FREQUENTLY-ASKED QUESTIONS
Guidelines on Contracts for Difference

(Date of Issuance: 6 April 2018)

1. GENERAL

1.1 What is a contract for difference (CFD)?

A CFD is a leveraged derivatives product that tracks the price movement of an underlying instrument. Essentially, a CFD is a contract an investor enters into with a CFD provider to gain exposure to an underlying instrument whereby differences between the closing and the opening value will be settled through cash payments.

Unlike options or futures contracts, a CFD does not have an expiry date and an investor's position can be closed by making a 'reverse' trade with the CFD provider.

The CFD offered by CFD providers are traded over-the-counter (OTC) or off-exchange. Thus, it is a bilateral trade where the CFD provider will be the investor's counterparty.

1.2 Why is the Securities Commission Malaysia (SC) introducing the CFD framework?

In line with the SC's *Capital Market Masterplan 2* to promote and develop the derivatives market, the CFD framework is intended to widen the range of investment products to cater to the needs and risk appetites of our investors. It is also in recognition of the increased sophistication of certain segments of the market.

Further, the framework provides additional opportunities to licensed intermediaries.

1.3 When will the requirements under the *Guidelines on Contracts for Difference* be implemented?

The Guidelines on Contracts for Difference is issued on 6 April 2018 to enable the industry to familiarise itself with the requirements for offering of CFDs.

It will be effective on 1 July 2018.

1.4 Would the offering of CFDs in Malaysia constitute a new regulated activity?

CFD is defined as derivatives under the *Capital Markets and Services Act 2007* (CMSA). Thus, the business of offering CFD is to carry out the activity of 'dealing in derivatives'.

2. PROVIDER

2.1 Who can offer CFD?

Entities who wish to offer CFD will be required to hold either a licence for dealing in derivatives or dealing in derivatives restricted to CFD, and comply with the requirements as specified in the *Licensing Handbook*.

Existing licensed intermediaries with licence to deal in derivatives are allowed to offer CFDs with prior notification to the SC. Other licensed intermediaries who wish to offer CFD must vary their licence to add on the required regulated activity.

2.2 How does one make an application for a licence?

A new applicant must complete the relevant forms as specified in the *Licensing Handbook* and submit the application to the SC's Authorisation and Licensing Department.

An application by existing licensed intermediaries for a licence variation to add on the regulated activity of dealing in derivatives must be made online to the SC via the Electronic Licensing Application system (ELA).

Detailed forms and application procedures are available on the SC website.

2.3 What is the financial requirement for a CMSL holder who is licensed for both activities of dealing in derivatives and clearing, who wishes to offer CFDs?

The financial requirements are as follows:

- Minimum paid-up capital and shareholders' funds unimpaired by losses of RM10 million at all times; and
- Minimum adjusted net capital: The higher of
  - RM500,000; or
  - 10% of aggregate margins

  at all times.

Once licensed, the CMSL holder must maintain at least the minimum financial requirement throughout the validity of its licence.

2.4 What is the financial requirement for a CMSL holder who is licensed for dealing in derivatives and wishes to offer CFDs?

The financial requirements are as follows:

- Minimum paid-up capital and shareholders' funds of RM10 million at all times; and

- Minimum adjusted net capital: The higher of
  - RM500,000; or
  - 10% of aggregate margins

  at all times.

Once licensed, the CMSL holder must maintain at least the minimum financial requirement throughout the validity of its licence.

2.5 What is the financial requirement for a CMSL holder that is licensed for dealing in derivatives restricted to CFD only?

The financial requirements are as follows:

- Minimum paid-up capital and shareholders' funds of RM10 million at all times; and
- Minimum 50% of total shareholders' funds in the form of liquid capital at all times.

Once licensed, the CMSL holder must maintain at least the minimum financial requirement throughout the validity of its licence.

2.6 How is liquid capital calculated?

In calculating the liquid capital, the provider must deduct all fixed or non-liquid assets whereby liquid asset means–

- securities or other current assets that have a ready market, or that are capable of realisation within 30 days; and
- in relation to an asset, "ready market" means a market where the asset can be realised without materially and adversely affecting that asset's value.

For avoidance of doubt–

(a) unaudited profits must be included in the computation of liquid capital;
(b) unaudited losses (including all unrealised losses except unrealised losses from principal positions that are mentioned in paragraph (d) must be deducted from liquid capital;
(c) unrealised gains from principal positions must be included in the computation of liquid capital; and
(d) unrealised losses from principal positions must be deducted from liquid capital.

2.7 Are there any examination requirements relating to the offering of CFDs?

In relation to the offering of CFDs by the CMSL holder, the following persons are required to sit for the relevant licensing examinations:

- Licensed director;
- Key management;
- Compliance officer; and
- CMSRL holders.

However, the SC may consider exempting the examination requirement if an applicant is able to demonstrate that he has–

(a) been licensed for at least three years in a recognised jurisdiction to undertake dealing in derivatives; and

(b) at least five years direct and relevant experience in the CFD business.

In respect of an existing CMSL holder for dealing in derivatives who wish to offer CFD, its licensed director, key management, compliance officer and CMSRL holders will not be required to resit the examinations.

2.8 Are there specific requirements relating to investor education?

Licensed intermediaries offering CFDs will be required to conduct educational programmes to assist investors to better understand CFDs and provide the necessary skills for trading. Such programmes must be held on a quarterly basis, at minimum.

2.9 Are CFD providers required to contribute to the Capital Market Compensation Fund?

The Capital Market Compensation Fund provides an avenue for recourse for individual investors in the event a licensed holder fails to pay amounts owing to its investors. Thus, licensed intermediaries offering CFDs will be required to contribute to the Capital Market Compensation Fund.

New licensed intermediaries will be required to contribute RM30,000 upon being licensed and thereafter RM5,000 on each licence anniversary date.

For an existing licensed intermediary who is a -

(a) holder of a CMSL for dealing in securities or dealing in derivatives, it will be required to contribute RM5,000 on each licence anniversary date, in addition to the contribution currently made under its existing licence;

(b) holder of a CMSL for other regulated activities, it will be required to contribute RM30,000 upon varying its licence and thereafter RM5,000 on each licence anniversary date, in addition to the contribution currently made under its existing licence.

3. DISCLOSURE DOCUMENT AND FEES

3.1 How is a registration of disclosure document and lodgment of PHS for CFD performed?

A lodgement and registration must be made to the SC by depositing the disclosure document and PHS together with relevant documentation required as specified in Chapter 6 of the *Guidelines on Contracts for Difference*.

Depositing the PHS and disclosure document to the SC does not mean that the SC has verified or endorsed the product or the CFD provider in any way.

3.2 When must the disclosure document and PHS be deposited with the SC?

The disclosure document and PHS must be deposited with the SC prior to the offer of the CFDs.

3.4 In what form must a disclosure document and PHS be provided to an investor of CFD?

A disclosure document and PHS can be provided to an investor in either a hardcopy version or in electronic form. However, a hardcopy version of these documents must be given if an investor requests for one. These documents must be provided to an investor before he makes an investment decision.

3.5 What are the applicable fees under this framework?

The relevant fees for the lodgement and registration of PHS and disclosure document are provided under the *Capital Markets and Services (Fees) Regulations 2012*.

4. PRODUCT PARAMETERS

4.1 What are the types of CFD that can be offered?

CFDs offered in Malaysia are only allowed to be based on shares and indices that meet the specified criteria prescribed in Chapter 3 of the *Guidelines on Contracts for Difference.*

Generally, the underlying shares have to meet the average daily market capitalisation requirement and the underlying companies listed are in compliance with the exchange's listing rules. For indices, the underlying index must consist of constituents that are listed on an exchange and is a recognised benchmark, among others.

4.2 Are there any minimum margin requirements on the CFD?

The SC is imposing minimum margin requirements on the CFD depending on the underlying instrument. The minimum margin requirements are necessary to prevent excessive leverage by investors.

The minimum margin requirements are set out in the table below:

Type of CFDs	Minimum margin
Single share CFDs	• 10% for shares index shares • 20% for non-index shares
Index CFDs	• 5%

For avoidance of doubt, a CFD provider may opt to set more stringent margin requirements.

4.3 Can an investor request for physical settlement of his CFDs position?

No. CFDs must be cash settled only. This serves to prevent any 'stealthy stake' build up in single shares CFDs.

5. INVESTORS

5.1 Who can invest in a CFD offered by a CFD provider?

Currently, CFDs can only be traded by sophisticated investors (i.e., any person who falls within any of the categories of investors set out in Part 1 of Schedule 6 and 7 of the CMSA). CFDs are a complex leveraged product and investors are advised to fully understand the risks associated with CFDs before trading them.

5.2 What information should investors expect to receive from a CFD provider?

Licensed intermediaries offering CFDs are required to provide potential clients the Product Highlights Sheet and any other disclosure documents on the CFDs. They are also required to obtain acknowledgement that the client has received the said documents and understand the risks associated with trading in CFD as stated in the risk statement.

5.3 What is the purpose of the risk statement?

The risk statement serves to ensure potential clients are aware and understand the risks involved in trading CFDs.

5.4 Is a CFD provider required to conduct a suitability assessment on an investor who wishes to invest in CFD?

Yes, a CFD provider must conduct a suitability assessment on an investor who wishes to invest in CFDs for the first time in Malaysia.

5.5 What happens when there is a complaint or dispute regarding the investment?

A CFD provider must have in place processes for complaints handling or dispute resolution. Such information must also be made accessible to all investors.