

## APAC Monthly Update

**January 2013**

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

### **Regulatory Activities**

#### **Asia Pacific:**

On January 10, ISDA sent a letter to Asian CCPs involved with clearing OTC derivatives. The purpose of the letter was to explain the extraterritorial implications of EMIR Article 25 and Section 5(b) of the Commodities Exchange Act. In the letter, ISDA highlighted the importance of Asian CCPs establishing dialogue with European/US regulators should they wish European/US person financial institutions to become clearing members of their clearing houses.

#### **Korea:**

On January 21, ISDA met with:

- Bank of Korea to discuss industry concerns with the BCBS-IOSCO "Proposed Margining of Uncleared Swaps.". ISDA explained the analysis it had conducted on the IM requirements and the impact that it might have on the cost of FX options and cross-currency swaps, important hedging products for Korea's real economy end users. ISDA also urged Bank of Korea, as co-chair of the Basel Emerging Market Committee, to make sure that committee members understand the proposals likely impact on emerging market economies.
- the Korean Financial Services Commission (FSC) to discuss central clearing in Korea. FSC advised that they expected the National Assembly to pass CCP-enabling legislation this February and that they would issue a consultation draft of the Enforcement Decree and FSC's CCP Regulations shortly after the bill is signed into law. ISDA reiterated the importance of CPSS-IOSCO compliance and the hope that FSC would be supportive of KRX opening a registration dialogue with US and European regulators.
- KRX to discuss their updated plans regarding clearing services for OTC derivatives.

### **Committee/Working Group Activities**

#### **North Asia L&R**

On January 29, ISDA held its North Asia L&R Members' meeting in Hong Kong. Topics discussed included the amended Securities Investment Funds Law in China, revision of the FX regulations for Qualified Foreign Institutional Investors by SAFE, HKMA's circulars on sale of investment products to corporate customers and applicability of SFC regulatory requirements to sale of structured products that are not regulated by SFO, Hong Kong trade reporting issues and the proposed new Credit Support Annex for Korean Won denominated securities. ISDA also updated members on the coming equity

documentation projects relating to Asia. Topics discussed regarding South East Asian included on-boarding of CCIL's FX forward segment, the publication of the Final GAAR Report, the RBI's Revised Guidelines on Credit Default Swaps for Corporate Bonds, the ISDA Survey on bilateral netting for regulatory capital purposes in India, the coming into force of the Capital Markets and Services (Amendments) Act 2012 and Guidelines on Sales Practices on Unlisted Capital Markets Products in Malaysia, the SGX-DC announcement that it is a Qualifying CCP, ISDA's submission to the MAS on the Proposed Amendments to the Monetary Authority of Singapore Act and MAS's Consultation Paper on Draft Regulations for Trade Repositories and Clearing Facilities Pursuant to the Securities and Futures Act.

### **South Asia L&R**

On January 31, ISDA held its L&R Members' meeting in Singapore. Topics discussed included an update on the on-boarding of CCIL's FX forward segment, the publication of the Final GAAR Report, the RBI's Revised Guidelines on Credit Default Swaps for Corporate Bonds, the ISDA Survey on bilateral netting for regulatory capital purposes and ISDA's trip to Mumbai in December and its various meetings with RBI. Also discussed was the coming into force of the Capital Markets and Services (Amendments) Act 2012 and Guidelines on Sales Practices on Unlisted Capital Markets Products in Malaysia, the Malaysian Financial Services Bill, Islamic Financial Services Bill and amendments to the Central Bank of Malaysia Act, the SGX-DC announcement that it is a Qualifying CCP, ISDA's submission to the MAS on the Proposed Amendments to the Monetary Authority of Singapore Act, MAS's Consultation Paper on Draft Regulations for Trade Repositories and Clearing Facilities Pursuant to the Securities and Futures Act. ISDA's trip to Seoul in January, the new Working Group on rehypothecation of Korean Won denominated securities and ISDA's letter to Asian CCPs on the extraterritorial implications of EMIR Article 25 and Section 5(b) of the Commodities Exchange Act (as amended by the Dodd-Frank Act). The meeting also discussed developments relating to the Dodd-Frank Act, including the CFTC's Final Exemptive Order on the Cross-Border Application of the Swaps Provisions of the Dodd-Frank Act and the various No-Action Letters issued by the CFTC in December.

### **Operations/Market Infrastructure**

On January 10, ISDA held its APAC Interest Rates Derivatives Operations Working Group meeting to discuss the addition / amendment of floating rate options / matrices, the status of electronically confirming certain products, the Calculation Agent mechanism for NDS, the confirmation template for compounding and in-arrears Asian NDS. A subgroup was also setup to discuss the structured rate mechanism.

On January 17, ISDA held its APAC Equity Derivatives Operations Working Group meeting to brief members on the latest confirmation template development for Asian products. The group also discussed the AEJ reference price source matrix and the eligibility in confirming certain products via an electronic confirmation platform. On the same day, ISDA also held its APAC Portfolio Reconciliation Sub Group meeting to discuss the latest portfolio reconciliation requirements in US and Europe

On January 18, ISDA held its APAC Implementation Group meeting to discuss the HK, Australia and Singapore trade reporting development. A subgroup was also set up to meet weekly to discuss regional trade reporting developments.

On January 25 and 29, ISDA held its APAC Trade Reporting Sub Group meetings to discuss the HK trade reporting matters.

On January 30, ISDA arranged a demo of DTCC regulatory portal (a portal for regulators globally to access data within the Global Trade Repository operated by DTCC) for its members.

## **Member Activities**

### **Asia Pacific:**

On January 11, ISDA organized a call for Asia-based members in which Davis Polk explained the implications of the CFTC Cross-border Exemptive Order.

### **Korea:**

On January 21, ISDA held its biannual Korean Members Meeting in Seoul. Topics discussed at the meeting included the proposed new Credit Support Annex for Korean Won denominated securities, the KRX central clearing proposal and ISDA's letters to Asian CCPs on EMIR and CEA extraterritoriality issues. ISDA also briefed members on the latest developments of the EU and US regulatory reforms including CFTC's Further Proposed Guidance on the Cross-Border Application of the Swaps Provisions of the Dodd-Frank Act, the Final Exemptive Order on the Cross-Border Application of the Swaps Provisions of the Dodd-Frank Act and a series of no-action letters issued by CFTC in December 2012.

## **Regulatory Developments**

### **China: SAC regulation for securities companies' OTC trading**

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On December 21, 2012, the Securities Association of China (SAC), a self-regulatory organization issued the Regulation of Securities Company's Over-the-Counter Trading Business (only Chinese is available). "OTC trading" is defined under the Regulation as (i) trading carried out between a securities company and its counterparty on a market other than a centralized exchange, or (ii) services provided by a securities company to investors in relation to transactions effected on a market other than a centralized exchange.

The products subject to the Regulation include any underlying or derivative financial products which have been approved, authorized by or filed with the relevant regulatory authority and are issued or sold outside a centralized exchange. A security company conducting OTC trading with counterparties must hold a proprietary securities trading license, and a securities company which provides services to investors in relation to OTC trading must hold a securities brokerage license.

The Regulation also provides that securities companies should comply with the relevant SAC documentation requirements when trading OTC financial derivatives. Securities companies are required to file an application with SAC before commencing OTC trading, and afterwards, monthly and annual reports on its OTC trading business. SAC will supervise and regulate the OTC trading business of securities companies. According to SAC, securities companies' OTC market is designed to be a platform for issuance, transfer and trading of privately offered products and investors will mainly be institutional. To start with, the market will mainly focus on wealth management products issued by securities companies and distribution of financial products. According to news reports in China, seven domestic securities companies have been approved to conduct OTC trading.

### **Hong Kong: HKMA consults on framework for revised LCR**

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

On January 17, the Hong Kong Monetary Authority (HKMA) released a memo on the revisions to the Liquidity Coverage Ratio (LCR). As Basel recently issued its full text with some changes from the original version published in 2010, the HKMA plans to develop, with industry consultation, a framework for local implementation of the revised LCR. Some issues under consideration include:

- Two-tiered approach: HKMA still maintains the view of adopting a two-tiered approach for Hong Kong banks. Under this approach, only Authorized Institutions (AIs) considered at the core of the local banking system will be subject to the LCR. All other AIs will be subject to a modified version of the existing Liquidity Ratio (LR);
- Phase-in of the LCR:HKMA is considering the BCBS phase-in arrangement and assessing the need to adhere to the original timetable;
- Level 2B Assets: HKMA will be examining the attributes of Level 2B assets to determine their level of liquidity in times of market stress. Specific focus will be placed on assessing the price volatility and market liquidity of these assets based on their historical performance in the local markets in times of stress as well as the potential for incentivizing banks to assume more proprietary risk through increased holdings of particular asset classes;
- Usability of High Quality Liquid Assets (HQLA) in times of stress: HKMA will incorporate into their rules the flexibility of banks to use their HQLA, even to the extent of causing their LCR to fall below the minimum requirement during a period of financial stress. HKMA will develop supervisory guidance to set out the circumstances under which such usage may be allowed and the considerations underlying HKMA's supervisory response in such circumstances;
- Use of alternative liquidity approaches (ALA): As there is limited supply of HQLA denominated in Hong Kong dollars. There are three ALA options, however, HKMA is most likely to adopt the second ALA option, i.e., the use of foreign currency HQLA to cover local currency liquidity needs for banks subject to the LCR;
- Implications for the modified LR (MLR) regime: HKMA will be reviewing the implementation timetable of the MLR and how this would be affected if a decision is made to phased-in the LCR. Further deliberation is required particularly in areas in which the LR adopts a more stringent approach than the LCR;
- Update of LM-2: In addition to meeting the LCR, banks will need to adhere to the enhanced liquidity standards set out in the BCBS Principles for Sound Liquidity Risk Management and Supervision. These Principles have been incorporated into the HKMA's Supervisory Policy Manual (LM-2) which will be updated later in the year.

## **India:**

### **RBI revised corporate bonds CDS guidelines**

*Contact: Jacqueline Low (jlow@isda.org) / Cindy Leiw (cleiw@isda.org)*

On January 7, RBI issued a Revised Guidelines on Credit Default Swaps (CDS) for Corporate Bonds. The changes to the guidelines are as follows:

- In addition to listed corporate bonds, unlisted but rated corporate bonds for issues other than infrastructure companies will be permitted;
- Users will be allowed to unwind their CDS bought position with original protection seller at a mutually agreeable or FIMMDA price. If no agreement is reached, then unwinding will be done with original protection seller at FIMMDA price;
- CDS will be permitted on securities with original maturity up to one year like commercial papers, certificates of deposit and non-convertible debentures with original maturity less than one year as reference/ deliverable obligations.

## **Draft guidelines on capital requirements for bank exposures to CCPs**

*Contact: Jacqueline Low (jlow@isda.org) / Cindy Leiw (cleiw@isda.org)*

RBI issued draft guidelines on Capital Requirements for Bank Exposures to Central Counterparties. The present framework assigns a risk weight of 0% for counterparty credit risk to a central counterparty (CCP). A credit conversion factor (CCF) of 100% is applied to the securities posted as collateral with the CCP and the resultant off-balance sheet exposure will be assigned a risk weight according to the ratings of the CCP. However, the Clearing Corporation of India Limited (CCIL) is assigned a 20% risk weight. The deposits kept by banks with the CCP will attract a risk weight appropriate to the rating of the CCP.

The proposed RBI guidelines differ from the Basel Committee on Banking Supervision (BCBS) interim framework in the following ways:

- The RBI capital framework considers a CCP a financial institution while the BCBS framework does not.
- If a bank is a clearing member (CM) of a qualifying CCP (QCCP), a risk weight of 2% applies to its trade exposures to the CCP. This exposure amount is calculated using the Current Exposure Method (CEM) only.
- In the case of CCIL, banks may calculate its total replacement cost on a net basis. All other CCPs will calculate their total replacement cost on a gross basis.
- A CM exposure to clients is treated as a bilateral trade. However, under the BCBS framework, in addition to the CM exposure being treated as a bilateral trade, a margin period of risk is calculated by multiplying the exposure at default (EAD) by a scalar of no less than 0.71 if a bank adopts either the CEM or the Standardized Method.
- Where a bank is a client of the CM, the client's exposures to the CM will be capitalized as its exposure (including potential CVA risk exposure) to the CM as bilateral trade. The BCBS framework allows a bank, as a client of a CM, to attain a 2% risk weight subject to certain conditions or a 4% risk weight under certain conditions.
- For collateral that is held by the CCP on a client's behalf and not held in a bankruptcy remote matter from the CCP, the relevant risk weight of the CCP will apply to the collateral posted. The risk weight for such a scenario under the BCBS framework will be 2% or 4% under certain conditions.
- A CM bank may apply a risk weight of 1111% to their default fund exposures to a QCCP, subject to an overall cap on the risk-weighted assets from all its exposures to the CCP equal to 20% times the trade exposures to the CCP. The risk weight is 1250% under the BCBS framework. The BCBS framework uses Method 1 and Method 2 to calculate the default fund exposures, as opposed to RBI which only uses Method 2.
- Banks must apply a risk weight of 1111% to their default fund contributions for a non-QCCP. The BCBS framework applies a 1250% risk weight to non-QCCP default fund contributions.
- In the case of CCIL, when a bank applies the Standardized Approach to calculate its trade exposure to a non-QCCP, a risk weight of 20% will be applied. Under the BCBS framework, the risk weight applied using the Standardized Approach will be according to the credit rating of the non-QCCP.

Submission deadline is January 31.

### **RBI standardizes IRS contracts**

*Contact: Keith Noyes (knoyes@isda.org) / Jacqueline Low (jlow@isda.org)*

On January 28, RBI issued a circular on the Standardization of Interest rate Swap (IRS) Contracts, which aims to facilitate central clearing and settlement of IRS contracts in the future and to improve tradability. FIMMDA will prescribe the terms of minimum notional principal amount, tenors, trading hours, settlement calculations etc., in consultation with market participants. Standardization will be mandatory for INR Mumbai Inter Bank Offer rate (MIBOR) Overnight Index Swap (OIS) contracts and for all IRS contracts other than client trades. All new INR MIBOR-OIS contracts executed from April 1 onwards will need to be standardized.

### **Malaysia: Capital Markets and Services Act, sales practices guidelines**

*Contact: Jacqueline Low (jlow@isda.org) / Erryan Abdul Samad (eabdulsamad@isda.org)*

On January 2, Securities Commission Malaysia (SC) announced the coming into force of the Capital Markets and Services (Amendment) Act 2012. The SC also issued relevant guidelines and FAQs on the Act. These amendments were passed by Parliament in April 2012 and came into effect on December 28.

The Act introduces a new approval framework intended to facilitate the offering of a broader array of capital market products and distinguishes between listed and unlisted. The definition of “capital market products” has been amended and includes, among others, derivatives and any product or arrangements which is based on securities or derivatives or any combination thereof. The Act also provides that the authorization of the SC is required for an unlisted capital market product or in the case of a foreign capital market product, recognition by the SC.

The SC also issued Guidelines on Sales Practices on Unlisted Capital Market Products which will govern all capital market products that are not listed on a stock exchange or derivatives exchange in Malaysia, regardless of whether they are manufactured within or outside Malaysia. The Guidelines require, among others, that a Product Highlights Sheet be prepared providing the salient information of an unlisted capital market product and a Suitability Assessment be conducted to ensure that the product recommendation provided by a product distributor is made on a reasonable basis. Additionally, the Guidelines include principles on treating investors fairly which require that product issuers and product distributors have in place certain policies and processes that give due regard to the interests of the investors.

Schedule 1 of the Guidelines sets out the different categorization of investors according to certain specified qualifying criteria. The requirements relating to Product Highlights Sheet and Suitability Assessment in the Guidelines will apply to all retail investors and high net-worth individuals. These requirements will also apply to high net-worth entities, unless they opt out. They will not however apply to accredited investors. The principles on treating investors fairly in the Guidelines will apply to all categories of investors.

The SC also released the Guidelines on Private Debt Securities, the Business Trusts Guidelines, the Guidelines on Sukuk, the Guidelines on Real Estate Investment Trusts, the Guidelines on Unlisted Capital Market Products: Structured Products and Unit Trust Schemes and the Prospectus Guidelines.

### **Philippines: BSP issues the Basel III implementing guidelines**

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

On December 26, the Monetary Board (MB) approved the implementing guidelines for the January 1, 2014 adoption of the revised capital standards under the Basel III Accord. Bangko Sentral Ng Pilipinas (BSP) maintained the minimum Capital Adequacy Ratio (CAR) at 10%. The revised Common Equity

Tier 1 (CET1) will be 6% and the Tier 1 ratio will be at a minimum of 7.5%. The new guidelines also introduce a capital conservation buffer of 2.5%, which will be comprised of CET1 capital. Banks that have issued capital instruments from 2011 will be allowed to count these instruments as Basel III-eligible until end-2015.

**Singapore:**

**MAS consults on amendments to MAS Act**

*Contact: Jacqueline Low (jlow@isda.org) / Cindy Leiw (cleiw@isda.org)*

On December 26, MAS issued a consultation paper on Proposed Amendments to the MAS Act regarding the Resolution of Financial Institutions. In the paper, MAS proposes expanding the existing resolution regime applicable to banks and insurers to a wider group of financial institutions. MAS also proposes to adopt some of the recommendations made by the Financial Stability Board in its Key Attributes of Effective Resolution Regimes for Financial Institutions document and to enhance MAS' powers to issue directions. Submission deadline is January 12.

**MAS seeks comments on draft regulations for trade repositories and clearing facilities**

*Contact: Keith Noyes (knoyes@isda.org) / Jacqueline Low (jlow@isda.org)*

MAS issued a Consultation Paper on Draft Regulations Pursuant to the Securities and Futures Act for Trade Repositories and Clearing Facilities. The Paper relates to the new Part IIA and Part III of the Securities and Futures Act (Cap. 289) (SFA), which was introduced by the Securities and Futures (Amendment) Act 2012 (SF(A)A 2012) that was passed in Parliament on November 15.

- The Securities and Futures (Trade Repositories) Regulations 2013 (SF(TR)R) (at Annex 1) will operationalize the Part IIA of the SFA, which provides for the regulation of licensed trade repositories (LTR) and licensed foreign trade repositories (LFTR). The SF(TR)R sets out requirements on the admission of trade repositories as LTRs or LFTRs, as well as the ongoing requirements on LTRs and LFTRs.
- The Securities and Futures (Clearing Facilities) Regulations 2013 (SF(CF)R) (at Annex 2) will repeal and replace the Securities and Futures (Clearing Facilities) Regulations 2005. The SF(CF)R will operationalize the new Part III of the SFA, which provides for the regulation of approved clearing houses (ACH) and recognized clearing houses (RCH). Similar to the SF(TR)R, the SF(CF)R sets out requirements on the admission of persons operating clearing facilities as ACHs or RCHs, as well as the ongoing requirements on ACHs and RCHs.
- In addition, the Securities and Futures (Clearing Facilities) (Transitional and Savings Provisions) Regulations 2013 (at Annex 3) will provide for the transition of existing persons operating clearing facilities to the new regulatory regime.

The SF(A) Act 2012:

- introduced a new regulatory regime for trade repositories;
- extended the regulatory regime for clearing facilities to OTC derivatives; and
- modified the regulatory regime for clearing houses.

Submission deadline is February 8.

## **MAS monograph on Supervision of Financial Market Infrastructures**

*Contact: Keith Noyes (knoyes@isda.org) / Jacqueline Low (jlow@isda.org)*

On January 14, the Monetary Authority of Singapore (MAS) issued a monograph on Supervision of Financial Market Infrastructures in Singapore. This monograph updates and replaces the monograph on MAS' Roles and Responsibilities in Relation to Securities and Clearing and Settlement Systems in Singapore issued in 2004; and complements earlier MAS monographs which set out MAS' overall approach to financial supervision.

The monograph sets out MAS' adoption of the CPSS-IOSCO Principles for Financial Market Infrastructures (PFMI) issued in April 2012. The PFMI sets the benchmark for the supervision of financial market infrastructures (FMIs) and are expressed as broad principles. FMIs are infrastructures that facilitate the clearing, settling or recording of payments, securities, derivatives or other financial transactions. In Singapore, FMIs are currently:

- Payment Systems comprising systemically important payment systems (SIPs) and system-wide important payment systems (SWIPs);
- SIPs: MAS Electronic Payments Systems (MEPS+);
- SWIPs: SGDCCS, USDCCS and IBG systems, operated by Singapore Automated Clearing House (the SACH systems);
- NETS Electronic Fund Transfers at Point of Sale (EFTPOS);
- Capital Market FMIs comprising central securities depositories (CSDs), securities settlement systems (SSSs), central counterparties (CCPs) and trade repositories (TRs)
- The Central Depository (Pte) Limited (CDP);
- Singapore Exchange Derivatives Clearing Limited (SGX-DC);
- Singapore Mercantile Exchange Clearing Corporation (SMXCC).

All SIPs, SWIPs, CSDs, SSSs, CCPs and TRs in Singapore are expected to comply with the PFMI. In summary, the Monograph:

- sets out MAS' supervisory objectives of safety and efficiency. To achieve these objectives, MAS monitors and assesses existing and new FMIs to ensure that FMIs have proper structures, processes and rules in place;
- introduces the regulatory framework for supervision of FMIs. MAS' powers for supervision of FMIs are derived from the Payment Systems (Oversight) Act (PS(O)A) and the Securities and Futures Act (SFA);
- articulates MAS's supervisory approach with respect to FMIs.

MAS may impose higher or more specific requirements on FMIs, as appropriate, in the context of specific risks, or in the context of wider financial stability.

Where relevant and practical, MAS also seeks to participate in the cooperative oversight of cross-border or multi-currency FMIs which may affect the stability of the financial system of Singapore. Presently, the Continuous Linked Settlement (CLS) is subject to cooperative oversight by MAS. CLS is the cross-border payment system that settles foreign exchange transactions for the major currencies on a payment-vs-payment (PVP) basis.

## **Thailand: BOT issued notification on Basel III capital framework**

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

On December 14, the Bank of Thailand (BOT) issued a notification on capital adequacy framework under Basel III. Thai banks will be required to maintain a minimum Common Equity Tier 1 (CET1) ratio of 4.5%, Tier 1 capital ratio of 6% and Total capital ratio of 8.5%, the latter of which remains unchanged from the Basel II ratio. Under the new Basel III capital framework, foreign bank branches will now be required to maintain a Total capital ratio of 8.5%, which is in line with the Thai banks. The new requirement became effective on January 1. BOT will assess the developments and impact studies on the Leverage ratio and Liquidity risk framework before adoption in Thailand.

## **Submission**

On January 12, ISDA made submission to Monetary Authority of Singapore (MAS) regards to Consultation Paper on Proposed Amendments to the Monetary Authority of Singapore Act. This submission is not yet public.

On January 29, ISDA made submission to Hong Kong Monetary Authority and Securities and Futures Commission regards to the “originate or execute” definition in the consultation paper on the proposed regulatory regime for the over-the-counter derivatives market in Hong Kong. This submission is not yet public.

## **Upcoming committee and working group meetings/conferences**

### **Meetings:**

APAC Legal Advisory Group Meeting	Feb 5
APAC IRD Operations Meeting	Feb 19
North Asia L&R Meeting	Feb 26
South Asia L&R Meeting	Feb 28
APAC Credit Operations Meeting	Feb 28

### **Conferences:**

Extra-Territoriality in International Derivatives Regulation and Singapore's Changing Regulatory Landscape for OTC Derivatives - Singapore	Feb 27
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## **ISDA APAC Monthly Update**

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