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Evolution of the US Retail Securities Market (Volume 2)

— Regulatory Reforms for Banking and Securities Markets —

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In the United States, the Financial Services Modernization Act of 1999 removed a boundary between banking and securities services that had existed since 1933. Under the interim rules announced by the Securities and Exchange Commission (SEC), banks are exempt from broker-dealer registration requirements with certain conditions, and banks' securities services are to be provided by affiliated securities firms, etc.

In 1999, Merrill Lynch, the largest securities firm, announced a fee-based account service in which fees are charged at a prescribed rate based on the balance of assets in the account instead of brokerage commissions. The start of such fee-based account services gave rise to the question of whether Merrill Lynch's registered representatives are required to register as investment advisors under the Investment Advisors Act of 1940. However, in the same year, the SEC permitted the provision of such services under certain conditions.

In December 2002, settlement was reached between the nation's top securities firms against which allegations were made regarding undue influence of investment banking departments on research departments that deceived investors and regulators such as the SEC. For the five years following July 2004, these securities firms were required to distribute research reports made by independent research firms to investors.

In Japan, the methods to provide financial services are significantly changing through the participation of banks in the securities brokerage business and the emergence of the agency business for banks, which is planned for April 2006. It is of urgent necessity for financial institutions to develop products that go beyond simple banking, securities or insurance products and that fully meet the needs of aging savers, and to re-establish a service structure to support such new products.

III Emergence of New Registered Representatives

1 Registered Representatives in the United States

In the United States, individuals who want to enter the securities industry to sell any type of securities products must pass the Series 7 examination. This represents one of the examinations under the qualification examination system managed and administered by the National Association of Securities Dealers (NASD). NASD was established in 1938 as a self-regulatory organization pursuant to federal law.

In addition to the Series 7 examination, as shown in Table 1, many other examinations are provided such as those for securities sales supervisors at securities firms (Series 4, Series 9, etc.), for securities principals (Series 24, Series 27, etc.) and for assistant representatives (Series 11) to test an individual's knowledge of trading, exchange rules and regulations applicable to the securities business.

An individual who passes the Series 7 examination is eligible to register with the Central Registration Depository (CRD) system managed and operated by NASD. A person can work as a registered representative only after recording the fingerprints of all ten fingers, a photograph of his or her face, any penalties imposed in the past, a history of conflicts with clients, securities firms, etc. in this system. A registered representative and the securities firm for which the representative works are required to immediately report any change in the recorded information.

Information on securities business records about registered representatives and securities firms that are stored in the CRD system is published on NASD's website by the NASD broker check system. Individual investors can view such information directly. NASD also provides information to investors via e-mail, etc.

Under the NASD Continuing Education Requirements Rule 1120, established in 1995, the registered representatives are required to complete a three-hour training program implemented by NASD on the second anniversary of their initial securities registration and every three years thereafter. (This program primarily consists of amendments to regulations, etc.) Up through March 2005, a registered representative who has ten years or more of experience in the securities business and has no history of penalties as of July 1, 1998, was exempted from such educational requirements. However, since April 2005, these experienced representatives are also required to take the training courses.

Similar to the CRD system, investment advisors registered with individual state authorities and the US Securities and Exchange Commission (SEC) pursuant to the Investment Advisors Act of 1940 are also required to enter their past business history, etc. in the IARD (Investment Advisor Registration Depository) system, which is operated and managed by the SEC. The SEC also publishes a database on its website.

2 Two Requirements of Registered Representatives

Two requirements are imposed on registered representatives from the day on which they are registered with NASD.

Table 1. Major Securities Qualification Examinations Administered by NASD

Examination category	Number of multiple-choice questions	Test time	Test content
(Sales Supervisors)			
Series 4: Registered Options Principal	125	3 hours	Compliance responsibilities related to options transactions
Series 9: General Securities Sales Supervisor-Options Module	200	90 minutes	Compliance responsibilities required for branch office managers and other sales supervisors
Series 10: General Securities Sales Supervisor-General Module	200	4 hours	Compliance responsibilities (SEC regulations) required for branch office managers and other sales supervisors
(Operations Principals)			
Series 24: General Securities Principal	150	3 1/2 hours	Compliance responsibilities related to investment banking business, direct investment programs, etc.
Series 27: Financial and Operations Principal	145	3 1/2 hours	Compliance responsibilities required for financial managers of securities firms
Series 28: Introducing Broker/Dealer Financial and Operations Principal	85	2 hours	Management responsibilities for record-keeping requirements involving clients of securities firms
(Others)			
Series 6: Investment Company and Variable Contracts Products Representative	100	135 minutes	Qualification examination to become investment trust and variable insurance products representatives
Series 7: General Securities Representative	250	6 hours	Qualification examination to become general securities representatives
Series 11: Assistant Representative-Order Processing	50	1 hour	Compliance responsibilities required of assistants of registered representatives
Series 14: Compliance Officer	100	3 hours	Qualification examination to become compliance officers of daily securities business activities
Series 16: Supervisory Analyst	100	3 hours	Compliance responsibilities related to the content of reports prepared by securities analysts

Notes: SEC = US Securities and Exchange Commission, NASD= the National Association of Securities Dealers.

The first requirement relates to "continuing education," as stated above, and reporting requirements to the securities firm for which the representative works. A registered representative must provide all personal information related to securities activities such as history as a registered representative, past conflicts, penalties, fines, and other punishments from an industry association, etc. to the employing securities firm. On behalf of the registered representative, the securities firm must report this personal information to NASD. If a registered representative moves to another securities firm, the representative is required to report the reason for such transfer to both the old and new firms and NASD.

The second requirement is related to clients. This requirement is divided into four responsibilities.

First, each client's age, financial status, investment objectives, etc. must be identified, recorded and assessed to determine if the securities investments are suitable for that particular client (Suitability Rules). If any change occurs in the information during the period of transactions with each client, the information must be updated and maintained. All client data must be stored in written document format.

Second, each registered representative is required to provide education and guidance to his or her clients concerning the trading of securities. Because securities trades are often conducted orally such as by telephone, this practice tends to invite problems with a client. Accordingly, the responsibility of explaining and confirming with a client the meanings of pertinent technical terms used for a trade prior to the trades is imposed on each registered representative. Confirming the rules of ordering and trading with the client also facilitates smooth settlement procedures.

Third, each registered representative must obtain the understanding of a client concerning brokerage fees. Generally, a securities firm employing the registered representative designates the brokerage fees. However, in some exceptional cases, fees are determined for each trade. In such cases, the registered representative is required to abide by NASD's "five-percent rules" (the maximum fee is 5% of the principal amount of a trade), and to make the utmost effort not to impose excessive burdens on a client.

Last, each registered representative is required to record and update his or her own personal information in the CRD system. This requirement is to ensure that data in the CRD system concerning registered representatives are always current.

3 Financial Services Modernization Act and Full-Scale Participation of Banks

The "Financial Services Modernization Act of 1999" (the 1999 Act) permitted financial conglomerates to comprehensively handle banking, securities and insurance business activities while leaving past finance-related laws in effect. However, under the Banking Act of 1933 (the Glass-Steagall Act: the 1933 Act), banks were not generally permitted to engage in the securities business.

After 1987, in accordance with a change in the interpretation of Section 20 of the 1933 Act by the FRB (Federal Reserve Board), banks were permitted to engage in limited securities activities by bank-affiliated securities firms although within "revenue test" limitations. The revenue test limits the revenues of a subsidiary to five percent of the annual gross revenues of a bank. In 1997, the limit under the "revenue test with respect to the establishment of a securities subsidiary" of Section 20 of the 1933 Act was raised from five percent to 25 percent. This increase has facilitated the establishment of securities subsidiaries and the acquisition of securities firms by banks.

Nevertheless, complete separation was imposed on the relationship between a securities subsidiary and a bank by the Section 20 "approval conditions for the establishment of securities subsidiaries" announced by the FRB in 1989. Under these conditions, it has become possible to totally subject securities subsidiaries to the supervision of the SEC.[1]

However, the 1999 Act necessitated new arguments concerning the supervisory responsibility of the regulatory authorities for banks, securities firms and insurance companies, which had been separated in the past. Because banks that were not permitted to register as securities firms (broker-dealers) under the Securities Exchange Act of 1934 (the 1934 Act) could engage in the securities business on a full-scale basis, it has become necessary for the SEC to study the supervision and regulations relating to bank securities businesses.

As its first step, the SEC temporarily established what it called Regulation B. This proposed regulation permits a bank's broker (securities intermediary trades) activities without registering with the SEC as a securities firm only for the following 11 exceptions:

(1) Entering into contractual arrangements with a securities firm under which the securities firm offers brokerage services to bank customers (networking)
(2) Trust and fiduciary activities concerning securities investments
(3) Permissible securities transactions such as commercial paper, bankers' acceptances, etc.
(4) Transactions of certain stock purchase plans
(5) No-fee securities transactions such as MMMF (Money Market Mutual Funds) by bank account transfer (sweep accounts)
(6) Transactions for affiliates, other than securities firms
(7) Transactions of privately placed securities
(8) Safekeeping and custody activities
(9) Buying and selling certain "identified banking products"[2] as defined in the 1999 Act

(10) Transactions of municipal securities
(11) Up to 500 transactions in any calendar year for securities other than those referred to in the exceptions above

With respect to a bank's dealer (securities transactions of their own accounts) activities, registration with the SEC as a securities firm is not required if the following two conditions are met:

(1) When a bank is not conducting securities transactions of their own accounts as daily business activities for profit-making purposes
(2) When a bank is conducting securities transactions of their own accounts for the following purposes as defined in the 1999 Act:
  a. Securities transactions for investments for banking and fiduciary activities
  b. Permissible securities transactions such as commercial paper, bankers' acceptances, etc.
  c. Buying and selling certain "identified banking products" as defined in the 1999 Act
  d. From among asset-backed securities (ABS), buying and selling securities using assets formed by a bank-affiliated company that is neither a bank nor a securities firm

Under the SEC's proposed Regulation B, as explained above, many major banks are exempt from broker-dealer registration requirements and are striving to expand their retail securities services by making use of bank-affiliated securities firms and by increasing the number of joint bank and securities branches.

4 Networking Regulations on Banks

As stated above, banks' retail securities services are being provided at joint branches with securities subsidiaries at major banks. However, middle-sized banks that do not have securities subsidiaries are providing securities services based on a networking arrangement, which is defined as one of the exceptions under Regulation B, explained above in Item 3. This is a partnership arrangement with a registered securities firm. Specifically, bank employees who are not registered as securities representatives with NASD conduct securities business by referring bank customers to the securities firm inside the bank branch. The responsibility for supervising such bank employees must be assumed by the partner securities firm.

In these cases, compensation (incentive compensation) for referring a customer by a bank employee constitutes the key factor. Under Regulation B, the SEC stipulated that this incentive compensation must be "a nominal one-time cash fee of a fixed dollar amount." In its definition of "a nominal one-time cash fee of a fixed dollar amount," the SEC provisionally provided that a referral payment must not exceed the greater of three alternative values: (1) the employee's base hourly rate of pay, (2) a dollar amount equal to 15 dollars in 1999 plus an adjustment for inflation, or (3) 25 dollars. These definitions also specify that the fee must be the same for any securities referral and does not vary based on factors such as the customer's financial status. The fee must be paid even if the customer does not express an interest in a particular type of securities product. Accordingly, in actual terms, it appears that the provision of securities services by banks in the form of the networking arrangement is not common.

IV Arguments over Fee-Based Securities Accounts

1 The Merrill Lynch Exemption

In 1999, the leading US securities firm, Merrill Lynch, inaugurated two new securities services.

One of the new services is fee-based securities accounts, as noted in Volume 1. Before the introduction of this service, a fixed amount or a fixed-rate fee was charged for each securities product traded. However, under fee-based accounts, a fixed rate (about 1%) of the average balance of assets in accounts for each quarter or half year is paid to the securities firm as the fee, regardless of the frequency of trades or the value of each trade.

The other new service relates to the start of online trade accounts requiring lower brokerage fees than those for ordinary securities accounts for which investment advice is provided by registered representatives. This type of securities trading service is already popular in Japan. The start of this service coincided with the period when the stock market was brisk as spurred on by a boom of initial public offerings involving IT (information technology) companies. At that time, the demands of clients were increasing to trade stocks of such companies, which were somewhat speculative but that offered a degree of fascination by not being subject to the stringent Suitability Rules required by registered representatives. It is assumed that online trade account services were started in response to these client demands.

In the United States, the 1934 Act and the Investment Advisors Act of 1940 (the 1940 Act) explicitly stipulate the fees paid to securities firms and investment advisory firms for securities trades. Specifically, the brokerage commission to be paid to a registered representative of a securities firm is defined under the 1934 Act as compensation for effecting securities trades, providing investment advice and for safekeeping and transferring securities. The act also stipulates that such commission shall be paid for each securities trade.

The business of investment advisory firms and independent investment advisors is defined under the 1940 Act as providing investment advice through securities investment discretionary accounts. Compensation for such services is specified as a fixed amount based on the balance of funds under management, etc. The act prohibits investment advisors from receiving a commission for each trade whereas registered representatives are permitted to receive such commissions.

Accordingly, a question arose at the start of a securities account service by Merrill Lynch for which the fee is based on the balance of funds in the account as to whether the registered representatives must be registered as investment advisors as stipulated in the 1940 Act.

Moreover, the brokerage commissions for an online trade account provided by Merrill Lynch are lower than those for ordinary accounts. This was considered that a two-tier commission structure had been established for identical brokerage services. In addition, the difference between these commissions was considered "special compensation" to an investment advisor as specified in the 1940 Act. These factors also led to the question of whether investment advisor registration is required of registered representatives.

In November 1999, in the midst of growing arguments among securities firms and investment advisory firms, the SEC announced a proposed regulation (the 1999 Proposal) for the two services started by Merrill Lynch. The 1999 Proposal exempted Merrill Lynch from the investment advisor registration requirement and permitted the provision of securities accounts for which the fee is based on the balance of funds in the account under the following conditions.

The following three conditions are specified in permitting the provision of securities accounts for which the fee is based on the balance of funds in the account:

(1) No securities investment advice on a discretionary basis is provided
(2) Any investment advice provided is solely incidental to brokerage services
(3) A securities firm must disclose that these accounts are securities transaction accounts to clients

With respect to online trade accounts, this proposal permitted full-service securities firms to provide discount trade account services including online trade accounts to their clients on the grounds that brokerage commissions have not been identical for all clients in the past as such commissions vary depending on, for example, the value of the trade.

The 1999 Proposal of the SEC is called "The Merrill Lynch Exemption" in the US Securities industry because it was triggered by the two new services offered by Merrill Lynch.

2 1999 Proposal and the SEC

Behind the SEC's 1999 Proposal that attracted the attention of related industries there were two problems regarding brokerage commissions. The first problem concerned the fact that disputes frequently occurred with respect to brokerage commissions that are charged for each trade because a registered representative recommended "a securities trade regardless of the client's best interests in order to maximize commissions (churning)" in the past. The second problem is related to problems caused by competition in opening securities accounts.

In order to address such conflicts of interest between investors and registered representatives, a special committee was established in 1994 at the request of Arthur Levitt, former head of the SEC. As the final opinion, this special committee concluded that a fee based on the balance of assets in the account could not only help align the interests of registered representatives with those of their clients, but could also serve as a condition for registered representatives to devote themselves to more important roles, i.e., providing appropriate investment advice rather than providing advice for the purpose of increasing brokerage commissions.

Actually, the SEC observed in its 1999 Proposal after its survey of the new services offered by Merrill Lynch that fee-based securities accounts and online trade accounts are essentially the same as traditional securities accounts. Subsequently, however, the SEC invited public comments on the 1999 Proposal, and the final rules were announced in April 2005. The contents of the final rules announced in 2005 were identical to those of the 1999 Proposal.

During this period, securities accounts where the fee is based on the balance of the assets in the account have become popular not only among major securities firms but also among second-tier brokerage firms. In 2001, Merrill Lynch changed the name of its registered representatives to "financial advisors." The number of securities firms following such a move has increased.

Responding to such moves among securities firms, the Financial Planning Association, whose members consist of registered investment advisors, instituted a lawsuit in July 2004 by seeking a ban on the use of the name, "financial advisor." This lawsuit was subsequently postponed. However, in April 2005, in response to the announcement of the final rules by the SEC, the Financial Planning Association filed a petition with the Federal Court of Appeals requesting modifications of the rules that permit the use of the name "financial advisor" by registered representatives.[3]

3 NASD Notification

In November 2004, NASD issued a notification concerning fee-based securities accounts, which are increasing in popularity. This notification indicated that a fee-based securities account is not necessarily a suitable option for all clients, and required securities firms to apply the Suitability Rules strictly in terms of the client's investment objectives. This is because the cost of securities investment is lower in traditional securities accounts than it is in such fee-based accounts for investors with long-term investment objectives.

In April 2005, NASD made its first decision related to this issue by imposing a penalty of 750,000 dollars on Raymond James, a second-tier securities firm, on the grounds that the company opened an unsuitable fee-based account for a client. Raymond James announced that it would voluntarily close all fee-based accounts by July 2005 and would resume such accounts after reconfirming its clients' investment objectives.[4]

V Fraudulent Research Reports and the Retail Securities Business

1 Cases of Fraudulent Research Reports Issued by the Top Securities Firms

On December 20, 2002, the Securities and Exchange Commission (SEC) and other securities regulators announced a historic agreement with the nation's top ten securities firms to implement business reforms on a global basis with respect to cases of fraudulent research reports. The top ten securities firms listed in Table 2 including Salomon Smith Barney, Merrill Lynch and Credit Suisse First Boston (CSFB) reached an agreement with the SEC, the New York State Attorney General's Office, NASD, the North American Securities Administrator's Association (NASAA), the New York Stock Exchange and New York state securities regulators with respect to the payment of penalties totaling about 1.4 billion dollars, structural reforms, and the establishment of a fund to educate investors.

These cases involve undue influence by investment banking departments (that engage in the procurement of funds for client companies) of securities firms on their securities research departments (where research analysts issue reports analyzing companies' performances) for the sake of client companies. Such inappropriate practices also included providing research analysts with excessive compensation for issuing fraudulent research reports.

UBS Warburg and Piper Jaffray received payments from client companies for issuing biased research reports. CSFB and Salomon Smith Barney engaged in inappropriate Initial Public Offering (IPO) allocations to client companies. The securities firms agreed on settlement terms including penalties and mandates on structural reforms, while they neither admitted nor denied the regulators' allegations.

With respect to structural reforms, first, the settlement terms to sever research departments from investment banking departments include the following specific measures:

(1) The firms will physically separate their research and investment banking departments to prevent the flow of information between the two groups.
(2) The firms' senior management will determine the research department's budget without input from investment banking and without regard to specific revenues derived from investment banking.
(3) Research analysts' compensation may not be based, directly or indirectly, on investment banking revenues or input from investment banking personnel.
(4) Research management will make all company-specific decisions to terminate coverage, and investment bankers will have no role in company-specific coverage decisions.
(5) Research analysts will be prohibited from participating in efforts to promote the investment banking business, including sales activities for issuing securities (e.g., roadshows).
(6) The firms will create and enforce firewalls restricting interaction between investment banking and research activities except in specifically designated circumstances.

As remedial measures for the research reports, the ten firms were required to pay penalties, disgorgement and funds, which totaled about 1.39 billion dollars. Of this

Table 2. Payments in Global Settlements Related to Firm Research and Investment Banking Conflicts of Interest

(Unit: Million dollars)

Securities firm	Penalty	Disgorgement	Independent research	Investor education	Total
Bear Stearns	25	25	25	5	80
CSFB	75	75	50	0	200
Goldman Sachs	25	25	50	10	110
JP Morgan	25	25	25	5	80
Lehman Brothers	25	25	25	5	80
Merrill Lynch	100	0	75	25	200
Morgan Stanley	25	25	75	0	125
Piper Jaffray	12.5	12.5	7.5	0	32.5
Salomon Smith Barney	150	150	75	25	400
UBS Warburg	25	25	25	5	80
Total	487.5	387.5	432.5	80	1,387.5

Notes: (1) Merrill Lynch's penalty includes payments to state governments. (2) CSFB = Credit Suisse First Boston LLC.
Source: Joint press release issued by the NASD, SEC and New York Stock Exchange (NYSE), April 28, 2003.

amount, about 430 million dollars were allocated to a fund to use independent research firms (a fund to cover the expenses of distributing a research report issued by a third party research firm together with a research report issued by firm analysts to investors). Because this amount almost equals the penalty amount, stringent measures were taken with respect to research reports.

In point of fact, since July 27, 2004, Merrill Lynch and some other securities firms have been providing research reports issued by at least two or three independent research firms (research firms that are not affiliated with securities firms) when distributing research reports issued by their analysts to clients (Table 3). The agreed settlement terms require that the firms make available research reports by independent research firms for a five-year period.

Last, mandates on structural reforms require that each firm prepare and disclose track records that enable the comparison of its analysts' performance to investors. Specifically, each analyst's historical and current ratings (e.g., recommendations on sell, hold or buy) and price target forecasts must be disclosed to investors in a manner enabling investor access to such information at any time.

2 Impact on the Retail Securities Business

Structural reforms of securities firms based on fraudulent research reports created by firms' research analysts have also had a major impact on the retail securities business. Securities firms other than those top ten firms against which enforcement actions were implemented have started to provide research reports made by third-party independent research firms. In addition, the number of investors requesting such third-party research reports has increased. These circumstances required registered representatives to further enhance the capabilities of information analysis concerning stock investment. This requirement is particularly prominent in cases where stocks recommended in research reports made by a firm's analysts are different from those in a report issued by a third-party research firm.

While the stock market has been sluggish since the terrorist attacks in September 2001, this incident has served to exacerbate the situation. Because a research report by a firm's analysts that was a "differentiation" weapon in the past has become no longer effective, securities firms have further accelerated their shift from competition by securities products to services in which registered representatives offer advice on full financial services and activities to develop banking products to realize such advice. Merrill Lynch's "Beyond Banking" service that emerged in 2003 can be considered as one service that was developed under these circumstances.

In any case, after this incident, the ability of providing advice to a client on solutions covering full financial

Table 3. Start of Distribution of Independent Research Reports by Major Securities Firms (after July 27, 2004)

Securities firm	Independent research reports distributed	Remarks
Bear Stearns	• BNY Jaywalk • Reports prepared by 22 other research firms	More than half of the recommended investments differ between the firm's reports and those prepared by independent research firms
CSFB	• Renaissance Capital • BNY Jaywalk • Standard & Poor's	Two types of reports prepared simultaneously by BNY Jaywalk and Standard & Poor's are provided.
Goldman Sachs	• Standard & Poor's • Morningstar • Renaissance Capital	Two types of reports prepared simultaneously by Standard & Poor's and Morningstar are provided.
JP Morgan	• Morningstar • Renaissance Capital • BOE Securities	Research reports prepared by at least one independent research firm are provided.
Lehman Brothers	• BNY Jaywalk	Research reports prepared by at least one independent research firm are provided. The differences in recommended investments from those in the firm's reports are provided and analyzed.
Merrill Lynch	• Morningstar • BNY Jaywalk • Reports prepared by 24 or more other research firms	Research reports prepared by at least two or more independent research firms are provided.
Morgan Stanley	• Reports prepared by eight independent research firms	Research reports prepared by at least three independent research firms are provided.
Piper Jaffray	• Buckingham Research Group • Morningstar • Renaissance Capital • Standard & Poor's • Zacks Investment Research	Independent research reports with respect to 581 companies are provided.
Salomon Smith Barney	• Standard & Poor's • Argus Research • Morningstar • Renaissance Capital • Thomson Financial	Research reports prepared by one to four independent research firms are provided. A summary table of recommendations is distributed by Thomson Financial.
UBS Warburg	• BNY Jaywalk • Reports prepared by 32 other independent research	Research reports prepared by at least two independent research firms are provided.

Source: Compiled based on materials of the SEC and each securities firm.

services started to be required of registered representatives engaged in retail securities service.

At the same time, chiefly among major securities firms, accelerated moves have been taking place that focus on the education and teamwork of registered representatives in addition to strengthening the lineup of banking products. In terms of educating representatives, stress has been given to the education of newly registered representatives. For example, Morgan Stanley increased the budget for the education of those who have newly become registered representatives from 26 percent of the total education budget to 52 percent in 2004. Similarly, at Merrill Lynch, the education period was extended to five years during which time representatives are expected to acquire the qualifications of a certified financial planner (CFP).

Moreover, in terms of improving the quality of advice and diversifying the fields where advice is provided through teamwork and role sharing among registered representatives, 45 percent of all registered representatives have already formed some type of team at Merrill Lynch.

In response to these moves in the securities industry, educational organizations that develop financial advisers for the wealthy class have strengthened their activities. Table 4 lists courses offered by universities and other educational organizations. The course durations vary from several hours and several days to one year. All of the courses provide a title (similar to "bachelor") certifying the completion of a course.

3 Improved Research Reports

With respect to the distribution of research reports issued by third-party research firms, regulators have not required the ten securities firms to record the actual status of distribution to and use by clients. Accordingly, there is only limited information about how investors actually reacted to such reports. However, investor reactions can be assumed based on a Standard and Poor's survey conducted in May 2005. This survey revealed that about 40 percent of investors did not know of this global settlement on structural reforms between regulators and the ten securities firms. The number of investors who knew of the provision of research reports by third-party research firms was also limited.[5]

Table 5 indicates the recommended stock ratings provided by major securities firms and third-party research firms to show whether any changes have taken place in the quality of research reports made by the ten securities firms required to provide research reports issued by independent research firms.

Comparing the results of investments (annual rate of return) based on the recommended ratings in the last four years (May 1, 2001 – May 1, 2005) with those in the year from May 1, 2004, shows that the quality of the reports made by the top securities firms against which enforcement actions such as penalties were implemented has no doubt improved. The ranks of Merrill Lynch, J.P. Morgan, Piper Jaffray and CSBF that were19th, 13th, 21st and 22nd, respectively, based on the results in the last four years were raised to 6th, 7th, 9th and 15th, respectively, during this last year.

However, the ratings of typical stocks such as GM (General Motors), AIG (American International Group) and Microsoft vary widely. For example, while many research providers recommended "sell" for GM stocks, only CSFB and J. P. Morgan recommended "buy." As explained previously, funds totaling about 430 million dollars were provided by securities firms against which enforcement actions were implemented for the provision of research reports by independent research firms. Nevertheless, it appears that these firms cannot neglect to monitor the reports made by their own analysts.

In any case, after the occurrence of this incident, clients' needs for simply receiving research reports and securities trading services are considered to be declining. It would be reasonable to consider that the moves of major securities firms to shift their focus on retail securities services by registered representatives to providing financial solutions for clients will be further expanded, while creating synergistic effects accompanying the increase in the number of retiring baby boomers.

Table 4. Financial Planner Qualifications and Educational Organizations

Qualification	Educational organization	Tuition fee	Content
Accredited Wealth Management Advisor	College for Financial Planning	$850 plus $150 admission fee	2-hour test based on a 1,000-page textbook and a collection of questions
Certification in Wealth Management	New York University	$5,000 – $5,600 (depending on courses)	Eight courses are provided; each course consists of 20 hours of lessons and a completion test
Wealth Management Certificate	Investment Management Consultants Association	$3,900 (member) $4,200 (non-member)	A course consists of 32 hours of lessons and about 180 hours of self-study; popular among securities brokers
Private Wealth Management Program	The Wharton School at the University of Pennsylvania	$8,000	5-day program; 6 to 8-hours of classroom instruction per day
Chartered Wealth Manager	American Academy of Financial Management	$600 (tuition) $300 (certification)	80 hours of online lessons and a test

Source: *Wall Street Journal*, October 27, 2004.

Table 5. Improvement in Quality of Equity Analysis by Securities Firms

Rank in the last year(1)	Percentage change of S&P500 in the last year (%)	Research firms (firms in boldface are securities firms and others are independent research firms)	Rank in the last four years(2)	Annual rate of return in the last four years (%)	Rating of typical stock issues at the time of research(3)		
					GM	AIG	Microsoft
1	19.73	Weiss Ratings	16	– 3.51	Sell	Hold	Buy
2	19.65	Columbine Capital Services	3	7.32	Sell	Hold	Hold
3	16.79	**Deutsche Bank Securities**	5	3.25	Sell	Hold	N.A.
4	16.50	Ford Equity Research	11	1.99	Sell	Hold	Hold
5	16.28	Channel Trend	2	8.10	Hold	Hold	Hold
6	15.05	**Merrill Lynch**	19	– 3.83	Hold	Buy	N.A.
7	9.20	**JP Morgan**	13	– 0.91	Buy	Buy	Buy
8	8.67	**Goldman Sachs**	6	3.03	Sell	Buy	Buy
9	8.04	**Piper Jaffray**	21	– 9.85	N.A.	N.A.	Buy
10	7.59	Callard Research	1	8.49	Hold	Buy	Hold
11	6.25	Thomas White International	10	2.22	Sell	Sell	Hold
12	5.02	**Lehman Brothers**	12	– 0.36	Sell	Buy	Buy
13	3.83	**UBS Investment Research**	8	2.79	Sell	Hold	Buy
14	2.88	Rochdale Research	N.A.	N.A.	Hold	Hold	Hold
15	2.02	**CSFB**	22	– 12.43	Buy	Buy	Hold
16	0.96	**Smith Barney**	14	– 1.34	Sell	Buy	Buy
17	0.45	S&P Equity Research	20	– 6.99	Sell	Buy	Buy
18	– 1.11	**Morgan Stanley**	16	– 3.51	Hold	Buy	Buy
19	– 1.39	**Thomas Weisel Partners**	9	2.58	Hold	N.A.	Buy
20	– 4.16	Argus Research Company	23	– 16.17	Sell	Buy	Buy

Notes: (1) One year from May 1, 2004, to May 1, 2005. (2) Four years from May 1, 2001 to May 1, 2005. (3) As of June 6, 2005. (4) S&P 500 = Standard and Poor's 500 Index, GM = General Motors Corporation, AIG = American International Group.
Source: *Wall Street Journal*, June 7, 2005.

4 Research Reports in Short Supply

There are about 70 independent research firms throughout the nation that have no association with securities firms. Among these independent research firms, many have a contract with securities firms for the preparation of research reports to compensate for the shortage of analysts in securities firms. This time, the terms of settlement prohibited an independent research firm from entering into a contract for preparing and providing research reports by receiving compensation from a securities firm unless a fully independent research department is established within the firm.

Because of this, with the exception of some major independent research firms such as Standard & Poor's, which is a subsidiary of McGraw Hill, research firms that must terminate service to prepare and provide research reports that have so far been provided to securities firms appeared after one the other. The shortage of research reports has become critical, particularly in second-tier securities firms that do not have many analysts and have depended on third-party research firms to provide reports to clients.

At securities firms, the costs for preparing research reports by analysts are covered by the brokerage commissions earned by registered representatives. Accordingly, greater needs naturally arise for research reports on issues with high trading volume on the securities market. In contrast, research reports on issues with little trading volume are less popular even if an issuing company appears promising from the long-term perspective. In terms of the purpose of finding growing companies, this situation has given rise to the question about the essential significance of research reports.

Because of the shortage of research reports prepared by independent research firms, two companies were established in September 2005 that search and provide research reports on an issue needed by a securities firm.[6]

These companies are Independent Research Network and National Research Exchange. The purpose of their business is to find a research report prepared by an independent research firm at the request of a securities firm and receive a handling fee for finding the report. The former is a joint venture established by NASDAQ and Reuters Group, a global information company; the latter was established by the former NASDAQ vice chairman. At present, the thinking is divided as to whether the emergence of these companies can play a meaningful role in eliminating the shortage of research reports and in improving the access to and quality of research reports.

VI Lessons for Japan's Securities Markets

1 Banks' Retail Securities Services and Sales of Investment Trusts

Securities services provided at bank branches are also rapidly expanding in Japan. The sales of public bonds at bank branches (over-the-counter sales or OTC sales) began in 1983 in order to handle the large volume of government bonds issued. OTC sales of securities investment trusts started in 1998.

The New Comprehensive Program for Promoting Securities Markets Reform announced by the Financial Services Agency in August 2002, which lifted a ban on the establishment of joint banking and securities branches, became effective in October 2002. This program also lifted a ban on securities brokerage services provided by ordinary, non-financial companies or individuals who entered into a contract with a securities firm. They act as agents for securities firms in opening securities trading accounts and intermediating the selling or purchases of securities such as stocks. These services began in April 2004.

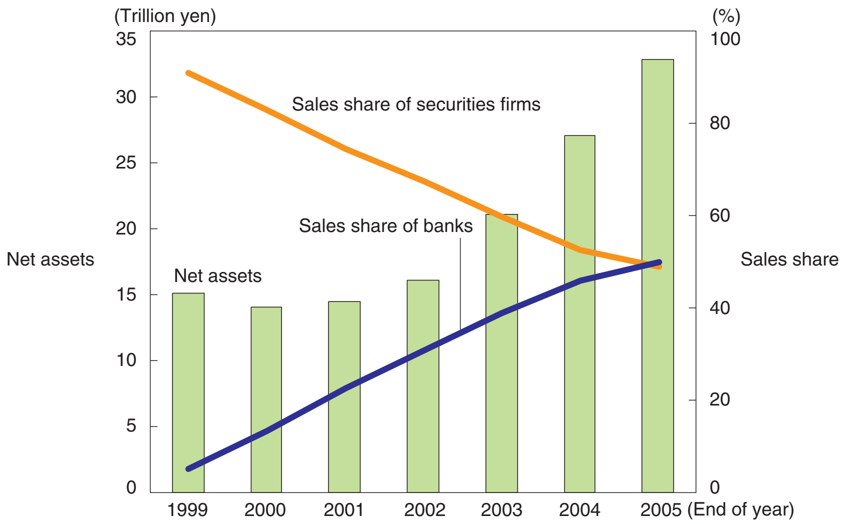
Subsequently, in December 2004, a ban on securities brokerage services provided by banks was also removed. Now, almost all financial products such as stocks and bonds are sold at banks. This means that one-stop service enabling the provision of banking and securities trading services at one location has become available, similar to the situation in the United States.

Furthermore, in April 2006, an amendment to the Bank Law is expected to give birth to new agency business for bank, which was previously permitted only to fully owned bank subsidiaries. This amendment will enable those agencies to handle deposits, intermediate foreign exchange transactions and process individual loans at sites other than bank branches and ATMs (automated teller machines). These services will strongly support physically disabled seniors that need financial services in an increasingly aging society.

Figure 1 shows the OTC sales of investment trusts at banks. In terms of investment trusts, in August 2005, the share (net worth) of OTC sales at banks exceeded the share (net worth) of sales by securities firms. It appears that the smooth recovery of the stock market and high sales commissions set at 2 to 3 percent of the principal have served as incentives for the OTC sales of investment trusts at banks.

The sales of bond investment trusts such as MMF (money market funds) at banks increased for about two years after the start of the OTC sales partly due to the fact that these products are similar to deposits and the yield is somewhat higher than deposits (Figure 2). However, after 2002, bank sales have been declining. This is because, in relation to the Enron scandal in the United States, in November 2001, the news media

Figure 1. Net Assets of Publicly Offered Stock Investment Trusts and Sales Share of Banks and Securities Firms



Note: The figure for 2005 covers through August.
Source: The Investment Trusts Association, Japan.

Figure 2. Net Assets of Publicly Offered Bond Investment Trusts and Sales Share of Banks and Securities Firms

Note: The figure for 2005 covers through August.
Source: The Investment Trusts Association, Japan.

reported a fall below par of some MMFs that included medium-term bonds issued by Enron.

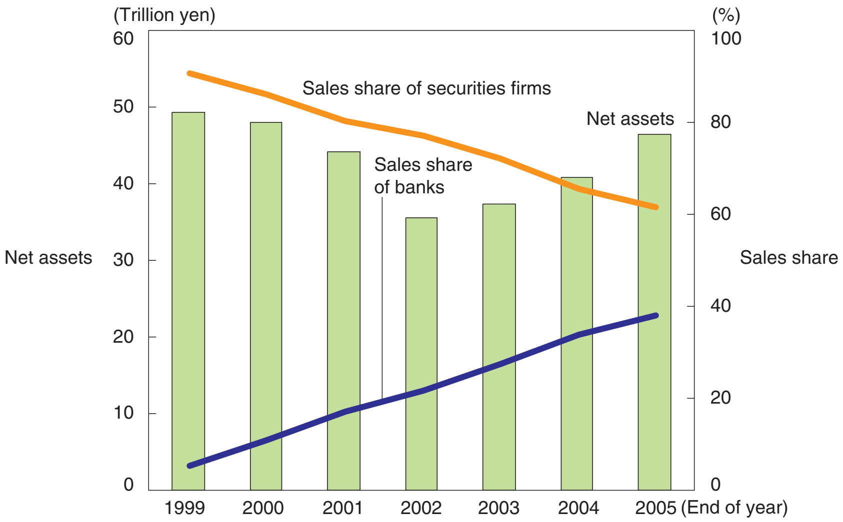
Nevertheless, as of August 2005, banks accounted for 38 percent of the sales of investment trusts as a whole, indicating smooth business deployment (Figure 3). It can be said that the OTC sales of investment trusts at banks has grown to a stage where such business is positioned as a primary business operation for banks that aim at expanding revenues by increasing commissions under a prolonged deflationary economy and an accompanying decline of demand for funds.

2 Recovery of the Stock Market and Popularization of Online Trades

A deflationary recession caused by the collapse of the bubble economy is finally ending, principally because of the elimination of non-performing assets and bad debt problems facing banks. With such economic recovery and the expansion of corporate revenues forming major background factors, the stock market has been on the way to revitalization since the first half of fiscal 2003. As shown in Figure 4, this situation is clearly indicated by the rapid increase in trading volume (based on turnover) in the stock market. In particular, an increase in the volume (based on turnover) of online trades via the Internet has been significant. These transaction amounts accounted for 26.5 percent of all transaction amounts in the second half of fiscal 2004.

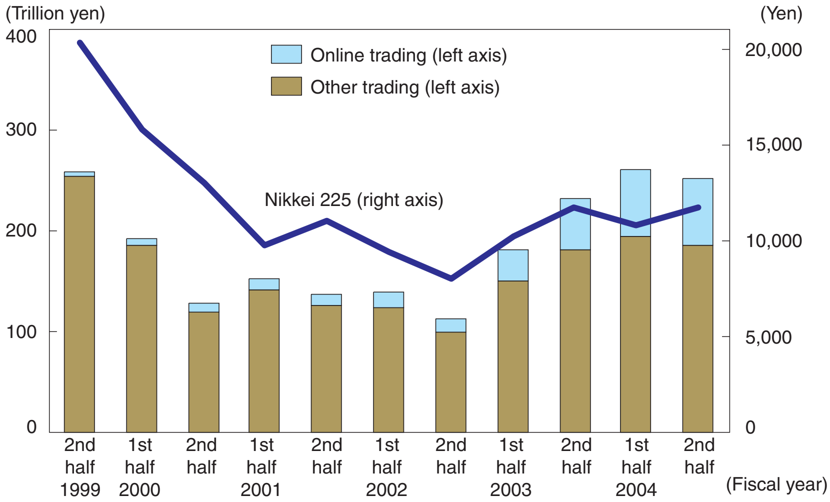
Diverse factors can be considered as reasons for the vitalization of online trades such as the recovery of the stock market. Among others, a principal factor is considered a rapid increase in margin trading using agreements for which a repayment date (settlement date) is not set.

Figure 3. Total Net Assets of Publicly Offered Investment Trusts and Sales Share of Banks and Securities Firms



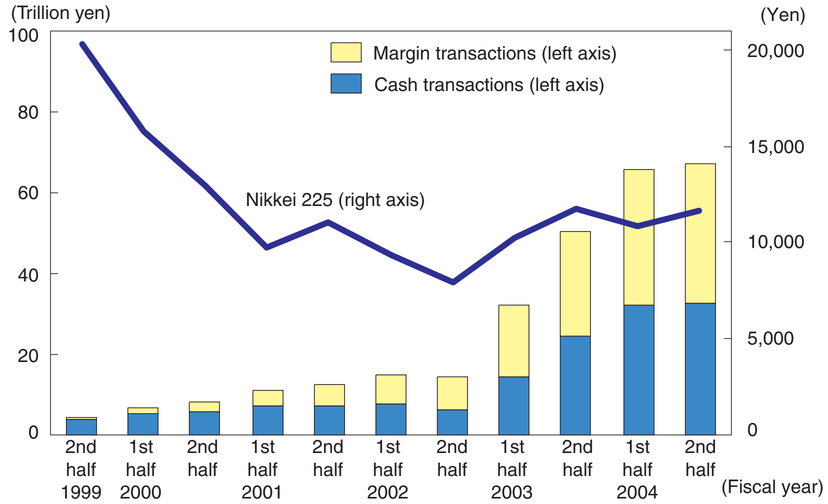
Note: The figure for 2005 covers through August.
Source: The Investment Trusts Association, Japan.

Figure 4. Online Trading in Stock Transactions (Based on Turnover)



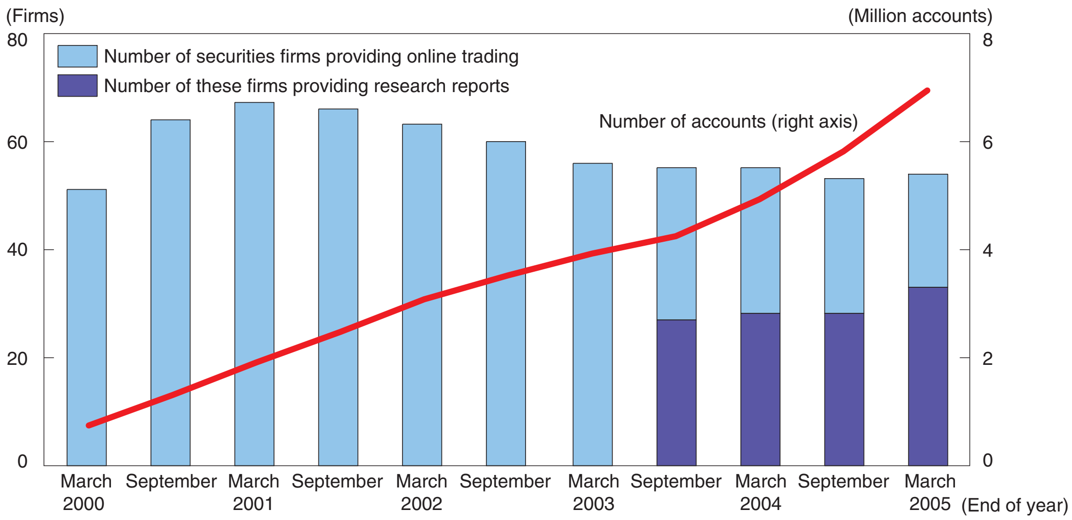
Note: (1) "Turnover" refers to the total turnover from stock agency transactions by all members in each period. (2) As to statistics in and after September 2001, the turnover from exchange-traded funds (ETFs), real estate investment funds and other transactions is included in the turnover from stock transactions. (3) Figures for Nikkei 225 are closing prices at the end of each period.
Source: Japan Securities Dealers Association, *Shokengyo ho* (Securities Dealers Report), May 2005.

Figure 5. Cash and Margin Transactions in Online Trading (Based on Turnover)



Note: (1) "Turnover" refers to the total turnover from stock agency transactions by all members in each period. (2) As for statistics in and after September 2001, the turnover from exchange-traded funds (ETFs), real estate investment funds and other transactions is included in the turnover from stock transactions. (3) Figures for Nikkei 225 are closing prices at the end of each period.
Source: Japan Securities Dealers Association, *Shokengyo ho* (Securities Dealers Report), May 2005.

Figure 6. Number of Securities Firms Providing Online Trading and Number of Online Trading Accounts



Source: Japan Securities Dealers Association, *Shokengyo ho* (Securities Dealers Report), May 2005.

The stock margin trades available in the past were only those to which stock exchange rules were applied, where a securities finance company licensed under the Securities and Exchange Law lends funds or stocks for six months to an investor through a securities firm. In addition to these transactions, in December 1998, margin trading where a contract to lend funds or stocks is made directly between an investor and a securities firm was introduced. Since the summer of 2003, transactions with investors without repayment (settlement) restrictions have been started by some online trading securities firms by using margin trading that enables a securities firm and an investor to freely enter into a contract. Since the beginning of 2004, this margin trading with no restrictions[7] has spread widely, and is considered to have resulted in increases in credit transaction amounts.

In addition, the fact that stock trading in small amounts has become possible as a result of reducing stock trading units through stock splits appears to have had a major impact on such increases. Incidentally, the stock of Livedoor, which attracted public attention by acquiring a large volume of shares of Fuji Television Network, can be traded in units of one share at a price of only 447 yen (closing price at the end of September 2005).

Figure 6 shows the number of securities firms providing online trading and the number of online trading accounts. While there were only 300,000 accounts at the end of the first half of fiscal 1999 when such service was started, the number of accounts increased at a pace of 300,000 to 600,000 every six months through the first half of fiscal 2003. This pace accelerated in the second half of fiscal 2003: the number of accounts started to increase by 700,000 to 1,100,000 accounts every six months. At the end of March 2005, there were nearly 7 million accounts.

Figure 6 also indicates the number of firms providing research reports. These data can be viewed in such a way that the number of new accounts increased rapidly during the period when securities firms providing online trading started to distribute research reports via the Internet. If the distribution of research reports is assumed to have triggered the increase in the number of online trading accounts, it can be assumed that among online traders, in addition to day traders who are simply watching only daily price movements, the number of investors with high needs for information such as the perspectives on corporate performance in relation to their stock investments is increasing.

Investors who started online trades by seeking such information have never experienced a major drop in stock prices such as what occurred in the United States due to the collapse of the IT bubble. Depending on the fluctuation of future stock market conditions, it is likely that Japanese investors may become "prudent investors (validators)" who require the advice of securities firms and second opinions of other investment advisors in the same way as individual American investors do.

Furthermore, the current online trading system is not yet developed as a convenient, easy-to-use system for the rapidly increasing number of senior savers chiefly due to the increase in the number of retiring baby boomers. In this respect, how best to use IT, such as a complete shift to interactive digital TVs after the termination of analog TV broadcasting scheduled for July 2011, will serve as a key factor for each securities firm in further popularizing online trading.

3 Securities Services by Banks

Pursuant to the provisions of Article 66-2 of the Securities and Exchange Law, ordinary companies and individuals can operate securities brokerage businesses by registering with the Financial Services Agency. The participation of banks in the securities brokerage business is now possible because such business was included in securities businesses that can be operated by registered financial institutions such as banks under Article 65-2 of the Securities and Exchange Law.

After taking and passing the securities representative examination, a bank employee as an agent can provide services such as opening securities trade accounts at a securities firm with which a bank has a contract and assisting in securities transactions. All responsibilities for managing a securities account, maintaining contact with a customer regarding a securities account and ensuring compliance lie with the contracting securities firm.

The lifting of the ban on securities brokerage business provided two options for the retail securities services provided by banks.

The first option involves the case of city banks owning securities subsidiaries in which joint banking and securities branch offices are established to provide securities service as well as banking services. In this case, as the counter space of a securities firm managing securities trade accounts is provided in a bank's branches, service can easily be provided. As shown in Table 6, all city banks, except for Resona Bank and Saitama Resona Bank, have started securities brokerage businesses in this format. Mizuho Corporate Bank does not engage in retail services.

To date, the Bank of Tokyo-Mitsubishi and UFJ Bank have shown particularly high interest and started securities

Table 6. Participation of City Banks in Agency Business for Securities Firm (As of September 30, 2005)

Bank	Affiliated securities firm	Number of domestic offices	Number of offices providing agency services	Service start	Remarks
Mizuho Bank	Mizuho Investors Securities, Shinko Securities and Monex Beans Securities	491	69	December 2004	60 Planet Booths, seven neighboring offices and two Customer Plazas of Shinko Securities
The Bank of Tokyo-Mitsubishi	Mitsubishi Securities and Me Net Securities	250	243	April 2005	25 joint offices (including MTFG Plazas) and 6 neighboring offices
UFJ Bank	UFJ Tsubasa Securities and kabu.com Securities	412	400	December 2004	Accounts can be opened and foreign bonds can be traded at about 400 offices throughout the country; securities trading desks are provided at 15 offices.
Sumitomo Mitsui Banking Corporation	SMBC Friend Securities	472	425	December 2004	Services are provided at each domestic office; private banking sales departments
Resona Bank	Nomura Securities and Matsui Securities	300	32	December 2004	About 1,000 employees acquired qualifications necessary for securities services at Resona Bank and Saitama Resona Bank
Saitama Resona Bank	Nomura Securities	105	10	December 2004	
Mizuho Corporate Bank	Mizuho Securities and Shinko Securities	33	1	April 2005	Service will be expanded gradually and handled by financial business customer departments (9 sales departments)

Sources: Website of each bank and Japanese Bankers Association, *Analysis of Financial Statements of All Banks (FY 2004).*

Table 7. Participation of Regional Banks in Agency Business for Securities Firm

	Affiliated securities firm	As of October 3, 2005		As of March 4, 2005	
		Number of offices providing securities services	Service start	Number of offices providing securities services	Service start
The Hokkaido Bank		–		–	
TheAomori Bank	Daiwa Securities* and Nomura Securities	3	March 2005	3	March 2005
The Michinoku Bank	(Under consideration)	–	(Under consideration)	–	(Under consideration)
Akita Bank	Daiwa Securities* and Nomura Securities	1	April 2005	1	April 2005
The Hokuto Bank	Nomura Securities and Nikko Cordial Securities	2	April 2005	2	April 2005
The Shonai Bank	Nikko Cordial Securities and Mizuho Securities	2	April 2005	Undecided	April 2005 (planned)
The Yamagata Bank	Nomura Securities	1	April 2005	1	April 2005
The Bank of Iwate	Daiwa Securities* and Nomura Securities	1	December 2004	1	December 2004
The Tohoku Bank	(Under consideration)	–	(Under consideration)	–	(Under consideration)
The 77 Bank	Nomura Securities*	1	April 2005	1	April 2005
The Toho Bank	Nomura Securities*	1	May 2005	–	(Under consideration)
The Gunma Bank	Nomura Securities*	1	August 2005	–	(Under consideration)
The Ashikaga Bank	(Under consideration)	–	(Under consideration)	–	(Under consideration)
The Joyo Bank	Nomura Securities*	2	May 2005	–	(Under consideration)
The Kanto Tsukuba Bank	Nomura Securities*	2	October 2005	–	(Under consideration)
The Musashino Bank	Nomura Securities*	1	December 2004	1	December 2004
The Chiba Bank	Chuo Securities and Mitsubishi Securities	25	February 2005	25	February 2005
The Chiba Kogyo Bank	Daiwa Securities* and Shinko Securities	4	December 2004	1	December 2004
The Tokyo Tomin Bank	Shinko Securities	1	February 2005	–	February 2005
The Bank of Yokohama	Nikko Cordial Securities*	9	June 2005	7 – 8 (planned)	June 2005 (target date)
The Daishi Bank	Nomura Securities	8	February 2005	1	February 2005
The Hokuetsu Bank	Nikko Cordial Securities	2	May 2005	–	April 2005
The Yamanashi Chuo Bank	Nomura Securities	1	April 2005	–	(Under consideration)
The Hachijuni Bank	Nomura Securities△	4	May 2005	4	May 2005 (target date)
The Hokuriku Bank	Nomura Securities	4	December 2004	4	December 2004
The Toyama Bank	(Under consideration)	–	(Under consideration)	–	(Under consideration)
The Hokkoku Bank	Daiwa Securities△	1	April 2005	1	April 2005
The Fukui Bank	(Under consideration)	–	(Under consideration)	–	(Under consideration)
The Shizuoka Bank	Shizugin TM Securities	6	December 2004	6	December 2004
Suruga Bank	Nomura Securities△	Appointed branch by reservation	April 2005	–	(Under consideration)
The Shimizu Bank	Daiwa Securities△	1	December 2004	1	December 2004
The Ogaki Kyoritsu Bank	Daiwa Securities and Toyota Financial Services Securities	–	June 2005	–	(Under consideration)
The Juroku Bank	Nomura Securities*	1	March 2005	1	March 2005
The Mie Bank	Daiwa Securities* and Daiwa Securities SMBC*	1	March 2005	1	March 2005
The Hyakugo Bank	Nomura Securities	10	January 2005	10	January 2005
The Shiga Bank	Nikko Cordial Securities*	1	April 2005	1	(Under preparation)
The Bank of Kyoto	Daiwa Securities△	15	December 2004	15	December 2004
The Kinki Osaka Bank	Nomura Securities	1	April 2005	1	April 2005
The Senshu Bank	UFJ Tsubasa Securities	5	December 2004	5	December 2004
The Bank of Ikeda	Nomura Securities△	11	December 2004	11	December 2004
The Nanto Bank	Nomura Securities* and Daiwa Securities	2	December 2004	2	December 2004
The Kiyo Bank	Daiwa Securities	1	April 2005	–	(Under consideration)
The Tajima Bank	(Under preparation)	–	(Under preparation)	–	(Under consideration)
The Tottori Bank	Nomura Securities△	3	June 2005	–	(Under consideration)
The San-in Godo Bank	Daiwa Securities	3	April 2005	–	(Under consideration)
The Chugoku Bank	Nikko Cordial Securities and Mizuho Securities	6	December 2004	6	December 2004
The Hiroshima Bank	Mizuho Securities	–		–	
The Yamaguchi Bank	Daiwa Securities△	8	December 2004	8	December 2004
The Awa Bank	Daiwa Securities△ and Nomura Securities	1	December 2004	1	December 2004
The Hyakujushi Bank	Nomura Securities*	2	April 2005	–	(Under consideration)
The Iyo Bank	Nomura Securities*	5	March 2005	5	March 2005
The Shikoku Bank	(Under consideration)	–	(Under consideration)	–	(Under consideration)
The Bank of Fukuoka	Maeda Securities and Nomura Securities	3	May 2005	0	April 2005
The Nishi-Nippon City Bank	Merrill Lynch Japan Securities and Nomura Securities*	1	December 2004	1	December 2004
The Chikuho Bank	(Under preparation)	–	(Under preparation)	–	(Under consideration)
The Bank of Saga	(Under consideration)	–	(Under consideration)	–	(Under consideration)
The Eighteenth Bank	Nomura Securities* and Nikko Cordial Securities	1	April 2005	1	April 2005
The Shinwa Bank	(Under consideration)	–	(Under consideration)	–	(Under consideration)
The Higo Bank	Nomura Securities	1	December 2004	1	December 2004
The Oita Bank	Nomura Securities△	1	December 2004	1	December 2004
The Miyazaki Bank	Nomura Securities△, Nikko Cordial Securities and Daiwa Securities	–	April 2005	–	April 2005
The Kagoshima Bank	Nomura Securities	2	April 2005	–	(Under consideration)
Bank of the Ryukyus	Nomura Securities*	1	July 2005	–	(Under consideration)
The Bank of Okinawa	Daiwa Securities*	1	May 2005	–	(Under consideration)
Total		171		131 – 132	

Notes: *= Lead managing underwriter, △ = Major managing underwriter.
Sources: Figures as of March 4, 2005, are based on *Kin'yu zaisei jijo* (Financial Affairs), March 14, 2005, and figures as of October 3, 2005, are based on the website of each firm.

brokerage businesses in almost all of their branches. Mizuho Bank is expanding the number of joint banking and securities branches, which had already accounted for more than 10 percent of all of its branches throughout the country.

Some major regional banks owning securities subsidiaries started this business in a similar format. However, many regional banks employed the second option of establishing partnerships with outside securities firms to start securities brokerage businesses (Table 7). In particular, regional banks located in the metropolitan areas of Kanto, Kinki and Tokai, such as Chiba Bank (using its securities subsidiary, Chuo Securities, and Mitsubishi Securities), Hyakugo Bank, the Bank of Kyoto and the Bank of Ikeda, are strengthening their efforts to offer this business.

To date, securities firms have played a major role in providing retail securities services. Tables 8 and 9 show the regional distribution of securities firm branch offices and registered representatives, respectively. Concentration in the Kanto region is prominent in terms of both the numbers of offices and representatives. These numbers are far greater than those in the Kinki region that ranks next to the Kanto region. These data suggest concentration of retail securities services provided by securities firms in Kanto.

In terms of the number of branch offices in particular, nearly half are located in Kanto. Branches located in the metropolitan areas of Kanto, Kinki and Tokai account for approximately 75 percent of all branches throughout the country. In terms of personnel as well, registered representatives in Kanto account for about 60 percent. If registered representatives in Kinki and Tokai were added, about 85 percent of all sales representatives are providing service in metropolitan areas. Consequently, securities services are in short supply in regional areas.

The participation of banks, in particular regional banks, in the securities brokerage business is expected to vitalize securities investments by individuals in regional areas where retail securities services are not adequately available. Table 10 outlines the participation of regional banks in the securities brokerage business. As of October 3, 2005, 53 out of 64 regional banks began such a business at about 170 branch offices.

Because the total number of regional bank offices throughout the country is slightly below 6,800 (as of the end of March 2005), the securities brokerage business was currently started at only a limited number of offices. Under these circumstances, it is too early to predict what impact the participation of banks in retail securities services through securities brokerage businesses would

Table 8. Number of Securities Firms' Offices by Region (As of the End of June 2005)

Region	Number of head offices			Number of offices other than head offices			Total
	Regular exchange members, etc.	Other than at left	Subtotal	Branch offices	Others	Subtotal	
Hokkaido	1		1	23	3	26	27
Tohoku		3	3	45	11	56	59
Kanto	(20) 91	(20) 85	(40) 176	610	117	727	(40) 903
Koshinetsu	4	3	7	67	24	91	98
Tokai	9	11	20	208	49	257	277
Hokuriku	1	10	11	40	16	56	67
Kinki	20	14	34	(1) 298	(1) 38	(2) 336	(2) 370
Chugoku	3	3	6	95	7	102	108
Shikoku		6	6	50	14	64	70
Kyushu	1	4	5	87	9	96	101
Okinawa		2	2	5	7	12	14
Total	(20) 130	(20) 141	(40) 271	(1) 1,528	(1) 295	(1) 1,823	(42) 2,094

Note: Figures in parentheses represent the number of foreign securities firms and are included in the number of offices.
Source: Japan Securities Dealers Association, *Shokengyo ho* (Securities Dealers Report).

Table 9. Number of Registered Representatives of Securities Firms by Region (As of the End of June 2005)

Region	Type 1 representatives	Margin trading representatives	Type 2 representatives	Total
Hokkaido	632	2	223	857
Tohoku	1,155	3	367	1,525
Kanto	37,455	29	6,096	43,580
Tokai	5,495	31	1,094	6,620
Hokuriku	978	5	253	1,236
Kinki	9,210	12	1,888	11,110
Chugoku	1,992		442	2,434
Shikoku	1,147	2	285	1,434
Kyushu	2,326	3	657	2,986
Total	60,390	87	11,305	71,782

Note: Representatives in Kanto includes those in Koshinetsu and Okinawa.
Source: Japan Securities Dealers Association, *Shokengyo ho* (Securities Dealers Report).

Table 10. Participation of Regional Banks in Agency Business for Securities Firm

Region	Total number of regional banks	Total number of domestic head and branch offices	Number of banks providing brokerage services	Number of head and branch offices of banks providing brokerage services	Number of offices providing brokerage services
Hokkaido	1	126	0	–	–
Tohoku	10	941	8	779	12
Kanto	9	992	8	893	45
Koshinetsu	4	441	4	441	15
Hokuriku	4	380	2	253	5
Tokai	7	784	7	784	19
Kinki	7	659	7	659	36
Chugoku	6	687	5	616	20
Shikoku	4	443	3	330	8
Kyushu	10	1,207	7	940	9
Okinawa	2	116	2	116	2
Total	64	6,776	53	5,811	171

Sources: Website of each company and Japanese Bankers Association, *Analysis of Financial Statements of All Banks (FY2004)*.

Table 11. Number of Securities Brokers by Region (As of the End of August 2005)

Region	Corporations	Individuals	Total
Hokkaido	5	6	11
Tohoku	13	4	17
Kanto	78	59	137
Koshinetsu	7	8	15
Tokai	22	21	43
Hokuriku	11	6	17
Kinki	32	30	62
Chugoku	6	6	12
Shikoku	3	3	6
Kyushu	18	22	40
Okinawa	0	2	2
Total	195	167	362

Source: Financial Services Agency.

have on the nationwide securities market, especially in areas other than metropolitan areas.

4 Financial Institutions in an Aging Society

Similarly, the concentration of securities brokerage businesses in metropolitan areas is also seen with respect to the participation of companies other than banks and individuals. Nevertheless, coverage is expanding to include regional areas (Table 11). Individuals who registered to operate agency businesses for securities firms include, in order of their number, financial planners, insurance agents, accountants and those who operate management consulting businesses. Companies that registered include credit card companies including Credit Saison and American Express, and Lawson, a chain of convenience stores.

Infrastructure to expand the coverage of the retail securities market is being developed with a focus shifting from “savings” to “investment.”

In the same way as in the United States, the number of seniors in Japan is expected to rapidly increase as baby boomers reach their retirement age in and after 2007. Whether it is possible to provide advisory services on asset management, inheritance, etc. that can fully meet the needs of senior savers whose revenues have decreased will be the key factor in becoming a winning financial institution in a highly competitive environment.

To this end, rather than just selling financial products under the concept of simply increasing assets, what is required is the ability to respond to diversified needs such as maintaining the liquidity of assets and taking measures for the inheritance of assets. It is also an urgent necessity to develop products that can go beyond simple banking, securities or insurance products and to re-establish a service structure to support such new products.

In addition, the living needs of seniors vary from working and building up assets to maintaining post-retirement life. Furthermore, their area of activities will become narrower than that in the past and tend to be limited to some areas centered on the living area. In this sense, the vital core of the retail sales strategy of financial institutions will consist of providing financial and securities services at branches adjacent to their customers’ homes in addition to the effective utilization of securities brokers and bank agents.

In any case, under the accelerated trend toward aging, the ability to provide high-quality advice that supports customer living from the financial perspective that fully meets customer needs and to develop products that can build high customer satisfaction will constitute the most important factors in determining a selected financial institution.

Notes

(1) See Akira Yasuoka, “Shoken shijo kaikaku no genjo to tenbo (Current Situation and Future Prospects of Securities Market Reforms),” *Knowledge Creation and Integration*, NRI, April 2003.

(2) Deposit products such as a certificate of deposit (CD) that is derived from a deposit, a letter of credit (LC), banker’s acceptance (BA), asset backed securities, etc.

(3) *Registered Representative*, April 29, 2005.

(4) *Registered Representative*, April 29, 2005.

(5) *Wall Street Journal*, June 7, 2005.
(6) *Wall Street Journal*, September 19, 2005.
(7) A settlement date (credit date) may be set in case of stock delisting, consolidation, split-up, etc, and for reasons such as the processing of stock rights.

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5. SEC, "International Series Release No. 1278," June 24, 2003.
6. SEC, "17 Code of Federal Regulation Part 275," April 15, 2005.

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