

Approach to the “Rules on Complex Investment Trusts Similar to Over-the-counter Derivatives Transactions” and “Regulations for Direct Offering, etc. of Beneficiary Certificates, etc.”

Established on February 17, 2011
Revised on December 13, 2012

- Interpretation of the provisions of Article 3, Paragraph 1 of the “Rules on Complex Investment Trusts Similar to Over-the-counter Derivatives Transactions” and Article 4, Paragraph 2 of the “Regulations for Direct Offering, etc. of Beneficiary Certificates, etc.”

Q1 It is stipulated that “when soliciting acquisition of beneficiary certificates of new investment trusts among those established by the Management Company and managed under instructions from the settlor, the Management Company shall fully understand the characteristics and risks of the investment trust and shall not solicit acquisition of those for which a suitable customer to acquire the investment trust cannot be supposed.” Why such provision was established?

This provision is one of the requirements by the Financial Services Agency in order to strengthen its sales and solicitation rules by voluntary regulation in the “Ideas for Restrictions on Uninvited Solicitation of Derivatives Transactions” published by the Agency on September 13, 2010.

In the provision, as part of “practicing the principles of suitability,” it is stipulated that “for complex structured bonds and investment trusts similar to over-the-counter derivative transactions, which are difficult for individual customers to understand, the development of voluntary regulations to exercise such principles of suitability is required.” Specifically, they demand “the establishment of standards to determine whether or not solicitation could be commenced in accordance with the risk characteristics of product and the nature of the customers (Criteria for the Commencement of Solicitation) as well as conducting prior verification of the product as to its suitability for sale to investors (Suitability on Reasonable Grounds).”

Behind these requirements are a large number of complaints received by consumer groups, which claim that certain complex products with risk characteristics similar to derivative transactions have been sold to the elderly who do not have substantial assets nor seem to have a high level of understanding for such investment, resulting in their unexpected large losses incurred.

This provision is prescribed to put into practice the abovementioned “Suitability on Reasonable Grounds.” It provides that whenever a Full Member (Management Company) solicits its customers to acquire a beneficiary certificate of a new investment trust, the Full Member shall verify in advance the relevant investment trust to be reasonable as an investment target at least for a certain type of customers and that any investment trust for which the Full Member cannot think of suitable customers to market based on reasonable grounds shall not be solicited for acquisition.

Q2 What does the “Suitability on Reasonable Grounds” mean?

Regarding the principle of Suitability, in Article 40 of the Financial Instruments and Exchange Act provides, it is provided that “investment management company shall not or cause to, fail to protect their investors by conducting solicitation deemed inappropriate in light of such investors’ knowledge, experiences, financial conditions and objectives of entering into such financial transaction.” In other words, suitability means the appropriateness of solicitation for each customer.

In contrast, “Suitability on Reasonable Grounds” is a concept to seek confirmation that an investment trust to be solicited is reasonable at least for a certain type of customers as an investment target. It should be noted that the term “certain type of customers,” as used herein, means the scope of target customers for the relevant investment for whom such investment is deemed reasonable in consideration of the attributes, financial status, investment experiences, risk tolerance, etc. thereof.

To confirm that an investment trust is reasonable for a certain type of customers as an investment target means, in other words, that the person soliciting such acquisition (Full Member (Management Company)) must have a sufficient understanding of the said investment trust. For example, with regard to an investment trust that is expected to be solicited for acquisition only to a certain type of customers as a result of prior verification, it is necessary to ascertain that appropriate solicitation activities be conducted by sharing the verification results among the departments concerned in accordance with certain internal rules, making the scope of the target customers widely known among the concerned parties, establishing the Criteria for the Commencement of Solicitation, if necessary, providing sufficient employee training, and so on.

Q3 What kind of investment trust does the “beneficiary certificate of new investment trust” mean?

“Beneficiary certificate of new investment trust” shall apply to investment trusts that are to be newly solicited by the Full Member (Management Company) to their customers for investment after the effective date of these Regulations.

However, no new verification process shall be required for any investment trust that has been once verified at each solicitation for acquisition. In addition, with regard to any investment trust that has the same product nature and risk characteristics as an investment trust that has already been verified, verification can be considered to have been made with the confirmation that such investment trusts are of the same type. Naturally, in soliciting investment in any of these investment trusts, the Management Company is expected to conduct their solicitation activities in conformity with the intentions and circumstances of the investors in light of such investors’ knowledge, experiences, financial conditions, and objectives of entering into such financial transaction contract.

In addition, among investment trusts that have been solicited to their customers prior to the effective date of the Regulations, for example, a complex investment trust similar to the over-the-counter derivatives transactions discussed herein may be examined again if it has not been properly established that the said

investment trust is reasonable for a certain type of customers as an investment target under the existing internal rules (e.g., the case where target party of the solicitation for acquisition has not been properly examined).

The Regulations provide for the beneficiary certificates of new investment trusts. However, where it is considered that there has been a material change in the risks, etc. (price fluctuation risk, credit risk, liquidity risk, etc.) of existing investment trusts that have been verified previously (including those that had been solicited prior to the effective date of the Regulations) as result of sudden change in the investment environment (e.g., fluctuations of market conditions, system change, increased consultation and complaints, etc.), such investment trusts may be re-examined as appropriate, and consideration may be possibly given to changes in the target customers for solicitation or suspension of the solicitation for acquisition.

Contents and depth, responsible division, and procedures concerned with the verification must be practically and appropriately determined in conformity with the actual conditions of each Management Company and implemented according to the type and risk characteristics of each investment trust.

Q4 What are specifically expected by the text “to verify in advance that the relevant investment trust to be solicited is reasonable at least for a certain type of customers as an investment target”?

Verification of the same detail is not necessary for all investment trusts, and flexible response is possible for plain products such as a listed share fund. Since the purpose of examining the Suitability on Reasonable Grounds is to ascertain that the relevant investment fund is reasonable at least for a certain type of customers as an investment target, vanilla funds without complex structure and widely recognized funds in society require only simplified examination to identify and set the scope of certain type of customers.

On the other hand, for complex investment trusts, etc. similar to over-the-counter derivative transactions, it will be imperative to perform more detailed examination. The following recommendations indicate the viewpoint from which verification should be performed, and do not require that verification process be performed in the order of (1), (2), and (3). These verifications may be performed as a single process, or may be conducted individually by different divisions. In addition, in the event that the solicitation for acquisition is limited to qualified institutional investors (equivalent to the verification in (2)), the verification in (1) may be simplified or omitted, depending on the subject investment trust and/or the target investors.

(1) Decision on investment trust to be solicited

(i) Nature and degree of risk

What kind of risk the customers would suffer and when such risk occurs. Then, it is reasonable to examine if the size of such risk is acceptable to the customers. First, it is recommended to check whether or not any investment trust with similar product and risk characteristics has already been verified. If there does not exist any similar investment trust already verified, then the relevant investment trust needs to be verified.

Verification shall be made in accordance with the characteristics of a product. Especially for products with complicated structure, verification may be made carefully by conducting various

simulations, comparisons, and analyses on items including the following. It should be noted that the types of risk are not limited to the following examples.

- Price fluctuation risk: Possible impact and its magnitude caused by fluctuations in interest rates, stock prices, exchange rates, commodity prices, etc.
- Credit risk: Possibility of default of the concerned investment trust and effects on such trust caused by credit deterioration of the issuer, guarantor, counterparty, underlying assets, etc.
- Liquidity risk: Liquidity of the concerned investment trust and effects on such trust caused by the lack of liquidity of the underlying assets.

(ii) Cost and performance

Verification is required for cost to be paid by the customers. Such cost may include fees, trust fees, interest rates, etc., but actual amount or rate itself does not represent an issue. It is more important to examine whether such amount or rate is reasonable and acceptable to the customers in light of the product characteristics, trade practices, etc. For example, when introducing an investment trust with higher sales commission and trust fee rates than those of investment trusts currently being offered, it is recommended to verify the reasonableness of such high rates.

In addition, verification is required to review whether the performance expectation for the customers is reasonable according to the product attributes, etc. For example, it is appropriate to verify whether the performance expectation of an investment trust with complicated structure is reasonable in comparison with existing products with similar schemes or securities to be invested in. Furthermore, it is appropriate to investigate whether or not the same level of performance can be obtained with a simpler structure or a lower risk while investing in the same type of asset. In this process, it is also important to investigate that the expected interest yield, return, etc. are reasonable.

(2) Identification of target investors for solicitation for acquisition

(i) Target customers

Based on the results of the verification in (1) above, the existence or non-existence and the scope of target customers for solicitation for acquisition will be identified.

As a result, the Full Member shall not engage in solicitation for acquisition of the concerned investment trust when they are unable to identify suitable target customers thereof.

In addition to the verification performed in compliance with the Regulations, if the Full Member determines that it is necessary to impose certain restrictions on solicitation activities with respect to an investment trust, which they market (including setting conditions for the target customers and selection of uninvited customers for the investment), they may clearly state substance of such restrictions.

(ii) Method of imposing possible restrictions

In addition to the verification performed in compliance with the Regulations, if the Full Member determines that it is necessary to impose certain restrictions on solicitation activities with respect to an investment trust, which they market, they need to decide which to apply the “Guidelines for the Commencement of Solicitation” or the “Criteria for the Commencement of Transactions” as a method of restriction, as well as whether or not to obtain the letter of understanding from the relevant

customers.

(3) Method of solicitation for acquisition

Based on the results of the verification described in (1) and (2) above and decision on the format of solicitation for acquisition (through public offering or private placement), it is required to examine the appropriateness of the necessary marketing materials such as the prospectus, pre-contract documents, advertising, etc.

Since it is important for the person who conducts solicitation for acquisition to have a sufficient understanding of the relevant investment trust with respect to its suitability on reasonable grounds, not only appropriateness of the marketing materials but also awareness and understanding of Sales Officers and Representatives to the effect shall be checked. In particular, regarding investment trusts with complex structure, it may be advisable to provide staff education such as in-house training.

Q5 Who should perform the prior verification? Should the Legal department or Compliance departments always perform them?

With regard to the decision on the suitability of an investment trust for solicitation for acquisition, the product department, which develops and creates such investment trusts, and/or the trading department, which purchases such products, should be involved in determining the level of risks, etc. Based on such decision, it is considered desirable that the Sales management department, the Legal department, and the Compliance department should jointly identify target customers who are suitable for such investment trust.

The legal and compliance check does not always have to be conducted by an independent specialized unit. For example, when attributes of the investment trust concerned are simple or degree of risk thereof is small, or when only qualified institutional investors are solicited for acquisition, the manager of the product department may conduct the legal and compliance check.

It is also possible to conduct the verification in committee or another organization in which each department concerned participates. Including such circumstances, it is indispensable to establish an internal system for prior verification in advance.

- Interpretation of the provisions of Article 3, Paragraph 2 of the “Rules on Complex Investment Trusts Similar to Over-the-counter Derivative Transactions” and explanation of “Significant Matters” as set forth in Article 4, Paragraph 3 of the “Regulations for Direct Offering, etc. of Beneficiary Certificates, etc.”

Q6-1 What are the “Significant Matters” in connection with the offering or private placement and other business (hereinafter collectively referred to as “Direct Offering, etc.”) of complex investment trusts similar to over-the-counter derivative transactions?

In the case of engaging in offering or private placement and other business (“Direct Offering, etc.”) of complex investment trusts similar to over-the-counter derivative transactions for the customers (excluding professional investors), the following items are regarded as Significant Matters among others, in addition to risk, fees, etc. stated in a prospectus.

- (i) Estimated losses (provisional estimate) assuming the worst-case scenario regarding the level of financial indices, etc. relevant to the complex investment trust similar to over-the-counter derivative transactions.
- (ii) Fact to the effect that in the event that the situation different from the premise assumed in (i) above occurs, the amount of loss may further increase (including an explanation of such situation).
- (iii) Details of the estimate amount to be received by an investor in case of premature sale (cancellation), including the estimate amount to be received in case of premature sale or cancellation assuming a worst-case scenario in relation to the level of relevant index, etc. and the fact to the effect that the actual amount to be received for such premature sale or cancellation may be less than the estimate amount provided.

Please refer to “Q6-2” and “Q6-4” for the method of explaining the estimate amount of loss on the assumption of the worst-case scenario mentioned in (i) and amount to be received as result of premature sales (cancellation) under the assumption of the worst-case scenario mentioned in (iii).

Q6-2 What kind of explanation is necessary for the “estimate loss amount assuming the worst-case scenario (at time of maturity/redemption of contract),” which is a Significant Matter for a complex investment trust similar to over-the-counter derivative transactions?

It is necessary to explain to the customers in plain language the extent to which losses are possible to be incurred by such transaction in regard to the “estimate amount of losses based on the worst-case scenario.” There are two ways to that effect:

- (Note) This “Q6-2” explains the estimated loss amount at the time of redemption for an investment trust similar to over-the-counter derivatives. Please refer to “Q6-4” for the estimated amount of loss caused by early cancellation or premature sale.

- (i) The extent to which losses are possible to be incurred in light of historical price movements (e.g., track records) of the referenced financial indices.
- (ii) The extent to which losses are possibly incurred when the referenced financial indicator falls (or rises) to a certain degree. (Conduct sensitivity analysis by assuming multiple degrees of declines (or rises) of the relevant financial indicator.)

The method described in (i) is referred to as “explanation based on historical data,” while the method described in (ii) is referred to as “explanation based on loss simulation.” In order to inform the customers of the amount of possible loss under the assumption of the worst-case scenario in an easy-to-understand manner, it is considered essential to include, in principle, the estimate amount derived from the method described in (i) in the explanatory materials of the transaction.

However, regarding the method in (i), there may be instances where there are no historical records available for reference or measurement using historical data is not appropriate in view of the product attributes. See below for the examples of such products. In such circumstance, it may be recommended to include the estimate amount derived from the method described in (ii), an explanation as to why the estimate based on method of (i) is not given (or cannot be given) as well as circumstances where the maximum loss may occur.

Even if the estimate derived based on the method (i) is stated, it does not prohibit from including the estimate derived based on the method (ii) in accordance with the attributes of the relevant product.

Moreover, bearing in mind that the estimate based on the method (i) is calculated as per past experiences, it is necessary to additionally state that the loss incurred may further increase in an event of situation different from the premise, including an explanation as to what such situation may be. The statement “there is a possibility of further increase in loss in an event of a situation different from the premise” is required for any investment trust similar to over-the-counter derivative transactions. In particular, regarding the product for which although there has been no major change in the index in the past, the potential loss could substantially exceed the figures calculated based on the method (i) in view of its product attributes, it is advisable to devise an explanation to prevent the customers from misunderstanding that maximum loss will be only in the scope of the estimates calculated based on the method (i).

On the other hand, if there is no clear reason not to state the estimate based on the method (i), it is considered necessary to include such estimate as well as the estimate based on the method (ii).

In any case, please keep in mind that the contents must be explained to the customers in such a manner as to be easy for them to understand and not to be misleading as to the extent of loss that such transaction could incur.

<Examples of Products Unsuitable for Measurement by Historical Data>

- Products for which the reference financial index has no historical data (If any index shows similar price movements to the reference index and can be substituted for it, such substitute index shall be applied for the explanation based on historical data.) [Examples: Products that refer to individual stocks that have not been listed long enough or newly designed financial index, those with a knock-in

clause but have not reached the knock-in level in the past, etc.]

- Products with a variety of reference financial indices for which it is difficult to assume a worst-case scenario based on historical data [Example: Products with reference to a large number of individual shares, each of which has a knock-in price with varying redemption price subject to the number of knocked-in shares, etc.]
 - Product whose price or cash flow will be 100 (par value) but become 0 (nil) if the reference index reaches a certain prescribed condition where the maximum expected loss is 100%, meaning no residual value to the product. [Example: Product the redemption price of which is nil if the price of the reference stock at the time of redemption is below a certain level with par value to be reimbursed in any other instance, interest rate swap product with the maximum loss expected when variable interest rate is 0%, etc.]
 - Products for which the credit risk of an individual enterprise such as an issuer is used as a reference financial index or those products for which the credit risk is a sole factor for damaging the redemption value [Example: Products whose prices fluctuate when a credit event occurs to the reference enterprise, products for which redemption will be made at a par value except when a credit event occurs to the issuer, etc.]
 - Products referring to financial indices that have been stable over a long period of time [Example: Products referring to yen interest rates, etc.]
- * If a Full Member reasonably judges that the estimate based on historical data is possible for any of those products listed above as examples (including those for which measurement is judged impossible at the time of redemption but possible in case of premature sale), such measurement shall not be prevented from being mentioned in the explanatory materials.

Q6-3 What period of time should be referred to when using historical data to estimate the possible loss? Also, how should I calculate the amount of loss?

No reference period is specified. However, since the purpose of using historical data is to clearly indicate losses expected under the worst-case scenario, it is desirable that the period of reference should be deemed reasonable by our Full Member in light of the product attributes and should include a period of time during which the reference data is judged to have fluctuated significantly. It is not essential to apply all available historical data of the financial indicator to which the concerned product refers, or to use the same reference periods of historical data for all when referencing multiple financial indices. However, it should be noted that these points have to be sufficiently understood by the customers.

The estimate of possible loss may be calculated by the Full Member in a manner that they believe is easy for their customers to understand and reasonably assume the worst-case scenario. For example, there is a calculation method based on the rate of change between the maximum and minimum values during the reference period, or calculation based on the maximum rate of decline during the relevant number of years

in the reference period according to the term to maturity of the financial product to be sold. However, the latter method may not be suitable for financial instruments for which the term to maturity (or contract period) is super long or conversely very short.

Although the same calculation method may not always be applicable to all transactions and products handled by a Full Member, it should be noted to apply the same calculation method at least to similar transactions or products as far as possible so as not to cause misunderstanding among customers.

The historical data used for calculation must be reviewed on a regular basis.

In the event that the current value of the referenced financial benchmark is significantly different from the one presented as the worst-case scenario in the explanatory material, a prompt change of the description shall be regarded appropriate. Especially when such a situation arises with respect to the products currently being sold, it is necessary to fully explain the situation to the customers.

Q6-4 What kind of explanation is necessary for “liquidation value to be received for premature sale (cancellation settlement) estimated under the worst-case scenario,” which is a Significant Matter for complex investment trusts similar to over-the-counter derivatives transactions?

1. With regard to the “Liquidation amount to be received by an investor for premature sale (cancellation settlement) estimated under the worst-case scenario,” it is also considered necessary, in principle, to provide an explanation based on the historical data as is the case with the estimate amount of possible loss assumed on the worst-case scenario.
2. The Japan Securities Dealers Association has the following views on over-the-counter derivative transactions:

Unlike redemption amount at the time of expiration of contract, the amount to be received by an investor for premature sale (cancellation settlement) is affected by the presence or absence of a penalty imposed for such cancellation in relation to over-the-counter derivative transactions and by the liquidity status at the time of sale and the level of yield over the remaining term in relation to structured bonds. Therefore, in preparing the relevant explanatory materials, it is essential to clarify the conditions applicable for premature sales or cancellation including the presence or absence of such penalty, assumed timing of the cancellation, etc. as consideration items. Then, if it is truly difficult to calculate the liquidation value to be received at the time of early cancellation in relation to over-the-counter derivative transactions and such an estimate based on historical data is not or cannot be provided as the supplementary explanation, the explanation based on loss simulation calculated in the method (ii) may be provided. However, the explanation based on loss simulation calculated on the method (ii) alone may not be able to adequately and sufficiently address the estimate of possible loss.

Under such a circumstance, it is also advisable to provide the following explanation instead of the explanation concerned with method (i) on top of showing the theoretical price level assumed in the method (ii).

- (a) There may be expenses or losses arising as a result of concluding an alternative transaction or a

counter transaction made by a member of the Japan Securities Dealers Association with a third party in connection with the cancellation of contract; (b) Such expenses or losses shall be borne by the customer at the time of early cancellation as a part of cancellation settlement (penalty); (c) With respect to such cancellation settlement (penalty), it is impossible to calculate an estimate; (d) Accordingly, it is difficult to calculate an estimate of possible loss; (e) The cancellation settlement (penalty) payable by the customer may exceed the estimated amount of loss based on the worst-case scenario at the time of contract maturity.

3. With regard to complex investment trusts similar to over-the-counter derivative transactions, if it is considered truly difficult to adequately and sufficiently explain the liquidation amount to be received by an investor for premature sale (settlement for cancellation) for reasons such as insufficient liquidity of the products concerned, as in the case of 2 above, it is also possible to explain that losses exceeding those calculated on the theoretical price level may be incurred after clearly describing the reason for the difficulty of calculation together with the theoretical price level assumed in method (ii).

Q7 What are the “Significant Matters” in connection with the Direct Offering, etc. of the leveraged investment trusts (excluding those listed on the Financial Instruments Exchange Market and those falling under 6; the same shall apply in 7.)?

When engaging in Direct Offering, etc. of the leveraged investment trusts to customers (excluding professional investors), as is the case with other investment trusts, the objectives, characteristics, risks, fees, etc. of the fund stipulated in the prospectus shall be explained. Furthermore, it is advisable to explain the following matters specifically.

In giving an explanation, since it is important for the customers to gain sufficient understanding, it should be contemplated to obtain a confirmation letter of understanding from such customers in order to ascertain their understanding.

- (i) Since the concerned fund is managed with the aim of achieving a higher return than the referenced index by a certain margin, in case such index falls, there is a possibility of incurring a larger loss compared with the index referenced.
 - (ii) In case when investment trust concerned is a bull or bear fund, the bear fund is managed with the aim of having an opposite investment effect against the referenced index by a certain factor. Accordingly, if such index rises, the fund has a possibility of incurring a larger loss compared with the index referenced.
- Interpretation of “Criteria for the Commencement of Solicitation” as set forth in Article 4 of the “Rules on Complex Investment Trusts Similar to Over-the-counter Derivatives Transactions” and Article 6-2 of the “Regulations for Direct Offering, etc. of Beneficiary Certificates, etc.”

Q8 Why did the “Criteria for the Commencement of Solicitation” become established?

“Criteria for the Commencement of Solicitation” are one of the standards required by the Financial Services Agency to strengthen its sales and solicitation rules by voluntary regulation in the “Ideas for Restrictions on Uninvited Solicitation of Derivatives Transactions” published by the Agency on September 13, 2010.

In the provision, as part of “practicing the principles of suitability,” it is stipulated that “for complex structured bonds and investment trusts similar to over-the-counter derivative transactions, which are difficult for individual customers to understand, the development of voluntary regulations to exercise such principles of suitability is required.” Specifically, they demand “the establishment of standards to determine whether or not solicitation could be commenced in accordance with the risk characteristics of product and the nature of the customers (Criteria for the Commencement of Solicitation) as well as conducting prior verification of the product as to its suitability for sale to investors (Suitability on Reasonable Grounds).”

The reason why the “Criteria for the Commencement of Solicitation” are required is a large number of complaints received by consumer groups, which claim that certain complex products with risk characteristics similar to derivative transactions have been sold to the elderly who do not have substantial assets nor seem to have a high level of understanding for such investment, resulting in unexpected large losses incurred.

It can be said that the substance of such complaints varies from one to another, but the fact that such complaints have arisen in large numbers is not a desirable situation in terms of fostering, maintaining, and improving the relationship of trust between investors and Full Members (Management Companies).

The purpose of the “Criteria for the Commencement of Solicitation” set forth in the rules of this Association is not only to put into practice the requirements by the Financial Services Agency that the standards for conducting solicitation in accordance with the risk characteristics of products and nature of customers (Criteria for the Commencement of Solicitation) should be established, but also to prevent Full Members (Management Companies) from engaging in solicitation activities for investments that are highly likely to create such complaints through self-regulating the scope of target customers.

Q9 Is the “Criteria for the Commencement of Solicitation” different from the “Criteria for the Commencement of Transactions”? If so, what is the difference?

As set forth in Article 4 of the “Rules on Complex Investment Trusts Similar to Over-the-counter Derivatives Transactions” and Article 6-2 of the “Regulations for Direct Offering, etc. of Beneficiary Certificates, etc.,” the “Criteria for the Commencement of Solicitation” shall establish the scope of customers for whom investment solicitation by visit, telephone call, or at the branch counter is allowed among those customers who have not asked for solicitation for the concerned investment. Accordingly, no solicitation shall be made to customers who do not meet the Criteria, whether or not such solicitation will result in the conclusion of a contract.

The term “solicitation,” as used herein, means, as provided for in Article 4 of the “Rules on Complex Investment Trusts Similar to Over-the-counter Derivatives Transactions” and Article 6-2 of the

“Regulations for Direct Offering, etc. of Beneficiary Certificates, etc.,” any solicitation for acquisition made to a customer who has not requested such solicitation for acquisition for the concerned investment by visit or telephone or at the head office or any business office of a Full Member (Management Company). Herein, the scope of customers is limited to individual investors excluding professional investors. Restrictions on uninvited solicitation provided for in Article 38, Paragraph 4 of the Financial Instruments and Exchange Act are only concerned for visits or telephone calls. However, it should be noted that the Criteria apply to a customer who visits a branch of the Full Member for the purpose of consultation or purchase of a different product because it is necessary to pay sufficient attention to the suitability, etc. of the customer when making solicitation for another product not contemplated by such customer.

Q10 What kind of standards do the “Criteria for the Commencement of Solicitation” are supposed to establish? Should specific numerical criteria be established?

“Criteria for the Commencement of Solicitation” must be determined in accordance with the risk characteristics of the product and the nature of the customer. In consideration of the principles of suitability and recent examples of trouble, it is advisable to prepare solicitation standards based on the following prerequisites:

1. Age and trading experience of investor

Since investment trusts subject to the establishment of the “Criteria for the Commencement of Solicitation” are complex products with risk characteristics similar to those of derivative transactions, it is natural that such investment trusts are intended for customers with a certain level of understanding and judgment. Therefore, it is reasonable to set standards based on the age and investment experience of an investor.

It is generally considered that as one ages, one’s ability to understand and make decisions declines, and in view of the fact that recent news reports have indicated that elderly people living alone or the elderly with dementia are suffering from property damage one after another, it is considered to be effective to develop standards with due consideration to one’s age, such as obliging more careful application of such standards to the elderly.

Of course, it does not mean everyone over a certain age has a lack of, or a low level of, understanding, and it depends on an individual. Therefore, when developing standards based on the customers’ age, it is conceivable to establish such standards taking into account not only their specific age but also their trading experience, financial status, etc., in addition to requiring an interview with the customers themselves or their family members to ascertain their level of understanding prior to any solicitation concerned with customers older than the specific age.

With regard to trading experience, for example, it is conceivable to require as criteria that the relevant customer has conducted similar transactions in the past. However, it does not necessarily indicate that solicitation must be prohibited for any customer without similar experience in the past. Because trading

experience is regarded as a part of basis for measuring their level of comprehension and judgment, it is also reasonable to require as condition having an interview with the relevant customer so as to ascertain their level of understanding.

Furthermore, as trading experience will change with time, it is necessary for each Full Member to make a judgment based on information obtained during the period of time considered reasonable rather than making a mechanical judgment based on information on the customer card created at the time of account opening many years ago.

2. Financial status of investor (Major form of income and holding status of financial assets)

Investment solicitation subject to the establishment of the “Criteria for the Commencement of Solicitation” would be suitable only for investors with a certain amount of income or financial assets. For example, products with a high level of minimum investment amount or with low liquidity should be sold only to customers with a certain degree of financial resources such as financial assets, etc.

Financial status of a customer may be measured by the total financial assets and revenues of the customer rather than by the assets held in custody of the Full Member. However, since these are difficult to measure accurately, it is necessary to take care not to overestimate them.

3. Investment objectives and policy of investor

In most cases, solicitation for acquisition subject to the establishment of the “Criteria for the Commencement of Solicitation” is not considered to be suitable for a customer whose investment objective is to secure the safety of principal or a customer who is investing from the fund for future living.

Moreover, even for speculative purposes, each investor is likely to have a difference tolerance level for risk. Consequently, it is appropriate to develop the criteria in consideration of the tolerance level for risk.

As investment objectives and policy are also likely to change with time, it is imperative to pay sufficient attention to the changing objectives and policy of existing customers as well. It should also be noted that investment objectives and policy of an investor may vary subject to the nature of the investment fund.

4. Others

In addition to the listed above, it is reasonable to include into the criteria matters which a Full Member (Management Company) considers appropriate in consideration of risk characteristics of the product, such as prior interview with the relevant customer.

Any standard that is not sufficiently specific, or which can be met by every customer, will be contrary to the intent of the establishment of the “Criteria for the Commencement of Solicitation.” Consequently, it is essential to make them effective.

Q11 Should the “Criteria for the Commencement of Solicitation” be established for each transaction or each product? Can it be established comprehensively?

There are many types of complex investment trusts similar to over-the-counter derivative transactions that are subject to the establishment of the “Criteria for the Commencement of Solicitation” in their product attributes and risk profile. However, given the possibility that the establishment of detailed standards for each investment trust may lead to operational difficulty and loss of effectiveness, this does not preclude the possibility of grading investment trusts into different groups dependent on their risk characteristics and then developing separate standards per risk grade group for the management of target customers per investment solicitation in accordance with the internal procedures. Under such circumstance, it is possible to establish in advance multiple types of the Criteria for the Commencement of Solicitation subject to the degree of risk characteristics, etc. of product and identify an appropriate type of the Criteria whenever handling a new product.

It is considered desirable for Full Members (Management Companies) to establish effective standards from the viewpoint of investor protection in accordance with the product attributes and risk profile of an investment trust to be solicited for acquisition.

Q12 What sort of system is required to confirm that the Criteria for the Commencement of Solicitation is satisfied?

The probable items to be provided for in the “Criteria for the Commencement of Solicitation” are expected to include those which cannot be measured by numerical values only as discussed in Q10 and those which may change constantly. In consideration of these points, it is appropriate that, with regard to items related to a customer’s capability to understand complex structure that cannot be measured by numerical values alone, a relevant manager (who is practically in charge of managing Sales Officers and Representatives and may belong to either the sales department or the internal control department) shall confirm or approve whether or not the concerned customer satisfies the Criteria for the Commencement of Solicitation by conducting a hearing from the responsible Sales Officers and Representatives regarding such customer’s latest conditions or conducting a direct interview with such customer, if appropriate.

In addition, where the relevant managers are obligated to check themselves any item established, which is difficult to confirm due to a lack of numerical criterion, it is considered appropriate to establish a control system in accordance with the business method and system environment of a Full Member (Management Company) so that such confirmation process can be verified later.

Q13 How often should the Criteria for the Commencement of Solicitation be applied?

It will be desirable to apply the Criteria for the Commencement of Solicitation to check whether or not the

customer satisfies such Criteria at each solicitation for acquisition based on the information available at the time of such solicitation. Meanwhile, in the event that the Full Member has already confirmed that the customer meets the Criteria for the Commencement of Solicitation for a certain range of transactions and has been recognized as such customer who can be solicited after having obtained confirmation and approval from the relevant managers, while continuously being engaged in transactions with the company thereafter, the company may not have to go through the same procedures for each solicitation to satisfy the Criteria.

However, in case of the elderly people, their understanding and judgment may deteriorate as they age, and their investment objectives and policy may also change in some cases. Therefore, it is considered important to periodically review customers' suitability for solicitation.

In the event that there is a substantial change in the situation of a customer who is classified to be suitable for solicitation after having started solicitation for a product, it is necessary to examine whether or not such customer should continue to be treated as a suitable customer in accordance with the internal procedures established before continuing the soliciting activities for the said investment. If, as a result of such review, it is determined based on new facts that the customer concerned doesn't satisfy the Criteria for the Commencement of Solicitation anymore, it is appropriate to recognize such customer not suitable for solicitation and record the result as such.

- Interpretation of the provisions of Article 5 of the "Rules on Complex Investment Trusts Similar to Over-the-counter Derivatives Transactions"

Q14 What is an "Alert Document"?

The purpose of the Alert Document is to enable customers to clearly and concisely understand whether or not the transaction to be solicited is subject to the restrictions on uninvited solicitation with higher risk compared with general transactions. Specifically, the Management Company will deliver and explain the document that includes (i) warning regarding risk and (ii) the availability of financial ADR institutions for filing complaint and dispute resolution together with their contact information.

Q15 Is the format of the "Alert Document" fixed?

Although the format to be used has not been fixed, please use the example format of Alert Document that is prepared as reference.

Q16 Is it possible to change the example format of the "Alert Document"?

Although it is not always necessary to follow the example format with regard to the expression, font size, character type, use of underlines, etc., in consideration of the purpose of such document as warning, it is recommended any Alert Document is prepared with reference to the example provided.

Please clearly and accurately describe those items to be included in the Alert Document as listed in (i) and (ii) in the answer to Q14.

Q17 At what timing should the “Alert Document” be delivered?

Basically, such document must be delivered to the customer before the conclusion of a contract. Therefore, it may be delivered at latest at the same time of delivering the pre-contract documents and prospectus. Please refer to Q18 and Q19 for the method of delivery.

Q18 Is it possible to deliver the Alert Document at the same time or being combined with the pre-contract documents and prospectus?

Since the purpose of the Alert Document is for the customers to understand its content in an easy and concise manner, it is basically assumed that to be delivered as a single independent document.

However, it is not to prohibit delivering such warning together with the pre-contract documents and prospectus (including delivery by mail, etc.). In such case, it is desirable that such an Alert Document be placed on top of the pre-contract documents and prospectus.

Although it is possible to deliver the Alert Document simultaneously with the pre-contract documents and/or prospectus in order to prevent any omission in delivering such Warnings, in such a case, it is indispensable to devise ways to ensure that the Warnings is read, by placing it on top of the pre-contract documents or inserting such an Alert Document between the first pages of the prospectus.

Thus, when delivering the Alert Document at the same time as other documents, it is recommended to pay attention to the delivery method so as to avoid the situation where such document is not recognized or read by the customer, being lost among other documents.

Q19 Is it possible to deliver the “Alert Document” by electromagnetic means?

Alert Document may be delivered electronically as provided in Article 7 of the “Rules on Complex Investment Trusts Similar to Over-the-counter Derivatives Transactions.” However, in such a case, it is imperative to devise ways to ensure that the Alert Document is read. For example, when registering a PDF file or displaying a link to such document, it is necessary to combine the files into one file or to set a button to confirm that the user has inspected the concerned document. When delivering the document by electromagnetic means and concluding the transaction by telephone or visit, it is reasonable to obtain oral confirmation from the customer at such occasion of verbal communication.

As for the contact information of ADR agencies, it should be presented in a manner that is easy for the customers to immediately find them when needed. For example, in addition to posting the contact information of the ADR agencies in an easy-to-find place on the home page of a Full Member (such as a site

where various policies obligated to be published under laws and various contact information for complaints are posted), the text that “contact information of the ADR agencies is also posted in xx (site address)” can be included in the Alert Document to be displayed on the trading site of company’s website so as to serve customers’ convenience.

○ Others

Q20 With regard to “complex investment trusts similar to over-the-counter derivatives” and “leveraged investment trusts,” should the investment trust management company inform the distribution companies selling such investment trusts of such facts?

In order not to create problems with handling of the relevant investment trust when distributed by multiple companies, it is desirable for the investment trust management company, developer of the relevant investment trust, to inform all the sales companies involved that the investment trust concerned is a “complex investment trust similar to over-the-counter derivatives transaction” or a “leveraged investment trust.”

Q21 In the definition of “complex investment trusts similar to over-the-counter derivatives transactions,” what is the significance of the text, “an investment trust which has the same product attributes as, or similar effects to, the structured bonds in which the concerned investment trust invests”?

The “Rules on Investment Solicitation and Customer Management by Association Members” of the Japan Securities Dealers Association impose restrictions on complex structured bonds similar to over-the-counter derivative transactions. Therefore, if a customer who purchases an investment trust that holds structured bond subject to such restrictions falls into the similar situation to investing directly in such restricted structured bond, this will create an act of regulatory arbitrage.

In order to prevent such regulatory arbitrage from occurring when investment trusts are developed to have the same effect as the structured bonds subject to the regulations by investing directly in such structured bonds or have similar effects as if such investment trust was itself structured bonds, the term has defined those investment trusts with the same as, or similar effects to, the structured bonds so that similar restrictions are applicable to such trusts as those imposed on the concerned structured bonds.

Q22 Item “b” in the definition of “complex investment trusts similar to over-the-counter derivative transactions” lists “trusts where redemption price could be below the par value.” Because unlike bonds, any investment trust has an inherent risk of falling below par value, isn’t this definition misleading as if it were referring to all investment trusts?

In the definition of Article 2, the items “a” through “e” describe certain prerequisites concerned with the

definition of “bonds” and not to describe investment trusts.

This definition is not concerned with the risk of falling below par value inherent in all investment trusts but with those bonds where their values could fall under par value.

Q23 If an investment trust is developed as to have the same effects as a leveraged investment trust by investing in leveraged structured bonds, is the product a “complex investment trust similar to an over-the-counter derivatives transaction” or a “leveraged investment trust”?

When an investment trust is developed so as to have the same effects as a “leveraged structured bond” by investing in leveraged “structured bonds,” all such products will be classified as complex investment trust similar to an over-the-counter derivative transaction.

Investment trusts developed to have correlation or inverse correlation to a variety of indices or assets through the direct investment in futures transactions in shares, over-the-counter forex option, etc. are not categorized as complex investment trusts similar to over-the-counter derivatives transactions. Such products are subject to the restrictions as leveraged investment trusts only if the definition of leveraged investment trust applies to them.

Q24 In the definition of the “complex investment trusts similar to over-the-counter derivatives transactions,” is it not possible to assume that the scope of application of such definition may vary depending on an investment trust management company that develops such investment trusts?

To prevent such situation from happening, in addition to the definitions set forth herein, details of the nature of complex structured bonds similar to derivative transactions are separately listed in the table, which is prepared by the Japan Securities Dealers Association and separately presented.

In the event that an investment trust is developed to which such table is not applicable or which is difficult to classify, the relevant committee, etc. within the Investment Trusts Association, Japan shall share information on the suitability of classification and take measures to serve the convenience of Full Members.

* This is a compilation of the interpretations and ideas regarding the “Regulations for Complex Investment Trusts Similar to Over-the-Counter Derivative Transactions” enforced on April 1, 2011.

Supplementary Provision

The amendments come into effect on December 13, 2012.