FSR — Financial System Report

Measures Taken by the Bank of Japan for Financial System Stability

Bank of Japan
August 2005

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Introduction

The Bank of Japan strives to maintain and improve the stability and efficiency of the financial system, while conducting monetary policy. To achieve this objective, the Bank has conducted various business operations including the provision of the Bank's current account services and has taken necessary measures as appropriate.

The following is a summary of the measures taken by the Bank mainly in fiscal 2004 under the conditions described in "An Assessment of Financial System Stability: Focusing on the Banking Sector."

I. Current Status of the Special Measures

A. Background

For the past decade, the most important tasks for Japan's financial system have been to overcome the nonperforming-loan (NPL) problem and to recover its soundness and stability as a whole. Before discussing the measures taken by the Bank in fiscal 2004, the Bank summarizes general conditions of the financial system and gives an outline of measures taken by the government and the Bank in this period as below.

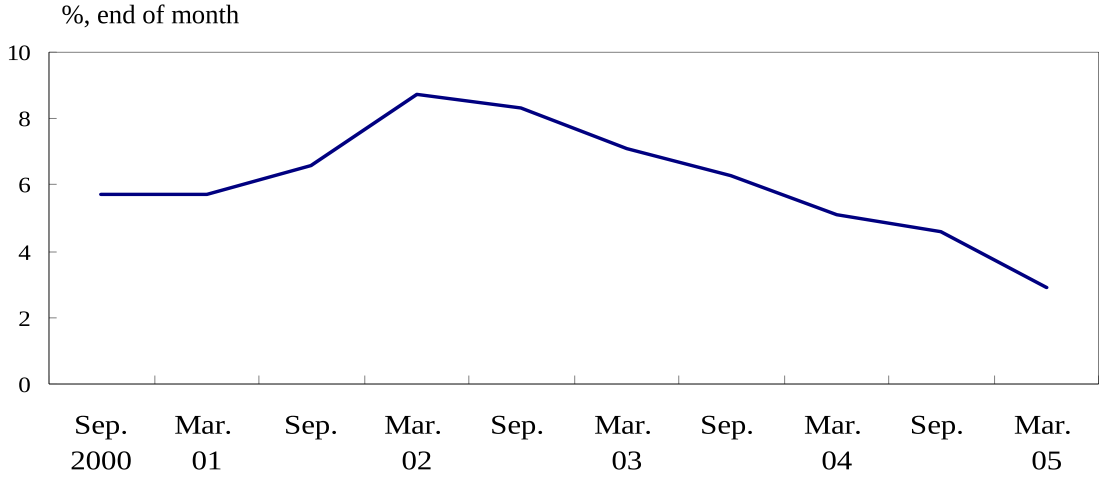
Japan's financial system has suffered from the NPL problem, which developed after the bursting of the bubble economy. The value of Japanese financial institutions' loan assets, which had been largely extended to the real estate sector, dropped sharply. The NPL problem undermined public confidence both at home and abroad in the soundness of the Japanese financial institutions. As a result, the financial system became so vulnerable that even a single bank failure posed a risk of causing a serious disturbance in the financial system. Although Japanese financial institutions subsequently disposed of a large amount of their NPLs, new NPLs continued to emerge due to several factors including the prolonged economic downturn and a decrease in corporate sales caused by intensified competition with emerging economies.

Under this situation, special measures to maintain financial system stability were considered to be necessary. The government provided a blanket guarantee on deposits to ease depositors' anxieties. To accelerate integrated revitalization and structural adjustments in the financial and industrial sectors, the government also took measures that enabled the Resolution and Collection Corporation (RCC) to purchase NPLs from sound financial institutions and enabled the Industrial Revitalization Corporation of Japan (IRCJ) to purchase loans from financial institutions.

Meanwhile, the Bank, in cooperation with the government, sought to maintain financial system stability by extending special loans needed for smooth resolution of failed financial institutions. In addition, the Bank purchased stocks held by banks, as the market risk stemming from these stockholdings could have posed a significant risk to banks' financial condition.

In fiscal 2004, the soundness and stability of the Japanese financial system recovered further as a result of considerable progress in resolution of the NPL problem. Supported by the special measures and economic recovery, financial institutions accelerated the removal of the NPLs from their balance sheets (Chart 1). In addition, their efforts to rehabilitate distressed borrower firms, including large ones, started to take effect. As a result, all of the special measures taken by the government ended on March 31, 2005. The Bank also wound up its stock purchasing program at the end of September 2004. The amount outstanding of loans extended under Article 38 of the Bank of Japan dropped to zero as of the end of March 2005.

Chart 1: Major Banks' Ratio of NPLs to Total Outstanding Loans



B. The Bank's Special Loans Pursuant to Article 38 of the Bank of Japan Law

The Bank extends loans pursuant to Article 38 of the Bank of Japan Law (hereafter the term "special loans" covers all such business) to maintain the financial system stability based on the Bank's four principles.[1]

The amount outstanding of the special loans marked a historical high of approximately 4 trillion yen in December 1997, but dropped to zero as of the end of March 2005. In fiscal 2004, the Bank ended provisions of special loans to two financial institutions, Minato Bank and Yamaichi Securities, as described below.

1. Subordinated loans extended to Minato Bank

On December 30, 2004, the Bank received full repayment of subordinated loans extended to Minato Bank before maturity, upon the borrower's proposal.

Upon the approval of the Minister of Finance pursuant to Article 25 of the Bank of Japan Law of 1942, the Bank extended subordinated loans to Midori Bank on January 29, 1996. The Bank extended the loans to Midori Bank, which was established to assume the business of the failed Hyogo Bank, to strengthen its capital base. When Midori Bank and Hanshin Bank merged on April

[1] Principle 1: There must be a strong likelihood that systemic risk may materialize.
Principle 2: There must be no alternative to the provision of central bank money.
Principle 3: All responsible parties are required to take clear responsibility to avoid moral hazard.
Principle 4: The financial soundness of the Bank of Japan itself must not be impaired.

1, 1999, the newly established Minato Bank assumed this debt. Minato Bank partly repaid the loans before maturity on March 31, 2000 and December 30, 2003.

2. Special loans extended to Yamaichi Securities

The Bank ended the extension of special loans to Yamaichi Securities after the Tokyo District Court made a decision to end the bankruptcy procedures for Yamaichi Securities on January 26, 2005.

Upon the approval of the Minister of Finance prescribed in Article 25 of the Bank of Japan Law of 1942, the Bank provided special loans to Yamaichi Securities when Yamaichi Securities announced its intention to close down its business and dissolve itself on November 24, 1997. The Bank provided necessary liquidity to help Yamaichi Securities return customer assets, orderly settle outstanding transactions, and withdraw from overseas activities.[2] The Bank collected loans extended to Yamaichi Securities after Yamaichi Securities was declared bankrupt on June 2, 1999, by mainly exercising its rights appropriately in the bankruptcy procedures.

In fiscal 2004, the Bank received repayment of 1.882 billion yen from Mizuho Corporate Bank (MCB), which was the amount MCB had received from the Japan Investor Protection Fund for transferring its claim on Yamaichi Securities. The Bank also received other payments including the dividends from bankruptcy proceedings. As a result, the total amount of loans to Yamaichi Securities collected by the Bank in fiscal 2004 reached 8 billion yen.

The Bank has collected a total of 226.5 billion yen, equivalent to 67.1 percent of the amount of loans extended to Yamaichi Securities, since Yamaichi Securities was declared bankrupt.

With the completion of bankruptcy procedures for Yamaichi Securities, the amount of special loans still outstanding (111.1 billion yen) became uncollectible, and this was written off by withdrawing the Bank's provisions for possible loan losses.

Upon the approval of the Minister of Finance as prescribed by Article 53, Paragraph 2 of the Bank of Japan Law, the Bank transferred net income of 5.5 billion yen[3] to its legal reserve in fiscal 2004 to

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[2] For details, see "Loan extension to Fuji Bank for provision of funds to Yamaichi Securities," announced on November 24, 1997 and available at www.boj.or.jp/en/about/_f.htm (a Japanese version is available at www.boj.or.jp/seisaku/97/giji97016.htm).

[3] The amount was calculated by multiplying uncollectible special loans to Yamaichi Securities of 111.1 billion yen by the required rate of 5 percent, as prescribed by Article 53, Paragraph 1 of the

prevent impairment of its financial soundness due to the loss of 111.1 billion yen arising from the special loans to Yamaichi Securities.

As the government determined the necessity of temporarily nationalizing Ashikaga Bank pursuant to Article 102, Paragraph 1, Item 3 of the Deposit Insurance Law on November 29, 2003, the Bank decided to provide necessary liquidity to Ashikaga Bank.[4]

Ashikaga Bank, however, has been able to raise necessary funds without loans from the Bank. As a result, the Bank has never extended special loans to Ashikaga Bank to date.

C. Winding Up of the Stock Purchasing Program

In the period starting from November 2002 through the end of September 2004, the Bank purchased stocks held by banks to encourage them to further reduce their exposure to the risk of stock price fluctuations, upon government approval pursuant to the proviso of Article 43, Item 1 of the Bank of Japan Law. The gross amount of stocks purchased by the Bank totaled 2.18 trillion yen (see charts 2 and 3, and Appendix 1).

In 2002, market risk associated with banks' stockholdings was considered as a destabilizing factor for bank management.[5] Thus, reducing such risk was seen as an urgent task to ensure financial system stability as well as lay the foundation for banks to deal with the NPL problem. In this context, the Bank established the stock purchasing program as a temporary measure.

The stock purchasing program has achieved its principal purpose. Banks managed to reduce their excessive stockholdings through this program and made progress in the disposal of NPLs.

For fiscal 2004, the Bank earned a profit of 38.5 billion yen from the purchased stocks. Of this

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Bank of Japan Law. This represented the amount that should have been transferred from net income to the legal reserve if these loans had been collected.

[4] For details, see "Special measures concerning loan extension to Ashikaga Bank in order to maintain an orderly financial system," announced on November 29, 2003, at www.boj.or.jp/seisaku/03/giji03122.htm, available only in Japanese.

[5] For the Bank's view on bank stockholdings and the NPL problem at that time, see "New Initiative Toward Financial System Stability," announced on September 18, 2002 and available at www.boj.or.jp/en/set/05/set_f.htm (a Japanese version is available at www.boj.or.jp/set/02/fss0209a.htm), and "Japan's Nonperforming Loan Problem," announced on October 11, 2002 and available at www.boj.or.jp/en/set/05/set_f.htm (a Japanese version is available at www.boj.or.jp/set/02/fss0210c.htm).

total, 31.7 trillion yen came from stock dividends, and 7.1 trillion yen came from sale of stocks at the request of issuers. As of the end of March 2005, the Bank's unrealized gains totaled 637.6 billion yen.

Chart 2: Total Amount of Stocks Purchased by the Bank of Japan through the Program

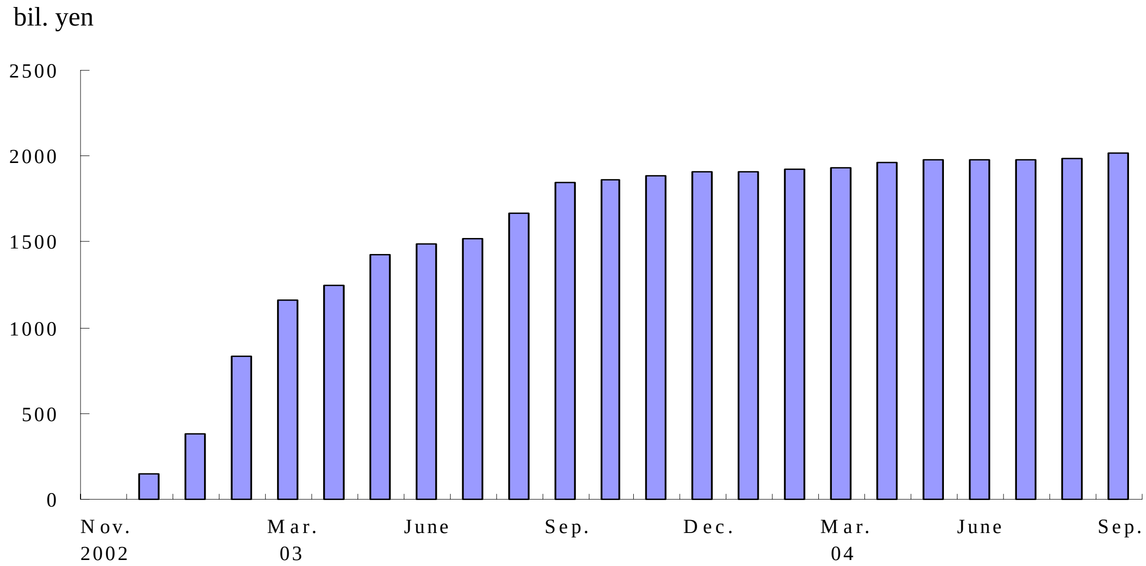
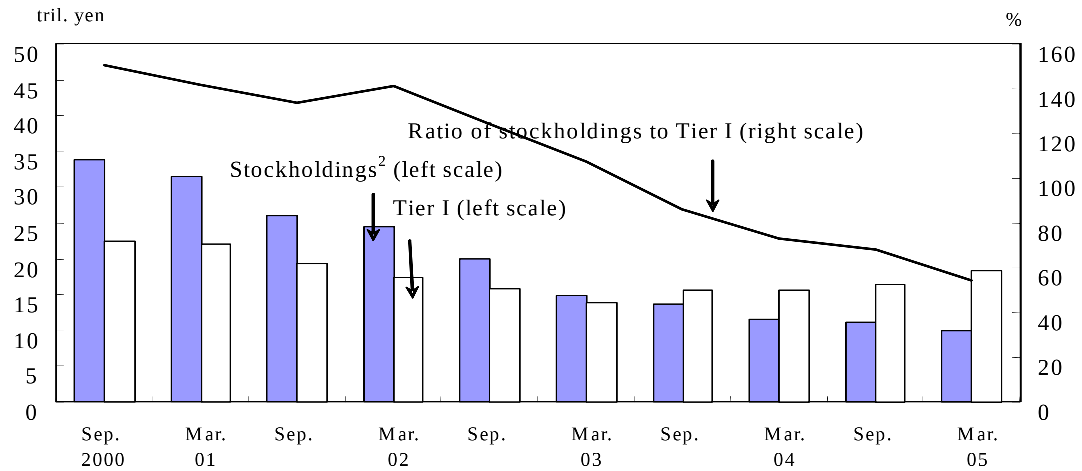


Chart 3: Major Banks' Stockholdings and Their Ratio to Tier I Capital[1]



Notes: 1. Excluding Shinsei Bank and Aozora Bank

2. Stocks for which market prices are available, excluding those held for investment and those of subsidiaries and affiliates. On a consolidated basis, excluding unrealized gains.

Appendix 1: Outline of the Stock Purchasing Program[6]

Size	Up to 3 trillion yen. Initially 2 trillion yen, but the amount was increased by 1 trillion yen on March 25, 2003.
Eligible institutions	Banks whose stockholdings exceed their Tier I capital.
Eligible stocks	Listed stocks with a rating of BBB- and above; and (1) such stocks need to be traded on a stock exchange for 200 days or more per year, and (2) such stocks need to have an annual turnover of 20 billion yen or more on a stock exchange.
Method	A trust is established and stocks are purchased as trust property.
Price	At the market price (the lesser of [1] the volume-weighted average price or [2] the day's closing price).
Limit per bank	The maximum amount of stocks purchased from a bank not exceeding the lesser of (1) the amount exceeding the bank's Tier I capital, or (2) 750 billion yen (increased from 500 billion yen on March 25, 2003).
Limit per issuer	The maximum amount/number of shares per issuer not exceeding the lesser of (1) 5 percent of all voting rights, or (2) amounts set forth based on rating and annual turnover.
Stock disposal policy	The Bank of Japan will not, in principle, sell purchased stocks until the end of September 2007 (however, the Bank may respond to the issuer's request to sell shares at market price on the condition that the Bank does not suffer a loss). The Bank will complete disposal of stocks by the end of September 2017 (while considering the impact of its action on the stock market and the Bank's risk of suffering losses).
Exercise of voting rights	The Bank of Japan will present basic principles regarding the exercise of voting rights to the trust bank ("the trustee"), and the trustee will exercise such rights taking due account of fiduciary responsibility.

II. The Bank of Japan's Current Account Services and Lending Facilities

A. Basic Policy regarding Provision of Current Account Services

In pursuing its objective of "ensuring smooth settlement of funds among banks and other financial institutions, thereby contributing to the maintenance of an orderly financial system" as prescribed in Article 1, Paragraph 2 of the Bank of Japan Law, the Bank provides current account services to financial institutions which satisfy certain criteria set by the Bank, for example, such financial institutions must play a major role in payments.

The Bank selects current account holders from financial institutions applying for the current account

[6] For details, see "Stock Purchase Guidelines," announced on October 11, 2002 and available at www.boj.or.jp/en/set/05/set_f.htm (a Japanese version is available at www.boj.or.jp/set/02/fss0210a.htm#betsu).

services (Appendix 2). In selecting current account holders, the Bank bases its decision on whether providing the services to the applicant financial institution will contribute to achieving the above objective of the Bank.

In addition, the Bank, if necessary, provides liquidity as the "lender of last resort" when a financial institution faces a problem which could result in a chain of settlement failures at other institutions or loss of public confidence, thus disrupting the overall functioning of the financial system. The Bank, as the "lender of last resort," extends certain types of loans including loans pursuant to Article 37 (temporary loans) and Article 38 (special loans) of the Bank of Japan Law.

The Bank extends credit in three forms: (1) loans on bills; (2) electronic loans, online loans provided through the Bank of Japan Financial Network System (BOJ-NET), other than overdrafts; and (3) overdrafts.[7] The Bank selects financial institutions with which it enters into lending contracts from current account holders applying for the service by each of the three forms of credit.

Appendix 2: Criteria for Parties Eligible to Hold Current Accounts with the Bank of Japan and That Have Access to the Bank's Lending

The Bank has set out specific eligibility criteria for selecting current account holders in "Criteria for Parties Eligible to Hold Current Accounts with the Bank and That Have Access to the Bank's Lending,"[8] which is publicly available.

The criteria specify the following categories of institutions as eligible current account holders: (1) institutions playing a major role in payments, e.g., banks, *shinkin* banks, central organizations of credit, agricultural and fishery cooperatives, and bankers' associations; (2) institutions playing a major role in securities settlement, e.g., securities companies, securities finance companies, and stock exchanges; and (3) institutions playing an intermediary role in interbank money markets, e.g., money market brokers.

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[7] Other than the above, the Bank has extended subordinated loans by accepting deeds upon approval of the Minister of Finance pursuant to Article 25 of the Bank of Japan Law of 1942. At present, however, the Bank does not extend loans on deeds. Also see Section I. B regarding the Bank's extension of subordinated loans.

[8] The complete version of the eligibility criteria is available at www.boj.or.jp/about/basic/touyo/touyo1.htm, available only in Japanese.

The Bank grants applications for the current account services submitted by the above-described parties, if they satisfy certain conditions such as the following: (1) they conduct their business properly; (2) they are in sound financial condition; and (3) they have appropriate operational capability. The Bank may grant applications submitted by those parties not included in the categories listed in the criteria in cases where the Bank considers that providing current account services to such parties will contribute to the achievement of the purpose of the Bank.

The Bank has also set out specific eligibility criteria for parties having access to the Bank's lending, together with the criteria for current account holders, in "Criteria for Parties Eligible to Hold Current Accounts with the Bank and That Have Access to the Bank's Lending," which is publicly available.

According to the criteria, parties seeking to apply for the Bank's lending need to satisfy the following conditions: (1) the applicants are the financial institutions as prescribed in Article 37 of the Bank of Japan Law; (2) the applicants hold a current account with the Bank; and (3) the applicants have no special causes that the Bank would consider inappropriate to grant the application (except for eligible parties for electronic loans: they are selected from current account holders that have access to the Bank's lending facilities).

B. New Current Account Holders

From April 2004 to July 2005, the Bank started to provide current account services to three institutions. As of the end of July 2005, the total number of current account holders was 596.

Chart 5: Number of Institutions Which Hold Current Accounts with the Bank

fiscal year-end

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005 (end-July)
City banks and long-term credit banks	12	12	12	10	9	9	8	8
Regional banks	64	64	64	64	64	64	64	64
Regional banks II	61	60	57	56	53	50	48	48
Foreign banks (branches in Japan)	90	84	79	73	72	71	68	68
Trust banks	33	32	30	28	27	27	26	26
Shinkin banks	353	348	338	321	300	285	280	279
Central institutions for cooperative financial institutions	5	5	5	5	5	5	5	5
Securities companies	57	52	48	46	44	42	42	42
Securities finance companies	3	3	3	3	3	3	3	3
Money market brokers (*tanshi*)	6	6	6	3	3	3	3	3
Bankers associations	1	1	33	33	33	33	33	33
Stock exchanges	2	2	2	2	1	1	1	1
Securities clearing corporations other than stock exchanges	-	-	-	-	1	1	2	3
Financial futures exchanges	-	-	1	1	1	1	1	1
Others	9	7	9	10	11	12	12	12
Total	696	676	687	655	627	607	596	596

Of these three new current account holders described above, two were non-banking institutions not listed in "Criteria for Parties Eligible to Hold Current Accounts with the Bank and That Have Access to the Bank's Lending." These are the JASDEC DVP Clearing Corporation, approved by the Policy Board on April 20, 2004, and the Japan Government Bond Clearing Corporation, approved by the Policy Board on April 19, 2005.

Although these institutions were not the types of institutions listed in "Criteria for Parties Eligible to Hold Current Accounts with the Bank and That Have Access to the Bank's Lending," they were approved by the Bank based on the following reasons:

(1) These institutions are either (a) a securities clearing corporation (JASDEC DVP Clearing Corporation) established to improve the safety of the securities clearing system, or (b) a securities clearing corporation (Japan Government Bond Clearing Corporation) established to further improve the safety and efficiency of the securities clearing system for Japanese Government Bonds (JGBs) and to enhance liquidity of the JGB market. Providing the Bank's current account services to these institutions for settlement of funds will contribute to ensuring smooth settlement of funds for transactions between financial institutions.

(2) These institutions (a) conduct their business properly, (b) maintain sound financial condition, and (c) have appropriate operational capability.

C. Review of the Bank's Current Account Services

In "The Bank of Japan's Measures regarding the Financial System after the Full Removal of Blanket Guarantee of Deposits" (hereafter, "Measures regarding the Financial System,") released on March 18, 2005,[9] the Bank announced its intention to review the policy relating to selection of current account holders to promote greater transparency and support new entry of financial institutions. On May 31, the Bank released a public statement regarding the review of the Bank's current account services. Its outline is as follows.

1. Disclosure regarding current account contracts and the list of current account holders[10]

The Bank has decided to disclose the rules for current account services, which provide the basic contractual rights and obligations between the Bank and current account holders, from July 5, 2005. Before this decision, the Bank had limited disclosure of these rules to a current account holder.

In addition, the Bank has decided to publicly disclose the list of current account holders from August 1, 2005. Before this decision, the Bank had limited disclosure of the list to current account holders.

2. Disclosure regarding selection process for account holders

The Bank has decided to disclose the application procedures for opening a current account with the Bank, including sample forms and the standard processing period, from July 6, 2005.

As part of the selection process, the Bank requires parties applying for current account services to submit documentation necessary to evaluate their operational and financial soundness, and operational reliability.

Before this decision, the Bank had notified the application procedures only to applicants.

Prior to the implementation of the above disclosure measures, the Bank announced its intention to invite comments from account holders and, if necessary, reflect these comments in the review process.

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[9] The English version of "The Bank of Japan's Measures regarding the Financial System after the Full Removal of Blanket Guarantee of Deposits," is available at www.boj.or.jp/en/set/05/set_f.htm (a Japanese version is available at www.boj.or.jp/set/05/data/fss0503a.pdf).

[10] For details, see "Current status of discussion on disclosure of current account contracts and the list of current account holders," announced on May 31, 2005, at www.boj.or.jp/about/05/un0505g.htm, available only in Japanese.

The Bank will continue to review its current account services for further improvement, while paying due attention to practices of financial transactions and exchanging views with the account holders.

D. General Principles concerning the Lender of Last Resort Function

In "Measures regarding the Financial System," the Bank has announced its intention to continue to perform the lender of last resort function appropriately, based on the following general principles.

General Principles concerning the Lender of Last Resort Function

1. Extension of loans against collateral pursuant to Article 33 of the Bank of Japan Law

The Bank extends loans against collateral pursuant to Article 33 of the Bank of Japan Law under a Lombard-type lending facility, called the complementary lending facility, with a view to facilitating monetary operations and thus ensuring the smooth functioning and stability of financial markets. In addition, the Bank will continue, where appropriate, to extend loans against collateral in a timely and flexible manner to meet the specific needs arising from business operations of individual financial institutions, giving due consideration to financial market developments.

2. Extension of temporary loans pursuant to Article 37 of the Bank of Japan Law

On the condition that financial institutions are solvent, the Bank will continue to provide them with uncollateralized loans pursuant to Article 37 of the Bank of Japan Law in a timely manner, when contingencies, such as computer system problems, cause solvent financial institutions to experience an unexpected temporary shortage of funds for payment purposes and when loans are necessary to secure the smooth settlement of funds among financial institutions.

3. Extension of special loans to maintain financial system stability pursuant to Article

38 of the Bank of Japan Law)

The Bank will, in cooperation with the government, take measures regarding the extension of special loans pursuant to Article 38 of the Bank of Japan Law in a timely and appropriate manner, while observing the Bank's four guiding principles for the extension of such loans.

Extension of loans (special loans) and other businesses to maintain an orderly financial system pursuant to Article 38 of the Bank of Japan Law is one of the financial safety nets to prevent financial crisis. When conducting the business, the Bank needs to take other frameworks of financial safety nets including the deposit insurance system into consideration. In this regard, the Deposit Insurance Corporation (DIC), under the current framework of the deposit insurance system, provides necessary funds to failed financial institutions prescribed in the Deposit Insurance Law in case they need to repay deposits.[11] Thus, the Bank only rarely extends special loans to failed financial institutions except in cases where the measure to prevent financial crisis, more specifically, the full protection of deposits pursuant to Article 102 of the Deposit Insurance Law, is in place.

E. Review of the Bank's Lending Facilities

In "Measures regarding the Financial System," the Bank has announced its intention to consider introducing a notice period before terminating contracts for the complementary lending facility. By introducing this measure, the Bank aims to encourage and assess financial institutions' efforts to restore their capital adequacy ratios when the ratios fall below the required standard.

III. On-Site Examinations and Off-Site Monitoring of Financial Institutions

A. Number of Financial Institutions Examined

In fiscal 2004, the Bank conducted on-site examinations at a total of 153 financial institutions: 46

[11] As prescribed in the Deposit Insurance Law, the Bank may extend loans to the Deposit Insurance Corporation (DIC), when the DIC faces a temporary shortage of funds necessary to conduct its business.

In April 2001, the DIC fully repaid all loans made by the Bank by refinancing them with loans from private institutions. Since then, the DIC has not borrowed funds from the Bank, as the DIC has managed to raise funds necessary to conduct business from the private institutions.

domestically licensed Japanese banks, 67 *shinkin* banks, and 40 other institutions including securities companies and Japanese branches of foreign banks.

B. On-Site Examination Policy for Fiscal 2005

As detailed in "Measures regarding the Financial System," the Bank will encourage financial institutions' efforts to improve their management of risks and business activities and develop innovative services tailored to customer needs. In accordance with this basic stance, the Bank will contribute to enhancing the functioning and robustness of the overall financial system.

Based on "On-Site Examination Policy for Fiscal 2005," approved by the Policy Board on April 1, 2005, the Bank will conduct its on-site examinations in fiscal 2005 in accordance with the above principles. Five points provide the core elements as shown below.

1. Assessing the economic value and associated risk of financial institutions' assets and financial transactions

It is important for financial institutions to properly assess the economic value and volatility, i.e., risk of the whole range of their assets, not just their loan portfolios, as well as their financial transactions.

To assess appropriately the economic value of loan assets, the Bank will apply an approach based on the discounted cash flow (DCF) method to a wider range of loan assets and share the assessment results with the financial institutions concerned.

The Bank intends to assess the economic value of assets for which market value is not available and other newly developed financial products, utilizing pricing models, i.e., the mark-to-model method.

2. Enhancing integrated risk management

The Bank will encourage financial institutions to introduce and utilize frameworks for integrated risk management, taking their specific financial and business conditions into full consideration.

The Bank will encourage financial institutions to further improve information disclosure regarding their risk management.

3. Promoting active credit portfolio management

The Bank will encourage financial institutions' efforts toward active credit portfolio management.

4. Ensuring smooth settlement

With a view to preventing the materialization of systemic risk, the Bank will identify risks inherent in the overall payment and settlement system.

The Bank will also carefully examine financial institutions' liquidity management after the full removal of the blanket guarantee of deposits.

5. Enhancing security measures attending financial transactions

The Bank will check whether financial institutions have established sufficient risk management systems such as compliance guidelines (guidelines on business operations in compliance with relevant laws and regulations), security measures for computer systems, internal inspections, and audits. The Bank will request them to improve their systems where necessary.

The Bank will support financial institutions' efforts to improve the functioning of their internal control governing the management of risks and business activities.

In conducting its on-site examinations in fiscal 2005, the Bank will continue to give due consideration to easing the burden of on-site examinations on financial institutions. The Bank will shift the focus of its on-site examinations from assessing financial institutions' evaluation of individual assets to examining their frameworks for risk management. This will result in reducing the number of loans extracted from financial institutions' overall loan portfolios so as to check the accuracy of their self-assessment in on-site examinations. In addition, the Bank will take a more flexible stance on the scope, size of examination teams, and duration of each on-site examination, depending on the financial and business conditions of each financial institution.

C. Enhanced Disclosure of the Bank's On-Site Examinations

The Bank has decided to make public on an annual basis the names of the financial institutions examined on site and the timing of the examinations conducted in the previous fiscal year in its *Annual Review* (first published in *Annual Review* for fiscal 2004). By means of this release, the Bank demonstrates that, as the central bank, it is keeping track of financial institutions' business management, with a view to securing public confidence in the financial system and to enhancing the transparency of its on-site examinations. The release covers the following.

(1) The Bank's on-site examinations:

The Bank's examinations of financial institutions' business operations and state of property of financial institutions that hold current accounts at the Bank (BOJ current account holders) based on contracts concluded with them, as prescribed by Article 44, Paragraph 1 of the Bank of Japan Law.

(2) Items disclosed:
(a) name of each financial institution examined;
(b) the day on which consent was received for on-site examination;*
(c) the first day of on-site examination;
(d) the last day of on-site examination;
(e) any periods of adjournment that took place between the first and last days of on-site examinations;
(f) the day the Bank gives feedback on its findings from the on-site examination to the financial institution concerned; and
(g) the type of on-site examination conducted, i.e., whether an ordinary or an area-specific on-site examination.

*The day the Bank receives formal consent from a financial institution in response to its prior notification regarding a pending on-site examination.

(3) In exceptional cases, the Bank may judge it appropriate not to disclose the above items for a particular on-site examination, in order to avoid possible negative repercussions for the financial system.

IV. Other Issues

A. Integration of the Financial Systems Department and the Bank Examination and Surveillance Department

With the release of "The Bank of Japan's Action Plans for Fiscal 2005" on March 18, 2005, the Bank announced the establishment of a new department, the Financial Systems and Bank Examination Department, by integrating the Financial Systems Department and the Bank Examination and Surveillance Department.

The Financial Systems and Bank Examination Department assumes responsibility for the maintenance of financial system stability, which had been separately assumed by the Financial Systems Department and the Bank Examination and Surveillance Department, and promotes the

Bank’s efforts to improve the functioning of the financial system.

As planned, the Financial Systems Department and the Bank Examination and Surveillance Department were integrated and the Financial Systems and Bank Examination Department was established on July 8, 2005.

B. Establishment of the Center for Advanced Financial Technology

The Bank established the Center for Advanced Financial Technology in its new Financial Systems and Bank Examination Department. The center is in charge of (1) planning and coordinating measures to encourage financial institutions to adopt advanced financial technology and, at the same time, ensuring the safety of financial transactions; (2) studying relevant developments in finance, including information security; and (3) developing more sophisticated techniques for on-site examinations and off-site monitoring.

In addition, the center will host open seminars on a regular basis, mainly targeting the management and officers of financial institutions to share with financial institutions its understanding of the issues that need to be addressed in enhancing the availability of more efficient and advanced financial services.