



22 January 2014

Ms. Melissa Jurgens  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Center  
1155 21<sup>st</sup> St., N.W.  
Washington, DC 20581  
United States of America

VIA EMAIL

Dear Ms. Jurgens,

**Submission of Swaps Contract for the Commission's Mandatory Clearing Determination**

**1 Introduction**

- 1.1 Singapore Exchange Derivatives Clearing Limited ("**SGX-DC**"), a derivatives clearing organisation ("**DCO**") registered with the Commodity Futures Trading Commission (the "**Commission**"), hereby submits the SGX Hot-Rolled Coil ("**HRC**") Steel CFR ASEAN Swap (the "**Contract**") for the Commission's mandatory clearing determination under Commission regulation 39.5(b).
- 1.2 The Submission Cover Sheet is attached as Appendix 1.

**2 Commencement of Clearing**

- 2.1 SGX-DC intends to begin accepting the Contract for clearing from 17 February 2014.

**3 Eligibility to Clear**

- 3.1 Pursuant to Commission regulation 39.5(a)(1), SGX-DC is eligible to clear the Contract as they are within the same class of swaps as those it already clears.

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**4 Required Information under Commission regulation 39.5(b)(3)**

*Existence of significant outstanding notional exposures, trading liquidity and adequate pricing data*

- 4.1 70% of the world's steel consumption is attributable to emerging economies such as China, India and countries in the Association of South-east Asian Nations ("**ASEAN**"), which are the three pillars of growth in Asia. According to the World Steel Association statistics, since 2009, ASEAN's apparent steel consumption has grown at a compound annual growth rate of 9% per annum to reach 60 million tons in 2012.
- 4.2 A significant amount is driven by the demand for flat rolled steel products and imported mainly from countries in North Asia. This demand is linked to ongoing urbanisation and industrialisation across Asia.
- 4.3 The Contract will be Asia's first seaborne steel derivatives contract. Given SGX-DC's leading liquidity in iron ore, participants are uniquely able to efficiently margin the "hot spread" between iron ore and finished steel, which represents the fundamental economics of steelmaking.

*Availability of rule framework, capacity, operational expertise and resources and credit support infrastructure to clear the contract*

- 4.4 The Contract will be cleared under an established rule framework and operational infrastructure already in place and accepted by SGX-DC's Clearing Members.
- 4.5 SGX-DC ensures that it has the appropriate risk management, operations and technology capabilities in place to ensure that it is able to liquidate positions in the Contract in an orderly manner in a default.
- 4.6 The Contract is subject to margin and clearing fund requirements as set out under SGX-DC's Clearing Rules, which are available at the following link: [http://rulebook.sgx.com/en/display/display\\_main.html?rbid=3271&element\\_id=1903](http://rulebook.sgx.com/en/display/display_main.html?rbid=3271&element_id=1903).

*Effect on the mitigation of systemic risk, taking in account the market size and resources of SGX-DC*

- 4.7 It is noted that one of the key drivers of the Dodd-Frank Act was to address systemic risk in the over-the-counter ("**OTC**") derivatives market through central clearing of such products.

- 4.8 The benefits of central clearing are well-documented and include standardisation of key contract terms when settling a contract, ease of position adjustment, reduction of counterparty risk by having the central counterparty interpose itself between the initial buyer and seller and the provision of efficiencies through the consolidation of collateral management at a central point.
- 4.9 These benefits need to be weighed against the concentration of risk in a select few central counterparties.
- 4.10 SGX-DC has the necessary capability to clear the Contract from a market size and resources perspective.

*Effect on competition, including clearing fees and charges*

- 4.11 SGX-DC does not believe that its clearing of the Contract would have a negative or material impact on competition. The fee schedule for the Contract is attached as Appendix 2.

*Existence of reasonable legal certainty in the event of SGX-DC's or its clearing members' insolvency with regard to the treatment of customer and counterparty positions and collateral*

- 4.12 SGX-DC observes the Principles for Financial Market Infrastructures jointly promulgated by the Committee on Payment and Settlement Systems and International Organisation of Securities Commissions (the "PFMI") and its procedures have been assessed to be legally certain in the event of its or its Clearing Members' insolvency with regard to the treatment of customer and counterparty positions and collateral<sup>1</sup>.
- 4.13 SGX-DC has also previously provided a legal memorandum to the Commission on the ring-fenced treatment of cleared swaps customer collateral pursuant to Part 22 of the Commission's regulations.
- 4.14 SGX-DC's insolvency and the operation of default management mechanisms under its Clearing Rules will be governed by Singapore law, save for certain specific Clearing Rules that relate to cleared swaps customer collateral that are governed by U.S. federal laws.

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<sup>1</sup> Please see <http://www.imf.org/external/pubs/ft/scr/2013/cr13345.pdf> for a detailed assessment of SGX-DC's observance of the PFMI by the International Monetary Fund under the Financial Sector Assessment Programme.

**5 Contract Specifications**

- 5.1 The specifications of the Contract are attached as Appendix 3.

**6 Participants Eligibility Standards**

- 6.1 The standards for participation in clearing of the Contract are similar to SGX-DC's usual membership standards for Clearing Members clearing OTC commodity contracts as set out in Chapter 2 of its Clearing Rules.
- 6.2 SGX-DC imposes no participation criteria on its Clearing Members' customers, given that it faces its Clearing Members on a principal-to-principal contractual basis.

**7 Pricing Sources, Models and Procedures**

- 7.1 The daily settlement price ("DSP") of the Contract will be determined through the average of daily forward assessments provided by panellists, which include independent price vendors and brokers.
- 7.2 This is consistent with the DSP methodologies of existing commodity futures products cleared by SGX-DC and also identical to the Contract's corresponding cleared futures contract to allow for fungibility.
- 7.3 The DSP methodology will be reviewed if and when liquidity in the Contract builds up to a substantial level.
- 7.4 The final settlement price for the Contract will be based on the arithmetic average of The Steel Index HRC – ASEAN Imports spot prices in the expiring month.
- 7.5 The mode of final settlement will be in cash.

**8 Risk Management Procedures**

- 8.1 SGX-DC's risk management policies and procedures are well-established through its experience in clearing of OTC derivatives products.
- 8.2 Maintenance margin is collected from each Clearing Member to minimise potential losses to other non-defaulting Clearing Members and SGX-DC in the event of a Clearing Member's default. The margining methodology, SPAN, evaluates overall portfolio risk

through a scenario grid-based approach with a loss or gain attached to a particular combination of price change, volatility change and decrease in time to expiration.

- 8.3 Variation margin is calculated each day during the duration of the Contract until final settlement to facilitate sufficient collateral against the mark-to-market valuation of the Contract. Such variation margin is marked-to-market daily and settled in cash.

## 9 **Applicable Rules, Policies and Procedures**

- 9.1 The rules, policies and procedures that apply to the clearing of the Contract are set out in SGX-DC's Clearing Rules, which are publicly available at the following link: [http://rulebook.sgx.com/en/display/display\\_main.html?rbid=3271&element\\_id=1903](http://rulebook.sgx.com/en/display/display_main.html?rbid=3271&element_id=1903).

- 9.2 Additional amendments to the Clearing Rules have been proposed in relation to the clearing of the Contract. SGX-DC has filed a self-certification submission pursuant to Commission regulation 40.6 for the Clearing Rule amendments on 22 January 2014.

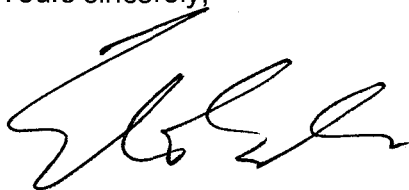
## 10 **Public Notice of Submission**

- 10.1 SGX-DC has made this submission publicly available on its website at the following address: [http://www.sgx.com/wps/portal/sgxweb/home/regulation/consult\\_pub/reg\\_ann](http://www.sgx.com/wps/portal/sgxweb/home/regulation/consult_pub/reg_ann).

## 11 **Contact Details**

- 11.1 Please do not hesitate to contact the undersigned at [eli.cohen@sgx.com](mailto:eli.cohen@sgx.com) or +65 6236 5104 should you require any clarification.

Yours sincerely,



Eli Cohen  
Head, Legal (Risk Management and Regulation)

**Appendix 1**

**Submission Cover Sheet**

## Appendix 2

### Fee Schedule

Clearing Fee Type	Description	Fee*
Cf 1	Trading Member (Individual)	US\$2.50
Cf 2	Clearing Member House Account	US\$2.50
Cf 3	Trading Member (Broker) House Account	US\$2.50
Cf 5	Clearing Member Customer Account	US\$3.50
Cf 6	Trading Member (Broker) Customer Account	US\$3.50
Cf 7	Trading Member (Proprietary) (Customer)	US\$2.50
Cf 8	Clearing Member Related Company House Account	US\$2.50
Cf E	Trading Member's Trading Representatives (House)	US\$2.50
Cf F	Trading Member's Trading Representatives (Customer)	US\$2.50
Cf G	Clearing Member's Trading Representatives (House)	US\$2.50
Cf K	Trading Member (Proprietary) (House)	US\$2.50

\*Fees shown are before the application of goods and services tax.

### Appendix 3

#### Contract Specifications

<b>Contract</b>	SGX Hot-Rolled Coil Steel CFR ASEAN Swap
<b>Contract size</b>	20 metric tons
<b>Ticker symbol</b>	HR
<b>Minimum price fluctuation</b>	US\$0.01 per metric ton
<b>Contract months</b>	24 consecutive months starting with the current month
<b>Position limits</b>	<p>A person must not own or control any combination of SGX Hot-Rolled Coil Steel CFR ASEAN Index Futures, Swaps and any other product traded by the Exchange and/or accepted by the Clearing House for clearing with an identical underlying, that exceeds an equivalent of 3000 regular-sized full month contracts on the same side of the Market and in all Contract Months combined.</p>
<b>Trade registration hours (Singapore time)</b>	<p>T session: 8:00am – 8:00pm T+1 session: 8:00:01pm - 4:00am Last Trading Day: 8:00am – 8:00pm</p>
<b>Last trading day</b>	Last publication day of The Steel Index Hot-Rolled Coil – ASEAN Imports reference prices in the contract month
<b>Final settlement price</b>	Cash settlement using the arithmetic average of all The Steel Index Hot-Rolled Coil – ASEAN Imports reference prices in the expiring month, rounded to two decimal places