

# Chapter 2. Government Bonds (JGBs)

Being the core of the debts associated with financing the activities of the central government such as JGBs, FBs, borrowings, and government-guaranteed debts, JGBs are regarded as credit risk-free financial instruments and play a central role in the bond market.

## 1. Legal Framework of JGBs

### (1) Legal Framework of JGBs

JGBs can be divided into two main categories: general bonds, and Fiscal Loan Fund Special Account bonds (FILP bonds). While the government mainly relies on tax revenue to redeem general bonds, the redemption and the interest payments on FILP bonds are covered through the recovery of loans to special public institutions. However, both general bonds and FILP bonds are JGBs and are the same financial instruments.

JGBs	General bonds	New Financial Resource bonds	Construction bonds Special deficit-financing bonds
		Refunding bonds	
	Fiscal Loan Fund Special Account bonds (FILP bonds)		

(Note) In addition to general bonds and FILP bonds, JGBs consist of subsidy bonds, subscription/contribution bonds and JGBs converted from the debts of various entities including Japanese National Railways Settlement Corporation.

#### A. General Bonds

General bonds consist of 1) New Financial Resource bonds and 2) refunding bonds.

##### 1) New Financial Resource Bonds

New Financial Resource bonds are categorized into construction bonds and special deficit-financing bonds. The former is issued based on the Article 4 of the Public Finance Law <sup>1)</sup> and used as a source of funds for public works, capital subscription and lending. And the latter is issued to cover recurring expenses such as labor costs that cannot be covered by construction bonds. The Public Finance Law does not permit the issuance of special deficit-financing bonds. Therefore, in a fiscal year when the government issues special deficit-financing bonds the Diet must legislate Special Deficit Financing Bond Law <sup>2)</sup>. Both construction bonds and special deficit-financing bonds are issued within the amount approved by the Diet, and the ceiling amount is provided under the General Account. The revenue from their issuance is reported as the government revenue of the General Account.

(Note 1) Public Finance Law (provisional translation)  
Article 4

Any expenditure of the State shall be covered by revenues other than public bonds or borrowings. However, public works, investments, and loans can be financed by the issuance of public bonds or borrowings within a specific amount approved by Diet resolution.  
(below omitted)

(Note 2) Law Concerning Special Cases of Issuance of Public Bonds for the Fiscal Administration, etc in FY2004  
(provisional translation)

Article 2

Other than public bonds issued subject to the proviso in Paragraph 1, Article 4 of Public Finance Law (Law No.34, 1947), the government may issue bonds for the purpose of financing the expenditure for the General Account in FY2004 not exceeding the amount approved by Diet resolution.  
(below omitted)

## 2) Refunding Bonds

Refunding bonds are the JGBs issued through the Special Account for Government Debt Consolidation Fund (GDCF) to raise funds to redeem outstanding JGBs. Revenues from refunding bonds are directly posted to the fund. The ceiling of issuance amount of refunding bonds is not subject to Diet approval in a form of the budget. In practice, however, the issuance amount is calculated so that full redemption completes after sixty years. This is called the "60-year redemption rule." It should be noted that issuance of refunding bonds does not necessarily correspond to the maturity date of specific issues. Refunding bonds are issued in a flexible manner within each fiscal year. Front-loading of refunding bond issuance that corresponds to the redemption due next fiscal year is also possible within the amount approved by the Diet.

(Note) Special Account Law for Government Debt Consolidation Funds (provisional translation)

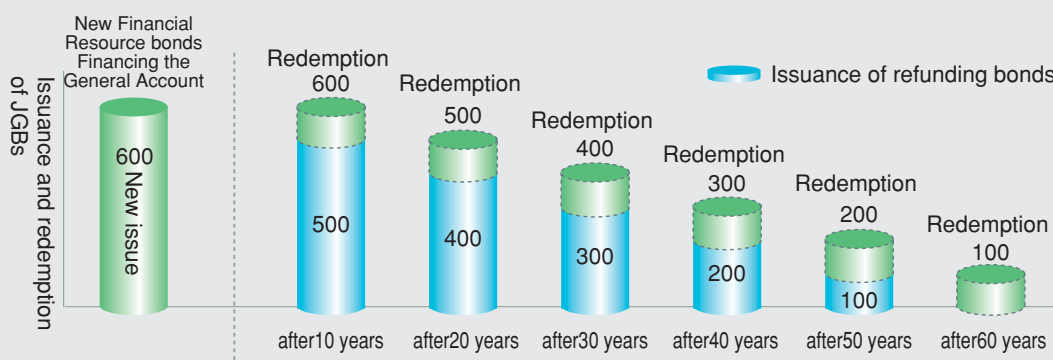
Article 5

The government may issue refunding bonds not exceeding the amount necessary for the consolidation or redemption of government bonds for each fiscal year (including those that should be redeemed during the same fiscal year as these bonds are issued).

(below omitted)

### \* 60-year Redemption Rule

Cash needed for redemption are allocated from the Government Debt Consolidation Fund (GDCF) and the revenues from issuing refunding bonds. The ratios of these resources are determined based on so-called "60-year redemption rule," which means redeeming JGBs 60 years after issuance. The rule stands on the fact that the average economic depreciation period of the assets purchased by construction bonds is about 60 years. Deriving from the rule is 1.6% ratio for fixed-rate transfer for each fiscal year, which is equivalent to one-sixtieth.



(Note) In order to promote fiscal reform, as to special deficit-financing bonds, the government attempts to reduce the outstanding debt as quickly as possible, regardless of the 60-year rule.

👉 See 2-4. (1) A. for information on the redemption mechanism.

## B. Fiscal Loan Fund Special Account Bonds (FILP bonds)

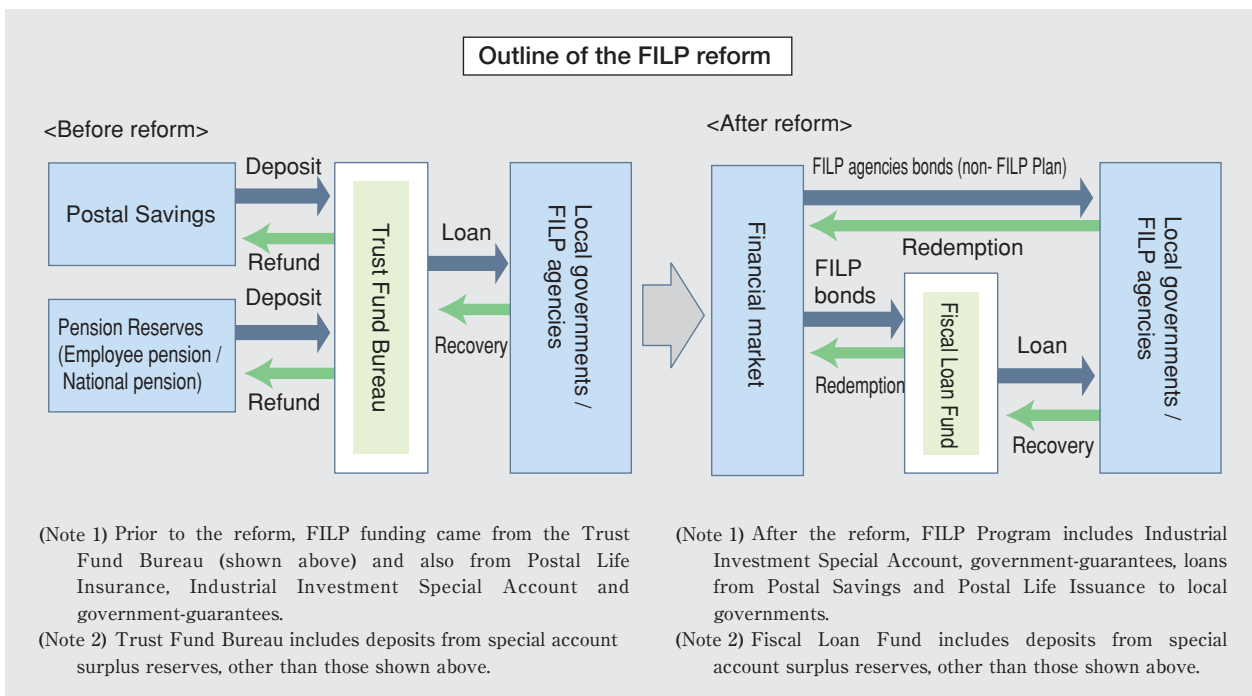
Before the FILP reform, Postal Savings and Pension Reserves were all obliged to be deposited in the Trust Fund Bureau. These deposited funds were the main source for the loans to local governments and FILP agencies, but this compulsory deposit was abolished <sup>(Note)</sup>. Since then, FILP bonds have been issued as a source of the Fiscal Loan Fund. Revenues from the FILP bond issuance is allotted to the annual revenue for the Fiscal Loan Fund Special Account.

(Note) Law for Fiscal Loan Fund Special Account (provisional translation)


Article 11

Public bonds may be issued or funds borrowed for liability under this account if required in order to allocate funding sources for the management of the Fiscal Loan Fund.

(below omitted)



Though, in principle, the government offers FILP bonds to the market, Postal Savings, Postal Life Insurance or Pension Reserves partly underwrite FILP bonds, for a period of seven years from FY2001 as transitional measures.

 See 2-2. (2) B. 4) for information on the transitional measures of FILP bond underwriting.

## (Reference) Other JGBs

In addition to general bonds and FILP bonds, JGBs include the following.

### 1) Subsidy Bonds

Subsidy bonds are issued in place of cash for various purposes such as subscriptions/contributions, condolence payments, and compensations.

At the end-FY2003, subsidy bonds consist of (a) narrowly defined "subsidy bonds" (JGBs issued to the bereaved families of the war dead in lieu of condolence money and other compensations in cash), and (b) subscription/contribution bonds (JGBs issued to pay subscriptions or contributions to organizations such as International Monetary Fund (IMF) and the World Bank in lieu of the amount to be paid in cash.).

### 2) JGBs converted from Japanese National Railways Settlement Corporation Bonds and the like

When the government inherited the debts of Japanese National Railways (JNR), Japanese National Railways Settlement Corporation (JNRSC), Honshu-Shikoku Bridge Authority (HSBA), and Japan National Oil Corporation (JNOC), part of the government-guaranteed bonds that these organizations had issued were converted into JGBs. The converted bonds from HSBA and JNOC were inherited by the government based on "Reorganization and Rationalization Plan for Special Public Institutions" from FY2003.

## (2) Treatment of Government Debt in the Budget

The government has to issue New Financial Resource bonds, FILP bonds, and carry out borrowings within the amount approved by the Diet, and the ceiling amount is provided under the general provisions of the budget. However, the government has the right to determine the amount of refunding bond issuance based on the Article 5 of the Special Account Law for Government Debt Consolidation Fund, and the government does not have to obtain an approval for the amount by the Diet. This is because issuance of refunding bonds does not lead to an increase in the government debt outstanding.

Based on the Article 28 of the Public Finance Law, the report on the estimated amount of JGBs (general bonds and FILP bonds) and borrowings at the end of the fiscal year and the redemption schedule are attached to the budget as reference material.

(Note) Public Finance Law (provisional translation)

Article 28

The budget to be submitted to the Diet shall be attached with the following documents for reference purposes:

(i-iv omitted)

- v Report on the results with regard to the state of government bonds and borrowing at the end of the year before last, report on the estimated amount for government bonds and borrowings at the end of both the previous fiscal year and the current fiscal year, and the redemption schedule.

 See 2-3. (2) (reference 2) for information concerning the redemption schedule for JGBs (general bond).