(Tentative translation)

Book-Entry Transfer Guidelines for “Corporate Bonds”

December 2019 Version
（Enforced on July 13, 2020）

Japan Securities Dealers Association

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I. General

1. Purpose

Amid the globalization of securities transactions, making the securities settlement system—the foundation for a market's international competitiveness—a highly reliable and efficient infrastructure is an extremely urgent issue. With this in mind, on January 4, 2001, the Bank of Japan introduced "Real Time Gross Settlement" (hereinafter referred to as "RTGS") for government securities settlements through "the Bank of Japan Financial Network System JGB Services" (hereinafter referred to as "the BOJ Net JGB Services") and for funds settlements through the funds transfer system of the BOJ Net. In addition, on March 31, 2003, the Japan Securities Depository Center Inc. (hereinafter referred to as the "JASDEC") began operations of a transfer and settlement system for short-term corporate bonds.

With the enforcement in Japan on January 6, 2003, of a law that changed the legal framework for securities to enable a strengthening of the securities market based on reform of the securities settlement and other systems, it became possible to introduce a paperless transfer system for corporate and municipal bonds etc. based on the "Law Concerning Book-Entry Transfer of Corporate Bonds, etc". As a result, JASDEC started operation of a Book-Entry Transfer System for "Corporate Bonds" on January 10, 2006. The system enables delivery versus payment (DVP) settlement if processed through JASDEC's Pre-Settlement Matching System (hereinafter the Book-Entry Transfer System for "Corporate Bonds" and Pre-Settlement Matching Systems together are referred to as the "Book-Entry Transfer System").

In view of the introduction of the new book-entry transfer system by JASDEC based on the revisions in the law, the Japan Securities Dealers Association (hereinafter referred to as the "Association"), produced these "Corporate Bonds" Book-Entry Transfer Guidelines. Their purpose is to lay out the practices that market participants should follow when trading corporate and municipal bonds etc. to reduce settlement risk and facilitate smooth settlement under JASDEC's book-entry transfer system.

In December 2013, the Guidelines were amended in line with the second phase launch of the new BOJ-NET. The amended Guidelines have been in force since the date of the second phase launch of the new BOJ-NET (October 13, 2015).

In December 2019, it was decided to amend the Guidelines to accommodate the shortening of the settlement period (T+2 effect)[1] of "Corporate Bonds" transactions in line with the "Final Report of the Working Group on Shortening Stock Settlement Cycle in the Japanese Market."[2], which was published in June 2016.

The Association hopes that all market participants will achieve smoother "Corporate

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[1] While T+2 settlement is desirable in principle on and after the effective date of T+2 effect, due to there being no uniform rule regarding the settlement date as of today (amendment in December 2019), it is deemed that the delivery date can continue to be discretionally determined by and between the transacting parties (in particular, considering that circumstances around system measures, etc. are assumed to vary by company, the amendment does not preclude companies from taking measures according to their individual circumstances).

[2] See page 28 and 29 of the "Final Report of the Working Group on Shortening Stock Settlement Cycle in the Japanese Market." (http://www.jsda.or.jp/shijyo/minasama/t2/e_final_houkokusyo20160630.pdf) by Working Group on Shortening Stock Settlement Cycle.

Bonds” transactions on the basis of the Guidelines.

It should be noted that the Guidelines do not inhibit, in anyway whatsoever, market participants’ rights as guaranteed by law.

2. Effective date of the amended Guidelines

These Guidelines as amended (December 2019 Version) will take effect on July 13, 2020.

II. Guidelines for ensuring smooth settlements

1. Limitation on size of settlements

(1) The upper limit on size of settlements through the Book-Entry Transfer System

Each market participant should set an upper limit on size of settlements processed through the Book-Entry Transfer System at ¥5 billion in face value, in order to curb the daytime accumulation of settlements outstanding and to resolve the delay of settlements, by reducing the amounts of bonds and funds necessary per settlement.

It should be noted that this provision does not hamper transactions with face value exceeding the said upper limit.

(2) How to handle transactions with face value exceeding the upper limit

(i) Market participants who have made bond transactions with face value exceeding the ¥5 billion limit should input processing data via the Book-Entry Transfer System by splitting the transactions in such a way that each size does not exceed ¥5 billion.

(ii) For the purpose of preventing confusion arising from the discrepancy between contract amount and settlement amount after splitting the transaction into smaller sizes, market participants concerned should split agreement slips into units each of which does not exceed ¥5 billion in face value.

(3) Exceptions to the upper limit on size of settlements

The upper limit on size of settlements does not apply to the following transactions in light of their character:

(i) New issue records (new issues) and removals (redemptions and buybacks, etc.);

(ii) Transactions relating to the pledge and release of collateral.

2. Establishment of Cut-off time and Reversal time

(1) Establishment of Cut-off time

(i) For the purpose of recognizing Fails[3] etc. aimed at completing all settlements on the day, Cut-off time shall be the deadline, which market participants decided in bond settlements, prior to the closing time of the Book-Entry Transfer System.

(ii) Market participants should complete sending all transfer messages by Cut-off time.

(iii) Cut-off time shall be 3:00 p.m.

(2) Establishment of Reversal time

[3] Refer to III. 1 regarding “Fails.”

(i) Reversal time is the period of which parties executing the relevant transaction can resolve Fails if they have agreed to extend the delivery deadline over Cut-off time, and correct errors in case of any errors in settlement procedures.

(ii) Reversal time shall be the period from Cut-off time to the closing time for DVP settlement transfer messages on the Book-Entry Transfer System[4].

(3) Guidelines for Cut-off time in the case where the closing time for DVP settlement transfer messages on the Book-Entry Transfer System is extended.

(i) Cut-off time shall be automatically moved backward to the moment 1 hour prior to the extended closing time for DVP settlement transfer messages on the Book-Entry Transfer System in the case where JASDEC has sent a notice of extension to its participants with the coordination with the Bank of Japan at least 15 minutes prior to the original Cut-off time.

(ii) To avoid confusion, Cut-off time shall not be changed in the case where JASDEC has sent a notice of extension to its participants less than 15 minutes prior to the original Cut-off time.

(iii) In the case where the original Cut-off time has been extended, Cut-off time shall be renewed pursuant to above (a) and (b) if JASDEC sends another notice of extension of the closing time for DVP settlement transfer messages on the Book-Entry Transfer System.

3. Guidelines for settlement activities of market participants

(1) Settlement method for "Corporate Bonds"

(i) In terms of reducing settlement risks, market participants should settle bonds on a DVP basis for both proprietary and customer accounts unless there is no other separate agreement between the two parties.

(ii) Market participants should promptly carry out matching after transactions are made in order to facilitate smooth completion of settlements on the settlement day. As a guide, this matching shall be completed by noon of the business day immediately before the settlement date.

However, this does not preclude the transacting parties from otherwise setting a matching time limit upon mutual accord.

(iii) When market participants use the "transfer message suspension function", they should understand that it is a measure to substantially control the timing of

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[4] As of the amendment of December 2019, the closing time for DVP settlement transfer messages on the Book-Entry Transfer System (closing time for the automatic processing from Pre-Settlement Matching System to the Book-Entry Transfer System for "Corporate Bonds") is 4:20 p.m. After this time corrections or reversals cannot be made to the daily DVP settlement transfers. However, adjustments to non-DVP transfers being made through the Pre-Settlement Matching System may occur up to 4:50 p.m. and up to 5:00 p.m. for non-DVP transfers not being made through that system.

sending transfer messages under the automatic processing from matching to transfer systems, and thus try to smoothen the settlements.

Moreover, if a balance remains when the "transfer message suspension function" is utilized, participants shall cancel the function as soon as possible.

(iv) Ordinarily, the first priority for order of settlement should be placed on large-size settlements to minimize the negative effects of Fails, and/or to enhance the progress of operations. However, because there may be cases where operations are delayed by giving priority to large-size settlements, the parties concerned should be aware of actual conditions and execute settlement procedures accordingly.

(v) For settlements, market participants shall, in principle, use their quoting and offsetting accounts with the Bank of Japan; provided that their home accounts may be used subject to their mutual agreement.

(2) Guidelines for activities up to the previous business day before the settlement day

In the case that participants receiving or delivering bonds are using a fund clearing company, the participants should promptly contact the clearing company with the settlement information as soon as possible after the matching of issue or transfer is completed[5].

(3) Guidelines for activities from 9 a.m. to 12:00 noon on the settlement day

(i) Market participants should make every effort to finish all settlements by 12:00 noon in order to facilitate smooth completion of settlements on the day.

(ii) Market participants remitting funds for bond issuance should pay the issuance price as soon as possible after 9 a.m. in order to ensure smooth settlements in the secondary market on the issuance day.

(4) Guidelines for activities from 12:00 noon to Cut-off time on the settlement day

(i) Parties who have settlements remaining unexecuted at 12:00 noon should contact the other parties and require immediate transmission of bonds or funds transfer messages, after making sure of the details of such transactions.

(ii) Where settlements have dragged on near to Cut-off time, the parties delivering bonds should inform the receiving parties of such matters in well advance to ensuring smooth settlements, and make efforts not to transmit bonds transfer messages without prior contact.

(iii) Market participants should observe Cut-off time based on an understanding that an appropriate period is essential as Reversal time to finish all settlements smoothly.

(5) Guidelines for activities after Cut-off time on the settlement day

[5] As an option, JASDEC may contact the clearing company directly with the information.

Market participants should take necessary steps faithfully to complete all settlements making good use of Reversal time.

4. Points to consider in ensuring smooth settlements

It is recommended that market participants handling a large volume of transactions establish their own internal organization to check settlement-related data in their computers, and to input necessary data quickly.

III. Guidelines concerning Fails

1. Definition of a Fail

A Fail means a situation whereby a party receiving "Corporate Bonds" has not received delivery of the relevant securities from the delivering party after the end of the scheduled settlement date.

2. Good-faith efforts to resolve Fails

Fails are not recommendable situations and the frequent occurrence thereof may hinder its primary purpose that is to facilitate smooth transactions and secure market liquidity. Market participants therefore should avoid Fails as much as they can. Upon the unavoidable occurrence of Fails, parties to the relevant transaction will be required to deal with such situations in good faith to resolve the Fail as soon as possible.

3. Conditions to Guidelines concerning Fails

(1) Market participants should note that in view of the policy regarding costs incurred under Fails as described below, they can treat situations as Fails only in respect of the DVP transaction for which bonds are delivered upon payment.

(2) Transactions that resolve Fails should be settled on a DVP basis by re-inputting the transaction from the pre-settlement matching stage.

(3) Market participants shall not exercise the rights of cancellation on the ground of the occurrence of Fails.

(4) It is not acceptable that parties receiving bonds leave settlements incomplete as a result of a shortage of funds.

(5) Market participants should mutually deal on their own with all settlements remaining incomplete other than Fails prescribed in these Guidelines.

4. Policy regarding costs incurred under Fails

(1) A party causing a Fail will, since it is unable to receive funds payable by the party receiving bonds, have to incur some funding costs for holding the bonds and will further have to give up profit that could be earned by investing such funds. Moreover, accrued interest to be received by such failing party will only be for the period up to the scheduled settlement date.

(2) A party suffering from a Fail will, contrary to the above, be able to receive interest accrued from the scheduled settlement date to the date of actual receipt of the bonds and will further also be entitled to invest funds in hand retained due to the uncompleted settlement.

(3) Therefore, no specific penal provisions have been established for Fails, and no payments of default interest, etc. will be required (see Exhibit).

5. Applications to Fails based on Cut-off time

(1) Any transactions that have not been registered in the transfer account by the Book-Entry Transfer System at the point of Cut-off time shall be defined as a Fail unless it is agreed in advance to extend the delivery deadline by the parties involved.

Market participants shall note that even in the case of making prior agreements for extended delivery, they have to treat transactions remaining unsettled by the closing time for DVP settlement transfer messages on the Book-Entry Transfer System as Fails.

(2) Market participants to whom the provision of (1) above applies should deal with such situations in good faith to avoid frequent occurrence of Fails.

6. Guidelines for payments and receipts in the case where coupon payment and/or redemption have occurred prior to resolution of Fails

(1) In the case where a coupon has been paid prior to resolution of a Fail[6], the receiving party shall claim against the delivering party for an amount equivalent to coupon payment receivable by the receiving party. And the delivering party should pay the amount to the receiving party.

(2) Where the securities are redeemed prior to resolution of a Fail[7] (excluding (3) and (4) below), the receiving party shall claim against the delivering party for an amount equivalent to coupon payment and redemption amount receivable by the receiving party. And the delivering party should then pay such amount to the receiving party on behalf of receipt of the original contract amount for the relevant securities.

In the case where the securities are redeemed prior to resolution of Fails, market participants should note that the contract between the parties is regarded as completed by this payment.

(3) Where the securities are partially redeemed and the coupon is paid prior to resolution of a Fail (excluding final redemption payment) and where the parties have recognized that the outstanding balance (original contract amount less partial redemption amount) can still be delivered to the receiving party, the receiving party shall claim against the delivering party for securities equivalent to the outstanding balance plus payment for the partial redemption amount and an equivalent coupon amount (*1) originally contracted for. And the delivering party should then deliver the securities equivalent to the outstanding balance and pay the partial redemption amount and an equivalent coupon amount to the receiving party on behalf of receipt of the original contract amount for the relevant securities.

With this payment, the transaction between the two parties shall be deemed completed.

(*1) Amount equivalent to the coupon for the originally contracted amount (the

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[6] This paragraph shall also apply to the case of a partial redemption where the partial redemption has not taken place and only the coupon has been paid.

[7] This shall include a partial redemption that is a final payment, and apply to calls as well as scheduled redemptions.

amount before the partial redemption)

(4) Where the securities are partially redeemed and the coupon is paid prior to resolution of a Fail (excluding final redemption payment) and where the parties have recognized that the outstanding balance (original contract amount less partial redemption amount) cannot be delivered to the receiving party, the receiving party shall claim against the delivering party for an amount equivalent to the partial redemption amount and an equivalent coupon amount originally contracted for (*1 above). And the delivering party should then pay such amount to the receiving party on behalf of receipt of the original contract amount for the partial redemption amount of securities (*2).

(*2) Original transaction amount[8] x (pre-redemption factor lesspost - redemption factor) + accrued interest

With this payment, the remaining contractual obligations for the two parties shall be the delivery of the outstanding balance of securities (original transaction amount less partial redemption) by the delivering party and the payment [original contract amount less original contract amount for the partial redemption (*2 above)] for those securities by the receiving party.

[8] The original contract amount is the selling price (bond price excluding accrued interest) x (face value /100)

IV. Guidelines concerning bilateral netting

Market participants shall use JASDEC's Book-Entry Transfer System. In principle, "Corporate Bonds" shall be settled and cleared using the gross-gross method of coordinated processing, with book-entry transfers being made by JASDEC and cash settlement made by the Bank of Japan.

However, based on previous agreement by both parties, it is possible that netting between two parties could be an effective method to use in terms of achieving smooth settlements. If such netting is used, it is necessary for both parties involved to understand the function (process) of the contract and pre-settlement matching systems of the Book-Entry Transfer System and to determine the feasibility of such a netting system.

The following are descriptions of possible netting schemes.

(1) In the case where the two parties can recognize that the frequency of netting between them will be high, they will only use trade matching on the Book-Entry Transfer System, and will carry out netting based on the Japanese Government Securities Guidelines for Real Time Gross Settlement (IV. The Guidelines concerning bilateral netting).

(2) In the case where it becomes necessary to carry out netting after the settlements matching on the Book-Entry Transfer System, the two parties shall cancel the settlement instructions on the Book-Entry Transfer System by the business day prior to the settlement date after confirming the details with each other by telephone or other means of communication beforehand. The parties shall do so based on the Japanese Government Securities Guidelines for Real Time Gross Settlement (IV. The Guidelines concerning bilateral netting).

Established on April 27, 2005
Enforced on January 10, 2006
Amended on December 10, 2013
Enforced on October 13, 2015
Amended on December 18, 2019
Enforced on July 13, 2020

(Exhibit)

Provisional treatment of
“Policy regarding costs incurred under Fails”

The “Policy regarding costs incurred under Fails” set out in paragraph 4 of “III. Guidelines concerning Fails”, aims to establish a market practice regarding non-payment of default interest, etc. among market participants in light of facilitating smooth operations of transactions and securing market liquidation, based on the conclusion that the occurrence of Fails can be sufficiently suppressed by the economic rationale set out in (1) and (2) of this paragraph 4. However, this economic rationale may not function effectively in the current situation of unusually low interest rate that can lead to frequent reoccurrence of Fails. This factor does not fit in with the purpose of settlement practices regarding Fails and may cause significant adverse effects on penetration of settlement practices for the “Corporate Bonds” market in Japan. Therefore it is defined, for the time being, as provisional treatment that the party receiving “Corporate Bonds” may, when suffering from Fails, claim against the delivering party for costs which are incurred for obtaining “Corporate Bonds” in securities lending transaction etc.

This provisional treatment will be reviewed when it is concluded that the “Policy regarding costs incurred under Fails” set out in paragraph 4 of the “III. Guidelines concerning Fails” provide sufficient economic rationales upon costs incurred under Fails, in light of situations in “Corporate Bonds” settlements and changes in market environment etc. after the start of the Book-Entry Transfer System for the “Corporate Bonds.”

[Reference]

Guidelines for ensuring smooth settlements through customers' accounts of the BOJ NET JGB Services System etc. (Framework)

IV. Guidelines concerning bilateral netting

1. Standard netting scheme

If market participants intend to use the netting scheme described below, an agreement to perform netting pursuant to these Guidelines shall be established in advance between the two parties intending to conduct or conducting mutual transactions, which agreement is not necessarily required to be in writing.[9]

(1) Netting structure

If there are such outstanding obligations due on the same day between two market participants that can pair with each other (whereby each participant is to deliver government securities and pay funds to the other), the two market participants shall offset their respective delivery and payment obligations for each security or fund and then settle the net balance between them. Unless and until such net balance is settled, the rights and obligations under the original contracts to be netted shall remain effective as they are. (This netting method is hereinafter referred to as "bilateral payments netting.")

(2) Volume to be netted

Bilateral payments netting may be performed for two offsetting transactions for the same issue of JGB with the same face value. (Netting for such paired transactions is hereinafter referred to as a "pair off.")

(3) Settlement methods that can be covered by netting

Bilateral payments netting may be performed for transactions subject to DVP settlement.

(4) Deadline for trade matching for netting

To perform bilateral payments netting for certain contracts, exchange of the information necessary for trade matching shall be completed by 4:30 p.m. on the business day immediately preceding the delivery date under those contracts, and their trade matching shall be completed on the same day from 4:30 p.m. to 4:45 p.m..

(5) Types of transactions eligible for netting

Bilateral payments netting may be performed for a combination of purchase and sale transactions (including conditional purchase and sale), a combination of cash-collateralized securities lending and borrowing transactions, and a combination of any of the foregoing transactions[10].

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[9] JSDA has obtained a legal opinion that bilateral netting prescribed by these Guidelines is valid under Japanese laws.

[10] In this context, the term "conditional purchase and sale" refers to initial sale transactions and repurchase transactions in conditional purchase and sale transactions, and the term "cash collateral securities borrowing and lending transactions" refers to borrowing and lending of relevant securities.

(6) Form of holding securities

Securities eligible for bilateral payments netting shall be book-entry transfer government securities.

(7) Transaction accounts eligible for netting

Bilateral payments netting shall be performed between the accounts of the same type and shall not be performed between different types of accounts.

(8) Pairing method

Pairing for bilateral payments netting shall be made in descending order of the amount to be delivered.

If there are multiple contracts with the same delivery amount, how to select the contracts to be paired shall be determined by the market participants concerned.

(9) Entry into effect of netting for contracts with the same delivery amount

If the delivery amounts to be netted for both contracts are equal to each other and both parties therefore does not need to pay and receive any difference amount in the bilateral payments netting operation, this netting shall take effect at 8:30 a.m. on the settlement date, which is the start time for settlements through the BOJ-NET on the said settlement date (or at 7:30 a.m. if the period of the BOJ-NET JGB services on the said settlement date is extended).

(10) Designation of the account used for fund settlement

For fund settlement for bilateral payments netting, market participants shall, in principle, designate their current accounts with the Bank of Japan.

2. Alternative netting based on the standard netting scheme

(1) With a view to reducing the settlement volume across the entire market with the aim of enhancing back-office efficiency and mitigating the burden of providing funds, market participants may adopt an alternative netting scheme if both parties agree to do so, on condition that priority is given to use of the standard netting scheme. The alternative netting scheme in this context means a scheme for netting for contracts for the same issue with different face values which is designed by adopting the scheme of “bilateral payments netting” defined in Section IV.1 “Standard netting scheme” and then modifying the conditions described in paragraphs (2) and (8) of Section IV.1 (hereinafter referred to as “bilateral payments netting between different face values”).

However, when using this alternative scheme, the conditions described in paragraphs (3) to (7), (9) and (10) of Section IV.1 shall be fulfilled in the same way as required under the standard netting scheme, with a view to ensuring settlement efficiency.

(2) Bilateral payments netting between different face values pursuant to paragraph (1) shall be performed by either one-to-one netting or consolidated netting described as follows, to be adopted based on mutual agreement between the market participants concerned, rather than following the condition of Section IV.1(8).

i. One-to-one netting between different face values

When pairing contracts to perform one-to-one netting between different face values, the following steps shall be taken for the contracts that have not been covered by any pair off under the standard netting scheme.

A) For the contracts not covered by any pair off, pairing is made in descending order of the face value.

B) If there are multiple contracts with the same face value, pairing is made in descending order of the amount to be delivered.

C) If there are multiple contracts bearing the same delivery amount and the same face value, pairing is made in chronological order of the contract date.

D) If there are multiple contracts bearing the same delivery amount, the same face value and the same contract date, how to select the contracts to be paired is determined by the market participants concerned.

ii. Consolidated netting between different face values

Consolidated netting between different face values is bilateral payments netting between different face values performed by settling the difference obtained by calculating the total amount to be settled for the contracts for the same issue that have not been covered by any pair off under the standard netting scheme.

When pairing contracts to perform consolidated netting between different face values, the following steps shall be taken.

A) For all the contracts not covered by any pair off, the total amount to be delivered by the delivering participant and the total amount to be received by the receiving participant are calculated for each issue[11].

B) All the contracts constituting the total amount to be delivered or the total amount to be received calculated under paragraph A), whichever is the greater, are sorted in accordance with the following steps.

(a) Sorting in descending order of the face value

(b) Sorting in descending order of the amount to be delivered, if there are multiple contracts with the same face value

(c) Sorting in chronological order of the contract date, if there are multiple contracts bearing the same delivery amount and the same face value

(d) Sorting by the method to be determined by the market participants concerned, if there are multiple contracts bearing the same delivery amount, the same face value and the same contract date

C) The contracts sorted pursuant to paragraph B) are added up in the sorting order specified therein until the aggregate amount reaches the total amount to be

[11] The total amount to be delivered and the total amount to be received are calculated based on the face values of relevant securities.

delivered or the total amount to be received calculated under paragraph A), whichever is the smaller.

D) The total amount to be delivered or the total amount to be received as calculated under paragraph A), whichever is the smaller, and the total amount obtained under C) are offset.

E) All other contracts not covered by consolidated netting between different face values under paragraph D) are settled on a gross basis.

(3) In order to further encourage market participants to adopt netting with a view to reducing the settlement volume across the entire market, market participants may adopt another alternative netting scheme incorporating modifications of the conditions described in Section IV.1(3) to (5), based on their mutual agreement, on condition that priority is given to use of the pairing off procedure in bilateral payments netting under the standard netting scheme.[12]

When using this alternative scheme, the conditions described in paragraphs (6) to (10) of Section IV.1 shall be fulfilled in the same way as required under the standard netting scheme, with a view to ensuring settlement efficiency.

(4) The legal validity of the alternative netting schemes specified in these Guidelines has been confirmed, as is the case with the standard netting scheme.

3. Operational procedures in netting

(1) Instructions for pairing and sorting

If the market participants concerned have mutually agreed to adopt the netting scheme, paring off or pairing and sorting for bilateral payments netting between different face values may be processed, without being required to give notice in each instance.

(2) Pre-settlement matching notice for netting

If a delivering participant and a receiving participant agree to perform netting for the contracts selected by them, each of them shall issue a pre-settlement matching notice listing the contracts to be netted and send this notice to the other party by 5:00 p.m. on the business day immediately preceding the delivery date. The form of pre-settlement matching notice is separately specified in the Practical Guidelines for Computerization and Standardization of Post-Trade Processing of JGB Transactions.

(3) Deadline for pre-settlement matching

Pre-settlement matching for netting shall be completed by 5:30 p.m. on the business day immediately preceding the delivery date.

(4) How to send pre-settlement matching notices

[12] For example, market participants may perform netting for pair offs in FOP settlements or uncollateralized securities lending transactions.

The method agreed upon by both parties is used.[13]

(5) Principle of cross-checking pre-settlement matching notices

Pre-settlement matching notices shall be cross-checked by both parties.

(6) Objection notice

If either party has any objection to the pre-settlement matching notice received from the other party, both parties shall complete their matching by 5:30 p.m. on the business day immediately preceding the delivery date by sending a correct matching notice.

(7) Departments responsible for pre-settlement matching

In general, the duties of pre-settlement matching are assigned to departments engaged in back-office operations. However, market participants may appoint other departments to control pre-settlement matching procedures and inform other relevant market participants according to circumstances.

4. Pre-settlement confirmation, pre-settlement notice, and their relation with pre-settlement matching notice

Market participants may exchange pre-settlement confirmations (cf. Model Form 1) and pre-settlement notices (cf. Model Form 2) at their option. Such correspondence may help confirm the mutually agreed-upon conditions, descriptions of the account to be used for fund settlement, contact persons, and other details of the scheme of standard netting or alternative netting adopted by relevant market participants.

The points to note when exchanging pre-settlement confirmations or pre-settlement notices are as follows.

(1) Pre-settlement confirmations and pre-settlement notices between two market participants shall, in principle, be sent to each other. If there is any discrepancy between the content mutually verified in advance and the confirmation or notice actually sent, the two parties shall recheck the content.

(2) Each pre-settlement confirmation, pre-settlement notice or pre-settlement matching notice is supposed to contain a statement, “Netting is based on ‘IV. Guidelines concerning bilateral netting’ of The Japanese Government Securities Guidelines for Real Time Gross Settlement of JSDA.” Therefore, any of these documents allows the market participants concerned to readily confirm their agreement to adopt the standard or alternative netting scheme.

    If pre-settlement matching notice is sent electronically, it may be difficult in practical operations to declare in the notice that netting is based on these Guidelines. It is therefore determined appropriate that the market participants concerned make it a practice to exchange pre-settlement confirmations and pre-settlement notices in advance wherein the

[13] Examples of specific sending methods are given in the Practical Guidelines for Computerization and Standardization of Post-Trade Processing of JGB Transactions.

method of sending pre-settlement matching notice and both parties' adherence to these Guidelines are confirmed. In addition, since it is practically difficult to affix signatures or seals on pre-settlement matching notices, exchanging pre-settlement confirmations or pre-settlement notices is a recommendable solution for market participants who prefer to rely on written instruments bearing the signatures or seals set by the parties concerned for the purpose of confirming their agreement.

(3) The practice of exchanging pre-settlement confirmations or pre-settlement notices may possibly cause discrepancies between the descriptions in such notice and those in a pre-settlement matching notice to be subsequently exchanged. In this case, the pre-settlement matching notices shall prevail over the pre-settlement confirmations because the former indicates the latest confirmation between the two parties just before the intended settlement. If, however, the parties cannot reach agreement on the content of the pre-settlement matching notices, the settlement shall be processed in accordance with the pre-settlement confirmations.

5. Netting other than bilateral payments netting

Some market participants may agree to perform netting under a non-standard netting scheme other than the standard netting scheme or alternative netting schemes specified in these Guidelines when such non-standard scheme is expected to reduce settlement volumes and thus contribute to enhancing back-office efficiency and mitigating the burden of providing funds.[14] If market participants intend to introduce any non-standard netting scheme, the points listed below must be noted.

(1) When market participants perform netting, they need to assume the possibility of Fails or failure to complete fund settlement. Therefore, market participants shall consider and establish the procedure to identify the contracts to be treated under a Fail or fund settlement failure which may occur and how to address the Fail or fund settlement failure.

(2) When market participants set a mutually agreeable netting scheme in place, due regard shall be given to operational efficiency, as well as to reduction of settlement risks, which the promotion of RTGS primarily aims for.

(3) If market participants intend to perform netting other than bilateral payments netting, they shall ascertain and accurately recognize the legal validity of their netting scheme.

[14] For example, one conceivable method is obligations netting; in the case where multiple receivables and payables may arise between two market participants that are supposed to be performed on the same day, whenever a new receivable is created, it is immediately offset against then outstanding payables without awaiting the maturity date; in this way, a net amount finally payable and receivable between the two parties on the maturity date is calculated by offsetting and consolidating all outstanding obligations due on the same day.