March 10, 2026

Bank of Japan

On-Site Examination Policy for Fiscal 2026

1. Introduction

The Bank of Japan (hereafter, the Bank) formulates the on-site examination policy every fiscal year based on the decision of the Policy Board.[1]

In conducting on-site examinations and off-site monitoring, it is becoming important to assess financial institutions' soundness and risk management in a swift and continuous manner and to monitor changes in the financial system as a whole in a timely fashion, in light of changes in the environment surrounding the financial system and various challenges faced by financial institutions.

Based on such recognition, the Bank conducts integrated operation of on-site examinations and off-site monitoring. In addition, it deepens coordination with the Financial Services Agency (FSA) through a wide range of initiatives, including joint surveys with the FSA targeting major financial institutions, and works on monitoring the financial system in detail.[2]

In the "On-Site Examination Policy for Fiscal 2026," the Bank outlines the situation of financial institutions' business management and risk management as assessed from on-site examinations and off-site monitoring in fiscal 2025. It also compiles issues key to conducting on-site examinations in fiscal 2026 and operations of on-site examinations while also taking into account recent changes in the environment. Moreover, with regard to off-site monitoring, while taking key issues in the on-site examination policy into

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[1] The Bank of Japan Act stipulates that "the content of a contract concerning on-site examinations" and "important matters concerning the implementation of on-site examinations for each business year" shall be determined by the Policy Board (Article 15, paragraph 2, item v).

[2] Topics of the joint surveys in fiscal 2025 include the following: the supervisory simultaneous stress testing based on common scenarios; joint surveys on foreign currency liquidity risk management and on cybersecurity management; and climate scenario analysis. Topics will be reviewed as appropriate in consultation with the FSA in line with their importance to the financial system.

account in order to ensure that off-site monitoring is well integrated with on-site examinations, the Bank will respond flexibly to changes in the environment.

2. On-Site Examinations in Fiscal 2025 and General Observations

(1) On-Site Examinations in Fiscal 2025

The Bank carried out on-site examinations of 66 financial institutions: 21 domestically licensed banks, 41 *shinkin* banks, and 4 other institutions, including securities companies as well as Japanese branches and subsidiaries of foreign banks.[3] From fiscal 2023, the Bank focused on hybrid-type examinations that combine on-site examinations and remote methods, and it continued to do so during fiscal 2025.

Number of Financial Institutions Examined

(number of entities)

	Fiscal 2023	Fiscal 2024	Fiscal 2025
Domestically licensed banks	20	20	21
Shinkin banks	42	41	41
Other institutions	5	7	4
Total	67	68	66

(2) Issues Identified through On-Site Examinations and Off-Site Monitoring

Financial institutions' profitability and financial soundness, business management, as well as their risk management examined in on-site examinations and off-site monitoring in fiscal 2025, are as follows.

Profitability, Financial Soundness, and Business Management

Looking at financial institutions' financial soundness, their capital levels are adequate relative to the amounts of various types of risk taken on, and they have sufficient capacity to absorb losses. The smooth functioning of financial intermediation has been maintained

[3] "Securities companies" in this document refers to firms that conduct securities-related business activities among those classified as Type I Financial Instruments Business in Article 28 of the Financial Instruments and Exchange Act.

even amid various uncertainties surrounding domestic and overseas financial and economic conditions.

Major financial institutions have strengthened the profitability of their domestic deposit-taking and lending activities that take into account rising yen interest rates. They have also pushed ahead with inorganic growth strategies involving acquisitions and investments at home and abroad and have continued to strengthen group-wide profitability and to broaden their revenue sources.

Regional financial institutions have continued to improve the profitability of their domestic deposit-taking and lending activities due to rising yen interest rates. They have also been active in pursuing risk taking in areas they are promoting, such as real estate lending, structured finance that includes financing for leveraged buyout (LBO) loans, renewable energy investment, and ship finance, and investment in private equity (PE) funds. On the other hand, core profitability of some regional financial institutions continued to be pushed down due to structural factors such as the declining population and to the increase in investment in computer systems and human capital, in addition to increases in interest payments on deposits following rising yen interest rates.

In this situation, in terms of business management, there were some financial institutions that faced challenges in estimating the impact of interest rate hikes on their profits. Some also experienced difficulties in conducting PDCA cycle management of deposit and loan balance targets and in assessing pass-through rates to deposit and loan interest rates, both of which are a prerequisite for estimating the impact of a hike. The Bank held discussions with financial institutions that were expected to see a deterioration in their profits regarding initiatives to strengthen their profitability. Moreover, the Bank also held discussions with some financial institutions experiencing the impact of personnel constraints on their business operations and anticipating further reductions in personnel. It encouraged these institutions to adopt organization-wide measures related to human resource management and branch operations.

Meanwhile, through the promotion of digital transformation (DX), including the use of generative artificial intelligence (AI), an increasing number of financial institutions have been improving the efficiency of their operations and enhancing non-face-to-face services for customers. Against this background, in fiscal 2025, the Bank, together with the FSA, implemented a self-assessment survey on cybersecurity for some major financial institutions, regional financial institutions, and securities companies, etc., returning the aggregated results of the survey to the financial institutions and exchanging views with the relevant industry associations. Moreover, the Bank has conducted joint climate scenario analysis on climate change risk with the FSA and some major financial institutions and published their findings.

Credit Risk

Looking at financial institutions' credit provision, some major financial institutions have been focusing on financing for non-bank financial intermediaries (NBFIs), including investment funds, and merger and acquisition (M&A) financing, along with real estate lending, data center investment, and renewable energy investment. Some regional financial institutions are focusing on real estate lending -- especially for the sale and purchase of real estate and real estate leasing businesses -- as well as housing loans and structured finance. Moreover, both major and regional financial institutions have been actively engaged in supporting firms' core businesses, providing financing support to firms, and supporting firms to improve their business conditions.

Against this background, credit costs have been leveling out.

With regard to risk management, there were some cases where financial institutions had problems not only in assessing borrowers' financial and funding conditions, but also in ensuring the effectiveness of support measures for low-performing firms and in conducting PDCA cycle management of their support plans. There were cases in which credit screening and monitoring in promoted areas were insufficient. For example, in the case of loans for real estate leasing businesses, there were issues in the project revenue and expenditure assessment and portfolio analysis; in the case of loans for real estate sales businesses, there were issues in assessing acquisition and sale prices of properties, and sales plans. In major metropolitan areas, there were cases of an increase in loans for short-term trading of properties as well as loans for real estate leasing businesses based on the assumption that properties will be sold. Moreover, in the case of structured finance, there were issues in examining income and expenditure forecasts and stress resilience, and in portfolio monitoring of both LBO financing and ship finance.

Market Risk

Looking at developments in securities investment, financial institutions have generally maintained a cautious investment stance, due mainly to increasing uncertainty surrounding market conditions. Moreover, among regional financial institutions, valuation losses on securities holdings, particularly domestic bonds, have increased, with many institutions experiencing valuation losses. In this situation, some financial institutions have continued to increase the amount outstanding of their yen-denominated bond investment to be held to maturity.

In terms of risk management, some financial institutions, especially regional ones, raised their loss limits without adequate deliberations due to inadequate organization-wide consideration and shared understanding of the level of risks or valuation losses acceptable from a management perspective. As a result, the institutions could not prevent an increase in valuation losses. In an environment of heightened market uncertainty, there have been cases where organization-wide consideration of management actions to prepare for market turmoil, as well as the management of distributable profits and net asset values, has been inadequate. Under such circumstances, the Bank had discussions with financial institutions holding large valuation losses relative to their profitability and financial soundness, presenting simulation results under certain assumptions. These discussions addressed the necessities of the policies for dealing with valuation losses and managing valuation losses on securities holdings as a whole, including held-to-maturity bonds.

Liquidity Risk

Major financial institutions have been making efforts with regard to foreign currencies to enhance funding stability by reducing dependence on FX and currency swap funding and strengthening efforts to acquire foreign currency deposits, the stickiness of which is relatively high. In this context, there were challenges in quantifying cash flow in liquidity stress testing and contingency funding plans.

Among regional financial institutions, there has been an increase in the number of institutions whose retail deposits have been declining or whose pace of increase in deposits has slowed. Under such circumstances, the share of large deposits has increased, indicating a change in the stickiness of deposits. In this context, there were cases where analysis of deposit developments was inadequate. Some of these institutions faced challenges in managing liquidity reserves and conducting liquidity stress testing while taking into account changes in risk profiles, such as the stickiness of deposits and the liquidity of assets in the asset-liability structures. Also, challenges existed in contingency funding plans in the event of stress. As for foreign currency funding, those institutions that have had an increase in funding needs compared with investment were facing challenges regarding the magnitude of liquidity stress testing and contingency funding plans in the event of stress.

Operational Risk[4]

With regard to IT system risks, while both major and regional financial institutions are increasingly using new digital technologies, cyber threats such as ransomware attacks are becoming more prevalent. Against this background, regarding cybersecurity management, there were some cases where adoption of the FSA's "Guidelines for Cybersecurity in the Financial Sector" released in October 2024 was inadequate. There were also cases where the management of third parties, such as group companies and outsourcee companies, and preparations for addressing disruptions related to the use of cloud computing were insufficient.

As in fiscal 2024, the Bank looked into financial institutions' frameworks for anti-money laundering and countering the financing of terrorism through the framework of coordination between the FSA's inspections and the Bank's on-site examinations. The examinations showed that, while institutions overall were making efforts to improve their frameworks, the responses of some institutions were inadequate.

3. On-Site Examination Policy for Fiscal 2026

On-site examination policy for fiscal 2026 is as follows (see attachment for more details on the key issues). With regard to off-site monitoring, while taking key issues in the on-site examination policy into account in order to ensure that off-site monitoring is well integrated with on-site examinations, the Bank will respond flexibly to changes in the environment.

[4] Operational risk refers to risks related to overall business operations, including, for example, risks related to business procedures, compliance, computer systems, and business continuity.

(1) Outlook for Profitability and Financial Soundness as well as Efficacy of Business Management

The Bank will examine (1) the respective boards of directors and senior management's view of the external environment, including changes in financial and economic conditions at home and abroad and structural challenges faced by regional economies, such as the declining population; (2) the feasibility of their medium- to long-term business strategies; (3) the outlook for profitability and financial soundness on that basis; and (4) the effectiveness of the financial institutions' business management. In doing so, the Bank will pay particular attention to the following issues:

- For major financial institutions, the status of efforts in a wide range of financial services through their global activities, group strategies, and inorganic growth strategies. In addition, the status of promoting DX and the use of generative AI, and that of developing risk-management frameworks concerning these initiatives.
- For regional financial institutions, the principles behind and the status of efforts toward building a sustainable business model, taking into account regional economies and management resources. In addition, (1) efforts to strengthen top-line earnings, and (2) the efficacy of measures to improve business efficiency through the promotion of DX, including the use of generative AI. For those that have been pushing ahead with strengthening business foundations through business integration, enhancement of group-wide business activities, business collaborations with other firms, and the joint use of administrative operations and computer systems, the status and efficacy of such efforts.

  -- With regard to regional financial institutions that are facing more severe staff constraints, the Bank will examine the effects on their business operations, and also examine resource management, including branch operations, staff allocations, and their efforts to raise human capital, and have dialogue with these institutions on the efficacy of such management and on business strategies, while taking into account the outlook for personnel.

  -- In cases where a substantial contraction in the business base is expected due to factors such as population decline, the Bank will have dialogue with the relevant institutions regarding their business strategies, taking into account the long-term outlook for loans, deposits, and personnel.

-- Through examinations of these issues, the Bank will continue dialogue with regional financial institutions on the status of implementing measures to support regional economies and strengthen their business foundations in coordination with off-site monitoring.

- The approach and framework for asset-liability management (ALM) -- that is, balance sheet management -- such as for loan and deposit operations and securities investment.
- The outlook for profitability and financial soundness in light of interest rates factored in by the markets, efforts to enhance top-line earnings, and the status toward the improvement in business efficiency. Discussions regarding the feasibility of deposit and loan balance and pass-through rates to deposit and loan interest rates using profitability simulations.
- The effectiveness of profit management -- including how return on risk-weighted assets (RORA) and other profitability indicators are used -- to improve profitability at institutions that aim to improve their return on equity (ROE), etc.
- Management of financial soundness mainly based on the valuation gains and losses on securities holdings and the amount of risk, including the effects on distributable profits and net asset values in the event of stress.
- ALM that takes into account interest rate risk in the banking book (IRRBB) and the status of internal models for core deposits.
- Whether financial institutions identify and manage climate-related financial risks, their information disclosure, and their engagement with corporate customers.

(2) Status and Efficacy of Governance Framework

The Bank will examine the status and efficacy of financial institutions' governance framework necessary to ensure the effectiveness of business management and risk management. In doing so, it will pay particular attention to the following issues:

- In the case of financial institutions that have overseas branches and subsidiaries and financial holding companies, their business management commensurate with their group strategies, global activities, as well as financial regulatory and supervisory frameworks in different jurisdictions.
- The effectiveness of internal audit functions and efforts to enhance them.

- The framework for the collection of the information necessary for effective business and risk management.

(3) Status of Various Risks and Risk Management Frameworks

Taking into account major risks that the respective boards of directors and senior management are aware of and the countermeasures against these risks, the Bank will review current developments and future directions of various risks faced by financial institutions and then examine the effectiveness of their risk management. In doing so, the Bank will pay particular attention to the following issues:

Credit Risk

- Whether financial institutions ascertain borrowers' financial and funding conditions, including the impact of rising interest rates, and portfolio characteristics, as well as changes therein. Moreover, whether their initial screening and interim management based on such information are appropriate, and the status of deliberations on methods for write-offs and loan-loss provisions (including the sufficiency of loan-loss provisions for large borrowers with unfavorable business conditions).
- Implementation of credit screening, management frameworks, and portfolio analysis -- including Loan-to-Value (LTV) and Debt Service Coverage Ratio (DSCR) analysis and stress testing -- and proactive monitoring of real estate lending and housing loans. The status of real estate lending in major metropolitan areas and the credit screening and management frameworks for such lending.
- Frameworks for credit screening and monitoring with regard to other promoted areas (financing for NBFIs such as investment funds, M&A financing, data center investment, and structured finance).
- The efficacy of support measures to address management challenges for borrowers with unfavorable business conditions, as well as PDCA cycle management of the support plans.
- Estimation of future credit costs and downside risks in light of financial and economic conditions and default cases.

- The status of initiatives and challenges to support firms in their respective business areas, including support for business succession, M&As, the use of corporate value security interests, and equity investment.

Market Risk

- Policies for dealing with valuation losses on securities.
- Whether financial institutions appropriately ascertain and share organization-wide their risk tolerance relative to their profitability and financial soundness.
- The effectiveness of the management of loss limits and the status of deliberations on management actions to be taken in the event of market turmoil, and the status of the use of market stress tests.

Liquidity Risk

- Implementation of analysis on deposit developments and their stickiness at financial institutions for which retail deposits have been declining or whose pace of increase in deposits has slowed, and at those paying relatively high interest rates on deposits. The effectiveness of managing liquidity reserves while taking into account changes in risk profiles, such as the stickiness of deposits and the liquidity of assets in the asset-liability structures, conducting liquidity stress testing, and also the effectiveness of contingency funding plans in the event of stress.
- Major financial institutions' frameworks for ascertaining and managing foreign currency liquidity risk.
- The status of investment-funding gaps, liquidity stress testing, and the effectiveness of contingency funding plans at regional financial institutions that focus on foreign currency-denominated loans and investments.

Operational Risk[5]

- The appropriateness of management frameworks for large-scale projects such as the upgrading of core banking systems and the effectiveness of measures to prevent computer

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[5] The Bank will review its examination of the enhancement of financial institutions' frameworks for anti-money laundering and countering the financing of terrorism while sharing its awareness of and perspectives on issues with the FSA through the framework of coordination between the FSA's inspections and the Bank's on-site examinations.

system failures and of recovery systems in the event of a failure (including with regard to cloud computing).

- The status of frameworks for cybersecurity management and PDCA cycle management in adopting the FSA's guidelines.
- The effectiveness of measures to prevent the occurrence and recurrence of fraud, etc., organizational checks and balances. The functioning of internal controls, including internal audits and compliance frameworks.

4. Operations of On-Site Examinations

(1) Hybrid-Type Examinations That Combine On-Site Examinations and Remote Methods

During the "regular examinations," which take about three weeks and consist of a comprehensive examination and assessment of regional financial institutions' business conditions and risk management frameworks, the first two weeks or so will basically be spent conducting on-site examinations, while the last week or so will be spent conducting examinations using remote methods. However, depending on factors such as examinee institutions' circumstances, the Bank may adjust the relative length, etc. of on-site and remote examinations and/or may conduct examinations entirely on-site.

(2) Giving Consideration to Financial Institutions' Operational Burden and Improving Efficiency

While making use of the information obtained through off-site monitoring, the Bank efficiently conducts examinations (hereafter referred to as on-site examinations or examinations using remote methods) based on a risk-based approach by deciding, in a flexible and efficient manner, the frequency, length, and scope of its examinations, as well as the documents to be submitted and the number of examiners involved, on the basis of a comprehensive assessment of individual financial institutions, such as from the following perspectives: (1) the impact on the financial system of the materialization of risks inherent in financial institutions; and (2) financial institutions' soundness and profitability, as well as the degree of risk taking.

In order to reduce the operational burden on examinee institutions and further improve the operational efficiency of examinations, the Bank will continue to conduct "short-term examinations" of some regional financial institutions; "short-term examinations" are examinations that have been shortened to about two weeks and are based on a risk-based approach, in which operational risk management, etc. are excluded from the scope of the examination.

In addition, the Bank will strengthen its coordination with the FSA by coordinating the planning of the FSA's inspections and the Bank's on-site examinations through the Joint Group for Coordinating FSA's Inspections and BOJ's On-Site Examinations and by sharing the findings of inspections and examinations. In conducting on-site examinations, the Bank will avoid overlapping with various joint surveys that it conducted with the FSA -- such as the supervisory simultaneous stress testing based on common scenarios, and joint surveys on foreign currency liquidity risk management and on cybersecurity management -- to take into account the operational burden on examinee financial institutions.

The Bank will share its awareness and cooperate with overseas regulators when conducting on-site examinations on internationally active major financial institutions.

(3) Gaining Financial Institutions' Understanding

The Bank will work to enhance its communication with financial institutions being examined through a post-examination survey and interviews conducted after the examinations as necessary to gain their full understanding of and trust in the examination process and results. The Bank will constantly work on improving on-site examination procedures by responding to opinions and requests gathered from examinee institutions.

Moreover, through the regular exchange of views with members of the financial industry, the Bank intends to continue exchanging views on the operation of its examination and monitoring, while focusing on efforts to further strengthen coordination between the FSA and the Bank.

Attachment

Issues Key to On-Site Examinations in Fiscal 2026

I. Outlook for Profitability and Financial Soundness as well as Business Management

The Bank will examine whether financial institutions are making necessary efforts from the perspective of both Subsections A and B below, in order to build a sustainable business model into the future.

In relation to this, in the on-site examinations, the Bank will examine whether financial institutions can ensure sustainable profits and maintain their financial soundness by conducting simulations of their profitability based on the interest rates factored in by the markets.[1] It will also conduct a profitability and capital adequacy ratio level simulation under certain standard stress scenarios and discuss with the respective boards of directors and senior management their awareness of issues regarding profitability and financial soundness, as well as policies to improve these. As for some major financial institutions, the Bank, together with the FSA, will conduct supervisory simultaneous stress testing based on common scenarios as part of off-site monitoring to gain a deep understanding of risk profiles inherent in their business models, thereby developing a comprehensive perspective for evaluating their financial soundness. The Bank will also have dialogue with these financial institutions on their business challenges, such as the sophistication of risk management frameworks.

A. Efforts to Achieve Profits and the PDCA Cycle for Business Operations

The Bank will examine whether financial institutions, in order to achieve the profits that they should aim for, have appropriately established and operate a system (a so-called PDCA cycle for business operations) under which they formulate and implement business strategies and plans while accurately understanding the domestic and overseas business environment, examine the results, and review such strategies and plans in a timely manner in response to changes in the business environment.

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[1] Profits here are defined as pre-provision net revenue (PPNR, excluding profits and losses from investment trusts due to cancellations) minus credit costs and losses on the redemption of mutual funds.

The Bank will collect information on changes in the environment surrounding financial institutions' business in a forward-looking manner, including through off-site monitoring. For example, it will examine a wide range of issues such as (1) uncertainties over financial and economic conditions at home and abroad, (2) the effects of the growing presence of NBFIs, (3) structural challenges faced by regional economies, (4) labor shortages, (5) the promotion of DX and the use of generative AI, and (6) developments in financial regulation and supervision at home and abroad, and also examine financial institutions' recognition of these issues and their innovative initiatives.

Based on such recognition of the environment, in the case of major financial institutions, the Bank will examine the following, in coordination with off-site monitoring: their global activities and group strategies (including those with regard to overseas branches and subsidiaries and inorganic growth) in light of changes in foreign currency funding conditions, international financial regulations, and financial regulatory and supervisory frameworks in different jurisdictions; efforts in a wide range of financial services, such as those toward the promotion of DX and the use of generative AI; and business process reengineering aimed at raising business efficiency. It will then analyze the details of their efforts and effectiveness from the standpoint of group-wide profitability.

With regional economies facing structural factors such as declining and aging populations, it is necessary for regional financial institutions to continue to contribute to achieving sustained growth in their region by performing their financial intermediation functions smoothly and making efforts to support their customers in tackling the challenges they face and enhancing their growth, and for the institutions to continue to endeavor to strengthen their own business foundations in order to firmly provide such support into the future. From this perspective, the Bank will examine the status and feasibility of efforts to strengthen top-line earnings, in order to build a sustainable business model, and of measures to improve business efficiency through the promotion of DX, including the use of generative AI. For institutions that are working to reinforce their business foundations through business integration and enhancement of group-wide business activities, such as in the form of holding companies, as well as through business alliances with other banks and firms from other industries and the joint use of administrative operations and computer systems, the Bank will examine the status and effectiveness of these efforts. Moreover, as for regional financial institutions that are facing more severe staff constraints, mainly due to increase in employee turnover and to recruitment difficulties, the Bank will also examine under these circumstances the effects on their business operations and also examine resource management, including branch operations, staff allocations, and efforts to raise human capital, and have dialogue with these institutions on the efficacy of such management and business strategies, taking into account the outlook for personnel. Particularly for institutions in which a substantial contraction in the business base is expected due to factors such as a decline in population and number of offices, the Bank will have dialogue with the relevant institutions regarding their business strategies, taking into account the long-term outlook for loans, deposits, and personnel. Through these examinations, the Bank will continue dialogue with regional financial institutions on the status of implementing measures to support regional economies and strengthen their business foundations, as well as their future policies and challenges in coordination with off-site monitoring.

The Bank will examine the outlook for financial institutions' future profitability and financial soundness through profitability simulations, etc. In doing so, it will examine the approach and framework for ALM -- that is, balance sheet management -- such as for loan and deposit operations and securities investment. On this basis, it will ascertain the outlook for profitability and capital adequacy ratio level, etc., based on financial institutions' outstanding amount of loans and deposits and the feasibility of expected pass-through of interest rates to loan and deposit interest rates, taking into account the interest rates factored in by the market. The Bank will also conduct simulations on profitability, capital adequacy ratio level, distributable profit, and net asset values under certain standard stress scenarios. Based on the results, it will engage in discussions regarding the necessity of initiatives to strengthen top-line earnings and to improve business efficiency, and, if necessary, encourage financial institutions to strengthen PDCA cycle management to enhance profitability.

In addition, the Bank will confirm whether financial institutions' profit management is appropriate, relative to risk, in employing the PDCA cycle for business operations. For financial institutions that aim to enhance ROE, etc., in addition to examining their status of risk taking, returns to shareholders, and the capital use of inorganic investment, the Bank will examine whether their company-wide financial goals are consistent with profitability indicators such as RORA for each business division and client firm, as well as whether profit management is effective. In the case of other financial institutions, the Bank will examine whether they have worked on basic matters such as ascertaining the profit outlook with a certain degree of accuracy. In addition, it will examine how these financial institutions make use of efficiency indicators, while taking into account their profitability, financial soundness, and business scope.

B. Understanding of and Response to Risks Related to Business Strategies and Plans

The Bank will examine whether financial institutions accurately identify risks accompanying the implementation of their business strategies and plans, and whether such identification is leading to a review of these items with the respective boards of directors and senior management being involved. The Bank will pay particular attention to whether financial institutions ascertain risks that take into account changes in their business environment and strategies, such as developments in financial markets -- including domestic and foreign interest rates and asset prices -- geopolitical risks, and responses to climate change. Moreover, the Bank will examine whether financial institutions have ascertained and managed quantitatively (1) risks acceptable relative to profitability and financial soundness and (2) valuation losses on securities holdings, under the integrated risk management framework.

In doing so, the Bank will examine whether financial institutions have analyzed the possible impact on profitability and financial soundness -- that is, their capital adequacy ratio levels, distributable profits, and net asset values -- in the event of significant changes in financial and economic conditions, including through the use of comprehensive stress testing, and examine whether the institutions have considered appropriate management actions in advance. With regard to comprehensive stress testing, the Bank will examine the following: (1) the involvement of the respective boards of directors and senior management and the control functions of the relevant divisions in charge of such activity; (2) the comprehensiveness of scenarios and coverage of the subjects of the stress testing; (3) schemes to develop and verify models and data; and (4) frameworks to utilize test results for the PDCA cycle for business operations and their operational implementation. In particular, the Bank will examine the impact of changes in interest rate environment on valuation losses on securities holdings, losses on the redemption of mutual funds, and the amount of risk. Moreover, it will check how financial institutions have placed and managed IRRBB in their risk management framework, and have dialogue on the status of their internal models for core deposits.

In the case of financial institutions for which there is concern about their future profitability and financial soundness, the Bank will focus its dialogue with the respective boards of directors and senior management on the balance between capital and risk-weighted assets to perform their financial intermediation function in a stable manner into the future, the framework to manage them, and their capital policies including dividend distributions. In off-site monitoring after the completion of on-site examinations, the Bank will maintain dialogue with the top management of such institutions.

Regarding Global Systemically Important Financial Institutions (G-SIFIs) and their equivalents, the Bank will examine the effectiveness of recovery plans and contingency plans. With regard to overseas G-SIFIs' Japanese branches and subsidiaries, the Bank will examine whether they have established an appropriate management framework in line with their business scope and risks while understanding their roles within the group. On this basis, it will examine (1) impacts on Japanese branches and subsidiaries under the assumption of stress events for the group as a whole and responses to them, and (2) the role of Japanese branches and subsidiaries within the recovery and resolution plans, including their involvement in these matters. Regarding those subsidiaries with corporate status in Japan, the Bank also will examine the support system provided by headquarters in the event of a deterioration in business conditions. If yen funding is managed by bases other than Japanese branches and subsidiaries, (3) the Bank will confirm the state of the management of the bases and their framework of communicating with the Bank in preparation for unexpected contingencies. Moreover, (4) it will conduct examinations, including the collection of information from their headquarters, of the impact on the Japanese financial system in the case of assumed stress events for the group as a whole.

With regard to climate change responses, the Bank will engage in dialogue with financial institutions on the following issues according to their size and characteristics: (1) the identification and management of climate-related financial risks; (2) information disclosure; and (3) engagement with corporate customers. In doing so, mainly through off-site monitoring, the Bank will urge financial institutions to enhance their climate-change scenario analysis according to their size and characteristics, taking into account the climate-change scenario analysis based on a common scenario between the FSA and the Bank, and also taking into account international discussions regarding regulation, supervision, and risk management of climate-related financial risks.

II. Governance

A. Ensuring the Efficacy of Governance

To ensure the efficacy of financial institutions' governance, the Bank will review whether management policies are disseminated throughout the organization, whether communication within the organization regarding the assessment of risks is smooth, and whether a governance framework is in place that enables the organization to properly harness its organizational capabilities to achieve its business strategies and plans. The Bank will examine whether they have established group-wide global governance frameworks, including business and risk management and internal audits, that are appropriate for their business strategies, such as initiatives to expand activities mainly through inorganic investment, and to strengthen the cross-selling of services on a group-wide basis.

In the on-site examinations, the Bank will conduct interviews with external directors and other officers as necessary.

B. Using and Enhancing Internal Audit Functions

With regard to the effectiveness of internal audits, the Bank -- depending on financial institutions' business scope, risk taking, and the materialization of risks -- will examine (1) whether the institutions appropriately decide the scope of internal audits and allocate audit resources through risk assessment that takes into account business strategies, risk taking, and the materialization of risks, (2) whether they have verified the appropriateness of their business operations and properly made improvements reflecting the results of the audits, and, in particular, whether headquarters audits examine in depth the effectiveness of risk management and lead to the consideration of effective improvement measures while making use of outside experts' knowledge as necessary, and (3) whether the results and recommendations of such audits are utilized in their business. To improve the effectiveness of on-site examinations, the Bank will conduct hearings with the respective internal audit divisions before on-site examination, if necessary.

C. Information Management Frameworks Necessary for Business Management and Risk Management

Concerning the global and group-wide financial information and risk information required for the respective boards of directors and senior management to make appropriate business decisions, the Bank will examine, particularly for major financial institutions, (1) whether they have appropriately set up a framework for the collection of the necessary information, such as a management information system (MIS), (2) whether sufficient management resources are allocated to this end, and (3) whether the completeness, accuracy, and timeliness of information, etc. are appropriate. In doing so, the Bank also will confirm the status of responses with regard to institutional frameworks, such as international financial regulations.

III. Credit Risk Management

A. Credit Screening and Monitoring

For both major and regional financial institutions, it is important to conduct credit risk management that takes into account changes in financial and economic conditions as well as individual borrowers' conditions. Regional financial institutions in particular need to conduct credit risk management in consideration of structural challenges faced by regional economies, such as a declining population.

Given this situation, the Bank will examine whether financial institutions (1) appropriately ascertain borrowers' financial and funding conditions at the individual borrower level as well as changes therein, and analyze their repayment capacity, including resilience to stress from rising interest rates; (2) analyze portfolio characteristics and changes; and (3) properly analyze cases of credit cost incurrence. Moreover, the Bank will also examine whether financial institutions accurately use these analyses in their initial screening and interim management of loans. In particular, it will carefully examine whether financial institutions sufficiently comprehend the business conditions of large borrowers that are low-performing or carry considerable business risks and whether their credit screening and monitoring are appropriate, including the accuracy of self-assessments. In doing so, the Bank will employ "line sheet reviews" (the same applies throughout this section).[2]

B. Responses to Promoted Areas

The Bank will examine whether appropriate risk management is being conducted in the areas that financial institutions promote.

For both major and regional financial institutions, the Bank will examine their lending stances and credit screening and monitoring frameworks with regard to loans to real estate businesses and housing loans, the outstanding amounts of which have been increasing, focusing mainly on loans in major metropolitan areas and taking into account the fact that real estate prices have continued to rise, particularly in these areas. In particular, with regard to loans to real estate sales businesses, the Bank will examine whether these are managed proactively based on the validation of project feasibility and progress management, real estate valuations, changes in the length of selling periods, and the monitoring of conditions in the real estate market. With regard to loans to real estate leasing businesses, such as loans for apartments and studio condominiums, the Bank will examine financial institutions' revenue and expenditure plans and the collectability of these loans, including rents, vacancy rates, and required expenses; the status of early repayments (early sale of properties); and financial institutions' portfolio management using indicators such as LTV ratios and DSCRs and analyses of borrower and property characteristics. In addition, the Bank will also examine the adequacy of credit screening and monitoring frameworks that assume stress events, such as rising interest rates and falling real estate prices.

With regard to other promoted areas, taking into account that some major financial institutions have been expanding their efforts globally in areas such as financing for NBFIs, including investment funds, M&A financing, as well as data center investment and renewable energy investment, the Bank will examine (1) whether the institutions are

[2] A line sheet review consists of (1) interviews with relevant divisions on the basis of documents ("line sheets") containing information on developments in the financial condition, developments in the borrowing and repayment situation, and future prospects of chosen individual borrowers, as well as the financial institution's self-assessment results, lending policy, etc.; and (2) the understanding and assessment of the borrowers' business environment, such as developments in regional economies and industries, as well as its credit management practices, etc.

appropriately managing individual credit screening and monitoring, as well as other operations, including the concentration of credit and the origination and distribution of loan-related instruments; and (2) whether their headquarters have established global management and reporting rules and are appropriately monitoring them. Regarding regional financial institutions that are focusing on structured finance, etc., the Bank will examine whether their credit screening and monitoring are appropriate in light of loan structures and borrower characteristics.

C. Support for Firms to Improve Business Conditions

In helping firms to improve their business conditions, it is important for both major and regional financial institutions to provide support that takes into account changes in financial and economic conditions, as well as individual borrowers' conditions. Regional financial institutions in particular need to ensure the effectiveness of this support from the viewpoint of increasing the sustainability of regional economies.

From this standpoint, the Bank will examine (1) whether financial institutions' headquarters and branches are cooperating and accurately identifying borrowers with unfavorable business conditions that require support to improve their business conditions, mainly taking account of individual borrowers' financial conditions and the status of loan coverage ratios and loan-loss provision ratios. In addition, the Bank will examine the efficacy of PDCA cycle management for financial institutions' support to improve business conditions of these borrowers, including the following: (2) whether financial institutions adequately analyze the current business conditions and future prospects of borrowers, and, after assessing the feasibility of business rehabilitation, share with them an understanding of the business challenges they face and possible countermeasures; (3) whether these institutions' headquarters and branches are cooperating in terms of offering advice, recommendations, and support to help borrowers overcome challenges; and (4) whether feasible and effective support plans are being formulated and whether appropriate progress management is being conducted. Particularly for large borrowers who have been experiencing unfavorable business conditions for a prolonged period, the Bank will deepen dialogue with financial institutions to examine whether risks have built up; for example, whether they have continued to provide loans without making efforts toward devising more drastic solutions to address management challenges.

D. Outlook for Credit Costs (Write-Offs and Loan-Loss Provisions)

The Bank will examine future credit costs and downside risks -- taking into account financial and economic conditions in Japan and abroad, recent default cases, borrowers' conditions both at the individual borrower level and the portfolio level, and the status of loan coverage ratios and loan-loss provision ratios -- and have dialogue with financial institutions on their adequacy. Moreover, the Bank will deepen its dialogue with financial institutions regarding the appropriate approach to calculating write-offs and loan-loss provisions, and exchange opinions with the accounting auditors of financial institutions as necessary. In particular, the Bank will engage in in-depth dialogue regarding large borrowers with unfavorable business conditions, including on the sufficiency of loan-loss provisions.

E. Initiatives to Support Firms in Their Business Areas

For regional financial institutions in particular, the Bank will examine the status of efforts aimed at promoting the sustainable growth of firms in their business areas and revitalizing regional economies, including support for business succession and M&As, the use of corporate value security interests, and the provision of capital-like funds such as equity investments. In addition, the Bank will engage in dialogue on their future approaches to these efforts and the challenges they face.

IV. Market Risk Management

A. Establishment of Management Frameworks Depending on Financial Institutions' Risk Taking

Some regional financial institutions have seen increases in valuation losses as a result of insufficient organization-wide consideration and sharing of loss limit frameworks, action plans, and risk tolerance relative to their profitability and financial soundness. Moreover, there have also been moves to increase the amount outstanding of yen-denominated bond investments to be held to maturity.

Against this background, the Bank will review financial institutions' market risk-taking policies (including hedging policies) based on changes in the interest rate environment, as well as their risk management frameworks, including the handling of held-to-maturity bonds. With respect to financial institutions experiencing significant valuation losses relative to their profitability and financial soundness, the Bank will engage in dialogues regarding their policies for addressing such valuation losses. Moreover, the Bank will examine whether financial institutions, when formulating investment plans, verify that the amount of risk relative to their profitability and financial soundness remains at acceptable levels if those investment plans are implemented. The Bank will also examine whether they assess the impact that an increase in valuation losses would have on their distributable profits and net asset values through the implementation, for example, of market stress test. In the case of financial institutions with increasing holdings of relatively illiquid risk assets, such as PE fund investments and private real estate investment trust (REIT) investments, the Bank will check whether risk profiles are properly identified, and whether risk management is being conducted appropriately, using market stress test.

B. Appropriateness of Various Risk and Loss Limits, and Responses to Market Turmoil

The Bank will examine whether financial institutions set various risk and loss limits at the appropriate levels relative to their financial soundness and profits, whether these are properly reviewed, and whether effective organization-wide action plans in case of market turmoil are considered. Moreover, the Bank will examine whether loss-cut rules are in place and functioning to allow for organizational review on the appropriateness of continuing to hold securities and for timely management action when a mandatory consultation framework becomes requisite, taking into account the impact on their financial soundness and profits.

V. Liquidity Risk Management

A. Yen Liquidity Risk Management

The Bank will examine, especially at financial institutions for which retail deposits have been declining as a trend or those whose increase in deposits has been sluggish, and at those paying relatively high interest rates on deposits, whether they are analyzing developments in deposits and their stickiness and examining as necessary countermeasures on an organization-wide basis. The Bank will also examine whether, in light of changes in risk profiles, such as the stickiness of deposits and the liquidity of assets in their asset-liability structures, financial institutions are appropriately reviewing their liquidity reserve management, liquidity stress testing, and contingency funding arrangements.

B. Foreign Currency Liquidity Risk Management

Given that internationally active major financial institutions have large amounts of foreign currency funding outstanding, the Bank will examine the following: (1) whether internationally active major financial institutions have set their indicators for the management of liquidity risk in line with their foreign currency balance sheet strategy; (2) whether such financial institutions have set up a framework for managing their funding gap based on their funding capacity, in terms of different currencies, and have a liquidity buffer to cope with sudden outflows of funds; and (3) whether they have developed liquidity stress testing and contingency funding plans in a consistent manner on a group-wide basis, based on reasonable capital flow assumptions.

In off-site monitoring, the Bank will also continue to examine major financial institutions' efforts to strengthen foreign currency funding bases and increase the sophistication of their risk management while cooperating with the FSA and overseas regulators that exercise jurisdiction over major financial institutions. The Bank will conduct joint surveys with the FSA on some major financial institutions.

Turning to regional financial institutions, particularly with regard to those that are actively lending or investing in foreign currency-denominated assets, as well as those that are highly dependent on short-term market funding, etc., the Bank will examine whether they have secured stable funding means that take into account changes in funding environment and market liquidity of assets and also examine their risk management frameworks, such as the conduct of and the use of liquidity stress testing and the effectiveness of contingency funding plans.

VI. Operational Risk Management

A. IT System Risk Management Frameworks

Regarding whether financial institutions, in large-scale upgrading of systems such as the move toward open and cloud core banking systems, are managing the various projects and outsourcee companies appropriately, the Bank will examine this while also investigating outsourcee companies, if necessary, and check deliberations for the next system (including joint systems to be used by regional financial institutions). Furthermore, focusing on critical computer systems, the Bank will examine the effectiveness of (1) measures to prevent computer system failures, including redundancy; and (2) recovery frameworks in the event of a failure, including the planning and training for contingencies. The Bank will also examine financial institutions' computer systems from the perspective of whether their risk management is in line with the use of new technologies and services brought about through the promotion of DX and the use of generative AI, including data management.

Moreover, in light of the growing trend toward financial institutions' business collaborations with third parties, such as the use of cloud computing and application programming interface (API) linkages, the Bank will examine whether they appropriately manage third parties, including outsourcee companies, in terms of the management of the development and operation of projects, a collaborative framework at times of system failures, and information security, such as with regard to customer data. In addition, the Bank will examine the effectiveness of financial institutions' IT governance -- their own and that of their group companies, etc. -- from the perspective of whether management resources are allocated to ensure both the efficacy of their system management, including cybersecurity, and efficiency with regard to their investment in computer systems.

B. Cybersecurity Management Frameworks

With respect to financial institutions' adoption of FSA guidelines, the Bank will examine whether, given the increase in cybersecurity threats and taking individual financial institutions' business scope (including the use of cloud computing) into account, they are identifying areas for improvement through gap analysis against the required level of cybersecurity management, making use of external assessments and other means. It will further examine whether, on the basis of this, they are formulating concrete action plans with established priorities and implementation timelines. In doing so, the Bank will examine whether, with the involvement of the boards of directors and senior management, budgetary and personnel resources are being allocated and PDCA cycle management toward the achievement of these action plans is being carried out appropriately.

The Bank will conduct joint examinations with the FSA on the cybersecurity management of some major financial institutions.

In cooperation with the FSA, the Bank will continue to implement a self-assessment survey on cybersecurity management frameworks, such as for regional financial institutions, and encourage institutions to ascertain their preparedness and strengthen their countermeasures.

C. Compliance Management Framework

The Bank will examine whether financial institutions have taken measures to prevent the occurrence and recurrence of fraud, whether organizational checks and balances including those carried out within front offices and risk management divisions, are properly established, as well as whether internal controls, including internal audits and compliance frameworks, are functioning effectively. In addition, especially for institutions that focus on fee-based business, it will examine the status of compliance frameworks, including with regard to the management of the abuse of dominant bargaining positions and conflicts of interest in relation to sales of financial instruments and advisory services.

D. Anti-Money Laundering and Countering the Financing of Terrorism

Given strong international requests to take measures specific to anti-money laundering and countering the financing of terrorism, it is essential for financial institutions to steadily implement these measures to ensure the proper conduct of their business operations and to maintain their credibility. On this basis, the Bank will review its examination of the enhancement of financial institutions' frameworks for anti-money laundering and countering the financing of terrorism while sharing its awareness and perspectives with the FSA through the framework of coordination between the FSA's inspections and the Bank's on-site examinations.

E. Administrative Risk Management

With a focus on financial institutions with a high frequency of operational accidents, the Bank will examine (1) whether effective measures to prevent recurrence have been implemented through understanding the actual situation of operational processing and analyzing the trends of such incidents; (2) whether financial institutions appropriately recognize changes in the risk profiles associated with centralizing business operations in head offices or reviewing branch functions, and whether they take appropriate countermeasures; and (3) whether they, including their major group companies and third parties such as their outsourcee companies and partners, have appropriately established and reviewed their management frameworks.

F. Business Continuity Management

The development of effective business continuity management is important to ensuring financial institutions' critical operations, as well as the smooth functioning of the payment and settlement systems in Japan. Based on this perspective, the Bank will examine whether business continuity management is reviewed appropriately in response to recent natural disasters -- such as earthquakes, typhoons, and floods -- and pandemics and cyber incidents. In doing so, it will take into account the expected scale of natural disasters, as well as individual financial institutions' presence in payment and settlement systems and in their respective business areas.[3]

[3] In the case of major financial institutions, etc., given changes in the environment, such as increased dependence on IT systems and third parties, the Bank will conduct examinations also from the perspective of the institutions' operational resilience in the event of system failures, terrorism and cyberattacks, pandemics, natural disasters, etc. (the establishment of early recovery and continuity systems based on the assumption that business operations may be disrupted even when all preventive measures have been taken).