

Tentative Translation

Abstract of the Interim Report of the Working Group on Shortening Stock Settlement Cycle

December 29, 2015

Working Group on Shortening
Stock Settlement Cycle

This translation is prepared solely for information purposes. The Japanese version should be referred to for the accurate content of the report.

I. Background & fundamental policy for study

Background of study

- Against the backdrop of shortening stock trading settlement cycle (towards T+2) in major overseas markets, a “working group (WG) on shortening stock settlement cycle” was established in July 2015 to start detailed discussion for realizing T+2 in Japan.
- Under the WG, two sub-working groups (Street-side sub-WG and Customer-side sub-WG) consisting of working-level personnel were established to study practical tasks for T+2 implementation.

Fundamental policy for WG study

- To come up with concrete measures for realizing T+2 at early stage, regarding concrete schedule, study on key aspects related to T+2 settlement flow and target implementation time should be concluded within 2015, and the other remaining tasks should be addressed by June 2016.
- Study should concentrate on essential tasks for T+2 implementation in order to come up with concrete measures within a short period of time. In this study, priority should be given to reducing total risks and securing settlement stability in the markets.
- Nevertheless, study items should be revised as appropriate from the viewpoints of more effective and rational markets, also considering the costs and benefits of each measure.

II. Policies on each task

(1) Transactions with non-residents

Study items

- There is a need to study measures on transactions with non-residents, because post-trade handling in such cases will become tight, considering time differences with European and U.S. markets and holidays.
- Settlement failure ratio is estimated to rise to some extent, especially in transactions with non-residents. There is a need to study flexible measures to avoid settlement failures in order to settle transactions as scheduled.

Policies

- Widely disseminate information on the T+2 initiative, in order to make settlement orders on non-resident transactions speedier and more accurate, and also to take prompt measures in such cases as matching discrepancies.
- Upon disseminating information overseas, English documents should also be prepared in order to start dissemination of information at early stage.
- Regarding flexible measures such as switching to non-DVP settlement after the cut-off time for settlement matching, study will be conducted by the “Study group on settlement failure” to be set up under the Customer-side sub-WG (by May 2016).

II. Policies on each task (2) Speed-up of loan transaction handling & improvement of the trade environment

Study item

There is a need to re-examine operation flow in stock lending, because T+1 and T+0 stock lending transactions will become more important for short coverage and fail coverage, etc. respectively.

Policies

- Set up a “Study group on stock lending,” under the customer-side sub-WG, to study following items (by May 2016)
 - Handling flow in stock lending T+1 & T+0 transactions
 - Cut-off time for stock lending T+1 & T+0 transactions
 - Price used for the collateral calculation
 - Others

II. Policies on each task

(3) Rules on Settlement Failure

Study item

Settlement failure ratio is estimated to rise to some extent, especially in transactions with non-residents. There is a need to review rules on settlement failure to promptly cope with it.

Policies

- Revision of rules on settlement failure between JSCC settlement participants
 - JSCC will establish “Guidance for Clearing Members upon occurrence of settlement failures on a record date” which describes standard manner for operational handling after settlement failure occurred on a record date (to be finalized by June 2016)
 - While current rate of charge for ordinary settlement failure should be maintained, study should be continued regarding the charges related to settlement failures on a record date.
 - The method for counting the settlement failure charge is to be changed from a business day basis to a calendar day basis.
 - Buy-in schedule should be shortened by 1 business day. (Buy-in execution day: Buy-in request day + 2 business days)
- Revision of rules on settlement failure with customers
 - “Study group on settlement failure” is to be set up, under Customer-side sub-WG, in order to study establishment of rules on settlement failure with non-resident /domestic transactions, reflecting JSCC’s Guidance above (by May 2016).

II. Policies on each task (4) Study of operation flow related to stock lending application for bidding

Study item

Study whether revision of operation flow and schedule are needed following implementation of T+1 cycle of procurement of stock lending excess issues at a securities finance company

Policies

- The schedule of stock lending application for bidding should not be moved forward but remain as the same, because decrease in bidders and rising of premium charge are expected if the cycle is shortened.
- At the end of accounting term when handling of lending stocks tends to be delayed, and when issues failing to be procured occur, delay to publish data for loans for margin transactions by the securities finance company should be avoided by the means of revision of operations at the securities finance company.
- Regarding operation flow for stock procurement in case of issues failing to procure through the bidding, the securities finance company and concerned people continue discussions (by May 2016).

II. Policies on each task (5) Revision in cut-off times in clearing & settlement infrastructures

Study item

- Study whether revision is necessary for settlement cut-off times in clearing and settlements infrastructures, since there would be an increase in daily operations processes resulting in a tighter schedule on the settlement day due to the move to T+2.
- In addition, study whether revision is necessary for deadline for error correction at stock exchanges, and for data distribution schedule from JSCC.

Policies

- Continue the study with the premise that the various settlement cut-off times should remain the same as now. Nevertheless, if necessity arises for extending the cut-off times after discussions on concrete operations, WG should revisit the extension.
- Deadline for error reports on stock exchange transactions should be prolonged from 13:00 to 14:00. Data distribution schedule from JSCC should also be optimized accordingly.

Various settlement cut-off times	Time
Cut-off time for settlement matching by non-residents	12:20
Cut-off time for JSCC's DVP Settlement (for transactions at exchanges)	13:00
Cut-off time for lending DVP settlement	13:30
Cut-off time for non-exchange DVP settlement	14:00
Cut-off time for FOP settlement	15:30

II. Policies on each task

(6) Other tasks

Study item

Also study the following items expected to arise due to the move to T+2

- Deadline for provision of customer margin and additional margin in margin transactions
- Transactions outside stock exchanges
- Whether to introduce give-up system in cash stock market
- Settlements related to a record date for convertible bonds
- Settlements related to exercise/assignment of securities options

Policies

1. Deadline for provision of customer margin and additional margin in margin transactions
 - Deadlines for margin payment are stipulated by laws and deadlines for additional payment by rules of the stock exchanges. Discussions should be continued on expected effects and operational influences in case of shortening the deadlines, while coordinating with related authorities. Direction should be decided by June 2016.
2. Transactions outside the stock exchanges
 - It is desirable that transactions outside stock exchanges become T+2 accordingly, but that should be still concluded between transaction parties bilaterally. On the other hand, coordination will be made for PTS, which transaction is subject to JSCC's obligation assumption, to be T+2, in line with stock exchanges.
3. Whether to introduce give-up system in cash stock market
 - There is little merit expected by introduction. Therefore, this is not to be discussed.
4. Settlements related to a record date for convertible bonds and exercise of securities options
 - The settlement cycle should be shortened by 1 business day.

III. Target schedule for T+2 implementation

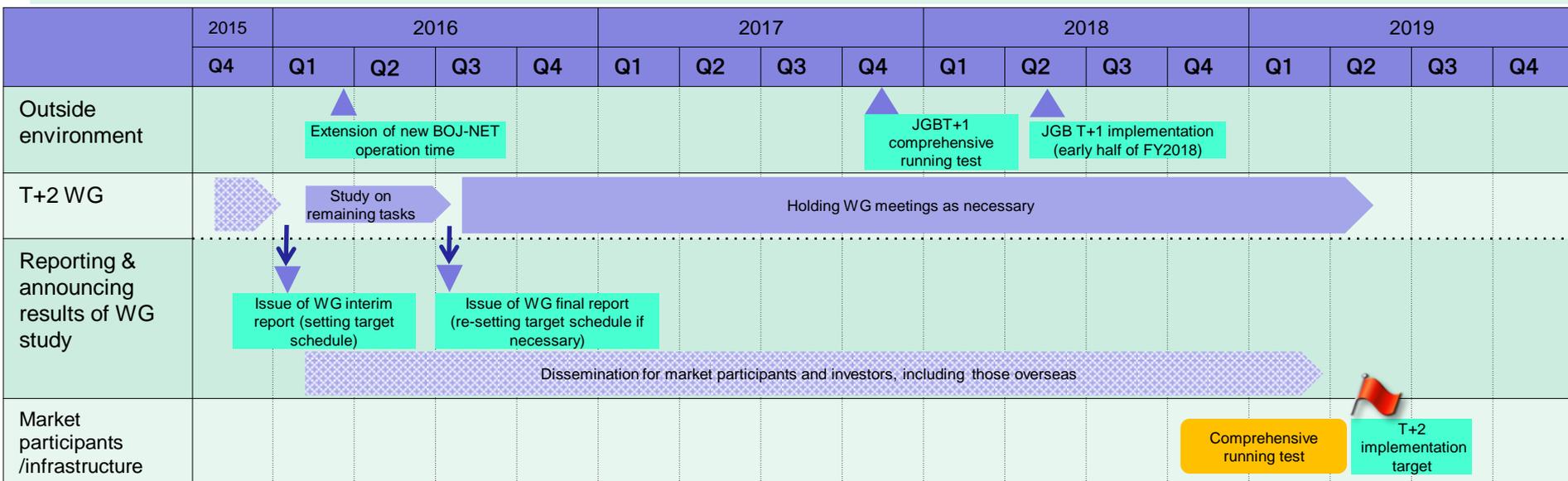
It is not easy to set the specific date of implementation now, but sharing target schedule for T+2 implementation among concerned parties will help achieve more smooth and effective preparation. The target schedule is set as follows.

Target schedule for T+2 implementation

- Target schedule “as early as possible in 2019”
- However, the target schedule should be revised as necessity arises.

Items considered for setting the target schedule

- (1) Procedures and time expected to be required for implementation of T+2
 1. WG discussion on remaining tasks and report of results (by June 2016)
 2. Preparation by concerned parties (market participants and infrastructures) (approx. 2 years)
 3. Implementation of comprehensive running test (approx. 6 months)
- (2) Confirm JGB T+1 stable operation slated for early FY2018 for settlement stability of entire markets.
- (3) T+2 operations in foreign nations



IV. Study to be made and measures to be taken

Study of remaining tasks

WG will continue the study and announce final report by June 2016.

Items for continuous study	<ul style="list-style-type: none">• Speed-up of loan transaction flow, improvement of the trade environment<ul style="list-style-type: none">➢ Improving stock lending market, handling schedule, collaterals, etc.• Rules on settlement failure and streamlining the settlement<ul style="list-style-type: none">➢ Rules on settlement failure (setting guidance upon occurrence of settlement failure on a record date), measures to avoid settlement failures, measures to remedy shareholders' rights in case of settlement failure on a record date, etc.• Study of operation flow related to stock lending application for bidding• Provision of customer margin and additional margin in margin transaction, etc.
Other items	<ul style="list-style-type: none">• Subscription certificates of the Bank of Japan and unlisted securities (bonds, foreign securities, investment trusts)• Stock lending contracts and additional documents, and trade reports, etc.

Dissemination of study results

Disseminate information on Japan's T+2 efforts to market participants and investors, including those overseas, and prompt needed measures and preparation.

Promotion of use of settlement infrastructure

Further promote use of systems helping STP settlement, such as JASDEC pre-settlement matching system, Non-exchange DVP and Lending DVP, etc.