(Tentative translation)

[II] Reports from the Sub-Group on Loans

■ Approach to Fallbacks for Loans

The following are the views of the members of the Sub-Group on Loans regarding the possible options for (1) trigger events, (2) replacement benchmarks, and (3) spread adjustments in fallbacks for syndicated and bilateral loans. The sub-group intends to continue further deliberation on the topic, taking into account ISDA's approach to fallbacks for derivatives and developments overseas (e.g., the hardwired/amendment approach proposal by the U.S.'s ARRC), and focusing on the minimization of economic value transfer.

(1) Trigger events

- ✓ Two trigger events -- the permanent discontinuation of LIBOR announced by the LIBOR administrator or its regulatory authority -- proposed in the ISDA consultation paper are expected to be included in the contracts.
- ✓ As for other triggers proposed in the United Kingdom and the United States, the choice to include them is left to the related parties after taking into account hedge accounting issues.

(2) Replacement benchmarks

- ✓ In light of the results of the ISDA public consultation, adopting compounding O/N RFR (fixing in arrears) could be an option to ensure hedge effectiveness against derivatives under the ISDA Master Agreement. However, there are non-negligible operational concerns and other challenges that need to be addressed.
- ✓ On the other hand, in view of the development of term reference rates, term reference rates, which have equivalent interest rate features with LIBOR, and TIBOR also remain options.

(3) Spread adjustments

- ✓ Although adopting the "historical mean/median approach" proposed by ISDA could be an option, it could cause operational challenges and/or data sourcing issues depending on the replacement benchmark.

■ Issues for Loans regarding Hedge Accounting

As for issues regarding hedge accounting, efforts will be made to consult the matter with the Accounting Standards Board of Japan and other related parties as deemed necessary. It is assumed that the main debate will be whether it is possible for the hedging relation to continue to be effective in the following scenarios. However, it is necessary to prioritize some issues over others since it may not necessarily be possible to achieve immediate resolution of all issues.

(1) When the replacement benchmark of a hedged item (loans) and that of its hedging instrument (derivatives) to be used after the activation of fallbacks differ

(2) (With the replacement benchmarks being the same,) when the timing of activation of fallbacks for a hedged item and its hedging instrument differ because of a difference in trigger events between the two products (e.g., in cases where loans are transitioned to their replacement benchmarks due to after fallbacks are triggered, while related derivative products are still referencing LIBOR.)

Note: Regarding hedge accounting, in addition to the above, issues such as the eligibility of a forecast transaction, derecognition of a hedged item, changes in the terms of delivery and payment of swap transactions, and the burden of verifying hedge effectiveness were raised. Other accounting issues may include fair valuation, deferred and accrued accounts (accrued interests) in compounding in arrears, and disclosure.

■ Contractual Issues

Contractual issues including the following will be explored while consulting with relevant parties as necessary. However, some issues need to be prioritized over others since it may not necessarily be possible to achieve immediate resolution of all issues.

- ✓ Whether or not there is room for streamlining contract amendment procedures
- ✓ The extent to which fallbacks need to be specified in view of the standardized contract format provided by the Japan Syndication and Loan-trading Association (JSLA)
- ✓ Considerations from the difference between individual loan contracts and the JSLA's standardized format