

CONSULTATION PAPER

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Chapter 3: Fidelity Funds of Securities and Futures Exchanges

MAS

Monetary Authority of Singapore

CHAPTER 3: FIDELITY FUNDS OF SECURITIES AND FUTURES EXCHANGES

Under Part XI of the SFA, each approved securities exchange / approved futures exchange is required to establish a fidelity fund for the purpose of compensating investors who suffer losses as a result of defalcation¹, bankruptcy or insolvency of the members of the exchange (“**exchange members**”). Section 186 of the SFA sets out the circumstances under which claims can be made on the fidelity fund. For ease of reference, in this consultation paper, the term “**securities exchange fidelity fund**” refers to a fidelity fund established by an approved securities exchange whilst the term “**futures exchange fidelity fund**” refers to a fidelity fund established by an approved futures exchange.

Section A: Transactions on Overseas Securities Exchanges

2 Under Sections 186(1) to 186(5) of the SFA, an investor can claim against the securities exchange fidelity fund for losses arising from securities transactions conducted through securities exchange members in the event of defalcation, bankruptcy or insolvency of these members. In its current form, the provisions are unclear as to whether losses arising from trades transacted on overseas securities exchanges can be claimed against the securities exchange fidelity fund. Transactions carried out on overseas exchanges would include those routed via cross-border exchange-to-exchange trading links, as well as those conducted via exchange members’ own access to overseas markets.

¹ Section 2 of the SFA defines defalcation as “misapplication, including misappropriation, of any property”.

3 We are of the view that the securities exchange fidelity fund should only cover losses arising from trades that (a) are carried out on the approved securities exchange in Singapore; or (b) if carried out on an overseas securities exchange, are routed to the approved securities exchange in Singapore via cross-border exchange-to-exchange trading links.

4 One of our main considerations is that the sufficiency of a securities exchange fidelity fund can only be tested against trades on the approved exchange and those routed via its cross-border exchange-to-exchange trading links. The securities exchange fidelity fund would be exposed to liability that cannot be determined if claims arising from overseas exchange transactions (other than those that are routed via cross border exchange-to-exchange trading links) are also allowed, thus adversely affect the rights of other investors who have traded through the approved exchange.

3.1 MAS seeks views on the proposal for the securities exchange fidelity fund to only cover losses arising from trades that (a) are carried out on the approved securities exchange in Singapore; or (b) if carried out on an overseas securities exchange, are routed to the approved securities exchange in Singapore via cross-border exchange-to-exchange trading links.

Section B: Transactions on Overseas Futures Exchanges

5 Section 186(14) of the SFA currently disallows a claim on a futures exchange fidelity fund if — *“(a) the person has suffered pecuniary loss because of a defalcation committed by a member of the*

exchange or by any agent of the member; and (b) such defalcation is ... in connection with the trading of a contract which is not a futures contract that is cleared or to be cleared by a designated clearing house or a futures exchange in Singapore”.

6 Consistent with the position for securities exchange fidelity funds, MAS is of the view that futures exchange fidelity fund should only cover losses arising from futures trades that:

- (a) Are carried out on the approved futures exchange in Singapore; or
- (b) If carried out on an overseas futures exchange, are routed to the approved futures exchange in Singapore via cross border exchange-to-exchange trading links.

7 Whilst Section 186(14) of the SFA is consistent with the policy intent to only cover losses arising from futures trades that are carried out on the approved futures exchange in Singapore, it refers only to the defalcation scenario. MAS proposes to amend that section to:

- (a) Include references to the bankruptcy and insolvency scenarios (these are scenarios that are currently covered by the securities exchange fidelity fund provisions); and
- (b) To cover losses arising from futures trades carried out on an overseas futures exchange if they are routed to the approved futures exchange in Singapore via cross border exchange-to-exchange trading links.

3.2 MAS seeks views on the proposal to amend the Section 186(14) of the SFA to (a) include references to the bankruptcy and insolvency scenarios; and (b) to cover losses arising from futures trades carried out on an overseas futures exchange if they are routed to the approved futures exchange in Singapore via cross border exchange-to-exchange trading links.



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