CONSULTATION PAPER

10 - 2003
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Policy Consultation on Amendments to the SFA and FAA

Monetary Authority of Singapore

PREFACE

On 2 September 2003, Parliament passed the Securities and Futures (Amendment) Bill 2003 and the Financial Advisers (Amendment) Bill 2003. The two Bills were the first of a two-phase amendment of the Securities and Futures Act ("SFA") and the Financial Advisers Act ("FAA").

2 This consultation paper sets out the key changes that MAS is considering for the second phase of amendments, which consists of a number of policy reforms to the regulatory framework for our capital markets. The current consultation focuses on issues of general application where MAS is of the view that it is especially important to seek public feedback. For issues pertaining to more specific aspects of the SFA and FAA, MAS may hold separate consultation processes.

3 MAS invites interested parties to forward their views and comments on the issues outlined in the consultation paper. Parties who do not wish to comment on all of the issues may confine their responses to the specific sections which are of interest. All comments should contain a reference to the ***Chapter*** to which the comment pertains. Written comments should be submitted to:

Market Conduct Policy Division
Market and Business Conduct Department
Monetary Authority of Singapore
10 Shenton Way
MAS Building
Singapore 079117
Email: amdt04@mas.gov.sg
Fax: (65)6225-9766

MAS would like to request all comments and feedback by 3 November 2003.

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

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EXECUTIVE SUMMARY

This consultation paper sets out the Monetary Authority of Singapore's ("MAS") proposals for the second phase amendment of the Securities and Futures Act ("SFA") and the Financial Advisers Act ("FAA").

PART I: OFFERS OF INVESTMENTS

2 MAS is reviewing the provisions in Part XIII (Offers of Investments) of the SFA, with a view to implement the remaining recommendations of the Company Legislation and Regulatory Framework Committee ("CLRFC") not addressed by the SF (Amendment) Bill 2003 and to fine-tune the regulatory framework for offers of investments.

3 ***Chapter 1*** covers exemptions from the prospectus requirements, in addition to those proposed by the CLRFC. MAS proposes introducing a new "safe harbour" relating to offers for no consideration. MAS is also inviting comments on whether to exempt offers made in connection with a compromise or arrangement involving a Singapore-incorporated company which does not result a change in effective control.

4 ***Chapter 2*** addresses the issue of liability for false or misleading statements in or material omissions from a prospectus. The proposal is to retain underwriters' liability for the contents of a prospectus. MAS is also considering extending prospectus liability to issue managers. Further, MAS proposes to modify the criminal liability provision so that a person will be guilty of a criminal offence only if the statement or omission is material. It is also proposed that criminal liability, if imposed on a person other than the offeror and its directors, would arise only if he had intentionally, recklessly or negligently made a false or misleading statement in or omitted information from the prospectus.

5 ***Chapter 3*** covers the rules on publicity for offers of investments. The changes being considered will align the rules for offers of shares and debentures, and offers of collective investment schemes. Other proposed changes will allow offerors to respond to media reports based on the contents of a lodged prospectus, and for pre-deal research reports to be issued to

institutional investors for international offers. Restrictions will also be imposed on advertisements after the registration of a prospectus.

6 MAS is also studying other areas, including the publication and distribution of supplementary and replacement documents, the validity period of base prospectuses for debenture issuance programmes, prospectus disclosure requirements for debenture issues, and financial disclosure requirements for prospectuses. MAS will consult the industry and other interested parties on these issues separately.

PART II: MARKETS AND CLEARING FACILITIES

7 ***Chapter 4*** further clarifies the type of entities which MAS will regulate as markets and clearing facilities. The proposal is to clarify that markets are facilities where price interaction occurs. MAS is also proposing to move from an authorisation to a designation approach for regulating clearing facilities.

8 ***Chapter 5*** explains MAS' proposal to expand the definition of futures contract to include over-the-counter ("OTC") derivatives to facilitate the regulation of markets and clearing facilities for OTC products. However, MAS is not proposing to regulate broking of OTC derivatives in the SFA.

PART III: SCOPE OF THE FAA

9 The FAA was enacted in October 2001 to regulate the advisory and sales process for investment products (i.e., capital market products and life policies). MAS considers it timely to review the product scope of the FAA, taking into account product innovation and market developments. Certain financial products, which are presently not included in the scope of the FAA, have an investment element and may expose investors to market risks. The proposals are designed to regulate the advisory and sales practices for such products under the FAA to adequately safeguard the interests of the investing public.

10 ***Chapter 6*** sets out MAS' approach towards structured deposits. MAS proposes to bring structured deposits under the ambit of the FAA by issuing guidelines on the sales process for structured deposits. The business conduct rules in the FAA will not apply in their entirety.

The proposed definition for structured deposits and a set of draft guidelines are included in this chapter.

11 ***Chapter 7*** is related to Chapter 5, and sets out MAS' proposal to include OTC derivatives as an investment product under the FAA. This addresses our concern that such products may be offered to retail investors without any statutory protections.

12 ***Chapter 8*** waives the requirement for a needs-based advisory process for generally circulated advice, where it is clear that such advice does not take into consideration the needs of any particular person.

13 ***Chapter 9*** explains the regulatory framework for financial advisers who provide financial advisory services to overseas investors. Such financial advisers will be exempt from the business conduct rules in the FAA, subject to appropriate safeguards.

PART IV: CHANGES AFFECTING BOTH THE SFA AND FAA

14 MAS proposes to rationalise the regulatory categories of non-retail investors under the SFA and FAA, in terms of the regulatory exemptions granted to entities that deal with or offers targeted at non-retail investors.

15 ***Chapter 10*** sets out a proposal to establish consistent thresholds throughout the SFA and FAA for individuals to qualify as non-retail investors and exempt intermediaries from the FAA in their dealings with institutional investors. MAS will also suggest a look-through provision for investment holding companies to enable them to qualify for certain prospectus exemptions.

16 ***Chapter 11*** addresses the proposal to lift the prohibition against holders of a capital markets services licence or a financial adviser's licence granting unsecured credit facilities to staff and directors to trade in capital market products. Under our risk-based supervisory regime, institutions should be given the discretion to decide whether to grant unsecured credit for staff trades and how to manage the resultant credit risks.

PART I: OFFERS OF INVESTMENTS

CHAPTER 1: ADDITIONAL EXEMPTIONS FROM PROSPECTUS REQUIREMENTS

Sections 240 and 296 of the SFA provide that no person shall make an offer to the public of securities unless it is made in or accompanied by a prospectus that has been registered by MAS. The term "offer to the public" is not defined, though it is an important criterion for determining if a prospectus is required.

2 In its final report (issued in October 2002), the CLRFC pointed out that the existing imprecision in distinguishing public offers from private ones has resulted in practical difficulties for issuers. The CLRFC recommended replacing this approach by abolishing the concept of a public offer and requiring a full prospectus for all offers of securities, except for exempted offers. The CLRFC further recommended that the existing exemptions under the SFA be retained, and new exemptions be introduced for private placements and small offerings so as to provide a comprehensive list of "safe harbours" from the general rule requiring a prospectus.

3 MAS will be proposing amendments to the SFA to implement these recommendations. In addition, MAS is considering whether further exemptions should be added.

PRACTICES IN OTHER JURISDICTIONS

4 A review of the relevant legislation in Australia, the United Kingdom, and the United States shows that these jurisdictions provide exemptions to prospectus requirements that are largely similar to the existing exemptions under the SFA. In addition, exclusions for private placements and small-scale offerings similar to those recommended by the CLRFC can be found under the laws of these jurisdictions.

5 Of the three, Australia is the only jurisdiction that has abolished the concept of a public offer. Under the Australian approach, additional "safe harbours" are provided for issues or transfers of securities for no consideration[1] and for offers made under a compromise or arrangement (whether or not involving a change in control).[2] While UK law still retains the public offer concept, it provides for exemptions for offers of free shares to existing holders of shares in the issuer[3] and for offers in connection with a merger.[4]

PROPOSED EXEMPTIONS

6 MAS proposes exempting offers of securities for no consideration from prospectus requirements under the SFA. The risk of abuse appears minimal as no consideration is involved. The main concern in these cases would appear to be the dilution of existing shareholdings as the result of an additional issue. This is addressed by safeguards in the Companies Act (Cap. 50) ["CA"][5] and listing rules of the Singapore Exchange ("SGX").[6]

1.1 MAS seeks views on the proposal to exempt from the prospectus requirements offers of securities for no consideration.

1 Section 708 (15) and (16) of the Corporations Act 2001 exempts an offer of –

(a) securities (other than options) if no consideration is to be provided for the issue or transfer of the securities; and

(b) options if no consideration is to be provided for the issue or transfer of the options and no consideration is to be provided for the underlying securities on the exercise of the options.

2 Section 708 (17) of the Corporations Act 2001 exempts offers of securities made under a compromise or arrangement under Part 5.1 of the Corporations Act 2001 approved at a meeting held as a result of an order under section 411(1) or (1A).

3 Schedule 11, paragraph 14 of the Financial Services and Markets Act 2000 exempts an offer of securities where the securities are shares and are offered free of charge to any or all the holders of shares in the issuer. "Holders of shares" is defined as the persons who at the close of business on a date specified in the offer, and falling within the period of 60 days ending with the date on which the offer is first made, were holders of such shares.

4 Schedule 11, paragraph 13 of the Financial Services and Markets Act 2000 exempts an offer of securities where the securities are offered in connection with a merger (within the meaning of Council Directive No. 78/855/EEC).

5 Section 161(1) of the CA requires shareholders' approval for the issue of new shares.

6 Chapter 8 of the SGX Listing Manual sets out requirements and restrictions in respect of the issue of securities by a listed company.

7 MAS is considering whether to exempt from prospectus requirements offers in connection with a compromise or arrangement involving a Singapore-incorporated company that would not result in a change in effective control of the company concerned. The current section 273(1)(a) of the SFA exempts from prospectus requirements offers made in connection with compromises or arrangements under section 210 of the CA that, if executed, would result in a change in effective control of a public company incorporated in Singapore. The rationale is that such offers would already be subject to the disclosure requirements under the Singapore Code on Take-overs and Mergers ("Take-over Code").

8 The Securities and Futures (Amendment) Bill 2003 extends the exemption under section 273 of the SFA to offers made in connection with a compromise or arrangement between a corporation not incorporated in Singapore and not listed on SGX with its creditors or with its members, whether or not the compromise or arrangement will result in a change in effective control of the corporation. This recognises that Singapore investors in a foreign corporation not listed on SGX could be disadvantaged if the requirement for a prospectus were to discourage a person from making available to them a compromise or arrangement which investors in other jurisdictions could participate in. This could be the case particularly where Singapore investors constitute only a small minority of the target corporation's shareholders.

9 Such concern should not arise where the target corporation is a Singapore-incorporated company. As the shareholders of such a company would in most cases be based in Singapore, the risk of a compromise or arrangement being offered to foreign investors but not Singapore investors in order to avoid prospectus requirements is remote. Further, where there is no change in effective control, the offer will not be subject to the disclosure requirements under the Take-over Code.

10 On the other hand, MAS notes that a compromise or arrangement under section 210 of the CA is typically subject to approval by shareholders or creditors. The notice convening the meeting to obtain such approval must be accompanied by a statement explaining the effect of the compromise or arrangement. However, there is no specific requirement that the statement contains information about any offer being made in connection with the compromise or arrangement.

1.2 MAS invites comments on whether to exempt from prospectus requirements offers of shares and debentures made in connection with a compromise or arrangement involving a Singapore-incorporated company that, if executed, would not result in a change in effective control of the company concerned.

CHAPTER 2: LIABILITY OF UNDERWRITERS AND OTHER PROFESSIONALS FOR PROSPECTUS DISCLOSURES

Currently, sections 253 and 254 of the SFA impose criminal and civil liabilities respectively for any false or misleading statement in or omission of information from a prospectus, on the following persons:

(a) the offeror;

(b) a director or proposed director of the offeror;

(c) an underwriter (but not a sub-underwriter);

(d) a person who has consented to the inclusion of the statement in the prospectus; and

(e) any other person who made a false or misleading statement or omitted to state required information in the prospectus.

2 Section 255 of the SFA provides that a person will not be held liable if he proves, among other things, that he had made all reasonable inquiries and has reasonable grounds to believe that there was no false or misleading statement in, or omission of information from, the prospectus. A person can also avoid liability if he proves that he has placed reasonable reliance on information given to him by an unconnected third party.

CLARIFICATION AND INDUSTRY FEEDBACK

3 Some practitioners have sought clarification whether sub-underwriters are subject to prospectus liability under sections 253 and 254. The SFA clearly states that sub-underwriters are excluded from prospectus liability (see paragraph 1(c) above). Whether a person is a lead underwriter or sub-underwriter is a matter of fact – it depends on whether he has a direct contractual relationship with the issuer to underwrite the offer. The distinction is well-established in Singapore market practice, although practices may differ in other jurisdictions.

4 While not subject to prospectus liability under the SFA, MAS recognises that a sub-underwriter may wish to be indemnified against any other liability that may arise as a result of the offering. This may be relevant particularly for international offerings where foreign laws may impose other requirements on a sub-underwriter. Whether and how such indemnification should be arranged is a commercial matter for the sub-underwriter to negotiate and agree on with the lead underwriter and/or the issuer. MAS does not consider this to be an issue that should be dealt with under the SFA.

5 Separately, some market participants have suggested that underwriters should not be held liable for prospectus disclosures, particularly where they have not provided any advice on the contents of the prospectus. In Singapore, it is typical for the issue manager rather than the underwriter (unlike in some jurisdictions such as the United States) to assist the issuer in preparing the prospectus.[7] In fact, where the issue manager out-sources underwriting to a third-party underwriter or appoints a co-underwriter, it is not uncommon for such an underwriter to be brought in only after the prospectus has been drafted. The commentators are of the view that imposing prospectus liability on underwriters exposes them to excessive risks, when they already undertake substantial commercial risks by underwriting the offer.

6 Another suggestion is that prospectus liability should be shared amongst all the professionals involved in preparing the prospectus, instead of resting solely on the underwriter. These commentators noted that lawyers and auditors also play significant roles in drafting the prospectus and should therefore be held liable.

PRACTICES IN OTHER JURISDICTIONS

7 In the UK, statutory liability for prospectus disclosures rests on the issuer, directors and proposed directors of the issuer, and persons who have accepted responsibility for or authorised the contents of the

[7] Rule 111 of the SGX Listing Manual requires an issuer applying for a listing on the Singapore Exchange to appoint an issue manager. Rule 114 further provides that the issue manager must exercise due care and diligence in ensuring the completeness and accuracy of the information contained in the prospectus.

prospectus.[8] Hong Kong's regime is similar, except that it extends liability to the promoters of the issuer as well.[9] It is not clear whether issue managers and underwriters come within the scope of any of these classes of persons who are liable for prospectus disclosures. There have been recent proposals in Hong Kong to amend the relevant laws and rules to extend prospectus liability specifically to issue managers, and possibly other IPO intermediaries.[10]

8 In Australia and the US, underwriters are held liable for any deficiencies in the prospectus.[11] While Australia excludes sub-underwriters from liability, the US extends liability to all underwriters including co-underwriters and sub-underwriters. However, under US case law, these other underwriters may rely on the lead underwriter if they are satisfied that the lead underwriter has made the kind of inquiries that they would have performed if they were the lead underwriter and such inquiries are adequate. Unlike the UK and Hong Kong, there is no defined role for an issue manager in Australia and the US. Instead, lead underwriters usually play an active role in preparing the prospectus in view of their liabilities under the law.

9 Unlike Hong Kong and Australia, the UK and the US distinguish between criminal and civil liability in terms of the test applied to determine liability. In the UK, a person is guilty of a criminal offence for prospectus disclosures only if he makes a statement, promise or forecast which he knows

[8] Section 90 of the Financial Services and Markets Act 2000 ("FSMA") imposes civil liabilities on persons who are responsible for the listing particulars (or prospectus). Under the FSMA (Official Listing of Securities) Regulations 2001, persons responsible would include the issuer, directors, proposed directors, persons who accept responsibility for the particulars and persons who authorised the contents of the particulars.

[9] Section 40 of the Companies Ordinance imposes civil liabilities on directors, proposed directors, promoters and persons who authorised the issue of the prospectus.

[10] One of the key initiatives of the Hong Kong Corporate Governance Action Plan 2003 is to amend the Companies Ordinance (Cap.32) to impose prospectus-related liability on issue managers and possibly other IPO intermediaries. The Hong Kong Securities and Futures Commission and Hong Kong Exchange has also proposed in a recent public consultation paper (*Consultation Paper on the regulation of Sponsors and Independent Financial Advisers, 30 May 2003*) to amend the listing rules to require issue managers and underwriters to declare in the prospectus that they have made reasonable inquiries and have reasonable grounds to believe that the information in the prospectus is not materially false or misleading.

[11] Section 729 of the Australian Corporations Act 2001 imposes civil liability on underwriters for prospectus disclosures. Professional advisers and experts, on the other hand, are liable only for statements included in the prospectus with their consent. In the United States, all underwriters are subject to civil actions by investors under Section 11 of the Securities Act 1933.

is misleading, false or deceptive in a material particular, if he dishonestly conceals any material facts, with the intention of inducing investment, or if he recklessly makes a statement, promise or forecast that is misleading, false or deceptive in a material particular.[12] Similarly, in the US, a person faces criminal liability only if he willfully makes an untrue statement of a material fact or omits to state any material fact in a prospectus.[13]

PROPOSED REGULATION

10 An underwriter, who like the issuer and its directors are liable for prospectus disclosures, has a significant economic interest in the success of an offer. If the underwriter fails to find purchasers, it will have to acquire the securities not taken up. Notwithstanding that the underwriter may not have been directly involved in preparing the prospectus, it will be using the prospectus to promote the offer. To the extent that the underwriter's interests may diverge from those of the investing public and hence there is a risk of abuse, suitable sanctions should be put in place to discourage inadequate or improper disclosure. MAS is therefore of the view that underwriters should continue to assume responsibility for the contents of the prospectus and propose accordingly that prospectus liability of underwriters be maintained. This is consistent with the practice in the US and Australia.

2.1 MAS seeks views on the proposal to continue holding underwriters liable for prospectus disclosures.

11 Although an issue manager typically plays a significant role in helping the issuer to prepare the prospectus, it is currently not subject to any liability for prospectus disclosures unless it also underwrites the offer or is quoted in the prospectus. Imposing prospectus liability on issue managers would help redress the apparent regulatory imbalance.

[12] In the UK, a person is guilty of a criminal offence under Section 397 of the FSMA if he makes a statement, promise or forecast which he knows is misleading, false or deceptive in a material particular, if he *dishonestly conceals* any material facts, or if he recklessly makes a statement, promise or forecast which he knows is misleading, false or deceptive in a material particular, for the purpose of inducing or is reckless as to whether it may induce another person to do or refrain from doing something in relation to an investment.

[13] In the US, section 24 of the Securities Act 1933 provides for criminal penalties on any person who *willfully* makes an untrue statement of a material fact or omits to state any material fact in a registration statement.

12 On the other hand, the issue manager in many cases is also the underwriter and would therefore already be liable. The proposal is relevant only where the issue manager out-sources underwriting to a third-party underwriter.

13 If the rationale is that persons who are involved in preparing the prospectus should be held responsible for its contents, then it could be argued that liability should be extended not only to issue managers but also other professionals, such as lawyers and accountants who are also involved in this regard.

14 None of the jurisdictions MAS studied currently imposes prospectus liability on issue managers and other IPO intermediaries, although that is being considered in Hong Kong. Indeed, UK law specifically provides that a person will not be held responsible for the prospectus by reason of him giving advice on its contents in a professional capacity. Extending the liability provisions to cover all IPO professionals could also increase the cost of fundraising.

15 On balance, MAS considers that there is a case in the Singapore context for extending prospectus liability to issue managers given the significant role they play in the offering process. Unlike other professionals such as lawyers and accountants, the issue manager's responsibilities are prescribed in SGX listing rules, as is the practice in the UK and Hong Kong. These include satisfying itself that the issuer is suitable for listing and exercising due care and diligence in ensuring the completeness and accuracy of the listing application (which includes a copy of the prospectus).

2.2 MAS seeks views on the proposal to extend prospectus liability to issue managers. MAS also invites comments on whether prospectus liability should be extended to other IPO intermediaries (e.g. lawyers, accountants).

16 MAS is proposing to modify the criminal liability provision in line with practices in other jurisdictions so that a person will be guilty of a criminal offence only if a false or misleading statement or omission is material. Further, MAS is proposing that criminal liability, if imposed on a person other than the offeror and its directors, would arise only if he had intentionally, recklessly or negligently made a false or misleading statement in or omitted information from the prospectus. The test would be the same as that used in section 203 of the SFA on continuous disclosure by listed companies. As the

proposal would shift the burden of proof from the person held liable to the prosecutor, the due diligence and reasonable reliance defences under section 255 of the SFA will not be applicable in such cases. MAS is also considering whether to provide for administrative penalties for less serious breaches of prospectus disclosure requirements that would no longer attract criminal liability. MAS does not propose to make any amendment to the civil liability provision.

2.3 MAS seeks views on the proposal to modify the criminal liability provision so that a person will be guilty of a criminal offence only if the statement or omission is material. For a person other than the offeror and its directors, MAS seeks views on the proposal to hold the person criminally liable only if he had intentionally, recklessly or negligently made a false or misleading statement in or omitted information from the prospectus.

CHAPTER 3: PUBLICITY FOR OFFERS OF INVESTMENTS

Currently, a person cannot advertise an offer or publish any statement that refers to or is likely to induce persons to subscribe to an offer requiring a prospectus, except as provided for under sections 251 and 300 of the SFA. The provisions aim to protect the investing public from being induced to purchase securities without adequate disclosure that is accorded by a prospectus.

2 For offers of shares and debentures, section 251 of the SFA differentiates between the periods before and after a prospectus is registered. Before registration, only "tombstone" advertisements identifying the issuer and the securities to be offered and stating how a copy of the prospectus may be obtained are permitted. After it has lodged a preliminary prospectus with MAS, an issuer may circulate the preliminary prospectus and conduct roadshow presentations to institutional and sophisticated investors. There are no restrictions on advertisements after the prospectus is registered as long as the advertisements provide information on how to obtain a copy of the prospectus and state that anyone wishing to subscribe for the offer should do so in the manner set out in the prospectus.

3 Section 300 of the SFA does not draw such a distinction for offers of collective investment schemes ("CIS"). Whether before or after a prospectus is registered, all CIS advertisements are subject to the same advertising regulations.

4 Some publications are exempted from sections 251 and 300 of the SFA. They include –

(a) a notice or report to the securities exchange (only from section 251);

(b) a notice or report of a general meeting of the issuer or unitholders of the CIS;

(c) a news report or genuine comment in a newspaper, periodical or magazine or on radio or television; and

(d) a research report published by someone who is not connected to the offeror and who does not have an interest in the success of the offer.

BEFORE REGISTRATION

5 Although permitted under the current framework, MAS has not seen extensive advertising of any CIS before its prospectus is registered. The risk of an investor being conditioned or induced into investing in a CIS by an advertisement would not be significantly different from that for an offer of shares or debentures. Therefore, we propose to allow only "tombstone" advertisements for CIS before a prospectus is registered, as is the practice for shares and debentures. Such "tombstone" advertisements can state only the name of the fund, the name of the manager and how a copy of the prospectus may be obtained. This approach is also adopted in the US and Hong Kong.

3.1 MAS seeks views on the proposal to allow only "tombstone" advertisements for CIS before a prospectus is registered, stating the name of the fund, the name of the manager and how a copy of the prospectus may be obtained.

6 To provide flexibility for CIS managers and distributors to conduct pre-marketing of CIS before a prospectus is registered, MAS proposes allowing a CIS prospectus that has been lodged with MAS to be circulated to institutional investors. This would be similar to the approach for offers of shares and debentures, where a preliminary prospectus may be distributed to institutional investors for whom there is no prescribed disclosure requirements to make an offer. The same safeguards as those for a preliminary prospectus for an offer of shares or debentures would apply.[14] Similarly, MAS intends to allow roadshow presentations to institutional investors based on information contained in the lodged prospectus.

[14] Section 251(3) of the SFA. These safeguards include disclaimers on the front cover of the marketing document, not attaching any application forms to the marketing document, and taking reasonable steps to notify recipients of the marketing document when the prospectus is registered.

7 MAS does not propose extending such pre-marketing of CIS offers to investors exempted under section 305 of the SFA because offers of CIS (unlike offers of shares and debentures) to such investors are subject to prescribed disclosure requirements.[15]

3.2 MAS seeks views on the proposal to allow the pre-marketing of CIS offers to institutional investors via circulation of prospectuses that have been lodged with MAS and roadshow presentations.

8 MAS has also received requests from some financial institutions to distribute "pre-deal research reports" before a prospectus is registered, particularly for offers that were being made concurrently in two or more jurisdictions. "Pre-deal research reports" refer to research reports that profile an issuer or CIS shortly before an offer is made. These reports are typically prepared by analysts in financial institutions with an interest in the offer, such as the issue manager or underwriter or their related corporations ("connected broker"). The reports may contain the analysts' valuations of the issuer, financial forecasts and recommendations on whether to subscribe to the offer. They are distributed to potential investors as part of the process to market an offer.

9 Unlike independent research reports that are exempted from sections 251 and 300 of the SFA (see paragraph 4(d) above), research reports prepared by connected brokers are subject to the advertising provisions in the SFA. The rationale is that there will always be a strong commercial interest for connected brokers to publish favourable reports in order to stimulate interest in and demand for the securities on offer. Such reports could confuse investors and undermine the value of the prospectus as the key document they should be relying on in making their investment decisions.

10 In addition, there is a concern that pre-deal research reports may be employed to disseminate information relating to an offer (e.g. profit forecasts) without prospectus liability. To the extent that these reports are distributed to selected investors, there is also a risk of selective disclosure of material information.

[15] Offers to investors pursuant to the exemption in section 305 of the SFA must be accompanied by an information memorandum.

11 MAS notes that pre-deal research reports are permitted in other markets. The practice in Australia is that an issuer may present any oral or written material (including pre-deal research reports) to securities intermediaries[16] before a prospectus is lodged[17]. As a safeguard against potential abuse, practitioners will normally circulate such research in individually-numbered hard copies. The recipients are also advised that they should rely on the prospectus in making any decision on the offer.

12 In the US, research reports by connected brokers are allowed only -

(a) in respect of securities that are not the subject of an offer (e.g. where the research is on non-convertible debentures when the securities being offered are shares)[18];

(b) for corporations that have been listed for 12 months or more and have a public float of at least US$75 million[19]; and

(c) where the report includes similar information, opinions or recommendations on a substantial number of companies in the issuer's industry or contains a comprehensive list of securities currently recommended by the connected broker, and information on the issuer is not given greater prominence than that given to other securities[20].

Where pre-deal research reports are allowed, there appears to be a market practice to observe a quiet period commencing around two weeks before filing the prospectus with the US Securities and Exchange Commission.

13 Neither the UK nor Hong Kong has any formal rule that prohibits or permits pre-deal research reports. The practice has evolved in these two jurisdictions where connected brokers would subject themselves to a two-week quiet period between the publication of a pre-deal research report

16 Securities intermediaries include dealers, investment advisers, exempt dealers, exempt investment advisers and representatives of such institutions.

17 In Australia, a prospectus can be used to make offers once it is lodged with the Australian Securities and Investment Commission ("ASIC"). ASIC does not register the prospectus.

18 Rule 138 issued under the Securities Act of 1933.

19 Rule 139 issued under the Securities Act of 1933.

20 Rule 139 issued under the Securities Act of 1933.

and the commencement of roadshows or the lodgment of a prospectus.[21] In the UK, practitioners can also rely on the exemption for financial promotions to investment professionals to distribute pre-deal research reports to them.[22]

14 MAS is considering whether to allow the circulation of pre-deal research reports to facilitate the marketing efforts of issuers and their advisers. In particular, where offers are being made concurrently in two or more jurisdictions, there is the question of whether Singapore investors would be disadvantaged vis-à-vis foreign investors if our investors cannot have access to pre-deal research reports that are permitted in other markets.

15 There are already some safeguards against the risks highlighted in paragraph 10 above. For example, section 243 of the SFA requires a prospectus to contain all the information that an investor would reasonably require to make an informed decision on the offer. If an issuer or its adviser tries to avoid prospectus liability or to disclose information selectively by including material information on an offer in a pre-deal research report but not in the prospectus, then the prospectus would not comply with section 243. Such a deficient prospectus would not qualify for registration or, if the deficiency were uncovered after registration, could be stopped.

16 Moreover, an issuer and its advisers are not free from liability for disclosures in a pre-deal research report. Section 199 of the SFA prohibits the making of false or misleading statements to induce people to subscribe for or buy securities. A contravention carries both criminal and civil liabilities.

17 Nonetheless, MAS recognises that the attendant risks are not completely mitigated and that practices in some jurisdictions are either unclear or still evolving. Thus, one option is to allow pre-deal research reports only in a limited way. An example would be for offers that are being made simultaneously in Singapore and one or more other jurisdiction where pre-deal research reports are permitted, so that Singapore investors would not be disadvantaged vis-à-vis their foreign counterparts.

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[21] The UK FSA is seeking public feedback on a proposal to require a quiet period from the time a prospectus is published until a reasonable period of time (say 30 days) after the securities are admitted to trading. CP171: Conflicts of Interests: Investment Research and Issues of Securities, 12 Feb 2003.

[22] Article 19 of the Financial Promotions Order 2001. Investment professionals include authorised persons, exempt persons, governments and local authorities.

18 Further, the circulation of pre-deal research reports could be limited to institutional investors. MAS understands this is the market practice in any case. Institutional investors are expected to have the necessary expertise and experience to assess such research, taking into account the connected broker's interest in the offer.

19 To reduce the risk of any information in the pre-deal research reports leaking to the retail public, the following safeguards can be considered:

(a) the person issuing the pre-deal research report must not disclose any information contained in the pre-deal research report to any person other than an institutional investor, including the media;

(b) the person issuing the pre-deal research report must observe a quiet period during which he will not publish or distribute the report, starting 2 weeks before the lodgment of the prospectus and ending at the close of the offer; and

(c) the pre-deal research report must state that it is for circulation to institutional investors only and that the information therein should not be disclosed by the investor to any other party, including the media.

3.3 MAS seeks views on the proposal to permit pre-deal research reports for offers that are made concurrently in Singapore and one or more other jurisdictions where pre-deal research reports are permitted. MAS also invites comments on whether to limit the circulation of such reports to institutional investors and the possible safeguards against leakage of information contained in the reports to retail investors.

20 Once a prospectus is lodged with MAS, its contents are available to the public on the OPERA website. Copies of the lodged prospectus would also be distributed to institutional and sophisticated investors at roadshows. With the prospectus in the public domain, there would very often be media reports or commentaries on the offer.

21 The issuer may on occasion need to communicate with the media to clarify inaccurate or misleading information in media reports. MAS proposes allowing communications with the media, where such communications are in response to news reports or genuine comments in a newspaper, periodical or magazine or on radio or television, or any other means of broadcasting or communication [i.e. communications that are themselves exempted from the advertising restrictions under section 251(9)(d) of the SFA]. The contents of such communications will be restricted to information in the lodged prospectus, as is the practice for roadshow presentations after lodgment.

3.4 MAS seeks views on the proposal to allow the issuer and its advisers to communicate with the media about an offer after lodgment of the prospectus provided that such communication is in response to news reports or genuine comments in the media and is restricted to the contents of the lodged prospectus.

BEFORE AND AFTER REGISTRATION

22 To provide for CIS that are listed on a securities exchange, MAS proposes to exempt from the SFA section 300 restriction on advertisements any notice or report by a responsible person[23] of a listed CIS to the securities exchange for the sole purpose of complying with the listing rules or other requirements of the securities exchange. The same safe harbour is available for issuers of shares and debentures.[24]

3.5 MAS seeks views on the proposal to dis-apply section 300 of the SFA for notices and reports by a responsible person of a listed CIS to a securities exchange solely for the purpose of complying with the listing rules or other requirements of the securities exchange.

23 In response to market feedback, MAS proposes extending the exemption to cover similar notices and reports by a listed offeror of shares, debentures or CIS, where such offeror is not the issuer of the shares or debentures nor the responsible person of the CIS (e.g. a vendor of existing shares, debentures or units of CIS).

[23] Defined in section 283(1) of the SFA.

[24] Section 251(9)(a) of the SFA.

3.6 MAS seeks views on the proposal to dis-apply sections 251 and 300 of the SFA for notices and reports by a listed offeror who is neither the issuer of the shares or debentures nor the responsible person of the CIS to the securities exchange on which the listed offeror is listed solely for the purpose of complying with the listing rules or other requirements of the securities exchange.

AFTER REGISTRATION

24 Currently, issuers can advertise their offers with few restrictions after the prospectus is registered, subject to sections 251 and 300 of the SFA. To discourage misleading advertisements that may include new information not found in the registered prospectus, MAS proposes that the contents of such advertisements be limited to information contained in the registered prospectus.

3.7 MAS seeks views on the proposal to restrict the contents of advertisements after registration to information in the registered prospectus.

INVITATION FOR COMMENTS

Chapter 1: Additional Exemptions from Prospectus Requirements

1.1 MAS seeks views on the proposal to exempt from the prospectus requirements offers of securities for no consideration.

1.2 MAS invites comments on whether to exempt from prospectus requirements offers of shares and debentures made in connection with a compromise or arrangement involving a Singapore-incorporated company that, if executed, would not result in a change in effective control of the company concerned.

Chapter 2: Liability of Underwriters and Other Professionals for Prospectus Disclosures

2.1 MAS seeks views on the proposal to continue holding underwriters liable for prospectus disclosures.

2.2 MAS seeks views on the proposal to extend prospectus liability to issue managers. MAS also invites comments on whether prospectus liability should be extended to other IPO intermediaries (e.g. lawyers, accountants).

2.3 MAS seeks views on the proposal to modify the criminal liability provision so that a person will be guilty of a criminal offence only if the statement or omission is material. For a person other than the offeror and its directors, MAS seeks views on the proposal to hold the person criminally liable only if he had intentionally, recklessly or negligently made a false or misleading statement in or omitted information from the prospectus.

Chapter 3: Publicity for Offers of Investments

3.1 MAS seeks views on the proposal to allow only "tombstone" advertisements for CIS before a prospectus is registered, stating the name of the fund, the name of the manager and how a copy of the prospectus may be obtained.

3.2 MAS seeks views on the proposal to allow the pre-marketing of CIS offers to institutional investors via circulation of prospectuses that have been lodged with MAS and roadshow presentations.

3.3 MAS seeks views on the proposal to permit pre-deal research reports for offers that are made concurrently in Singapore and one or more other jurisdictions where pre-deal research reports are permitted. MAS also invites comments on whether to limit the circulation of such reports to institutional investors and the possible safeguards against leakage of information contained in the reports to retail investors.

3.4 MAS seeks views on the proposal to allow the issuer and its advisers to communicate with the media about an offer after lodgment of the prospectus provided that such communication is in response to news reports or genuine comments in the media and is restricted to the contents of the lodged prospectus.

3.5 MAS seeks views on the proposal to dis-apply section 300 of the SFA for notices and reports by a responsible person of a listed CIS to a securities exchange solely for the purpose of complying with the listing rules or other requirements of the securities exchange.

3.6 MAS seeks views on the proposal to dis-apply sections 251 and 300 of the SFA for notices and reports by a listed offeror who is neither the issuer of the shares or debentures nor the responsible person of the CIS to the securities exchange on which the listed offeror is listed solely for the purpose of complying with the listing rules or other requirements of the securities exchange.

3.7 MAS seeks views on the proposal to restrict the contents of advertisements after registration to information in the registered prospectus.

PART II: MARKETS AND CLEARING FACILITIES

CHAPTER 4: REFINING THE LEGISLATIVE FRAMEWORK FOR MARKETS AND CLEARING FACILITIES

MAS is currently reviewing the provisions in Part II (Markets) and Part III (Clearing Facilities) of the SFA in order to -

(a) better focus on entities that pose risks to MAS' regulatory objectives; and

(b) enhance its flexibility to tailor requirements to address the specific risks that arise from different business models.

The scope of Parts II and III will be determined by the *activities* that constitute a "market" and "clearing facility" respectively, as well as the *products* regulated by the SFA.

TYPES OF FACILITIES REGULATED AS MARKETS

2 MAS regulates markets to achieve three key objectives – to foster investor confidence, minimise systemic risk, and facilitate efficient capital flows and risk transfers. The efficiency and quality of the price formation process are therefore core regulatory concerns. MAS therefore proposes to refine the definition of "securities market" and "futures market" to regulate only those facilities where price interaction takes place, that is, where bids or offers are exposed to competition from bids or offers of other participants. This will include platforms that pull together or consolidate multiple single-dealer bulletin boards to the extent that they perform a price interaction function. This will exclude platforms that facilitate over-the-counter ("OTC") trading of individually tailored and bilaterally negotiated contracts, as price interaction would not take place on those platforms.

4.1 MAS seeks views on the proposal to regulate as "markets" only facilities where price interaction takes place.

4.2 MAS seeks views on whether platforms that facilitate OTC trading of individually tailored and bilaterally negotiated contracts should be regulated as "markets".

3 The existing definition of "securities market" extends to markets for "issued securities" only. The Guidelines on the Regulation of Markets explain that "issued securities" are "listed or unlisted securities that have been previously offered either by means of private placement or public offering to investors which are now available for secondary trading". The policy intent was to limit the regulatory framework for markets to secondary markets. Primary markets are regulated through different mechanisms such as the prospectus requirements in Part XIII of the SFA.

4 Industry practices and technology are challenging the traditional boundaries between primary and secondary markets. For example, trading platforms for credit default swaps referenced to an underlying security have emerged. Such swaps fall within the meaning of "security" under the SFA. However, they may not fall within the meaning of "issued security" because the distinction between primary and secondary offerings for such instruments is often blurred. When the operation of these facilities poses risks to MAS' regulatory objectives, they should be subject to appropriate regulation. To allow the regulation of such markets (when necessary), MAS proposes deleting the word "issued" from the definition of "securities market" in the First Schedule of the SFA. Instead, the following exclusions will be introduced:

(a) facilities used for the offer of shares, debentures, or units of shares or debentures which have not been previously issued and where the offers are made in compliance with section 240 of the SFA;

(b) facilities used for the offer of units in a collective investment scheme ("CIS") which have not been previously issued and where the CIS is authorised under section 286 or recognised under section 287 of the SFA;

(c) facilities used for the offer of shares, debentures or CIS which have not been previously issued and which are exempted by Part XIII of the SFA; and

(d) any other facility or class of facilities prescribed by MAS.

5 The proposed approach ensures that the regulatory regime for markets applies to trading platforms for less conventional securities for which it may be difficult to distinguish between primary and secondary offerings. At the same time, it does not over-extend MAS' regulatory reach by excluding from the regulatory regime primary offerings of more conventional instruments such as shares and debentures (where it is possible to distinguish between primary and secondary markets).

4.3 MAS seeks views on the proposal to delete "issued" from the definition of "securities market" and to insert the exclusions in paragraph 4. MAS invites comments on whether the proposed exclusions are sufficient to exclude from the scope of the SFA, facilities that do not pose risks to the regulatory objectives described in paragraph 2.

INTRODUCING A DEFINITION FOR "CLEARING AND SETTLEMENT"

6 The scope of the SFA's regulatory framework for clearing and settlement is circumscribed by the definition of "clearing facility", which is defined as a facility for the clearing or settlement of transactions in securities or futures contracts traded on a securities or futures market, or any other clearing or settlement facility as MAS may prescribe.

7 "Clearing and settlement" is not defined in the SFA, creating uncertainty over whether various elements of the post-trade process are regulated by the SFA. To provide industry players with greater certainty, MAS proposes that "clearing and settlement" will include one or more of the following activities:

(a) *post-trade matching and confirmation*, which is the process of confirming that the counterparties agree on the terms of the trade;

(b) *novation*, where the clearing facility substitutes itself as the counterparty to a trade, i.e. the trade between a buyer and seller is split into two separate trades, with the clearing facility substituted as buyer to the seller and seller to the buyer;

(c) *clearance*, which involves the computation of the counterparties' obligations to deliver or pay on the settlement date; and

(d) *settlement*, which involves the transfer of title to the security and a corresponding funds transfer or settlement of net obligations arising from settlement variations. This excludes banks and custodians carrying out instructions to make payments or transfer securities in their ordinary course of business as a bank or custodian.

4.4 MAS seeks views on the proposed definition of "clearing and settlement".

INTRODUCING A DESIGNATION APPROACH FOR REGULATING CLEARING FACILITIES

8 Not all clearing facilities that engage in the activities referred to in paragraph 7 pose threats to MAS' regulatory objectives of minimising systemic risk and maintaining confidence in key markets. The extent to which difficulties in a clearing facility would threaten MAS' objectives would depend on an evaluation of –

(a) whether the facility acts as a central counterparty (CCP) and hence assumes credit and delivery risks;

(b) the systemic importance of the market served by the facility, which includes a consideration of the size of the market, the types of investors and participants, and the existence of alternative trading venues;

(c) the volume and value of trades cleared by the facility;

(d) the number and nature of participants that clear through the facility;

(e) the parties that would be exposed to losses should the facility run into difficulties, including the impact on payment systems and clearing facilities utilised by or related to the facility; and

(f) the public interest.

9 MAS therefore proposes to introduce a designation approach for the regulation of clearing facilities. Under this approach, any person that seeks to engage in the clearing and settlement of securities and futures contracts will be required to notify MAS at least 60 working days prior to commencement of operations. MAS' approval would not be required for the facility to commence operations.

10 MAS will then decide whether a facility should be designated following an assessment of the nature and extent of the risks posed by the facility. Facilities identified for designation are those that are considered important in terms of financial stability and public confidence based on the factors in paragraph 8. Only designated facilities will be regulated by MAS. MAS expects to designate the Central Depository (Pte) Ltd and the Singapore Exchange Derivatives Clearing Limited, both of which are already regulated by MAS.

11 Recognising that the impact of a clearing facility operations on MAS' regulatory objectives may evolve with the growth of the clearing facility, the amendments to Part III of the SFA will allow MAS to obtain information from any clearing facility, whether designated or not, and to designate the facility should it pose risks to our regulatory objectives.

12 Entities that are already regulated by MAS and who currently provide clearing and settlement services, or wish to expand their services to do so would not be subject to the notification requirement referred to in paragraph 9. The entities exempted from the notification requirement are –

(a) payment systems designated/regulated under the proposed Payment Systems Oversight Act ("PSOA");

(b) holders of a Capital Markets Services licence; and

(c) banks and merchant banks regulated by MAS.

4.5 MAS seeks views on the proposed criteria for evaluating whether to designate a clearing facility.

4.6 MAS seeks views on the proposed designation approach for clearing facilities.

4.7 MAS seeks views on the proposed list of institutions to be exempt from the notification requirement.

ENHANCING FLEXIBILITY

13 The SFA introduced a new framework for regulating alternative trading platforms or Recognised Trading Systems ("ReTS"), as imposing the full gamut of exchange requirements on ReTS would stifle industry development and innovation. Based on the experience gained from implementing the SFA over the last two years, MAS proposes to introduce greater flexibility into the regulatory framework for ReTS. ReTS will also be renamed as "Recognised Markets" to align the nomenclature with Exempted Markets.

14 MAS is proposing a bottom-up regulatory approach, which would apply minimal baseline regulatory obligations to all Recognised Markets, but grant MAS the power to apply additional obligations depending on the functions undertaken by the facility. Such an approach would facilitate the tailoring of institution-specific regulatory requirements that address the specific risks posed by the diverse range of business models eligible to be recognised under the regime. These amendments will make it easier for new and innovative trading platforms to operate in Singapore.

CHAPTER 5: RE-DEFINING "FUTURES CONTRACTS"TO INCLUDE OVER-THE-COUNTER DERIVATIVE PRODUCTS

The definition of "futures contract" under the SFA is currently limited to forward delivery or difference-settled contracts which are settled pursuant to the business rules of a futures market. Derivative products traded over-the-counter ("OTC") are not subject to the SFA. This has placed restrictions on MAS' oversight of markets and clearing facilities for OTC derivatives.

2 OTC derivative products have many of the characteristics of futures contracts: they are highly leveraged and sophisticated financial instruments whose values fluctuate depending on the underlying instrument. Where such products are available to retail investors, they are as risky as other investment products (especially futures contracts) and may require some form of regulation.

PROPOSED REGULATORY FRAMEWORK

3 MAS proposes to amend the definition of "futures contract" in section 2(1) of the SFA to mean 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.

and includes a futures option transaction.

4 MAS notes that there is a large variety of OTC derivatives in the marketplace, such as forward contracts, interest rate swaps and non-equity contracts for differences. Existing provisions in Parts IV, V and VI of the SFA on licensing and conduct of business relating to the trading of

futures contracts were drafted with traditional exchange-traded futures in mind, such as the need to maintain margins. These provisions may not be suitable for OTC derivatives. More fundamentally, it would be onerous for institutions to ensure compliance with the SFA for intermediation in OTC derivatives. Existing market players have developed their own conventions to address risks, and self-regulation has served the industry well in this regard.

5 MAS is of the view that broking in OTC derivatives does not involve systemic risks or pose regulatory concern in terms of access to retail investors. Hence, MAS does not intend to make trading in OTC derivatives a regulated activity under the SFA. However, there will be no change in MAS' oversight of exchange-traded futures contracts.

5.1 MAS seeks views on its proposal -

(a) to amend the definition of "futures contract"; and

(b) not to regulate broking in off-exchange derivative transactions under the SFA;

and invites comments on whether any exemption should be provided, such as for certain specified products or transactions.

6 Despite the fact that MAS will not regulate dealing in OTC derivatives, such products will be included within the scope of investment products under the FAA. Please see Chapter 7 for more details.

INVITATION FOR COMMENTS

Chapter 4: Refining the Legislative Framework for Markets and Clearing Facilities

4.1 MAS seeks views on the proposal to regulate as "markets" only facilities where price interaction takes place.

4.2 MAS seeks views on whether platforms that facilitate OTC trading of individually tailored and bilaterally negotiated contracts should be regulated as "markets".

4.3 MAS seeks views on the proposal to delete "issued" from the definition of "securities market" and to insert the exclusions in paragraph 4 of the chapter. MAS invites comments on whether the proposed exclusions are sufficient to exclude from the scope of the SFA, facilities that do not pose risks to the regulatory objectives described in paragraph 2 of the chapter.

4.4 MAS seeks views on the proposed definition of "clearing and settlement".

4.5 MAS seeks views on the proposed criteria for evaluating whether to designate a clearing facility.

4.6 MAS seeks views on the proposed designation approach for clearing facilities.

4.7 MAS seeks views on the proposed list of institutions to be exempt from the notification requirement.

Chapter 5: Re-defining "Futures Contract" to Include Over-the-Counter Derivative Products

5.1 MAS seeks views on its proposal -

(a) to amend the definition of "futures contract"; and

(b) not to regulate broking in off-exchange derivative transactions under the SFA;

and invites comments on whether any exemption should be provided, such as for certain specified products or transactions.

PART III: SCOPE OF THE FAA

CHAPTER 6: STRUCTURED DEPOSITS

Currently deposits fall outside the product scope of the FAA because they are generally simple and well understood. However, structured deposits are complex products that bear many of the characteristics of an investment. This chapter clarifies MAS' position on whether structured deposits are investment products, and seeks views on the appropriate sales and advisory rules that should apply.

PRODUCT DEFINITION

2 Structured deposits offer depositors enhanced returns through the use of embedded options. Returns on such products are usually contingent on the performance of a reference instrument or asset, such as a basket of equities, foreign exchange or interest rates, or the occurrence of an underlying credit event.

3 Such products are increasingly being made available to retail investors. Retail investors may be attracted to structured deposits in a low interest rate environment because they offer the same capital guarantee feature associated with conventional fixed deposit products, coupled with the potential of enhanced returns. However, unlike fixed deposits, structured deposits offer returns that may not be realised at maturity. The formulas used to compute potential returns on structured deposits may also be complex. The investing public may not fully understand the complexity of structured deposits or appreciate all the risks involved in investing in such products.

4 Based on their product characteristics, MAS is of the view that structured deposits can be regarded as investment products. MAS proposes to include structured deposits as a class of investment products in the FAA. The proposed definition for structured deposits is as follows:

A structured deposit means any deposit[25] under which any interest or premium will be paid, or is at risk, according to a formula which involves:

(a) the performance of any financial instrument[26]; or

(b) the occurrence of any credit event.

6.1 MAS seeks views on whether the proposed definition of structured deposits captures all such products currently available in the market.

PROPOSED GUIDELINES

5 MAS is of the view that the market conduct practices of institutions marketing structured deposits were, in some cases, less than satisfactory. MAS has identified the following key areas of concerns:

(a) inadequate and unclear disclosure of the risks associated with such products;

(b) excessive focus on potential returns, including the use of headline rates which are unrealistic and unlikely to be achieved; and

(c) marketing of such products as conventional fixed deposits.

6 However, MAS acknowledges that these concerns should be addressed in a manner commensurate with the risks posed to investors. MAS notes that, as deposits, such products are capital-guaranteed by the issuing deposit-taking institution. Furthermore, the claims of depositors may enjoy priority over the claims of all other unsecured creditors in the event that the deposit-taking institution becomes insolvent. For these reasons, structured deposits may be regarded as less risky than other investment products, and hence may not warrant the application of the

[25] As defined in the Banking Act (Cap. 19).

[26] A financial instrument has the same meaning as defined in section 2(1) of the SFA, which includes any currency, currency index, interest rate instrument, interest rate index, share, share index, stock, stock index, debenture, bond index, a group or groups of such financial instruments and such other financial instruments as MAS may prescribe.

detailed requirements on the sales and advisory process under the FAA. The imposition of rules that are too stringent may impose costs on institutions that exceed the potential benefits to investors.

7 Thus, instead of subjecting structured deposits to the business conduct rules under the FAA, MAS proposes that only a set of tailor-made Guidelines need apply. These Guidelines will apply to structured products that meet the definition of a deposit in the Banking Act (Cap. 19). All other structured investment products will continue to be subject to the full set of business conduct rules under the FAA.

8. A draft of our proposed Guidelines is shown below:

Separation of sale of structured deposits from other deposit products

Institutions should ensure that the sale of all structured deposits is conducted through a process that is distinct from the process through which other deposit products are sold. Deposit-taking institutions should note that tellers or other employees in the deposit-taking area should not be involved in the provision of any financial advisory service, or the sale of, any investment product, including structured deposits.

Clear and adequate product disclosures

Institutions are expected to ensure that, in general, all product disclosures are clear, adequate and not false or misleading.

Institutions should also ensure that in the marketing of structured deposits they provide a fair and adequate description of the –

- Nature of the investment;
- Commitment required, including the minimum deposit amount, the tenure of the deposit, any early withdrawal penalty and, where it is the case, the fact that it could be some time before a person reaps a return on his investment; and
- Risks involved, including any circumstance under which interest may not be payable or only the minimum interest would be payable.

In giving a fair and adequate description firms should avoid accentuating the potential benefits of the product, including headline rates that are unrealistic and unlikely to be obtained.

In all marketing materials, whether written or otherwise, institutions should clearly state that any forecast or information about past performance is not necessarily indicative of the future performance of the product.

Disclosure of the relationship between the marketer and product provider

Institutions should also provide details of the product provider if the marketing institution is not the provider. These details should include the name and business address of the product provider, and the relationship between the product provider and marketing institution

Application of Guidelines

These Guidelines need not apply in the sale of structured deposits to non-retail investors (as defined in Chapter 10), and to overseas investors (as defined in Chapter 8).

6.2 MAS seeks comments on the content of the above Guidelines.

6.3 MAS seeks views on whether these Guidelines are adequate in addressing the risks posed by structured deposits.

CHAPTER 7: OVER-THE-COUNTER DERIVATIVES

As mentioned in Chapter 5 earlier, the definition of "futures contract" under the SFA will be widened to include non-exchange traded forward and difference settled contracts. Consequently, over-the-counter ("OTC") derivatives will fall within the scope of investment products under the FAA. MAS is of the view that regulating OTC derivatives under the FAA will address the risk that OTC derivatives may be offered to retail investors without a proper needs-based analysis and adequate disclosure of product information and risks. A provision similar to Section 128 of the SFA requiring retail investors to sign a risk disclosure (acknowledging they are aware of the risks) may also be mandated for OTC derivative products.

7.1 MAS seeks views on its proposal to include OTC derivative products as investment products under the FAA and subject financial advisory services on OTC derivatives to the business conduct rules in the FAA.

2 Under the proposed framework for non-retail investors outlined in Chapter 10, the provision of financial advisory services to non-retail investors, such as institutional or accredited investors, will be given broad exemptions from requirements in the FAA. Thus, there will be minimal impact on the business conduct of institutions that deal in OTC derivatives with only accredited investors or other institutional investors.

CHAPTER 8: REGULATORY TREATMENT OF GENERALLY CIRCULATED ADVICE

Financial advisers ("FAs") must have a reasonable basis for their recommendations on investment products and have regard to the investment objectives, financial situation and particular needs of the person receiving the advice. This requirement is enunciated in section 27 of the FAA and the FAA Notice on Recommendations on Investment Products ("recommendation requirement").

2 An exemption from compliance with the recommendation requirement is provided for under Regulation 34 of the Financial Advisers Regulations ["FAR 34(1)"], to research reports which are intended for general circulation and issued without regard to any person's situation and needs. Advice provided in such reports is not targeted to meet the needs and circumstances of specific individuals (referred to in this consultation paper as "untargeted advice"). MAS considers it neither necessary nor practical for FAs providing "untargeted advice" to conduct the full range of procedures in order to comply with the "know your client" and suitability requirements stipulated under the FAA.

3 MAS recognises that such "untargeted advice" may be provided in other forms, such as by means of seminars and talks. In such cases, MAS is of the view that the recommendation requirement is, on balance, too restrictive to FAs.

4 MAS is proposing that FAs need not comply with the recommendation requirement if the following conditions are met:

(a) the advice, whether oral or written, is not targeted at a specified individual but is generally disseminated to the public or a section thereof; and

(b) the advice does not purport to take into account the recipient's investment objectives, financial situation and particular needs.

Examples of such advice include, but are not limited to, generally circulated research reports, talks and seminars which are made available to the public or a section of the public.

5 The exemption from the requirement to comply with the recommendation requirement will be contingent upon FAs issuing an up-front disclosure informing the recipients of such advice that the advice does not take into account their specific investment objectives, financial situation and particular needs. FAs should also disclose that section 27 of the FAA and the FAA Notice on Recommendations on Investment Products will not apply to advice provided in these circumstances.

8.1 MAS seeks views on the proposal for other forms of "untargeted advice" to be excluded from the application of section 27 of the FAA and FAA Notice on Recommendations on Investment Products.

8.2 MAS seeks views on the proposed criteria set out in paragraph 4 for determining when advice provided is considered to be "untargeted advice".

8.3 MAS seeks views on the types of "untargeted advice", other than those mentioned above, which may meet the proposed criteria.

CHAPTER 9: REGULATORY TREATMENT OF THE PROVISION OF FINANCIAL ADVISORY SERVICES TO OVERSEAS INVESTORS

The FAA aims to safeguard the interests of investors in Singapore while fostering the growth of Singapore's financial advisory industry. Nevertheless, MAS must exercise some regulatory oversight in relation to FAs' activities (undertaken partly or wholly in Singapore) in providing financial advisory services to overseas investors.[27] This is because of the potential risk to Singapore's reputation as a sound and well-regulated international financial centre.

2 Section 90 of the FAA, read together with a primary offence-creating provision such as section 6, gives the FAA extra-territorial jurisdiction over an act done partly in and partly outside Singapore that would have constituted an offence had it been done wholly in Singapore. Through the application of this clause, the provision of financial advisory services to overseas investors, if conducted wholly or partly in Singapore, is covered by the FAA.

3 MAS recognises that FAs will be subject to the applicable laws and regulations of the foreign jurisdictions in which they offer financial advisory services. It is not MAS' policy intent to impose additional compliance obligations on FAs by applying the FAA's conduct requirements to them when they are carrying on business for offshore clients.

PROPOSED IMPLEMENTATION

4 Pursuant to section 6(1) of the FAA, FAs are required to hold a licence to conduct financial advisory services in Singapore, unless exempted under other provisions (e.g. section 23 of the FAA). MAS proposes to exempt FAs from the business conduct provisions in Part III of the FAA, except section 33 of the FAA ("Negotiation and placement of risk with unregistered insurer"), when they provide financial advisory services to overseas investors.

[27] Overseas investors refer to investors who are not resident in Singapore.

Some of the notices issued by MAS[28] will also not apply to FAs when they are providing financial advisory services to overseas investors.

9.1 MAS seeks views on the proposal to exempt FAs from business conduct rules in the FAA when they provide financial advisory services to overseas investors.

NEW CONDITIONS OF LICENCE OR EXEMPTION

5 With this clarification of the scope of the FAA, MAS will add new conditions of licence or exemption relating to FAs' dealings with overseas investors. FAs will be required to –

(a) comply with the applicable laws and rules in the foreign jurisdictions in which they target overseas investors;

(b) refrain from holding out that their conduct is regulated by MAS when they provide financial advisory services to overseas investors; and

(c) disclose to their overseas clients that the FAA's protections do not cover overseas investors.

In addition, MAS expects all FAs to conduct their activities in an ethical manner and ensure fair dealing when providing financial advisory services to all their clients. This requirement will also be reflected as either a new condition of the licence or exemption.

9.2 MAS seeks views on the proposed conditions of either the licence or exemption.

[28] These Notices relate to "Recommendations on investment products" and "Information to clients and product information disclosure" respectively.

INVITATION FOR COMMENTS

Chapter 6: Structured Deposits

6.1 MAS seeks views on whether the proposed definition of structured deposits captures all such products currently available in the market.

6.2 MAS seeks comments on the content of the proposed Guidelines that apply to structured products that meet the definition of a deposit in the Banking Act (Cap. 19).

6.3 MAS seeks views on whether these Guidelines are adequate in addressing the risks posed by structured deposits.

Chapter 7: Over-the-Counter Derivatives

7.1 MAS seeks views on its proposal to include OTC derivative products as investment products under the FAA and subject financial advisory services on OTC derivatives to the business conduct rules in the FAA.

Chapter 8: Regulatory Treatment of Generally Circulated Advice

8.1 MAS seeks views on the proposal for other forms of "untargeted advice" to be excluded from the application of section 27 of the FAA and FAA Notice on Recommendations on Investment Products.

8.2 MAS seeks views on the proposed criteria set out in paragraph 4 of this chapter for determining when advice provided is considered to be "untargeted advice".

8.3 MAS seeks views on the types of "untargeted advice", other than those mentioned in this chapter, which may meet the proposed criteria.

Chapter 9: Regulatory Treatment of the Provision of Financial Advisory Services to Overseas Investors

9.1 MAS seeks views on the proposal to exempt FAs from business conduct rules in the FAA when they provide financial advisory services to overseas investors.

9.2 MAS seeks views on the proposed conditions of either the licence or exemption.

PART IV: CHANGES AFFECTING BOTH THE SFA AND FAA

CHAPTER 10: TREATMENT OF NON-RETAIL INVESTORS UNDER THE SFA AND FAA

The full range of regulatory protection set out in the SFA and the FAA is targeted at retail investors. In line with the practice in other major financial centres, MAS differentiates between retail and non-retail investors in recognition of the latter category's lesser need for regulatory protection.

2 This differentiated approach is implemented through exemptions from a number of provisions in the SFA and FAA for entities which deal with non-retail investors or, in the case of offers of investment, to offers that are targeted at non-retail investors. For example, intermediaries are exempted from licensing and/or certain business conduct rules when dealing with accredited investors. In addition, issuers of securities are not required to provide a full prospectus in respect of offers that are made only to sophisticated investors or specified institutions.

RATIONALISING THE CRITERIA FOR INDIVIDUALS TO QUALIFY AS NON-RETAIL INVESTORS

3 At present, an individual will be classified as a non-retail investor if he qualifies as an accredited investor or a sophisticated investor. To qualify as an accredited investor, he must have net personal assets of at least $5 million, while to qualify as a sophisticated investor, he must have net personal assets of at least $2 million or annual income of at least $300,000 in the preceding year. These high net worth individuals are generally considered to be sufficiently knowledgeable and experienced in managing their financial affairs and therefore require less regulatory protection.

4 MAS is of the view that applying a consistent set of criteria to determine whether an individual qualifies as a non-retail investor would improve the regulatory framework and facilitate the compliance process. MAS proposes to remove the class of *sophisticated investor* and set the threshold for high net worth individuals qualifying as an accredited investor when the individual has $2 million in net personal assets or $300,000 in annual income.

5 An intermediary who wishes to deal with a client on an accredited investor basis will be required to take reasonable measures to ascertain the financial standing of the client, and to disclose to the client the SFA/FAA provisions in general that it is exempted from complying with when it is dealing with the client as an accredited investor.

10.1 MAS seeks views on the proposal to rationalise the criteria in the SFA and FAA for an individual to qualify as an accredited investor.

6 The threshold for a corporation to qualify as an accredited investor remains unchanged, i.e., it must have total net assets exceeding $10 million (or its equivalent in a foreign currency) as determined by the last audited balance sheet of the corporation, if it is required to prepare audited accounts periodically. If the corporation is not required to prepare audited accounts, a balance-sheet of the corporation certified by the corporation as giving a true and fair view of the state of affairs of the corporation may be used instead.

7 Though the term "sophisticated investor" will no longer exist, the exemptions from prospectus requirements set out in sections 275 and 305 of the SFA will continue to apply where the offer is made to –

(a) any person who meets the accredited investor test as stated at paragraphs 4 or 6;

(b) a person who acquires securities pursuant to the offer or invitation in question, as principal if the aggregate consideration for the acquisition is not less than $200,000 (or its equivalent in a foreign currency) for each transaction whether such amount is paid for in cash, by exchange of shares or other assets; and

(c) an officer of the person making the offer or invitation or a spouse, parent, brother, sister, son or daughter of that officer or of the person making the offer or invitation, if he is a natural person.

10.2 MAS invites comments on the proposal to remove the term "sophisticated investor".

RATIONALISING THE CATEGORIES OF NON-RETAIL INVESTORS

8 For a more coherent regulatory framework that applies to non-retail investors, MAS will introduce two other categories of non-retail investors –

(a) ***Institutional investors*** – These are regulated financial institutions or other entities that deal in financial products in the course of ordinary business (the institutions listed under sections 274 and 304 of the SFA will be used as a reference). Institutional investors should have the expertise to engage in such activities without regulatory protection. MAS will fully exempt intermediaries from the FAA requirements when they deal with institutional investors, in addition to exempting offers of investments made to such investors from the prospectus requirements.

(b) ***Expert investors*** – These are persons whose business involves the acquisition and the disposal of, or the holding of, capital markets products, whether as principal or agent. This category will also include individuals who deal in capital markets products in the course of their employment and therefore possess the necessary knowledge to trade a particular product (e.g., professional traders trading for their own account). Exemptions currently available when the investor is a person whose business involves the acquisition and disposal of, or the holding of, specific capital markets products (whether as principal or agent) will continue to apply when the investor is an expert investor.

10.3 MAS invites comments on the proposed definition of institutional and expert investors, and if there should be any additional regulatory exemptions for institutions dealing with such investors.

REVIEWING THE CRITERIA FOR OTHER ENTITIES AND STRUCTURES

9 MAS has received feedback that, for tax planning purposes, it is increasingly common for individuals who currently qualify as sophisticated investors to invest through an investment holding company or limited liability trust instead of purchasing securities directly. Such an investment holding company or trust would not qualify for prospectus exemptions under

sections 275 and 305 of the SFA unless it satisfies the net assets requirement for a corporation (i.e., $10 million) or purchases at least $200,000 of securities in value in a single transaction. MAS is considering whether the SFA should adopt a "look-through" approach such that investment holding companies and trusts, where the beneficial owners are sophisticated investors, can also be exempted from the prospectus requirements.

10 To give investors the flexibility to invest directly or via investment vehicles that they own or operate, MAS is considering whether to extend the scope of the exemption from the prospectus requirements under sections 275 and 305 to include a corporation whose sole business is to hold investments and whose shareholders would each qualify for the exemption on their own.

11 MAS is aware that the prospectus requirement may be circumvented by first offering securities to an investment vehicle and then having the shares in the investment vehicle sold to a retail investor. To prevent this, MAS proposes to restrict shareholders of the investment vehicle from selling their shareholdings in the investment vehicle except to other institutional investors or investors who would qualify for exemption under sections 275 and 305. This would be consistent with section 276 and section 305A inserted by the SF (Amendment) Bill 2003, which restrict the resale of securities acquired pursuant to the exemptions under sections 275 and 305.

10.4 MAS invites comments on the proposal to extend the scope of the exemption from the prospectus requirements under sections 275 and 305 as outlined above, as well as the safeguards for preventing circumvention.

12 As part of the study on the qualifying criteria for entities and structures, MAS will also review the criteria – or the application of the criteria – for entities or structures such as special purpose vehicles, investment holding companies, trusts or foundations, limited partnerships or partnerships and joint accounts to qualify as accredited investors.

CHAPTER 11: UNSECURED CREDIT FACILITIES TO DIRECTORS, OFFICERS AND EMPLOYEES

Section 119 of the SFA prohibits holders of a capital markets services licence ("licence holders") from granting unsecured credit facilities to their officers, employees and their associated or connected persons ("relevant persons"), for the purpose of dealing in any capital markets product, including securities. MAS has received feedback from the industry that such prohibitions should not apply to relevant persons' trading in securities on an exchange if the trades are settled in accordance with the rules of the exchange. The industry also suggested that associated and connected persons should not be subject to the prohibition as it is unduly onerous for licence holders to keep track of the trades by associated or connected persons.

2 MAS has reviewed Section 119 of the SFA together with Regulation 43 of the Securities and Futures (Licensing and Conduct of Business) Regulations ["SFR"]. Regulation 43 of the SFR restricts licence holders from granting any unsecured credit facility to their directors. However, they may provide unsecured credit facilities to their officers and employees, subject to prescribed limits. An unsecured credit facility includes any unsecured advance, loan or credit facility, and any guarantee given for any loan, advance or credit facility obtained by the officers or employees for any purpose.

3 MAS believes that with the adoption of the risk-based supervisory approach, licence holders should have the discretion to decide whether to grant unsecured credit for staff trades and how to manage the resultant credit risks. Accordingly, MAS proposes to repeal section 119 so that unsecured credit for staff trades will no longer be prohibited, and make minor modifications to Regulation 43 of the SFR.

AMENDMENT OF REGULATION 43 OF THE SFR

4 In view of the proposed repeal of Section 119, Regulation 43 will be amended to make it clear that the limit imposed on an unsecured loan and credit facility would apply to any unsecured loan granted for the purpose of trading in any capital market product. In addition, to better achieve the

purpose of Regulation 43, the limit imposed would cover transactions in the account of any person over which the officers and employees have control or influence. In this respect, the meaning of "unsecured advance, unsecured loan or unsecured credit facility" in regulation 43(3) will be amended to include –

> "Any other unsecured debt arising from any transaction in capital market products: (1) entered into by the director, employee or officer for his own account; or (2) entered into by another person who acts jointly or otherwise acts under or in accordance with the instruction or direction of the director, employee or officer in relation to the transaction."

11.1 MAS invites comments on the proposal to repeal section 119 of the SFA.

11.2 MAS seeks views on the proposal to revise the meaning of "unsecured advance, unsecured loan or unsecured credit facility" as stated at paragraph 4 above.

5 MAS will also review Section 24(1) of the FAA at the same time, as it is substantively similar to Section 119 of the SFA.

11.3 MAS invites comments on the proposal to repeal section 24(1) of the FAA.

INVITATION FOR COMMENTS

Chapter 10: Treatment of Non-Retail Investors under the SFA and FAA

10.1 MAS seeks views on the proposals to rationalise the criteria in the SFA and FAA for an individual to qualify as an accredited investor.

10.2 MAS invites comments on the proposal to remove the term "sophisticated investor".

10.3 MAS invites comments on the proposed definition of institutional and expert investors, and if there should be any additional regulatory exemptions for institutions dealing with such investors.

10.4 MAS invites comments on the proposal to extend the scope of the exemption from the prospectus requirements under sections 275 and 305 as outlined in this chapter, as well as the safeguards for preventing circumvention.

Chapter 11: Unsecured Credit Facilities to Directors, Officers and Employees

11.1 MAS invites comments on the proposal to repeal section 119 of the SFA.

11.2 MAS seeks views on the proposal to revise the meaning of "unsecured advance, unsecured loan or unsecured credit facility" in Regulation 43 of the SFR.

11.3 MAS invites comments on whether section 24(1) of the FAA should be repealed.

ANNEX: SUMMARY OF KEY RECOMMENDATIONS

Policy Issues	Key Recommendations
Offers of investment	1. To exempt from prospectus requirements offers for no consideration. 2. Not to exempt from prospectus requirements offers in connection with a compromise or arrangement of a Singapore-incorporated company where there is no change in effective control. 3. To retain prospectus liability for underwriters. 4. To make issue managers liable for prospectus contents. 5. Not to make other professionals involved in an offer liable for prospectus contents. 6. To subject a person to criminal liability only if the false or misleading statement included in or information omitted from the prospectus, is material. 7. For persons other than the offeror and its directors, to require intention, recklessness or negligence before imposing criminal liability for prospectus contents. 8. To allow the dissemination of pre-deal research reports to institutional investors, for offers made concurrently in Singapore and another jurisdiction where pre-deal research reports are permitted.
Markets and clearing facilities	9. To move from an authorisation to a designation approach for clearing facilities. 10. To include price interaction as a key criterion for an entity to be considered as a market.

Policy Issues	Key Recommendations
Definition of "futures contract" and broking of OTC derivatives	11. To amend the definition of "futures contract" to include OTC derivatives. 12. Not to regulate the broking of OTC derivatives
Product scope of FAA	13. To include structured deposits as investment products and to issue Guidelines on the sale of such products. 14. To include OTC derivatives as investment products.
Generally circulated advice	15. To waive the needs-based advisory process for generally circulated advice.
Advice to overseas investors	16. To exempt financial advisers from the business conduct rules under the FAA in respect of their offshore business.
Non-retail investors	17. To remove the class of "sophisticated Investors" from the SFA. 18. To set the threshold for individuals to qualify as "accredited investors" at having at least $2 million in net personal assets or $300, 000 in annual income. 19. To exempt intermediaries dealing with institutional investors from business conduct rules under the FAA. 20. To adopt a look-through provision to exempt investment holding companies from prospectus requirements.
Unsecured Credit facilities to directors, officers and employees	21. To lift the prohibition against intermediaries granting unsecured credit facilities to staff and directors for the purpose of trading in capital market products.