

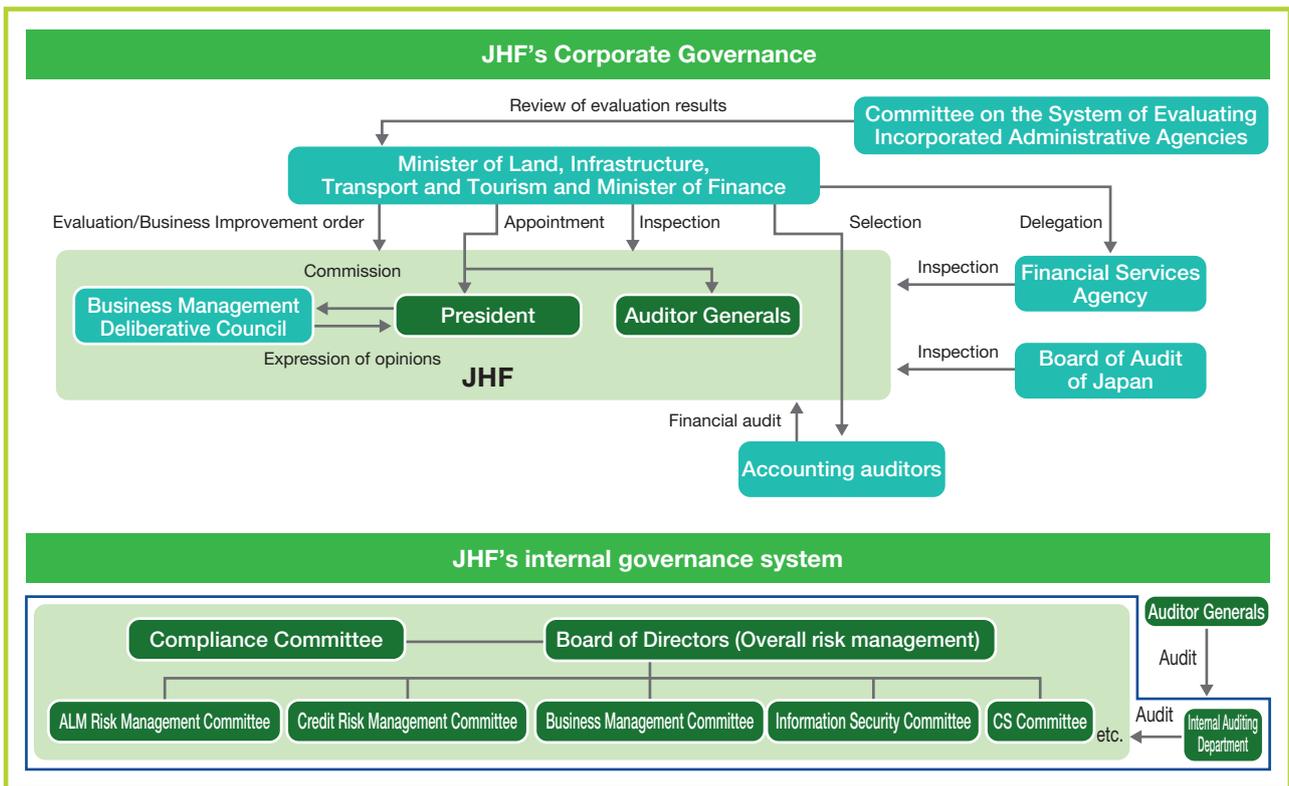
# Corporate Governance

## Governance Structure

Recognizing its basic mission and social responsibility as an Incorporated Administrative Agency, JHF acknowledges strengthening of corporate governance is an important business issue, therefore, actively implements activities to ensure sound and proper conduct of its business with high ethical standards and wisdom under transparent and efficient management based on the Act

on General Rules for Incorporated Administrative Agency.

Moreover, in order to develop its internal governance system to assure appropriate business operations, JHF has established the Basic Policy on Internal Governance and promotes appropriate internal governance by the PDCA cycle as well as further sophistication of internal governance by enhancing the governance environment.



## Business Management Deliberative Council

The Business Management Deliberative Council was established to conduct review by external experts regarding the validity of the business management and by a neutral position in accordance with the Basic Policy on Reform of Incorporated Administrative Agencies (Cabinet decision on December 24, 2013).

### <Business Management Deliberative Council Members>

As of April 1<sup>st</sup>, 2018

○Kazuhiro Ikee	Professor of Economics and Finance, Faculty of Economics, Risho University
Sayuri Kawamura	Advanced Senior Economist, Economics Department, The Japan Research Institute, Limited
Toru Kurahashi	Professor, Faculty of Economics, Dokkyo University
◎Takaaki Wakasugi	Professor Emeritus, The University of Tokyo, Co-director, Mitsui Life Financial Research Center, Ross School of Business, The University of Michigan
Kuniaki Watanabe	CEO, Winworks K. K.

(◎: Chairman, ○: Deputy Chairman)

(Honorific titles omitted)

## About the Business Management Deliberative Council Report

Since the first meeting held in May 2014, JHF received from the Council suggestions related to improvement of the product feature of loans and business operations, and a report was issued by the Council in March 2018.

The report describes how JHF has been addressing the suggestions made by the Council along with an evaluation by the Council on the relevant JHF's effort.

Of the evaluations made by the Council, JHF received an evaluation that "JHF is sharing roles with private financial institutions" with regards to private-sector supplementation.

Meanwhile, challenges such as providing further assistance to resolve regional policy issues were also indicated. JHF prefers that the Council continues to deliberate on the validity of business operations, and JHF will refer to the results of such deliberations for future business operations.



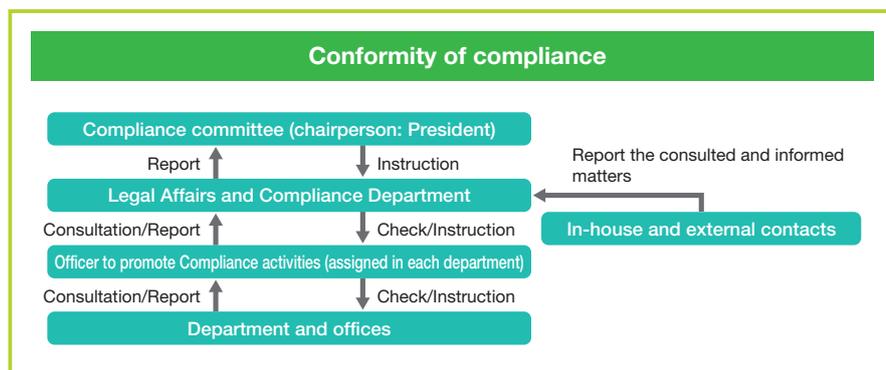
# Compliance

## Conformity of compliance

In order to surely implement JHF compliance, JHF established the Compliance Committee (chaired by the President) comprised of all of the executives and directors from related departments where JHF discuss and decide important matters related to compliance. In addition, JHF established the Compliance and Legal Department as the head department managing compliance and assigned officers to promote compliance activities within

each department.

Furthermore, in order to prevent compliance violations within JHF, an in-house contact (Compliance Help Line) and external contact for external persons were established.



JHF distributed a pocket-size edition of compliance manual to all of the executives and employees, which serves as a guide to reconsider the activity of JHF business and to make decision in difficult times.

## Compliance activities

JHF has established the Compliance Charter as its basic principles of compliance and issued a compliance manual that stipulates the laws and regulations, rules, social requirements, and business related and concerned matters to conform, which has been notified to all of the executives and employees.

Every year, JHF stipulates and executes the Compliance Program as an active plan for our compliance.

Concrete activities under the Compliance Program include e-learning available to all of the executives and employees, compliance meeting conducted by each busi-

ness units (a small group case method discussion will be conducted), and compliance-related information sharing by using the internal LAN, which are dedicated to enhance individual understanding of compliance and promote self-awareness and action by themselves.

In addition, JHF has steadily promoted compliance activities conducting the PDCA cycle in a form of quarterly monitoring of the Compliance Program by the Compliance Committee and modifications of Compliance Program policies, if necessary.

### The Compliance Charter (excerpts)

- 1. We comply with laws, rules and regulations as well as social norms, and strive to undertake all tasks properly in efforts to ensure public confidence.
  - (1) Compliance with laws and regulations as well as social norms
  - (2) Proactive and fair disclosure of information
  - (3) Strict information management
  - (4) Resistance against all anti-social parties
- 2. We thoroughly strive to pursue customer confidence and satisfaction.
  - (1) Provide comprehensive housing loan services
  - (2) Conduct appropriate and sufficient explanations
  - (3) Respond sincerely to customer voices
- 3. We respect the personality of each executive and employee and endeavor to secure a pleasant working environment.
  - (1) Respect the personality and character of individuals
  - (2) pleasant working environment

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## Responses to Anti-social Forces

To reject any relationship with anti-social forces such as organized crime syndicates, JHF has explicitly stated the resistance against all anti-social parties in its compliance charter and established the Basic Policy Against Anti-social Forces, which is available on our website. In addition, regulations and manuals for dealing with such anti-social forces have been prepared. Through these efforts, JHF has established a framework for reporting to and consulting immediately and properly with management and the Legal Affairs and Compliance Department, the department that oversees responses to anti-social forces, in case JHF identifies business related with such anti-social forces or undue

claim from such forces.

JHF also conducts training and other sessions to address undue claims in cooperation with the police and other relevant institutions.

JHF stipulates article on rejection of anti-social forces in its business contracts and eliminates any relationship not only with organized crime syndicates but also with individuals coexisting with anti-social forces trying to illegally receive loans for the benefit of anti-social forces related with organized crime syndicates.

As an organization, JHF will continue its commitment towards rejecting relationship with anti-social forces.

### Basic Policy against Anti-social Forces

1. JHF commits to have no relationship with any anti-social forces, and the President, including the management and all employees shall never compromise with such forces.
2. JHF commits to establish a framework to reject anti-social forces and distribute to all of the management and employees the manual describing how to deal with such forces.
3. JHF commits to ensure the safety of management and employees who deal with undue claims from anti-social forces.
4. JHF commits to cooperate closely with external institutions, such as the police, National Center for Removal of Criminal Organization, and lawyers.
5. JHF commits to take both civil and criminal law related actions against undue claims from anti-social forces.
6. JHF commits to never conduct "backstage deals" to conceal facts that undue claims from anti-social forces were made to JHF due to misconduct of JHF's business activities or its employees.
7. JHF commits to never provide funds to anti-social forces.

## Information Security

JHF has been dedicated to conducting information security measures.

In FY2017, JHF enhanced the framework to promote information security measures as follows:

- JHF established information security measures in accordance with "FY2016 Common Standards for Information Security Measures for Government Agencies" established by NISC (National Center of Incident Readiness and Strategy for Cybersecurity).
- JHF implemented information security measures pursuant to FY2017 Information Security Measures Promotion Plan and defined FY2018 Information security Measures Promotion Plan to continue its effort on information security measures.
- JHF conducts training and drills to promote and maintain literacy of JHF's managers and employees on information security measures but also revise the practice pursuant to self assessment and other results.

## Risk Management

In order to maintain the healthiness of JHF’s business and gain understanding and trust of the general public, JHF sustains an organizational structure to properly manage the various risks associated with its day-to-day operations.

To be specific, JHF has established risk management regulations, such as “Risk Management Basic Rules” that stipulate the purpose of risk management, characteristics and definitions of individual risks, and methods and audit-

ing of the status of risk management implementation and also “Credit Risk Management Rules” that stipulates specific risk management method of individual risks. Based on these rules, JHF implements risk management incorporating features of businesses, such as housing loans and others, and conducts comprehensive risk management by understanding and valuing the individual risks as a whole considering JHF’s business and characteristics.

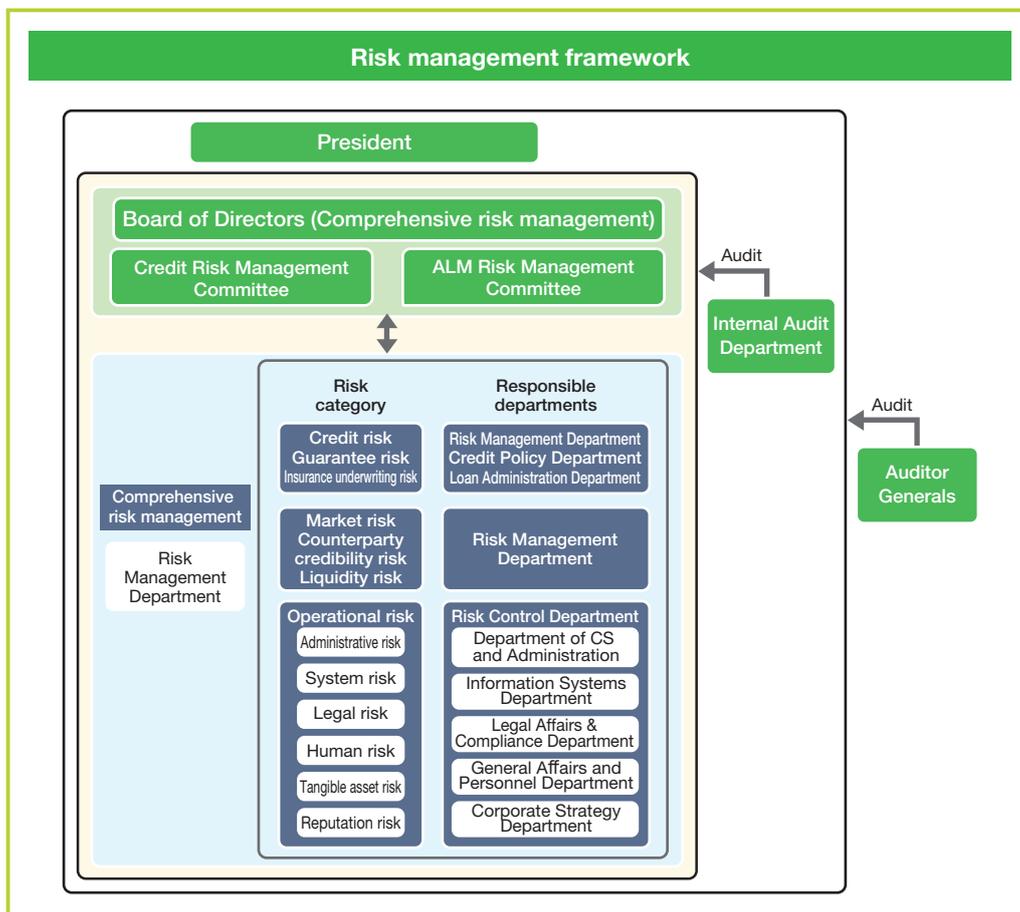
### Risk management framework

JHF classifies risks as credit risk, guarantee risk, insurance risk, market risk, counterparty credibility risk, liquidity risk, and operational risk. In the event of a significant change in economic situation, JHF will correspondingly specify the new risk to be managed.

JHF sustains the framework to properly manage these risks in qualitative and quantitative aspects by appointing an executive and a department responsible for managing each risks. In particular, the “Credit Risk Management Committee” was established to manage credit risk, guarantee risk, and insurance risk, and the “ALM Risk Management Committee” was established to manage

market risk, counterparty credibility risk, and liquidity risk. These committees monitor the status of each risk and discuss the risk arrangement planning and proposals.

In addition, JHF assigns an executive and a department responsible for comprehensive risk management to conduct comprehensive risk management on each risk and maintains the framework to track and evaluate the quantified result and the management status of each risk and periodically report the results to the Board of Directors.



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## Risk categories

### Credit risk

Credit risk is defined as the risk of JHF suffering from a loss due to decline or disappearance of asset value caused by deterioration of the creditworthiness of a debtor, which JHF holds as a loan receivable. Since housing loans constitutes major portion of JHF's assets, JHF endeavors to properly underwrite the credit risk of the loans JHF purchases or originates, and properly manage and perform self-assessment of the loans that JHF holds, and track, analyze, and manage the overall credit risk.

#### ▶▶ Underwriting of purchasing and original loans

JHF defines criteria and methods of underwriting and properly underwrites the credit risk of purchasing and originated loans.

#### ▶▶ Self-assessment

JHF properly manages the credit risk of retained loan claims and conducts self-assessment according to JHF defined self-assessment criteria complying with the "Financial Inspection Manual" of the Financial Service Agency in order to properly disclose financial information pursuant to the "Accounting Standards for Incorporated Administrative Agencies." To be specific, JHF calculates the necessary reserves for non-performing loans by classifying JHF's assets in accordance with the uncollectibility and loss severity and then multiplying the expected loss given default ratio calculated based on historical performance of non-performing loans.

#### ▶▶ Credit portfolio management

Using the credit portfolio management system for periodical monitoring, JHF analyzes the utilization status of housing loans, forecasts future losses, and reviews the necessary credit risk premium in order to accurately evaluate the overall credit risk of all the debts that JHF holds and the location of risks. JHF also endeavors to further improve risk quantification by utilizing the credit portfolio management system to strengthen credit risk management.

### Guarantee risk

Guarantee risk is defined as risk of JHF suffering from a loss due to opposed fluctuation of a guarantee incident against the estimate made at the time of the guarantee fee calculation. JHF guarantees mortgage-backed securities (MBS) under the securitization support business (guarantee program). JHF performs proper underwriting and endeavors to track, analyze, and manage the overall guarantee risk.

### Insurance underwriting risk

Insurance underwriting risk is defined as the risk of JHF suffering from a loss due to opposed fluctuation of an insurance incident against the estimates made at the time of the insurance premium calculation. JHF underwrites insurance for non-performing housing loans originated by private financial institutions. JHF performs proper underwriting and endeavors to track, analyze, and manage the overall insurance risk by monitoring utilizing the credit portfolio management system and by verifying whether the unused policy reserve is sufficient by conducting future cash flow analysis.

### Market risk

Market risk is defined as the risk of fluctuation of periodic income and loss due to changes in the risk factors, such as the interest rates and others. Since housing loan constitutes major portion of JHF's asset, market risk includes prepayment risk, refinancing and reinvestment risks, and pipeline risk and others.

#### ▶▶ Prepayment risk

Prepayment risk is defined as the risk of deterioration of periodic income and loss due to loss of expected interest income caused by an increase in the loan prepayment amount triggered by a decline in the interest rate. JHF manages the risk by estimating the prepayment amount using the prepayment model and by securitizing the housing loans and by issuing bonds of various maturities.

#### ▶▶ Refinancing and reinvestment risks

Refinancing and reinvestment risks are defined as the risk for deterioration of periodic income and loss due to increased interest payment caused by increased funding cost or due to decreased interest income caused by decreased interest on investment under the circumstances of refinancing or reinvestment. JHF manages the risk by utilizing the interest model to estimate the cash flow of assets and debts incorporating future interest rate fluctuations and forecasting periodical income and loss according to such cash flow, and by periodically monitoring the risk indexes, such as duration and others.

#### ▶▶ Pipeline risk

Pipeline risk is defined as the risk of fluctuation of periodic income and loss due to fluctuation of interest rate between settlement of housing loan interest rate and determination of funding interest rate applicable to such housing loan. JHF manages the risk by conducting interest rate swaps for hedging purpose.

### Counterparty credibility risk

Counterparty credibility risk is defined as the risk of JHF suffering from a loss due to decline or disappearance of asset values caused by financial deterioration of bond issuers which JHF invests its surplus funds and of JHF's interest rate swap transaction counterparties. JHF defines the counterparty credibility risk management methods of bond issuers and interest rate swap transaction counterparties and conducts monitoring.

### Liquidity risk

Liquidity risk is defined as the risk of JHF forced to fund raise necessary monies at cost significantly higher than normal or JHF falls into cash shortage by financial deterioration and incur losses under such situations: or the risk of transaction unavailability in the market due to market turmoil or the risk of JHF forced to conduct transaction at adverse price and incur losses under such situations. JHF sets the minimum retained amount of liquidity assets as a management standard and as a measure against liquidity risk, which JHF conforms to maintain in daily operations, therefore, JHF conducts stable cash management operations. In addition, emergency credit line is set to achieve secured funding source and JHF sets liquidity management classifications (defined as normal, cautious, and crisis situations) according to the urgency of funding needs and sets actions of JHF under cautious and crisis situations." Furthermore, JHF sustains an organizational structure and defines an action plan so called contingency funding plan to enable prompt response when liquidity risk becomes eminent.

### Operational risk

Operational risk is defined as the risk of JHF suffering from a loss due to improper operational processes, improper behavior of executives and employees, or improper operation of information systems, or an external event. The risk includes administrative risk, system risk, legal risk, human risk, tangible asset risk, and reputation risk. JHF is improving the organizational structure to manage the operational risk by tracking the occurrence of evident risks by collecting information, by defining measures based on causality analysis, by self-analyzing the internal risk of operations and the control method of constraining, and by implementing RCSA (Risk & Control Self-Assessment) to improve operations based on the results of self analysis. The following are the definitions and control methods of main operational risks.

### ▶▶ Administrative risk

Administrative risk is defined as the risk of JHF suffering from a loss due to inaccurate administration work, accident, or misconduct and others by the executives and employees (including others excluding JHF's executives and employees engaged in JHF's operations), or by misconduct of those not engaged in JHF's operations. JHF endeavors to reduce administrative risk by preparing administration work manuals, by improving administrative work, by completing crosschecking between employees, by providing instructions and training on administrative work, by performing internal self-check ups, and by collecting and analyzing information on administrative errors and taking preventive measures against recurrence.

### ▶▶ System risk

System risk is defined as the risk of JHF suffering from a loss due to failure, malfunction, defect, or misuse of information systems. JHF endeavors to reduce system risk by taking measures based on classifications according to importance and risk assessment, by developing systems with functionalities, reliability, and information security considered, and by collecting and analyzing information on system failures and taking preventive measures against recurrence. In preparation for serious failures, JHF prepared crisis management manual and endeavors to maintain stable operations by taking necessary measures, such as duplexing systems, establishing backup centers, and conducting emergency drills.

### ▶▶ Legal risk

Legal risk is defined as the risk of JHF suffering from a loss due to unlawful acts, inappropriate contracts, or uncertainty in legal matters related to business transactions. JHF endeavors to reduce legal risk by conducting legal check of Legal Affairs & Compliance Department performs before establishing internal regulations, creating contracts, and posting advertisements. JHF also prevents violations of laws and regulations by collecting information on new legislation, amendments and others, and business related legal precedents.

### Others

As a measure for comprehensive risk management, JHF conducts simulation of life-time future income for mid-to-long term.

Based on cash flow incorporating future interest rates fluctuation, the cross-sectional risk simulation calculates whether losses resulting from both credit risk and market risk are covered by interest income.

The simulation also performs stress tests on the two risks and scenario analyses based on business volume change to verify financial resilience.