



MIC

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

**Ministry of Internal Affairs
and Communications**

**JLGB Asian Road Show
October 2009**



- I Executive Summary
- II Market Overview
- III Credit Outlook
- IV Attractiveness
- V Outreach efforts to foreign investors



Executive Summary

Japanese Local Government Bond – A Safe Investment

(1) Market Overview

- ◆ Similar credit status to JGB with strong national government support and check
- ◆ Second largest muni market in the world (\$2 trillion)
- ◆ Sharp increase of public offering (No. of issuers: 29 to 47 in 6 years, Issuance: Triple in 10 years)

(2) Attractiveness

- ◆ Stable spread range over JGB market with average pick up of 10 ~ 30 basis points
- ◆ Public Offering Joint-Local Government Bond - High liquidity with \$1.2 billion issue monthly
- ◆ Multiple Maturities available from 3, 5, 7, 10, 15, 20 or 30 years

(3) Credit Outlook

- ◆ Japanese local governments are supported by the central government:
 - Local Allocation Tax System, Consultation System, Fiscal Rehabilitation Law
- ◆ Increasing number of credit ratings, 12 entities by Moody's and 7 entities by S&P
- ◆ 0% BIS risk weight and No legal concept of bankruptcy and debt discharge in Japan

(4) Outreach efforts to foreign investors

- ◆ Tax Exemption for Interest Received by Non-Residents on Book-Entry Transfer System
- ◆ Enable to issue yen-denominated LGBs on overseas markets (Euroyen bonds)
- ◆ Regular overseas road show



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Introduction to Japan's Local Government System

< The Basis of Local Government >

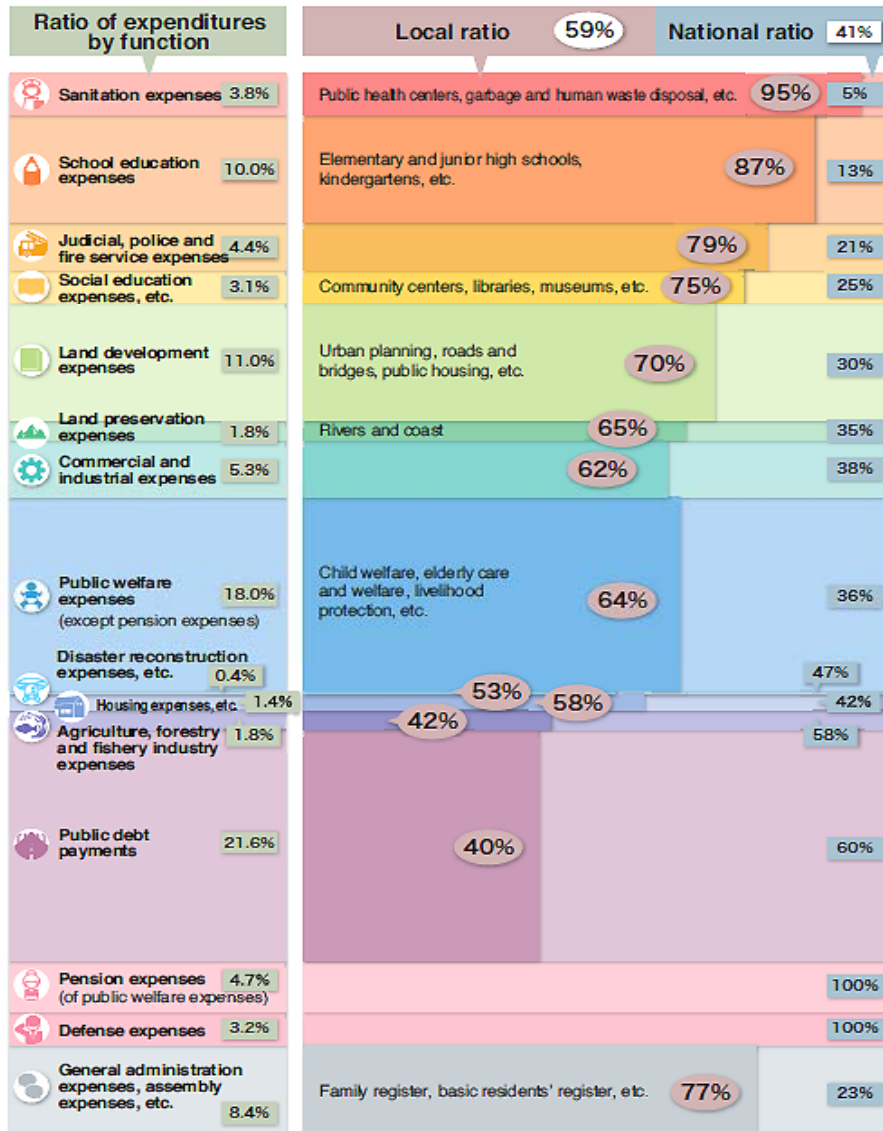
- ◆ Japan has a 'two-tier' system of local governments, which consists of prefectures and municipalities (cities, towns, and villages).
- ◆ The total number of local governments (i.e. prefectures and municipalities) was 1,844 as of Sep, 2009 – 47 prefectures (including Tokyo Metropolis), 18 designated city and 1,779 municipalities.



- ◆ 47 (29 prefectures and 18 designated cities) entities issue public offering bond independently in FY2009.

Source: Local Government Bond Association

Functions of Japanese Local Governments



◆ Local governments have relatively large responsibilities & functions.

◆ The greatest portion of local government annual expenditures is directed toward supporting everyday public services: public health and sanitation, education, social education, and police and fire prevention.

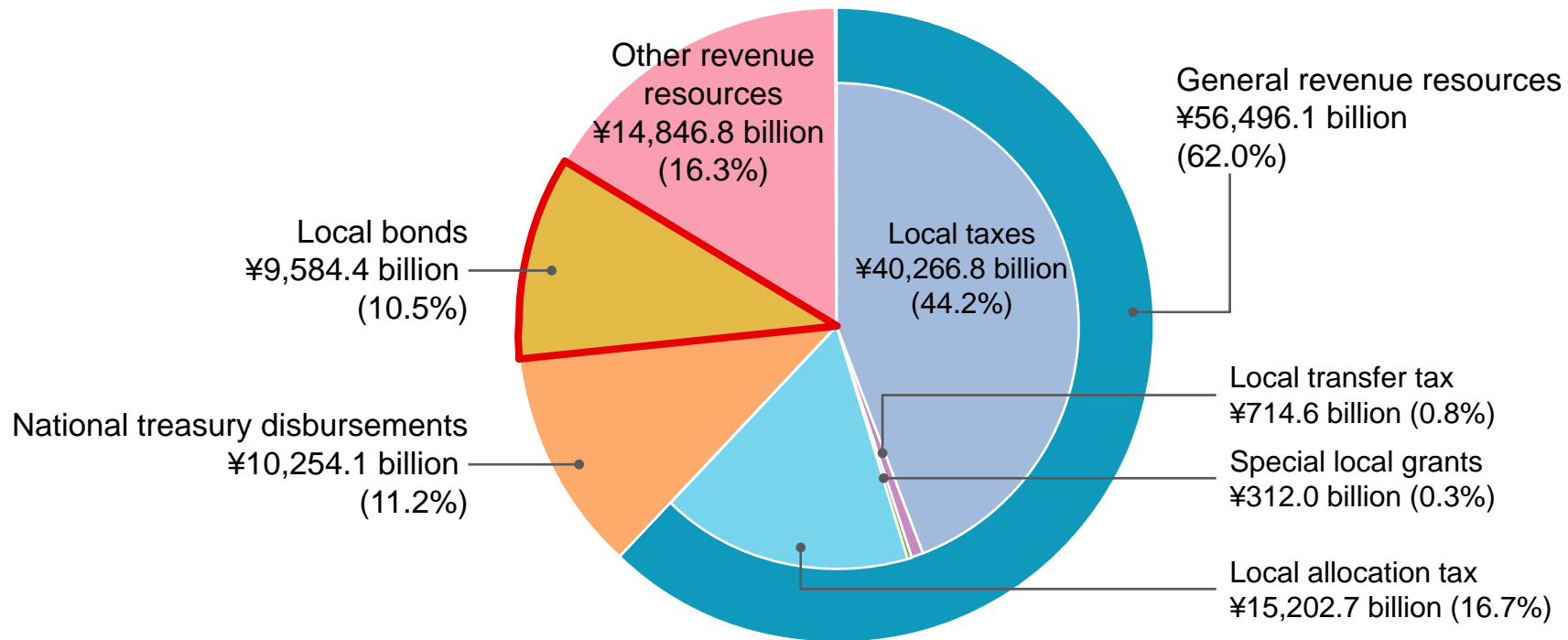
Source: White Paper on Local Public Finance, 2009 by Ministry of Internal Affairs and Communications

The revenue of local governments

- ◆ The revenue of local governments comes mainly from local taxes, local allocation tax(LAT), national treasury disbursements, and local bonds.

< Revenue Breakdown (FY2007 settlement) >

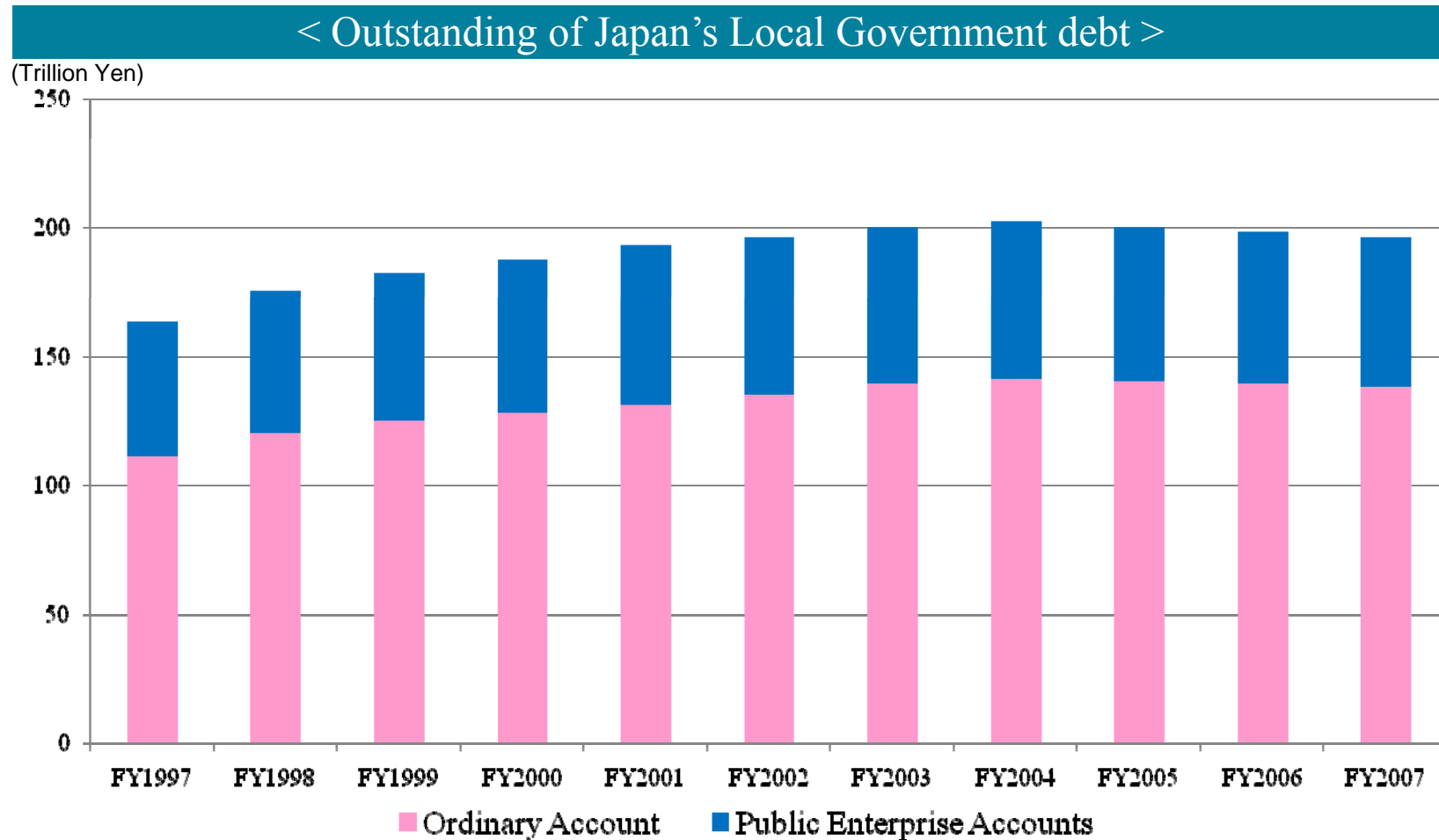
Net total ¥91,181.4 billion





Existing Local Public Entity Borrowing

- ◆ Japan's Local Government debt has ¥196 trillion (equivalent to about \$2 trillion) outstanding. Japan sits on second only to the U.S.



Source: Ministry of Internal Affairs and Communications



Funds for Local Government Bond/Loan

Category		Details
Public Funds	National Government Funds	Government funds consist mainly of Fiscal Loan Funds. Fiscal Loan Funds have been decreasing since the drastic reforms in Treasury Investment and Loan System in 2001.
	Japan Finance Organization for Municipalities (JFM)	JFM lends money on attractive long-terms and low-interests to local governments. The major source of revenue for the JFM are its own bonds. JFM raises funds mainly in debt capital market.
Private Funds	Public Offering	<p>A number of large local governments issue their bonds on the open market. At present, 47 local governments issue this kind of bond.</p> <ul style="list-style-type: none"> - The maturity is 3, 5, 7, 10, 15, 20 and 30 years. - Redemption Method is bullet. - Setting Coupon is Fixed Rate.
	Private Placement	Most local governments borrow long-term money from financial institutions, such as commercial banks, Agricultural Co-operative Associations, and Insurance Companies .



Funding Breakdown for Fiscal-Year 2009

Local Government Bond Plan

- ◆ The Government formulates the ‘Local Government Bond Program’ in advance of the beginning of every fiscal year.
- ◆ This program sets guidelines for the size of local bond/loan. This is one of the main instruments for the Central Government to keep public expenditure effectively under control.

(Billions of yen)

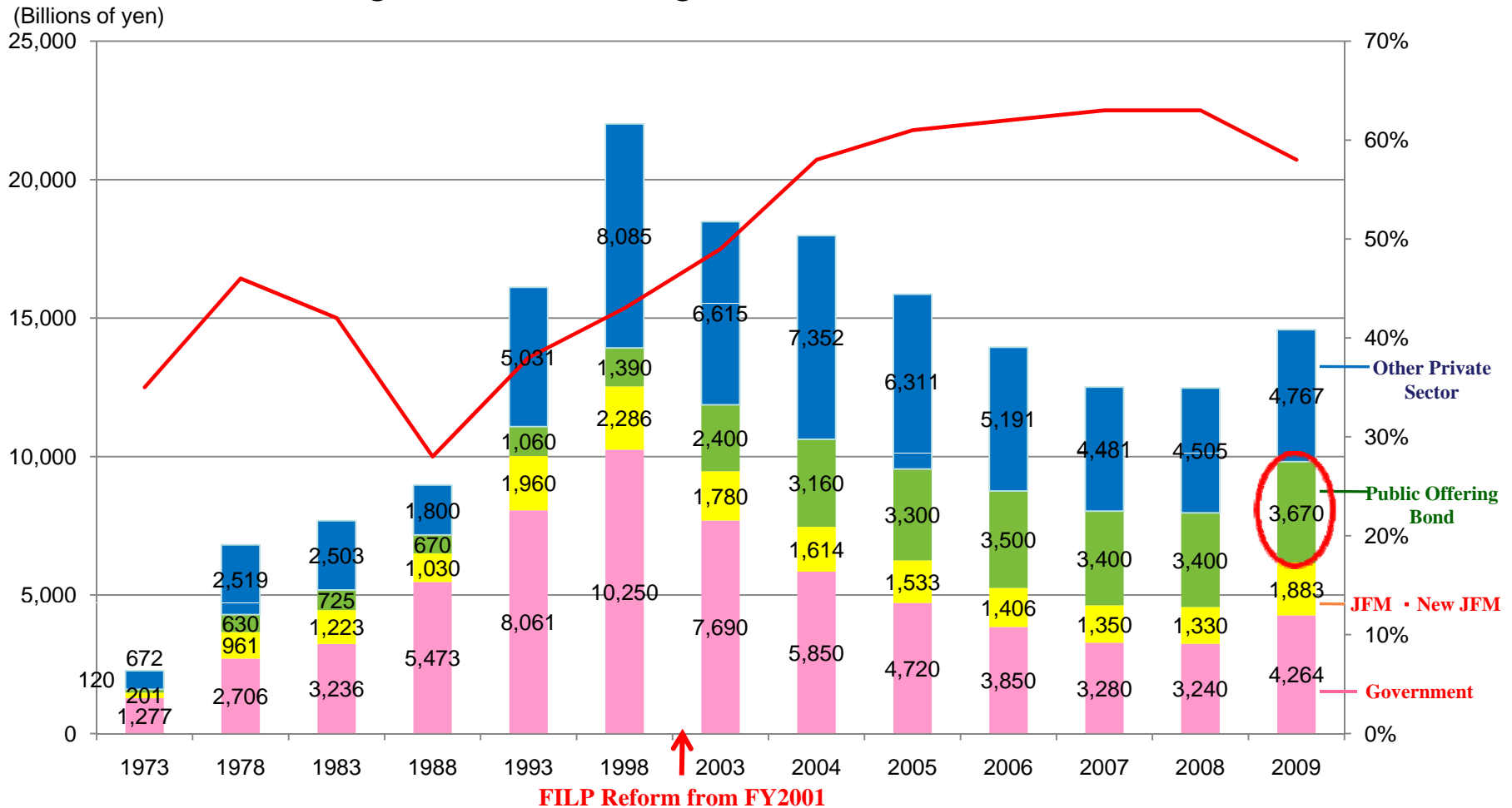
Category	FY2009 Plan		FY2008 Plan		Difference	
	(A)	%	(B)	%	(A-B)	(A-B)/(B) (%)
Government Funds	3,934	27.7	3,240	26.0	694	21.4
Japan Finance Organization for Municipalities Funds	1,833	12.9	1,333	10.7	500	37.5
Loans from National Budget	(182)	-	(213)	-	(-31)	(-14.5)
Public Sector Total	5,767	40.7	4,573	36.6	1,194	26.1
Public Offerings	3,670	25.9	3,400	27.2	270	7.9
Private Placements	4,747	33.5	4,505	36.1	243	5.4
Private Sector Total	8,417	59.3	7,905	63.4	513	6.5
Total	14,184	100.0	12,478	100.0	1,707	13.7

Source: The above figures are based on the LGB plan announced by MIC in Feb 2009 .



Historical changes of annual issue amount

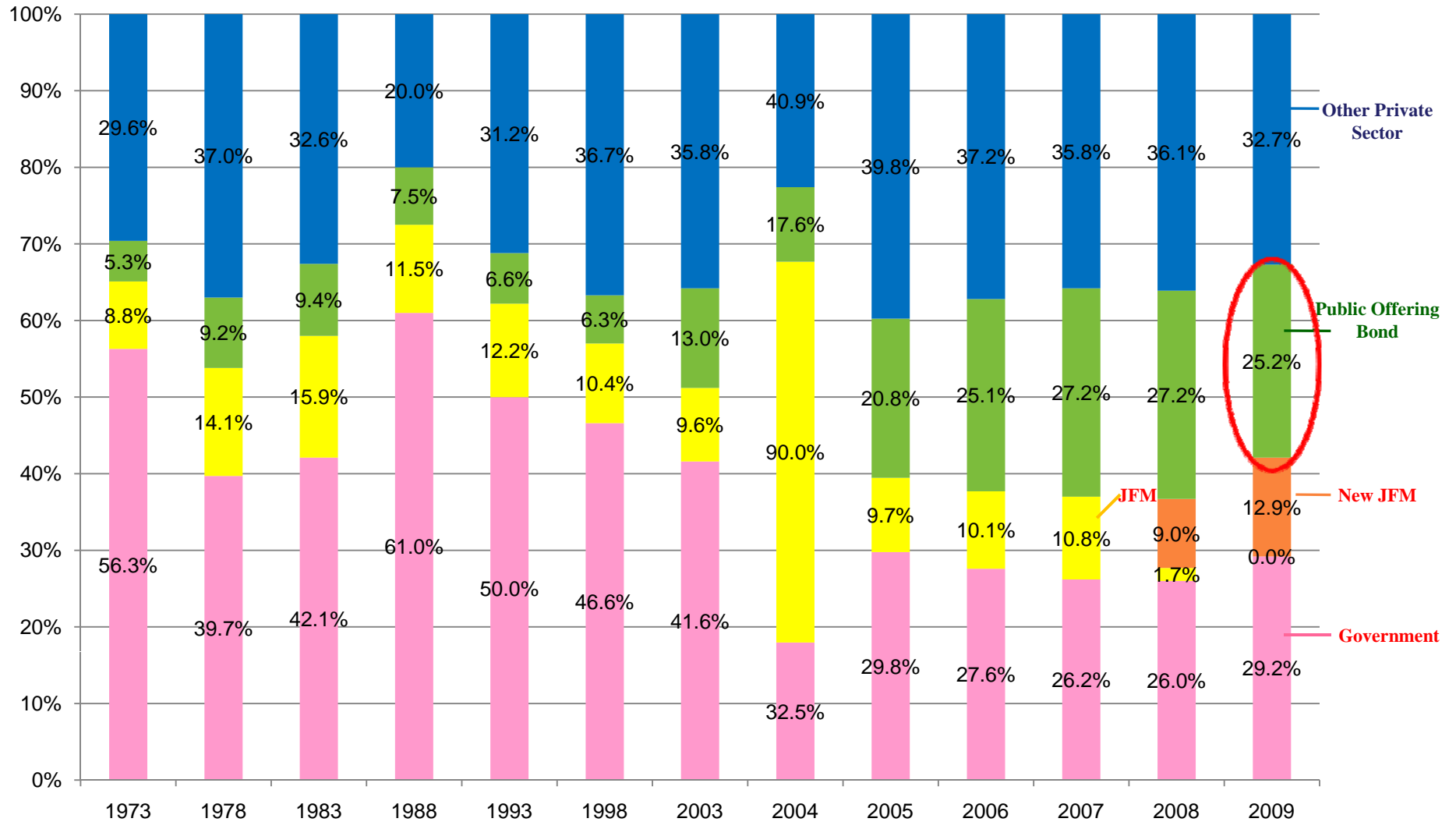
- ◆ Reduction in government funding due to FILP (Fiscal Investment and Loan Program) Reform to minimize government funding role from FY2001.



Source: Ministry of Internal Affairs and Communications
 ※The above is the revised figures made by MIC



Composition of Funds of Local Government debt

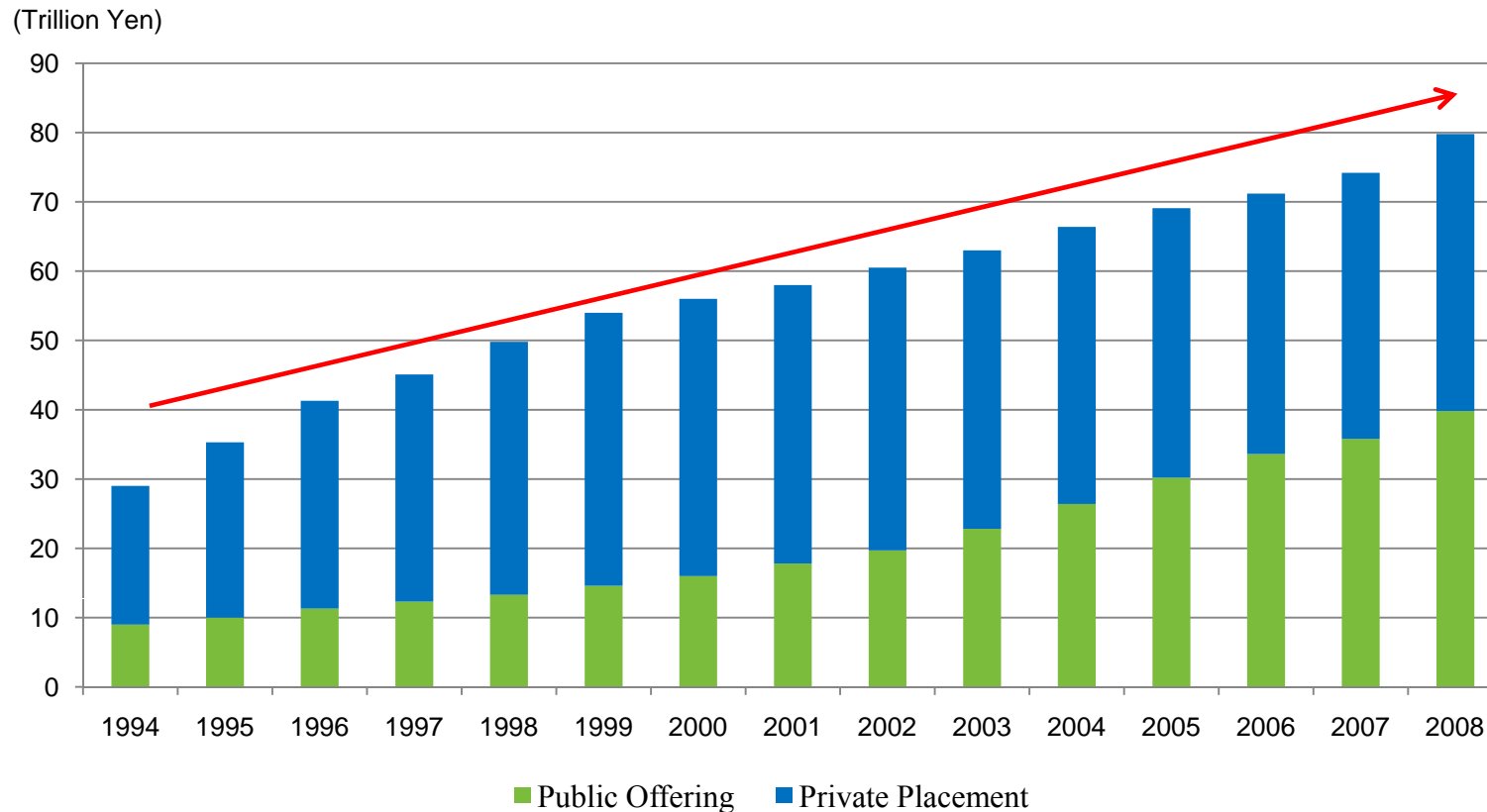


Source: Ministry of Internal Affairs and Communications
 ※The above is the revised figures made by MIC



Trends of LGB outstanding (Private sector funding)

- ◆ 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.



Source: Local Government Bond Association



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Safety of Japanese LGB

- ◆ There is strong financial support system and check system for Local Governments (LGs) by the Japanese central government as follows.

1. Secured resources for debt payment of LGB
– Local Allocation Tax System

2. Consultation system for the issuance of LGB

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



Creditworthiness of LGB

- ◆ With regard to the selection of nationwide public offering LGB issuers, no special designations or permits are required to become a public offering LGB issuer.
- ◆ Up to now, 47 (29 prefectures and 18 designated cities) entities issue public offering bond independently in FY2009.
- ◆ All LGB issuers are supported by the following recognitions of Japanese LGB.

1. High Credit Rating

2. 0% risk weight to LGB in the standardized approach of
BIS regulations (Basel II)

3. No legal concept of bankruptcy and debt discharge in Japan



1. Secured resources for debt payment of LGB

1. Own authority of taxation

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

2. 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.

3. 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.

4. 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 to the amount of five national taxes (32% of income tax and liquor tax, 34% of corporate tax, 29.5% of consumption tax, 25% 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

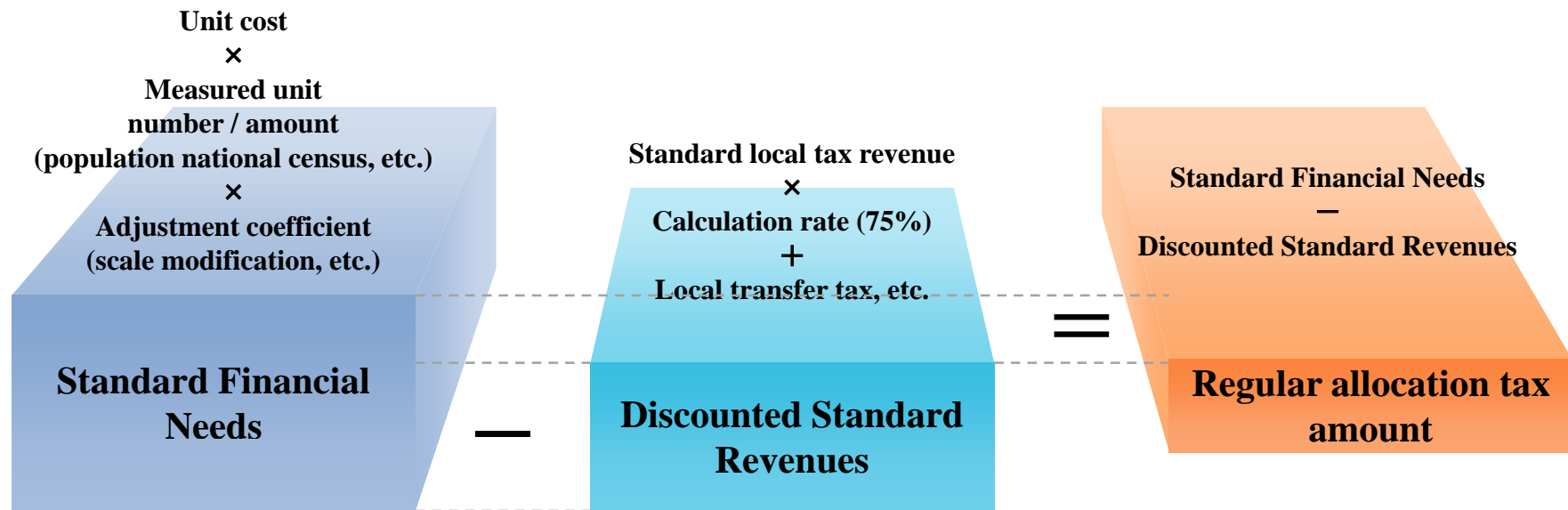
- ◆ The allocation tax shall be equal to 32% of income tax and liquor tax revenue, 34% of corporation tax revenue, 29.5% of consumption tax revenue and 25% of tobacco excise revenue.
2. The total sum of allocation tax to be granted every fiscal year shall be calculated by summing up 32% each of the estimated revenues of income tax and liquor tax, 34% of corporation tax, and 29.5% of the estimated revenue of consumption tax, and 25% 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.



Local Allocation Tax System

LAT distribution: Calculating Standard Financial Needs&Revenues

- ◆ The Central Government protects revenue sources required for principal/interest redemption on local government bonds by adding a considerable portion to the standard fiscal demand amount when calculating local allocation tax.
- ◆ 94% of the LAT is distributed to each LGs as the following mechanism:
[Standard Financial Needs] — [Discounted Standard Revenues]
- ◆ 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

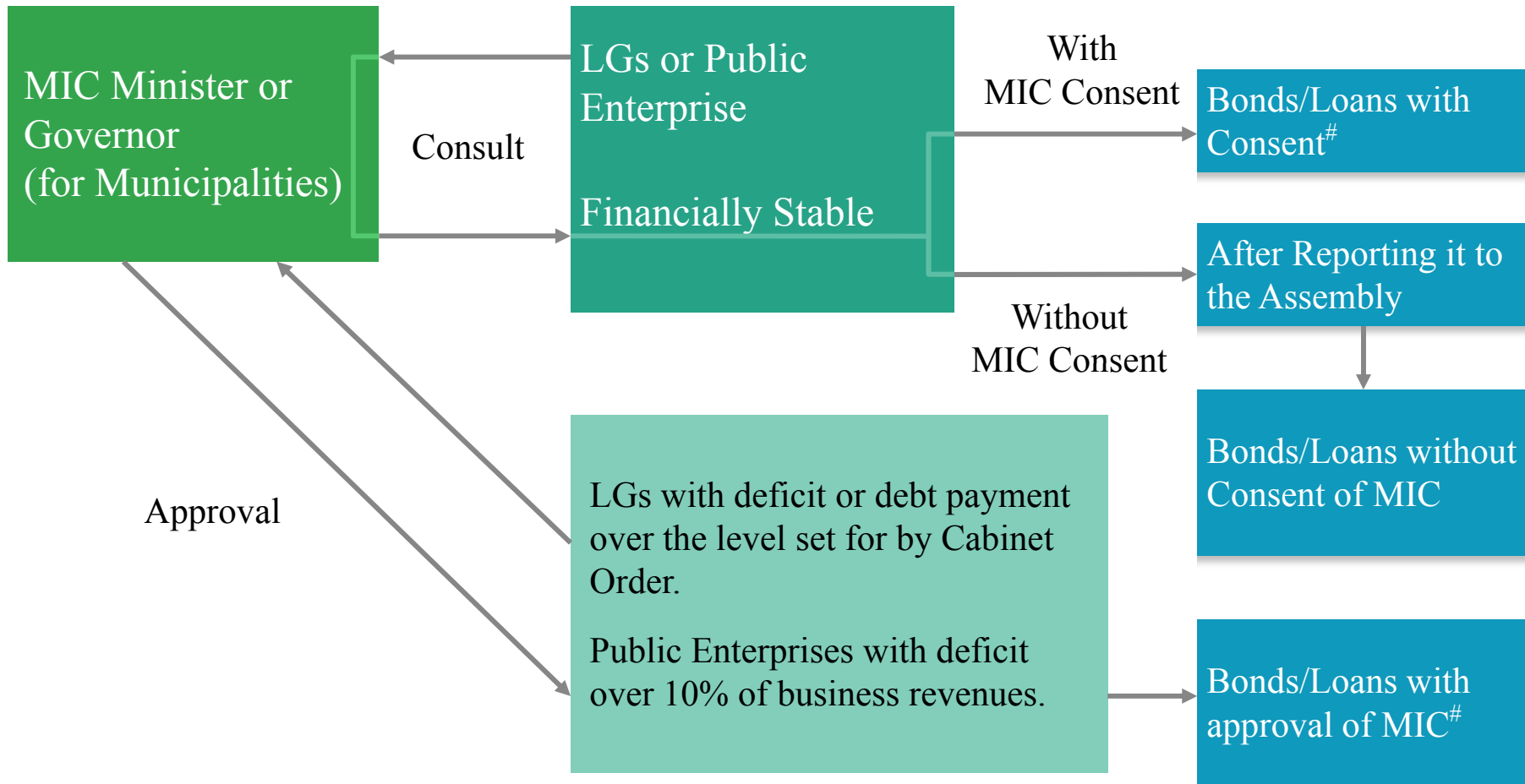
In order to issue the LGBs without the consent, the head of the local government must report it to the assembly.

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

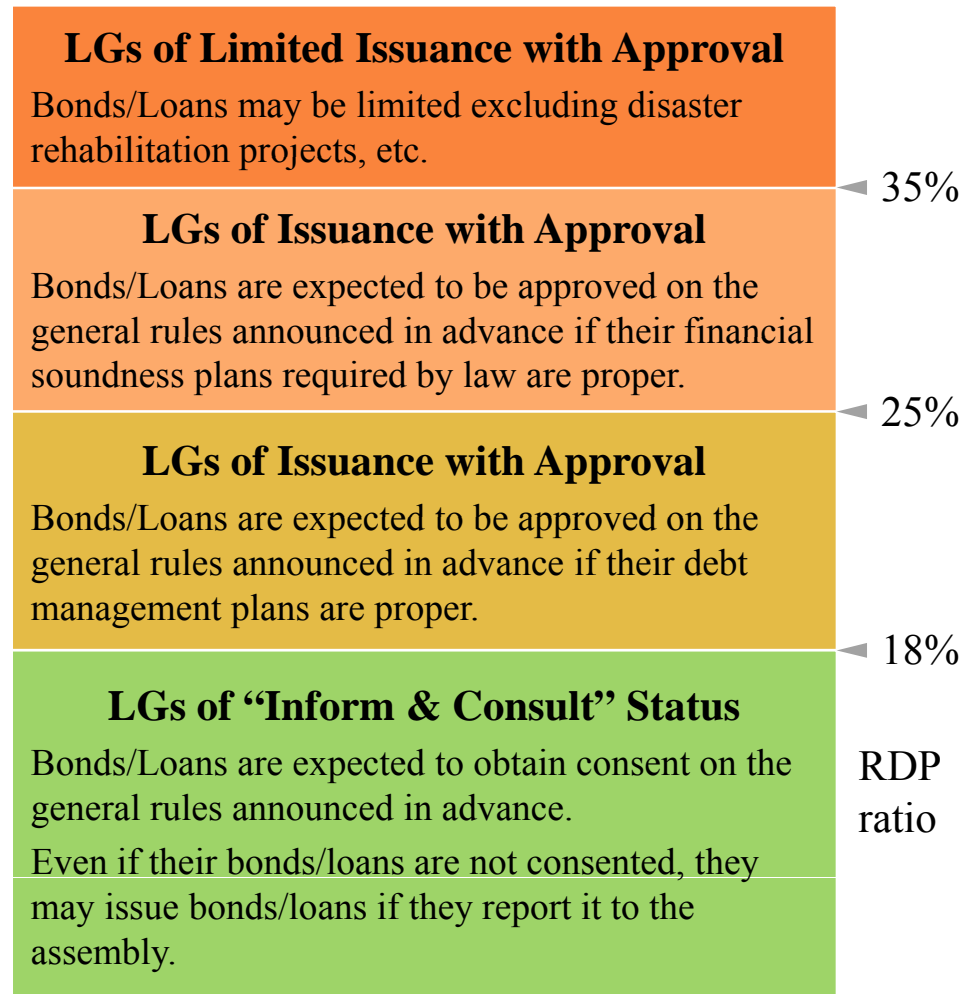


2. Consultation system for the issuance of LGB ②

- ◆ 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/loan 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 draft a debt management plan and obtain approval of the MIC minister, based upon general approval standard.
- ◆ Issuers with the ratio between 25% ~ 35% must draft a financial soundness plan required by law and obtain approval of the MIC minister, based upon general approval standard.
- ◆ Issuers with the ratio of 35% or more must draft a financial rebuilding plan and obtain approval of the MIC minister. Otherwise, Issuers are prohibited from debt issue excluding disaster rehabilitation projects, etc.





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

The Law to strengthen the Fiscal Soundness of Local Governments

- ◆ The Law Relating to the Fiscal Soundness of LGs became effective from FY2008.

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 the 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.



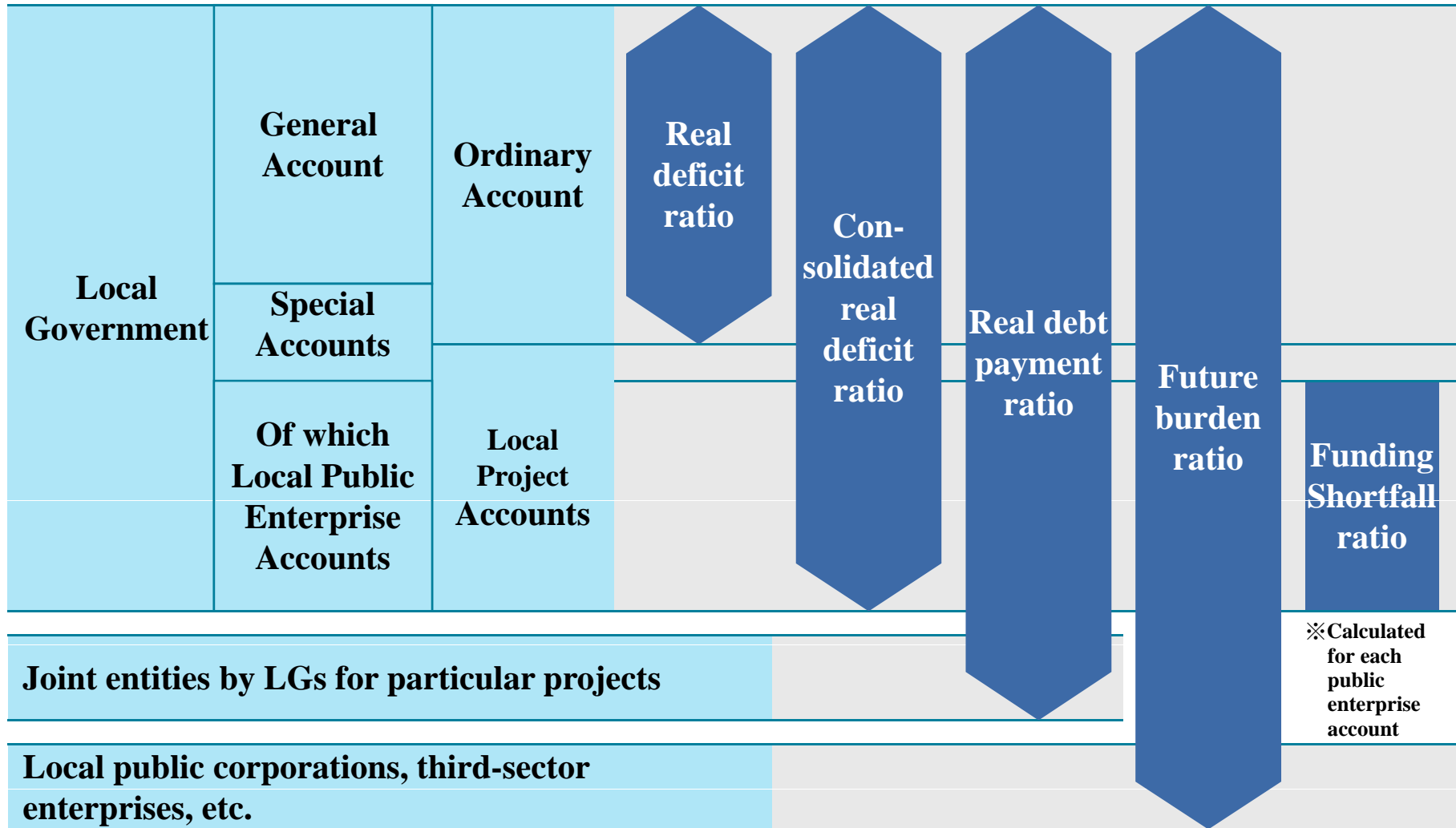
Limits for Early warning and reconstruction

	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: 35%
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 (25%→25%→20% for prefectures and 40%→40%→35% for cities, towns and villages) will be set up for reconstruction limit for the consolidated effective fiscal deficit ratio.

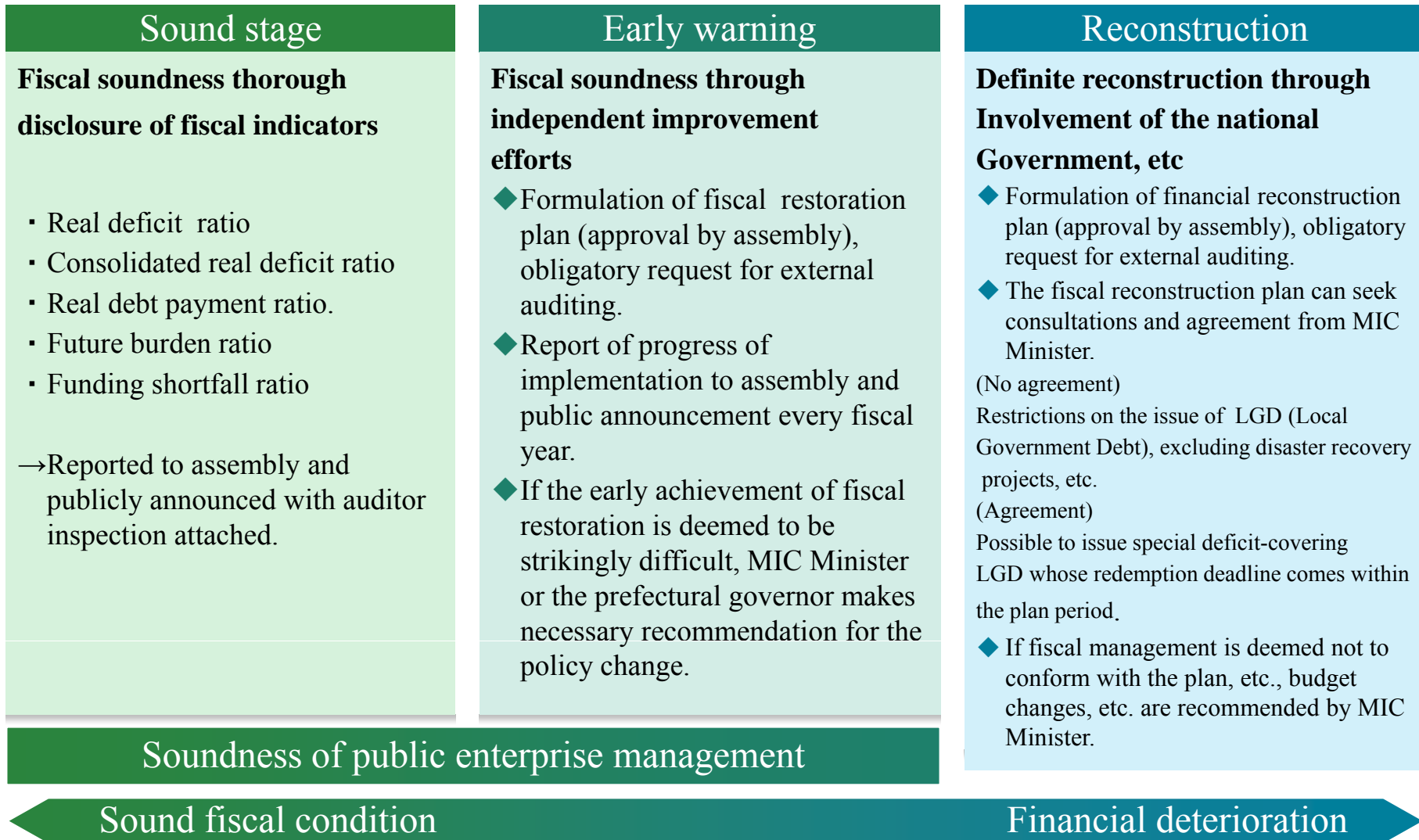


Scope of fiscal indicators in the Law





Early Warning System and Reconstruction System





Credit Rating

Local Government	Ratings			
	Moody's	S&P	R&I	JCR
JGB(NG)	Aa2/Stable	AA/Stable	AAA/Negative	AAA/Stable
Tokyo	-	AA/Stable	-	-
Tochigi Prefecture	-	-	AA+/Stable	-
Saitama Prefecture	-	-	AA+/Stable	-
Niigata Prefecture*	Aa2/Stable	-	-	-
Shizuoka Prefecture*	Aa2/Stable	-	AA+/Stable	-
Aichi Prefecture	-	AA/Stable	AA+/Stable	AAA
Okayama Prefecture	-	-	AA/Stable	-
Hiroshima Prefecture*	Aa2/Stable	-	-	-
Fukuoka Prefecture	Aa2/Stable	-	-	-
Sapporo City	Aa2/Stable	-	-	-
Chiba City*	-	A+/Positive	-	-
Yokohama City	-	AA-/Positive	-	-
Niigata City*	-	AA-/Stable	-	-
Shizuoka City*	Aa2/Stable	-	-	-
Hamamatsu City	Aa2/Stable	-	-	-
Nagoya City	Aa2/Stable	-	-	-
Kyoto City*	Aa2/Stable	A+/Stable	-	-
Osaka City*	Aa2/Stable	AA-/Stable	-	AA+
Sakai City	Aa2/Stable	-	-	-
Kobe City*	-	-	AA/Stable	-
Fukuoka City*	Aa2/Stable	-	-	-

*Issuers for Joint-LGB



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.

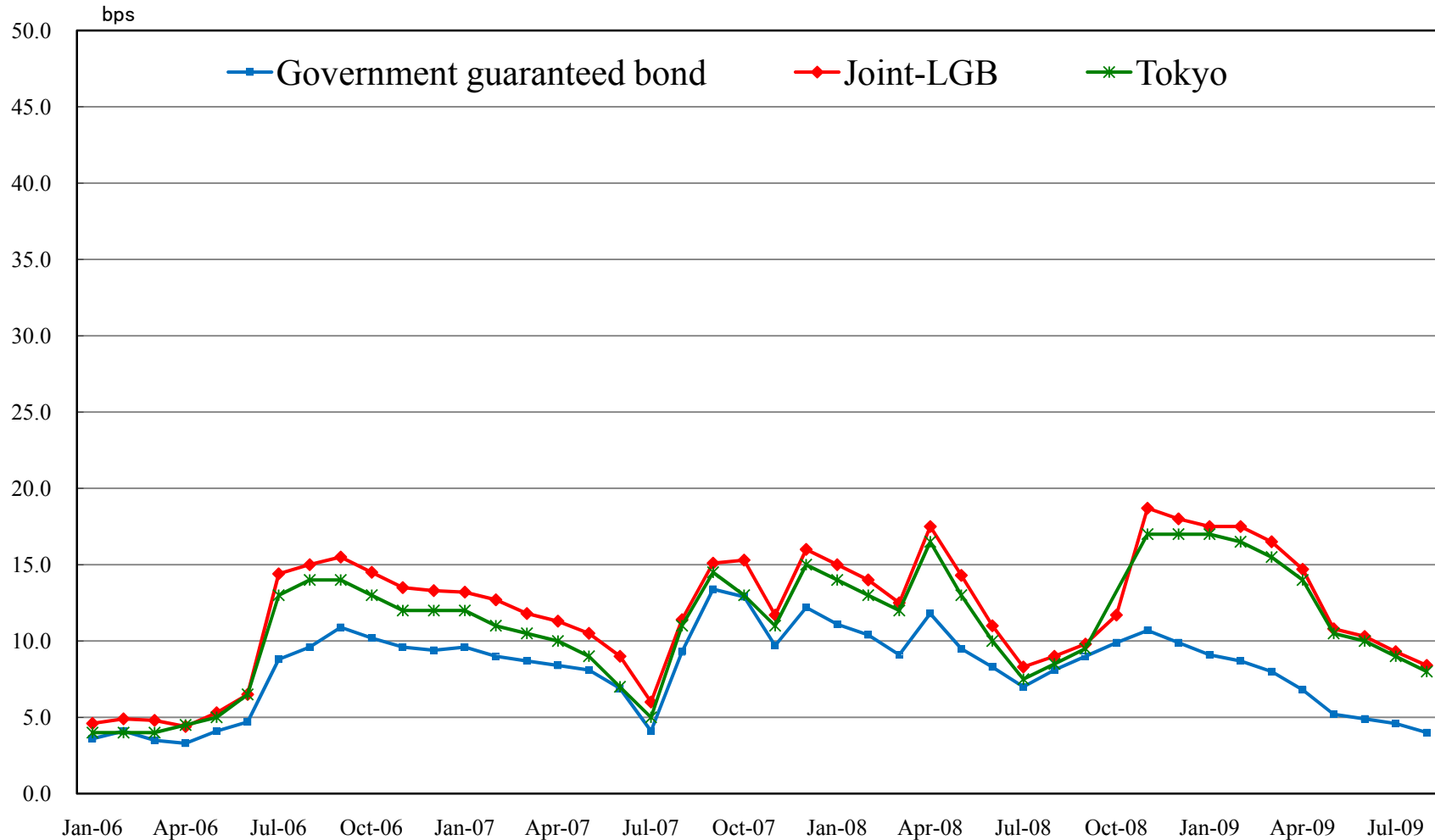


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Attractive yield spread over JGB

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



※ Issuance Yield (Jan 2006 – Aug 2009)

Source: Japan Local Government Bond Association

Nationwide Public Offering LGB Issuers

- ◆ The number of public offering issuer increase sharply from 29 to 47 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
2009	Fukui Nara	Okayama	47



Planned Issuance for Nationwide Public Offering LGBs in Fiscal-Year 2009

Local Government	Fiscal-Year 2009 (Unit: Hundred Million Yen)					Local Government	Fiscal-Year 2009 (Unit: Hundred Million Yen)				
	Total	5y	10y	20 or 30y	Joint-LGB		Total	5y	10y	20 or 30y	Joint-LGB
Hokkaido	3,600	1,200	1,800	-	600	Fukuoka	1,600	500	500	400	-
Miyagi	830	350	-	-	480	Kumamoto	500	100	100	-	300
Fukushima	600	200	200	-	200	Oita	300	-	100	-	200
Ibaragi	370	-	-	-	370	Kagoshima	700	100	-	-	600
Tochigi	100	-	100	-	-	Sapporo City	1,100	300	300	200	300
Gunma	200	-	200	-	-	Sendai City	560	100	-	200	460
Saitama	3,500	-	2,400	600	500	Saitama City	100	-	100	-	-
Chiba	3,740	600	2,000	600	540	Chiba City	800	-	300	100	400
Tokyo	8,100	800	5,600	1,700	-	Kawasaki City	1,200	350	250	300	300
Kanagawa	4,400	1,200	2,000	600	600	Yokohama City	2,300	300	1,200	800	-
Niigata	1,200	-	600	-	600	Niigata City	200	-	100	-	100
Fukui	100	-	100	-	-	Shizuoka City	150	-	-	-	150
Yamanashi	100	-	100	-	-	Hamamatsu City	100	-	100	-	-
Nagano	800	200	-	-	600	Nagoya City	1,300	200	800	300	-
Gifu	300	100	-	-	200	Kyoto City	1,300	300	300	100	600
Shizuoka	2,300	400	900	400	600	Osaka City	3,100	400	1,200	500	400
Aichi	4,000	400	2,400	600	600	Sakai City	100	-	100	-	-
Osaka	6,900	2,900	2,600	-	600	Kobe City	1,200	100	200	500	400
Hyogo	3,400	1,200	1,200	400	600	Hiroshima City	800	-	400	-	400
Nara	100	100	-	-	-	Kita-Kyushu City	800	100	200	200	300
Shimane	100	100	-	-	-	Fukuoka City	1,100	300	3000	200	300
Okayama	300	-	200	-	100	Total	67,650	13,200	30,050	9,000	13,900
Hiroshima	1,500	-	600	200	600						
Tokushima	200	-	100	-	100						

※This is based on the figures of domestic bonds announced by Ministry of Internal Affairs and Communications in Feb 2009.



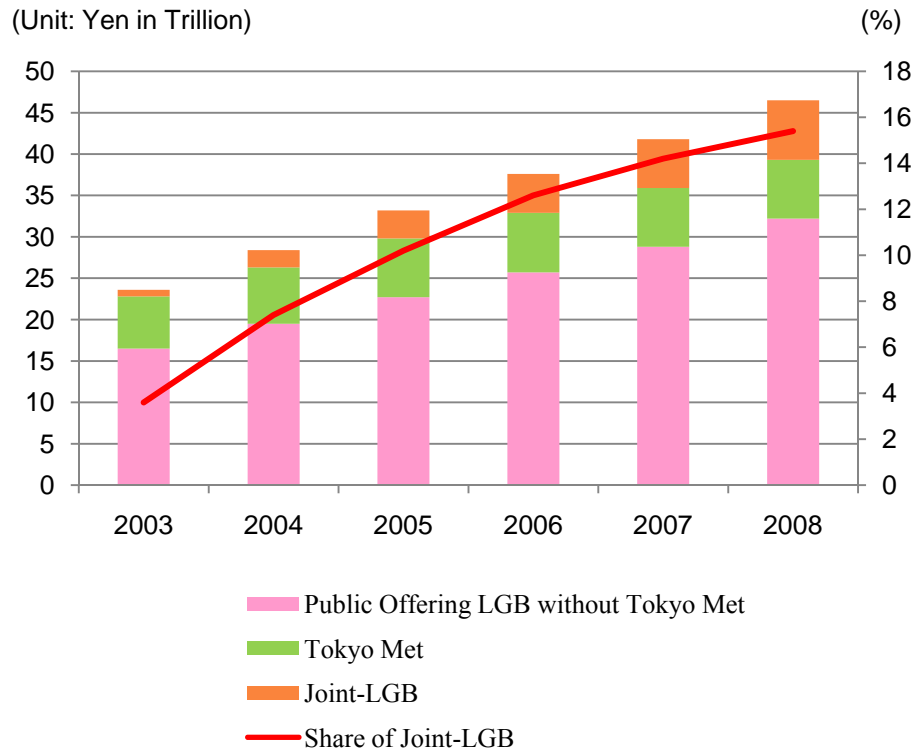
Public Offering Joint-LGB

– 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.

Outstanding of LGBs and Joint-LGB's share in the Public Offering LGB



Issuance Terms

FY2009 total Issuance	Total of ¥1.39 trillion (about ¥120 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

Source: Japan Local Government Bond Association



Public Offering Joint-LGB

– High liquidity with \$1.2 billion issue monthly

1. High credit

- ◆ Joint-LGB (Local Government Bond) is publicly-offered joint obligations issued by 33 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 \$1.2 billion, which is one of the largest sizes among Japanese non-JGB bonds. Currently total outstanding bonds will be nearly \$8.5 trillion(FY2009).

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 33 issuers in total set aside an amount equivalent to 10% of the higher monthly principal/interest payment of either February or August during that fiscal 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.

Multiple maturities and types of Public Offering

- ◆ 47 (29 prefectures and 18 Designated Cities) entities issue public offering bond independently in FY2009.
- ◆ 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: Billion Yen)

	FY1997		FY2003		FY2009(scheduled)*2	
	No. of Entities	Total Amount	No. of Entities	Amount Issuance	No. of Entities	Amount Issuance
10 y	28	1,851	29	2,371	37	3,005
3 y					1	80
5 y			19	1,045	27	1,240
7 y*1						
20 y					19	710
30 y					7	150
Joint LGB			27	847	33	1,390
Total	28	2,281	29	4,353	46	6,765

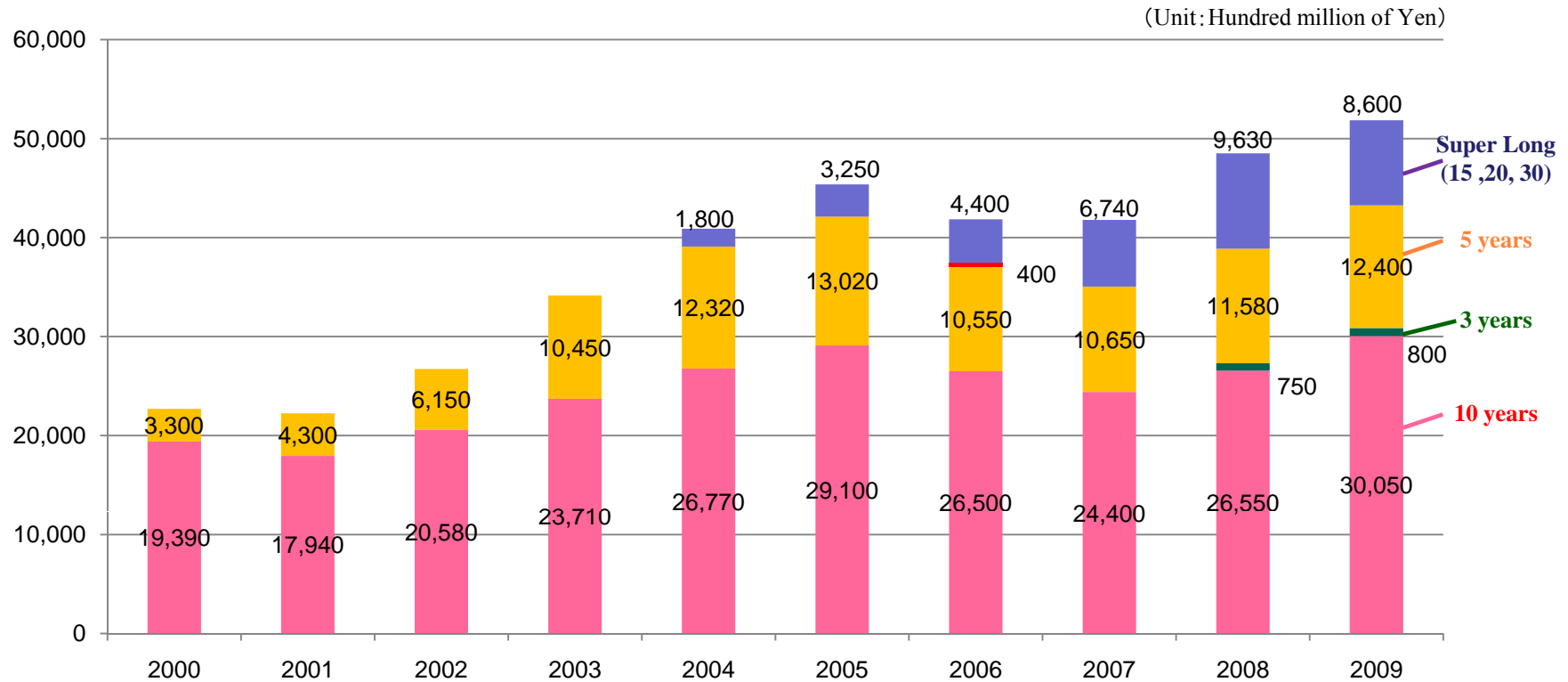
Source: Japan Local Government Bond Association

*1: 7 years LGB was issued in 2006. *2: Okayama City is not included.



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.



Source: Japan Local Government Bond Association

※The figure of Joint-LGB is not included.



I Executive Summary

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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-residents or foreign corporations settled by the book-entry system are exempted from withholding tax. Previously, 15% withholding tax 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.)

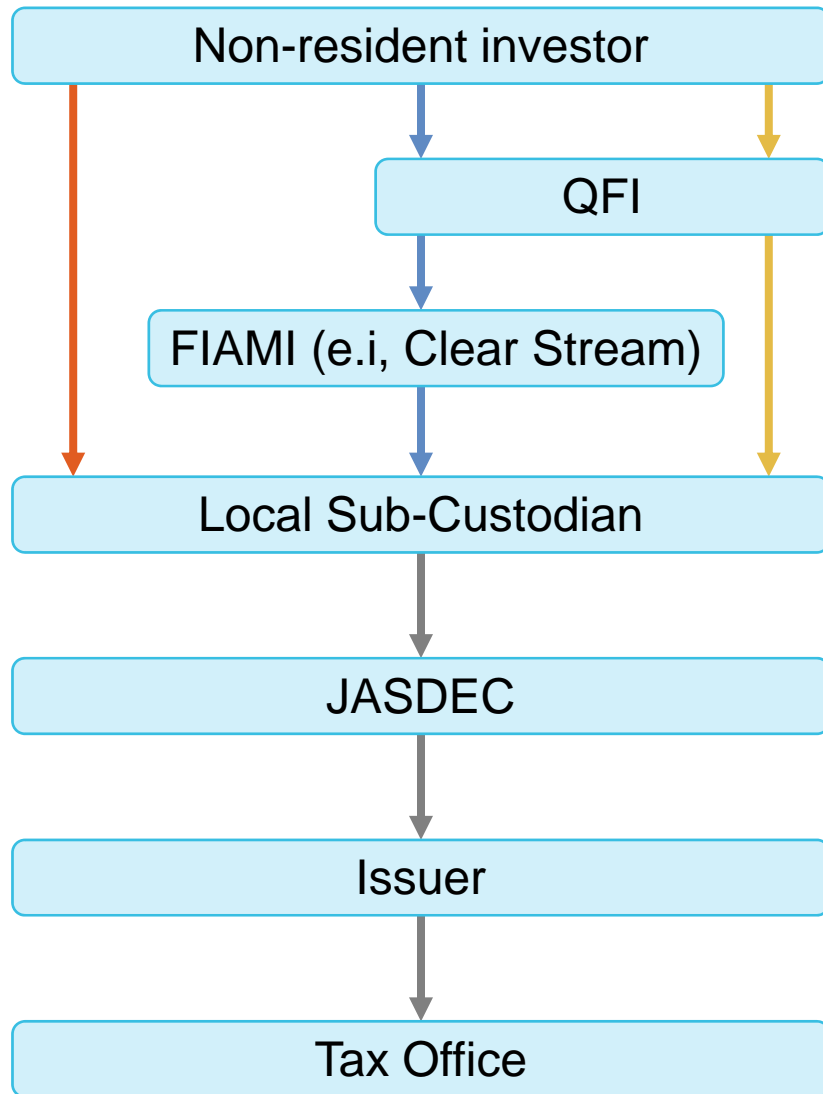
Conditions

- ◆ Non-JGB securities are required to be settled through Japan Securities Depository Center (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 custodian).
- ◆ 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 LGBs.

※FIAMI= Foreign Indirect Account Management Institution



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 listed in the left.
- ◆ However, in the case of investors having exempt status of JGB, they can submit just the copy of existing JGB application, which local custodians usually take care of.
- ◆ Up to now, 26 Global Custodians have registered as QFI (Qualified Foreign Intermediary on the next page).
- ◆ Also Clear Stream was designated as FIAMI. Therefore investors can use the service of Clear Stream through blue line scheme.



List of QFI for LGB

1	BARCLAYS BANK PLC	14	JP Morgan Chase Bank, N.A.
2	BNP Paribas Securities Services	15	KAS BANK N.V.
3	BNY Mellon Asset Servicing B.V.	16	KBL European Private Bankers S.A.
4	BROWN BROTHERS HARRIMAN&CO.	17	Mellon Bank, N.A.
5	BROWN BROTHERS HARRIMAN (LUXEMBOURG)S.C.A	18	Norddeutsche Landesbank Luxembourg S.A.
6	CACEIS Bank	19	Northern Trust Fiduciary Services (Ireland) Limited
7	CACEIS Bank Luxembourg	20	Northern Trust Global Services Limited
8	Citigroup Global Markets Inc.	21	Skandinaviska Enskilda Banken AB (publ)
9	CLEARSTREAM BANKING S.A.	22	State Street Bank and Trust Company
10	Deutsche Bank Aktiengesellschaft	23	State Street Trustees Limited
11	DnB NOR Bank ASA	24	The Bank of New York Mellon
12	HSBC Bank Plc	25	The Bank of New York Mellon (SA/NV)
13	HSBC Institutional Trust Services (Singapore) Limited	26	The Northern Trust Company

Source: Japan Securities Depository Center, Inc. (JASDEC)



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))

住所等 (注 1) Address of the applicant (Note 1)	
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 (Note 2)	

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 (Note 4)
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 (Note 3)	<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 (Note 4)
		特定振替機関等の受理日付(注 4) Date of receipt by the Sub-custodian (Note 4)



FSA's FY2010 tax revision requests

Simplification of procedures of tax exemptions for interest on LGB investment by non-residents

- ◆ The Financial Services Agency (FSA) announced its FY2010 Tax Revision Request Items, which includes simplification of procedures of tax exemptions for interest on JGBs and LGBs for non-resident investors.

1. Simplification of procedures

It is to change the application procedures for tax exemptions from one for each Issuer to one for each book-entry transfer institution (JASDEC only in the case of LGB).

2. Clarification of non-residents

It is to clarify the scope of non-residents so that overseas pension funds are eligible.



Tax Exemption Scheme by bilateral treaties

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

- ◆ In addition to the tax exemption scheme, 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 simple document first to Japanese tax authorities.
- ◆ Other bilateral treaties have the possibility for the same amendment in the future.



Yen-denominated LGBs on overseas markets

- ◆ With the Cabinet approval for the amendment of Cabinet Order in September 2008, local governments 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.



(Reference)

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.

Regular overseas road shows


- ◆ Japanese LGs have held overseas road shows as below.

Entities	Activities
Tokyo Metropolitan Government	Visit: London (May 2007) London, Paris, Frankfurt (Oct 2007) Seoul, Beijing, Hong Kong (July 2008) Europe (June 2009)
Fukuoka Prefecture	Visit: Frankfurt, Dusseldorf, Paris Period: January 2008
Japan Local Government Bond Association	Visit: London, Frankfurt, Paris Period: from 16 to 27 February 2008
JLGB European Road Show 2008	Visit: London, Berlin, Frankfurt, Paris, Dublin Period: from 6 to 11 October 2008 Participants: Ministry of Internal Affairs and Communications, Kyoto City, Shizuoka Prefecture, Kawasaki City, and JLGBA
JLGB Asian Road Show 2009	Visit: Seoul, Singapore, Hong Kong, Beijing Period: from 12 to 16 October 2009 Participants: Ministry of Internal Affairs and Communications, Shizuoka Prefecture, Kawasaki City and Japan Finance Organization for Municipalities
Road Show 2010	To be confirmed



Information of JLGB Road Shows on Website

Japan Local Government Bond Association Website
(<http://www.chihousai.or.jp/english/07/investor.html>)



JAPAN LOCAL GOVERNMENT BOND ASSOCIATION

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Information in English Available on Website

Japan Local Government Bond Association Website

(<http://www.chihousai.or.jp/english/07/investor.html>)

English Publications on JLGBs	
Presentation Materials	Local Government Bond System and Market in Japan
	Public Offering Joint-Local Government Bond
	Japan Finance Organization for Municipalities
	Shizuoka Prefecture and Kawasaki City
Some other issuers	Tokyo Metropolitan Government (TMG), Chiba Prefecture, Kyoto Prefecture, Fukuoka Prefecture
	Sapporo City, Yokohama City, Osaka City, Kobe City
Statistics*	Statistics of 46 Public Offering Local Government Bond Issuers (To be updated shortly)
	Revenue and Expenditure of 47 Prefectures and 17 Designated Cities (To be updated shortly)
White Paper	FY2007 Settlement White Paper on Local Public Finance, 2009
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



For further information

- **Japan Local Government Bond Association**

Website <http://www.chihousai.or.jp/english>

(This includes most comprehensive information in English)

8F, Zenkoku Choson Giin Kaikan, 25 Ichibancho, Chiyodaku, Tokyo, 102-0082, Japan

TEL +81-(0)3-5211-5291 FAX +81-(0)3-5211-5294

- **Local Bond Division, Local Public Finance Bureau, Ministry of Internal Affairs and Communications**

<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>

Address) 2-1-2, Kasumigaseki, Chiyoda-ku, Tokyo 100-8926, Japan

TEL +81-(0)3-5253-5630 FAX +81-(0)3-5253-5631



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