ISDA Safe, Efficient Markets

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Dear Sirs,

Capital Markets and Services (Amendment) Bill 2011

We understand that the Capital Markets and Services (Amendment) Bill 2011 (the "**Bill**") has been gazetted on September 15 but has yet to come into force. Our members have a number of concerns with the Bill and we would like to bring this to your attention.

1. Extension of "*regulated activities*" to "*dealing in OTC derivatives*"

1.1 Prior to the Bill, the activities that have been regulated by the Capital Markets and Services Act 2007 ("**CMSA**") included "*dealing in securities*" and "*trading in futures contracts*". The Bill extends the regulated activities to "*dealing in derivatives*" by effectively replacing "*trading in futures contracts*" with "*dealing in derivatives*" and defining "*derivatives*" to include over-the-counter ("**OTC**") derivatives (other than those solely derived from, referenced to or based on exchange rates, or those to which Bank Negara Malaysia ("**BNM**") or the Government of Malaysia is a party). However, for the purpose of mandatory trade reporting under Section 107J, OTC derivatives includes derivatives derived from, referenced to or based on exchange rates. We presume that appropriate amendments will be made to Part 2 of Schedule 2 to introduce a definition of "*dealing in derivatives*".

1.2 Unlike the securities market where retail investors not only form a significant group of market participants but are often the target market of a securities offer, trading in OTC derivatives occurs almost exclusively among counterparties that would be considered "*wholesale*". In addition, one party to an OTC derivative would almost invariably be a financial institution that is licensed and regulated by BNM. Unlike futures contracts which are standardized contracts specified by the relevant exchange and where parties assume exposure not to each other but to the clearing house of such exchange, OTC derivatives are customized, bilaterally negotiated contracts between the parties where

each assumes exposure to the other (but usually, the parties enter into bilateral margining arrangements to collateralize or secure their exposures to each other). A fundamental tenet is that parties to an OTC derivative transact on a principal-to-principal basis and at arm's length. OTC derivatives markets also tend to be global in nature, that is, cross-border transactions between parties in two different countries are common.

1.3 The global market standard documentation used for OTC derivatives is the ISDA Master Agreement and ISDA Credit Support Documents, together with the relevant ISDA Definitions and Confirmations. The keystone of the ISDA documentation is close-out netting – the ability to terminate all outstanding transactions and to net the positive and negative replacement costs of the outstanding transactions in the event of a counterparty's default. Where close-out netting is legally enforceable, a non-defaulting party is entitled to reckon its credit exposure to its counterparty as the net close-out amount and will thus have a lower counterparty credit exposure. For non-defaulting parties that are financial institutions subject to regulatory capital requirements, close-out netting enforceability means that it needs to set aside a lower amount of capital since its counterparty credit exposure will be reduced as a result of the netting of the positive and negative replacement costs.

1.4 In addition, all non-defaulting parties need to be able to re-hedge or manage their risks promptly and with certainty. Where the non-defaulting party is a corporate end-user, the transaction will usually be to hedge one or more specific underlying risk(s). Where the non-defaulting party is a financial institution, it will still need to manage its risks on a portfolio basis. If the non-defaulting party's ability to close-out net is constrained in any manner, it will be faced with a choice between Scylla and Charybdis. If it were to re-hedge before it can close-out the transactions with the defaulting party, it runs the risk that it ends up being over-hedged if it is forced to continue with such transactions with the defaulting party. Even if it is ultimately allowed to terminate the transactions with the defaulting party, it runs the risk that the price at which it has re-hedged may be higher than the price at the point when it can close-out the transactions with the defaulting party and it would not be entitled to claim the difference in price from the defaulting party. If it decides not to re-hedge until it can close-out its transactions with the defaulting party, it may find that the cost of re-hedging at that point will be prohibitive (and the right to claim this cost from the defaulting party is of cold comfort where the defaulting party is in bankruptcy proceedings).

1.5 The importance to systemic stability of respecting the sanctity of close-out netting rights is globally accepted and many countries have created an explicit statutory safe harbour for close-out netting rights. The *Report and Recommendations of the Cross-border Bank Resolution Group* of the Basel Committee on Banking Supervision of March 2010 and the Financial Stability Board's Consultative Document on *Effective Resolution of Systemically Important Financial Institutions* of July 19, 2011 continue to recognize the importance of close-out netting.

1.6 Given the very different nature of the market-place for securities, futures contracts and OTC derivatives, a regulatory regime that may be appropriate for securities and futures contracts would not be appropriate for OTC derivatives.

2. Blanket exemption where one party to the OTC derivative is an institution licensed by BNM

2.1 Schedule 4 needs to be appropriately amended so that institutions licensed by BNM are deemed to be registered persons in respect of any dealing in OTC derivatives and would therefore not be required to hold a Capital Markets Services Licence under Section 58(1) of the CMSA.

2.2 Further, given that BNM has issued extensive guidance to its licensees in this regard (e.g., BNM's Guidelines on Introduction of New Products, BNM's Minimum Standards on Risk Management Practices for Derivatives and BNM's Guidelines on Product Transparency and Disclosure), our members submit that BNM licensed institutions and their employees should be totally exempt from all provisions of the CMSA (including the Guidelines on Investor Protection by the Securities Commission ("**SC**") and SC's "*fit and proper*" requirements for employees of the registered persons) in respect of any dealing in OTC derivatives. This will avoid the need for BNM licensed institutions and their employees to comply with two different sets of regulatory requirements, which at best will require them to incur extra cost and expend additional time, and at worst, may require them to comply with conflicting and inconsistent requirements.

2.3 At a minimum, as the prescribed business of commercial banks and investment/merchant banks under BNM's Guidelines on Introduction of New Products include "*transacting in any form of derivatives subject to compliance with [BNM]'s guidelines*" commercial and investment/merchant banks and their employees should be completely exempted from the licensing and other requirements under the CMSA. As for other BNM licensed institutions and their employees, complete exemption should at least apply to any dealing in OTC derivatives that are derived from, referenced to or based on any, or any combination, of exchange rates, interest rates, bonds or loans or other debt securities, credit ratings, or any index involving any of the foregoing. The rationale for this is that these asset classes are traditionally within the purview of the central bank.

3. Blanket exemption for dealings between exempt persons or in exempt transactions

3.1 Our members understand that the key concern of the SC is to protect retail investors. Thus, for the same reasons as offers and invitations are excluded under Section 229 of the CMSA, our members submit that there should be complete exemption from the licensing and other requirements under the CMSA where the OTC derivative is between two exempt persons or is an exempt transaction. Without such an exemption, corporate treasuries that engage in OTC derivatives to hedge or manage their underlying business exposures may potentially be deemed to be "*dealing in derivatives*" and become subject to the licensing and other requirements under the CMSA.

3.2 As for the definitions of "*exempt person*" and "*exempt transaction*", our members are of the view that Schedule 6 to the CMSA would be the right starting point. We note from the SC's Public Response No. 1/2011 on the *Review of Sophisticated Investors and Sales*

Practices for Unlisted Capital Markets Products that the SC proposes to revise the categorisation of investors. While our members agree with this revision, they believe that it would be appropriate to have a ticket size exemption in the case of OTC derivatives. Australia, for example, exempts OTC derivative transactions with a notional amount of AUD500,000. We believe that it may be instructive for the SC to consider the exemptions for OTC derivatives provided in the Australian regime as well as the proposed exemptions in New Zealand which has recently released its draft Financial Markets Conduct Bill. In addition, our members propose that an additional exemption for transactions entered into for hedging or risk management purposes be introduced. We would be pleased to provide a draft defining "*exempt persons*" and "*exempt transactions*" if this may be of help to the SC.

4. OTC derivatives between an onshore party and an offshore party

4.1 We understand that there is a significant amount of non-MYR OTC derivatives transacted on a cross-border basis. These cross-border transactions fall into two broad categories:

(a) Although it has a Malaysian banking subsidiary, a bank may choose to book a trade with a Malaysian counterparty in an offshore office (e.g., for centralized risk management purposes, banks may book transactions of a particular type, say USD interest rate swaps, in one location) instead of in the Malaysian subsidiary. Alternatively, although the Malaysian subsidiary faces the Malaysian party, the Malaysian subsidiary will enter into a back-to-back trade with its offshore office in order to pass the risk onto the offshore office.

(b) Malaysian counterparties (especially Malaysian banks) may choose to trade with an offshore party that has no presence in Malaysia as the offshore party can put together a transaction that no onshore party can provide and/or as the offshore party quotes a better price and terms.

In the case of (a), the staff of the Malaysian subsidiary will likely be involved in the discussions with the Malaysian counterparty. In the case of (b), the offshore party may in the course of negotiating these transactions visit Malaysia to discuss the transaction with the Malaysian counterparty.

4.2 As a person who carries on, or holds himself out as carrying on, the business of dealing in derivatives will now be required to hold a Capital Markets Services Licence under Section 58 of the CMSA, these cross-border transactions will be affected. Offshore parties will need to seek legal counsel's advice on the nature and scope of activities that they can conduct without being deemed to be carrying on, or holding themselves out as carrying on, the business of dealing in derivatives in Malaysia. However, as there is no clear bright line test on the nature and scope of activities that can be conducted before one is deemed to be carrying on, or holding oneself out as carrying on, the business of dealing in derivatives in Malaysia, legal counsel's advice is unlikely to provide any definitive clarity. This will lead to at least some offshore parties withdrawing from dealing with Malaysian parties, resulting in a reduction in market liquidity and higher

prices in the OTC derivatives market in Malaysia or indeed, in a particular OTC derivative type becoming unavailable altogether to Malaysian parties.

4.3 To avoid these harmful consequences to the Malaysian OTC derivatives market, a clear bright line test should be introduced in the form of complete exemption from the licensing and other requirements under the CMSA for offshore parties that deal with exempt persons or in exempt transactions.

5. Specific provisions

Our members would like to seek clarification of a number of provisions. Further, without prejudice to our above submissions for exemptions, our members are of the view that it would not be appropriate for certain CMSA provisions to apply to OTC derivatives:

(a) **Section 2 *Definitions of "derivatives" and "securities***: "*Derivatives*" is defined to exclude "*securities*". "*Securities*" is defined to include "*any right, option or interest*" in respect of inter alia shares, bonds and debentures issued by any government or body corporate or unincorporated body, and to exclude "*futures contracts*". The Bill does not provide for the reference to "*futures contracts*" in the definition of "*securities*" to be changed to "*derivatives*". Some OTC derivatives may create a right, option or interest in respect of shares, bonds and debentures, e.g., a credit default swap or a bond forward or an equity swap. Prior to the Bill, where the person engaging in such OTC derivatives is deemed to be carrying on the business of "*dealing in securities*" in Malaysia, such person would have been required to obtain a Capital Markets Services Licence (unless exempted, e.g. as a registered person) and to comply with the relevant provisions of the CMSA. Given that the Bill proposes to include "*dealing in derivatives*" as a new class of regulated activity, our members believe that OTC derivatives that create a right, option or interest in securities should more properly be regulated as "*dealing in derivatives*" instead of as "*dealing in securities*". However, the current definitions of "*securities*" and "*derivatives*" would seem to lead to the opposite result with dealings in such OTC derivatives being treated as "*dealing in securities*" and not "*dealing in derivatives*".

(b) **Section 2 *Definitions of "approved clearing house", "derivatives exchange", "derivatives market" and "standardized derivatives"*; Section 7 *Establishment of stock markets or derivatives markets* and Section 105 *Trading in standardized derivatives outside Malaysia***:

(i) Section 2 provides inter alia as follows:
"*approved clearing house*" means a clearing house that has been approved under section 38.
"*derivatives exchange*" means any body corporate in relation to which an approval under subsection 8(2) is in force.
"*derivatives market*" means a market or other place at which, or a facility by means of which, derivatives are regularly traded.

"*standardized derivatives*" means a derivative, including a futures contract, that is traded on a derivatives exchange, whose intrinsic characteristics is determined by the derivatives exchange and whose trade is cleared and settled by an approved clearing house.

(ii) Section 7(2) prohibits a person from establishing, operating or maintaining, or assisting in establishing, operating or maintaining, or holding himself out as providing, operating or maintaining, a derivatives market that is not a derivatives market of a derivatives exchange, a derivatives market of an exchange holding company that is itself approved as a derivatives exchange, an exempt derivatives market or a registered electronic facility under subsection 34(1). Given the broad definition of "*derivatives market*" that includes a "*market … at which derivatives are regularly traded*", any participant in the OTC derivatives market is potentially caught by the prohibition in Section 7(2). Our members assume that this is not the intention and would seek confirmation to this effect.

(iii) Given the mandatory requirement in the US for cleared OTC swaps to be executed on a swap execution facility and the anticipated analogous requirement in the EU for cleared OTC derivatives to be executed on an organized trading facility, it is likely that more and more OTC derivatives will, going forward, be executed on a facility. Where there is a Malaysian party to an OTC derivative executed on such a facility, this will be potentially caught by the definition of "*derivatives market*" as a "*facility by means of which derivatives are regularly traded*". As the "*wholesale*" nature of participants in the OTC derivatives market will not change despite the execution of the transactions on a swap execution facility/organized trading facility, our members submit that it would be appropriate to exempt such facilities as exempt derivatives market pursuant to Section 7(3)(a). We would also point out that the definition of "*exempt futures market*" in Section 2 needs to be amended by substituting "*derivatives*" for "*futures*" where it appears.

(iv) Section 105 prohibits a holder of a Capital Markets Services Licence carrying on the business of dealing in derivatives or fund management in relation to derivatives from trading standardized derivatives on a derivatives market outside Malaysia unless the derivatives market is a derivatives market of a Specified Exchange, or the standardized derivative is of an approved class of standardized derivatives. A "*Specified Exchange*" is defined as "*such derivatives market as may be provided in the rules of the derivatives exchange as a Specified Exchange*" and an "*approved class of standardized derivatives*" as "*such class of standardized derivatives of the derivatives market of a Specified Exchange as provided in the rules of the derivatives exchange as an approved class of standardized derivatives*". We understand that Bursa Malaysia has currently approved the list set out in the Annex as Specified Exchanges

and approved classes of [futures contracts] and assume that the intention is for this list to continue to apply. However, given that the definition of "*standardized derivatives*" requires such derivative to be traded on a derivatives exchange and for that trade to be cleared and settled by an approved clearing house, a standardized derivative by definition must be traded on a Malaysian derivatives exchange and cleared through a Malaysian clearing house. It is thus not possible for a standardized derivative to be traded in a derivatives market outside Malaysia in the first place.

(c) **Section 91** ***Disclosure of certain interests in securities***: Section 91 refers to making recommendations in relation to securities or classes of securities and (unlike Section 92) has no express reference to futures contracts. Please confirm that Section 91 would not apply to OTC derivatives even though some OTC derivatives may create a right, option or interest in respect of shares, bonds, debentures, etc. Our comments in paragraph (d) below are also relevant here.

(d) **Section 92** ***Recommendations by licensed person***: Section 92 refers to making recommendations in relation to securities and futures contracts and the Bill provides that "*futures contracts*" in Section 92 be replaced with "*derivatives*". Parties to an OTC derivative transact on an arm's length basis and almost invariably provide mutual representations to this effect[1]. While it is general market practice (as well as a requirement under BNM's Guidelines) for a BNM licensed institution to provide a term sheet for a transaction that is not a plain vanilla OTC derivative, the provision of the term sheet does not detract from the arm's length basis on which the parties transact and the term sheet is clearly not a recommendation by the term sheet provider. Care needs to be taken to ensure that

[1] The following is the standard form representation provided in the Schedule to the 2002 ISDA Master Agreement:
Additional Representation [will][will not]* apply. [For the purpose of Section 3 of this Agreement, the following will constitute an Additional Representation:
[[(i)] ***Relationship Between Parties.*** Each party will be deemed to represent to the other party on the date on which it enters into a Transaction that (absent a written agreement between the parties that expressly imposes affirmative obligations to the contrary for that Transaction):
[(1)] *Non-Reliance.* It is acting for its own account, and it has made its own independent decisions to enter into that Transaction and as to whether that Transaction is appropriate or proper for it based upon its own judgment and upon advice from such advisers as it has deemed necessary. It is not relying on any communication (written or oral) of the other party as investment advice or as a recommendation to enter into that Transaction, it being understood that information and explanations related to the terms and conditions of a Transaction will not be considered investment advice or a recommendation to enter into that Transaction. No communication (written or oral) received from the other party will be deemed to be an assurance or guarantee as to the expected results of that Transaction.
[(2)] *Assessment and Understanding.* It is capable of assessing the merits of and understanding (on its own behalf or through independent professional advice), and understands and accepts, the terms, conditions and risks of that Transaction. It is also capable of assuming, and assumes, the risks of that Transaction.
[(3)] *Status of Parties.* The other party is not acting as a fiduciary for or an adviser to it in respect of that Transaction.]]*

the application of Section 92 to OTC derivatives does not upset the established market practice and understanding with regard to term sheets.

(e) **Section 92A *Information to be given to a person who invests in capital market product***:

(i) As mentioned above, one party to an OTC derivative would usually be a BNM licensed institution that would already be subject to comparable BNM requirements in this regard. Further, participants in the OTC derivatives market tend to be "*wholesale*" in nature. Although there may not be equality of information (or even equality of access to information), this is something that such "*wholesale*" participants routinely face and accept in transacting. Where this is of particular concern to a counterparty in a specific circumstance, it will generally have the capability to take steps to address or mitigate the inequality. Thus, our members submit that the SC should not exercise its powers under this provision to be prescriptive in relation to OTC derivatives. At a minimum, our members hope that the SC will conduct a public consultation before prescribing any measures under Section 92A in relation to OTC derivatives. Our comments in paragraph (d) above are also relevant here.

(ii) Unlike the other capital market products, each OTC derivative is bespoke and customized on a trade-by-trade basis. It follows from this that each term sheet is unique and that term sheets are many in number. Thus, unlike say an offering document for a securities offer which is extensively reviewed both internally as well as by outside legal counsel and other external advisers, it is not practicable to perform anywhere near the same level of due diligence for an OTC derivative term sheet. In the circumstances, to make a false or misleading OTC derivative term sheet an offence punishable by fine and imprisonment for up to 10 years is manifestly excessive. Civil liability for a false and misleading OTC derivative term sheet is the appropriate redress.

(f) **Section 97 *Dealings as principal***: Please confirm that Section 97 would not apply to OTC derivatives even though some OTC derivatives may create a right, option or interest in respect of shares, bonds, debentures, etc. In any event, as parties to an OTC derivative generally transact on a principal-to-principal basis, it would be superfluous to require the parties to first inform each other that they are dealing as principal.

(g) **Part III, Division 3, Subdivision 3 *Futures contracts***: It is not clear whether these provisions will apply to OTC derivatives, and if so, how they would apply. However, many of these provisions are not appropriate to OTC derivatives, e.g. Section 99 (*Trading in futures contracts on own account*) since parties will invariably be on the other side of the trade as principal and Section 104 (*Sequence of sending and carrying out of orders*) since each OTC derivative is a unique

bespoke transaction. In relation to Section 100 (*Documents to be given to prospective clients*), in relation to BNM licensed institutions, they would already be subject to comparable BNM requirements. In the interest of a level playing field, for non-BNM licensed institutions, the documentation requirements prescribed by the SC should be consistent with the BNM requirements. Please see our comments in paragraph 6 below with regard to Section 101 (*Trading limits in futures contracts*), paragraph (k) below with regard to Section 102 (*Reportable positions*) and paragraph (b) above with regard to Section 105 (*Trading in futures contracts outside Malaysia*).

(h) **Part III, Division 4, Subdivision 3** ***Treatment of client's assets in respect of futures contracts***: It is not clear whether these provisions will apply to OTC derivatives, and if so, how they would apply. However, our members believe that it would not be appropriate to apply these provisions to OTC derivatives as parties to an OTC derivative generally transact on a principal-to-principal basis. Where the parties have entered into a bilateral margining arrangement, cash or other assets may be posted as collateral by one party to the other pursuant to such margining arrangement. But such posting of collateral (even if one-way only) should not be treated on the same basis as the provision of assets by a client to a futures broker.

(i) **Part V, Division 2** ***Prohibited Conduct – Futures Contracts***:

(i) It is not clear whether these provisions will apply to OTC derivatives, and if so, how they would apply. While our members agree that fraudulent conduct should be punished, we think that the provisions will need to be modified to take into account the nature of the OTC derivatives market.

(ii) In relation to Section 207 (*False or misleading statements*) read with Section 209 (*Penalties for offence under Subdivision 1*), we would emphasize the point set out in paragraph (e)(ii) above.

(iii) In relation to Section 208 (*Prohibition of abuse of information obtained in official capacity*), our members are of the view that there needs to be explicit recognition of "*Chinese Wall*" arrangements and parity of information defences. Certain persons within an institution may have relevant information but so long as such information is not passed on to those persons that transact an OTC derivative on behalf of the institution due to the existence of a "*Chinese Wall*", there should be no breach of Section 208. Unlike futures contracts traded on an exchange, where a party faces the exchange rather than an identifiable counterparty, in an OTC derivative, the parties to an OTC derivative are known to each other. Thus, it should be a defence to a breach of Section 208 that there was parity of information between the parties so that neither had an advantage over the other.

(j) **Section 353** ***Disclosure of information relating to dealing in securities or trading in futures contracts***: It is not clear whether this provision will apply to OTC derivatives. Given that a trade repository for OTC derivatives will be established and that BNM licensed institutions are also subject to reporting requirements of BNM, it is important that duplicative and/or overlapping requirements be avoided. Insofar as BNM licensed institutions are concerned, (without the written consent of the counterparty) they would not in any case be permitted by BNM under extant regulations to make such disclosures to the SC. It should also be borne in mind that given the volume of transactions that licensed institutions engage in, they would need to select and implement technological solutions to meet reporting requirements – any change or ad hoc requirements will require costly and time-consuming modifications to systems or manual extraction of data (with its attendant risk of errors).

6. Position limits

With regard to the power under Section 101 (*Trading limits in standardized derivatives*) of the SC or a derivatives exchange with the SC's approval to impose position limits on standardized derivatives, our members hope that any proposal will be issued in draft form for public consultation before finalization. As you are no doubt aware, the imposition of position limits continues to generate much debate in both the US and EU. As such, and given the relative size of the futures markets there and in Malaysia, the best course of action may be to await the outcome of the debate in the US and EU before proceeding with any proposal in this regard. If it would be of help, we would be pleased to arrange a briefing for the SC on this topic.

7. Trade repository and mandatory reporting of OTC derivatives

7.1 Part III, Division 3, Subdivision 4 (*Over-the-counter derivatives*) sets out the regulatory regime for a trade repository for OTC derivatives and mandatory reporting. Our members are glad to note that this part will only come into operation at the expiration of 2 years after the date that the Bill comes into operation (and that the Minister of Finance may extend this period for up to one year).

7.2 OTC derivatives reporting will also be mandated in both the US and the EU and many other countries and this will have an impact at least on cross-border OTC derivatives transactions involving a Malaysian counterparty. Our members thus request that the SC take into account global developments in the implementation of the trade reporting requirements. There is, for example, a global initiative to develop common Legal Entity Identifiers, Product Identifiers and Unique Trade Identifiers.

7.3 The decisions that the SC will need to make include (i) the types of transactions that should be required to be reported, bearing in mind the purpose to be achieved by having such information reported and the cost to participants of having to report such information, (ii) the nature and frequency of the information to be reported, (iii) whether there will be a requirement to "*back-load*" outstanding legacy transactions, (iv) whether a

domestic trade repository should be operated under a "*utility*" or "*for profit*" model, (v) the technology and middleware choices to be made by a domestic trade repository and (vi) whether it will recognize a foreign trade repository for this purpose. Given that the definition of OTC derivatives for the purpose of mandatory reporting includes OTC derivatives derived from, referenced to or based on exchange rates, please confirm that FX spots will not be required to be reported (which is the position in the US and EU). It is also of key importance that any determinations be in compliance with the principles set out in the joint Consultative Report on *Principles of Financial Market Infrastructures* dated Mar 2011 by the Committee on Payment and Settlement Systems and the International Organization of Securities Commissions. At any rate, our members request that the SC conduct a public consultation before making any determinations. If it would be of help, we would be pleased to arrange a briefing for the SC on trade repositories.

7.4 From our members' standpoint, the best solution would be for mutual recognition of trade repositories so that a participant would be able to satisfy their Malaysian reporting requirements by reporting to either a Malaysian or foreign trade repository. At minimum, the data that is required to be reported to a Malaysian trade repository should be the same or a subset of the data required to be reported in the US and EU (given that these markets account for over 90% of global interest rate OTC derivatives, market participants will inevitably have to meet the US and EU reporting requirements). Although this will mean that a participant may have to report the data twice (or even more times) to different trade repositories, this will still be manageable so long as the data set is the same. However, where the data set is different, this will require market participants to develop and implement more than one technological solution to meet the different reporting requirements and the cost associated with this will be prohibitive.

7.5 We would again highlight that (except where it has obtained the written consent of the counterparty) BNM licensed institutions would not be permitted by BNM under extant regulations to make any disclosures to a trade repository.

7.6 We note that apart from disclosure to the SC where the SC is of the view that such disclosure is necessary in the interest of the public or for the protection of investors and disclosure pursuant to Section 107G (*Permitted disclosure*) a trade repository and its directors, officers, servants and agents are under a duty to maintain secrecy of the information provided to the trade repository. Please confirm that the SC will not require or permit the trade repository to publish or release any information to the general public.

8. Central clearing of OTC derivatives

We note that the Bill does not introduce any mandatory central clearing requirement for OTC derivatives. Our members hope that this means that Malaysia has no plans to mandate central clearing of OTC derivatives. If this is not the case, our members request that a public consultation be conducted before any mandatory central clearing requirement is introduced. Mandatory central clearing is an even more complex issue than mandatory trade reporting – and unlike reporting where a trade can be reported more than once to more than one trade repository, a trade can only be cleared once through one

central clearing house. Again, if it would be of help, we would be pleased to arrange a briefing for the SC on central clearing counterparties.

9. Part IXA powers of the SC

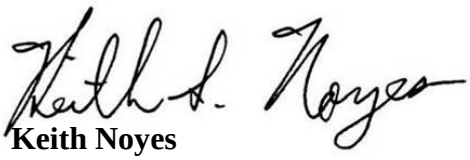
9.1 Section 346B empowers the SC to request any person to provide any information or document which the SC considers necessary for the purposes of monitoring, mitigating and managing systemic risks in the capital market or upon request from BNM pursuant to Section 30 of the Central Bank of Malaysia Act 2009. While our members concede that it is not possible to fully anticipate the kind of information or document that may be necessary in this regard, our members hope that any such information would largely be available through the trade repository.

9.2 Section 346B further provides that where the person concerned is solely under the supervision or oversight of BNM, the request notice should be issued through BNM. An analogous provision should be introduced in respect of persons that are solely under the supervision or oversight of the Labuan Financial Services Authority.

9.3 Section 346C empowers the SC to issue a directive requiring any person to take such measures as the SC may consider necessary in the interest of monitoring, mitigating or managing systemic risk in the capital market, taking into consideration the interest of financial stability. As such measures could conceivably extend to prohibiting parties from exercising their close-out netting rights under the ISDA Master Agreement, Section 346C does have an adverse impact on the legal enforceability of close-out netting rights under the ISDA Master Agreement. Thus, as elaborated on in paragraph 1 above, this does result in a higher counterparty credit exposure against which capital must be set aside by a non-defaulting bank counterparty. In addition, the re-hedging dilemma that a non-defaulting party would face is likely to be even more pronounced in such circumstances as markets would likely be highly volatile where the SC chooses to exercise its powers under this provision.

Please feel free to contact Jacqueline Low (jlow@isda.org, +65 6538 3879) or Keith Noyes (knoyes@isda.org, +852 2200 5909) at your convenience.

Yours faithfully,
For the International Swaps and Derivatives Association, Inc.



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