

JPFSA Consults on NAV Materiality Management

Last Friday, the Financial Services Agency in Japan (JPFSA) published a draft of partial amendment of Comprehensive Guidelines for Supervision of Financial Instruments Business Operators, etc (the Guidelines) for consultation to add supervisory viewpoints for encouraging Japanese investment trust management companies to manage materiality of error in the calculation of net asset value (NAV). This amendment aims to promote new entries of foreign investment companies or schemes into Japanese financial market.

In Japan, no rules or regulations on the materiality management are implemented; investment trust management companies uniquely develop, but do not make public, their own materiality policies, in which some companies set the materiality threshold as 0.5% of the NAV, whereas others as 0.3%. JPFSA has pointed out regulatory clarification of material policies for investment trusts as one of the major significant challenges to make financial regulations in Japan as advanced as the world's best practice. The US case, for example, is that while declining to establish a specific NAV error threshold as a regulatory standard, the Securities and Exchange Commission agree that relying upon the threshold generally utilized in the industry at \$0.01 a share or 0.5% of the NAV would not be unreasonable.

The supervisory viewpoints drafted are assumed to be applied to investment trust management companies which have developed materiality policy: set an appropriate level of NAV materiality threshold for the purpose of investor protection; ensure the commitment of management to develop and implement the policy with their understanding of its intent; disclose the basic idea of the materiality policy through media including the website; have in place the practice to fairly manage and review the calculation process, which is supposed to minimize errors in the calculation of NAV potentially taking place all the more often because of the implementing the materiality policy.

JPFSA in this proposal do not refer to any specific number of the NAV materiality threshold,

which allows the situation that the threshold varies by company so that trustees of investment trusts as administrator continuously have a lot of operational burden. Accordingly, fees for trustees of investment trusts are expected to remain high. Therefore, it would be uncertain whether this amendment in the Guidelines attract foreign investors to Japanese financial market. The consultation period ends on 13 May.

Supervisory Viewpoints on NAV Materiality Management

Investment trust management companies which have developed NAV materiality policy are required to the following:

- ✓ Set an appropriate level of NAV materiality threshold for the purpose of investor protection
- ✓ Ensure the commitment of management to develop and implement the policy with their understanding of its intent
- ✓ Disclose the basic idea of the materiality policy through media including the website
- ✓ Have in place the practice to fairly manage and review the calculation process