

# Compliance Group-wide efforts

Compliance is the basis of CSR. The Group is therefore strengthening its initiatives to achieve this goal, in terms of group-wide policies as well as of policies at the individual group company level.

Issues and targets for fiscal 2005	Results and progress for fiscal 2005
Strengthen cooperation between the legal compliance department in Daiwa Securities Group Inc. and its counterparts in each group company.	The checking operations at group headquarters concerning legal and compliance risk management by each group company were made more rigorous.
Raise level of internal understanding of Corporate Ethics Hotline and periodically survey awareness.	Increased the level of awareness and the number of hotline reports by promoting in-house PR activities and organizing training at each sales branch.
Examine establishment of Voluntary Action Standards.	Emphasized the further application of the existing code of conduct and principles; also, continued investigating the establishment of a new code.

## Approach to compliance and initiatives

The Corporate Principles of the Daiwa Securities Group are underpinned by the concept of total compliance, which, in turn, forms the basis for the Group's approach to corporate social responsibility (CSR). As the Group consists of different types of companies, the laws that apply are also varied. For this reason, detailed compliance rules and initiatives are established at the group company level. Still, compliance at the group level is also essential; close cooperation between the legal and compliance department at Daiwa Securities Group Inc. and the legal and compliance departments of each group company is emphasized.

## Initiatives to spread compliance awareness among employees

Daiwa Securities Group Inc. and Daiwa Securities Co. Ltd. are jointly conducting training on corporate ethics, CSR, and compliance. The Group works to raise awareness of these matters during new employee training and highlights their importance in contributing to the development of sound securities markets.

## Structure and performance of the Corporate Ethics Hotline

The Corporate Ethics Hotline, is an internal reporting system for all employees group-wide to directly report ethical problems related to business operations and the workplace to either headquarters or an external legal body. There were 30 reports made through the hotline during 2005. This was a marked increase from the 13 reports made in 2004; the rise is attributed to increased awareness of the hotline within the Group, as well as greater confidence in the anonymity of the program. There were many reports relating to the length of working hours in 2004. However, due to proper guidance on time management, such reports decreased this year, revealing a definite improvement resulting from the hotline.

### Examples of reports made through the Corporate Ethics Hotline

Report	Response
Misuse of power and position, character disparagement, etc.	After an investigation of the situation, a warning was issued to the higher-ups and guidance was provided
Sexual harassment	After an investigation of the situation, a warning was issued to the staff and guidance was provided
Breaches of sales ethics and rules	After an investigation of the situation, special training and guidance was provided to the individuals concerned
Impoliteness	A warning was issued at a general meeting concerning proper business practices and conduct

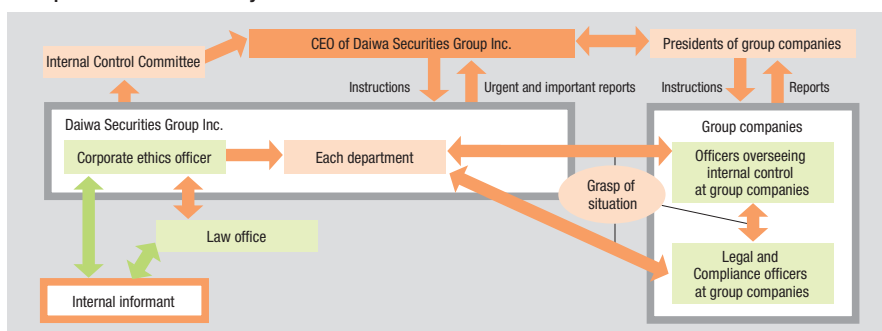
## Employee awareness survey for the Corporate Ethics Hotline

The Group surveyed all executives and managers with a questionnaire about the Corporate Ethics Hotline. This year the executives were asked about the hotline, and 90% indicated awareness, while 77% responded that they would make a hotline report if there was a problem. However, since only 51% thought the hotline provides anonymity, it is clear that there is still a lack of understanding in the program. Therefore, the Group will seek to build confidence in the hotline.

## Postponement of voluntary action standards and future initiatives

A yearlong investigation was carried out concerning the establishment of voluntary action standards, including surveys of executives and managers. The results suggested that rather than creating a new Code of Conduct and Ethics, it would be better to first promote a deeper comprehension of the current code at each group company. Training was therefore carried out at all sales locations and succeeded in building understanding of the existing code. However, the company will continue considering a new code.

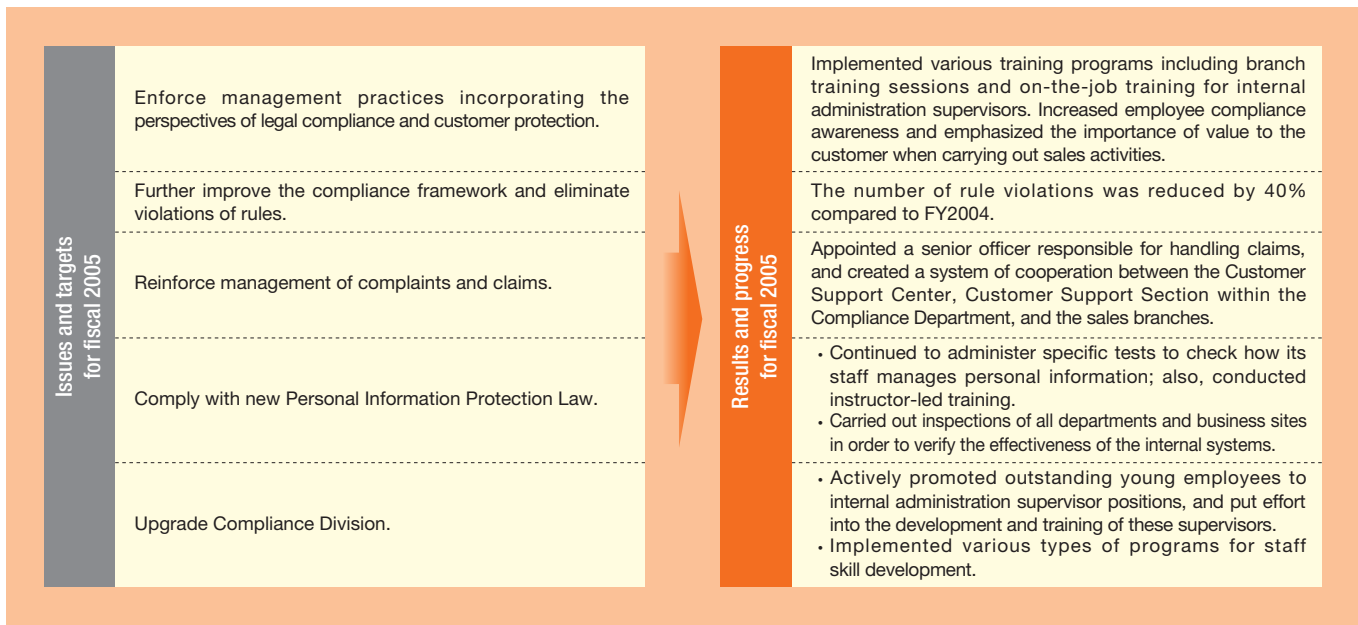
### Corporate Ethics Hotline system



### Future issues and fiscal 2006 targets

Although most of the reports made through the Corporate Ethics Hotline have come from Daiwa Securities Co. Ltd., awareness-raising activities are being carried out at the other group companies. Moreover, through the collaboration between the compliance departments at the Daiwa Securities Group Inc. and Daiwa Securities Co. Ltd., efforts to eliminate antisocial influences are being stepped up.

# Initiatives at Daiwa Securities Co. Ltd.



## Approach to compliance and initiatives

Compliance is an issue of utmost importance and forms the foundation of a company that contributes to society. To improve its ability to attain a better level of compliance, Daiwa Securities Group has taken various initiatives to improve practices, reducing administrative errors, combating antisocial influences, and strengthening claim handling. It emphasizes the importance of adopting the customer's point of view as the employees carry out sales activities.

## Initiatives to improve the quality of operations activities

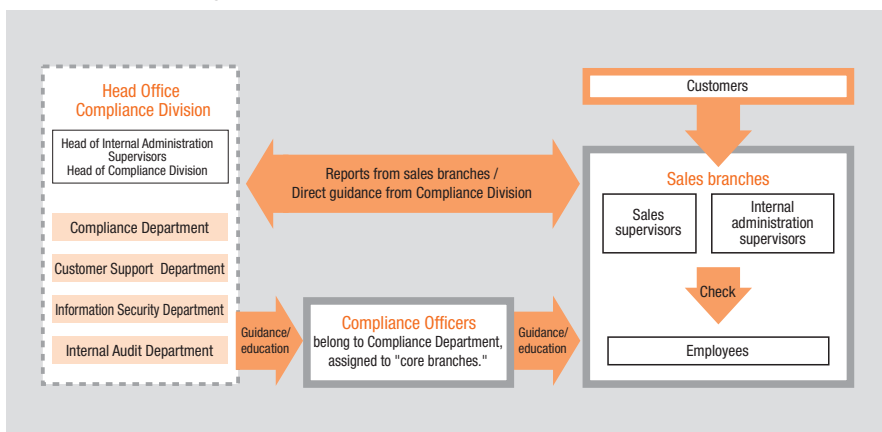
Compliance involves more than just an adherence to laws and regulations; it covers all awareness, attitudes, and actions that are necessary to earn the maximum confidence from customers. Therefore, starting in the second half of fiscal 2005, the Daiwa Securities Co. Ltd. has made the quality of operations activities a key compliance issue. Daiwa Securities Co. Ltd. is working hard to properly understand the needs and wishes of investor clients, to provide them with suitable

investment advice, while offering easy-to-understand explanations, and taking care to avoid errors at the time of order placement. Daiwa Securities Co. Ltd. intends to improve the quality of its operations, and increase customer confidence through these efforts.

## Approach to promoting compliance

Compliance officers have been appointed in each of the 24 area groups that coordinate the network of Daiwa Securities Co. Ltd. branches across Japan. In fiscal 2005, Daiwa Securities Co. Ltd. actively promoted and groomed young employees for internal administration supervisor positions, as representatives of the next generation of compliance supervisors in each of the branches. In order to enhance the ability of departments and branches to uncover and resolve their own problems, a system has been created whereby the internal administration supervisors and compliance officers check management conditions in their sales branches and file monthly management reports with the Compliance Division.

### Approach to promoting compliance



## Initiatives at Daiwa Securities Co. Ltd.

### Conducting training to raise compliance awareness

Daiwa Securities Co. Ltd., provides ongoing training for executives, sales staff, managers, and new employees, according to the type of job and position. This includes branch visits and training by a team of Compliance Department staff, as well as Joint Compliance Training sessions conducted at the branches. The latter program is a collaborative effort between the departments in the Daiwa Securities Group Inc. responsible for corporate ethics and CSR. In addition, the company uses the intranet and small-group training sessions in the Compliance Division for the improvement of quality of operations activities, while also providing special training to conduct activities such as the mandatory testing of employees' knowledge of laws and regulations.



Joint Compliance Training

### Eliminating compliance violations and protecting investor clients

Compliance violations or incidents arising from improper execution of securities transactions occur when someone deviates from the various laws and regulations that govern a securities company and its executives and employees. A prime example of this is the failure to deliver prospectuses that should be given to customers before or at the time of investment. In fiscal 2005, Daiwa Securities Co. Ltd. was able to reduce the number of compliance violations by 40%, compared to the previous fiscal year. This was mainly due to the tight control over the staff's email communication, leading to a substantial reduction of cases where sales staff electronically sent unapproved investment promotion materials to customers.

In fiscal 2005, the internal detection rate\* of compliance violations dropped from 74% in the previous fiscal year to 63%. This was due to

the large drop in compliance violations related to unapproved electronically-available materials, as mentioned above. In the future, the company will continue to work towards zero compliance violations by making properly executed sales activities the primary compliance objective, in line with legal adherence and customer protection.

\*The internal detection rate is the percentage of incidents not revealed by customer complaints or external inspection, out of all the compliance violations reported to the Financial Services Agency.

### Combating unfair transactions and antisocial influences

In order to promote sound securities markets, Daiwa Securities Co. Ltd. is stepping up its efforts to combat illegitimate influences such as organized crime and corporate racketeers. The company provides data from various sources and guidance by specialized staff, and is determined to completely eliminate such influences from the market. Daiwa has also built a system to stop identity theft where criminals attempt to establish accounts in other people's names to carry out unlawful transactions.

### Compliance measures under the Personal Information Protection Law

Daiwa Securities Co. Ltd. continues to administer specific tests to check how its staff manages personal information, in order to promote awareness of the need to protect such information. In order to verify the

effectiveness of internal information management, the company carries out inspections at all branches and strives to make improvements. The TRUSTe Certification program has been updated as a means of evaluation from outside organizations. Further measures are planned in fiscal 2006 in business units at high risk of personal information leakage.

#### Future issues and fiscal 2006 targets

In order to maximize customer confidence, it is of utmost importance for Daiwa Securities Co. Ltd. to further improve the quality of its operations and sales. The company continually monitors and guides its sales staff to ensure the quality of their efforts and has also created procedures to properly ascertain customer intentions and hence, provide appropriate advice. Therefore, the customer interview process is being made more rigorous. Also, steps are being taken to eliminate unfair transactions and antisocial behavior.

#### Comments from stakeholders

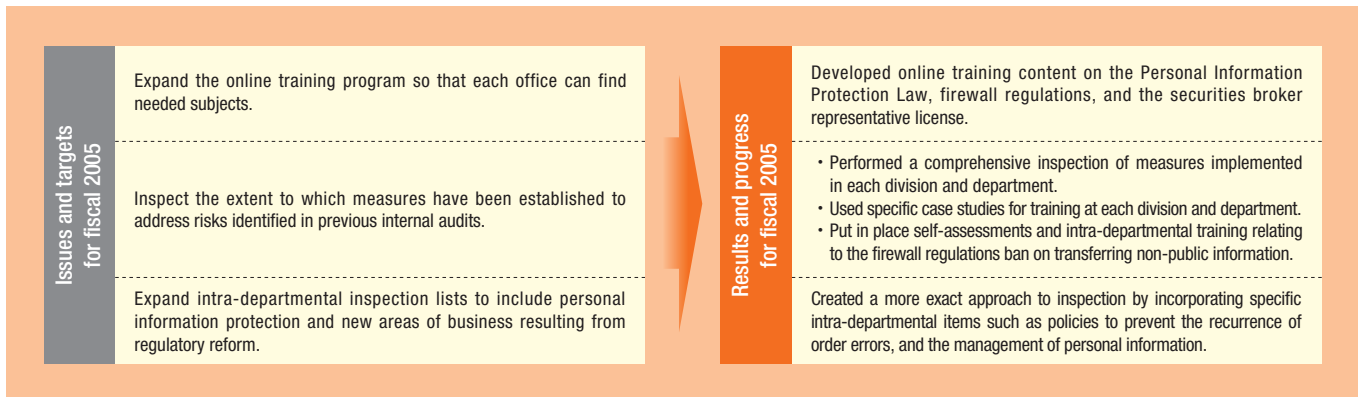
##### My expectations of the Daiwa Securities Group

The Corporate Ethics Hotline now plays a major role in the Group's determination to achieve a higher level of compliance. However, what is the most important element for this system of internal monitoring to work? I think it is the confidence employees have in it. Without this confidence, the company cannot quickly identify in-house problems through internal reporting. I am of the view that the higher number of reports from the Daiwa Securities Group companies is a reflection of increased confidence in the system's effectiveness. However, the Group still needs to further boost employee confidence. In the end, the fastest way to achieve this will be to address each and every incident report in an honest and effective manner. I hope that the Daiwa Securities Group will continue its efforts in this area.



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## Initiatives at Daiwa Securities SMBC Co. Ltd.



### Basic approach to compliance

Compliance is one of the key management issues for Daiwa Securities SMBC Co. Ltd. The company emphasizes proper operations under an effective system for monitoring compliance.

The company expects the following measures to ensure that the system is effective: 1) Establishing business conduct rules in line with all laws and regulations; 2) making the rules known and understood throughout the organization and following them strictly; 3) monitoring compliance with these rules; 4) developing and enforcing procedures to tackle identified problems; and 5) incorporating these procedures into the rules.

### System of achieving compliance

Daiwa Securities SMBC Co. Ltd. has appointed internal administration supervisors and internal administrators for each department who provide compliance guidance for daily operations. The Legal & Compliance Department, which coordinates these efforts, monitors and offers legal counsel on operational issues, watches out for unfair transactions, and provides guidance for intra-departmental inspections conducted by individual departments. This intra-departmental inspection watches for the effectiveness of the management of high-risk issues by having each division and department perform a self-assessment of its potential operational risks. The company is working towards a better approach to achieving compliance by creating procedures to deal with problems identified during inspections,

incorporating these procedures into operational manuals, and then putting them into practice. The Internal Audit department confirms that operations are being properly carried out through department audits and spot audits on specific issues.

### Improving compliance training

Daiwa Securities SMBC Co. Ltd. holds instructor-led training as necessary for newly appointed executives, fresh hires, recently transferred employees, and employees leaving for overseas posts. The company is developing intra-departmental training to include selected operational topics for each department and division. In fiscal 2005, online training content was prepared on the Personal Information Protection Law, firewall regulations, and the securities broker representative license. The company plans to continue its efforts building its online training content.

### Examining the implementation of measures resulting from internal audits

Between April and August of 2005, Daiwa Securities SMBC Co. Ltd. performed a comprehensive inspection of progress made on measures implemented to tackle issues highlighted in past internal audits at each division and department. The company carried out intra-departmental training that incorporated actual examples from other companies, including recommended administrative initiatives, as well as disciplinary action taken for violations. Self-assessments and training relating to the firewall regulations ban on transferring non-public information was also carried out.

### Complying with the Personal Information Protection Law

In addition to examining how personal information is handled in an internal assessment ordered by the Legal & Compliance Department, the company also prepared information management manuals and held training sessions for internal administration supervisors and information security managers. A system has been created through the preparation of indexes and individual management tables for each division and department to use in managing personal data.

#### Daiwa Securities SMBC's approach to promoting compliance

