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Shanghai International Energy Exchange  
500 Pudian Road, Pudong New District  
Shanghai 200122  
People's Republic of China

Email: [ine.advice@ine.cn](mailto:ine.advice@ine.cn)

Dear Sirs and Madams

**Re: Public Comment on the Trading Rules of Shanghai International Energy Exchange, the Standard Crude Oil Futures Contract and other Implementing Rules (together, the "Exchange Rules")**

On behalf of the membership of Futures Industry Association Asia ("FIA Asia") we welcome the opportunity to respond to the public consultation on the third and final set of Exchange Rules published by the Shanghai International Energy Exchange ("INE").

We refer to our previous letters submitted in response to the first and second sets of Exchange Rules and reiterate the comments raised in those letters particularly in relation to "QCCP status", adoption of international standards and industry best practice and disclosure of PFMI compliance.

We also wish to highlight the following key issues arising from the third set of Exchange Rules:

**1. Cross border regulation**

As indicated in our earlier letters, it will be necessary for the INE to be licensed, authorized or exempted in relevant overseas jurisdictions for trading and clearing to help foster overseas participation. The type of authorization or exemption will depend on the nature of the services provided, the products offered and the types and location of customers.

It would be helpful to market participants if the INE can publish and maintain a list of jurisdictions where the INE is permitted to grant access to its trading system and which jurisdictions it is seeking regulatory permission or exemption. Many exchanges and markets around the globe currently disclose this information. This disclosure will assist international participants in assessing which jurisdictions are available for the trading of INE's contracts and products.

**2. Trading Rules**

Under Article 16 of the Trading Rules, it states that a maximum of 500 lots and a minimum of one lot may be executed in each order. As set out in our earlier letters, we recommend that the INE consider the provision of a block trading facility in the Exchange Rules consistent with the majority of international exchange traded derivatives markets.

We have set out further detailed comments on the Trading Rules in the Schedule to this letter.

### **3. Trading Hours and Holidays: Cross border implications**

We note that in the Crude Oil Contract Specification, the trading hours are set at 9.00 – 11.30am and 1.30-3.00pm Beijing Local Time. We recommend that the trading hours be extended until at least 4.30pm to facilitate trading by international participants and to take into account regional time differences.

As set out in our earlier letters, the ability to facilitate cross border transfer and flow of funds is essential to attracting and supporting international participation and trading in the INE's markets. We request that the INE consider the impact of public holiday bank closures and time zone differences which may result in delay of fund transfers between domestic and international entities. For example, long holiday periods such as during the Lunar New Year period will have a significant impact on cross border funding arrangements.

The current processes and regulatory filings required for cross border transfers and remittance may also result in further delays. Where possible, we recommend the INE consider these issues and make necessary contingency arrangements and help to seek further clarity and guidance from the relevant regulatory bodies.

### **4. Central Clearing**

We would be grateful if the Exchange Rules can clearly state the contractual relationship between INE, its members and overseas participants and the legal capacity in which transactions are entered into by all stakeholders (including members, Overseas Special Participants and clients).

We strongly support central clearing and we note under the Exchange Rules, the INE will act as central counterparty. However the INE's capacity in this role is only mentioned in the Clearing Rules and not in the Delivery Rules. We would be grateful if the INE can clarify whether or not it will also be acting as central counterparty throughout the trade cycle including at the clearing and delivery stage.

We encourage, to the maximum extent possible under PRC law, that the clearing structure allow for legal title to be transferred or novated to the central counterparty. This will help to align the clearing structure with international standards and global best practice.

#### **(a) Default management**

Chapter 7 of the Clearing Rules currently sets out how default situations will be managed and particularly where a member is unable to perform its contractual obligations and responsibilities.

We would be grateful for further clarification on what actions can be taken by the INE in such a situation and whether the 'clearing reserves' of non-defaulting members will be affected and if the liability of clearing members will be limited. We would also be grateful if the INE can clarify how and when the clearing reserve of each member is required to be replenished.

We also understand that the INE will maintain a 'Risk Reserve fund'. As stated in Article 87 of the Clearing Rules, the Risk Reserve fund will be used as a financial guarantee fund when necessary and to protect the Exchange against any losses due to unexpected risks. We would be grateful if the INE can clarify how and when the Risk Reserve fund will be used and replenished.

#### **(b) Clearing Rules**

We have set out further detailed comments on the Clearing Rules in the Schedule to this letter.

## **5. Delivery**

### **(a) Delivery Warehouses**

We understand the INE will be announcing details for delivery warehouses separately and we look forward to publication of further information on capacity and availability.

### **(b) Delivery Grades**

We note the draft contract specification does not currently set out deliverable grades of the crude oil. Many of our global member firms are required to comply with sanctions administered and enforced by overseas government bodies including the US Department of the Treasury's Office of Foreign Assets Control ("OFAC"). Therefore, many of our member firms are required to ensure that the deliverable grades of crude oil are not subject to any sanctioned or high risk countries.

We respectfully request that the INE provide further clarity on the deliverable grades and countries for the standard crude oil contract to assist members with sanctions compliance. Other global exchanges have included this information in their rules and contract specifications, for example:

- CME: <https://www.cmegroup.com/rulebook/NYMEX/2/200.pdf>
- ICE EU [https://www.theice.com/publicdocs/contractregs/18\\_SECTION\\_L.pdf](https://www.theice.com/publicdocs/contractregs/18_SECTION_L.pdf)

Having this information available will help to ensure consistent global market standards and transparency and to assist fostering international participation in the INE's markets.

### **(c) Delivery Rules**

We have set out further specific comments on the Delivery Rules in the Schedule to this letter.

## **6. Data retention periods**

As noted in our previous letters, the data retention periods stated in the Exchange Rules (including the Clearing Rules) is 20 years. This period appears excessive and conflicts with requirements in other jurisdictions and may prove impractical with changes and advancements in technology. We recommend that the data retention period be reduced to 7 years.

## **7. Standard documentation**

The Exchange Rules reference various documents required to be provided and signed by market participants including risk disclosures and undertaking letters. We would be grateful if the INE can confirm whether there will be standard form documentation that will be available and can be used by all relevant market participants.

## **8. Audit and inspection**

As noted in our previous letters, we appreciate the need for INE to have audit, investigative and enforcement powers (including in the Enforcement and Clearing Rules) over participants to ensure to ensure a fair and transparent marketplace.

However, for overseas special participants, overseas intermediaries and overseas clients there may be practical challenges in applying these powers due to potential conflicts with existing laws and obligations in home jurisdictions eg due to bank secrecy laws, data protection laws and confidentiality obligations. We therefore recommend that the Exchange Rules state that the audit, investigative and enforcement powers

are subject to any information sharing agreements or memorandums of understanding entered into by the CSRC and other third country regulators or agencies.

We also recommend that the INE amend the rules to expressly introduce a concept of 'reasonableness' in relation to its requests for information so that these are limited in nature and primarily relate to the relevant overseas market participant's ability to perform their obligations under the Exchange Rules.

## **9. Governance**

At this stage, it is not clear whether members and overseas participants can participate in the governance of the Exchange. At many other exchanges and central counterparties around the globe, members are able to participate in risk committees and advisory committees to share their views and perspectives. We recommend where possible, that members and overseas participants be given the opportunity to have input into governance decisions such as risk assumption. This will help to reduce conflicts of interest and better allow for risk assumption and management for both the central counterparty and participants.

## **10. Conclusion**

Thank you for considering the issues raised in this letter.

We would be happy to meet with you further to discuss the issues raised in this letter and our earlier letters. Please contact Phuong Trinh at [ptrinh@fiaasia.org](mailto:ptrinh@fiaasia.org) or telephone: +65 6549 7335.

Yours faithfully,



Bill Herder  
President, FIA Asia

### Schedule: FIA Asia Comments on Exchange Rules

No.	Rule	Comment
<b>Delivery Rules</b>		
1.	Article 31	<p>The Rule relating to non-standard warrants states that <i>“The Exchange will be relieved from any responsibilities of guaranty for the performance of the contract”</i>.</p> <p>We would be grateful if the INE can clarify whether or not the INE has CCP status at the delivery stage or whether it only provides guaranty of performance to the delivery stage. For non-standard warrants, is it correct for us to interpret that the INE does not have guaranty responsibilities?</p>
2.	Article 60	<p>Under this Rule it appears that INE is not guaranteeing delivery but is imposing a 5% penalty on the non-defaulting party and providing an option to the buyer to either enter into new trade and be compensated for costs or unwind the trade. Is this correct, or will INE guarantee delivery (or use best efforts to source for delivery?)</p> <p>We would be grateful if the INE can clarify why the “compensation for difference” is limited to 15% of value of contract? This could potentially encourage non-delivery in times of significant market value (where price goes beyond 15% compensation and 5% penalty).</p>
3.	Alternative Delivery Procedures	<p>We note that in other global markets, participants are able to agree alternative delivery procedures. This is particularly helpful for international and global firms who manage various risk appetites and standards across many countries. The INE may wish to consider adopting a similar approach and we have included some CME procedures for your information and reference:</p> <ul style="list-style-type: none"> <li>• CME – 200109. Alternative Delivery Procedures <a href="https://www.cmegroup.com/content/dam/cmegroup/rulebook/NYMEX/2/200.pdf">https://www.cmegroup.com/content/dam/cmegroup/rulebook/NYMEX/2/200.pdf</a></li> <li>• CME – 771. Alternative Notice of Intention to Deliver (ANID) <a href="http://www.cmegroup.com/toolsinformation/lookups/advisories/clearing/Chadv14-462.html#pageNumber=1">http://www.cmegroup.com/toolsinformation/lookups/advisories/clearing/Chadv14-462.html#pageNumber=1</a></li> </ul>
<b>Clearing Rules</b>		
4.	Article 24	<p>This Rule describes the ‘clearing reserve’ for each member as a type of guarantee fund that shall not be applied as trading margin. In the interests of clarity, would it be possible to reword this as we understand there will be no member based guarantee fund.</p> <p>We would be grateful if the INE can clarify the basis for determining the minimum balances required for FF Members, client authorized Members and other non-FF Members.</p>
5.	Article 28	<p>Under this Rule, the INE may apply trading margin in a number of different circumstances including in “other circumstances as the Exchange deems necessary”. These powers seem very wide and unfettered and we would be grateful if the INE can consider setting out and clarifying the powers under this Rule.</p>
6.	Article 30	<p>This Rule refers to “Clearing Delivery Principal”. Could the INE clarify and define this term?</p>
7.	Article 38	<p>The formula refers to margin requirements for the ‘current day’. Could the INE clarify if this is intended to mean margin requirement for the ‘previous day’?</p>
8.	Article 41	<p>Could the INE clarify if this is intended to refer to ‘intraday margining’ instead of ‘intraday clearing’?</p>
9.	Article 44	<p>We would be grateful if the INE can clarify that this Rule is to be interpreted that a member is only required to collateralize its positions up to 80% and any amount above that can be withdrawn.</p>
10.	Article 45	<p>Under this Rule it appears that the INE has broad powers to effectively prohibit a member to withdraw member funds for any reason. We would be grateful if the INE can consider setting out and clarifying the powers under this Rule.</p>
11.	Article 49	<p>Under this Rule a member has 30 minutes prior to the opening of the next trading day to disagree with the accuracy of clearing data. We would recommend that the INE consider amending this to one business day from the date of transmission of clearing data in line with international standards.</p>

No.	Rule	Comment
12.	Article 54	We would be grateful if the INE can clarify how a client position can be transferred if this is margined on a net basis (under article 28) and not on a gross basis.
13.	Article 61	We would be grateful if the INE can clarify if there are any other penalties or consequences relating to failure to submit required receipts. Will the trade be unwound or will the INE procure payment or delivery of the underlying?
14.	Article 72	Under this rule, certain market participants are able to can post certain types of instruments as collateral. Would the same options apply to Members and OSPs?
15.	Article 77	We would be grateful for further clarification on what is intended under this Rule as it is currently unclear.
<b>Risk Management Rules</b>		
16.	Article 9	Under this Rule it appears that the INE has broad powers to effectively prohibit a member to withdraw member funds. We would be grateful if the INE can consider setting out and clarifying the powers under this Rule.
17.	Article 19	Under this Rule it appears that INE has a broad and sole discretion with respect to additional margin on long, short or both positions. In the interests of clarity and transparency we would be grateful if the INE can consider setting out and clarifying the powers under this Rule.
18.	Article 25	We note there are different position limits across various market participants. We would be grateful for clarification on the basis for distinction between position limits between FF members, OSBPs and Overseas Intermediaries compared to Non-FF members, OSNBPS and clients.
19.	Article 26	We would be grateful for clarification on the intent behind the second paragraph in this rule as it is currently unclear.
20.	Article 58	We would be grateful for clarification on what is intended by 'designated media' when making reprimands and sanctions.
<b>Trading Rules</b>		
21.	Articles 48 and 60	The Rules refer to "material change of production and operation conditions happens". We would be grateful for clarification on what is intended by this phrase.