

Risk Management and Compliance Initiatives



Message from the Executive in Charge

Establish self-directed, sound compliance and risk-consciousness as a corporate culture and create the foundation to realize our Purpose

Satoshi Yamaguchi
Managing Executive Officer,
Head of Risk Management Unit

Reflecting on the misconduct in crisis response operations announced in 2016, the Shoko Chukin Bank has continued our compliance initiatives.

We have been working to develop our compliance systems by establishing a Compliance Committee that consists of a majority of external lawyers and by formulating the Code of Ethics and the Code of Behavior that serve as standards for employees to judge the performance of their duties. We believe that the self-directed initiatives and awareness of each employee at each workplace are the most important. Gradually, it is becoming more common for employees to think of the idea of “how our workplace and organization should be” as something that we need to take ownership of; however, we are aware that there is a risk that such initiatives could be ruined if we are not cautious enough. We will continue our efforts to reiterate our firm determination never to tolerate injustice that betrays the trust of our stakeholders and never to turn a blind eye to it.

In the past, risk management tended to fall into the idea of minimizing risk or a rule-based approach, and as a result, it was undeniable that our business operations were inefficient. Currently, we focus on the basic idea of “there is no profit

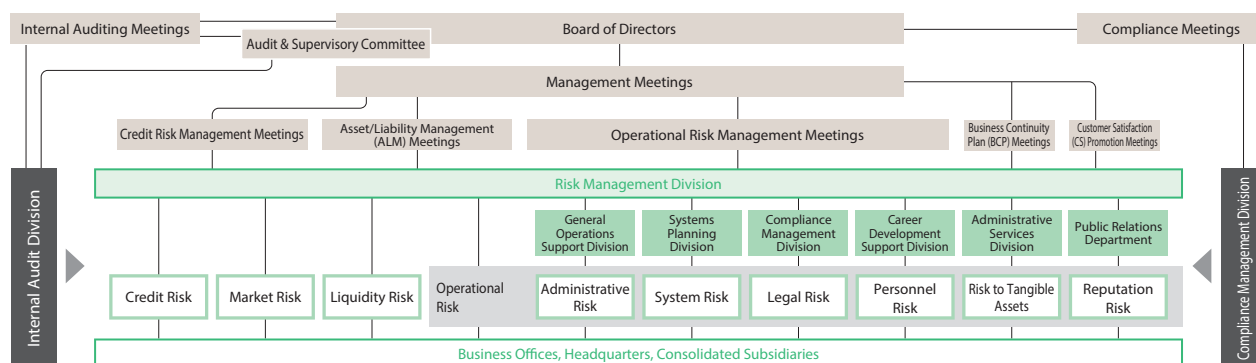
without taking risks, and we must think properly about which risks to take.” In line with this policy, I would like to further strengthen our efforts to encourage customer-facing divisions/departments to take more self-directed approaches to raise awareness of risk ownership, including by balancing this with appropriate pricing. In fiscal 2021, the Shoko Chukin Bank adopted “top risk management,” which, based on discussions by senior management, recognizes risk events thought to have a particularly significant impact on management. For the top risks determined, we prepare for materialized risks by formulating the management policy and monitoring the status of risks, as well as utilize the information to discuss where management resources should be allocated.

In order to promote more efficient and effective compliance systems and risk management, we have established the Risk Management Unit to strengthen cooperation between the two divisions and oversee them. I believe that self-directed, sound compliance and a risk-conscious culture serve as the foundation to realize our Purpose. To this end, the management team will take the lead in improving and strengthening the effectiveness of our compliance systems and risk management.

Risk Management Initiatives

In order to sufficiently exhibit our role as a financial institution specializing in SMEs while maintaining the soundness of management, the Shoko Chukin Bank has laid down its basic policy for risk management of thoroughly communicating the importance of risk management to all officers and employees, and accurately grasping and managing risks by defining the type of risks that should be recognized, their content and the organizational structure for managing such risks.

► Risk Management Structure and System



I. Integrated Risk Management

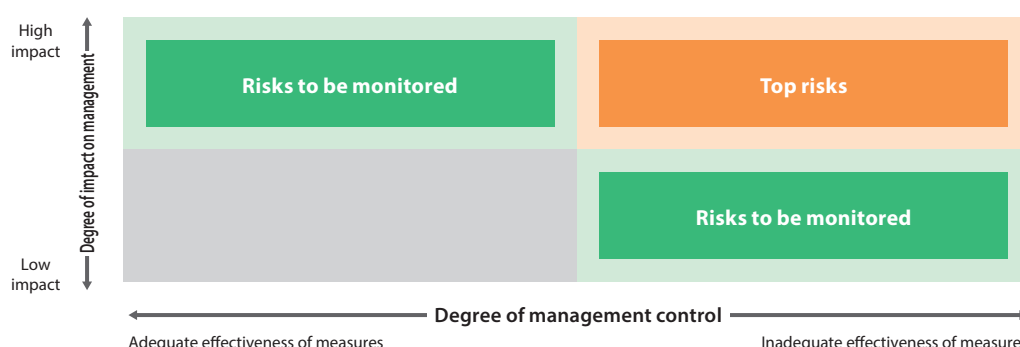
The Bank comprehensively understands risks that have been qualitatively or quantitatively assessed and ensures the soundness of management by comparing and contrasting such risks against its financial stability while allocating appropriate management resources commensurate with such risks. Top risk management and risk capital allocation management are undertaken as a concrete process within this framework.

II. Top Risk Management

The Bank has adopted “Top risk management,” which, based on the discussions of senior management, recognizes risk events thought to have a particularly significant impact on management as top risks.

Specifically, every half-year period, the Board of Directors selects risk events surrounding the Bank and determines top risks by utilizing a risk map, which takes into account the degree of impact of such risks on management and the adequacy of the countermeasures.

For the top risks determined, risk management is conducted that allows for flexible responses in preparing for the materialization of risks, by determining the management policy and monitoring the risks, among others.



► Shoko Chukin Bank's Top Risks (for FY2024)

Risk events	Risk scenarios (examples)
Responses against climate change risks	<ul style="list-style-type: none"> The transition to a low-carbon society may affect customers' businesses and increase credit-related expenses. Perceived inadequate climate change efforts and disclosures may cause reputational damage.
Changes in industrial structure	<ul style="list-style-type: none"> Changes in the external environment may affect customers' businesses and increase credit-related expenses. The competitive environment may change drastically, resulting in an erosion of the effects of strategic investments, a shortage of human resources, etc.
Risks related to the Shoko Chukin Bank Group's business strategies	<ul style="list-style-type: none"> Amid major changes in industrial and social structures in the green and digital fields, we may be unable to adapt our business strategies and fulfill our functions and roles for our customers.
Occurrence of large-scale natural disasters	<ul style="list-style-type: none"> Customers' businesses may be affected and credit-related expenses may increase. The Shoko Chukin Bank's domestic and overseas offices may be damaged, making it difficult to continue operations.
System failure	<ul style="list-style-type: none"> We plan to renew our accounting system in 2025. In case of some system failure, there is a possibility that the suspension of our operations and services may have a significant impact on our customers and society.
Risks related to cyber attacks	<ul style="list-style-type: none"> The Shoko Chukin Bank's operations or services may be shutdown, customer information may leak, or unauthorized transfer of funds through Internet banking may occur which could have a significant impact on its management.
Securing and developing human resources	<ul style="list-style-type: none"> The lack of progress in securing and training human resources may make it impossible to implement strategies in key areas as expected. Perceived inadequate human capital management efforts and disclosures may cause reputational damage.
Inadequate measures against money laundering and terrorist financing	<ul style="list-style-type: none"> Measures against money laundering may not function effectively and administrative penalties may be imposed by the financial authorities, which may result in the termination of the correspondent arrangements and may impede international operations such as overseas remittance operations.

[Reference] Risks to be monitored

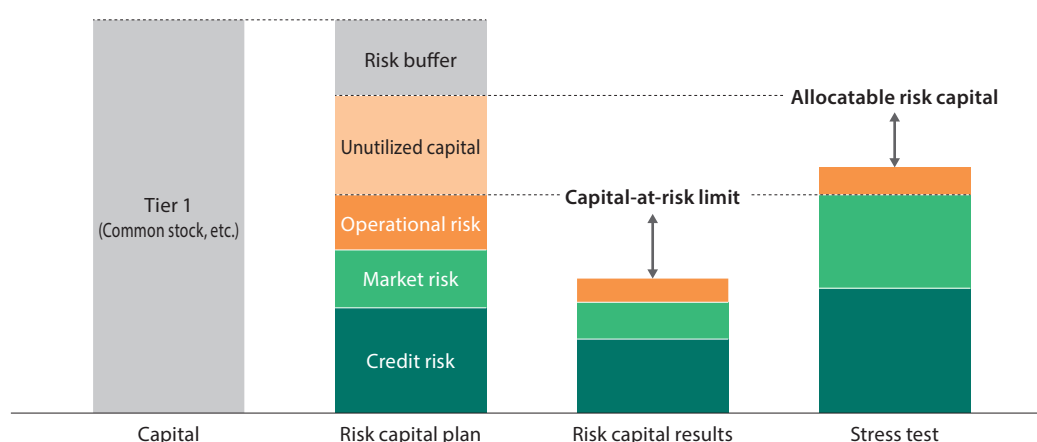
Fostering a healthy corporate culture; deteriorating financial and economic environments in Japan and overseas; risks related to the Bank of Japan's monetary policy; increase in corporate bankruptcies; deteriorating financial performance of major borrowers; risks related to generative AI; deteriorating fund-raising environment; downgrades in credit ratings; deteriorating corporate governance; geopolitical/economic security; addressing human rights issues; spread of infectious diseases

III. Risk Capital Allocation Management

At the Shoko Chukin Bank, we manage risks by quantifying various risks using criteria that are as uniform as possible, aggregating the quantified risks and comparing the risks with capital (integrated capital management). The Board of Directors determines the capital-at-risk limit for overall and each risk, while periodically monitoring the status of the use of risk capital and reports to the Asset/Liability Management (ALM) Meetings and the Management Meetings.

Additionally, we set multiple stress scenarios, including the re-emergence of past stress events and the occurrence of specific stress events, and conduct stress tests based on these scenarios to evaluate internal capital adequacy.

► Overview of Risk Capital Allocation Management



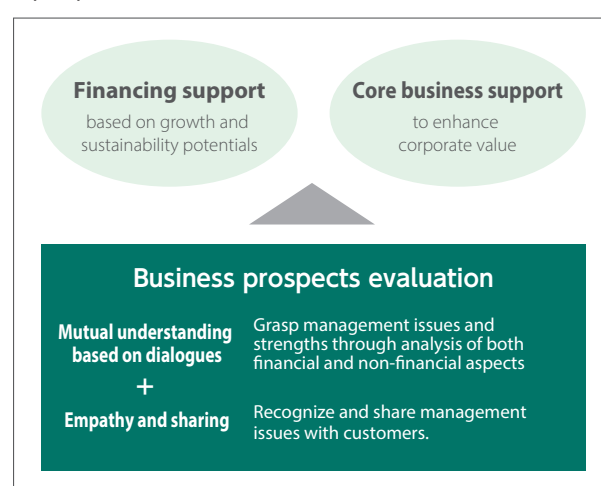
IV. Credit Risk Management

The Bank undertakes self-assessment of its assets to identify and control credit risk in an appropriate manner and has introduced an internal credit rating system for this purpose. The Bank's internal credit rating system uses an optimal set of financial indicators to assess the creditworthiness of SMEs and also incorporates a range of qualitative assessment criteria.

Additionally, we analyze and assess the credit portfolio from various perspectives, such as by credit rating, business sector, and geographical region, aiming to secure the soundness of the Bank's assets, while also quantifying credit risk to understand and manage credit risk quantitatively.

In terms of credit screening, the Finance Unit strives to maintain and improve the soundness of assets through appropriate screening and management based on business prospects evaluations. The Bank has also established the Corporate Support Division as a specialist unit to provide customers with support for management improvement and revitalization. This department proactively works with customers in this area.

► Our approach to customer support based on business prospects evaluations



V. Market Risk Management

The Bank controls the volume of market risk within a certain range by setting risk limits within the scope of the capital-at-risk limit allocated to market risk by objectives of the task and type of risks, and also setting limits on amount of positions and valuation gains and losses, and managing these limits.

VI. Liquidity Risk Management

The Bank appropriately controls liquidity risk by setting various limits related to liquidity risk involving yen and foreign currencies and managing such limits, as well as by classifying the status of cash flows into three categories, “Normal times,” “Times of concern,” and “Times of crisis,” managing the cash flows according to each category, and formulating specific measures at Times of concern and Times of crisis.

VII. Operational Risk Management

The Shoko Chukin Bank manages operational risk by classifying it into the six sub-risks consisting of administrative risk, system risk, legal risk, personnel risk, risk to tangible assets, and reputation risk.

The Risk Management Division is responsible for managing and minimizing operational risk, as it relates to the Bank as a whole. In this context, the Division has formulated the Basic Guidelines on Operational Risk Management. In addition, we have established a department in charge of each sub-risk to manage risk according to the attributes of each risk.

A Risk Control Self-Assessment (RCSA) has been introduced for risk management, whereby the department in charge of operations monitors losses that occur and also identifies and evaluates inherent risk. The Bank is promoting initiatives to make improvements based on this evaluation.

In addition, at the Operational Risk Management Meetings, we deliberate on matters relating to operational risk. These include efforts to clearly identify operational risks and responses to ensure their reduction.

We also address cross-cutting risks related to sustainability, such as climate change risks and human rights issues. This information is provided on other pages.

TOPIC Advancing Our Cybersecurity

In order to respond to the risk of cyber attacks, which have become increasingly sophisticated and ingenious in recent years, the Shoko Chukin Bank has positioned “risks related to cyber attacks” as one of top risks, and has been implementing cyber security measures under the leadership of management.

Specifically, management takes the lead in raising cybersecurity awareness through measures such as response drills attended by executives themselves and study sessions for the president and other members of the management team.

Shochu-SIRT, a cross-organizational in-house CSIRT, collects information on, analyzes, and responds to cyber attacks on a daily basis in cooperation with external specialized organizations, and has established a system to systematically respond to cyber attacks.

We have also formulated a medium-term action plan and worked to further advance our cybersecurity measures based on this plan.



Compliance Initiatives

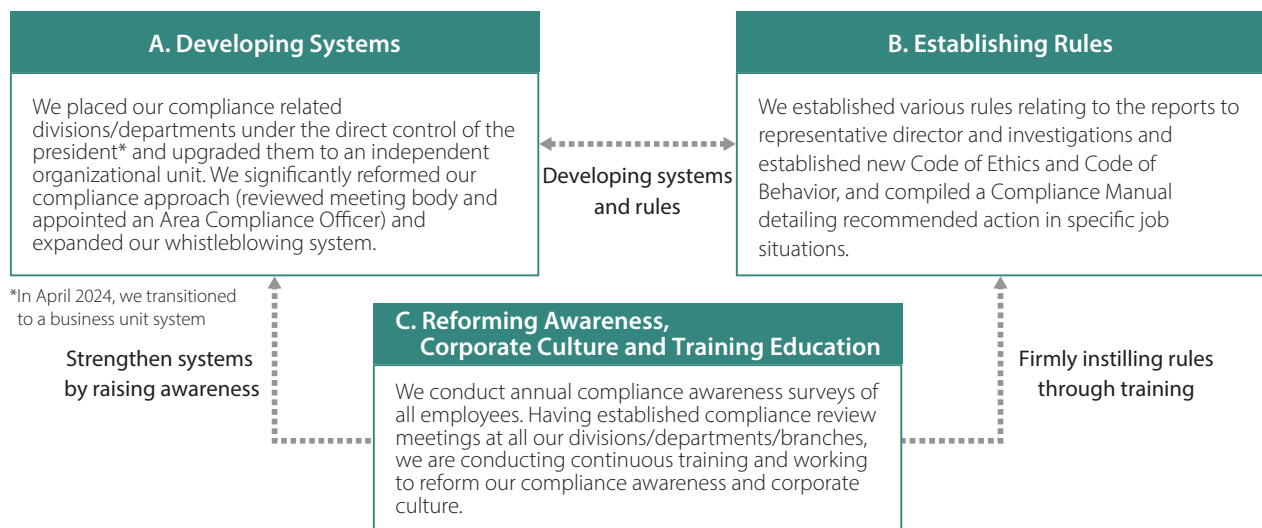
Status of the initiatives to develop compliance systems in the wake of misconduct in crisis response operations

At the Shoko Chukin Bank, we sincerely reflected on the misconduct in our crisis response operations that was announced in 2016, and have since been working to fundamentally overhaul our compliance systems.

We recognize that the four fundamental causes of the misconduct in the past were: (1) a lack of internal control and excessive pressure for business performance in crisis response operations; (2) the use of crisis response loan facilities as a dominant tool; (3) the attitude of the Bank's Headquarters and management, as well as a decline in compliance awareness that led to misconduct; and, (4) a lack of governance. Based on that recognition, we have developed various approaches and have been steadily raising the officers and employees' compliance awareness.

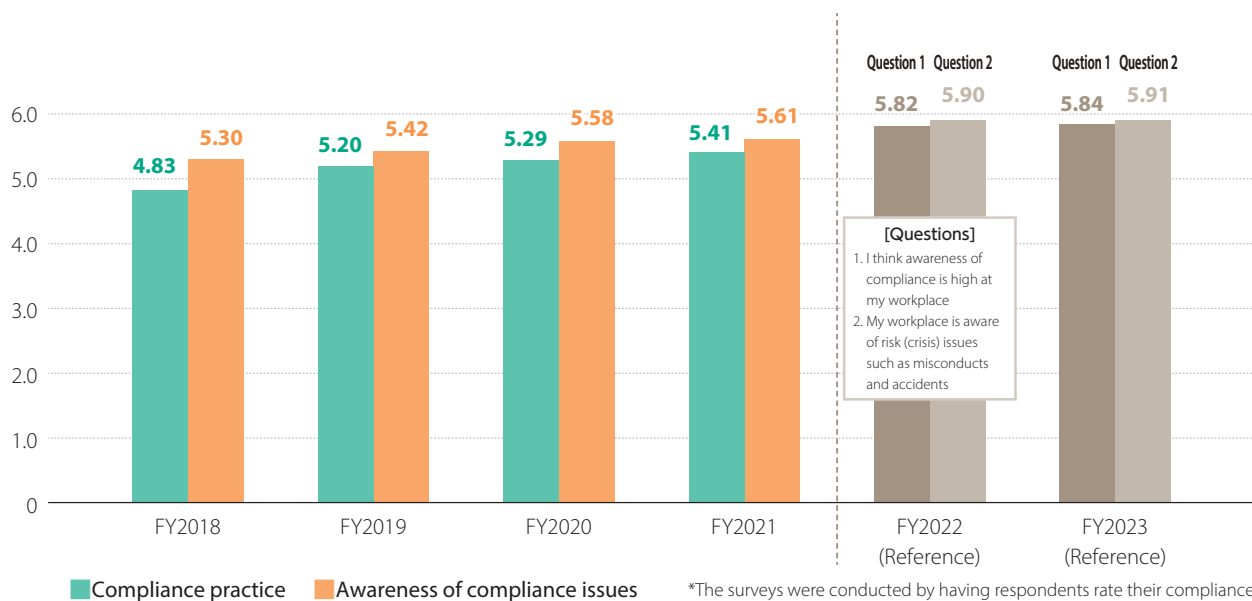
Going forward, we will aim to transition from uniform companywide measures to the promotion of self-directed measures tailored to the issues facing each division, department and branch and to shift away from headquarters-led initiatives to "self-directed compliance" that is planned, reviewed, and operated independently by each division, department and branch.

► Three Initiatives to Rebuild Organization After the Misconduct Incident

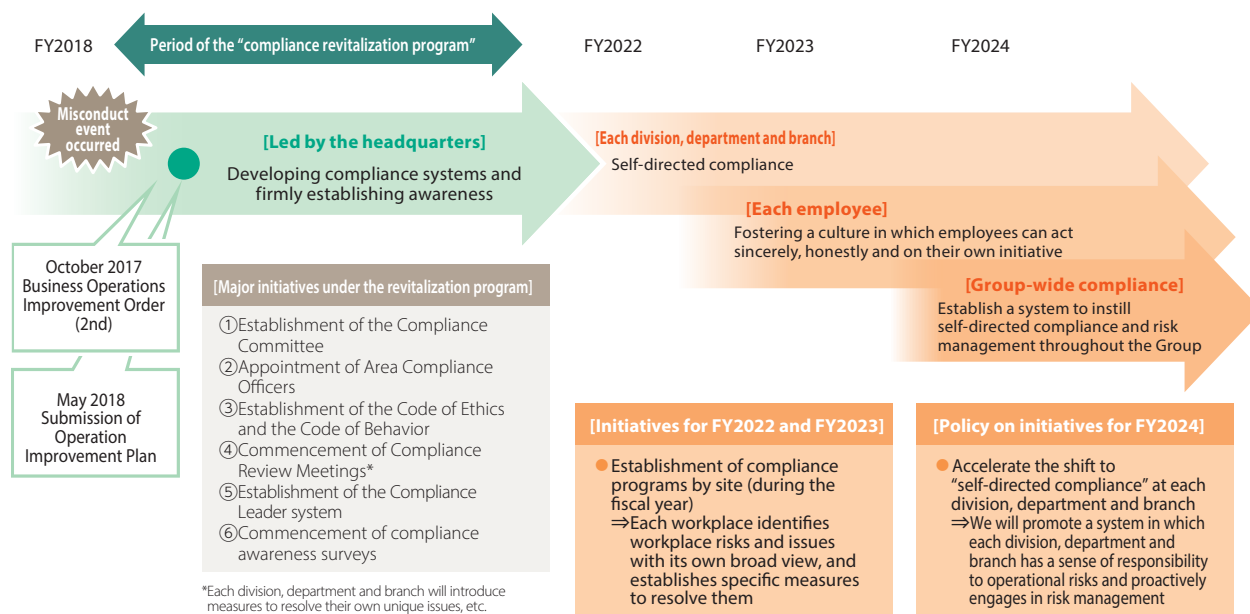


► Change in Compliance Awareness

We have been conducting an annual survey of employees compliance awareness since fiscal 2018. (Due to a change in the survey method, figures for fiscal 2022 and onward are for reference only)



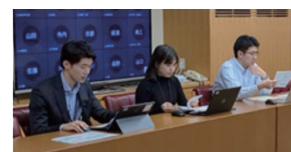
► Initiatives after discovering the misconduct event [overview of future initiatives]



► Exchanging of opinions between Compliance Leaders and external directors

Compliance Leaders, who are responsible for promoting overall compliance-related activities in each division, department and branch, had a meeting to exchange opinions with external directors.

Each leader shared the initiatives of his or her own division, department or branch, and the external directors gave advice such as the importance of constantly being aware of current trends.



Opinion exchange meeting

● Example of initiatives for self-directed compliance

An example of initiatives for self-directed compliance at each workplace is introduced below.

Sendai Office

As part of our compliance program, employees held discussions to realize that our efforts to achieve the SDGs were inadequate. Therefore, we decided on a policy to become more closely linked to the local communities through volunteer activities, etc. outside our business. We joined the Jozenji Street Jazz Festival as volunteers and invited visitors to sort their garbage at the recycling station in the venue.



INTERVIEW

Compliance Leader

Compliance Leaders are responsible for promoting overall compliance-related activities in each division, department and branch.

As one of such leaders, I try to take the initiative in activities to foster and deepen compliance awareness at my branch.

I feel that self-directed efforts at each workplace lead to promoting active communication and improving the workplace environment.

Keiko Ishida, Sendai Office



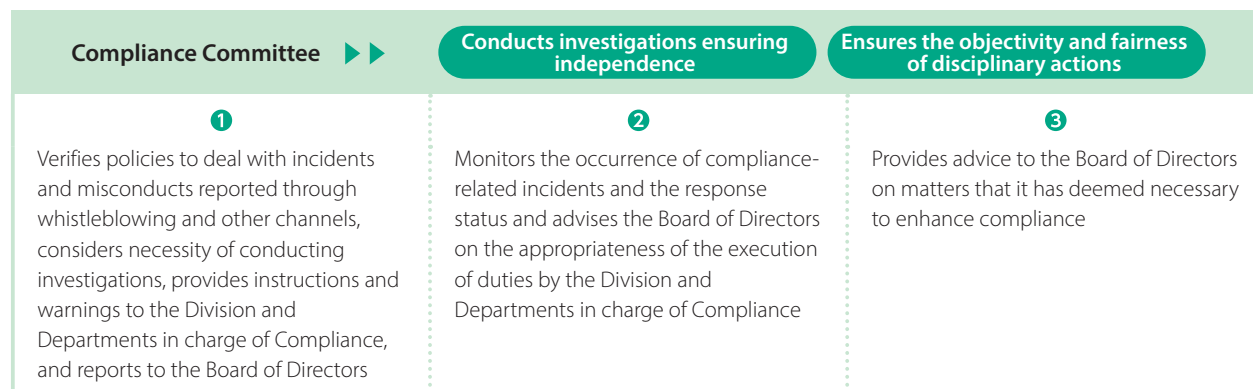
At the Shoko Chukin Bank, we formulate compliance programs for each branch and direct activities by ourselves based on risks and issues in the workplace. We have set October of each year as a month to enhance compliance, and conduct organizational initiatives. The Bank provides us with substantial support, such as a compliance review meeting for branch managers inviting our director with expertise in compliance as a lecturer, which gives us a good opportunity to think about compliance. I feel that such efforts made over the past few years have steadily increased the awareness of compliance in our workplace.

Naohiro Kuroda, General Manager of Sendai Office

Compliance Committee

► The Role of the Compliance Committee

The Compliance Committee is delegated by the Board of Directors to engage in the following three tasks, (1) to (3). The Committee is consulted on all incidents that involve personnel decisions and other disciplinary actions, ensures objectivity and fairness, and provides guidance and checks so that appropriate actions are taken.



► Compliance Committee Members

Compliance Committee members are appointed by the Board of Directors and its chairperson is elected from among members who are outside attorneys-at-law by mutual election.

Compliance Committee	Chairperson	Akira Ehira	(Attorney at law, Mori Hamada & Matsumoto)
	Vice chairperson	Katsumi Nakamura	(Attorney at law, T. Kunihiro & Co., Attorneys-at-Law)
	Member	Hideyuki Makino	(Director and Senior Managing Executive Officer, the Shoko Chukin Bank)

► Activities of the Compliance Committee

The Compliance Committee meets once a month in principle to carefully examine various agendas under the guidance of outside attorneys at law. In fiscal 2018, monitoring commenced under the Committee members (chairperson and vice chairperson) to verify the process of agenda submission to the Committee, which has contributed to preventing omissions in the agenda to be submitted to the Committee while also improving efficiency.

- **Monitoring details:** In addition to the monthly Committee meetings, the chairperson and vice chairperson (outside attorneys-at-law) also conduct monitoring of operational risk events. They also confirm whether there are any omissions in the agenda to be discussed by the Committee on a risk basis and do the process verification including giving instructions to submit the necessary agenda to the Committee.

[Monitoring of operational risk events]

- Monitoring of operational risk events which occurred in the previous month (a certain number is randomly extracted)
- Verifies the investigation results of incidents determined to pose compliance risks and the status of formulating measures to prevent such recurrences, and confirms the appropriateness of decisions on matters which were not submitted as agenda to the Compliance Committee (provides instructions to refer the matter to the Committee, as necessary)

Compliance Committee

● Number of the Committee and Monitoring held

	FY2019	FY2020	FY2021	FY2022	FY2023
Compliance Committee	13	13	12	12	11
Monitoring	12	13	12	12	12
Total	25	26	24	24	23

