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**Local Government Bond System
and Market in Japan**

**Ministry of Internal Affairs
and Communications**

**JLGB European Road Show
October, 2008**



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 - II Market potential
 - III Attractiveness
 - IV Outreach effort to foreign investors
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Executive Summary

Japanese Local Government Bond – A Safe Investment

(1) Market potential

- ◆ Second largest muni market in the world (\$2 trillion)
- ◆ Sharp decline in government funding (60% to 36% in 8 years)
- ◆ Decline of private placement
- ◆ Sharp increase of public offering (No. of issuers: 28 to 44 in 6 years, Issuance: Triple in 10 years)
- ◆ Increasing number of credit ratings, 16 entities in 2 years (11 entities for Aa1 by Moody's)

(2) Attractiveness

- ◆ Stable spread range over JGB market with average pick up of 10 ~ 30 basis points
- ◆ 0% BIS risk weight in Japan and No legal concept of bankruptcy and debt discharge
- ◆ Similar credit status to JGB with strong national government support and check
- ◆ Introduction of new law to strengthen high credit and full disclosure from this year
- ◆ Multiple Maturities available from 5,10,15,20 or 30 year and Increase in 20&30 year
- ◆ High liquidity with \$1 billion issue monthly (Joint bond with full guarantee by all issuers)

(3) Outreach effort to foreign investors

- ◆ Withholding tax exemption from this year
- ◆ Amendment of Cabinet Order to enable Euroyen bond issue besides existing foreign bond
- ◆ English Information to be readily available via website (www.chihousai.or.jp) or hardcopy
- ◆ Regular overseas road shows from this year

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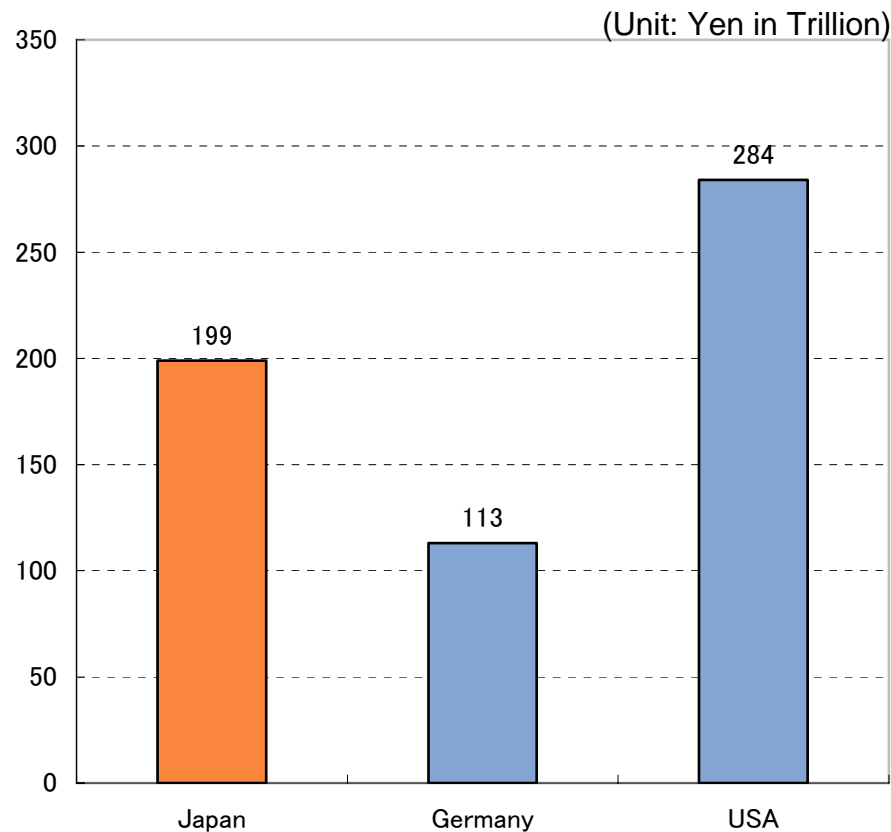
V Appendix



Second largest muni market in the world

- ◆ Japan's Local Government debt has ¥199 trillion (equivalent to about \$2 trillion) outstanding. Japan sits on second only to the U.S.

LGs' Debt Outstanding (2007) Japan/Germany/USA



Source: Japan Local Government Bond Association, FRB, Bundesbank



Characteristics of Various Types of Funds with Local Government Bonds

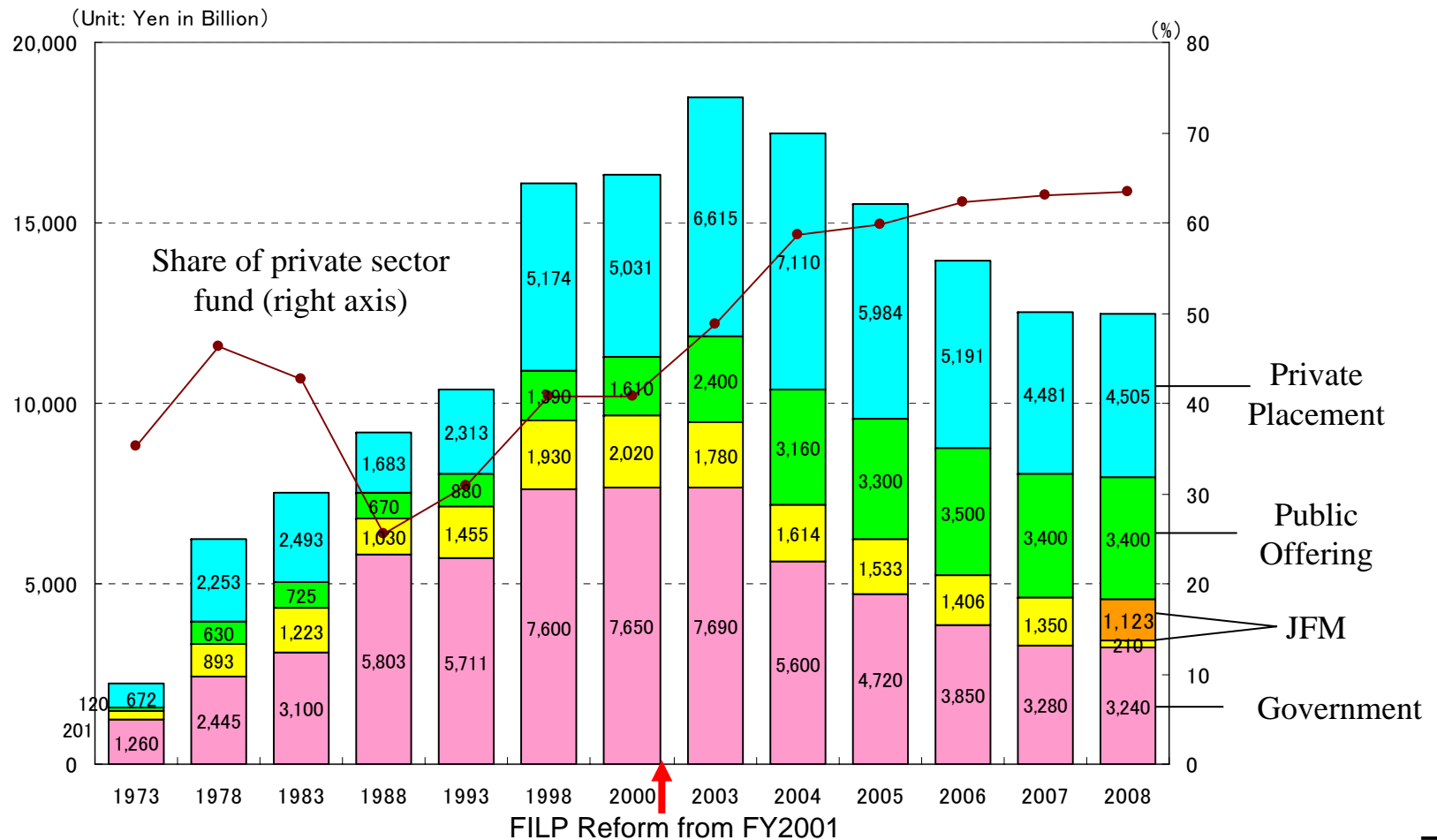
Category		Issuance Method	Maturity	Redemption Method	Setting Coupon
Private Funds	Private Placement	bond, loan	Mainly 10 years. Various Other Maturities, such as 5 years, Based on Agreements with Banks	amortization bullet	Local Government's Discretion
	Public Offering	bond	5 years and 10 years (Some Super-Long-Term Bonds, 20 years or 30 years)	bullet	Fixed Rate
Public Funds	JFM	loan	5-28 years, Mainly Super-Long-Term(20+years)	amortization	Choice of Fixed Rate or Rate-Review Method
	National Government Funds	loan	5-30 years, Mainly Super-Long-Term(20+years)	amortization	Choice of Fixed Rate or Rate-Review Method



Government funding decreases while Private sector funding increases ①

- ◆ Reduction in government funding due to FILP (Fiscal Investment and Loan Program) Reform to minimize government funding's role from FY2001.

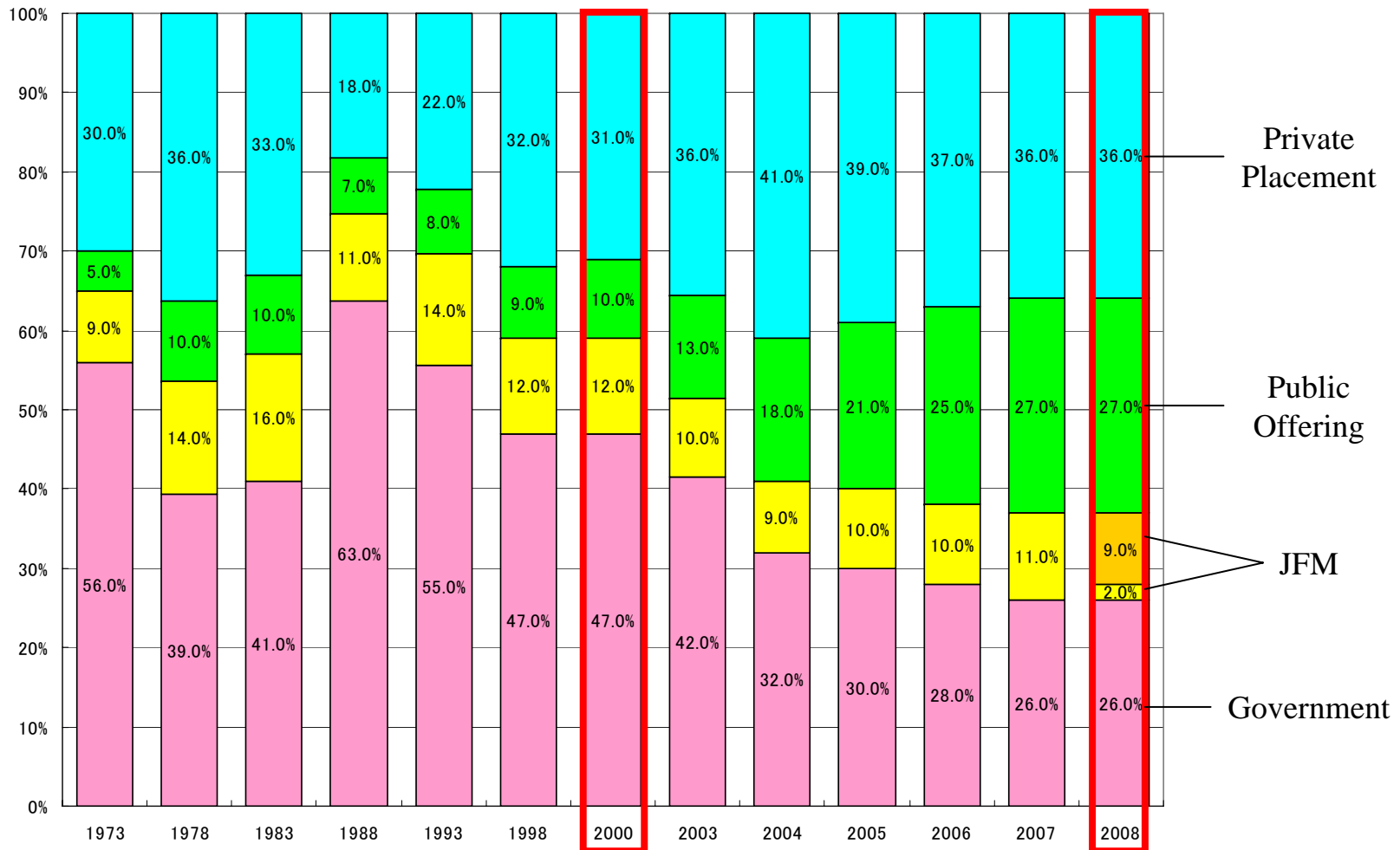
Breakdown of funding source





Government funding decreases while Private sector funding increases ②

Composition of Funds of Local Government debt

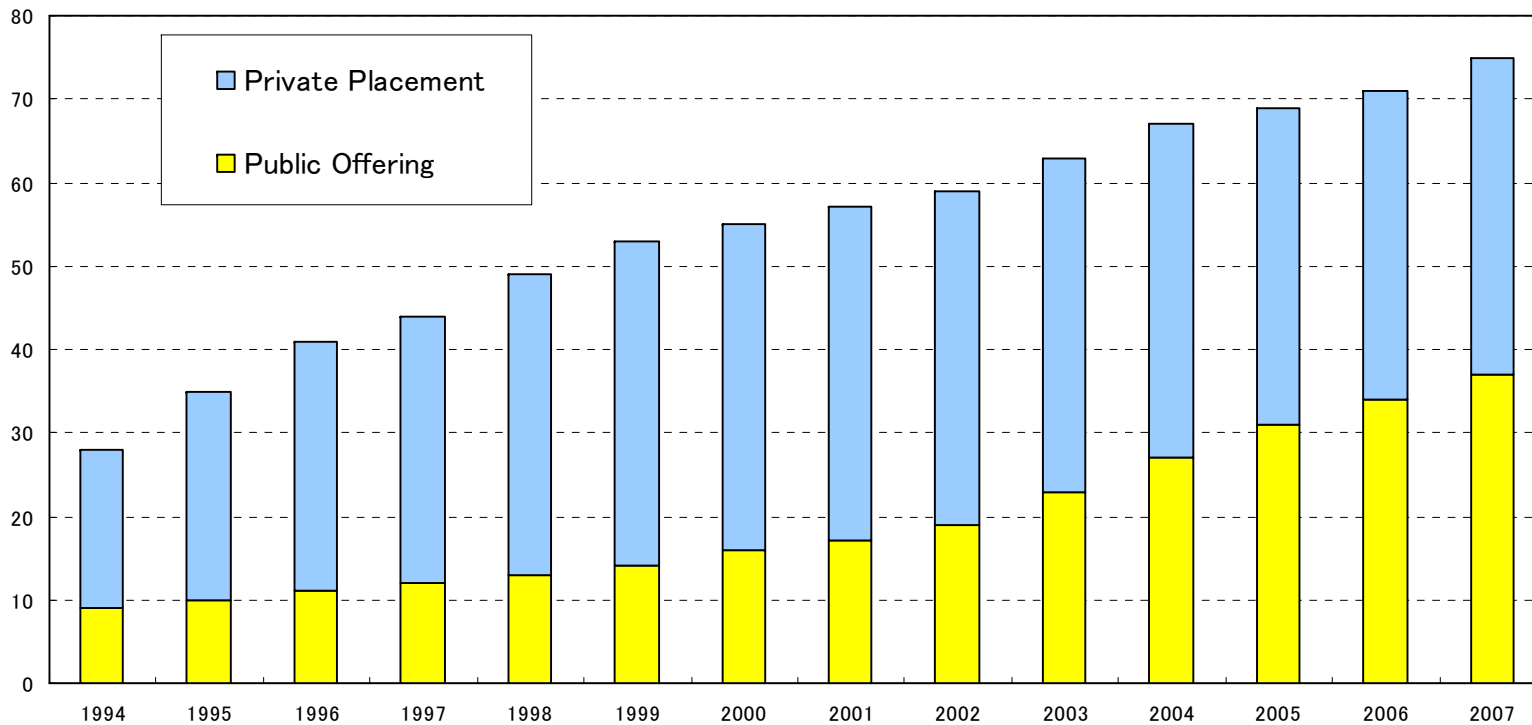


Expanding public issues of local government bonds

- ◆ The number of issuers and the issuance amount of public offering LGB (Local Government Bond) have been increasing due to the sharp reduction of government funding.

Trends of LGB Outstanding (Private sector funding)

(Unit: Yen in Trillion)





Nationwide Public Offering LGB Issuers

- ◆ The number of public offering issuer increase sharply from 28 to 44 issuers in 6 years, and the amount of issuance is triple in 10 years.

	Prefectures	Designated Cities	No. of LG (Total)
1952	Tokyo Osaka Hyogo	Yokohama Nagoya Kyoto Osaka Kobe	8
1973	Hokkaido Kanagawa Shizuoka Aichi Hiroshima Fukuoka	Sapporo Kawasaki Kitakyushu Fukuoka	18
1975	Miyagi Saitama Chiba Kyoto		22
1982		Hiroshima	23
1989	Ibaraki Niigata Nagano	Sendai	27
1994		Chiba	28
2003		Saitama	29
2004	Fukushima Gunma Gifu Kumamoto		33
2005	Kagoshima	Shizuoka	35
2006	Shimane Oita	Sakai	38
2007	Yamanashi Okayama	Niigata Hamamatsu	42
2008	Tochigi Tokushima		44



Increasing number of credit ratings

Local Government	Ratings			
	Moody's	S&P	R&I	JCR
JGB (National Government)	Aa3/Stable(Aaa/Stable)	AA/Stable	AAA/Negative	AAA/Stable
Tokyo	Aa1/Stable (Aaa/Stable)	AA/Stable	-	-
Niigata Prefecture*	Aa1/Stable (Aaa/Stable)	-	-	-
Shizuoka Prefecture*	Aa1/Stable (Aaa/Stable)	-	AA+/Stable	-
Okayama Prefecture	-	-	AA/Positive	
Hiroshima Prefecture*	Aa1/Stable (Aaa/Stable)	-	-	-
Fukuoka Prefecture	Aa1/Stable (Aaa/Stable)	-	-	-
Chiba City*	-	A+/Positive	-	-
Yokohama City	-	AA-/Positive	-	-
Niigata City*	-	AA-/Stable	-	-
Hamamatsu City	Aa1/Stable	-	-	-
Nagoya City	Aa1/Stable (Aaa/Stable)	-	-	-
Kyoto City*	Aa1/Stable	A+/Stable	-	-
Osaka City*	Aa1/Stable (Aaa/Stable)	AA-/Stable	-	AA+
Sakai City	Aa1/Stable			
Kobe City*	-	-	AA/Stable	-
Fukuoka City*	Aa1/Stable (Aaa/Stable)	-	-	-

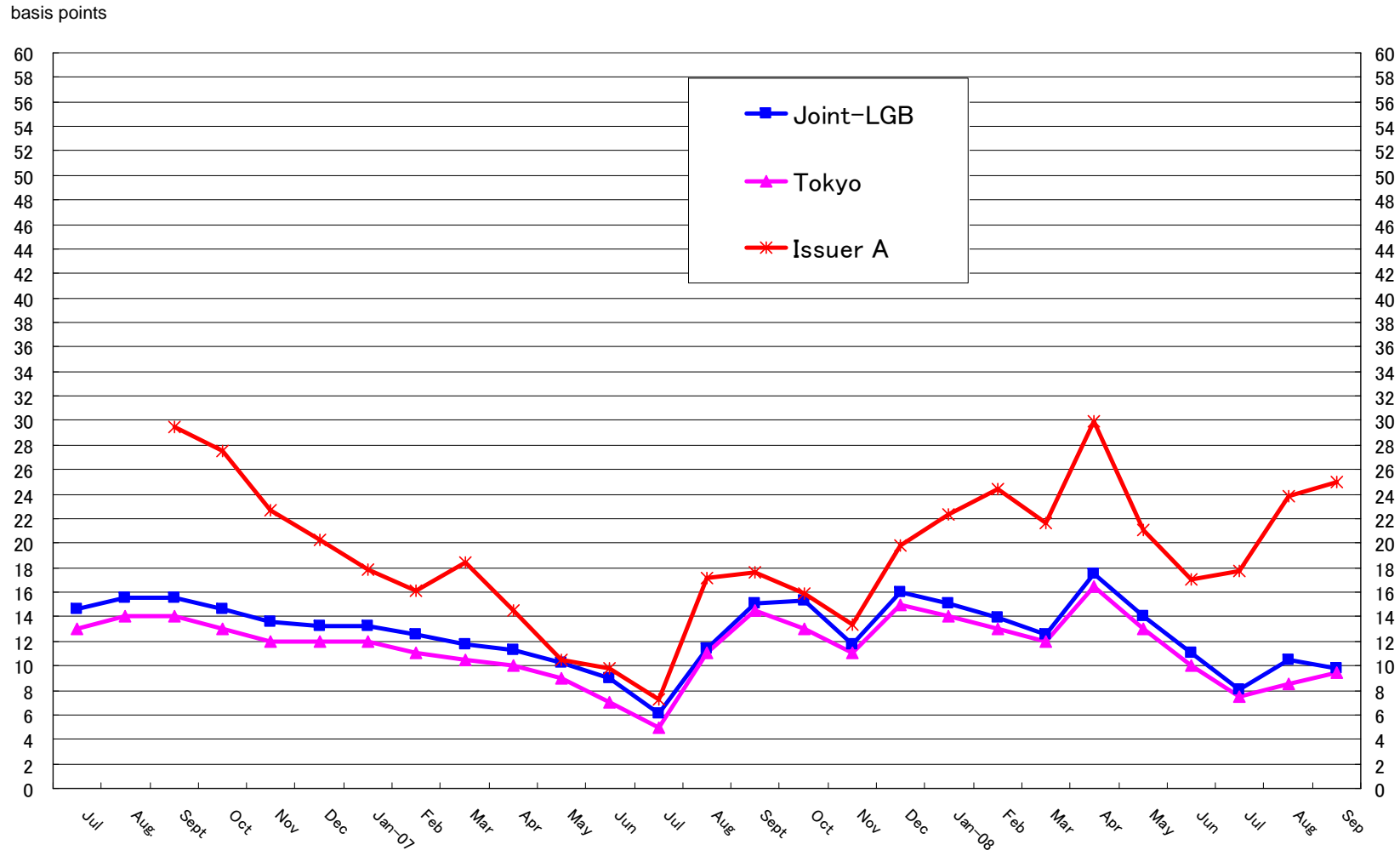
*Issuers for Joint-LGB * () = Foreign bond

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Attractive yield spread over JGB

◆ Spreads on Ten - Year Public Offering LGB over JGB.



※ Issuance Yield of LGBs (July 2006 – Sep 2008)



Safety of Japanese LGB

- ◆ Japanese LGB is issued under the following conditions.
- ◆ There is strong financial support system and check system for LGs by NG (National Government).
- ◆ The bankruptcy of LGs (Local Governments) and debt discharge of LGB is NOT allowed under current Japanese system.
- ◆ Therefore, payment failure has NOT happened up to now.
- ◆ From these facts, Japanese financial authority assigned 0 % risk weight to LGB in the standardized approach of BIS regulations (Basel II).

1. Secured resources for debt payment of LGB including NG's financial support

2. Consultation system for the issuance of LGB

3. Early warning system and reconstruction system to assure fiscal soundness



1. Secured resources for debt payment of LGB

Own authority of taxation

Can ensure tax revenue based upon own authority to tax and change the rate.

1. NG needs to prepare enough fund for LGs through Local Public Finance Program

Laws oblige LGs to perform standard public service. For this reason, Laws also oblige NG to create Local Public Finance Program in order to prepare enough fund to perform standard public service including standard debt payment.

2. Local Allocation Tax System

Local Allocation Tax system allows NG to balance local authority revenues and guarantee a standard level of service throughout all LGs by transferring fund to LGs.

3. Sinking fund

LG is required under MIC's ordinance to accumulate sufficient sinking fund annually for the debt payment of bullet type bonds.



Laws related to balancing local authority revenues ①

Article 232. Scope of Expenditures, Local Autonomy Law

- ◆ Each ordinary local public body shall bear the expenses necessarily incurred in the performance of its own affairs and other expenses falling to the ordinary local public body in accordance with laws or cabinet orders founded in law.
- 2. When the State, by laws or cabinet orders founded in law, obliges any ordinary local public body to perform functions, the State shall take the necessary measures for financing of the expenses thereby made necessary.

Article 13. Newly Added Affairs, Local Finance Law

- ◆ When new affairs are by law or cabinet order added to the affairs of local public bodies or the organs of the State whose expenses are borne by local public bodies, the State shall take necessary measures to finance such newly added affairs.
- 2. Any local public body dissatisfied with such financial measures may tender its letter of opinion to the Diet through the Cabinet.

Article 11-2. Financial Needs, Local Finance Law

- ◆ That part of the expenses enumerated in Article 10 – 10-3 which shall be borne by the local public body (except expenses borne by the local public body as provided by item 13-5 of Article 10 to be appropriated by fiscal stabilization funds for nursing care insurance) shall be included in the amount of its financial needs to be considered in the computation of local allocation tax granted thereto under the Local Allocation Tax Law. However, such rule shall not apply to the expenses enumerated in item 16 of Article 10 (except the reduction of the national health insurance premium and tax for the low-income persons to be transferred to the special account of the national health insurance), item 4 of Article 10-2 and item 5 of Article 10-3.



Laws related to balancing local authority revenues ②

Article 1. Object of this Law, Local Allocation Tax Law

- ◆ The object of this Law is to contribute toward realization of the principles of local autonomy and to strengthen the self-dependence of local bodies, by equalizing the financial resources of local bodies and by assuring the systematic operation of local administration through the establishment of allocation standards of local allocation tax, without impairing the rights of such local bodies to administer their property, perform their affairs and execute their administration autonomously.

Article 3. Basic Principles, Local Allocation Tax Law

Article 3-2

- ◆ The State shall, in granting allocation tax, respect the principles of local autonomy and shall attach no conditions or impose no limitations on the use thereof.

Article 3-3

- ◆ Each local body shall make best efforts to maintain a reasonable and appropriate level of administration, and see to it that it conform at least to the minimum standards of scale and quality established by laws or cabinet orders duly delegated by laws.



Local Allocation Tax (LAT) system: Securing standard public service for All LGs

Purpose

- ◆ To make up for imbalances between standard tax revenue and standard service cost.
- ◆ To ensure LGs' revenues to enable LGs to provide a standard public services for residents all over Japan.

Features

- ◆ The total local allocation tax available in any one year is tied to national tax revenues, and is a more stable form of income than other sources of subsidy. It has the additional benefit of being treated as part of local authorities' independent sources of income, and no restrictions are put on its use.
- ◆ Basics: Total amount is legally linked directory to the amount of five national taxes (32% of income tax and liquor tax, 34% of corporate tax, 29.5% of consumption tax, 27.5% of tobacco tax). If that is not enough to make up for all imbalances, national government needs to increase the amount or take other measures under the law.

Article 6, The Total Sum of Allocation Tax, Local Allocation Tax Law

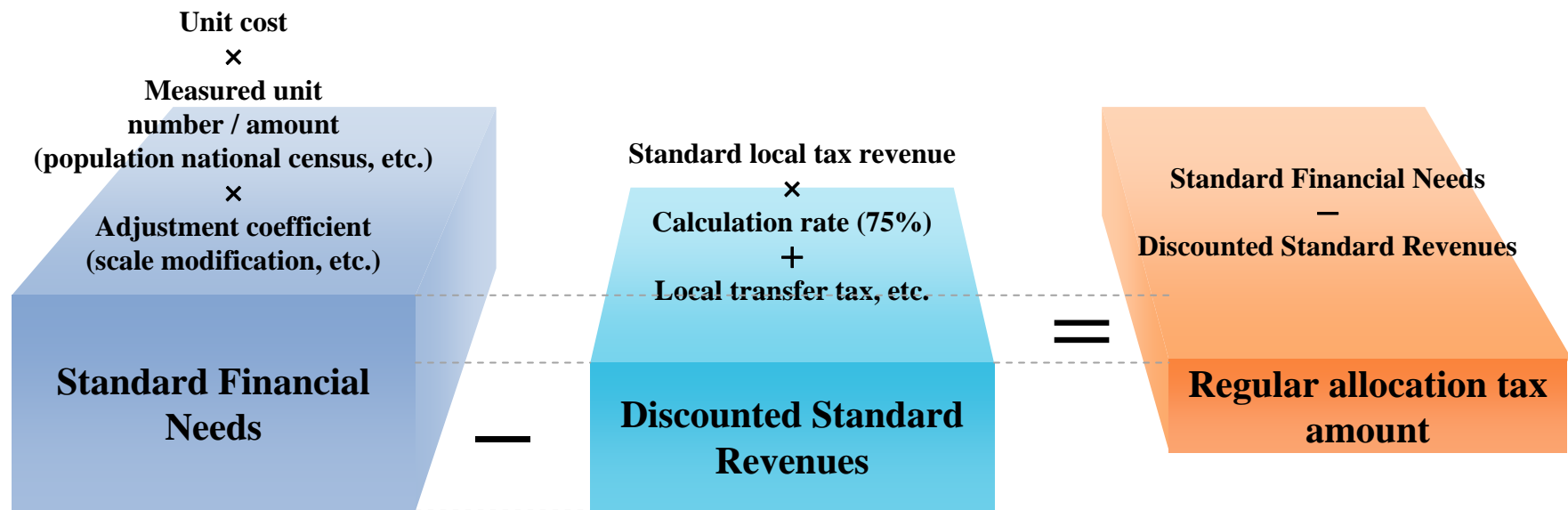
- ◆ The allocation tax shall be equal to 32 per cent of income tax revenue, corporation tax revenue and liquor tax revenue, 29.5 per cent of consumption tax revenue and 25 per cent of tobacco excise revenue.
 2. The total sum of allocation tax to be granted every fiscal year shall be calculated by summing up 32 per cent each of the estimated revenues of income tax, corporation tax and liquor tax, 29.5 per cent of the estimated revenue of consumption tax, and 25 per cent of the estimated revenue of tobacco excise, plus such portion of the allocation tax for the preceding fiscal years which has yet to be granted, or less such amount granted over and above the due amount in the preceding fiscal years.



LAT distribution: Calculating Standard Financial Needs & Revenues

Calculation Formula

- ◆ 94% of the LAT is distributed to each LGs as the following mechanism:
$$\frac{[\text{Standard Financial Needs}] - [\text{Discounted Standard Revenues}]}{[\text{Standard Financial Needs}]}$$
- ◆ SFN is calculated to ensure the basic financial needs including some debt payment as diagram below indicates;
- ◆ DSR accounts for 75% of estimated standard tax revenues to give incentive to collect taxes as diagram below indicates;



Source: White Paper on Local Public Finance, 2007 - Illustrated -, MIC

2. Consultation system for the issuance of LGB ①

- ◆ JLGB system changed from approval system to consultation system in FY06 due to decentralization.

1. Consultation

LGs must consult with the Minister of Internal Affairs and Communications (prefectures and government designated cities) or the prefectural governor (in the case of municipalities) before debt issue.

2. Allocation of public funds for LGB with consent

Only LGB with consent by MIC Minister or the prefectural governor may borrow public funds [Government funds, JFM funds].

3. Debt payment for bonds with consent included in Local Allocation Tax formula

Debt payment for LGBs with consent by MIC Minister or governors are included in Local Allocation Tax formula by NG.

4. LG must report issuance of the bond without consent to its assembly

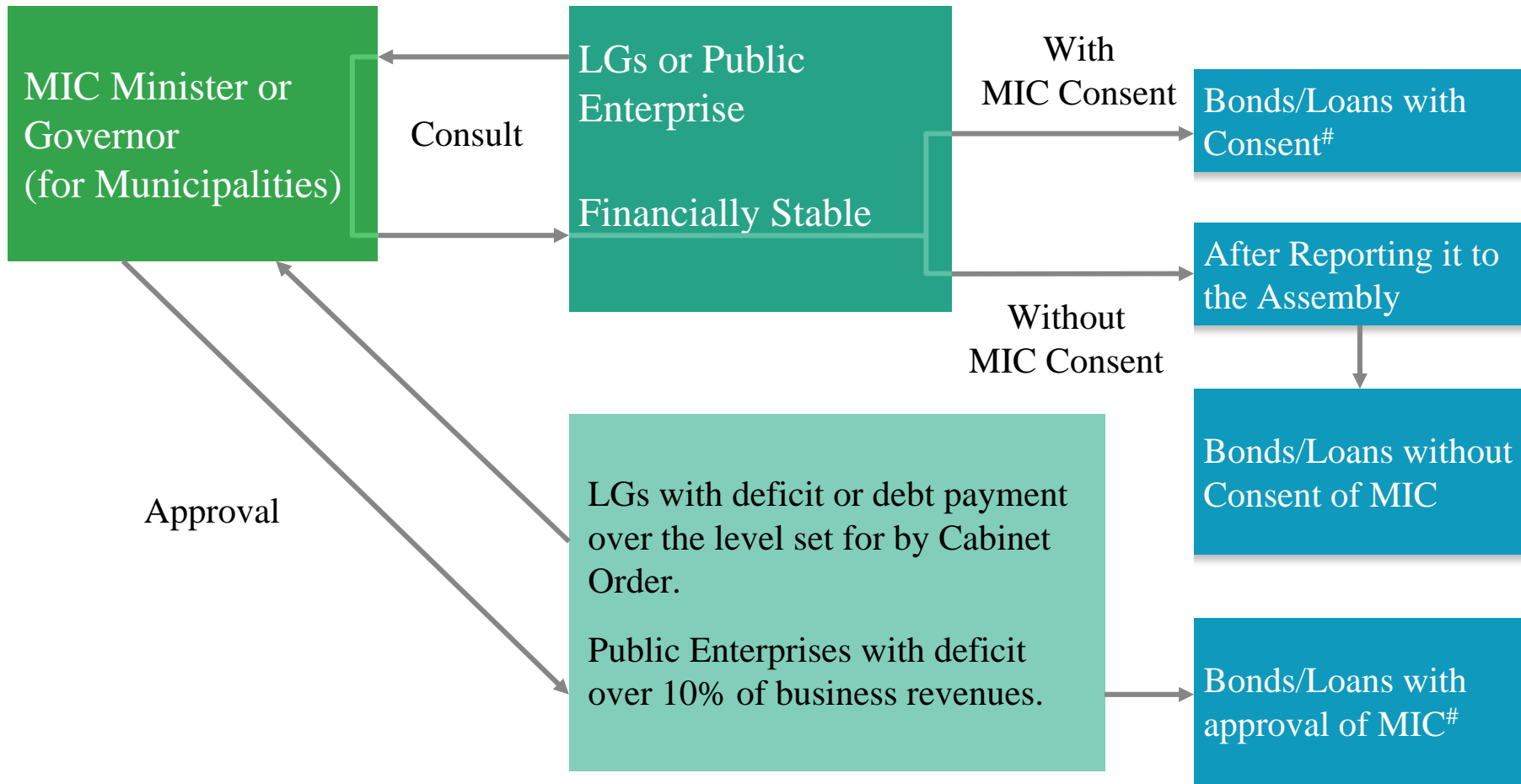
In order to issue the LGBs without the consent, the head of the local government must report it to the assembly.

5. Standard for consent by NG

MIC Minister releases the standard for consent every fiscal year. Issuers in high deficit, issuers with high real-debt-payment-ratio, and public enterprises in high deficit, etc. must obtain the approval of issuance from the Minister or governors.



LGB Consultation System



Only the bonds/loans which obtained the consent or approval of MIC, LGs may borrow from the Government funds or JFM

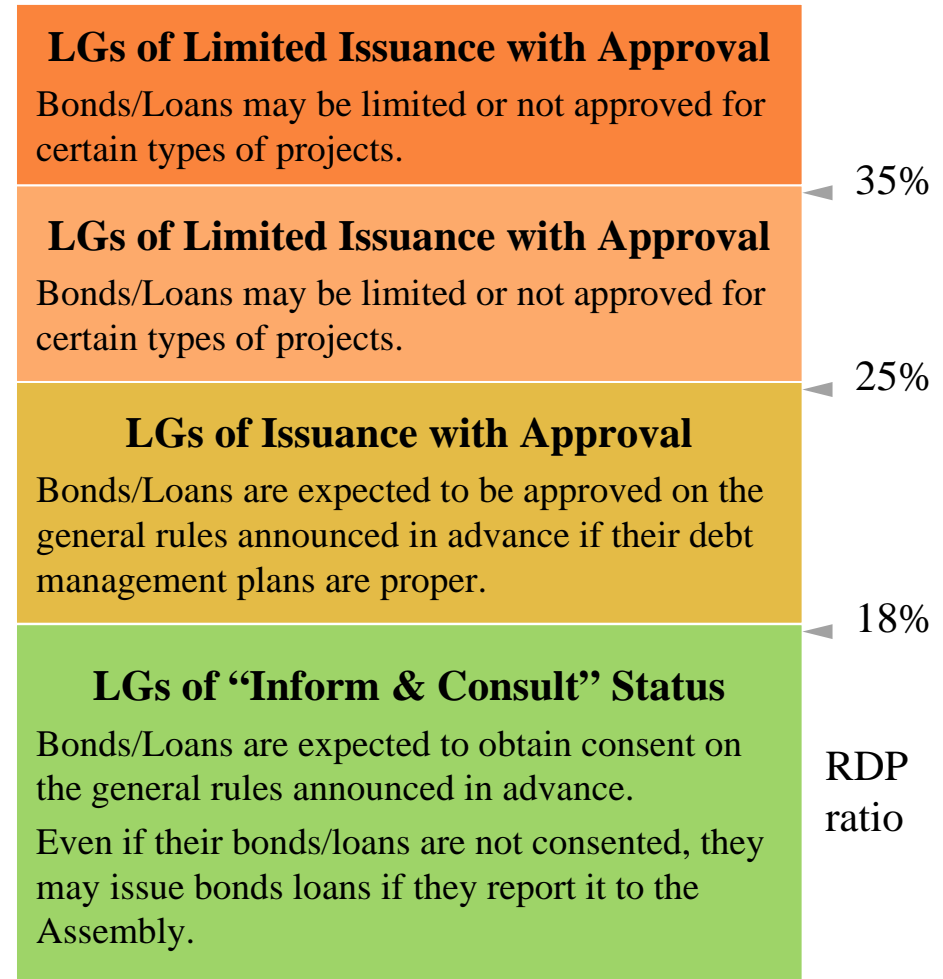


2. Consultation system for the issuance of LGB ②

- ◆ In order to secure fiscal soundness, local governments with higher real-debt-payment-ratio or higher deficit than a set limit are required to get approval for bond issue instead of consultation.

Approval required if real debt payment ratio is 18% or more

- ◆ Issuers with real-debt-payment-ratio between 18% ~ 25% must first draft a debt management plan and obtain approval of the MIC minister, based upon general approval standard.
- ◆ Issuers with the ratio of 25% or more are prohibited from debt issue for certain types of projects by local government.





3. Early warning system and reconstruction system to assure fiscal soundness (from this year)

The Law to strengthen the Fiscal Soundness of Local Governments

- ◆ The Law Relating to the Fiscal Soundness of LGs became effective from this fiscal year.

Purpose

1. Full disclosure of comprehensive fiscal condition including contingent liabilities

- ◆ Five fiscal indicators (see next page) disclose LGs fiscal condition thoroughly and strengthen public check on fiscal condition. This makes LGs much more accountable for the public and investors.

2. Early Warning System

- ◆ Each fiscal indicator must meet set limit and if one of them fails, the LG needs to make a fiscal restoration plan to meet the limit in years. This plan must be checked by outside auditors, authorized by the local assembly and reported to the NG. Also, the LG needs to make a progress report annually to the assembly, the public and NG and if there is problem, NG is supported to make a recommendation to change the fiscal policy to the LG.

3. Reconstruction System

- ◆ If fiscal indicators fail to meet highest set limit, it needs to make a fiscal reconstruction plan with heavy oversight by NG. In this state, the LG needs to take severe measures to cut expenditure and increase tax and other revenue. Importantly, even in this state, both bankruptcy and discharge of debt is not allowed under legal scheme and LG needs to repay full amount of debt.



Disclosure of five fiscal indicators

- ◆ LGs must report the following ratios every year after receiving assessment by outside auditor, to the assembly, and disclose those to the public.

Fiscal indicator	Definition
1. Real deficit ratio	The ratio of deficit to the standard fiscal scale
2. Consolidated real deficit ratio	The ratio of consolidated deficit in the all accounts to standard fiscal scale
3. Real dept payment ratio	The ratio of debt payment by general revenue to standard fiscal scale
4. Future burden ratio	The ratio of outstanding debt including future burdens of public enterprises and government affiliates, to standard financial scale
5. Funding Shortfall Ratio at Public Enterprises	The ratio obtained by dividing the previous fiscal year's shortfall in funds for each public enterprise, calculated in the manner specified by Cabinet Order, by the previous fiscal year's business scale calculated in the manner specified by Cabinet Order.



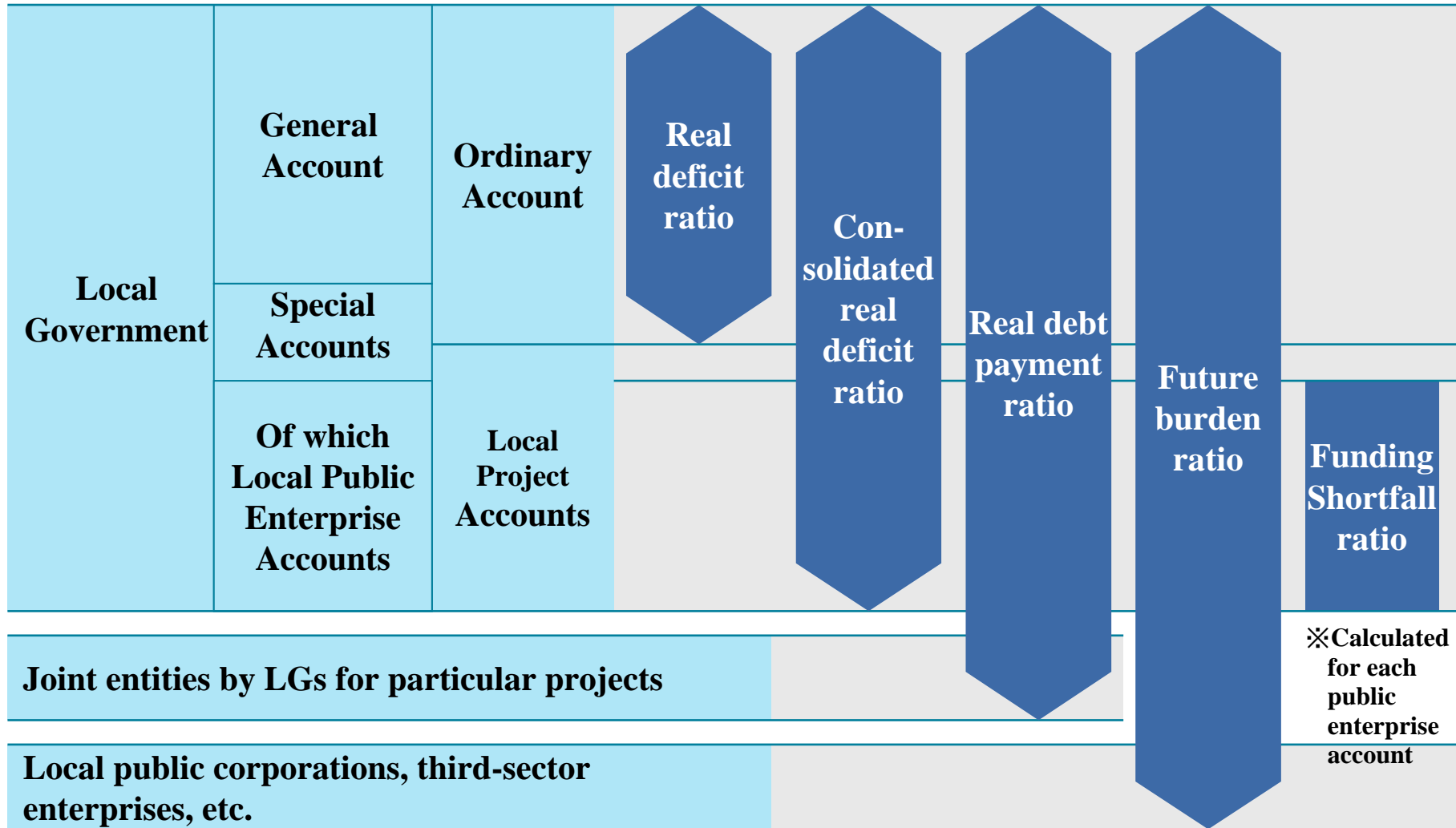
Limits for Early warning and reconstruction

	Early warning limit	Reconstruction limit
1. Real deficit ratio	Prefectures: 3.75%	Prefectures: 5%
	Municipalities, depending on fiscal size: 11.25 ~ 15%	Municipalities: 20%
2. Consolidated real deficit ratio	Prefectures 8.75%	Prefectures: 15%
	Municipalities, depending on Fiscal size: 16.25 ~ 20%	Municipalities: 30%
3. Real debt payment ratio	Prefectures, and Municipalities: 25%	Prefectures, Municipalities: 25%
4. Future Burden Ratio	Prefectures and government-designated cities: 400%	
	Municipalities: 350%	
Management Improvement limit		
5. Funding Shortfall Ratio at Public Enterprises	20%	

Note: Three-year transitional limit(40%→40%→35%for cities, towns and villages) will be set up for reconstruction limit for the consolidated effective fiscal deficit ratio.

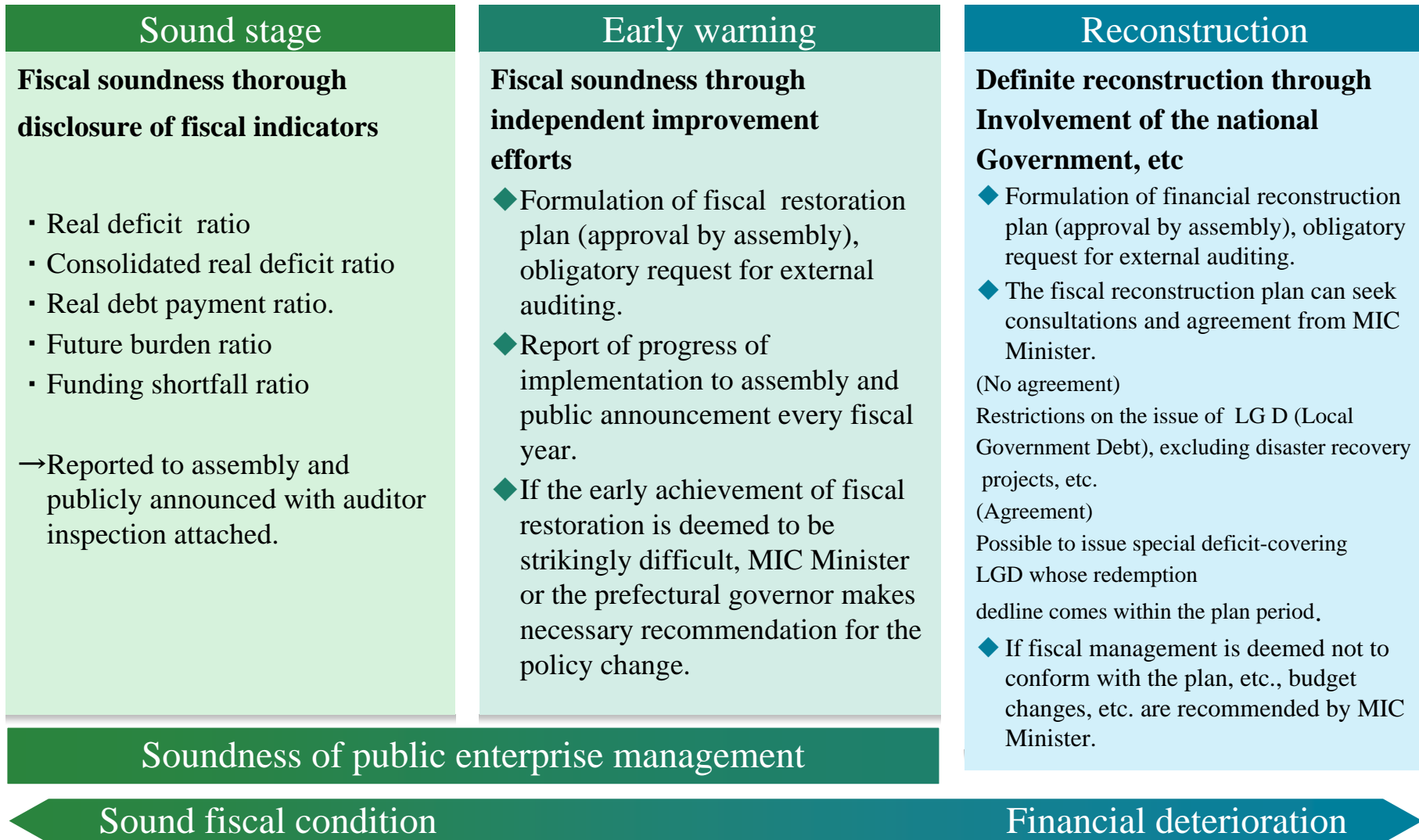


Scope of fiscal indicators in the New Law





Early Warning System and Reconstruction System



Multiple maturities and types of Public Offering

- ◆ 44 (27 prefectures and 17 Designated Cities) entities issue public offering bond independently in FY2008.
- ◆ Terms & Conditions are decided mainly by negotiation with syndicated underwriters as well as bidding. Maturities are 5,7,10,15,20,or 30 years, the majority of which is 10 years.

(Unit: Yen in Billion)

	FY1997		FY2002		FY2008(scheduled)	
	No. of Entities	Total Amount	No. of Entities	Amount Issuance	No. of Entities	Amount Issuance
10y	28	185	28	179	36	2,570
7y					1	20
5y			15	43	26	1,120
20y					19	570
30y					10	175
Joint LGB (10year)					30	1,230
Foreign Bond	2	43	0	0	1	50
Total	28	228	29	222	44	5,735



Planned Issuance for Nationwide Public Offering LGBs in Fiscal-Year 2008

Local Government	Fiscal-Year 2008 (Unit: Yen in Billion)						Local Government	Fiscal-Year 2008 (Unit: Yen in Billion)					
	Total	5y	10y	20 or 30y	Joint	Foreign bond		Total	5y	10y	20 or 30y	Joint	Foreign bond
Hokkaido	360	120	180	-	60	-	Fukuoka	160	50	70	40	-	-
Miyagi	68	15	-	-	53	-	Kumamoto	60	10	20	-	30	-
Fukushima	40	20	20	-	-	-	Oita	20	-	10	-	10	-
Ibaragi	37	-	-	-	37	-	Kagoshima	45	10	-	-	35	-
Tochigi	10	-	10	-	-	-	Sapporo City	110	30	30	20	30	-
Gunma	20	-	20	-	-	-	Sendai City	40	10	-	-	30	-
Saitama	225	-	150	40	35	-	Saitama City	10	-	10	-	-	-
Chiba	265	40	150	40	35	-	Chiba City	65	-	35	-	30	-
Tokyo	550	-	400	100	-	50	Kawasaki City	110	35	10	30	35	-
Kanagawa	345	110	140	65	30	-	Yokohama City	240	30	120	90	-	-
Niigata	100	-	40	-	60	-	Niigata City	20	-	10	-	10	-
Yamanashi	10	-	10	-	-	-	Shizuoka City	15	-	-	-	15	-
Nagano	80	20	-	-	60	-	Hamamatsu City	10	-	10	-	-	-
Gifu	30	10	10	-	10	-	Nagoya City	130	20	80	30	-	-
Shizuoka	220	30	80	50	60	-	Kyoto City	140	30	40	10	60	-
Aichi	240	40	120	20	60	-	Osaka City	330	60	150	60	60	-
Kyoto	130	20	40	20	50	-	Sakai City	10	-	10	-	-	-
Osaka※	580	240	260	-	60	-	Kobe City	130	20	30	40	40	-
Hyogo	310	100	110	40	60	-	Hiroshima City	65	-	25	-	40	-
Shimane	10	10	-	-	-	-	Kita-Kyushu City	80	10	20	20	30	-
Okayama	20	-	20	-	-	-	Fukuoka City	150	30	55	20	45	-
Hiroshima	150	-	70	20	60	-	Total	5,750	1,120	2,575	755	1,230	50
Tokushima	10	-	10	-	-	-							

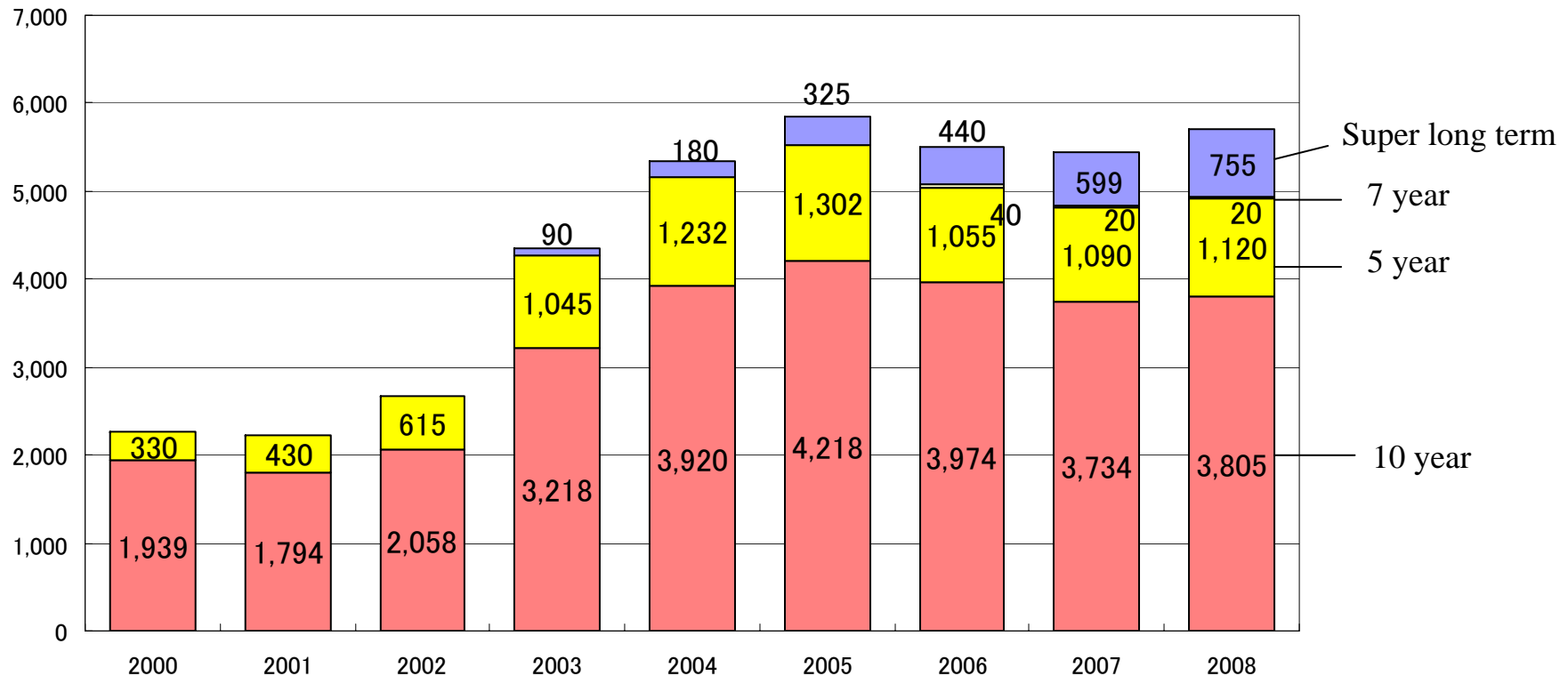
※Osaka's plan includes 7y bond(20Billion)



Trends in Issuance of Public Offering Bonds by Maturity

- ◆ Japanese LGs (local governments) are showing an increasing preference for super long-term (20&30 years) issues, with desire to lower refinancing risk and their shift to public offerings as the availability of super long-term public funds has decreased due to the decentralization and the FILP (Fiscal Investment and Loan Program) reform.

(Unit: Yen in Billion)





Public Offering Joint-LGB

– High liquidity with \$1 billion issue monthly

1. High credit

- ◆ Joint-LGB (Local Government Bond) is publicly-offered joint obligations issued by 30 local governments throughout Japan. It was first issued in April 2003. Each issuer guarantees the full amount of debt payment at each issue.

2. High liquidity

- ◆ Joint-LGB is issued monthly for ¥100 billion (equivalent to about \$1 billion), which is one of the largest sizes among Japanese non-JGB bonds. Currently total outstanding bonds are nearly ¥6 trillion. Due to large issuance amount and frequency, Joint-LGB has certain share in Yen-denominated portfolio of the Lehman Aggregate Index.

3. Special Sinking Fund for liquidity

- ◆ Funds are established with the commissioned bank to ensure timely payment of principal and interest without delay in the event of an unforeseen emergency. These are from the debt payment sinking funds of each issuer. Specifically, the 30 issuers as a whole put aside approximately 10% of the amount of the one month payment each year.

4. Benchmark bond future potential

- ◆ Thus, Joint-LGB becomes one of the leading benchmark bonds among non-JGB bonds. More LGs plan to join the Joint-LGB issuers and outstanding Joint -LGBs will keep accumulating. Thus, this will increase the presence in the bond market more in the future.

5. Trading Indication

- ◆ We are about to start Joint -LGB trading indication in English site of Bloomberg in order to provide transparent price of major underwriters every day.

6. Issue Outline of Joint-LGB

- ◆ We prepared the issue outline of the Joint-LGB. Please refer to the attached document or web site. (<http://www.chihousai.or.jp/english>)



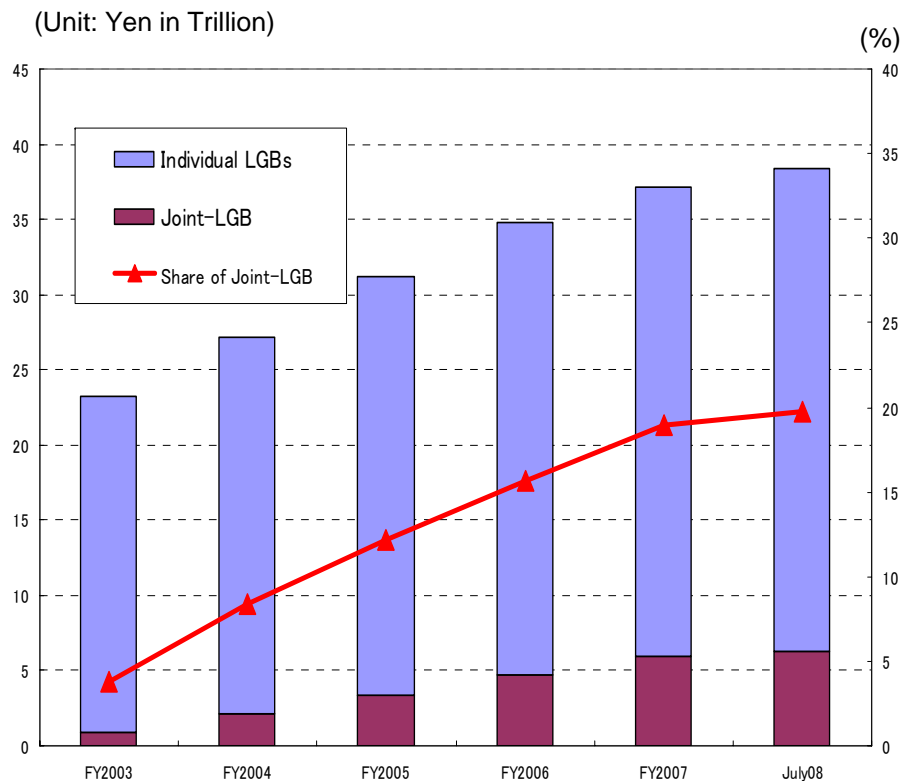
Public Offering Joint-LGB

– High credit and high liquidity

Article 5-7 (Joint Issuance of Local Bonds, Local Finance Law)

- ◆ When local debts are raised by issuing bonds two or more local public bodies may, on approval of their respective assemblies, issue bonds jointly. Such local public bodies shall be collectively responsible for the redemption of the local debts and the interest payment.

Individual LGBs and Joint-LGB outstanding



Issuance Terms	
FY2008 total Issuance	Total of ¥1.23trillion (about ¥100 billion issued every month)
Redemption method/Maturity	Bullet redemption / 10 years
Amount of Minimum Unit	100,000 yen
Issue Date	25 th of every month
Coupon	Fixed (rate differs based on issuance month)
Coupon Payment	25 February and 25 August, irrespective of issuance month

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Tax Exemption Scheme

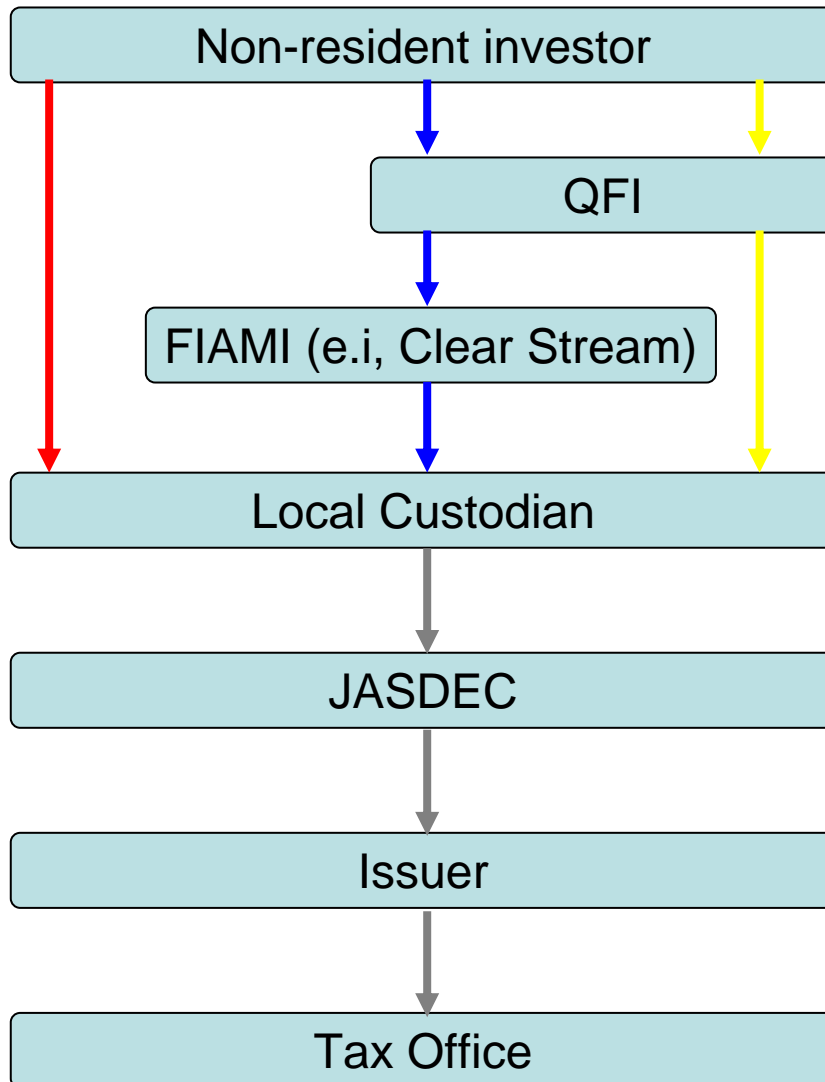
- ◆ Starting in 2008, with the Article 5-2 Act on Special Measures Concerning Taxation (Limited to the provisions related to nonresidents and foreign corporations), the interest gains on LGBs owned by non-resident or foreign corporations which settled by the book-entry system are exempted from withholding tax. Previously, 15% WHT rate was applied to foreign investors. (※With the bilateral tax treaty, the tax charged shall not exceed 10 per cent of the gross amount of the interest)

Conditions

- Non-JGB securities are required to be settled through Japan Securities Depository Centre (JASDEC) - Japan's central securities custody and book-entry transfer system.
- Non-resident investors can enjoy tax exemption only when they hold LGBs through a direct participant of JASDEC (i.e., a local sub-custodian in Japan) or via a designated FIAMI/QFI (i.e., a global custodians).
- In case the beneficiary holds LGBs through a global custodian, such global custodian needs to be FIAMI/QFI.
- Entities who are exempted for JGBs are also eligible for the tax exemption on local government bonds.



Settlement Flow through JASDEC for Tax-Exemption - Requirements



Application form for Tax Exemption

- ◆ When seeking the attached application of LGB tax exemption for the first time, nonresident or foreign corporation are required to submit an application form to the tax office via the institutions as left.
- ◆ However, in the case of investors having exempt status of JGB, they can submit just the copy of existing JGB application, which usually local custodian take care of.
- ◆ Up to now the 16 Global Custodian have registered as QFI (Qualified Foreign Intermediary on the next page).
- ◆ Also Clear Stream was designated as FIAMI this September. Therefore investors can use the service of the Clear Stream through blue line scheme.

※FIAMI= Foreign Indirect Account Management Institution



List of QFI for LGB

1	The Bank of New York	9	BNP PARIBAS Securities Services
2	JPMorgan Chase Bank, N.A	10	Barclays Bank Plc
3	State Street Bank and Trust Company	11	CACEIS Bank Luxembourg
4	HSBC Institutional Trust Services (Singapore) Limited	12	Brown Brothers Harriman & CO.
5	KAS Bank N.V.	13	State Street Trustees Limited
6	Brown Brothers Harriman (Luxembourg) S.C.A.	14	CACEIS BANK
7	Mellon Bank, N.A.	15	Norddeutsche Landesbank Luxembourg S.A.
8	Kredietbank S.A. Luxembourgeoise	16	DnB NOR Bank ASA



Application Form for Withholding Tax Exemption and Notification Form

別紙 3

振替地方債の利子課税の特例に関する非課税適用申告書
 振替地方債の利子課税の特例に関する特例書類
 Application Form for Withholding Tax Exemption based on the Special Taxation Measures Law (Article 5-2, paragraph 1 Item 2)
 Special Document for Withholding Tax Exemption based on the Enforcement Ordinance of the Special Taxation Measures Law (Article 3, paragraph 5)

平成 年 月 日
 Date:

税務署長殿 To: the District Director of _____ Tax Office
 (発行体 _____ 経由 (発行体の名称を記載) Via: _____ (Name of the Issuer))

ｱｶﾀ 住所等 (注 1) Address of the applicant (Note1)	
ｱｶﾀ 氏名又は名称 Name of the applicant	
適格外国証券投資信託の名称 (注 2) Name of the Qualified Foreign Securities Investment Trust (Note2)	

本様式により : 下記の特定振替機関等又は適格外国仲介業者から振替記載等を受けている振替地方債の利子につき租税特別措置法第 5 条の 2 第 1 項第 2 号の規定の適用を受けたいので、この旨申告します。
 With this form : We hereby file for tax-exemption based on the Special Taxation Measures Law Article 5-2, paragraph 1, Item 2 and the relevant regulations thereunder, with regard to Japanese Local Government Bonds recorded in an account established in the Japan Securities Depository Center Book-entry System through a Sub-custodian or Qualified Foreign Intermediary (QFI) stated as below.

特定振替機関等の営業所等又は適格外国仲介業者の特定国外営業所等の名称及び所在地 Name and Address of the Sub-custodian or specified foreign branch of the QFI		適格外国仲介業者の特定国外営業所等 (の長) による署名及び受理日付(注 4) Signature of the qualified person at the QFI's specified foreign branch and Date of receipt by it (Note4)
納税管理人の氏名及び住所 Name and Address of the applicant's tax agent (if any)		
摘要 (注 3) Remarks (Note3)	<div style="border: 1px solid black; border-radius: 50%; width: 30px; height: 30px; display: flex; align-items: center; justify-content: center;"> 非 </div>	特定国外営業所等が確認した確認書類の名称(注 4) Name of the ID Document by which the QFI's specified foreign branch identified the applicant (Note4)
		特定振替機関等の受理日付(注 4) Date of receipt by the Sub-custodian (Note4)



Amendment of Cabinet Order to enable Euroyen bond issue

- ◆ There have been strong needs from international investors and LGs to amend the Cabinet Order to enable the issuance of Euroyen bond.
- ◆ In order to prepare investment environment, Japanese Government amended the Cabinet Order this September to enable the issuance of Euroyen bond which is yen-denominated LGB issued in overseas markets.
- ◆ With the Cabinet approval for the amendment of Cabinet Order, LGs are allowed to issue yen-denominated LGBs on overseas markets (euroyen bonds).

Article 36. Special Case for Overseas Local Government Bonds

- ◆ The provisions in Article 24 – 35 notwithstanding, the following transactions related to overseas local government bonds which issued outside of Japan may be conducted in accordance with the laws or the practices of the market of issuance: (1)issuance, (2)transfers between registered and bearer bond systems, (3) the keeping of ledgers for such bonds, payments related to redemptions of bonds that have had coupons detached, and interest payments to bearers of the detached coupons.



Information in English Available on Website

Japan Local Government Bond Association Website (<http://www.chihousai.or.jp/english>)

English Publications on JLGBs

Presentation Materials	Local Government Bond System and Market in Japan
	Public Offering Joint-Local Government Bond
	Shizuoka Prefecture, Kyoto City, Kawasaki City and some other issuers
Statistics*	Statistics of 44 Public Offering Local Government Bond Issuers
	Revenue and Expenditure of 47 Prefectures and 17 Designated Cities
White Paper	FY2006 Settlement White Paper on Local Public Finance, 2008
Laws and Ordinances	Law on the Fiscal Consolidation of Local Governments
	Local Autonomy Law
	Local Finance Law
	Local Allocation Tax Law
Others	Issue Outline of Joint Local Government Bond
	Terms and conditions of Tokyo Metropolitan Government Bond

* Available in PDF and Excel file

Regular overseas road shows from this year

- ◆ Japanese LGs have held overseas road shows and will increase its frequency.
- ◆ NG and Japanese LGs jointly hold the first overseas road show this time and will continue them annually.

Entities	Activities
Tokyo Metropolitan Government	Visit: London (May 2007) London, Paris, Frankfurt (Oct 2007) Seoul, Beijing, Hong Kong (July 2008) North America (Autumn 2008)
Fukuoka Prefecture	Visit: Frankfurt, Dusseldorf, Paris Period: January 2008
Japan Local Government Bond Association	Visit: London, Frankfurt, Paris Period: from 16 February to 27 February 2008
JLGB European Road Show 2008	Visit: London, Berlin, Frankfurt, Paris, Dublin Period: from 6 October to 11 October 2008 Participants: Ministry of Internal Affairs and Communications, Shizuoka Prefecture, Kyoto City, Kawasaki City, and JLGBA
Road Show 2009 2010	To be confirmed

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Decentralization Reform & Local Bond/Loan System

First Step 1993-2001

- 1993 The Diet resolution of decentralization
- 1995 Decentralization Promotion Law enacted
Decentralization Promotion Committee (DPC) was established.
- 1997 DPC's 4 recommendations submitted to the Prime Minister.
- 1998 The Cabinet decided the Decentralization Promotion Plan
- 1999 The Decentralization Package Law was promulgated.



Many reforms were conducted aiming to change the relationship between the central and local governments to a new more equal and cooperative one.

As a part of the first step of decentralization reform, Gov. control of LGs' Bond/Loan was reformed. It took effect on April 1, 2006.

Second Step 2001-2006

Tax and financial system between the central and local governments are considered and "Three-Part Reform Package" has been decided to promote decentralization.

- ¥4 tr. earmarked grants abolished.
- ¥3 tr. Income Tax has decided to be transferred to LGs as Local Taxes
- LAT system has been reviewed and reformed

Also new legal scheme to assure sustainable finance of LGs is submitted to the Diet.

Third Step 2007-2009

- 2006 Decentralization Reform Promotion Law enacted
- 2007 Decentralization Reform Promotion Committee (DRPC) started on April 1.
- 2008 DRPC will submit the recommendation.



BIS risk weight

Article 58 (Exposure to Japanese Local Governments)

- The risk weight for that portion of yen-denominated exposure to Japanese local governments (excluding that which will be repaid out of income from specific projects only) that is funded in yen will be 0%.
- (2) Excluding the above, the risk weight for exposure to Japanese local governments (excluding that which will be repaid out of income from specific projects only) will be as stipulated in the left-hand column of the table in Article 56-1, in accordance with the credit rating assigned to the Japanese government or the credit risk classification in line with the country score.

Article 56 (Exposure to Central Government and Central Bank)

- The risk weight for exposure to the central government and central bank will be as stipulated in the left-hand column of the following table, in accordance with credit ratings or credit risk classifications in line with the country risk score. However, the risk weight will be 100% if there is no credit rating.

1 In case of credit rating assigned by qualified rating agency

Credit risk classification	1-1	1-2	1-3	1-4	1-5	1-6
Risk weight(%)	0	20	50	100	100	150

2 In case of country risk score

Credit risk classification (country risk score)	0	1	2	3	4	5	6	7
Risk weight(%)	0	0	20	50	100	100	100	150

Source: FSA Notification #19 Standards for Banks to Assess Whether Their Adequacy is Appropriate Given Asset Holdings Based on Article 14-2 of the Banking Law, 27 March 2006, Financial Services Agency.



Act on Special Measures Concerning Taxation

Article 5-2 (Special Provisions for Taxation on Interest on Book-Entry Transfer National Government Bonds)

- (1) Where a nonresident or foreign corporation who satisfies the requirements specified in each of the following items for the category of bonds listed in the relevant item that are held thereby, receives payment of interest (excluding interest subject to the provision of Article 8(1) or (2)) on book-entry transfer national government bonds prescribed by Article 88 of the Act on Book-Entry Transfer of Company Bonds, etc. (excluding coupon-only book-entry transfer national government bonds prescribed in Article 90(3) of the said Act; hereinafter referred to in this Article as `book-entry transfer national government bonds`) or local government bonds which shall be subject to the provisions of the said Act pursuant to Article 66 of the said Act as applied mutatis mutandis pursuant to Article 113 of the said Act (hereinafter referred to in this Article as `book-entry transfer local government bonds`), for which the nonresident or foreign corporation has made entries or records under the book-entry transfer system in his/her or its account established with a specified book-entry transfer institution, specified account management institution or specified indirect account management institution (hereinafter referred to in this Article as a `specified book-entry transfer institution, etc.`) or a qualified foreign intermediary, via a business office or any other office of the said specified book-entry transfer institution, etc. located in Japan (including a post office; hereinafter referred to in this Article as a `business office, etc.`) or a specified overseas business office, etc. of the said qualified foreign intermediary, income tax shall not be imposed with respect to such interest to be received (limited to the part of interest equivalent to the amount calculated pursuant to the method specified by a Cabinet Order as the amount corresponding to the period during which the nonresident or foreign corporation has continued to hold the said book-entry transfer national government bonds or the said book-entry transfer local government bonds (limited to the period during which he/she or it has continued to hold entries or records under the book-entry transfer system regarding the said book-entry transfer national government bonds or the said book-entry transfer local government bonds; hereinafter referred to in this Article as the `holding period`):

Source: Section 1 Interest Income and Dividend Income, Chapter II Special Provision for the Income Tax Act, Act on Special Measures Concerning Taxation (Limited to the provisions related to nonresidents and foreign corporations).



Tax Exemption Scheme by bilateral treaties

Financial institution domiciled in United Kingdom, France, United States and Australia

- ◆ In addition to the tax exemption scheme 1 , the following tax exemption scheme is also available for the mentioned investors.
- ◆ Based on bilateral treaties between Japan and United Kingdom, France, United States and Australia, financial institutions, such as bank, insurance company, securities firm, pension fund and so on can be exempted from the interest tax of LGBs as long as they submit the following simple document first to Japanese tax authorities. (Please refer to the attached treaty).
- ◆ Other bilateral treaties have the possibility for the same amendment in the future.



Convention for avoidance of double taxation

CONVENTION BETWEEN JAPAN AND THE UNITED KINGDOM OF GREAT BRITAIN AND NORTHERN IRELAND FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL GAINS

Japan and the United Kingdom of Great Britain and Northern Ireland,
Desiring to conclude a new Convention for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital gains,
Have agreed as follows:

Article 11

1. Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other Contracting State.
2. However, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that Contracting State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 10 per cent of the gross amount of the interest.
3. Notwithstanding the provisions of paragraph 2 of this Article, interest arising in a Contracting State shall be taxable only in the other Contracting State if:
 - (a) the interest is beneficially owned by the Government of that other Contracting State, a political subdivision or local authority thereof, or the central bank of that other Contracting State or any institution wholly owned by that Government;
 - (b) the interest is beneficially owned by a resident of that other Contracting State with respect to debt-claims guaranteed, insured or indirectly financed by the Government of that other Contracting State, a political subdivision or local authority thereof, or the central bank of that other Contracting State or any institution wholly owned by that Government;
 - (c) the interest is beneficially owned by a resident of that other Contracting State that is either:
 - (i) a bank
 - (ii) an insurance company;
 - (iii) a securities dealer; or
 - (iv) any other enterprise, provided that in the three taxable years preceding the taxable year in which the interest is paid, the enterprise derives more than 50 per cent of its liabilities from the issuance of bonds in the financial markets or from taking deposits at interest, and more than 50 per cent of the assets of the enterprise consist of debt-claims against persons that do not have with the resident a relationship described in subparagraphs (a) or (b) of paragraph 1 of Article 9 of this Convention;
 - (d) the interest is beneficially owned by a pension fund or pension scheme that is a resident of that other Contracting State, provided that such interest is not derived from the carrying on of a business, directly or indirectly, by such pension fund or pension scheme; or
 - (e) the interest is beneficially owned by a resident of that other Contracting State and paid with respect to indebtedness arising as a part of the sale on credit by a resident of that other Contracting State of equipment or merchandise.
4. For the purposes of paragraph 3 of this Article, the terms 'the central bank' and 'institution wholly owned by that Government' mean:
 - (a) in the case of Japan:
 - (i) the Bank of Japan;
 - (ii) the Japan Bank for International Cooperation;
 - (iii) the Nippon Export and Investment Insurance; and
 - (iv) such other similar institution the capital of which is wholly owned by the Government of Japan as may be agreed upon from time to time between the Governments of the Contracting States through an exchange of diplomatic notes.



Convention for avoidance of double taxation

(b) in the case of the United Kingdom:

- (i) the Bank of England;
- (ii) the Commonwealth Development Corporation; and
- (iii) such other similar institution the capital of which is wholly owned by the Government of the United Kingdom as may be agreed upon from time to time between the Governments of the Contracting State through an exchange of diplomatic notes.⁰

5. The term 'interest' as used in this Article means income from debt-claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures, and all other income that is subjected to the same taxation treatment as income from money lent by the tax laws of the Contracting State in which the income arises. Income dealt with in Article 10 of this Convention shall not be regarded as interest for the purposes of this Convention.

6. The provisions of paragraphs 1, 2 and 3 of this Article shall not apply if the beneficial owner of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arises, through a permanent establishment situated therein and the debt-claim in respect of which the interest is paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 of this Convention shall apply.

7. Interest shall be deemed to arise in a Contracting State when the payer is a resident of that Contracting State. Where, however, the person paying the interest, whether such person is a resident of a Contracting State or not, has in a state other than that of which such person is a resident a permanent establishment in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by such permanent establishment, then:

- (a) if the permanent establishment is situated in a Contracting State, such interest shall be deemed to arise in that Contracting State; and
- (b) if the permanent establishment is situated in a state other than the Contracting States, such interest shall not be deemed to arise in either Contracting State.

8. Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the interest exceeds, for whatever reason, the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.

9. A resident of a Contracting State shall not be considered the beneficial owner of interest in respect of a debt-claim if such debt-claim would not have been established unless a person:

- (a) that is not entitled to benefits with respect to the interest arising in the other Contracting State which are equivalent to, or more favourable than, those available under this Convention to a resident of the first-mentioned Contracting State; and
- (b) that is not a resident of either Contracting State;
Held an equivalent debt-claim against the first Contracting State;

10. No relief shall be available under this Article if it was the main purpose or one of the main purpose of any person concerned with the creation or assignment of the debt-claim in respect of which the interest is paid to take advantage of this Article by means of that creation or assignment.



For further information

- **Japan Local Government Bond Association Website**
(This includes most comprehensive information in English)
<http://www.chihousai.or.jp/english>
- **Ministry of Internal Affairs and Communications (MIC) Website**
<http://www.soumu.go.jp/english>
- **Local Public Finance Bureau, MIC Website**
<http://www.soume.go.jp/english/c-zaisei>
- **Contact point of Japan Local Government Bond Association**
2-11-1, Nagata-cho, Chiyoda-ku, Tokyo 100-6125, Japan
TEL +81-(0)3-3508-1751 FAX +81-(0)3-3501-7723
- **Local Bond Division, Local Public Finance Bureau, Ministry of Internal Affairs and Communications**
2-1-2, Kasumigaseki, Chiyoda-ku, Tokyo 100-8926, Japan
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This is the presentation material made by Ministry of Internal Affairs and Communications in use of a seminar in Europe October 2008.

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