

Comments by the International  
Swaps and Derivatives  
Association, Inc. on the  
Consultation Paper on the  
Proposed SGX-DC Remote  
Clearing Membership and  
Derivatives Clearing  
Organization Rules

November 15, 2013

Singapore Exchange Limited  
2 Shenton Way  
#19-00 SGX Centre 1  
Singapore 068804  
Attention: Jeth Lee  
[rules@sgx.com](mailto:rules@sgx.com)

Dear Sirs

## **Proposed Amendments to SGX-DC Remote Clearing Membership and Derivatives Clearing Organization Rules**

1. **Introduction:** The International Swaps and Derivatives Association, Inc. (“ISDA”)<sup>1</sup> welcomes the opportunity to respond to the Consultation Paper on Proposed SGX-DC Remote Clearing Membership and Derivatives Clearing Organization Rules (the “**Consultation Paper**”) issued by the Singapore Exchange Derivatives Clearing Limited (“SGX-DC”) on October 25, 2013. Individual members will have their own views on different aspects of the Consultation paper, and may provide their comments to SGX-DC independently.

2. **General Comments:** Before responding to the specific questions posed in the SGX-DC Consultation Paper, we would like to make the following general comments:

1.1 **DCO:** We have no objection to SGX-DC’s application as a derivatives clearing organization (“DCO”) with the United States (“US”) Commodity Futures Trading Commission (“CFTC”). The introduction of remote clearing members (“RCMs”) as a new category of SGX-DC’s clearing membership to clear Non-Relevant Market Contracts, and/or customer OTC financial derivative contracts (“OTCF Contracts”) will aid in meeting the G20 commitment to clear standardized OTC derivatives contracts through a central counterparty (“CCP”).

1.2 **Client Clearing Model:** There are two operating models of OTC derivatives client clearing - the *Principal* or *SCM* model<sup>2</sup> and the *Agency* or *FCM* model<sup>3</sup>.

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<sup>1</sup> Since 1985, ISDA has worked to make the global over-the-counter (OTC) derivatives markets safer and more efficient. Today, ISDA has over 800 member institutions from 60 countries. These members include a broad range of OTC derivatives market participants including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure including exchanges, clearinghouses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's web site: [www.isda.org](http://www.isda.org).

<sup>2</sup> In the *Principal* or *SCM* model, the clearing member is described as being the principal to the client’s transactions, and the clearing member enters into “back-to-back” transactions between it and the clearing house. The clearing house does not deal directly with the client and, for the most part, recognizes only the clearing member in relation to the cleared transactions.

Under the Agency model, segregation and portability depends upon various US statutes, namely, the Commodity Exchange Act, the CFTC Regulations and the Bankruptcy Code. The introduction of the FCM Clearing Member as a category of clearing membership, subject to the US federal laws, enables the agency model to be adopted by SGX-DC. While we support the introduction of the FCM Clearing Member, we would like to ensure that any potential conflicts of law are identified and a legal opinion provided to Clearing Members.

3. **Response to Proposals:** We set out below our responses to the questions raised in the Consultation Paper (capitalized terms used below but not defined have the meaning given to such terms in the Consultation Paper):

Proposal	Response
<p>(1) SGX-DC seeks your views on its proposal to introduce remote clearing members as a new class of clearing membership and the corresponding membership criteria.</p>	<p>We have no objection to SGX-DC introducing remote clearing members (“RCMs”) as a new class of clearing membership.</p> <p>We seek further understanding on the determination process SGX-DC will undertake in determining whether a jurisdiction is regulated and licensed by a recognized regulator and governed by the laws of a jurisdiction acceptable to SGX-DC as stated in Rule 2.02C.1.1<sup>4</sup>. As no two jurisdictions will have the exact rules and regulations, the determination process should be outcomes based and not rules based.</p> <p>Paragraph 2.4<sup>5</sup> of the Consultation Paper allows a futures commission merchant (“FCM”) to be admitted as an SGX-DC clearing member under one of the other clearing membership types. These membership types are: (i) General Clearing Member (“GCM”); (ii) Bank Clearing Member (“BCM”), (iii) RCM and (iv) FCM Clearing Members. However, Paragraph 2.5<sup>6</sup> of the Consultation Paper states that FCMs will only be initially accepted as RCMs. We seek further clarity on the clearing membership process for a FCM in SGX-DC.</p>

<sup>3</sup> In the Agency or FCM model, the clearing member is described as being the agent of the client, so that the client deals with the clearing house through the agency of the clearing member. The two principals to these dealings are described to be the clearing house and the client. The clearing member is not described as being a principal counterparty to those dealings. However, to ensure the stability of the clearing system, the clearing member guarantees its client’s performance to the clearing house.

<sup>4</sup> Singapore Exchange, *Consultation Paper on proposed SGX=-DC remote Clearing membership and Derivatives Clearing Organization Rules*, 25 Oct 2013, Appendix, Rule 2.02C.1.1, Page 13.

<sup>5</sup> Singapore Exchange, *Consultation Paper on proposed SGX=-DC remote Clearing membership and Derivatives Clearing Organization Rules*, 25 Oct 2013, Paragraph 2.4, Page 1.

<sup>6</sup> Singapore Exchange, *Consultation Paper on proposed SGX=-DC remote Clearing membership and Derivatives Clearing Organization Rules*, 25 Oct 2013, Paragraph 2.5, Page 1.

If the aim for introducing the remote clearing membership is to allow FCMs as clearing members of SGX-DC and to “clear Non-Market contracts and OTC financial derivative contracts (“**OTCF Contracts**”) on behalf of their U.S. customers”<sup>7</sup>, will U.S.-based FCMs be allowed to apply as FCM Clearing Members or will they only be allowed to apply as a RCM in the initial phase? Additionally, Rule 1.06.4<sup>8</sup> applies solely to FCM Clearing Members and allows certain clearing rules to be governed and construed in accordance with the federal laws of the US. Consequently, if a FCM is under a different membership category such as a RCM, will Rule 1.06.4 still apply to them as they are not in the clearing membership category of a FCM Clearing Member?

Paragraph 2.8<sup>9</sup> of the Consultation Paper states that the Rule amendments as proposed in the Appendix will be subject to regulatory concurrence by the Monetary Authority of Singapore (“**MAS**”). We seek further details on the process for rules amendment, particularly, in the event there is no regulatory concurrence by MAS. In such an instance, will there be any consultation with the industry on the revised Rules?

Paragraph 3.9 of the Consultation Paper states that “RCMs have to submit to SGX-DC any reports it provides to its foreign regulator or to a foreign self-regulatory organization with oversight over the RCM”. We seek further details on this reporting requirement and the expected timeframe for submission of these reports to SGX-DC.

In Rule 7A.02.1.5(b) of the Consultation Paper, for the open positions in OTCF Contracts of a defaulted/ suspended Clearing Member, an auction may be conducted for such open positions. In such an instance, how will the auction process work? If a FCM Clearing Member defaults, will a non-FCM Clearing Member be required to bid in the auction process? Or conversely, will a FCM Clearing Member or a RCM be required to bid in the auction process for non-FCM Clearing Member?

<sup>7</sup> Singapore Exchange, *Consultation Paper on proposed SGX-DC remote Clearing membership and Derivatives Clearing Organization Rules*, 25 Oct 2013, Paragraph 4.1, Page 6.

<sup>8</sup> Singapore Exchange, *Consultation Paper on proposed SGX-DC remote Clearing membership and Derivatives Clearing Organization Rules*, 25 Oct 2013, Appendix, Rule 1.06.4, Page 10.

<sup>9</sup> Singapore Exchange, *Consultation Paper on proposed SGX-DC remote Clearing membership and Derivatives Clearing Organization Rules*, 25 Oct 2013, Paragraph 2.8, Page 2.

<p>(2) SGX-DC seeks your views on its proposal to allow the admission of FCM as clearing members and the corresponding membership criteria.</p>	<p>Please refer to the responses above.</p>
<p>(3) SGX-DC seeks your views on the proposed Rule amendments for alignment with Part 39 of the CFTC regulations.</p>	<p>Part 39.12(a)(5)<sup>10</sup> of the CFTC regulations mandates a DCO to require all Clearing Members, including non-FCMs to provide periodic financial reports to the DCO or, if requested, to the CFTC. If SGX becomes a DCO, will other types of Clearing Members, such as a General Member, be subject to a potential request from the CFTC for this information? Will Clearing Members, which are not FCMs, be subject to the DCO requirements, such as the recordkeeping requirement in Part 39.20<sup>11</sup> of the CFTC regulations?</p> <p>Section 39.21<sup>12</sup> of the CFTC regulations requires a DCO to disclose publicly information, such as the terms and conditions of each transaction cleared and settled by the DCO; the clearing and other fee a DCO charges its Clearing Members and the margin-setting methodology. Will SGX-DC be disclosing the required information publicly?</p> <p>Section 39.27(c)<sup>13</sup> of the CFTC regulations requires a DCO clearing outside the U.S. to identify and address any material conflict of law issues and the ability of the DCO to demonstrate the enforceability of its choice of law, its rules and procedures and contracts in relevant jurisdictions. Will SGX-DC be providing a legal opinion to Clearing Members on these issues?</p> <p>Rule 2.14.6 of the Consultation Paper states the following: “Clearing Members who are subject to Part 45 of the CFTC Regulations, which pertain to swap data recordkeeping and reporting requirements, shall as soon as technologically practicable after registration of a Non-Relevant Market Transaction or an OTCF Transaction for the Clearing</p>

<sup>10</sup> <http://www.gpo.gov/fdsys/pkg/FR-2011-11-08/pdf/2011-27536.pdf>, *Derivatives Clearing Organization General Provisions and Core Principles; Final Rules*, Federal Register, Vol. 76, No. 216, 8 Nov 2011, 39.12(a)(5), Page 69437.

<sup>11</sup> <http://www.gpo.gov/fdsys/pkg/FR-2011-11-08/pdf/2011-27536.pdf>, *Derivatives Clearing Organization General Provisions and Core Principles; Final Rules*, Federal Register, Vol. 76, No. 216, 8 Nov 2011, 39.20, Page 69446.

<sup>12</sup> <http://www.gpo.gov/fdsys/pkg/FR-2011-11-08/pdf/2011-27536.pdf>, *Derivatives Clearing Organization General Provisions and Core Principles; Final Rules*, Federal Register, Vol. 76, No. 216, 8 Nov 2011, 39.21, Page 69446.

<sup>13</sup> <http://www.gpo.gov/fdsys/pkg/FR-2011-11-08/pdf/2011-27536.pdf>, *Derivatives Clearing Organization General Provisions and Core Principles; Final Rules*, Federal Register, Vol. 76, No. 216, 8 Nov 2011, 39.27(c)(1) – 39.27(c)(2), Page 69447.

House: (a) report all primary economic terms data of the relevant transaction, as defined in the CFTC Regulation 45.1 to the Clearing House; and (b) inform the Clearing House of the identity of the swap data repository that the relevant transaction was previously reported to, if any”. As there will be Clearing Members who are not RCMs or FCM Clearing Members but may be registered with the CFTC as Swap Dealers (“SDs”), Rule 2.14.6 would require these SDs to report to SGX-DC on a real-time basis. As real-time reporting requires a certain amount of information technology (“IT”) build, it may be prudent to ensure all existing Clearing Members who are CFTC registered SDs have the necessary IT infrastructure to meet this reporting requirement. SGX-DC should also ensure its IT infrastructure is able to support real-time reporting.

As you may be aware, CFTC regulation 39.13(8)(E)(ii)<sup>14</sup> requires a DCO’s Clearing Member to collect customer initial margin for non-hedge positions at a level that is greater than 100 percent of the DCO’s initial margin requirement with respect to each product and swap portfolio. However, the DCO has the discretion in determining the percentage by which customer initial margins must exceed the DCO’s initial margin requirements. When client clearing is introduced in SGX-DC, will this requirement be applicable to the clients of all categories of Clearing Members or only FCM Clearing Members?

In the Consultation Paper, Rule 7.02A.2 and 7.02AA.2 states that for registration of Non-Relevant Market Transactions and OTCF Transactions, “a submission for registration will be accepted or rejected by the Clearing House as quickly after submission as would be technologically practicable if fully automated systems were used”<sup>15</sup>. However, in Paragraph 5.3, the Consultation Paper states that the CFTC requirement is “for acceptance and rejection to be within 60 seconds of the submission of a trade to SGX-DC”<sup>16</sup>. As the Rules do not specifically indicate the rejection or acceptance of a trade within 60

<sup>14</sup> <http://www.gpo.gov/fdsys/pkg/FR-2011-11-08/pdf/2011-27536.pdf>, *Derivatives Clearing Organization General Provisions and Core Principles; Final Rules*, Federal Register, Vol. 76, No. 216, 8 Nov 2011, 39.13(8)(E)(ii), Page 69439.

<sup>15</sup> Singapore Exchange, *Consultation Paper on proposed SGX=-DC remote Clearing membership and Derivatives Clearing Organization Rules*, 25 Oct 2013, Appendix, Rule 7.02A.2 and 7.02AA.2, Page 26.

<sup>16</sup> Singapore Exchange, *Consultation Paper on proposed SGX=-DC remote Clearing membership and Derivatives Clearing Organization Rules*, 25 Oct 2013, Paragraph 5.3, Page 8.

	seconds, will SGX-DC accept or reject a trade within 60 seconds after it receives a trade to be compliant with the CFTC Regulations? Also, if a Clearing Member does not have fully automated systems and its trades cannot be accepted or rejected within 60 seconds by SGX-DC, would SGX-DC fail in its compliance as a DCO?
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Yours sincerely,  
**For the International Swaps and Derivatives Association, Inc.**

  
**Keith Noyes**  
**Regional Director, Asia Pacific**

  
**Cindy Leiw**  
**Director of Policy**