

# Legal Commentary

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## Futures Law (Draft) – More Than Futures

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### Preface

On 26 April 2021, the *Futures Law of the People's Republic of China (Draft for Consultation)* ("**Futures Law (Draft)**") was deliberated at the 28<sup>th</sup> Meeting of the 13<sup>th</sup> Standing Committee of the National People's Congress, and was later issued for public consultation on 29 April 2021, receiving keen, widespread interest of the domestic futures industry and the over-the-counter ("**OTC**") derivatives market. Currently, the regulatory framework overseeing China's futures market comprises the *Regulations on Administration of Futures Trading* ("**Futures Trading Regulation**"), issued in 2007 and last amended in 2017 by the State Council, and other administrative regulations and the *Measures for Administration of Futures Exchanges*, first issued by the China Securities Regulatory Commission ("**CSRC**") in 2007 and last amended in 2021, amongst other relevant departmental rules and regulatory documents, as well as self-regulations issued by the China Futures Association ("**CFA**") and futures exchanges. These regulatory mechanisms have been sufficient in relation to futures trading, trading venues (futures exchanges), transaction parties and supervision. However, on a legislative level, China has lacked an overarching basic law that standardizes the overall structure of the futures market. In contrast, the *Securities Law of the People's Republic of China* ("**Securities Law**") was adopted in 1998 for the securities market as an overarching basic law, and has been amended thrice and revised twice to accommodate the evolving climate and to adapt to new developments in the securities market. Similarly, other financial industries, such as funds, banking and insurance, are all respectively subject to basic laws as industry guidelines. The Futures Law (Draft) is an important step toward refining legislation surrounding the futures market and to systematize financial laws and regulations.

### Key analysis

The Futures Law (Draft) comprises 14 chapters and 173 articles, which can be categorized into six aspects: (1) clarification of legislative purpose, principles, and regulatory mechanisms; (2) systematization of futures transactions, settlement, and clearing framework; (3) regulation of other derivative transaction frameworks; (4) certifying protection of the rights and interests of futures traders; (5) standardizing the operation of futures business institutions, futures exchanges, futures clearing agencies and futures service agencies; and (6) clarifying supervisory responsibilities and legal liabilities in the futures market.

The Futures Law (Draft) provides innovative rules on multiple dimensions in response to strong concerns of domestic and foreign market participants, including applicable objects, business scope of futures companies, close-out netting, and extraterritorial application, and contains a rather complete regulatory framework for futures and other derivatives. It should be noted, however, that the Futures Law (Draft) remains in draft form and numerous clauses await further clarification or improvement.

## I Applicable objects – other derivatives

Chapter 1, “General Provisions”, of the Futures Law (Draft) clearly states that “This law applies to futures transactions and other derivatives transactions and relevant activities within the territory of the PRC”, suggesting that while the law bears the name “Futures Law”, it would supersede the concept of “futures” and include in its scope “other derivatives”. “Other derivatives” mainly incorporates non-standardized options contracts, swaps contracts, and forwards contracts in OTC transactions.

Despite the broad coverage of other derivatives, repo transactions are not currently subject to regulation in the Futures Law (Draft). We understand that international investors hope for repo transactions to be included in the Futures Law (Draft) due to the following reasons: (1) repo transactions, in essence, are similar to other derivatives in that both are transactions derived from underlying assets; for example, outright transfer bond repos, in essence, are a combination of a spot and a forward transaction in respect of the same financial instrument (bonds), (2) the inclusion of repo transactions and recognition of the applicability to repo transactions of the concepts of single agreement and close-out netting would align the Chinese repo market with international norms, because the *Global Master Repurchase Agreement (GMRA)* and the *International Swaps and Derivatives Association (ISDA) Agreement* both adopt a single agreement and close-out netting system.

We understand the possible reasons that regulatory authorities have not included repos in the Futures Law (Draft) to be as follows:

1. China’s repo market is dominated by pledged repo transactions, which however are unlikely to be considered derivative transactions.

China’s repo market includes outright transfer repo and pledged repo markets. Outright transfer repo transactions could not only provide an efficient source of funding and financing to repo investors, but also allow the relevant reverse repo party to acquire ownership of repurchased securities, fund long positions in securities and cover short positions for speculative, arbitrage or hedging purposes, thus making outright transfer repos an attractive tool for risk management by international investors. In that sense, outright transfer repos are similar to other derivatives. However, pledged repo transactions only contemplate the lending of money secured by a pledge over underlying securities, but no legal title to the underlying securities is transferred and no rehypothecation right is available, thus pledged repo transactions are more of a financing tool but less likely to be derivative transactions.

Pledged repos have dominated China’s repo market. According to the *2020 Financial Market Performance*, issued by the People’s Bank of China (“PBoC”), the volume of 2020 interbank bond market reached a total of RMB 1106.9 trillion for credit lending and repo transactions, of which pledged

repos accounted for RMB 952.7 trillion and outright transfer repos, RMB 7 trillion<sup>1</sup>. Therefore, not including repos in the Futures Law (Draft) might be a decision reflecting the climate of China's repo market.

2. Pledged repo transactions do not apply the single agreement or close-out netting system. Inclusion of repo transactions in the Futures Law would have a negligible effect on the overall repo market.

Currently, the guiding bond repo agreement in the PRC market is the *NAFMII Bond Repurchase Master Agreement (2013)* ("**Repo Master Agreement**"), issued by the National Association of Financial Market Institutional Investors ("**NAFMII**"), which applies to both outright transfer repos and pledged repos. Under the Repo Master Agreement, only outright transfer repos adopt a single agreement and close-out netting system, while each pledged repo transaction is subject to an independent agreement (even though an overarching master agreement and supplementary agreement apply to all pledged repo transactions). Consequently, including repos into the regulatory scope of the Futures Law (Draft) would not affect pledged repos and would thus have negligible impact on the overall repo market.

3. Inclusion of repo transactions in the Futures Law would require significant coordination among regulatory authorities.

China's repo market is regulated by multiple authorities; interbank market bond repos are mainly supervised by PBoC and NAFMII; exchange bonds and stock repo market are mainly supervised by CSRC and the stock exchanges. Inclusion of repos into the regulatory scope of the Futures Law (Draft) would require coordination between multiple regulatory authorities.

Based on the views mentioned above, it may currently be premature to include repos into the regulatory scope of the Futures Law (Draft). Nonetheless, we look forward to further clarification on the regulation of repo transactions by legislative and regulatory authorities.

## II Investor protection system

### 1. Investor classification system

The *Measures for the Supervision and Administration of Futures Companies* ("**Futures Companies Measures**"), issued by CSRC in 2019, require futures companies to implement an investor eligibility system and provide services and products pursuant to the investors' risk tolerance, based on their economic strength, professional knowledge, investing experiences, and risk appetite. Building on the investor eligibility system, the Futures Law (Draft) further classifies traders into ordinary and professional traders, where the eligibility of professional traders is subject to separate rules from the futures regulatory authority under the State Council. The trader classification system serves to protect and manage investors, as well as strengthen regulations on market innovation, prevent and mitigate systematic risk. Moreover, the investor classification would provide synchrony among rules applicable in the futures industry, such as the *Measures for Suitability Management of Securities and Futures Investors*<sup>2</sup> ("**Suitability Measures**"). Article 7 of the Suitability Measures states "Investors

<sup>1</sup> See: <http://www.pbc.gov.cn/goutongjiaoliu/113456/113469/4169040/2021012714175422623.pdf>.

<sup>2</sup> Suitability Measures: "Article 2 These Measures shall apply to sale of publicly-offered or privately-offered securities, publicly-offered or privately-offered securities investment funds and equity investment funds (including venture capital

shall comprise ordinary investors and professional investors. Ordinary investors shall be entitled to special protection in terms of information notification, risk warning, suitability matching, etc.” and further defines “professional investors”<sup>3</sup>. The investor classification system in the Futures Law (Draft) would provide a stronger legal basis for investor protection and be beneficial in aligning China’s investor protection system with international practice.

## 2. Diversified dispute resolution mechanism

Article 61 of the Futures Law (Draft) states that in the case of dispute between traders and futures business institutions, both parties can approach CFA to apply for settlement; Article 62 states, clearly, in the event that a trader files for civil compensation such as for market manipulation, insider trading and other futures-related issues, a class action suit could be launched when certain conditions are met, which resonates with the class action system in Article 95 of the Securities Law. Moreover, Article 56 reverses the burden of proof from ordinary traders to futures business institutions so that they bear the responsibility of proving that their acts are not misleading or fraudulent, etc. Where a futures business institution is unable to provide sufficient evidence, it would bear relevant liability and be liable for compensation in the event such acts led to traders’ losses. These provisions clarify the rights and obligations of various market players and would provide investors with greater assurance in resolving disputes.

## III Business scope of futures companies

Article 68(1) of the Futures Law (Draft) states that upon approval, futures companies are permitted to engage in the following businesses: (1) futures brokerage; (2) futures investment advisory; (3) futures market making; and (4) other futures businesses; futures companies engaging in asset management, other derivatives transactions among other businesses, need to seek approval from the futures regulatory authority under the State Council. Compared with the Futures Trading Regulation, the

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investment funds, hereinafter referred to as the “funds”), publicly-transferred or privately-transferred futures and other derivatives to investors, or provision of the relevant business services to investors.”

<sup>3</sup> Suitability Measures: “Article 8 Investors who satisfy any of the following criteria shall be recognized as professional investors: 1. financial institutions established with approval by the relevant financial regulatory authorities, including securities companies, futures companies, fund management companies and their subsidiaries, commercial banks, insurance companies, trust companies, finance companies etc., subsidiaries of securities companies, subsidiaries of futures companies, and managers of privately-offered funds, which are filed or registered with the industry associations. 2. wealth management products issued by the aforesaid organizations to investors, including but not limited to asset management products of securities companies, products of fund management companies and their subsidiaries, asset management products of futures companies, wealth management products of banks, insurance products, trust products, and privately-offered funds filed with the industry associations. 3. pension funds such as social security funds, enterprise annuities etc., social community funds such as charity funds etc., as well as qualified foreign institutional investors (QFII) and Renminbi qualified foreign institutional investors (RQFII). 4. legal persons or any other organizations which satisfy all the following criteria: (1) the net assets as at end of last year shall not be less than RMB20 million; (2) the financial assets as at end of last year shall not be less than RMB10 million; (3) they have two years or more of investment experience in securities, funds, futures, bullion, foreign exchanges etc. 5. natural persons who satisfy all the following criteria: (1) the financial assets shall not be less than RMB5 million, or the average annual personal income for the past three years shall not be less than RMB500,000; (2) they shall have two or more years of investing experience in securities, funds, futures, bullion, foreign exchanges, etc., or have two or more years of working experience in financial products design, investment, risk management and other related fields, or the senior management personnel of professional investors prescribed by Item 1 of this Article, or certified accountants or lawyers with recognized professional qualifications who engage in financial-related practices.

For the purpose of the preceding paragraph, financial assets shall refer to bank deposits, stocks, bonds, fund units, asset management plans, bank wealth management products, trust plans, insurance products, futures and other derivatives, etc.

Futures Law (Draft) (1) clearly authorizes futures companies to engage in market making transaction business and other derivatives transaction business; and (2) lifts the restriction that the futures companies cannot directly or indirectly (in any form) engage in proprietary futures business.

Under current regulations, pursuant to the *Guidelines for Business Pilot Programs by the Risk Management Companies of Futures Companies*, futures companies can establish risk management subsidiaries and engage in risk management services-based pilot business work, including OTC derivatives business, market making business and other risk management services-related businesses. The Futures Law (Draft) would expand the business scope of futures companies to market-making transactions and other derivatives businesses and revoke the prohibition on proprietary business, leaving more room for business development and innovation. This would improve investment research and asset allocation capabilities of futures companies. The Futures Law (Draft) does not provide guidelines that refer to qualifications futures companies need to engage in market making business; however, considering risk management in the early stages of such business, we expect CSRC to amend the Futures Companies Measures to manage market-making risks of futures companies, such as setting a high entry bar for market making and requiring an increased level of risk supervision, information disclosure, account separation and other measures.

#### IV Conditional recognition of single agreement and close-out netting

Close-out netting is not a legal concept expressly recognized under PRC law, which leads to uncertainty in terms of its actual enforceability. This is despite the fact that regulatory authorities have given support on multiple occasions to the single agreement and close-out netting system introduced by master derivatives agreements prevalent in the PRC market, including the *Master Agreement for Derivatives Transactions in the China Securities and Futures Market* (“**SAC Master Agreement**”) and *NAFMII Master Agreement (2009 Version)* (“**NAFMII Master Agreement**”), which borrow from the *ISDA Master Agreement*. For example, in the event of bankruptcy under the *Enterprise Bankruptcy Law of the People’s Republic of China* (“**Bankruptcy Law**”), the bankruptcy administrator is entitled to rescind or continue the performance of contracts that were concluded prior to the acceptance of the bankruptcy application but the performance of which has not been completed by both the debtor and the counterparty. This “cherry-picking right” puts into question the enforceability of close-out netting under the Chinese legal framework, and the time that elapses pending the exercise of “cherry-picking right” further adds to the market risk of derivative transactions. Moreover, the bankruptcy administrator can rightfully request the courts to rescind settlements with individual creditors within six months prior to acceptance of the bankruptcy application, which may also affect the enforceability of close-out netting.

Article 35 of the Futures Law (Draft) recognizes that a master agreement, together with all the supplementary agreements pursuant to the master agreement and agreements made by both parties to each specific transaction thereunder constitute a complete, single and legally binding agreement between the parties. Thus, a bankruptcy administrator would be unable to “cherry pick” and continue a favorable contract but terminate an unfavorable one. Article 37 further confirms and acknowledges that, upon the termination of the single agreement, the profits and losses of all the transactions under a single agreement would be settled on a net basis and close-out netting would not be invalidated or

revoked due to the commencement of any bankruptcy proceeding with respect to any party to the transaction in accordance with the law. The aforesaid provisions would validate that, on a legal level, China's derivative transaction close-out netting system is unaffected by the trading party's bankruptcy. If the Futures Law (Draft) is adopted in its current form, the single agreement and close-out netting clauses will prevail over the Bankruptcy Law, pursuant to the PRC legislative principle that special laws are superior to general laws in the hierarchy of legal authorities.

However, the single agreement and close-out netting system under the Futures Law (Draft) would be conditional upon the filing of relevant master derivatives agreements and other standard contracts with the State Council-authorized departments in accordance with Article 34 of the Futures Law (Draft). Some notable points regarding Article 34 include:

1. Filing obligor: Obligors imposed with filing obligations consist of industry associations and entities organizing other derivatives transactions activities, but not entities carrying out derivatives transactions. Therefore, NAFMII, SAC and other industry associations would need to fulfill filing duties but entities that carry out derivatives transactions (e.g., banks), should not be responsible for filing. However, it is unclear whether international associations such as ISDA would be responsible for filing; if yes, their filing procedures are currently undefined. In addition, in practice, some financial institutions may self-formulate a master derivatives agreement (mini-master agreements, e.g., a master agreement on foreign exchange derivative transactions), and as financial institutions are not "industry associations or organizing entities", they are not responsible for filing duties, raising uncertainty for such unfilled master agreements as to the applicability of single agreement and close-out netting. This awaits further clarification from regulatory authorities.
2. Filing content: It is explicitly provided that filing is required for "master agreements and other standard contracts in other derivatives transactions". Thus, contracts that include specific commercial terms would not need to be filed.
3. Filing regulatory body: The Futures Law (Draft) only stipulates, in principle, the filing regulatory body to be a State Council-authorized department, though the definition of State Council-authorized department remains unclear. Considering China's current derivatives regulatory environment, possible filing channels are as follows: interest/foreign exchange rate underlying derivatives transaction agreements need to be filed with PBoC/SAFE, while commodities and securities underlying derivatives transaction agreements need to be filed with CSRC. This raises the question and requires further clarification as to whether a derivatives transaction agreement that applies to different types of underlyings is required to be filed with each different regulatory authority, which would inevitably add to the burden of filing obligors and be disadvantageous for the conduct of derivatives transactions in practice. We suggest the regulatory authorities to consider authorizing one State Council department to oversee the filing of derivative agreements, lessening the filing burden of filing obligors.
4. Effect of filing: Articles 35 and 37 of the Futures Law (Draft) stipulate that filed master agreements, supplementary agreements to the master agreement and agreements made by both parties to each specific transaction thereunder constitute a single agreement, and derivatives transactions documented by a single agreement can be granted close-out netting protection. Nevertheless, the

Futures Law (Draft) does not provide guidelines with regard to the enforceability of single agreement and close-out netting in the event that the filing obligor fails to fulfill its filing obligations. This is unclear and will require further clarification and practical testing to determine whether a court would view the filing obligation in the Futures Law (Draft) as a mandatory requirement and a condition for the enforceability of single agreement and close-out netting, and would subsequently deny enforceability on the basis that the agreement had not been filed.

Separately, it is noteworthy that PBoC issued a consultation draft of the revised *Law of the People's Republic of China on Commercial Banks* ("**Commercial Bank Law (Draft)**") on 16 October 2020. The Commercial Bank Law (Draft) provides a comprehensive legal framework for the banking industry, and has specially addressed the pending issues in relation to the dissolution and bankruptcy of PRC commercial banks by drawing references from, and with a view toward conforming to, international standards. Articles 95 and 101 of the Commercial Bank Law (Draft) imply legislative support for the enforceability of close-out netting arrangements involving a commercial bank and expressly recognize and supplement the legislative support for settlement finality of outstanding payments and settlement transactions of a commercial bank upon any declaration of bankruptcy against it. We suggest legislators and regulatory authorities to coordinate the provisions under the Futures Law (Draft) and the Commercial Bank Law (Draft) to avoid inconsistency, especially to clarify whether a commercial bank could still enjoy the protection of close-out netting for the transactions documented by an unfiled master derivatives agreement by operation of the Commercial Bank Law (Draft).

## V Performance assurance system

Article 36 of the Futures Law (Draft) stipulates that other derivatives transaction participants can provide performance assurance in respect of other derivatives transactions, in accordance with the law by means of pledge contracts or other contracts with security features. We understand the original intent of Article 36 is to provide a legal basis for the performance assurance documents supplementary to the master derivatives agreements. The prevalent performance assurance documents in the current market include: the 1994 Credit Support Annex (Security Interest – New York Law) issued by ISDA and the *NAFMII Pledge Performance Assurance Document (2009 Version)* issued by NAFMII (collectively "**Performance Assurance Document (Security Interest)**"); the 1995 Credit Support Annex (Transfer – English Law) issued by ISDA and *NAFMII Title Transfer Performance Assurance Document (2009 Version)* issued by NAFMII (collectively "**Performance Assurance Document (Transfer)**").

The Performance Assurance Document (Security Interest) is a classic contract with security features, where the performance assurance provider submits margin, negotiable securities, and others to create security interest for transactions under the master derivatives agreement and, being a subordinate contract, it does not belong to the construct of a single agreement. Conversely, the Performance Assurance Document (Transfer) is a transaction under the master derivatives agreement, belonging to the construct of a single agreement, and enjoys the close-out netting provided by the master derivatives agreement in the event of default. The Performance Assurance Document (Transfer) does not create a security interest, but instead relies on the transfer of title to collateral in the form of cash or securities to adjust the transferor's risk exposure to the transferee and gives rise to the effect

that either party has no risk exposure to the other via netting.

The Performance Assurance Document (Transfer) does not fall under the “transfer by way of security” provided in Article 68 of the *Interpretation of the Supreme People’s Court of the Application of the Relevant Security System of the Civil Code of the People’s Republic of China*, with the main difference being under “transfer by way of security”, collaterals are only transferred in form, the creditor/beneficiary cannot dispose of the collateral at will with limited exceptions, nor can the creditor/beneficiary request complete rights to the collateral; under the Performance Assurance Document (Transfer), the assignee enjoys unrestricted/complete ownership to performance assurance assets, which the assignee can dispose of at will. Specifically, the NAFMII Master Agreement, to eschew the Performance Assurance Document (Transfer) being viewed as creating a security interest, avoids potentially misleading wording such as “security document”, and defines performance assurance documents as “legal documents with specific arrangements in respect of performance assurance of transactions under the supplementary agreements”, thus pertaining to documents that are “specifically arranged” (i.e. outright transfer of ownership) to realize assurance capabilities.

Based on the above, “other contracts with security features” as stated in Article 36 of the Futures Law (Draft), differs from the nature of, and may not cover the market prevailed, Performance Assurance Document (Transfer). Moreover, uncertainty exists around the recharacterization of outright transfers contemplated under the Performance Assurance Document (Transfer) into transfer by way of security. We suggest the Futures Law (Draft) to expressly acknowledge the performance assurance function of the Performance Assurance Document (Transfer) and clarify its independence from transfers by way of security, in order to align with international practices and provide a more solid legal basis.

## VI Extraterritorial application

Identical to the Securities Law, Article 2 of the Futures Law (Draft) establishes extraterritorial application, regulating foreign futures and other derivatives transactions that disrupt the domestic market order or damage the rightful interests of domestic traders. Based on our interpretation of Article 2, foreign derivatives linked with domestic underlyings, and through the transaction of such derivatives in the foreign market that subsequently affects the price or transaction volume of domestic underlyings amongst other market disrupting acts, will be within the applicable scope of the Futures Law (Draft).

To date, the extraterritorial application of the Securities Law has yet to be triggered in practice, thus there exist no precedents for reference with regards to future application of the Futures Law (Draft) internationally.

## VII Long-arm jurisdiction and cross border regulatory cooperation

In recent years, China’s futures market has fervently engaged in two-way opening through important “bringing in” measures such as designating specified futures products open for trading by foreign investors, and allowing the establishment of wholly foreign-owned futures companies<sup>4</sup>. Additional

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<sup>4</sup> On September 2020, by approval of CSRC, Shanghai Futures Exchange (SHFE) authorized the closing settlement price of pulp futures to NOREXCO, for launching based on SHFE’s pulp futures closing settlement price as the standard in



“going out” measures will be beneficial, such as further cooperation on settlement price between domestic futures exchanges, foreign exchanges, and foreign financial institutions, and greater support for qualified domestic futures companies to set up, acquire, and invest in futures business institutions. Conforming to the two-way opening direction, legislation needs be refined to improve the corresponding arrangements for cross-border supervision and cooperation, and futures markets need be further modernized and globalized. In comparison to the currently effective Futures Trading Regulation, Chapter 12 of the Futures Law (Draft) would provide for cross-border regulatory and coordination mechanisms, confirming the long-arm jurisdictional system. Foreign futures exchanges, futures business institutions providing domestic services, establishing branches, and engaging in marketing, promotion, and solicitation, and both domestic and foreign traders engaging in cross-border transactions should abide by the relevant guidelines. The Futures Law (Draft) also clarifies cross-border regulatory cooperation mechanisms between the State Council futures regulatory authorities and foreign regulatory authorities, prohibiting foreign regulatory authorities from directly engaging in investigation and evidence collection in the PRC.

### **VIII Cross-border data transfers**

Since the introduction of the *Cybersecurity Law of the People’s Republic of China*, regulatory authorities have placed greater emphasis on data sovereignty and regulations over cross-border data transfers. Parallel to Article 177 of the Securities Law, Article 136 of the Futures Law (Draft) prohibits units or individuals from providing offshore documents and information relevant to futures business without the consent of the futures regulatory authority and relevant departments of the State Council. The Futures Law (Draft) does not further explain the definition of “documents and information relevant to futures business”, which we interpret has been left vague purposefully to allow greater discretion for regulatory authorities regarding the scope of documents and information. Cross-border data transfers should also consider relevant important data and personal information rules set by the national cyberspace authorities. For foreign-invested futures companies, it would be advisable to pay attention to these restrictions when conducting cross-border data transfers with their overseas parent companies, so as to avoid triggering compliance issues.

### **IX Other notable items**

Other notable items not discussed above include:

1. Article 31 of the Futures Law (Draft) specifies that other derivatives transactions can adopt agreement transfer as well as other State Council-approved transaction methods. The definition of “agreement transfer” is unclear, some reckon agreement transfer should be interpreted as two distinct transaction methods, agreement and transfer, such that the agreement refers to both parties who, through negotiation, sign an agreement to carry out the derivatives transaction, and that transfer refers to the novation by the central counterparty when other derivatives transactions are centrally cleared. We suggest legislative and regulatory authorities to provide further clarification on the “agreement transfer”

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cash settlement futures contracts. This marks the first authorization to foreign exchanges of directly utilizing domestic futures products for closing settlement price and is also a first in distributing Chinese futures contracts standards to a foreign exchange.

transaction method.

2. Building upon experiences from the Securities Law in securities registration-based IPOs, the Futures Law (Draft) would simplify the procedures for launching futures products. Article 13 of the current Futures Trading Regulation directs that “[t]he futures supervision and administration department of the State Council shall seek the opinion of the relevant department of the State Council before approving the launch of a new futures product in a futures exchange” and, in practice, futures products launch adopts the parallel examination and approval method, futures exchanges will file an application for proposed futures product launches with CSRC, which would then seek parallel opinions from industry associations and relevant ministries before submission to the State Council. Upon receiving approval from the State Council, CSRC will then give a green light to the futures exchanges. This method requires a strenuous approval process as well as numerous examiners, and the futures exchange does not have a clear timeline in respect of each futures product launch. During this year’s Two Sessions, some members proposed to simplify the launch process for futures products<sup>5</sup>. Heeding to market and development demands, the Futures Law (Draft) has simplified the futures products launch process from the parallel examination and approval process to an exchange application and CSRC registration process.
3. The Futures Law (Draft) adds no new descriptions to market manipulation behaviors on the basis of the Futures Trading Regulation and the *Provisions of the China Securities Regulatory Commission on “Other Acts Manipulating the Futures Trading Price” Set out in Subparagraph 5 of Article 70 of the Administrative Regulations on Futures Trading*. However, the Futures Law (Draft) would substantially increase the severity of punishment in relation to market manipulation behaviors. Pursuant to Article 142 of the Futures Law (Draft), market manipulators would be ordered to make corrections, have their illegal gains confiscated, and be fined for no less than once but no more than ten times the resulting illegal gains; for those with no illegal gains, or illegal gains under RMB 1 million, violators would be fined no less than RMB 1 million but no more than RMB 10 million. Current penalties in respect of market manipulation behaviors, in accordance with Article 70 of the Futures Trading Regulation, are less than once but not more than five times the total illegal gains; for violators with no illegal gains, or illegal gains under RMB 200,000, they will be fined no less than RMB 200,000 but no more than RMB 1 million. The Futures Law (Draft) would also increase the severity of punishments for other violative behaviors.

## Outlook

The extensive development and higher quality opening-up of the futures market has called for an increasingly comprehensive legal framework. In the context of “bringing in”, the Futures Law (Draft) integrates valuable legal precedence/practice, drawing lessons from foreign market designs to further strengthening the construction of China’s futures and other derivatives markets; on the other hand, “going out” has provided China’s futures market with greater room for internationalization, strengthening China’s competitiveness in international pricing power. Overall, the Futures Law (Draft) would add

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<sup>5</sup> See news:“全国政协委员解冬：探索以市场需求为导向的期货品种上市机制”，<https://baijiahao.baidu.com/s?id=1693382269407218156&wfr=spider&for=pc>.

comprehensiveness, openness, and innovation to the top-level design of China's legal infrastructure, providing a solid rule of law guarantee and developmental momentum. However, questions and ambiguities within the Futures Law (Draft) still await further clarification. For example, the law covers more than simply futures products, hence perhaps it is necessary to change the name to the *Futures and Derivatives Law*; will repo transactions be included in the regulated scope of the Futures Law (Draft) and, if not, how will the difference in domestic and international repo markets be bridged in the future; scope and effect of the master derivatives agreements filing; how will the extraterritorial application of the Futures Law (Draft) be realized in practice; further clarification on the transactional methods of other derivatives; and will the future OTC derivatives regulatory system be consolidated or remain separate. With regards to these concerns and opinions, we will actively provide feedback to the regulatory authorities in hope of seeing further refinements in legislation relating to the futures industry and help ease the concerns of market participants. We will continue to follow the latest developments of the Futures Law (Draft) and provide timely updates.

## ***Important Announcement***

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