

Rapid Progress



in Dematerialization

Domestic securities clearing and settlement reform has made progress toward the final goal: dematerialization of stock certificates. As the organization responsible for the infrastructure of securities clearing and settlement in Japan, the JASDEC Group is tackling several issues that will lead to the improved safety, efficiency and convenience of inherent systems.

TARGETS FOR 2009

MEDIUM-TERM THEMES

The JASDEC Group will concentrate on five themes over the next three fiscal years, but the No. 1 priority will be dematerialization of securities.

PROGRESS IN DEMATERIALIZATION

BOOK-ENTRY TRANSFER SYSTEM FOR INVESTMENT TRUSTS We are working to implement a book-entry transfer system for investment trusts and to ensure stable operation thereof. We are currently implementing processes that will achieve the smooth conversion of outstanding physical certificates into a dematerialized form.

DEMATERIALIZATION OF STOCK CERTIFICATES Based on the System Outline for dematerialization of stock certificates, we are pursuing discussions to fine-tune administrative processes and practical conversion techniques and to address necessary system development in our quest to build a new book-entry transfer system for stock certificates.

PROMOTING USE OF BOOK-ENTRY TRANSFER SYSTEMS FOR CP AND CORPORATE BONDS To elicit greater interest in dematerialization of CP and to firmly establish the book-entry transfer system for Corporate Bonds, we maintain a steady stream of activities to raise awareness in the market and address concerns to support smooth transition of outstanding physical bonds and recorded bonds to dematerialized form. We undertake necessary responses, such as function upgrades to relevant systems, to enhance convenience for users, and strive to expand use of our systems.

PROMOTING STP

We will boost the capacity of PSMS to include a matching function for stock lending and a new issuing record matching function, paralleling the move toward dematerialization of stock certificates.

RAISING NUMBER OF STOCK CERTIFICATES IN CUSTODY

By encouraging more investors and issuers to grant us custody of stock certificates, we will achieve smooth conversion of paper certificates into dematerialized form and expand use of the book-entry system.

REINFORCING CUSTODY FUNCTION

STRONGER SYSTEM INFRASTRUCTURE Based on the formation of a medium- to long-term plan for systems—including the system for dematerialization of stock certificates, as well as system replacement, transfer of information to our data center and other aspects related to systems—we will strive to build an infrastructure featuring higher levels of safety, efficiency and convenience. This will ensure stable clearing and settlement operations.

ENHANCED RISK MANAGEMENT STRUCTURE We will continue to improve information security and work toward the establishment of a structure that supports business continuity in the event of an emergency. We will also introduce system audits and other actions to enhance our risk management structure.

STRONGER TIES WITH OVERSEAS COUNTERPARTS We will forge stronger ties with counterpart organizations abroad and create networking opportunities with other central securities depositories, primarily through the activities of hosting overseas seminars and the 9th Conference of CSDs in the Asian region.

Activities to date are described as follows.

Implemented

January 2006

Book-Entry Transfer System for Corporate Bonds

BOOK-ENTRY TRANSFER SYSTEM FOR CORPORATE BONDS

Main Features of the System

The prevailing registration system requires certain responses to the physical issue of bonds because beneficiaries have the right to request the issue of such certificates. The book-entry system, however, is completely electronic, and thereby eliminates costs associated with issuing denominations and reduces the burden of office

paperwork. Under our system, we revised custody procedures—from issuance to redemption, including transfers—into a management structure, based on the balance recorded in the transfer account book, and realized DVP (gross-gross formation known as BIS model 1) and STP by linking to PSMS.

BOOK-ENTRY TRANSFER BASED ON BALANCE MANAGEMENT

Under the prevailing registration system, registration institutions enter the denomination type and serial



Implemented

April 2006

Depository and Book-Entry Transfer System for Foreign Stocks

number as well as ownership in their register book. Under the new book-entry system, transfer of ownership is executed by entering the net increase or decrease in the transfer account book, thereby expediting transition in secondary markets.

MULTILAYER HOLDING STRUCTURE OF PARTICIPATION

Account management institutions are positioned in the multilayer holding structure in order to facilitate flexibility of business development and to promote affiliation among international institutions. In addition, under the book-entry transfer system, payment of principal is executed by the issuer's agent paralleling the layered structure.

ELIGIBLE SECURITIES

A variety of bonds is eligible, excluding Japanese Government Bonds, regardless of whether the securities are public or private offerings. In addition, the system is flexibly designed and will accommodate floating-rate notes and foreign-currency-denominated bonds.

- Corporate bonds
- Municipal bonds
- Investment company bonds
- Corporate bonds issued by mutual companies prescribed in the Insurance Business Act
- Specified corporate bonds prescribed in the "Law Concerning Liquidation of Assets"
- Rights that should be represented by bond certificates issued by companies under a special law
- Rights that should be represented by bond certificates issued by any government or by companies in foreign countries, excluding those with the characteristics of bonds

with subscription rights, such as Samurai Bonds and Shogun Bonds.

Notes:

1. Corporate bonds with subscription rights will become dematerialized when stocks are dematerialized.
2. Corporate bonds issued in overseas markets, such as euro-yen bonds, are excluded from eligibility.

SMOOTH TRANSITION OF OUTSTANDING BONDS

From January 6, 2008, preferential tax treatment on interest income for such entities as tax-free corporations will apply only to book-entry bonds; recorded bonds and physical bonds will no longer be eligible for preferential tax treatment. In response, JASDEC will maintain efforts to promote the transition of outstanding bonds to book-entry bond status.

DEPOSITORY AND BOOK-ENTRY TRANSFER SYSTEM FOR FOREIGN STOCKS

DETAILS ON SYSTEM START

In response to requests from participants in the foreign securities market in Japan regarding promotion of the reliability and safety of depository and book-entry transfer services for listed foreign stocks etc., JASDEC applied to the Financial Services Agency and the Ministry of Justice for approval to handle the depository and book-entry transfer services for listed foreign stocks and the like offered by Japan Securities Settlement & Custody, Inc. (JSSC). In March 2006 the above-mentioned authorities confirmed that JASDEC could undertake such operations in line with the CSD Law, enabling JASDEC to add these services for JASDEC participants.

For Implementation

January

2007

Book-Entry Transfer System for Investment Trusts

With the enforcement of Business Regulations Relating to Depository and Book-Entry Transfer of Foreign Stock Certificates, etc., on April 1, 2006, JASDEC began transferring balances from JSSC at the end of April. The transfer of foreign stocks listed in Japan is expected to be complete by summer 2006.

SYSTEM SUMMARY

By opening a deposit account for foreign stock certificates, JASDEC's participants can execute either book-entry transfer for exchange transactions settled by instruction of Japan Securities Clearing Corporation or non-exchange trade transfers, in line with Business Regulations and Rules Relating to Depository and Book-Entry Transfer of Foreign Stock Certificates, etc.

When a participant deposits listed foreign stock certificates to undergo book-entry transfer by JASDEC, the stock certificates must be deposited with JASDEC's relevant foreign depository. If the foreign stock certificates are already entrusted to a JASDEC account and sold in the home market by participants, JASDEC transfers or delivers to the account designated by the participant. These deposits and transfers are made via message creation and automated dispatch between JASDEC's book-entry transfer system for foreign stocks and SWIFT (the Society for Worldwide Interbank Financial Telecommunication).

In regard to the treatment of rights held by beneficial shareholders, Share-Handling Services Agents, such as trust banks, which execute share-handling processes, must create a list of beneficial shareholders, based on JASDEC participants' data on the record date. Rights will be granted only to shareholders on this list.

BOOK-ENTRY TRANSFER SYSTEM FOR INVESTMENT TRUSTS**INVESTMENT TRUST MARKET IN JAPAN**

In recent years, the investment trust market in Japan has undergone a huge transformation, highlighted by the start of sales through Japan Post in October 2005. Interest in investment trusts is growing stronger, supported by greater investment activity by individual investors. According to the Investment Trusts Association of Japan, net investment trust assets reached ¥85.79 trillion, as of March 31, 2006. Of this amount, investment trusts offered to the general public represented ¥58.47 trillion while investment trusts for private placement represented ¥27.32 trillion.

SYSTEM SUMMARY

JASDEC aims to implement a book-entry transfer system for investment trusts, like those for CP and Corporate Bonds, in January 2007. With this system, subscription, transfer and redemption of beneficiary rights following the establishment, transfer and cancellation of investment trusts will be recorded in the transfer account book.

Book entry will ensure safety and efficiency in the settlement of investment trusts and support further growth of the investment trust market in Japan. In addition, dematerialization will eliminate paper-based beneficiary certificates, which are required under the current system, and thereby streamline administrative processes.

ELIGIBLE CERTIFICATES

This book-entry transfer system for investment trusts will extend to beneficiary rights recognized under the Investment Trust and Investment Corporation Act but

For Implementation No Later than
June

2009

Dematerialization for Stock Certificates

will not initially cover those on foreign investment trusts established overseas or on mother funds.*

*Exchange-Traded Funds (ETFs) are different from other investment trusts. JASDEC's basic stance on ETFs, as settlement is carried out by the same procedures applied to stocks, is to use the same system platform used for stocks, and to pursue further improvements consistent with those applied to the book-entry transfer system for stocks.

TOWARD IMPLEMENTATION

Leading up to the implementation of the book-entry transfer system for investment trusts, we will run a series of system-related tests from August to December 2006.

DEMATERIALIZATION FOR STOCK CERTIFICATES

DEMATERIALIZATION OF STOCK CERTIFICATES IN JAPAN

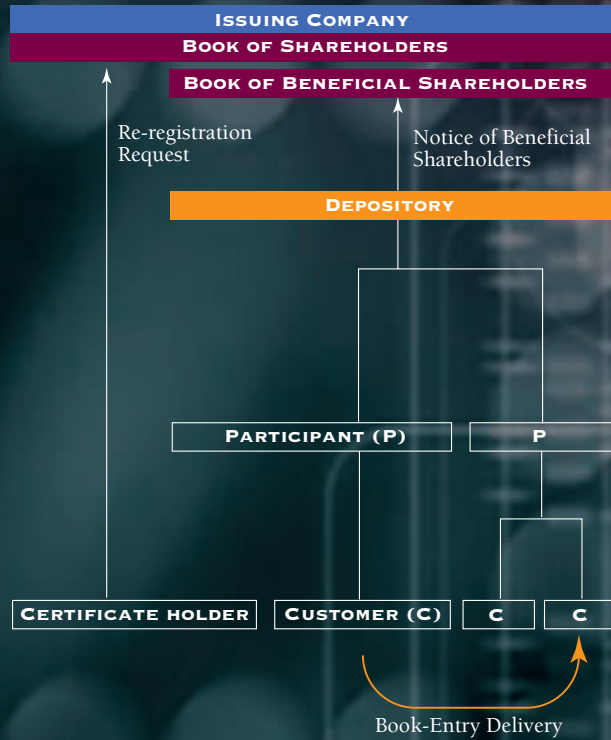
In 2004, the Stock Settlement Rationalization Law (the Law for partial amendments to the Law concerning Book-entry Transfer of Corporate Bonds and Other Securities) was introduced in Japan to streamline settlement procedures for trades of stocks and other securities. This legislation allows the stock of non-stock-issuing companies to be handled by the book-entry transfer system. All listed companies will be required to make their stock paperless as of a date, determined by government ordinance, within five years of the day the aforementioned legislation was announced (June 9, 2004).

BASIC STRUCTURE OF THE NEW SYSTEM

- Under the new book-entry transfer system, the ownership of stocks shall be determined by the record in the ledger of book-entry transfer accounts, and shall be transferred by account transfer.
- Twice a year, in principle, the central securities depository—namely, JASDEC—will give to issuers of shares in custody information regarding shareholders (general shareholders' notification), based on entries in the transfer account book. This service is similar to the one for beneficial shareholder notification, under the current depository and book-entry transfer system. It differs, however, in that issuers may request the central securities depository to extend a general shareholders' notification at any time, provided that the reason for such a request is justified.
- Issuers will update their respective lists of shareholders, based on the aforementioned general shareholders' notification. Under the prevailing securities custody and book-entry transfer system, two lists of shareholders' ownership interests are maintained for stock certificates in the custody of the central securities depository: the shareholders' registry with the name of the central securities depository, and the beneficial shareholders' registry with the names of actual shareholders. The new system, however, will consolidate management of shareholders' ownership interests into the shareholders' registry alone, and only the names of actual shareholders will be recorded therein.
- When issuers undertake corporate actions, such as stock splits, bonus issues and mergers, the central securities depository and the account management institution, following notification from the issuer, will undertake procedures that automatically revise the record of shareholders' accounts.
- When shareholders wish to exercise minority shareholder and single-unit shareholder rights on shares in custody, they need to instruct their respective account management institution to notify the issuer of the data in the ledger of book-entry transfer accounts. The central securities depository will then notify the issuer

STRUCTURAL DIFFERENCES BETWEEN THE CURRENT AND DEMATERIALIZED SYSTEMS

Current System



Dematerialized Book-Entry Transfer System



Note 1. Account management institutions in the dematerialized system and participants in the current system are essentially the same. Securities firms, banks, transfer agents (trust banks, etc.) are able to have such status.
 2. Participants in the dematerialized system and customers in the current system are essentially the same. Investors are able to obtain such status by opening accounts with AMIs.

(specific shareholder notification) and within a specified period thereafter, shareholders may exercise rights.

- When the reason is justifiable, an issuer can request the central securities depository or an account management institution to provide information on record in the ledger of book-entry transfer accounts.

CONCRETE SYSTEM OUTLINE

JASDEC has explored various aspects of the new book-entry transfer system, including practical procedures and techniques, to facilitate implementation and use.

- The new system will handle listed stocks, subscription rights to new shares, corporate bonds with subscription rights to new shares, beneficiary ownership and preferred capital contribution, as well as subscription rights for new shares of unlisted stock and corporate bonds with subscription rights to new shares of unlisted stock, as long as specific criteria are satisfied.
- We will apply shareholders names, addresses and number of shares received from account management institutions for general shareholders' notifications, specific

shareholder notifications and responses to requests for data on the ledger of book-entry transfer accounts.

- We will introduce DVP to eliminate settlement risk occurring when shares and corporate bonds with subscription rights to new shares are newly issued for public offerings.
- We will disclose on a daily basis foreign shareholder ratios on stock in companies in such industries as broadcasting and aerospace, where shareholdings by foreigners is limited to a certain percentage.
- We will establish a registered account method for taking in shareholders' dividends. We will also consider a pro-rata allocation method based on the number of shares.

To ensure a smooth start to the new book-entry transfer system, which will be no later than June 2009, we have been collaborating closely with representatives from relevant industries and authorities, and have been independently pursuing various systems development activities. All interested parties have agreed to set January 2009 as the target for the commencement of dematerialization of stock certificates.