

CONSULTATION PAPER

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Policy
Consultation on
Amendments to
the SFA and the FAA

MAS

Monetary Authority of Singapore

**AMENDMENTS TO THE SECURITIES AND FUTURES ACT AND
THE FINANCIAL ADVISERS ACT**

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PREFACE

MAS issued two consultation papers on 25 September 2006 and 5 December 2006 on policy reforms and amendments that were being considered for the Securities and Futures Act, Cap. 289 (“SFA”) and the Financial Advisers Act, Cap. 110 (“FAA”). The amendments were aimed at achieving greater consistency in our regulations, facilitating new business activities and products and refining our supervisory and enforcement toolkit. MAS’ responses to the comments received during the two prior policy consultations were released on our website on 11 October 2007.

2 This policy consultation paper is in relation to the third and final set of proposed amendments to the SFA and the FAA. This consultation paper covers:

- a. amendments to enhance MAS’ supervisory oversight of capital market services and financial advisers’ licence holders; and
- b. amendments to further enhance the responsiveness of MAS’ regulatory framework to market innovation.

3 MAS invites interested parties to forward their views and comments on the issues outlined in the policy consultation paper.

4 Parties who do not wish to comment on all of the issues may confine their responses to the specific sections that are of interest. Written comments should be submitted to:

Market Conduct Policy Division
Capital Markets Department
Monetary Authority of Singapore
10 Shenton Way
MAS Building
Singapore 079117
Email: sfa_faa06@mas.gov.sg
Fax: (65) 6225-4063

MAS would like to request for all comments and feedback to be submitted by 9 November 2007.

5 Please note that all submissions received may be made public unless confidentiality is specifically requested for the whole or part of the submissions.

AMENDMENTS TO THE SECURITIES AND FUTURES ACT AND THE FINANCIAL ADVISERS ACT

INTRODUCTION

This consultation paper sets out MAS' policy in relation to proposed amendments to the Securities and Futures Act, Cap. 289 (“**SFA**”) and the Financial Advisers Act, Cap. 110 (“**FAA**”).

2 Sections 1 to 12 relate to amendments to the SFA and the FAA to enhance MAS' supervisory oversight of capital market services (“**CMS**”) and financial advisers' (“**FA**”) licence holders. These amendments propose, *inter alia*, (i) implementing perpetual licensing for holders of CMS and FA corporate licences; (ii) empowering MAS to grant permission to foreign regulators to inspect CMS and FA licence holders, subject to certain conditions; (iii) extending the prohibition order (“**PO**”) regime under the SFA; (iv) compliance arrangements of licence holders, (v) adjustments to some licensing exemptions; and (vi) extension of fit and proper requirements.

3 Section 13 proposes amendments to the definitions of “securities” and “futures contract” in the SFA and the FAA to enable MAS to prescribe new products as securities, as well as to exclude products from the definition of “securities” and “futures contract” via the promulgation of regulations. The amendments are aimed at making our legislation more flexible and responsive to market innovation so that new products can be brought within our regulatory regime expeditiously.

SECTION 1: PERPETUAL LICENSING REGIME FOR CORPORATE LICENCE HOLDERS

1 Currently, capital markets services (“CMS”) and financial advisers’ (“FA”) licence holders and their representatives are required to renew their licence every three years. MAS is proposing to remove the requirement for licence renewals and to implement a perpetual licensing regime for CMS and FA licence holders. This is in line with MAS’ earlier proposal to move to a notification regime for representatives, whereby representatives would not be required to renew their notifications¹.

2 The proposal would align the licensing regime for corporates under the Securities and Futures Act (“SFA”) and the Financial Advisers Act (“FAA”) with those of other financial institutions regulated by MAS such as banks and insurance companies. It would reduce administrative burden to the industry by removing the need to apply for renewal of licences.

1.1 MAS seeks views on the proposal to implement perpetual licensing for CMS and FA licence holders under the SFA and the FAA.

SECTION 2: REGULATORY ASSISTANCE TO FOREIGN REGULATORS

3 In response to the increasing globalisation of capital markets and the growth of internationally active broker-dealers, supervisors have moved towards consolidated supervision. As a reflection of this trend, MAS has been receiving more requests from foreign regulators to inspect licence holders

¹ Please refer to the Policy Consultation on Amendments to the SFA and FAA [P014-2006] issued on 25 September 2006.

whose parent entities they supervise. Currently, the SFA and the FAA do not explicitly provide the power for MAS to either accede to or reject such requests to inspect CMS and FA licence holders by the regulators of the parent entities. In practice, the foreign regulator is asked to seek the consent of the licence holder before carrying out the inspection.

4 MAS proposes to amend the legislation to make explicit that foreign regulators are required to obtain MAS' permission to inspect CMS and FA licence holders. Such inspections should be for the sole purpose of enabling the foreign regulators to carry out their supervisory function. Consent need not be sought from CMS and FA licence holders. Such inspections would be subject to safeguards. These include the requirement to protect the confidentiality of information, the right of MAS to impose conditions on the inspection conducted by the foreign regulator and reciprocity by foreign regulators to MAS' requests.

2.1 MAS seeks views on the proposal to provide legal certainty for MAS to grant permission to foreign parent regulators to inspect licence holders in Singapore for the sole purpose of carrying out their supervisory functions.

2.2 MAS also seeks views on the proposed safeguards under which inspections of licence holders may be conducted.

SECTION 3: PROHIBITION ORDER (“PO”) REGIME

(A) Extending the PO Regime to Persons Exempt from Licensing Under the SFA

5 MAS is empowered under the SFA to issue POs against CMS licence holders and their representatives to prohibit them from performing regulated activities that they have been licensed to conduct. However, the PO regime does not apply to banks, merchant banks, insurance and finance companies which are exempt from licensing under section 99(1)(a), (b), (c) and (d) of SFA (“**exempt FIs**”) and their representatives

6 To level the playing field across CMS licence holders and exempt FIs, MAS proposes to extend the power to issue POs to an exempt FI or representative of an exempt FI. The grounds for issuing a PO would include those applicable to the revocation of a licence in the case of a CMS licence holder.

7 In addition, MAS proposes to extend the grounds for issuing a PO under the SFA to include cases where MAS has reason to believe that the person has contravened any provision of the SFA; where the person has been convicted of an offence involving fraud or dishonesty; or where the person is required to pay a civil penalty in respect of a market misconduct offence under Part XII of the SFA.

3.1 MAS seeks views on the proposal to extend the powers to issue a PO under the SFA to include the following cases:

a. where the person is an exempt FI or representative of an exempt FI – the grounds for which would include those applicable to the revocation of a licence in the case of a licensee;

- b. where MAS has reason to believe that the person has contravened the SFA;**
- c. where the person is convicted of an offence involving fraud or dishonesty in Singapore or elsewhere; or**
- d. where the person is required to pay a civil penalty in respect of a market misconduct offence under Part XII of the SFA.**

(B) Extending the PO Regime to Prohibit Persons from Carrying Out Certain Activities Under the SFA and the FAA

8 A person issued with a PO is not allowed to conduct regulated activities under the SFA and the FAA. However, the person is not explicitly prohibited from assuming a management role or becoming a director or substantial shareholder in a capital markets intermediary or FA².

9 A person in a management position, a director or substantial shareholder has the ability to direct or influence the way in which the business of a capital markets intermediary or FA is conducted. Accordingly, MAS is of the view that a person deemed unfit to conduct regulated activities as a representative should not be allowed to take part in the management or be a director or substantial shareholder of a capital markets intermediary or FA. MAS proposes to extend the PO regime under the SFA and the FAA to empower MAS to issue POs to prohibit a person from taking part directly or indirectly in the management, or becoming a director or substantial shareholder of a capital

² Capital market intermediaries and FAs in this context include:-

- (i) holders of CMS licence under the SFA;
- (ii) banks, merchant banks, insurance and finance companies which are exempt from licensing under section 99(1)(a), (b), (c) and (d) of SFA;
- (iii) entities exempted from licensing pursuant to paragraphs 4(1)(c), 5(1)(d), 7(1)(b) of the Second Schedule to the Securities and Futures (Licensing and Conduct of Business) Regulations;
- (iv) licensed FAs under the FAA; and
- (v) exempt FAs exempt under S23(1) of the FAA from holding a FA licence.

markets intermediary or FA.

3.2 MAS seeks views on the proposed extension of the scope and effect of the PO regime under the SFA and the FAA, in particular on any practical difficulties or unintended consequences that may arise.

SECTION 4: COMPLIANCE ARRANGEMENTS OF LICENCE HOLDERS

10 The Chief Executive Officer (“CEO”) and directors of CMS and FA licence holders are currently required under Regulation 13 of the Securities and Futures (Licensing and Conduct of Business) Regulations (“**SF(LCB) Regs**”) and Regulation 14 of the Financial Advisers Regulations (“**FAR**”) respectively to discharge specified duties. These include ensuring the licence holders’ compliance with rules and regulations.

11 MAS proposes to make explicit that as part of ensuring licence holders’ compliance with rules and regulations, the CEO and directors of licence holders are required to put in place compliance arrangements that are commensurate with the nature, scale and complexity of the licence holder’s business. This proposed requirement is aimed at focusing board and senior management attention on establishing compliance arrangements. This includes identifying issues relating to regulatory requirements as well as in designing controls, policies and procedures for ensuring compliance with regulatory requirements. This proposal is in line with international best practices³.

³ In March 2006, the International Organisation of Securities Commissions (“IOSCO”) released a paper entitled, “Compliance Function at Market Intermediaries”. The paper sets out supplementary principles to assist intermediaries to increase the effectiveness of their compliance function. More specifically, on the role of senior management, the paper notes that it is the role of senior management to establish and

4.1 MAS seeks views on the proposal to make explicit that the CEO and directors of licence holders have to put in place appropriate compliance arrangements for their conduct of regulated activities under the SFA and the FAA.

SECTION 5: LICENSING EXEMPTION FOR PERSONS CONDUCTING FUND MANAGEMENT

12 A person resident in Singapore who conducts fund management on behalf of not more than 30 qualified investors is, upon notification to MAS, exempted from the need to hold a CMS licence pursuant to paragraph 5(1)(d) of the Second Schedule to the SF(LCB) Regs. Such persons are also known as exempt fund managers (“EFMs”). Some EFMs have recently used investment vehicles to solicit investments from non-qualified investors, either directly or indirectly. This does not accord with the basis of the exemption, which is that entities which only deal with a restricted number and specific type of clientele pose a lower supervisory risk. MAS proposes to amend the definition of “qualified investor” to limit mechanisms that have the effect of circumventing the current restrictions on clientele.

(A) Underlying Investors of Local and Foreign Collective Investment Scheme (“CIS”) to be Accredited Investors

13 Currently, a CIS that is offered in Singapore is required to ensure that its underlying investors are all accredited investors for it to be considered a “qualified investor”. For a CIS that is not offered in Singapore, there is no requirement that the underlying investors must be accredited investors. In line with the MAS’ policy intent that an EFM should only serve investors who are

maintain a compliance function, compliance policies and compliance procedures designed to achieve compliance with securities regulatory requirements.

sufficiently sophisticated and able to protect their own interests, MAS proposes to require all underlying investors of a CIS to be accredited investors in order for the CIS to be considered a “qualified investor”, regardless of where a CIS is being offered.

(B) Underlying Investors of Specific Accredited Corporations or Entities to be Accredited Investors

14 MAS seeks to prevent exempt persons from circumventing the clientele restriction by the use of innovative investment vehicles to target retail investors. MAS proposes that a corporation or entity that is an "accredited investor", and which:

- a. is controlled by an EFM or its key officers or shareholders; and
- b. is the subject of an offer or invitation made for subscription or purchase in shares or debentures,

will only be counted as one "qualified investor", if all underlying investors in this corporation or entity are themselves accredited investors.

(C) Extend “Qualified Investor” to Include Closed-End Funds Meeting a Specific Condition

15 In response to industry feedback that the requirements on closed-end funds and CIS should be aligned, MAS proposes to include “closed-end funds” within the definition of “qualified investor”, on the condition that all participants or shareholders of the closed-end fund are accredited investors.

5.1 MAS seeks views on the proposed amendments to the definition of “qualified investor”, and whether there are any conceptual or implementation difficulties with the proposed amendments.

**SECTION 6: LICENSING EXEMPTION FOR PERSONS
CONDUCTING LEVERAGED FOREIGN EXCHANGE
TRADING AND ADVISING ON CORPORATE
FINANCE**

16 Persons conducting leveraged foreign exchange trading or advising on corporate finance to a restricted clientele are exempted from licensing under paragraphs 4(1)(c) and 7(1)(b) of the Second Schedule to the SF(LCB)Regs.

17 MAS intends to amend the above provisions to clarify that the exemptions for conducting these two activities regulated under the SFA apply only to persons who establish, and operate out of, a physical office in Singapore. This is to ensure that the exemption is not abused by fly-by-night operators or shell companies without a physical presence in Singapore.

6.1 MAS seeks views on the proposal to amend paragraphs 4(1)(c) and 7(1)(b) of the Second Schedule to the SF(LCB)Regs to require an exempt leveraged foreign exchange trader or an exempt corporate finance adviser relying on the licensing exemption to be resident in Singapore and to carry out the regulated activity in Singapore.

**SECTION 7: OFFENCES REGULATIONS UNDER THE
SECURITIES AND FUTURES (LICENSING AND
CONDUCT OF BUSINESS) REGULATIONS**

18 MAS intends to amend the SF(LCB)Regs to make non-compliance with requirements under paragraphs 4(6), 5(7) or 7(6) of the Second Schedule to the SF(LCB)Regs offences. These requirements relate to the lodgement of forms

with MAS for the purposes of commencement of business, changes of particulars, cessation of business, and annual declaration.

**SECTION 8: AMENDMENT TO THE DEFINITIONS OF
“ACCREDITED INVESTOR”, “EXPERT INVESTOR”
AND “INSTITUTIONAL INVESTOR” IN THE FAA**

19 Currently, the definitions of “accredited investor”, “expert investor” and “institutional investor” are in both the SFA and the FAA. However, the definitions in the FAA are more restrictive as they exclude certain categories of persons and do not provide MAS power to vary the definitions through subsidiary legislation. MAS proposes to amend the FAA to align the definitions of “accredited investor”, “expert investor” and “institutional investor” in the FAA with those under section 4A of the SFA.

**SECTION 9: AMENDMENT TO PROVISION ON EXEMPTION FOR
GIVING ADVICE OR ANALYSIS ON BONDS**

20 Currently, regulation 28 of the FAR provides exemption to FAs and their representatives who give advice or analysis on bonds to an expert investor or an accredited investor from most of the business conduct requirements. This includes the obligation to disclose product information to clients as stipulated under section 25 of the FAA.

21 The disclosure requirements of section 25 only apply to a CIS or a life policy (including a group life policy). Section 25 does not apply to the provision of advice on bonds. MAS proposes to rectify the technical error by deleting the reference to section 25 from regulation 28 of the FAR.

SECTION 10: CONFIDENTIALITY OF INSPECTION AND INVESTIGATION REPORTS

22 MAS is empowered to inspect the books of an approved holding company, a securities exchange, a futures exchange, a recognised market operator, a person operating an exempt market, an exempt market operator, a designated clearing house, a CMS licence holder, an exempt person or a representative under Section 150 of the SFA in relation to their capital markets activities. MAS may also conduct any investigation it considers necessary pursuant to Section 152 of the SFA. Sections 70 and 71 of the FAA contain similar provisions for inspection and investigation of financial advisory activities.

23 Persons inspected or investigated by MAS are currently not permitted to disclose the contents of MAS inspection or investigation reports to anyone other than an officer or auditor of the inspected or investigated entity, in connection with the execution of their official duties. To give legal certainty to this existing practice, MAS proposes to amend the SFA and FAA to make explicit the existing requirement. Any exception to the existing practice would require MAS' written approval.

SECTION 11: REQUIREMENT TO SEEK APPROVAL FOR TAKE-OVER OF LICENSEES

24 Under Regulation 39(1) of the FAR, should a person enter into any arrangement which if carried out, would result in his obtaining effective control of a licensed FA, he must obtain MAS' prior approval for the arrangement. There is no similar provision in the SFA.

25 To ensure effective gatekeeping, MAS proposes to make it a requirement under the FAA and the SFA for a potential owner or controller to seek MAS' prior approval before entering into an arrangement which would result in him obtaining effective control⁴ of a holder of a FA licence or a CMS licence or both. This requirement would apply to potential owners or controllers both in Singapore or elsewhere.

11.1 MAS seeks views on the proposal to make it a requirement for a potential owner or controller, whether in Singapore or elsewhere, to seek MAS' prior approval before entering into an arrangement which would result in him obtaining effective control of a holder of a FA licence or a CMS licence.

SECTION 12: FIT AND PROPER REQUIREMENTS IN RELATION TO CERTAIN EXEMPT PERSONS

26 Currently, MAS requires exempt leveraged foreign exchange traders⁵, EFMs⁶, exempt corporate finance advisers⁷ and exempt FAs serving not more than 30 accredited investors⁸ (collectively referred to as "**exempt persons**") to ensure that they and all their directors and representatives are fit and proper. This is because MAS expects exempt persons, their directors and representatives to be competent, honest, to have integrity and to be of sound financial standing.

⁴ A person shall be regarded as entering into an arrangement by virtue of which he would obtain effective control of a holder of aFA licence and/or a CMS licence if the person alone or acting together with any connected person would be in a position to control not less than 20% of the voting power in the licence holder or would hold interests in not less than 20% of the issued shares of the licence holder.

⁵ Exempted from licensing under paragraph 4(1)(c) of the Second Schedule to the SF(LCB) Regs.

⁶ Exempted from licensing under paragraph 5(1)(d) of the Second Schedule to the SF(LCB) Regs.

⁷ Exempted from licensing under paragraph 7(1)(b) of the Second Schedule to the SF(LCB) Regs.

⁸ Exempted from licensing under regulation 27(1)(d) of the FAR.

27 Substantial shareholders of an exempt person and any other person who has effective control over an exempt person are able to affect the way the exempt person functions. MAS proposes to extend the fit and proper requirements to:

- a. substantial shareholders of an exempt person (and their equivalent where the exempt person is not a corporation); and
- b. any other person who has effective control⁹ over an exempt person

12.1 MAS seeks views on the proposal to extend the fit and proper requirements to:

- a. substantial shareholders of an exempt person (and their equivalent where the exempt person is not a corporation); and**
- b. any other person who has effective control over an exempt person.**

SECTION 13: AMENDING THE DEFINITION OF “SECURITIES” AND “FUTURES CONTRACT” IN THE SFA AND THE FAA

28 The definitions of securities¹⁰ in the SFA and the FAA take the form of a list of products that are designated as securities, and also lists products that are explicitly excluded as securities. It is necessary to amend the SFA each time MAS decides to bring a new product within its regulatory ambit. This affects the time-to-market for new products.

⁹ As defined in footnote 4, or its equivalent in a non-corporate structure.

¹⁰ “Securities” is defined at section 2(1), section 196A, section 214 and section 239 of the SFA. The FAA definition of “securities” references section 2(1) of the SFA.

29 We propose to amend the definitions of “securities” to enable MAS to prescribe new products as “securities” in the SFA and the FAA.

30 We also propose to give MAS the ability to exclude products which might otherwise be caught under the “securities” or “futures contract”¹¹ definitions in the SFA and the FAA. This would allow MAS to remove from its regulatory ambit, those products which may not normally be characterised by market participants as financial instruments.

13.1 MAS seeks views on the proposal to amend the definitions of “securities” and “futures contract” in the SFA and the FAA to enable MAS to:

- a. prescribe new products as “securities”; and**
- b. prescribe excluded products from the definitions of “securities” and “futures contract”.**

¹¹ “Futures contract” is defined at section 2(1) of the SFA and at section 2(1) of the FAA.



Monetary Authority of Singapore