

REGULATORY MEMO**FROM: NIZAM ISMAIL****TO: SINGAPORE GLOBAL GINSENG EXCHANGE PTE LTD****DATE: 18 DEC 2017**

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REGULATORY ANALYSIS UNDER THE COMMODITY TRADING ACT/ SECURITIES AND FUTURES ACT

THIS REGULATORY MEMORANDUM (THIS “REGULATORY MEMO”) IS INTENDED SOLELY FOR THE USE OF SINGAPORE GLOBAL GINSENG EXCHANGE PTE LTD (“THE COMPANY”), FOR THE PURPOSES OF DETERMINING IF ITS ACTIVITIES INVOKE ANY LICENSING OR REGULATORY REQUIREMENTS UNDER SINGAPORE’S COMMODITY TRADING ACT AND THE SECURITIES AND FUTURES ACT.

SECTION I: GLOSSARY

In this Regulatory Memo, the following expressions have the following meaning:

“CTA”	Commodity Trading Act (Chapter 48A)
“IES”	International Enterprise Singapore, the commodities regulator in Singapore
“MAS”	Monetary Authority of Singapore, the financial services regulator in Singapore
“SFA”	Securities and Futures Act (Chapter 289)

SECTION II: BACKGROUND

1. The Company proposes to set up a platform (the **“Proposed Exchange”**) for the electronic spot trading of Ginseng Products in Singapore.
2. Under this proposed business, the Proposed Exchange will function as a “many-to-many” model – where it will receive many buy and many sell orders from participants on the Exchange in its order book. The Proposed Exchange will use a technology platform to match buy and sell orders.
3. To facilitate clearing and settlement, the Proposed Exchange will work with a Singapore-licensed bank, which will provide segregated customer accounts (to members of the Exchange) to facilitate clearing and settlement.
4. Under this proposed arrangement, the Proposed Exchange will open a main account at the bank.

It will have its own segregated sub-account with the bank. The sub-accounts are segregated – in that there will be no co-mingling of customer sub-accounts. Each sub-account can generate its own statement on a daily basis. Upon a trade is executed on

the Proposed Exchange, the Proposed Exchange will send payment instruction to the bank to debit buyer's sub-account and credit supplier's sub-account, and the ownership of the associated ginseng will be transferred from the supplier to the buyer.

6. Before a trade can be executed on the Proposed Exchange, a buyer has to fund its sub-account with sufficient monies to pay for the trade intended. Similarly, before a trade can be executed on the Proposed Exchange, a supplier has to deliver the ginseng intended to be sold to the third-party warehouse appointed by the Proposed Exchange.
7. Once a trade is executed, the monies are transferred, and the buyer will issue instruction to the 3rd party warehouse operator for delivery instructions for the ginseng. Buyers can choose to take physical delivery of the ginseng or hold the ginseng in the warehouse for sale in future.
8. Buyers and suppliers will also be able to access their sub-accounts through the Proposed Exchange's trading system, as there will be integration between the Proposed Exchange's trading system and the bank's accounts for the Proposed Exchange and the sub-accounts. The buyers and suppliers can also transfer the balances in the sub-accounts to themselves in other banks' accounts.
9. The advantage of the above structure is that it ensures an independent and robust clearing and settlement framework involving a Singapore-licensed bank, ensuring integrity and confidence for the Proposed Exchange's framework.

SECTION III: SCOPE OF REGULATORY MEMO

10. This Regulatory Memo seeks to address the following issue:

Whether the Proposed Exchange's business model brings into play any licensing or regulatory issue under the CTA or SFA, or any other statute administered by the MAS.

SECTION IV: REGULATORY FRAMEWORK AND ANALYSIS

Commodity Trading Act

11. The CTA generally governs the regulation of commodities.
12. A "**commodity**" is defined under Section 2 of the CTA as follows:

"commodity" means any produce, item, goods or article that is the subject of any :

- commodity forward contract;

- leveraged commodity trading;
- contract made pursuant to trading in differences; or
- spot commodity trading,

and includes an index, a right or an interest in such commodity, and such other index, right or interest of any nature as the Board may, by notification in the *Gazette*, prescribe to be a commodity; but does not include any produce, item, goods or article that is the subject of a commodity futures contract and any index, right or interest in such produce, item, goods or article.

13. The definition is very wide and intentionally so. The Commodities Futures Act was renamed the CTA in 2001. The definition of commodity was widened, designed to keep out bucket shops. The CTA also provides carve outs for legitimate or bona fide activities.
14. The product that is intended to be traded by the Proposed Exchange, wild Ginseng, will be a commodity under the CTA. Specifically, it will be a spot commodity, which defined under section 2 of the CTA as “...the purchase or sale of a commodity at its **current market or spot price**, where it is intended that such transaction results in the physical delivery of the commodity”.

Commodity Broker?

15. We now consider whether the Proposed Exchange is a spot “commodity broker” in terms of Section 13A of the CTA. This governs the issuances licences for spot commodity brokers and their representatives, spot commodity pool operators and representatives. **Licensing exemptions** for spot commodity trading activities are set out from paragraphs 1(e) to 1(f) of the Schedule to the CTA. This includes an exemption for a person trading on his own account and who does not solicit funds from the public to carry out spot commodity trading.
16. The term “commodity broker” is defined as follows:

“commodity broker” means a person who (whether as principal or agent) carries on the business of soliciting, or accepting orders, for the purchase or sale of any commodity by way of or relating to any commodity contract, whether or not the business is part of, or is carried on in conjunction with, any other business.
17. The key focus of a broker is that of the business of soliciting or accepting orders as an intermediary. Here, the Proposed Exchange is not in the business of soliciting or accepting orders from customers, but receives many buys and many sells orders through its members. The Proposed Exchange will work with its members, which may be traders, brokers or individuals.
18. In other words, the Proposed Exchange will work with multiple commodity brokers and perform a matching function of these multiple buys and sell orders.

19. Therefore, in our view, the Proposed Exchange will not fall under the definition of “commodity brokers” under the CTA>

Commodity Market?

20. We now consider whether the Proposed Exchange will be deemed to be a commodity market under the CTA.
21. The intent is for the Proposed Exchange to provide a market – where there will be an order book of multiple buy and sell orders, and which will be matched by the Proposed Exchange’s trading engine.
22. The term “**commodity market**” is defined under Section 2 of the CTA as follows:

“**commodity market**” means:

- (a) a market, whether in Singapore or elsewhere, at which **commodity contracts** are regularly made; or
 - (b) an electronic system, whether operating in Singapore or elsewhere, through which trading in **commodity contracts** is carried out, but excludes an electronic facility which merely provides price or other information relating to commodity contracts (whether that facility is part of or carried on in conjunction with the provision of any other information not related to commodity contracts) and which does not permit users of the facility to channel orders for, execute transactions in, or make markets in, commodity contracts;” *[emphasis added]*
23. The definition of a “commodity market” is therefore only applicable where a market place trades products which fall under the definition of “**commodity contracts**”.

Commodity Contract

24. The term “**commodity contract**” is defined under Section 2 CTA as follows:

“commodity contract” means —

- (a) a **commodity forward contract**;
- (b) any contract made pursuant to **trading in differences** with respect to a commodity, not being a commodity futures contract; or
- (c) any contract made pursuant to a transaction in **leveraged** commodity trading.

25. The products which can be considered as “commodity contract” are further defined as follows:

“commodity forward contract” means a contract the effect of which is that one party agrees to deliver a specified commodity, or a specified quantity of a specified commodity, to another party at a specified future time and at a specified price payable at that time, but does not include a commodity futures contract;

“leveraged commodity trading” means —

- (a) the act of entering into or offering to enter into, or inducing or attempting to induce a person to enter into or offer to enter into, a contract or an arrangement **on a margin basis** (other than a commodity futures contract) whereby a person undertakes as determined by the terms and conditions of the contract or arrangement —
 - (i) to make an adjustment between himself and another person according to whether a commodity is worth more or less, at a specified point in time;
 - (ii) to pay an amount of money determined or to be determined by reference to the change in value of a commodity over a specified period of time; or
 - (iii) to deliver to another person at an agreed future time an agreed amount of commodities at an agreed price;
- (b) the provision by any person referred to in paragraph (a) of any advance, credit facility or loan, directly or indirectly, to facilitate an act of the description referred to in that paragraph; or
- (c) the act of entering into or offering to enter into, or inducing or attempting to induce a person to enter into, an arrangement with another person (whether on a discretionary basis or otherwise) to enter into any contract to facilitate an act of the description referred to in paragraph (a) or (b)”

26. The term **“contract for differences”** is not defined under the CTA. There is a similar concept defined under the SFA, in connection with contract for differences for **securities**, which is defined under Section 2 as follows:

“any right under a contract for differences or under any other contract the purpose or pretended purpose of which is to secure a profit or avoid a loss by reference to fluctuations in —

- (i) the value or price of any such debentures, stocks or shares;
- (ii) the value or price of any group of any such debentures, stocks or shares; or

(iii) an index of any such debentures, stocks or shares;

27. Generally, a contract for differences is a derivative instrument that promises profits or losses by referencing against price movements of underlying commodities (whether on an individual basis, or on a collective / index basis.

Application of Definitions to Proposed Activities of Proposed Exchange

28. Turning to the Proposed Exchange, the intent is to provide a marketplace to trade wild ginseng contracts on a spot basis. This means that the contracts are **not** :
- a. Commodity forward contracts – as the delivery of these wild ginseng contracts are not done “at a specified future time and at a specified price payable at that time”.
 - b. Leveraged commodity contracts – as the contracts are concluded on a spot basis, and not **“on a margin basis”**. There is also no credit facility put in place to facilitate any margin trading, nor is there any arrangement (whether on a discretionary basis or otherwise) to facilitate any form of margin trading.
 - c. Contracts for differences. There is no synthetic or derivative contracts that move in tandem with movements of underlying commodities (or any index).
29. Therefore, these spot commodity contracts that are proposed to be traded on the proposed Exchange will **not** be considered as **“commodity contracts”** under the CTA.
30. The consequence of this is that a market place to trade wild ginseng spot contracts will **not** fall under the definition of **“commodity market”**, given that no **“commodity contracts”** will be traded on the proposed Exchange.
31. The proposed activity, will, in our assessment, not be subject to regulation under the CTA.

Securities and Futures Act

32. The SFA currently regulates activities relating to **commodity futures** in Singapore.
33. The SFA defines the “trading in futures contracts” in Schedule 2 as follows:

“Trading in futures contracts” means (whether as principal or agent) —

- (a) making or offering to make with any person, or inducing or attempting to induce any person to enter into or to offer to enter into any agreement for or with a view to the purchase or sale of a futures contract; or
- (b) soliciting or accepting any order for, or otherwise dealing in, a futures contract.

34. The term “futures contract” is further defined as follows:

- (a) for the purposes of Part I of the First Schedule of the SFA (regulation of markets)—
 - (i) a contract the effect of which is that —
 - (A) one party agrees to deliver a specified commodity, or a specified quantity of a specified commodity, to another party at a specified future time and at a specified price payable at that time; or
 - (B) the parties will discharge their obligations under the contract by settling the difference between the value of a specified quantity of a specified commodity agreed at the time of the making of the contract and at a specified future time,
 - (C) and includes a futures option transaction, but does not include such contract or class of contracts as the Authority may prescribe; or
 - (ii) such other contract or class of contracts as the Authority may prescribe;

(b) for the purposes of any other provision in this Act —

- (i) a contract the effect of which is that —
 - (A) one party agrees to deliver a specified commodity, or a specified quantity of a specified commodity, to another party at a specified future time and at a specified price payable at that time pursuant to the terms and conditions set out in the business rules of a futures market or pursuant to the business practices of a futures market; or
 - (B) the parties will discharge their obligations under the contract by settling the difference between the value of a specified quantity of a specified commodity agreed at the time of the making of the contract and at a specified future time, such difference being determined in accordance with the business rules or practices of the futures market at which the contract is made,
 - (C) and includes a futures option transaction, but does not include such contract or class of contracts as the Authority may prescribe;

35. The central concepts of a futures contract is that there is an agreement for parties to settle their obligations at a specified future time and for a specified price payable, and that there are prescribed rules that govern the trading of these contracts.

36. On the facts at hand, the Proposed Exchange is handling spot commodity, not futures. Hence, the activities will not be governed as futures contracts (and subject to futures markets regulation) under the SFA.
37. On 11 February 2015, MAS issued a Consultation Paper on Proposed Amendments to the SFA, proposing amendments to extend the SFA scope to regulate over-the-counter (“OTC”) derivatives (including the transfer of regulatory oversight of commodity derivatives from the CTA to the SFA.
38. These are contained in the Securities and Futures (Amendment) Act (“SFAA”), which has been passed by Parliament in January 2017, but yet to take effect. Essentially, the SFAA extends the scope of the SFA to OTC derivatives by empowering MAS to regulate market operators and capital markets intermediaries in respect of their OTC derivatives activities. Regulatory oversight of commodity derivatives, under the CTA, administered by IE Singapore, will consequently be transferred to the MAS under the SFA.
39. The SFAA defines “derivatives” as follows:

“derivatives contract” means —

(a) any contract or arrangement under which —

- (i) a party to the contract or arrangement is required to, or may be required to, discharge all or any of its obligations under the contract or arrangement at some future time; and
- (ii) the value of the contract or arrangement is determined (whether directly or indirectly, or whether wholly or in part) by reference to, is derived from, or varies by reference to, either of the following:

(A) the value or amount of one or more underlying things;

(B) fluctuations in the values or amounts of one or more underlying things; or

(b) any contract or arrangement that is, or that belongs to a class of contracts or arrangements that is, prescribed to be a derivatives contract,

but does not include —

- (iii) securities;
- (iv) any unit in a collective investment scheme;
- (v) **a spot contract;**

...

40. Again, the Proposed Exchange intends to handle spot commodities, not derivatives. It is notable that there is an explicit carve out for **spot contracts**, defined as:

“spot contract” means a contract or arrangement for the sale or purchase of any underlying thing at the spot price, where it is intended for a party to the contract or arrangement to take delivery of the underlying thing immediately or within a period which must not be longer than the period determined by the market convention for delivery of the underlying thing.

41. The definition of a spot contract will apply to the intended activity of the Proposed Exchange. Therefore, the exclusion from the definition of “derivatives” will apply .
42. Hence, even if the SFA were to implement the new changes, the Proposed Exchange’s intended activities will not be regulated under the SFA.

SECTION V: CONCLUSION

43. It is our view that the intended activities of the Proposed Exchange will not trigger any regulatory or licensing requirements under the CTA or SFA, nor any other statute administered by the MAS.



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