ISDA® JAPAN MONTHLY UPDATE

August 2014

COMMITTEE ACTIVITIES

REGULATORY: Contact: Tomoko Morita (tmorita@isda.org)

On August 4, ISDA submitted a comment letter to JFSA on its proposed amendments (Japanese only) to the Cabinet Orders and Supervisory Guidelines implementing margin rules for non-cleared derivatives. Comment letter is available at http://www2.isda.org/regions/japan/ (Japanese only).

Summary of the key comments:

- Scope of entities: With regards to requirements on cross-border transactions, ISDA requested clarification that transactions with a foreign counterparty established in non-netting jurisdictions will not be subject to the rules, as two-way posting of collateral may increase counterparty credit risk if netting is not enforceable. ISDA also requested clarification on how firms can determine that a counterparty has a correctly estimated thresholds, and whether firms can rely on a representation by a counterparty.
- Margin calls: On the requirement for daily variation margin (VM) calls, ISDA argued it is necessary to set some exceptions in a subordinate rule and include some flexibility on the timing of margin calls. ISDA noted the requirements will be operationally challenging, particularly for smaller institutions such as regional banks or credit unions, given that some of them have not signed credit support annexes. These institutions may stop trading unless they set up an operational infrastructure for daily margining by December 2015.
- Haircuts: ISDA requested that the 8% haircut for currency mismatch would not be applicable to both IM and VM, at least until practical solutions can be identified. If the haircut must be applied, then it should not be applied to the VM, as it will create additional counterparty risk. The relevant currency risk should be considered in an IM calculation model. Continued discussions between the industry and regulators are requested.
- Implementation timing for VM: ISDA believes the phase-in should be the same as that for IM. There are many end-user financial institutions that do not use collateral for OTC derivatives, and they need to be prepared by December 1, 2015. In addition, there are new requirements, such as the additional 8% haircut for currency mismatches. Many firms need to rebuild their collateral management framework in order to comply with the requirements in a short period of time. Therefore, the transition measures should be considered for VM as well.

DOCUMENTATION/REGULATORY: Contact: Tomoko Morita (tmorita@isda.org)

Cleared Derivatives Execution Agreement:

On August 6, ISDA circulated the list of issues that could be arisen when using the ISDA/FIA Europe Cleared Derivatives Execution Agreement for OTC derivatives that are intended to be cleared by Japan Securities Clearing Corporation (JSCC). The issue list was prepared by Linklaters to review whether the template can be used between execution brokers and the clients that are using JSCC.

COLLATERAL: Contact: Tomoko Morita (tmorita@isda.org)

Members of IM Segregation Working Group met to discuss the structures of the documentations between parties posting collateral, receiving collateral and a trust account. Members also reviewed the operational flows for IM that will be segregated at third party custodians or trust accounts, and discussed issues arisen from cross-border transactions.

UPCOMING COMMITTEE AND WORKING GROUP MEETINGS / CONFERENCES

OTC Derivatives Working Group **September 30**
(Japanese language meeting)

2014 ISDA Annual Japan Conference **October 30**
(English and Japanese language conference)