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1999 APR 30 P 1:52

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COMMENT

(BY FAX AND POST)

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RECORDS
Jean A Webb
Secretary of the Commission
Commodity Futures and Trading Commission
1155 21st Street NW
Washington DC 20581
USA

16 April 1999

ACCESS TO AUTOMATED BOARDS OF TRADE

I am writing in response to the CFTC's invitation for comments on the proposed rule for access in the US to foreign automated boards of trade. As I'm sure you are aware, this is an important issue for several UK exchanges and we support their wish to introduce screens into the US.

The Treasury welcomes the publication of this draft rule to allow foreign exchanges access into the US market. Clearly you will need to reflect upon the replies to the consultation. But these matters have been under consideration for some time already and so we would urge you to publish a final rule as soon as possible after the expiry of the 30 day consultation period. If publication of a final rule cannot be made within a month or two, we would urge you to consider either some form of no action regime (on an interim basis only) or possibly the separation of the direct execution system and automated order routing system issues. This would allow the relatively uncontentious treatment of DESs to be settled quickly, whilst AGRSS could be considered at further length.

As regards the draft rule itself, the FSA have provided detailed comments in their letter of 16 April and we support these. Our comments are focussed on the comparability of your proposed procedure and our Recognised Overseas Investment Exchange (ROIE) regime.

As you know, the ROIE regime in the United Kingdom allows non-UK exchanges access into the UK market, and there are currently five US ROIEs here. We agree that the draft rule is broadly similar to the ROIE regime. However there are a number of significant differences on which we wish to comment.

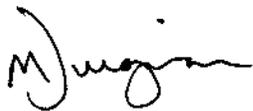
Under exemptions for overseas persons, it is possible for non-UK exchanges to operate in the UK without being covered by the ROIE regime at all. Foreign exchanges wishing to set up screens in the UK for use by authorised persons only (ie not for client business) may do so without having to seek ROIE status. We consider that professional firms should not require the investor protection appropriate to private individuals and therefore that it would not be warranted to make foreign exchanges only doing business with such firms go through the recognition procedure.

The foundations on which the ROIE regime is based is that non-UK exchanges should, by a combination of exchange rules and domestic regulation, afford investor protection equivalent to that afforded by UK exchanges and allow co-operation and exchange of information between the exchange, the overseas regulator and the UK regulator. The exchange obviously has to satisfy the Treasury on this score. But once an exchange is recognised, we believe the overseas regulator has the major role in ensuring that the exchange is properly regulated.

We therefore regard the degree of information which it is proposed foreign exchanges should be required to provide to the CFTC, and the regularity with which they should provide it, is beyond what we would consider appropriate. In the UK, ROIEs are required to provide to the Treasury two sets of information, one on an annual basis in the form of their annual summary, and the other on information arising from events "on occurrence". I attach the guidance sent to ROIEs which give examples of the types of information required.

As we said in our response to the concept release, we also have concerns that a UK exchange would be required to register as a US exchange because of a mechanistic approach, for example if trading volumes exceeded a certain level. This would seem to go against the "totality of the application" approach in the concept release, of which we approved.

On an administrative level, foreign exchanges applying for ROIE status and those which are subsequently granted it are subject to fees charged by the Treasury to cover the costs of processing applications and monitoring the recognised exchanges. The draft rule makes no reference to such fees. I would be interested to know if you intend to charge fees for approval and/or monitoring and if so, what level these fees might be. You should also be aware that the Treasury endeavours to process all applications within three months, and therefore advises applicants that they should apply no later than the three months before recognition is desired to take effect (although there can be no guarantee of a decision being made during this time).



MIKE DUIGNAN
Financial Stability and Markets

**REVISED ARRANGEMENTS FOR MONITORING COMPLIANCE WITH
RECOGNITION CRITERIA FOR OVERSEAS EXCHANGES**Information Required in Annual Summary, in respect of the main Recognition Criteria

- i) *The exchange is subject to supervision which, together with its rules and practices, offer investor protection equivalent to that provided by the Financial Services Act to UK investors.*

In order to assess whether this criteria continues to be met, the Treasury will require an analysis of the effect of any significant changes to the laws or regulations governing the exchange, or to the rules, practice or guidance of or issued by the exchanges:

- a. which are designed to prevent insider dealing, or market manipulation (ie. making of false or misleading statements or engaging in conduct creating a false or misleading impression of the price or value of any investments);
- b. which bring about a substantial change in the nature of investment business done in the UK;
- c. which concern the disclosure of information by companies about their business or prospects;
- d. which concern the reporting of transactions conducted on the exchange;
- e. which are designed to protect the interests of clients of members (eg. by restricting the use of client funds; imposing a duty of best practice or best advice; constraining own account dealing when acting for a client etc);
- f. which affect eligibility for membership of the exchange;
- g. which affect the security and reliability of clearing and settlement;
- h. which affect the ability of the exchange to monitor compliance with its rules and to investigate breaches and complaints.

In addition, the Treasury will require any information relating to the financial position of the recognised body or to its future prospects which it is required under the law of the head office country to submit to the authorities in that country or territory (and an English translation if the information is not in English). This requirement will not apply to a recognised body which is an overseas company within the meaning of Section 744 of the Companies Act 1985.

- ii) *The ROIE must be able and willing to cooperate, by the sharing of information or otherwise, with the regulatory authorities in the UK.*

In order to assess whether this criteria continues to be met, the Treasury would require an analysis of any significant changes which:

- a. affect the ability of the exchange to seek information (whether compulsorily or voluntarily) from its members or directly, concerning for example the price and volume of transactions, the identity of parties to transactions; and the movement of funds associated with transactions;
- b. affect the ability of the exchange to pass such information, on request, to UK regulatory authorities.

- iii) *There must be adequate arrangements for cooperation between those responsible for supervising the ROIE in its home country and the UK authorities.*

This is not primarily a matter for the exchange, but the Treasury would wish to have an analysis of any significant changes in the exchange's rules, practices or guidance which would affect cooperation between regulatory authorities.

- iv) *The rules and regulations of the ROIE do not and are not intended, or likely, to have any significant anti-competitive effect (other than the minimum such effect which may be necessary to protect investors).*

This is a matter which the Treasury and the Director-General of Fair Trading is required to keep under review. In order to assist him the Treasury would require an analysis of:

- a. significant rule changes relating to the structure of the market and membership requirements; and analysis of membership applications and a summary of reasons for refusals of requests for admission to each category, along with current levels of membership in each category;
- b. summary of trading halts - eg. whether frequency has risen or fallen, and an assessment of the causes and rationale;
- c. similar information about any other matters affecting the flow of trading such as the introduction of, or changes to, speculative position limits;
- d. any new agreements made with other exchanges or changes to existing ones.

On Occurrence

- i) Any change in the kind of the business which the recognised body is, or anticipates, carrying on in the United Kingdom;
- ii) Any change as to the supervisory bodies to which the recognised body is subject under the law of the head office country; the status of the recognised body under that law; or the legal provisions under which the supervision is conducted;
- iii) Any change in the recognised body's memorandum or articles of association or constitution;
- iv) Any amendment, revocation or addition to the recognised body's rules¹ or to any guidance² issued by it intended to have continuing effect;
- v) Any change as to the persons responsible for monitoring compliance with the recognised body's rules or as to the supervisory arrangements for monitoring compliance with those rules insofar as those rules apply to investment business being carried out in the United Kingdom;

¹ Definitions in the Financial Services Act 1986 relevant to potential applicants for recognition as an overseas investment exchange or overseas clearing house

Rules of a recognised overseas investment exchange (Sections 36(2) and 40(4)) are the rules made or conditions imposed by the exchange with respect to matters corresponding to those specified in Schedule 4 to the Act and to admission of persons to or their exclusion from use of the exchange's facilities or otherwise relating to its constitution.

Rules of a recognised clearing house (Section 38(2)) are the rules made, or conditions imposed by the clearing house with respect to the provision by it or its members of clearing services under clearing arrangements ie. arrangements with any recognised investment exchange for the provision of clearing services in respect of transactions effected on that exchange.

² Guidance of a recognised investment exchange (Section 36(3)) is any guidance issued or any recommendation made by the exchange to all or any class of its members or users or persons seeking to become members of the exchange or to use its facilities; which, if it were a rule, would fall within the definition above of rules of an overseas investment exchange.

Guidance of a recognised clearing house (Section 38(3)) is any guidance issued, or any recommendation made, by the clearing house to all or any class of its members or persons using or seeking to use its services, which, if it were a rule, would fall within the definition above of rules of a recognised clearing house.

- vi) Any event which means that the recognised body is no longer able to cooperate, by the sharing of information or otherwise, with the authorities, bodies and persons responsible in the United Kingdom for the supervision and regulation of investment business or other financial services;
- vii) In the case of an overseas investment exchange only:-
 - a. the making, termination or variation of any clearing arrangements;
 - b. any change in the category of investments dealt with on the exchange; and
 - c. the discontinuation or suspension of dealings in any category of investments; and
- viii) In the case of an overseas clearing house only, any change in the nature or extent of the clearing, settlement and guarantee services to be provided by the clearing house (including any change in the persons to whom it provides clearing services).

The above information must be given in writing to the Treasury not later than 7 days after the date on which it is required to be submitted to the relevant overseas authorities (in the case of the material to be provided annually) or not later than 7 days after the occurrence (in the case of other material specified); with the exception of notifications falling within paragraph (vi) above which would have to be made forthwith eg. by telex or equivalent means.

The recognised body must notify the Treasury in writing in advance of any change of address of the recognised body's head office or of the address in the United Kingdom given by the recognised body for the services of notices or other documents required or authorised to be served on it under the Act.

By virtue of Section 162 of the Companies Act 1989 (as amended by the Financial Markets and Insolvency Regulations 1991) a recognised investment exchange or recognised clearing house will be under a duty to report to the Treasury on the completion of default proceedings in relation to market contracts, where the Treasury determines that such a report is required for the purpose of instructing insolvency proceedings in the United Kingdom.

The Treasury has power - under Section 104(2) of the Act - to require a recognised body to furnish it also with other information which may reasonably be required for the exercise of its functions under the Act.

Periodical Fees

Overseas investment exchanges and overseas clearing houses will be required to pay annual fees to the Treasury. Fees will be payable at the commencement of each 12 month period starting from the date on which the recognition order takes effect. The Treasury will advise prospective applicants of the current level of the annual fees.