

Specialist Working Group for Recurrence Prevention Measures
Summary of 4th Meeting

1. Date and time: December 18, 2020 16:00 – 17:35

2. Venue: Meeting room at Tokyo Stock Exchange and online

3. Agenda

- a) Clarification of standards, etc. for trading resumption under the Contingency Plan
- b) Development of rules regarding handling of orders and procedures for resuming trading in the event of a system failure, etc.
- c) Responses in the event of a FLEX failure
- d) System failure drill program for FY2021
- e) Information provision policy in the event of a system failure

4. Summary of discussion

(1) Comments on specific issues

(On order acceptance time/trading hours after recovery)

- As it is likely that HFTs, which have a share of around 45% of trading, would not take part in a trading period of 15 minutes or so, there is a question mark around whether fair price formation could take place. I would like it to be clear that this is a concern.
- If appropriate price formation does not happen because of HFTs or institutional investors not taking part in trading, it is doubtful as to whether the market would need to be opened in that situation. Since those prices are used to calculate base prices for investment trusts, can TSE keep track of whether they are appropriate?
- The ideal would be to ensure as long a trading period as possible, but to make sure that enough care is taken over the restart, I think a minimum period of 15 minutes would be fine. However, there is still doubt over whether fair price formation would be possible with a low participation rate, and I am not sure that trading in that kind of environment would be desirable from a customer perspective.
- As it is important for trading participants to have appropriate price formation from a fiduciary duty perspective, in the unlikely event that a plan like the one we are considering now should actually be put into practice, TSE should carry out verification on the prices that are formed in that short time.

(On extension of trading hours)

- Consideration of topics like extending trading hours on a permanent basis and extra trading sessions should be discussed outside this Working Group.
- I would like you to also consider pushing back the time limits for uploads of base prices from trustee companies, and the deadlines for companies that deal with loan applications to Japan Securities Finance Co., Ltd. and fractional shares.
- I am concerned that if trading hours are extended, they may go on for even longer than originally planned.
- PTS night trading and trading of US stocks continue after trading closes at TSE, so as there is a need to confirm customer information through batch processing, to be safe, an extension of around 30 minutes would be appropriate.
- We can deal with a trading hours extension of around an hour, but anything more than that would be difficult as it would disrupt batch processing.
- As it will have an impact on calculation of base prices, any extension above 30 minutes would mean we have to fundamentally review the current process.
- As it will have an impact on calculation of base prices, we will need to confirm the system/workflow cut-off points for what can be done until when.
- Base prices for investment trusts have to be sent to local newspapers by 19:00 and the Nikkei by 19:30 or the section will be left blank, so I am concerned that an extension of trading hours would affect the media as well. As systems will also have to be altered, I would like you to look into different solutions such as using the night session.

(On information provision regarding trade resumption)

- I would like for TSE to announce information on the plan for trade resumption and trading hours, etc. as early as possible, as if there is no announcement beforehand, we cannot communicate with our fund distributors.
- For communication with fund distributors, considering the procedures that need to be carried out afterwards, realistically we would need to confirm whether or not to accept an order by around lunchtime. As we need to give fund distributors definitive information about the timing of a trading resumption, TSE should set a deadline for deciding this.
- If there is a trading resumption, investment trusts also need to send orders, so we would like TSE to send out information on the expected time for trading resumption at an early stage.

(On the opinion gathering process)

- I think prescribing persons responsible for securities trading as the contact persons for each participant is a transparent framework, but I would like for TSE to also

contact the persons responsible for securities trading for individual communications, such as additional questions.

- TSE should set up some kind of help desk that can answer questions about IT and systems, etc.

(On response procedures for non-acceptance of orders)

- On page 13 of the reference document, Priority 2 suggests that virtual servers will be disconnected after orders are not accepted, but it would be better if these were the other way around.
- As Priority 3 would place a large burden on systems, TSE should consider abandoning this option altogether.
- I would like to confirm the thinking behind Priority 3. I am not sure it is necessary to prepare for a situation where neither 1 nor 2 are implemented – is it really alright to include it just for a once-in-a-blue-moon possibility? It may just be a wording issue but "Order of priority" is surely misleading.

(On inconsistency resolution by system reboot)

- Regarding the handling of sequence numbers shown on page 16, (1) on its own would not be enough to send a sequence number change notification, so TSE should send details of sequence number changes separately using Target, etc., including in the case of rounding up sequence numbers in (2).
- In the case of rounding up sequence numbers, system responses will be different depending on whether the number is changeable or not changeable, so I would like to have an exchange of views on this on a practical level.

(On inconsistency in execution data)

- If execution notices are delayed, the customer may have already taken their next action such as another trade, so contact with the customer will be crucial.
- If error corrections increase because of execution cancellations, processing might not be possible before the deadline, so TSE should think about changing this deadline.
- In the case that some trades have been matched, if trades for which execution notices have been returned are not automatically considered as valid it would surely be difficult to resume trading. Cancelling trades for which securities companies have already received execution notices could definitely lead to trouble.

(On handling of entrusted orders)

- If there is a trading suspension, the plan is that on trading resumption, securities

companies should resend to the Exchange any entrusted orders which have not been executed unless there is a separate instruction from the customer to void them. I would like the Exchange to send a notice to investors about this as a reminder at the same time as announcing the trading suspension.

- Since it would not be desirable for DMA orders and orders for high-speed trading to be resent, and also because of their volume, TSE should specify in the rules in advance that resending these orders is not necessary.
- When securities companies resend an order, I presume that they would need to create a new order slip, but there is a need to confirm whether asset management companies would also need to invalidate their first order and create a new order slip.

(On system failure drills)

- TSE should only change rules after carrying out a sufficient volume of non-business day tests, etc.
- Drills should include market markets and data vendors.

(On recovery responses in the event of a FLEX failure)

- We use trading volume data as volume limits on a real-time basis, and there are a large number of algorithms which are based on these parameters, so if the data is wrong there is a high possibility of incorrect trades being made. For this reason, even if the data is provided after the trading close, it would not work for us.

(The TSE Equity Department is responsible for the wording of the meeting summary. This English translation is for reference purposes only.)