

CATEGORIES OF BROKERS IN SINGAPORE							
Type of Membership	Number	SES Member	Minimum Capital (S\$m)	Turnover (S\$ bn)		Market Share (%)	
				Yr 1996	Yr 1997	Yr 1996	Yr 1997
Local Member	17	Yes	30	143.967	185,911	43.6	46.8
Members with Foreign Partners	9	Yes	30	117,649	132.466	35.6	33.4
International Members	7	Yes	30	42.563	46.888	12.9	11.8
Approved Foreign Brokers	5	No	3	10.352	13.591	3.1	3.4
Foreign Brokers	52	No	2*	15.722	18.265	4.8	4.6

* Net Head Office Funds for branches or S\$2 m shareholders' funds

MARKET TURNOVER (JAN96 - DEC 97)

[S\$]

	S\$ TRADES		NON S\$ TRADES	
	1996	1997	1996	1997
APPROVED FOREIGN BROKERS (THRU' MCs)	9,486,214,821.54	12,608,809,249.43	0.00	0.00
APPROVED FOREIGN BROKERS	0.00	0.00	866,084,377.91	983,172,185.56
INTERNATIONAL MEMBERS	19,637,402,259.56	24,480,810,141.24	22,926,010,134.20	22,407,597,702.34
MEMBER COMPANIES	135,517,519,979.76	165,097,865,835.42	126,098,687,454.57	153,278,532,093.52
FOREIGN BROKERS (THRU' MCs)	10,417,273,039.29	10,655,770,044.71	5,305,355,312.16	7,610,027,614.05

	1 - 99K			100-249K			250-499K			500-749K			750-999K			1-1.499M			ABV 1.5M			TOTAL		
	Contracts [no]	Proceeds [\$]	Ave Proceeds [\$]	Contracts [no]	Proceeds [\$]	Ave Proceeds [\$]	Contracts [no]	Proceeds [\$]	Ave Proceeds [\$]	Contracts [no]	Proceeds [\$]	Ave Proceeds [\$]	Contracts [no]	Proceeds [\$]	Ave Proceeds [\$]	Contracts [no]	Proceeds [\$]	Ave Proceeds [\$]	Contracts [no]	Proceeds [\$]	Ave Proceeds [\$]	Contracts [no]	Proceeds [\$]	Ave Proceeds [\$]
1996	7,510,936 94.7%	80,980,582,859 26.6%	10,782	217,337 2.7%	34,146,926,002 11.2%	157,115	99,778 1.3%	35,068,743,366 11.5%	351,468	38,971 0.5%	23,790,711,143 7.8%	610,472	19,751 0.2%	17,050,611,096 5.6%	863,278	20,832 0.3%	25,433,292,813 8.4%	1,220,876	27,377 0.3%	87,708,752,549 28.8%	3,203,739	7,934,982 100.0%	304,179,619,828 100.0%	6,417,730
1997	10,825,603 95.9%	100,073,702,150 27.4%	9,244	232,374 2.1%	36,431,047,916 10.0%	156,778	105,691 0.9%	37,166,955,134 10.2%	351,657	41,865 0.4%	25,537,133,016 7.0%	609,988	22,467 0.2%	19,432,710,100 5.3%	864,945	23,222 0.2%	28,245,278,829 7.7%	1,216,316	34,623 0.3%	118,377,978,628 32.4%	3,419,056	11,285,845 100.0%	365,264,805,772 100.0%	

* Proceeds refer to (stock price) x (volume)

SUMMARY OF ANALYSIS OF OPTION 1

		YEAR				
		1993	1994	1995	1996	1997
SCENARIO 1:	First S\$250,000	0.5%				
	> S\$250,000	0.1%				
	Number of Profitable Firms	13	12	9	14	12
	Profit Range (S\$ mil)	0.002 - 24.5	0.5 - 48.9	0.3 - 26.8	0.07 - 24.8	0.3 - 18.4
	Greatest Losses (S\$ mil)	(17.9)	(34.1)	(22.7)	(36.3)	(25.9)
SCENARIO 2:	First S\$250,000	0.5%				
	> S\$250,000	0.2%				
	Number of Profitable Firms	16	15	11	15	15
	Profit Range (S\$ mil)	0.06 - 26.9	0.2 - 51.3	0.3 - 28.3	0.3 - 26.4	0.3 - 27.7
	Greatest Losses (S\$ mil)	(16.4)	(22.2)	(14.3)	(29.8)	(24.3)
SCENARIO 3:	First S\$250,000	0.5%				
	> S\$250,000	0.25%				
	Number of Profitable Firms	16	18	13	16	16
	Profit Range (S\$ mil)	0.09 - 28.1	0.1 - 52.4	0.4 - 29.0	0.7 - 27.1	0.3 - 33.9
	Greatest Losses (S\$ mil)	(15.7)	(16.3)	(11.3)	(26.6)	(23.5)
SCENARIO 4:	First S\$250,000	0.5%				
	> S\$250,000	0.3%				
	Number of Profitable Firms	16	19	15	18	19
	Profit Range (S\$ mil)	0.1 - 29.4	0.02 - 53.6	0.4 - 29.8	0.6 - 27.9	0.2 - 40.1
	Greatest Losses (S\$ mil)	(15.0)	(11.7)	(8.5)	(23.4)	(22.7)
SCENARIO 5:	First S\$250,000	0.5%				
	> S\$250,000	0.4%				
	Number of Profitable Firms	18	23	23	24	20
	Profit Range (S\$ mil)	0.2 - 42.8	0.2 - 55.9	0.06 - 31.2	0.2 - 35.3	0.6 - 52.5
	Greatest Losses (S\$ mil)	(13.5)	(9.6)	(6.9)	(17.0)	(21.1)

SUMMARY OF ANALYSIS OF OPTION 2

		YEAR				
		1993	1994	1995	1996	1997
SCENARIO 1:	First S\$250,000	0.75%				
	> S\$250,000	0.1%				
	Number of Profitable Firms	26	22	19	19	22
	Profit Range (S\$ mil)	0.05 - 33.8	1.3 - 84.3	0.07 - 42.6	0.9 - 34.6	0.2 - 27.2
	Greatest Losses (S\$ mil)	(4.8)	(11.0)	(18.9)	(34.0)	(21.5)
SCENARIO 2:	First S\$250,000	0.75%				
	> S\$250,000	0.2%				
	Number of Profitable Firms	26	24	21	21	24
	Profit Range (S\$ mil)	0.3 - 36.2	1.9 - 86.7	0.7 - 44.1	0.07 - 36.1	0.2 - 30.1
	Greatest Losses (S\$ mil)	(3.7)	(7.4)	(11.3)	(27.6)	(20.3)
SCENARIO 3:	First S\$250,000	0.75%				
	> S\$250,000	0.25%				
	Number of Profitable Firms	26	29	24	24	25
	Profit Range (S\$ mil)	0.3 - 37.4	0.04 - 87.8	0.1 - 44.9	0.07 - 36.9	0.4 - 36.3
	Greatest Losses (S\$ mil)	(3.3)	(5.6)	(8.3)	(24.3)	(19.8)
SCENARIO 4:	First S\$250,000	0.75%				
	> S\$250,000	0.3%				
	Number of Profitable Firms	27	30	25	24	25
	Profit Range (S\$ mil)	0.3 - 41.0	0.3 - 89.0	0.1 - 45.6	0.2 - 37.6	0.5 - 42.6
	Greatest Losses (S\$ mil)	(3.0)	(3.8)	(5.3)	(21.1)	(19.2)
SCENARIO 5:	First S\$250,000	0.75%				
	> S\$250,000	0.4%				
	Number of Profitable Firms	28	31	28	27	27
	Profit Range (S\$ mil)	0.4 - 51.3	0.4 - 91.3	0.3 - 47.1	0.3 - 39.2	0.09 - 55.0
	Greatest Losses (S\$ mil)	(2.5)	(0.3)	(1.6)	(14.7)	(18.1)

ACTUAL P/L

	1993	1994	1995	1996	1997
Aggregate Profits Before Tax:	775,809,774	1,025,408,166	548,348,144	460,602,996	482,176,641
Aggregate Losses Before Tax:	(1,154,285)	0	(345,445)	(20,393,239)	(32,430,933)
P/L AFTER SCENARIO 2 OF OPTION 1*					
	1993	1994	1995	1996	1997
Aggregate Profits Before Tax:	110,142,163	141,982,399	90,040,041	137,193,425	135,321,395
Aggregate Losses Before Tax:	(90,034,893)	(106,480,587)	(97,829,778)	(83,325,519)	(107,919,324)
P/L AFTER SCENARIO 2 OF OPTION 2**					
	1993	1994	1995	1996	1997
Aggregate Profits Before Tax:	303,570,406	398,793,906	234,855,120	240,461,074	256,901,437
Aggregate Losses Before Tax:	(13,731,744)	(13,791,343)	(38,374,421)	(50,025,175)	(62,000,164)

Proposed Brokerage Structures:

* First S\$250,000: 0.5%; above S\$250,000: 0.2%

** First S\$250,000: 0.75%; above S\$250,000: 0.2%

RECOMMENDATIONS ON COMPETITION*

SES Membership	<p>1 ä Current restrictions on local ownership of SES members to be removed. All financially sound local entities will be allowed to buy stakes of any size in local member companies.</p> <p>2 ä All securities professionals dealing in SES-listed and/or quoted securities are required to pass the Dealer's Representative's (DR) examination. Securities professionals dealing solely in non-SES listed and/or quoted securities should either possess a DR licence or possess an appropriate professional qualification to deal in those securities as determined by SES.</p> <p>3 ä No additional Approved Foreign Brokers (AFB) would be admitted and existing AFBs would be encouraged to seek International Member (IM) status.</p> <p>6 ä IMs be allowed to trade freely with any foreign clients and SES-approved local financial institutions.</p> <p>7 ä IMs be allowed to stand for election as SES Committee members and vote on election of SES Committee members.</p>			
	<p><u>INTERIM (Subject to McKinsey-MAS Review)</u></p>			
	<p><u>INTERIM</u></p> <p>8 ä No new seats to be issued.</p>		<p><u>FROM 1.1.2000</u></p> <p>8 ä New seats may be issued if current ownership structure of SES remains.</p>	
Commission	<p><u>FROM 1.1.1999</u></p>		<p><u>FROM 1.1.2000</u></p>	
	<p>10 ä Amalgamation of trades allowed for approved fund managers.</p> <p>11 ä Life insurance companies, finance companies, and fund management companies which are exempt IAs under Regulation 41(1)(e) of Securities Industry Regulations to be eligible for rebate of 25% of brokerage.</p>	<p>12 ä Minimum commission rates to be reduced by 5% for all transactions until 31.12.1999.</p> <p>13 ä Minimum brokerage per contract raised from \$2 to \$10.</p> <p>14 ä Commission for pure fixed income securities and non-Singapore dollar denominated securities should be fully negotiable.</p>	<p>15 ä All rebates to be eliminated.</p> <p>16 ä Commission for : Trades at or below S\$150,000 minimum 0.75 % Trades above S\$150,000 will be freely negotiable.</p> <p>17 ä Commission for approved fund managers to be freely negotiable.</p> <p>18 ä Stamp duty and GST to be eliminated.</p>	<p><u>BY 1.1.2003</u></p> <p>19 ä Commission for all trades to be fully negotiable.</p>

* The number of the recommendation corresponds with that in Part 4 of the SESRC which should be consulted for details.

OTHER RECOMMENDATIONS OF THE REGULATORY ENVIRONMENT

S/N	Issue/Existing Rule	Proposed Change(s)	Analysis
1	<u>Relationship between SES and Member Firms</u>	<ul style="list-style-type: none"> • Prior to amending its Bye-Laws or the issue of any practice notes, the SES should consult member companies for feedback; and • A quarterly forum or workshop should be conducted to allow SES and member firms to discuss problems/difficulties faced. 	To allow for two-way dialogue between SES and member firms and to promote transparency in regulation.
2	<u>Discipline of Brokers</u>	The underlying reason for imposing any operational directive or administrative sanction against a member firm, for example, imposing a cap on the number of DRs which the member firm could engage, should be specified clearly to the affected member firm.	To ensure transparency in regulation.
3	<u>Education</u>	As in the case of DRs, all mid-office/back-office personnel (of officer level) of member firms should be required to attend compulsory courses.	To ensure that mid-office/back-office personnel are up to scratch so that they are able to support the other proposals for stockbroking companies to venture into other businesses.
4	<u>Dealer's Representative (DR)'s Clerks</u> DR's clerks presently share the same dealing IDs and terminals as their principals.	Consideration could be given to allow DR's clerks to have their own terminals but with the same ID as their principals.	

S/N	Issue/Existing Rule	Proposed Change(s)	Analysis
5	<p><u>Dealer's Representatives (DRs)</u></p> <p>A DR shall not have an interest in a stockbroking company, other than the stockbroking company to which the DR is attached as employee or agent.</p>	<p>DRs should be permitted to have an interest in stockbroking companies (other than the one to which the DR is attached as employee or agent), provided that such interest does not exceed 5% of the issued capital of the company and is confined to SES member firms.</p>	

LICENSING REQUIREMENTS

1 Recommendation to Change Licensing Requirements

1.1 Currently, the existing regulatory structure permits SES members to engage in all securities-related activities. It is proposed that in addition to the core activities of stockbroking, SES members could be permitted to perform transactions in the following additional expanded listed and over-the-counter (OTC) securities-related activities and financial instruments:

- (i) securities-linked futures derivatives;
- (ii) tax investment vehicles;
- (iii) mutual funds / unit trust (discretionary and non-discretionary);
- (iv) securities-linked insurance products;
- (v) bonds / convertible bonds;
- (vi) corporate finance activities
- (vii) money market instruments such as cash deposits and Treasury bills in selected countries;
- (viii) Exchange traded and OTC financial futures contracts;
- (ix) interest rate, currency and equity swaps; and
- (x) options to acquire or dispose of any of the above financial instruments

1.2 It is recommended that securities-related activities be generally classified into core investment services and non-core investment services. Core investment services would include:

- (i) reception and transmission, on behalf of investors, of orders in relation to one or more of the defined financial instruments;
- (ii) execution of such orders other than for their own account;
- (iii) dealing as principal in any of the financial instruments;
- (iv) discretionary management of investment portfolios which include financial instruments;

- (v) underwriting or placing of financial instruments; and
- (vi) corporate finance activities

1.3 Non-core investment services would include:

- (i) providing finance to an investor to allow him to carry out a transaction in a financial instrument and the firm providing the finance is involved in the transaction;
- (ii) providing advice on capital structure, industrial strategy, mergers and acquisitions and related matters;
- (iii) services related to underwriting such as arranging syndications; and
- (iv) investment advice on one or more of the financial instruments

1.4 It is recommended that the size of shareholders funds or net asset valuation be used as a key quantitative factor to limit the permissible range of activities which each SES member is allowed to perform. It implies that SES members with larger shareholders' funds or net asset valuation will automatically qualify to engage in a wider range of activities.

1.5 The following table outlines the category of Investment Financial Services (IFS) Licence, including the corresponding activities that the SES members may engage, based on their level of shareholders' funds.

Category	Authorised Activities	Note	Shareholders Funds
A	<ul style="list-style-type: none"> • provide one or all of the core and non-core investment services including client assets. 		S\$200 Million
B	<ul style="list-style-type: none"> • receiving and transmitting orders (core) • executing orders on an agency basis (core) • dealing as principal (core) but only holding positions as a result of its failure to match investor's orders precisely, and <ul style="list-style-type: none"> - such positions are incidental and provisional in nature and strictly limited to the time required to carry out the transaction in question; and 	It is not authorised to hold client money or assets and for that reason may not at any time place itself in debit with its clients.	S\$150 Million

Category	Authorised Activities	Note	Shareholders Funds
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B	<ul style="list-style-type: none"> - the total market value of all such positions does not exceed a percentage of the firm's initial capital • managing investments on a discretionary basis (core) • non-core investment services • client money and safeguarding of client assets. 		
C	<ul style="list-style-type: none"> • receiving and transmitting orders (core) • executing orders on an agency basis (core) • managing investments on a discretionary basis (core) • dealing as principal (core) but only holding positions as a result of its failure to match investor's orders precisely, and <ul style="list-style-type: none"> - such positions are incidental and provisional in nature and strictly limited to the time required to carry out the transaction in question; and - the total market value of all such positions does not exceed a percentage of the firm's initial capital • non-core investment services 	It is not authorised to hold client money or assets and for that reason may not at any time place itself in debit with its clients.	S\$75 Million
D	<ul style="list-style-type: none"> • receiving and transmitting orders on behalf of investors in relation to one of more of the financial instruments (core). It cannot execute such orders or take on any proprietary positions. • dealing as principal (core) but only holding positions as a result of its failure to match investor's orders precisely, and <ul style="list-style-type: none"> - such positions are incidental and provisional in nature and strictly limited to the time required to carry out the transaction in question; and 	Not authorised to hold client money or assets and for that reason may not at any time place itself in debit with its clients.	S\$30 Million

Category	Authorised Activities	Note	Shareholders Funds
D	- the total market value of all such positions does not exceed a		

	percentage of the firm's initial capital		
	<ul style="list-style-type: none">• non-core investment services		

DEVELOPMENT OF A SECURITIES BORROWING AND LENDING PROGRAM IN SINGAPORE

1 **Characteristics of a Securities Borrowing and Lending (SBL) Program**

1.1 The following outline the characteristics of a SBL program in most developed markets:

- (i) SBL entails the transfer of the securities' ownership from the lender to the borrower. This transfer is matched by a corresponding transfer of collateral from the borrower to the lender. The collateral may be in the form of cash, equity, convertible bonds holdings, letters of credit and G7 bonds;
- (ii) in any SBL transaction, the lender should be made whole in the event of a corporate action. Since ownership has been transferred from the lender to the borrower, and the borrower gets to retain the entitlements, the borrower should make good these entitlements to the lender;
- (iii) lenders may recall the shares any time, and this is usually effected by the settlement date of the market i.e. T+2 in Hong Kong. To avoid the need to recall shares frequently to meet other obligations, most lenders will only lend up to 50-60% of the available stock of any security;
- (iv) the SBL market is an over-the-counter ('OTC') driven market where the quotes are usually obtained and traded via the phones or Bloomberg terminals;
- (v) lenders may conduct SBL transactions in the following manner:
 - ❖ as principal;
 - ❖ out-source the assets to a custodian bank to lend to a few designated borrowers;
 - ❖ lend only to the entity that it provides exclusive bids in the market;
 - ❖ appoint broker/dealer to handle the transactions.

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- (vi) the SBL documentation should provide for either parties to liquidate the borrowed securities holdings or collateral in the event that the counterparty should suffer a financial default. In the case of Peregrine, a hitch occurred as the lenders of securities to Peregrine moved these securities on Asian time and expected the cash collateral to come in on U.S. time. In between the timing, the public announcement of Peregrine's dire financial situation resulted in the U.S. banks withholding the cash collateral designated for the lenders' account although the securities had already moved to Peregrine's account. Because the principal risk is counterparty risk, this is a credit risk exercise;
 - (vii) in Malaysia, the Securities Commission requires that the lender appoint an external auditor to audit the borrowing party's financial credibility. The results of the audit will then be submitted to the Commission for its approval. There is also a need to have an efficient operating system, including a daily 'mark to markets' system and a 105% collateral for the loan. In addition, there should be a 6 month credit review;
 - (viii) SBL participants may design their own system or buy one off the shelf to manage the SBL business;
 - (ix) fund managers in the past were not that interested in the SBL business as it might only offer a 1-2% return compared with the market's return of about 50%. This has since changed due to the lower returns from the market and fund managers have increasingly begun to re-look at the SBL business;
 - (x) Japan has the largest regional market in the SBL business. Although 93% of the Japanese equity market is held by the locals, about 95-97% of the SBL activities is conducted by offshore participants. It would certainly make more business sense for the Japanese market if more of the SBL business is conducted locally;
 - (xi) in Hong Kong , there are plans in the pipeline to revise the rules to permit all securities to be eligible for SBL transactions which in turn implies that all securities be eligible for short selling. The Hong Kong authorities are also looking at liberalising the rules to permit the lending of new IPOs securities and securities held by the Provident Fund;
 - (xii) the lender of the borrowed securities may only sell them once in the securities market, and not multiple times as is conceived by some quarters. The downward pressure on short selling borrowed securities may eventually be neutralised by an upward pressure when the lender has to buy back the securities;
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- (xiii) there should be no time frame for expiry of stock lending as this is disruptive to the trade; and
 - (xiv) it is essential that all 'stock loan' transactions be exempted from tax, GST, stamp duty for there are promises to repay the stock borrowed and these are really 'manufactured transactions'.

2 Benefits of a SBL Program

2.1 The prerequisites and benefits of a successful SBL program may be outlined as follows:

- (i) market makers who provide liquidity need an efficient successful SBL market.
- (ii) a successful and efficient SBL is essential to a vibrant options/derivatives market e.g. hedge trading;
- (iii) to attract hedge fund managers (estimated at 2,000), a successful and efficient SBL market is essential; and
- (iv) SBL provides more liquidity in the cash equity market for domestic and international players.

2.2 With the likely implementation of a SBL program in Singapore, there will be more onshore activity brought back from outside centres like Hong Kong. For activities that are conducted offshore of Singapore, the revenue will be brought back onshore.

3 Proposed Steps for SES to Adopt to Embark on a SBL Program

3.1 The following are the proposed steps that SES may consider adopting to embark on a successful SBL program:

- (i) impose no time frame on the duration of the SBL transaction. In Hong Kong, the time frame for an open SBL transaction is 1 year, whereby both borrowers and lenders have to renew the transaction after every year;
- (ii) to include all securities as eligible for SBL;
- (iii) incorporate the disclosure of counterparty identities in the SBL agreements;

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- (iv) address the issue of stamp duty and GST on SBL transactions with the tax authorities. Any tax on SBL transactions will effectively remove any profit incentive to undertake such a transaction;
 - (v) study the feasibility of introducing a circuit breaker to the SES to reduce any downfall in the market which may be resulted from short selling; and
 - (vi) study the ways to allow holders of securities invested using CPF funds to lend these securities for a higher return.

4 Considerations

- 4.1 A SBL program for all SES stocks might not be possible as it would subject the market to manipulation since some companies have low market capitalisation.
- 4.2 Although the SES Bye-Laws on SBL have already been drafted, a major foreseeable hurdle is the SES regulation which only covers SES members but not custodian banks.
- 4.3 Some participants might have an advantage in the SBL business over the SES members since they are not subject to any adjusted net capital ('ANC') requirements. For example, foreign brokers might have an advantage over the SES members in the SBL business since they are not subject to the single security exposure clause in the Bye-Laws.

REGULATED SHORT SELLING

1 Framework for a Regulated Short Selling Environment

- 1.1 Short selling provides a useful price stabilization mechanism and adds liquidity to the market. Sharp market declines can be smoothed since short sellers will buy stock when they attempt to lock in their profits by covering their short positions in a falling market. Over-valuation of individual stocks can also be prevented. Short selling is critically important to the growth of any equity capital market. The development of any equity index/stock futures or options contract must include the ability to hedge in the cash market via short selling. Short selling allows investors to hedge their futures/options positions by taking offsetting positions in the cash market.
- 1.2 Short selling refers to the sale of securities, which the seller does not own at the time of the sale. It is a technique used to take advantage of an anticipated decline in stock price or alternatively to protect (hedge) against a long position (equities, futures or options).
- 1.3 To settle the transaction, the short seller borrows the securities for delivery. The short seller will borrow the shares from a lender. The borrower is required to put up collateral and he will pay a fee to borrow. If the stock price falls, he can purchase the securities at a lower price to return the shares to the lender.
- 1.4 In most developed markets such as the UK, US, Australia, Hong Kong short selling is legal. Malaysia and Thailand both introduced regulated short selling in the past year.
- 1.5 It is generally agreed that short selling should be subject to regulations and should be transparent as possible. Legislation in different markets have passed specific regulations to promote and monitor short selling.
- 1.6 Some of the issues that need to be addressed are as follows:
 - (i) tax issues;
 - (ii) designated Issues for short selling;
 - (iii) at what price can the short sale be executed – uptick or zero tick rule;

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- (iv) short selling must be indicated on the contract note;
 - (v) broker must ensure that the short seller has made prior arrangement to borrow;
 - (vi) reporting of short sales to the Exchange;
 - (vii) can the short sale be traded direct or through automated trading system;
 - (viii) who is permitted to engage in regulated short selling;
 - (ix) internal systems/procedures/training must be in place;
 - (x) will the SES or MAS have the power to prohibit short selling at any time;
 - (xi) stamp duty;
 - (xii) margin requirements; and
 - (xiii) maximum or minimum shorting periods – would have to be in line with limits on SBL

DEVELOPMENT OF LISTED PROPERTY TRUSTS IN SINGAPORE

1 Characteristics of Listed Property Trusts (LPTs) Vehicles in Australia

1.1 The following characteristics outline how a LPT is structured in Australia. Singapore can draw the experiences in Australia to develop its own LPT vehicles. This is especially relevant considering the similarities of existing corporation laws in both countries.

- (i) Definition
LPTs are closed-end listed vehicles that pool the funds of a number of unitholders for the sole intention of real estate investment.
- (ii) Legal Structure
Trustee holds assets on behalf of unitholders under deed of trust. There is no perpetual existence to the trust.
- (iii) Corporate Structure
Primarily Trust Structure - unitholder owns a unit in the vehicle which holds the property.
- (iv) Management
External manager appointed by Trustees. Generates fees as a percentage of gross assets.
- (v) Tax Structure
No corporate tax payable if 100% of taxable income is distributed to unitholders. Unitholders' yield from the trust are then taxed at their individual income bracket level.

2 The Case for Developing LPT Vehicles in Singapore

2.1 Based on the Australian and US experience, maturing real estate markets tend to follow a transition from private to public ownership, in order to address management succession and to secure reliable, less expensive sources of capital.

2.2 As Singapore's real estate market matures, the trend towards unitisation/ securitisation of property is likely to gain momentum, as it is in many other economies of the world.

2.3 An LPT market would provide Singapore with:

- (i) a more stable and mature property investment climate with a clear division between property development companies and property investment companies;
- (ii) an additional investment instrument, which would add further credence to Singapore's aspirations of being a world-class financial centre;
- (iii) a mechanism for both individual and institutional investors to participate in the longer-term investment returns available from real estate;
- (iv) a more efficient property sector, characterised by greater liquidity, a redistribution of capital and free flow of information;
- (v) improved real estate skills and management expertise; and
- (vi) greater levels of foreign investment

2.4 An LPT market would provide existing owners of Singapore real estate with the following benefits:

- (i) allow unlisted entities to liberate capital from their balance sheet, enabling proceeds to be used to reinvest or repay debt;
- (ii) sale price of properties sold into trust structure will be dependent on the individual characteristics of the property (i.e. location, age, lease profile) and will be subject to a more rigorous valuation approach;
- (iii) the Singapore property owner can retain a controlling interest in an LPT by
 - ❖ selling down a minority interest in individual properties;
 - ❖ retaining a majority interest in individual property trust to ensure the largest voting rights; and
 - ❖ creating a separate trust management entity that will externally manage day-to-day property operations on behalf of the trust's unitholders.
- (iv) the prevailing market conditions are not conducive to property development, with development projects in both Singapore and the region unlikely to become viable over the short term.

3 Considerations

3.1 To successfully develop the LPT market in Singapore, the authorities have to resolve the following issues which may prove to be impediments.

3.2 LPTs are structured such that 100% of the taxable income all flows through to the unitholders. The LPTs are then taxed in the hands of the unitholders based on their individual tax bracket level. This is similar to the taxation policy on equity unit trusts.

The successful development of a LPT market in Singapore hinges on the authorities' views towards the taxation policy on LPT. The LPT market will receive a more favourable response from investors if LPTs are taxed at the unitholders' level and not corporate level.

3.3 Residential property transactions in Singapore do not attract capital gains tax unless the purchase and sale transaction effected by the same party is made within 3 years. This is a result of the 1996 May 15 initiatives on residential property transactions by the Government to curb excessive speculation in the property market.

It remains unclear whether unitholders of LPT (assuming of residential nature) who have made a purchase and sale transaction in the units within 3 years are subject to some form of capital gains tax similar to those applicable to investors who have made direct investments in residential properties.

3.4 Currently, Central Provident Fund (CPF) holders who use their CPF funds to invest in the stock market are only permitted to purchase trustee stocks designated by CPF. Trustee stocks are selected based on certain quantitative criteria including a satisfactory track record in profitability.

Since LPTs, like equity unit trusts, are launched without any previous track record, CPF rules will prohibit holders from using their CPF funds to invest in the LPT fund upon its launch. This will substantially reduce the demand for LPTs. The authorities may wish to consider lifting this track record requirement to permit CPF funds to be invested in LPT funds.

A substantial portion of the contents of this paper is extracted from the presentation delivered by SBC Warburg Dillon Read to the SES Review Committee.

DEVELOPMENT OF A MULTI-CURRENCY MULTI-ASSET MANAGEMENT ACCOUNT

1 Characteristics of a Multi-Currency Multi-Asset Management Account

- 1.1 The object of this Paper is to outline the framework of the Brokerage account that US Brokers use for their Retail clients. It has enabled firms like Merrill Lynch to be a Global player and increase shareholders' capital by thirty-fold over 15 years.
- 1.2 For stockbrokers (dealers) in Singapore it is important to overcome its biggest limitation to its self-development. This is the inability of member firms to book customers' assets in its own accounting system and hold multi-currency assets on behalf of its customers.
- 1.3 A multi-currency multi-asset management account (MMA) would give investors the convenience of not only transacting any range of products eg unquoted equity linked notes but also have their investment portfolios "housed" in one central location. In addition, clients can write cheques or borrow against the loan value of their investment portfolio.
- 1.4 This will be the best generator of large Regional accounts a Singapore broker can have. See Charts Appendix 11.1 and 11.2.
- 1.5 The features are as follows:-
 - i) an automatic computerised sweep of any idle cash into a choice of multi-currency money market accounts which is free from income tax, GST, etc. The Bye-laws will need to be changed;
 - ii) automatic sweep when purchases are made, firstly from idle cash and then, secondly from the money market funds and thirdly from margin facilities if there are insufficient funds;
 - iii) easy access to your assets with bank cheques and a Visa card that can be used worldwide;
 - iv) margin facilities that are based on the marginability or loan value of the assets held. This gives instant borrowing powers at attractive rate (broker loan rate);

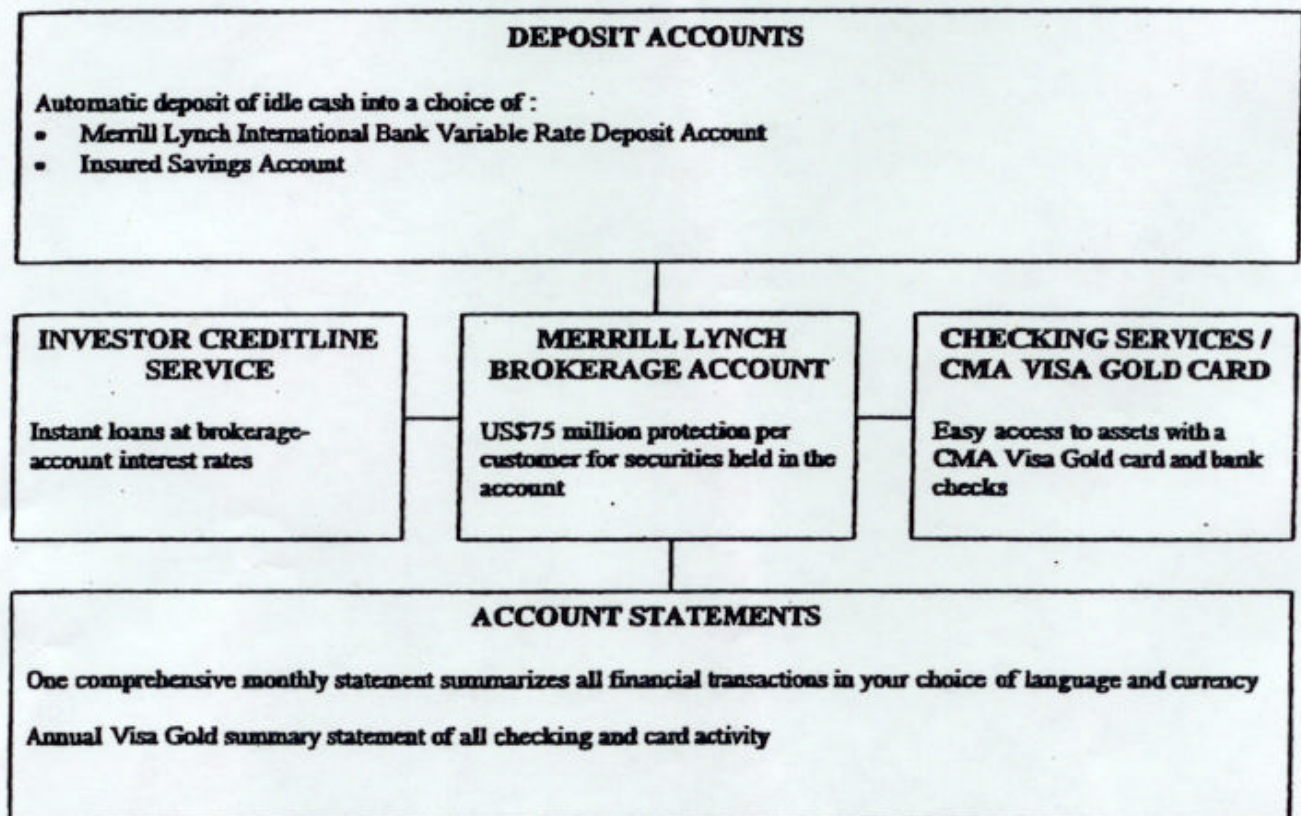
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- v) travel accident insurance and a protection for securities or assets by the firm through an insurance corporation eg. SIPC which is the “Statutory Investor Protection Corporation”. This acts like a lifeboat fund to protect the separate assets “Cash” and “Securities” of customers in case of failure of that broker. Also broker firms can take additional insurance coverage for the additional assets of its customers elsewhere;
 - vi) one comprehensive multi-currency monthly statement in your choice of language that summarises all the purchases, sales, cash transactions, borrowings, dividend receipts, interest payouts, details of cheques written and Visa transactions; and
 - vii) professional advice from a dealer. However we may have to change regulations to allow development of dealer representatives to a financial planner or private banker but employed by a stockbroking firm.

1.6 In summary, this integrated account has the following advantages:-

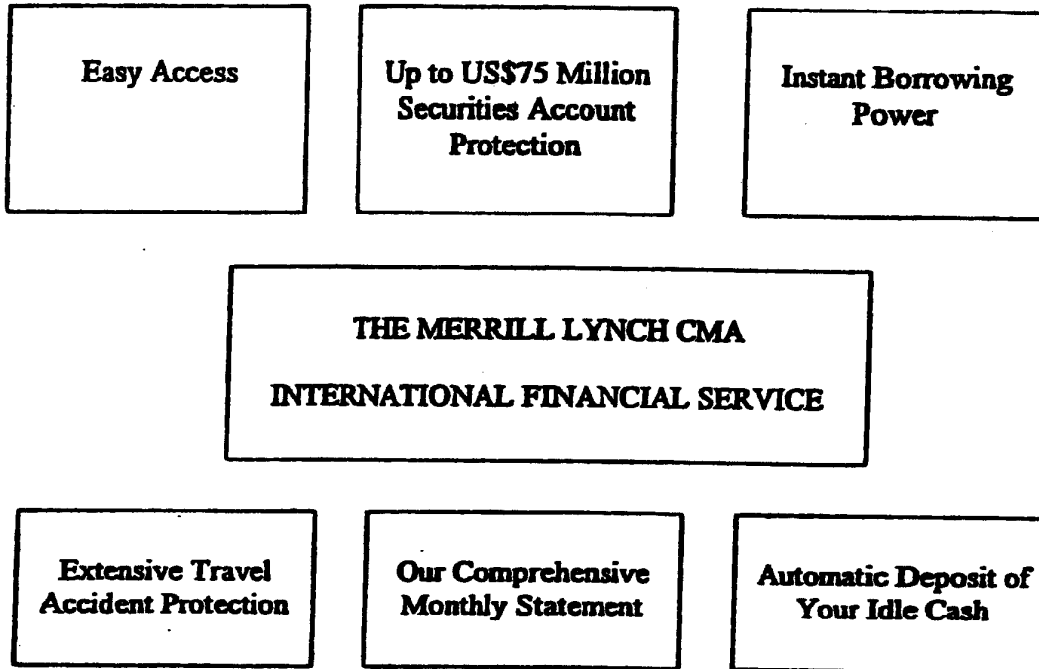
- i) it would add dedicated liquidity and assets for customer's investment portfolio and give them an opportunity to build up assets with different risk return profiles over the long term;
 - ii) it would give Brokerage firms incentives to create new products on a continuous basis for clients for the long term. The learning curve and sophistication of the products, dealers and clients will climb;
 - iii) it would train dealers to think “long term” investments as opposed to “short term” speculative trading and move towards financial consulting or financial planning. Dealers or Financial Consultants will be compensated on “assets” not on “churning”;
 - iv) it would allow customers who have made profits in speculative trading to reallocate assets to safe investments for the long term;
 - v) invariably, customers will tend to have only one loyal account with a broker unlike the present system where speculators end up having as many as five to six accounts with different brokers. This provides for more transparency to the system;
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- vi) it would allow Singapore member firms, subject to adequate liquidity ratios and minimum capital safety standards, to expand into new areas and develop expertise in financial planning, mutual funds, Asian bond markets, etc. In time this will allow Capital to expand faster;
 - vii) brokers may overlap with Private Banking and corporate finance but the net result are flow of regional funds into Singapore; and
 - viii) this integrated account can be extended to Institutional clients without the “retail frills” eg Visa Card. Thus to be able to book multi-currency multi-asset and linked with Euroclear, etc to partly to bring some Institutional business back from Hong Kong to Singapore.
- 1.7 There will be other issues that have to be worked out such as “GST”, stamp duty, 2-tier CLOB requirements, sub-allocation of Block booking that has to be corrected before the bulk of Institutional Business done for Singapore/Malaysia comes back to Singapore, presently booked in HONG KONG (turnover unknown but estimated at US\$160 Billion). Please note:-
- i) that this type of MMA account actually is being offered from Hong Kong, another competitive location where Singaporeans and regional customers already have funds put out there without having to worry about the tax or licence implications;
 - ii) there will be operating issues to cross along the way such as how to separate funds and assets of the company which cannot be co-mingled with the customers;
 - iii) it is important that Singapore member firms redo minimum capital safety standards and liquidity ratios such as say the total aggregate indebtedness formulae. So long as these safety standards are followed then the firm has the freedom and ability to house new products on a continuous basis for customers. This would also allow firms more time to service its customers and create products. As an example, in DBS Securities we deal with five different sets of auditors during the one year; and
 - iv) changes to the bye-laws and SIA Act must be made as presently brokers can only maintain trust accounts for assets only in Singapore Dollars in a Singapore bank.
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- 1.8 In conclusion, imagine the scenario of two dealers who in 1998 know that the markets are going to be bad. These two dealers under the current regulations are compensated on “turnover commissions” instead of “Assets” accumulated. One of them (Dealer A) decides to trade his customers’ portfolio. The other dealer preserves his client’s capital by doing little transactions in the volatile market. At the end of 1998, Dealer A has made \$300,000 worth of commissions which looks good for himself and his firm but his customers have lost half their net worth. The second dealer decides to advise his clients to leave the money in bonds or money market trust units. He has only earned \$20,000 commissions but his customers have preserved their capital. Which dealer is the winner and which dealer is the one that will be retrenched because he has not produced enough income for his firm? The argument for a multi-currency management account is it would provide enough variety of products so that dealers do not need to feel that they have to “churn” the customers’ portfolio.



Source : Merrill Lynch CMA Brochure



Source : Merrill Lynch CMA Brochure