Guidelines on Investment Restrictions on Derivative Transactions, etc.

Established on December 21, 2007
Revised on September 19, 2008
Revised on December 20, 2012
Revised on July 17, 2014
Revised on November 20, 2014
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1. Purpose

The purpose of these Guidelines is to state the basic principles of proper management and operation of a Member Management Company (meaning a Member that is an Investment Trust Management Company as defined in Article 2, Paragraph 11 of the Act on Investment Trusts and Investment Corporations (Act No. 198 of 1951); the same shall apply hereafter) so that such Member does not infringe on the investment restrictions on Derivative Transactions etc. (hereinafter referred to as the "Derivative Transactions") set forth in Article 130, Paragraph 1, Item 8 of the Cabinet Office Order on Financial Instruments Business (Act No. 52 of 2007; hereinafter referred to as the "Cabinet Office Ordinance") and Article 17 of the Rules on Management of Investment Trusts, etc.

2. Basic Principle and Treatment

With regard to the method of managing investment pertaining to Derivative Transactions, the Member Management Company shall provide for risk management method in the internal rules with reference to the risk management method set forth in "3.," and shall properly manage and perform such investment so as not to commit the prohibited acts set forth in the Cabinet Office Order.

It should be noted that the risk management methods described in the Guidelines are merely examples and do not preclude a Member Management Company from prescribing in its internal rules other risk management measures that such member deems appropriate.

3. Examples of Risk Management Methods

(1) In the event that investment is to be made only in real assets such as stocks and bonds and no investment instructions are to be given for Derivative Transactions, (including cases where investment instructions are not actually given for Derivative Transactions for the investment trust property for which Derivative Transactions are available for investment instructions), it is considered that no special management is necessary.

(2) Where investment instructions for Derivative Transactions are to be given solely for the purpose of hedging, any one of the following measures in (i) through (iii) can be selected and applied.

(3) Where investment instructions for Derivative Transactions are to be given for other purposes than for hedging (including the case of giving investment instructions for Derivative Transactions for both hedging purpose and non-hedging purpose in an investment trust), either of the following (ii) or (iii) may be selected for application.

(i) Simple method

Method of management that prevents the notional principal amount of the Derivative Transactions engaged from exceeding the total net asset value of the concerned investment trust property

(ii) Standard Method

Method of management that controls the risk amount under 80% of the total net asset value of the investment trust property. Such risk amount shall be derived from adopting the standard method for calculating the market risk equivalent among other methods of calculating the market risk equivalent according to the capital adequacy requirements for Financial Instruments Business Operators (according to Notification No. 59 of the Financial Services Agency, “Establishment of Standards for Calculating Market Risk Equivalent, Counterparty Risk Equivalent and Fundamental Risk Equivalent concerned with Financial Instruments Business Operators”).

(Note)

- Calculation method shall be applied for the entire portfolio, not limited to derivative products. (The same applies in (iii).)
- Market risk equivalent shall be calculated by multiplying the exposure value of individual investment target by ratio set forth in the “Establishment of Standards for Calculating Market Risk Equivalent, Counterparty Risk Equivalent and Fundamental Risk Equivalent concerned with Financial Instruments Business Operators.”
- For derivative products, calculation shall be made by basically converting to the position of the underlying assets and then multiplying such converted amount by the relevant ratio. In the event that the position of the derivative product equals the corresponding position of the underlying asset, such positions may be set off against each other.

(iii) VaR method

Method of management that keeps the risk amount under 80% of the total net asset value of the investment trust property. Such risk amount shall be derived from adopting the method for calculating the market risk equivalent under the internal control model (VaR method) among other methods of calculating the market risk equivalent according to the capital adequacy requirements for Financial Instruments Business Operators.

(Note)

- The holding period shall be 10 business days or more in principle. However, if mainly dealing with those with high liquidity such as listed futures instruments, the holding period may be five business days or more.
- It is essential for the Member Management Company to appropriately manage the situation at the time of stress. In this case, in addition to the calculation method of applying to the concerned portfolios the relevant historical data during the stress period after specifying such period of 12 months that should include the period of stress, it is also considered appropriate for each Member Management Company to prescribe proper management practices.

- It is essential for the Member Management Company to appropriately manage their risk by utilizing measures such as back-testing of their risk measurement model. In such a case, in addition to setting the multiplier at 3 to 4, they may select an appropriate multiplier.

4. Inclusion of investment restrictions on Derivative Transactions in the investment trust contract and disclosure of risk management measures

With regard to investment trusts for which the basic terms and conditions of the investment trust stipulate that Derivative Transactions may be made, the management method of Derivative Transactions as set forth in the Guidelines shall be included in the basic terms and conditions of the investment trust, and published on the website of the investment management company in accordance with the provisions of Article 38 of the Rules on Investment Reports, etc. Pertaining to Investment Trusts and Investment Corporations.

Supplementary Provision

The Guidelines shall come into effect on December 21, 2007.

Supplementary Provision

The amendments shall come into effect on October 1, 2008.

Supplementary Provision

The amendments shall come into effect on January 4, 2013.

Supplementary Provision

The amendments shall come into effect on December 1, 2014.

* The amended provisions are as follows:

(1) Revisions to the title and Articles 1 and 2 of the Guidelines.

(2) Revisions to (1) through (3) and establishment of (i), (ii), and (iii) concerned with Article 3.

(3) Establishment of Article 4.

Supplementary Provision

The amendments shall come into effect on December 1, 2014.

* The amended provisions are as follows:

Revisions to Articles 1 and 2

Supplementary Provision

The amendments shall come into effect on July 16, 2015.

* The amended provisions are as follows:

Revisions to Article 4.