RESPONSE TO FEEDBACK RECEIVED – POLICY CONSULTATION ON AMENDMENTS TO SECURITIES AND FUTURES ACT AND THE FINANCIAL ADVISERS ACT

On 11 October 2007, MAS issued the third policy consultation paper in relation to proposed amendments to the Securities and Futures Act ("**SFA**") and the Financial Advisers Act ("**FAA**"), together with the draft Securities and Futures (Amendment) Bill and draft Financial Advisers (Amendment) Bill ("**the Amendment Bills**").

The proposed amendments deal primarily with licensing and business conduct issues, and also the proposal to amend definitions of "securities" and "futures contract".

We have carefully considered all comments received in our policy deliberation. We thank all respondents for their comments.

MAS' responses to the proposals set out in Sections 5 to 9, and 12 of the policy consultation paper were published on 8 May 2008. They can viewed at http://www.mas.gov.sg/publications/consult_papers/Reports_and_Consultation_Papers.html.

Comments of wider interest in relation to Sections 1 to 4, 10, 11 and 13 of the policy consultation paper and the draft Amendment Bills are set out below, together with MAS' responses.

(I) Policy Consultation on Amendments to the SFA and the FAA (11 October 2007)

SECTION 1: Perpetual Licensing Regime for Corporate Licence Holders

MAS has proposed implementing perpetual licensing for holders of Capital Markets Services ("**CMS**") and Financial Advisers ("**FA**") licences. This means the requirement that holders of CMS and FA licences renew their licences every three years would be removed. This would align the licensing regime for corporate licensees under the SFA and the FAA with those of other financial institutions regulated by MAS, such as banks and insurance companies. It would also mean lower compliance costs to the industry.

All respondents welcomed the proposal.

SECTION 2: Regulatory Assistance to Foreign Regulators

MAS had proposed including a provision in legislation to clarify that foreign regulators would be required to obtain prior approval from MAS before inspecting CMS and FA licence holders, whose parent entities they supervise. The inspection would be for the purpose of carrying out their supervisory functions. Relevant safeguards and conditions would be imposed on such inspections.

A number of respondents suggested that licence holders should be notified prior to the commencement of inspections by foreign regulators. Several respondents suggested that foreign regulators of any company (not necessarily the parent company) related to the licence holder should be allowed to inspect the licence holder in respect of activities or services which have been outsourced to Singapore.

Another suggestion was to empower MAS to limit the scope of the inspection, so as to prevent foreign regulators from accessing information and documents which would not be required for the purposes of the foreign authority's regulatory functions.

<u>MAS' response</u>

It is MAS' intention to give CMS licence holders reasonable notice ahead of the conduct of such inspections by foreign regulators.

In response to industry feedback, MAS will consider requests for inspections by foreign regulators of related companies of CMS licence holders. MAS will approve such requests based on the merits of each case.

MAS will have powers under the SFA to impose conditions or restrictions on inspections by foreign regulators relating to:(i) the classes of information the foreign regulator will or will not have access to; (ii) the conduct of the inspection; (iii) the use or disclosure of any information obtained in the course of the inspection; and (iv) other matters as determined by MAS.

At this stage MAS will not be including this amendment in the FAA given the nature and scope of financial advisory business.

SECTION 3: Prohibition Order Regime

(A) <u>Extending the Prohibition Order Regime to Persons Exempt from Licensing Under the SFA</u>

The current prohibition order regime empowers MAS to issue prohibition orders ("**POs**") only to CMS licence holders and their representatives to prohibit them from performing regulated activities. MAS had in the policy consultation indicated the intention to extend MAS' powers to issue POs

under the SFA to:(i) exempt FIs and their representatives; (ii) persons who MAS believes have contravened the SFA; (iii) persons convicted of an offence involving fraud or dishonesty in Singapore or elsewhere; and (iv) persons required to pay a civil penalty in respect of a market misconduct offence under Part XII of the SFA.

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

MAS had proposed that a person who has been issued a PO under the SFA or the FAA be prohibited from assuming a management role in, or becoming a director or substantial shareholder of, a CMS or FA licence holder or an exempt person.

Several respondents had concerns that the grounds for issuing POs include minor offences and were of the view that POs should be issued when a person has been conclusively determined to have breached the SFA, and not when there is only reason to believe there is contravention. One respondent asked if information on POs issued against representatives would be made available on the public register of representatives.

MAS' response

After considering the feedback and upon further deliberation on this issue, MAS has made some adjustments to the proposed extension of the PO regime. To level the playing field between CMS licence holders and exempt financial institutions ("**FIs**"), and to keep out unsuitable persons from the industry, the PO regime will be extended to: (i) exempt FIs and their representatives, (ii) persons previously regulated by MAS; and (iii) persons convicted of conducting SFA-regulated activities without being regulated by MAS. MAS is also proposing an additional ground for issuance of prohibition orders under the extended regime to persons who have been ordered by the court, or have entered into an agreement with MAS, to pay a civil penalty for market misconduct.

The objective of issuing POs is to keep unfit persons from engaging or participating in any or all of the regulated activities. MAS does not take the issuance of a PO lightly. A PO will be issued where a serious offence has been committed. The affected person will be notified of MAS' intention to issue the PO and will be granted an opportunity to be heard, prior to MAS issuing the PO. The affected person will therefore have an opportunity to show cause why the PO should not be issued against him. In addition, should the affected person feel he has been aggrieved by MAS' decision to issue the PO, he may lodge an appeal to the Minister. The appeal will be heard by the Appeals Advisory Committee, comprised of independent members appointed by the Minister.

POs issued will be reflected against the representatives' names on the public register of representatives.

SECTION 4: Compliance Arrangements of Licence Holders

MAS had proposed to make it clear in legislation that the CEO and directors of licence holders are required to put in place appropriate compliance arrangements. This is to be done as part of ensuring licence holders' compliance with rules and regulations. The compliance arrangements would have to be commensurate with the nature, scale and complexity of their business.

Some respondents sought clarification on what "appropriate compliance arrangements" mean and suggested that MAS give industry guidance in this regard. Other respondents expressed a preference for a principles-based, as opposed to a prescriptive, approach to defining "appropriate compliance arrangement".

<u>MAS' response</u>

MAS notes the industry's queries on what would constitute "appropriate compliance arrangements". We agree that taking a principles-based approach rather than a prescriptive one in relation to this regulatory requirement would better accommodate licence holders that vary in the size and nature of their businesses. The CEO and directors must be able to demonstrate that their compliance arrangements are adequate for the purpose of ensuring compliance with all relevant rules and regulations. The proposed amendment is aimed at focusing the board's and senior management's attention on establishing adequate compliance arrangements.

SECTION 10: Confidentiality of Inspection and Investigation Reports

MAS had proposed a provision in legislation to make it clear that the contents of MAS' inspection and investigation reports, on persons inspected or investigated by MAS, are to be kept confidential. The proposed provision makes it explicit that the contents of MAS' inspection and investigation reports should not be disclosed to anyone other than an officer or auditor of the inspected or investigated entity, in connection with the execution of their official duties. Any exception to this rule would require MAS' written approval.

Respondents were generally supportive of the proposal, but highlighted the need to circulate MAS' inspection and investigation reports to group-level external audit and senior management, and to their legal, internal audit and compliance functions. One respondent asked if the confidentiality requirement will be imposed on FIs exempted from holding CMS and FA licences.

MAS' response

The proposed amendment will provide legal certainty to MAS' current practice of not permitting the disclosure of MAS' inspection and investigation reports to any person other than an officer or auditor of the inspected or investigated entity. MAS has reviewed the feedback and will consider requests for the disclosure of inspection and investigation reports to group-level officers of the parent entity on a case-by-case basis. The confidentiality requirement will also be imposed on FIs exempted from holding CMS and FA licences.

SECTION 11: Requirement to Seek Approval for Take-over of Licensees

MAS proposed making it a requirement for a potential owner or controller of a CMS or FA licence holder, to seek MAS' prior approval before entering into an arrangement which would result in him obtaining effective control of the licence holder. This is to ensure that MAS is effective in its gate-keeping role in respect of persons owning or controlling CMS or FA licence holders.

Most respondents agreed with the proposal. Two respondents suggested that where effective control over a licence holder is retained within the same corporate group structure and under the same ultimate holding company, these arrangements within the intermediate holding structures should be excluded from this requirement to seek MAS' approval.

MAS' response

MAS' approval must be sought even in cases where the ultimate owner or effective control remains unchanged, if shareholding structure of the licence holder has changed due to group restructuring. The nature of such changes will need to be explained to MAS. MAS will generally approve such arrangements so long as there are no concerns over the owners or controllers of the licence holder.

This requirement is in line with MAS' current practice, where a licence holder is required to seek MAS' approval prior to any change of its shareholders and members, that would result in any person (whether alone or acting together with any connected person), obtaining effective control of the licence holder. This is integral to MAS' gate-keeping role in ensuring that shareholders and controllers of CMS and FA licence holders are fit and proper.

SECTION 13: Amending the Definitions of "Securities" and "Futures Contract" in the SFA and the FAA

MAS had proposed amending the definition of "securities" to enable MAS to prescribe new products as "securities" in the SFA and the FAA, and to also

exclude products as "securities" in the SFA and the FAA. It was also proposed to amend the definition of "futures contract" in the SFA to allow MAS to exclude contracts from the definition of "futures contract". This was proposed in response to comments from the industry that the time required for a new product to be brought within MAS' regulatory ambit via legislative amendments to the SFA is too long.

Respondents generally expressed support for the addition of prescription powers in the definitions. In particular, there was positive feedback for what is viewed as a progressive move that will increase MAS' responsiveness to innovation and facilitate introduction of new financial products to the market.

Some respondents enquired whether MAS will be issuing guidelines as to the type of products that would be prescribed or excluded from the definitions. Other respondents suggested that the industry should be consulted prior to any product being prescribed within, or excluded from the definitions. Some respondents expressed the view that legislative debate in Parliament should be required before products are prescribed as "securities", especially if the definition is to be broadened. This would be akin to the process of amending primary legislation.

MAS' Response

The proposed amendments to the definitions of "securities" and "futures contract" in the SFA and the FAA represent a streamlining of MAS' administrative process by dispensing with the need to amend the SFA each time a new product is to be brought within MAS' regulatory ambit. MAS is encouraged by the industry's positive response to this proposal.

MAS notes that some respondents have expressed concern regarding the scope and type of products that could be prescribed as "securities". As a guideline, new products that could be prescribed as "securities" will be of the same general kind or class as the products already set out in definitions in the SFA. MAS does not envisage major deviations from the products currently defined as "securities".

In relation to the issuance of guidelines as to what products will be prescribed within, or excluded from the definitions, MAS is of the view that this could lead to an overly-restrictive regime. It would work against the intended effect of these amendments, which is to enable the timely introduction of new products to the capital markets. As for consulting the industry before prescribing products, MAS' general policy is to conduct public consultations on proposed changes to the regulatory environment, for example, where new legislation is being introduced or where amendments are being effected to existing legislation. This practice has been useful in helping MAS better understand, and more effectively respond to the industry's needs and feedback. However, for the prescription of new products, MAS is of the view that conducting public consultation each time

before MAS prescribes a new product would adversely affect the time-to-market for new products. Nevertheless, MAS does recognise the benefits of soliciting the industry's views and comments and will generally seek to do so in instances where the proposed prescription or exclusion of a product from may have a large impact upon the industry.

Some respondents highlighted the need for legislative debate especially in instances where the definition of "securities" would be broadened. MAS would like to clarify that the prescription of new products as "securities" will not lead to a general broadening of the definition of "securities" beyond the current scope of products set out in the definitions. The ability to prescribe new products as "securities" would be exercised within the scope of the general kind or class of products already set out in the SFA. MAS acknowledges that there are merits to having legislative debate in Parliament concerning fundamental changes to the scope of the definitions of "securities" and "futures contract". However, as mentioned in relation to the feedback regarding conducting industry consultation, having legislative debate in Parliament for every new product to be added to the definition of "securities" would adversely affect MAS' ability to facilitate the timely introduction of new products to the capital markets.

(II) Securities and Futures (Amendment) Bill

MAS received some comments in relation to the draft Securities and Futures (Amendment) Bill that was published for consultation. These comments were in relation to the draft provisions on the disclosure of interests (Part VII of the SFA), market conduct (Part XII of the SFA) and offers of investments (Part XIII of the SFA).

Disclosure of Interests (Part VII of the SFA)

Shareholdings notification requirements: Proposal to rationalise the notification requirements of directors and substantial shareholders of listed companies.

The requirements for reporting of interests by directors and substantial shareholders of listed companies currently reside in both the SFA and the Companies Act (Cap. 50) ("**CA**"). The amendments will streamline the notification process by:

- (i) migrating the requirements for directors and substantial shareholders to notify the listed company from the CA to the SFA;
- (ii) removing the requirement for directors and substantial shareholders to notify the SGX of changes in their interests; and
- (iii) making it a legal requirement for the listed company to notify investors of any changes in interests of directors and substantial shareholders.

The shareholding notification requirements will also be extended to foreign companies with a primary listing on the SGX. Where a person has the authority to acquire, dispose or exercise voting rights over securities, he shall be deemed to have an interest in those securities under section 4 of the SFA[1].

(a) Several respondents were concerned with the requirement for disclosure of interests in shares over which a person does not exercise voting rights. One comment was the possible increase in compliance costs for fund managers. Respondents requested that fund management activities be exempted from the substantial shareholding notification requirements.

MAS' Response

The requirement for disclosure of significant shareholdings ensures that the market is kept informed of changes in ownership and voting control in the corporation on a timely basis. Transparency of shareholdings is important in a fair and efficient market that inspires public confidence. MAS is therefore not inclined to exempt fund managers from the notification requirement. Fund managers are similarly not exempted from substantial shareholding reporting requirements in other major jurisdictions.

Nonetheless, MAS notes that fund managers, being in the business of managing securities, should have some flexibility to deal in securities without being subject to overly onerous reporting requirements. MAS is prepared to introduce a more flexible reporting regime with the notification thresholds for fund managers, open-ended investment companies and equivalent entities set at 5%, 10% and thereafter, at every 1% change in percentage level of shareholding. This is in line with the practice in the United Kingdom. This exemption will be provided for in the regulations, which will be released for public consultation.

(b) Respondents sought clarification on whether custodial services, escrow services and security trustee arrangements will be excluded from the substantial shareholding notification requirements, under section 4(10)(a) of the SFA.

MAS' Response

Section 4(10)(a) provides that a person who holds securities as a bare trustee will not be regarded as having an interest in those securities. Accordingly, where a person engaging in custodial services, escrow services or trustee arrangements holds securities as a bare trustee, such holdings will not give rise to any disclosure obligation under Part VII of the SFA.

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[1] MAS' responses to feedback on Policy Consultation on amendments to the SFA and the FAA published on 11 October 2007.

(c) Section 137(6) (*renumbered section 130(6)*) provides that "*a person shall conclusively be presumed to have been aware of a fact or occurrence at a particular time of which he would, if he had acted with reasonable diligence in the conduct of his affairs, have been aware at that time*".

One respondent commented that this provision is unclear if the substantial shareholder is a company. As a company can only act through its agents (e.g. its directors, officers and employees), the question is when such persons' knowledge can be attributed to the company.

MAS' Response

We agree with the respondent. The provision will state that where a person is an entity, it shall be presumed to be aware of a fact or occurrence if its officer, had he acted with reasonable diligence in the conduct of the entity's affairs, would have been aware.

(d) Section 137H (*renumbered 137A*) will impose responsibility on a beneficial owner, who has authorised another person to hold, acquire or dispose of securities on his behalf, to ensure that the second-mentioned person, his agent, notifies him of any acquisitions or disposals of those securities which may give rise to a disclosure obligation on his part.

One respondent felt it would be practically and commercially difficult for a beneficial owner to ensure actual compliance of this provision by his agent. The word "ensure" appears to impose a strict liability on the beneficial owner. If the intent is to ensure that the agent of the beneficial owner keeps him notified of changes in his shareholdings, section 137I could deal with such a situation.

MAS' Response

Under the shareholdings notification requirements in Part VII, a person's obligation to notify the corporation of changes in his shareholdings is triggered only upon the person becoming aware of the change. Section 137A is meant to prevent a beneficial owner from avoiding responsibility by claiming that his agent failed to notify him of the change in his shareholdings. The Hong Kong Securities and Futures Ordinance has a similar provision.

Section 137I (*renumbered 137B*) imposes responsibility on a registered holder of securities to notify persons who may have an interest in those securities of any disposals or acquisitions. An example is where a subsidiary acquires or disposes of securities of a corporation, which is not made on its parent company's behalf. As its parent company would be deemed to have an interest in securities held by the subsidiary, the parent company would be subject to notification requirements. Accordingly, the subsidiary is under

a duty to inform the parent company, so that the parent company can fulfill its notification obligations.

To address the respondent's concerns that the provision may be read to impose strict liability on the beneficial owner, the provision will use the words "take reasonable steps".

Market Conduct (Part XII of the SFA)

Corporate Derivative Liability: Proposal to make a company liable for the misconduct of its employees where the misconduct was committed with the consent, connivance or is attributable to any neglect on the part of the employee.

MAS had proposed[2] to make a company liable for market misconduct committed by its employees whilst trading on the company's behalf where the company had failed to take "*reasonable steps*" to prevent the misconduct.

In response to feedback raising concerns regarding the term "*reasonable steps*", MAS agreed to use the existing language in section 331 of the SFA instead, namely to make a company liable where the misconduct was committed with the *consent, connivance or is attributable to any neglect* on the part of its employee.

One respondent was concerned that the use of the term "*neglect*" which is a non-standard term, would introduces a level of doubt as to the standard of duty of care imposed. In particular, the respondent asked whether the term "*neglect*" was used expressly and deliberately by MAS, as opposed to the legal standard of "*negligence*". If there was not meant to be a difference, the respondent suggested using the term "negligence", instead of "neglect" for clarity.

MAS' Response

We agree with the respondent and will instead use the term "*negligence*" instead of "*neglect*" in the proposed legislation. There are case precedents explaining the legal concept of negligence and the term is also used in the relevant statutes of comparable foreign jurisdictions.

MONETARY AUTHORITY OF SINGAPORE
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[2] Policy consultation paper on the amendments to the SFA and the FAA published on 5 December 2006.

ANNEX

LIST OF RESPONDENTS TO POLICY CONSULTATION ON AMENDMENTS TO THE SFA AND THE FAA

- Allen & Gledhill LLP
- American International Assurance Co. Ltd
- Citibank NA, Singapore
- Clifford Chance Wong Pte. Ltd. (Singapore)
- Fidelity Investments (Singapore)
- FPA Financial Corporation Pte. Ltd.
- Institute of Certified Public Accountants of Singapore
- Khattar Wong & Partners
- Law Society of Singapore
- Lehman Brothers Singapore
- Life Insurance Association
- Macquarie Capital Securities (Singapore) Pte. Limited
- NTUC Income
- SG Asset Management (Singapore) Ltd
- Singapore Exchange Ltd.
- The Association of Banks in Singapore
- WongPartnership LLP