U.S. COMMODITY FUTURES TRADING COMMISSION
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Mr. Konuma Yasuyuki
President and Chief Executive Officer
Japan Securities Clearing Corporation
2-1 Nihombashi-Kabuto-cho
Chuo-Ku
Tokyo 103-0026, Japan

Re: No-Action Letter with Regard to Sections 4d(f) and 4m(1) of the Commodity Exchange Act and Commission Regulation 39.6(b)(1)

Dear Mr. Yasuyuki:

This is in response to the Japan Securities Clearing Corporation ("JSCC") letter dated April 7, 2025, to the Division of Clearing and Risk and Market Participants Division ("Divisions") of the Commodity Futures Trading Commission ("Commission"). In the letter, you request that the Divisions confirm that they will not recommend that the Commission take enforcement action against (i) JSCC with respect to failure to satisfy the restrictions in Commission Regulation 39.6(b), or (ii) JSCC's clearing members that are not incorporated in the United States ("U.S.") with respect to futures commission merchant ("FCM") registration requirements in Commodity Exchange Act ("CEA") Section 4d(f)[1] and commodity trading advisor ("CTA") registration requirements in CEA Section 4m(1).[2]

The letter represents that JSCC is making the request to enable U.S. market participants to clear Japanese Yen ("JPY") denominated interest rate swaps ("IRS") through clearing members of JSCC that are not incorporated in the U.S nor registered with the Commission as FCMs.

Statement of Facts

Based on the representations made in the letter, we understand the relevant facts to be as follows:

JSCC was established as a joint-stock company under the Companies Act of Japan on July 1, 2002. JSCC is licensed to perform clearing services under Japan's Financial Instruments and Exchange Act and regulated by the Japanese Financial Services Authority.

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[1] 7 U.S.C. § 6d(f).

[2] 7 U.S.C. § 6m(1).

JSCC obtained from the Commission an exemption from registration as a derivatives clearing organization ("DCO") in 2015.[3] Under the conditions set forth in the exemption order and Commission Regulation 39.6(b)(1), JSCC, like other exempt DCOs, is limited to clearing swaps for only U.S. persons that are clearing members of JSCC or affiliates of JSCC clearing members ("proprietary swaps"). In other words, U.S. persons that are neither clearing members of JSCC nor affiliates of JSCC clearing members ("U.S. customers") are currently not permitted to clear at JSCC.

JSCC attempted to register with the Commission as a DCO in 2014, which would have allowed JSCC to clear for U.S. customers. However, JSCC was unable to do so due to a conflict between Section 4d(f) of the CEA, which requires a registered DCO to segregate FCM customer funds at all times from the DCO's own funds to ensure that the funds are protected under U.S. bankruptcy law, and Japanese law. Specifically, JSCC states that it holds all customer property in a trust account to ensure that the property is remote from any Japanese bankruptcy proceeding against JSCC. However, customer funds transferred by clearing members to or from JSCC are held for a short period of time (approximately one hour) in JSCC's account at the Bank of Japan in a commingled manner with JSCC's proprietary funds and other funds, which is inconsistent with the segregation requirements of Section 4d(f) of the Act.

In 2024, JSCC cleared approximately 55% of the global JPY-IRS market, as measured by the volume of traded notional.

<u>Discussion of Request for No-Action Position and Applicable Legal Requirements</u>

JSCC claims that the prohibition on U.S. customer clearing at JSCC forces U.S. customers to trade and clear JPY-IRS in markets with lower liquidity, creating increased risk and leading to more disadvantageous prices than those available to non-U.S. customers who can access the higher liquidity and competitive pricing at JSCC.

JSCC further claims that current market conditions are exacerbating the need for U.S. customers to hedge JPY interest rate risk. JSCC notes that, starting in 2016, the Bank of Japan ("BoJ") maintained a Yield Curve Control Policy ("YCC"), which had targeted a 0% yield for 10-year Japanese Government Bonds ("JGBs"), with a cap of 0.25%. Recently, the BoJ implemented the following amendments to the YCC:

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[3] Section 5b(h) of the CEA gives the Commission the authority to conditionally or unconditionally exempt a DCO from the registration requirement for the clearing of swaps if the Commission determines that the DCO is subject to comparable, comprehensive supervision and regulation by the appropriate government authorities in the home country of the DCO. 7 U.S.C. § 7a-1(h). The Commission originally issued an exemptive order to JSCC on October 26, 2015. The Commission issued an amended exemptive order on May 15, 2017, which expanded the scope of products that JSCC is permitted to clear as an exempt DCO, subject to several conditions set forth in the order. *See* In the Matter of the Petition of Japan Securities Clearing Corporation For Exemption from Registration as a Derivatives Clearing Organization, Amended Order of Exemption From Registration (May 15, 2017), available at https://www.cftc.gov/sites/default/files/idc/groups/public/@otherif/documents/ifdocs/jsccdcoexemptamdorder5-15-17.pdf.

- In December 2022, the YCC cap was amended to 0.5%. In response to this change, the 10-year JGBs immediately spiked to 0.5% (i.e., the new cap) from 0.25% (i.e., the previous cap).
- In July 2023, the YCC cap was amended to 1%.
- In October 2023, the YCC cap was further amended to allow 10-year JGB yields to exceed 1%.

In March 2024, the BoJ abolished the YCC and started targeting 0 ~ 0.1% for the overnight unsecured call rate. The BoJ further amended the targeted rate as follows:

- In July 2024, the targeted overnight unsecured call rate was raised to 0.25%.
- In January 2025, the targeted rate was further raised to 0.5%.

JSCC notes that, driven in part by these changes, increased volatility has been observed in the JPY interest rate markets, with market participants anticipating additional interest rate volatility to come. Given this anticipation, participants have been seeking to hedge this risk using JPY-IRS, thus making the hedging of JPY interest rate risk an urgent risk management matter for market participants.

With the above as background, JSCC is requesting a no-action letter that would enable U.S. customers to clear at JSCC. Among other needs, this would allow them to hedge their JPY interest rate risk in what has been an increasingly volatile and uncertain interest rate environment. JSCC states that this access would decrease the risks to U.S. customers, and ultimately the United States, by (1) providing access to the most liquid venue for clearing JPY-IRS and (2) eliminating the counterparty credit risk associated with alternative hedging products that are not cleared.

JSCC notes that U.S. customers clearing JPY-IRS must qualify as eligible contract participants,[4] which includes investment firms, life insurance companies and asset managers. Because these U.S. customers transact internationally, their ability to access available liquid markets and clearing solutions for interest rate swaps directly impacts their ability to manage and hedge risks across global markets, obtain reasonable returns on investments, and remain competitive with their non-U.S. peers. JSCC argues that recent global interest rate trends, including expectations for Japanese interest rates as described above, have further raised the priority for efficient risk management of interest rate risks.

JSCC is requesting that only JSCC clearing members affiliated with registered FCMs incorporated in the United States (which are in the same corporate group) be able to clear for U.S. customers under the no-action letter, arguing the overall impact of competition between non-U.S. clearing members of JSCC and the registered FCMs would be minimal. Rather, these corporate groups could efficiently use the capacity for customer clearing available in their non-U.S. affiliates, thus mitigating any capacity issues at their registered FCM entities while

[4] 7 U.S.C. §§ 1a(18) and 2(e).

providing their U.S. customers access to the liquidity of JPY-IRS at JSCC. Additionally, this approach would not lead to additional costs for the corporate group as their non-U.S. affiliates in Japan are already onboarded as JSCC clearing members.

With regard to customer protection, JSCC states that it holds all customer property in a trust account with the customers as beneficiaries to ensure that the customer property is remote from any Japanese bankruptcy proceeding against JSCC. JSCC further states that title to the customer property is transferred to JSCC to ensure that (i) the customer collateral is not subject to any claim from third-party creditors of a defaulted clearing broker clearing on behalf of customers, and (ii) the customer collateral could be used only to cover losses from a customer's own positions, as prescribed in JSCC's rulebook, in the case of a default of the customer's clearing broker.

JSCC also notes that it discloses the details of its own rulebook, as well as the bankruptcy regime in Japan on its website, including comparisons between them and the customer protections available under the U.S. regime.[5] JSCC believes that, by using this public information, as well as information provided by JSCC's clearing members, U.S. customers could readily assess JSCC's customer protection regime. JSCC notes that some major U.S. and non-U.S. asset managers have already onboarded their non-U.S. funds onto JSCC as customers. JSCC assumes that since professional asset managers would normally conduct their own due diligence on risk management and customer protections at DCOs prior to onboarding their funds, those U.S. asset managers must be satisfied with JSCC's customer protection regime.

JSCC notes in its request that Section 5b(h) of the CEA authorizes the Commission to "conditionally or unconditionally" exempt a DCO from registration, and JSCC acknowledges that the Commission has conditioned its exemption on JSCC not clearing swaps for U.S. customers, as also required by Commission Regulation 39.6(b)(1). JSCC indicates that it is separately requesting that the Commission amend its exemption order to remove this restriction. Accordingly, JSCC is requesting that the Division of Clearing and Risk take a no-action position, pursuant to Commission Regulation 140.99, with respect to Commission Regulation 39.6(b)(1).

In addition, JSCC states in its request that Section 4d(f) of the CEA would require a clearing member that clears swap transactions on behalf of U.S. customers to register with the Commission as an FCM. JSCC is requesting, on behalf of its clearing member firms that are incorporated outside of the U.S., that the Market Participants Division (MPD) take a no-action position, also pursuant to Commission Regulation 140.99, that it will not recommend enforcement action to the Commission if such clearing members clear JPY-IRS at JSCC on behalf of U.S. customers without registering as FCMs in violation of Section 4d(f) of the CEA.

JSCC further requests a no-action position from the commodity trading advisor ("CTA") registration requirements of Section 4m(1) of the CEA. A CTA is defined as any person who, for compensation or profit, engages in the business of advising others, either directly or through publications, writing, or electronic media, as to the value of or the advisability of trading

[5] *See* https://www.jpx.co.jp/jscc/otc/u89at30000007w62-att/bankruptcyprotections_20250106.pdf.

commodity interest.[6] JSCC states that its clearing members in soliciting and accepting orders from U.S. customers for JPY-IRS may provide advice regarding such transaction, which may trigger CTA registration requirements. JSCC notes that a CTA registration requirement would be a potential impediment or disincentive for clearing members to accept U.S. customers. Therefore, JSCC requests that MPD confirm that it will not recommend an enforcement action for failure to register as a CTA against a JSCC clearing member incorporated outside of the U.S. that provides trading advice to a U.S customer solely with respect to the clearing of JPY-IRS.

No-Action Position

Based on the facts presented and the representations JSCC has made, the Divisions will not recommend that the Commission take enforcement action against JSCC or its non-U.S. incorporated clearing members for failure to comply, as appropriate, with the FCM and CTA registration requirements of Sections 4d(f) and 4m(1) of the CEA and Commission Regulation 39.6(b)(1), subject to the following conditions:

1. JSCC clearing members may only solicit and accept orders for JPY-IRS from U.S. customers that are eligible contract participants as defined under Section 1a(18) of the CEA and Commission Regulation 1.3;

2. JSCC clearing members that solicit and accept orders from U.S. customers for JPY-IRS may not be registered with the Commission as FCMs nor incorporated in the United States;

3. JSCC clearing members that solicit and accept orders from U.S. customers for JPY-IRS must be affiliates of Commission-registered FCMs;

4. JSCC must adopt rules that require any clearing member seeking to clear for a U.S. customer to provide written notice to, and to obtain an acknowledgment from, the U.S. customer prior to clearing that explains that (i) the clearing member is not registered with the CFTC as an FCM, nor a member of the National Futures Association; (ii) JSCC is exempt from registration with the Commission as a DCO; (iii) in the event of the bankruptcy of JSCC or a JSCC clearing member holding U.S. customer property, the bankruptcy would be governed by the laws of a non-U.S. jurisdiction; and (iv) in the event of the bankruptcy of JSCC or a JSCC clearing member holding U.S. customer property, the protections of the U.S. Bankruptcy Code, as defined in CFTC Regulation 190.01, that are applicable to customers of a registered FCM and DCO do not apply to the U.S. customers, or to the funds and positions of the U.S. customers. The written notice must include an explicit comparison of the protections available to the U.S. customer positions and funds under the U.S. Bankruptcy Code and Part 190 of the Commission's regulations and JSCC's home country regulatory regime. JSCC's rules

[6] 7 U.S.C. 1a(12).

shall require the JSCC clearing member to retain the U.S. customer's acknowledgment of the receipt of the written notice in its records;

5. JSCC clearing members and JSCC must hold funds received from U.S. customers to margin, guarantee, or secure JPY-IRS, or funds accruing to U.S. customers as a result of JPY-IRS, in accordance with applicable Japanese laws, regulations, and JSCC rules; and

6. This no-action letter shall expire upon a determination by the Commission to either grant or deny JSCC and its clearing members an exemption, pursuant to Section 4(c) of the CEA, from Sections 4d(f) and 4m(1) of the CEA and related Commission regulations.

The position taken herein concerns enforcement action only and does not represent a legal conclusion with respect to the applicability of any provision of the CEA or the Commission's regulations. In addition, the Divisions' position does not necessarily reflect the views of the Commission or any other division or office of the Commission. Because this position is based on the representations contained in JSCC's request letter, any different, changed, or omitted material facts or circumstances may require a different conclusion or render this letter void. Finally, as with all no-action letters, the Divisions retain the authority to condition further, modify, suspend, terminate, or otherwise restrict the terms of this letter, in their discretion.

Sincerely,

Richard Haynes	Thomas J. Smith
Acting Director	Acting Director
Division of Clearing and Risk	Market Participants Division