Outlines related to Risk Management Framework associated with Introduction of Derivatives Holiday Trading

June 15, 2021

Japan Securities Clearing Corporation

I. Purpose

In association with an introduction of the derivatives holiday trading at Osaka Exchange, Inc. (hereinafter referred to as "OSE") and Tokyo Commodity Exchange, Inc. (hereinafter referred to as "TOCOM"), JSCC introduces the risk management framework to deal with expansion of Clearing Participants' exposures which might occur in the holiday trading[1].

As to the holiday trading, as in the case of night sessions on the business day before the day designated as holiday trading day (hereinafter referred to as "Holiday Trading Day") at OSE and TOCOM, there will be neither settlement of VM/OP premium nor update of initial margin requirements on a Holiday Trading Day. So, in order to suppress accumulation of current exposures as requested in the PFMI and other regulations, JSCC establishes a framework of increasing initial margin requirements in advance of the Holiday Trading Days.

Moreover, during the period of consecutive holidays, such as Golden Week Holidays, there will be holiday trading during multiple consecutive holidays. So, in order to suppress excessive accumulation of exposures specifically during consecutive holidays, JSCC establishes Holiday Clearing Participants monitoring framework under which, when an exposure of a Clearing Participant becomes greater than the value of posted collaterals, such as initial margin requirements, the Clearing Participant will be asked to

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[1] For specific and detailed studies of the holiday trading framework, OSE established the "Working Group on Derivatives Holiday Trading" comprised of market participants last year. The summaries of the discussions at the Working Group published in June 2020 is available on below link. In addition, for details of the holiday trading framework at OSE and TOCOM, please refer to the outlines OSE and TOCOM published as of today.
＜Publication of Report of the Working Group on Derivatives Holiday Trading＞
https://www.jpx.co.jp/corporate/news/news-releases/0060/20200630-01.html
＜Introduction of Derivatives Holiday Trading＞
https://www.jpx.co.jp/english/rules-participants/public-comment/detail/d08/20210615-01.html

post additional collateral or execute risk reduction trades, and if it fails to do so by the deadline, JSCC is allowed to suspend assumption of obligations related to holiday trading of such Clearing Participant.

II. Outline

Item	Outline	Remarks
1. Clearing / Settlement Framework related to Holiday Trading (1) Securities and Similar Contracts Clearing Business to be Conducted on Holiday Trading Days	・ On Holiday Trading Days, JSCC shall provide services related to the assumption obligations concerning the Listed Derivatives that are subject to the holiday trading on OSE and TOCOM, but no other services under the Securities and Similar Contracts Clearing Business.	・ JSCC will provide neither any service related to the Listed Derivatives other than those specified in these Outlines (such as services related to application and renunciation of Clearing Qualifications and settlement by delivery operations for Commodity Derivatives) nor Cash Products Clearing Service. Furthermore, Holiday Trading Days will not be included when counting number of days to be counted based on ordinary business days, such as number of days up to the renunciation when request for renunciation of Listed Derivatives Clearing Qualification has been

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	・ JSCC assumes obligations on Holiday Trading Days for a Clearing Participants which is the trading participant given an advance notification of participation in the Listed Derivatives holiday trading of OSE and TOCOM (hereinafter referred to as "Holiday Clearing Participant") with respect to all Clearing Qualifications such Holiday Clearing Participant holds; provided that, when a trading participant, which has given an advance notification of participation in the holiday trading, submits a notification of its non-participation on a certain Holiday Trading Day to OSE and TOCOM, JSCC shall not treat the Clearing Participant for the relevant trading participant as Holiday Clearing Participant in respect to the relevant Holiday Trading Day. ・ The method of settlement of the contracts for clearing, etc. related to the holiday trading shall be the same as the contracts executed at the night session on the ordinary business day immediately preceding the Holiday Trading Day (hereinafter referred to as "Business Day Before Holiday Trading Day"). Services JSCC provides with respect to the Listed Derivatives on ordinary business days, such as a determination of settlement prices, a settlement of VM/OP premium and update of initial margin requirements, will not be provided on Holiday Trading Days.	submitted, and Default Settlement Period to be set at the time of settlement failure of a Clearing Participant. ・ On any Holiday Trading Day, JSCC will accept no clearing for Clearing Participants that are not Holiday Clearing Participants. ・ OSE and TOCOM accept the notification of participation at each trading participant level. JSCC will cover all Clearing Qualifications the Holiday Clearing Participant holds. ・ The contracts for clearing related to trading at night session are settled together with trading at day session on the next ordinary business day as those executed on the next ordinary business day.

Item	Outline	Remarks
(2) Participants subject to Risk Management Framework related to Holiday Trading	・ The Holiday Clearing Participants are subject to the risk management framework related to holiday trading (2. Preliminary Initial Margin Add-on Framework and 3. Holiday Clearing Participants Monitoring Framework).	
2. Preliminary Initial Margin Add-on Framework		
(1) Preliminary Add-on Calculation Method	・ The preliminary add-on amount to be added to the initial margin requirement shall be decided, respectively for all accounts of a Holiday Clearing Participant managing positions and collaterals related to products listed on OSE governed by the Financial Instruments and Exchange Act (hereinafter referred to as "OSE Accounts") and all accounts of a Holiday Clearing Participant managing positions and collaterals related to products listed on TOCOM governed by the Commodity Derivatives Act (hereinafter referred to as "TOCOM Accounts"), as a sum of the amount equal to certain percentage, prescribed by JSCC according to the number of upcoming Holiday Trading Days and subject contracts for clearing, of the SPAN Margin portion of the initial margin requirement for each account of a Holiday Clearing Participant calculated through SPAN® methodology (margin calculation method developed by Chicago Mercantile Exchange).	・ Under current plan, the percentage to be prescribed by JSCC will be 30% in case of 1 Holiday Trading Day, 45% in case of 2 consecutive Holiday Trading Days, and 60% in case of 3 consecutive Holiday Trading Days. However, it will be revised as necessary based on future market conditions of each product, and the rate to apply at the launch timing will be announced around the end of this year.

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(2) How to Apply Preliminary Add-on	・ As to SPAN Margin calculated for the initial margin requirement called for deposit by the Holiday Clearing Participant on the day immediately preceding the Business Day Before Holiday Trading Day, the preliminary add-on calculated through a method outlined in (1) above will be added to the house initial margin requirement of the Holiday Clearing Participant subject to the Financial Instruments and Exchange Act and those subject to the Commodity Derivatives Act, respectively. ・ However, when a Holiday Clearing Participant desires to exclude a certain customer from an application of the preliminary initial margin add-on framework by reason of such customer not participating in holiday trading, such customer may be excluded from an application of the preliminary initial margin add-on framework if the Holiday Clearing Participant notifies to JSCC the effect that it has business structure in place and has taken measures for restricting such customer's participation in holiday trading and obtains JSCC's approval.	・ See Reference 1 for Illustration of Preliminary Add-on Framework. ・ See Reference x for outline of method of excluding certain customer from an application of the preliminary initial margin add-on framework. ・ Required notification shall also be submitted to OSE and TOCOM, and if it is approved, measures of restricting order from such customer will be taken.
(3) Preliminary Add-on Deposit Method	・ When a Holiday Clearing Participant's house deposited initial margin is insufficient to cover its initial margin requirement including the preliminary add-on, it shall make additional deposit to cover such shortfall by 11:00 a.m. on the next day following the day on which such shortfall arises (calculation day).	・ Handling, such as collateral posting, will be the same as current initial margin deposit.

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(4) Other	・ The preliminary add-on shall not be included in the initial margin requirement and base prorated IM amount in the calculation of base PML amount for the required amount for clearing fund for each Clearing Qualification.	
3. Holiday Clearing Participant Monitoring Framework (1) Benchmark for Holiday Clearing Participant Monitoring	・ On Holiday Trading Days, JSCC will monitor "Risk/Collateral Ratio" as defined below with respect to OSE Accounts and TOCOM Accounts, respectively, of Holiday Clearing Participants: Risk/Collateral Ratio $= \dfrac{\text{Holiday Clearing Participant Risk Amount (Risk at House + Total Risk Exceeding Collateral Deposit at Customer Accounts)}}{\text{Collateral, etc. of Holiday Clearing Participant (House Initial Margin Deposited Amount + Sum of Clearing Fund Deposit for its Clearing Qualifications)}}$	・ In addition to the Holiday Clearing Participant Monitoring, the Holiday Clearing Participants are subject to the monitoring under the framework of emergency margin for specified party on Holiday Trading Days in the same manner as ordinary business days.
(2) Judgement of Excessive Risk in Holiday Clearing Participant Monitoring	・ During consecutive Holiday Trading Days, if, at the judgment timing prescribed by JSCC, "Risk/Collateral Ratio" at either OSE Accounts or TOCOM Accounts of a Holiday Clearing Participant is 100% or more, and the amount of collateral, etc. required to bring such ratio down to less than 100% (hereinafter referred to as "Additional Deposit	・ JSCC currently plans to make judgment at 16:00. For 2 consecutive Holiday Trading Days, JSCC will make judgment at 16:00 on

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	Requirement") is more than the amount of holiday trading reserve (see 4. (2)) related to each account, JSCC judges that the risk of such Holiday Clearing Participant is excessive and ask the relevant Holiday Clearing Participant to take measures for a reduction of "Risk/Collateral Ratio" down to less than 100% (hereinafter referred to as "Resolution of Risk Excessiveness"), through deposit of initial margin in the amount equal to or more than the Additional Deposit Requirement or execution of trades for risk reduction, by 11:00 a.m. on the next Holiday Trading Day following the Holiday Trading Day on which such judgement was made.	the first day, and, for 3 consecutive Holiday Trading Days, JSCC will make judgment at 16:00 on the first and second days.
(3) Additional Deposit Requirement Deposit Method	・When a Holiday Clearing Participant is to deposit initial margin in the amount at least equal to the Additional Deposit Requirement under (2) above, it shall deposit it as its house initial margin by 11:00 on the next Holiday Trading Day.	・ As to the types of currencies and securities eligible for deposit of Additional Deposit Requirement and their deposit method, only those available under the collateral posting scheme on Holiday Trading Days to be designated and announced by JSCC can be used. The collateral appraisal method and other handling shall be the same as initial margin on ordinary business days.

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(4) Treatment when Failing Resolution of Risk Excessiveness	・ When JSCC asks a Clearing Participant to resolve risk excessiveness under (2) above, if no additional deposit has been made as of 11:00 a.m. on the next Holiday Trading Day and JSCC considers that "Risk/Collateral Ratio" of the relevant Holiday Clearing Participant is more than 100%, JSCC may take measures of suspension of clearing of all holiday trading of the relevant Holiday Clearing Participant.	・ Regardless of the account for which risk excessiveness has not been resolved (OSE Accounts or TOCOM Accounts), clearing of holiday trading related to all accounts shall be suspended. ・ When an occurrence of a settlement failure is unlikely in respect of the Holiday Clearing Participant subject to the suspension of clearing related to holiday trading, clearing for the relevant Holiday Clearing Participant on and after the next ordinary business day following the Holiday Trading Day shall be performed normally.
4. Measures Taken upon Settlement Failure of Clearing Participant		
(1) Measures in Case of Settlement Failure on Holiday Trading Day	・ When a Holiday Clearing Participant fails, or JSCC considers it is likely to fail, to perform its settlement of contracts for clearing on a Holiday Trading Day, JSCC will take necessary	・ In principle, the settlement failure on the next ordinary business day

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	measures, such as suspension of clearing for the relevant Holiday Clearing Participant (hereinafter referred to as "Defaulted Holiday Clearing Participant"), make necessary arrangements, such as transfer of unsettled contracts to other Clearing Participants, on the next ordinary business day following the relevant Holiday Trading Day and fix the amount of loss.	following the Holiday Trading Day on which the holiday trading is executed shall be the settlement failure concerning the holiday trading.
(2) Compensation of Loss arising from Settlement Failure related to Holiday Clearing Participant's Holiday Trading	・ When JSCC judges that the Defaulted Holiday Clearing Participant caused the settlement failure concerning the holiday trading, the loss arising from such settlement failure shall be covered, by each Listed Derivatives Clearing Qualification, by the holiday trading reserve contributed from the market operator as a third party contribution which is the 2nd priority loss compensation financial resources in the loss compensation waterfall in advance of the contribution from the market operator under current framework.	・ The loss compensation framework, such as priority of application of resources other than holiday trading reserve, shall be the same as ordinary default of a Clearing Participant. See Reference 2 for priority of loss compensation in case of ordinary settlement failure and settlement failure concerning Holiday Trading Day.

III. Implementation Timing (Tentative)

To be implemented at the same timing as OSE's and TOCOM's introduction of holiday trading framework.

End of Document

Outline of Scheme of Excluding Customer from Preliminary Initial Margin Add-on

Reference 1

- The scheme of excluding a customer from preliminary initial margin add-on is a scheme of allowing a Clearing Participant to exclude certain "customer" from application of preliminary initial margin add-on when the Clearing Participant has in place a framework that is considered to be sufficient to ensure that ordering/execution at an exchange and clearing at JSCC for certain "Customer" of a Participant are restricted, and it is confirmed that the Participant (and "customer") will implement such framework.
- Specifically, under current plan, when conditions listed below are met and letter of understanding is given and other necessary procedures are taken, such customer will be excluded from preliminary initial margin add-on (details are to be announced)

  ① Exchange/JSCC identify "customer" who desires to be excluded from preliminary initial margin add-on, and control so that it will not participate in holiday trading

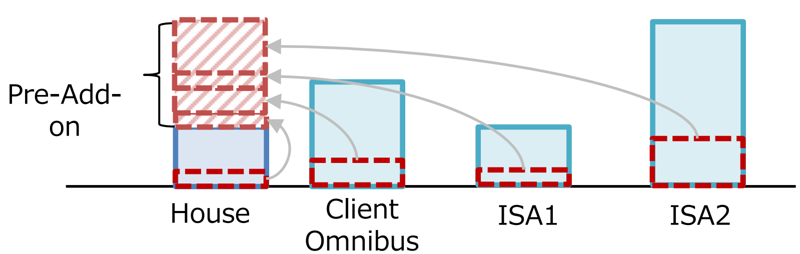
  * Under current plan, segregate "customer" through Sub-Participant Code on J-GATE and ISA account on clearing system, and, upon approval, restrict ordering on Holiday Trading Day from such Sub-Participant Code

  ② Contracts/position related to holiday trading at ISA managing "customer" has not been changed

  * Ex-post facto status check for the relevant account

Ordinary Preliminary Add-on

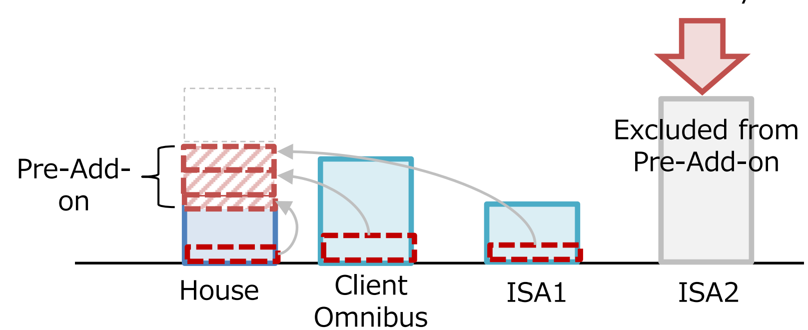
- Apply preliminary add-on to all accounts under the Clearing Participant



When Exclusion Scheme Apply

- Approved account is excluded from application of preliminary add-on

When JSCC considers that "customer" is identified and is under restriction of holiday trading



Loss Compensation Waterfall after Introduction of Listed Derivatives Holiday Trading

Reference 2

Current		
Ordinary Case		
1st	Defaulter's Collateral	
2nd	Market Operator's Contribution	
3rd	JSCC's Contribution	
4th	Survivors' Clearing Fund	
5th	First Special Clearing Charge	
6th	Second Special Clearing Charge	
Unable to Cover by Above	Consultation	
	Early Termination of Position	

After Holiday Trading Launch		
	Ordinary Case	**When Using Holiday Trading Reserve**
1st	Defaulter's Collateral*	Defaulter's Collateral*
2nd	Market Operator's Contribution	**Market Operator's Holiday Trading Reserve**
3rd	JSCC's Contribution	Market Operator's Contribution
4th	Survivors' Clearing Fund	JSCC's Contribution
5th	First Special Clearing Charge	Survivors' Clearing Fund
6th	Second Special Clearing Charge	First Special Clearing Charge
7th	-	Second Special Clearing Charge
Unable to Cover by Above	Consultation	Consultation
	Early Termination of Position	Early Termination of Position

* Including initial margin with preliminary add-on