

# Financial Services



The Financial Services Working Group of the Japan-U.S. Business Council and the U.S.-Japan Business Council endorse collective actions in five areas: *Maintaining a Healthy Financial System, Realizing a Sustainable Society, Advancing International Cooperation in Finance, Promoting Digital Financial Innovation, and Securing a Brighter Future.*

## 1. Maintaining a Healthy Financial System

### Level Playing Field

The Councils embrace innovation and the healthy introduction of new financial products and services both by incumbent players and new entrants.

At the same time, the lines between traditional and new financial products — as well as between traditional financial institutions and tech-focused newer entrants — are becoming increasingly blurred. We urge supervisory authorities to be vigilant as technologies rapidly advance. For competition and innovation to thrive in finance under the principle of a level playing field, it is essential that governments and authorities evaluate a product's potential impacts on consumers and the financial system when assessing the appropriate regulations and standards to apply.

### Regulatory Coherence

Regulatory fragmentation has been exacerbated by strategic, environmental, and technological developments that have motivated national governments to act before international best practices can be established. In this environment, it is critical that the U.S. and Japanese governments align on the development of appropriate regulations that are coordinated, strike the right balance between global consistency and local relevance, and move us toward financial regulatory coherence. The Councils believe an institutionalized approach should be implemented, as in the formation of other bilateral financial regulatory fora. Such a step would be a natural progression and a work product that can be produced by the ministerial Japan-U.S. Economic Policy Consultative Committee (the Economic "2+2") and the "Japan-U.S. Competitiveness and Resilience (CoRe) Partnership" created by the leaders of the two countries at their meeting in January 2022.

### Careful Consideration in the Review of Financial Regulation and Supervision

The stress of regional bank failures in the U.S. in March 2023 highlighted the vulnerabilities of selected individual financial institutions, but the global financial system has shown itself to be more resilient due to the regulatory reforms implemented following the Global Financial Crisis in 2008, as reaffirmed at the recent G7 Finance Ministers and Central Bank Governors' Meeting 2023. Both Councils support the efforts of international financial regulatory agencies such as the FSB to carry out ongoing analysis of recent events to derive their causes and implications. Measures towards the improvement of future regulation and supervision should be carefully calibrated in their breadth and scope based on this analysis.

## 2. Realizing a Sustainable Society

### Appropriate Evaluation of the Initiatives of Financial Institutions

The importance of transition finance was reaffirmed at the G7 Hiroshima Summit, and there is a growing international understanding of its significance. Financial institutions are expected to support companies' efforts towards decarbonization through transition finance and similar initiatives. However, there is a concern that the efforts of financial institutions that are actively supporting decarbonization through transition finance are not currently evaluated under a consistent set of rules for measuring and disclosing financed emissions. Both governments should establish a framework for appropriately evaluating investments and loans aimed at achieving net zero emissions.

### Promotion of Blended Finance

In order to further attract private investment towards the realization of Green Transformation, it is of utmost importance for public institutions, including multilateral development banks (MDBs), export-import banks, aid programs, and others, to establish a Blended Finance framework through measures such as assuming risks that cannot be fully covered by the private sector, including debt guarantees. Both governments should strive to create an environment and legal framework conducive to the promotion of Blended Finance.

### Reporting and Disclosure

Both countries' financial regulatory agencies should engage in a public-private dialogue to consider disclosure and reporting standards related to sustainable financing activities, and climate-related risks and opportunities. The goal should be to establish a globally harmonized framework for reporting and disclosure that balances investor needs for transparency and informed decision-making with the need for financial institutions and reporting entities to have flexibility within the framework. Such flexibility is critical in view of the uncertainties and subjective interpretation inherent in any analysis of the assessment and impact of climate change and sustainable financing activities.

### Supporting Small and Medium-Sized Enterprises

Small and medium-sized enterprises (SMEs) constitute the backbone of our economies, responsible for the vast majority of jobs, tax payments, innovation, and resiliency. But in the new era of geopolitical stress, energy transitions, digital transformation, market volatility and attendant regulatory fragmentation, SMEs are experiencing unsustainable burdens. Both governments should make it a priority to foster the diversification of SME financing instruments and channels to enable them to build resilience and undertake crucial investments, such as those in digitalization and decarbonization. This should also include non-financial support which is key to strengthen SME awareness about the steps towards net zero and provide the necessary tools that can enable them to embark and stay on the journey.

## 3. Advancing International Cooperation in Finance

### Supporting the Global South

The Councils welcome efforts by both governments to support financial inclusion of developing countries (often called the Global South). Efforts such as the Partnership for Global Infrastructure and Investment (PGII) and the G20 Principles for Quality Infrastructure Investment are necessary to help the Global South meet its development needs. We are pleased to see the inclusion of private sector perspectives and participation in these efforts and urge the two governments to continue to integrate private sector input going forward. The Councils believe that the initiatives to promote sustainable finance and blended finance mentioned in Chapter 2 of this statement are important in supporting the Global South. In addition, aligning the global interpretation of Basel III capital rules and country regulations, sharing expertise of the development banks and financial institutions, and streamlining

documentation and standardizing contracts would remove significant barriers that currently prevent or delay banks' ability to provide capital to infrastructure investments associated with MDBs and their related organizations.

Both Councils urge their respective governments to take measures to prevent debt crises from forming in emerging economies. Such events delay the implementation of the aforementioned initiatives and introduce instability to financial markets across the world.

### Economic Security

Both Councils understand that finance represents a critical infrastructure, and that it is necessary for the public and private sectors to work together to ensure cybersecurity and other measures to provide safe and sustainable services. When considering various economic security regulations, both governments should coordinate appropriately to ensure national security while taking care not to hinder free economic activity.

Furthermore, in view of the growing complexity of financial sanctions that prohibit transactions with specific targets, both governments should consider implementing close communication between the public and private sectors to enhance the effectiveness of sanctions and reduce the compliance risks of financial institutions.

## 4. Promoting Digital Financial Innovation

### Central Bank Digital Currency (CBDC)

The Councils appreciate that both governments and central banks are deliberating CBDC policy to harness the benefits of innovation while addressing potential risks to the financial system. The Councils encourage both governments to evaluate the need for CBDCs before actually issuing them by identifying whether there is a shortcoming with other payment initiatives that a government or central-bank-issued CBDC would be able to address more effectively than private alternatives.

### Data Connectivity

The Councils recommend both governments prioritize data connectivity for financial services and promote public-private collaboration to pursue high-standard rules in the digital economy. We welcome the establishment of the Institutional Arrangement for Partnership (IAP) to operationalize Data Free Flow with Trust (DFFT) and appreciate that particular attention will be paid in the IAP to areas such as data localization and regulatory cooperation in financial services.

### Innovation

The Councils recognize the importance of the continued efforts by both governments to resolve regulatory and operational issues to promote digital financial innovation. Particularly, with the emergence of decentralized finance (DeFi), cryptocurrencies, non-fungible tokens (NFTs), and other digital assets, the development of legal frameworks has become crucial in balancing the utilization of digital financial innovation with the stability of the financial system and the protection of users. Therefore, the financial regulatory authorities of both countries should continue to provide timely, clear, and integrated guidance to market participants in this field.

### AI/Generative AI

The use of AI in financial institutions continues to advance and global interest in generative AI is rapidly increasing. Both Councils welcome the agreement reached at the G7 Digital and Technology Ministers' Meeting to promote the mutual operation of AI governance and the adoption of trustworthy international AI technology standards through international discussions. Both national governments need to collaboratively review the various systems and guidelines related to the use of AI and the policies for dealing with associated risks to ensure that any AI-specific

regulations complement and align with existing sector-specific regulations to avoid duplicative efforts or conflicting requirements that could increase risk. We also recommend both governments focus on the development of human resources for the development and application of AI.

## 5. Securing a Brighter Future

### Personal Financial Assets

The Councils recommend both governments adopt a policy framework, such as through tax incentives or subsidies, which supports adequate individual asset formation. We also recommend both governments to strengthen public and private collaboration in enhancing the incentives for the building of personal financial assets, including through insurance, private pension funds, and financial planning. The Councils support the GOJ's "Doubling Asset-based Incomes Plan" under Prime Minister Kishida's economic policy, which will help large personal financial assets to be more effectively invested. We recommend that the GOJ consider and implement strategies to optimize the allocation of financial assets across the investment spectrum in Japan, from corporate and public pensions to defined contribution plans and individual savings.

### Insurance

The Councils recommend that both governments ensure that the insurance sectors are able to meet the evolving financial protection needs of consumers, to include maintaining the wide availability of long duration insurance and savings products. We encourage regulators to facilitate the insurance sectors' appropriate provision of more innovative insurance products that meet changes in customer needs while ensuring sufficient customer protection. We also recommend that both governments establish appropriate capital standards for insurers at the global, national, and jurisdictional levels.

### Financial Literacy

As individuals take a more active role in managing their personal investments, increasing financial literacy becomes even more important. The Councils recommend public-private collaboration on increasing technology and financial literacy, particularly for vulnerable populations, as well as on financial education for youth.

### Japan's Development as an International Financial Center

The opportunity for Japan to reestablish its prominence as a global and regional financial center has never been greater. Japan possesses all the necessary attributes to become a top global financial center and attract far larger amounts of foreign investment than at present. The efforts of the Japanese government and authorities to strengthen their outreach to overseas businesses by holding promotional events, such as so-called "Japan Weeks," is highly appreciated. The Councils urge the GOJ to implement policies to establish Japan more prominently as an international financial hub for the world and Asia and as a nation facilitating asset management. This includes policies for attracting foreign financial specialists to Japan, encouraging financial firms to invest in technology, and diversifying the asset management industry to cultivate globally competitive talent. The Councils believe that the financial sectors of both countries can play a role in fostering these initiatives and contribute to the growth of financial business in Japan.

The Councils welcome progress has been made on the negotiations of the IPEF. We hope that its Pillar III (Clean Economy), if enacted, would be a catalyst for Japan becoming an International Financial Center, especially on sustainable finance.

## Promoting Foreign Direct Investment (FDI) Into Japan

The Councils welcome Prime Minister Kishida's efforts to raise FDI via the Cabinet Office's "Action Plan for Attracting Human and Financial Resources from Overseas" and appreciate the GOJ's efforts to implement measures in the Plan promptly. We are pleased to support their undertakings especially in areas such as the formation of Asia's largest startup hub and improving the business environment. The Councils look forward to maintaining an open line of communication with the Cabinet Office on inbound FDI issues and stand ready to provide advice and support.