

particularly with the privatization of Japan Post now in the cards, the forward-looking agenda is ambitious. This agenda has the potential to bring very positive change to the financial sector in Japan, as well as direct benefits to savers, investors and consumers of financial services. The wider economy would also benefit through a more efficient financial system.

Competition is increasing in the marketplace, non-performing loans are on a downward trend and on track to meet the government target for their reduction, and credit practices are improving. Financial reconstruction has proceeded, notably thanks to a clear target and clear enforcement (including sanctions) by the Financial Services Agency (FSA), and a more resilient financial system has emerged. Canada welcomes proposed changes in the distribution channel, in particular the easing of restrictions on bank branches selling securities and insurance. We are also encouraging the Japanese government in its efforts to widen consumer choice, which will facilitate a more varied use of household savings and greater risk-taking by individual investors.

However, the system still remains vulnerable, and new lending is still on a downward trend. Continued and robust financial sector supervision, increased shareholder accountability and continued action on industrial revitalization are required to foster a dynamic, sustainable and efficient financial sector.

Canada continues to request that the Financial Services Agency offer a more flexible regime that is sensitive to smaller institutions' need to contain costs. A longer-term goal, which fits with the FSA's current efforts to define a medium-term "vision" for the financial sector, should be to move regulation to a more macro-level approach.

#### **Supervision and Regulation: Greater Simplification and a Regime More Supportive of Product Innovation Are Needed**

To introduce genuine and transparent regulatory reform, a regulatory system that focuses on macro-level financial supervision is desirable. Applying an *ex post* supervisory approach that promotes efficiency and competition (in place of the current *a priori* regulation and supervision approach) would enhance the efficiency of Japan's financial system without harming its safety or soundness.

With the purported goal of ensuring consumer transparency, the FSA applies a micro-level analysis to product and rate approvals. This supervisory approach hinders competition because it is time-consuming and stifles the forces of innovation. We have noted the progress achieved since the establishment of the FSA, but we are requesting that greater efforts be made to move from a system of prior product approval to a system of notification combined with clear standards of disclosure. Supervision should move to a focus on solvency ratios, capital adequacy and appropriate modern accounting practices.

Canada is also of the view that, although the independence of the inspection division is of prime importance under the current supervisory regime of the FSA, better coordination and communication between the inspection division and the supervisory division is needed to ensure a more efficient supervisory administration. Canada is requesting that firms be given more complete feedback on the results of discussions and consultations with the supervisory division; these results should also be well communicated to the inspection division. Such feedback would help firms ensure their compliance with laws and regulations ahead of inspections.

Finally, in order to lighten the burden of regulatory compliance, we are encouraging agencies with a role in regulating the financial sector to harmonize their information requirements. In this way, financial institutions would only need to provide one standard set of information, which could then be used by all regulators.

#### **Public Sector Financial Institutions Still Distort the Market: Privatizing Japan Post Could Resolve This Issue in the Long Run**

There continues to be a general concern that government financial institutions in Japan provide many services that private sector institutions can provide efficiently. The involvement of government enterprises in the financial sector, some of which have very sizable market shares, distorts competition significantly and could be seen to contravene Japan's General Agreement on Trade in Services commitments. Examples of government institutions that have large market shares are the Postal Savings system (*yucho*) and the Postal Life Insurance system (*kampo*).