

New Japanese Margin Regulations for Non-cleared OTC Derivative Transactions

1 Introduction

Following the publication of a policy framework establishing margin requirements for non-centrally cleared derivatives agreed by the Basel Committee on Banking Supervision and the International Organisation of Securities Commissions, the Financial Services Agency of Japan (the “**FSA**”) published a set of final regulations on margin requirements on 31 March 2016 following the publication of the first draft regulations dated 3 July 2014 and the revised draft regulations dated 11 December 2015. The final regulations comprise the Cabinet Office Ordinance on Financial Instrument Businesses, etc. (*kin'yuu shouhin torihiki gyou tou ni kansuru naikaku furei*)¹ (the “**Cabinet Office Ordinance**”), the Supplementary Provisions (*fusoku*) (the “**Supplementary Provisions**”), the Financial Services Agency Public Notice No. 17 (*kin'yuu chou kokuji dai juunana gou*) (the “**Public Notice No. 17**”), the Financial Services Agency Public Notice No. 15 (*kin'yuu chou kokuji dai juugo gou*) (the “**Public Notice No. 15**”), the Financial Services Agency Public Notice No. 16 (*kin'yuu chou kokuji dai juuroku gou*) (the “**Public Notice No. 16**”), the revised Comprehensive Guidelines for Supervision of Major Banks, etc. (*shuyou kou tou muke no sougouteki na kantoku shishin*), the revised revised Comprehensive Guidelines for Supervision of Small- and Medium-Sized and Regional Financial Institutions (*chuushou chiiki kin'yuu kinan muke no sougouteki na kantoku shishin*), the revised Comprehensive Guidelines for Supervision of Cooperative Banks (*keitou kin'yuu kinan muke no sougouteki na kantoku shishin*), the revised Comprehensive Guidelines for Supervision of Financial Instruments Business Operators, etc. (*kin'yuu shouhin torihiki gyousha muke no sougouteki na kantoku shishin*), the revised Comprehensive Guidelines for Supervision of Insurance Companies (*hoken gaisha muke no sougouteki na kantoku shishin*) and the revised Comprehensive Guidelines for Supervision with respect to Trust Companies, etc. (*shintaku kaisha tou ni kansuru sougouteki na kantoku shishin*).² Under the final margin regulations, financial instruments business operators, such as securities companies, and

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¹ Cabinet Office Ordinance No. 52 of 2007, as amended.

² <http://www.fsa.go.jp/news/27/syouken/20160331-4.html> (in Japanese)

registered financial institutions, including licensed banks and licensed insurance companies (“**FIBOs**” and each a “**FIBO**”) that engage in OTC derivative transactions as a business will be required to exchange variation margin and/or initial margin when they trade OTC derivative transactions other than those subject to mandatory clearing³ or transactions which have gone through a clearing process on a voluntary basis (each a “**Relevant Transaction**”). Under the final regulations, the implementation of the requirement to exchange margin when conducting non-centrally cleared derivatives transactions will take place on 1 September 2016 (the “**Effective Date**”).

2 Variation Margin

More specifically, the final variation margin regulations are as follows.

2.1 Detailed obligations⁴

Each FIBO is required to:⁵

- 2.1.1 calculate, every day, on a per counterparty basis (a) the total amount of the mark-to-market value of the Relevant Transactions and (b) the total amount of (x) the value of variation margin received from the counterparty or (y) the value of variation margin delivered to the counterparty;
- 2.1.2 submit an immediate request following the calculation pursuant to paragraph 2.1.1 above to the counterparty to deliver variation margin in an amount equal to the aforementioned mark-to-market value (a) plus the total amount of variation margin delivered to such counterparty or (b) minus the total amount of variation margin delivered by such counterparty (as applicable),⁶ except in the case where the difference does not exceed an amount pre-agreed by the parties (provided that such pre-agreed amount needs to be 70 million yen or less in total with the pre-agreed amount in respect of the initial margin exchange);

³ Since November 2012, the FIBOs have been required to clear certain types of OTC derivative transactions via the mandatory use of central clearing under the FIEA.

⁴ A FIBO is exempt from such obligations with respect to a Relevant Transaction until 28 February 2017 if the following condition is satisfied with respect to either party (or both parties) to the Relevant Transaction: the average amount of reference notional amount (with respect to OTC derivatives, OTC commodity derivatives (in each case, excluding those cleared at Japanese or non-Japanese central counterparties) and FX forwards and swaps where both parties are (i) a Non-Japanese Party (as defined in paragraph 2.2.1 or (ii) a Reporting FIBO (as defined in paragraph 2.2.4) on the last day of each Relevant IM Month, together with such reference notional amount of the other companies in the same group (excluding such reference notional amount with respect to the transactions between the same group companies), is equal to or less than 420 trillion yen. See Article 2, paragraphs 1 and 2 of the Supplementary Provisions.

⁵ Article 123, paragraph 1, item 21-5 of the Cabinet Office Ordinance

⁶ Only if the difference is plus.

- 2.1.3 receive from the counterparty the variation margin without delay if the amount calculated based on paragraph 2.1.1 is plus or post to the counterparty the variation margin if the amount calculated based on paragraph 2.1.2 is minus (as applicable);⁷ and
- 2.1.4 where it enters into several Relevant Transactions with the same counterparty on behalf of several different trust accounts, comply with the obligations set out in paragraphs 2.1.1 to 2.1.3 above separately for each such trust account.

2.2 Exempt cases

However, a FIBO is exempt from such obligations in respect of a Relevant Transaction if, as of the VM Calculation Time (as defined below):⁸

- 2.2.1 either party to the Relevant Transaction is neither (a) a FIBO nor (b) a VM Non-Japanese Party;

where “**VM Non-Japanese Party**” means an entity which (i) engages in OTC derivative transactions in a country outside Japan where it is recognised that agreements on the Close-out (*ikkatsu seisan*) (the “**Close-out**”) as defined in Article 2, paragraph 6 of the Act on Close-out Netting of Specified Financial Transactions Conducted by Financial Institutions, etc. (*kin'yu kikan tou ga okonau tokutei kin'yu torihiki no ikkatsu seisan ni kansuru houritsu*) (the “**Netting Act**”)⁹ and similar agreements are valid in light of the laws and regulations of such country as a business (excluding non-Japanese governments, central banks of non-Japanese states, multilateral development banks, and the Bank for International Settlements) (the “**Non-Japanese Party**”) and (ii) whose average amount of reference notional amount with respect to the Relevant Transactions on the last day of each Relevant VM Month is estimated to be equal to or exceed 300 billion yen, determined in a reasonable manner based on various factors including, but not limited to, certain features of the transactions;

“**Relevant VM Month**” means each month from April in the year that is two years before the VM Calculation Year until March in the year that is one year before the VM Calculation Year (from April one year before the VM

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2015, Capital Markets:
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⁷ If there is a difference between the amount of the variation margin calculated based on the provisions in paragraph 2.1.1 and the amount calculated by a counterparty as the amount of the variation margin, receive from the counterparty the amount calculated based on the pre-agreed methods without delay or deliver to the counterparty such amount (as applicable).

⁸ Article 123, paragraph 10 of the Cabinet Office Ordinance

⁹ Act No. 108 of 1998, as amended.

Calculation Year until March in the VM Calculation Year if the VM Calculation Time falls within December);

“**VM Calculation Time**” means the time at which the calculation described in paragraph 2.1.1 above is made by the relevant FIBO; and

“**VM Calculation Year**” means the year in which the VM Calculation Time falls.

- 2.2.2** the Relevant Transaction belongs to a trust account whose average amount of reference notional amount (with respect to Reported Transactions) on the last day of each Relevant VM Month is less than 300 billion yen;

where “**Reported Transactions**” means such OTC derivative transactions which are subject to information recording and reporting obligations under the provisions of the Financial Instruments and Exchange Act (*kin'yuu shouhin torihiki hou*)¹⁰ (the “**FIEA**”).

- 2.2.3** the parties to the Relevant Transaction are within the same group;

- 2.2.4** either party (or both parties) to the Relevant Transaction is a FIBO, which is not a Reporting FIBO;

where “**Reporting FIBO**” means (i) a financial instruments business operator engaging in a Type I Financial Instruments Business (*dai isshu kinyuu shouhin torihiki gyō*) as defined under Article 28, Paragraph 1 of the FIEA, (ii) (a) a bank that is a registered financial institution, (b) an insurance company that is a registered financial institution, (c) The Shoko Chukin Bank, Ltd. (as a registered financial institution), (d) Development Bank of Japan Inc. (as a registered financial institution), (e) Shinkin Central Bank (as a registered financial institution), or (f) The Norinchukin Bank (as a registered financial institution).

- 2.2.5** either party (or both parties) to the Relevant Transaction is a FIBO whose average amount of reference notional amount with respect to Reported Transactions¹¹ on the last day of each Relevant VM Month is less than 300 billion yen. Where a transaction is exempt under paragraph 2.2.4 above, the exemption in paragraph 2.2.4 shall prevail. Transactions which belong to a trust account do not qualify for exemption under this paragraph, but might qualify for the exemption in

¹⁰ Act No. 25 of 1948, as amended.

¹¹ Reported Transactions which are in respect of a trust account are not being taken into account for the calculation of this average.

paragraph 2.2.2 depending on the features of the transaction;
or

- 2.2.6 the Relevant Transaction is designated by the authorities as exempt on the basis that it is likely that it is not contrary to public interest or does not prevent the protection of investors. (e.g. because it is already in compliance with the laws of a non-Japanese jurisdiction or other similar circumstances regarding the relevant FIBOs.)

3 Initial Margin

The final initial margin regulations are as follows.

3.1 Detailed obligations

Each FIBO is required to:¹²

- 3.1.1 calculate, on a per counterparty basis, a reasonable estimate for the potential costs or losses arising from Relevant Transactions¹³ (the “**Loss Estimate**”) based on the calculation methods as provided in paragraph 3.3 in the following cases (each case, the “**IM Calculation Time**” and the year in which the IM Calculation Time falls, the “**IM Calculation Year**”);
- (i) a Relevant Transaction is entered into, terminated or rights or obligations under a Relevant Transaction are otherwise changed;
 - (ii) one month has passed since the day on which the Loss Estimate was last calculated; or
 - (iii) a request to that counterparty for delivery of the initial margin is deemed necessary due to a fluctuation in quotations or another reason (excluding the cases listed in (i) and (ii) above);
- 3.1.2 submit a request to the counterparty to deliver initial margin in an amount equal to:
- (i) the Loss Estimate; minus
 - (ii) (a) the total amount of initial margin delivered by such counterparty; and
 - (b) if there is any threshold agreed by the parties, the threshold (not to exceed 7 billion yen in total for the party and the other companies within the same group¹⁴), except in the case where the difference does not exceed an amount pre-agreed by the parties

¹² Article 123, paragraph 1, Item 21-6 of the Cabinet Office Ordinance

¹³ Excluding transactions (or a part thereof) associated with the exchange of principal of cross-currency swaps. The same shall apply hereafter in paragraph 3.1.

¹⁴ Article 3 of the Public Notice No.17

(provided that such pre-agreed amount needs to be 70 million yen or less in total with the pre-agreed amount in respect of the variation margin exchange);

- 3.1.3 receive from the counterparty the initial margin without delay if the amount calculated based on paragraph 3.1.1 is plus or post to the counterparty the initial margin if the amount calculated based on paragraph 3.1.1 is minus (as applicable);¹⁵
- 3.1.4 manage the posted initial margin by means of methods including, but not limited to, establishing a trust so that it can be (a) utilised upon a default of the counterparty or (b) be returned when a Close-out Event (*ikkatsu seisan jiyuu*) as defined in Article 2, paragraph 4 of the Netting Act or any other similar event occurs with respect to the relevant FIBO;
- 3.1.5 not create a security interest in or lend such posted initial margin excluding the cases where such posted initial margin comprises cash and such creation or lending is conducted by using a safe method incidentally with the management of the initial margin pursuant to paragraph 3.1.4 above; and
- 3.1.6 where it enters into several Relevant Transactions with the same counterparty on behalf of several different trust accounts, comply with the obligations set out in paragraphs 3.1.1 to 3.1.5 above separately for each such trust account.

3.2 Exempt cases

However, a FIBO would be exempt from such obligations in respect of a Relevant Transaction if, as of the IM Calculation Time:¹⁶

- 3.2.1 either party to the Relevant Transaction is neither (a) a FIBO nor (b) a VM Non-Japanese Party¹⁷ whose average amount of reference notional amount (with respect to OTC derivatives, OTC commodity derivatives (in each case, excluding those cleared at Japanese or non-Japanese central counterparties) and FX forwards and swaps where both parties are (i) a Non-Japanese Party or (ii) a Reporting FIBO on the last day of each Relevant IM Month, together with such reference notional amount of the other companies in the same group (excluding such reference notional amount with respect to the transactions between the same group companies), determined in a reasonable manner based on various factors

¹⁵ If there is a difference between the amount of the variation margin calculated based on the provisions in paragraph 3.1.1 and the amount calculated by a counterparty as the amount of the variation margin, receive from the counterparty the amount calculated based on the pre-agreed methods without delay or deliver to the counterparty such amount (as applicable).

¹⁶ Article 123, paragraph 11 of the Cabinet Office Ordinance

¹⁷ In this sentence, "VM Non-Japanese Party" has the meaning given to it in paragraph 2.2.1, provided that "VM Calculation Time" in its definition shall be replaced with "IM Calculation Time".

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including, but not limited to, certain features of the transactions, is estimated to exceed 1.1 trillion yen¹⁸ (an “**IM Non-Japanese Party**”);

where “**Relevant IM Month**” means each month from March in the year that is one year before the IM Calculation Year until May in the year that is one year before the IM Calculation Year (from March until March in the IM Calculation Year if such IM Calculation Time falls between September and December);

- 3.2.2 the Relevant Transaction belongs to a trust account (a) whose average amount of the reference notional amount regarding the Reported Transactions on the last day of each Relevant IM Month is less than 300 billion yen or (b) whose average amount of the reference notional amount regarding Relevant Transactions, OTC commodity derivative transactions (excluding those cleared at Japanese or non-Japanese central counterparties) and FX forwards and swaps where both parties are (i) a Non-Japanese Party or (ii) a Reporting FIBO on the last day of each IM Relevant Month is equal to or less than 1.1 trillion yen;¹⁹
- 3.2.3 the parties to the Relevant Transaction are within the same group;
- 3.2.4 either party (or both parties) to the Relevant Transaction is a FIBO, which is not a Reporting FIBO;
- 3.2.5 either party (or both parties) to the Relevant Transaction is a FIBO whose average amount of reference notional amount (regarding Reported Transactions²⁰ on the last day of each Relevant IM Month is less than 300 billion yen. Where a transaction is exempt under paragraph 3.2.4 above, the exemption in paragraph 3.2.4 shall prevail. Transactions which belong to a trust account do not qualify for exemption under this paragraph, but might qualify for the exemption in paragraph 3.2.2 depending on the features of the transaction;
- 3.2.6 either party (or both parties) to the Relevant Transaction is a FIBO whose average amount of reference notional amount (with respect to OTC derivatives, OTC commodity derivatives (in each case, excluding those cleared at Japanese or non-Japanese central counterparties) and FX forwards and swaps

¹⁸ According to the transitional measures, from 1 September 2016 to 31 August 2017, 420 trillion yen; from 1 September 2017 to 31 August 2018, 315 trillion yen; from 1 September 2018 to 31 August 2019, 210 trillion yen; from 1 September 2019 to 31 August 2020, 105 trillion yen and from 1 September 2020, 1.1 trillion yen. See Article 2, paragraphs 1 and 3 of the Supplementary Provisions.

¹⁹ The same transitional measures as footnote 18 will apply.

²⁰ Reported Transactions which are in respect of a trust account are not being taken into account for the calculation of this average.

where both parties are (i) a Non-Japanese Party or (ii) a Reporting FIBO) on the last day of each Relevant IM Month, together with such reference notional amount of the other companies in the same group (excluding such reference notional amount with respect to the transactions between the same group companies), is equal to or less than 1.1 trillion yen.²¹ Where a transaction is exempt under paragraphs 3.2.4 or 3.2.5 above, the exemption in paragraph 3.2.4 or 3.2.5 (as applicable) shall prevail. Transaction which belong to a trust account do not qualify for exemption under this paragraph, but might qualify for the exemption in paragraph 3.2.2 depending on the features of the transaction; or

- 3.2.7 the Relevant Transactions is designated by the authorities as exempt on the basis that it is likely that it is not contrary to public interest or does not prevent the protection of investors. (e.g. because it is already in compliance with the laws of a non-Japanese jurisdiction or other similar circumstances regarding the relevant FIBOs.)

3.3 IM calculation method

Each FIBO is required to calculate, on a per counterparty basis, the Loss Estimate based on a method using the quantitative calculation model (the “**Model**”), of which the Commissioner of the Financial Services Agency must be notified in advance, or the standardised approach (the “**Standardised Approach**”) with respect to the Relevant Transactions where such FIBO cannot calculate the Loss Estimate based on the Model.²²

3.3.1 Model

A summary for the Model is as follows:²³

- (i) each FIBO must use a one-tailed 99% confidence interval over 10-day or more horizons;
- (ii) each FIBO must calculate the Loss Estimate as the sum of the initial margin calculated for each risk category (credit, commodity, equity, FX and interest rates and others) (each a “**Risk Category**”);
- (iii) each FIBO can reflect risk offset, diversifications and other hedging benefits within the same Risk Category (not across the Risk Categories);
- (iv) each FIBO must use historical data that meets the following conditions;

²¹ The same transitional measures as footnote 18 will apply.

²² Article 1 of the Public Notice No. 15

²³ Articles 3 to 6 of the Public Notice No. 15

- (a) whose observation period is from (and including) 1 year to (but excluding) 5 years;
- (b) that covers the stress period;
- (c) that includes the recent market data;
- (d) that is not weighted data; and
- (e) that will be recalibrated at least annually;
- (v) the Model must recognise non-linear risks, basis risks and risks that have a material impact on the exposures; and
- (vi) each FIBO must arrange a system for the management of the Model that meets certain requirements.

3.3.2 Standardised Approach

The Standardised Approach adopts the following formula whereby the Loss Estimate is calculated on a per master agreement (that includes the agreement on the Close-out) basis (on a per Relevant Transaction basis if the Relevant Transaction is not based on such master agreement):²⁴

(formula)

$$IM = 0.4 \times \text{Gross IM} + 0.6 \times \text{NGR} \times \text{Gross IM}$$

IM: Loss Estimate

Gross IM = the notional amount for a Relevant Transaction multiplied by the percentage depending on each Risk Category and the remaining period for maturity

NGR = Net Reconstruction Cost / Gross Reconstruction Cost (if the gross Reconstruction Cost is zero, the NRG is one)

Net Reconstruction Cost: total amount of the market value of the Relevant Transaction (zero if that total amount falls below zero)

Gross Reconstruction Cost: total amount of the market value of the Relevant Transaction (zero if that market value falls below zero).

4 Voluntary Inclusion into the In-scope Transactions

A FIBO can voluntarily include one or more transactions that fall within the category provided as below into the transactions subject to the variation and/or initial margin regulations on the condition that (i) such FIBO complies with the obligations as provided in paragraph 2.1 and

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²⁴ Article 9 of the Public Notice No. 15

(ii) such FIBO continuously includes such transaction(s) with a counterparty into the Relevant Transactions.²⁵

- 4.1.1 the Relevant Transactions that are entered into prior to the Effective Date or whereby a FIBO is exempt in accordance with the transitional measures as provided in footnote 4 and 18;
- 4.1.2 with respect to the exchange of initial margin, transactions (or a part thereof) associated with the exchange of principal of cross-currency swaps;
- 4.1.3 OTC commodity derivative transactions (excluding those cleared at Japanese or non-Japanese central counterparties);
- 4.1.4 FX forwards and swaps;
- 4.1.5 transactions exempted from the obligations as provided in paragraphs 2.1 and 3.1 in accordance with paragraphs 2.2 and 3.2; and
- 4.1.6 transactions that are conducted based on a master agreement that includes the agreement on the Close-out (limited to where such FIBO conducts the Relevant Transactions pertaining to the obligations as provided in paragraph 2.1 and 3.1 pursuant to that master agreement, and excluding transactions listed in paragraph 4.1.1 through 4.1.5).

5 Eligible Collateral

5.1 Types of eligible collateral

The types of eligible collateral are as follows (applicable to both variation margin regulations and initial margin regulations):²⁶

- 5.1.1 cash;
- 5.1.2 government debt securities, local government debt securities, supranational organisations' debt securities, (if applicable) with specific ratings by eligible rating firms (excluding securities issued by a group company of the relevant FIBOs) (collectively the “**Governmental Debt Securities, etc.**”);
- 5.1.3 other debt securities (excluding a securitisation exposure or a re-securitisation exposure and securities issued by a group company of the relevant FIBOs) (if applicable) with specific ratings by eligible rating firms (collectively, the “**Other Debt Securities**”);

²⁵ Article 123, paragraph 7 of the Cabinet Office Ordinance and Article 2, paragraph 1 of the Supplementary Provisions

²⁶ Article 123, paragraph 8 of the Cabinet Office Ordinance and Article 1 of the Public Notice No.16.

- 5.1.4 equities included in a main index or convertible bonds whereby bonds can be converted into such equities with specific ratings by eligible rating firm (excluding equities or convertible bonds issued by a group company of the relevant FIBOs) (collectively the “**Relevant Equities**”); and
- 5.1.5 investment trusts, etc. whose investment target is limited to the items as provided in paragraph 5.1.2 through 5.1.4) and transaction price in the market is published every transaction date (collectively, the “**Investment Trusts, etc.**”).

5.2 Haircuts

The haircut percentage applicable to each eligible collateral is as follows:²⁷

- 5.2.1 cash
0%;
- 5.2.2 the Governmental Debt Securities, etc.
0.5% to 15% depending on the remaining period for maturity and credit ratings;
- 5.2.3 the Other Debt Securities
1% to 12% depending on the remaining period for maturity and credit ratings;
- 5.2.4 the Relevant Equities
15%; and
- 5.2.5 Investment Trusts, etc.
0.5% to 15% depending on the remaining period for maturity and credit ratings of the investment target of the Investment Trusts, etc.

Further, if the currency of the eligible collateral and the currency predetermined for a party with respect to one or more Relevant Transactions are different, an additional 8% haircut percentage applies when calculating the value of the relevant eligible collateral.²⁸

6 Applicability of regulations to cross-border transactions

The exemptions from the margin requirements are provided on a transaction basis and are complex particularly where a non-Japanese entity is involved. We have summarised how the regulations apply in such a circumstance.

²⁷ Article 2, paragraph 1 of the Public Notice No.16

²⁸ Article 2, paragraph 2 of the Public Notice No.16

6.1 Case study

The margin regulations target FIBOs as provided in Article 40, Item 2 of the FIEA and accordingly, in principle a non-Japanese entity that is not a FIBO would not be subject to the margin regulations. However, even if a non-Japanese entity itself is not subject to the margin regulations, there might be situations where compliance with the margin regulations by its counterparty has an indirect impact on the non-Japanese entity.

If, for example,²⁹ a non-Japanese entity enters into a Relevant Transaction with a Japanese counterparty³⁰ that (a) is a Reporting FIBO and (b) has a sufficient volume of transactions so that it can not satisfy the conditions for exemption provided in paragraph 2.2.5 (or paragraph 2.2.2 in the case where the Japanese counterparty is acting as trustee for a trust) and in paragraphs 3.2.5 and 3.2.6 (or in paragraph 3.2.2 in the case where the Japanese counterparty is acting as trustee for a trust) in respect of the Relevant Transaction and:

- 6.1.1 if the non-Japanese entity is a Reporting FIBO³¹ and does not satisfy the conditions for exemption provided in paragraph 2.2.5 (and those provided in paragraph 3.2.5 and 3.2.6) in respect of the Relevant Transaction, the variation margin regulations (and initial margin regulations, if applicable) apply to both parties;
- 6.1.2 if the non-Japanese entity is neither a Reporting FIBO, a VM Non-Japanese Party nor an IM Non-Japanese Party in respect of the Relevant Transaction, the initial and variation margin regulations do not apply to either party; and
- 6.1.3 if the non-Japanese entity is not a Reporting FIBO but is a VM Non-Japanese Party and/or an IM Non-Japanese Party in respect of the Relevant Transaction, the variation margin regulations and/or initial margin regulations (as applicable) do not directly apply to such non-Japanese entity but apply to the Japanese counterparty. In this case, since the Japanese counterparty is required to comply with the variation and/or initial margin regulations, the non-Japanese counterparty would practically be required to agree to post margin and

²⁹ The analysis is based on the following assumptions: (i) the parties are not within the same group, (ii) neither party meets the conditions for exemption provided in paragraph 2.2.6 (in respect of the variation margin regulations) and paragraph 3.2.7 (in respect of the initial margin regulations) and (iii) the foreign entity does not act as trustee for a trust.

³⁰ A Japanese entity acting through a foreign branch is included.

³¹ If a foreign entity acts through a Japanese branch that is a registered financial institution, such foreign entity falls within the Reporting FIBOs.

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otherwise respond to the performance by the Japanese counterparty to the extent necessary for the Japanese counterparty to comply with the regulations.

6.2 Substituted compliance

In light of the provisions described in paragraphs 2.2.6 and 3.2.7, if a FIBO (including a non-Japanese entity that is a FIBO) follows the requirements in a jurisdiction with regulations which are recognised as equivalent to the Japanese margin regulations, such FIBO might be deemed to have complied with the Japanese margin regulations. However, details of the substituted compliance provision will be determined in a notice by the Commissioner of the FSA, and currently the FSA has not published a draft of such notice.

7 Implications for repackaging transactions

The new regulations mainly apply to inter-bank transactions and in most cases derivatives transactions with a typical SPC incorporated in a tax haven in connection with repackaging transactions are exempt from the regulations (as the SPC will not fall into the category of a VM/IM Non-Japanese Party). Derivatives transactions with a Japanese trust (in the case where the trustee is a trust bank) are usually exempt since repackaging transactions using a Japanese trust typically do not reach 300 billion yen (see paragraphs 2.2.5 and 3.2.5) (the 300 billion yen threshold is counted for each trust account, rather than each trust bank).

Accordingly, the impact of the new regulations on repackaging transactions is negligible.

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This publication is intended merely to highlight certain key issues that arise in the context of carrying on banking business in Japan or lending to a Japanese borrower. This publication is not intended to be comprehensive, nor to provide legal advice. It must not be relied on in relation to a particular transaction. Should you have any questions on issues reported here or on other areas of Japanese law, please contact one of your regular contacts at Linklaters Tokyo, or contact the editors.

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