**Outlines concerning Introduction of Variation-Margining-as-Settlement**

October 27, 2016
Japan Securities Clearing Corporation

| Item | Outlines | Remarks |
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| 1. Purpose | ・Currently, in order to collateralize outstanding obligations related to changes in net present values of cleared contracts for Interest Rates Swap Clearing Participants (hereinafter referred to as "Clearing Participant(s)"), etc., JSCC and Clearing Participants post variation margin (hereinafter referred to as "VM") on a daily basis to each other. However, in order to compress regulatory exposures of Clearing Participants, etc., JSCC will review the treatment of VM and introduce the option of VM-as-Settlement in lieu of VM as collateral. | ・VM is defined in Article 2-63 of Interest Rate Swap Clearing Business Rules. |
| 2. Introduction of VM-as-Settlement<br>(1)Exchanging Mark-to-Market Difference. | ・In the case where a Clearing Participant or its Customer selects cleared contracts as stated in 2. (3) below, Mark-to-Market Difference shall be exchanged on a daily basis in lieu of VM in order to cover risks arising from fluctuations in net present values of the relevant cleared contracts.<br>・By charging Mark-to-Market Difference daily, the net present value of the relevant cleared contract shall be reset to "0." | ・ Mark-to-Market Difference means the net increase/decrease calculated after valuating net present value of a cleared contract with market value on a daily basis. It is a cash amount to be exchanged daily to settle exposure related to the relevant cleared contract. |
| (2) Exchanging PAA | ・Together with the Mark-to-Market Difference, PAA shall be | ・PAA (Price Alignment Amount) replicates the economics |

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| | exchanged. | of PAI (Price Alignment Interest=interest on VM) deposited for the OTC Interest Rate Swap transactions (hereinafter referred to as “OTC IRS”), in order to prevent an occurrence of basis risk between uncleared OTC IRS contract and the cleared contract.<br>・Since Mark-to-Market Difference is not treated as collateral, PAA is not an interest.<br>・When calculating PAA, the current PAI calculation formula shall be used. |
| (3) Cleared Contracts subject to VM-as-Settlement | ・Out of all the IRS positions including foreign-denominated cleared contracts, a Clearing Participant or its Customer selects cleared contracts for which Mark-to-Market Difference shall be exchanged with JSCC in lieu of VM. | ・For cleared contracts other than those selected on the left, VM shall be exchanged as collateral.<br>・Once specifying as a cleared contract for which Mark-to-Market Difference is exchanged, it shall not be possible to return to the original VM as collateral.<br>・With regard to collateral other than VM, such as Initial Margin, Collateral, etc., there is no change from the current treatment. |

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| (4) Notification of Cleared Contracts subject to VM-as-Settlement | ・If intending to exchange Mark-to-Market Difference, a Clearing Participant or its Customer shall notify JSCC of the cleared contracts which shall be subject to VM-as-Settlement in advance. | ・If intending that all of cleared contracts recorded in the Proprietary account or Customer account are subject to VM-as-Settlement, the relevant account shall be notified to JSCC in advance.<br>・If intending that some of cleared contracts recorded in the Proprietary account or Customer account are subject to VM-as-Settlement, a Clearing Participant or its Customer shall notify the relevant contracts to JSCC according to the method determined by JSCC on the date determined by JSCC (once a month or so). (For other cleared contracts (including cleared contracts of which obligations are newly assumed), VM shall be exchanged as collateral)<br>・Customer shall make a request via its Clearing Participant. |
| (5) Treatment of New Cleared Contracts to Come into Effect as a Result of Compression, etc. | ・With regard to a new cleared contract following various compressions, position transfer or auction of the defaulter Clearing Participant's position during default management process, it shall come into effect as cleared contract subject to exchange of VM as collateral. | ・ If a new cleared contract comes into effect in the account where notification of the treatment of VM-as-Settlement has been made, it shall be subject to VM-as-Settlement. |
| (6) Operational Treatment | ・With regard to exchange of Mark-to-Market Difference, for operational process such as cash settlement, etc., the current process for deposit of VM shall be followed. | ・No system change anticipated. No change to current daily reports, as well.<br>Also, other procedures, such as compression, etc. remain unchanged. |

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| | | ・When part of cleared contracts recorded in the Proprietary account or Customer account shall be subject to VM-as-Settlement, notification process shall be made via e- mail, etc. |
| 3. Implementation Timing | ・Aimed at December 2016. (Subject to approval of the Commissioner of the Financial Services Agency.) | |

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