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05 April 2012

To
Capital Markets Department
Monetary Authority of Singapore
10 Shenton Way
MAS Building
Singapore 079117

Re: Consultation Paper P003-2012 Feb 2012 – Proposed Regulation of OTC Derivatives

Dear Sir/Madam,

CFA Institute¹ and CFA Singapore² (collectively “CFA”) are pleased to comment on the proposed regulatory regime for the over-the-counter derivatives (OTC) in Singapore. CFA Institute, through its members’ experience in international markets and different investment disciplines, represents the views of investment professionals before standard setters, regulatory authorities, and legislative bodies worldwide. CFA promotes fair, open, and transparent global capital markets, and advocates for investors’ protection.

CFA supports the Council’s efforts to improve the OTC Derivatives regime in Singapore. We believe the changes suggested by the Council will improve the regulatory regime and also improve investor confidence in the market. CFA Institute has also commented our members’ views on this topic to the Hong Kong Monetary Authority and European Monetary Authority in 2011.

¹ CFA Institute is a global, not-for-profit professional association of over 108,000 investment analysts, advisers, portfolio managers, and other investment professionals in 137 countries, of whom more than 99,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 135 member societies in 58 countries and territories.

² Established in September 1987, CFA Singapore (formerly known as the Singapore Society of Financial Analysts - SSFA) is a professional body that brings together practitioners of the investment and fund management industry in Singapore. Its objectives are to lead the investment profession in Asia by setting the highest standards of ethics, education, and professional excellence and be considered the thought leader in shaping ethical and professional standards and, in furtherance of that goal, frequently partners with a diverse range of stakeholders including employers, regulators, and investment professionals in Asia. With a membership base of more than 3,500, CFA Singapore runs programs for members, CFA candidates, and the investment community, including professional development talks and seminars, networking sessions, CFA Program information sessions and examination review classes, and career development talks.

EXECUTIVE SUMMARY

We appreciate the opportunity to comment on the proposals to introduce the legislative framework of reporting and clearing of over-the-counter (OTC) derivative contracts. These two elements have a significant impact on the microstructure of derivatives markets, which are currently dominated by dealer participation and bilateral trade execution.

Standardization of derivatives currently traded on OTC markets is a necessary step to facilitate greater market transparency through the use of exchanges and other organized, non-discretionary multilateral electronic trading venues. Transparency alleviates information asymmetry, enables price formation, underpins investor confidence and liquidity, and facilitates calculation and monitoring of risk exposures. These factors strengthen the functioning and resiliency of markets and thus benefit both investors and regulators. CFA is therefore supportive of reforms that introduce a reporting regime and a platform for centralized clearing of OTC derivatives.

In general, CFA Institute is supportive of the introduction of both a reporting regime and central clearing of OTC derivative markets in Singapore with an ultimate goal of greater use of exchange trading for such contracts. In a survey of CFA Institute members in October 2009, 68 percent of members agreed that all standardized and standardizable derivative contracts that currently trade over-the-counter should be required to trade on a regulated exchange. Likewise, 78 percent of members agreed that such contracts should have to clear centrally. Finally, 66 percent of members agreed that electronic reporting of over-the-counter trades would provide an appropriate level of transparency for all investors for those derivatives that continue to trade over the counter. The survey results are based on the responses of 755 CFA Institute members based in the United States. The results are available at http://www.cfainstitute.org/Survey/us_iwg_poll_report.pdf.

Accordingly, CFA supports complementary initiatives to strengthen post-trading infrastructure through central counterparty clearinghouses and trade repositories. We note, however, that such initiatives are not substitutes for on-exchange trading, which addresses the separate issues of trading transparency, liquidity, and price discovery. CFA Institute's other positions are that price transparency is one of the most important goals of financial markets, and that investors should have full access to relevant market information. Standardization and exchange trading further these goals.

COMMENTS ON SPECIFIC PROPOSALS**Question 1: MAS seeks views on the proposal to expand the scope of SFA to cover derivative contracts on commodities, credit, equities, foreign exchange and interest rates.**

As described in the question above, the proposal identifies the classes of underlying assets covered under “derivative contracts.” The class of assets is logical and easy to understand but does not carve out the exact scope of “derivative contracts.”

The proposed scope will necessarily form the basis for a robust and practical derivatives regulatory regime and hence should have greater clarity and leave little room for ambiguity.

Question 2: MAS seeks views on:

- (i) The proposal to adopt top-down and bottom-up approaches to identify products suitable for mandatory central clearing;**
- (ii) The proposed criteria (paragraph 3.1.4) for determining whether a product is suitable for mandatory central clearing by a CCP;**
- (iii) The feasibility of mandating central clearing for SGD IRS, USD IRS, NDFs in selected Asian currencies.**

CFA supports the proposal and believes it is both prudent and operationally feasible. We also believe it will enhance market transparency about such instruments while increasing oversight of potential systemic risks for those instruments that will be cleared centrally. Furthermore, the proposal is consistent with what has been proposed by U.S. Commodity Futures and Trading Commission (“CFTC”) and what is being adopted internationally in the U.S., EU and Hong Kong. It promotes prudent reform of the OTC derivatives markets in Singapore.

However, some of our members who are practitioners in Singapore are concerned that the approach used does not impact the current price-discovery process. Products that have a very limited number of participants or where the liquidity and activity are generally low could be centrally cleared but given the relatively small size of their market, the cost of clearing may outweigh the benefits to users. Moreover, limited liquidity and activity may make it difficult to accurately price such instruments, thus increasing the potential risk for the central clearinghouse. Hence testing the market first with NDF and IRS would be ideal; given the scale the activity of IRS and NDF appear to be systematically more important to Singapore Derivatives market.

Question: 3: MAS seeks views on the proposal to exempt foreign exchange forwards and swaps from mandatory central clearing.

MAS proposes to exempt foreign exchange forwards and swaps from the clearing obligation. Other foreign exchange derivatives such as currency options, non-deliverable forwards (NDFs) and currency swaps are not exempted from mandatory central clearing. MAS has identified SGD interest rate swaps (“IRS”), USD IRS and non-deliverable forwards (“NDFs”) denominated in selected Asian currencies as products that are eligible for central clearing.

CFA supports the phased approach of extending the mandatory clearing obligations of instruments. However, we are in favor of a mandatory central clearing regime for all standardized and standardizable derivatives (including foreign exchange forwards and swaps) ultimately in a cost effective manner to ensure an appropriate level of transparency to investors, to minimize risk and to address the issues of liquidity and price discovery. In order to ensure a central counterparty (CCP) does not face excessive risks clearing OTC derivatives, the derivative product or the underlying instrument that is subject to central clearing must be liquid, the exposure must be closed out in a timely manner and the derivative product must be accurately priced and margined. It is advisable, therefore, to take a phased approach to ensure that there is sufficient liquidity and a high level of integrity.

Question: 4 MAS seeks views on the proposal to require transactions which fulfill the criteria stated in para 3.2.1 to 3.2.2 to be subject to clearing obligation.

The proposal would require a product to centrally clear under two scenarios. First, it would have to centrally clear if it is mandated to do so. Second, it would centrally clear if at least one leg of the contract is booked in Singapore and either a) both parties are resident or have a presence in Singapore and are subject to the clearing mandate, or b) one counterparty is resident or present in Singapore and the other would have been subject to the clearing mandate if it had been a resident or present in Singapore.

CFA supports introducing a CCP for central clearing of OTC derivative contracts in Singapore together with more exchange trading for such derivatives.

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However, some of our members do anticipate interpretation and implementation issues relating to issues that revolve around foreign laws, transparency of transactions, insolvency protection of clearing parties and the political aspects of currency restrictions. In particular, such rules may create legal conflicts for counterparties that may be legally required under other laws to clear centrally within their jurisdictions. Indeed, such conflicts are a significant concern for dealers and end-users throughout the world, as conflicts in law will make it difficult for counterparties to comply in every case.

Consequently, we first suggest that Singapore work and coordinate these rules with regulators in other jurisdictions to make sure that if such conflicts, there is a standard and binding manner in which such conflicts are addressed. Secondly, we reiterate the suggestion made elsewhere in this response about the need to use a phased approach to implementation to permit authorities to monitor the effects of implementation and, where needed, to adjust rules to prevent widespread problems from unintended consequences.

QUESTION5: MAS seeks views on the proposed scope of entities to be subject to clearing obligations and on the factors to be taken into account when determining the clearing thresholds.

Under the proposal, MAS would include all financial entities regulated by MAS that exceed the relevant thresholds (to be determined by MAS) for central clearing, taking into account the size of the entity's derivatives exposure in aggregate and by product class. It also would include non-financial entities (NFEs)—firms not regulated by MAS but are resident or present in Singapore—under similar conditions, with an exception for derivatives used to enable customized hedging of risks.

CFA believes that all standardized and standardizable OTC contracts should be subject to central clearing and that any exemptions should be strictly limited. We believe that only transactions where an NFE specifically hedges a legitimate, identifiable commercial risk should be exempt. For example, an NFE that uses a bespoke contract transacted bilaterally with a bank should be exempted from the central-clearing requirement because such a contract would be ill-suited to central clearing due to difficulty of accurately margining the contract. Even in this example, however, we believe the trade should be centrally cleared if it is of a size significant to create hardships for the CCP or other counterparty should the firm fail to live up to its

obligations. Of equal importance, we believe even such bespoke contracts should be reported to the markets for transparency purposes.

QUESTION 6: MAS seeks views on the proposal to exempt certain public bodies from the clearing obligation.

The proposal would exempt central banks, central governments and supra-national organizations—such as the Bank for International Settlements, the International Monetary Fund, the World Bank and other multilateral development banks—from the central clearing requirement. The reasoning given is that requiring clearing for these entities would unnecessarily constrain these public bodies from performing their roles effectively. CFA recommends that a clearer definition of public bodies is required. Likewise, issues related to capital charges need clarification. We recommend that with a clear definition exempting public bodies from clearing is acceptable but there should be no exception to reporting requirements.

QUESTION 7: MAS seeks views on:

- (i) The proposal to exempt intra-group trades of both financial and non-financial entities from the clearing obligation but subject these trades to appropriate collateralization requirements;**
- (ii) Whether such a proposal would pose any implementation issues; and**
- (iii) Whether there are other appropriate risk mitigating measures apart from subjecting the exempt intra-group trades to collateralization requirements.**

Transactions conducted among affiliated companies within the same corporate group to achieve efficient and effective enterprise-wide risk management would be termed intra-group transactions under the proposal.

CFA's primary concern is that such transactions are transparent to investors and that the dealers involved in such transactions are sufficiently capitalized and regulated to avoid significant financial disruptions. With these goals in mind, we support the proposal regarding intra-group activities, but would request and suggest that the proposal include reporting requirements as a necessary part of all such transactions.

QUESTION 8: MAS seeks view on the proposal not to exclude pension schemes from clearing requirements.

CFA supports the proposal not to exclude pension schemes from clearing requirements for a couple of reasons. First, we believe that exempting such entities from these requirements creates unfair advantages that will eventually lead to distortions in the market. Second, the size of such entities and their potential effect on market performance means that failure could have severe repercussions for other market participants and for the markets themselves. Finally, the magnitude of such entities, both on an individual basis and collectively, means that these entities significantly affect market activities.

Question 9: MAS seeks views on the proposal not to require central clearing through only domestic CCPs.

Being a central infrastructure, CCPs play a critical role in financial markets. Their central position makes them important to overall efficiency of the market. We believe that CCPs should be subject to adequate regulation, supervision and, as part of these efforts, sufficient capitalization. The regulatory approach towards CCPs should be consistent across jurisdictions so as to reduce the potential for CCPs competing on the basis of lower costs or reduced requirements.

CFA is aware of research³ that suggests that attempting to specialize in clearing on the basis of products or regions will not provide the needed level of diversification to effectively manage the risks concentrated in a CCP. On the basis of this research, we would be concerned about a regionalized approach to central clearing, and would prefer a system that recognizes and utilizes appropriately regulated and capitalized CCPs, regardless of their domiciles. At the same time, we believe it is imperative that regulators work together regarding such activities. We also believe it is imperative that such transactions be fully transparent to all market participants.

Based on this perspective, we believe the MAS's approach to this issue is appropriate.

³ See “Does a Central Clearing Counterparty Reduce Counterparty Risk?,” by Darrell Duffie and Haoxiang Zhu (2010). <http://www.stanford.edu/~duffie/DuffieZhu.pdf>

QUESTION 10: MAS seeks views on:

- (i) The proposal to require backloading of outstanding derivative contracts with remaining maturity of more than one year and**
- (ii) Any potential implementation challenges in requiring back loading of outstanding derivative contracts.**

CFA agrees with this proposal as it is in line with what is being adopted internationally and it promotes prudent reform of and greater transparency for the OTC derivatives markets in Singapore.

However, some of our members highlighted the practical difficulties and the cost involved to backload all outstanding contracts and hence would suggest including contracts with at least three years to maturity instead of all outstanding derivative contracts with remaining maturity of more than one year.

QUESTION 11: MAS seeks views on the proposal to implement the reporting obligation in phases, specifically on the proposal to include interest rate, foreign exchange and oil derivative contracts in the first phase.

CFA understands and supports the phased approach of extending the mandatory reporting of these instruments. CFA Institute has consistently called for a central data repository to enhance market transparency in general. However, it is imperative that investors should have full access to relevant market information.

A uniform market data collection facility that stores all relevant trading data would provide a standardized format for data collection and distribution and would eliminate the need for legal structures directing cooperation among regulators. Such a repository would therefore make collection, submission, and review of relevant market data easier for regulators and investors from disparate markets.

QUESTION: 12 MAS seeks views on the proposal to require all transactions booked or traded in Singapore to be reported.

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In general, CFA supports this proposal as one means of ensuring that all transactions originating or occurring in Singapore are reporting to the market. CFA advocates price transparency as one of the most important goals of financial markets and that investors and regulators should have access to relevant market information. Trade Repositories can help achieve these goals.

At the same time, CFA is concerned about the potential for double-counting of trades on a regional or global basis. We have consistently called for a central data repository to enhance market transparency in general. Trade Repositories enable regulators to assimilate an aggregate view of OTC derivative contract exposures and are therefore an important tool to facilitate monitoring of aggregate market developments. If there are multiple Trade Repositories per asset class within a jurisdiction, regulators should be provided with sufficient means to consolidate the information contained within the TRs, so that their ability to monitor aggregate exposures is not obfuscated by a fragmentation of data across multiple TRs for a given class of financial instrument.

To avoid such conflicts, we recommend more consultation and coordination with other regulators on this matter to determine feasibility and practical issues with this proposal.

Question13: MAS seeks views on:

- (i) The proposal to require reporting by all financial entities, as well as non-financial entities above a reporting threshold and**
- (ii) The proposal to determine the reporting threshold based on the asset size of the non-financial entity**

CFA upholds that price transparency is one of the most important goals of financial markets and regulation of OTC derivatives markets globally, as investors need access to relevant market information to make informed decisions. Trade Repositories that convey such information can help achieve these goals.

CFA Institute has consistently called for a central data repository to enhance market transparency in general. TRs and CCPs act as complementary post-trading infrastructure initiatives that would improve transparency and minimize risk, respectively.

The reporting proposal is aligned with the centralized clearing proposal. However, it is important to ensure that the reporting threshold for NFEs be meaningful, taking into account

the market structure for the particular class of derivatives and the regulatory need to measure, monitor and mitigate operational and credit risk. We recommend considering transaction size in addition to the asset size of the non-financial entity to determine the reporting thresholds.

Question 14: MAS seeks views on the proposed protocols for single-sided reporting and the use of third-party service providers to fulfill reporting obligations.

MAS' protocol is to allow single-sided reporting (reporting by one party only), including the use of a third party (e.g. CCP) to report on their behalf, as long as the original counterparties retain responsibility for the timeliness and accuracy of the information reported.

As noted in response to Question 7, the United States is considering exempting intra-group and foreign-entity trading from relevant parts of Dodd-Frank, but only if the U.S.-based dealer to the transaction takes responsibility for reporting the transaction to the trade repository. CFA believes that a similar requirement from the MAS would add clarity to the reporting responsibilities of the involved counterparties, thus avoiding the ambiguities that have created problems in other markets.

Question 15: MAS seeks views on the proposal to exempt certain public bodies from the reporting obligation.

As noted in response to Question 6, CFA recommends that a clearer definition of public bodies is required. We recommend that exempting public bodies from clearing is acceptable but there should be no exception to reporting requirements.

Question 16: MAS seeks views on the proposal to adopt international data reporting and aggregation standards recommended by CPSS-IOSCO, including the requirement for parties to derivative contracts to provide information updates to the TR to ensure that the TR data on the transaction remains accurate through the life of the transaction.

We support this initiative.

Question 17: MAS seeks views on the adoption of a legal entity identifier (“LEI”) and a product classification system aligned with international standards.

We support this proposal as it will make it easier for investors and regulators to track, monitor and analyse market trends, problems and risks. Even if the individual firms are not listed through the LEI, the product classification system also should make it easier for investors to comprehend what is happening in the market.

Question 18: MAS seeks views on the proposal to require reporting of contracts (and any updates) within one business day of the transaction.

We support this initiative, though we propose one to two business days to report, “depending on system capabilities”.

Question 19: MAS seeks views on the proposal to backload relevant pre-existing derivative contracts with remaining maturity of more than one year.

Please see our response to Question 10 above.

Question 20: MAS seeks views on the proposal not to require reporting to domestic TRs only.

We support this proposal for the same reasons identified in our response to Question 12 above.

Question 21: MAS seeks views on the proposal not to impose a trading mandate at this stage.

We understand there is a need to let the market and market systems prepare themselves before imposing a trading mandate. But the transition period should be short and exemptions should be kept to a minimum.

Question 22: MAS seeks comments on the benefits of introducing a trading mandate, taking into consideration the characteristics of the derivative markets in Singapore, and alternatives to a trading mandate, in moving derivative contracts to be traded on organized platforms.

Our survey from summer 2009 indicated that while members support exchange trading and central clearing, that at the very least, trading in these instruments should be reported to the market at large.

Concluding Comments

CFA Institute and CFA Singapore are pleased to submit our views on these proposed revisions to the OTC Derivatives regulatory regime in Singapore. If you or your staff have questions or seek clarification of our views, please feel free to contact James Allen, CFA, at 1.434.951.5558 or james.allen@cfainstitute.org; Tony Tan, CFA, at 65.9455.7295 or secretariat@cfasingapore.org; or Padma Venkat, CFA at 852.3103.9307 or padma.venkat@cfainstitute.org.

Sincerely,

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