

IN THE FOLLOWING Q&A SECTION, PRESIDENT TAKEUCHI TOUCHES ON ISSUES PERTAINING TO THE DOMESTIC SECURITIES CLEARING AND SETTLEMENT SYSTEM AND JASDEC'S RESPONSES.



## DOMESTIC SECURITIES CLEARING AND SETTLEMENT SYSTEM REFORM

### Question

What progress has Japan made in securities clearing and settlement system reform?

In 2000, the Financial Services Agency released a report highlighting “safety” and “efficiency” in securities clearing and settlement system reform, and Japan embarked on the task of creating an internationally competitive financial infrastructure of the world’s highest standard.

Three issues have been raised with regard to the domestic securities clearing and settlement system.

The first issue is costs — that is, the time and money expended by users — arising from clearing and settlement functions separated by type of securities, be they stocks, government bonds, corporate bonds, investment trusts or some other type of securities.

The second issue is the realization of straight-through processing (STP), which has been tipped as the key to trimming costs and reducing the settlement risks that accompany shorter settlement cycles.

The third issue is the standardization of trading data and the harmonization of communication protocols.

Efforts to achieve reform thus hinge on the question of how to maintain safety and efficiency — specifically, how to minimize inherent risks and costs by enhancing system design and applying information technology — while successfully addressing the three issues outlined above.

JASDEC has tackled its reform in three particular areas.

First, to improve efficiency of the systems used in securities clearing and settlement, we worked to promote STP for the PSMS and expand eligible securities and applicable trades.

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**Straight-through processing (STP)** An electronic system that eliminates human intervention from all trade-to-settlement processes involved in securities transactions.

**T+1 (Trade date plus one day)**

A movement to compress the settlement cycle — from trade date to payment and settlement — to one day after trading, from the current three days after trading.

TARGET AND THEME

Target 1 →

Catch up with major foreign markets

THEME

Reducing Principal Risk

PROMOTING DVP

- MAY 2004  
Start DVP for NETD

Target 2 →

Establish competitive market infrastructures

THEME

Improving Efficiency

PROMOTING STP

- SEPTEMBER 2001  
Start PSMS

INCREASING ELIGIBLE SECURITY TYPES

- NOVEMBER 2001  
Start convertible bond transactions

ENHANCING CSD GOVERNANCE

- JUNE 2002  
Reorganization of JASDEC

PROMOTING DEPOSITS

Target 3

Realize most advanced market infrastructures

THEME

Improving Efficiency

PROMOTING PAPERLESS SYSTEM

Start of book-entry transfer system:

- MARCH 2003  
Electronic CP
  - JANUARY 2006  
Corporate and Municipal SBs
  - 2006–  
Investment trust beneficiary rights
  - 2009–  
Stocks
- REDUCING LIQUIDITY RISKS
- Shorter settlement cycle (T+1)

Second, we utilized our transformation into a stock company to reinforce our corporate governance capabilities as a central securities depository, while raising our profile through advertising to attract more investors and issuers to our services.

And third, to minimize principal risk, we targeted the development of a DVP settlement system, and in May 2004, we connected the PSMS to our newly implemented DVP system for NETD.

Through these efforts, we have contributed to the establishment of an internationally competitive financial market infrastructure in Japan and the achievement of first-half objectives set out for securities clearing and settlement system reform.

## JASDEC's TOPICS

Question

What major systems issues must be tackled now and how will JASDEC respond?

The next major task of reform is dematerialization. In March 2003, JASDEC began providing book-entry transfer services for dematerialized CP. As of



March 31, 2004, these services covered 257 issues, and the outstanding amount stood at ¥1,403.2 billion.

By and large, dematerialization of securities removes the risks inherent in transporting physical certificates and cuts the cost of safekeeping them. Moreover, dematerialization leads to safer, more efficient settlement and clearing operations, because no certificates have to be produced, delivered or presented, and CP trades are now settled with the DVP system. Dematerialization also boosts trading of CP, because issuers can use smaller denominations without worrying about the cost of stamp duties on every certificate.

In addition to a book-entry transfer system for corporate and municipal straight bonds scheduled for implementation in January 2006, JASDEC is currently preparing for the introduction of a book-entry transfer system for investment trust beneficiary rights as well as the further implementation of a system geared to the dematerialization of stock certificates, the final goal of the reform process. This corresponds to legislative amendments such as revision of the Commercial Code.

A higher custody ratio will facilitate the conversion of paper stocks into dematerialized form, so we aim to pull our custody ratio into the 80% range through the use of advertising aimed at investors, including individual investors.

## RISK MANAGEMENT

### Question

### How is JASDEC reinforcing computer system management?

We are fortifying computer systems considerably, paralleling expansion of services. Coinciding with the May 2001 start of DVP for exchange trade deliveries of stock certificates, etc., we upgraded central processing units to double their processing capability. Then, in March 2002, we installed new storage equipment in order to boost processing capacity for beneficial shareholder notifications from 21.6 million cases to 30 million cases for each record date.

On the safety front, we established a backup center in September 2000 with the Bank for International Settlements' Lamfalussy Standards in mind. In addition, we have set up an action plan incorporating all possible measures to deal with a natural or non-natural disaster.

To reinforce management of information systems, we formulated our own security policy, based on such international standards as BS ISO/IEC17799 for information security management.

