Fintech

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Preface

Fintech 2019
Third edition

Getting the Deal Through is delighted to publish the third edition of Fintech, which is available in print, as an e-book and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Getting the Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, Angus McLean and Penny Miller of Simmons & Simmons, for their continued assistance with this volume.

London
August 2018
Financial services regulation

1 Which activities trigger a licensing requirement in your jurisdiction?

- Engaging in the arrangement of investment deals or making arrangements with a view to transactions in investments in either case for an investment fund that invests mainly in financial instruments, comprises an ‘investment management business’ under the Financial Instruments and Exchange Act (FIEA), and registration is required.
- Engaging in the management of an investment fund that invests mainly in financial instruments also comprises investment management business under the FIEA regardless of whether such management is made as principal or agent, and registration is required.
- Giving advice on investments under a contract for a fee comprises ‘investment advisory business’ under the FIEA, and registration is required.
- Engaging in ‘banking business’ requires a banking licence under the Banking Act. ‘Banking business’ is defined as the acceptance of deposits or instalment savings, loan of funds (when conducted together with acceptance of deposits or instalment savings) or funds transfer service. Loan of funds, when not conducted with acceptance of deposits or instalment savings, is generally regarded as a ‘money-lending business’, which requires registration as a money lender under the Money Lending Business Act.
- If a factoring transaction is with recourse, such transaction can be deemed as a lending, and thus engaging in such transaction may require registration as a money lender under the Money Lending Business Act.
- Invoice discounting does not trigger a licensing requirement.
- Secondary market loan trading does not trigger a licensing requirement.
- Acceptance of deposits is prohibited without a banking licence under the Japanese Banking Act.
- Some foreign exchange trading (such as foreign exchange margin trading transactions, non-deliverable forwards, forward rate agreements) comprises ‘over-the-counter transactions of derivatives’ under the FIEA and registration is required.
- A bank may conduct funds transfer services with a banking licence. If not a bank, a registration under the Payment Services Act as a funds transfer service provider is needed before conducting payment services. Also, if the issuance of prepaid payment instruments is conducted, then under the Payment Services Act, registration is required (see question 15). If the payment service is provided as a later payment using a credit card, then registration under the Instalment Sales Act is required.

2 Is consumer lending regulated in your jurisdiction? Describe the general regulatory regime.

A lender conducting a consumer lending business (excluding the business of accepting deposits or instalment savings, which requires a banking licence under the Banking Act) has to register as a money lender under the Money Lending Business Act.

There is a limit on the total lending to any individual and a cap on the interest rate chargeable. The total lending limit is one-third of the borrower’s annual income and the cap is 15 to 20 per cent per annum depending on the amount of the loan. The money lender is required to appoint a chief of money-lending operations to each business office.

3 Are there restrictions on trading loans in the secondary market in your jurisdiction?

If a money lender transfers loan claims, the transferee will be subject to the same restrictions under the Money Lending Business Act that apply to the original money lender and the transferor must notify the operating transferee that those restrictions will also apply to the transferee. There is no such restriction for a bank under the Banking Act.

4 Describe the general regulatory regime for collective investment schemes and whether fintech companies providing alternative finance products or services would generally fall within the scope of any such regime.

The FIEA requires those who engage in either the acceptance of applications for shares for subscription in collective investment schemes or investment management of assets collected through such subscription or contribution, in principle, to register as a financial instruments business operator.

If a crowdfunding company raises funds for lending money to a company seeking funds through a form of silent partnership, an invitation to invest in the silent partnership would, in principle, be a collective investment scheme and so the crowdfunding company would need to be registered under the FIEA.

If an investor makes a direct investment in a silent partnership established with respect to a company seeking funds and receives a share in the silent partnership, dealing with the issuance of such a share could also be characterised as a collective investment scheme, subject to certain exceptions introduced in 2015.

Under such exceptions, a company that deals with a small fund-raising on the internet may register as Type I Small Amount Electronic Public Offering Business or Type II Small Amount Electronic Public Offering Business, and, if registered, some requirements that apply to financial instruments business operator will be mitigated.

5 Are managers of alternative investment funds regulated?

Managing funds as investments in assets such as real estate (excluding rights in relation to negotiable securities and derivative transactions) are not subject to the FIEA. As such, those activities are not regarded as being a financial instruments business.

6 May regulated activities be passported into your jurisdiction?

Japan is a member of the Asia Region Funds Passport (ARFP). The ARFP framework is intended to standardise mutual participation conditions for APEC member countries and regions signatory to the Memorandum of Co-operation on the establishment and implementation of the ARFP (the ARFP MoC) that meet certain requirements and offer funds (investment trusts and investment corporations) operated in accordance with the ARFP MoC. This will promote clarity and efficiency of registration standards in ARFP fund exporter countries (the home country) and authorisation procedures in ARFP fund importer countries (the host country).
When importing funds into Japan based on the ARFP MoC, the application procedure should be as follows if authorisation as an ARFP fund is made under the Financial Services Agency (FSA):

- the applicant (operator of the fund being imported into Japan) is required to establish an agent in Japan when exporting ARFP-registered funds from its home country. The agent shall submit to the Agent Association Member (defined in the Rules Concerning Foreign Securities Transactions (JSDA Rules) prescribed by the Japan Securities Dealers Association (JSDA)) copies of documentation certifying compliance with the ARFP rules issued by the home country and base documents for ‘the Statement of Notification of Dealing in Foreign Investment Trust Securities’, certificates relating to the fulfilment of selection criteria, and any other documentation deemed necessary by the JSDA (collectively, ‘the Statement of Notification of Dealing in Foreign Investment Trust Securities, etc’). The Agent Association Member should submit the Statement of Notification of Dealing in Foreign Investment Trust Securities, etc, to the JSDA after confirming the relevant fund satisfies the selection criteria;
- the JSDA should review the Statement of Notification of Dealing in Foreign Investment Trust Securities, etc, against the selection criteria of the foreign investment trust securities prescribed in the JSDA Rules, and notify the Agent Association Member of the result. The Agent Association Member receiving the result will inform the applicant’s agent of the result;
- the applicant’s agent will submit the Statement of Notification of Dealing in Foreign Investment Trust Securities, etc, and copies of documentation certifying compliance with ARFP rules issued by the home country to the FSA. The FSA confirms conformity as an ARFP fund based on the ARFP MoC, and notifies the agent of the result; and
- on receiving a notification from the FSA of the conformity with the ARFP requirements, the agent shall notify the FSA under the Act on Investment Trusts and Investment Corporations, either for foreign investment trusts or for foreign investment corporations.

7 May fintech companies obtain a licence to provide financial services in your jurisdiction without establishing a local presence?

It will depend on the nature of the services the fintech company will provide. Under the Banking Act, a foreign bank that wishes to engage in banking in Japan must obtain a licence by specifying a single branch office that will serve as its principal base for banking in Japan. To be registered as an electronic settlement agent (see question 15), foreign juridical entities must register a branch and a representative in Japan, and foreign individuals without an address in Japan must appoint an agent in Japan. Overseas money lenders cannot be registered under the Money Lending Business Act. To avoid an investor being required to be registered as a money lender under the act, market players must register a branch and a representative in Japan, and foreign individuals without an address in Japan must appoint an agent in Japan. Overseas money lenders cannot be registered under the Money Lending Business Act, provided that, for registration of an investment trust, the issue is, in many cases, whether or not registration as a financial instruments business is required under the FIEA.

8 Describe any specific regulation of peer-to-peer or marketplace lending in your jurisdiction.

A person who intends to engage in the business of lending money or acting as an intermediary for the lending or borrowing of money must be registered under the Money Lending Business Act. To avoid an investor being required to be registered as a money lender under the act, marketplace lending in Japan generally takes the form of a tokumai kumiai (TK) partnership, in which a registered operator collects funds from TK partnership investors, then advances the funds to enterprises as loans. The operator then receives principal and interest payments from the enterprises and distributes the funds as dividends and return of capital to investors. In this structure, the operator is required to be registered both as a money lender under the Money Lending Business Act (in order to provide the loans), and as a financial services provider under the FIEA in order to solicit TK partnership investors.

9 Describe any specific regulation of crowdfunding in your jurisdiction.

Crowdfunding in Japan is categorised as donation-based crowdfunding, reward-based crowdfunding and investment-based crowdfunding. Investment-based crowdfunding is further categorised as equity-based crowdfunding, fund-based crowdfunding and lending-based crowdfunding. See question 8 for regulation specific to lending-based crowdfunding.

Equity-based crowdfunding and fund-based crowdfunding are regulated under the FIEA, which defines certain internet-based solicitations and such as ‘electronic solicitation handling services’. Different rules apply to electronic solicitation handling services for certain non-listed securities, etc, from those that apply to ordinary solicitation handling services for securities. Special rules apply in particular when these electronic solicitation handling services are conducted entirely via a website, right through to application for the purchase of securities, referred to as ‘electronic purchase-type solicitation handling services’. In order to encourage new market entrants, requirements for the registration of electronic solicitation handling services handling the issuance of securities with less than ¥100 million in the issuance volume and with ¥500,000 or less in the investment amount per investor are relaxed.

Reward-based crowdfunding is regulated by the Specified Commercial Transactions Act, which, in particular, restricts advertising and gives consumers a cancellation right.

10 Describe any specific regulation of automated investment advice in your jurisdiction.

Specific regulations addressing automated investment advice itself have not yet been introduced. The required licences and permits for automated investment advice depends on the respective services that are provided. If the service provided is related to investment management, the issue is, in many cases, whether or not registration as a financial instruments business is required under the FIEA. Here are some illustrative examples of different ways that automated investment advice can be regulated differently:

- if the service is limited to providing advice relating to the value of securities, such as stocks and mutual funds (including exchange-traded foreign ETFs), then it is regulated as an investment advisory business;
- if the service involves entreatment with discretion to make investment decisions and authority necessary to make investments on behalf of clients by using a robo-adviser, then it is regulated as an investment management business; and
- if a service includes sales and purchases of securities or intermediary, introducing brokerage or agency services for entrustment of securities to be traded on the market as a business, then it is regulated as a Type I Financial Instruments Business.

As mentioned above, the requisite permits and licences depend on the nature of the services provided.

11 Describe any specific regulation of invoice trading in your jurisdiction.

If an entity engages in invoice trading in Japan, there are some legal and regulatory issues to note. If there is an agreement between a supplier and a buyer to prohibit the transfer of invoices, there is a risk that a funder cannot acquire invoices pursuant to the Civil Code. Further, there is also a risk that a supplier will sell its invoices to another party outside the trading platform in addition to a funder via the platform. To ensure that the funder obtains the invoices, the debt transfer must be perfected by the buyer being notified of or approving the transfer pursuant to the Civil Code, or it must be registered in the debt transfer registration system. The invoice-trading platform must not be detrimental to a supplier that is a subcontractor which is protected by the Act against Delay in Payment of Subcontract Proceeds, Etc to Subcontractors.

There is some invoice-trading business recourse for a supplier if there is no repayment from a buyer. If this is the case, the transaction
may be characterised as secured lending and thus the business would be required to obtain a money-lending business licence under the Money Lending Business Act.

12 Are payment services a regulated activity in your jurisdiction?
Payment services may fall within the scope of exchange transactions and therefore fall within the definition of banking business and require a banking licence under the Banking Act. Obtaining this licence is quite onerous and it is unlikely that a fintech company would be eligible for one.

Other exchange transactions are not defined in the Banking Act, but according to a precedent set by a Supreme Court decision, ‘conducting an exchange transaction’ means accepting a request from a customer to transfer funds using the mechanism of transferring funds between parties at a distance without actually transporting cash, or accepting and actually carrying out the request. If payment services, something that many fintech businesses are involved in, fall into this definition, the operator could be required to obtain a banking licence or register under the Payment Services Act.

While the Banking Act regulates exchange transactions, the Payment Services Act allows non-banks registered thereunder to engage in exchange transactions in the course of their business even if not permitted under the Banking Act, provided that the amount of each exchange transaction is not greater than $1 million.

The Payment Services Act also regulates prepaid payment instruments which are issued in exchange for the receipt of consideration corresponding to the amount recorded using electromagnetic means which can be used for the purpose of paying consideration for the purchase or leasing of goods or the receipt of provision of services from the person designated by the issuer. Prepaid payment instruments are sometimes used in peer-to-peer (P2P) payment platforms. The issuer could require registration or notification subject to the conditions provided by the Payment Services Act.

Recent amendments to the Banking Act requires a business operator providing payment initiation services to be registered as an electronic settlement agent (see question 15).

13 Do fintech companies that wish to sell or market insurance products in your jurisdiction need to be regulated?
Yes. In Japan, when a fintech company carries out any of the following, it must register as an insurance agent as such actions correspond to ‘insurance solicitation’ under the Insurance Business Act: (i) soliciting the conclusion of insurance contracts; (ii) providing explanations of insurance products for the purpose of soliciting the conclusion of insurance contracts; and (iii) accepting applications for insurance contracts; or (iv) acting as an intermediate or agent for the conclusion of other insurance contracts.

Providing information on prospective customers to insurance companies and insurance agents without recommending or explaining insurance products, and the mere reprinting of information from insurance companies and insurance agents where the service’s main purpose is to provide product information, such as comparison sites, do not in themselves constitute ‘insurance solicitation’; however, these acts are ‘solicitation related acts’, and insurance companies and insurance agents who entrust such acts to other persons have an obligation to manage and supervise those persons to ensure that they do not violate insurance offering regulations.

14 Are there any legal or regulatory rules in your jurisdiction regarding the provision of credit references or credit information services?
In general, while credit references of individuals are subject to the Act on Protection of Personal Information, credit references of corporations are subject to confidentiality obligations under financial services regulations and confidentiality agreements between financial institutions and corporates.

In Japan, personal credit information agencies collect information on the ability of persons to make credit repayments and provide such information to financial institutions which are members of such agencies. Financial institutions using credit information services of such agencies may not use information on the ability of individuals to meet repayments (‘personal credit information’), which is part of the financial information provided by personal credit information agencies, for purposes other than the investigation of the ability of fund users to make repayments.

In addition, under the FSA guidelines, when financial institutions provide personal information to personal credit information agencies, they must state to their customers that they provide personal information to personal credit information agencies and obtain the consent from the customers.

The FSA’s guidelines that regulate personal credit information agencies require that they ensure that their member financial institutions appropriately obtain and record personal credit information via such agencies, and that it is not used for purposes other than the investigation of the subject’s repayment ability. To that end, personal credit information agencies are required to take measures such as screening a financial institution’s qualifications at the time it applies for membership, monitoring of members, and the imposition of sanctions for the improper use of personal credit information.

15 Are there any legal or regulatory rules in your jurisdiction that oblige financial institutions to make customer or product data available to third parties?
Yes. In order to encourage financial institutions to make customer data available to third parties, recent amendments to the Banking Act came into force on 1 June 2018. Under the amendments, the FSA will develop a registration system for electronic settlement agents providing payment initiation services and/or account information services, which is expected to be simpler than the existing system applicable to funds transfer service providers, to promote innovation and ensure user protection. In addition, the FSA is attempting to improve the current situation where it is extremely difficult for fintech companies using open application programming interface (API) to share data or revenue with banks due to restrictions on bank agency businesses. The FSA’s main aim is to enhance the effectiveness of open API by encouraging banks to develop their API systems and prohibiting discriminatory treatment among service providers. Discussions on the subject within the FSA are focused on the development of an open API-friendly environment in which, although fintech companies will still be subject to a registration system, will require the reorganisation of existing regulations and the development of systems by participating financial institutions.

16 Does the regulator in your jurisdiction make any specific provision to encourage the launch of new banks?
No.

17 Describe any specific rules relating to notification or consent requirements if a regulated business changes control.
The conclusion will vary according to the applicable regulatory law; examples include:

In the case of a bank’s shareholders, a shareholder holding more than 5 per cent but less than 20 per cent of the bank’s shares (which is referred to as a ‘Major Holder of Voting Rights in a Bank’) is required to notify to the FSA (i) when it acquires more shares; or (ii) when there is a change in its percentage holding. Moreover, a shareholder who will have actual power to influence the bank’s management (such as an individual or a group of shareholders intending to hold 20 per cent or more of the shares) (referred to as a ‘Bank’s Major Shareholder’), must obtain authorisation from the FSA to acquire such a shareholding. Further, the FSA has, in certain circumstances, the authority to request that a shareholder who holds 50 per cent or more of the voting rights in a bank (referred to as a ‘Bank’s Controlling Shareholder’) submits an improvement plan for ensuring soundness in the bank’s management. If the Bank’s Controlling Shareholder changes an improvement plan that has been submitted; or issues orders with respect to measures necessary from a supervisory perspective.

Similar major shareholder regulations are imposed on Type 1 Financial Instruments Business and investment management business. Under these regulations, a person that has become a major shareholder (in principle, person holding 20 per cent or more of the voting rights) of a Type 1 Financial Instruments Business and/or investment management business, is required to submit a notification of holdings in voting rights to the director-general of the relevant local finance bureau, which states, among other things, (i) the percentage of voting rights held; and (ii) the purposes for holding such shares, etc, immediately after becoming a major shareholder. Similar notification is also required when a
major shareholder ceases to be a major shareholder. This regulation is less onerous than the major shareholder regulations applicable to banks.

Virtual currency exchange services providers are required to submit their shareholder registry to the Director-General of the relevant local finance bureau at the time of applying for registration, and to update the shareholder registry thereafter on a change in its major shareholder(s) (ie, in this case, a person holding 10 per cent or more of the voting rights).

18 Does the regulator in your jurisdiction make any specific provision for fintech services and companies? If so, what benefits do those provisions offer?

In December 2015, the FSA set up a ‘fintech support desk’ to provide a unified response to handle enquiries from the private sector and to exchange information regarding the fintech industry. This desk fields enquiries from a wide range of businesses operating or considering various fintech-related innovations, and specific business-related matters regarding the finance aspects of these plans. It also actively seeks public opinion, requests and proposals, and actively shares general information and opinions in relation to fintech innovation.

In September 2017, the FSA established the FinTech PoC (Proof-of-Concept) Hub to accelerate business operators’ challenge to innovation using financial technology. The Hub will offer continuous support in cooperation with other relevant authorities as necessary by forming a special working team within the FSA for each selected PoC project. There have been three PoC projects so far.

The Act of Special Measures for Productivity Improvement was promulgated on 23 May 2018. This new Act seeks to establish a ‘regulatory sandbox’ to develop an environment in which businesses are able to conduct demonstration tests and pilot projects for new technologies and business models, such as AI and IoT, which are not envisaged under existing regulations, with a limited number of participants and predetermined implementation periods. This environment will allow businesses to conduct pilot projects and demonstration tests quickly and collect data that may contribute to regulatory reforms.

19 Does the regulator in your jurisdiction have formal relationships or arrangements with foreign regulators in relation to fintech activities?

On 9 March 2017, the FSA announced that it had exchanged letters with the UK’s FCA on a cooperation framework to support fintech companies. This arrangement provides a regulatory referral system for innovator businesses from Japan and the UK seeking to enter the other’s market. The arrangement also encourages the regulators to share information about financial services innovation in their respective markets, reduce barriers to entry in a new jurisdiction and further encourage innovation in both countries.

On 13 March 2017, the FSA announced that it had established a framework with the Monetary Authority of Singapore (MAS) to enhance fintech links between Japan and Singapore. The framework enables the FSA and the MAS to refer fintech companies in their country to the other’s markets, and outlines how the referred companies can initiate discussions with the regulatory bodies in the respective jurisdictions and receive advice on their regulatory frameworks. The framework also sets out how the regulators plan to share and use information on financial services innovation in their respective markets.

20 Are there any local marketing rules applicable with respect to marketing materials for financial services in your jurisdiction?

There are a number of important rules in relation to marketing materials for financial services. For example, the following financial services require licences under the respective laws listed, and these laws regulate the content and manner of advertisements conducted by firms licensed for those services:

- banking services – the Banking Act;
- services related to securities or derivatives (including securities offering (such as crowdfunding), investment management or advisory services) – the FIEA;
- lending-related services (to the extent not banking businesses) – the Money Lending Business Act;
- funds transfer service – if allowed as an exemption from regulation under the Banking Act by operating the businesses under a fund transfer service provider licence to the extent not exceeding limit of the amount for transfer – the Payment Services Act;
- credit card issuing services, merchant acquiring services, acquirer’s agency services – the Instalment Sales Act;
- prepaid card issuing services – the Payment Services Act; and
- insurance services – the Insurance Business Act.

Although details of the regulations vary among the above laws, generally speaking, they require that advertisements include certain information, such as names, licence numbers and contact information of the licensed firms, as well as certain other information that is specifically set out in the respective laws as being important to the customer in its decision-making, and also stipulate other matters regarding the form of any advertisement, such as minimum font size, among others.

In addition, the Specified Commercial Transactions Act sets forth certain requirements regarding advertisements for services provided by mail or online-order systems (whether a cooling-off period applies, etc). It is currently proposed by the government that the Consumer Protection Act be amended to regulate ‘annoying’ advertisements via email or internet (eg, pop-up messages warning of virus infection that cannot be closed until the user subscribes to the anti-virus software).

21 If a potential investor or client makes an unsolicited approach either from inside the provider’s jurisdiction or from another jurisdiction, is the provider carrying out a regulated activity requiring a licence in your jurisdiction?

Yes.

22 If the investor or client is outside the provider’s jurisdiction and the activities take place outside the jurisdiction, is the provider carrying out an activity that requires licensing in its jurisdiction?

As long as the banking corporation or securities firm that provides the service is a company established under the laws of Japan (or the Japanese branch of a foreign banking corporation), then yes. For example, if a Japanese company provides investment advice to a person outside Japan, the company is required to be registered under the FIEA. As long as the banking corporation or securities firm that provides the service is a company established under the laws of a foreign jurisdiction (and without an office or branch in Japan), it is generally understood it will not require a licence in Japan.

23 Are there continuing obligations that fintech companies must comply with when carrying out cross-border activities?

In addition to licensing requirements, fintech companies must comply with various obligations applicable to the specific business. For example, banks, securities firms and certain other businesses are required to verify the identity of customers when facilitating cross-border transactions.

Distributed ledger technology

24 Are there any legal or regulatory rules or guidelines in relation to the use of distributed ledger (including blockchain) technology in your jurisdiction?

Other than rules applicable to virtual currencies (see question 25), there are no legal or regulatory rules or guidelines specifically applicable to the use of distributed ledger (including blockchain) technology in Japan, though it is necessary to consider legal issues based on existing laws and regulations. Some self-regulating organisations are considering what kind of guidelines for use of distributed ledger technology they should have; however, at present, there are no guidelines that may be relied upon by operators in the field.

Digital currencies

25 Are there any legal or regulatory rules or guidelines applicable to the use of digital currencies or digital wallets, including e-money, in your jurisdiction?

The Payment Services Act is the principal law regulating the use of digital currencies or digital wallets. Digital currencies or digital wallets (IC-type, server-type, or otherwise) may be categorised as ‘prepaid payment instruments’ under...
the Act. An issuer of prepaid payment instruments ‘for own business’ (ie, prepaid payment instruments that can only be used for the purpose of paying consideration for certain types of transactions with the issuer of the instruments, or those who have a close relationship with the issuer) is required to file a written notification with the local finance bureau when the total amount of the unused balances (the ‘unused base date balance’) arising from all such instruments exceeds ¥10 million on 31 March and 30 September (and, in certain exceptional cases, 30 June and 31 December) of any year.

Only a corporation that is registered with the relevant regulatory authority may issue prepaid payment instruments that are ‘for own business’.

An issuer of prepaid payment instruments (whether instruments ‘for own business’ or not) that does not comply with these requirements will be liable to criminal punishment. An issuer of prepaid payment instruments that has filed the written notification or is registered is also subject to other requirements (eg, when the unused base date balance exceeds ¥10 million, the issuer must make a security deposit in an amount equivalent to at least half the amount of the unused base date balance).

Virtual currencies such as bitcoin are not be categorised as ‘prepaid payment instruments’. Businesses engaged in the sale and purchase of, or certain other transactions in, virtual currencies may be categorised as ‘virtual currency exchange operators’. Those permitted to engage in such businesses are limited to (i) stock companies under Japan’s Companies Act; and (ii) foreign companies that have a business office in Japan which has an individual domiciled in Japan as its representative in Japan, and which carry out that business in the course of trade in a foreign jurisdiction under a registration that is equivalent to the registration under the Payment Services Act pursuant to the provisions of laws and regulations of that foreign jurisdiction equivalent to that Act. No person may engage in a ‘virtual currency exchange operator’ business unless registered with the relevant regulatory authority. A person who operates a business as a registered virtual currency exchange operator who does not comply with these requirements will be liable to criminal punishment.

In addition to the requirements above, both issuers of prepaid payment instruments who filed the written notification or are registered, and registered virtual currency exchange operators, must comply with other applicable laws, such as requirements for confirming the personal identity of customers, for compiling and retaining personal identification records and transaction records, and for notifying the authorities of suspicious transactions under the Act for Prevention of Transfer of Criminal Proceeds (see question 31).

26 Are there any rules or guidelines relating to the operation of digital currency exchanges or brokerages in your jurisdiction?

The Payment Services Act regulates the operation of digital currency exchanges or brokerages in Japan. The FSA is developing administrative guidelines related to virtual currency exchange service providers. These administrative guidelines were originally prepared in order to clarify the regulatory perspective of the FSA in cases where the FSA supervises virtual currency exchange services providers. However, in practice, they are obligatory guidelines for individual virtual currency exchange service providers to comply with. These administrative guidelines require that individual virtual currency exchange service providers (a) institute an implementation plan for compliance with applicable laws and regulations (‘compliance programme’) and a code of conduct (code of ethics, compliance manual); and (b) properly implement several measures, such as know-your-customer procedures, and anti-money laundering measures, from the perspective of ‘appropriateness of the service’. The guidelines also require that the service providers:

- consolidate a system for providing explanations and information to clients in accordance with the nature of the virtual currencies handled and such clients’ trading posture;
- consolidate a system-risk management structure; and
- properly implement the supervision, management and monitoring of outsourced contractor, from the perspective of ‘administrative operations’.

27 Are there legal or regulatory rules or guidelines in relation to initial coin offerings (ICOs) or token generating events in your jurisdiction?

At present, clear rules and guidelines have not been introduced for ICOs (see ‘Update and trends’). It appears that the FSA categorised ICO tokens into security tokens and other tokens, including utility tokens. The regulatory regime will differ depending on the categorisation of the token.

Virtual currency type

When the token (i) can be used for the purpose of paying consideration for the purchase of goods or services to unspecified persons, and can be exchanged with fiat currency with unspecified persons acting as counterparties, or (ii) can be mutually exchanged with another virtual currency with unspecified persons acting as counterparties, it falls under the virtual currency type (see question 25 regarding the concept of virtual currency), and thus the provision of the token by its issuer will fall under either ‘sale of virtual currency’ or ‘exchange of virtual currency for another virtual currency’. When a business is engaging in this activity, it is required to register as a virtual currency exchange services provider.

Security token type

The security token holder is entitled to receive a distribution of the profits made from the projects operated using the proceeds/funds collected through issuance of a token. Where the token can be purchased by fiat currency, or virtual currency, which is deemed as a purchase by fiat currency, the token falls under collective investment scheme; the issuer’s solicitation of the token acquisition will be a financial instruments business (Type II Financial Instruments Business); and registration as such is required under the FIEA.

Characteristics of tokens

ICOs are classified in terms of the rights granted to token holders. In addition to the FSA’s classification mentioned above, there may be tokens that could fall under ‘prepaid payment instruments’ (see question 25 regarding the concept of ‘prepaid payment instruments’). In that case, depending on whether the tokens are ‘prepaid payment instruments for own business’ or ‘prepaid payment instruments for a third-party’s business’, the issuer will either be required to file a notification (when the unused base date balance of its prepaid payment instruments for own business exceeds a specific amount) or register. It is also necessary to provide a security deposit when issuing tokens categorised as ‘prepaid payment instruments type’.

Securitisation

28 What are the requirements for executing loan agreements or security agreements? Is there a risk that loan agreements or security agreements entered into on a peer-to-peer or marketplace lending platform will not be enforceable?

For loan agreements, pursuant to the Interest Rate Restriction Act, interest plus lending-related fees must generally not exceed 15 per cent per annum; an agreement by a borrower to pay interest or fees (or both) would be void to the extent exceeding the limit. Regarding security agreements, a principle under the Civil Code is that a security interest grantees must be the holder of the secured obligation. This means that it would be difficult to adopt a structure in which a single security agreement is entered into by and between a security grantor and a single security grantee (eg, a security agent) to secure loans provided and held by multiple investors. Solutions for this issue can include: a lending platform provider receiving funds as a borrower from investors as lenders and then turning around and providing loans to target businesses in its own name; or multiple investors becoming direct lenders to target businesses, a ‘parallel debt’ corresponding to the loans being created and granted to the platform provider, with a security interest being granted to the platform provider to secure the parallel debt. The latter approach is, however, not well tested in P2P or marketplace lending practice so far.

Under Japanese law, a blanket security arrangement covering all types of assets to be provided as collateral is not available; a separate security agreement is needed to be executed to create a security interest per asset. Typically, these might include a real estate mortgage,
share pledge, pledge or security assignment of patents, trademarks, security assignment of trade receivables, security assignment of inventories, among others.

Methods of perfection of security interests differ depending on the asset. The following are some examples:

- real estate mortgage – registration;
- pledge – receipt and holding of share certificates;
- pledge or security assignments of patents or trademarks – registration;
- security assignment of trade receivables – notice to or acknowledg- edgement by debtors by a letter with a fixed date stamp on it, or registration; and
- security assignment of inventories – notice to or acknowledg- edgement by debtors with an affixed date stamp on it, or registration.

There are no particular general requirements (such as use of ‘deeds’ and such like) under Japanese law for the execution of loan agreements and security agreements; how a Japanese party executes such an agreement would need to be examined in each case. Given these complexities, experienced legal counsel should be sought before starting up a P2P lending platform in Japan.

29 What steps are required to perfect an assignment of loans originated on a peer-to-peer or marketplace lending platform? What are the implications for the purchaser if the assignment is not perfected? May these loans be assigned without informing the borrower?

Perfection of assignment of a loan originated on a P2P lending platform would most likely be made by notice to or acknowledgement by the borrower by a letter with an affixed date stamp on it. If the assignment is not perfected, the borrower can be discharged from the loan by repayment to the loan assignor, and a third party that obtains an interest in the loan after the assignment (eg, a tax authority seizing the loan to collect tax from the loan assignor or a bankruptcy receiver of the loan assignee) can assert a position prioritised over the loan assignee.

These loans may be assigned by an agreement between an assignor and an assignee (where informing the borrower is not required) unless assignments are contractually restricted by an agreement between the assignor and the borrower, where the borrower’s waiver of the restriction is required for the assignment.

Regarding perfection, the method of perfection as an alternative to a notice to or acknowledgement by a borrower is a registration of the assignment with a legal affairs bureau. Once an assignment is registered, the assignment is perfected against a third party (without informing the borrower), and the borrower must be notified only at the time of the assignee demanding or receiving a payment (the notice must be made by delivering a certificate of the registration).

30 Will the securitisation be subject to risk retention requirements?

The supervisory guidelines prepared by the FSA provide for the application of risk retention requirements for financial institutions handling deposits, such as banks, insurance companies and securities companies (banks, etc) when the banks, etc are handling securitised financial products. (Note: The FSA’s supervisory guidelines are given the status of a manual for the internal use of FSA staff responsible for administrative supervision, but they are also made public and, in practice, financial institutions are required to observe these guidelines.)

Under the risk retention requirements:

(i) when banks, etc invest in securitised products, they are required to confirm that the originator continues to hold a certain portion of the risk in the underlying asset; and

(ii) in cases where the originator does not continue to hold such a risk of the underlying asset, the banks, etc, are required to closely scruti-nise the involvement of the originator in the underlying asset, and the quality of the underlying asset.

Under the risk retention requirements, an originator is expected to retain the risk. However, such supervisory guidelines are applicable only to banks, etc, rather than the originator. Also, under the risk retention requirements, the compulsory obligation to continuously hold a portion of the risk of the securitised product is not imposed upon the originator, but, instead, (i) and (ii) above are required by banks, etc, that are investing in such securitised products. Accordingly, even in cases where risk retention is not maintained by the originator, the bundling and acquisition of securitised products itself is not forbidden, and by carrying out close scrutiny of the involvement of the originator in the underlying asset, and the quality of the underlying asset, banks, etc, are permitted to bundle or acquire the securitised products.

Also, under the supervisory guidelines, there are no provisions regarding the risk posture that the originator should have regarding securitised products, nor is there a specific risk retention ratio that the originator must hold continuously.

31 Would a special purpose company for purchasing and securitising peer-to-peer or marketplace loans be subject to a duty of confidentiality or data protection laws regarding information relating to the borrowers?

A special purpose company (SPC) is subject to the Personal Information Protection Act regarding personal information of individuals in relation to borrowing. This is Japan’s main data protection law. The SPC may also be subject to a confidentiality obligation to the borrowers.

Intellectual property rights

32 Which intellectual property rights are available to protect software, and how do you obtain those rights?

Both copyright and patent protections are available for software. Software may be registered as a patent under the Patent Act if it can be deemed as a ‘computer program, etc’, which means a computer program or any other information that is to be processed by an electronic computer equivalent to a computer program. Registration as a patent (a prerequisite to receiving patent rights) takes time because the Patent Office conducts a detailed examination of the application. However, copyright protection is available without registration in the case of software that includes thoughts or sentiments expressed creatively; these rights can also be registered through the Software Information Center.

33 Is patent protection available for software-implemented inventions or business methods?

Business methods may be registered as patents in Japan if the method can be demonstrated to be a new ‘highly advanced creation of technical ideas utilising the laws of nature’. However, the requirements for business method patent registration are stringent, and, as a practical matter, even once registered, the methods can often be reasonably easily imitated without infringement by sidestepping the patent. For these reasons, business method patent applications are rare. In practice, business methods are commonly protected through trademarks used in association with the methods and through a web of licensing and other agreements.

34 Who owns new intellectual property developed by an employee during the course of employment?

The Patent Act allows an employer to acquire the right to obtain a patent for an employee’s invention created in the course of employment from the time that the invention is created, either by prior agreement with the employee, or by prior inclusion of the right in its employment regulations and such like. Any assignment by the employee of its right of a patent to a third party in breach of the employer’s rights is invalid.

The Copyright Act stipulates that where a computer program is created by an employee in relation to the business of the employer (if a legal entity), on the initiative of the employer, then the authorship of the program is attributed to the legal entity unless otherwise stipulated by contract, employment regulations or the like at the time of the creation of the work.

35 Do the same rules apply to new intellectual property developed by contractors or consultants? If not, who owns such intellectual property rights?

Contractors and consultants can acquire the right to obtain a patent or copyright for inventions developed by them unless the engagement
contract provides for the acquisition of such intellectual property or licenses by the client; the contract can be agreed either before or after the invention is created or the computer software is made.

36 Are there any restrictions on a joint owner of intellectual property’s right to use, license, charge or assign its right in intellectual property?

When a patent is jointly held, each of the joint owners may independently use the patent and seek damages or injunctions against infringing third parties. However, the sale or licensing of the patent requires the consent of the other joint patent holders.

When a copyright is jointly held, each of the joint owners may seek damages or injunctions from infringing third parties. The consent of other joint copyright holders is required for the licensing, and use by third parties of the copyrighted work.

37 How are trade secrets protected? Are trade secrets kept confidential during court proceedings?

Trade secrets are protected under the Unfair Competition Prevention Act. A trade secret under the act is a production method, sales method, or any other technical or operational information useful for business activities that is controlled as a secret and is not publicly known. Separately from the legislation itself, administrative principles for interpretation of the Unfair Competition Prevention Act provide a flexible interpretation of what constitutes control which will most likely impact future judicial rulings on the point. For example, the principles can be read as stipulating that strict restriction of access to information is not a prerequisite of control.

During court proceedings for the infringement of business interests by unfair competition, trade secrets may be protected by protective order based on the Unfair Competition Prevention Act or an order with respect to Restriction on Inspection, etc., for Secrecy Protection in Protection based on the Civil Procedure Act.

38 What intellectual property rights are available to protect branding and how do you obtain those rights?

Brands are usually protected by trademark. It is necessary to register a trademark with the Patent Office in order to enjoy protection as a trademark, although in some cases protection may also be available under the Unfair Competition Act for brands that are not registered as a trademark. Causing confusion between one’s own products or services and those of another party (known as the ‘act of causing confusion’) or wrongly using a famous indication of another person as one’s own, by displaying the name of a well-known product, etc., of another party on similar or identical products, etc., is prohibited. However, these cases are less successful than trademark cases because it must be proven that the product or indication is well known or famous.

39 How can new businesses ensure they do not infringe existing brands?

It is relatively easy to look up whether a brand is a registered trademark or a registered trade name. Registered trademarks can be looked up at www3.j-platpat.inpit.go.jp/cgi-bin/TF/TF_AREA_E.cgi?1470219995846. (Registered trade names can also be searched online.)

Some attorneys and most patent attorneys are accustomed to doing these searches.

40 What remedies are available to individuals or companies whose intellectual property rights have been infringed?

A patent holder or the exclusive licensee or copyright holder can claim for actual damages (but not punitive damages) from the infringer for losses incurred as a consequence of the infringement. The court can also be requested to issue an injunction order or take similar action.

In the case of injunctions, the requirements are the presence of protected rights and circumstances whereby an injunction is necessary to avoid irreparable damage. Japanese courts will require the claimant to post a security deposit before injunctive relief is ordered.

Although injunctive relief can expedite dispute resolution, Japanese courts, in principle, will not issue ex parte orders and will have one or more hearings to hear the arguments from both parties, which means both parties will be called to the hearings.

41 Are there any legal or regulatory rules or guidelines surrounding the use of open-source software in the financial services industry?

There are no specific legal or regulatory rules or guidelines surrounding the use of open-source software.

Data protection

42 What are the general legal or regulatory requirements relating to the use or processing of personal data?

The Personal Information Protection Act applies to the handling and processing of data including personal information. The My Number Act sets out rules regarding the handling of numbers under the My Number system, which is used for tax and administrative procedures relating to employment. The Personal Information Protection Act and the My Number Act stipulate different requirements for entities in particular industries. Detailed guidelines for some industries, such as telecommunications, finance and healthcare, have been issued, and the guidelines for the fintech industry are described in question 43.

43 Are there legal requirements or regulatory guidance relating to personal data specifically aimed at fintech companies?

The Personal Information Protection Committee and the FSA have set out guidelines in relation to the Personal Information Protection Act, the ’Guidelines for Personal Information Protection in the Financial Field’, which set out guidelines for the treatment of sensitive information, restrictions based on the purpose of use, supervision of trustees, among others, and ’Practical Guidelines for the Security Policies Regarding the Personal Information Protection in the Financial Field’. The entities regulated under the Instalment Sales Act must comply with the ’Guidelines Regarding Personal Information Protection Regarding Credit Among Economic Industry’. The ’Guidelines for the Proper Handling of Specific Personal Information in the Finance Industry’ apply to the My Number Act in the financial field.

44 What legal requirements or regulatory guidance exists in respect of anonymisation and aggregation of personal data for commercial gain?

Amendments to the Personal Information Protection Act added the concept of ‘anonymised personal information’, which is information regarding individuals, obtained by anonymising personal information or otherwise processing personal information so that it is no longer able to identify the particular individual. When processing anonymised personal information, it is necessary to release to the public the items regarding such anonymised personal information that have been created. When providing anonymised personal information to a third party, it is necessary to specify publicly the kinds of information that are provided to the third party, and inform the third party that the personal information is anonymised. Creators of anonymised personal information are prohibited from disclosing deleted items, methods of processing, or referencing the anonymised information against other information for the purpose of identifying the person related to the personal information used in the creation of the anonymised information, and the recipient is prohibited from acquiring such deleted items, methods of processing and references.

A recent amendment to the Banking Act stipulates that entities (such as fintech companies) that acquire bank account information in digital form from banks by electronic means are required to register with the FSA. In addition, under the amendment and in order to acquire such information from banks, such entities must enter into contracts with the supplying banks that contain clauses stipulated in the amendments before the grace period. Most of such entities have yet to enter into contracts with banks containing these provisions, and many fintech companies may find it difficult to obtain the banks’ approval to do so.

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45 Are there legal requirements or regulatory guidance with respect to the outsourcing by a financial services company of a material aspect of its business?

With regard to outsourcing by banks, it is required that specified measures be taken to ensure that the provider of the outsourced services has the capability to carry out such services accurately, fairly and efficiently in accordance with the nature of the services outsourced; and to ensure the necessary and proper supervision, and such like, of the service provider of the outsourced services.

Similarly, with regard to outsourcing by virtual currency exchange service providers, depending on the nature of the services outsourced, it is required that (i) measures be taken to ensure that the provider of the outsourced services has the capability to carry out the services properly and reliably; (ii) measures be taken to ensure the necessary and proper supervision of the provider of the outsourced services, and such like, through confirmation of, both regularly and whenever necessary, how the provider of the outsourced services is actually implementing the relevant services, and (iii) other measures to be predetermined.

A risk-based approach and an IT governance framework were adopted with regard to the security management measures for outsourced information systems in the Report of the Council of Experts on Outsourcing in Financial Institutions issued in June 2016 by the Center for Financial Industry Information Systems (FISC).

Further, in June 2017, the FISC suggested that when banks open their API with an eye to cooperating with fintech firms, in certain cases the responsibility for safety measures imposed upon fintech firms at the request of financial institutions may be less onerous than that imposed upon providers of outsourced services.

46 How common is the use of cloud computing among financial services companies in your jurisdiction?

The use of cloud computing is relatively widespread among major financial institutions and internet banks. In contrast, many small and medium-sized financial institutions are struggling to make use of cloud computing due to a lack of IT manpower and concerns over cybersecurity.

However, the ‘FISC Security Guidelines on Computer Systems for Banking and Related Financial Institutions’ (FISC Guidelines) were revised in March 2013. This revision was intended to spread the use of cloud computing, and the FISC has correspondingly promoted the use of cloud services, so it is likely that more financial institutions will come to use cloud computing more extensively.

47 Are there specific legal requirements or regulatory guidance with respect to the use of cloud computing in the financial services industry?

The Banking Act and other legislation stipulates that financial institutions are obliged to carry out safety measures for their systems, among other things. Based on such provisions, subordinate rules, guidelines, and inspection manuals describe the actions to be taken to comply with these obligations.

If inspectors find problems with an organisation’s risk management systems in relation to information security they can require that the business be inspected further for conformity to the ‘FISC Security Guidelines on Computer Systems for Banking and Related Financial Institutions’. These financial institutions therefore see these guidelines as a kind of regulation. The Report of the Council of Experts on the Usage of Cloud Computing by Financial Institutions serves as a useful reference as it formed the basis of the revision of the above-mentioned guidelines.

48 Are there specific legal requirements or regulatory guidance with respect to the internet of things?

There is no specific legal requirement and regulatory guidance with respect to the internet of things.

Tax

49 Are there any tax incentives available for fintech companies and investors to encourage innovation and investment in the fintech sector in your jurisdiction?

There are no tax incentives introduced especially for fintech companies. However, as of June 2018, there are some more general tax incentives available to fintech companies and investors, as follows:

- Individual investors who invest in qualified small to medium-sized companies (start-ups) can deduct one of the following under certain conditions:
  - the amount invested in the start-up minus ¥2,000 from taxable income (maximum deduction is 40 per cent of total taxable income or ¥10 million, whichever is lower); or
  - the whole amount invested in the start-up from capital gains (there is no maximum amount).
- If individuals investing in a qualified unlisted start-up have a capital loss after the sale of shares in the start-up, then such individuals can offset this against other capital gains and the losses can be carried forward for up to three years.
- Companies may elect to claim accelerated depreciation of the acquisition cost or a tax deduction if they purchase certain equipment under certain conditions.
Until March 2019, 14 per cent (17 per cent for small to medium-sized corporations) of qualified research and development (R&D) expenses are deductible from annual corporate tax. Those rates will become 8 per cent to 10 per cent (12 per cent for small to medium-sized corporations) from April 2019. Additional tax incentives are available for special, qualified R&D expenses, among others.

**Financial crime**

51 Are fintech companies required by law or regulation to have procedures to combat bribery or money laundering?

Two recent amendments have been made to the Act on Prevention of Transfer of Criminal Proceeds. The first, which came into force in October 2016, includes treating transactions between politically exposed persons as high-risk transactions. The second amendment, which came into force in April 2017, requires virtual currency exchange operators to confirm the personal identity of customers, to compile and retain personal identification records and transaction records, and to notify the authorities of suspicious transactions. Also, under the Payment Services Act, virtual currency exchange operators must submit annual reports on their businesses and quarterly reports on management of customers’ assets to the regulator and the regulator has the right to conduct on-site inspection and to issue business improvement orders. These requirements and powers in effect require virtual currency exchange operators to combat bribery and money laundering.

52 Is there regulatory or industry anti-financial crime guidance for fintech companies?

No.

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**Competition**

50 Are there any specific competition issues that exist with respect to fintech companies in your jurisdiction or that may become an issue in future?

Earlier this year, the Japanese government started discussions on whether to regulate large IT companies’ unfair trade practices; the direction of these discussions will be announced by the end of 2018.