

## Client Alert

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For more information,  
please contact:

**Stephanie Magnus**

+65 6434 2672

[stephanie.magnus@bakermckenzie.com](mailto:stephanie.magnus@bakermckenzie.com)

**Liew Ying Yi**

+65 6434 2288

[YingYi.Liew@bakermckenzie.com](mailto:YingYi.Liew@bakermckenzie.com)

## Amendments to Securities and Futures Act Passed: Bringing into effect final OTC derivatives regulations reform, accredited investors regime and enhanced enforcement regime for market misconduct

On 9 January 2017, the Securities and Futures (Amendment) Bill 2016 was read for the second time in Parliament and passed introducing wide ranging amendments to the Securities and Futures Act on four key areas:

- (i) Enhancing regulatory safeguards for retail investors including the introduction of an opt-in regime for accredited investors  
*(please click here to see our earlier alert on this);*
- (ii) Completing derivatives reform and enhancing the supervisory oversight of the Monetary Authority of Singapore ("MAS") of the over-the-counter ("OTC") derivatives markets operators and intermediaries  
*(please click here see our earlier alert on this);*
- (iii) Enhancing credibility and transparency of the capital markets including introducing a new regulatory framework for financial benchmarks and strengthening the disclosure requirements for the short selling of listed securities in line with other jurisdictions such as Australia, Europe and Hong Kong; and
- (iv) Strengthening the MAS' powers to take enforcement actions to address market misconduct and enhancing the civil penalty regime to among others, increase the maximum penalty to the greater of SGD 2 million, or three times the amount of benefits gained or losses avoided.

The effective date of the amendments have yet to be announced. The bill can be found [here](#).

Some key changes are:

Topic	Key Changes
<b>Regulatory Safeguards for retail investors</b>	<ul style="list-style-type: none"><li>• Accredited investors definition which includes individuals who have more than SGD2 million of net personal assets will be amended in the following ways:<ul style="list-style-type: none"><li>• The way net personal assets are calculated will be changed so that the net equity of an individual's primary residence can only contribute up to \$1 million of the \$2 million threshold.</li></ul></li></ul>



	<ul style="list-style-type: none"> <li>• Individuals can qualify as accredited investors if they have more than \$1 million of financial assets, net of any related liabilities.</li> <li>• An opt-in regime which will be introduced in subsidiary legislation (to be issued) such that even if an investor qualifies as an accredited investor, intermediaries cannot automatically treat him as such. The investor must be informed that he will forego the relevant regulator safe guards if he chooses not to opt-in and remain a retail investor. For intermediaries who are not permitted to deal with retail investors, e.g. licensed fund managers who are restricted to dealing with accredited and institutional investors may no longer be able to service such persons who opt-in to be treated as a retail investor.</li> <li>• The definition of institutional investor will be expanded to include financial institutions regulated by foreign regulators, foreign central government and sovereign wealth funds.</li> <li>• The definition of collective investment schemes ("CIS") (which must be authorised or recognised by the MAS for public offers to retail investors) will be widened and will no longer require investors' contributions and profits to be pooled for a scheme to be recognised as a CIS, so long as the scheme is managed as a whole.</li> <li>• Buy-back arrangements involving gold, silver and platinum which are in substance similar to collateralised borrowing arrangements will be classified as debentures and may attract prospectus registration requirements .</li> </ul>
<p><b><i>Regulating OTC derivatives</i></b></p>	<ul style="list-style-type: none"> <li>• No requirement for derivatives contracts meeting prescribed criteria to be traded on organised trading facilities or exchanges instead of over-the-counter, as yet while the MAS is empowered to impose this in the future.</li> <li>• Operators of organised trading facilities for OTC derivatives products will have to be authorised by MAS.</li> <li>• Intermediaries in OTC derivatives markets will be subject to regulation.</li> <li>• Commodity derivatives market operators and intermediaries will be transitioned to come under the MAS' supervision rather than IE Singapore.</li> </ul>
<p><b><i>Financial benchmarks regulation</i></b></p>	<ul style="list-style-type: none"> <li>• New regulatory framework for financial benchmarks introduced and MAS will be able to designate key financial benchmarks (this will include SIBOR and SOR).</li> <li>• Once designated, MAS will regulate those who administer</li> </ul>



	<p>the benchmarks as well as those who submit the information required to compute those benchmarks.</p> <ul style="list-style-type: none"><li>• Criminal sanctions and civil penalties will be introduced in relation to manipulation of financial benchmarks.</li></ul>
<b>Short-selling disclosure requirements</b>	<ul style="list-style-type: none"><li>• Disclosure requirements for the short selling of listed securities previously required under the trading rule of the Singapore Exchange and MAS guidelines will now be statutorily set out.</li><li>• Holding outstanding short positions above a prescribed threshold will need to be reported to the MAS.</li><li>• Information on aggregated short sell orders and short positions will be made available to the public.</li></ul>
<b>Market misconduct rules</b>	<ul style="list-style-type: none"><li>• The current prohibition against disclosure of statements that are false or misleading in a material aspect and are likely to have an effect on the market price of securities will be amended to apply regardless of price effect.</li><li>• There will also be a statutory definition of persons "who commonly invest" in relation to insider trading cases in reaction to case law. The MAS will also issue guidelines to further elaborate on interpretation of the statutory definition.</li></ul>
<b>Civil penalty</b>	<ul style="list-style-type: none"><li>• The civil penalty regime will be enhanced to standardise the maximum penalty that can be awarded in all civil penalty cases to the greater of (i) \$2 million, or (ii) 3 times the amount of benefits gained or losses avoided.</li><li>• The MAS' civil penalty claims will also have priority over private unsecured claims that accrue subsequent to a contravention of the Securities and Futures Act to strengthen the MAS' enforcement regime.</li></ul>

In tandem with these final legislative amendments for OTC derivatives reform, the MAS has also pushed ahead issuing guidelines on the margin requirements for non-centrally cleared OTC derivatives contracts, details below.



## Guidelines on Margin Requirements for Non-Centrally Cleared Derivatives effective from 1 March 2017

On 6 December 2016, the MAS issued guidelines on Margin Requirements for Non-Centrally Cleared Derivatives (the "Guidelines"), which will take effect on 1 March 2017. MAS initially proposed implementing the requirements in phases beginning 1 September 2016 when it issued the Consultation Paper on Margin Requirements for Non-Centrally Cleared Derivatives issued on 1 October 2015 ([see our earlier alert here](#)). However, it was announced in the MAS circular issued on 22 August 2016 that there would be a deferral of the 1 September 2016 date due to changes to the implementation schedules of other major markets. The recent issue of these Guidelines are in line with international efforts to meet the 1 March 2017 variation-margin rule deadline.

We outline in the table below some key provisions of the Guidelines. Please [click here](#) for the full Guidelines.

Guidelines	
<b>1.</b>	<p><b>Products Covered</b></p> <p>The exchange of margins applies to uncleared derivatives contracts booked in Singapore. It does not apply to the following uncleared derivatives contracts -</p> <ul style="list-style-type: none"><li>(a) A physically-settled foreign exchange (FX) forward or swap;</li><li>(b) A fixed physically settled FX transaction associated with the exchange of principal of a cross-currency swap;</li><li>(c) A commodity derivatives contract entered into for commercial purpose;</li><li>(d) An uncleared derivatives contract without a legally enforceable netting agreement; and</li><li>(e) An uncleared derivatives contract without a legally enforceable collateral arrangement.</li></ul> <p>To align with international standards, the MAS has expanded this scope of the exclusions, having previously proposed that these margin requirements apply to all OTC derivatives contracts not cleared on a qualifying central counterparty ("QCCP"), apart from physically settled FX forwards and swaps. Amendments to uncleared derivative contracts before the commencement of these margin requirements ("legacy trades") are excluded. However, new contracts resulting from portfolio compression of legacy trades are not.</p>



## Guidelines

### 2. Entities Covered

The Guidelines apply to MAS Covered Entities, at the moment this generally refers to licensed banks and merchant banks. The MAS will consult on phasing in the implementation of these Guidelines on investments funds and other non-bank FIs at a later stage.

An MAS Covered Entity should undertake the exchange of margins with a counterparty to an uncleared derivatives contract if that counterparty is an MAS Covered Entity or a Foreign Covered Entity. A Foreign Covered Entity is a person operating outside of Singapore who, if operating in Singapore, would have been a person within the meaning of MAS Covered Entity. There are exclusions to this, including where the uncleared derivative contract is entered into with a counterparty who falls within a list of prescribed persons, including the Government, statutory boards, central banks or central governments and certain multilateral organisations or where the entity belongs in the same consolidation group as the MAS Covered Entity.

#### Deemed Compliance

The MAS may deem that an MAS Covered Entity is in compliance with the Guidelines if the MAS Covered Entity is already subject to margin requirements in a foreign jurisdiction which the MAS has assessed to be comparable to the requirements in the Guidelines and the MAS Covered Entity can demonstrate that it has complied with the margin requirements of that foreign jurisdiction. Further, the MAS may still impose additional conditions to be met.

### 3. Exchange of Margins

An MAS Covered Entity should exchange IM on a gross basis. (i.e. no netting of IM payments between the two counterparties).

The following exclusions may be applied -

- (a) IM threshold of not more than \$80,000,000. This is applied at the level of the consolidation group and is based on uncleared derivatives contracts between the two consolidation groups of the MAS Covered Entity and its counterparty respectively;
- (b) De-minimis transfer amount of not more than \$800,000 for all margin (combination of IM and VM) transfers.



## Guidelines

### Timings:

- (a) Margin calls should be made at the earliest time possible after the transaction date ("T") or margin recalculation date ("R") but no later than the end of the next day after the transaction date or margin recalculation date;
- (b) Exchange of margins should take place no later than three local business days from the transaction date or from the day that margins have to be recalculated.

## 4. Margin Calculations and Methodologies

### For Initial Margins ("IM")

- (a) The amount of IM to be exchanged should be calculated by reference to either (i) a quantitative portfolio margin model; or (ii) a standardised margin schedule prescribed in the Guidelines. An MAS Covered Entity may opt for either approach, and is not restricted to one approach for the entirety of its derivative activities.
- (b) IM should be exchanged on a routine and consistent basis upon changes in measured potential future exposure. At a minimum, IM shall be recalculated and exchanged in each of the following circumstances: a new contract is executed with a counterparty; an existing contract with a counterparty terminates or expires; the IM model (if applicable) is recalibrated due to changes in market conditions; changes to the asset classification of existing trades (if they are computed under the standardised approach); or no IM recalculation has been performed in the last 10 local business days.

If the quantitative portfolio margin model is elected, additional requirements apply including among others, additional notification requirements to the MAS prior to adopting such model and upon any material changes to the model. The MAS may also stipulate further testing or improvements to the model.

### For Variation Margins ("VM")

- (a) VM should be posted or collected to fully collateralise the changes in the mark-to-market exposure of the uncleared derivatives contracts entered into by an MAS Covered Entity.
- (b) In the event that the exposures cannot be marked-to-market due to market conditions, an alternative process may be used.
- (c) VM should be calculated and collected on an aggregate net basis across all uncleared derivatives that are executed under a single, legally enforceable netting agreement.
- (d) If a margin dispute arises, the non-disputed amount should be



<b>Guidelines</b>	
	collected, while taking all necessary and appropriate efforts to resolve the dispute and collect the remaining VM amount in a timely fashion.
<b>5.</b>	<b>Eligible Collateral, Haircuts and Treatment of Collateral Eligible Collateral</b>  The Guidelines prescribe eligible collateral to meet IM and VM requirements, including among others, cash, gold, any equity security (including convertible bonds) included in a main stock index of a regulated exchange, debt securities (which satisfy certain prescribed conditions) and units in collective investment schemes (which satisfy certain prescribed conditions). However, an MAS Covered Entity should not include specific types of collateral as eligible collateral in cases where – <ul style="list-style-type: none"><li>(a) The MAS Covered Entity determines that it would not be able to liquidate such collateral in a timely manner in case of default of the posting counterparty; or</li><li>(b) The securities are issued by the MAS Covered Entity (or its related entities) or a counterparty (or its related entities).</li></ul> <b>Haircuts</b>  An MAS Covered Entity should – <ul style="list-style-type: none"><li>(a) Perform daily valuation of collateral exchanged to meet IM and VM requirements and apply haircuts to the value of the eligible collateral.</li><li>(b) Apply standardised schedule-based haircuts as prescribed in the Guidelines, based on the type of collateral posted or received, to the value of eligible collateral to meet margin requirements.</li><li>(c) Apply an additive currency mismatch haircut of 8% to all non-cash collateral that is posted or received in a currency other than the ones agreed in the relevant contract to meet VM requirements</li><li>(d) Apply an additive currency mismatch haircut of 8% to all cash and non-cash collateral that is posted or received in a currency other than the termination currency that the counterparty which has posted the collateral has designated in the relevant contract to meet IM requirements</li></ul> Additional requirements apply to require an MAS Covered Entity to manage risks associated with collateral exchanged to meet the IM and VM requirements as well as to ensure the safekeeping of IM.
<b>6.</b>	<b>Keeping of Books and Other Information</b>  An MAS Covered Entity should ensure that all relevant books,



## Guidelines

transaction information and related information are kept until at least five years after the last date of the expiry or termination of a contract, an agreement or a transaction to which the book or information relates.

## Implementation Schedule

The exchange of IM applies from each phase-in date where both the MAS Covered Entity and counterparty each belong to a consolidation group whose aggregate notional amount of uncleared derivative contracts exceeds the respective thresholds as set out below:

Obligation		Commencement Date
<b>Commencement of Exchange of Variation Margin (VM)</b>		1 Mar 2017
<b>Commencement of Exchange of Initial Margin (IM)</b>		
<b>Threshold</b>	S\$4.8 trillion	1 Mar 2017
	S\$3.6 trillion	1 Sept 2017
	S\$2.4 trillion	1 Sept 2018
	S\$1.2 trillion	1 Sept 2019
	S\$13 billion	From 1 Sept 2020 for each subsequent 12-month period

[www.bakermckenzie.com](http://www.bakermckenzie.com)

Baker McKenzie Wong & Leow  
8 Marina Boulevard  
#05-01 Marina Bay Financial Centre  
Tower 1  
Singapore 018981

Tel: +65 6338 1888  
Fax: +65 6337 5100

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