

(Tentative translation)

## **Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks**

### **Minutes for the November 5, 2020 Meeting**

**5:00—6:00 PM**

**(Meeting Room in the Bank of Japan and via Webex Meetings)**

#### **I. Update on International Discussions on Interest Rate Benchmarks**

1. The Secretariat informed the Committee of the latest discussions on interest rate benchmarks in major jurisdictions.
2. The International Swaps and Derivatives Association (ISDA) explained the overview on the fallback provisions in derivative contracts as well as its future work plan.

#### **II. Report from the Sub-group and the Task Force on Term Reference Rates**

The chair of the Sub-Group on Loans and the Task Force on Term Reference Rates (hereinafter the Task Force) reported what had been discussed so far in the sub-group and the Task Force since the last meeting.

The chair of the Sub-Group on Loans reported on the results of the consultation on the use of the "historical median approach over a five-year lookback period" as a spread adjustment methodology when using TIBOR as the fallback rate. In particular, members of the sub-group shared the view that there might be conduct risk if the lender's explanation to the borrower was not sufficient when using the historical median approach. In addition, regarding the spread adjustment for TIBOR, the results of the consultation on the calculation methodology based on the "historical median approach over a five-year lookback period" were reported. Furthermore, the chair reported that many members had supported the "Lookback without Observation Shift" method as the interest calculation methodology for TONA (Fixing in Arrears) in loans, as a result of the consultation conducted by the sub-group, and that members had shared the view that the sub-group would continue with its deliberations in the future if necessary, especially concerning the deliberations and publication of items that might be able to receive support from many members.

The Task Force informed the Committee of the daily publication of prototype rates for Term Reference Rates that QUICK Corp. had begun on October 9, 2020, and also explained that it had been proceeding with the preparatory work on the publication of production rates as planned, in accordance with the schedule displayed in the second public consultation paper. Moreover, as examples of the progress in the preparatory work, the Task Force explained

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the following two points: establishing the governance system and improving the preciseness of and transparency in calculation methodologies.

### III. Discussion about the Outcome of the Second Public Consultation

1. The Secretariat reported that a total of 35 entities from a wide range of industries provided comments to the public consultation during the comment solicitation period from August 7 to September 30, 2020.
2. The Secretariat explained the main points of the outcome of the second public consultation as follows.

It was reported that, in general, most respondents supported the waterfall structures and the spread adjustment methodologies which the Committee had recommended for the fallbacks in both loans and bonds.

Regarding the issues that market participants should address in order to make JPY OIS transactions more active, respondents mainly indicated the following: (1) increasing cash products referencing O/N RFR Compounding (Fixing in Arrears), (2) encouraging market participants' proactive engagement in OIS transactions, and (3) creating an environment that would make it easier for dealers to submit quote data.

The Committee was planning to publish the results of the consultation by the Sub-Group on Loans on the spread adjustment methodologies when TIBOR would be used as the fallback rate for loans, along with the points to note, in the final report on the results of the second public consultation. In addition, the Committee was also planning to publish the calculation methodologies organized by the Sub-Group on Loans on the Committee's website, together with the results of the second public consultation.

- Given the explanation above, a securities company member made the following comments.

It was still unclear to market participants whether the principal alternative reference rate for yen-denominated derivatives transactions would be the Tokyo Term Risk Free Rate (TORF) or the Tokyo O/N Average rate (TONA). Therefore, it would be desirable for the Committee to show the direction in this regard. In particular, the use of TONA in the derivatives markets has not increased in Japan as much as that of the Sterling Overnight Index Average (SONIA) in the United Kingdom and of the Secured Overnight Financing Rate (SOFR) in the United States, so it seemed necessary to take more active measures

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to promote the use of TONA in the derivatives markets. In addition, with a view to aiming the publication of production rates for TORF by the middle of 2021 at the latest, there was concern that the measures to make the JPY OIS market more active, which were shown in the draft of the final report on the results of the second public consultation, would be insufficient given the limited time available.

Based on this point of view, we would like to propose the following measures: in anticipation of the transition from LIBOR, the Committee should (1) clarify that the alternative interest rate benchmark that had been supported the most for derivatives was TONA, not TORF, (2) hold market-wide events to boost the activities of the JPY OIS market participants (e.g., in the case of the United Kingdom, additional recommendations on the transition to SONIA had been issued to interest rate swap market participants), and (3) introduce initiatives to make the JPY OIS market more active in the form of a roadmap (e.g., to help identifying when financial institutions should cease conducting new derivative transactions referencing JPY LIBOR with a maturity date after the end of 2021).

- In response, the Secretariat provided the following comments.

From the perspective of supporting OIS transactions to improve the robustness of TORF, the position of TONA in the derivatives markets seemed to be one of the important issues as it had been pointed out. The Secretariat would like to consider how the Committee should address this issue.

On the other hand, there was a view that the selection of the alternative interest rate benchmark in the markets should depend on market participants' demands and therefore be decided by the markets themselves. Accordingly, the Secretariat would like to expect more efforts to be made by market participants themselves to further promote the use of TONA.

- A bank member asked if the Committee planned to publish a transition plan for derivatives in the future, similar to the one that the Committee had published for cash products. In response, the chair replied that there were no such plans so far and the Secretariat provided a supplementary explanation that the timing of developing systems and operations for O/N RFR Compounding (Fixing in Arrears) had been set at the end of March 2021 in the transition plan and that it could imply that the transition for derivatives should also be carried out around the end of March 2021.

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3. Finally, the chair noted that the final report on the results of the second public consultation would be published around the end of November 2020, and this was approved by the members.

#### IV. Adherence to the ISDA IBOR Fallbacks Protocol

1. The Secretariat explained the document on the recommendation for market participants concerning the adherence to the ISDA IBOR Fallbacks Protocol at an early stage.
2. Additionally, the Financial Services Agency (hereinafter the JFSA) made the following comments.
  - It would be desirable for many institutions to adhere to a related protocol and widely use fallback provisions to ensure a smooth transition from LIBOR given the limited time available before the end of 2021, when the permanent discontinuation of LIBOR was highly likely to take place.
  - However, adherence to the protocol would only be an application of fallback provisions. The JFSA would like to reemphasize that it was important to make an early transition to the alternative interest rate benchmark in advance, as it was the preferred response to the permanent discontinuation of LIBOR.
3. Finally, the chair noted that the document on the recommendation concerning the adherence to the protocol would be published after receiving approval from the Committee members, and this was approved by the members.

#### V. AOB

1. The Secretariat explained the "Practical Solution on the Treatment of Hedge Accounting for Financial Instruments that Reference LIBOR," which was published by the Accounting Standards Board of Japan (ASBJ) on September 29, 2020.
2. The vice-chair made several announcements about the Committee's commitment to external communication and its future policy.

## Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks

### Attendance for the November 5, 2020 Meeting

#### (Members)

Chair	MUFG Bank	GODA Kenichiro
Vice Chair	Nomura Securities	NONOMURA Shigeru
	Mizuho Bank	KOBAYAKAWA Motomu
	Sumitomo Mitsui Banking Corporation	ORIHARA Takashi
	Bank of Yokohama	ARAI Tomoki
	North Pacific Bank	TAKAHASHI Kazuhiro
	Deutsche Bank	MORITA Shigeki
	Daiwa Securities	INADA Yuichiro
	Goldman Sachs	TAGUCHI Kengo
	Morgan Stanley MUFG Securities	EZUKA Takeshi
	Japan Post Bank	ICHIKAWA Tatsuo
	The Norinchukin Bank	CHIBA Yuji
	Shinkin Central Bank	TANAKA Hiroyuki
	Nippon Life Insurance Company	OKAMOTO Shinichi
	Tokio Marine Holdings	NIKKAWA Shinya
	Daiwa Asset Management	KOMIYA Tsutomu
	Mitsubishi Corporation	OKAWARA Makoto
	Mitsui Fudosan	KANEKO Yutaka
	East Japan Railway Company	ISHIMARU Mikito
	Mitsubishi UFJ Lease & Finance	TOMINAGA Osamu
	Nippon Telegraph and Telephone Corporation	OTSUBO Yasufumi

#### (Observers)

JBA TIBOR Administration	KOYAMA Hirotake
International Swaps and Derivatives Association	MORITA Tomoko
Financial Law Board	TOTSUKA Takaharu (Attorney-at-Law)

Tokyo Financial Exchange	SEO Ryosuke
Japan Securities Clearing Corporation	KANEKO Takahiko
Japanese Bankers Association	TAKAHASHI Tetsuo
Japan Securities Dealers Association	MATSUNAGA Hideaki
Financial Services Agency	NOBUMORI Takehiro
Bank of Japan	INAMURA Yasunari
Bank of Japan	CHIBA Makoto

The chairs of the sub-groups and the coordinator of the working group attended the meeting.

Chair of the Sub-Group on Loans	Mizuho Bank	SHIBATA Noriyuki
Chair of the Sub-Group on Bonds	Nomura Securities	HASHIMOTO Shigeru
Chair of the Sub-Group for the Development of Term Reference Rates	MUFG Bank	AMAGI Yutaka
Chair of the Sub-Group for the Development of Term Reference Rates	Citigroup Global Markets Japan	WATANABE Atsuya
Coordinator of the Working Group on Currency Swaps	Sumitomo Mitsui Banking Corporation	ISHIKAWA Satoshi