



Appendixes

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APPENDIX 1: OVERVIEW OF AUDITS OF THE BANK OF JAPAN

Pursuant to the provisions of the Bank of Japan Act and in accordance with the Bank's internal rules, the following audits were conducted by the Auditors of the Bank in fiscal 2009 and at the beginning of fiscal 2010.

I. Audits of the Bank's Financial Statements and Other Documents⁷**A. Financial statements and other documents for fiscal 2008**

From April through to early May 2009, the Auditors audited the Bank's financial statements and other documents, specifically, the inventory of property, the balance sheet, the statement of income, the annual report on the settlement of accounts, the appropriation of net income, and the schedule for the financial statements for fiscal 2008 (the 124th fiscal year) as well as the statement of income for the second half of fiscal 2008.

The Auditors submitted to the Governor their written opinions indicating that the financial statements and other documents presented fairly the state of property, the results of operations, and the expenses for fiscal 2008 as well as the results of operations for the second half of fiscal 2008.

B. Financial statements and other documents for the first half of fiscal 2009

From October through to early November 2009, the Auditors audited the Bank's financial statements and other documents, specifically, the inventory of property, the balance sheet, the statement of income, and the

schedule for the financial statements for the first half of fiscal 2009 (the 125th fiscal year).

The Auditors submitted to the Governor their written opinions indicating that the financial statements and other documents presented fairly the state of property and the results of operations for the first half of fiscal 2009.

C. Financial statements and other documents for fiscal 2009

From April through to early May 2010, the Auditors audited the Bank's financial statements and other documents, specifically, the inventory of property, the balance sheet, the statement of income, the annual report on the settlement of accounts, the appropriation of net income, and the schedule for the financial statements for fiscal 2009 as well as the statement of income for the second half of fiscal 2009.

The Auditors submitted to the Governor their written opinions indicating that the financial statements and other documents presented fairly the state of property, the results of operations, and the expenses for fiscal 2009 as well as the results of operations for the second half of fiscal 2009.

II. Field Audits of Banknotes, Securities, and Books

In fiscal 2009, the Auditors conducted a total of 56 field audits of banknotes and securities in the custody of as well as books kept by 7 departments of the Bank's Head Office and 32 branches.

7. The first half of the fiscal year runs from April 1 through September 30, and the second half from October 1 through March 31.

III. Audits of the Bank's Business Operations

In fiscal 2009, the Auditors conducted field audits of the Bank's business operations at 32 branches, 12 local offices in Japan, and 3 overseas representative offices, in addition to field audits of operations relating to expenses and contracts at 2 Head Office departments. They also conducted a total of 192 meetings, at which

they reviewed the execution of the Bank's business operations, receiving explanatory overviews from each of the Head Office departments as well as reports from relevant departments concerning other high-priority issues. In addition, they conducted 365 examinations of key documents and 4 special on-site visits to the Bank's premises.

APPENDIX 2: THE BANK OF JAPAN'S STRATEGIC PRIORITIES FOR FISCAL 2010–2012**I. Introduction**

"The Bank of Japan's Strategic Priorities for Fiscal 2010–2012" describes the basic principles for its business operations and organizational management during the three-year period.

The Strategic Priorities have a rolling three-year horizon. At the end of every fiscal year, the Bank conducts a performance review and then updates the Strategic Priorities accordingly, resetting the horizon to cover the next three years. Under the framework, the Bank keeps a medium-term perspective and responds flexibly to any changes in circumstances, so as to ensure that its business operations and organizational management are conducted in a timely manner.

II. Background

Structural changes have been taking place in Japan's economic and financial environment, including globalization, the growing significance of emerging economies—especially those in Asia—to the world economy, the diversification of financial transaction needs, and the innovations in financial engineering and information processing technology accompanying these. These trends seem set to continue.

While the structural changes may well contribute to future global economic growth, they are also likely to lead to greater complexity and wider fluctuations in economic and financial developments. This may cause imbalances to accumulate in the economy, triggering occasional large-scale economic adjustments. The

current global economic adjustment is a case in point.

Japan's economic conditions are likely to continue improving, albeit moderately, and the year-on-year pace of decline in consumer prices is expected to slow gradually. However, the outlook continues to be attended by a significant level of uncertainty. Regional differences in economic structure as well as consequent disparities in profitability and financial strength among regional financial institutions are likely to remain.

Meanwhile, in response to the recent global financial crisis, progress has been made in establishing new rules for financial regulation and supervision that are consistent internationally. At the same time, the outbreak of the H1N1 influenza virus has increased demand for the upgrading of business continuity arrangements.

The Bank needs to respond flexibly to these changes in its environment; at the same time, in order to provide a stable foundation for financial and economic activity, it also needs to continue conducting its central banking operations properly.

The Bank must maintain the stability and efficiency of its central banking operations, while ensuring a diversity of working arrangements so that employees may improve their work-life balance⁷ in response to changes in Japan's social structure. As a public organization, the Bank is also required by the public to further improve the fairness and efficiency with which it runs its business.

7. This refers to the achievement of a balance between work and personal life: employees should feel motivated and fulfilled by their duties and responsibilities at work; at the same time, depending on their stage of life, as parents or otherwise, they should have a wide range of choices and opportunities for personal fulfillment at home and in their communities.

III. Management Principles

Based on the above understanding, in order that the Bank's full resources may be deployed smoothly and in an integrated fashion to fulfill its mission, the following three management principles have been set out under the Strategic Priorities: stability and efficiency in all business operations; learning in action; and enhancement of communication channels.

A. Stability and Efficiency in All Business

Operations

The Bank's mission, ensuring price stability and financial system stability, is achieved through its banking operations. It is therefore important for the Bank to ensure the stable conduct of all its banking operations, thereby raising public confidence. This is vital not only for banking operations but also for other activities such as the compilation of statistics, research and analysis activities, and organizational management. The Bank must, at the same time, continue to step up its efforts to conduct these operations efficiently.

B. Learning in Action

The Bank should continue to enhance its research activities on a wide range of economic and financial issues, since conducting high-quality research is a significant precondition for successfully achieving its mission. In its conduct of central banking operations, the Bank must take into account the surrounding circumstances, innovations in financial and information technology, and changes in public needs. Continuation of research and planning is needed to achieve further improvements in central banking services and thereby respond effectively to any changes in circumstances. It is also important for the Bank to conduct performance reviews and make revisions as appropriate. It is vital for

the Bank to continue to foster an organizational culture, shared with other central banks, that encourages continuous "learning" in this broad sense.

C. Enhancement of Communication Channels

In order to maintain its independence and to conduct its policies and business operations appropriately, the Bank must be accountable for its activities and willing to disseminate related information widely. Moreover, ensuring that reviews of the Bank's policies and services are based on a firm grasp of any changes in circumstances or public needs requires that the Bank listen to outside opinions and properly understand the thinking behind them. Furthermore, to acquire and train the employees needed for its business operations and organizational management, the Bank needs to promote personnel exchange with outside institutions. From this perspective, the Bank will look for further ways to consolidate external relationships and enhance communication channels.

IV. Issues and Action Plans

In accordance with the three management principles described in Section III above, the Bank has continued to address a wide range of issues and has moved forward with a number of action plans. In fiscal 2009, the Bank generally made the anticipated progress in addressing and implementing the issues and action plans outlined for fiscal 2009–2011.²

Given the above assessment as well as the recent developments in Japan's economic and financial environment described in Section II, the Bank will address new issues and implement appropriate new action plans during fiscal 2010–2012. The following is an overview of these.

2. For the Bank's evaluation of the progress made during fiscal 2009 toward achieving its Strategic Priorities for fiscal 2009–2011, see "Implementation of the Bank's Strategic Priorities: Progress Made during Fiscal 2009" on pages 31–46.

A. Matters Relating to the Conduct of Monetary Policy

The Bank will enhance the quality of its research and analysis regarding developments in economic activity, prices, and the financial environment at home and abroad so as to make appropriate policy decisions. In particular, the Bank will devise better methods of monitoring the financial environment and further strengthen analysis related to the relationship between financial and economic activity. To this end, the Bank recognizes the importance of assessing risks in the financial system as a whole—i.e., taking a macroprudential perspective—in light of Japan's past experiences as well as the recent global financial crisis and subsequent policy responses by authorities worldwide.

The Bank will study the frameworks for money market operations so as to ensure that appropriate policy decisions are made.

At the same time, the Bank will communicate its research findings regarding the conduct of monetary policy to the public effectively.

B. Matters Relating to the Financial System

In light of the recent global financial crisis, there has been increasingly lively international discussion focused on macroprudence, and progress has been made in establishing new rules regarding financial regulation and supervision that are consistent internationally. Given these developments, the Bank will conduct research and planning related to the financial system, giving due consideration to institutional factors unique to each country as well as Japan's past experiences. The Bank will make use of the findings to actively contribute to policy formulation both at home and abroad.

The business environment surrounding financial institutions is undergoing significant changes, and there

remain disparities among institutions in terms of their profitability and financial strength. Under these circumstances, the Bank will ensure that it accurately grasps the business conditions at financial institutions by strengthening the feedback between its on-site examinations and off-site monitoring as well as by conducting them efficiently and effectively. The Bank will also encourage financial institutions to step up efforts to improve their management of risks through activities organized by the Bank's Center for Advanced Financial Technology (CAFT). The Bank will further refine its methods for macroprudential analysis and assessment of the financial system in Japan, as well as its microprudential on-site examinations and off-site monitoring of financial institutions, ensuring that each type of activity benefits fully from the findings of the other. The Bank will also communicate its findings to the public effectively.

The Bank will make use of the findings of such analysis in developing financial system policies and implementing monetary policy.

C. Matters Relating to Payment and Settlement Systems and Market Infrastructure

The Bank will conduct research and planning to promote improvement in the safety and efficiency of Japan's payment and settlement systems, and implement measures as necessary to respond to the following: (1) structural changes, such as the diversification of financial instruments and transactions, globalization of financial markets, and advances in information processing technology, as well as the resultant calls from market participants for payment and settlement systems that accommodate these; and (2) discussions, taking place both at home and abroad in the wake of the recent financial crisis, on reviewing payment and settlement practices and reforming the framework of

financial regulation and supervision.

As part of these measures, the Bank, together with relevant parties, will proceed steadily with the establishment of a new Bank of Japan Financial Network System (BOJ-NET).

At the same time, the Bank will firmly monitor the safety and efficiency of payment and settlement systems from the standpoint of the central bank and encourage relevant parties to improve these systems, in accordance with a new set of basic oversight policies to be formulated in due course.

With a view to further enhancing the stability and efficiency of financial markets and in consideration of international developments, the Bank will carry out research and planning related to improving financial market structures and making requisite adjustments to market infrastructure. It will work toward securing improvements in these areas, in discussion and cooperation with relevant parties at home and abroad.

The Bank, in cooperation with relevant parties, including ministries and government agencies as well as financial institutions, will steadily enhance business continuity arrangements, so as to be ready for emergency situations, such as pandemics, like the H5N1 avian influenza virus, and natural disasters.

In addition to the above efforts, on the international financial front, the Bank will contribute to the stability of the international currency system by, for example, promoting efforts to ensure the stability of the currency system in Asia, and strengthening cooperation with overseas authorities, especially central banks, through personnel exchange and technical assistance.

D. Matters Relating to the Regional Economic and Financial Environment

With regional differences in Japan's economic structure continuing to be observed, the Bank will maintain a

sound grasp of regional economic and financial conditions, keeping up a close dialogue with local financial and business communities. The Bank will make use of its findings in its conduct of monetary policy and other actions.

The Bank will strengthen its grasp of business conditions at regional financial institutions—including their performance as financial intermediaries—through its on-site examinations and off-site monitoring, and will carry out more in-depth discussions with regional financial institutions on issues relating to business conditions. The Bank will also support regional financial institutions' efforts to improve their management of risks through, for example, local seminars organized by the CAFT. By means of these activities, the Bank will contribute to efforts to improve the functioning of the financial system in regional economies.

E. Matters Relating to Banknotes, Treasury Funds, and Japanese Government Securities (JGS) Services

The Bank will continue to work toward securing confidence in banknotes and coins, and will conduct further research on anti-counterfeiting technologies as part of this effort.

With regard to banknote examination and treasury funds services, the Bank will examine the likely changes in the future workload at its Head Office and branches in view of recent changes in the delivery routes of banknotes between financial institutions and the Bank as well as recent institutional changes related to treasury funds services. The Bank will then consider changes in the division of roles between its Head Office and branches, as well as among branches; it will also consider changes in its operational framework for examining banknotes and for providing treasury funds services. Through these efforts, the Bank will seek to

make its operational framework in these areas even more stable and efficient.

F. Matters Relating to Communication with the Public

In the course of implementing measures in a number of areas, the Bank will work to improve the effectiveness of its communication with the public so as to ensure the transparency of its policies and overall business operations. As part of this effort, the Bank will enhance its dissemination of English-language materials and the reports and research papers it releases.

Given the increasing significance of the Internet as a tool for communication, the Bank will start operating a thoroughly revised web site to better respond to users' diverse needs and to further enhance the effectiveness of its communication with the public.

V. Organizational Management

With a view to addressing the issues and moving forward with the action plans stated in Section IV above, the Bank will implement the following measures with respect to organizational management.

A. Stable and Efficient Business Operations

The Bank will continue to ensure that all operations are backed up by accurate practical knowledge and executed with precision and deliberation. In particular, it will ensure that the necessary operational procedures are put in place in a swift and appropriate manner to implement policy measures effectively. The Bank will assess its business processes so as to identify where operational risks, including those associated with information security, exist and how such risks are controlled. It will then revise its business processes as necessary and work toward further strengthening its risk management.

Moreover, the Bank will raise the efficiency with

which it uses management resources by implementing operational restructuring and improving its business processes in light of changes in the business environment, as well as by further promoting computerization and the use of outsourcing. The Bank plans to achieve wide-ranging efficiency gains across areas that include, specifically, the establishment of a new BOJ-NET, the provision of services relating to banknotes and treasury funds, and the compilation of statistics. The Bank will also work to improve the efficiency of its system development through streamlining development processes, employing new technology, and promoting outsourcing.

At the same time, the Bank will continue to ensure the fairness of its business operations and organizational management by means of thorough compliance with all requisite laws and regulations.

B. Human Resources

Following the basic guideline for managing personnel numbers, the Bank has been working to realize a net reduction of 5 percent or more in the number of its full-time employees during the five-year period from fiscal 2006 to 2010, in line with the Administrative Reform Promotion Act (Act No. 47 of 2006) and with the General Principles of Administrative Reform decided by the Cabinet on December 24, 2005. In fiscal 2011 and 2012, the Bank will apply itself to further increasing the overall efficiency of its business operations, while securing the staff needed to enhance its capabilities in both policy formulation and the system development necessary for successful policy implementation. In addition, the Bank will work to expand the diversity of working arrangements so as to improve employees' work-life balance, while holding down total personnel expenses.

With these precepts guiding its human resource

management, the Bank has set the ceiling on the number of full-time employees for fiscal 2010 at 4,980, a decrease of 20 employees from fiscal 2009.

The Bank will continue to acquire and train employees, while further raising employee motivation. To this end, job rotation and career development programs will be improved. The Bank will also be more active in sending/receiving employees to/from outside institutions, with a view to enhancing communication channels.

C. Budget for Expenses

The Bank will keep any increase in expenses to a minimum by thoroughly examining each item of expenditure and achieving a more streamlined overall budget; at the same time, it will appropriate a portion of the budget to deal with the issues and implement the action plans outlined in the Strategic Priorities.

In keeping with these principles, the Bank has set its

budget for expenses for fiscal 2010 (the 126th fiscal year) as shown in the Attachment.

D. Performance Reviews

The Bank will evaluate the progress made in the improvement of business operations and organizational management described in the Strategic Priorities at the end of every fiscal year. It will release the results of this evaluation in the *Gyoumu Gaikyo Sho* (Outline of Business Operations), which is translated into English as the *Annual Review*.

In addition to these regular and comprehensive reviews, the Bank will conduct performance reviews of major projects some time after their completion. The Bank will examine, for example, whether the projects have achieved the desired results and whether unanticipated risks have arisen. The results of such reviews will be made available to the public.

Attachment

BUDGET FOR EXPENSES FOR FISCAL 2010

The Bank of Japan's budget for expenses for fiscal 2010 (the 126th fiscal year) is as follows (Table 1).³ While appropriating a significant portion of the budget to deal with the issues and implement the action plans outlined in the Strategic Priorities, the Bank has also thoroughly examined each item of expenditure to achieve a more streamlined overall budget.

1. The budget for expenses for fiscal 2010 (excluding the cost of fixed-asset purchases and contingency funds) decreased by 0.6 percent from the previous year to 181.3 billion yen, although one particular item, "other general and administrative expenses and costs," increased by 5.4 percent mainly in accordance with efforts to establish a new BOJ-NET. The overall decrease was due to reductions in the following items from the previous year: 2.0 percent in the cost of production of banknotes; 5.2 percent in administrative expenses for treasury business and Japanese government securities; 2.9 percent in personnel expenses; 2.8 percent in expenses for transportation and communications; and 0.9 percent in expenses for maintenance and repairs.

3. The Bank prepares a budget for expenses every fiscal year. Its budget for core operations, excluding the cost of purchasing fixed assets used for the Bank's business operations, is subject to the approval of the Minister of Finance under Article 51, paragraph 1 of the Bank of Japan Act before the beginning of each fiscal year. For fiscal 2010, the Bank sought approval on March 19, 2010 and will implement the budget upon authorization from the Minister of Finance. All figures, including those in Table 1, are rounded off to the nearest whole number.

2. The Bank appropriated a total of 11.0 billion yen for fixed-asset purchases, a decrease of 17.8 percent from the previous year, mainly due to the decrease in expenses incurred in updating and repairing automatic banknote examination machines. The Bank appropriated 1.0 billion yen for contingency funds in fiscal 2010, which was the same amount as in the previous year.

Table 1

Budget for Expenses for Fiscal 2010 (The 126th Fiscal Year)

Item	Initial budget (thous. yen)	Share ¹ (percent)	Change from the previous year (percent)
Cost of production of banknotes	50,945,064	28.1	-2.0
Administrative expenses for treasury business and Japanese government securities	19,525,768	10.8	-5.2
Personnel expenses	50,701,300	28.0	-2.9
Remuneration of the officers	427,252	0.2	-2.0
Remuneration of the employees	40,385,783	22.3	-2.7
Retirement allowances	9,888,265	5.5	-3.5
Expenses for transportation and communications	5,373,769	3.0	-2.8
Expenses for transportation	2,189,708	1.2	-2.7
Expenses for communications	3,184,061	1.8	-2.9
Expenses for maintenance and repairs	2,095,695	1.2	-0.9
Other general and administrative expenses and costs	52,631,051	29.0	5.4
Cost of expendable supplies	1,592,087	0.9	-3.3
Expenses for electricity and water supply	2,190,095	1.2	-3.7
Leasing fees for buildings and equipment	11,642,087	6.4	16.9
Expenses for maintenance of buildings and equipment	9,937,843	5.5	0.8
Miscellaneous expenses	27,268,939	15.0	4.1
Subtotal	181,272,647	100.0	-0.6
Cost of fixed-asset purchases	11,014,691	...	-17.8
Of which: Subject to the approval of the Minister of Finance ²	3,578,910	...	-55.4
Contingency funds	1,000,000	...	0.0
Total³	193,287,338	...	-1.8
Of which: Subject to the approval of the Minister of Finance ²	185,851,557	...	-2.9

Notes: 1. "..." indicates that figures are not applicable.

2. Excludes the cost of purchasing fixed assets used for the Bank's business operations.

3. Of the budget for expenses, those related to computerization amounted to 31,316,813 thousand yen, a 10.7 percent increase from the previous year, and are included in expenses for communications, leasing fees for buildings and equipment, expenses for maintenance of buildings and equipment, and miscellaneous expenses.

Budget estimates of computerization expenses assume required outsourcing man-hours of approximately 8,699 person-months (one person-month describes the workload equivalent to one person working for one month in system development), and total man-hours of approximately 11,467 person-months if the workload of the Bank's employees is included.