

APAC Monthly Update

March 2012

APAC Monthly Update summarizes important regulatory developments, meetings, committee activities and conferences in the region.

Regulatory Activities

China:

On March 13, ISDA met with the China Banking Regulatory Commission (CBRC) to discuss issues relating to the enforceability of close-out netting in China and the impact of regulatory reforms in the US and EU on Asian financial institutions. On the same day, ISDA also met with NAFMII to discuss issues relating to the recent Determination Committee's decision on CDS referencing Greece.

India:

On March 5, ISDA met with various departments of RBI:

- with the Payment and Settlements department to discuss issues surrounding central clearing and CCPs
- with the Internal Debt department to discuss the issues on the CDS market
- with DBOD to discuss the netting issues in India.

On March 6, ISDA met with CCIL to discuss issues on central clearing and trade repositories.

Hong Kong:

On March 19, ISDA joined the HKMA/TMA group meeting to discuss progress on regulatory reforms in Hong Kong and progress made by the HK Exchange in setting up the CCP. On the same day, ISDA also met with HKMA to discuss the recent consultation papers on Basel III capital and liquidity requirements.

On March 20, ISDA visited Julia Leung, Hong Kong Undersecretary of the Treasury to discuss the Greek sovereign CDS auction and other challenges faced by the European credit market.

Korea:

On March 28, ISDA met with the Financial Services Commission (FSC) to discuss Korea's plans for establishing a CCP. Enabling legislation has been sent to the National Assembly, but has not been voted on yet. After passage of the bill, the FSC would draft a Presidential Decree providing greater detail on the regulatory framework and scope of the clearing mandate. On the same day, ISDA met with the Bank of Korea to discuss macro-prudential issues related to clearing. Bank of Korea is also studying the potential for central clearing of Korea's repo market.

Committee/Working Group Activities

North Asia L&R

On March 27, ISDA held its monthly L&R meeting in Hong Kong. At the meeting, ISDA briefed members on the latest regulatory and documentation developments in this region. Topics discussed regarding North Asia include China's central clearing proposal for onshore IRS denominated in RMB, progress of the regulatory reform of the OTC derivatives market in Hong Kong and the draft Korean CDS index documentation. Latest regulatory developments in South Asia and other ISDA efforts and documentation projects were also discussed at the meeting.

South Asia L&R

On March 29, ISDA held its monthly L&R meeting in Singapore. At the meeting, ISDA briefed members on the latest regulatory and documentation developments in this region. Topics discussed regarding South Asia included PIDM's response on "Qualified Third Party", PIDM and BNM's joint concept paper on Recordkeeping and Reporting requirement for OTC derivatives, RBI's notice on Reporting Platform for OTC Foreign Exchange and Interest Rate Derivatives, FEDAI's circular for member banks to join CCIL's Forex Forward Guaranteed settlement, ISDA's drafts of Indicative and Final Term-Sheets, Generic Risk Disclosure Statement, MTM Valuation Disclaimer and Board resolutions to meet RBI's Comprehensive Guidelines on Derivatives, MAS's consultation paper on Covered Bonds and ISDA's submissions to MAS on the Proposed Regulation of OTC Derivatives and the Transfer of Regulatory Oversight of Commodity Derivatives from IE to MAS. Latest regulatory developments in North Asia and other ISDA efforts and documentation projects were also discussed at the meeting

Market Infrastructure

On March 1, ISDA held its APAC Interest Rates Derivatives Operations Working Group meeting to address the electronic confirmation format of onshore CNY swaps, addition / amendment of floating rate options and certain market practices of India swap fixing.

On March 15, ISDA held its APAC Credit Derivatives Operations Working Group meeting to discuss the India CDS market, novation electronic confirmation practice and the treatment of a name change event.

On March 22, ISDA held its APAC Equity Derivatives Operations Working Group meeting to address the counterparty on-boarding issue, the documentation of local taxes in China H-stock, MSCI swap and Pan-Asia interdealer swap. The group also discussed the AEJ reference price source matrix.

Country Working Groups

On March 6 ISDA held an Indian Working group meeting in Mumbai. Topics discussed included clearing and reporting of FX derivatives through CCIL, and how to meet the mandatory margining requirement for onshore CDS from a documentation perspective.

On March 14 ISDA held a China Working Group meeting in Beijing. Topics discussed included RQFII and revised drafting of financial institution bankruptcy regulation.

On March 28 ISDA held a Korea Working Group meeting in Seoul. The issue receiving the most attention was KRX's plans to establish a CCP and whether Korean netting laws would allow porting of client accounts and if clearing members could close-out and net positions with KRX in the event of the CCP becoming insolvent.

Regulatory Developments

Hong Kong: Legco passes Banking (Amendment) Ordinance

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On March 9, the Hong Kong Monetary Authority (HKMA) released a notice that the Banking (Amendment) Bill 2011 was passed by the Legislative Council (Legco) on February 29, and enacted as the Banking (Amendment) Ordinance 2012 (BAO 2012). BAO 2012 empowers the HKMA to prescribe:

- capital and liquidity requirements to locally incorporated Authorized Institutions (AIs);
- the disclosure of information to the public by AIs related to their state of affairs, profit and loss or compliance with the capital and liquidity requirements;
- and to issue and approve codes of practice.

BAO 2012 also widens the Tribunal remit to be a forum for appeals against decisions by the HKMA to vary capital and liquidity requirements for individual AIs, or to require remedial actions by individual AIs when they fail to meet the capital and liquidity requirements prescribed to them by HKMA. The provisions of BAO 2012 will be phased in, starting with the capital and disclosure requirements with effect from January 1, 2013.

India:

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Interbank OTC FX derivatives transactions to be reported to CCIL

On March 9, Reserve Bank of India (RBI) released a notice that all interbank OTC foreign exchange derivatives will be reported on a platform developed by CCIL. All/selective trades in OTC foreign exchange and interest rate derivatives between Category I Authorized Dealer Banks/market makers (banks/PDs) and their clients will report on the CCIL platform, subject to a mutually agreed confidentiality protocol.

FEDAI member banks to join CCIL's FX forward guaranteed settlement

On February 28, the Foreign Exchange Dealers' Association of India (FEDAI) released a circular for an amendment of FEDAI rule 8 that all member banks should join CCIL's forex forward guaranteed settlement by June 30 and start routing all eligible forex forward transactions by October 1.

Korea: FSC proposed amendments to FSCMA

Contact: Jing Gu (jgu@isda.org)

The Financial Services Commission (FSC) announced proposed amendments to the Enforcement Decree of the Financial Investment Services and Capital Markets Act (FSCMA) on February 24. The draft amendments will be reviewed by the Regulatory Reform Committee and the Ministry of Government Legislation and are expected to take effect in the first half of 2012. The draft amendments seek to, among other things, clarify the regulations on issuance of derivatives-linked securities (DLS) by foreign financial institutions and exempt the foreign issuers which satisfy certain requirements from the licensing requirement under the FSCMA. These requirements include (1) the foreign issuer is subject to the sufficient supervision by an overseas regulatory body from who the FSC is able to obtain certain information, and (2) the DLS must be sold to the professional investors (i) through underwriting by a

domestic investment dealer or (ii) through brokerage by a domestic investment broker. This amendment aims to resolve the confusion in the market about whether DSL issued by a foreign financial institution can be sold in Korea.

Malaysia:

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PIDM issues responses on qualified third party criteria

On March 26, the Malaysia Deposit Insurance Corporation (PIDM) issued its Response to the Consultation Paper on Criteria for Qualified Third Party. Taking the industry's comments into consideration, PIDM will now define a Qualified Third Party that would be eligible to assume Qualified Financial Agreements (QFAs), which includes OTC derivatives, from a failing Member Institution or Affected Person as being any of the following entities:

- an institution, other than a bridge institution, licensed under the Banking And Financial Institutions Act 1989, the Islamic Banking Act 1983, the Insurance Act 1996 and the Takaful Act 1984 or an institution prescribed under the Development Financial Institutions Act 2002 which is in compliance with the capital and prudential requirements of Bank Negara Malaysia (BNM);
- an institution licensed under the Labuan Financial Services and Securities Act 2010 and Labuan Islamic Financial Services and Securities Act 2010, which is in compliance with capital and prudential requirements of the Labuan Financial Services Authority;
- a public entity established under its own statutory act; or
- an entity whose obligations under the QFAs will be guaranteed by the Government of Malaysia, Bank Negara Malaysia or PIDM.

PIDM and BNM issue concept paper on reporting requirements

On March 26, PIDM, together with Bank Negara Malaysia (BNM), issued a joint concept paper on Recordkeeping and Reporting Requirement for Over-the-Counter Derivatives. These requirements will apply to banks and insurance companies regulated by BNM and all Member Institutions of PIDM, and are intended as an interim measure pending the establishment of the trade repository in Malaysia. The paper proposes the potential standardized counterparty identifiers that are being considered. The data proposed to be reported comprises of:

- aggregate level data on both OTC and exchange-traded derivatives used for hedging and non-hedging purposes (reported quarterly);
- participant level data on OTC derivatives (reported quarterly);
- transaction level data on OTC derivatives (reported within 24 hours of request by the regulators);
- qualitative information, including maintained copies of all relevant agreements (reported within 24 hours of request by the regulators).

Deadline for submission of comments is April 30.

New Zealand: Reserve Bank consults on Basel III capital adequacy requirements

Contact: Keith Noyes (knoyes@isda.org) / Cindy Leiw (cleiw@isda.org)

On March 23, The Reserve Bank of New Zealand (Reserve Bank) issued a Consultation Paper on Further Elements of Basel III Capital Adequacy Requirements in New Zealand. The Reserve Bank proposes the adoption of the Capital Conservation Buffer (CCB) to be comprised of 2.5% of Common Equity Tier 1, above the minimum capital requirement and to be fully implemented by January 1, 2014. It proposes that, once the CCB has been drawn down, a bank must fully restrict distributions until the buffer is restored to 2.5% of Common Equity Tier 1. The Reserve Bank can also impose a time limit on banks operating within the buffer range and require banks operating within the buffer range to submit a capital plan for

rebuilding the buffer. The restrictions on distributions will be applied at the banking group level but the Reserve Bank may apply this at the registered bank level.

The paper also introduces a framework for implementing the Countercyclical Buffer (CB) which will be initially applied to registered banks but may extend it to include other lenders, such as non-bank deposit takers, in the future. The CB will be comprised of Common Equity Tier 1 and may range from 0%-2.5%. Registered banks will be given a 12-month notice and will be required to submit a capital plan on its method of raising capital to comply with the requirement when it becomes effective. Restrictions on distributions will apply if a bank operates within the buffer range. The Reserve Bank and the Treasury will undertake further work to determine appropriate governance and accountability arrangements for the operation of the CB. The Reserve Bank will give notice to banks to apply the CB from January 1, 2014.

The Reserve Bank introduces the Basel III requirement that regulatory capital instruments are capable of absorbing losses. The paper proposes that the terms and conditions of all non-common equity Tier 1 capital and Tier 2 instruments must have a provision that requires such instruments, at the option of the relevant authority which would be either the Reserve Bank or the Statutory management, to be converted into common equity upon occurrence of a trigger event. The paper proposes two possible trigger events:

- when the Reserve Bank determines a bank is non-viable, without reference to a particular measure of non-viability, determined on an *ex-ante* basis;
- to define a quantitative trigger point that a bank must breach before the conversion to equity is triggered.

However, the Reserve Bank envisions the application of the loss absorbency requirement would be discretionary rather than automatic. The recognition of non-qualifying instruments issued before September 12, 2010, will be gradually phased out from January 1, 2013 and fully phased out from January 1, 2015. Deadline for submission of comments is April 13.

Singapore: MAS proposes rules for issuance of covered bonds

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On March 9, MAS released a consultation paper on the proposed rules for Issuance of Covered Bonds by Banks Incorporated in Singapore. MAS proposes that banks incorporated in Singapore may issue covered bonds subject to an aggregate value of assets in the cover pool, capped at 2% of the value of total assets of the bank.

In addition, a bank incorporated in Singapore must comply with a set of conditions, including: (a) only mortgage loans secured by residential property and derivatives held for the purpose of hedging risks arising from issuing covered bonds will be included in the cover pool; (b) a 80% loan-to-value (LTV) limit will be applied to the residential mortgage loans; (c) value of the assets in cover pool shall be 103% of the face value of the covered bonds secured at all times; (d) an appointed, external qualified third party auditor will certify and verify annually that the bank has an accurate register of assets in the cover pool, that the bank complies with all the conditions pertaining to the issuance of a covered bond, will assess the adequacy of the bank's risk management process, submit a certified report to MAS on the last day of the 3rd month immediately following the end of the bank's financial year and internal controls and report to MAS if any breach has occurred. Deadline for submission is April 10.

Submissions

On March 26, ISDA made two submissions to the Monetary Authority of Singapore (MAS) in response to their consultation papers on the Proposed Regulation of OTC Derivatives and the Transfer of Regulatory Oversight of Commodity Derivatives from IE to MAS.

Upcoming committee and working group meetings/conferences

Meetings:

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| Meeting on PIDM consultation paper and PIDM & BNM Joint Concept Paper – Singapore | Apr 2 |
| L&R Advisory Meeting | Apr 3 |
| Taipei Members Meeting | Apr 23 |
| L&R North Asia Meeting | Apr 24 |
| APAC Commodity Meeting – Singapore | Apr 25 |
| L&R South Asia Meeting | Apr 26 |

Conferences:

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| Impact of US and European Regulatory Changes on Global and Asian Financial Markets – Taipei | Apr 25 |
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