

Commodities regulation in Singapore Part 1: Licensing

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Introduction

For commodity groups with operations in Singapore, navigating the regulatory perimeter is becoming ever more complex. Recent years have seen an increase in regulatory requirements affecting commodities businesses, largely owing to reforms driven by the G20 and implemented by the Monetary Authority of Singapore (MAS). Groups operating in this sector therefore need to verify which, if any, of their activities are subject to regulation, and ensure that their regulated activities are conducted in a compliant manner.

We have prepared a **four-part guide** setting out the key Singapore regulatory requirements and restrictions which groups operating in the commodities sector need to be aware of, and the practical steps they can apply to remain compliant. These four parts cover (1) licensing, (2) derivatives trade reporting, (3) market conduct, and (4) anti-money laundering and countering the financing of terrorism.

This first part of our guide outlines how commodity groups may be affected by the Singapore licensing framework.

MAS licensing requirements

Licensable activities relating to commodities

On 8 October 2018, supervision of regulated activities concerning over-the-counter (OTC) commodity derivatives contracts moved from Enterprise Singapore (ES) to the MAS. The transfer was effected by corresponding amendments to relevant legislation, principally the Commodity Trading Act (CTA) and the Securities and Futures Act (SFA).

The change in supervision of OTC commodity derivatives did not affect the oversight of commodity futures contracts, which has always been the responsibility of the MAS under the SFA. Further, the supervision of activities relating to spot commodity contracts remains the responsibility of ES under the CTA.

Activities relating to commodities which now fall under MAS supervision include (among others):

- **Capital markets services.** These are regulated under the SFA and include any of the following, where conducted by way of business in relation to OTC commodity derivatives contracts and/or commodity futures contracts:
 - dealing;
 - fund management (e.g., investment decisions on behalf of another person);
 - operating an organised market; and
 - operating a clearing facility.

Depending on the facts, other regulated activities under the SFA may also be relevant – e.g., dealing in units of a collective investment scheme which invests in commodities.

- **Financial advisory services** (e.g., investment recommendations or research) provided by way of business in respect of OTC commodity derivatives contracts and/or commodity futures contracts, which are regulated under the Financial Advisers Act (FAA).

Entities conducting any of the above activities in Singapore, or with or for Singapore-based entities, may trigger a licensing requirement, and representatives of such entities may need to be registered with the MAS, unless a licensing exemption applies.

Other licensable activities

In addition to the activities outlined above relating to commodities, commodity groups should consider whether they conduct any other activities which may be licensable in Singapore – e.g., treasury activities. Licensable activities may include dealing in OTC derivatives contracts and futures contracts with an interest rate or foreign exchange (FX) underlying, and dealing in spot FX for the purposes of leveraged FX trading.¹

Territorial scope of the Singapore licensing regime

The Singapore licensing regime under the SFA and FAA has extraterritorial effect. Its application is therefore not limited to activities conducted within Singapore (e.g. by Singapore-incorporated trading entities), but may also capture activities conducted by persons outside Singapore (e.g. overseas trading entities) with counterparties or for persons based in Singapore. Even where activities regulated under the SFA or FAA are conducted wholly outside of Singapore, if they have a substantial and reasonably foreseeable effect in Singapore, they may trigger a licensing requirement unless an exemption applies.

Definition of ‘derivatives contract’

The definition of ‘derivatives contract’ does not include (among others) spot contracts.²

Further, in relation to contracts and arrangements relating to commodities, the following considerations apply:

- In relation to both OTC commodity derivatives contracts and commodity futures contracts, generally only derivatives contracts with a tangible underlying commodity are regulated (subject to exceptions, e.g., for certain futures contracts).
- Physically settled commodity forwards are not regulated as a derivatives contract where they have the purpose of fulfilling the needs of the day-to-day operations of the business of one or more of the parties. The availability of this carve-out depends principally on whether the criterion referring to the “needs of the day-to-day operations of the business of one or more of the parties” can be fulfilled, especially where the relevant transaction is entered into by entities that are solely trading intermediaries and none of the entities is a producer or end user of the underlying commodity.

Licensing exemptions

In respect of an activity falling within the scope of the SFA or FAA, a licensing requirement will not be triggered where an exemption applies. Exemptions which may typically be relevant to trading activities of commodity groups include the following:

- dealing in OTC commodity derivatives contracts solely with persons qualifying as ‘accredited investors’, ‘institutional investors’ and/or ‘expert investors’ under the SFA;
- dealing in OTC derivatives contracts (of any type) on own account or for the account of a related corporation and with:
 - a related corporation; or
 - another type of eligible counterparty (e.g. a Singapore-licensed bank or approved merchant bank, or an equivalent overseas entity (each a Licensed Intermediary)), provided the person does not receive any spread or remuneration in connection with such dealing;
- dealing in futures contracts (of any type) for any person carrying on such dealing on own account or for the account of a related corporation;
- dealing in spot FX contracts for the purposes of leveraged FX trading for any person carrying on such dealing on own account or for the account of a related corporation, and:
 - with a related corporation; or
 - with or through another type of eligible counterparty (e.g. a Licensed Intermediary);

¹ Under a spot FX contract for the purposes of leveraged FX trading, the parties enter into a spot FX contract pursuant to which one counterparty provides to the other counterparty or the counterparty’s agent money, securities, property or other collateral which represents only a part of the value of the spot FX contract. For further details on what constitutes a ‘spot contract’ please see “Definition of ‘derivatives contract’”.

² Broadly defined as contracts or arrangements for the sale or purchase of an underlying at the spot price, where delivery is to occur immediately or within a period reflecting market convention.

- providing financial advice or research on OTC commodity derivatives contracts solely to persons qualifying as ‘accredited investors’, ‘expert investors’ and/or ‘institutional investors’ under the FAA;
- providing financial advisory services solely to persons qualifying as ‘institutional investors’ under the FAA, and for advising solely related corporations; and
- an approved global trading company dealing in or providing financial advice or research on OTC commodity derivatives contracts.

Further licensing exemptions and exceptions may be relevant, depending on the facts.

Timing considerations

In connection with the changes to the SFA which took effect on 8 October 2018, the MAS put in place transitional arrangements for licensing requirements relating to OTC derivatives contracts.

Under these transitional arrangements:

- any unregulated entity which, prior to 8 October 2018, dealt solely in OTC derivatives contracts which were not regulated prior to that date, will need to apply to the MAS for a capital markets services (CMS) licence by 8 October 2020, unless an exemption applies; and
- any unregulated entity which intends to start dealing in OTC derivatives contracts (of any type) only after 8 October 2018 will need to obtain a CMS licence prior to commencing such dealing, unless an exemption applies.

ES licensing requirements

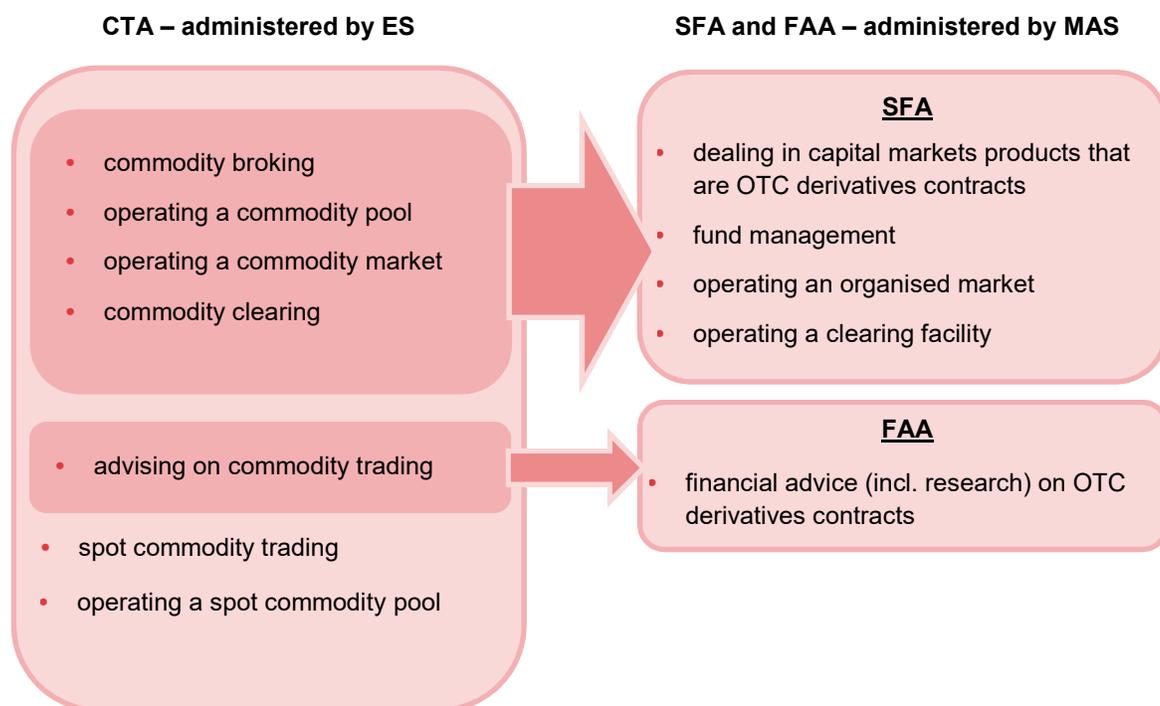
Licensing requirements under the CTA

As a result of the recent changes to the CTA and SFA, the supervision of certain persons by ES under the CTA moved to the MAS under the SFA. Broadly, this concerns persons (and representatives of persons) who, under the CTA, conducted activities in relation to ‘commodity contracts’ (effectively, OTC commodity derivatives contracts) – specifically:

- commodity brokers;
- commodity pool operators;
- commodity trading advisers;
- commodity market operators; and
- commodity clearing houses.

However, ES’ supervision under the CTA still covers activities relating to ‘spot commodity trading’ – in summary, the purchase or sale of a tangible commodity at its current market or spot price, where the commodity is to be physically delivered. Persons regulated under the CTA in relation to this activity include:

- spot commodity brokers;
- spot commodity pool operators; and
- representatives of any spot commodity broker or spot commodity pool operator.



8 October 2018: Transfer of supervision from ES to MAS

Licensing exemptions

Persons engaging in spot commodity trading who would in principle trigger a licensing requirement under the CTA will be automatically exempt from licensing where they:

- carry on the trading for their own account and in doing so, do not solicit any funds from any member or section of the public; or
- are not a party to any contract for the purchase or sale of the commodity, do not carry the customer's position, margin or account in their own books, and do not accept money or assets from the customer as settlement, margin, guarantee or security for any such purchase or sale.

Timing considerations

In connection with the changes to the SFA which took effect on 8 October 2018, transitional arrangements for licensing requirements relating to commodity contracts were inserted into the CTA.

Under these transitional arrangements, any person who was granted a licence or approval under the CTA for an activity relating to commodity contracts prior to 8 October 2018 and whose licence or approval subsisted at that date remains subject to the CTA until 8 October 2020, unless that licence or approval is terminated or a corresponding licence or approval is approved or refused under the SFA at an earlier date.

Other licensing requirements

Depending on the activities undertaken by a commodity group, other Singapore licensing requirements may arise. For example, moneylending under the Moneylenders Act (Cap. 188) (MLA) may be relevant to the activities of commodity groups that are active in trade financing. If the lending entity and/or borrower is based in Singapore, a licensing requirement under the MLA will in principle be triggered, unless an exemption applies.

Recommended practical steps

To ensure that your group operates in compliance with the Singapore licensing regime, you may wish to ensure that the following practical steps have been taken:

- **Territorial considerations:** In the first instance, those activities of the group with Singapore touchpoints should be identified. Activities conducted from within Singapore (e.g., by Singapore-based employees) will clearly fall within the territorial scope of the Singapore licensing regime. However, activities which occur outside Singapore – liaison with trading counterparties, execution of trades, etc. – may also be caught by the regime.
- **Nature of the activity:** If any activities of your group have Singapore touchpoints, assess whether those activities are, in principle, licensable in Singapore.
- **Availability of exemptions:** If it has been established that your group does conduct activities that are licensable in Singapore, the availability of licensing exemptions should be assessed.
- **Practical safeguards:** To ensure that your group’s activities continue to comply with the Singapore licensing regime on an ongoing basis, it is advisable to ensure that appropriate practical safeguards are built into the group-wide compliance infrastructure - for example, safeguards in relation to parameter management and ensuring new activities are assessed against the licensing framework.



“The Singapore licensing regime has extraterritorial effect. Its application is therefore not limited to activities conducted within Singapore”

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