



SINGAPORE EXCHANGE DERIVATIVES CLEARING LIMITED (“SGX-DC”)

PUBLIC CONSULTATION

PURSUANT TO SECTION 71(2) OF THE SECURITIES AND FUTURES ACT AND REGULATION 22 OF THE SECURITIES AND FUTURES (CLEARING FACILITIES) REGULATIONS 2005, SGX-DC HEREBY CONSULTS ITS PARTICIPANTS ON THE PROPOSED AMENDMENTS TO ITS BUSINESS RULES.

PROPOSED AMENDMENTS TO THE SGX-DC CLEARING RULES IN RELATION TO:

- A. CLEARING BY SGX-DC OF PHYSICAL DELIVERY CONTRACTS TRADED ON THE JOINT ASIAN DERIVATIVES EXCHANGE MARKET;**
- B. HARMONISATION OF THE RULES WITH THE SGX-DT TRADING RULES; AND**
- C. REPORTING BY MEMBERS ON: (I) ALL THEIR CREDIT FACILITIES WITH FINANCIAL INSTITUTIONS AND CHANGES TO CREDIT FACILITIES (II) IDENTIFICATION OF ACCOUNTS.**

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A. Background

1. SGX and Chicago Board of Trade (“CBOT”) have entered into a joint venture to establish an Asian-based commodity derivatives market named Joint Asian Derivatives Exchange (JADE). JADE products will be traded on CBOT’s electronic trading platform, e-cbot and cleared by SGX-DC.
2. The first JADE product targeted to be launched in September 2006 is TSR 20 Rubber Futures Contract, which will be settled by physical delivery. The public will be consulted on the contract specifications for TSR 20 Rubber Futures Contract separately.
3. This Consultation Paper sets out the proposed amendments to the SGX-DC Clearing Rules (the “Rules”) to provide for:-
 - 3.1. clearing of physically delivered commodity products by SGX-DC;and to revise the Rules in relation to the following matters:
 - 3.2 harmonisation of the Rules to be consistent with the SGX-DT Trading Rules (“Trading Rules”); and
 - 3.3 requiring Members to report to the Clearing House on: (a) all their credit facilities with financial institutions and any changes to their credit facilities; (b) the identification of their accounts.
4. SGX-DC invites comments on the proposals in this paper. The proposals may change in response to comments and feedback.
5. The amendments to the SGX-DC Clearing Rules are subject to notification to the Monetary Authority of Singapore (“MAS”).

B. Proposed Rule Amendments

1. A table setting out the existing Rules, the proposed amendments and the reasons for the amendments is set out at Appendix A. All capitalized terms used herein have the same meaning as defined in the proposed Rules.

2. Clearing of physically delivered commodity products

2.1 In summary, the main proposed Rule amendments to provide for clearing of physical commodity products are necessitated by the common features of JADE products as follows:

- 2.1.1 JADE products involve agriculture commodities;
- 2.1.2 may be physically delivered;
- 2.1.3 are traded on e-CBOT instead of on SGX Quest; and
- 2.1.4 cleared by SGX-DC.

2.2 The amendments pertain to the following matters:

Matching process

- 2.2.1 The Clearing House matches a seller and buyer through their respective Members (see proposed Rule 6.02A.8).
- 2.2.2 If a Member becomes insolvent, the Clearing House may, but is not obliged to match a buyer or seller for whom the insolvent Member acts, and the opposite Member (see proposed Rule 6.02A.4).
- 2.2.3 The list of events which give rise to a Member being deemed insolvent, has been expanded (see proposed Rules 2.30.1 and 2.30.1A).

Event of default and default procedure

- 2.2.4 In addition to the events of default listed in Rule 7.03.2.1, an event of default will also occur in a contract subject to physical delivery when a Member fails to submit the prescribed forms or documents necessary for Clearing House to effect the matching (see proposed Rule 6.03.1). Failure of a Member to comply with this Rule may constitute a major offence.
- 2.2.5 The Clearing House has the right to cash-settle by invoicing back against other Members holding opposite positions at a price that Clearing House deems fair and reasonable, if there is a default by a Member prior to matching (see proposed Rule 2.31.1.4).

Cessation of Clearing House duty as central counterparty upon matching

- 2.2.6 The Clearing House's duties as a central counterparty ceases once the Clearing House matches the buyer and seller (through their respective Members) upon the maturity of the contract (see proposed Rule 6.02A.7).

Clearing House's role as escrow agent

- 2.2.7 The Clearing House merely facilitates the delivery process by acting as an escrow agent in respect of the Performance Deposits and the exchange of Title Documents and payment between the buyer and seller (see proposed Rules 6.07.1 and 6.07.2).
- 2.2.8 The Clearing House has a right to commingle Performance Deposits with margins and security deposits (see proposed Rules 6.07.3).
- 2.2.9 The Clearing House has a right to deduct an administrative fee for carrying out its role as an escrow agent (see proposed Rule 6.07.4).

- 2.2.10 The Clearing House shall credit interest on Performance Deposits except for (a) money continued to be held subsequent to a Member's failure to perform or default, and (b) administrative fees payable to the Clearing House for carrying out its role as an escrow agent (see proposed Rules 6.07.5).
- 2.2.11 The Clearing House shall release the Performance Deposits only upon the occurrence of certain events such as when both the Buying Member and Selling Member have mutually agreed to the release etc (see proposed Rule 6.07.6).
- 2.2.12 The Clearing House has no obligation to authenticate Title Documents delivered to or through a Member. The Clearing House also has no liability in respect of forged Title Documents (see proposed Rules 6.02A.12 and 6.02A.13).

Exclusion of liability

- 2.2.13 The Clearing House is not liable for:
 - 2.2.13.1 the acts, omissions, default or insolvency of organizations involved with delivery of commodities under any Contract cleared by the Clearing House.
 - 2.2.13.2 the delivery or non-delivery of Title Documents.
 - 2.2.13.3 the transfer of title, or failure to transfer title, of a Commodity by an Approved Warehouse.
 - 2.2.13.4 the limitation or exclusion of liability by an Approved Warehouse.(see proposed Rule 6.02A.14).

Members' duty to procure performance of delivery obligations by sellers or buyers

- 2.2.14 A Member carrying or qualifying a Trading Member carrying an account for a Customer or a related corporation that is a seller required to make delivery or a buyer required to accept delivery of any Commodity under a Contract, guarantees and assumes complete responsibility for the performance of all delivery obligations under the Contract. Similarly, a Member having any open position for its proprietary account assumes complete responsibility for the performance of all delivery obligations (see proposed Rules 6.02A.1, 6.02A.2 and 6.02A.3.) Failure of a Member to comply with any of these Rules may constitute a major Rule violation.

Resolution of disputes

- 2.2.15 Disputes between Members or their buyers and sellers in relation to JADE contracts are to be referred by the Members to the SIAC for arbitration. The Clearing House will deal with the Performance Deposit in the manner ordered in the final arbitral award (see proposed Rules 5.01.2 to 5.01.4).

Q1: PHYSICAL DELIVERY CONTRACTS

SGX-DC seeks your views on the proposed new Rules on:

- a. the matching process;**
- b. the expanded list of events stating when a Member is deemed insolvent;**
- c. the event of default and default procedure;**
- d. cessation of the Clearing House’s role as a central counterparty once matching has been effected; and**
- e. the Clearing House’s role as an escrow agent;**
- f. the exclusion of liability for:**
 - i. the acts, omissions, default or insolvency of organizations involved with delivery of commodities under any Contract cleared by the Clearing House;**
 - ii. the delivery or non-delivery of Title Documents;**
 - iii. the transfer of title, or failure to transfer title, of a Commodity by an Approved Warehouse ; and**
 - iv. the limitation or exclusion of liability by an Approved Warehouse.**
- g. a Member’s duty to ensure the compliance of delivery obligations; and**
- h. the resolution of disputes.**

If you do not agree with any of the foregoing, please suggest alternatives.

3. Harmonisation of the Rules with the Trading Rules

Contract Specifications

- 3.1 On 15 March 2006, the Exchange undertook a public consult entitled “FUTURES TRADING RULES -A NEW REGIME FOR ACCESS AND MEMBERSHIP.” This consultation set forth the new revised streamlined architecture of the Trading Rules. One of the key aspects relating to the revisions relate to the treatment of Contract Specifications. Save for terms relating to final settlement price, position limits, price limits and accumulation of positions, Contract Specifications shall no longer be part of the Trading Rules. In view of this new framework, we are proposing that references to “rules of Relevant Market” be supplemented with or substituted by “Contract Specifications” in Chapter 6 (see Chapter 6 generally and the definition of “Contract Specifications at Rule 9.1).

Incorporation of Daily Settlement Price

For OTC Contracts

- 3.2 The current Rule 7.11.1.2 provides that the daily settlement price (“DSP”) of OTC Contracts shall be determined by using price data from market participants or derived from pricing models selected or established by the Clearing House. As the procedures for determining

DSP for OTC Contracts have not been described previously, Clearing House intends to set out these procedures in a Practice Note, attached at Appendix B1.

For exchange-traded Contracts

- 3.3 The current Rule 7.11.1.2 provides that the daily settlement price (“DSP”) of Contracts (other than OTC contracts) shall be settled in accordance with the rules of the Relevant Market where it is traded. Similarly, the Trading Rules provide that for each Contract the DSP shall be determined by the Exchange in accordance with the relevant formula and procedures applicable to each Contract as set forth in the Clearing Rules. We believe that the market needs some certainty and assurance that the methodology adopted for the calculation of DSP are transparent, rigorous and accepted in the industry. Hence we have included a Practice Note that clearly sets out the formulas we would adopt generally and in exceptional cases for the computation of DSP. In most cases, the Clearing House adopts the following methods to compute DSP in descending order of preference:

- 3.3.1 the last traded price;
- 3.3.2 the bid and offer spread at the close of market; and
- 3.3.3 price data derived from pricing models, as stated or established by the Clearing House.

(see proposed Rule 7.11.1.2).The procedures for determining DSP for Contracts other than OTC Contracts are set out in a Practice Note, attached at Appendix B2.

Final Settlement Price

- 3.3.4 Rule 7.11A of the Clearing Rules, which currently only deals with FSP of OTC Contracts, will be expanded to provide that the FSP for all other Contracts will be determined in the manner as set out in the Trading Rules.

Q2: HARMONISATION OF THE RULES WITH THE TRADING RULES

SGX-DC seeks your views on:

- a. the procedures for determining DSPs for OTC Contracts; and**
- b. the factors to be taken into consideration and procedures for determining DSPs for Contracts other than OTC Contracts.**

- 3.3.5 Rule 7.11A of the Clearing Rules, which currently only deals with FSP of OTC Contracts, will be expanded to provide that the FSP for all other Contracts will be determined in the manner as set out in the Trading Rules or Contract Specifications.

4. Reporting by Members on all their credit facilities with financial institutions and changes to credit facilities

- 4.1 During volatile market conditions, the Clearing House may call on Members for intra-day margins which have to be paid in cash. Such calls are usually issued in the morning and are

required to be met within 1 hour (or within any deadline as may be specified) under the present Clearing House policy.

4.2 Where the margin call is in respect of a Member's customers' account, if there are insufficient margins in the customers' account, the Member would have to rely on its own available cash funds as well as any credit facilities it may have, for example, standby bank overdraft facilities to provide funds to meet the calls. If a Member fails to meet the Clearing House's margins calls within the specified deadline, the Clearing House may declare this as an event of default.

4.3 As a control measure to ensure that Members have sufficient funds to meet margin calls on their customers' accounts, Members are presently already required, pursuant to Circulars issued by the Clearing House, to submit a monthly report on all their credit facilities with their financial institutions. In addition, Members are required to immediately update the Clearing House of any changes to their credit facilities, such as addition or termination of credit facilities, or variations in credit limits. These reporting requirements will be incorporated in the Rules. (see proposed Rule 2.14.3A). The regulatory circular to be issued in relation to this new Rule is attached at Appendix C1 for Members' information.

5. Identification of Accounts

5.1 Members are currently required, pursuant to Circulars issued by the Clearing House, to submit an Account Identity Form (Form BC4A) for House Accounts and Customer Accounts which are used for trading or carrying of Contracts or which contain positions that are required to be reported, in relation to position change sheets (Rule 7.09.1) or large positions (Rule 7.16.1). The submission must be done within the time prescribed by the Clearing House. This reporting requirement will be incorporated in the Rules as well (see Rule 2.14.3A). The regulatory circulars to be issued in relation to this new Rule and Rule 7.16.1 are attached at Appendices C2 and C3 respectively, for Members' information.

6. Limits of Positions

6.1 The Clearing House had previously issued a Circular in relation to limits of positions dealt with by Rule 2.20. The Circular has been updated. One of the changes is to ensure that the references to contracts in the Letter of Awareness (required to be furnished by Members pursuant to this Rule) are consistent with the additional classes of contracts that Clearing House now clears (e.g such as OTC contracts). The regulatory circular to be issued in relation to Rule 2.20 is attached at Appendix C4 for Members' information.

Q3: REPORTING REQUIREMENTS

SGX-DC seeks your view on the requirement for Members to submit:

- a. reports on all their credit facilities with financial institutions, on a monthly basis;**
- b. changes to their credit facilities, immediately upon such change; and**
- c. Account Identity forms for House Accounts and Customer Accounts which are used for trading of Contracts or carrying of Contracts or which contain positions required to be reported pursuant to Rules 7.09.1 and 7.16.1, within such time as prescribed by the Clearing House.**

C. Procedure and Deadline to submit comments

1. Written submissions are to be sent to SGX-DC through email *and* either by post/courier or by fax:

Email: rules@sgx.com

AND

Post/Courier: Singapore Exchange Derivatives Clearing Limited
2 Shenton Way, SGX Centre 1
#19-00,
Singapore 068804

Attn: Mr Low Teng Yong, SVP / Ms Ng Ee San, AVP

2. Comments should be organized in the following manner:
- (a) cover page (including the information specified in paragraph 4 of this Section);
 - (b) statement of interest
 - (c) table of contents;
 - (d) summary of major points;
 - (e) comments; and
 - (f) conclusion.
3. Supporting material may be placed in an annex. All submissions should be clearly and concisely written, and should provide a reasoned explanation for any proposed revision to the rules. Where feasible, participants should identify the specific rule on which they are commenting. In any case in which a participant chooses to suggest revisions to the text of the rules, the participant should state clearly the specific changes to the text that they are proposing.
4. All submissions should reach us by **19 June 2006**. Submissions must be submitted in both hard and soft copies (in Microsoft Word format) and font size should be no smaller than Times New Roman 11pt. Participants submitting comments should include their personal/company particulars as well as their correspondence address, contact numbers and email addresses on the cover page of their submissions.
5. SGX-DC reserves the right to make public all or parts of any written submission and to disclose the identity of the source. Participants may request confidential treatment for any part of the submission that the participant believes to be proprietary, confidential or commercially sensitive. Any such information should be clearly marked and placed in a separate annex. If SGX-DC grants confidential treatment, it will consider but will not publicly disclose the information. If SGX-DC rejects the request for confidential treatment, it will return the information to the party that submitted it and will not consider the information as part of its review. As far as possible, participants should limit any request for confidential treatment of information submitted. SGX-DC will not accept any submission that requests confidential treatment of all, or a substantial part, of the submission.
