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26 March 2012

Re: Consultation Paper on Proposed Regulation of OTC Derivatives (P003 – 2012, Feb 2012)

The Global Foreign Exchange Division (GFXD) of the Global Financial Markets Association (GFMA) welcomes the opportunity to comment on behalf of its members on the consultation paper issued by the Monetary Authority of Singapore (MAS). The GFXD was formed in co-operation with the Association for Financial Markets in Europe (AFME), the Securities Industry and Financial Markets Association (SIFMA) and the Asia Securities Industry and Financial Markets Association (ASIFMA). Its members comprise 22 global FX market participants[1], collectively representing more than 90% of the FX market[2]. Both the GFXD and its members are committed to ensuring a robust, open and fair market place and welcome the opportunity for continued dialogue with Global regulators.

The FX market is the world's largest financial market. Effective and efficient exchange of currencies underpins the world's entire financial system. Corporations and investors regularly participate in the market for operational needs: to reduce risk by hedging currency exposures; to convert their returns from international investments into domestic currencies; and to make cross-border investments and raise finance outside home markets.

Many of the current legislative and regulatory reforms will have a significant impact upon the operation of the global FX market and we feel it is vital that the potential consequences are fully understood and that new regulation improves efficiency and reduces risk, not vice versa. The

[1] Bank of America Merrill Lynch, Bank of New York Mellon, Bank of Tokyo Mitsubishi, Barclays Capital, BNP Paribas, Citi, Credit Agricole, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, JP Morgan, Lloyds, Morgan Stanley, Nomura, RBC, RBS, Société Générale, Standard Chartered Bank, State St., UBS, and Westpac
[2] According to Euromoney league tables

GFXD is committed to ensuring a robust, open and fair market place and welcomes the opportunity to set out its views in response to your consultation paper.

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1. Proposal for Expanding the Scope of the SFA to Regulate OTC Derivatives

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

The proposal to define derivative contracts to include asset classes such as FX is generally consistent with the approach taken in a number of other jurisdictions. However, as noted in our responses below, there are products within the foreign exchange asset class, specifically FX forwards and FX swaps which should be appropriately exempted from most, but not all (e.g., still reporting to a trade repository), regulatory requirements that will apply to derivative contracts.

In defining derivatives transactions we would welcome clarification that spot trades are excluded from this definition. Accordingly and consistent with common market definitions, practice and understanding, transactions with value dates less than or equal to T+2 business days should therefore be excluded.

FX trades also act as supporting trades for security settlements, which may occur on a greater than T+2 basis. Such supporting transactions, up to the standard security settlement maturity in the relevant currency and market, which may be up to T+5, should be excluded from the scope of the rules.

Question 2: MAS seeks views on (i) the proposal to adopt top-down and bottom-up approaches to identify products suitable for mandatory central clearing; (ii) the proposed criteria (paragraph 3.1.4) for determining whether a product is suitable for mandatory central clearing by a CCP; and (iii) the feasibility of mandating central clearing for SGD IRS, USD IRS, and NDFs in selected Asian currencies.

The proposal to adopt top-down and bottom-up approaches to identify products suitable for mandatory central clearing is generally consistent with the approaches taken in a number of other jurisdictions, as are the proposed criteria for determining whether a product is suitable for mandatory clearing by a CCP. We believe, however, that it is important to consider the following additional criteria/factors within these processes:

- *Specific documentation / additional information requirements for CCPs to assist MAS.* To assist in the MAS's review of a product's suitability for mandatory clearing, we urge the MAS to require specific information from the CCP on the end-to-end testing conducted with its clearing members for that market. For example, in the case of FX derivatives, specific information should be required on:

    i. the scenario analyses / stress testing performed by the CCP, the default management processes for the CCP and resulting impact on the underlying liquidity in the FX product(s) that the CCP clears or plans to clear, and the arrangements in place to address management of sovereign risk events (e.g., suspension of trading, sovereign default, unexpected bank holiday or other significant disruption to valuation, payment or settlement processes; and

ii. the level of disclosure provided by the CCP to the central banks of the relevant currencies on its clearing of FX products, including but not limited to the information outlined in (i) above, and a summary of any views expressed by the central banks to this information.

Because the FX market is a central component of the global payment system, central banks have expressed a need to understand and evaluate the impact of clearing by CCPs, individually and collectively, on the FX market from a broad policy perspective.

- *More granular grouping of OTC derivatives within product types.* Careful consideration needs to be given to the "grouping" of products within each asset class, as a one size fits all approach is inappropriate for determining whether derivative contracts should be mandatorily cleared. Additionally, the MAS should have the ability to subdivide a CCP's submission for review. We firmly believe that appropriateness for mandatory clearing is likely to depend on the characteristics of each of the different underlying products within each asset class. FX products are not homogenous, and the possibility of different trade features requires that each currency pair should be reviewed and separately approved. In particular, liquidity by currency pair varies significantly. We believe that clearing is only warranted for the most liquid currencies that offer a material reduction in replacement risk across the market. As CCP's launch additional products, we believe that the MAS should give each new product due and careful consideration to ensure that any mandatory clearing is warranted. Approving FX derivative contracts (e.g., FX non-deliverable forwards (NDFs)) by currency pair will also enable consideration of the pace of development at competing CCPs to ensure market participants have a choice of venues to ameliorate systemic risk and encourage competition.

Scope of products covered by clearing

Whilst we note that the paper only refers to clearing of certain Asian NDF products, we wished to make the following comments in regard to clearing of FX options should they be considered at a later stage.

As we set out in the rationale for excluding FX forwards and swaps from central clearing (see Q3 and Appendix A) settlement risk is the main risk in the FX market because of the physical exchange of currencies upon maturity. CLS Bank has long been identified as a critical part of the solution to enable the market to function as a payment versus payment market.

Current proposed principles for financial market infrastructure issued by BIS in conjunction with CPSS/IOSCO in March 2011[3] lay out a number of key principles that need to be considered for CCPs in the FX market. The industry has been focused on these principles over the past twelve months in the context of FX Options. Notable are Principle 7 – Liquidity Risk, Principle 8 – Settlement Finality, and Principle 12 – Exchange-of-Value settlement systems. Taken as a whole, and confirmed through our conversations with key regulatory oversight groups, it is our understanding[4] that these principles require any CCP looking to clear FX products to meet fully the following requirements:

- An FX CCP will need to guarantee the full settlement of currencies of the trade[5];
- An FX CCP must be able to deliver required currency at the latest by the end of the settlement day; and
- An FX CCP must be covered against Settlement Halt Risk[6].

The FX industry has been working with regulators and CCPs and is acutely aware that to meet these requirements for the mainstream FX market a CCP would face significant challenges. This is especially true in light of the need for immediate access to sufficient liquidity in all currencies to be able to meet in full the settlement obligations of a defaulting member, and in a manner that does not put the CCP itself at significant risk during stressed market conditions. The specific settlement characteristics of the FX market make this issue significantly more acute than in other asset classes. This is a formidable challenge for which, to date, no satisfactory solution has been found.

Introducing CCPs into the FX market without ensuring that they only bear risks that they can properly manage would clearly increase, rather than decrease, potential systemic risk, especially in times of crisis.

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

We strongly agree and support the proposal to exempt FX forwards and FX swaps from the clearing obligation. International convergence is paramount for FX forwards and FX swaps where the predominant risk is settlement risk. Following extensive study of settlement risk by the central banks as a source of systemic risk for the FX market and therefore the global financial markets, the FX market went to considerable lengths to address this risk, ultimately leading to the creation of CLS Bank (CLS) in 2002. CLS's settlement system today eliminates virtually all settlement risk to its participants. Additionally, CLS's activities are subject to a

[3] CPSS Technical Committee of the International Organization of Securities Commissions, "Principles for financial market infrastructures", Bank for International Settlement IOSCO, Consultative Report March 2011.

[4] See Global FX Division Discussion Document at http://www.afme.eu/AFME/What_We_Do/FX%20Clearing%20Settlement%20Challenges%20Discussion%20Document%201%203.pdf

[5] This applies to the vast majority of FX trades where settlement is via exchange of principal; clearly it does not apply to FX trades involving non-deliverable contracts, e.g. NDFs

[6] This is the potential risk of mark to market loss on settlement day if settlement is halted intra-day and therefore not all trades settle (NB: this is different from FX settlement risk).

cooperative oversight protocol arrangement among 22 central banks whose currencies are settled.

The addressing of the key risk – settlement risk – through CLS mitigates by far the majority of the risk present in an FX trade. Extending the scope of regulation (particularly as regards clearing) to include these trades would be a disproportionate. We have expressed this position to other international regulators and the different characteristics of the FX asset class and its products has been acknowledged in both legislation and consultation in a number of international jurisdictions including the US, Europe, Hong Kong and Australia. As the MAS notes in its consultation paper, this proposed exemption in Singapore is in line with the US's proposed determination to exclude FX forwards and swaps from the mandatory clearing and trading requirements under Dodd Frank. We include in Appendix A some further background on our rationale for viewing FX products differently but would be happy to discuss this in more detail.

We wish to draw the MAS's attention to the fact that under Dodd-Frank, the US Treasury determination regarding FX forwards and FX swaps would have the effect of excluding these products from the definition of "swaps" (effectively the equivalent of "derivative contracts" in Singapore). As a result, FX forwards and FX swaps would not only be exempt from mandatory clearing or trading requirements, but also any mandatory margin requirements that may apply to "uncleared swaps". We agree with and support this approach as it allows for a more dynamic risk assessment. Notwithstanding these exemptions, the obligations to report such products a trade repository and to comply with business conduct rules would of course apply.

We also note that the Singapore Foreign Exchange Market Committee (SFEMC) does not class either Foreign Exchange Outright Forwards or Foreign Exchange Swaps as derivatives in the October 2011 Survey tables.

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

No comment.

Question 5: MAS seeks views on the proposed scope of entities to be subject to clearing obligations and on the factors to be taken into account when determining the clearing thresholds.

It is our view that regulators should focus on the systemic risk arising from a participant's use of instruments. Where an end-user does not pose a material risk, it would be proportionate to exempt that end-user from mandatory clearing and capital, margin and / or collateral requirements.

Affordable access to appropriate methods of hedging is vital to end-users to mitigate risks. We therefore support an approach that exempts certain classes of participants from any clearing and margin requirements, as the increased collateral and operational requirements would be too burdensome and the reduction in systemic risk is insufficient to justify the imposition of these costs. OTC positions which are hedges of business risk should be exempt from any central clearing or margin obligations. Any mandatory clearing requirement would affect end-users' ability to use derivatives for risk management purposes as many of these firms, especially non-financial end-users, need their most liquid assets for working capital and investment purposes.

Dealers facing end-users that do not pose a threat to financial stability should be permitted to evaluate and underwrite the credit risk of such end-users and negotiate bilateral collateral or credit support arrangements as they deem necessary.

These issues are particularly pertinent for the FX market, which differs from the OTC derivative markets in that it has many more participants and transactions that will be affected and is predominantly very short dated. The impact of disproportionate mandatory clearing and margin / collateral requirements will therefore be felt widely.

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

No comment.

Question 7: MAS seeks views on: (i) the proposal to exempt intra-group trades of both financial and non-financial entities from the clearing obligation but subject these trades to appropriate collateralisation requirements; (ii) whether such a proposal would pose any implementation issues; and (iii) whether there are other appropriate risk mitigating measures, apart from subjecting the exempt intra-group trades to collateralisation requirements.

We believe that trades that settle with affiliated third parties (intra-group transactions) should be out of scope of the regulation.

Inter-affiliate trades represent allocation of risk within a corporate group and do not give rise to the same systemic risk issues that are raised by trades by one corporate group with another. Many millions of trades occur daily between different affiliates of the same institution which are not relevant to that institution's external market positioning. They are a common feature of international financial markets and enable clients to deal with local entities whilst providing those firms with the ability to manage risk in a consolidated way. Regulators are able to consider a firm’s consolidated risk position, the need for which is acknowledged in the consultation paper.

Unlike other asset classes, the FX market is characterised by a high number of both trades and participants. A clearing requirement for intra-group transactions would increase operational risk due to the volumes of transactions that would clear, without materially reducing counterparty risk. Similarly, a reporting requirement for these intra-group trades would significantly increase ticket volumes at any trade repository without increasing transparency and without giving meaningful indications about the overall FX market or the overall exposure of the relevant corporate group.

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

No comment.

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

We agree with and support the proposal not to require central clearing through only domestic CCPs. As the MAS acknowledges in the consultation paper, any mandate to clear through domestic CCPs only could limit choices for market participants, lead to fragmentation of liquidity, reduce netting benefits and increase costs.

One major factor underpinning significant advances in the efficiency and effectiveness of the global FX market over recent years has been the ability to trade FX contracts seamlessly and fungibly, regardless of geography or time zone. This has helped bring about very high levels of market transparency and straight through processing efficiency. There is clearly a risk that new regulatory regimes might impair this global efficiency by imposing new restrictions on who can trade with whom and under what conditions.

In the FX market a significant proportion of business is transacted between counterparties in different jurisdictions, sometimes in currencies that are foreign to both counterparties (e.g. a Singapore and a UK counterparty executing a JPY-EUR trade). In order to mitigate potential cross-jurisdictional conflicts, recognition should be granted to FX CCPs meeting appropriate standards. This would allow parties to the trade to agree between themselves where the contract should be cleared, with the following benefits:

- This avoids potential conflict where each counterparty would be required to clear the same trade in a different jurisdiction.
- It allows counterparties to select the CCP that is most efficient in terms of cost and collateral efficiency for that trade (e.g. where there are offsetting positions).

The worst case would be for each jurisdiction to mandate use of local CCPs, which (a) would lead to an unnecessary proliferation of CCPs in each asset class and (b) would likely lead to each major participant having to set up new legal entities within each jurisdiction, especially for FX as it is ubiquitous. This would significantly diminish the efficiency of the global FX market, the cost of which would be felt as much by end users as by market professionals. For smaller jurisdictions, the effect may be to restrict the access of local participants to the global FX market, increasing costs for the local participants and making the jurisdiction a less attractive centre for global businesses.

Finally, it is important to note that, unlike most financial derivatives, the fundamental asset being exchanged in most FX transactions is sovereign currency *per se*, and this is often the sovereign currency of a third country and is therefore of significant interest to the third country's central bank. CLS provides an exemplary model whereby regulation of the market infrastructure is lead by one central bank (the Federal Reserve) and additional oversight is provided by the central banks (e.g., the MAS) whose currencies are settled in CLS under a cooperative framework amongst the central banks. This aspect should be considered with respect to FX clearing policy, including whether such a governance model would be appropriate.

Question 10: MAS seeks views on: (i) the proposal to require backloading of outstanding derivative contracts with remaining maturity of more than one year; and (ii) any potential implementation challenges in requiring backloading of outstanding derivative contracts.

We do not support the proposal to require backloading of contracts with maturities of greater than one year.

Such contracts would not have been priced to factor in the costs of clearing fees and funding initial margin. Because clearing changes the fundamental nature of the cash flows of the trade, they may render such contracts no longer commercially viable even though they were viable at the time the deal was struck. We also note that since the average tenor of an FX trade is significantly less than one year, the risk reduction achieved from a backloading requirement would be minimal.

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

An orderly and efficient transition of the OTC derivatives market to the new market structure and regulatory regime required by financial reform in Singapore and other jurisdictions is critical. We agree that a phased approach to extending any of the mandatory obligations is sensible to limit implementation risks.

Overview and current FX industry initiatives.

The GFXD welcomes the goals of enhancing regulatory oversight and promoting greater transparency. GFXD members announced last year their recommendation to partner with DTCC and SWIFT to develop a global foreign exchange trade repository. This selection was the result of an open and transparent Request for Information (RFI) and Request for Proposal (RFP) process that began back in December 2010, with the RFP issued in April 2011.

The project has been running since August 2011 and work has covered key areas such as technology, connectivity, messaging, data formats and regulatory permissioning and access, amongst other areas. However, this, as with any other piece of regulatory infrastructure, must be developed in the context of various regulators' objectives.

There are a number of key benefits from implementing global trade repositories, rather than multiple, fragmented local repositories. Appendix B sets these out in greater detail but in summary they relate to comprehensive oversight and enhanced efficiency of data capture for both regulators and market participants alike. This is particularly the case for the FX market which is characterised by vastly higher number of transactions and participants when compared to other asset classes given its position as the basis of the global payments system.

Phasing by type of market participants

We suggest that phasing should occur by sub-categories of market participant. Hence the initial phase should focus on major / systemically important dealers, with subsequent phases dealing with other financial institutions and corporates (if not subject to an exemption).

Broader sequencing considerations

We believe the regulators should focus, and therefore prioritize, efforts on mandatory reporting. Once data begins to be compiled for FX, the MAS will be well-positioned to determine possible future appropriate regulatory policy based on analysis of actual market activity.

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

We agree with the proposal and welcome MAS's proposal to work closely with other regulators to obtain relevant information for entities that are non-resident or which do not have a presence.

Confidentiality

A number of jurisdictions, including Singapore, place restrictions on the trade details that may be reported to a trade repository. Reporting participants may therefore face legal conflicts arising from local data protection and client confidentiality laws. Whilst obtaining client consent may mitigate these issues, there is a risk that consent may not be forthcoming or that this maybe insufficient in certain jurisdictions.

We believe the appropriate course is for relevant local laws to be changed to allow disclosure of such details in specific circumstances to support data gathering by repositories, including through third party service providers. This provision is present in European legislation. Until such conflicts are resolved we urge MAS to provide appropriate exemptions where local confidentiality laws prohibit trade reporting. In the meantime, data may need to be submitted by masking certain trade details such as client names. Even in doing this, submitting firms may face legal and reputational risks.

Inter-affiliate trades

As per our response to question 7, we believe that inter-affiliate trades should be out of scope of the reporting requirements.

Question 13: MAS seeks views on: (i) the proposal to require reporting by all financial entities, as well as non-financial entities above a reporting threshold; and (ii) the proposal to determine the reporting threshold based on the asset size of the non-financial entity.

No comment.

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

We agree with the protocol for single-sided reporting but would suggest that the final rules need not be specific as to whether single-sided or dual-sided reporting be required other than to ensure that regulatory reporting is not duplicative.

Furthermore we welcome the acknowledgement by MAS that an entity may use a third party to report on its behalf (and this should include the other counterparty to any trade i.e. allowing a smaller corporate to designate its financial counterparty to report on its behalf). There are various scenarios that would make this beneficial. Non financial intermediaries executing a low-volume of trades (depending on where the relevant thresholds are set), for instance, may not have, or desire to build, the necessary infrastructure to fulfil the reporting requirements. Such participants may find the build-out costs to be prohibitive, or will prefer to avoid them. This will be particularly prevalent given the number of market participants in FX.

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

No comment.

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

Any trade repository must meet the needs of the multiple regulators that it serves. In order to do that, the GFXD and its members support the efforts being made across international forums to standardise both data formats and reporting requirements. Please refer to Appendix B for a summary of our rationale for supporting the adoption of international reporting and aggregation standards.

Given the cross-border nature of the FX market and the likely need for participants to report to multiple jurisdictions, we believe it is in the interests of regulators and participants alike to harmonise the data requirements on a global scale. Whilst we appreciate that regulators may have specific additional data requirements, agreed global data formats and standards for LEIs and product and trade identifiers will promote significant benefits for all users.

Where local repositories prevail, regulators will need to be able to interpret and aggregate data across a number of differently formatted outputs, which can be inefficient at best. Timely access to and interpretation of a comprehensive data set will be important in times of market crisis; this will be enhanced where regulators have access to consistent data sets if required to seek trade and position data from a number of repositories.

Harmonisation should extend to common definitions for each of the data items between regulators. This will help avoid confusion and allow for an international, standard reporting language (FPML) to be used. Otherwise participants may be required to persist and transmit two different elements for the same data field e.g. price.

Question 17: MAS seeks views on the adoption of an LEI and a product classification system aligned with international standards.

LEI

The industry strongly supports the use of LEI for the identification of counterparties and is awaiting approval from the global regulatory community under the auspices of the FSB. In order to provide transparency and allow for monitoring of systemic risk on a global basis, it is imperative that a standard is designed for global use.

We fully support the Financial Stability Board's (FSB) current LEI process and are actively involved through the Industry Advisory Panel. While we fully recognize and support that the FSB yet has to make recommendations on a global LEI standard and its implementation, we respectfully would like to draw your attention to the efforts of a coalition of global financial services trade associations and organizations (the 'Trade Associations') which have made the following recommendations for the LEI Solution Providers, which was originally released in July 2011:

- Standards body – The International Organization for Standardization, i.e., ISO's new standard, ISO 17442, is recommended for use as the new, authoritative legal entity identification standard.
- Core Issuing and Facilities Manager – The Depository Trust & Clearing Corporation (DTCC) and the Society for Worldwide Interbank Financial Telecommunications (SWIFT), along with DTCC's wholly-owned subsidiary AVOX Limited, are recommended as key partners to operate the core LEI utility as the central point for data collection, data maintenance, LEI assignment, and quality assurance.
- Federated Registration – ANNA, through its network of local national numbering agencies (NNAs), is recommended as a key partner in the solution for registering, validating and maintaining LEIs for issuers, obligors, and other relevant parties in their home markets. The NNAs are envisioned to serve as the "face" of the LEI Utility to those markets.

The Trade Associations believe that the LEI standard, and the issuance capability and management solution recommended by the industry can be implemented and available for use before January 2013, such that MAS and the other G20 countries can meet their G-20 commitments. We hope that this will allow MAS to recommend the use of the global LEI standard. If, however, the use of another code is required as an interim step, as a precautionary measure we would suggest providing for a 20 digit field identifier in the report formats to be able to accommodate the ISO LEI at a later date.

A timely approval by the regulatory community, which allows for sufficient implementation time, is one of the key challenges for the implementation of LEI.

Notwithstanding that the industry is looking to implement a solution for LEI by January 2013, the implementation presents some issues, particularly for FX given the breadth of market participants. It may take some time for all participants in the market to register, particularly smaller corporates. There is also likely to be a significant cost associated in registering all users of FX transactions. We believe that until such time as an appropriate LEI database is up and running and market participants have registered, MAS should allow participants to use a substitute counterparty identifier. The mandatory use of the LEI should be phased in by market participant within the FX industry type to support this, for example by large financial counterparties, other financial counterparties, non-financial counterparties.

Product classification

With regard to product classification, we support MAS's proposal to follow an industry developed product classification system. The GFMA Global FX Division is working closely with ISDA to develop approaches across asset classes for the industry. To the extent possible, we would urge consistency in approach and to that end would welcome early review by MAS in order to provide feedback and guidance to support global adoption.

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

In terms of the reporting deadlines to be implemented, we encourage global regulators to agree a standard end of day cut-off in order to allow coordinated timings for delivering data to regulators. This is particularly important for a globally traded market such as FX and would not only assist in meeting reporting deadlines but would enable firms to increase operational efficiency and implement consistent best practices across various reporting obligations.

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

No comment.

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

We agree with and support the proposal not to require reporting to domestic TRs only for the reasons noted in our response to question 11 above.

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

We agree with proposal not to impose a trading mandate at this stage. As noted in our response to question 11 above, we believe the regulators should focus, and therefore prioritize, efforts on mandatory reporting. Once data has been compiled for FX, the MAS will be well-positioned to determine, e.g., whether FX NDF products should be subject to mandatory clearing obligations *as well as* trading requirements. Mandatory trading on exchanges or other trading facilities is not a necessary condition for financial stability and could have a negative impact, for example, in reducing liquidity in the market where the mandatory trading rules apply.

The FX market has been at the forefront of electronic trading, developing a range of execution methods including multi-dealer and single dealer platforms. As an OTC marketplace, these venues take into account the specific nature of the end client, size of order and credit worthiness. The choice of venue for trading in OTC markets should be driven by both the type of contract and type of customer. Any requirements governing market structures and trading venues, to the extent that they are applicable, should preserve the flexibility that exists to trade across existing execution venues.

Mandatory trading obligations, depending on how they are applied, can restrict the ability of end-users to enter into hedging arrangements by forcing economic standardisation of products to fit e.g. an exchange-traded model. We are strongly against this since the main use of the OTC FX market is to allow users to hedge specific future exposures in a tailored manner.

Should a mandatory trading obligation be imposed at a future date, we believe MAS should consider single dealer platforms (SDPs) in the FX market as qualifying venues for such a trading obligation.

SDPs provide significant liquidity to the dealer-to-customer FX market (c. 25% of dealer-to-customer flows[7]), facilitating a direct trading relationship and promoting innovation and quality in executing client business. The model is highly competitive, providing end users with a variety of products based on their specific needs particularly given the bespoke hedging nature required for FX products. SDPs also enable clients to develop relationships that cover more than solely execution including research and advice.

The G20 commitment refers to moving trading in standardised OTC derivatives to exchanges or electronic trading platforms. SDPs, in our view, clearly qualify as electronic platforms and are referred to in the IOSCO Report on Trading of OTC Derivatives (the "Trading Report"), published in February 2011. The Trading Report does not make a clear recommendation as to whether SPDs should or should qualify as a venue for mandatory trading. However, certain IOSCO members recognised that *"benefits can be realised where the opportunity to seek liquidity and trade with multiple liquidity providers is offered within a product market as a whole, irrespective of whether a particular platform offers access to multiple liquidity providers"* further recognising that *"benefits of centralisation may differ according to market structure [and] that a market consisting of a mix of single and multi-dealer platforms for standardised derivatives may also provide systemic risk benefits."* The Trading Report conclusion advocates for a flexible approach encompassing a range of platforms that would qualify as "exchanges or electronic trading platforms".

Finally, we propose that any proposals regarding mandatory trading should be subject to a full consultation process.

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

Please refer to our response to question 21 above.

Question 23: MAS seeks views on the proposed scope of the definition of "derivative market".

[7] According to Oliver Wyman analysis

No comment.

Question 24: MAS seeks views on the proposal to extend the existing two-tier regulatory regime to derivative market operators.

No comment.

Question 25: MAS seeks views on the proposed refinements of the RMO regime for locally-incorporated and overseas RMOs.

No comment.

Question 26: MAS seeks views on the proposed amendment of the definition of “clearing facility” to include the clearing and settlement of derivative contracts.

No comment.

Question 27: MAS seeks views on the proposed authorization framework for clearing facilities.

No comment.

Question 28: MAS seeks views on the proposal to extend insolvency protection to all ACHs and RCHs.

No comment.

Question 29: MAS seeks views on the proposed definition of trade repositories to be regulated under the SFA.

No comment.

Question 30: MAS seeks views on the proposed authorization framework for trade repositories, including whether to impose minimum base capital requirements and governance standards on trade repositories.

No comment.

Question 31: MAS seeks views on the proposal to not require foreign regulators to provide indemnification to an ATR/ROTR and MAS prior to obtaining data from the ATR/ROTR.

We agree with this approach.

Question 32: MAS seeks views on: (i) the proposal to regulate non-bank intermediaries dealing in derivative contracts as CMS licensees under the SFA; and (ii) the proposed scope of activities for dealing in derivative contracts.

No comment.

Question 33: MAS seeks views on the proposed exemption for derivative brokers.

No comment.

Question 34: MAS seeks views on the proposal not to regulate end users as CMS licensees under the SFA.

No comment.

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We appreciate the opportunity to share our views on the MAS’ consultation paper. Please do not hesitate to contact me at +44 (0) 207 743 9319 or at jkemp@gfma.org should you wish to discuss any of the above.

Yours sincerely,

James Kemp

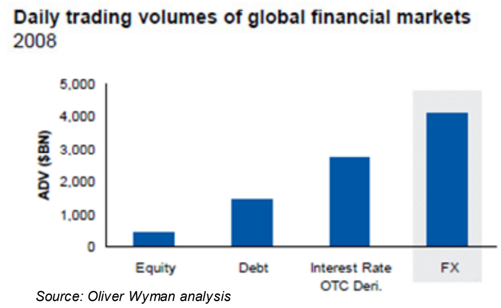
Managing Director

Global Foreign Exchange Division, GFMA[8]

[8] The Global Finanical Markets Association (“GFMA”) brings together three of the world’s leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA.

Appendix A

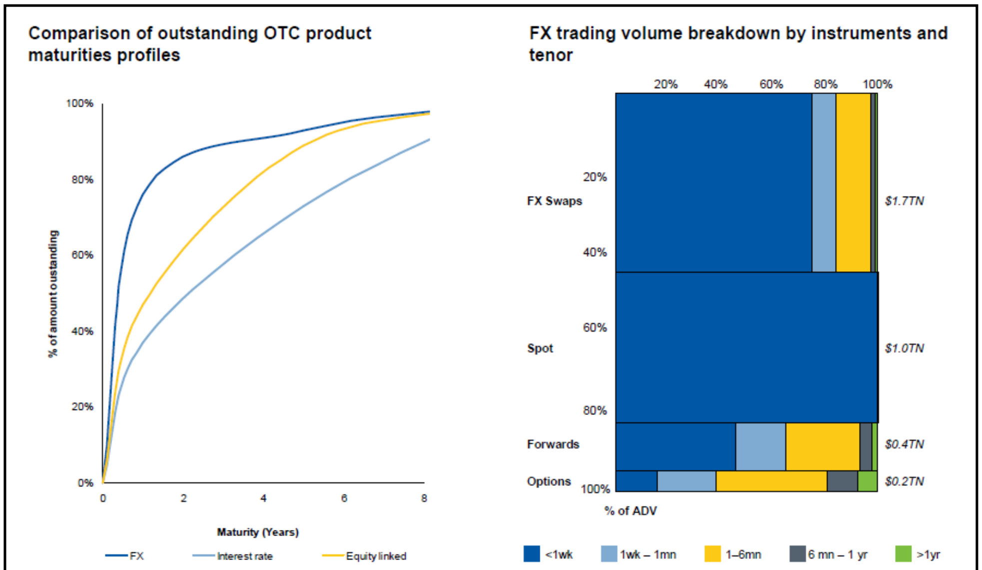
The FX market is the world's largest and most liquid financial market. It forms the basis for international trade and supports the functioning of the global payments system. Its importance in effecting monetary policy has been long established and as such has historically been subject to central bank oversight.



FX has many more participants and transactions than other asset classes. Notwithstanding this, the vast majority of transactions are simple, comprising spot, forward or swap transactions. Forwards are simply an agreement to exchange principle at a pre-determined rate, whilst swaps are simply a combination of i) a spot and a forward or ii) a forward and a forward. Crucially, there are no contingent outcomes for these types of transactions; cash flows are known at the outset. BIS data shows that these products accounted for 95% of 2010 daily traded volumes.

Instrument	1998	%	2001	%	2004	%	2007	%	2010	%
Spot	568	*37%*	386	*31%*	631	*33%*	1,005	*31%*	1,490	*38%*
Outright forwards	128	*8%*	130	*11%*	209	*11%*	362	*11%*	475	*12%*
Swaps	734	*48%*	656	*53%*	954	*50%*	1,714	*52%*	1,765	*45%*
Options and other	87	*6%*	60	*5%*	119	*6%*	212	*6%*	207	*5%*
Total	**1,517**	***100%***	**1,232**	***100%***	**1,913**	***100%***	**3,293**	***100%***	**3,938**	***100%***

Additionally, the vast majority of FX transactions are short term. The chart that follows on the left contrasts the short maturity profile of outstanding FX instruments with those of interest rate and equity derivatives. The 16% of outstanding FX contracts with maturities longer than 2 years contrasts with more than 55% of interest rate derivatives and 40% of equity derivatives with maturities longer than two years. Of daily traded volume in 2007, more than 98% of FX forwards and 99% of FX swaps were of maturities of less than a year, as illustrated in the chart that follows on the right.



Source: BIS, BoE, NY Fed, OW analysis

The BIS Triennial survey from 2010 sets out the following statistics for foreign exchange market activity for Singapore. Outright forwards and swaps comprise, according to the BIS, USD 158bn USD of USD 174bn (c. 91%) of all non-spot foreign exchange activity with the remaining 9% representing options. The majority of activity is under 1 year in maturity.

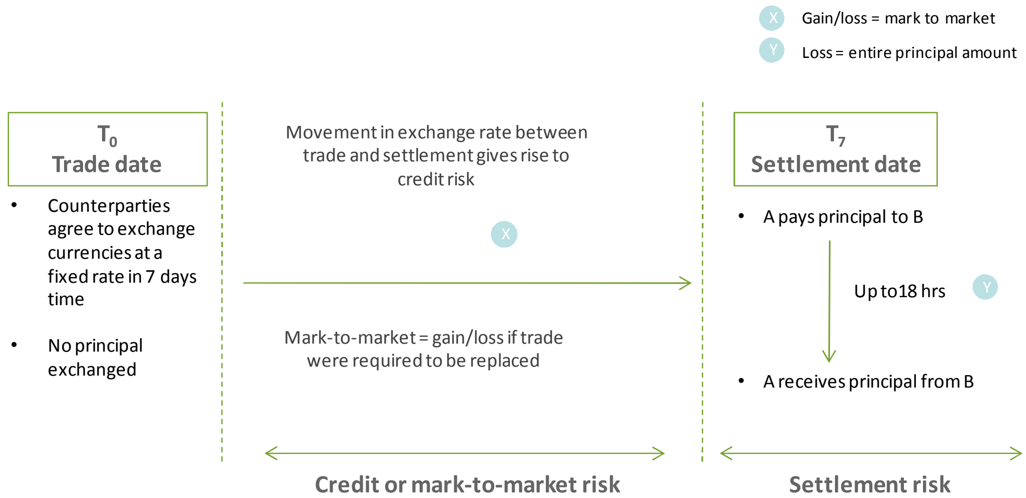
% share of trades	<= 7 days	> 7 days and <= 1year	> 1 year
Outright forwards	16	81	3
Swaps	76	24	1

Note: The most recent SFEMC October 2011 figures confirm that similar to the global picture (and excluding currency swaps), FX forwards and swaps make up 16% and 44% of the Singapore average daily volume, with only 6% FX options and spot 34%.

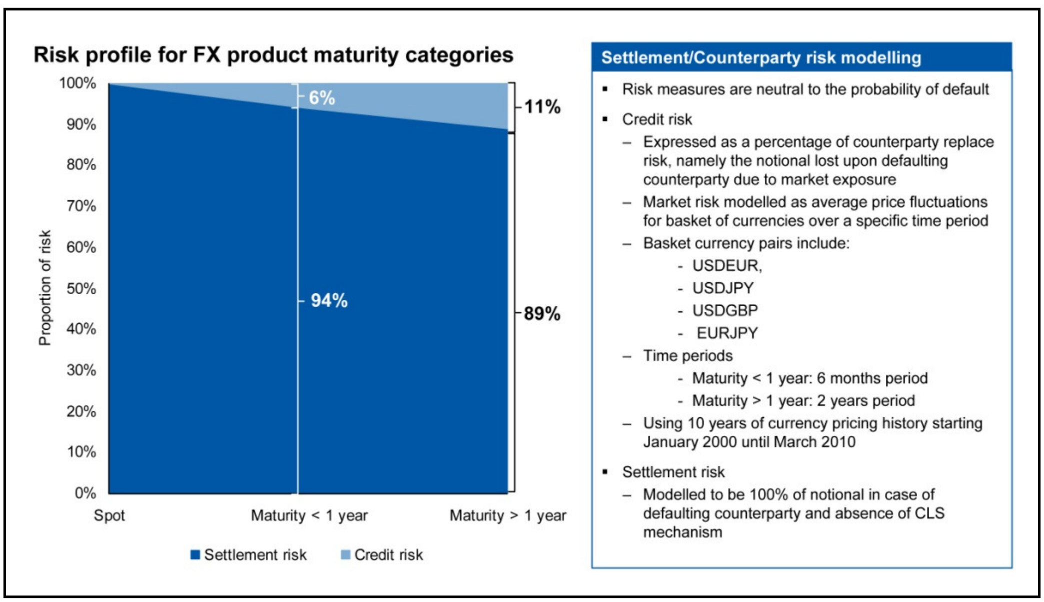
Settlement risk is the key risk in foreign exchange transactions

FX transactions typically involve exchange of principal. These settlement exposures represent the key risk in a transaction. Because of their size, settlement risk loss may be sufficient to trigger insolvency, with knock on effects to other counterparties (commonly referred to as Herstatt Risk).

7 day foreign exchange forward transaction



The graph below, based on an Oliver Wyman study, illustrates that settlement risk comprises 94% of the estimated maximum loss exposure in a trade for foreign exchange instruments with maturity of 6 months. This reduces to 89% for instruments with a maturity of 2 years.



Settlement risk is adequately addressed through CLS

CLS Bank was created in 1997 as a global settlement bank to address the concerns surrounding the systemic impact of potential settlement risk failures. By operating a payment versus payment model, whereby payments are process simultaneously, it eliminates virtually all settlement risk to its participants. CLS Bank settles almost 90% of all inter-dealer FX trades and has had no settlement failures since it was created. CLS is regulated directly by the Federal Reserve with the active support of all major central banks (including MAS). Efforts to extend the reach of CLS Bank are under way, with broad support from both FX dealers and central banks around the globe.

CCPs address mark-to-market credit risk. This is relatively small for FX transactions because of their short maturities.

Mark to market risk is the main residual counterparty credit risk not addressed by CLS. Since most foreign exchange contracts have short maturities, the foreign exchange rate is unlikely to change significantly between the inception and maturity of most foreign exchange contracts. As a result, the in-the-money portion of the trade tends to be small relative to the principal value. Accordingly, the potential loss on foreign exchange transactions consists overwhelmingly of settlement risk.

To put this into context, for FX trades with a maturity of less than one year, Oliver Wyman analysis approximates that only 6% of the maximum risk of loss is mark-to-market credit risk. This rises to only 11% for instruments with a maturity of 2 years.

Because of their short duration, these transactions stand in sharp contrast to most other swaps, for which counterparty risk is comprised almost exclusively of credit risk on the mark-to-market value of the swap, which is the risk that CCPs are primarily designed to address.

Mark to market credit risk is addressed through the widespread use of CSAs. These are particularly effective because of high price transparency and deep liquidity.

Credit support annexes ("CSAs") are heavily used in the FX market and are a particularly effective risk mitigation tool for addressing mark-to-market credit risk.

The deep liquidity and high price transparency of the market allows for a high level of confidence that initial margin levels will cover losses in these markets. Because the FX market is a highly liquid market in which prices are widely available 24 hours a day, market participants can also reliably determine the net amount of their exposure and therefore the appropriate amount of mark-to-market collateral.

Upon a default, the liquidity in the FX market means that the non-defaulting party can generally replace a transaction quickly and easily. Due to these characteristics of the FX market, existing bilateral agreements have been successful in mitigating counterparty credit risk exposures following the default of large FX counterparties, such as Lehman Brothers in 2008.[9]

The only portion of the foreign exchange market where trades are generally unsecured is where transactions are effected with corporates. Corporates use FX transactions to hedge business risks and do not generally have excess capital to use for CCP margining purposes. Aside from the issue of whether certain classes of FX are exempt from any clearing obligation, we assume that corporate would be subject to some sort of non-financial counterparty exemption, in line with other international proposals. Mandatory clearing would therefore not result in mandatory clearing for the portion of the market that is most often unsecured.

[9] Bank of England Foreign Exchange Joint Standing Committee. FXJSC Paper on the Foreign Exchange Market. September 2009. p. 2. ("**FXJSC**")

The remaining mark-to-market credit risk that would be addressed by a CCP is therefore minimal

A CCP for FX would deliver almost no incremental credit risk mitigation because most of that risk has been covered by CSAs. The Global FX Division has undertaken indicative analysis of dealers accounting for approximately 66% of the market (by reference to Euromoney league tables). This analysis indicates that approximately 85% or more of mark-to-market exposure in 2010 relates to counterparties (excluding corporates) for which CSAs have been put in place.

Applying the Oliver Wyman analysis that 6 month instruments have potential mark to market risk of 6%, we estimate the total remaining uncovered risk to be only 0.9%. On the same basis for FX transactions with maturities greater than a year, where 11% of the potential loss is mark-to-market credit risk[10], we estimate the total remaining uncovered risk to be less than 1.7%.

FX Market volume profile and Uncovered Credit Exposure (forwards & swaps)

	< 1yr Tenor	**> 1 yr Tenor**
Risk Profile:		
Credit / Counterparty Risk	6.00%	11.00%
Settlement Exposure %	94.00%	89.00%
CSA Usage @ 85%	5.10%	9.35%
Uncovered Credit Exposure	0.90%	1.65%

Introducing a CCP to address mark to market credit risk would be disproportionate, increase operational risk and potentially systemic risk, and undermine the effectiveness of existing efforts further to address settlement risk.

Settlement of FX transactions involves extensive interconnectedness across payment and foreign exchange systems. This is illustrated by the relationships that CLS has with central banks to facilitate the funding process that supports payment-vs-payment settlement.[11]

A central clearing regime would be either global or accomplished through a network of local CCPs. A global CCP for a market the size of the FX market would pose significant systemic risk.

[10] These calculations assume that all trades under 1 year have the MTM credit risk vs. settlement risk breakdown of a 6 mo. trade, and that all trades over 1 year have the breakdown of a 2 yr trade (based on Oliver Wyman analysis). In reality, the MTM credit risk number is probably even lower, since 68% of FX forwards and swaps have a maturity of less than 1 week.

[11] In its 2008 review of the interdependencies of payment and settlement systems, the CPSS concluded:

"Over the past 30 years, technological innovations, globalisation and financial sector consolidation have fostered a broad web of interconnections among a large number of payment and settlement systems, both within and across CPSS countries. These interconnections reflect efforts on the part of systems and institutions to seek new business opportunities and to reduce clearing and settlement costs. They also reflect efforts by central banks and the financial industry to promote the low-cost and safe transfer of money and financial instruments. The focus of the CPSS on reducing foreign exchange settlement risk and the work of the G30 to reduce risk in securities settlement systems, for example, have both led to tighter, more integrated settlement processes."

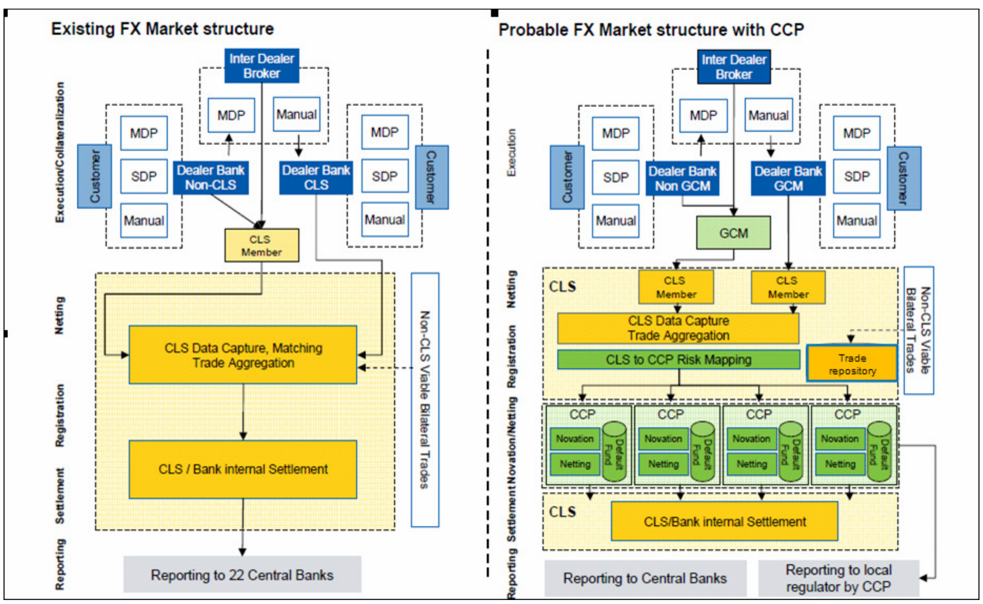
"The development of tighter interdependencies has helped to strengthen the global payment and settlement infrastructure by reducing several sources of cost and risk. Yet, tightening interdependencies have also increased the potential for disruptions to spread quickly and widely across multiple systems and markets." Interdependencies Report, p. 1.

Local CCPs would fragment the market and reduce liquidity through the dispersal of trades, positions and collateral across many jurisdictions.

The charts below illustrate the increased operational complexity and interdependencies that one or more CCPs would likely introduce into the FX market. Given the importance of foreign exchange to the global payments system, any CCP would require the same operational infrastructure, robustness and oversight currently afforded to CLS Bank.

A CCP would also introduce concentration risk, creating a potential single point of failure where none exists today, simply to address limited residual credit risk exposure. CCPs can and have failed – largely as a result of financial distress arising as a result of unmet margin calls. Because the FX market is an integral part of the global payments system, the failure of an FX CCP would likely be significant, with destabilizing effects on foreign exchange and the global economy as a whole.

Introducing CCP clearing also risks undermining the significant gains that have been made in addressing settlement risk. Efforts to introduce a CCP model could either distract from current industry plans to increase usage of CLS Bank, or worse, cause participants to cease using CLS Bank, for cost or operational reasons, thereby increasing settlement risk.



Overall, we believe that the significant operational risk and costs to the global payments system of implementing a mandatory CCP are disproportionate when compared to the benefits in addressing the 0.9% - 1.7% of mark-to-market credit risk for counterparties not using CSAs.

International convergence

The US Treasury is proposing to exclude FX forwards and swaps from the majority of regulations under the Dodd-Frank Act. The statute further exempts commodity swaps where physical delivery of the commodity is contemplated. FX is more closely related to this exempt class as it calls for the delivery of currencies. The Global FX Division has submitted a public response to US Treasury's recent invitation to comment on whether an exemption is warranted. It is also seeking to ensure that appropriate exemptions are secured under the equivalent European OTC derivatives legislation.

The proposed determination would mean that FX forwards and swaps would not be regulated as swaps under Dodd-Frank. Most importantly, this means they would be subject to neither mandatory clearing, nor mandatory trading on Swap Execution Facilities or DCMs, nor the real-time public reporting requirements. They would also be exempt from the proposed margin requirements for uncleared swaps. The proposal has clear implications for regulatory convergence, particularly in a market as liquid and global as FX.

In reaching its proposed determination, the US Treasury recognises the key characteristics of FX products and the way the market functions at present. The US Treasury:

- Acknowledges the high levels of transparency and liquidity existing in the FX markets as a result of the heavy trading on electronic platforms and the diverse availability of market pricing information
- Points to additional transparency through trade reporting to a trade repository, the requirements of which are already being addressed with GFXD members through the recent announcement of the DTCC and SWIFT as partners to provide global FX trade repository services.
- Recognises the unique factors limiting risks in the FX forwards and swaps market, pointing to the fixed terms (i.e. non-contingent outcomes), the physical exchange of currencies, the well-functioning settlement process and the shorter duration of contracts.
- Highlights the existing strong, comprehensive and internationally coordinated oversight framework prevalent in the FX markets.

In terms of identifying OTC derivatives that are capable of being cleared, we believe the overriding objectives for regulators should be to implement measures that are proportionate to the systemic risks being addressed. Consideration should therefore be given to whether mandatory clearing is a proportionate response when taking into account the pertinent systemic risks, which for FX comprise settlement risk that far outweighs counterparty credit risks that CCPs address, and the measures that are already in place to deal with those risks. The analysis should also take into account factors such as the cost of clearing and the ability of the CCP to deal with and manage the volume and risks (including risk of default) associated with clearing of relevant contracts.

Appendix B – rationale for centralised data sets and repositories

Comprehensive oversight

Trade repository information must be consistent, complete and as non-duplicative as possible in order for it to be meaningful, both for market surveillance and systemic risk monitoring. Global trade repositories provide a centralised point for submission of data, giving regulators access to both on and offshore trades and allowing them to build a complete picture regarding the positions of overseen entities. Since local regulators may typically only exert jurisdiction over local firms, currencies traded offshore by offshore entities would not be subject to regulation. They would therefore not be reported to the local repository, limiting the usefulness of that subset of data. Building an accurate picture of systemic risk or trade activity becomes significantly more difficult where the trade population is fragmented across a number of localised trade repositories, particularly considering the volume of participants and transactions present in the FX market, and in the absence of standardised global formats. The value of a comprehensive data set can also extend to implementation of other regulatory initiatives, for example, in analysing whether to mandate clearing for particular products and in establishing block trade sizes and appropriate reporting delays.

Efficiency

There are a number of efficiency arguments for global trade repositories from all market participants' perspectives.

- Cost – global trade repositories reduce the implementation costs related to building out and connecting to relevant trade repositories for both regulators and market participants alike. For reporting parties, global trade repositories allow a centralised reporting channel with common technology, messages and trade formats. Given the number of market participants engaging in cross-border transactions, local repository reporting may add significant costs for both buy and sell side participants as they are required to report to a number of repositories. Hardest hit might be the smaller, regional banks that would likely be expected to undertake the burden of international reporting on behalf of their clients. Centralised client due diligence would also produce significant savings.
- Data consistency and common standards – agreed global data formats and standards for LEIs and product and trade identifiers would also promote significant benefits for all users. The industry is making progress in this regard and we fully support these efforts. Where local repositories prevail, regulators will need to be able to interpret and aggregate data across a number of differently formatted outputs, which can be inefficient at best. Timely access to and interpretation of a comprehensive data set will be important in times of market crisis and this will be hindered if regulators are required to seek trade and position data from a number of repositories.
- Implementation – global trade repositories may also help to minimise the risks of conflicting implementation deadlines and reduce time to market.