and international monetary systems and their stability, adjustments of balance of payments, management of the Foreign Exchange Special Account, foreign exchange rates, international organizations related to economic cooperation or development, and loans and investment.

3. Bank of Japan

The BOJ decides and implements monetary policy with the aim of maintaining price stability. In implementing monetary policy, the BOJ influences the volume of money and interest rates through its operational instruments, including money market operations such as buying and selling JGBs, for the purpose of currency and monetary controls.

To contribute to the maintenance of the financial system's stability, the BOJ conducts on-site examinations and off-site monitoring of the institutions under its purview, and acts as the lender of last resort to provide liquidity as necessary. The BOJ is responsible for the entire operation of Japanese government securities, including issuance, registration, interest payment, and redemption.

4. Japan Securities Dealers Association

The JSDA is an association functioning as an SRO and as an interlocutor for the securities industry. Its legal status is as a Financial Instruments Firms Association authorized by the Prime Minister pursuant to Article 67-2, Paragraph 2 of the FIEA.

As a fully empowered SRO, the JSDA extensively regulates market intermediaries. Its self-regulatory functions encompass rule making, enforcement, inspection, disciplinary actions, accreditation of sales representatives, and dispute mediation. For a detailed review of the membership, roles, and functions of the JSDA, please refer to section E in this chapter.

5. Japan Exchange Regulation

Established under the FIEA as the self-regulatory arm of JPX, JPX-R is an entity specializing in the self-regulatory operations of financial instruments exchanges, such as Listing Examination, Listed Company Compliance, Market Surveillance, and Participants Inspection and Examination. JPX-R is conducting self-regulatory activities delegated by the TSE and the Osaka Exchange (OSE).

For a detailed review of the role and functions of JPX-R, please refer to section E in this chapter.

6. Tokyo Stock Exchange Regulation

As part of JPX, the TSE operates and governs the TPBM, the professional bond market in Japan. The TSE issues rules and regulations specifically for the TPBM as an SRO under the FIEA.³

For a detailed review of the role and functions of the TSE, please refer to section E in this chapter.

E. Self-Regulatory Organizations and Their Roles in the Japan Bond Market

As far as the bond market in Japan is concerned, the participation and daily business activities are organized, governed, and administered by the three SROs described in detail in this section.

1. Japan Securities Dealers Association

Today, the JSDA comprises less than 500 members consisting of securities firms (categorized as Regular Members) and other financial institutions operating securities businesses in Japan (categorized mostly as Special Members and in a certain case as Specified Business Members).⁴ As of 1 March 2016, JSDA members (Association Members) include 255 Regular Members, 212 Special Members, and 3 Specified Business Members.

In addition to its regulatory functions, the JSDA also provides vehicles for policy dialogue among the industry, the government, and other related parties; conducts and promotes investor education; and implements studies for further activating the market. The JSDA also has the authority to impose penalties upon Association Members. The purposes of the JSDA are to contribute to the protection of investors by ensuring fair and smooth trading in securities or other transactions by Association Members and promoting the sound development of the Japanese financial instruments business. Although there are other institutions performing SRO functions in Japan, their coverage of business and products is not as extensive as that of the JSDA.

The JSDA covers most of the transactions in Japan's capital market including those involving bonds, equities, and derivatives. In relation to the bond market, the JSDA is mainly concerned with rule-making, the establishment of best practices, and the bond price dissemination service. However, the JSDA does not operate a bond trading venue. The JSDA's bond market rule-making covers primary market underwriting rules (corporate bonds only) and secondary market trading rules. At the same time, in the context of the recently established market for bonds and notes issued under the ASEAN+3 Multi-Currency Bond Issuance Framework (AMBIF), the most relevant rules are provided by the TSE, which is the operator of the TPBM and its corresponding SRO.

The JSDA has also been providing a bond price dissemination service by gathering price information (based on the theoretical quotation) from designated Association Members and publishing these prices on a delayed basis (once a day). In addition to the existing system, the

³ See <http://www.jpx.co.jp/english/equities/products/tpbm/index.html>

⁴ Specified Business Members are financial instrument business operators exclusively dealing with specified over-the-counter derivatives transactions and/or crowd funding and other such activities.

JSDA started a new bond price dissemination service in November 2015 using actual traded prices for certain types of corporate bonds. For more details on the bond pricing service, please refer to Chapter III.I and Chapter IV.E.

In light of the fact that most bond and note transactions are being conducted in the over-the-counter (OTC) market in Japan, the JSDA in effect becomes a significant part of the regulatory structure. As a full-fledged independent SRO for the securities industry in Japan, the JSDA has issued a variety of rules, guidelines, and market practices for bond market participants. The main categories of these rules and guidelines are presented below.

a. Self-Regulatory Rules

JSDA members must comply with their own self-regulatory rules and guidelines. Their coverage ranges from items to be observed in outright transactions (sale or purchase) such as compliance with laws and regulations; maintenance of fairness of transactions; prohibition of extraordinary transactions; preparation and maintenance of trading records; and reporting of trade turnovers to items to be complied with in special transactions such as repurchase (repo) transactions and OTC options transactions requiring contracts or limiting the types of counterparties, among others. Regarding the rule requiring contracts, the JSDA has prepared a model format that has become the de facto standard in Japan.

The JSDA takes into account market conditions and the practical reality of transactions in establishing, revising, and abolishing rules for the purpose of achieving fair and smooth transactions in the Japanese securities market, thereby contributing to the protection of investors. During the rule-making process, a draft of rules is prepared first through deliberations mainly by JSDA members, subjected to public comment and other processes, and finally approved by the JSDA.

For easy reference, a list of the JSDA's Self-Regulatory Rules for Bond Transactions can be found in Table A3.2 in Appendix 3.

b. Guidelines

Guidelines are practical rules that the JSDA requests participants in the bond market to comply with and are thus recognized as best practices. As they are merely practices, those who do not comply with these guidelines are not penalized. However, as voluntary compliance with these guidelines in the overall market contributes to smooth and efficient transactions, most market participants observe the guidelines. Consequently, the JSDA collects and considers the opinions of market participants when setting new guidelines or revising or abolishing old ones. To date, the JSDA has published guidelines concerning delivery and settlement practices such as Deadline for Settlement (Cut-Off Time), Handling of Fails Charges, and order conclusion practices for When Issued Transactions, etc. for JGBs.

For easy reference, a list of the JSDA's recent guidelines related to the bond market can be found in Table A3.3 in Appendix 3.

c. Others

In addition to the above rules and guidelines, the JSDA occasionally issues advance notices to Association Members regarding standard procedures, such as the standard

calculation method of accrued interest, to eliminate the necessity of getting individual consensus between related parties regarding the unification of procedures among market participants.

2. Japan Exchange Regulation

JPX-R is the self-regulatory arm of JPX.

JPX was established via the combination of the TSE and the OSE on 1 January 2013. JPX operates financial instruments exchange markets to provide market users with reliable venues for trading listed securities and derivatives instruments. In addition to providing market infrastructure and market data, JPX also provides clearing and settlement services through a central counterparty and conducts trading oversight to maintain the integrity of the markets. In the course of working together as an exchange group to offer a comprehensive range of services, JPX continues to make every effort to ensure reliable markets and create greater convenience for all market users.

The TSE, OSE, JPX-R, and Japan Securities Clearing Corporation are JPX subsidiaries. Japan Securities Depository Center (JASDEC) is a JPX affiliate.

JPX-R's Self-Regulatory Function⁵

Established under the FIEA as the self-regulatory arm of JPX, JPX-R is an entity specializing in self-regulatory operations of financial instruments exchanges such as Listing Examination, Listed Company Compliance, Market Surveillance, and Participants Inspection and Examination. JPX-R conducts self-regulatory activities delegated by the TSE and OSE.

On 1 April 2014, the corporate name was changed from Tokyo Stock Exchange Regulation to Japan Exchange Regulation, or JPX-R, as part of JPX's corporate restructuring.

JPX-R fulfills a number of duties related to the operation of a securities market. It examines companies to assess their suitability as listed companies, requires these companies to comply with disclosure requirements so that investors are able to make informed decisions, and provides a marketplace for these companies' shares to be traded.

Pursuant to the FIEA, JPX-R has self-regulatory functions to maintain a transparent, equitable, and reliable market in support of a healthy economy.

3. Tokyo Stock Exchange's Role as a Self-Regulatory Organization for the TOKYO PRO-BOND Market

The TSE operates and governs the TPBM, the professional bond market in Japan. The TSE issues rules and regulations specifically for the TPBM as an SRO under the FIEA.⁶

Among other things, general disclosure requirements laid out in the FIEA such as the Securities Registration Statement (SRS) do not apply to the securities listed on the TPBM.

⁵ JPX-R. <http://www.jpx.co.jp/english/regulation/index.html>

⁶ See <http://www.jpx.co.jp/english/equities/products/tpbm/index.html>

Instead, specific disclosure requirements for the TPBM are stipulated in the rules and regulations of the TSE, such as the Specified Securities Information (SSI) and the Issuer Filing Information.

In principle, information on the TPBM-listed bonds and notes and information on their issuers shall be disclosed pursuant to the TSE's TPBM Listing Regulations and Enforcement Rules. A list of relevant TSE rules and regulations can be found in Table A3.4 in Appendix 3.

The TSE's TPBM Listing Regulations and Enforcement Rules and the JSDA's Self-Regulatory Rules for Bond Transactions have a mutually important and complementary relationship. The actual trading of bonds and notes in the OTC market is regulated under the JSDA's Self-Regulatory Rules for Bond Transactions (see also section D.1).

4. Outline of Coverage of the Three Self-Regulatory Organizations for the Japan Bond Market

For practical reference, the coverage of the three SROs with relevance for the bond market in Japan, including across its various segments, is provided in Table 9. Please refer to the relevant sections in this chapter for a detailed review of the roles and functions of each of the individual SROs.

Table 9: Coverage of the Three Self-Regulatory Organizations in the Japan Bond Market

		Primary Market	Secondary Market		
		OTC	OTC		EXCHANGE Trading System
JGBs		Government-Driven Market	JSDA		JPX-R (Conventional Market)
Corporate Bonds	Non-TPBM Listed Bonds	JSDA	JSDA		JPX-R (Only CBs are listed on the TSE)
	TPBM Listed Bonds (Profile Listing)	TSE	TSE	JSDA	n.a.

CB = convertible bond, JGB = Japanese Government Bond, JPX = Japan Exchange Group, JSDA = Japanese Securities Dealers Association, n.a. = not applicable, OTC = over-the-counter, TPBM = TOKYO PRO-BOND Market, TSE = Tokyo Stock Exchange.
Sources: JSDA and ABMF SF1.

The JSDA's SRO rule-making function provides a common platform for the securities business covering all types of financial instruments, including JGBs and corporate bonds, as far as the JSDA's member firms are involved in such business. At the same time, as shown in Table 9, the JSDA's rule-making does not apply to the JGB primary market and the trading of bonds and notes on exchanges.

In turn, JPX-R organizes and governs the trading of bonds and notes on the exchanges of JPX and across the conventional market in JGBs, as well as the trading of listed corporate bonds.

The TPBM features its own bond trading system in the TSE. However, all of the trading of its listed corporate bonds occurs on the OTC market, with market participants needing to observe certain selling and transfer restrictions.

Relationship between the TPBM and the JSDA's Rules. As the TPBM is operated by the TSE, the rules, in particular those related to private placement, are considered not applicable in the primary market of the TPBM. However, transactions involving TPBM-listed bonds in the secondary market depend upon the JSDA's rules and practices, including the price information of such bonds that are to be disseminated via the JSDA's statistical reference price system (see also Chapter III.I).

F. Legal Framework of Public Offering and Private Placement

In the Japanese corporate bond market, the FIEA distinguishes between a public offering of securities and a private placement of securities, irrespective of whether those securities are issued domestically or outside of Japan.

Table 10 contains a matrix of the applicable regulatory framework for the issuance and the secondary distribution of bonds and notes via both public offering and private placement in Japan.

Noteworthy matters in relation to the newly established professional securities market regime will be the introduction of the following two concepts: (i) the Solicitation for Acquisition to Professional Investors; and (ii) the Solicitation for Selling, etc. to Professional Investors. (These correspond to Newly Issued Securities and Already-Issued Securities, respectively. Please see 2-2 and 4-2 in Table 10.)

The objective of the introduction of these two concepts had been to stipulate an exemption from the statutory disclosure requirement on the securities for the benefit of Professional Investors, and the implementation of selling and transfer restrictions on the securities aimed at general investors, while also paying close attention to their mutual relations. In other words, Japan had been faced with the difficult challenge that was thought to be near impossible to achieve: combining strong and effective investor protection with ensuring the efficiency of a professional market. Hence, it became a policy objective for Japanese regulatory authorities to establish the necessary legal infrastructure to address this challenge.

Table 10: Regulatory Framework Matrix in the Corporate Bond Market in Japan

N: Notification duty to the authority D: Disclosure requirements	Newly Issued Securities (Primary Market) (新発債発行市場)		Already-Issued Securities (Secondary Market) (既発債流通市場)	
(PO/SD)	1. Public Offering (PO) of Securities (公募) (A Solicitation of an application to acquire newly issued securities)		3. Secondary Distribution (SD) of Securities (売出し) (Offers to sell and solicitation of offers to purchase already-issued securities)	
N: Yes—SRS D: Yes—Prospectus (Articles 4 (1) and 5 (1) of the FIEA)	1-1 Public Offering of Securities (有価証券の募集) (Solicitation of an application to acquire newly issued securities)	(Definition) Article 2-3 (1), (2), (3) of the FIEA (excluding Article 2-3 (ii) (a) (b)) (Notification) Article 4-1 of the FIEA	3-1 Secondary Distribution of Securities (有価証券の売出し) (Offers to sell and solicitation of offers to purchase already-issued securities)	(Definition) Article 2-4 (1), (2), (3) of the FIEA (excluding Article 2-4 (ii) (a) (b)) (Notification) Article 4-1 of the FIEA
N: No, but in case total amount is more than JPY10 million, Securities Notice (SN) is required D: No	1-2. Small Amount Issuance: (Total amount of the issue price of securities offered is less than JPY100 million) [Note: However, small amount issuances are typically not evident in the market. Please refer to the explanation in the text (1-2).]	Article 4-6 of the FIEA (Disclosure) Article 13-1 of the FIEA	3-2. Small Amount Secondary Distribution (SD): (Total amount of the secondary distribution price of securities placed is less than JPY100 million) (However, small amount secondary distributions are typically not evident in the market. Please see the explanation in text (3-2).)	Article 4-6 of the FIEA (Disclosure) Article 13-1 of the FIEA
N: Yes—SRS D: Yes—Prospectus (Article 4-3 of the FIEA)	(Outside of Scope—Logically Impossible)		3-3. General Solicitation of Already-Issued Securities that Have Been Acquired by Professional Investors, Etc. (特定投資家等取得有価証券一般勧誘)	(Notification) Article 4-3 of the FIEA (exceptions apply)
N: No D: No, but it requires concise and simplified information	(Outside of Scope—Logically Impossible)		3-4. Secondary distribution of certain foreign-issued securities by Financial Instruments Business Operators (Foreign Securities-SD) (外国証券売出し)	Article 4 (1) (iv) of the FIEA, Article 2 (12) (ii), (iii) of the Order for Enforcement of the FIEA
(PP/PSD)	2. Private Placement (PP) of Securities (私募) (A Solicitation for Acquisition which does not come within the purview of Public Offering of Securities)		4. Private Secondary Distribution (PSD) of Securities (私売出) (Offers to sell and solicitation of offers to purchase which do not come within the purview of Secondary Distribution of Securities)	
N: No D: No	2-1. Private Placement to Qualified Institutional Investors (QII-PP) (適格機関投資家私募)	(Definition) Article 2-3 (ii) (a) of the FIEA (Notification) Article 4-3 (1) of the FIEA	4-1. Private Secondary Distribution to Qualified Institutional Investors (QII-PSD) (適格機関投資家私売出し)	(Definition) Article 2-4 (ii) (a) of the FIEA (Notification) Article 4-2 of the FIEA
N: No D: No, but it requires Specified Securities Information (SSI: 特定証券情報) (Article 27-31 of the FIEA)	2-2. Private Placement for Professional Investors (PP for PI, or Offer to PI) (特定投資家私募) (Solicitation for Acquisition to Professional Investors) (特定投資家向け取得勧誘)	(Definition) Article 2-3 (ii) (b) of the FIEA (Notification) Article 4-3 (1) of the FIEA Article 40-5 (2) of the FIEA (Listing) Article 117-2 of the FIEA	4-2. Private Secondary Distribution to Professional Investors (PSD to PI) (特定投資家私売出し) (Solicitation for Selling, etc. to Professional Investors) (特定投資家向け売付け勧誘等)	(Definition) Article 2-4 (ii) (b) of the FIEA Article 2-6 of the FIEA (Notification) Article 4-3 (2) of the FIEA (Listing) Article 117-2 of the FIEA
N: No D: No	2-3. Small Number Private Placement (SN-PP) (少数私募)	(Definition) Article 2-3 (ii) I of the FIEA	4-3. Small Number Private Secondary Distribution (SN-PSD) (少数私売出し)	(Definition) Article 2-4 (iii) of the FIEA

FIEA = Financial Instruments and Exchange Act, SRS = Securities Registration Statement.

Notes: Private Secondary Distribution (PSD: 私売出し) is not an official term in the FIEA, but has been used in market practice. PSD is basically exempt from the statutory disclosure obligations in the Secondary Distribution.

Source: ABMF SF1.

The explanations in text of the individual bond and note issuance formats are provided in the order—and with the numbering—used in Table 10.

1. Public Offering (公募)

As a general rule, both 1. Public Offering and 3. Secondary Distribution shall not be made unless an SRS is filed by the issuer or the seller (offeror) or, alternatively, a Shelf Registration with the Japanese FSA. Both forms of offer are subject to notification to the authority and statutory disclosure requirements under the FIEA.

The seller (offeror) in both the Public Offering and the Secondary Distribution must prepare and deliver a prospectus to each prospective investor. Also, the issuer of any securities offered either through Public Offering or Secondary Distribution shall be subject to continuous disclosure obligations under the FIEA.

The public offering of corporate bonds, securitized (asset-backed) bonds, and nonresident bonds—except supranational institutions of which Japan is a member—are basically subject to disclosure requirements under the FIEA. All other government bonds and public bonds are exempt from FIEA disclosure requirements.

1-1. Public Offering (公募) (represents Solicitation of Acquisition of securities)

The term Public Offering of Securities as used in the FIEA represents solicitations of an application to acquire newly issued securities, referred to as a Solicitation for Acquisition. The seller (offeror) of the securities will incur the notification obligations of the filing of the Securities Registration Statement (SRS: 有価証券届出書) or, alternatively, the Shelf Registration (SR: 発行登録書) with the Director-General of the Kanto (or other applicable) Local Finance Bureau. The disclosure requirements, by way of filing an SRS or SR and delivering a prospectus (目論見書) under the FIEA and a related Order for Enforcement and Cabinet Office Ordinances, are applicable to this solicitation.

1-2. Small Amount Issuance (Not typically evident, except for SME bonds)

A public offering shall not be made unless the issuer has filed an SRS or unless any of the possible exemptions apply. One such exemption is the Small Amount Issuance under which the total amount of the issue price of the securities offered in Japan (Issue Price) is less than JPY100 million. In calculating the JPY100 million, the amount of certain simultaneous and/or past offerings shall be aggregated. The Small Amount Issuance is not a private placement as such, but rather a special form of public offering exempted from the notification and filing requirement under the FIEA.

In the case of a Small Amount Issuance, a Securities Notice (SN: 有価証券通知書), instead of the SRS, is required if the total amount of newly issued securities is larger than JPY10 million but less than JPY100 million. If the total amount of newly issued securities is equal to or less than JPY10 million, no such SN is required. If required, an SN must be submitted to the Local Finance Bureau. The SN, which is not made available for public inspection, must be filed by one day before the commencement of solicitation.

In reality, no market exists for corporate bonds with an issuance size of less than JPY100 million. At the same time, the Small and Medium Enterprise Agency (中小企業庁) reports that the majority of SME bonds are issued in sizes of less than JPY100 million.

2. Private Placement (PP) (私募)

The term Private Placement of Securities means a solicitation for acquisition which does not come within the purview of a Public Offering of Securities in the FIEA. The seller (offeror) of the securities will not need to observe the statutory disclosure obligations. It should be noted that in the case of a private placement, the seller (offeror) is obliged to make notice to the acquirer of the securities that (i) it is an issue by private placement, (ii) the securities have not been notified to the authority (neither SRS nor SR has not been filed), and (iii) specific transfer restrictions are attached to them. The acquirer should understand them and acknowledge the contents of said transfer restrictions.

The FIEA prescribes the following three offer types as private placements. As to newly issued securities, any offering other than these three categories is basically categorized as under the purview of a Public Offering.

2-1. Qualified Institutional Investor-Private Placement (QII-PP or Offer to PI) (適格機関投資家私募):

Qualified Institutional Investors (QIIs) include securities companies, investment management companies, investment corporations, foreign investment corporations, banks, insurance companies, certain pension funds, and general partners of certain partnerships.

The QII-PP is an offer for acquisition to be made exclusively to QIIs. The following are the requirements for the QII-PP:

- (i) Offerees are limited to QIIs only.
- (ii) The kind of securities offered is not the same as (a) securities for which continuous disclosure is made or (b) securities for Professional Investors.
- (iii) Any transfer of the securities is prohibited unless the transferee is a QII; such transfer restriction is (a) written on the certificates of the securities to be delivered, (b) written on the offering document, or (c) disclosed through the book-entry system of JASDEC.

In addition, the seller (offeror) of the securities must deliver a document that states that no SRS has been filed for the QII-PP and describes the contents of the transfer restriction.

Using this scheme, many of Japan's SMEs have been issuing bank-underwritten private placement bonds.

In the event that the issuer of the newly issued securities under a QII-PP is a foreign entity, the issuer is required to appoint an issuer's agent who is a resident of Japan, according to Article 1-3 of the Cabinet Office Ordinance on Disclosure of the Contents of Foreign Bond Issuers (外国債等の発行者の内容等の開示に関する内閣府令). The objective of this ordinance is to determine if there is a breach of obligation of the notice relating to the restrictions on resale. This ordinance is applicable only to the QII-PP, and not the TPBM.

2-2. Private Placement for Professional Investors (PP for PI, or Offer to PI) or Specified Solicitation for Acquisition (特定投資家私募 又は 特定投資家向け取得勧誘):

The PP for PI is a newly added provision in 2008. Article 2 (3) (ii) (b) and Article 2 (4) (ii) (b) of the FIEA stipulate the exclusions of the Private Placement (PP for PI) and Private

Secondary Distribution (PSD to PI) from the definitions of Public Offering and Secondary Distribution, respectively. By introducing these offering types, a new market for Professional Investors only (TPBM) was created in Japan in 2011.

The following is a summary of the requirements for the Private Placement to Professional Investors (PP for PI):

- (i) PP for PI is to be made exclusively to Professional Investors [投資勧誘の対象は特定投資家に限定] .
- (ii) Solicitations are made by Financial Instruments Business Operators (e.g., securities companies). In principle, they cannot make any offer to a person other than Professional Investors [発行と転売は原則証券会社経由] .
- (iii) The issuer of the securities is required to provide a concise SSI such as the issuer's web address where Professional Investors can find the issuer's corporate information and financials, etc. The issuer, of course, is not prohibited from making full disclosure in the SSI. The issuer can also flexibly choose disclosure such as (a) documents incorporated by reference or (b) documents not incorporated by reference but for information purposes only. The distinction is that, typically, documents incorporated by reference may need to be given an endorsement by a third party, while documents not incorporated by reference but for information purposes only will typically not require such an endorsement [簡潔な特定証券情報の提供による発行体の開示負担軽減] .
- (iv) The offerors are obliged to make a notification to the acquirer of the securities that (a) it is an issue by private placement, (b) the securities have not been notified to the authority (neither SRS nor SR has been filed), and (c) the applicable selling and transfer restrictions are attached to them [特定投資家への告知義務] .

The economic nature of the Offer to PI can be similar to a public offering because the concept of Professional Investors is much broader than QII and the number of offerees is not limited under the Offer to PI.

Specified Securities Information and the TOKYO PRO-BOND Market

Since the PP for PI is categorized as the Private Placement principally focusing on Professional Investors, and the PP for PI is excluded from the definition of public offering, the statutory disclosure requirements do not apply. However, the issuer of the securities is required to provide a concise SSI (特定証券情報) with respect to the securities and the issuer. The SSI basically combines two sets of information about (i) securities that are issued to Professional Investors and (ii) issuer information. If the issuer is a company listed on any Japanese financial instruments exchange or a nonlisted Japanese company with continuous disclosure, or a foreign company with continuous disclosure in its country of domicile, the SSI would typically represent information about the securities in question.

The TPBM was created as the specified financial instruments exchange market for providing this kind of concise SSI, based on the PP for PI scheme introduced in the FIEA.

2-3. Small Number Private Placement (SN-PP) (少数人数私募):

The SN-PP is a private placement to fewer than 50 persons (general investors).

The following are the requirements for an issuance of an SN-PP:

- (i) The total number of persons to whom the solicitation of an offer for acquisition is to be made, within any 6-month period in case of newly issued securities or 1-month period in case of already-issued securities, is 49 or less. In calculating the number of solicited persons for the purpose of the SN-PP, the number of the QIIIs is excluded from the total number of solicited persons only if the offer to such QIIIs fulfills the requirements of the QII-PP (see 2-1. i-iii).
- (ii) The kind of securities offered is not the same as (a) securities for which continuous disclosure is made or (b) securities for Professional Investors.
- (iii) Depending on the kind of securities, certain transfer restrictions are required. For instance, an SN-PP of bonds requires either
 - (a) a restriction of transfer other than en bloc transfer, or
 - (b) the number of the investment unit (e.g., number of bond certificates to be delivered) being less than 50 (dividing the investment unit is prohibited).

Such a transfer restriction must be written on the bond certificates to be delivered, written on the offering document, or disclosed through the book-entry system of JASDEC.

In addition, the seller (offeror) of the securities must deliver a document that states that neither an SRS nor an SR has been filed for the SN-PP and describes the contents of the transfer restrictions.

3-1. Secondary Distribution of Already-Issued Securities

As to secondary transactions for already-issued securities, these shall not be made unless the seller (offeror) has filed an SRS or SR with the Director-General of the Kanto (or other applicable) Local Finance Bureau.

There are several exemptions from notification and disclosure requirements attached to these secondary distributions. For instance, government bonds and public bonds are exempt from these requirements.

3-2. Small Amount Secondary Distribution of Already-Issued Securities (less than JPY100 million) (typically not evident in the corporate bond market)

A secondary distribution shall not be made unless the seller (offeror) has filed an SRS or unless any one of the potential exemptions applies. One such exemption is the Small Amount Secondary Distribution, under which the total amount of the price of securities offered in Japan is less than JPY100 million. In calculating the JPY100 million, the amount of certain simultaneous and/or past offerings shall be aggregated. The Small Amount Secondary Distribution is a special form of secondary distribution exempted from the notification and filing requirement under Article 4 (1) (v), Article 4 (5), and Article 4 (6) of the FIEA.

For this transaction, in case the issuance amount is more than JPY10 million, the filing of a Securities Notice (SN) may be required. If the issuer is either a listed company who has already been filing disclosure documents (securities reports and quarterly reports) continuously with the FSA, or a nonlisted entity who has already been continuously filing disclosure documents (annual securities reports and semiannual reports), who are collectively known as *kaiji kaisha*, then no notification is required for a secondary distribution of securities that amounts to less than JPY100 million. If the issuer is an entity who has not filed any disclosure documents with the FSA, who are collectively known as *hi-kaiji kaisha*, then a notification is required for a secondary distribution that amounts to more than

JPY10 million but less than JPY100 million. However, no notification is required if the total amount is less than JPY10 million.

3-3. General Solicitation of Already-Issued Securities That Have Been Acquired by Professional Investors (特定投資家等取得有価証券一般勧誘)

The transactions listed in i-iii below are categorized as 3-3. General Solicitation of Already-Issued Securities that Have Been Acquired by Professional Investors, which are exempted from the need to file an SRS (Article 2-12-4 (2) (i) of the Order for Enforcement of the FIEA):

- (i) Secondary Distribution of Already-Issued Securities for which Continuous Disclosure is made (Article 4 (1) (iii) and Article 4 (3) of the FIEA);
- (ii) Solicitation for Delivery of Existing Securities, etc. made by a Financial Services Provider, etc. to Professional Investors, etc. for himself or herself (Article 2-12-4 (2) (i) of the Order for Enforcement of the FIEA and Article 4 (3) of the FIEA); and
- (iii) Solicitation for Delivery of Existing Securities, etc. made to Nonresidents by entrusting it to a Foreign Securities Services Provider (Article 2-12-4 (2) (ii) of the Order for Enforcement of the FIEA and Article 4 (3) of the FIEA).

For the transactions above, an SRS (有価証券届出書) is not required (Article 4 (3) of the FIEA). A prospectus and the filing of a Securities Notice (SN: 有価証券通知書) are required only under limited circumstances.

3-4. Secondary Distribution of Certain Foreign-Issued Securities by Financial Instruments Business Operators (Foreign Securities-SD) (外国証券売出し)

This is categorized as a kind of secondary distribution but is exempted from filing an SRS. Other disclosure requirements are modified, although the provision of concise and simplified information is still necessary.

For this type of transaction, defined as a Secondary Distribution of Securities That Have Already Been Issued in a Foreign State, or for securities specified by a Cabinet Order as being equivalent (外国証券売出し), neither an SRS, a prospectus, nor an SN are required under Article 4 (1) (iv) of the FIEA or Article 2 (12) (ii), (iii) of the Order for Enforcement of the FIEA.

Under certain conditions in which disclosure has been made overseas, the required information on the securities and the trading price of the securities in Japan, etc. should be provided to the investors, etc. (Article 27-31 and Article 27-32 of the FIEA).

Although the Financial Instruments Business Operators offering foreign securities must provide a minimum necessary level of information on the securities and the issuer at the time of offering, any time the investors make a request after the offering, and at the time when certain material events (such as default of the issuer) occur after the offering.

4. Items Categorized as Private Secondary Distribution (PSD)

Private Secondary Distribution (PSD: 私売出し) is not an official term in the FIEA, but the term is used in market practice and therefore is included in this guide. PSD is basically exempt from the statutory disclosure obligations for Secondary Distribution.

As such, the offer types shown under 4-1, 4-2, and 4-3 are not deemed to be instances of Secondary Distribution, but are instead treated as PSDs.

4-1. Qualified Institutional Investor-Private Secondary Distribution (QII-PSD)

(適格機関投資家私売出し)

In the case that

- (i) all counterparties in the offering are QIIs,
- (ii) the issuer is not subject to continuous disclosure obligations in relation to securities of the same kind as the securities to be offered, and
- (iii) a transfer restriction is imposed on the acquirers prohibiting transfer to any person other than QII(s),

then the secondary offering may constitute a QII-PSD, in which case the issuer will not be subject to any disclosure obligations. When considering item (ii) above, such exemptions may only be available in the case of foreign (nonresident) securities.

4-2. Private Secondary Distribution to Professional Investors (PSD to PI)

(特定投資家私売出し)

PP for PI and PSD to PI are excluded from the definition of public offering and secondary distribution, respectively. Hence, the statutory disclosure requirements do not apply to them.

4-3. Small Number Private Secondary Distribution (SN-PSD)

(少人数私売出し)

In the following case that

- (i) the issuer is not subject to continuous disclosure obligations in relation to securities of the same kind as the securities to be offered;
- (ii) the number of counterparties in the offering is less than 50,
- (iii) for certain types of securities, the acquirer is prohibited from transferring the acquired securities (transfer restriction) except to a single person in a single transaction; or
- (iv) for foreign securities, privately distributed and already issued outside Japan to a small number of Japanese residents,⁷

⁷ In cases where foreign (nonresident) securities were privately brought to Japan, if the financial institution has made an SN-PSD of foreign bonds in Japan, by the rules of the JSDA, the financial institution must notify the JSDA of the number of owners and other information about the securities that the financial institution has dealt with. The JSDA, based on the notifications received from each financial institution, should aggregate the number of owners of the same securities. If the number exceeds 1,000, it is not allowed to continue bringing newly issued securities of the same type into Japan.

then the secondary offering may constitute an SN-PSD, in which case the issuer will not be subject to any disclosure obligations. When considering item (i), such an exemption may only be available in the case of foreign (nonresident) securities.

5. Other Transaction Types Excluded from the Definition of Secondary Distribution

Transactions (i)–(v) listed below are excluded from the definition of secondary distribution of securities and, therefore, the filing of an SRS and disclosure requirements do not apply (Article 1-7-3 of the Order for Enforcement of the FIEA):

- (i) transactions on a stock exchanges or proprietary trading system (PTS); the sale and purchase of securities conducted on a financial instruments exchange market or on a PTS (Article 2 (17) and Article 67 (2) of the FIEA);
- (ii) block trades between Financial Instruments Business Operators (e.g., securities companies and other financial institutions authorized to operate a securities business) or Professional Investors;
- (iii) certain transactions between Financial Instruments Business Operators;
- (iv) sale of securities, for which any PP has not been made in the past, between people who have close relationships with the issuer (e.g., directors of the issuer, major shareholders of the issuer, parents or subsidiaries of the issuer) or Financial Instruments Business Operators, provided that transactions are excluded, if both parties are Financial Instruments Business Operators; and
- (v) sale of securities, for which any PP has not been made in the past, by a person who is not listed in (iv).

G. Securities Issuance Regulatory Processes

1. Overview of Regulatory Processes in Japan

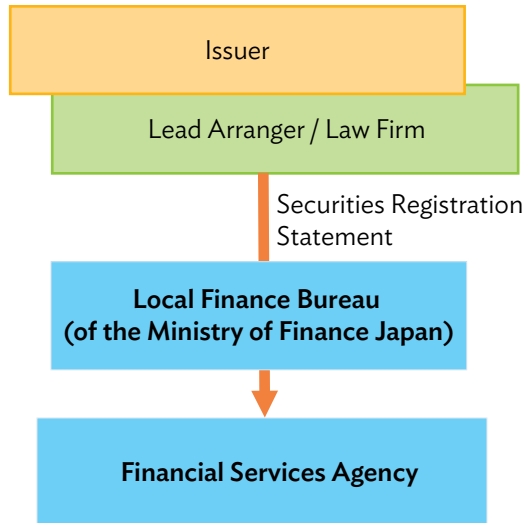
In Japan, the regulatory processes for the issuance of bonds and notes are inherent in the disclosure requirements for the respective type of offering, whether a public offering or a private placement. There are no approvals required from regulatory authorities for the public offering of bonds or notes, but issuers are required to file an SRS as part of the disclosure requirements for public offers. In turn, no approvals are required for the issuance of bonds or notes via private placement; instead, the issuer is required to provide the SSI as part of the respective disclosure requirements.

Only in the case of a listing for profiling of a private placement on the TPBM is an approval for said listing required by the TSE.

2. Regulatory Process Map—Public Offering

Figure 10 illustrates the regulatory process for the issuance of bonds and notes through a public offering. The process fundamentally consists of the filing of the SRS with the responsible Local Finance Bureau of the MOF, which is then to be directed to the FSA.

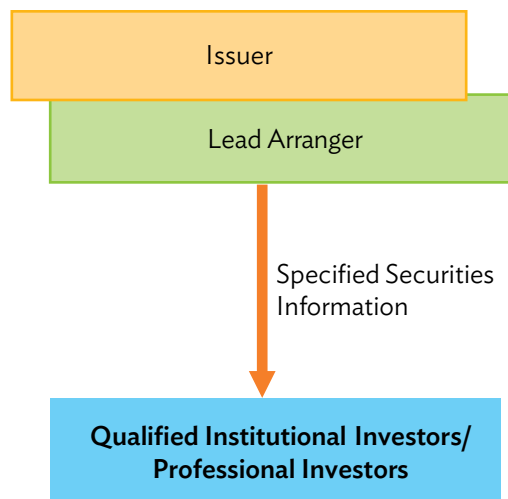
For a description of the necessary disclosure requirements, which include the submission of the SRS to the FSA, please see Chapter II.F. For the details on disclosure for public offerings, please see Chapter II.H.

Figure 10: Regulatory Process Map—Public Offering

Source: ABMF SF1.

3. Regulatory Process Map—Private Placements

Figure 11 details the regulatory process for the issuance of bonds and notes via a private placement. The process consists only of the provision of the SSI to the QII and/or Professional Investors.

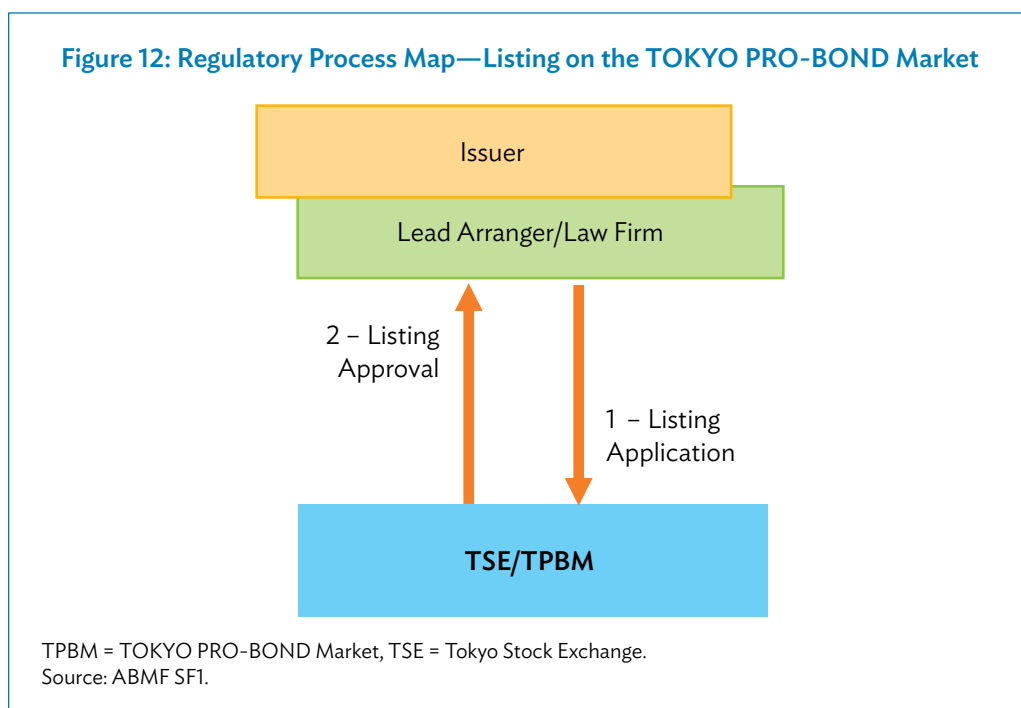
Figure 11: Regulatory Process Map—Private Placement

Source: ABMF SF1.

For a detailed description of the necessary disclosure requirements, including the provision of the SSI, please refer to Chapter II.F. For the application of these requirements, please refer to Chapter III.H, which details the profile listing on the TPBM.

4. Regulatory Process Map—Profile Listing on the TOKYO PRO-BOND Market

Figure 12 shows the regulatory process for the listing of bonds and notes on the TPBM. The process consists only of the listing application for the TPBM and approval by the TSE.



For a detailed description of the listing process and eligibility criteria for these securities and their issuers, please refer to Chapter III.H.

H. Disclosure Requirements for the Public Offering of Securities

The disclosure requirements for bonds and notes issued in the Japan bond market via a public offering are prescribed in the FIEA, and further detailed in the relevant Cabinet Ordinance. Distinctions are made in the regulations between the initial disclosure—in the form of the SRS—and the continuous disclosure requirements during the lifetime of the bond or note, as well as the disclosure requirements for foreign issuers.

In contrast, requirements for the disclosure of bonds or notes issuance via private placements are covered in the context of the TPBM (Chapter II.I).

1. Initial Disclosure: Securities Registration Statement

To make the information contained in the SRS (有価証券届出書) and its attachments accessible to general investors, the FIEA requires the SRS and its attachments to be filed by the issuer with the Director-General of the Kanto Local Finance Bureau of the MOF (e.g., if the bond or note issuance is to occur in Tokyo) or the relevant Local Finance Bureau, and for such filings to remain open for public inspection for a period of 5 years. In addition, the issuer must keep such documents at its head office and principal branch offices, and make them available for public inspection.

Once the SRS is filed with the relevant Local Finance Bureau, solicitation can be made; but before the securities are acquired by investors, the registration must have become effective. The registration becomes effective generally after a 15-day waiting period has elapsed from and excluding the day of filing.

In many cases, if the issuer is already filing continuous disclosure documents in relation to other securities issued, the waiting period is shortened to 7 days. If, prior to the effective date of the registration, any changes occur with respect to any material fact that should be stated in the SRS, or if there arises any situation prescribed by a relevant Cabinet Ordinance calling for the modification of the contents of the registration documents, the registrant should file an amendment to the SRS.

The SRS is generally composed of three sections: (i) Information Concerning Securities, (ii) Information Concerning Issuer, and (iii) Information Concerning Guarantor and Special Information. For the SRS for foreign-specified securities referenced in section 3, Information Concerning the Legal System of the Home Country of the Issuer must also be disclosed. In addition to the disclosure requirements, there are regulations concerning securities transactions under the FIEA designed to ensure fair trading.

2. Methods of Filing the Securities Registration Statement

The SRS may be filed using one of the methods described below.

a. Complete Full Disclosure SRS Method

The SRS must be filed by the issuer with the Director-General of the relevant Finance Bureau before the commencement of a public offering.

The issuer may instead choose one of the other methods—(b), (c), or (d)—provided the issuer satisfies certain conditions, as outlined.

b. Documents Embedded into SRS Method

Companies that filed an annual securities report for the previous year may embed annual securities reports, semiannual securities reports, or quarterly securities reports and their amendments into the SRS to avoid duplicate filing.

c. Documents Incorporated into SRS by Reference Method

Companies that already list their shares on the stock exchanges, or bonds and notes on OTC markets, and also satisfy additional requirements under a Cabinet Ordinance, may make reference in the SRS to the documents identified in (b), or those eligible

documents already submitted for disclosure for the other securities, rather than completing the entire SRS document.

d. Shelf Registration Method

Issuers that qualify to use the Reference Method can also use Shelf Registration to render their issue more cost-efficient and timely. Pursuant to a Cabinet Ordinance, any issuer who satisfies the requirements for registration by the Reference Method may register proposed offering(s) by filing with the relevant Finance Bureau a Shelf Registration Statement setting out the period during which the securities are intended to be offered, the kind of securities, and the proposed total amount of offering.

The Shelf Registration becomes effective after a shorter period (usually 7 days) than the period after filing the SRS. Once the Shelf Registration becomes effective, no individual SRS need be filed for the offering of any part of the securities covered by the Shelf Registration, but the registrant should file with the relevant Finance Bureau (i) an amendment to the Shelf Registration each time a new disclosure document such as a quarterly securities report is filed, and (ii) a supplement to the Shelf Registration setting out the amount of offering and other terms of the offering when new securities issued from the Shelf Registration are priced.

The Shelf Registration expires upon the last day of the intended period. If, prior to such expiry, the offerings of the total amount registered have been completed, the registrant should file a Shelf Registration Withdrawal Statement with the relevant Finance Bureau.

If, during the effective period of the Shelf Registration, a certain situation arises as prescribed by the FIEA and Cabinet Ordinance, such as new disclosure documents needing to be incorporated, the registrant should file an Amendment SRS. No such amendment can be made to increase the total amount of offerings, change the proposed period of offerings, or change the kind of securities subject to the registration.

Special provisions are made with respect to the Shelf Registration Method for commercial paper.

3. Forms of Initial Disclosure for Nonresident Issuers (Public Offerings)

A number of Cabinet Office Ordinances stipulate relevant notifications and the forms of initial disclosure by foreign issuers; these are provided in the following in the context of the necessary disclosure subjects.

a. Disclosure of Information Concerning Corporations

The Cabinet Office Ordinance on the Disclosure of Corporate Affairs, etc. (企業内容等の開示に関する内閣府令) stipulates the necessary notifications and disclosure of public offerings or secondary distributions of securities, and the necessary information about a foreign corporation to be submitted.⁸

⁸ See <http://law.e-gov.go.jp/htmldata/S48/S48F03401000005.html> (In Japanese; latest amendment date: 25 September 2015); <http://www.japaneselawtranslation.go.jp/law/detail/?id=2341&vm=04&re=02> (In English; translation date: 3 February 2010).

When a foreign company is issuing bonds in Japan, the appointment of an Issuer's Agent is necessary in most cases.

b. Disclosure of Information Concerning Issuers of Foreign Government Bonds

The Cabinet Office Ordinance on Disclosure of Information, etc. on Issuers of Foreign Government Bonds, etc. (外国債等の発行者の内容等の開示に関する内閣府令) details the notifications and disclosure of public offerings or secondary distributions of securities on issuers of foreign government bonds.⁹

c. Provision and Publication of Foreign Securities Information

The Cabinet Office Ordinance on the Provision and Publication of Information on Securities (証券情報等の提供又は公表に関する内閣府令) details the required information on securities issued by the foreign issuer in markets outside Japan (foreign securities). The relevant Articles (Articles 12–17) are contained in Chapter III (Provision and Publication of Foreign Securities Information) of the Cabinet Ordinance and are referenced as listed below:¹⁰

Article 12: Contents of Foreign Securities Information

Article 13: Cases Where the Provision or Publication of Foreign Financial Information Is Not Required

Article 14: Persons Equivalent to Those Who Have Entrusted the Custody of Securities

Article 15: Cases Where an Event That May Have a Material Influence on Investors' Investment Judgments Has Occurred

Article 16: Cases Deemed to Be Cases Where Protection of Investors Would Not Be Impaired

Article 17: Method of Provision or Publication of Foreign Securities Information

4. No Disclosure Requirements for Exempted Securities

JGBs, municipal bonds, bonds issued by judicial persons pursuant to special law, capital contribution certificates issued by a corporation established by a special law, beneficial certificates of loan trusts, bonds guaranteed by the Japanese government, and bonds issued by an international organization of which Japan is a member (e.g., International Bank for Reconstruction and Development [IBRD] bonds and Asian Development Bank [ADB] bonds) are exempted from the registration and continuous disclosure requirements described in this section.

⁹ See http://law.e-gov.go.jp/cgi-bin/idxselect.cgi?IDX_OPT=2&H_NAME=&H_NAME_YOMI=%82%a0&H_NO_GENGO=H&H_NO_YEAR=&H_NO_TYPE=2&H_NO_NO=&H_FILE_NAME=S47F03401000026&H_RYAKU=1&H_CTG=1&H_YOMI_GUN=1&H_CTG_GUN=1 (In Japanese; latest amendment date: 25 September 2015); <http://www.japaneselawtranslation.go.jp/law/detail/?id=2598&vm=04&re=02> (In English; translation date: 5 February 2010)

¹⁰ See <http://law.e-gov.go.jp/htmldata/H20/H20F10001000078.html> (In Japanese; latest amendment date: 15 May 2015); <http://www.japaneselawtranslation.go.jp/law/detail/?id=2063&vm=04&re=02> (In English; translation date: 2 June 2010)

5. Continuous Disclosure Requirement

Any (i) issuer of securities listed on any financial instruments exchange, (ii) issuer of securities that were subject to the registration requirement with respect to their public offering for initial issue or sale, and (iii) corporation whose number of shareholders at the end of any of the past 4 business years was 1,000 or more is generally required to prepare and file with the relevant Finance Bureau an annual securities report and quarterly securities report in the case of (i) (limited to the issuers of shares), or a semiannual securities report in the case of other issuers every year, and, from time to time, an extraordinary report. In the case of (i) (limited to the issuer of shares), an internal control report is also required. This is collectively referred to as the Continuous Disclosure Requirement as stipulated by the FIEA.

Such a Continuous Disclosure Requirement ceases when the listed securities are delisted—but as long as the company exists and outstanding shareholders exist, the issuer may have to continuously submit annual and semiannual securities reports—or upon obtaining the approval of the FSA when the issuer goes into liquidation or suspends its business for an extended period of time, or if the number of holders of the securities which were sold in the public offering for initial issue or sale is reduced to less than 25 or under certain circumstances set out in the Order for Enforcement.

Any issuer subject to the continuous disclosure requirement should prepare an annual securities report in the prescribed form within 3 months after the end of each of business year (in the case of foreign governments or corporations, within 6 months) and file the same with the Finance Bureau as provided in Article 24 (1) of the FIEA, for each year as prescribed by the Cabinet Office Ordinance.

If the business year of the issuer is 1 year, the issuer must generally prepare a semiannual securities report in the prescribed form covering the first 6 months of each business year and file it with the relevant Finance Bureau within 3 months from the end of such a 6-month period as the Continuous Disclosure Requirement. If the issuer is a company whose shares are listed on a securities exchange in Japan, the issuer must file a quarterly securities report instead of a semiannual securities report within 45 days from the end of such a quarterly period. The issuer also has to file an internal control report together with an annual securities report once every year.

When a certain important event occurs with respect to an issuer subject to the Continuous Disclosure Requirement, it should prepare and file with the Finance Bureau an extraordinary report without delay.

The annual securities report, semiannual securities report, quarterly securities report, internal control report, and extraordinary report are to be made available for public inspection via the Internet through a system named the Electronic Disclosure for Investors' Network (EDINET).¹¹

The FIEA contains provisions similar to those applicable to the SRS for amendments to the annual securities report, semiannual securities report, quarterly securities report, internal control report, and extraordinary report, as well as relevant parties' liabilities resulting from material misstatements and omissions.

In addition, issuers of listed securities are subject to various disclosure requirements prescribed by the relevant securities exchange, such as those for timely disclosure or material events.

¹¹ See <http://disclosure.edinet-fsa.go.jp/EKW0EZ1001.html?lgKbn=1&dflg=0&iflg=0>

6. Electronic Disclosure for Investors NETWORK

Disclosure documents, such as the SRS, are effectively filed using EDINET, which is an electronic system designed to accept disclosure documents filed under the FIEA. EDINET content is basically available in Japanese, but a search in English is possible. Documents written in English are marked with an indicator (“English”) on the left side of the name of the document submitted.

This system, which has digitized former paper-based disclosure procedures, was developed to make the securities market more efficient by reducing the reporting burden on companies and making it easier for investors to access company information.

Under this system, disclosure documents are filed online with the Finance Bureau and are made available to the public through the Internet. By using this system, issuers do not have to go to the Finance Bureau in person to file their disclosure documents. Furthermore, investors can browse through all of the filed documents on the Internet and access issuer information more easily.

The programming languages used to prepare the information required in the disclosure documents are HTML and XBRL.

I. Establishment of the TOKYO PRO-BOND Market

The TPBM represents the professional bond market in Japan, in contrast to the practices and the requirements for the public offering market discussed earlier. This section highlights the need for (and the purposes and processes behind the establishment of) the TPBM (Figure 13).¹²

1. The Need for a Market for Professional Investors

In a statement released on 21 December 2007, the FSA explained the need for a dedicated market for Professional Investors and the objective for the new professional market. The excerpt provided below best relates what led to the creation of the TPBM.¹³

I. Creation of reliable and vibrant markets

(ii) Development of a framework for markets intended for professionals

In other countries, markets with a high degree of freedom intended for Professional Investors are expanding, such as the AIM (Alternative Investment Market) in the United Kingdom and the market based on Rule 144A of the United States (US) Securities and Exchange Commission (SEC). This trend has been intensifying the international competition in creating attractive markets.

¹² Japan Exchange Group. TOKYO PRO-BOND Market. <http://www.jpx.co.jp/english/equities/products/tpbm/outline/index.html>

¹³ Financial Services Agency (FSA). 2007. *Statement on the Development of Markets for Professional Investors: Plan for Strengthening the Competitiveness of Japan's Financial and Capital Markets*. Tokyo

Investor protection, including through disclosure, will continue to gain greater importance in Japan. However, it is also essential to differentiate Professional Investors from general investors and allow the former more freedom in transactions under the principle of self-responsibility, from the viewpoints of making the country's financial and capital markets more vibrant and strengthening their international competitiveness.

Measures will be taken to establish markets among professionals that allow a high degree of freedom in transactions. The aim of this work is to raise the attractiveness of Japan's financial and capital markets as the places for financing and investment by expanding financing opportunities for foreign companies and Japanese start-ups in Japan, and to promote financial innovation through competition among Professional Investors. To this end, a framework utilizing the existing systems, including of private offerings to professionals, will be put in place by the end of 2008. This will be followed by the development of a new framework, based on new disciplines, for an exchange market, the participants of which will be expanded to include Professional Investors.

As announced, in 2008, the FSA revised the FIEA as part of its plan to enhance the competitiveness of Japan's financial and capital markets, establishing the legal framework for markets oriented toward Professional Investors, including an offering system for Specified (Professional) Investors and Specified Financial Instruments Markets as stipulated in the FIEA. This provided the legal framework for the establishment of a new securities market, which is different from the general public offering system and has a wider range of investors than, for example, the US Rule 144A market.¹⁴

An extract from the FSA's Newsletter in January 2008 explained the salient details of the law and regulations enacted regarding the establishment of new markets intended for Professional Investors.¹⁵

1. Introduction (excerpt)

Following the enactment and promulgation on 6 June and on 13 June of 2008, respectively, of the Act for the Amendment of the Financial Instruments and Exchange Act (hereinafter referred to as the Amendment Act), which includes provisions for institutional improvements necessary for strengthening Japan's financial and capital markets, the government decided, at a cabinet meeting on 2 December 2008, the Cabinet Order Concerning the Establishment and Revision of Relevant Cabinet Orders Related to the Enforcement of the Act for the Amendment of the Financial Instruments and Exchange Act and promulgated it on 5 December.

The key points of the revisions of the Cabinet Orders and Cabinet Office Ordinances that entered into force at this time are as follows:

¹⁴ The US Rule 144A market is a market for private offerings exempted from disclosure under Rule 144A, which was introduced to the Securities Act, 1933 by the US Securities and Exchange Commission in 1990. When bonds and other instruments targeting Professional Investors are issued in US markets, rather than employing public offerings, which entail stringent legal standards for document disclosure, it is normal to follow Rule 144A by making the offering exclusively to qualified institutional buyers. In the US, the Rule 144A market is available as a domestic professional investor market. The re-sale of such offerings within the US is on principle restricted to qualified institutional buyers under Rule 144A.

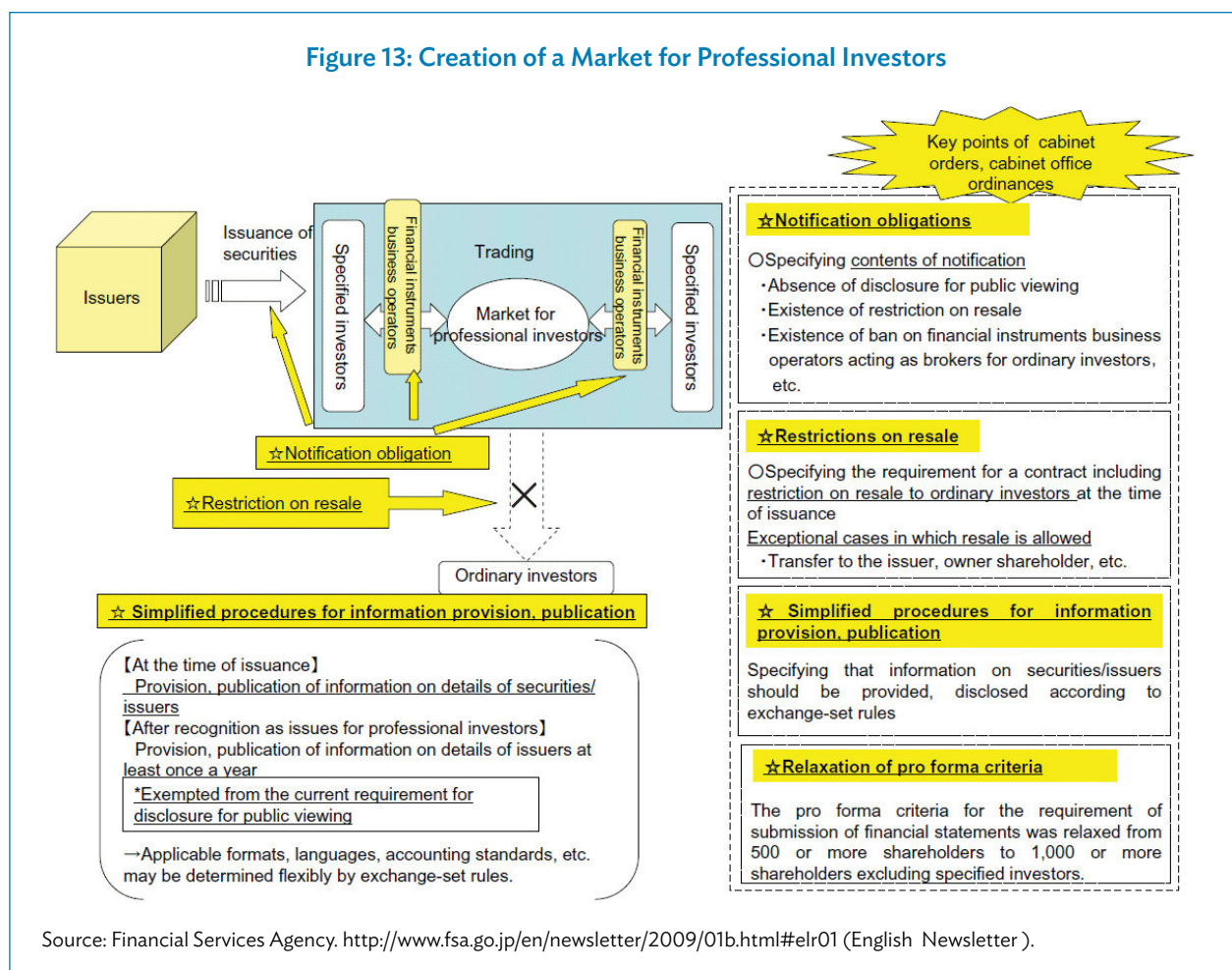
¹⁵ Financial Services Agency (FSA). 2008. Cabinet Orders and Cabinet Office Ordinances Concerning the 2008 Amendment of the Financial Instruments and Exchange Act. *FSA Newsletter*. Tokyo. January.

2. Establishment of new markets intended for Professional Investors (excerpt)

The Amendment Act puts in place an institutional framework for new markets intended for Professional Investors (specified investors), and instead of imposing the current disclosure rules requiring the availability of information for public view as a prerequisite on issuers which are to be listed on such new markets, it allows such issuers to use simplified procedures for the provision and publication of information.

The Cabinet Orders and Cabinet Office Ordinances that entered into force at this time include the following provisions for institutional improvements:

- (i) Specifying the details of the obligation for the notification of solicitation activities and transactions related to financial instruments intended for Professional Investors as well as the details of the restriction on the resale of such financial instruments that is aimed at preventing resale to ordinary investors
- (ii) Specifying that the contents of information regarding securities and issuers and the method of information provision should be based on rules set by exchanges.



In addition, the taxation system was reformed in FY2010 to remove the tax on revenues from domestic bonds held by nonresidents. The creation of the TPBM and removal of taxes addressed measures in the legal and taxation systems, respectively, that had previously separated domestic bonds from Eurobonds and other international bonds in Japan, and led to a new phase in the Japanese bond market in which the choice of issuance of either domestic or international bonds came down to the circumstances and/or preferences of issuers and investors alike.

2. The TOKYO PRO-BOND Market as a Professional Investors Market in Japan

Following the introduction of the necessary legal framework through the FIEA, the financial instruments exchanges were allowed to create a market in which the listed securities may not be transferred to any person other than specified investors or certain nonresidents of Japan. Such a financial instruments exchange market is defined as a specified financial instruments exchange market in the FIEA.

Securities that are listed on a Specified Financial Instruments Exchange Market but not listed on a regular financial instruments exchange market are defined as Specified Listed Securities in the FIEA. Holders of Specified Listed Securities may not transfer them to any person other than specified investors or certain nonresidents of Japan, whether at the financial instruments exchange or in the OTC market, unless the issuer of the securities files an SRS in advance.

Table 11 compares the terms used in the FIEA with the ones used in actual market practice that are referenced above and throughout this guide.

Table 11: Comparison of Financial Instruments and Exchange Act Terms with Market Practice Terms

Financial Instruments and Exchange Act Term	Market Practice Term
Private offerings to professionals	Private Placement for Professional Investors (PP for PI, or Offer to PI)
Specified Financial Instruments Exchange Market	TOKYO PRO-BOND Market (TPBM)
Specified Investors	Professional Investors
Specified Listed Securities	TPBM listed PRO-BOND

Source: ABMF SF1.

Under these provisions, the JPX Group established the listing system as outlined below for bonds and notes on the TPBM in May 2011. The TPBM is operated by the TSE as a market distinct from the TOKYO PRO market, which focuses on the listing of equities.

The TPBM is the single market in Japan for listed programs or listed bonds and notes under the appropriate extent of disclosure aimed at Professional Investors as a Specified Financial Instruments Exchange Market pursuant to Article 2 (32) and Article 117 (2) of the FIEA.

With the TPBM being a Specified Financial Instruments Exchange Market, its member securities companies are not allowed to deal with investors other than Professional Investors when soliciting for, or transacting in, bonds or notes listed on the TPBM.

3. Basic Principle of the TOKYO PRO-BOND Market

The relevant articles of the FIEA stipulate the exclusions of the Offer to PI and PSD to PI from the definitions of Public Offering and Secondary Distribution. Under these Offer to PI and PSD to PI schemes introduced in 2008, participation in the TPBM only requires the issuer to provide concise information, through the SSI, aimed at the professional market. The objective is to deal with the solicitation that does not correspond to a public offering or a secondary distribution, which require full statutory disclosure.

Hence, the basic principle of the TPBM concept can be described as follows: the issuers and the intermediary financial institutions incur the obligation to provide Professional Investors with certain specified information (in the form of the SSI) required by the TSE, in exchange for being exempted from the strict statutory disclosure requirement of filing the SRS, etc. under Article 2 (31), (32); Article 2 (3) (ii) (b); and Article 2 (4) (ii) (b) of the FIEA.

For further detailed information on the actual listing requirements imposed by the TSE and the listing process on the TPBM, please refer to Chapter III. H.

J. Participation of Nonresidents in the Japan Bond Market

This section covers the general considerations of nonresident, or foreign, issuers and investors in the Japan bond market, as well as specific requirements that may exist for nonresidents at market entry and exit.

1. Nonresidents Are Treated as Professional Investors

The Professional Investor System under the FIEA classifies “investors [or] customers eligible to be protected by way of regulation” and applies regulation in accordance with the investor or customer classes to ensure regulatory flexibility. Therefore, “investors not eligible to be protected by way of regulation” are not covered by the Professional Investor System in the first place.¹⁶

As the FIEA is basically intended to protect residents in Japan, foreign investors who are nonresidents are presumed to not necessarily be eligible for protection. However, foreign investors (nonresidents) are presumed to be eligible for protection and to be covered by the Professional Investor System when Financial Instruments Business Operators, such as securities companies, sell products to them or solicit them as customers in Japan.

When these Financial Instruments Business Operators conduct transactions with foreign juridical persons in Japan, it is presumed to not always be necessary to apply various investor protection laws. In light of this, as well as for the convenience of foreign investors (nonresidents), foreign juridical persons among foreign investors (nonresidents) are treated as “Professional Investors who may change their status to general investors as an option.”¹⁷

On the other hand, individual foreign investors are treated in the same way as domestic individual investors. However, with regard to individuals who are managers of partnerships

¹⁶ Excerpt (partly amended by ABMF SF1) from Financial Services Agency. 2015. *FAQ on Financial Instruments and Exchange Act: Section 6*. http://www.fsa.go.jp/en/laws_regulations/faq_on_fiea.pdf

¹⁷ Government of Japan. 1948. *Financial Instruments and Exchange Act Article 2-31 (iv), and Article 23 (x) of the Definition Ordinance*. Tokyo.

based on foreign laws and regulations, it is presumed to be difficult to check whether they meet the requirements for Professional Investors who may change their status to general investors as an option given the diverse types of partnerships based on foreign laws and regulations. Therefore, in order to facilitate the conduct of practical affairs and for other objectives, such individuals are not treated as “Professional Investors who may change their status to general investors as an option.”¹⁸

Individuals who are managers of anonymous partnerships, those who are operating partners of partnerships as specified by the Civil Code, or those who are involved in decisions on the execution of important business operations of limited liability partnerships and execute them are treated as “Professional Investors who may change their status to general investors as an option under certain conditions.”¹⁹

2. No Specific Limitations for Nonresidents

There are no restrictive regulations or limitations for nonresidents, which in this context is taken to mean foreign juridical persons, preventing them from being issuers of and investors in bonds and notes in the Japanese market.

3. Market Entry Requirements for Nonresidents

a. Foreign Issuers

Nonresident (foreign) issuers can issue bonds and notes in Japan. The issuance of JPY-denominated bonds and notes is not subject to approval from the government. The issuance of bonds and notes denominated in a foreign currency is also not subject to approval from the government. A public offering of bonds or notes issued by nonresidents are subject to statutory disclosure requirements under the FIEA.

In cases of nonresident issuers offer debt securities for sale to Japanese investors, the issuer may need to appoint a so-called Representative in Japan in order to be able to distribute information on bond and note issues, and to be available for any queries or information requests from investors.

With respect to a private placement of newly issued securities for QIIs, see also Chapter III.K and Chapter III.E. If the issuer of the securities is a foreign entity, the issuer is required to appoint an issuer’s agent who is a resident of Japan, according to Article 1-3 of the Cabinet Office Ordinance on Disclosure of Information, etc. on Issuers of Foreign Government Bonds (外国債等の発行者の内容等の開示に関する内閣府令). The objective of this ordinance is to identify if there is a breach of obligation of the notice relating to the restrictions on resale and, ultimately, to ensure that there is no breach. This ordinance is applicable just for the QII-PP and not applicable for TPBM.

The regulations and practices of the TPBM do not distinguish between resident and nonresident issuers. The scope of issuers on the TPBM includes

¹⁸ Government of Japan. 1948. *Financial Instruments and Exchange Act Article 34-4 (1) (i), and Article 61 (2) of the Financial Instruments Business Ordinance*. Tokyo.

¹⁹ Government of Japan. 1948. *Financial Instruments and Exchange Act Article 34-4 (1) (i), and Article 61 of the Financial Instruments Businesses Ordinance*. Tokyo.

- foreign corporations,
- foreign financial institutions,
- sovereign and government-sponsored issuers,
- Japanese corporations,
- Japanese public entities (e.g., local governments).

All eligible issuers may utilize note issuance programs as a form of bond and note issuance.

b. Foreign Investors

Nonresident (foreign) investors may invest in any bonds or notes issued in Japan without any restrictions.

4. Market Exit Requirements for Nonresidents

a. Foreign Issuers

There are no specific market exit requirements for foreign issuers.

b. Foreign Investors

There are no market exit requirements for foreign investors.

5. English Disclosure for Nonresident Issuers

a. General Disclosure in English

As far as the information disclosure in English in the public debt market is concerned, by the amendment of the Securities and Exchange Act, 2005 and the subsequent revision of the FIEA in 2011, if the issuer is a foreign company, it is permitted for the issuer to submit the continuous disclosure documents in English with the public inspection in a foreign country based on the foreign disclosure rules (FIEA Article 24 (8)).

b. Listing with English Disclosure on the TOKYO PRO-BOND Market

On the other hand, concise information disclosure in English for the TPBM professional investor market is also available under the applicable TSE Rules. Foreign companies are able to raise funds without a disclosure of relevant information in Japanese. In addition, it is also possible that Japanese domestic issuers conduct information disclosure in English.

Foreign issuing entities (e.g., corporations, organizations) likewise stand to benefit from the added convenience. Whereas conventional Samurai Bond issuance requires Japanese-language full disclosure, the TPBM allows concise English-language disclosure or a combination of the two.

A foreign issuing entity may decide to present disclosure materials in Japanese and English at the time of the issuance and later follow with English-language disclosure. However, it would be necessary to take measures to ensure that investors are clear about the disclosure language being adopted by, for example, letting them know at the time of issuance that subsequent disclosure will be conducted only in English. Also, an

issuing entity may use both Japanese and English in the same disclosure material for the sake of convenience of both the issuer and the investor.

The TSE's Special Regulations of Securities Listing Regulations Concerning Specified Listed Securities, Rule 202 states the following:

When an entity carrying out program listing (where the scheduled issuance period contained in the Program Information announced by such entity has passed, excluding such entity; the same shall apply hereinafter), an initial listing applicant (limited to an entity which applies for initial listing of a bond; the same shall apply hereinafter in this part), or an issuer of a listed bond prepares material for disclosure, it must use either the English language or the Japanese language, or both languages.

Domestic and foreign investors will benefit from the increased variety of securities in the Japanese market because more domestic and overseas issuers will be able to issue in Japan through the TPBM. Overseas investors will find it easier to invest in the Japanese market thanks to increased disclosure in English.

K. Regulations on Credit Rating Agencies

This section covers the regulations and requirements applicable to credit rating agencies (CRAs) and their business. For the application of credit ratings in the issuance process of bonds and notes in the TPBM, please refer to Chapter III.L.

Credit ratings were introduced in Japan in the 1980s. Since then, it has become general practice in the issuing of and investing in corporate bonds. After the 1996 abolishment of the “eligibility standards”—the policy which excluded bonds that did not meet the eligibility standards established by the market participants—credit ratings have not been a regulatory requirement for bond issuances. However, credit ratings have been prevailing along with the growth of the corporate bonds market (see also Chapter III.L).

In 1992, the MOF started the designation system of the CRAs. However, following the global financial crisis, there were significant controversies about the regulating of CRAs. A new regulatory system followed in Japan: the Amendment of the FIEA, which was put in force in April 2010, established a registration system for CRAs.²⁰ The registered CRAs have since been supervised by the FSA. The purpose and process of the introduction of the registration system is explained in Figure 14, and the Guidelines for the Supervision of CRAs are summarized in Figure 15.²¹

The registered CRAs are subject to a number of requirements, including the (i) duty of good faith; (ii) duty to maintain an operational management system that prevents conflicts of interest and ensures the fairness of the credit rating process; (iii) prohibition on giving a credit rating to a security that they hold; and (iv) the duty to disclose information, including to prepare and make available for public inspection the policies for credit ratings and the documents for public release and explanation.

²⁰ Financial Services Agency. 2010. *Financial Instruments and Exchange Act Related to Regulation on Credit Rating Agencies*. <http://www.fsa.go.jp/en/news/2010/20100331-4/02.pdf>

²¹ Financial Services Agency, Securities Business Division Supervisory Bureau. 2014. *The Guidelines for Supervision of Credit Rating Agencies*. <http://www.fsa.go.jp/en/refer/guide/rating.pdf>

Registered CRAs in Japan as of 31 March 2016 include the following:

- Fitch Ratings Japan Limited
- Japan Credit Rating Agency, Ltd. (JCR)
- Moody's Japan K.K. Moody's SF Japan K.K
- Rating and Investment Information (R&I)
- Standard & Poor's Ratings Japan K.K. / Nippon Standard & Poor's K.K.

Bond issuers shall note ratings in the Securities Registration Statement (SRS) and its attachments and prospectus or offering circulars, and indicate ratings from registered CRAs as such. Financial instruments business operators, such as securities firms, have the obligation to explain whether the ratings are from a registered CRA or not and other required matters.

In soliciting customers, financial instruments operators, such as securities companies, shall not use the credit ratings provided by unregistered CRAs without informing customers of (i) the fact that those CRAs are not registered and (ii) the significance and limitations of credit ratings.

CRAs shall provide or make available to the public the credit ratings it determined without delay after the determination or withdrawal of such credit ratings by posting them on its free website with statutory disclosure items under Japanese laws and ordinances.

A foreign CRA is an unregistered CRA, even if it belongs to the same group of a registered CRA. In the Cabinet Ordinance related to the CRA regulations, however, there is the easing explanation rule that admits to feature the name and registered number, etc., of the registered group company, if the group and the unregistered company fulfill the required conditions about the quality and simultaneity of publicized information and rating methodology, etc.

Figure 14: Introduction of Regulation for Credit Rating Agencies

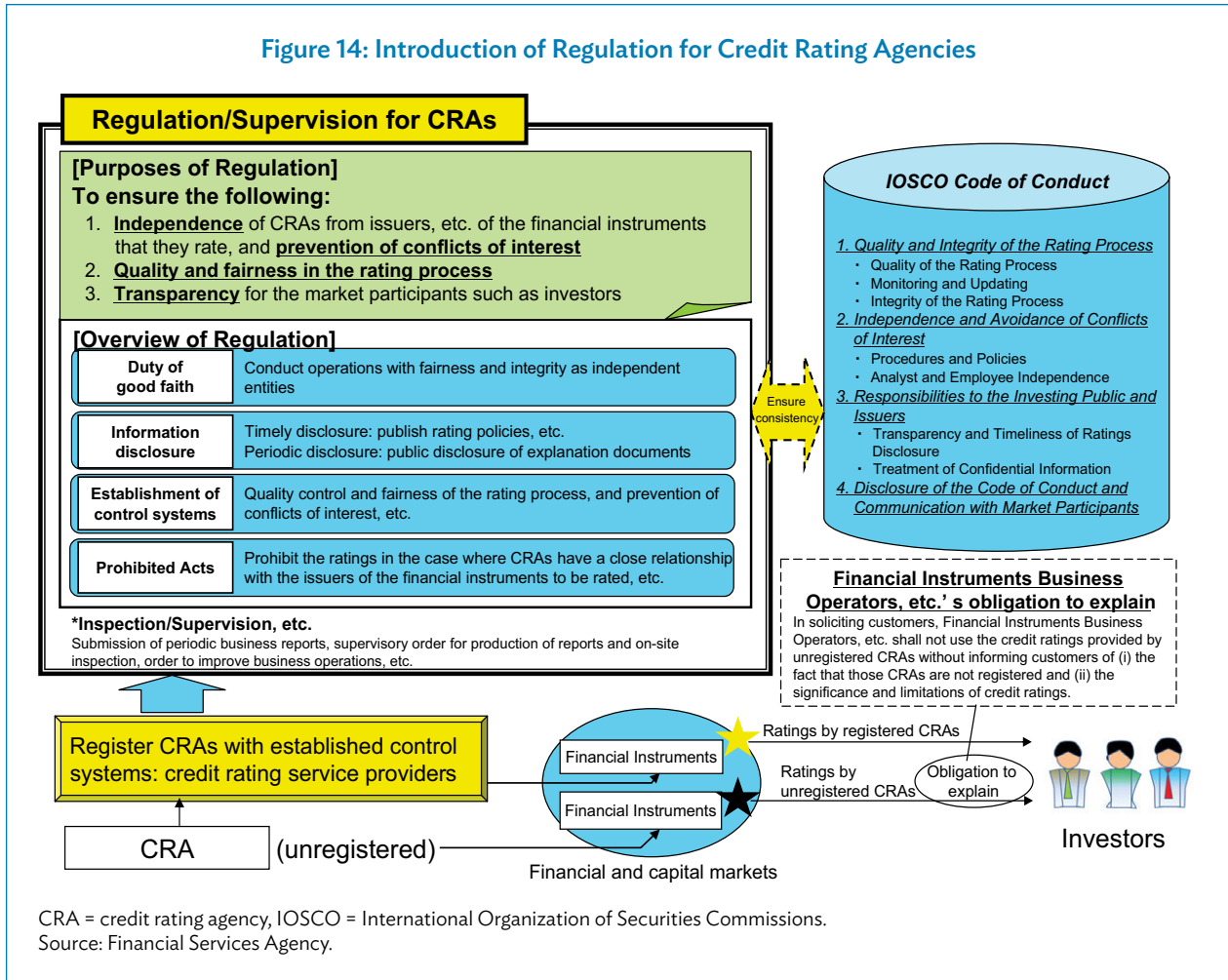
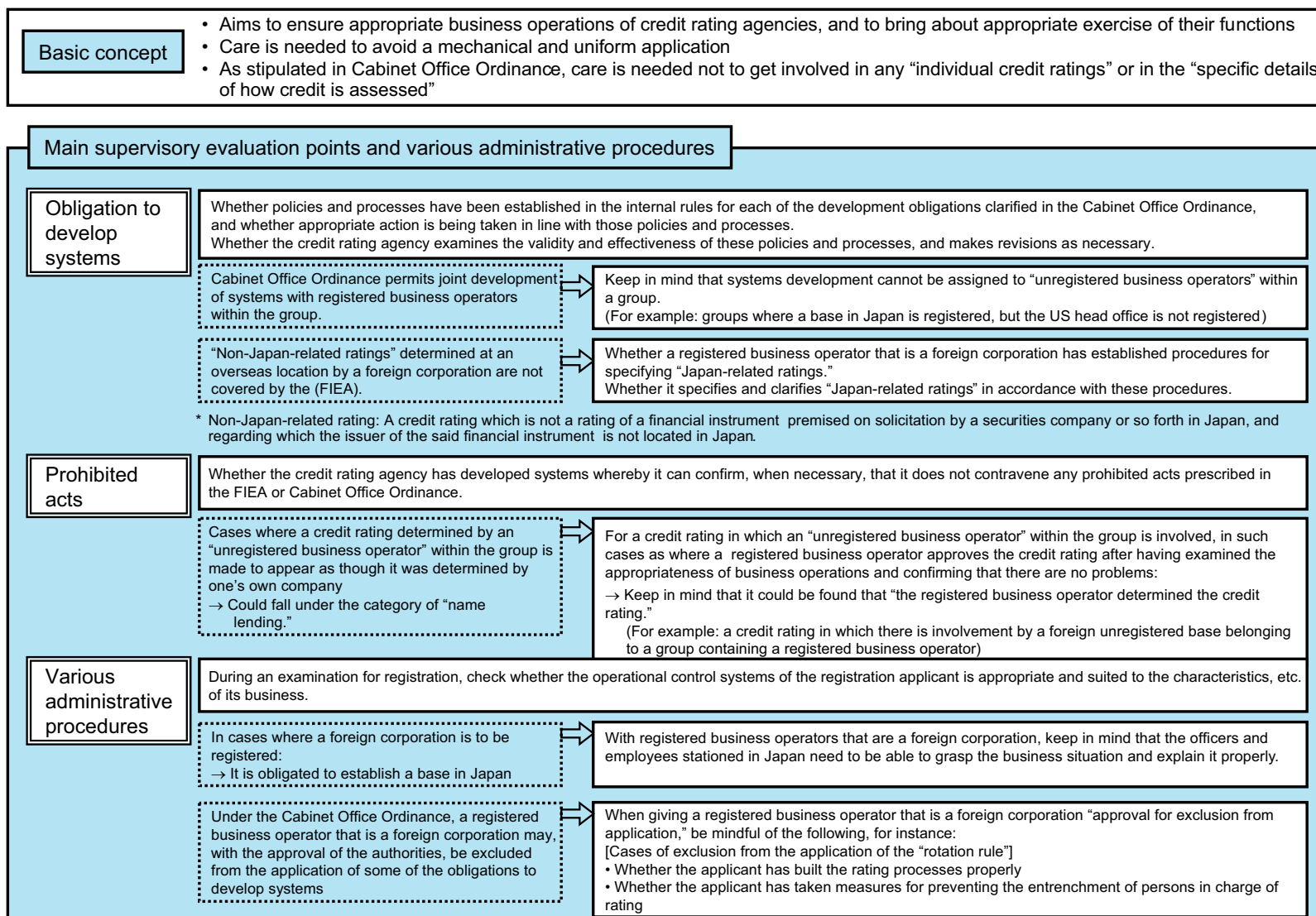


Figure 15: Summary of Guidelines for Supervision of Credit Rating Agencies



Source: Financial Services Agency.



Characteristics of the Japan Bond Market

A. Definition of Corporate Bond

Article 2 (23) of the Companies Act defines a corporate bond. Bond means any monetary claim owed by a company by allotment under the provisions of the Companies Act and which will be redeemed in accordance with the provisions on the matters listed in the items of Article 676 (Determination of Matters on Bonds for Subscription).

B. Types of Bonds and Notes

The term bonds generally refers to debt securities issued by governments and other public entities as well as by private companies. The issuance of bonds is a means of direct financing, through which the issuer raises funds but, unlike equity financing, the issuer has an obligation to repay the principal at maturity.

Table 12 provides an overview of the types of bonds and notes in Japan, and their classification into the categories shown, while the individual types of bonds and notes are explained in greater detail over the subsequent sections.

Table 12: Overview of Types of Bonds and Notes Issued in Japan

Type of Issuing Institution	Typical Term Used (including abbreviation and Japanese characters)	Types and Varieties	Explanatory Remarks
Public	1. Japanese Government Bond (JGB: <i>koku-sai</i> , 国債) ^a	<ul style="list-style-type: none"> Interest-bearing: Fixed-rate (2yr, 5yr, 10yr, 20yr, 30yr, 40yr), Floating-rate (15yr), Inflation-indexed (10yr) JGB for Retail(Individual) Investor: Fixed-rate (3yr, 5yr), Floating-rate (10yr) Separate Trading of Registered Interest and Principal of Securities (STRIPS) 	
	2. Treasury Discount Bills (T-Bill) (国庫短期証券) (While maintaining their respective position in the financial system, TBs and FBs have been called and issued as T-Bill with an integrated manner in the market.) (“T-Bill” is the sum of “Treasury Bills (TBs)” and “Financial Bills (FBs)” with a maturity of 1 year or less and TBs and FBs have been jointly issued since February 2009.)	<ul style="list-style-type: none"> Treasury Bills (TBs) (6m, 1yr) (割引短期国債) Financing Bills (FBs) (2m,3m,6m, 1yr) (政府短期証券) 	<p>To finance fiscal expenditures (the same as JGBs with other maturities)</p> <p>To finance the National Treasury on a short-term basis or cover temporary fund shortage in a special account</p>

continued on next page

Table 12 continued

Type of Issuing Institution	Typical Term Used (including abbreviation and Japanese characters)	Types and Varieties	Explanatory Remarks
Public	3. Local governments bond or Municipal Bond (<i>chiho-sai</i> , 地方債)	<ul style="list-style-type: none"> Publicly offered Regional Bond (3yr–30yr) Citizen participatory-type Public Market Offering Bond (3yr–10yr) Privately Offered Regional Bond 	Issued by prefectures, municipalities (cities, towns, and villages)
		<ul style="list-style-type: none"> Local governments agency bond (Japan Finance Organization for Municipalities [JFM] bond) (<i>chihoukoukyoudantaikinyukikou-sai</i>, 地方公共団体金融機構債) 	The Japan Finance Organization for Municipalities was founded by all local governments (prefectures, cities, wards, towns, and villages).
	4. Government Agency Bond, etc. (<i>seifukankeikikan-sai tou</i> , 政府関係機関債等)	(Government-Guaranteed Bond) <ul style="list-style-type: none"> Japanese Government-Guaranteed Bond (2yr–40yr) (<i>seifuhosho-sai</i>, 政府保証債) 	
		(Non-Government-Guaranteed Bond) <ul style="list-style-type: none"> Fiscal Investment and Loan Program (FILP) Agency Bond (2yr–40yr) (<i>zaitokikan-sai</i>, 財投機関債) Government-Affiliated Corporation Bond (<i>hi-koubo-tokushu-sai</i>, 非公募特殊債) 	
(Non-Government-Guaranteed Bond) <ul style="list-style-type: none"> Local Public Corporation Bonds (<i>chihoukousha-sai</i>, 地方公社債) 			
Private	5. Corporate bonds (<i>shasai</i> , 社債)	<ul style="list-style-type: none"> a. Straight corporate bonds, etc. (<i>futsu-shasai</i>, 普通社債等) b. Asset-backed corporate bonds (<i>shisantanpogata-shasai</i>, 資産担保型社債) c. Convertible bonds (<i>tenkan-shasai</i>, 転換社債) 	
		6. Bank debentures (<i>kinyu-sai</i> , 金融債)	
Nonresident	7. Nonresident bonds (foreign bonds) (<i>hikyojusha-sai</i> , 非居住者債)	<ul style="list-style-type: none"> JPY-denominated foreign bonds (<i>endate-gaisai</i>, 円建て外債; <i>samurai-sai, tou</i>, サムライ債等) Asset-backed foreign bonds (<i>shisantampogata-hikyojusha-sai</i>, 資産担保型非居住者債) 	
Resident and Nonresident (Private)	8. Commercial paper	Short-term corporate bonds (See III. C. 2. (a) of this bond market guide)	

m = month, NHK = NHK Corporation (Japanese broadcaster), yr = year.

^a Ministry of Finance Japan. Debt Management Report. http://www.mof.go.jp/english/jgbs/publication/debt_management_report/index.htm

Source: ABMF SF1.

Public offerings of corporate bonds, asset-backed bonds and nonresident bonds (as indicated under Nos. 5, 6, and 7 in Table 12) are subject to disclosure requirements under the FIEA. All other bonds are exempt from FIEA disclosure requirements. For further details on disclosure requirements for such bond and note issuances, kindly refer to Chapter II.F–H.

1. Government Bonds

Government bonds are the securities issued by the central government of Japan. The central government pays the bondholders interests on the securities and repays the principal amount, which is referred to as redemption. Interest is payable on a semiannual basis, except for short-term T-Bill, and the principal amount is redeemed at maturity.

The JGBs currently issued can be classified into four categories:

- (a) medium-term notes (2-year and 5-year bonds);
- (b) long-term bonds (10-year bonds);
- (c) super-long-term bonds (20-year, 30-year, and 40-year bonds); and
- (d) JGBs for retail investors (3-year, 5-year, and 10-year bonds).

During FY2002 (ending on 31 March 2003), the government introduced the Separate Trading of Registered Interest and Principal of Securities (STRIPS) and (variable-rate) retail 10-year JGB programs. The principal and individual interest payment components of JGBs designated by the MOF as book-entry securities eligible to be stripped have been traded as separate zero-coupon government bonds. Subsequently, the government started issuing

- (a) 10-year Consumer Price Index-linked bonds;
- (b) 5-year and 3-year bonds for retail investors; and
- (c) 40-year fixed-rate bonds in FY2003, FY2005, and FY2007.

All medium-, long-, and super-long-term bonds and JGBs for retail investors (with 3-year or 5-year tenures) are bonds with fixed-rate coupons. With fixed-rate coupon-bearing bonds, the interest calculated by the coupon rate determined at the time of issuance is paid on a semiannual basis until the security matures and the principal is redeemed at face value.

JGBs for retail investors (10-year floating rate) are JGBs with coupon rates that vary over time according to certain rules. The 15-year floating-rate bonds, as well as the JGBs for retail investors (10-year) feature coupon rates that vary according to certain rules. New issuance has been put on hold for the 15-year floating-rate bonds, however.

Issuance has also been put on hold for Inflation-Indexed Bonds, which are securities whose principal amounts are linked to the Consumer Price Index as stated above. Thus, although their coupon rates are fixed, the interest payment also fluctuates. The outstanding amount of JGBs has steadily increased in the past 5 years, as shown in Table 13. For reference, the trading volumes of JGBs, by the main categories mentioned above, over an 11-year period (2005–2015) are illustrated in Figure 16 and the underlying numbers are provided in Table 14.

2. T-Bill

Treasury Bills (TBs) and Financial Bills (FBs) have been called and issued as T-Bill with an integrated manner in the market. “T-Bill” is the sum of “Treasury Bills (TBs)” and “Financial Bills (FBs)” with a maturity of 1 year or less and TBs and FBs have been jointly issued since February 2009. T-Bill are all discount notes, meaning that they are issued at a price lower than the face value. No interest payments are made, but at maturity the principal amounts are redeemed at face value.

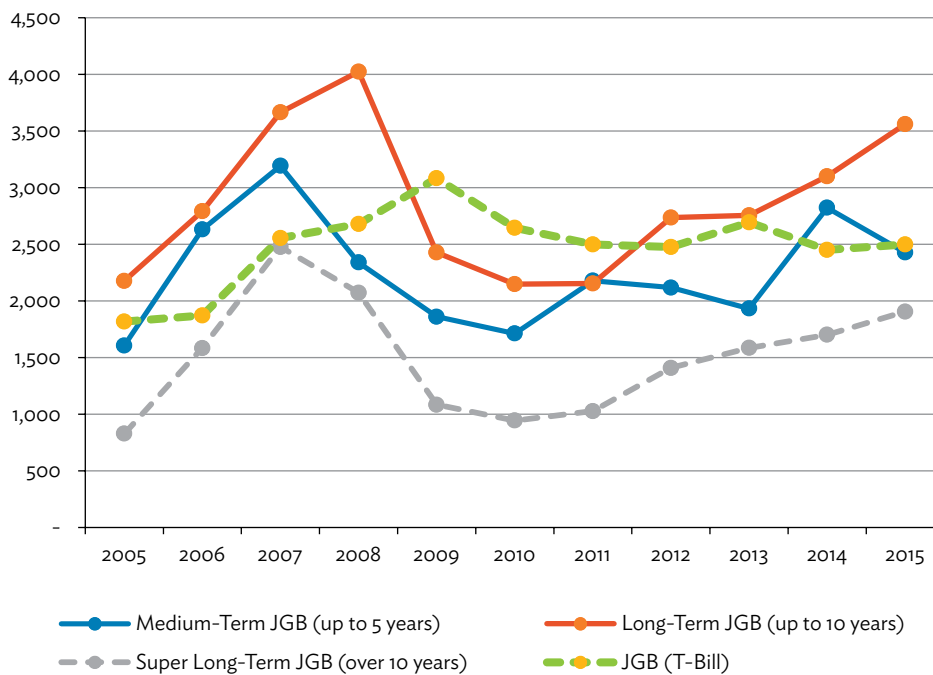
In contrast to JGBs, the outstanding amount of T-Bill over the most recent 5-year period has declined (Table 13).

Table 13: Japanese Government Bonds Outstanding (JPY trillion)

	2011	2012	2013	2014	2015
JGBs	676.9	715.3	760.7	802.7	830.0
JGBs for Retail Investors	23.4	20.3	17.8	14.9	11.2
JGBs (T-Bill)	30.0	30.0	30.0	28.1	25.7
JGBs Total	730.3	765.5	808.5	845.7	866.9
Excluding JGB Holdings by the BOJ	66.6	59.2	52.3	34.4	27.6

BOJ = Bank of Japan, JGB = Japanese Government Bond.
 Note: Data as of end of December for each calendar year.
 Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryotoukei/hakkou/files/hakkougakushoukanngaku.xls>

Figure 16: Trading Volume of Japanese Government Bonds by Category (JPY trillion)



JGB = Japanese Government Bond.
 Note: Data as of end of December for each calendar year.
 Source: Japan Securities Dealers Association (JSDA)—Trading Volume of Over-the-Counter Bonds.
<http://www.jsda.or.jp/shiryotoukei/shurui/files/srb.xls>

Table 14: Trading Volume of Japanese Government Bonds by Category (JPY trillion)

	Medium-Term JGBs (up to 5 years)	Long-Term JGBs (up to 10 years)	Super-Long-Term JGBs (over 10 years)	JGBs (T-Bill) (with a maturity of 1 year or less)	TOTAL
2005	1,606	2,175	829	1,818	6,428
2006	2,631	2,794	1,585	1,872	8,882
2007	3,193	3,666	2,477	2,555	11,890
2008	2,339	4,025	2,073	2,681	11,118
2009	1,860	2,429	1,084	3,084	8,458
2010	1,712	2,150	944	2,647	7,452
2011	2,179	2,155	1,028	2,498	7,860
2012	2,118	2,737	1,408	2,476	8,739
2013	1,934	2,756	1,585	2,694	8,969
2014	2,824	3,101	1,701	2,449	10,075
2015	2,427	3,560	1,907	2,500	10,393

JGB = Japanese Government Bond.

Note: Data as of end of December for each calendar year.

Source: Japan Securities Dealers Association—Trading Volume of Over-the-Counter Bonds. <http://www.jsda.or.jp/shiryotoukei/shurui/files/srb.xls>

3. Local Government Bonds

Local governments and municipalities borrow funds on deeds from banks or issue debt securities in the market. Sometimes, they are called municipal debt. Those issued in the bond market are generally called local government bonds. Of these, securities that are placed with an unspecified number of investors are called publicly offered municipal bonds.

These bonds are issued as a single entity, but some bonds are issued as a joint issue with several local governments. In contrast, those placed privately with local banks and other financial institutions are called privately placed municipal bonds.

Table 15 provides details on local government bonds outstanding over the most recent 5-year period.

Table 15: Local Government Bonds Outstanding by Type (JPY trillion)

	2011	2012	2013	2014	2015
Municipal bonds (publicly offered)	51.0	54.3	56.9	58.1	58.9
Municipal bonds (privately placed)	17.8	16.4	14.9	13.3	12.1
Local Government Bonds Total	68.7	70.7	71.8	71.4	71.0

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

4. Government Agency Bonds

Government agency bonds are debt securities issued by various government-affiliated entities, such as incorporated administrative agencies. Agency bonds are divided into

- (a) government-guaranteed bonds that are backed by the full faith and credit of the government,
- (b) FILP-agency bonds that are issued by fiscal investment and loan agencies that do not enjoy such guarantee, and
- (c) government-affiliated corporation bonds.

The three categories of debt securities mentioned above are sometimes collectively called public sector bonds, and their outstanding values from 2011 to 2015 are presented in Table 16.

Table 16: Government Agency Bonds Outstanding by Type (JPY trillion)

	2011	2012	2013	2014	2015
Government-guaranteed bonds (public offering)	35.1	35.6	36.6	36.5	35.2
FILP-agency bonds (public offering)	28.7	30.5	31.8	32.4	32.9
Government-associated organization bonds (private offering)	7.5	7.2	6.2	4.7	3.9
Bonds issued by the public corporations related to the regional governments (public offering)	0.7	0.8	0.9	0.9	1.0
Bonds issued by the public corporations related to the regional governments (private offering)	0.4	0.4	0.4	0.3	0.3
Government Agency Bonds Total	72.4	74.5	75.9	74.9	73.2

FILP = Fiscal Investment and Loan Program.

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

5. Corporate Bonds

Except for issuances by SMEs via private placement, the issuance of corporate bonds in Japan is still limited to fairly high-rated companies in specific sectors such as electric power and telecommunications, and Japan Rail Group companies. In addition to nonfinancial enterprises, banks and consumer finance companies may also issue corporate bonds in accordance with the Companies Act.

Table 17 illustrates how the value of outstanding corporate bonds has generally remained stable over the last 5 years.

6. Bank Debentures

Over the same period, the outstanding value of bank debentures has steadily decreased, as shown in Table 18. Bank debentures are debt securities issued by certain banking institutions—JA Bank, Shoko Chukin Bank, and Shinkin Central Bank—under special laws and play a fundraising role as an alternative to deposits. They are principally issued as either 5-year interest-bearing or 1-year discounted debentures.

Table 17: Corporate Bonds Outstanding by Type (JPY trillion)

	2011	2012	2013	2014	2015
Corporate bonds (public offering)	62.1	61.2	60.8	59.8	57.9
Corporate bonds (public offering)— general mortgage bonds	0.0	0.0	0.0	15.4	14.3
Corporate bonds (private offering)	8.6	8.6	8.6	8.0	8.7
Corporate bonds (private offering)— general mortgage bonds	0.0	0.0	0.0	1.4	1.4
Total	70.7	69.8	69.4	84.6	82.3

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

Table 18: Bank Debentures Outstanding (JPY trillion)

	2011	2012	2013	2014	2015
Bank debentures—Interest-bearing (public offering)	14.0	13.1	12.2	11.5	11.3

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

7. Nonresident Bonds (Foreign Bonds)

Table 19 indicates that the value of foreign bonds issued in Japan fluctuated little over the period 2011–2015. Foreign bonds are defined as debt securities issued in Japan by non-Japanese resident issuers. Those denominated in Japanese yen, in particular, are separately classified as JPY-denominated foreign bonds or Samurai Bonds.

Nonresident bonds that are profile listed on the TPBM can be included among JPY-denominated foreign bonds, but it is not appropriate to call these Samurai Bonds because Samurai Bond issuers are required to observe full disclosure in Japanese, while an issuer profile listed on the TPBM only need to observe the TSE's disclosure requirements (possibly in English).

Table 19: Nonresident Bonds Outstanding by Type (JPY trillion)

	2011	2012	2013	2014	2015
JPY-denominated foreign bonds— Samurai Bonds (public offering)	9.9	9.6	9.1	9.6	9.4
JPY-denominated foreign bonds— Samurai Bonds (private offering)	1.1	1.5	1.6	1.7	1.7
Asset-backed Samurai Bonds (private offering)	0.1	0.1	0.1	0.0	0.0
Total	11.2	11.2	10.8	11.3	11.1

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

C. Money Market Instruments

Money market instruments are short(er)-term debt instruments issued by either the Japanese government or the private sector. Money market instruments are generally limited to instruments with a maturity of less than 1 year.

Money market instruments are traded in the OTC market, scripless (since dematerialized by default), and settled in either BOJ-Net (T-Bill) or JASDEC (commercial paper).

(1) Issued by the Government of Japan

T-Bill:

T-Bill are the main short-term instrument issued by the MOF in the money market to address short-term funding needs (for more details, see section B.2 in this chapter).

(2) Issued by the Corporate Sector

Commercial paper:

Commercial paper refers to short-term corporate bonds issued on a book-entry basis only. Corporate paper transactions are governed by the Act on Book-Entry Transfer of Bonds, Shares, etc. (Act No.75 of 2001).

The major product attributes of commercial paper include the following:

- (i) Eligible commercial paper issuers are corporates, investment companies, or special purpose companies (SPCs), among others. Foreign corporations, are also eligible to issue commercial paper.
- (ii) So far, commercial paper may only be denominated in Japanese yen.
- (iii) The total amount of the commercial paper issue is underwritten by agreement.
- (iv) Commercial paper is mainly issued through financial institutions (as underwriting or agent financial institution), but direct commercial paper (without the use of an intermediary) issuance is also possible.
- (v) The total amount of each issue cannot be less than JPY100 million, while the value of each individual commercial paper note should be equal to or in excess of JPY100 million and a multiple of JPY1 million.
- (vi) Commercial paper should be issued in Japan and with an original issue discount.
- (vii) The principal maturity term is less than 1 year.
- (viii) The issues may not be secured by collateral.
- (ix) A credit rating is not mandatory but most of commercial paper is rated a-1 or better.
- (x) Although a prospectus is not required to be delivered when soliciting prospective investors, the financial institution (underwriter or agent, and JSDA member) and the issuer shall have to agree to produce a briefing memo regarding the information about the issuer and the conditions of the commercial paper and the financial institution shall have to deliver the briefing memo to a prospective investor upon soliciting the commercial paper.
- (xi) Commercial paper is settled in JASDEC on a delivery-versus-payment (DVP) basis, like other debt securities. In addition, the total issue amount can be subdivided into smaller lots of the value of each commercial paper note (equal to the minimum unit of transfer) in the secondary market.

Commercial paper are issued and sold on a private placement basis, which refers to the action of soliciting the purchase of newly issued securities and does not fall under a public offering of securities. For details on the types of private placements typically used in the Japanese bond market, please refer to section F in the previous chapter.

At the same time, in the event that a commercial paper issuance consists of less than 50 notes and each note is not further divisible, placing such commercial paper is deemed as complying with the necessary transfer restrictions by default, and no reselling restriction contract between financial institution and investor needs to be executed to satisfy such conditions.

As Table 20 indicates, the outstanding value of commercial paper in the Japanese market did not substantially change between 2011 and 2015. In fact, the distribution of the outstanding value by issuer type was also reasonably consistent, as illustrated in the 10-month period in 2015 displayed in Figure 17.

Table 20: Commercial Paper Outstanding (JPY trillion)

	2011	2012	2013	2014	2015
Commercial paper (private placement)	16.5	16.2	15.0	16.4	16.4

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

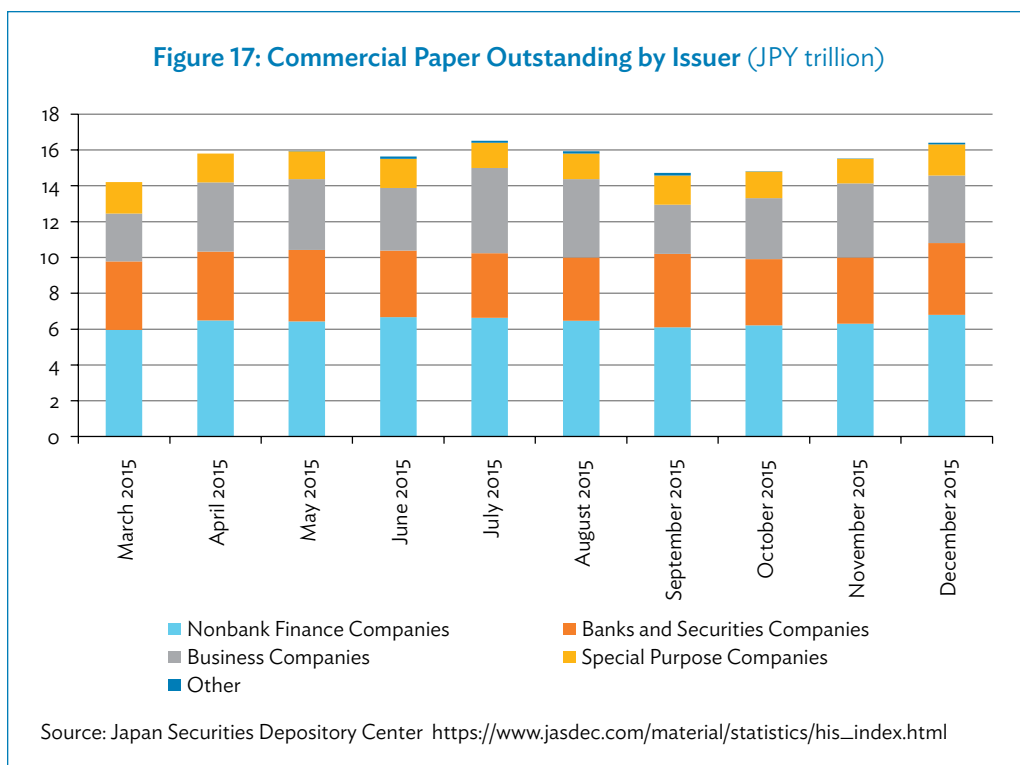


Table 21: Commercial Paper Outstanding by Issuer (JPY trillion)

	Mar 2015	Apr 2015	May 2015	Jun 2015	July 2015	Aug 2015	Sep 2015	Oct 2015	Nov 2015	Dec 2015
Nonbank Finance Companies	6.0	6.5	6.4	6.7	6.6	6.5	6.1	6.2	6.3	6.8
Banks and Securities Companies	3.8	3.8	4.0	3.7	3.6	3.5	4.1	3.7	3.7	4.0
Business Companies	2.7	3.9	4.0	3.5	4.7	4.4	2.7	3.4	4.1	3.8
Special Purpose Companies	1.8	1.6	1.5	1.6	1.4	1.4	1.6	1.5	1.4	1.7
Other	0.0	0.0	0.0	0.1	0.1	0.1	0.2	0.0	0.0	0.1
Total	14.2	15.8	15.9	15.6	16.5	15.9	14.7	14.8	15.5	16.4

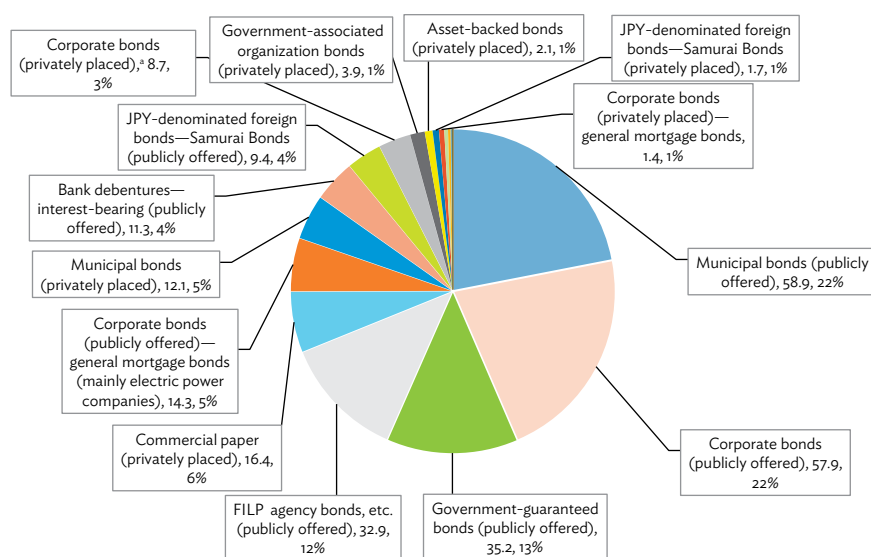
Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

D. Segmentation of the Market (Except for Japanese Government Bonds)

To provide a better illustration of the segmentation of the book-entry debt securities other than JGBs issued in Japan, Figures 18, 19, 20, and 21 and Tables 22, 23, 24, and 25 present a breakdown of the outstanding value and number of issues of each type of debt securities detailed in section B.

All the book-entry debt securities except for JGBs are settled at Japan JASDEC.

Figure 18: Bonds, Notes, and Commercial Paper Outstanding by Type (JPY trillion)



FILP = Fiscal Investment and Loan Program.

^a Most privately placed corporate bonds are considered to be bank-underwritten small and medium-sized enterprise (SME) bonds.

Source: ABMF SF1 based on Japan Securities Depository Center https://www.jasdec.com/en/download/statistics/e_data.pdf

Table 22: Bonds, Notes, and Commercial Paper Outstanding by Type (JPY trillion)

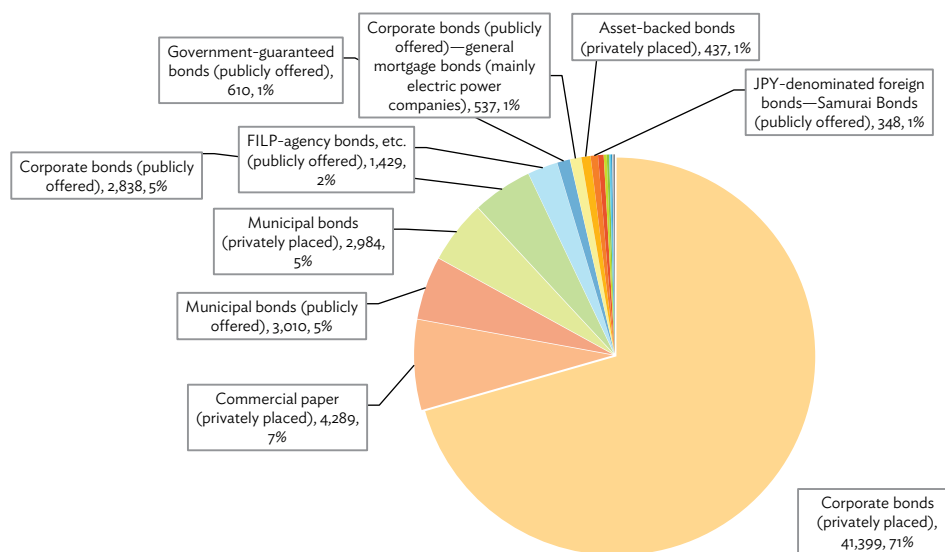
Bond Type	Outstanding (Market Value) at the End of December 2015
Municipal bonds (publicly offered)	58.9
Corporate bonds (publicly offered)	57.9
Government-guaranteed bonds (publicly offered)	35.2
FILP-agency bonds, etc. (publicly offered)	32.9
Commercial paper (privately placed)	16.4
Corporate bonds (publicly offered)—general mortgage bonds (mainly electric power companies)	14.3
Municipal bonds (privately placed)	12.1
Bank debentures—interest-bearing (publicly offered)	11.3
JPY-denominated foreign bonds—Samurai Bonds (publicly offered)	9.4
Corporate bonds (privately placed) ^a	8.7
Government-associated organization bonds (privately placed)	3.9
Asset-backed bonds (privately placed)	2.1
JPY-denominated foreign bonds—Samurai Bonds (privately placed)	1.7
Corporate bonds (privately placed)—general mortgage bonds	1.4
Bonds issued by the public corporations related to the regional governments (publicly offered)	1.0
Asset backed bonds (publicly offered)	0.7
Bonds issued by the public corporations related to the regional governments (privately placed)	0.3
Convertible bonds (publicly offered)	0.3
Asset-backed samurai bonds (privately placed)	0.0
Others (privately placed)	0.0
Others (publicly offered)	0.0
Total outstanding of Bonds, Notes, and Commercial Paper, except for JGBs	268.3
Publicly offered Total	221.7
Privately placed Total	46.6

FILP = Fiscal Investment and Loan Program, JGB = Japanese Government Bond.

^a Most privately placed corporate bonds are considered to be bank-underwritten small and medium-sized enterprise (SME) bonds.

Source: ABMF SF1 based on Japan Securities Depository Center https://www.jasdec.com/en/download/statistics/e_data.pdf

Figure 19: Bonds, Notes, and Commercial Paper Outstanding by Type
(number of issues)



Notes: Data as of end of December 2015. Most privately placed corporate bonds are considered to be bank-underwritten small and medium-sized enterprise (SME) bonds.

Source: ABMF SF1 based on data from Japan Securities Depository Center https://www.jasdec.com/en/download/statistics/e_data.pdf

Table 23: Bonds, Notes, and Commercial Paper Outstanding by Type (number of issues)

Bond Type	Number of Issues Outstanding at the End of December 2015 (number of issues)	Outstanding Account Balances (Market Value) at the End of December 2015 (JPY trillion)	Value per Issue (JPY million)
Corporate bonds (privately placed) ^a	41,399	8.7	211
Commercial paper (privately placed)	4,289	16.4	3,824
Municipal bonds (publicly offered)	3,010	58.9	19,564
Municipal bonds (privately placed)	2,984	12.1	4,046
Corporate bonds (publicly offered)	2,838	57.9	20,397
FILP-agency bonds, etc. (publicly offered)	1,429	32.9	23,025
Government-guaranteed bonds (publicly offered)	610	35.2	57,652
Corporate bonds (publicly offered)—general mortgage bonds (mainly electric power companies)	537	14.3	26,625
Asset-backed bonds (privately placed)	437	2.1	4,764

continued on next page

Table 23 continued

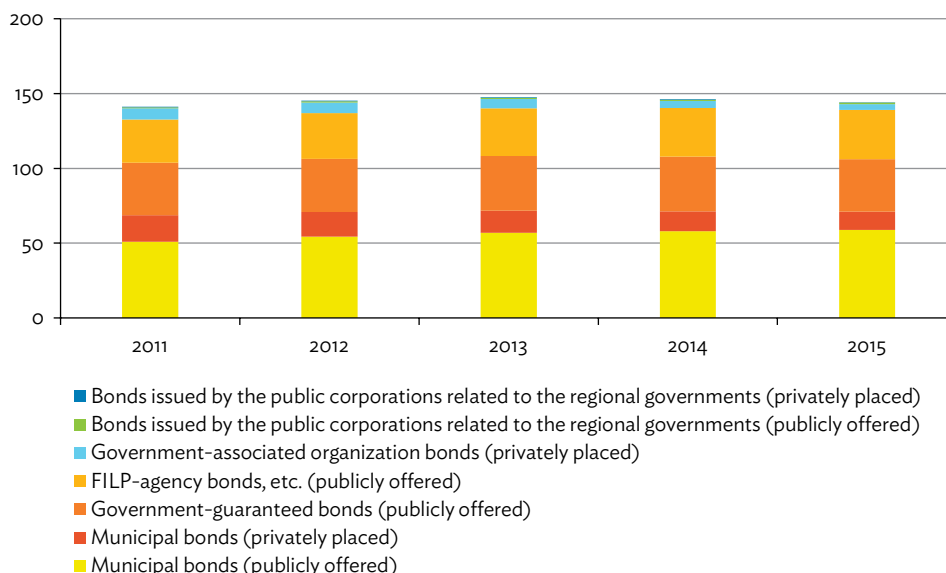
Bond Type	Number of Issues Outstanding at the End of December 2015 (number of issues)	Outstanding Account Balances (Market Value) at the End of December 2015 (JPY trillion)	Value per Issue (JPY million)
JPY-denominated foreign bonds—Samurai Bonds (publicly offered)	348	9.4	27,014
Bank debentures—interest-bearing (publicly offered)	266	11.3	42,365
Government-associated organization bonds (privately placed)	142	3.9	27,482
Corporate bonds (privately placed)—general mortgage bonds	114	1.4	12,103
Bonds issued by the public corporations related to the regional governments (publicly offered)	94	1.0	10,320
Asset-backed bonds (publicly offered)	45	0.7	14,465
JPY-denominated foreign bonds—Samurai Bonds (privately placed)	38	1.7	45,189
Bonds issued by the public corporations related to the regional governments (privately placed)	34	0.3	8,427
Convertible bonds (publicly offered)	29	0.3	9,732
Asset-backed Samurai Bonds (privately placed)	13	0.0	2,347
Others (privately placed)	11	0.0	597
Others (publicly offered)	1	0.0	3,000
Bonds, Notes, and Commercial Paper except for JGBs Total	58,668	268.3	4,574
Publicly offered Total	9,178	221.7	24,158
Privately placed Total	49,490	46.6	942

JGB = Japanese Government Bond.

^a Most privately placed corporate bonds are considered to be bank-underwritten small and medium-sized enterprise (SME) bonds.

Source: ABMF SF1 based on Japan Securities Depository Center https://www.jasdec.com/en/download/statistics/e_data.pdf

Figure 20: Public Sector Bonds Outstanding by Type (JPY trillion)

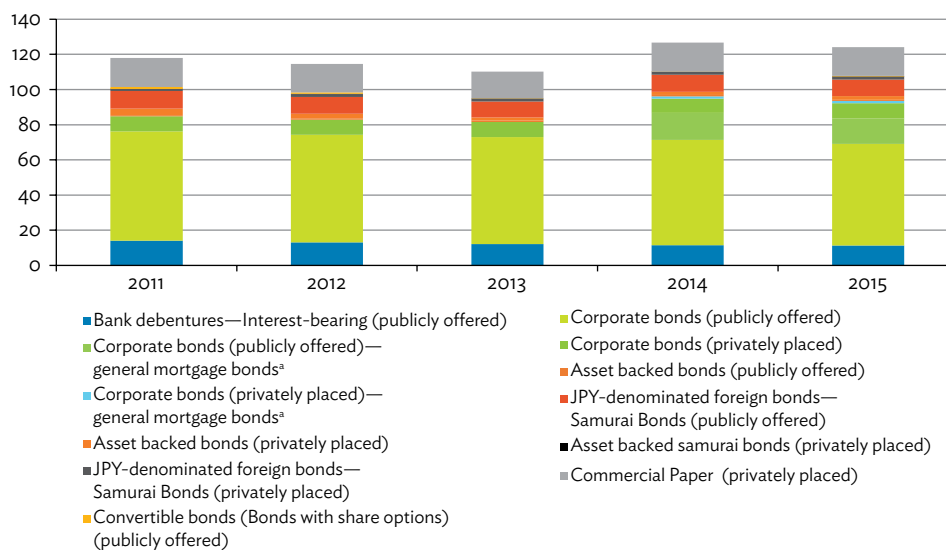


FILP = Fiscal Investment and Loan Program.

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

Figure 21: Corporate Bonds, Notes, and Commercial Paper Outstanding by Type (JPY billion)



^a A breakout of general mortgage bonds within corporate bonds was newly introduced in 2014.

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

Table 24: Public Sector Bonds Outstanding by Type (JPY trillion)

	2011	2012	2013	2014	2015
Municipal bonds (publicly offered)	51.0	54.3	56.9	58.1	58.9
Municipal bonds (privately placed)	17.8	16.4	14.9	13.3	12.1
Government-guaranteed bonds (publicly offered)	35.1	35.6	36.6	36.5	35.2
FILP-agency bonds, etc (publicly offered)	28.7	30.5	31.8	32.4	32.9
Government-associated organization bonds (privately placed)	7.5	7.2	6.2	4.7	3.9
Bonds issued by the public corporations related to the regional governments (publicly offered)	0.7	0.8	0.9	0.9	1.0
Bonds issued by the public corporations related to the regional governments (privately placed)	0.4	0.4	0.4	0.3	0.3
Public Sector Bonds Total	141.2	145.2	147.7	146.3	144.2
Publicly offered Total	115.5	121.2	126.1	128.0	127.9
Privately placed Total	25.7	24.0	21.5	18.3	16.3

FILP = Fiscal Investment and Loan Program.

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

Table 25: Corporate Bonds, Notes, Commercial Paper Outstanding by Type (JPY trillion)

	2011	2012	2013	2014	2015
Bank debentures—Interest-bearing (publicly offered)	14.0	13.1	12.2	11.5	11.3
Corporate bonds (publicly offered)	62.1	61.2	60.8	59.8	57.9
Corporate bonds (publicly offered)—general mortgage bonds ^a	0.0	0.0	0.0	15.4	14.3
Corporate bonds (privately placed)	8.6	8.6	8.6	8.0	8.7
Corporate bonds (privately placed)—general mortgage bonds ^a	0.0	0.0	0.0	1.4	1.4
Asset-backed bonds (publicly offered)	0.7	0.8	0.8	0.8	0.7
Asset-backed bonds (privately placed)	3.7	2.6	1.8	1.9	2.1
JPY-denominated foreign bonds—Samurai Bonds (publicly offered)	9.9	9.6	9.1	9.6	9.4
JPY-denominated foreign bonds—Samurai Bonds (privately placed)	1.1	1.5	1.6	1.7	1.7
Asset-backed Samurai Bonds (privately placed)	0.1	0.1	0.1	0.0	0.0
Convertible bonds (bonds with share options) (publicly offered)	1.1	0.9	0.2	0.2	0.3
Commercial paper (privately placed)	16.5	16.2	15.0	16.4	16.4
Book-Entry Corporate Bonds, Notes, and Commercial Paper Total	118.0	114.6	110.2	126.7	124.1
Publicly offered Total	87.9	85.5	83.1	97.2	93.8
Privately placed Total	30.1	29.1	27.1	29.5	30.4

^a A breakout of general mortgage bonds within corporate bonds was newly introduced in 2014.

Note: Data as of end of December for each calendar year.

Source: Japan Securities Depository Center https://www.jasdec.com/material/statistics/his_index.html

The outstanding bond totals included in Table 13 (JGBs), Table 24 (Public Sector Bonds), and Table 25 (Corporate Bonds, Notes, and Commercial Paper) collectively represent the entire bond market in Japan.

More information on outstanding book-entry bond and note issues and other statistics on the Japanese bond market other than JGBs can be found on the website of JASDEC.²² In addition, *AsianBondsOnline* is a bond information portal operated by ADB under an ASEAN+3 initiative. Detailed information on Japanese public debt is also available on the BOJ website.²³

E. Methods of Issuing Bonds (Primary Market)

1. Government Bonds

JGBs and other government debt securities are mainly either underwritten by Primary Dealers (also referred to as Special Participants, see 1.b below) and resold to the public market, or issued as direct subscription by BOJ and other government-affiliated parties. The major volume of JGB issuance and distribution is sustained by Primary Dealers, while BOJ underwriting is seen as an assurance of a given balance of supply and demand in the JGB market.

a. Methods of Japanese Government Bond Issuance

Methods of JGB issuance are broadly categorized as either issuance to the market, issuance to retail investors, or issuance to the public sector. Table 26 provides an overview of the various methods of JGB issuance and a detailed explanation of each method.

Table 26: Methods of Japanese Government Bond Issuance

Methods of JGB Issuance	Explanation
A. Offering to the Market	JGBs are principally issued in public offering on market-based terms of issuance.
a. Price- and yield-competitive auction	<p>Price- and yield-competitive auction is a method in which each auction participant submits a bidding price (or yield) and bidding amount in response to the issue terms (e.g., issue amount, maturity, coupon rate) presented by the MOF. The issue price and amount will then be determined based on the bids.</p> <p>In this type of auction, the issuing authority starts selling first to the highest price bidder in descending order (or to the lowest yield bidder in ascending order) until the cumulative total reaches the planned issue amount. In Japan, the auction method varies by type of security. One is the conventional method by which each winning bidder purchases the security at his bidding price. The other is the Dutch-style method by which all winning bidders pay the same lowest price of their biddings regardless of their original bid.*</p> <p>* Except for Inflation-Indexed Bonds and 40-year bonds offered via Dutch-style yield-competitive auction, all the JGBs are offered via the conventional price competitive auction.</p>

continued on next page

²² JASDEC. https://www.jasdec.com/en/download/statistics/e_data.pdf (English, PDF only); https://www.jasdec.com/material/statistics/his_index.html (Japanese, EXCEL, and PDF)

²³ BOJ. <http://www.boj.or.jp/statistics/sj/>

Table 26 continued

Methods of JGB Issuance	Explanation
b. Noncompetitive auction	<p>Besides competitive auction, 2-year, 5-year, and 10-year bonds are also issued through noncompetitive auction. This approach is to take into account small and medium-sized market participants who tend to submit a smaller bid than their larger counterparts. Biddings for noncompetitive auction are offered at the same time as for the price-competitive auction, and the price offered equals the weighted average accepted price of the price competitive auction. One can bid for either the price-competitive auction or for the nonprice competitive auction. The maximum issuance amount is 10% of the planned issuance amount. Each participant is permitted to bid up to JPY1 billion.*</p> <p>* The Shinkin Central Bank, Shinkumi Federation Bank, Rokinren Bank, and Norinchukin Bank are excluded.</p>
c. Nonprice competitive auctions I and II	<p>Nonprice Competitive Auction I is an auction in which biddings are offered at the same time as for the price-competitive auction. The maximum issuance amount is set at 10% of the total planned issuance amount and the price offered is equal to the weighted average accepted price of the price competitive auction. Only the JGB Market Special Participants are eligible to bid in this auction. Each participant is allowed to bid up to the amount set based on the result of its successful bids during the preceding two quarters.</p> <p>Nonprice Competitive Auction II is an auction carried out after the competitive auction is finished. The price offered is equal to the weighted average accepted price in the price-competitive auction or lowest accepted price in Dutch-style yield-competitive auction. Only the JGB Market Special Participants are eligible to bid in this auction. Each participant is allowed to bid up to the amount set based on the result of its bids during the preceding two quarters.*</p> <p>* Each participant is allowed to bid up to 15% of one's total successful biddings in the competitive auction and Nonprice Competitive Auction I.</p>
B. Methods for Selling JGBs to Retail Investors	
a. JGBs for retail investors	<p>In March 2003, issuance of a 10-year floating-rate bond for retail investors was launched in order to promote JGB ownership among individuals. Moreover, in order to respond to retail investors' various needs and to promote further sales, the government has been improving bond features by introducing 5-year fixed-rate and 3-year fixed-rate JGBs.</p> <p>Issuance of JGBs for retail investors rests on their handling and distribution by their handling institutions comprising security companies, banks, and other financial institutions as well as post offices (about 1,090 institutions). The handling institutions are commissioned by the government to accept purchase applications and to sell JGBs to retail investors. Handling institutions are paid a commission by the government corresponding to the handled issuance amounts.</p> <p>From January 2012 to June 2013, all JGBs for retail investors were issued as Reconstruction Bonds. In addition, Reconstruction Supporters' Bonds for Retail Investors were issued a total of four times (April, July, and October 2012; and January 2013).</p>

continued on next page

Table 26 continued

Methods of JGB Issuance	Explanation
b. New OTC sales system for selling marketable JGBs	<p>In addition to JGBs for retail investors, in October 2007 a new OTC sales system for marketable JGBs was introduced in order to increase retail investor purchase opportunities with regard to JGBs (2-year, 5-year, and 10-year marketable bonds).</p> <p>With regard to this new OTC sales system, it allows private financial institutions to engage in subscription-based OTC sales of JGBs in a manner previously exclusive to post offices. This development allows retail investors to purchase JGBs via financial institutions with whom they are familiar, it also allows them to purchase JGBs in a manner that is essentially ongoing.</p> <p>As with JGBs for retail investors, for the new OTC sales system, the MOF has commissioned financial institutions (about 750 institutions) to conduct subscriptions and sales of JGBs. Note that while these financial institutions are required to subscribe and sell JGBs at prices defined by the MOF within a defined period, they are not required to purchase any unsold JGBs.</p>
C. Offering to the Public Sector (Bank of Japan Switch)	<p>While Article 5 of the Public Finance Act prohibits the BOJ from underwriting government bonds, a proviso to the article allows the BOJ to extend credit to the government, up to an amount authorized by the Diet, in exceptional cases. In practice, such cases are limited to underwriting of Refunding Bonds within the amount of JGBs that are held by the BOJ and have reached maturity (often referred to as a “Bank of Japan Switch”).</p> <p>Through its market operations, the BOJ holds a large amount of government bonds. If the BOJ tried to have its JGB holdings redeemed in cash, the MOF would be required to issue Refunding Bonds in the market to raise the fund needed for redemption. A massive issuance of Refunding Bonds in the market, however, could invite a fund shortage in the private sector, thus obliging the BOJ to provide the private sector with funds by purchasing a substantial amount of the Refunding Bonds from private sector. To avoid such roundabout, the BOJ is exceptionally allowed to underwrite only up to the amount necessary to roll over its maturing bonds.</p>

BOJ = Bank of Japan, JGB = Japanese Government Bond, MOF = Ministry of Finance Japan, OTC = over-the-counter.

Source: Ministry of Finance Japan website with adjustments from ABMF SF1. https://www.mof.go.jp/english/jgbs/publication/debt_management_report/2014/saimu2-1-1.pdf

b. Japanese Government Bonds Market Special Participants Scheme

Amid expectations that JGB issuance in large volumes would continue, the JGB Market Special Participants Scheme was introduced in October 2004. This scheme was designed based on the Primary Dealer System generally maintained in major European countries and the US to facilitate secure and stable issuance, and to maintain and enhance the liquidity of government bond markets.²⁴

Under the scheme, the MOF grants special entitlements to certain auction participants when they carry out responsibilities essential to debt management policies, such as active participation in JGB auctions. The MOF expects the scheme to facilitate secure and stable

²⁴ For reference, please also see https://www.mof.go.jp/english/jgbs/debt_management/pd/index.html

issuance of JGBs and to maintain and enhance the liquidity of the JGB market. The following is an outline of the scheme.

(i) Responsibilities of Special Participants

- Bidding responsibility

In every auction, the Special Participants shall bid for an adequate amount (at least 3% of the planned issuance amount) at reasonable prices.

- Purchasing responsibility

The Special Participants shall purchase and underwrite at least a specified share of the planned total issuance amount (0.5% for the short-term zone; and 1% for other zones) in each of the super-long-term, long-term, medium-term, and short-term zones in auctions for the preceding 2 quarters.

- Responsibility in the secondary market

The Special Participants shall provide sufficient liquidity to the JGB secondary market.

- Information sharing

The Special Participants shall provide information on JGB markets and related transactions to the MOF.

(ii) Entitlements of Special Participants

- Meeting of JGB Market Special Participants

Through this meeting, Special Participants can exchange opinions with the MOF on JGB management policies. For general information, minutes of these meetings and other information are available in English on the MOF website.²⁵

- Participation in Auctions for Buybacks

The Special Participants can take part in Auctions for Buybacks.

- Separation and integration of STRIPS Bonds

The Special Participants can apply for the separation and integration of STRIPS Bonds.

- Participation in Nonprice Competitive Auctions I and II

The Special Participants can take part in Nonprice Competitive Auction I (held concurrently with normal competitive auctions) and Nonprice Competitive Auction II (held after normal competitive auctions). These auctions enable Special Participants to obtain bonds at the weighted average accepted price at a competitive price auction, up to a purchasing limit preset for each Special Participant on the basis of past successful bids (Nonprice Competitive Auction I) and past subscriptions (Nonprice Competitive Auction II).

- Participation in Auctions for Enhanced Liquidity

The Special Participants can take part in Auctions for Enhanced Liquidity that are designed to maintain and improve liquidity of the JGB market.

²⁵ See http://www.mof.go.jp/english/about_mof/councils/jgbsp/index.html

- Preferential Participation in Interest Rate Swap Transactions
The Special Participants can be preferential counterparties for the interest rate swap transactions implemented by the MOF.

c. *Current Japanese Government Bonds Issuing Market Situation*

The MOF defines and publishes a number of governing policies for the issuance of Japanese government bonds for each fiscal year. Highlights of the government's Debt Management Policy FY2015 (1 April 2015–31 March 2016) and FY2016 (1 April 2016–31 March 2017) are reproduced below. The latest policies may be found on the MOF website.

Issuance Size

Highlights of FY2015 Debt Management Policy.²⁶ The total estimated issuance amount in the initial FY2015 JGB Issuance Plan declined to JPY170.0 trillion from JPY181.5 trillion in the initial FY2014 JGB Issuance Plan, mainly because of the decrease in the volume of newly issued National Government Bonds (Construction Bonds and Special Deficit-Financing Bonds) and Refunding Bonds.

The calendar-year-based initial issuance plan in January–December 2015 was also set to decline to JPY152.6 trillion from JPY155.1 trillion in the initial issuance plan in January–December 2014.

Highlights of FY2016 Debt Management Policy.²⁷ The total estimated issuance amount in the initial FY2016 JGB Issuance Plan declined to JPY154.4 trillion from JPY162.2 trillion in the initial FY2015 JGB Issuance Plan, mainly because of the decrease in the volume of newly-issued bonds (Construction Bonds and Special Deficit-Financing Bonds), Reconstruction Bonds, and Refunding Bonds.

The calendar-year-based initial issuance plan in January–December 2016 was set to decline to JPY147.0 trillion from JPY152.6 trillion.

Extending the Average Maturity

In order to lower refinance risk and medium- to long-term financing costs, the average maturity of issuances in FY2015 was extended by between 6 months and 9 years. Reflecting the desire of market participants, the extension was achieved with a well-balanced mixture of maturity terms from short to super-long. Meanwhile, the average maturity of outstanding JGBs is estimated to have increased by 5 months to 8 years and 5 months at the end of FY2015.

Enhancing the Market Liquidity

The amount of Auctions for Enhanced Liquidity is to increase to JPY800 billion per month from JPY700 billion per month, or an additional JPY1.2 trillion per year, in order to maintain and enhance the liquidity of the JGB secondary market.

²⁶ Ministry of Finance Japan. Debt Management Plan FY2015. http://www.mof.go.jp/english/jgbs/debt_management/plan/e20150114overview.pdf

²⁷ Ministry of Finance Japan. Debt Management Plan FY2016. https://www.mof.go.jp/english/jgbs/debt_management/plan/e20151224overview.pdf

In order to ensure stable issuance of JGBs, the maximum amount of bidding by each auction participant will be decreased to one-half of the planned issuance amount from the full amount, while the responsibility to bid of Market Special Participants will be raised to 4% or more of the planned issuance amount from 3% or more.

Encouraging the Inflation-Indexed Bonds Market

In view of the changing market conditions after moving away from a period of deflation, and in order to diversify the product designs of JGBs, the issuance of Inflation-Indexed Bonds increased to JPY500 billion from JPY400 billion per auction for a total increase of JPY0.4 trillion per year. The volume of the issuance will be flexible, in response to the needs of a variety of entities and market conditions.

Sales of Inflation-Indexed Bonds to retail investors by a new OTC sales system is planned to launch in the second half of FY2016.

2. Local Government Bonds

Local government bonds include prefecture bonds and municipality (city, town, and village) bonds. Under local finance law, the concept of local government bonds excludes financing of less than 1 year, and includes not only bonds but also loans. To avoid complication, loans are hereafter excluded from the definition of local government bonds.

The Local Autonomy Law authorizes Japanese local governments—prefectures, municipalities, Tokyo's special wards, and local government cooperatives—to borrow money provided that the following conditions are fulfilled:

- A local public body must prepare a budget plan that defines the use of proceeds from the proposed bond issue and obtain the approval of the local assembly.
- The actual issuance for a prefecture and a designated city is also subject to consultation with the Minister of Internal Affairs and Communications, and issuance for an ordinary city, town, or village is subject to consultation with the governor of the prefecture concerned (local bond consultation system).
- Use of proceeds is confined to what local finance law determines.

Issuance of Local Government Bonds

A total of 32 prefectures and 20 designated cities have issued local government bonds through public offerings. Local government bond issuance terms are determined based on negotiations between the issuer and the underwriting syndicate. They take into account a broad range of factors, including trading conditions, spreads over JGBs, and trends in the overall bond market.

There are also joint local government bonds which are issued in the form of public offerings each month by 35 local governments under joint and several guarantees. A single participant may be claimed upon to repay the whole amount of an issue despite it originally only shares in the proceeds.

3. Government Agency Bonds

(a) Government-Guaranteed Bonds

The issuance of government-guaranteed bonds is part of the Fiscal Investment and Loan Program (FILP), and annual ceilings on the issue amount must be approved by the Diet. All government-guaranteed bonds are issued in the form of interest-bearing debt securities with maturities of 2–30 years. Government-guaranteed bonds are issued by way of either (i) negotiated underwriting by a so-called national syndicate, or (ii) Dutch auction. In the former method, the terms of issue are determined based on the average of premarketing results of all national syndicate members; in the latter, the terms are set through competitive bidding.

(b) Fiscal Investment and Loan Program-Agency Bonds

FILP-agency bonds are also issued as interest-bearing bonds with maturities ranging from 5 years to 10 years. In issuing them, the issuing agency usually selects a lead manager, which, in turn, forms an underwriting syndicate.²⁸

4. Corporate Bonds

The issuance of corporate bonds had long been subject to strict regulation. However, the Commercial Code was amended in 1993 to drastically change the system and the regulations on the issuance of corporate bonds were substantially eased. In 1996, almost all of the regulations related to the issuance of corporate bonds were abolished.

A bond or note offering in the private sector may be done through either a public offering or as a private placement:

(a) Public Offering

Bonds and notes issued through a public offering can be bought and sold by any investor.

In the case of a public offering of corporate bonds, the issuing corporation (the issuer) first appoints a lead manager and other underwriters that together constitute an underwriting syndicate, a commissioned company for bondholders (please see Chapter III.M for more details) or a fiscal agent, and providers of other relevant services, such as JASDEC acting as a central securities depository (CSD), issuing agent, and paying agent. In turn, the underwriting syndicate applies for a credit rating.

Under normal circumstances, the lead manager(s) go ahead with price discovery followed by a book-building process involving all syndicate members.

The issue terms of the bonds are finalized first thing in the morning on the pricing date based on the book that had been closed prior to the pricing. Then, the subscription starts immediately after final terms and conditions are electronically filed with the Local Finance Bureau. Subsequently, the payment for the bonds is made, and the issuance of the corporate bonds is completed.

²⁸ Japan Securities Research Institute. 2014. *Securities Market in Japan 2014*. Tokyo. pp.79–82. http://www.jsri.or.jp/publish/english/english_07.html

As for price talk and pricing, more recently, an increasing number of issuers employ a method known as spread pricing under which the investors' demand is measured in terms of a spread over JGB yield or the LIBOR rate. Top-tier issuers are priced based upon JGB yield.

Since 2000, a new practice known as Internet-based bond issue, which is a series of new issue procedures covering price discovery, book building, and pricing carried out through the Internet—has become more prevalent.

Discounted bank debentures were issued by banking institutions, such as Aozora Bank, that once belonged to the long-term credit banking sector.²⁹ These banks would commission securities companies to sell bank debentures on their behalf. Meanwhile, interest-bearing bank debentures were issued in two ways: (i) issuing debentures through a public offering on a fixed day, or (ii) selling them during a certain selling period of time.³⁰

(b) *Private Placement*

As previously mentioned, the term private placement of securities means a solicitation for acquisition of newly issued securities that does not come within the purview of a Public Offering of Securities in the FIEA. The seller (offeror) is obliged to make notice to the acquirer of the securities that (i) it is an issue by private placement, (ii) the securities have not been notified to the authority (an SRS or SR has not been filed), and (iii) comes with transfer restrictions. The acquirer is required to acknowledge such notice.

The FIEA prescribes three categories of private placements. Any offering of newly issued securities other than these three categories falls under the purview of a public offering. The legal framework for private placements is described in detail in Chapter II.F.

(i) Qualified Institutional Investor-Private Placement (QII-PP or Offer to PI) (適格機関投資家私募)

The QII-PP is an offer for acquisition of debt securities to be made exclusively to QIIs, which include securities companies, investment management companies, investment corporations, foreign investment corporations, banks, insurance companies, certain pension funds, and general partners of certain partnerships.

No continuous disclosure is offered for these debt securities and they are not to be offered to Professional Investors.

Any transfer of the securities is prohibited unless the transferee is a QII; such a transfer restriction is either written on the certificates of the securities to be

²⁹ Formerly, the Japanese private banking system was divided into (i) Deposit-Taking Banks (commercial banks), which were not allowed to issue bank debentures because they were limited to short-term lending only; and (ii) Bank Debenture Issuing Banks (long-term credit banks), which were not allowed to take deposits because they were limited to long-term lending only. Following market deregulation and the removal of distinctions between these two banking categories, the bank debenture issuing limitations remained.

³⁰ Japan Securities Research Institute. 2014. *Securities Market in Japan 2014*. Tokyo. pp. 82–85. http://www.jsri.or.jp/publish/english/english_07.html

delivered, written on the offering document, or disclosed through the book-entry system of JASDEC.

In addition, the seller (offeror) of the securities must deliver a document that states that no SRS has been filed for the QII-PP and describes the contents of said transfer restriction.

In the event that the issuer of the securities under a QII-PP is a foreign entity, the issuer is required to appoint an issuer's agent who is a resident of Japan, according to Article 1-3 of the Cabinet Office Ordinance on Disclosure of the Contents of Foreign Bond Issuers (外国債等の発行者の内容等の開示に関する内閣府令). This ordinance is applicable just for the QII-PP, and not the TPBM.

(ii) Private Placement for Professional Investors (PP for PI, or Offer to PI) or Specified Solicitation for Acquisition (特定投資家私募 又は 特定投資家向け取得勧誘):

Available since 2008, the PP for PI, and also the corresponding Private Secondary Distribution (PSD to PI) in the secondary market, has been made distinct from the definitions of public offering and secondary distribution, respectively.

The PP for PI is for Professional Investors (投資勧誘の対象は特定投資家に限定) only. Professional Investors are defined in the FIEA, with detailed information available in section N in this chapter.

Solicitations are made by Financial Instruments Business Operators (e.g., securities companies); in principle, they cannot make any offer to a person other than a Professional Investor (発行と転売は原則証券会社経由).

In addition, the seller (offeror) of the securities must deliver a document that states that no SRS has been filed for the PP for PI and describes the contents of said transfer restriction. The offerors are obliged to make notification to the acquirer of the securities that (i) it is an issue by private placement, (ii) the securities have not been notified to the authority (an SRS or SR has not been filed), and (iii) point out the enclosed selling and transfer restrictions (特定投資家への告知義務).

The issuer of the securities is required to provide a concise SSI, such as issuer's web address where Professional Investors can obtain the issuer's corporate and financial information. The issuer, of course, is not prohibited to make full disclosure in the SSI. The issuer may also choose disclosure through documents incorporated by reference or through documents not incorporated by reference but for information purposes only. The distinction is that, typically, documents incorporated by reference may need to be given an endorsement by a third party, while documents not incorporated by reference but for information purposes only will typically not require such an endorsement (簡潔な特定証券情報の提供による発行体の開示負担軽減).

The economic nature of the Offer to PI can be similar to a public offering because the concept of Professional Investors is much broader than QII and the number of offerees is not limited under the Offer to PI.

A bond or note offered through a private placement is negotiated and traded in the OTC market. For more details on the trading of bonds and notes, please refer to Chapter IV.

Private placement debt securities may be listed for profiling on the TPBM (see section H in this chapter for more information).

(c) Reverse Inquiry

Bank debentures have also been issued as a response to an issue-as-reverse inquiry, typically twice a month, and based on demand. In a reverse inquiry, investors with an appetite for specific debt securities would approach a potential issuer about issuing debt securities within their expectations. The actual issuance process is similar to private placement.

Corporate bonds are held at and settled by JASDEC, which prescribes a number of practices prior to the actual issuance of corporate bonds through its book-entry system. Issuers are required to provide prior consent on the handling of their corporate bonds at JASDEC, and make use of Issuing Agents and Paying Agents, the name of which should be advised to JASDEC in advance.

Upon receipt of an application from a financial institution for the depository of a to-be-issued bond or note, JASDEC shall designate such an institution as an Issuing Agent, pursuant to the provisions of JASDEC Business Regulations. Issuing Agents shall undertake to follow the procedure for the issue of corporate bonds required by JASDEC, on behalf of the issuers.

Upon receipt of an application from a financial institution for this service, JASDEC shall designate such an institution as a Paying Agent, pursuant to the provisions of JASDEC Business Regulations. Paying Agents shall undertake to follow the procedure between JASDEC and the Issuer, after the day of the issue to the day of redemption of the relevant corporate bonds, on behalf of the issuers.

F. Governing Law and Jurisdiction (Bonds and Notes Issuance)

The choice of governing law and the jurisdiction for specific service provisions in relation to bonds and notes issuance or contractual preferences of stakeholders may affect the accessibility to a specific investor universe that may otherwise not be accessible if the bonds or notes were issued under the laws of the place of issuance or the issuer's domicile.

1. Public Offers

When issuing a bond or note to the public in Japan, the choice of governing law and jurisdiction is limited to the laws of Japan and Japanese courts, respectively.

2. When Listing on the TOKYO PRO-BOND Market

Governing law and jurisdiction, with respect to the Terms and Conditions of the Notes, may be agreed among the contract parties, subject to relevant provisions in applicable laws and regulations.

In particular, provisions for the TPBM may be determined with elements of intraregional bond markets or practices, as well as general international capital market agreements.

3. Samurai Bonds issued by Nonresidents

For instance, in the case of nonresident-issued Samurai Bonds, the considerations for investor protection in the domestic Japanese market as the place of issuance and sale dictate Japanese law as the governing law, and jurisdiction rests with Japanese courts. From this point of view, for bonds and notes settled in Japan (Japanese domestic bonds), JASDEC requires that the Terms and Conditions of the Notes be governed by Japanese law.

4. Choice of Jurisdiction and the Use of Arbitration

Under Japanese law, it is possible to choose the governing law of the contract by agreement of the parties. In addition, it is also possible for contracting parties to agree on the choice of jurisdiction.

In Japan, the judge may often recommend a settlement on a lawsuit in the middle of a trial. If the settlement of the litigation has been established, this has the same effect as a final and binding judgment.

Japan is a member of the New York Convention.³¹ It is possible to enforce the result of an arbitral award in Japan in other member states. Also, it is basically possible to enforce in Japan an arbitral award made in other member countries.

However, litigation and jurisdiction systems are quite different in each country and their stages of market developmental may differ. If the place of issuance of the bonds or notes is a foreign country and the investors are foreign residents, the arbitration procedure is often used as dispute resolution mechanism as an alternative to bringing the matter to court.

The availability of domestic arbitration systems and those available internationally is an important future research topic for ABMF SF1.

G. Language of Documentation and Disclosure Items

The language of documentation for bond and note issuance, as well as the related initial and continuous disclosure items, is a significant factor of consideration for issuers. While English is the preferred language for most issuers, simply because it allows the issuers to re-use documentation already issued in international markets. However, each domestic bond market in ASEAN+3 may require the submission of approval-related information in their prescribed format and in the local language, particularly in the case of offers to the general public or retail investors.

ABMF is working toward concessions from the relevant regulatory authorities for the submission of required information in English in addition to the local language and formats. This specifically applies to cases of offers to Professional Investors only.

³¹ United Nations. 1958. Convention on the Recognition and Enforcement of Foreign Arbitral Award. New York.

1. Public Offers

If bonds or notes are intended to be offered to the public in Japan, issuers or their agents are required to produce the relevant documentation and disclosure items in Japanese.

At the same time, the possibility exists for the issuer or their agents to produce documentation in English, for example, in the form of a summary of the disclosure information. English documentation and disclosure items may also be submitted via EDINET, the filing system for SRS for public offerings of bonds and notes. Users are able to inquire on English documents in the system, as they are marked as such.

2. Private Placements

In the case of a private placement of bonds or notes in Japan, issuers or their agents may provide documentation in Japanese or English, or a combination of both languages. The key driver for the language of documentation is likely to be the targeted investor universe for the private placement.

3. When Listing on the TOKYO PRO-BOND Market

Documentation and disclosure items in English are accepted by the TPBM. Efforts have been made to reduce the cost for preparing additional documentation at the TPBM.

H. Listing on the TOKYO PRO-BOND Market

A listing of debt securities may occur for the purpose of trading (similar to equities) or for the purpose of profile or reference listing.

In Japan, the listing of a bond or note is not a regulatory requirement stipulated by either the FSA or MOF, and not a specific requirement in the case of foreign issuers.

However, should an issuer wish to list a bond or note for profiling in Japan, the issuer may take advantage of the offering on the TPBM.³² The TPBM is the only profile listing place in Japan. For detailed information regarding the purpose and establishment of the TPBM, please refer to Chapter II.H.

Issuers need to list a note issuance program, such as a medium-term note (MTN) program, or bonds or notes on the TPBM in order to issue bonds and notes through the TPBM system to Professional Investors.

Japan features one of the most comprehensive definitions of Professional Investors in ASEAN+3, which includes institutional and high net worth investors with specific qualifying criteria, and also foreign institutional investors. Only Professional Investors and nonresident (foreign) investors are able to participate in TPBM. Please refer to Chapter III.K for more information on the framework of Professional Investors in Japan.

³² For more detail, please refer to <http://www.jpx.co.jp/english/equities/products/tpbm/outline/index.html>

1. Profile Listing Process and Practices

In contrast to public offerings, to issue bonds for the purpose of listing on the TPBM, there is no need to submit any documents to the Kanto Local Finance Bureau or the FSA. Instead, the relevant documents—including information on listed bonds or notes and information on their issuers—shall only be submitted to the TSE, pursuant to the TSE Listing Regulations and Enforcement Rules for TPBM. For further information on these regulations, please refer to Table A3.4 in Appendix 3.

(a) Initial Listing Application

- (i) The listing of bonds and notes on the TPBM is carried out through an application by the issuer. The issuer may decide to retain a nominated advisor (arranger) for the TPBM.
- (ii) The initial listing applicant is required to submit an initial listing application and initial listing application documents to the TSE for listing.
 - (1) The initial listing applicant may consult or make inquiries with the TSE prior to listing regarding the initial listing application.
 - (2) The initial listing applicant shall state in the initial listing application documents that there are no false statements in the documents.
- (iii) The initial listing applicant is required to submit the SSI and other forms to the TSE, as may be stipulated.³³ The TSE typically also accepts an information memorandum or offering circular prepared for the relevant bonds and notes, together with additional documents as may be necessary. The Single Submission Form (SSF) for bonds and notes issued under the ASEAN+3 Multi-Currency Bond Issuance Framework (AMBIF) is accepted as a TSE-approved form.
 - (1) The SSI is required to be prepared based on the format stipulated by the exchange or other formats approved by the exchange as an appropriate form. For example, the disclosure formats utilized in the Eurobond market may be approved to be used. The SSF, which includes the contents of the SSI, can be used for the issuance of AMBIF bonds and notes. The SSF can be treated as the SSI by mentioning clearly on the SSF that it is an SSI. Then, the SSF can be applied to the listing process on the TPBM. The language of disclosure in the SSI can be either Japanese or English, or both. Foreign issuers do not have to translate their English documents into Japanese.
 - (2) Under a note issuance program, parties seeking to apply for a bond listing can register the maximum aggregate amount of bonds and notes issued in a program by publishing the Program Information pursuant to the rules established the exchange. Specifically, information on the maximum limit of the outstanding balance and other information shall be described in the Program Information, the validity period of which is 1 year (equivalent to the Euro MTN

³³ Please see current formats at <http://www.jpx.co.jp/english/equities/products/tpbm/outline/02.html>

program). In the case where an issuer publishes the Program Information, such an issuer is allowed to prepare the SSI only with the remaining information. In the case where the issuer publishes the adequate SSI after the registration of the Program Information, the listing will be accepted by the exchange following the submission of an initial listing application and initial listing application documents including the SSI.

Under the FIEA, if the initial listing applicant is a continuous disclosure company (a company which is obliged to submit the Annual Securities Report), publishing Issuer Filing Information is not required. Also, under the rules established by the exchange, the disclosure company can omit the corporate information from the description in the SSI provided that the SSI contains a notice that the company already submits the Annual Securities Report.

(b) Eligibility and Scope of Issuers

The regulations and practices on the TPBM do not distinguish between resident and nonresident issuers. The scope of issuers on the TPBM include

- (i) foreign corporations,
- (ii) foreign financial institutions,
- (iii) sovereign and government-sponsored issuers,
- (iv) supranational institutions,
- (v) Japanese corporations, and
- (vi) Japanese public entities (e.g., local governments).

All issuers may utilize note issuance programs as a form of bond or note issuance.

(c) Listing Eligibility Requirements for Initial Listing Companies

Issuers need to fulfill the following requirements to list on the TPBM:

- (i) The bonds or notes must obtain a credit rating from a rating company. The term rating agency noted here refers to a rating company that is recognized internationally and by Japanese investors. For eligibility information on credit rating agencies, please refer to Chapter II.J. A credit rating for the abovementioned Program Information may be used as the credit rating.
- (ii) The principal underwriter for the bonds or notes must be registered on the Lead Managing Underwriter List at the exchange. Securities companies registered on the Lead Managing Underwriter List are leading securities firms with experience in bond underwriting in Japan and/or overseas.

(d) Lead Managing Underwriter List

In Japan, an issuer needs to choose a lead managing underwriter for a note issuance program or bonds and notes to be listed on TPBM from among the Lead Managing Underwriter List prepared by TSE. The Lead Managing Underwriter List is simply a list of securities companies that could potentially serve as a lead managing underwriter

when listing bonds or notes on the TPBM or when disclosing program information. This list will be updated by TSE according to the applications from securities companies.³⁴

A securities company wishing to register on the list is to file an application with the TSE. The TSE, which will then examine the application by considering such factors as that party's appropriate domestic and overseas experience as a lead managing underwriter. Conversely, if the TSE deems the continued inclusion on the list of a party to be inappropriate (e.g., if that party decides to withdraw from the bond underwriting business), the TSE, at its discretion, may remove that party from the list.

A securities company is not required to pay a fee for inclusion on the Lead Managing Underwriter List.

One exception exists for the need to select an underwriter from the Lead Managing Underwriter List in cases where a financial institution deemed suitable by the TSE purchases the whole amount of a bond issue. Here, the financial institution would confirm the quality of the bonds or notes.

(e) Appointment of a Commissioned Company for Bondholders (Bond Trustee)

The appointment of a bond trustee or Commissioned Company or Person for Bondholders, also known as a Bond Manager (社債管理者), for bonds and notes to be listed on the TPBM is optional. The majority of bonds and notes listed on the TPBM feature a fiscal agent (財務代理人) as an agent of the issuer. For more information on the Commissioned Company for Bondholders (Bond Managers), please refer to Chapter III.M.

(f) Accepted Financial Reporting Standards

The TSE recognizes the Japanese Generally Accepted Accounting Principles, US Generally Accepted Accounting Principles, and financial reporting standards for the disclosure information to be provided by an issuer. The TSE rules prescribe that any alternative accounting standard may be recognized the TSE deems it to be equivalent to the Japanese Generally Accepted Accounting Principles, the US Generally Accepted Accounting Principles, or International Financial Reporting Standards.

(g) Eligible Bond and Note Types to be Listed the TPBM

The following are types of bonds and notes that are eligible to be listed on the TPBM:³⁵

- corporate bonds issued by Japanese or foreign companies; straight bonds; corporate bonds listed in Article 2 (1), Item 5 of the FIEA (including bonds issued by mutual companies, but excluding bonds with warrants (as prescribed by Article 2, Item 22 of the Companies Act));
- bonds issued by Japanese companies or government agencies in accordance with special laws; bonds issued by legal entities pursuant to the special laws listed in Article 2 (1), Item 3 of the FIEA;
- investment company bonds; bonds issued by funds; investment corporation

³⁴ The current list can be found at <http://www.jpx.co.jp/english/equities/products/tpbm/listing/04.html>

³⁵ Japan Exchange Group. Types of Bonds. <http://www.jpx.co.jp/english/equities/products/tpbm/listing/index.html>

- debentures and those foreign investment securities that are similar to investment corporation debentures, as prescribed in the Act on Investment Trusts and Investment Corporations, as outlined in Article 2 (1), Item 11 of the FIEA;
- foreign investment securities that are similar to investment company bonds;
 - municipal bonds issued by Japanese issuers; municipal bonds listed in Article 2 (1), Item 2 of the FIEA;
 - specified corporate bonds issued by Japanese or foreign companies; specified corporate bonds prescribed in the Act on the Liquidation of Assets listed in Article 2 (1), Item 4 of the FIEA;
 - beneficiary certificates of special purpose trusts that pay a fixed dividend; securities enumerated in Article 2 (1), Item 13 of the FIEA, and the amount of cash distributions of which during the trust period are predetermined;
 - beneficiary certificates of special purpose trusts issued by foreign issuers; bonds issued by foreign companies; and
 - sovereign bonds issued by foreign governments; among the securities listed in Article 2 (1), Item 17 of the FIEA, instances that have the qualities of the securities listed in Item 1 of the said paragraph.

Straight bonds and structured bonds that fit the definition of corporate bonds are eligible for listing, but convertible bonds and exchangeable bonds are not allowed to be listed on the TPBM.

Pursuant to Rule 2, Paragraph 9 of the Special Regulations of Securities Listing Regulations Concerning Specified Listed Securities, the listing of *sukuk* (Islamic bonds) is possible in form of a beneficiary certificate of a special purpose trust (please see Chapter VIII).

(h) *Choice of Currencies*

In principle, the TPBM does not have any limitation on the choice of currencies in which bonds or notes can be denominated. Domestic bonds and notes in the Japanese market are typically issued in yen. In addition to settlement for bonds and notes issued in yen, JASDEC is able to transfer (on a free-of-payment basis) foreign-currency-denominated bonds and notes issued by foreign governments or companies, such as those denominated in US dollars or other currencies including the Chinese renminbi.

(i) *Approval of Listing*

The TSE will check the application for listing, following the submission of the relevant information in documentation and disclosure items. The TSE will confirm that the bonds or notes satisfy the necessary conditions for listing eligibility in accordance with TSE rules. The TSE will simply confirm that certain formal requirements have been met and, therefore, the TSE's examinations will not require much time.

In principle, under the standard schedule, the administrative review for the acceptance of program information (Type-P of the SSF) submitted to the TSE may be completed by the acceptance date. The TSE may, at its discretion, request from the issuer supplementary information.

When individual bonds or notes are to be issued and listed based on the program information, if the listing application (Type-D of the SSF) is submitted simultaneously with the determination of the Terms and Conditions of the Notes as in the model

case, the TSE may approve the listing—normally within the same day but no later than the following business day—after promptly confirming that the listing eligibility requirements are satisfied.

Upon approval of the listing of the bonds or notes, the TSE publicly announces the listing straightaway in a timely manner.

(j) Actual (Effective) Listing of Bonds, Notes, or Program

Under the standard schedule, the submission date of the program information (or SSF) will be the disclosure date of the Program Information, which will also be the Note Issuance Program listing date.

The listing date of book-entry transfer bonds or notes is usually 1 business day after the settlement date. In the case of book-entry transfer bonds or notes, the Terms and Conditions of the Notes are generally determined within 4 business days before the settlement date in order for the paying agent to complete the necessary procedure.

(k) Obligations after Listing—Timely Disclosure

The issuer of listed bonds and notes must disclose the Issuer Filing Information:

- (i) Timely disclosure is required for dissolutions, bankruptcies, and dishonored notes. Compared to stock listings, the items required for disclosure are extremely limited. Companies with shares listed on exchanges in Japan will not be burdened with additional disclosures.
- (ii) Issuers of listed bonds or notes are required to provide Issuer Filing Information at least once a year. The Issuer Filing Information corresponds to financial statements. However, when the issuer is providing ongoing disclosure, there is no need for additional disclosure. When the issuer has securities listed overseas, disclosure information for those listings may be used as is.

2. Pricing after Listing

Bonds or notes listed on the TPBM or issued based on the Program Information submitted to the TSE are included within the JSDA's Reference Statistical Prices (Yields) for OTC transactions.

3. Listing Fees

Listing fees to be paid by the issuer of bonds or notes to be listed on the TSE are charged at the time of registration of the program information and the listing of the bonds or notes. In the TSE Enforcement Rules, listing fees are divided into two categories: (i) the fee for program listing (program fee) and (ii) the fee for listing bonds and notes (bond, etc. listing fee).³⁶

³⁶ Tokyo Stock Exchange. Enforcement Rules for Special Regulations of Securities Listing Regulations Concerning Specified Listed Securities, Rule 220. <http://www.jpx.co.jp/english/equities/products/tpbm/outline/tvdivq00000006xw-att/b7gie60000013xzd.pdf>

The program fee is JPY1 million. Any drawdown issuance of notes under the program will not incur an additional listing fee. The bond listing fee—in cases where program information is not used—is JPY1 million for any new listing.

No fees would normally be incurred at the annual renewal of the program, but an additional procedural fee of JPY1 million would be incurred if the issuer intends to raise the maximum outstanding amount under the program (program amount).

The fees are subject to applicable consumption taxes.

4. Trading, Clearing, and Settlement of TOKYO PRO-BOND Market-Listed Bonds and Notes

(a) Trading of TPBM-Listed Bonds and Notes

The TPBM launched a trading system and a settlement and clearance system, but investors can choose to trade in the OTC market. It is assumed that the main market for the bonds and notes listed on the TPBM will be the OTC market. Please also see Chapter IV for more information on trading of bonds and notes in Japan.

(b) Minimum Trading Unit

For a JPY-denominated bond, the minimum trading unit is JPY100 million (face value). For a bond denominated in a foreign currency, it is the face value of that series.

(c) Clearing and Settlement of TPBM-listed Bonds and Notes

All JPY-denominated domestic bonds and notes, other than JGBs, are settled at JASDEC. Foreign-currency-denominated domestic bonds and notes are also settled at JASDEC, though the settlement is effected on a non-DVP basis. JASDEC's Book-Entry Transfer System for Corporate Bonds handles registration and transactions in corporate bonds, municipal bonds, specified corporate bonds issued by SPCs, and rights that should be represented by bond certificates issued by any governments or companies in foreign countries (Samurai Bonds and Shogun Bonds). All transactions are conducted on an electronic basis only, since debt securities in Japan have been completely dematerialized.

The TPBM accepts the listing of foreign bonds and notes that are settled at other CSDs abroad.

5. Selling and Transfer Restrictions on the TOKYO PRO-BOND Market

Professional bonds are also subject to selling and transfer restrictions for domestic retail investors.³⁷ Transfer restrictions in the Japanese market are comprehensive and specific.

Bonds and notes issued through the TSE's TPBM shall not be sold or transferred to any person other than Professional Investors or nonresidents (Professional Investors, etc.).

³⁷ Japan Exchange Group. Who Can Invest in the TOKYO PRO-BOND Market? <http://www.jpx.co.jp/english/equities/products/tpbm/outline/03.html>

The FIEA requires that a contract on restriction on transfer (transfer restriction agreements) should be entered into between the issuer and the person (Professional Investor) seeking to purchase the bonds or notes, and between the solicitor or offeror (securities company) and the purchaser or acquirer.

The FIEA also requires notification to the purchaser to the effect that if the bonds or notes are not notified to the authority, the SRS or SR is not registered with the FSA, and the bonds or notes may be sold only to Professional Investors.

In addition, a restriction on transfer contract and notification with a Professional Investor for all TPBM-related bonds and notes transactions in a comprehensive way may be allowed in current market practice. For further details, please refer to Questions 55 and 56, and the answers thereto, in the Q&A section on the TPBM website.³⁸

In July 2015, the FSA opened a public consultation on the potential relaxation of the defined measures for selling and transfer restrictions laid out in Article 12 (i) (b) of the related Cabinet Office Ordinance.³⁹

According to the FSA proposal, in addition to the current method for entering into contracts between issuer and acquirer and between the intermediary and Professional Investor, other methods can be used, including a description of the selling and transfer restrictions in the Terms and Conditions of the Notes, or in the SSI (or SSF), in combination with other measures that will relate this information to the Professional Investor by the intermediary; in turn, the Professional Investor would have to acknowledge the contents, including the observance of these selling and transfer restrictions.

One possible such combination would be the description of selling and transfer restrictions and the aforementioned acknowledgement process in the Terms and Conditions of the Notes, or in the SSI (or SSF), and the sending of the information to the Professional Investor by the intermediary, as long as a record of sending the document to the registered e-mail address on the investor's trading account with the intermediary is retained. The forms of the acknowledgment could be expected to develop in line with market practices following the public consultation and resulting changes to the aforementioned Article 12.

Inclusion of selling and transfer restrictions in the Term and Conditions of the Notes is one way to fulfill a part of the requirements of the FIEA. The sample wording of the Selling restriction in the Terms and Conditions of the Notes is shown in the text box for reference.

³⁸ Japan Exchange Group. Q&A about the TOKYO PRO-BOND Market. <http://www.jpx.co.jp/english/equities/products/tpbm/outline/02.html>

³⁹ Article 12 (i) (b) of the related Cabinet Office Ordinance states: “[The] Solicitation of Offers to Acquire includes, as a condition of the acquisition, the conclusion of a contract on transfer specifying the matters provided in paragraph (1) of the preceding Article between the Issuer of the relevant Securities and the person who wishes to acquire said Securities in response to the Solicitation of Offers to Acquire them (hereinafter referred to as the “Acquirer” in this item), and between the person who is carrying out the Solicitation of Offers to Acquire said Securities and the relevant Acquirer.”

Table 27: Sample Wording of the Transfer Restrictions in the Terms and Conditions of Notes

Restriction on Transfer of Notes

1. Japanese Transfer Restriction

The Notes shall not be sold, transferred, or otherwise disposed to any person other than Professional Investors, Etc. (*Tokutei Toushika tou*) (Professional Investors, Etc.), as defined in Article 2, paragraph (3), Item 2 (B) 2. of the Financial Instruments and Exchange Act of Japan (Act No. 25 of 1948, as amended) (FIEA), except for the transfer of the Notes to the following:

- a. the Issuer, or the Officer (meaning directors, company auditors, executive officers or persons equivalent thereto) thereof who holds shares or equity pertaining to voting rights exceeding 50% of all the voting rights in the Issuer which is calculated by excluding treasury shares or any nonvoting rights shares (the Voting Rights Held by All the Shareholders, Etc. (*Sou Kabunushi Tou no Giketsuken*)) (as prescribed in Article 29-4, paragraph (2) of the FIEA, the same shall apply hereinafter) of the Issuer under his or her own name or another person's name (hereinafter such Officer shall be referred to as the Specified Officer (*Tokutei Yakuin*) in this paragraph), or a juridical person (excluding the Issuer) whose shares or equity pertaining to voting rights exceeding 50% of the Voting Rights Held by All the Shareholders, Etc. are held by the Specified Officer (the Controlled Juridical Person, Etc.) (*Hi-Shihai Houjin Tou*) including a juridical person (excluding the Issuer) whose shares or equity pertaining to voting rights exceeding 50% of the Voting Rights Held by All the Shareholders, Etc. are jointly held by the Specified Officer and the Controlled Juridical Person, Etc. (as prescribed in Article 11-2, paragraph 1, Item 2 (c) of the Cabinet Office Ordinance on Definitions under Article 2 of the Financial Instruments and Exchange Act (MOF Ordinance No. 14 of 1993, as amended)); or
- b. a company that holds shares or equity pertaining to voting rights exceeding 50% of the Voting Rights Held by All the Shareholders, Etc. of the Issuer in its own name or another person's name.

2. Matters Notified to the Noteholders and Other Offerees

When (i) a solicitation of an offer to acquire the Notes or (ii) an offer to sell or a solicitation of an offer to purchase the Notes (collectively, Solicitation of the Notes Trade) is made, the following matters shall be notified from the person who makes such Solicitation of the Notes Trade to the person to whom such Solicitation of the Notes Trade is made:

- a. no Securities Registration Statement (pursuant to Article 4, paragraphs 1 through 3 of the FIEA) has been filed with respect to the Solicitation of the Notes Trade;
- b. the Notes fall, or will fall, under the Securities for Professional Investors (*Tokutei Toushika Muke Yukashoken*) (as defined in Article 4, paragraph 3 of the FIEA);
- c. any acquisition or purchase of the Notes by such person pursuant to any Solicitation of the Notes Trade is conditional upon such person entering into an agreement providing for the restriction on transfer of the Notes as set forth in (1) above, (i) with each of the Issuer and the person making such Solicitation of the Notes Trade (in the case of a solicitation of an offer to acquire the Notes to be newly issued), or (ii) with the person making such Solicitation of the Notes Trade (in the case of an offer to sell or a solicitation of an offer to purchase the Notes already issued);
- d. Article 4, paragraphs 3, 5, and 6 of the FIEA will be applicable to such certain solicitation, offers and other activities with respect to the Notes as provided in Article 4, paragraph 2 of the FIEA;
- e. the Specified Securities Information, Etc. (*Tokutei Shouken Tou Jouhou*) (as defined in Article 27-33 of the FIEA) with respect to the Notes and the Issuer Filing Information, Etc. (*Hakkosha Tou Jouhou*) (as defined in Article 27-34 of the FIEA) with respect to the Issuer have been or will be made available for the Professional Investors, Etc. by way of such information being posted on (i) the website maintained by the TOKYO PRO-BOND Market (TPBM) (<http://www.jpx.co.jp/english/equities/products/tpbm/issues/index.html>), or (ii) the Issuer's web-site that discloses the information concerning the respective Issuers (the URL of which will be made available on the website maintained by the TPBM), in accordance with Articles 210 and 217 of the Special Regulations of Securities Listing Regulations Concerning Specified Listed Securities of the Tokyo Stock Exchange; and
- f. the Issuer Filing Information, Etc. will be provided to the Noteholders or made public pursuant to Article 27-32 of the FIEA.

6. Delisting

(a) *Conditions for Delisting*

In instances where the TSE deems delisting appropriate, the TSE will delist the said listed bonds, if any one of the events enumerated below occurs:

- (i) bonds or notes reach the final redemption date;
- (ii) acceleration of the final redemption date in relation to the full amount of bonds;
- (iii) absorption-type corporate split or new incorporation with succession by a new entity to obligations related to a listed bond issue; or
- (iv) material misstatement by an issuer of listed bonds in the SSI, Issuer Filing Information, or the Annual Securities Report; and
- (v) call for immediate redemption of listed bonds due to a default event;

or further to the above, determination by the TSE that delisting is appropriate.

(b) *Warning Measures*

In instances deemed necessary, the TSE will take warning measures, or impose a penalty or other means on the issuer of listed bonds, and, if deemed necessary, may publicly announce this measure.

I. Bond and Note Pricing

In most mature bond markets, bonds are usually traded OTC. As OTC bond trading is a negotiated process between a securities company and a client, it is difficult for a third party to discover the price at which a transaction is consummated. The publication of prices and other information concerning OTC bond transactions not only helps efficient and orderly trading of bonds but is also of critical importance from the standpoint of investor protection by promoting the formation of fair prices and facilitating investors' access to trading at the best possible price. Publication of bond prices is thus indispensable for the development of bond markets.

The JSDA provides a variety of bond-related statistical data, including Reference Statistical Prices (Yields) for OTC Bond Transactions, that are the most frequently used sources of price information for understanding current bond market trends in Japan. These data are calculated mainly based on reports received from JSDA member firms, and are disseminated on the JSDA website.⁴⁰

For more details on the Reference Statistical Prices (Yields) for OTC Bond Transactions, please refer to Chapter IV.D.

⁴⁰ See <http://www.jsda.or.jp/en/statistics/bond-market/index.html>

J. Transfer of Interests in Bonds and Notes

1. Book-Entry Framework as Prerequisite for Securities Transfer

The Law Concerning Book-Entry Transfer of Corporate Bonds, Stocks, and Other Securities provides a uniform legal framework for all types of book-entry securities, the legal basis for the book-entry transfer system, and the dematerialization of all securities.

In principle, all securities in the Japanese market have since been dematerialized. While the Companies Act continues to allow that physical bond certificates may be issued regardless of the book-entry transfer method, the distribution in the market of such physical certificates cannot be widely expected. Such securities are also not allowed to be owned under a tax-exempt status under the Japanese taxation system. For all intents and purposes, hence, the legal ownership structure of the dematerialized securities is clear. Except for a few non-CSD based private placed notes, the book-entry ownership type is the only practical alternative in Japan.

JASDEC performs the role of a CSD in the book-entry transfer system in securities other than government bonds. The BOJ performs the role of CSD for Japanese government bonds. In the abovementioned law, the term CSD is referred to as a Designated Depository Institution. Book-entry bond transfer system participants must observe the rules established by the respective depository institution.

2. Actual Book-Entry Transfer Process

The actual process of transfer of interest (change in ownership) in bonds and notes occurs in the book-entry transfer system through the accounts of the designated depository institutions held by investors and/or their intermediaries.

(a) *Participation in the Book-Entry System*

Securities companies and financial institutions open and maintain, as account management institutions (intermediary), an account for securities transfer at the designated depository institution. Bondholders (investors) open a transfer account in the depository institution or the account management institution (intermediary), depending on their service needs.

(b) *Book-Entry Transfer Process*

In the transfer account, the balance of the account management institutions' (intermediary's) own account and the overall customer account are recorded. In turn, the bondholder's account balance is recorded in the transfer account they maintain with the account management institution (intermediary). Securities to be issued are initially recorded in the issuer's own account.

The existence of a book-entry recording in the bondholders account constitutes the ownership of the bonds or notes by the bondholder. The ownership of the rights of the book-entry bonds shall be determined by the description or record in the book-entry transfer account registry. The transfer of the book-entry bonds shall not take effect unless there has been an increase in the amount described or recorded in the ownership column of the assignee's account through application for the book-entry transfer (Articles 66, 73, and 88 of the Act on Book-Entry of Company Bonds, Shares, etc.)

At the time of issuance of bonds or notes, by performing an electronic transfer on the basis of an account transfer description or a record through application of an underlying transaction (e.g., subscription or purchase), the securities are moved from the issuer's account to the investor's account and are entitled to be owned by the bondholder.

In other words, the presence of the recording represents a perfection against third party. In law, generally, perfection relates to making an interest or ownership here in debt securities effective against third parties. In Japan, the book-entry recording represents said perfection. Should there be an insufficient transfer-account book record in the customer's account due to the over-recording, the duty of retirement of over-recording is generated by account management institutions (intermediary).

K. Definition of Professional Investor and Related Classifications

Japan features one of the most comprehensive definitions of Professional Investors in ASEAN+3, which includes institutional and high net worth investors with specific qualifying criteria, and also includes foreign institutional investors.

1. Definition of Professional Investor

The definition of Professional Investor is stipulated in Article 2, Paragraph 31 and Article 34-4 of the FIEA, and in the Cabinet Office Ordinance on Definitions under Article 2 of the FIEA, as follows.

- (a) The term Professional Investor as used in Article 2, Paragraph 31 of the FIEA comprises
 - (i) Qualified Institutional Investors,
 - (ii) Government of Japan,
 - (iii) Bank of Japan, and
 - (iv) Investor Protection Funds prescribed by Article 79-21 and other juridical persons (including nonresident juridical persons) specified by Article 23 of the Cabinet Office Ordinance on Definitions under Article 2 of the FIEA.
- (b) The term Professional Investor as used in Article 34-4 of the FIEA comprises designated individuals who satisfy certain other requirements and are allowed to change their status to that of a Professional Investor by request (approved individuals with net financial assets of at least JPY300 million and at least 1 year of trading experience).
- (c) The term Professional Investor as used in the Article 23 of the Cabinet Office Ordinance on Definitions under Article 2 of the FIEA comprises
 - (i) local governments;
 - (ii) juridical persons incorporated by a specific act of incorporation pursuant to the provisions of any specific act;
 - (iii) an Investor Protection Fund as prescribed in Article 79-21 of the FIEA;
 - (iv) Deposit Insurance Corporation of Japan;
 - (v) the Agricultural and Fishery Cooperative Savings Insurance Corporation;
 - (vi) the Insurance Policyholders Protection Corporation of Japan prescribed in Article 259 of the Insurance Business Act;
 - (vii) an SPC;

- (viii) a company that issues share certificates which are listed on a financial instruments exchange;
- (ix) a stock company whose stated capital is expected to amount to JPY500 million or more, reasonably judging from the status of the transactions thereof or any other circumstances;
- (x) a Financial Instruments Specialist, or a juridical person that falls under the category of a Notifier of Specially Permitted Business Activities as prescribed in Article 63 (3) of the FIEA; and
- (xi) a foreign juridical person.

In summary, Professional Investors include pension funds, life insurance companies and other accredited institutional investors, listed companies, joint stock corporations with at least JPY500 million in capital, government agencies, the BOJ, and other approved corporations and local governments, together with approved individuals with net financial assets of at least JPY300 million and at least 1 year of trading experience. (Here, approved means that the entity must first seek and obtain approval for the status of Professional Investor from a securities company.)

In effect, only Professional Investors and nonresident (foreign) investors are able to participate in the TPBM.

2. Scope of Professional Investor

The concept of Professional Investors was formed by the FIEA from the viewpoint of ensuring regulatory flexibility; attaining more appropriate investor protection; and, at the same time, allowing Professional Investors more freedom in transactions as professional market participants. As such, investors have been divided into nonprofessionals and professionals, depending on their knowledge and experience, and the status of their property. And when financial institutions do business with professionals, the regulations designated for nonprofessionals (e.g., investor protections) need not be applied. As a result, a softening of regulations has been achieved through the introduction of this concept. On the other hand, for the purpose of protecting general and retail investors, if the customer is nonprofessional, the applicable codes of conduct and regulations will have to be applied by the financial institutions.

3. Scope of Professional Investor, Etc.

The use of the term Professional Investors, Etc. refers to Professional Investors or Nonresidents and is defined in Article 2 (3) (ii) (b) 2 of the FIEA.⁴¹ This term and its components are included within the scope of the Professional Investor concept in Japan. As an example, it is not regarded as a public offering of securities if solicited securities are not likely to be transferred from the acquirer to a person other than Professional Investors, Etc. (Professional Investors or nonresidents) by satisfying transfer restrictions.

The definition of Professional Investors, Etc. is stipulated in a distributed manner at several locations in the FIEA and the Cabinet Office Ordinance. For instance, in Article 1 (3) (iii) 2 of the Cabinet Office Ordinance on Definitions under Article 2 of the FIEA, Professional Investors, Etc. is referred to as defined in Article 2 (3) (ii) (b) 2 of the FIEA.

⁴¹ As defined in Article 6 (1) (vi) of the Foreign Exchange and Foreign Trade Act, nonresident shall mean natural persons and juridical persons other than residents.

4. Scope of Qualified Institutional Investor

The QII scheme was created for the purpose of achieving a softening of the disclosure regulations toward expert institutional investors. Offerings of securities are exempted from public disclosure requirements if a solicitation is made only to qualified institutional investors. QIIs refer to persons specified by the FIEA and a Cabinet Office Ordinance as those having expert knowledge of and experience with investment in securities and other financial instruments.

A juridical person QII includes

- (a) those that automatically constitute as a QII (e.g., certain Financial Instruments Business Operators as well as banks), including insurance companies, securities firms, investment managers, and other institutional investors; and
- (b) those that may become QIIs as a result of filing the necessary notification with the Commissioner of the FSA:
 - (i) trust companies and foreign trust companies (excluding custodial trust companies);
 - (ii) corporations that hold and manage at least JPY1 billion in securities—a juridical person that falls under the category of a Specially Permitted Business Notifying Person as prescribed in Article 63 (3) of the FIEA; and
 - (iii) nonresident juridical persons (e.g., foreign governments, foreign financial institutions).

An Individual QII includes

approved individuals with net financial assets of at least JPY1 billion and at least 1 year of trading experience—a Financial Instruments Specialist person that falls under the category of a Specially Permitted Business Notifying Person as prescribed in Article 63 (3) of the FIEA.

A cooperative, etc. QII includes

- (a) an Investment Limited Partnership, and
- (b) a juridical person and individual of the union, including executive union members that obtained the consent of all of the union members and the securities holdings of the union is more than JPY1 billion.⁴²

5. Classification and the Change of Status of Investors in Japan



As shown in Table 28, a change of status from that of a Professional Investor to a general investor, or vice versa, is carried out within the relationship with each securities company by the investor making a request to such a securities company. In consequence, under the suitability principle, a securities company may from time to time assure itself of the status of the investor based on the investor's intentions.⁴³

⁴² In order to eliminate the QIIs without actual business, for the Investment Limited Partnership which is a QII, the FSA is planning to define the conditions in the Cabinet Office Ordinance to be with assets under management (excluding borrowings) of JPY500 million or more.

⁴³ The suitability principle (FIEA, Article 40) states that a financial institution should make a solicitation that is commensurate with the situation of the customer in view of the customer's knowledge and experience, and the status of the property and purpose of the purchase.

Professional Investors who are residents in Japan can invest in overseas bonds and notes without any legislative restrictions.

Table 28: Classification and the Change of Status of Investors in Japan

Professional Investor	1. Cannot request nonprofessional treatment a. Qualified institutional investor b. Government of Japan c. Bank of Japan	Always treated as a professional investor
	2. Can request nonprofessional treatment (designated companies and organizations) a. local government b. public companies c. joint stock companies whose capital is reasonably believed to be JPY500 million or more d. foreign corporations (foreign juridical persons) e. others	Option to be nonprofessional ^a 
General Investor	3. Can request professional treatment a. designated individual (i) with trading experience of one year or more, and (ii) whose net asset, and invested assets, are reasonably believed to be each worth JPY300 million or more b. others	 Option to be professional ^a
	Cannot request professional treatment (individuals other than above in 3)	Always treated as a general investor

^a Opt-in-opt-out treatment
Sources: Financial Services Agency; ABMF SF1.

L. Credit Rating Requirements

This section covers the applicable credit rating requirements for bonds and notes issued in Japan. For more details on the underlying regulations governing eligible credit rating agencies, please refer to Chapter II.J.

1. Public Offers

The use of credit ratings for bonds or notes to be issued via a public offering is no longer mandated by the financial market regulators. However, the use of credit ratings has continued along with the growth of the corporate bond market in Japan, and credit ratings are widely used.

Bonds issuers shall note the credit ratings in the SRS and its attachments and prospectus filed or published prior to the issuance of bonds or notes via a public offering, and need to indicate whether the credit rating have been obtained from registered CRAs.

Financial instruments business operators involved in a public offering of bonds or notes, such as securities firms, have the obligation to explain whether the credit ratings are from a registered CRA or not.

2. TOKYO PRO-BOND Market

Note issuance programs or corporate bonds and notes listed on the TPBM must obtain a rating from a CRA recognized internationally and/or by Japanese investors. The rating needs to be disclosed, but the level of the rating is not an eligibility criterion for the TPBM.

With regard to bonds and notes issued by a foreign government or local government (both domestic and foreign), or guaranteed by a national or local government (domestic or foreign), or by certain financial institutions recognized by the TSE, a credit rating is not required.

CRAs recognized by the TPBM include

- Standard & Poor's,
- Moody's,
- Fitch Ratings,
- Rating and Investment Information,
- Japan Credit Rating Agency, and
- RAM Rating Services.

M. Commissioned Company for Bondholders (Bond Managers)

1. Summary

In cases where a company will issue bonds in Japan, generally speaking the company must specify a commissioned company or person for bondholders (Bond Managers) and entrust the receipt of payments, the preservation of rights of claim on behalf of the bondholders, and other administration of the bonds to that manager; provided that this shall not apply in cases where the minimum issuing amount (face value) of each bond is JPY100 million or more as prescribed by the Companies Act.⁴⁴

This implies that the minimum face value of the note of JPY100 million or more will only be sold to Professional Investors and will not be sold to individuals. Other cases prescribed by the applicable ordinance of the Ministry of Justice are cases where it is unlikely that the protection of bondholders will be compromised.

2. Commissioned Company (Bond Managers) for Bondholders System

A drastic reform of the conventional corporate bonds trustee system was carried out by amending the Commercial Code in June 1993. Under this amendment, the conventional name, Bond Trustee Company, was changed to commissioned company (Bond Managers), and its function was clarified. Specifically,

- (i) establishment of a commissioned company (Bond Managers) was made mandatory, in principle, and the eligibility for becoming one is restricted to banks, trust companies, and companies that have received a license under the Mortgage Bond Trust Law;
- (ii) services to be provided by a commissioned company (Bond Managers) are restricted to the management of bonds that have been issued and are outstanding; and

⁴⁴ Government of Japan. 2005. *The Companies Act Article 702*. Tokyo.

- (iii) the power, duty, and liability of the commissioned company (Bond Managers) have been clarified.

The impact of the amendment may be summarized as follows:

- (i) the fee the trustee bank had been collecting was renamed commissioned companies fee;
- (ii) by instituting exceptional provisions with respect to the mandatory engagement of a commissioned company (this applies when the minimum face value of a bond is not less than JPY100 million), issuers can appoint a fiscal agent; and
- (iii) the previous practice that the lump purchases of defaulted bonds that trustee banks have been making were discontinued, and discontinuation has been established.

Under the current Companies Act adopted in June 2005 (enacted in May 2006), a commissioned company for bondholders (Bond Managers) and its liability and power have been expanded (Articles 702–712). Specifically,

- (i) under the former Commercial Code, the term “administration of bond” referred only to the exercise of power legally granted to the commissioned company and person for bondholders (Bond Managers) and did not include the exercise of power based on an agreement, commissioning the administration of bonds (contractual power); under the new Companies Act, however, the exercise of the contractual power is included in the administration of bonds and the commissioned company and person for bondholders (Bond Managers) owes the duty of impartiality and good faith and the duty to exercise reasonable care and skill in exercising such contractual power;
- (ii) when the agreement commissioning the administration of bonds contains a provision to that effect, the commissioned company and person for bondholders (Bond Managers) act in relation to filing a lawsuit and taking bankruptcy or rehabilitation proceedings for the bond as a whole without obtaining a resolution of the bondholders’ meeting; and
- (iii) in taking steps to protect the creditors in the case of a capital reduction or a merger, the commissioned company and person for bondholders (Bond Managers) may, in principle, object to such capital reduction or merger without obtaining a resolution of the bondholders’ meeting.

In an investment environment where there have been very few corporate bond defaults, a commissioned bank or person (Bond Manager) has not been appointed in many cases, except for corporate bonds targeting individual investors. Therefore, there is no consensus about the role of a commissioned bank or person (Bond Manager), the preservation attachment for corporate bondholders when the corporate bond is in default, and not so much discussion has been held regarding cost sharing.

3. Recent Japan Securities Dealers Association Initiative in the Discussion about a Bond Administration System

As a part of the recent JSDA initiative for the vitalization of Japan’s corporate bond market, the JSDA deliberated about a corporate bond administration system in Japan. The interim report of this initiative states as follows:

(a) *Credit Risk of a Corporation and Corporate Bond Administration*

- (i) A Corporate Bonds Manager is in principle appointed at the time of issuance of the corporate bonds under the Companies Act and acts as a statutory agent of corporate bondholders to monitor the financial condition of the issuer and preserve or recover the debts at the time of default.⁴⁵
- (ii) Currently, while the Corporate Bonds Manager is appointed for corporate bonds targeting individual investors, most corporate bonds targeting institutional investors do not appoint Corporate Bonds Managers.
- (iii) It is necessary to maintain the current system that enables a corporation with relatively lower credit risk and a high profile in the corporate bond market to issue corporate bonds flexibly at lower cost. On the other hand, for the purpose of promoting issuance of and investment in corporate bonds of a corporation with relatively higher credit risk, it must be possible to grant various covenants on such corporate bonds. It might be necessary to develop an environment where the Corporate Bonds Manager can sufficiently fulfill the role of monitoring financial conditions and preserving or recovering debts and where such covenants can be properly reflected in the issuance conditions.
- (iv) It is also necessary to prepare a system in which the absence of a Corporate Bonds Manager would not damage the credibility of the corporate bonds issued by such companies and the corporate bond market as a whole if the credit risk increases due to deterioration in the business conditions of the issuer.
- (v) Two approaches are available regarding the appointment of a Corporate Bonds Manager: (a) appoint a Corporate Bonds Manager for all corporate bonds; or (b) appoint a Corporate Bonds Manager for corporate bonds issued by a corporation with relatively higher credit risk. For the time being, while discussing the tasks taken by the Corporate Bonds Manager, it may be useful to establish approach (b) as a market practice.
- (vi) In the case of corporate bonds issued by a corporation with relatively higher credit risk, a standard model of appointing a Corporate Bonds Manager is needed that can be used as a reference for issuers, investors, and securities companies in order that the appointment of a Corporate Bonds Manager can be established as a market practice.
- (vii) Currently, many main banks play the role of Corporate Bonds Manager. Some market participants are concerned that a conflict of interest could occur before or after corporate bonds default if, in the future, corporate bond issuers become more diversified and more corporations with relatively higher credit risk issue corporate bonds. Therefore, it is necessary to increase the credibility and transparency of tasks assumed by Corporate Bonds Managers, as well as discuss what tasks are to be assumed by them.

(b) *Corporate bonds administration in the future*

- (i) One of the reasons why many issuers do not appoint a Corporate Bonds Manager is that issuers are doubtful about whether the tasks assumed by the Corporate Bonds Manager justify the costs incurred by the issuer. On the other hand, Corporate Bonds Managers point out that their responsibilities under the Companies Act are substantial.

⁴⁵ In its documents, JSDA uses this Alternative Expression to Bond Manager (see also Appendix 5).

- (ii) The relationship between the responsibilities and costs of the Corporate Bonds Manager should be considered carefully based on the fact that the credit risk of the issuer closely relates to the responsibilities of the Corporate Bonds Manager. The tasks assumed by Corporate Bonds Managers need to be defined and a system established in which these various factors can be properly reflected in the costs through a market mechanism.
- (iii) The tasks assumed by Corporate Bonds Managers in the US, where they are known as Trustees, are significantly different before and after a corporate bonds default. Particularly, the tasks before default include only administrative processes, such as receiving a disclosure document including the annual report on a regular basis, and do not include the tasks of requesting financial information, monitoring, and review.

N. Securitized Products Market

1. Securitized Products

The income-generating assets of a company are pooled separately from its balance sheet into a special purpose vehicle (SPV), and the SPV issues a security backed by the cash flow to be generated by such assets and sells the security to investors. This method is called securitization. The security issued through such a process is generally called a securitized product.

Business enterprises use their assets—such as auto loans, mortgage loans, commercial real estate loans, leases receivable, and business loans—as collateral to back up their securitized products.

As defined by the Ordinance for Enforcement of the Act on Securitization of Assets, not only monetary claims, but also securities, real estate, movable properties, ships, aircrafts, automobiles, and intellectual property such as copyrights and patents can be securitized.

2. Basic Mechanism of Issuing Securitized Products

Generally, many of the securitized products are issued through the following mechanism. First, the holder of assets (originator), such as mortgage loans and accounts receivable that are to be securitized, assigns them to an SPV. By doing so, such assets are separated from the balance sheet of the originator and become assets of the SPV, which becomes the holder of the assets. An SPV may take the form of a partnership, a trust, or an SPC. Most SPVs take the form of an SPC.⁴⁶ The next step is to formulate the terms of issuance for the securitized product to be issued by the SPV. If the originator opts for the trust method, it issues certificates of beneficial interest like those of a trust company. If it chooses the SPC method, it issues the kinds of securities decided upon by the SPC, but it does not have to issue them based on the same terms.

In short, it can design each type (tranche) of security with a different character by differentiating the order of priority with respect to the payment of interest and redemption

⁴⁶ An SPC established under the Act on Securitization of Assets, later revised as the Special-Purpose Company (SPC) Law (2000年改正SPC法 or 資産流動化法) is called *tokutei mokuteki kaisha* (特定目的会社: TMK, or a specific-purpose company).

of principal, by varying maturities, or by offering the guarantee of a property or casualty insurance company.

By adding such variation, the originator can issue securities that meet the diverse needs of investors. In the order of priority for payment, such securities are called senior securities, mezzanine securities, or subordinated securities.

When the originator plans to sell its securitized products to an unspecified large number of investors, it should make them readily acceptable to investors by offering them objective and simple indicators (credit ratings) for independently measuring the risks involved.

In addition, there are other players involved in different processes of securitized products, such as servicers, who manage assets that have been assigned to an SPV and securitized, and also recover funds under commission from the SPV and bond management companies, which administer the securitized products (corporate bonds) purchased by investors.

Firms that propose such a mechanism for securitizing assets and that coordinate the issuing and the sale of such products are called arrangers, and securities companies and banks often act as arrangers.

3. Description of Major Securitized Products

Securitized products are divided into several groups according to the types of assets offered as collateral and the character of the securities issued. Among these, the group of products that are backed by monetary claims and group of products backed by real estate, which comprise exchange-listed real estate investment trusts (J-REIT) and OTC-traded real estate investment trusts, are popular.

The groups of products backed by the claims collateralized by real estate are residential mortgage-backed securities (RMBS) and commercial mortgage-backed securities (CMBS). RMBS are issued in retail denominations against a portfolio that pools home mortgage loans. The first securitized product based on residential mortgage loans was the Residential Mortgage Loan Trust (住宅ローン債権信託) launched in 1973 for the purpose of handling the liquidation of mortgage loans of mortgage companies. However, this product failed to attract the attention of both issuers and investors because it had too many limitations.

This scheme had been regulated by the MOF and was fully liberalized in June 1998. As a scheme based on SPCs became available thereafter as a result of the enactment of the previous SPC Law in 1998 (1998旧SPC法 or 特定目的会社による特定資産の流動化に関する法律), the volume of this type of issue has increased since 1999.

The bonds which are backed by housing loans and issued by the Japan Housing Finance Agency since 2001, Japan Housing Finance Agency Mortgage-Backed Securities, are usually included among RMBS, although they are not issued through SPCs.

CMBS are backed by loans given against the collateral of commercial real estate (e.g., office buildings). The mechanism of issuing them is almost the same as that for RMBS.

J-REITs, which became available by virtue of implementation of the Investment Trust and Investment Corporation Law (投資信託及び投資法人に関する法律) in May 2000, are investment trusts investing in real estate and real estate trust beneficiary rights.

Another group consists of securities backed by assets, or asset-backed securities (ABS) narrowly defined, such as accounts receivable, leases receivable, credits, auto loans, and consumer loans, among others. Sales of these products began to increase following the enactment of the Specified Claims Law (特債法 or 特定債権法) in June 1993.

Other securitized products are called collateralized debt obligations (CDOs), which are securities issued against the collateral of general loans, corporate bonds, and credit risks of loans that are held by banking institutions. For instance, loans to SMEs that are securitized may be considered CDOs. CDOs include collateralized loan obligations (CLOs), collateralized bond obligations (CBOs), and synthetic collateralized debt obligations, which include synthetic CLOs and CBOs that generally uses credit default swaps and other derivatives.

4. Issuing Market for Securitized Products

As the bulk of securitized products are issued in private placement transactions between the parties concerned, it is difficult to accurately grasp the size of their market. To remedy this shortcoming, underwriters that are involved in the transactions and credit rating agencies have been tracking the market on their own.

According to the JSDA and the Japan Bankers Association, the total value of securitized products backed by monetary claims was about JPY2.3 trillion in FY2014. Securitized product issuance reached a peak of JPY9.8 trillion in FY2006 and levels have declined sharply over the past few years amid various impacts of the subprime loan problem.

5. Secondary Market for Securitized Products

With the exception of beneficiary certificates of J-REIT, trading in securitized products is not conducted on stock exchanges. As is the case with bonds, securitized products and their transactions are too complex and varied to lend themselves to exchange trading. This has led to the dependence on an OTC inter-dealer market for their trading.

Table 29: Change in Number and Value of Securitized Product Issuance Market

	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
Number of Issuance of securitized products	312	314	261	204	146	107	91	90	110	164
Issuing amount of securitized products (JPY trillion)	8.2	9.8	6.8	3.7	2.9	2.6	3.4	2.9	1.9	2.3
Issuing amount of corporate bonds (JPY trillion)	7.4	7.5	9.6	9.9	10.6	10.1	8.5	8.4	8.8	8.5

FY = fiscal year (April 1–March 31).

Sources: Japan Securities Dealers Association and the Japan Bankers Association. <http://www.jsda.or.jp/shiraberu/syoukenka/doukou/index.html>

6. Enactment of Securitization-Related Laws

The existing legal system of Japan is built around business-specific laws, and the regulatory system of financial products is vertically divided along the lines of business-specific laws. As these laws contain many provisions regulating or banning business activities outright, to spur the development of new business, such as the securitization of assets, the existing laws have to be amended and new laws must be enacted.

Table 30: Summary of the Enactment of Securitization-Related Laws

Year	Name of Law in English	Name of Law in Japanese
1993	Specified Claims Law	特債法 or 特定債権法
1996–2001	Financial Big Bang in Japan	日本版金融ビッグバン
1998	Financial System Reform Law	金融システム改革法
1998	Revised Securities and Exchange Law	改正証券取引法
1998	SPC Law	SPC法
1998	Perfection Law	債権譲渡特例法
1998	Revised Investment Trust Law	改正投資信託法
1999	Servicer Law	サービサー法 or 債権管理回収業に関する特別措置法
1999	Nonbank Bond Law	ノンバンク社債法
1999	Revised Equity Contribution Law	改正出資法
2000	Revised SPC Law	改正SPC法
2000	Act on Securitization of Assets	資産流動化法
2000	Revised Investment Trust Law (Act on Investment Trust and Investment Corporation)	改正投資信託法
2001	The First Listing of J-REIT Securities	J-REIT上場開始
2005	Revised Civil Code	改正民法
2007	FIEA	金融商品取引法
2007	Abolishment of Mortgage Securities Law	抵当証券法廃止
2011	Revised Act on Securitization of Assets	改正資産流動化法

FIEA = Financial Instruments and Exchange Act, REIT = real estate investment trust, SPC = special purpose company.

Source: ABMF SF1.

As regards the securitization of assets, the Specified Claims Law (特債法 or 特定債権法) was enacted as an independent law in 1993. Since the enforcement of this law, the legal infrastructure has been developed steadily. Under the Specified Claims Law, the liquidation and securitization of assets classified as specified claims, such as leases receivable and credit card receivables, started. Thereafter, various laws were enacted to help the banking institutions meet the capital ratio requirements imposed by the Bank for International Settlements and to encourage the securitization of their assets to deal with the bad loan problem that had become serious since the beginning of the 1990s.

Under the SPC Law enacted in 1998 and the Act on Securitization of Assets enacted as the revised SPC Law in 2000, structures incorporating SPVs, including specific-purpose companies (TMKs) and specific-purpose trusts (SPTs), may be used for securitizing specified assets designated in the provisions of the said laws—real estate, designated money

claims, and beneficiary certificates issued against such assets in trust—in the form of ABS (e.g., senior subscription certificates, specified corporate bonds, and specified promissory notes). Under the SPC Law, the system of disclosing an asset liquidation plan and individual liquidation projects was introduced, in addition to the disclosure requirements of the Securities and Exchange Law (the FIEA now).

In 1998, the Perfection Law (債権譲渡特例法) was enacted as a law prescribing exceptions to requirements under the Civil Code (民法) for the perfection of the assignment of receivables and other properties, and it was amended in 2005. The Civil Code provides the legal requirements for the assertion of the assignment of nominative claims (claims with named creditors) against obligors or third parties. Designated claims were transferable, but the provisions of the Civil Code had been a major hurdle in securitizing them. The Perfection Law set forth simple procedures for the perfection of such interests.

The Servicer Law, enacted to account for exceptions to the provisions of the Practicing Attorney Law (弁護士法), allows accredited joint stock companies to provide the services of administering and collecting debts. Under the 1999 Servicer Law (サービサー法 or 債権管理回収業に関する特別措置法), a debt collection company may be established to provide a bad debt collection service without conflicts with the Practicing Attorney Law.

By amending the Equity Contribution Law (出資法), the Nonbank Bond Law (ノンバンク社債法) conditionally lifted the ban imposed on nonbanks on the issuance of corporate bonds and commercial paper for the purpose of raising capital for lending operations and on ABS.

As a result of the revision of the Securities and Exchange Law (証券取引法) as required by the 1998 Financial System Reform Law (金融システム改革法) and the enforcement of the FIEA (金融商品取引法), beneficiary certificates of and trust beneficiary interests in assets that are deemed eligible for securitization by the provisions of the Act on Securitization of Assets (改正SPC法 or 資産流動化法) and mortgage certificates under the Mortgage Securities Law (抵当証券法) are now legally considered securities.

Furthermore, pursuant to the enactment of the Investment Trust Law (投資信託法) as revised, real estate was included in eligible assets, which paved the way for the issuance of J-REIT securities.

O. Bankruptcy Procedures

There are four statutory insolvency proceedings that apply to Japanese corporations. Each can be categorized into one of two general types, depending on whether the aim of the proceedings is to liquidate the company (Liquidation-Type Proceedings) or rehabilitate the company (Rehabilitation-Type Proceedings):

- (1) Liquidation-Type Proceeding
 - (a) Bankruptcy proceedings (*hasan*) under the Bankruptcy Act
 - (b) Special liquidation proceedings (*tokubetsu seisan*) under the Companies Act
- (2) Rehabilitation-Type Proceedings
 - (a) Corporate reorganization proceedings (*kaisha kosei*) under the Corporate Reorganization Act

- (b) Civil rehabilitation proceedings (*minji saisei*) under the Civil Rehabilitation Act

At the time of the filing of the application for or the commencement of any of those insolvency proceedings or both, depending on the language of the default clause of the relevant bonds, the bonds will be accelerated. If a commissioned company for bondholders has been appointed for the bonds, the commissioned company will act for the benefit of the bondholders as creditors of the issuer in the proceedings. If no commissioned company has been appointed, individual bondholders will be expected to act for themselves in the proceedings.

As an alternative to commencing one of the four types of statutory insolvency proceedings above, a Japanese corporation in financial distress may seek to negotiate an out-of-court restructuring of the corporation with its creditors. In the course of such negotiations, a bondholders' meeting may determine the amendment to the terms and conditions of the bonds, such as installment repayment of principal amount or reduction of the interest rate, though a court approval will be required to have the decision of the meeting take effect. The statutory bondholders' meeting system set out in the Companies Act is applicable only to bonds issued by Japanese corporate issuers under Japanese law.

Further details on the restructuring and insolvency frameworks of Japan and other Asia-Pacific economies can be found in *The Asia-Pacific Restructuring and Insolvency Guide 2006*⁴⁷ and *A Guide to Asia-Pacific Recovery and Insolvency Procedures*.⁴⁸

P. Event of Default

In the context of a bond issuance, if a certain event of default has occurred in the issuer, the principal of the debt, regardless of its maturity, must be immediately repaid.

Examples of typical events of default of debt securities include

- (i) if the interest is not paid on the interest payment date;
- (ii) if matters in violation of the provisions in the terms and conditions of the bond occur, and are left uncured;
- (iii) if substantially all of the business is transferred or terminated;
- (iv) if the risk of bankruptcy is caused, such as the payment stop or the bankruptcy petition; or
- (v) if an event of default has occurred to other debentures that the issuer has issued, (cross-default clause).

Generally, an event of default is stipulated in the terms and conditions of a debenture. Under Japanese law, the terms and conditions are deemed to be an agreement between the debenture issuer and the debenture holder.

In principle, the event of default is described in the Companies Act in the context of a defaulting company (issuer); the act regards failure of payment of interest or principal for a certain period as an event of default:

⁴⁷ Globe White Page. 2006. *The Asia-Pacific Restructuring and Insolvency Guide 2006*. London.

⁴⁸ Clifford Chance. 2013. *A Guide to Asia-Pacific Recovery and Insolvency Procedures*. <http://financialmarketstoolkit.cliffordchance.com/en/financial-markets-resources/resources-by-type/guides/restructuring-and-insolvency-guide-asia-pacific.html>

Companies Act, Article 739 (1)

If a bond-issuing Company fails to pay interest on bonds, or fails to periodically partially redeem bonds in cases where it must carry out that redemption, pursuant to a resolution of a bondholders' meeting, the person who executes such resolution may give written notice to the bond-issuing Company to the effect that that bond-issuing Company must make payment within a defined period of time, and to the effect that, if payment is not made within such period of time, the bond-issuing Company shall forfeit the benefit of time as to the total amount of such bonds, provided, however, that such period may not be less than two months.

Generally, financial covenants are stipulated in the condition of the bonds and failure to perform the financial covenants for a certain period shall be regarded as an event of default. The most typical single financial covenant on Japanese domestic unsecured senior corporate bond is a negative pledge.

Negative pledge is a provision in the terms and conditions that prohibits the contract party from creating any security interests over certain property specified in the provision. In other words, a negative pledge clause is a negative covenant in the terms and conditions stating that the bond issuer will not pledge any of its assets on other bonds.

Also, a pari passu clause is a standard clause found in many bond issues. The clause is a covenant or a warranty that the bonds rank pari passu with all the other unsecured debt of the issuer. The clause appears in both corporate and sovereign debt obligations. The pari passu clause stipulates that the bond has the same rank with the other unsecured debt of the issuer in terms of the repayment order terms and has no subordination to the others.

If the issuer is a foreign government, unlike the private sector, a situation referred to as bankruptcy does not occur since a government is not a company, and, hence, the provisions of the Companies Act will not apply. Therefore, in many cases, nonpayment of interest will become a trigger of default. As a result, Japan's Civil Code is applied to those cases.

Triggered by the default of sovereign debt, including Samurai Bonds, international controversy on the interpretation of the pari passu clause, including the application of judgments of US federal courts, continues in relation to the debt restructuring by said government.

Trading and Transactions of Bonds and Notes, and Trading Market Infrastructure

A. Participants in the Secondary Bond Market

This section provides an overview of the major participants in the secondary bond market in Japan, on the basis of the transaction statistics by type of transaction party, as detailed in Table 31. The following types of participants, listed in alphabetical order, represent the largest shares of market volume.

When measured in terms of net trading volume over the past 13 years, almost all participant categories have been net buyers of bonds, mostly JGBs and other public sector bonds.

1. Bank of Japan and Other Government Agencies

The BOJ is buying and selling a range of debt securities as part of its open market operations, including JGB and money market instruments. Government agencies buy JGBs to park or administer their liquidity. This category known as Others in Table 31 has become a consistent and substantial net seller of bonds because JGBs issued by auction in the primary market are settled via the BOJ and reported as sales by the central bank

2. Intermediaries

Trading in the secondary bond market is dominated by bond dealers, such as securities companies and banks, for both proprietary purposes and client accounts.

City banks (large commercial banks) and trust banks trade large volumes of bonds. Based on their own market view, city banks vigorously engage in bond trading in pursuit of trading profits as well as resell municipal and other bonds underwritten by them. It should also be noted that trust banks have traditionally allocated large portions of assets under management or administration, including pension assets, to bonds.

3. Investors

Nonresident investors also play an increasingly significant role in the Japanese bond market through investments in JPY-denominated government bonds and notes, in line with the flight-to-quality movement after the global financial crisis. They are also active participants in the short-term JGB market, trading T-Bill.

Table 31: Bond Market Transactions by Type and Party (JPY billion)

Participant	Activity	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
City (commercial) banks	Sell (a)	80,125	92,172	79,387	75,391	120,557	129,292	126,905	146,494	213,866	237,881	110,436	147,606	81,791
	Purchase (b)	136,553	173,056	153,964	101,749	130,459	154,818	163,965	144,559	198,905	212,185	80,380	124,789	63,195
	Net (a)-(b)	-56,428	-80,884	-74,577	-26,358	-9,902	-25,527	-37,060	1,934	14,961	25,696	30,056	22,817	18,596
Regional banks	Sell (a)	14,001	10,980	10,442	9,814	15,104	13,657	16,535	18,641	21,994	27,934	18,352	21,591	16,843
	Purchase (b)	22,420	19,385	16,967	14,375	21,141	23,678	28,251	29,938	31,852	35,037	23,343	24,737	18,120
	Net (a)-(b)	-8,419	-8,406	-6,525	-4,561	-6,037	-10,021	-11,716	-11,297	-9,858	-7,103	-4,992	-3,146	-1,277
Trust banks	Sell (a)	68,158	69,171	77,368	84,376	100,520	80,563	82,886	92,597	84,088	73,769	58,476	62,415	51,299
	Purchase (b)	102,617	117,218	119,187	128,489	141,377	120,323	158,872	156,712	164,139	155,978	127,931	80,128	61,014
	Net (a)-(b)	-34,459	-48,047	-41,819	-44,113	-40,857	-39,760	-75,986	-64,115	-80,051	-82,208	-69,455	-17,713	-9,716
Agriculture-related banking institutions	Sell (a)	8,188	8,505	7,164	12,599	8,908	6,646	7,159	4,953	6,041	4,595	5,577	4,122	3,975
	Purchase (b)	19,517	12,008	12,959	14,377	9,231	20,007	37,145	44,972	29,241	29,342	13,855	9,365	7,379
	Net (a)-(b)	-11,328	-3,503	-5,796	-1,778	-323	-13,360	-29,986	-40,019	-23,200	-24,747	-8,278	-5,243	-3,404
2nd regional banks	Sell (a)	3,833	4,057	4,104	2,628	2,571	2,910	4,716	4,899	4,976	6,969	4,636	4,144	2,758
	Purchase (b)	5,451	5,435	5,232	3,191	5,007	5,444	7,563	6,958	6,665	7,981	5,335	4,610	2,935
	Net (a)-(b)	-1,618	-1,378	-1,128	-564	-2,436	-2,534	-2,846	-2,059	-1,689	-1,012	-699	-466	-177
Shinkin banks	Sell (a)	9,086	9,157	7,002	4,571	7,170	9,997	9,963	15,361	12,847	15,095	10,310	10,464	7,445
	Purchase (b)	15,909	17,940	24,217	15,279	26,889	30,588	31,911	28,825	19,343	22,422	15,452	14,147	9,429
	Net (a)-(b)	-6,824	-8,783	-17,216	-10,708	-19,719	-20,590	-21,947	-13,464	-6,496	-7,327	-5,142	-3,684	-1,985
Other banks and financial institutions	Sell (a)	41,274	18,830	16,404	19,375	26,341	22,250	12,586	11,642	15,796	8,753	7,353	9,916	6,955
	Purchase (b)	68,761	50,153	38,933	48,635	62,832	54,833	45,359	44,382	38,650	35,911	31,232	17,124	15,801
	Net (a)-(b)	-27,487	-31,323	-22,529	-29,259	-36,491	-32,583	-32,773	-32,740	-22,854	-27,158	-23,879	-7,208	-8,846
Life and property casualty insurance companies	Sell (a)	14,807	13,802	12,556	13,684	14,076	16,805	9,539	13,642	13,034	16,043	16,461	8,808	7,802
	Purchase (b)	19,879	22,515	20,255	22,090	23,485	29,140	26,968	28,216	31,418	33,299	30,778	19,060	12,871
	Net (a)-(b)	-5,072	-8,713	-7,698	-8,405	-9,409	-12,335	-17,429	-14,574	-18,384	-17,256	-14,317	-10,252	-5,070
Investment trusts	Sell (a)	7,140	5,828	4,338	5,529	6,210	7,108	4,833	4,615	3,792	4,081	5,486	6,037	8,159
	Purchase (b)	27,766	26,171	28,313	28,238	25,992	22,088	23,730	24,216	24,047	24,146	37,971	34,364	37,832
	Net (a)-(b)	-20,626	-20,343	-23,976	-22,709	-19,782	-14,981	-18,896	-19,601	-20,256	-20,065	-32,485	-28,328	-29,673
Public employees mutual aid associations	Sell (a)	794	1,529	1,631	1,288	877	880	612	515	604	410	320	327	397
	Purchase (b)	6,535	7,235	7,542	6,930	6,983	5,469	3,065	2,596	2,286	2,391	2,154	975	732
	Net (a)-(b)	-5,741	-5,706	-5,911	-5,642	-6,107	-4,589	-2,453	-2,081	-1,682	-1,981	-1,834	-649	-335
Business corporations	Sell (a)	906	647	1,033	935	851	1,133	255	494	403	445	1,007	298	316
	Purchase (b)	7,225	8,849	8,125	11,230	10,453	9,996	12,759	13,894	9,889	11,542	11,779	7,692	4,173
	Net (a)-(b)	-6,319	-8,203	-7,092	-10,295	-9,602	-8,862	-12,504	-13,400	-9,486	-11,097	-10,772	-7,394	-3,858

continued on next page

Table 31 continued

Participant	Activity	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Other corporations	Sell (a)	1,185	1,433	1,301	982	814	927	1,034	1,870	971	794	1,146	1,129	852
	Purchase (b)	4,598	4,652	5,334	7,659	6,240	5,929	5,626	6,162	6,171	5,503	6,954	7,272	4,291
	Net (a)-(b)	-3,413	-3,220	-4,033	-6,677	-5,426	-5,002	-4,591	-4,293	-5,200	-4,709	-5,808	-6,143	-3,439
Nonresident investors	Sell (a)	58,329	71,436	86,480	99,016	122,127	103,251	91,808	99,307	106,784	98,219	93,420	79,225	74,018
	Purchase (b)	82,909	110,803	119,945	149,582	180,207	185,088	176,542	211,437	247,878	256,141	249,621	275,329	288,052
	Net (a)-(b)	-24,580	-39,367	-33,465	-50,565	-58,079	-81,836	-84,734	-112,129	-141,094	-157,922	-156,201	-196,104	-214,034
Individuals	Sell (a)	621	610	471	328	303	322	492	629	524	506	429	495	533
	Purchase (b)	1,345	1,241	936	1,008	702	632	388	283	279	326	240	160	158
	Net (a)-(b)	-724	-632	-465	-681	-399	-310	104	345	245	180	189	335	375
Others (BOJ and government sector and related agencies)	Sell (a)	291,187	357,108	313,203	334,295	334,439	358,574	437,704	403,892	399,988	450,786	443,026	427,722	439,234
	Purchase (b)	114,136	118,786	110,883	123,337	114,014	99,983	95,594	97,911	92,812	135,468	178,022	176,691	191,608
	Net (a)-(b)	177,051	238,322	202,320	210,957	220,425	258,591	342,109	305,981	307,176	315,317	265,004	251,031	247,626
Bond dealers	Sell (a)	724,262	788,988	755,991	874,516	978,710	868,471	842,434	908,691	870,027	882,695	796,726	916,036	771,626
	Purchase (b)	724,235	785,890	753,012	872,644	974,208	870,291	844,919	905,541	866,349	870,711	787,733	914,969	767,399
	Net (a)-(b)	27	3,098	2,979	1,872	4,503	-1,820	-2,485	3,150	3,678	11,984	8,993	1,067	4,227
Total	Sell (a)	1,323,896	1,454,252	1,378,873	1,539,328	1,739,578	1,622,784	1,649,462	1,728,243	1,755,734	1,828,975	1,573,162	1,700,333	1,474,000
	Purchase (b)	1,359,855	1,481,338	1,425,804	1,548,812	1,739,219	1,638,304	1,662,656	1,746,602	1,769,924	1,838,381	1,602,782	1,711,411	1,484,989
	Net (a)-(b)	-35,960	-27,086	-46,931	-9,484	359	-15,520	-13,194	-18,359	-14,189	-9,406	-29,619	-11,079	-10,989

BOJ = Bank of Japan.

Notes: Data uses calendar year basis. Figures exclude *gensaki* transactions.Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryō/toukei/toushika/tkb/files/koushasaiichiran.xls>

B. Trading of Bonds and Notes on Exchange

The TSE and the Nagoya Stock Exchange (NSE) have bond trading facilities but very few listings, except for JGBs and convertible bonds. The trading volume on exchange, particularly of corporate bonds, is negligible. The OSE is the exchange specializing in derivatives under JPX. The OSE provides market facilities for conducting market derivative transactions, such as JGB futures trading and JGB options trading.

In turn, the TPBM will provide bond issuers with defined disclosure and a listing place for the profile listing of bonds and MTNs, which are aimed at Professional Investors and continue to be traded OTC.

C. Over-the-Counter Trading of Bonds and Notes

The OTC market is not a trading platform but an organized market nevertheless. Trades of bonds and notes are concluded directly between institutional counterparties via phone or using the services of a voice broker or inter-dealer broker (IDB), or through the use of a PTS (see next section for more details).

The majority of bond transactions in Japan—and in other markets—take place OTC rather than on exchanges; the secondary market is a dealer-driven market instead of being order-driven like on an exchange. A number of reasons contribute to this fact:

- (i) there are so many bond and note issues that it is practically impossible to list all of them on exchanges;
- (ii) due to the wide variety of types of transactions and other deal specifications that different buyers and sellers require, it is difficult to instantly locate a matching counterparty for a particular transaction;
- (iii) the tax on bond interest varies according to the tax profiles of bondholders; and
- (iv) corporate investors, who account for the bulk of the bond trading volume, tend to trade in large lots and often carry out complex transactions involving more than one issue.

Given these reasons, bond transactions do not lend themselves to trading on exchanges where the terms of transactions need to be standardized. Bonds are rather more effectively traded in the OTC market, where trades are executed based on the terms individually negotiated between buyers and sellers.

D. Proprietary Trading System for Fixed-Income Securities

1. Overview

The revision of the Securities Exchange Law in December 1998 led to the birth of the concept of the PTS. The FSA announced the PTS Guidelines in November 2000. According to the guidelines, although PTS operators are highly regulated by the FSA and are required to obtain approval for a PTS license, some entrepreneurs and innovators have launched electronic trading systems.

Unlike stock trading, bonds are traded mostly OTC and therefore the need for improving transparency, efficiency, and accuracy in trading is strong. It became stronger in the past

several years due to the increase in compliance and/or governance requirements. The advent of PTS was supposed to be ideal to enhance trading governance. In reality, however, the use of PTS has not been very successful in Japan; it still has a long way to go.

2. Inter-Dealer Broker and Broker-to-Customer Market

There are two types of PTS operators: broker-to-broker (B-to-B, or the IDB market) and broker-to-customer (B-to-C, the institutional investor market).

(a) Inter-Dealer Broker Market

The IDB market adopted the concept of PTS promptly. The main operator of the IDB market is the broker's broker, which in this case is Nihon Sogo Shoken (日本相互証券). Totan ICAP (東短ICAP) and Central Tanshi (セントラル短資) subsequently established PTS in the IDB market.

The B-to-B market has been active in e-trading and its PTS operation, while other brokers have been lagging somewhat behind. It is estimated that the broker's broker trades comprise 80% of the trading volume handled through PTS.

(b) Institutional Investor Market

The B-to-C market has developed in a very different manner from the IDB market. There have been two main facilitators in this market: JBOND (ジェイ・ボンド東短証券) and Yensai.com (エンサイドットコム証券). Please see section 4 for more details on these facilitators.

The FSA has encouraged asset management companies to adopt a trader system, in which dealers concentrate on dealing and fund managers focus on portfolio management. These FSA guidelines encourage dealers to use electronic trading (e-trading) more often. At the same time, due to increased compliance needs, investment management companies with fiduciary responsibility have been required to obtain several quotes before a trade is completed to ensure the best executions.

Investors have gradually shown increased interest in PTS platforms. Still, the combined share of all the PTS facilitators is estimated to be less than 5% of the JGB wholesale market. The JGB PTS market is still negligible in terms of trade volume.

(c) Inter-Dealer Broker versus Broker-to-Customer Market

As mentioned above, e-trading has grown in the IDB market in a short period of time, while the B-to-C market has demonstrated very slow growth. The reason for this is not clear, but it has been attributed to differences in trading attitude. Market makers want to know why investors are selling or buying in order to see where the market is heading. One of the important responsibilities of bond sellers is to find out investors' thinking and behavior. Thus, they call investors incessantly and provide the information back to dealers, which will be the basis for dealers in building up their positions. On the other hand, the IDB market is the place for squaring positions. The brokers' task is to match the trades. Therefore, telephone conversations are not very important in the IDB market. As brokers do not lose much by switching to e-trading, they did not resist the change much.

3. Pricing Method

The FSA's guidance provides four pricing methods:

- (i) **Market price-trading method** uses current prices and quotes on the stock exchanges.
- (ii) **Direct-negotiation method** uses a price negotiated between customers. It is often called negotiation method as sellers and buyers negotiate the price, volume, settlement date, and other conditions. As this method is similar to the way bonds are traded over the phone, all PTS operators in the B-to-C market have adopted this method.
- (iii) **Order-matching method** under the order-matching method orders from customers are matched with each other. A trade is done when an order from a buyer and a seller is matched. PTS operators provide the screen where buyers and sellers put in their orders. Counterparties who wish to trade will click orders and trades are done. As the monitor screens are similar to the ones that IDBs use, IDB PTS operators use this method. The JBOND Repo System also adopted this method.
- (iv) **Quote-driven method** market makers show their quotes and stand ready to trade with customers. It is often called the market-making method. Market makers show their bids and offers for bonds they wish to trade. They are not obliged to show the quotes for all the bonds and, in the case of Yensai.com, securities dealers must confirm the trade before it is done. Therefore, this click-and-trade quote-driven method is not popular among institutional investors.

For bonds traded via PTS, only the pricing methods (ii)–(iv) are applicable.

4. Facilitators

(a) *Yensai.com* (エンサイドットコム証券)

Yensai.com was founded by seven major securities dealers in January 2001, following the business model of TradeWeb (トレードウェブ・ヨーロッパ証券), and started its PTS operations upon receipt of its PTS license in March 2002. It is differentiated from other PTS facilitators among major Japanese market makers. It provides two types of trading methods: a real-time order system (quote-driven system) and an inquiry system (order-driven system). The real-time order system shows all the bids and offers for JGBs with tradable amounts on the side. This click-and-trade system looked handy and attractive, but in reality, the usage has been pretty limited. Most users look at the monitor screen to find out the current yield curve, and not to do trades. As securities dealers did not feed the best prices, investors used the bid-offer prices as indication.

The order-driven system, on the other hand, has been relatively successful. Currently, there are 13 securities dealers who participate as market makers for all interest-bearing JGBs.

(b) *JBOND* (ジェイ・ボンド東短証券)

JBOND was founded in April 2000. It started operation in June 2001 as a quotes comparison site. JBOND became a securities company in September 2002, received its PTS license in October 2002, and began PTS operations in November 2002. It

started its repo PTS in October 2009. Its participating market makers were mainly foreign banks.

JBOND shifted its focus from outright JGB trades to the JGB repo market in June 2010. It is the first and only PTS player for repo e-trading. Its users are limited to the Japan Government Bond Clearing Corporation members. It is still too early to determine if it will take off in Japan. The broker's broker runs a similar system but it does not operate as a PTS.

(c) *TradeWeb* (トレードウェブ・ヨーロッパ証券)

TradeWeb, a dominant player in Europe and the US, was slow to enter the Japanese market. It was founded in 2004, received its PTS license in 2005 to trade foreign bonds, and started trading Japanese bonds in 2008. About 10 broker-dealers are participating but their activities are rather limited.

(d) *Bloomberg*

Bloomberg also has a PTS license but its system is a gateway to lead an inquiry into a certain broker-dealer and is not regarded as a fully-fledged multi-dealer system provider and does not have significant influence in the market.

E. Publication of Reference Statistical Prices for Over-the-Counter Bond Trading

1. Historical Background

With a view to providing investors, securities companies, and other stakeholders in Japanese bond markets with updated bond market price information, the JSDA instituted the system for publishing the Reference Statistical Prices (Yields) for OTC Bond Transactions. Under this system, the JSDA receives the quotation information from a certain number of designated reporting members (securities companies and banks) and publishes the average price, median price, and highest and lowest prices (each price representing the midpoint of ask and bid prices that the designated reporting members intend to quote) in each issue of publicly offered public sector and corporate bonds that meet certain criteria.

The program was originally instituted in August 1965 by the Bond Underwriters Association of Japan for publishing OTC Quotes for Industrial Debentures and was succeeded by the Tokyo Securities Dealers Association, the predecessor of the JSDA, which began the publication of OTC Quotes for Public and Corporate Bonds in March 1966. The initiatives were implemented with a backdrop of social necessity to promote the formation of fair prices and efficient and orderly trading of JGBs, issuance of which had been resumed after World War II. The program has since undergone many changes and improvements in response to the changing environment surrounding the bond market. During that period, the number of published issues has ballooned from about 300 when the system was introduced, to approximately 8,200 as of December 2015.

In August 2002, the JSDA changed the name of the data to “reference prices (yields)” from “standard quotes” with the intent to clearly indicate that it was for reference purposes only. At the same time, the program was enhanced by publishing, as mentioned above, “high, low,

and median values of surveyed quotes” in addition to their averages, which were the only data previously published. That system continues today.

The program started publishing bond quotes nearly 50 years ago, and it is fair to say that it has since made measurable contributions by providing benchmark prices for OTC bond trading in Japan. The use of data is no longer limited to price references for trading bonds but serves a wide variety of public purposes, including mark-to-market valuation for financial reporting and tax accounting purposes, and the valuation of collateral for different types of transactions.

2. Challenges of the Past Dissemination System for Bond Price Information and Necessity for Further Improvement of its Infrastructure

As mentioned earlier, the JSDA manages the system of Reference Statistical Prices (Yields) for OTC Bond Transactions (hereinafter referred to as Reference Prices) as an infrastructure for public and corporate bond pricing information. The Reference Prices system is widely used by investors and market participants, and is indispensable infrastructure in the financial and securities markets. For example, Reference Prices are used as a reference purchase or sell price of a bond, for the fair value appraisal as a pledge, for the calculation of a base price of investment trusts, and as a reference price and indicator at the time of pricing of bonds to be newly issued.

However, as the Reference Prices sometimes diverges from the actual price, such as the execution price and the bid offer, and there is a time lag, the system needs to be reviewed and improved.

The JSDA and market participants have been improving the current system based on the cases witnessed in the Republic of Korea, United Kingdom, and US to improve the transparency of bond price information and build up the credibility of the information.

The JSDA did not have access to actual price data information on a daily basis at the time. However, in the deliberations of the Study Group to Vitalize the Corporate Bond Market it was judged that, in light of practices conducted in many other markets in ASEAN+3, actual traded price information would be more useful as a source of bond price dissemination.

3. Introduction of New Measures since January 2014

Following the conclusions of the deliberations of the above-stated study group and its succeeding Working Group,⁴⁹ the JSDA decided to introduce two fundamental measures to improve its pricing concept:

(a) *Improvement of Credibility and Accuracy of the Reference Price*

As implemented with effect from 1 January 2014

- (i) Designated reporting members shall be required not to take any action that would damage the adequacy or fairness of quotes such as making a prior exchange of information or adjustment of the level of quotes to be reported to JSDA with any other designated reporting member(s).

⁴⁹ See JSDA Working Group Discussion (in Japanese). <http://www.jsda.or.jp/katsudou/kaigi/jisyukisei/gijigaiyou/syasaiinhura.html> (in Japanese).

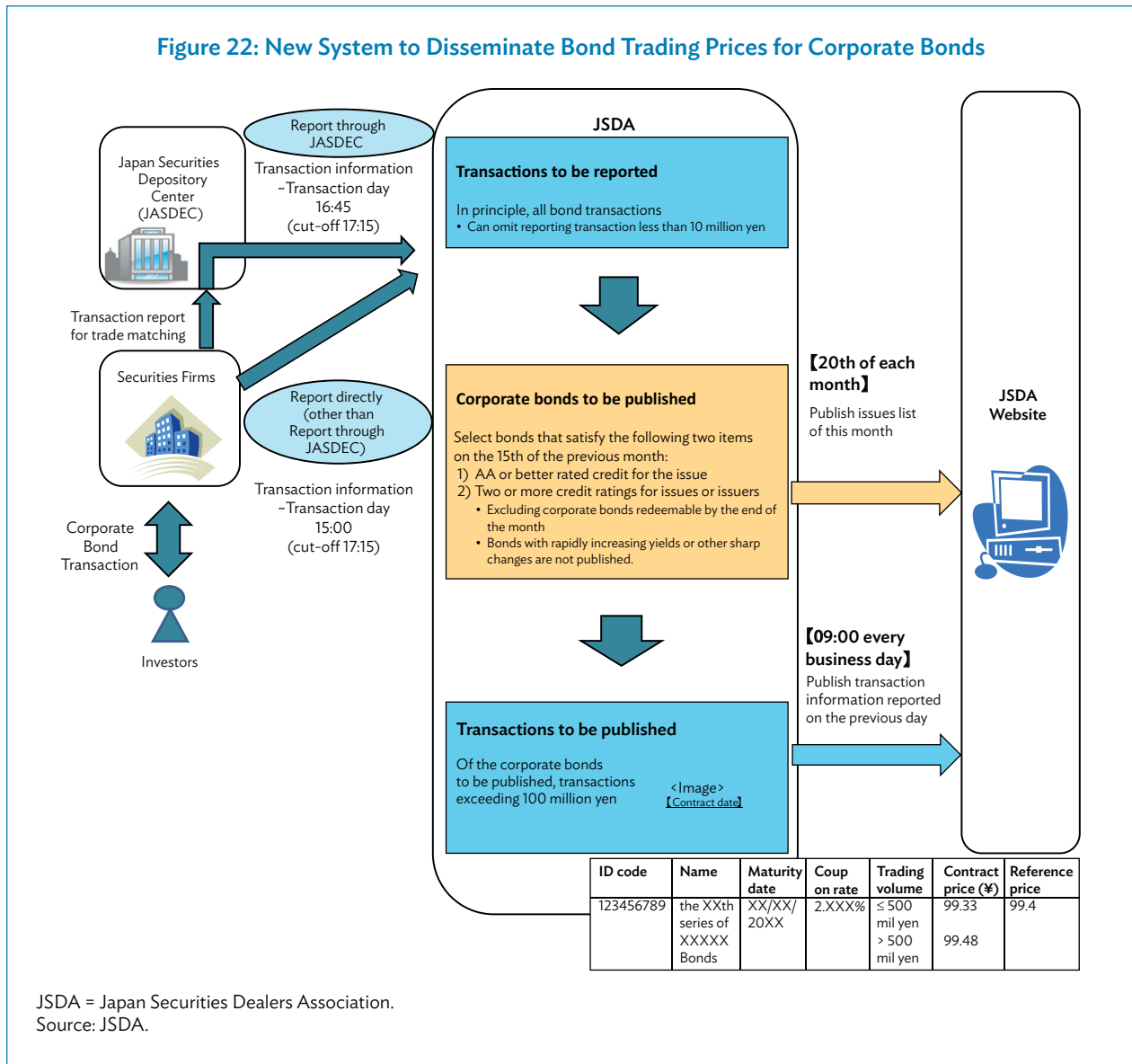
As implemented with effect from 2 November 2015

- (ii) The deadline by which designated reporting members are required to report their quotes on corporate bonds, specific corporate bonds, and Samurai Bonds (hereinafter referred to as “corporate bonds, etc.”) will be moved to 5:45 p.m. from 4:30 p.m. previously, while the deadline for other bonds will remain the same (4:30 p.m.). It is also expected that the JSDA’s publication timing for quotes of corporate bonds, etc. will be moved to 6:30 p.m. from 5:30 p.m., while that of other bonds will remain unchanged. This measure was introduced for the purpose of facilitating participation of Association Members (e.g., Association Members with a high share of trading turnover, lead-managing firms) that are able to report appropriate quotes regarding a wide range of issues.
- (iii) The standards for becoming and remaining a designated reporting member were changed. Designated reporting members will now also be required to have corporate bonds, etc. trade turnover ranking among the top 20 member firms except in the case of lead-managing firms that can make quotes for their lead-managing issues.
- (iv) The JSDA will check daily reported quotes and reporting system of designated reporting firms.
- (v) Outlying figures will not be excluded in calculating Reference Prices for corporate bonds, etc. Average, median, highest, and lowest prices shall be calculated using all of the reported figures.

(b) *Introduction of Reporting and Publication System for Traded Prices of Corporate Bonds, with Effect from 2 November 2015*

Based on the thought that enhancing transparency and maintaining credibility of bond price information by publishing actual traded corporate bonds prices is crucial to activating the corporate bond market, the JSDA has created a reporting and publication system for actual traded prices of corporate bonds that satisfy the rating criteria (AA rated or more) with trading size exceeding JPY100 million. Under this system, which is illustrated in Figure 22, the transaction information will be reported to the JSDA through its member firms, the JASDEC, within the transaction day and the executed prices and other related information—contract dates, ISIN codes, names of bond issues, maturity dates, coupon rates, and trading volumes—will be publicly disseminated on the JSDA website at 9 a.m. on the following business day.

Figure 22: New System to Disseminate Bond Trading Prices for Corporate Bonds

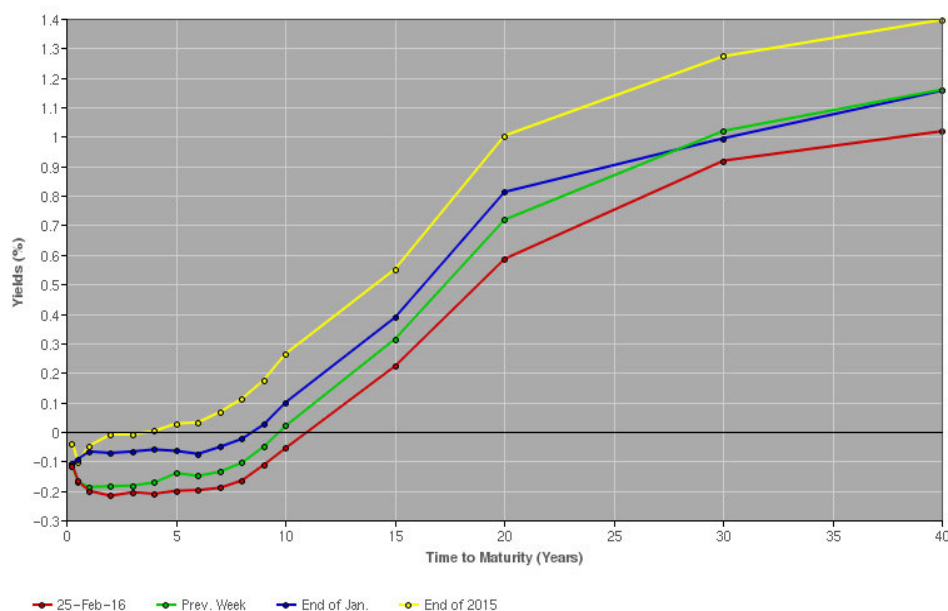


F. Secondary Market Yields and Bond Indexes

1. Secondary Market Yield Curves

Since bond yield information is a significant piece of information for secondary market trading, government bond and corporate bond yields are not displayed on the websites of the regulatory authorities in Japan. Instead, information on JGB yields and corporate bond yields is widely available from securities firms and commercial data providers such as Bloomberg. At the same time, JGB yields are provided as part of a larger offering of Japanese bond market statistics by *AsianBondsOnline*, an initiative of ADB under ASEAN+3. Figure 23 gives an example of a recent image from *AsianBondsOnline* of yield curves for a selected period.

Figure 23: Japanese Government Bond Yield Curve for Selected Periods on AsianBondsOnline



Source: AsianBondsOnline. https://asianbondsonline.adb.org/japan/data/marketwatch.php?code=government_bond_yields

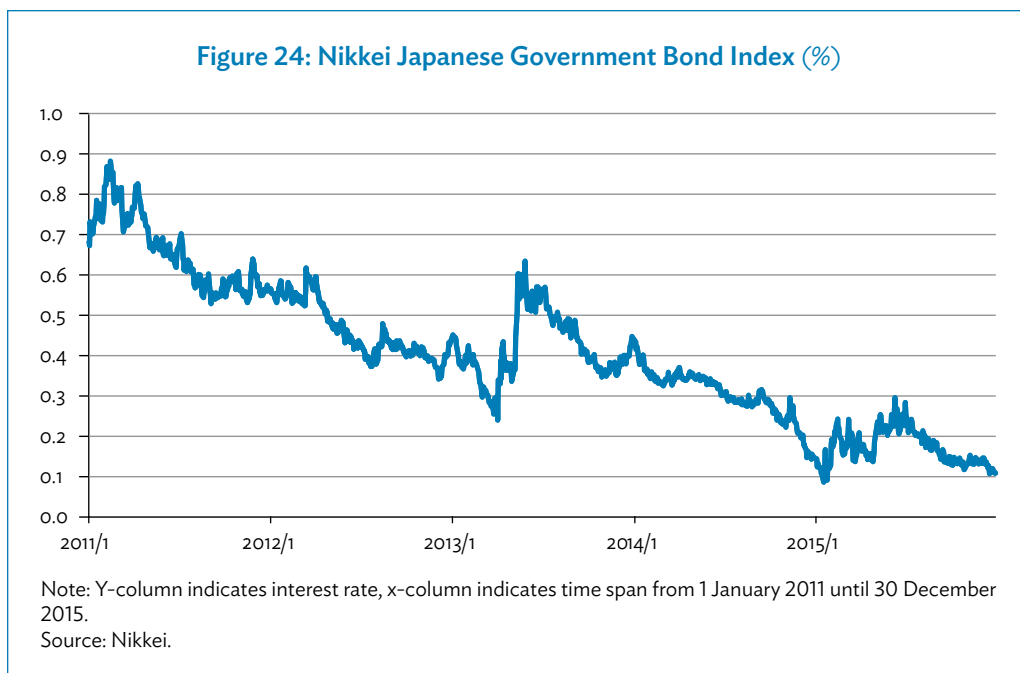
2. Bond Indexes

Nikkei has been providing the Nikkei JGB Index since October 1995 and publishes the index in the morning edition of the Nikkei daily newspaper.⁵⁰ Figure 24 gives an illustration of the yield tracking available in the Nikkei JGB Index.

Nikkei also provides the Nikkei Bond Index, which represents the overall bond market movement (compound average yield), broken down into three subindexes classified according to the remaining period to maturity: (i) long-term (maturity equal to or more than 7 years), (ii) medium-term (maturity equal to or more than 3 years but less than 7 years), and (iii) short-term (maturity less than 3 years). The prices used for the index calculation are taken from the Reference Statistical Prices (Yields) for OTC Bond Transactions provided by the JSDA. The Nikkei Bond Index has been calculated since January 1979 and also appears in the morning edition of the Nikkei daily newspaper.⁵¹

⁵⁰ Nikkei JGB Index Fact Sheet. http://indexes.nikkei.co.jp/nkave/archives/file/nikkei_jgb_index_factsheet_en.pdf

⁵¹ Nikkei Bond Index Fact Sheet. http://indexes.nikkei.co.jp/nkave/archives/file/nikkei_bond_index_factsheet_en.pdf



G. Repurchase (*Gensaki*) Market for Bonds

Japan's repo market consists of (i) bond borrowing and lending transaction, which is the borrowing and lending of bonds with cash as collateral; usually known as the repo market in Japan; and (ii) *gensaki* transactions, which are the combination of sale and purchase transactions for bonds; in effect, the equivalent of the more typical repo transactions practiced in the US and other ASEAN+3 markets.

Historically, *gensaki* transactions were subject to a securities transaction tax; however, this has since been abolished. In order to avoid such taxation, the cash collateralized bond borrowing and lending transaction was conceived as an alternative and has become known as Japan's repo, or cash collateralized repo, transaction.

Japan's repo transactions expanded after the turmoil in Japanese financial markets surrounding the Asian financial crisis because of its suitability for risk management and adoption of new means of financial adjustment by the BOJ in 1997. The replacement of the conventional *gensaki* market as a means of fundraising (mainly for securities companies) has been recognized by investors as a safer means of fund management.

The features of the cash collateralized repo in the form of bond borrowing and lending transactions are unique to Japan. In April 2001, the new *gensaki* transactions that utilize a form of the sale and purchase transaction method based on the global standard were introduced. However, these transactions are not currently popular because the cash collateralized repo market had already established a solid position in the money market before the new *gensaki* market started. Currently, *gensaki* transaction volume is significantly less than that for cash collateralized repo transactions. As of now, the overall market size remains at JPY20 trillion (Figure 25) and the expected shift from the cash collateralized repo market has been limited.

For the purpose of describing the traditional repo business as it is conducted in Japan, this section will focus on the *gensaki* transaction and the market it occupies.

1. Overview of *Gensaki* Market

Repurchase transactions, also called “conditional sale and purchase of bonds, etc.,” or more customarily referred to as *gensaki* transactions in the Japanese market, are bond transactions where the parties agree at the time of trading to execute offsetting trades of the same type and volume of bonds at a predetermined date and price. In *gensaki* transactions, there are brokered *gensaki*, in which a Financial Instruments Business Operator acts as broker between a seller that wants to raise funds and a purchaser that wants to invest funds, and there are dealer *gensaki*, in which the Financial Instruments Business Operator itself becomes the seller or the purchaser. Normally, purchases conditioned on their sellback are called a *gensaki* buy transaction (*kai gensaki*) and sales conditioned on their buyback are called a *gensaki* sell transaction (*uri gensaki*).

Gensaki transactions are bond transactions in which the seller and purchaser mutually agree to fix the yield for the period in a way that is completely unrelated to market fluctuations. While they assume the form of bond trades, *gensaki* are actually a system to fix the yield for a certain period through a combination of interest and the difference between the initial trading price and the offsetting trading price. *Gensaki* transactions also possess the characteristics of financing transactions with bonds as collateral.

In the past, the majority of *gensaki* transactions were for short-term government securities (Treasury Bills and Financing Bills). Despite intensifying competition with other increasingly diversified money market instruments, these government bills have dominated the *gensaki* market, as the bills, which have maturities and credit quality more suitable for *gensaki* transactions, are being increasingly issued to the public.

Although the *gensaki* market developed against the backdrop of this expansion of the short-term government securities market, interest-bearing JGBs have taken center stage since late 1990s, partially because of the massive overall issuance of government bonds. In an effort to modernize and strengthen the international competitiveness of Japan’s money market, the *gensaki* market underwent reforms to improve its functions as a repo market that meets the needs for both short-term financing and bond borrowing, and thus were called “new *gensaki* transactions” starting from April 2001. Up to that point, *gensaki* transactions were bought and sold much like the transactions commonly known as repo trades in Europe and the US but had various shortcomings that necessitated reform. In particular, the *gensaki* market did not have functional risk management facilities or standard rules for dealing with counterparty default. Through these reforms, new measures were instituted and existing provisions were enhanced for risk management and other purposes, establishing the *gensaki* market in accordance with global standards. The newly introduced provisions for risk management and other purposes (clauses in the repo agreement) can be summed up as follows:

(a) Risk Control Clause

The amount of collateral (bonds) shall be adjusted flexibly so as not to cause a shortage of collaterals on account of a fall in the price of bonds submitted as collateral.

- (i) **Application of the Ratio for Computing the Purchase or Sale Value of Bonds (Haircut Clause).** Under this clause, the unit price of bonds (collateral) on the basis of which a repurchase agreement is concluded

is fixed at a level that is a certain percentage point lower than the price prevailing at the time the repurchase agreement is concluded. This is done so that the value of the collateral will not be affected even when the market price of the underlying bonds falls.

- (ii) **Introduction of Management of Collateral (Margin Call Clause).** Under this clause, when the market value of the underlying bonds changes during the period of the repurchase agreement, the amount of credit extended to a party to the repurchase agreement is maintained by adjusting the collateral.
- (iii) **Introduction of the Re-pricing System.** In instances when the market price of the underlying bonds falls sharply from the prevailing market price at the time of the repurchase agreement, the parties to the agreement agree to cancel the agreement and renegotiate a new agreement on the basis of a price then prevailing, on terms and conditions identical to those of the agreement thus canceled.

(b) *Substitution of Underlying Bonds*

Under this clause, the seller of bonds can replace the underlying bonds with other bonds with the consent of the buyer, allowing the seller to use the underlying bonds, if necessary.

(c) *Institution of Netting-Out System*

If the other party goes into default for any reason, such as through bankruptcy, the value of all transactions covered by the agreement will be reassessed based on market prices, and the difference between claims and obligations will be settled.

Gensaki agreements can also be concluded for commercial paper, certificates of deposit, and commercial paper issued overseas. As *gensaki* transactions conveniently meet the short-term funding and cash management needs of investors, their trading volume increased steadily, thanks particularly to the adoption of the new *gensaki* regime by the BOJ for its money market operations. However, recently, the *gensaki* transaction volume has remained stagnant due to the wider use of the cash collateralized repo transaction type that developed historically in Japan.

2. Acceptance of Standards

Under the *gensaki* regime, participants may rely, as an option, on the Global Master Repurchase Agreement provided by the International Capital Market Association.

As the SRO for securities market participants, the JSDA prescribes the rules for the short selling and borrowing and lending transactions of bonds, conclusion of borrowing and lending the transactions of bonds, scope of eligible bonds, and trading method with regard to OTC repo. JSDA also provides sample formats for the Master Agreement of Borrowing and Lending Transactions of Bonds and the consent letter to the Master Agreement of Borrowing and Lending Transactions of Bonds.

The Master Agreement must be executed in advance with the counterparty and the following items must be included: the method of concluding an individual agreement of borrowing and lending of bonds; the payment method for the borrowing fee; the delivery method for the bonds; receipt for collateral money; payment method in the case of foreign

currency; transfer of rights and its pledging; treatment of interests of bonds subject to borrowing and lending transactions; and, lastly, measures for dealing with insolvency.

3. Specific Repo Practices

This section summarizes a number of relevant practices in the repo market in Japan.

The JSDA provides the basic trading framework, rules, and other market practices with the consensus of market participants. In addition, the BOJ regulates the market to a certain extent, being the settlement organization for JGBs.

(a) Types of Repo

In Japan, there are different types of repo transactions within *gensaki*, namely the Special Collateral transactions, which target a specific bond issue, focusing on the borrowing and lending transaction rather than on the financial transaction. The General Collateral transactions do not specify a bond issue and focus on the financial transaction, actually functioning as fundraising tools using the bonds as collateral.

The BOJ is also conducting repo transactions as part of its open market operations.

The introduction of tri-party repo in the context of *gensaki* transactions is presently being discussed in the market, with the idea of a central clearing institutions being mooted.

(b) Eligible Securities

Eligible securities for repo transactions include short-term government securities such as Treasury Discount Bills (Treasury Bills and Financing Bills, collectively T-Bill), coupon-bearing JGBs, commercial paper, certificates of deposit, and commercial paper issued overseas.

(c) Margin

In principle, initial margin and variation margin apply to repo transactions in Japan. At the same time, as most of the *gensaki* transactions involve JGBs, which are considered risk-free collateral in Japan, the haircut for JGB transactions is effectively zero.

(d) Accounting and Tax Treatment

The classic repo, such as the *gensaki* transactions, combines the spot selling and forward buying of bonds or notes, typically in a single contract. A transfer of ownership takes place through the transaction.

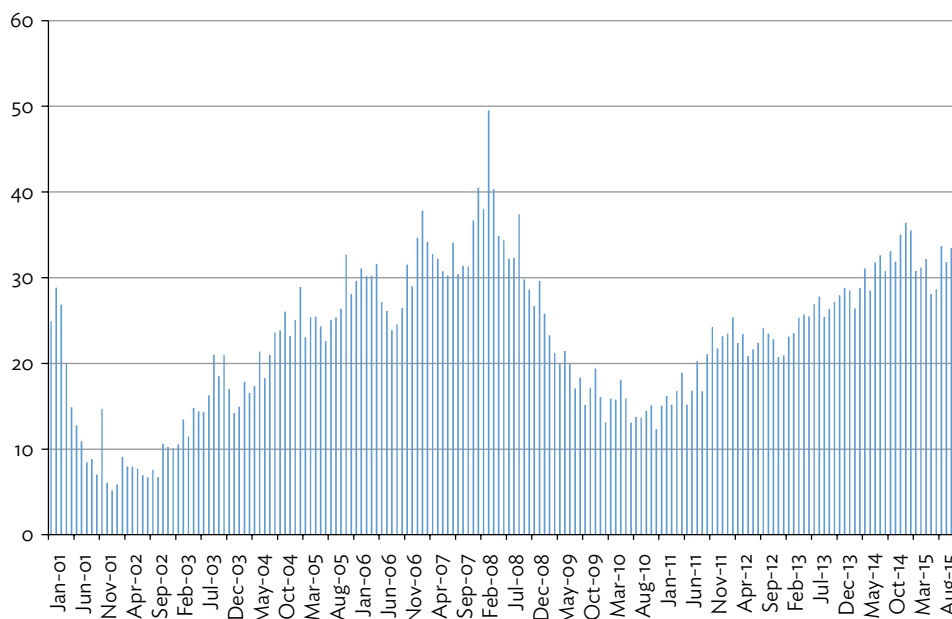
Gensaki transactions are no longer subject to transaction tax (removed in 1999), but are subject to stamp duty. The bond buyer is not subject to withholding tax, but capital gains from the resale of the bonds are subject to corporate tax. Coupon payments arising from holding bonds during a repo transaction are taxable on the basis of applicable corporate tax, but tax exempt for nonresident investors.

(e) Market Participants

Market participants include both domestic and overseas institutional investors, as well as large corporations with their own treasury operations. The main liquidity providers in the repo market are the BOJ, through its open market operations, and typically institutional investors in a surplus position who provide liquidity to investors short of funds but with eligible securities holdings.

Foreign institutional investors may participate in the repo market in Japan, but have to make use of a domestic intermediary to access the market.

Figure 25: End-of-Month Balances of Bond Transactions with Repurchase Agreements (JPY trillion)



Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryō/toukei/jyouken/files/gst.xls>

H. Bond Borrowing and Lending

When investors have shorted bonds (or sold bonds that they do not own) and failed to buy them back before the settlement date, they turn to bond lending services to borrow bonds to deliver. Such transactions are also known as *saiken* repo (bond repo) in Japan. For the purposes of this type of transactions, the use of bonds and notes is just referred to as bond lending.

When cash is used as collateral, bond lending is economically equivalent to *gensaki* transactions. Since market participants can obtain bonds through bond lending facilities after trades are consummated, they can sell bonds that they do not own (sell short) when

they feel that the bond market is too expensive or particular issues are overvalued. Such operations contribute to greater liquidity in the market.

Bond lending was instituted by legislation in 1989, following the lifting of the practical ban on bond short selling. In fear of potential effects on the financial health of brokers and dealers and bond pricing, market participants had previously been requested to refrain from selling bonds short. The ban, however, was lifted to help encourage active market making in cash bonds, and arbitrage between cash bonds and futures, and bond borrowing and lending was introduced as one of the means to locate bonds to deliver.

Initially, cash-collateral bond borrowing and lending was restricted in light of potential conflicts with the *gensaki* market and other considerations and, subsequently, most transactions were uncollateralized. However, with credit fears rising, the bond lending market remained stagnant, and cash collateral bond borrowing and lending transactions were effectively deregulated in 1996 to invigorate the market.

When viewed from a legal standpoint, a bond lending transaction is deemed to be a contract for a loan for consumption—a borrower borrows bonds for the purpose of consumption and, when due, the borrower has only to return bonds identical in kind and quantity to those originally borrowed.

Bond lending transactions may be broadly classified into unsecured transactions and secured transactions depending on whether they are collateralized or not. Secured bond lending transactions may be further divided into cash-collateralized transactions and securities-collateralized transactions by the type of collateral being pledged. Cash-collateralized transactions used to borrow specific bond issues are called specified collateral *torihiki* (specified collateral trades), while those for financing and cash management without such specification are termed general collateral *torihiki* (general collateral trades).

The size of the bond lending market (in terms of the balance of outstanding loans) has generally been growing since cash-collateralized transactions were deregulated in 1996. The market has grown from approximately JPY30 trillion at the end of FY1996, including approximately JPY17 trillion in cash-collateralized transactions, to JPY106 trillion at the end of FY2008, including approximately JPY97 trillion in cash-collateralized transactions. After the global financial crisis, the balance has taken time to reach the same levels and was at JPY104 trillion at the end of May 2014, including approximately JPY101 trillion in cash-collateralized transactions. The breakdown of institutions engaged in bond lending transactions is shown in Table 32. The majority of bond lending transactions are conducted with government securities.

I. Bond Market-Related Derivatives

In Japan, investor can trade bond futures and bond options. Short-term interest rate futures were discontinued in 1998. JGB futures and options on JGB futures are currently traded on OSE under the JPX Group.

In Europe and the US, where options trading has long been conducted, investors are quite familiar with the relevant system. However, in Japan, investors utilize options trading less often than futures trading. Particularly, the amount of trading in options on 10-year JGB futures is far smaller than that of 10-year JGB futures trading.

Table 32: Bond Lending Balances (JPY billion)

Market Participants	Borrowing Balance	Lending Balance
City banks	5,900	960
Regional banks	1,082	45
Trust banks	27,772	17,612
Financial institutions for agriculture and forestry	1,222	4
Second-tier regional banks	337	0
Shinkin banks	460	100
Other financial institutions	14,994	7,706
Life and non-life insurance	4,161	491
Investment trust	0	639
Mutual aid associations of government offices	0	0
Business corporations	24	10
Other organizations	0	10
Nonresidents	167	204
Others	12,593	19,287
Bond dealers	35,410	57,054
Total	104,122	104,122
Collateralized portion	101,233	101,233

Notes:

1 Figures are as of 31 May 2014, based on reports by all members of the Japan Securities Dealers Association.

2 Trading in financial accounts is not included.

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/shiryō/toukei/taishaku/files/tst/tst.xls>

Table 33: Bond Market-Related Derivatives Products on the Osaka Exchange

Underlying JGB	Related Derivatives
Standardized 3%, 5-year JGB	5-year JGB futures
Standardized 6%, 10-year JGB	10-year JGB futures
	Options on JGB futures
Price of standardized 6%, 10-year JGB	Mini-10-year JGB futures
Standardized 3%, 20-year JGB	20-year JGB futures

JGB = Japanese Government Bond.

Source: Japan Exchange Group. <http://www.jpx.co.jp/english/derivatives/products/jgb/index.html>; <http://www.jpx.co.jp/english/derivatives/products/jgb/jgb-futures/01.html>; <http://www.jpx.co.jp/english/derivatives/products/jgb/jgbf-options/01.html>; <http://www.jpx.co.jp/english/derivatives/products/jgb/mini-jgb-futures/01.html>

This section details some of the available derivatives related to the bond market in Japan and their characteristics.

1. Japanese Government Bond Futures

Trading in 10-year JGB futures was introduced on TSE in 1985—the year in which JGBs were issued in massive amounts—representing the first financial futures trading in Japan.

In 1988, super-long 20-year JGB futures—which were discontinued in 2002 before trading resumed in 2014 on the OSE—were listed on the TSE. With the trading in 5-year JGB futures starting on the TSE in 1996, Japan had finally developed a futures product mix comparable to that of other developed economies.

The OSE still offers these three types of JGB futures contracts. In addition, the OSE also offers a contract of mini-10-year JGB futures.

2. Futures Market Characteristics

All the bond futures have been traded on the OSE since 2014.

One of the characteristics of the bond futures market of Japan is that trading is concentrated in 10-year JGB futures. This reflects the fact that the maturities of government bonds are heavily concentrated in 10-year issues, as with cash bond trading, which is not unique to the bond futures market.

Another specific feature of the bond futures trading in Japan, in particular compared to other mature markets, is that a trading unit has a par value of JPY100 million, about 10 times as large as trading units in other markets. Due to the large unit size, the number of bond future contracts traded tends to be smaller.

Since the mid-1990s, however, the concentration of cash-based JGB trading on the benchmark issue, which was a phenomenon peculiar to Japan, has eased. Since the end of March 1999, the practice of designating a certain JGB as a benchmark issue has been discontinued, with 10-year JGB futures assuming the role played by such benchmark issues.

In addition, a futures type known as contract-for-difference was introduced on mini-10-year JGB futures, which are one-tenth the amount of normal 10-year JGB futures, and have been listed on the TSE since the end of March 2009. This sought to address the original larger unit size of bond futures contracts, but its trading has remained at less than 1% of 10-year JGB futures overall.

3. Options on Japanese Government Bond Futures

In Japan, the first bond options trading was conducted on the OTC market under the name of “trading in bonds with options” in April 1989. Trading in options on 10-year JGB futures started in 1990, and trading in options on 5-year JGB futures commenced in 2000—before being discontinued in 2002—both on the TSE.

At present, the OSE, which is part of the JPX Group, only offers one option contract on 10-year JGB futures.

4. Bond Options Market Characteristics

Options on bond futures are traded on the OSE or in the OTC market.

Unlike bond futures trading, which are conducted on the basis of a benchmark issue, OTC bond options are traded on the basis of individual issues, such as JGBs, corporate bonds, or foreign bonds. Because they are traded on the OTC market, bond options agreements cannot be assigned to a third party (most of the transactions are for JGBs).

As with JGB futures trading, bond options are traded in units with a par value of JPY100 million. Because their life (from the date of contract to the date of delivery) is restricted to a maximum period of 1 year, and as they cannot be resold to a third party, contracts usually run a relatively long period—6 months or 1 year.

By contrast, options on 10-year JGBs futures are available in the form of OSE-listed American options (the option can be exercised any day during its life), and their trading mechanism is similar to that of 10-year JGB futures. While 10-year JGB futures have only three contract months with a maximum period of 9 months, options on 10-year JGB futures offer up to 4 contract months with a maximum period of 6 months. In addition, compared with OTC bond options, transactions in 10-year JGB futures and options on 10-year JGB futures are concentrated in those with a short remaining life.



Description of the Securities Settlement System

This chapter, as included in the original ASEAN+3 Bond Market Guide published in 2012, has been discontinued in favor of a more comprehensive and updated description in the Phase 2 Report of ABMF Sub-Forum 2 (SF2), Information on Transaction Flows and Settlement Infrastructures, dated 13 June 2014. The SF2 Phase 2 report contains information on the post-trade features of the Japan bond market, its market infrastructure and settlement system, interest payment and redemption practices, as well as market and message standards (pp. 134–156). In addition, the SF2 Phase 2 report contains detailed infrastructure and flow diagrams for Japan (pp. 423–448).

The SF2 report is available at www.asianbondsonline.adb.org as well as through a number of mirror sites.⁵²

⁵² See <http://www.adb.org/publications/asean3-information-transaction-flows-and-settlement-infrastructures>

Bond Market-Related Costs and Taxation

This chapter details the typical costs incurred by issuers and investors in the Japan bond market, with a particular emphasis on costs associated with bond and note issuance and settlement.

For ease of reference, the descriptions of the types of costs are given in the context of the actions to be taken by issuers or investors (as explained in this document), and follow the life cycle of a bond or note in the Japan bond market.

A. Costs Associated with Bond and Note Issuance

1. Filing of Securities Registration Statement and Other Statutory Documents

All bond and note issuances via a public offering in Japan require the filing of an SRS or SR with the FSA through EDINET via the Local Finance Bureau (e.g., the Kanto Finance Bureau if bonds or notes are to be issued in Tokyo) of the MOF. For details and conditions of the application and filing process, please refer to Chapter II.G.

In Japan, no filing fee for the SRS and other statutory documents (such as the SR, or documents for incorporation) is charged by the FSA. This also applies to nonresident issuers of Samurai Bonds.

2. Standard Underwriting Fee Schedule for Public Offering Bonds

Public offers of bonds and notes in Japan often feature the creating of an underwriting syndicate. Table 34 details the market-typical fees charged by these underwriters for their service in issuing corporate bonds via a public offering in Japan.

3. Standard Fiscal Agent Fee

Table 35 provides the standard fees—tiered according to maturity—charged by fiscal agents for their services to an issuer of a corporate bond issued via a public offering in Japan.

Table 34: Standard Underwriting Fee Schedule for a Public Offering of Bonds
(basis points)

Maturity ^a	Subsovereign and Agencies	Corporate	
		Prime	Standard
2 years	12.5 ^b	12.5 ^b	30.0
3 years	17.5	17.5	35.0
5 years	22.5	22.5	40.0
7 years	27.5	27.5	40.0
10 years	30.0	30.0	45.0
12 years	30.0	30.0	45.0
15 years	35.0	35.0	50.0
30 years	47.5	47.5	^c

^a Gross fee consists of management fee (5) + underwriting fee (5) + selling concession (= total gross fee less management fee and underwriting fee).

^b Exception to 2-year maturity; SSA and prime issuers may get cap on total amount of management fee, which may result in the actual gross fee fall to a range of 10.8–11.5 bps.

^c Fee not easily available; due to long date maturity feature, few investors may have appetite for buying a 30-year nonprime issuer's bonds.

Source: ABMF-J member.

Table 35: Standard Fiscal Agent Fee for a Public Offering of Corporate Bonds

Maturity	Total Payable Amount for a JPY10 Billion Bond
3 years	JPY12 million
5 years	JPY13 million
7 years	JPY14 million

Source: ABMF-J member.

4. Legal Fees (optional)

In the event of a domestic issuance of bonds or notes in Japan, the arranger (lead underwriter) of the bonds or notes will support the issuer in raising the necessary documentation, as part of their service provision. As such, no separate legal fees would be incurred in this instance.

However, in case of a nonresident issuer issuing Samurai Bonds, it is common practice for a Japanese law firm to be appointed to help raise the necessary Japanese documents and corresponding versions translated into English. In turn, the securities firm(s) that are participating in the deal will typically only review the documents when actual issuance transactions are imminent. Such legal fees are based on time and effort spent, and are typically not disclosed in the public domain.

B. Ongoing Costs (Agent Fees) for Issuers of Corporate Bonds and Notes, and Commercial Paper

Fees to the Fiscal Agent, Paying Agent, and Other Agents

Table 36 gives an overview of the various ongoing service fees charged by the agents typically servicing a corporate bond or note, or commercial paper—the fiscal agent and or paying agent, and the Commissioned Company for Bondholders—during the life cycle of such instrument issued in Japan.

Table 36: Standard Fee Rates for Applicable Agent Services

Fee Item	Portion and Rating	Rate
Coupon Payment Fee (one time: twice a year)	Total Outstanding Amounts	JPY0.075 per 10,000 for JPY1
Redemption Fee	Total Redemption Amounts	JY0.075 per 10,000 for JPY1
Paying Agent for commercial paper issuance and redemption	Per one payment	Several thousand yen per issue or redemption
Agent Fee Related to Bonds		
a. Fiscal Agent Annual Fee (Yearly) (Outstanding Amount)	Total Outstanding Amounts (JPY10 billion)	JPY0.075 per 10,000 for JPY1 (JPY75,000)
a. CCB (Commissioned Company for Bondholders) Fee	-AA	1 bps/p.a. x Outstanding Amount
	A	2 bps/p.a. x Outstanding Amount
	BBB	4.5 bps/p.a. x Outstanding Amount
In case of the CCB attached bonds, both of above fees (a. + b.) will be charged.		

bps = basis points, p.a. = per annum.

Source: ABMF-J Member.

C. Costs Associated with Deposit, Withdrawal, Settlement (Set-Up, Book-Entry, and Transfer Fees) for Japan Securities Depository Center Account Holders

JASDEC is the central depository and settlement center for corporate bonds and notes and commercial paper issued in the Japan market. The comprehensive fee schedule for commercial paper and corporate bonds, which is included in Tables 37–40 and is also available in the public domain, effectively details JASDEC's service provisions to issuers and investors as account holders.

JASDEC does not distinguish between the settlement of ordinary transactions and those transfers as a result of securities lending or repo transactions. Therefore, the cost is the same for all transactions.

Table 37: Short-Term Corporate Bonds—Participation in the Book-Entry System

Item of Service Fees	Parties to Pay	Service Contents	Rates
Account opening fees and system connection preparation fees	JASDEC Participants	Processing for opening accounts and setting up a system connection	1. In the case where a party to pay newly becomes a JASDEC Participant: JPY200,000 Provided, however, that, when two or more Classified Accounts are opened with the same account name, the account opening fees and system connection preparation fees shall be JPY200,000, increased by the amount calculated based on the rate set forth in (2) below for each of such Classified Accounts in excess of one.
			2. In the case where Classified Accounts are opened (excluding the cases falling under (1) above): JPY50,000 per account Provided, however, that, when Classified Accounts are opened with the same account name for the first time, the account opening fees and system connection preparation fees shall be the amount calculated based on JPY50,000 per Classified Account to be opened, minus JPY50,000.
System connection preparation fees	Issuers	Processing for Issuer registration	JPY50,000
	Persons appointed as Issuing Agents or Paying Agents; except for persons who have already been appointed as Issuing Agents or Paying Agents	Processing for setting up a system connection	JPY50,000
Terminal connection fees	All users of the Integrated Web Terminal (excluding Fund Settlement Corporations)	Use of system resources through a continuous terminal connection	The rate of fees for use of system when the number of user IDs of an operational user is between one and five: JPY10,000 per month, for each company The rate of fees for use of system when the number of user IDs of an operational user is six or more: a. Rate applicable to five user IDs: JPY10,000 per month for each company b. Rate applicable to the number of user IDs in excess of five: JPY1,000 per month for each user ID.
Fixed fees to be borne by Indirect Account management institutions (intermediary)	Parties approved as Indirect Account management institutions (intermediary)	Processing of the approval as Indirect Account management institutions (intermediary)	JPY50,000 for each approval

JASDEC = Japan Securities Depository Center.

Source: JASDEC.

Table 38: Short-Term Corporate Bonds—Book-Entry-Related Fees

Item of Service Fees	Parties to Pay	Service Contents	Rates
New record service fees	Issuers relating to the new record	Administration of the Information of the Issue and administration of the balance of issue from the time of issuance until the time of redemption	JPY0.19 per 10,000 for JPY1 of the subscription price (for each issue), for each subscription (annualized rate) The monthly amount shall be equal to the amount calculated based on the annualized service fee rate set forth above, multiplied by the number of calendar days during the issue period (including the Issue Date but excluding the Redemption Date) and divided by 365; provided, however, that, if the foregoing amount exceeds JPY100,000, the monthly amount shall be JPY100,000.
Book-entry transfer service fees	Issuers and Purchaser JASDEC Participants relating to the new record	Processing for increasing the details recorded in the Transfer Account Book	In the case of the DVP settlement: JPY100 per transaction
			In the case of the non-DVP settlement: JPY50 per transaction
Purchase and cancellation service fees	Transferor JASDEC Participants and Transferee JASDEC Participants relating to the book-entry transfer	Processing for changing the details recorded in the Transfer Account Book	In the case of the DVP settlement: JPY100 per transaction Provided, however, that the rate of fees for the book-entry transfer implemented between the classified accounts of the same JASDEC Participant shall be JPY50 per transaction.
			In the case of the non-DVP settlement: JPY50 per transaction Provided, however, that the rate of fees for the book-entry transfer implemented between the Classified Accounts of the same JASDEC Participant shall be JPY25 per transaction.
	Issuers and Obliteration Applicant JASDEC Participants relating to the obliteration	Processing for decreasing the details recorded in the Transfer Account Book	In the case of the DVP settlement: JPY100 per transaction
			In the case of the non-DVP settlement: JPY50 per transaction
Purchase and Cancellation Applicant JASDEC Participants	Processing for decreasing the balance in the Transfer Account Book through purchase and cancellation	JPY50 per transaction	
Account balance administration service fees	JASDEC Participants	Administration of the Transfer Account Book during the holding period	JPY0.065 per 10,000 for JPY1 of the monthly average account balance, for each JASDEC Participant (annualized rate) The monthly amount shall be equal to the amount calculated based on the annualized service fee rate set forth above, multiplied by the number of calendar days during the applicable month and divided by 365.

DVP = delivery versus payment, JASDEC = Japan Securities Depository Center.

Source: JASDEC.

Table 39: Corporate Bonds—Participation in the Book-Entry System

Item of Service Fees	Parties to Pay	Service Contents	Rates
Account opening fees and system connection preparation fees	JASDEC Participants	Processing for opening accounts and setting up a system connection	<p>1. In the case where a party to pay newly becomes a JASDEC Participant: JPY200,000</p> <p>Provided, however, that, when two or more sets (<i>kumi</i>) of the Classified Accounts are opened with the same account name, the account opening fees and system connection preparation fees shall be JPY200,000, increased by the amount calculated based on the rate set forth in (2) below for each set (<i>kumi</i>) of the Classified Accounts in excess of one. In such case, Trust Account (1), Trust Account (2), Trust Account (3), Trust Account (4) and Trust Account (5) (hereinafter referred to as Each Trust Account in the Holding Account) and Customer Account and Nonresident, Etc. Account (hereinafter referred to as Customer Account, Etc.) shall be treated as having the same account name.</p>
			<p>2. In the case where Classified Accounts are opened (excluding the cases falling under (1) above): JPY50,000 per set (<i>kumi</i>)</p> <p>Provided, however, that, when Classified Accounts are opened with the same account name for the first time, the account opening fees and system connection preparation fees shall be the amount calculated on JPY50,000 per set (<i>kumi</i>) of the Classified Accounts to be opened, minus JPY50,000. In such case, Each Trust Account in the Holding Account and the Customer Account, Etc. shall be treated as having the same account name.</p>
System connection preparation fees	Parties appointed as the Issuing Agents and the Paying Agents	Processing for setting up a system connection	JPY50,000
Terminal connection fees	All users of the Integrated Web Terminal (excluding Fund Settlement Corporations)	Use of system resources through a continuous terminal connection	<p>The rate of fees for use of system when the number of user IDs of an operational user is between one and five: JPY10,000 per month for each company</p> <p>The rate of fees for use of system when the number of user IDs of an operational user is six or more:</p> <p>a. Rate applicable to five user IDs: JPY10,000 per month, for each company</p> <p>b. Rate applicable to the number of user IDs in excess of five: JPY1,000 per month, for each user ID in excess of five</p>
Fixed fees to be borne by Indirect Account management institutions (intermediary)	Parties approved as Indirect Account management institutions (intermediary)	Processing of the approval as Indirect Account management institutions (intermediary)	JPY50,000 for each approval

JASDEC = Japan Securities Depository Center.
Source: JASDEC.

Table 40: Corporate Bonds Book-Entry-Related Fees

Item of Service Fees	Parties to Pay	Service Contents	Rates
New record service fees	Issuers relating to the new record	(i) Administration of the Information of the Issue, (ii) administration of balance, and (iii) notice to Paying Agents of information concerning the redemption and interest payment, from the issuance until the redemption	With respect to the total issue amount of each issue: 1. Rate applicable to the portion equal to or less than JPY100 million: JPY0.95 per 10,000 for JPY1 2. Rate applicable to the portion equal to or more than JPY100,000,001 and less than or equal to JPY500 million: 80% of the rate set forth in (1) above 3. Rate applicable to the portion equal to or more than JPY500,000,001 and less than or equal to JPY1 billion: 60% of the rate set forth in (1) above 4. Rate applicable to the portion equal to or more than JPY1,000,000,001 and less than or equal to JPY5 billion: 40% of the rate set forth in (1) above 5. Rate applicable to the portion equal to or more than JPY5,000,000,001 and less than or equal to JPY10 billion: 20% of the rate set forth in (1) above 6. Rate applicable to the portion equal to or more than JPY10,000,000,001 and less than or equal to JPY50 billion: 10% of the rate set forth in (1) above 7. Rate applicable to the portion equal to or more than JPY50,000,000,001 and less than or equal to JPY100 billion: 5% of the rate set forth in (1) above 8. Rate applicable to the portion equal to or more than JPY100,000,000,001: 2.5% of the rate set forth in (1) above
Book-entry transfer service fees	Transferor JASDEC Participants and Transferee JASDEC Participants relating to the book-entry transfer	Processing for changing the details recorded in the Transfer Account Book	In the case of DVP settlement: JPY100 per transaction Provided, however, that the rate of service fees for the book-entry transfer implemented between the Classified Accounts of the same JASDEC Participant shall be JPY50 per transaction. In the case of the non-DVP settlement: JPY50 per transaction Provided, however, that the rate of service fees for the book-entry transfers implemented between the Classified Accounts of the same JASDEC Participant shall be JPY25 per transaction.
Purchase and cancellation service fees	Purchase and Cancellation Applicant JASDEC Participants	Processing for decreasing the balance under the Transfer Account Book through purchase and cancellation	JPY50 per transaction

continued on next page

Table 40 continued

Item of Service Fees	Parties to Pay	Service Contents	Rates
Account balance administration service fees	JASDEC Participants	Administration of the Transfer Account Book during the holding period	<p>With respect to the monthly average account balance for each JASDEC Participant: (annualized rate)</p> <ol style="list-style-type: none"> Rate applicable to the portion equal to or less than JPY500 billion: JPY0.065 per 10,000 for JPY1 Rate applicable to the portion equal to or more than JPY500,000,000,001 and less than or equal to JPY1 trillion: 60% of the rate set forth in (1) above Rate applicable to the portion equal to or more than JPY1,000,000,000,001 and less than or equal to JPY5 trillion: 40% of the rate set forth in (1) above Rate applicable to the portion equal to or more than JPY5,000,000,000,001 and less than or equal to JPY10 trillion: 20% of the rate set forth in (1) above Rate applicable to the portion equal to or more than JPY10,000,000,000,001 and less than or equal to JPY20 trillion: 10% of the rate set forth in (1) above Rate applicable to the portion equal to or more than JPY20,000,000,000,001 and less than or equal to JPY30 trillion: 5% of the rate set forth in (1) above Rate applicable to the portion equal to or more than JPY30,000,000,000,001: 2.5% of the rate set forth in (1) above <p>The monthly amount shall be equal to the amount calculated based on the annualized service fee rates set forth above, multiplied by the number of calendar days during the applicable month and divided by 365; provided, however, that, if the foregoing amount is less than JPY100,000, the monthly amount shall be JPY100,000.</p>
New Record Service Fees			
Scale	Total issue amount of each issue	Rate	
Range 1	The portion up to JPY100 million	Base rate = 0.95bp	
Range 2	The portion over JPY100 million and up to JPY500 million	80% of base rate	
Range 3	The portion over JPY500 million and up to JPY1 billion	60% of base rate	
Range 4	The portion over JPY1 billion and up to JPY5 billion	40% of base rate	
Range 5	The portion over JPY5 billion and up to JPY10 billion	20% of base rate	
Range 6	The portion over JPY10 billion and up to JPY50 billion	10% of base rate	
Range 7	The portion over JPY50 billion and up to JPY100 billion	5% of base rate	
Range 8	The portion over JPY100 billion	2.5% of base rate	

DVP = delivery versus payment, JASDEC = Japan Securities Depository Center, JPY = Japanese yen.
Source: JASDEC. <https://www.jasdec.com/en/system/sb/rule/fee/new.html>

D. Other Fees and Costs

Table 41 details a number of other typical fees incurred by the issuer and/or market participants in the context of a corporate bond or note issuance in Japan.

Table 41: Other Typical Fees and Costs in the Context of Corporate Bond Issuance

Item	Details
Credit Rating Fee	Credit rating fee will vary greatly depending on the target, content, and size.
Stamp Duty	The buyer pays a stamp duty of JPY200 per trade for physical certificate transfers. JASDEC-held securities are exempt from stamp duty.
Registration Costs	Registrars do not charge to register equity share certificates, but may pass on their agents' costs in terms of transporting and processing the registration documents. For bonds other than JGBs, registrars charge JPY800–JPY1,200 for registration per transaction.

JASDEC = Japan Securities Depository Center, JGB = Japanese Government Bond.
Source: JASDEC.

E. Taxation (Withholding Tax on Interest Income, Etc.)

Residents and nonresidents investing in the bond market in Japan are subject to a number of taxes on fixed-income securities, as detailed in this section. The taxation treatment for nonresidents or foreign juridical persons is highlighted in Table 42, while the treatment for resident Japanese investors is displayed in Table 43. The application of the various taxes, or corresponding concessions, is explained in subsequent sections.

Table 42: Taxation Treatment for Nonresident Investors (Foreign Juridical Persons)

Applicable Taxes	Type of Book-Entry Bonds	Tax Rate
Withholding Tax	Government and Municipal	Exempt ^a
	Corporate	Exempt ^a
Capital Gains Tax	Government	Exempt ^a
	Corporate	Exempt ^a
Value-Added Tax	Both	Not applicable

^a For application of exemptions, please refer to sections below; otherwise, a withholding tax of 15.315% will apply.
Source: ADB Consultants for SF1 based on data from PricewaterhouseCoopers Services LLP.

Table 43: Taxation Treatment for Resident Japanese Investors

Applicable Taxes	Type of Bonds	Tax Rate (%)
Income Tax or Corporate Tax	Government	20.315
	Corporate	20.315
Value-Added Tax	Both	8 ^a

^a The value-added tax rate is expected to increase to 10% in 2017.
Source: ADB Consultants for SF1.

1. Tax-Exemption System for Interest and Profits from Redemption on Corporate Bonds in Book-Entry Form Held by Nonresidents or Foreign Juridical Persons

This section provides an outline of the applicable taxation system for nonresident investors or foreign juridical persons prior to and following the 2013 Tax Reform.

(a) *Prior to the 2013 Tax Reform*

Interest on corporate bonds in book-entry form received by foreign investors had been exempt from tax in the same manner as JGBs and local government bonds, subject to certain procedural requirements.⁵³ However, the scope of this tax exemption had been limited to corporate bonds in book-entry form issued on or before 31 March 2013.

In June 2010, a tax-exemption system for interest and profits from redemption on corporate bonds in book-entry form held by nonresidents or foreign juridical persons was enacted as a 3-year temporary measure (Japanese Bond Income Tax Exemption Scheme).

Although this measure was introduced with a view to further promote investment in Japanese corporate bonds by nonresidents, etc. and to vitalize Japan's financial and capital markets as well as smoothing corporate fundraising activities, it remained effective as a temporary measure only until the end of March 2013.

(b) *Following the 2013 Tax Reform*

The FSA, JSDA, and market participants requested to upgrade the aforementioned temporary measure to a permanent system due to the recognition that such a tax-exemption system had been widely adopted worldwide as a permanent regime and the temporary treatment had led to a deficiency in the international competitiveness of corporate bonds issued in Japan.

In April 2013, this temporary tax exemption measure became permanent. Interest and profits from redemption of corporate bonds in book-entry form received by foreign investors have since been permanently exempt from tax, while still subject to certain procedural requirements.

2. Foreign (non-Japanese domestic) Corporate Bonds Issued by Japanese Resident (including AMBIF bonds issued outside Japan)

This section explains the applicable taxation for bonds and notes issued outside Japan by Japanese resident issuers. This treatment also applies to bonds and notes, which are issued under AMBIF in other ASEAN+3 markets.

Effective 1 April 2010, the Japanese Tax Act (Act on Special Measures Concerning Taxation) instituted a new tax certification procedure. Under the act, a bondholder that is a Specially Related Person to the Issuer had previously not been entitled to withholding relief on the interest payment and was subject to a 15.315% Japanese withholding tax.

⁵³ These concessions were introduced for JGBs in September 1999 and for local government bonds in January 2008.

As a result of the 2010 amendment, the exemption from Japanese taxation available under the act will remain in force indefinitely.⁵⁴ Under the rules, issuers and paying agents will not be required to withhold Japanese tax from interest paid to holders that establish their status as Gross Recipients.

(a) A Gross Recipient for this purpose is

- (i) a beneficial owner that is, for Japanese tax purposes, neither (a) an individual resident of Japan or a Japanese corporation, nor (b) an individual nonresident of Japan or a non-Japanese corporation that in either case is a person who has a special relationship with the issuer of the Securities as described in Article 6, paragraph (4) of the act (such a person is hereinafter referred to as a Specially Related Person of the Issuer);
- (ii) a Japanese designated financial institution holding securities for its own proprietary account; or
- (iii) an individual resident of Japan or a Japanese corporation whose receipt of interest on the securities is made through a payment handling agent in Japan as defined in Article 2-2 paragraph (2) of the Cabinet Order.

(d) Illustration of the Case of the Gross Recipient Being a Nonresident Investor

- (i) If the recipient of interest on the bonds is an individual nonresident of Japan, or a non-Japanese corporation having no permanent establishment within Japan, or having a permanent establishment within Japan but where the receipt of the interest on the bonds is not attributable to the business of such individual nonresident of Japan or non-Japanese corporation carried on within Japan through such permanent establishment, no Japanese income tax or corporate tax is payable with respect to such interest whether by way of withholding or otherwise, if such recipient complies with certain requirements, including, among others
 - (a) if the relevant bonds are held through a certain participant in an international or foreign clearing organization or a certain financial intermediary prescribed by the Special Taxation Measures Act and the relevant Cabinet Order (together with the Special Taxation Measures Act and the ministerial ordinance and other regulations thereunder) (each, a Participant), the requirement to provide, at the time of entrusting a Participant with the custody of the relevant bonds, certain information prescribed by the law to enable the Participant to establish that the recipient is exempt from the requirement for Japanese tax to be withheld or deducted (Interest Recipient Information), and to advise the Participant if such individual nonresident of Japan or non-Japanese corporation ceases to be so exempted (including the case where it became a Specially Related Person of the Issuer); and
 - (b) if the relevant bonds relating thereto are not held by a Participant, the requirement to submit to the relevant paying agent a Written

⁵⁴ The Amendment, which amended Article 6 of the Act on Special Measures Concerning Taxation (Act No. 26 of 1957) (as amended by the 2010 Amendment), was implemented by Article 3-2-2 of the related Cabinet Order (Cabinet Order No. 43 of 1957, as amended in April 2010 by Cabinet Order No. 58 of 2010), and entered into force on 1 April 2010.

Application for Tax Exemption (*Hikazei Tekiyo Shinkokusho*), together with certain documentary evidence.

Failure to comply with such requirements described above, including the case where the Interest Recipient Information is not duly communicated, as required under the law will result in the withholding by the Issuer of income tax at the rate of 15.315% of the amount of such interest.

- (ii) If the recipient of interest on the bonds is an individual nonresident of Japan or a non-Japanese corporation having a permanent establishment within Japan and the receipt of interest is attributable to the business of such individual nonresident of Japan or non-Japanese corporation carried on within Japan through such permanent establishment, such interest will not be subject to a 15.315% withholding tax by the Issuer, if the recipient provides the Interest Recipient Information or submits the Written Application for Tax Exemption as set out in (i). Failure to do so will result in the withholding by the Issuer of income tax at the rate of 15.315% of the amount of such interest. The amount of such interest will be aggregated with the recipient's other Japanese source income and will be subject to regular income tax or corporate tax, as appropriate.
- (iii) Notwithstanding paragraphs (i) and (ii) above, if an individual nonresident of Japan or a non-Japanese corporation mentioned above is a person who has a special relationship with the Issuer (that is, in general terms, a person who directly or indirectly controls or is directly or indirectly controlled by, or is under direct or indirect common control with, the Issuer) within the meaning prescribed by the Cabinet Order under Article 6, Paragraph 4 of the Special Taxation Measures Act (such person is referred to as a Specially Related Person of the Issuer) as of the beginning of the fiscal year of the Issuer in which the relevant interest payment date falls, the exemption from Japanese withholding tax on interest mentioned above will not apply, and income tax at the rate of 15.315% of the amount of such interest will be withheld by the Issuer. If such individual nonresident of Japan or non-Japanese corporation has a permanent establishment within Japan, regular income tax or corporate tax, as appropriate, collected otherwise by way of withholding, could apply to such interest under Japanese tax law.
- (iv) If an individual nonresident of Japan or a non-Japanese corporation (regardless of whether it is a Specially Related Person of the Issuer) is subject to Japanese withholding tax with respect to interest on the bonds under Japanese tax law, a reduced rate of withholding tax or exemption from such withholding tax may be available under the relevant income tax treaty between Japan and the country of tax residence of such individual nonresident of Japan or non-Japanese corporation.

For instance, Japan has an income tax treaty with Thailand, whereby the above-mentioned withholding tax rate is reduced to 10% only if the Thai resident who is the recipient of the interest is a financial institution as defined under that treaty. Japan also has income tax treaties, conventions, or agreements whereby the above mentioned withholding tax rate is reduced, generally to 10%, with, among others, Australia; Austria; Belgium; Canada; Denmark; Finland; France; Germany; Hong Kong, China; Ireland; Italy; Luxembourg; the Netherlands; New Zealand; Norway; Portugal; Singapore; Spain; Switzerland; and the US. Japan signed with the United Kingdom and Sweden protocols amending the tax treaties between the respective governments, whereby interest paid to qualified United Kingdom and Swedish residents is generally exempt from Japanese

withholding tax, which apply to interest to be payable on or after 1 January 2015. Japan and the US have also signed an amending protocol generally exempting interest from Japanese withholding tax; however, this amending protocol has not yet entered into force. Under the current income tax treaty between Japan and the US, certain limited categories of qualified US residents receiving interest on the bonds may, subject to compliance with certain procedural requirements under Japanese law, be fully exempt from Japanese withholding tax for interest on the bonds. Under the income tax treaties with Australia, France, the Netherlands, and Switzerland, similar exemptions to those provided in the current income tax treaty between Japan and the US will be available (provided that no exemption will apply to pension funds in the case of Australia).

In order to avail themselves of such reduced rate of, or exemption from, Japanese withholding tax under any applicable income tax treaty, individual nonresidents of Japan or non-Japanese corporations which are entitled, under any applicable income tax treaty, to a reduced rate of, or exemption from, Japanese withholding tax on payment of interest by the Issuer are required to submit an Application Form for Income Tax Convention regarding Relief from Japanese Income Tax and Special Income Tax for Reconstruction on Interest (as well as any other required forms and documents) in advance through the Issuer to the relevant tax authority before payment of interest.

- (v) Under the Law,
 - (a) if an individual nonresident of Japan or a non-Japanese corporation that is a beneficial owner of the bonds becomes a Specially Related Person of the Issuer, or an individual nonresident of Japan or a non-Japanese corporation that is a Specially Related Person of the Issuer becomes a beneficial owner of the bonds, and
 - (b) if such bonds are held through a Participant, then such individual nonresident of Japan or non-Japanese corporation should notify the Participant of such change in status by the immediately following interest payment date of the bonds.

As described in (iii), as the status of such individual nonresident of Japan or non-Japanese corporation as a Specially Related Person of the Issuer for Japanese withholding tax purposes is determined based on the status as of the beginning of the fiscal year of the Issuer in which the relevant interest payment date falls, such individual nonresident of Japan or non-Japanese corporation should, by such notification, identify and advise the Participant of the specific interest payment date on which Japanese withholding tax starts to apply with respect to such individual nonresident of Japan or non-Japanese corporation as being a Specially Related Person of the Issuer.

3. Relevance for AMBIF Bonds and Notes Issued outside Japan

As a regional initiative, AMBIF encourages the issuance of corporate bonds and notes by issuers resident in ASEAN+3 markets, such as Japan, in member countries of ASEAN+3 in which they are not resident (cross-border issuance). This is expected to generate a number of tax-related issues for consideration of parties involved in a bond or note issuance, such as those detailed in F.2 earlier.

It is, hence, of particular importance that specific AMBIF bonds and notes related tax practices and procedures for regional nonresident investors should be developed accordingly and continuously.

F. Taxation for Resident Japanese Investors (Integration of Taxation on Financial Income and Gains)

The integration of taxation on financial income and gains for Japanese resident individuals commenced with effect from 1 January 2016 (金融所得一体課税の開始).

This integration of financial income taxation for resident individuals is a system aiming to implement an integral taxation of income arising from a wide range of financial instruments.

To facilitate individual investors' participation to the financial and securities markets, it is essential to create an environment where such investors will easily invest in a variety of financial instruments.

Previously, given the fact that stock dividends and its capital gains or loss could not be aggregated with interest, profit or loss from the transfer or redemption on bonds (including corporate bonds), the range of aggregation for the profits and losses among financial instruments was very limited, resulting in individual investors not being well motivated to invest in multiple types of financial products.

The comprehensive taxation method under the self-assessment taxation system has become a basic principle in the overall taxation system in Japan. However, depending on the type of financial instruments described in Table 44, the separated and withheld taxation method (c) or the self-assessed separated taxation method by filing tax returns (a) has been imposed, respectively, on the income and capital gains generated from these financial instruments. In addition, for each type of financial instrument, there was a difference in the tax rate. And, the extent of profit-loss offsetting among different financial products was very limited. In addition, differences existed in the taxation methods between the system for public and corporate bonds and the system for listed shares. Therefore, it was hard for individual investors to make effective investment in diversified financial products.

Consequently, with a view of expanding the range of aggregation for profits and losses relating to financial instruments, and creating an environment to promote active participation of individual investors to the market, an overall reform of taxation methods regarding public and corporate bonds and bond investment trusts (profit and loss aggregation with stock, etc. becoming possible) has started effective January 2016. This reform is now known as “integration of taxation on financial income and gains.”

In the past, the tax law regarding investments in financial instruments by Japanese resident individuals had been revised many times. In contrast, for the corporate bond market, it had been repeatedly pointed out that the withholding tax system on interest payment—which generated serious segregation issues between taxable bonds and nontaxable bonds—created impediments for the liquidity of the market. However, following the changes from this taxation reform, the need and rate of the withholding tax to be deducted will be judged on the basis of the taxation attribute of the bondholder on the coupon payment date. At the same time, interest of corporate bonds held by nontaxable persons or organizations on the coupon payment date will be exempted from tax during the term, regardless of its holding

period. Moreover, the previous market practice of deducting the withholding tax equivalent amount upon the delivery and receipt of accrued interest will also be phased out.

As Table 44 indicates, the previously “separated and withheld taxation method (c)” had been applied to “bonds, such as government bonds, public bonds, and corporate bonds.” It has been changed to the “self-assessed separated taxation method by filing tax returns (a)” in the same manner as for listed shares. Effective 1 January 2016, the taxation scheme for each financial instrument has been changed as follows:

- Capital gains arising from sales and redemptions of bonds are taxed as “separate taxation by and upon filing individual income tax returns (a)” and capital losses are recognized and used to offset profits subject to a limitation as shown in category A of Table 44.
- For bond investors, an expansion of the scope of profit or loss offset arising from listed shares has become possible.
- Furthermore, this tax reform includes changes to the “separated taxation method (a)” for capital gains or losses arising from the sales of shares and bonds held together in specified accounts (*tokutei kouza*).
- Specified accounts (*tokutei kouza*) were introduced in Japan in order to simplify the filing and tax payment procedures of individual investors. A securities company will create a specified account annual transaction report, which compiles the trading gains or losses for 1 year, and is delivered to investors by the end of January of the following year. Once selected, the withholding account in the specified account tax return is not required for that part. However, the profit-loss offsetting of the income of more than one withholding account must be accomplished on the final tax return.

This will simplify and increase the efficiency of tax procedures for individual investors.

As for the tax rate, in the past, tax on the interest from public and corporate bonds was 20.315% using the “withholding tax method (c),” while the capital gain from a sale was tax-free. Effective 1 January 2016, the tax rate has been changed to a generally applicable rate of 20.315% (15.315% national income tax + 5% local tax) based on the “self-assessed separated taxation method by and upon filing tax returns (a).”

Under the new tax rule, the “separated and withheld taxation method (c)” was abolished. With this change any withholding of tax is no longer applicable. This also resulted in being able to effect settlement using the gross amount in all cases for resident individuals. This change is expected to simplify the tax-related handling procedures in financial institutions and at institutional investors.

Table 44: Summary of Taxation System for Financial Products for Japanese Resident Individuals before and after Reform

	Income		Capital Gains or Losses		Category for Profit-Loss Offsetting After (from 1 Jan 2016)
	Before	After (from 1 Jan 2016)	Before	After (from 1 Jan 2016)	
Listed shares and publicly offered stock investment trusts	Separated taxation by filing (a) (tax rate 20.315%)		Separated taxation by filing (a) (tax rate 20.315%)		A
Specified bonds (b) (specified public and corporate bonds) and publicly offered bond investment trusts	Separated and withheld as a final tax (c) (tax rate 20.315%)	Separated taxation by filing (a) (tax rate 20.315%)	Tax-free (Exempt from taxation)	Separated taxation by filing (a) (d) (tax rate 20.315%)	
Nonlisted shares and privately offered investment trust	Not applicable for separated taxation by filing		Separated taxation by filing (a)		B
General bonds (bonds other than specified bonds)	Separated and withheld as a final tax (c)		Tax-free (exempt from taxation)	Separated taxation by filing (a) (e)	
Bank deposits	Separated and withheld as a final tax (c)		-		
Derivatives	Separated taxation by filing (a) (f)				

Notes:

- (a) Self-assessed separated taxation method by and upon filing tax returns is a method in which, rather than tax being deducted before payment, taxpayers who understand the financial transactions-related income and tax rate, pay via a tax return. On the other hand, general taxation is a method in which the tax rate is determined depending on the sum of the various types of income (e.g., salary and interest income).
- (b) Specified bonds include Japanese Government Bonds and foreign government bonds, publicly offered bonds, listed bonds, bonds issued by corporates with a filed securities report within 6 months prior to issuance, and bonds issued on or before 31 December 2015 excluding discount bonds where tax is withheld at the time of issuance.
- (c) Separated and withheld taxation is a final tax method in which the payer makes a withholding of the tax portion within the income from financial instruments, etc. In other words, the tax amount is deducted before interest, etc. is paid.
- (d) Profit-loss offsetting is newly allowed. Profit-loss offsetting is available among category A.
- (e) Profit-loss offsetting is newly allowed. Profit-loss offsetting is available among category B.
- (f) To be deliberated, paying attention to contribution to achievement of comprehensive exchanges.

Source: ABMF SF1 based on information from the Financial Services Agency.

Market Size and Statistics

The original ASEAN+3 Bond Market Guide was published in April 2012 and included 12 pages of Japan bond market statistics, including historical data, such as bond holdings, bondholder distribution, outstanding amounts and trading volumes. Not surprisingly, this data became stale soon after publication.

Since the ASEAN+3 Bond Market Guide is most likely to be updated on a biannual basis, it is not the best channel for the dissemination of market statistics. Hence, a chapter comprising bond market statistics has been discontinued and replaced with a list of recommended sources for detailed, accurate, and current information sources on the Japan bond market. These sources are listed below in alphabetical order.

- *AsianBondsOnline* (an ASEAN+3 initiative lead by ADB)
<https://asianbondsonline.adb.org/japan.php>
 - Market-at-a-Glance
 - Data (yields, indicators, and ratings, including historical data)

- Bank of Japan
<https://www.boj.or.jp/en/paym/bond/index.htm/>
 - Monetary survey
 - Bond market survey
 - Liquidity indicators
 - Bond Market Group (Primary Dealer) meeting minutes

- Japan Securities Dealers Association
<http://www.jsda.or.jp/shiryō/toukei/hakkou/files/hakkougakushoukangaku.xls>
<http://www.jsda.or.jp/shiryō/toukei/shurui/files/srb.xls>

- Japan Securities Depository Center
<http://www.jasdec.com/en/material/statistics/>
 - Integrated statistics on, e.g., number of issues, size, amounts (for all book-entry securities except for JGBs)
 - Stocks, convertible bonds
 - Corporate bonds
 - Commercial paper

- Ministry of Finance Japan
<https://www.mof.go.jp/english/jgbs/reference/gbb/index.htm>
 - Central government debt
 - Outstanding government bonds

Islamic Finance in Japan

A. Background on Introducing Islamic Finance in Japan

Japan has strong economic ties with Islamic countries, particularly Middle Eastern oil-producing countries, as evidenced by huge cash outflows from Japan to those countries every year. Facilitating the reverse flow of investment from Islamic countries into Japan and other Asian economies is important for the balanced growth of the global economy.

In 2007, a number of Japanese public and private institutions started to explore Islamic finance as one of the means to attract Islamic investors (particularly those with petrodollars) to invest in Japan by participating as an observer in the Islamic Financial Services Board, an international standard-setting organization for the Islamic finance services industry headquartered in Kuala Lumpur, Malaysia (Table 45).

Table 45: Japanese Organizations in the Islamic Financial Services Board

Name	Country or Origin	Member Status
Bank of Japan	Japan	Observer Member
Bank of Tokyo-Mitsubishi (Malaysia)	Malaysia	Observer Member
Japan Bank for International Cooperation	Japan	Observer Member
Japan Securities Dealers Association	Japan	Observer Member
Mizuho Corporate Bank	Japan	Observer Member
Nomura Asset Management Malaysia	Malaysia	Observer Member
Sumitomo Mitsui Banking Corporation	Japan	Observer Member

Source: Japan Securities Dealers Association.

In terms of private transactions, in addition to the early commitment of Tokio Marine Group to *Takaful* operations since the beginning of the 21st century, several companies and their overseas subsidiaries have carried out Islamic capital market transactions overseas as follows:

- (i) The Malaysian subsidiaries of AEON Credit Service and Toyota Financial Service issued MYR-denominated *sukuk musharakah* in 2007 and 2008, respectively.
- (ii) Daiwa Asset Management arranged the listing of the first Shariah-compliant exchange-traded fund for Japanese stocks in Singapore in 2008.
- (iii) Nomura Holdings issued the first USD-denominated *sukuk Ijarah* (USD100 million) in July 2010 in Malaysia based on aircraft leasing.
- (iv) Daiwa Securities Capital Markets acted as co-lead arranger for Islamic real estate investment trusts listed on the Singapore Exchange in November 2010.

- (v) The Bank of Tokyo-Mitsubishi UFJ launched a USD500 million multicurrency *sukuk* issuance program using *wakala al isthismar* for 1 year in 2014, and has already issued the first JPY-denominated *sukuk* under this program.

B. Regulatory Framework for Islamic Finance in General

For the time being, Japan is not equipped with a full-ranged regulatory framework for operating Islamic finance. However, in December 2008, Japanese banking and insurance business regulations were relaxed to allow subsidiaries of Japanese banks and insurance companies to provide certain Islamic finance services in such forms as *murabahah* (cost-plus sale) or *Ijarah* (leasing) by amending the Ordinance for Enforcement of the Banking Law and the Insurance Business Law.

At present, there is not an explicit movement for Japanese banks to set up such subsidiaries in Japan, except for a few cases where subsidiaries of Japanese banks are applying for the regulatory authorization required for conducting Islamic financial operations in overseas. Consequently, issues of Shariah compliance, or that of supervision of the market, have not yet been taken up for discussion in Japan.

C. Regulatory and Legal Framework for Islamic Bonds (J-Sukuk)

1. Background on the Amendment of Legislation for Fostering J-Sukuk Market

In 2010, further steps were contemplated to facilitate *sukuk* issuance by Japanese domestic corporations (or other public or quasi-public entities) under the Japanese legal system. Since the latter half of 2010, the momentum within the governmental agency, the FSA became explicit:

- (i) Recommendation by expert advisory group within the FSA (July 2010) that “it would be necessary to improve the tax treatment of Islamic finance by taking certain measures such as treating the dividends on *sukuk* in the same manner as interests on bonds.” Interests on book-entry bonds paid to nonresidents and foreign entities are excluded from taxation following the tax reform in 2010.
- (ii) Policy assessment by the FSA (August 2010);
- (iii) Submission of the tax reform request by the FSA (August 2010) (Tax Reform Request);
- (iv) Assessment and acceptance of the Tax Reform Request by Tax Commission (December 2010);
- (v) Outline of the tax reform 2011 announced by the government (December 2010) (Tax Reform Outline 2011); and
- (vi) Action Plan for Japan’s New Growth Strategy, announced by the FSA on 24 December 2010: the FSA will promote the development of the environment for Islamic bond issuance in Japan.

2. Amendment of Legislation for Issuing *Sukuk* under Japanese Law

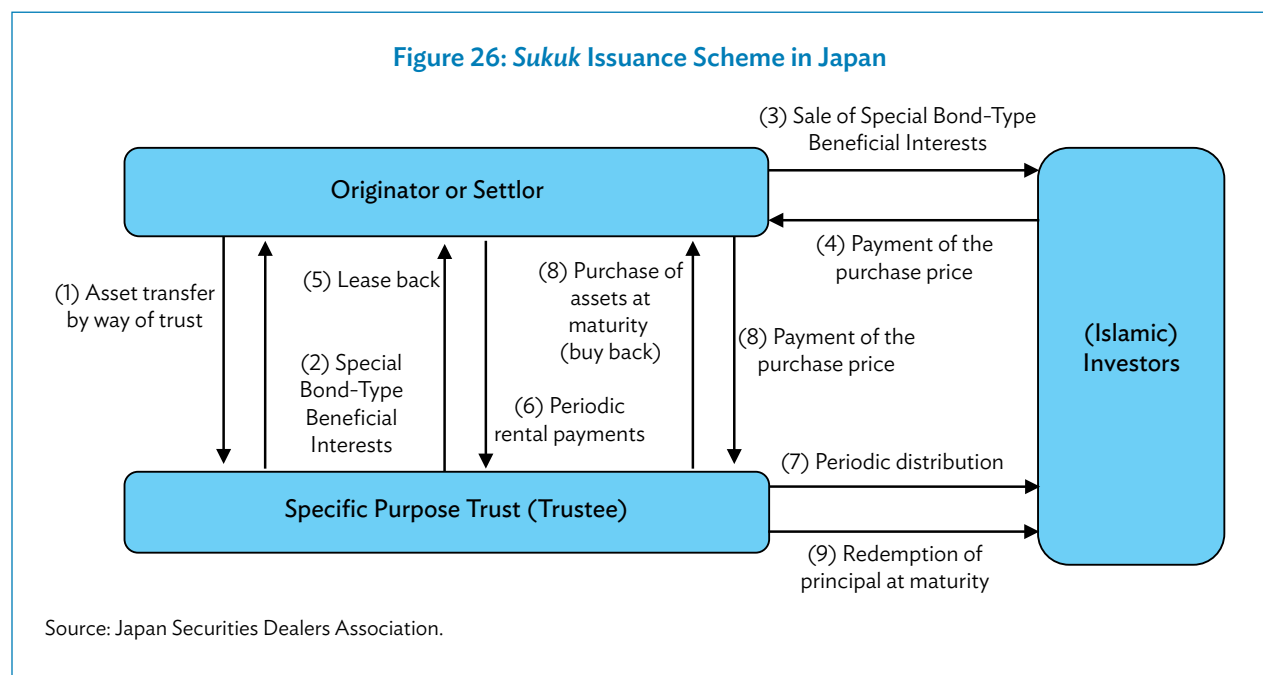
Following the momentum described above, the National Diet passed a bill on 17 May 2011 to facilitate *sukuk* issuance in Japan by way of amendment of the Asset Securitization Act (*shisan ryudoka ho* 「資産流動化法」). The bill is accompanied by amendments on relevant

tax legislation with a view to creating a level tax playing field compared to conventional bonds.

The Financial Instruments and Exchange Act (Amendment) for Reinforcement of Infrastructure of the Capital Market and Financial Business was presented before the National Diet on 1 April 2011 by the Government of Japan. The bill involves an amendment of the Asset Securitization Act that anticipates accommodating a legal framework for the issuance of *sukuk*, particularly *sukuk Ijarah*, in Japan. *J-Sukuk*, under the new legal framework, will be established typically by taking the form of Bond-Type Beneficial Interests (*Shasai-teki jueki-ken* 「社債的受益権」) to be issued under the architecture of a specific purpose trust (SPT) (*tokutei mokuteki shintaku* 「特定目的信託」), pursuant to the amended Asset Securitization Act. And, more specifically, if *J-Sukuk* takes a form of *sukuk Ijarah*, with the buyback commitment of underlying assets at its maturity by the originator, it will be legally constructed under the scheme titled Special Bond-Type Beneficial Interests (*Tokubetu shasai-teki jueki-ken* 「特別社債的受益権」).

The Special Bond-Type Beneficial Interest is a certain type of beneficial interest under an SPT, for which a predetermined amount of money is distributed and a condition is attached to the effect that the originator shall purchase (buy back) the underlying assets or such other terms to be prescribed in the Cabinet Order. The following is the outline of the structure, whereby steps are taken in the manner illustrated in Figure 26:

- (1) A Japanese institution acting as the originator (or settlor in the context of the SPT Agreement) and a trustee, which would typically be a trust bank, enters into a specific purpose trust agreement (SPT Agreement) whereby the originator transfers the ownership of an asset (such as real estate, Underlying Asset) to the trustee who holds the same on trust.



- (2) The originator acquires Special Bond-Type Beneficial Interests in exchange for the transfer of the Underlying Asset to the trustee pursuant to the SPT Agreement.
- (3) The originator sells the Special Bond-Type Beneficial Interests to investors that include Islamic investors.
- (4) Investors pay the amount equivalent to the purchase price for the Special Bond-Type Beneficial Interests to the originator.
- (5) The originator enters into an *Ijarah* lease agreement with the trustee in respect of the Underlying Asset.
- (6) The originator makes periodic rental payments to the trustee under the *Ijarah* lease agreement.
- (7) The trustee makes periodic distribution of the profit to the investors by way of dividends on the Special Bond-Type Beneficial Interests, which are funded by the rental payments under the *Ijarah* lease agreement.
- (8) At maturity, the originator purchases (buys back) the Underlying Asset at a predetermined price equivalent to the Special Bond-Type Beneficial Interests amount then outstanding.
- (9) The trustee redeems the Special Bond-Type Beneficial Interests by utilizing the purchase price received from the originator.

In order for an instrument to fall within the definition of the (Special) Bond-Type Beneficial Interests under the new Article 230 of the Asset Securitization Act, it needs to have all the following key characteristics:

- (i) **Amount of distribution.** The amount of distribution must be set out in the SPT Agreement in the form of a predetermined amount or such other calculation whose method is to be prescribed in the Cabinet Order, which deems to result a predetermined amount.⁵⁵
- (ii) **Structure of payments.** The principal must be redeemed at a predetermined point in time. The payment structure must allow not only payment at the end of the *sukuk* term but also in installments.
- (iii) **Voting rights.** The holders of the (Special) Bond-Type Beneficial Interests are not granted voting rights save for prescribed resolutions such as amendment and termination of the SPT Agreement.
- (iv) **Asset-based nature (rather than asset backed).** The credit standing of the originator (settlor of the SPT) should have a material effect on the investment decision of the investors. On the face of the provision of the Asset Securitization Act, the asset-based nature of the (Special) Bond-Type Beneficial Interests is recognized by a purchase undertaking of the Underlying Asset by the originator under the SPT Agreement or other alternative arrangements to be prescribed in the Cabinet Order, which would likely be an arrangement where the Underlying Assets are recognized in the balance sheet of the originator, regardless of the transfer of its ownership to the trustee pursuant to the SPT Agreement.

3. Recognition of *Sukuk* Issued under Foreign Law

It has not been explicitly reported that the *sukuk* issued under overseas jurisdiction have been offered in Japan. Some factors that are attributable to the above include uncertainty of

⁵⁵ The draft Cabinet Order has not yet been disclosed to the public as of 11 July 2011 but is expected to allow periodic distribution determined by reference to market rate of interest such as LIBOR.

tax treatment, a lack of market demand within Japan which has a small Muslim population, and challenges over regulatory definitions of overseas Islamic products.

D. Type of Instruments Available, Segments, and Tenure

The (Special) Bond-Type Beneficial Interests (which is anticipated to be recognized as *sukuk* by Islamic investors) introduced in the amended Asset Securitization Act aim typically at the issuance of the *sukuk Ijarah* within the context of Japanese legislation. However, by amendment of the Implementation Rule on Asset Securitization Act in November 2011, participating interests in the silent partnership or partnership based on the Civil Code, which are equivalent to the interests in *mudarabah* and *musharakah*, respectively, became also allowable as underlying assets of SPT.

E. Tax-Related Issues

There are four key measures in the amendment of the relevant tax legislation to address taxation issues that would otherwise put the (Special) Bond-Type Beneficial Interests at a disadvantage in view of conventional bond issues:

1. Exclusion from Taxation on the Distribution of Profits

The distributions of profit on the book-entry Special Bond-Type Beneficial Interests payable to

- (i) foreign corporations and nonresidents (who do not have permanent establishment in Japan) shall be excluded from taxation, and
- (ii) domestic banks and other Japanese financial institutions shall be exempted from withholding tax.

This measure was initially enacted as a temporary measure effective until March 2013. However, in line with the perpetuation of other preferential tax treatment regarding bond investment by nonresidents, etc. (e.g., Japanese Bond Income Tax Exemption Scheme), it was extended for 3 years until March 2016.

2. Tax Transparency of the Special Purpose Trust

The conditions for deductibility of dividends paid by the SPT have been amended to the effect that the Special Bond-Type Beneficial Interests have been exempted from the requirement that more than 50% of the issue amount must be offered domestically.

3. Exclusion of Asset Transfer-Related Tax

The purchase (buyback) transaction of the underlying asset from SPT to the originator (or the settlor of the SPT) shall be excluded from

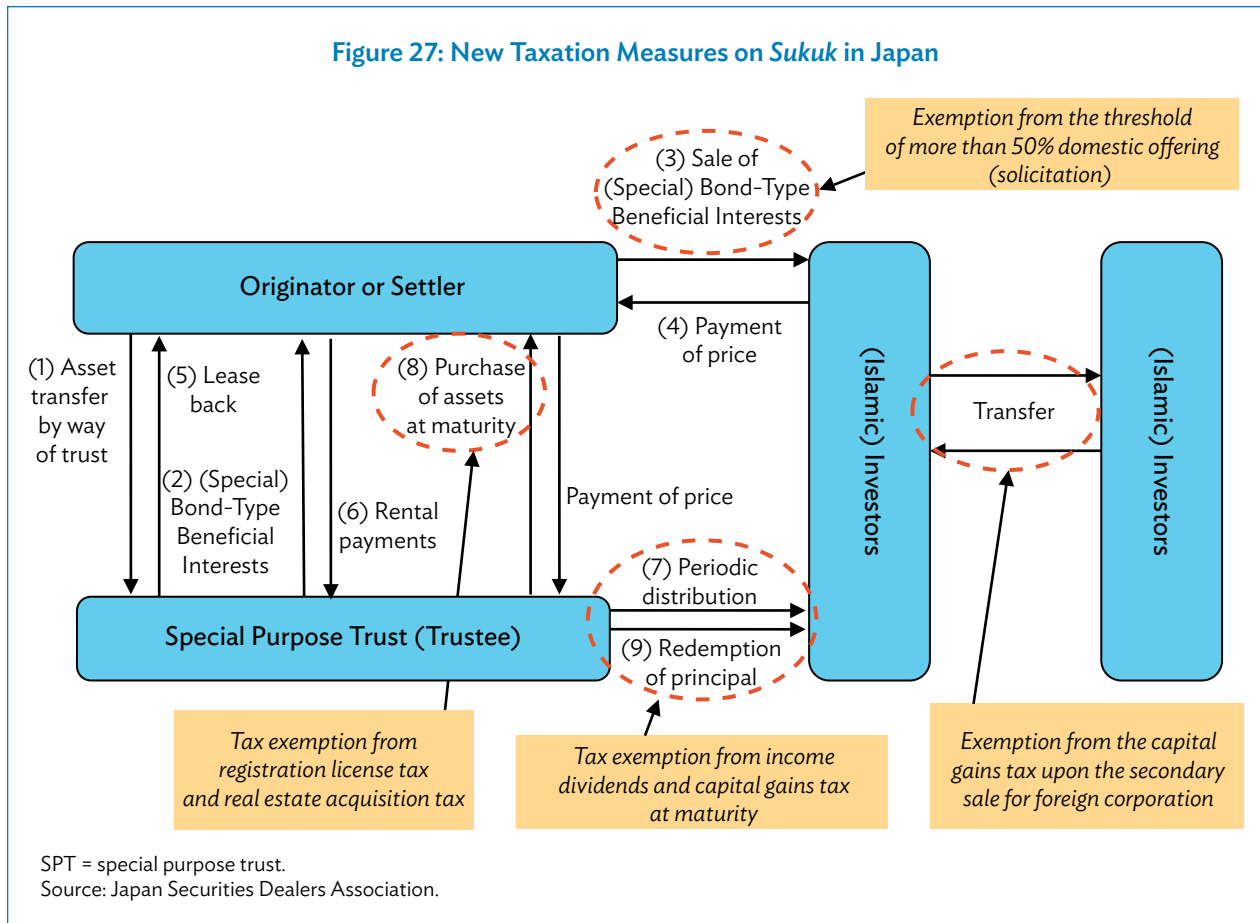
- (i) registration license tax, and
- (ii) real estate acquisition tax (in respect of the SPT involving real estate as an underlying trust asset) in relation to the Special Bond-Type Beneficial Interests under the SPT.

This measure was initially enacted as a temporary measure effective until March 2014. However, it was extended for 2 additional years until March 2016.

4. Exemption from Capital Gains Tax

Foreign corporations shall be exempted from capital gains tax upon the secondary sale of the (Special) Bond-Type Beneficial Interests.

Figure 27: New Taxation Measures on Sukuk in Japan



F. Impediments for Structuring Sukuk

Aside from the tax-related issues above, a number of other impediments continue to affect the issuance of *sukuk* in Japan:

- (i) The *J-sukuk* is a (Special) Bond-Type Beneficial Interests issued by SPT under the amended Asset Securitization Act, which is legally unique compared with the most commonly used type of trust certificates based on the Declaration of Trust. Thus, the usability of such vehicle is not well tested in the international context.
- (ii) As this structure presupposes the underlying assets that actually exist and produce a stream of fixed cash-flows, it would be difficult to be used for the

- development-type real-estate leasing projects where the underlying assets do not physically exist yet.
- (iii) Relevant infrastructure such as a settlement system, listing, implementation rules, accounting treatment, etc. should be developed concomitantly for facilitating the issuance of *J-sukuk*.

G. Significance of the Islamic Finance and Islamic Bonds (*Sukuk*) Market

Only one Shariah-compliant finance deal has been reported in Japan involving *tokumei kumiai*, a statutory category of partnership established by an agreement between a business operator and an investor who invests in a specified business of the operator, in the field of real-estate finance transaction. However, other types of Islamic financial transactions have not yet been achieved within Japan, including Islamic banking and *sukuk* issuance.

In this regard, the TPBM, which was initially established by TOKYO AIM as a joint venture between the TSE and the London Stock Exchange in May 2011, and is now functioning as one segment of the TOKYO PRO-BOND Market under the TSE, has included the (Special) Bond-Type Beneficial Interests among its eligible bonds for listing and trading.

As mentioned above, several Japanese entities have issued *sukuk* in overseas markets.

Bond Market Challenges and Opportunities

A. Corporate Bond Market Characteristics and Issues

The Japanese corporate bond market has developed its flexibility and efficiency through system reforms such as the abolishment of regulations on corporate bonds issuance limits and the revision of the trustee company system (1993), the abolishment of eligibility standard for corporate bond issuance and deregulation of bond covenants (1996), and the electronic registration of corporate bond certificates (2006). The credibility of corporate financial reporting has been boosted by developing accounting standards and enhancing the audit system. The above actions have also increased the attractiveness of corporate bonds as financial instruments among investors. Because many companies have recently issued corporate bonds targeting individual investors, corporate bonds are also becoming an attractive investment instrument for individual investors.

On the other hand, in spite of the system reforms mentioned above, the corporate bond market in Japan is still small. As has been pointed out, this situation lies in the complex interaction of various factors such as the following:

- (i) As for the flow of funds in Japan, while the public sector has been significantly short of funds, private nonfinancial corporations tend to have a surplus of funds. Particularly, in a situation where economic growth is slow and capital investment is restrained, the demand for long-term funds has been sluggish and many companies have issued corporate bonds not to raise new long-term funds but to roll over their existing long-term borrowings.
- (ii) In an environment marked by low SME corporate finance demand, resulting from the government's supportive measures and financial policies to help SMEs and intensifying loan competition among financial institutions, including city banks and regional banks, large corporations and SMEs have long been able to finance themselves at lower cost with bank loans rather than corporate bond issuance.
- (iii) The so-called chicken-or-egg problem—the inactive issuance of corporate bonds results in and is caused by low liquidity in the corporate bond market—has yet to be solved. Consequently, the liquidity of corporate bonds remains low. As a result, conditions in the secondary market have not been properly reflected in the primary market in a timely manner. Additionally, although market participants need to improve the transparency of corporate bond prices in the secondary market, the Reference Statistical Prices (Yields) for OTC Bond Transactions published by the JSDA was not sufficiently reliable to serve the role of properly reflecting secondary market conditions (see Chapter IV. E). There may be room for further development and improvement of a settlement and clearing system and corporate bond repo market that can contribute to stimulating the secondary market (see Chapter X.B).
- (iv) Due to corporate bond underwriting practices, flexible issuance in accordance with needs is difficult because the issuable period of the publicly offered corporate bonds is limited and the issue timing is concentrated. The publicly

- offered corporate bond issuance procedures are not flexible nor agile because the roles and responsibilities among securities companies conducting underwriting examinations (Type I Financial Instruments Business Operators), issuer, audit corporations, and certified public accountants have not been defined and the handling rules for the comfort letter have not been clarified. Furthermore, the pot system, which is popular in Europe and the US as a standard method of determining the conditions of issuance, has not been established in Japan; as a result, the conditions of issuance cannot be quickly set.
- (v) Due to the small size of the corporate bond market in Japan, some Japanese institutional investors have not established an adequate research system nor trained sufficient analysts to conduct credit analysis of corporations, which has been a mid- to long-term issue in the market. Moreover, when investing in corporate bonds, investors in some cases significantly rely on external rating agencies and tend to adopt a similar investment strategy with those adopted by other institutional investors. Individual investors have difficulty obtaining information on corporate bonds.
 - (vi) There was no sufficient tax exemption system for investment in corporate bonds by nonresident investors until June 2010, when such a system was introduced to promote investment in and the holding of corporate bonds by foreign investors. Consequently, the corporate bond market is not a good place to actively invest for investors with a higher risk appetite.
 - (vii) Defaults by issuing companies have been very rare in Japan. Therefore, sufficient data on the relationship between the credit risk of the issuers and issuance conditions have not been accumulated yet.
 - (viii) In many cases, a negative pledge giving all corporate bonds the same priority is attached to corporate bonds.⁵⁶ As a result, when the issuer is in default, there is a concern that the rights of corporate bondholders will be subordinate to the rights of other creditors. As the covenants that are also attached to debts other than the corporate bonds are not fully disclosed, the preferred or deferred relationship between corporate bonds and other debts is unclear. This point should be improved from the perspective of investor protection.
 - (ix) In Japan, a commissioned bank or commissioned person (Corporate Bonds Manager) has not been appointed in many cases except for corporate bonds targeting individual investors. Therefore, there is no consensus about the role of a commissioned bank or commissioned person (Corporate Bonds Manager) and the preservation attachment for corporate bondholders when a corporate bond is in default. There also has been no discussion held regarding cost sharing.
 - (x) As laws and regulations, the concept of bankruptcy, and the role of financial institutions in the corporate reconstruction process in Japan are different from those in Europe and the US, many people in Japan believe that only companies that have a certain level of credit strength can issue corporate bonds.
 - (xi) There remain taxation complexities in the market, such as different tax treatments depending on the type of assigner of corporate bonds. This is one of the factors that impede higher liquidity for corporate bonds.

One of the reasons why the corporate financing structure in Japan relies heavily on bank loans rather than corporate bond issuance is that the risk premium of bank loans is lower than that of corporate bonds due to the reasons listed in (a), (b), and (c). This is particularly significant in Japan. Therefore, the funding cost of borrowing is cheaper than that of

⁵⁶ A negative pledge clause is a covenant provision in a bond agreement whereby the issuer agrees not to pledge any assets if such pledging would result in less security for the agreement's bondholders.

corporate bond issuance. If an appropriate spread could be set that reflects the credit risk, market liquidity, and the handling of pledges regardless of bank loans or corporate bonds, corporate bonds would become more attractive for issuers of corporate bonds as well as for investors, contributing to the diversification of financing methods for corporations and the variety of investment instruments for investors. While setting an appropriate risk premium on bank loans is an important issue for the strengthening of the financial system in Japan, it is necessary to reduce the risk-premium gap between bank loans and corporate bonds by improving the efficiency, transparency, and liquidity of the corporate bond market. This issue needs to be solved by both market participants and banks by tackling their own issues one by one based on their individual viewpoints, as well as through cooperation with each other in establishing more transparent and sound market practices.

- (i) In circumstances where companies have less demand for funds because of the sluggish economy, banks have made transactions with borrowers from a mid- and long-term viewpoint and/or under a comprehensive service scheme, including settlements and foreign exchange. Due to public supportive measures and financial policy and intensifying lending competition among banks, lenders cannot set loan interest rates that are appropriate for the real credit risk of the borrower. The related party has to carefully analyze and determine how to evaluate the compensation gained by banks that provide comprehensive financial services and the long-term credit risk involved, and how to compare the cost of corporate bond issuance based on liquidity.
- (ii) Banks lend money based on detailed information such as the pledge provided by a borrower company and the short-term funding requirements of the borrower, while the issuance of and the investment in corporate bonds are based on disclosed information such as timely disclosure by securities exchanges, prospectuses, and securities reports. In this manner, banks obtain a broader and more detailed range of information that seems to affect their loan conditions. The related party needs to consider how the market evaluates and determines the above facts.
- (iii) Financial institutions such as banks have taken provisional measures through the management of pledges provided by borrowers before executing loans. Also, when the borrower falls into management difficulties, banks not only preserve and recover the debts, but, in some cases, also play a certain role in the insolvency, reorganization, or reconstruction process of the borrower.

Corporate bonds are more specific in nature than shares, and their issuing conditions vary in each case. A syndicate loan is also an agile funding method with high liquidity that is similar to corporate bonds. To vitalize the corporate bond market, it is necessary to develop infrastructure while taking into consideration the similarity of corporate bonds to syndicate loans.

Credit default swap (CDS) transactions have recently increased in the European and US markets, with some large-sized companies in Japan also actively conducting CDS transactions. It is necessary to promote the sound development of CDS transactions and the CDS market in Japan, as it supplements the liquidity of the corporate bond market. It will also be necessary to carefully monitor the relationship between the CDS market and the corporate bond market.

B. Reducing the Blackout Period and Expanding Funding Sources

The professional securities market as shown above will increase the convenience for Japanese and Asian issuers and holders of corporate bonds by reducing the blackout period in Japan, simplifying or omitting issuance procedures, omitting procedures in the secondary market, and reducing procurement-related costs, including disclosure costs. This can be done through the establishment of a public issue market for Professional Investors that eschews the legal disclosure requirements applied to retail investors.

The expansion and diversification of funding sources (greater distribution of debt portfolios) can be carried out by

- (i) creating a professional issuing market employing English-language disclosure, increasing convenience for overseas issuers; and
- (ii) limiting market participants to institutional investors and other professionals to ease the obligation of disclosure for issuing companies, and thus expand opportunities for funding for Japanese and regional issuers.

C. Inconvenience of the Current Disclosure System for Public Offering

Many Japanese corporate bond issuers have critical views of the current disclosure system. The Japanese public offering market for domestic corporate bonds has been subjected to strict disclosure requirements that were originally designed for the Japanese retail investors. In reality, most of the bonds issued have been purchased by Professional Investors. On the other hand, existing private placement markets in Japan are not easy to use for issuers and investors. They do not have a secondary market. As a result, due to strict restrictions, the chance and the period that issuers can make quick and timely issuance of corporate bonds in the Japanese domestic market are extremely limited through the year in comparison to the Eurobond market.

Instead, domestic securities regulations for retail investors, such as legal disclosure regulations, will not apply in the TPBM. By excluding ordinary and amateur investors, such as private individuals, and catering exclusively to Professional Investors, this new market will be able to waive the legal obligation of disclosure that is applied to retail investors.

D. Underwriting Examination (Due Diligence) by Securities Companies

1. Current Practice of Underwriting Examination by Securities Companies

a. Public Offering

All public offerings in the Japanese domestic bond market are subject to an underwriting examination (due diligence), which are conducted in line with JSDA Rules Concerning Underwriting, etc. of Securities and Detailed Rules Relating to Rules Concerning Underwriting, etc. of Securities (hereafter JSDA Underwriting Rules) by each underwriting syndicate member's Underwriting Examination Department or Underwriting Examination Board who is obliged to manage the underwriting examination independently from underwriting business promotion units such as corporate finance groups, debt capital markets, and investment banking groups. Unless JSDA Underwriting Rules are fulfilled and

approved by the Underwriting Examination Department or the Underwriting Examination Board, the securities company is not allowed to underwrite the bonds.

Also, the JSDA Underwriting Rules require the lead manager(s) to obtain a comfort letter. Exempt issuers such as sovereign and quasi-sovereign issuers may be outside the scope of the comfort letter.

The JSDA Underwriting Rules specify what items need to be checked from the viewpoint of the FIEA and other relevant rules and regulations. The major items of the present underwriting examination, to be conducted by the (lead) underwriting securities company, are referenced in Table 46.

Table 46: Excerpt of Underwriting Examination Items from the Rules and Detailed Rules Concerning Underwriting, Etc. of Securities

Excerpt of Rules Concerning Underwriting, Etc. of Securities	Excerpt of Detailed Rules Relating to the Rules Concerning Underwriting, Etc. of Securities
<p>(Underwriting Examination Items of Corporate Bond Certificates)</p> <p>Article 18 When a Regular Member Underwriter underwrites the public offering or secondary distribution of Corporate Bond Certificates, it must conduct a strict examination on at least the Underwriting Examination Items set forth in each Item below:</p> <ol style="list-style-type: none"> (1) Eligibility; (2) Financial condition and cash flow; (3) Purpose of use of the funds to be raised; (4) Proper disclosure of company's business, etc.; and (5) Other matters that the Regular Member deems necessary. <p>2. In case other Regular Member Underwriter underwrites the public offering or secondary distribution of Corporate Bond Certificates under the shelf registration (registration prescribed in the Article 23-3, paragraph 1 of the FIEA; the same shall apply hereinafter), and if the Underwriting is subject to either of the criteria set forth in each Item below, it shall examine the matters that it deems necessary in its judgment and responsibility regardless of the Article 12, paragraph 1 and the preceding paragraph:</p> <ol style="list-style-type: none"> (1) The amount of each Corporate Bond Certificate is 100 million yen or more; or (2) The total amount of the corporate bonds divided by the minimum amount of each Corporate Bond Certificates is less than 50. <p>3. Details of the Underwriting Examination Items prescribed in paragraph 1 shall be defined in the Detailed Rules.</p>	<p>(Details for Underwriting Examination Items of Corporate Bond Certificates, etc.)</p> <p>Article 11 When underwriting the public offering or a secondary distribution of Corporate Bond Certificates prescribed in the provision of Article 18, paragraph 3 of the Rules, the details of Underwriting Examination Items shall be set forth in each Item below:</p> <ol style="list-style-type: none"> (1) Eligibility; Whether it falls under anti-social forces, and whether there is a relationship with anti-social forces; (2) Financial condition and cash flow <ol style="list-style-type: none"> (i) Soundness of the financial conditions and cash flow; (ii) Analysis of changes in the financial conditions, business performance, and cash flow; (3) Purpose of use of the funds to be raised <ol style="list-style-type: none"> (i) Appropriateness of the purpose of use of the funds to be raised; (ii) Proper disclosure of the purpose of use of the funds to be raised; (iii) Appropriation of funds raised in the past. (4) Proper disclosure of company's business, etc. <ol style="list-style-type: none"> (i) Appropriateness of company information disclosed such as the business risks, completeness of the scope of the disclosure, and adequacy of the representation of the disclosed information; (ii) Proper disclosure of the status after the end of the latest business year.

FIEA = Financial Instruments and Exchange Act.
Source: JSDA.

b. Private Placement

The JSDA Underwriting Rules will not officially apply to SN-PP, QII-PP, or Offers to Professional Investors. Underwriting examinations will be conducted depending on an underwriter's judgment on its necessity. In the private placement scheme, an underwriter may acquire a comfort letter as long as the relevant parties agree.

2. Critical Feedback on the Practice of Underwriting Examination

In light of the stagnant issuance of corporate bonds in Japan, the JSDA started its initiative for the vitalization of Japan's corporate bond market by establishing a dedicated study group in 2008 in which the practice of underwriting examination was recognized as one of the major subjects to be further deliberated.

In fact, issuing companies and other stakeholders in Japan's corporate bond market indicated various critical impediments in Japan's bond issuance environment and the current practice of underwriting examination as follows:

a. Issuers' Viewpoint

- (i) Listed companies are already required to comply with the prescribed quarterly disclosure, internal control reporting, and confirmation document requirements under the FIEA for the purpose of ensuring timely disclosure of financial and corporate information, and are subject to an audit and review by a certified public accountant or audit corporation. Given that the financial statements are prepared using such a comprehensive quality control system, securities companies should simplify and adopt a more flexible process for the underwriting examination.
- (ii) Currently, companies tend to avoid the issuance of corporate bonds during periods when a quarterly report needs to be submitted between the determination of corporate bond issuance conditions and payment for the bonds. Securities companies also are generally conservative in their underwriting examinations even after the submission of a quarterly report. These attitudes limit and concentrate the issuable period for corporate bonds and thus impede flexible issuance (see also section C for related information).

b. Underwriting Securities Companies' Viewpoint

Securities companies need to conduct a certain level of checking in their underwriting examinations to protect investors. However, to simplify and flexibly carry out the underwriting examination, it has been suggested that those compiling a prospectus must take responsibility for it. It is also necessary to clearly indicate the policy under the FIEA on how to share the responsibilities in cases when an error is found in the financial information of a prospectus, and to fully disseminate such a policy to the relevant stakeholders

3. Framework of the Underwriting Examination by Securities Companies

On 25 May 2011, JSDA formulated based on the above deliberation, the Guideline for Corporate Bond Underwriting Examination under the Shelf Registration System by the Securities Company, and notified it to securities companies.

4. Basic Framework of Underwriting Examination for Bonds under Shelf Registration System by a Securities Company

In order to enhance the contents of underwriting examination from the viewpoint of investor protection and to enhance a more flexible bond issuance, the review of underwriting examination practices has been carried out as follows:

(a) *Development of the Basic Framework of Underwriting Examination of Corporate Bonds*

In order to ensure a more flexible corporate bond issuance, when examining continuous disclosure of corporate bonds, a securities company shall carry out, as a general rule, at the time of submission of a securities report, a confirmation to issuing company that made a shelf registration and to auditors by means of Common Questions. At the time of submission of a quarterly report, it shall conduct an in-house examination, focusing on quarterly reports, press releases made by issuing company that made a shelf registration, rating information, and other publicly disclosed information; and update its underwriting stance.

(b) *Review of the Basic Contents of Underwriting Examination of Corporate Bonds*

- (i) When conducting an underwriting examination of corporate bonds on the assumption that the quality assurance of the financial statements, etc. by an issuing company that made a shelf registration and auditors have been made sufficiently, the underwriting securities company shall examine by focusing on the capacity of paying bond principal and interest and disclosure of risk factors (analysis and disclosure of certain matters affecting the future cash flow generation force) that are considered to have a large impact on investment decisions by investors.
- (ii) When conducting an underwriting examination of financial statements, etc., the underwriting securities company shall stand in a position to analyze the financial statements, etc. from the outside, and if it finds any suspicious events or there is a concern that a suspicious event has occurred, it shall collect additional information from the issuing company and auditors, and deepen the study.
- (iii) For Common Questions that are available in examining continuous disclosure of corporate bonds, in order to ensure they reflect the real status of each issuing company that made a shelf registration, a sample of the Common Questions shall be compiled and reviewed as needed in the future.

5. How to Conduct Underwriting Examination of Financial Statements, Etc. by the Lead Underwriting Securities Company

For the underwriting examination of financial statements, etc. by the lead underwriting securities company, the Guideline for Underwriting Examination of Financial Statements, Etc. has been compiled based on the securities regulations and precedent cases in the US market, and after having made deliberations and analysis as stated below:

(a) *Civil Responsibility under Financial Instruments and Exchange Act Regarding False Statements, Etc. of Financial Statements, Etc.*

- (i) When a lead underwriting securities company underwrites securities, if there was a misstatement or lack of statements regarding material facts in the financial statements that have been audited by the auditor, it may bear the liability together with the issuing companies and auditors for damages to investors under Article 21(1) iv. of the FIEA, and it may also bear the same liability as a user of a prospectus under Article 17 of the FIEA. This liability prescribed by the FIEA states that if such a securities company does not prove that it has paid “due care,” it cannot be exempted from such liability (FIEA, Article 17, proviso).
- (ii) The discipline required by Article 17 of the FIEA is based on the expectation regarding the roles and functions of the lead underwriting securities company as a gatekeeper on the accuracy of the description of the financial statements, etc. On the other hand, as the definition of due care is somewhat ambiguous, there is criticism that the underwriting examination by the lead underwriting securities company becomes overly conservative and impedes the flexible offering or secondary distribution of securities.

(b) *Regarding Due Care*

The due care that the lead underwriting securities company must pay can be understood as follows:

- (i) As the lead underwriting securities company carries out the underwriting examination from the standpoint of the outsider who cannot enter the internal controls related to the accounting system and financial reporting of the issuing company, such a lead underwriting securities company is considered not to be required to conduct again the same act as an audit by auditors with due care.
- (ii) For this reason, it is thought to be rational and practical that the lead underwriting securities company examines focusing on the presence or absence of the facts that may suspect the appropriateness of trust on the audit certificates made by the auditor as an expert.

(c) *Formulation of Guideline for Underwriting Examination of Financial Statements, Etc.*

- (i) In order to streamline and improve the efficiency of practices relating to underwriting examination in the lead underwriting securities company, based on the above arrangement of the basic idea,

the (Draft) Guideline for Underwriting Examination of Financial Statements, Etc. has been compiled to deal with how to confirm the presence or absence of suspected facts that will make audit certificates untrustworthy and matters to be noted and confirmed for making an underwriting decision.

- (ii) This (draft) guideline is to be applied when conducting the underwriting examination for corporate bonds, while the underlying principles can be applied to the entire underwriting examination of securities.
- (iii) On 9 May 2012, based on the above consideration and targeting the underwriting examination of offering or underwriting of the secondary distribution of shares, etc. and corporate bonds (except for the underwriting of the initial public offering), the Guideline for Underwriting Examination of Financial Statements, etc. was compiled and notified to the securities companies by the JSDA.

6. Positioning and Treatment of Comfort Letter

- (1) When the lead underwriting securities company conducts an underwriting examination, it shall request auditors to create a comfort letter in order to conduct an investigation, etc. regarding the accuracy of the financial information that is described in the Securities Registration Statement, etc. in connection with the offering or sale of shares, etc. or bond certificates, and the posterior changes of the financial information.
- (2) A comfort letter is a research report on the issuing company and is created according to the Summary of the Letter from Auditors to Lead Underwriting Securities Company by Japanese Institute of Certified Public Accountants and JSDA. It is also based on the Practical Guidelines of Japanese Institute of Certified Public Accountants: Audit and Assurance Practice Committee Report No. 68 About the Letter from Auditors to Lead Underwriting Securities Company.
- (3) The JSDA and the Japanese Institute of Certified Public Accountants have exchanged views regarding identification and analysis of challenges in the practice of treatment of the comfort letter in view of ensuring the accuracy and reliability of financial information and disclosure documents to investors, reduced issuing company burden, timely issuance of corporate bonds, and practical feasibility by certified public accountants. It is desired that further deliberation on and development of specific measures, such as a compilation of questions to be addressed to auditors from underwriting securities companies, are made through the continuous exchange of views.

E. Determination Process for Corporate Bond Issuance Conditions

The establishment of a rational determination process for corporate bond issuance conditions is necessary.

While securities companies conduct a bond demand estimate survey in the process of determining conditions of issuance, the resultant conditions do not necessarily reflect market conditions due to duplicated or false demands. This is one of the factors that triggers a sale

at a discount, or a sale under conditions inferior to the conditions of issuance, of corporate bonds in the secondary market.

For instance, in the US the so-called pot system is commonly used for the determination of corporate bond issuance conditions. The system eliminates the duplicate or false-investor demand and increases the transparency of the conditions determination process. It also standardizes the corporate bond issuance procedure and shortens the period required for issuance, resulting in smoother issuance of corporate bonds.

Market participants have seen some corporate bond issuances that used the pot system in Japan. Market participants believe that it is necessary to establish a guideline to share common views on practical issues, such as thorough control of client data by securities companies, and to find a solution as soon as possible for the purpose of establishing a rational determination process for corporate bond issuance conditions. Introducing the pot system in Japan may be one option. In any case, careful examination is required.

F. Measures to Cope with Default Risk

For the vitalization of the corporate bond market, it is necessary to develop and construct a lower-rated corporate bond market that enables not only high-rated issuers but also corporations with relatively higher credit risk to use the corporate bond market. The JSDA and market participants plan to develop the following measures that will protect investors when business conditions deteriorate in issuing companies or companies default on their corporate bonds, for the purpose of expanding the investment in corporate bonds issued by companies with relatively higher credit risk.

1. Granting of Covenants and Information Disclosure

(a) Granting of Covenants

- (i) Since the abolishment of eligibility standard and the deregulation of the financial special contract in 1996, issuers can flexibly grant covenants on corporate bonds issued in and after 1996 reflecting the financial condition of the issuer. The JSDA believes that such a flexible scheme should be maintained and enhanced in the future for vitalization of the corporate bond market.
- (ii) Currently, covenants granted on corporate bonds issue mainly cover the negative pledge clause (a clause prohibiting the issuer from creating any security interest over a certain property specified in the provision) and cross acceleration.
- (iii) While the negative pledge clause is a special agreement to protect investors that prohibits the issuer from creating a security interest over other nonsecured debts, it is usually effective only among corporate bonds. In 2009, only two corporate bonds targeting individual investors had covenants covering other debts and loans. On the other hand, for loans, a certain preservation measure is generally taken in response to the condition of the debtor at the time of executing the loan. In this regard, corporate bonds that were issued before the loan are likely to defer to other debts and loans from a property preservation viewpoint. Therefore, theoretically, the granted

covenants may affect the recovery of debt in the case of a corporate bond default by a company with relatively higher risk.

- (iv) In the future, when the JSDA and market participants promote expanding issuance of and investment in corporate bonds issued by corporations with relatively higher credit risk, it will be necessary to develop an environment where various kinds of covenants can be granted flexibly to reflect the capital and financial policies of the issuer and to meet the needs of investors, with such covenants being fully reflected in the issuance conditions for corporate bonds. Yet, difficulties can arise when the bond issuer disapproves the covenants to avoid the issue.
- (v) Taking into consideration examples in the US, the JSDA and market participants need to prepare a model of standard covenants for corporate bonds issued by corporations with relatively higher credit risk as a reference for issuers, investors, and securities companies. It will also be necessary to disseminate market practices that enable fundraisers to grant flexible covenants and determine reasonable issuance conditions. But, in Japan, as a general practice, the secured bank loans system has been established; it may be difficult to introduce the US system directly.
- (vi) Among these issues, the JSDA and market participants should address the use of secured corporate bonds issued by corporations with relatively higher credit risk and the relationship of these corporate bonds to the order of priority of loan pledges.

(b) Disclosure of Information on Covenants

- (i) The type of covenants granted affects the holder of corporate bonds when the corporate bond is in default and the holder tries to recover the debt. Therefore, it is important for holders to check the covenants granted on other corporate bonds and loans. Holders cannot be confident in making an investment in corporate bonds without proper disclosure of covenants granted on other debts.
- (ii) In Japan, covenants granted on corporate bonds are disclosed in a prospectus as a disclosure item at the time of issuance. In the standard form, covenants of debts including loans are to be disclosed in the annual securities report. However, it may be difficult to say whether that is a standard practice in Japan.
- (iii) As of the end of FY2009, 219 companies had disclosed the covenants of loans and other debts in their annual securities reports. Many covenants relate to financial indicators such as maintenance of net assets and maintenance of profits. There were a few companies that disclosed covenants relating to default such as cross acceleration.
- (iv) In the US, covenant information on corporate bonds and loans is disclosed as follows:
 - (1) The annual Form 10-K discloses basic information such as the type of covenants, whether or not the covenants are granted, and the compliance status. JSDA does not know these details, as no indication is made as to which covenants are granted on which debts.

- (2) If the corporate bond or loan is subject to important events that require submission of the current report Form 8-K, the detailed information is disclosed on that form. Form 8-K is a very broad form used to notify investors of any material event that is important to shareholders or the US Securities and Exchange Commission (SEC). This is one of the most common types of forms filed with the SEC. After a significant event like bankruptcy or the departure of a Chief Executive Officer, a public company generally must file a current report on Form 8-K within 4 business days to provide an update to previously filed quarterly reports on Form 10-Q and/or annual reports on Form 10-K. Form 8-K is required to be filed by public companies with the SEC pursuant to the Securities Exchange Act, 1934 (as amended). A Form 10-K is an annual report required by the SEC that gives a comprehensive summary of a public company's performance. Although similarly named, the annual report on Form 10-K is distinct from the often glossy "annual report to shareholders," which a company must send to its shareholders when it holds an annual meeting to elect directors (though some companies combine the annual report and the 10-K into one document). The 10-K includes information such as company history, organizational structure, executive compensation, equity, subsidiaries, and audited financial statements, among other information.
- (v) For the purpose of developing an environment where investors can be confident in making an investment in corporate bonds, the JSDA and market participants need to discuss the following issues based on the disclosure system in the US, and take measures to properly disclose the necessary information on covenants from an investor-protection viewpoint.
 - (1) Disclosure in an annual securities report (promotion of disclosure of covenants about default)
 - (2) Statutory disclosure equivalent to the current report Form 8-K in the US
 - (3) Timely disclosure required by securities exchanges.

2. Commissioned Company for Bondholders

- (a) *Credit Risk of Corporation and Commissioned Company for Bondholders*
 - (i) A commissioned company for bondholders is in principle appointed at the time of issuance of corporate bonds under the Companies Act and acts as a statutory agent of corporate bondholders to monitor the financial condition of the issuer and preserve or recover the debts at the time of default.
 - (ii) While the commissioned company for bondholders is appointed for corporate bonds targeting individual investors, most corporate bonds targeting institutional investors do not appoint a commissioned company for bondholders.
 - (iii) It is necessary to maintain the current system that enables a corporation with relatively lower credit risk and a high profile in the corporate bond market to issue corporate bonds flexibly at lower

cost. On the other hand, for the purpose of promoting issuance of and investment in corporate bonds of a corporation with relatively higher credit risk, it is possible to grant various covenants as mentioned above on such corporate bonds. Market participants also need to develop an environment where the commissioned company for bondholders can sufficiently fulfill the role of monitoring financial condition and preserving or recovering debts, and where such covenants can be properly reflected in the issuance conditions.

- (iv) Market participants also need to prepare a system whereby the absence of a commissioned company for bondholders would not damage the credibility of the corporate bonds issued by such companies and the corporate bond market as a whole if the credit risk increases due to deterioration in the business conditions of the issuer.
- (v) Market participants can choose two approaches regarding the appointment of a commissioned company for bondholders: (a) appoint a commissioned company for bondholders for all corporate bonds, or (b) appoint a commissioned company for bondholders of corporate bonds issued by a corporation with a relatively higher credit risk. For the time being, while discussing the tasks of the commissioned company for bondholders, it is useful for market participants to establish approach (b) as a market practice.
- (vi) In the case of corporate bonds issued by a corporation with relatively higher credit risk, market participants will need to prepare and illustrate by example a standard model of appointing a commissioned company for bondholders that can be used as a reference for issuers, investors, and securities companies, and establish the appointment of a commissioned company for bondholders as a market practice.
- (vii) Many house banks of the issuers, referred to as main banks in Japan, play the role of a commissioned company for bondholders. Some market participants are concerned that a conflict of interest could occur before or after corporate bonds default if, in the future, corporate bonds issuers become more diversified and more corporations with relatively higher credit risk issue corporate bonds. Therefore, market participants need to take measures to increase the credibility and transparency of tasks assumed by the commissioned company for bondholders, as well as discuss what tasks they are to assume.

(b) Commissioned Company for Bondholders in the Future

- (i) One of the reasons why many issuers do not appoint a commissioned company for bondholders is that issuers are doubtful about whether the tasks assumed by the commissioned company for bondholders justify the cost incurred by the issuer. On the other hand, commissioned companies for bondholders point out that their responsibilities as a commissioned company for bondholders are substantial under the Companies Act.
- (ii) The relationship between the responsibilities and costs of the commissioned company for bondholders should be considered carefully based on the fact that the credit risk of the issuer closely

relates to the responsibilities of the commissioned company for bondholders. Market participants need to define the tasks assumed by a commissioned company for bondholders and also establish a system in which these various factors can be properly reflected in the costs through a market mechanism.

- (iii) Tasks assumed by a commissioned company for bondholders in the US (Trustees) are significantly different before and after corporate bonds default. Particularly, the tasks before default include only administrative processes, such as receiving a disclosure document, including the annual report, on a regular basis. They do not include the tasks of requesting financial information, monitoring, and review.
- (iv) Based on the tasks of a Trustee in the US, there is a need to consider that, for example, the tasks of a commissioned company for bondholders will be limited to the preservation and recovery of debts after the default of corporate bond, or that different requirements will be set for appointing a commissioned company for bondholders and for its tasks depending on the credit risk of the issuer or the type of investors.
- (v) It is possible that the position and the rights of corporate bondholders will be affected by an event concerning the corporate bond issuer besides default, such as a merger or acquisition. Therefore, market participants need to discuss how to handle event risk as one of the issues relating to the tasks assumed by a commissioned company for bondholders.

G. Bond Investment Education and Bond Investor Relations

There are few opportunities in Japan to educate individual investors about corporate bonds and there is not sufficient basic data provided for the investment in and the analysis of corporate bonds, such as which corporate bonds are issued and traded, interest rates, and prices.

Some institutional investors have yet to establish an adequate research system and nurtured enough analysts to conduct credit analysis of individual issues, which has become a mid- to long-term issue in the market. Moreover, when investing in corporate bonds, investors, in some cases, significantly rely on external rating agencies, and tend to adopt a similar investment strategy with those adopted by other institutional investors.

Investor relation activities for corporate bonds are important as an interactive communications tool between the issuer and investors. Some parties insist that the issuer should carry out investor relation activities proactively and continuously.

In addition to enhancing and organizing corporate bond investment education programs and basic data on the corporate bond market, it is necessary to exchange opinions with institutional investors and actively encourage corporate bond investor relation activities by issuers to promote further understanding of corporate bond investment.

H. Opportunities for the Japanese Market and Its Participants

ASEAN+3 Multi-Currency Bond Issuance Framework

The ASEAN+3 Multi-Currency Bond Issuance Framework (AMBIF) is a policy initiative under the Asian Bond Markets Initiative (ABMI) to create a nexus among domestic professional bond markets in the region to help facilitate intraregional transactions through standardized bond and note issuance and investment processes.

The implementation of AMBIF is expected to benefit not only AMBIF issuances, but the Japanese—and other ASEAN+3—bond markets at large. ABMI and Japanese policy bodies and regulatory authorities are focused on achieving a suitable balance between bank loans and capital market funding opportunities for corporates. AMBIF was created to provide an additional bond and note issuance avenue for these corporates. In Japan, AMBIF focuses on the issuance and listing of bonds and notes on TPBM (please see Chapter II.H and Chapter III.H for more details on the TPBM legal framework and listing practices, respectively).

Recent Developments and Future Direction

A. Recent Major Developments

1. Japan Securities Clearing Corporation Merged with Japan Government Bond Clearing Corporation in October 2013

The merger between the Japan Securities Clearing Corporation (JSCC) and Japan Government Bond Clearing Corporation (JGBCC) took effect on 1 October 2013. JGBCC's OTC JGB clearing was amalgamated with JSCC's other clearing services. This combination of OTC JGBs, JGB futures, and interest rate swaps broadened JSCC's coverage of JPY-denominated bonds and interest rate products.

2. Shortening the Japanese Government Bond Settlement Cycle (T+1)

In November 2014, the Working Group on Shortening the JGB Settlement Cycle released the Grand Design for Shortening the JGB Settlement Cycle (T+1) to illustrate an overview of the policy for the domestic market participants to set T+1 as the standard settlement cycle for outright transactions of JGBs.⁵⁷

In June 2015, the Working Group on Shortening the JGB Settlement Cycle agreed to set the first half of FY2018 as the target implementation timing for T+1, based on the survey results from market participants. While transactions with nonresidents are outside the scope of the T+1 implementation, the Working Group will encourage market participants to take appropriate measures in accordance with the policy discussed by major market participants to enable a faster and smoother settlement administration.⁵⁸

3. Japanese Securities Depository Center Upgrades Book-Entry System and Adopts ISO20022 Standards

In January 2014, JASDEC adopted a Pre-Settlement Matching System and Book-Entry Transfer System based on ISO20022 standards, the next-generation international standard message format.

Also in January 2014, JASDEC further enhanced settlement safety by introducing delivery-versus-payment (DVP) settlement for stock lending transactions to reduce settlement risk relating to stock lending and borrowing transactions, which can also be used for corporate bonds.

⁵⁷ Outline of the Grand Design for Shortening the JGB Settlement Cycle (T+1): http://market.jsda.or.jp/shiraberu/saiken/kessai/jgb_kentou/files/grand-design_english.pdf

⁵⁸ Target Implementation Timing for Shortening the JGB Settlement Cycle to T+1: http://www.jsda.or.jp/en/newsroom/researches-studies/files/Target_Implementation_Timing.pdf

4. ASEAN+3 Multi-Currency Bond Issuance Framework Pilot Issuance Listed on TOKYO PRO-BOND Market

Please also see the reference to the purpose of the AMBIF and resulting opportunities for the Japan bond market in Chapter IX.J.

On 28 September 2015, the TSE, part of the JPX Group and the operator of the TPBM, approved the listing of the first AMBIF bond issued in ASEAN+3. Figure 28 provides a screenshot of the announcement on the JPX website.



The listing of this bond issued in Thailand also represents the first listing of THB-denominated debt securities on TPBM. For further information on the listing process on the TPBM, please refer to Chapter III.H.

5. Launch of New Bank of Japan Financial Network System in October 2015

The BOJ launched a completely updated version of its Bank of Japan Financial Network System (BOJ-NET) on 13 October 2015. BOJ-NET, which began operations in 1988, supports two separate services, the BOJ-NET funds transfer services, and the BOJ-NET JGB services for the settlement of government bonds.

Among its many features, the new BOJ-NET contains the following three significant distinguishing features:

- (i) use of the latest information technology infrastructure and standards including the adoption of the XML message format and the ISO20022 standard for greater interoperability with other market institutions;

- (ii) high flexibility to adapt to changes in financial services and the various needs of its participants and stakeholders; and
- (iii) enhanced accessibility to cope with changes in the financial environment, such as the globalization of financial transactions and the networking of settlement infrastructures.

As a result, financial institutions using the new BOJ-NET system are expected to improve their collateral and cash management efficiency, and achieve smoother settlement of JGBs. In addition, the new BOJ-NET allows BOJ to extend operating hours until 9 p.m., effective 15 February 2016. This gives the Japanese market a longer overlap time with the operating hours of international markets and encourages smoother cross-border settlement of Japanese yen and JGBs.

B. Future Direction

1. Enhancement of the Repo Market and Its Infrastructure

To vitalize the corporate bond secondary market, it is necessary to develop and enhance infrastructure and market features such as the corporate bond repo market and the corresponding clearing and settlement functionality. Such efforts are also likely to contribute to the expansion of the primary market.

Although the corporate bond repo market is expected to work as a financing and fund management tool for market participants and, potentially, even as a means of avoiding settlement failures, the drive for repo transactions is hampered by the fact that investors buy to hold, with only a small portion of the issuance volume remaining in the market for trading.

The JSDA and market participants are engaged in discussions on how to enhance the securities settlement service functions in advance based on the corporate bond repo market and the lending functions in Europe and the US in order to cope with the anticipated growth in issuance size and the expanding needs of corporate bond repo transactions in the future.

2. Enhancement of Functions of Settlement and Clearing Systems

A clearing house is an indispensable tool to mitigate settlement risk, improve efficiency for investors and market participants, and ensure liquidity. However, as the issuance sizes of and transactions in the corporate bond market are limited and the netting effect of corporate bonds would not be significant, the JSDA and market participants have not yet established a clearing agency like the one that exists for government bonds. Market participants need to hold discussions about the establishment of a clearing house for corporate bonds and other functional enhancements of a settlement and clearing system for corporate bonds in order to meet the anticipated growth in issuance size and other factors, including risk mitigation and regulatory requirements, that point to the need for a clearing house.

3. Promotion for Issuance and Intraregional Distribution of Foreign-Currency-Denominated Bonds Issued in the Tokyo Market

For the development of the bond market, the promotion of the issuance and intraregional transactions of foreign-currency-denominated bonds issued in the Tokyo market is an important issue.

For the smooth issuance and distribution of the foreign-currency-denominated bonds issued in the Tokyo market, it is important to be able to achieve DVP settlement for investors. In Japan, in the case of JPY-denominated bonds, DVP settlement is already possible by linking the securities transfer through JASDEC and the yen settlement through the BOJ.

Also, in overseas markets, international CSDs can provide the settlement function of foreign currency funds together with the securities settlement function. By doing so, they can achieve DVP settlement of foreign-currency-denominated bonds. However, JASDEC is currently not able to support such a function.

In Japan, private financial institutions already offer a settlement function for foreign currency funds. However, the full DVP settlement function for foreign-currency-denominated bonds issued in the Tokyo market has not been realized yet.

Taking into consideration the above mentioned points, and toward promotion of foreign-currency-denominated bonds issued and distributed in the Tokyo market, there will be a need to continue discussions and seek a better solution among market participants and related institutions.

4. Effective Use of New Bank of Japan Financial Network System

Please also refer to the information on the implementation of the new BOJ-NET system in section A.6 in this chapter.

The comprehensive implementation of various international regulations would generally increase demand for collateral, particularly for high-quality collateral assets that are typically government bonds such as JGBs or very high-quality corporate bonds. For example, demand for high-quality liquid assets is expected to increase as a result of the introduction of the Liquidity Coverage Ratio, which took effect in January 2015. As for the regulations for OTC derivatives transactions, mandatory central clearing of standardized OTC derivatives transactions would increase demand for collateral to be posted to central counterparties. In addition, margin requirements for non-centrally cleared derivatives, which took effect in December 2015, are very likely to increase the total amount of posted collateral and have a significant operational impact because of the resulting frequent deliveries of collateral.

As previously explained, it is becoming increasingly important to optimize the use of collateral across borders and to move collateral flexibly. Under these circumstances, enabling greater use of JGBs as prime high-quality collateral assets both in Japan and abroad will benefit not only financial institutions in Japan but also financial institutions elsewhere and, ultimately, the global financial system.

The recent launch and the extended operating hours of the New BOJ-NET system will help facilitate the use of JGBs as high-quality collateral assets worldwide.

Appendix 1

Group of Thirty Compliance

The Group of Thirty recommendations were originally conceived as the group's standards on securities settlement systems in 1989, detailing in a first-of-its-kind report nine recommendations for efficient and effective securities markets covering legal, structural, and settlement process areas. The recommendations were subsequently reviewed and updated in 2001 under the leadership of the Bank for International Settlements and through the efforts of a joint task force of the Committee on Payment and Settlement Systems and the technical committee of the International Organisation of Securities Commissions. Compliance with the Group of Thirty recommendations in individual markets is often an integral part in securities industry participants' and intermediaries' due diligence process.

Table A1: Group of Thirty Compliance for Japan

Recommendation	Implemented
1 Eliminate paper and automate communication, data capture, and enrichment	Yes
2 Harmonize messaging standards and communication protocols	Yes
3 Develop and implement reference data standards	Yes
4 Synchronize timing between different clearing and settlement systems and associated payment and foreign exchange systems	Yes
5 Automate and standardize institutional trade matching	(Yes)
6 Expand the use of central counterparties	(Yes)
7 Permit securities lending and borrowing to expedite settlement	Yes
8 Automate and standardize asset servicing processes, including corporate actions, tax relief arrangements, and restrictions on foreign ownership	Yes
9 Ensure the financial integrity of providers of clearing and settlement services	Yes
10 Reinforce the risk management practices of users of clearing and settlement service providers	Yes
11 Ensure final, simultaneous transfer and availability of assets	Yes
12 Ensure effective business continuity and disaster recovery planning	Yes
13 Address the possibility of failure of a systematically important institution	Yes
14 Strengthen assessment of the enforceability of contracts	Yes
15 Advance legal certainty over rights to securities, cash, or collateral	Yes
16 Recognize and support improved valuation methodologies and closeout netting arrangements	Yes
17 Ensure appointment of appropriately experienced and senior board members (of the boards of securities clearing and settlement infrastructure providers)	Yes
18 Promote fair access to securities clearing and settlement networks	Yes
19 Ensure equitable and effective attention to stakeholder interests	Yes
20 Encourage consistent regulation and oversight of securities clearing and settlement service providers	Yes

Source: Group of Thirty (G-30), 2003. Global Clearing and Settlement – A Plan of Action. <http://newsite.group30.org/publications/detail/123>

Appendix 2

Group of Experts Report— Market Barriers Assessment

The Group of Experts (GoE) Report refers to the published results in 2010 of the GoE formed under Task Force 4 of the Asian Bond Markets Initiative. In the report, published under the leadership of the Asian Development Bank, a group of securities market experts from the private and public sectors in ASEAN+3 economies, as well as international experts, assessed the region's securities markets for potential market barriers, the costs of cross-border bond transactions, and the feasibility of establishing a Regional Settlement Intermediary.¹ The findings in the GoE Report led to the creation of the ASEAN+3 Bond Market Forum.

Table A2: Summary of the Group of Experts Market Barriers Assessment

Japan			
Potential Barrier	Status as of 2010	Market Assessment Questionnaire Scores	Overall Barrier Assessment
Quotas	There are no market entrance requirements for foreign investors.	OK	OK
Investor registration	There are no registration requirements for foreign investors.	OK	OK
FX controls—conversion	The Japanese yen is freely convertible. There are no foreign exchange restrictions. Both third-party foreign exchange (FX) and offshore FX transactions are possible.	OK	OK
FX controls — repatriation of funds	As above. Sale proceeds or income from investments can be freely repatriated.	OK	OK
Cash controls—credit balances	Foreign investors can freely open cash accounts in Japanese yen. Credit balances are allowed.	OK	OK
Cash controls—overdrafts	There are no restrictions on overdrafts for nonresidents.	OK	OK
Taxes	Taxation generally works well. However, extensive documentation may be required for exemptions. In particular, gaining exemption for municipal bond issues is onerous. As a result, International Central Securities Depositories (ICSDs) do not currently provide a service for these bonds. The calculation of tax requires historical information in some exceptional cases.	LOW	LOW

continued on next page

¹ ASEAN+3 refers to the 10 members of the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China, Japan, and the Republic of Korea.

Table A2 continued

Japan			
Potential Barrier	Status as of 2010	Market Assessment Questionnaire Scores	Overall Barrier Assessment
Omnibus accounts	Omnibus accounts are permitted.	OK	OK
Settlement cycle	The settlement cycle is T+3.	OK	OK
Message formats	The Japan Securities Depository Center (JASDEC) (the central securities depository [CSD] for corporate bonds), and most local market participants, use SWIFT message formats. However, BOJ-NET (the CSD for government bonds) does not use SWIFT formats.	OK	OK
Securities numbering	ISIN codes are available for all local bond issues, and are available at the time of issue. JASDEC and most local market participants use ISIN. However, BOJ-NET does not use ISIN.	OK	OK
Matching	There are trade matching and pre-settlement matching systems for bonds.	OK	OK
Dematerialization	Most corporate bonds and municipal bonds are held in JASDEC in dematerialized form. (Some physical certificates still exist.)	LOW	LOW
Regulatory framework	The regulatory regime is regarded as stable and consistent and no adverse comments were received in this area.	-	OK

BOJ-NET = Bank of Japan Financial Network System, ISIN = International Securities Identification Number, SWIFT = Society for Worldwide Interbank Financial Telecommunication.

Source: Asian Development Bank. 2010. ABMI Group of Experts Final Report Part III: Barriers to Cross-Border Investment and Settlement in the ASEAN+3 Bond Markets. Manila. [https://wpqr1.adb.org/LotusQuickr/asean3goe/Main.nsf/h_58E34A1388F9070B48257729000C0A4E/90F408746827C16248257729000C1334/\\$file/Part3.pdf](https://wpqr1.adb.org/LotusQuickr/asean3goe/Main.nsf/h_58E34A1388F9070B48257729000C0A4E/90F408746827C16248257729000C1334/$file/Part3.pdf)

Appendix 3

List of Bond Market-Related Legislation and Rules

Table A3.1: Examples of Bond Market-Related Legislation in Each Legislative Tier

Constitution	Principles, Rights, and Obligations
Statutes and Acts (Key legislation for the market and market participants)	<ul style="list-style-type: none"> • Companies Act (会社法) http://law.e-gov.go.jp/htmldata/H17/H17HO086.html (in Japanese: Latest amendment date: September 2015) (Latest version is available only in Japanese) Companies Act (Part I, Part II, Part III and Part IV) (会社法第一編第二編第三編第四編) http://www.japaneselawtranslation.go.jp/law/detail/?id=2035&vm=04&re=02 (English Translation date: 1 April 2009) Companies Act (Part V, Part VI, Part VII and Part VIII) (会社法 第五編第六編第七編第八編) http://www.japaneselawtranslation.go.jp/law/detail/?id=2052&vm=04&re=02 (English Translation date: 1 April 2009) • Banking Act (銀行法) http://law.e-gov.go.jp/htmldata/S56/S56HO059.html (in Japanese: Latest amendment date: 27 June 2014) (Latest version is available only in Japanese) http://www.japaneselawtranslation.go.jp/law/detail/?id=1870&vm=04&re=02 (English Translation date: 16 June 2009) • Financial Instruments and Exchange Act (FIEA: 金融商品取引法) http://law.e-gov.go.jp/htmldata/S23/S23HO025.html (in Japanese: Latest amendment date: 4 September 2015) (Latest version is available only in Japanese) http://www.japaneselawtranslation.go.jp/law/detail/?id=1911&vm=04&re=02 (English Translation date: 16 June 2009. Note: There is no reflection of the recent changes related to the Professional Investors Private Placement scheme in English) • Act on Book-Entry of Company Bonds, Shares, etc. (社債、株式等の振替に関する法律) http://www.japaneselawtranslation.go.jp/law/detail/?id=2451&vm=&re (Tentative English Translation date: 31 May 2013) • Act on the Securitization of Assets (資産の流動化に関する法律) http://law.e-gov.go.jp/htmldata/H10/H10HO105.html (in Japanese: Latest amendment date: 27 June 2014) (Latest version is available only in Japanese) http://www.japaneselawtranslation.go.jp/law/detail/?id=1971&vm=04&re=02 (English Translation date: 11 November 2009) • Act on Special Measures Concerning Taxation (Limited to the provisions related to nonresidents and foreign corporations) (租税特別措置法) http://law.e-gov.go.jp/htmldata/S32/S32HO026.html (in Japanese: Latest amendment date: 28 September 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=1847&vm=04&re=02 (English Translation date: 1 April 2009) (Latest version is available only in Japanese)

continued on next page

Table A3.1 continued

Constitution	Principles, Rights, and Obligations
Subordinate Legislation (Cabinet Order or Ministerial Ordinance)	<p>E.g.</p> <ul style="list-style-type: none"> • Order for Enforcement of the Companies Act (会社法施行令) http://law.e-gov.go.jp/htmldata/H17/H17SE364.html (in Japanese: Latest amendment date: 31 March 2008) http://www.japaneselawtranslation.go.jp/law/detail/?id=1932&vm=04&re=02 (English Translation date: 24 March 2010) • Ordinance for Enforcement of the Companies Act (会社法施行規則) http://law.e-gov.go.jp/htmldata/H18/H18F12001000012.html (in Japanese: Latest amendment date: 8 January 2016) (Latest version is available only in Japanese) • Ordinance for Enforcement of the Banking Act (銀行法施行規則) http://law.e-gov.go.jp/htmldata/S57/S57F03401000010.html (in Japanese: Latest amendment date: 26 November 2015) http://www.japaneselawtranslation.go.jp/law/detail/?ft=1&re=01&dn=1&x=31&y=17&co=01&ia=03&ky=%E9%8A%80%E8%A1%8C%E6%B3%95%E6%96%BD%E8%A1%8C%E8%A6%8F%E5%89%87&page=1 (English Translation date: 1 October 2010) (Latest version is available only in Japanese) • Order for Enforcement of the Financial Instruments and Exchange Act (金融商品取引法施行令) http://www.japaneselawtranslation.go.jp/law/detail/?re=02&dn=1&x=37&y=24&co=1&ia=03&yo=&gn=&sy=&ht=&no=&bu=&ta=&ty[]=B&ky=order+for+enforcement+of+the+financial+instruments+and+exchange+act&page=5 (Tentative English Translation date: 27 March 2015) • Cabinet Office Ordinance on Definitions under Article 2 of the Financial Instruments and Exchange Act (金融商品取引法第二条に規定する定義に関する内閣府令) http://law.e-gov.go.jp/cgi-bin/idxselect.cgi?IDX_OPT=5&H_NAME=&H_NAME_YOMI=%82%A0&H_NO_GENGO=H&H_NO_YEAR=&H_NO_TYPE=2&H_NO_NO=&H_FILE_NAME=H05F03401000014&H_RYAKU=1&H_CTG=1&H_YOMI_GUN=1&H_CTG_GUN=1 (in Japanese: Latest amendment date: 25 September 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=1966&vm=04&re=02 (English Translation date: 25 June 2010) (Latest version is available only in Japanese) • Cabinet Office Ordinance on the Disclosure of Corporate Affairs, etc. (企業内容等の開示に関する内閣府令) http://law.e-gov.go.jp/htmldata/S48/S48F03401000005.html (in Japanese: Latest amendment date: 25 September 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2341&vm=04&re=02 (in English. Translation date: 3 February 2010) (Latest version is available only in Japanese) • Cabinet Office Ordinance on Disclosure of Information, etc. on Regulated Securities (特定有価証券(外国投資信託証券/資産流動化証券)の内容等の開示に関する内閣府令) http://law.e-gov.go.jp/htmldata/H05/H05F03401000022.html (in Japanese: Latest amendment date: 25 September 2015) (Latest version is available only in Japanese) • Cabinet Office Ordinance on the Provision and Publication of Information on Securities (証券情報等(特定証券情報等)の提供又は公表に関する内閣府令) http://law.e-gov.go.jp/htmldata/H20/H20F10001000078.html (in Japanese: Latest amendment date: 15 May 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2063&vm=04&re=02 (in English. Translation date: 2 June 2010) (Latest version is available only in Japanese)

continued on next page

Table A3.1 continued

Constitution	Principles, Rights, and Obligations
Subordinate Legislation (Cabinet Order or Ministerial Ordinance)	<ul style="list-style-type: none"> <li data-bbox="613 369 1427 680"> <p>• Cabinet Office Ordinance on Disclosure of Information, etc. on Issuers of Foreign Government Bonds, etc. (外国債等の発行者の内容等の開示に関する内閣府令) http://law.e-gov.go.jp/cgi-bin/idxselect.cgi?IDX_OPT=2&H_NAME=&H_NAME_YOMI=%82%a0&H_NO_GENGO=H&H_NO_YEAR=&H_NO_TYPE=2&H_NO_NO=&H_FILE_NAME=S47F03401000026&H_RYAKU=1&H_CTG=1&H_YOMI_GUN=1&H_CTG_GUN=1 (in Japanese: Latest amendment date: 25 September 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2598&vm=04&re=02 (English Translation date: 5 February 2010) (Latest version is available only in Japanese)</p> <li data-bbox="613 680 1427 877"> <p>• Cabinet Office Ordinance on Financial Instruments Business, etc. (金融商品取引業等に関する内閣府令) http://law.e-gov.go.jp/htmldata/H19/H19F10001000052.html (in Japanese: Latest amendment date: 4 September 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2540&vm=04&re=02 (Tentative English Translation date: 24 March 2015) (Latest version is available only in Japanese)</p> <li data-bbox="613 877 1427 1226"> <p>• Ref. materials: Comprehensive Guidelines for Supervision of Financial Instruments Business Operators, etc. June 2014 (金融商品取引業者等向けの総合的な監督指針) http://www.fsa.go.jp/en/refer/guide/instruments.pdf (in English. June 2014) http://www.fsa.go.jp/en/refer/guide/instruments_b.pdf (Attached List of Formats II-1) http://www.fsa.go.jp/common/law/guide/kinyushohin/index.html (in Japanese. March 2016) http://www.fsa.go.jp/common/law/guide/kinyushohin.pdf (in Japanese. March 2016) http://www.fsa.go.jp/common/law/guide/kinyushohin_b.pdf (別紙様式II-1) (Latest version is available only in Japanese)</p> <li data-bbox="613 1226 1427 1423"> <p>• Cabinet Office Ordinance on Financial Instruments Exchanges, etc. (金融商品取引所等に関する内閣府令) http://law.e-gov.go.jp/htmldata/H19/H19F10001000054.html (in Japanese: Latest amendment date: 15 May 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2378&vm=04&re=02 (Tentative English Translation date : 22 May 2010) (Latest version is available only in Japanese)</p> <li data-bbox="613 1423 1427 1621"> <p>• Cabinet Office Ordinance on Financial Instruments Firms Associations, etc. (金融商品取引業協会等に関する内閣府令) http://law.e-gov.go.jp/htmldata/H19/H19F10001000053.html (in Japanese: Latest amendment date: 15 May 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2539&vm=04&re=01&new=1 (English Translation date: 15 December 2010) (Latest version is available only in Japanese)</p> <li data-bbox="613 1621 1427 1818"> <p>• Cabinet Office Ordinance on Restrictions on Securities Transactions, etc. (有価証券の取引等の規制に関する内閣府令) http://law.e-gov.go.jp/htmldata/H19/H19F10001000059.html (in Japanese: Latest amendment date: 2 September 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2507&vm=04&re=02 (English Translation date: 3 February 2010) (Latest version is available only in Japanese)</p>

continued on next page

Table A3.1 continued

Constitution	Principles, Rights, and Obligations
Subordinate Legislation (Cabinet Order or Ministerial Ordinance)	<ul style="list-style-type: none"> <li data-bbox="391 369 1192 594"> <p>• Cabinet Office Ordinance on Special Provisions, etc. for Procedures by Use of Electronic Data Processing System for Disclosure (開示用電子情報処理組織による手続の特例等に関する内閣府令) http://law.e-gov.go.jp/htldata/H14/H14F10001000045.html (in Japanese: Latest amendment date: 15 February 2012) http://www.japaneselawtranslation.go.jp/law/detail/?id=2552&vm=04&re=02 (English Translation date: 15 December 2010) (Latest version is available only in Japanese)</p> <li data-bbox="391 594 1192 905"> <p>• Order on Book-Entry of Company Bonds, Shares, etc. (社債、株式等の振替に関する命令) http://law.e-gov.go.jp/htldata/H14/H14F10002002005.html (in Japanese: Latest amendment date: 28 April 2015) http://www.japaneselawtranslation.go.jp/law/detail/?ft=1&re=01&dn=1&x=31&y=13&co=01&ia=03&ky=%E7%A4%BE%E5%82%B5%E3%80%81%E6%A0%AA%E5%BC%8F%E7%AD%89%E3%81%AE%E6%8C%AF%E6%9B%BF+%E3%81%AB%E9%96%A2%E3%81%99%E3%82%8B%E5%91%BD%E4%BB%A4&page=5 (English Translation date: 20 March 2015) (Latest version is available only in Japanese)</p> <li data-bbox="391 905 1192 1108"> <p>• Order for Enforcement of the Act on Book-Entry of Company Bonds, Shares, etc. (社債、株式等の振替に関する法律施行令) http://law.e-gov.go.jp/htldata/H14/H14SE362.html (in Japanese: Latest amendment date: 28 January 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2062&vm=04&re=02 (English Translation date: 26 November 2010) (Latest version is available only in Japanese)</p> <li data-bbox="391 1108 1192 1312"> <p>• Cabinet Office Ordinance on Financial Instruments Clearing Organizations, etc. (金融商品取引清算機関等に関する内閣府令) http://law.e-gov.go.jp/htldata/H14/H14F10001000076.html (in Japanese: Latest amendment date: 28 April 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2486&vm=04&re=02 (Tentative English Translation date: 30 April 2014) (Latest version is available only in Japanese)</p> <li data-bbox="391 1312 1192 1516"> <p>• Cabinet Office Ordinance on Financial Instruments Business, etc. (金融商品取引業等に関する内閣府令) http://law.e-gov.go.jp/htldata/H19/H19F10001000052.html (in Japanese: Latest amendment date: 4 September 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2540&vm=04&re=02 (Tentative English Translation date: 24 March 2015) (Latest version is available only in Japanese)</p> <li data-bbox="391 1516 1192 1803"> <p>• Order for Enforcement of the Act on Securitization of Assets (資産の流動化に関する法律施行令) http://law.e-gov.go.jp/cgi-bin/idxselect.cgi?IDX_OPT=5&H_NAME=&H_NAME_YOMI=%82%A0&H_NO_GENGO=H&H_NO_YEAR=&H_NO_TYPE=2&H_NO_NO=&H_FILE_NAME=H12SE479&H_RYAKU=1&H_CTG=1&H_YOMI_GUN=1&H_CTG_GUN=1 (in Japanese: Latest amendment date: 15 May 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2363&vm=04&re=02 (English Translation date: 14 June 2010) (Latest version is available only in Japanese)</p>

continued on next page

Table A3.1 continued

Constitution	Principles, Rights, and Obligations
Subordinate Legislation (Cabinet Order or Ministerial Ordinance)	<ul style="list-style-type: none"> <li data-bbox="613 369 1406 646"> <p>• Ordinance for Enforcement of the Act on Securitization of Assets (資産の流動化に関する法律施行規則) http://law.e-gov.go.jp/cgi-bin/idxselect.cgi?IDX_OPT=5&H_NAME=&H_NAME_YOMI=%82%A0&H_NO_GENGO=H&H_NO_YEAR=&H_NO_TYPE=2&H_NO_NO=&H_FILE_NAME=H12F03101000128&H_RYAKU=1&H_CTG=1&H_YOMI_GUN=1&H_CTG_GUN=1 (in Japanese: Latest amendment date: 28 April 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2517&vm=04&re=02 (English Translation date: 14 June 2010) (Latest version is available only in Japanese)</p> <li data-bbox="613 657 1406 877"> <p>• Order for Enforcement of the Act on Special Measures Concerning Taxation (Limited to the provisions related to nonresidents and foreign corporations) (租税特別措置法施行令 非居住者, 外国法人関連部分) http://law.e-gov.go.jp/htmldata/S32/S32SE043.html (Whole text in Japanese: Latest amendment date: 29 January 2016) http://www.japaneselawtranslation.go.jp/law/detail/?id=1886&vm=04&re=02 (English Translation date: 18 August 2009) (Latest version is available only in Japanese)</p> <li data-bbox="613 888 1406 1108"> <p>• Ordinance for Enforcement of the Act on Special Measures Concerning Taxation (Limited to the provisions related to nonresidents and foreign corporations) (租税特別措置法施行規則 非居住者, 外国法人関連部分) http://law.e-gov.go.jp/htmldata/S32/S32F03401000015.html (Whole text in Japanese: Latest amendment date: 2 October 2015) http://www.japaneselawtranslation.go.jp/law/detail/?id=2189&vm=04&re=02 (Tentative English Translation date: 26 October 2009) (Latest version is available only in Japanese)</p>

Source: Compiled by ABMF SF1 based on public domain information as of 21 March 2016.

Table A3.2: Japan Securities Dealers Association Self-Regulatory Rules, Etc. for Bond Transactions

<p>Rules Concerning Underwriting, Etc. of Securities (Note: These rules are based on the version in effect as of 1 January 2015) 有価証券の引受け等に関する規則</p>	<p>1992-2015/01E 2015/05J</p>	<p>CHAPTER I. GENERAL PROVISIONS CHAPTER II. APPROPRIATE UNDERWRITING SECTION 1 Conduct of Appropriate Underwriting SECTION 2 Development of Underwriting System SECTION 3 Elimination of Antisocial Forces SECTION 4 Underwriting of Parent Corporation, Etc. or Subsidiary Corporation, Etc. SECTION 5 Implementation of Proper Underwriting Examination SECTION 6 Underwriting Examination Items, Etc. CHAPTER III. CONFIRMATION WITH ISSUER AND REQUEST FOR DISCLOSURE CHAPTER IV. DETERMINATION OF FAIR TERMS AND CONDITIONS CHAPTER V. STANDBY RIGHTS OFFERING CHAPTER VI. MISCELLANEOUS http://www.jsda.or.jp/en/rules-guidelines/E41.pdf http://www.jsda.or.jp/shiryō/web-handbook/105_kabushiki/files/150519_hikiuke.pdf</p>
<p>Detailed Rules Relating to the Rules Concerning Underwriting, Etc. of Securities (Note: These rules are based on the version in effect as of 1 January 2015.) 「有価証券の引受け等に関する規則」に関する細則</p>	<p>1996-2015/01E 2015/05J</p>	<p>http://www.jsda.or.jp/en/rules-guidelines/E42.pdf http://www.jsda.or.jp/shiryō/web-handbook/105_kabushiki/files/150519_hikiuke_saisoku.pdf</p>
<p>Rules Concerning Publication of Over-the-Counter Trading Reference Prices, Etc. and Trading Prices of Bonds 公社債の店頭売買の参考値等の発表及び売買値段に関する規則 (2013/12と2014/03改正規則の施行は2015/11予定)</p>	<p>1976-2014/01E 2015/11J</p>	<p>http://www.jsda.or.jp/en/rules-guidelines/content/140101E45.pdf http://www.jsda.or.jp/shiryō/web-handbook/106_saiken/files/20151102_3goukisoku.pdf.pdf</p>
<p>Detailed Rules Relating to the Rules Concerning Publication of Over-the-Counter Trading Reference Prices, Etc. and Trading Prices of Bonds (Note: This rule is based on the 1 January 2013 edition of the original Japanese text.) 「公社債の店頭売買の参考値等の発表及び売買値段に関する規則」に関する細則</p>	<p>1991-2013/01E 2015/11J</p>	<p>http://www.jsda.or.jp/en/rules-guidelines/files/46_131025.pdf http://www.jsda.or.jp/katsudou/kisoku/files/3gousaisoku.pdf</p>

continued on next page

Table A3.2 continued

Rules Concerning Publication, Etc. of Over-the-Counter Quotation of Corporate Bonds, Etc. For Retail Customers 個人向け社債等の店頭気配情報の発表等に関する規則	2003-2009/12E 2009/12J	http://www.jsda.or.jp/en/rules-guidelines/files/47_131025.pdf http://www.jsda.or.jp/katsudou/kisoku/files/c016.pdf
Rules Concerning Solicitation, Etc. of Sale and Purchase, Etc. of Domestic CPS Etc. and Private Placement Corporate Bonds 国内C P等及び私募社債の売買取引等に係る勧誘等に関する規則	1998-2012/07E 2015/03J	http://www.jsda.or.jp/en/rules-guidelines/files/48_131025.pdf http://www.jsda.or.jp/shiryoweb-handbook/106_saiken/files/cpkisoku.pdf
Rules Concerning Handling of Sale and Purchase of Bonds with Options (Note: These rules are based on the version in effect as of 1 January 2015.) 選択権付債券売買取引の取扱いに関する規則	1992-2015/01E 2014/12J	http://www.jsda.or.jp/en/rules-guidelines/E49.pdf http://www.jsda.or.jp/katsudou/kisoku/files/201412_teikankisoku2sentakukentuki.pdf
Rules Concerning Handling of Conditional Sale and Purchase of Bonds, Etc. (Note: This rule is based on the December 2011 edition of the original Japanese text.) 債券等の条件付売買取引の取扱いに関する規則	1992-2011/12E 2010/07J	http://www.jsda.or.jp/en/rules-guidelines/files/50_131025.pdf http://www.jsda.or.jp/katsudou/kisoku/files/201504_teikankisoku1joukentukizenbun.pdf
Rules Concerning Handling of Sale and Purchase of Bonds, Etc. with Delayed Settlement (Note: This rule is based on the 1 April 2010 edition of the original Japanese text.) 債券等の着地取引の取扱いに関する規則	1992-2010/04E 2010/04J	http://www.jsda.or.jp/en/rules-guidelines/files/51_131025.pdf http://www.jsda.or.jp/katsudou/kisoku/files/201302_teikankisoku4chakutitorihiki.pdf
Rules Concerning Handling of Short Selling, and Borrowing and Lending Transactions of Bonds (Note: These rules are based on the version in effect as of 1 January 2015) 債券の空売り及び貸借取引の取扱いに関する規則	1992-2015/01E 2014/12J	http://www.jsda.or.jp/en/rules-guidelines/E52.pdf http://www.jsda.or.jp/katsudou/kisoku/files/201412_teikankisoku3taisyakurepo.pdf
Rules Concerning Distributions, Etc. of Securitized Products Standardized Information Reporting Package: SIRP (2015/06E) 証券化商品の販売等に関する規則+証券化商品標準情報レポート・パッケージ (SIRP) (2015/06J) ガイドブック (2015/09J) (Only in Japanese)	2009-2015/06E 2015/06J	http://www.jsda.or.jp/en/rules-guidelines/files/56_131025.pdf http://www.jsda.or.jp/shiryoweb-handbook/108_syoudenka/files/20151001_sirp_en.pdf http://www.jsda.or.jp/katsudou/kisoku/files/20150616_shoukennka.pdf http://www.jsda.or.jp/shiryoweb-handbook/108_syoudenka/files/20150617_SIRP.pdf http://www.jsda.or.jp/shiryoweb-handbook/108_syoudenka/files/20150907_sirp_guidebook.pdf

continued on next page

Table A3.2 continued

Rules Concerning Foreign Securities Transactions (Note: These Rules are based on the version in effect as of 1 January 2015.) 外国証券の取引に関する規則	1973- 2015/01E 2014/12J	http://www.jsda.or.jp/en/rules-guidelines/E53.pdf http://www.jsda.or.jp/shiryō/web-handbook/107_foreign/files/gaikokukisoku.pdf
Rules Concerning Solution of Fail in Bond Settlement, etc. (Only Japanese version is available) 債券等のフェイルの解消に関する規則	2000- 2016/03J	http://www.jsda.or.jp/shiryō/web-handbook/201_kansyuu/files/b004.pdf

Source: Japan Securities Dealers Association. <http://www.jsda.or.jp/en/rules-guidelines/index.html>; <http://www.jsda.or.jp/shiryō/web-handbook/index.html>

Table A3.3: Japan Securities Dealers Association Recent Guidelines Related to the Bond Market

JSDA Guideline for Ensuring Fairness in OTC Bond Transaction (Only Japanese version is available) 公社債店頭取引における公正性確保のためのガイドラインについて	1998- 2007/09J	http://www.jsda.or.jp/shiryō/web-handbook/106_saiken/files/106_saiken_kisoku-07.pdf
JSDA Guidelines for Ensuring Fairness in Domestic OTC Transactions of Foreign Stocks, Etc. and Foreign Bonds (Only Japanese version is available) 外国株券等及び外国債券の国内店頭取引における公正性確保のためのガイドラインについて	1998/11J	http://www.jsda.or.jp/shiryō/web-handbook/107_foreign/files/107_a024-04.pdf
Japanese Government Securities Guidelines for Real-Time Gross Settlement 国債の即時グロス決済に関するガイドライン (Related Q&A) Questions & Answers about Settlements under Japanese Government Securities Guidelines for Real-Time Gross Settlement and Practical Guidelines for Handling of Fails Charges (2010/11) 「国債の即時グロス決済に関するガイドライン」、「フェイルチャージの実務に関する取扱指針」及び「相對ネットィング照合等の実務に関する取扱指針」に基づく決済についてのQ&A (2013/05)	2015/10E 2016/03J 2013/12E 2013/12J	Current Version http://market.jsda.or.jp/shiraberu/saiken/kessai/rtgs/rtgs/files/151013rtgsguideline_e.pdf New BOJ-NET Version http://market.jsda.or.jp/shiraberu/saiken/kessai/rtgs/rtgs/files/160315_rtgs_gline.pdf (Related Q&A) http://market.jsda.or.jp/shiraberu/saiken/kessai/rtgs/files/shishin_qa_e.pdf http://market.jsda.or.jp/shiraberu/saiken/kessai/rtgs/files/20130515_rtgsfailaitaiqa.pdf
Practical Guidelines for Handling of Fails Charges フェイルチャージの実務に関する取扱指針	2013/05E 2013/05J	http://market.jsda.or.jp/shiraberu/saiken/kessai/rtgs/rtgs/files/20130529_shishin_e.pdf http://market.jsda.or.jp/shiraberu/saiken/kessai/rtgs/files/20130515_failshishin.pdf
JSDA Guideline for When-Issued Transactions of Japanese Government Bonds 国債の発行日前取引に関するガイドライン	2003/10E 2007/09J	http://market.jsda.or.jp/shiraberu/saiken/wi/files/wi_guideline0310.pdf http://market.jsda.or.jp/shiraberu/saiken/wi/files/gline070928.pdf

continued on next page

Table A3.3 continued

Book-Entry Transfer Guideline for Corporate Bonds 一般債の振替決済に関するガイドライン	2013/12E 2013/12J	New BOJ-NET Version http://market.jsda.or.jp/shiraberu/saiken/kessai/furikae/files/151013ippansai_guideline_e.pdf http://market.jsda.or.jp/shiraberu/saiken/kessai/furikae/files/151013ippansai_guideline.pdf
---	----------------------	---

BOJ-NET = Bank of Japan Financial Network System. OTC = over-the counter.
Source: Japan Securities Dealers Association.

Table A3.4: List of the Tokyo Stock Exchange Rules and Regulations Related to the TOKYO PRO-BOND Market

Special Regulations of Securities Listing Regulations Concerning Specified Listed Securities (as of 11 September 2015) 特定上場有価証券に関する有価証券上場規程の特例	2012- 2015/09E 2015/05J	Part 3 Bonds Chapter 1 General Provisions Chapter 2 Program Listing Chapter 3 Initial Listing Chapter 4 Obligations After Listing Section 1 Obligation to Disclose Information on Issuer, etc. Section 2 Other Obligations Chapter 5 Maintaining Order in the Market Section 1 Measures for Ensuring Effectiveness Section 2 Delisting, etc. http://www.jpx.co.jp/english/rules-participants/rules/regulations/tvdivq0000001vyt-att/specified_listed_securities_special_regulations_20150911.pdf (Part 3 Bonds, P.37-) http://jpx-gr.info/rule/tosho_regu_201305070010001.html
Enforcement Rules for Special Regulations of Securities Listing Regulations Concerning Specified Listed Securities (as of 11 September 2015) 特定上場有価証券に関する有価証券上場規程の特例の施行規則	2012- 2015/09E 2015/05J	Chapter 3 Bonds Rule 201. Disclosure Information on Websites of Issuers, etc. Rule 202. Program Listing Rule 203. Listing Agreement Rule 204. Documents to be Submitted, etc. pertaining to Initial Listing Application Rule 205. Method of Announcement at Time of Initial Listing Application Rule 206. Listing Eligibility Requirements Rule 207. Disclosure of Important Issuer, etc. Information Rule 208. Issuer Filing Information Rule 209. Fees Related to Listing Rule 210. Improvement Report Rule 211. Violation Penalty Rule 212. Period of Designation as Securities under Supervision in Measures for Ensuring Effectiveness

continued on next page

Table A3.4 continued

		<p>Rule 213. Handling of Delisting Rule 215. Handling of Delisting Day http://www.jpx.co.jp/english/rules-participants/rules/regulations/tvdivq0000001vyt-att/specified_listed_securities_special_reg_enforcement_rules_20150911.pdf (Chapter 3 Bonds, P.49-59) http://jpx-gr.info/rule/tosho_regu_201305070047001.html</p>
<p>Special Regulations of Business Regulations and Brokerage Agreement Standards Concerning Specified Financial Instruments Exchange Markets (as of 30 April 2015) 特定取引所金融商品市場に関する業務規程及び受託契約準則の特例</p>	<p>2014-2015/04E 2015/04J</p>	<p>http://www.jpx.co.jp/english/rules-participants/rules/regulations/tvdivq0000001vyt-att/specified_financial_instruments_exchange_market_special_regulations_20150430.pdf http://jpx-gr.info/rule/tosho_regu_201305070011001.html</p>
<p>Enforcement Rules for Special Regulations of Business Regulations and Brokerage Agreement Standards Concerning Specified Financial Instruments Exchange Markets (as of 12 March 2015) 特定取引所金融商品市場に関する業務規程及び受託契約準則の特例の施行規則</p>	<p>2012-2015/03E 2015/03J</p>	<p>http://www.jpx.co.jp/english/rules-participants/rules/regulations/tvdivq0000001vyt-att/specified_exchange_market_special_reg_enforcement_rules_20150312.pdf http://jpx-gr.info/rule/tosho_regu_201305070048001.html</p>

Source: Japan Exchange Group. <http://www.jpx.co.jp/english/>.

Appendix 4

Practical References

For easy access to further information about the market features described in the Japan Bond Market Guide—including the policy bodies, regulatory authorities, and securities market institutions—interested parties are encouraged to utilize the following links (all websites available in English).

AMBIF Implementation Guideline for Japan (Appendix 5: pp. 92-108)
<http://www.adb.org/publications/implementation-ambif-asean3-bond-market-forum-sf1-p3>

AMBIF—Single Submission Form (as accepted by Tokyo Stock Exchange, Listing Authority of TOKYO PRO-BOND Market [TPBM]) (Appendix 1: pp. 37-55)
<http://www.adb.org/publications/implementation-ambif-asean3-bond-market-forum-sf1-p3>

AsianBondsOnline, Asian Development Bank (ADB)
<http://asianbondsonline.adb.org/index.php>
<http://asianbondsonline.adb.org/japan/structure/overview.php>

Financial Services Agency (FSA), Government of Japan
<http://www.fsa.go.jp/en/index.html>

Japan Credit Rating Agency
<http://www.jcr.co.jp/english/>

Japan Exchange Group-Tokyo Stock Exchange (JPX-TSE)
<http://www.jpx.co.jp/english/>

TOKYO PRO-BOND Market (TPBM)
<http://www.jpx.co.jp/english/equities/products/tpbm/index.html>

Japan Securities Dealers Association (JSDA)
<http://www.jsda.or.jp/en/index.html>

Japan Securities Depository Center (JASDEC)
<http://www.jasdec.com/en/>

Japan Securities Research Institute (JSRI)
Securities Market in Japan 2014
http://www.jsri.or.jp/publish/english/english_07.html

Ministry of Finance Japan (MOF)
Debt Management Report
http://www.mof.go.jp/english/jgbs/publication/debt_management_report/ (English)

National Institute for Research Advancement of Japan
Grand Design for an Asian Inter-Regional Professional Securities Market (AIR-PSM),
March 2008
<http://www.nira.or.jp/pdf/airpsm.pdf>

Rating and Investment Information
<https://www.r-i.co.jp/eng/index.html>

Appendix 5

Recommended Expression of Related Translations

AE = alternative expression, RE = recommended expression.

(1) Laws and Ordinances

- (a) (RE) Act on *Special Measures Concerning Taxation* (Japanese law translation by Ministry of Justice) = 租税特別措置法 (*sozei tokubetsu sochihou*)
(AE) *Special Taxation Measures Law*
- (b) (RE) *Companies Act* (Japanese law translation by Ministry of Justice) = 会社法 (*kaishahou*) (AE) *Company Law*, (AE) *Corporations Act*, (AE) *Corporations Law*
- (c) (RE) *Financial Instruments and Exchange Act* 【Abbreviation: FIEA】 (Japanese law translation by Ministry of Justice) = 金融商品取引法 (*kinyuu shouhin torihikihou*) (AE) *Financial Instruments and Exchange Law* 【Abbreviation: FIEL】
- (d) (RE) *Order for Enforcement* = 施行令 (*sekourei*), Reference: Cabinet Order = 政令 (*seirei*), Cabinet Office Ordinances = 内閣府令 (*naikakufurei*)
The Order for Enforcement of the Financial Instruments and Exchange Act = 金融商品取引法施行令 (*kinyuu shouhin torihikihou sekourei*)

(2) Disclosure Documents

- (a) (RE) Specified securities information = 特定証券情報 (*tokutei shouken jouhou*)
- (b) (RE) Issuer filing information = 発行者情報 (*hakkoushajouhou*)
- (c) Securities registration statement (SRS) = 有価証券届出書 (*yuukashouken todokedesho*)
- (d) (RE) Annual securities report = 有価証券報告書 (*yuukashouken houkokusho*) (AE) securities report
- (e) (RE) Semiannual securities report = 半期報告書 (*hanki houkokusho*) (AE) Semiannual report
- (f) (RE) Quarterly securities report = 四半期報告書 (*shihanki houkokusho*) (AE) Quarterly report
- (g) (RE) Extraordinary report = 臨時報告書 (*rinji houkokusho*) (AE) Current report
- (h) (RE) Shelf registration statement = 発行登録書 (*hakkoutourokusho*)
- (i) (RE) Supplement to shelf registration statement (Practical term) = 発行登録追補書類 (*hakkoutouroku tsuihoshorui*) (AE) Shelf registration supplement (Japanese law translation by the Ministry of Justice and the Financial Service Agency's [FSA] official translation)
- (j) (RE) Securities notice = 有価証券通知書 (*yuukashouken tsuuchisho*)

(3) Offering and Distribution

- (a) (RE) Public offering 【Abbreviation: PO】 = 募集 (*boshuu*)
(Japanese law translation by Ministry of Justice and FSA's official translation) Under the FIEA, an offering which is subject to requirements to disclose the solicitation documents stipulated in the FIEA is called "public offering," and an offering which is not subject to such requirements is generally called "private placement." However, the expression does not always reflect the economic nature of the offering. For example, offering to Professional Investors is in a strict legal sense "private placement," but is similar to "public offering" by its true nature. Issuers are required to submit Specified Securities Information (SSI) to the TSE in place of Securities Registration Statement (SRS).
- (b) (RE) Public offering of newly issued securities = 新発債公募 (*shinpatsusai koubo*) Especially in the context that needs to distinguish between a public offering and a secondary distribution, this term is used.
- (c) (RE) Secondary distribution = 売出し (*uridashi*)
(Japanese law translation by Ministry of Justice and FSA's Official translation) Especially in the context that does not need to distinguish between a public offering and a secondary distribution, "public offering" is sufficient for general translation.
- (d) (RE) Professional Investor = 特定投資家 (*tokutei toushika*)
This is the most frequently used expression in the practice of business in Japan. (Japanese law translation by Ministry of Justice and FSA's official translation) Alternative expression (AE) 1 = Specific investor (This word was used in relatively old public relations [PR] materials in the FSA.)
Alternative expression (AE) 2 = Specified investor¹ (This expression had been used in the FSA's early stage PR materials.)
- (e) (RE) Private Placement for Professional Investors 【Abbreviation: PP for PI】 = 特定投資家私募 (*tokutei toushika shibo*) This word is legally correct because this is part of private placement in Japanese law (FIEA).
(RE) Offer to Professional Investors 【Abbreviation: Offer to PI】 = 特定投資家公募 (*tokutei toushika koubo*)
This word is a practical translation focusing on the reality that many investors can be subject to public offering.
(RE) Offer of newly issued securities to Professional Investors = 特定投資家(新発)公募 (*tokutei toushika shinpatsu koubo*)
If the primary market offering of the new issue is distinguished from the private placement of already-issued securities, the above expression may be used.
(AE) Primary offering to Professional Investors
- (f) (RE) Private Secondary Distribution to Professional Investors = 特定投資家私売出し (*tokutei toushika shiuridashi*) 【Abbreviation: PSD to PI】
(AE) Private placement for Professional Investors
(RE) Offer of already-issued securities to Professional Investors = 特定投資家(既発)公募 (*tokutei toushika kihatsu koubo*)
(AE) Secondary offering to specified investors
Especially in the context that needs to distinguish between a private

¹ See <http://www.fsa.go.jp/sesc/english/aboutsesc/all.pdf>; <http://www.fsa.go.jp/en/newsletter/2009/01b.html>

placement of newly issued securities and an offer of already-issued securities, this term may be used.

- (g) (RE) Securities for Professional Investors = 特定投資家向け有価証券 (*tokutei tousehika muke yuukashouken*)
This expression is used in the SESC's PR materials while the expression "(AE) Securities intended for specified investors" is used in the FSA's PR materials.²
 - (h) (RE) Private Placement for Qualified Institutional Investors (QIIs)
【Abbreviation: QII-PP】 = 適格機関投資家私募 (*tekikaku kikan tousehika shibo*)
 - (i) (RE) Private Placement of newly issued securities for QIIs
(AE) primary private placement for QIIs
 - (j) (RE) Private Secondary Distribution for QIIs 【Abbreviation: QII-PSD】 = 適格機関投資家私売出し (*tekikaku kikan tousehika shiuridashi*)
 - (k) (RE) Private Placement of already-issued securities for QIIs
(AE) secondary private placement for QIIs
 - (l) (RE) Private Placement for small number of people 【Abbreviation: SN-PP】 = 少人数私募 (*shouninzuu shibo*)
 - (m) (RE) Private Placement of newly issued securities for small number of people
(AE) Primary Private Placement for small number of people
 - (n) (RE) Private Secondary Distribution for small number of people 【Abbreviation: SN-PSD】 = 少人数私売出し (*shouninzuu shiuridashi*)
 - (o) (RE) Private Placement of already-issued securities for small number of people
(AE) secondary private placement for small number of people
- (4) Others
- (a) (RE) commissioned company or person for bondholders (practical and understandable term) = 社債管理者 (*shasaikanrisha*)
(AE) bond manager (Japanese law translation by Ministry of Justice)
(AE) Corporate Bonds Manager (used in official documentation by JSDA)
 - (b) (RE) financial instruments business operator = 金融商品取引業者 (*kin-yuushouhin torihiki gyousha*)
 - (c) (RE) registered financial institution = 登録金融機関 (*touroku kin-yuukikan*)
 - (d) (RE) financial instruments business operator, etc. = 金融商品取引業者等 (*kin-yuushouhin torihiki gyousha tou*)
 - (e) (RE) Director-General of the Kanto Local Finance Bureau = 関東財務局長 (*kantouzaimukyokuchou*)
 - (f) (AE) Director of the Kanto Local Finance Bureau (old expression)

² See <http://www.fsa.go.jp/sesc/english/aboutsesc/all.pdf>; <http://www.fsa.go.jp/en/newsletter/2009/01b.html>

Appendix 6

Glossary of Technical Terms

Listing	Typically, action of submitting a bond, note, or <i>sukuk</i> to an exchange for the purpose of price finding, disclosure, or profiling
Registration	Action of registering a bond issue, as may be applicable
<i>sukuk</i>	Islamic finance securities
<i>sukuk Ijarah</i>	specific form of <i>sukuk</i> prevalent in Japan's Islamic financial market

ASEAN+3 Bond Market Guide 2016 Japan

ASEAN+3 Bond Market Guide is a comprehensive explanation of the region's bond markets. It provides various information such as the history, legal and regulatory framework, specific characteristics of the market, trading and transaction including settlement systems, and other relevant information. Bond Market Guide 2016 for Japan is an outcome of the strong support and kind contributions of ASEAN+3 Bond Market Forum members and experts, particularly from Japan. The report should be recognized as a collective good to support bond market development among ASEAN+3 members.

About the Asian Development Bank

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to the majority of the world's poor. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

