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OFFICE OF
GENERAL COUNSEL

August 29, 1997

Philip McBride Johnson, Esquire
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1440 New York Avenue, N.W.
Washington, D.C. 20005-2111

Re: Singapore International Monetary Exchange Morgan Stanley Capital International Taiwan Stock Index Futures Contract

Dear Mr. Johnson:

This is in response to your letters dated December 12, 1996 through January 24, 1997 on behalf of the Singapore International Monetary Exchange, Limited ("Simex") requesting a no-action letter allowing the Simex futures contract (and options thereon)[1] based on the Morgan Stanley Capital International ("MSCI") Taiwan Stock Index ("Taiwan Index" or "Index") to be offered or sold in the United States.[2]

We understand the facts to be as follows. The Simex is located in Singapore and has been in operation since September 1984. The Simex is regulated by the Monetary Authority of Singapore ("MAS") as a futures exchange under the Futures Trading Act of 1986. The Simex is not designated as a contract market under the Commodity Exchange Act ("CEA" or "Act") and does not intend to seek such designation.[3]

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[1]This no-action position is directed to the Simex futures contract based on the MSCI Taiwan Index. No additional relief or approval is necessary for the offer and sale within the United States of the option on the MSCI Taiwan Index futures contract. See 61 Fed. Reg. 10891 (Mar. 18, 1996).

[2]As you are aware, the Office of the General Counsel issued a no-action letter to the Simex with respect to the futures contract based on the Nikkei Stock Average on December 5, 1986, to the futures contract based on the MSCI Hong Kong Index on June 1, 1994 and to the futures contract based on the Nikkei Stock Index 300 on December 13, 1995.

[3]On August 28, 1984, the Commission approved certain rule changes of the Chicago Mercantile Exchange ("CME") to facilitate the Mutual Offset System ("MOS") between the CME and Simex whereby positions established on one exchange can be transferred to or

The Simex has a licensing agreement for the Taiwan Index from Morgan Stanley & Co., Inc. ("Morgan Stanley"), of which MSCI is a department. The Taiwan Index is constructed and maintained for MSCI by Capital International Perspective, S.A. ("CIPSA") which has no corporate affiliation with Morgan Stanley.[4] CIPSA uses certain specialized criteria and standards to calculate and adjust the Taiwan Index.[5] The Taiwan Index is a market capitalization weighted index and uses the Laspeyres calculation method. As of November 29, 1996, the Taiwan Index was made up of the stocks of 77 companies located in Taiwan, representing nearly 61% of total market capitalization of the Taiwan market. As of January 6, 1997, the total capitalization of the stocks included in the Taiwan Index equaled over U.S. $156 billion. As of the same date, the highest weighted stock in the Taiwan Index, Cathay Life Insurance, accounted for 12.13 percent of the market capitalization of the Taiwan Index. The five highest weighted stocks in the Taiwan Index, as of January 6, 1997, constituted 35.52 percent of the market capitalization of the Taiwan Index with the ten highest weighted stocks totaling 53.35 percent of the Index.

The Taiwan Index level is based on the number of outstanding shares and last sale price in Taiwanese dollars of each component stock The Index is calculated and disseminated in real-time by CIPSA via major news vendors like Reuters, Bloomberg and Telerate.

The Simex MSCI Taiwan Index futures contract began trading on January 9, 1997. The futures contract on the Taiwan Index is denominated in United States dollars and is cash settled. The contract value is determined by multiplying the Taiwan Index by U.S. $100. The futures contract has a daily price limit equal to 7 percent, in either direction, from the previous day's settlement price and an expanded limit set at 10 percent above or below the previous day's settlement price. The final settlement price is based on the closing prices of the component stocks on the last day of trading.

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liquidated on the other exchange. This no-action position is not applicable to the trading of the MSCI Taiwan Index futures contract on the MOS.

[4]CIPSA has a policy prohibiting communication of potential changes in index components to Morgan Stanley employees and no Morgan Stanley personnel receive such data before dissemination to the general public. Moreover, Morgan Stanley maintains a separation between its proprietary trading and brokerage operation from the maintenance of the Taiwan Index. Finally, CIPSA does no securities or futures or options trading on any MSCI Index, including the MSCI Taiwan Index.

[5]The methodology used to produce and adjust the Taiwan Index is the same as for Simex's MSCI Hong Kong Index futures contract for which a no-action request was granted by the Office of the General Counsel on June 1, 1994. See infra, note 1.

The offer and sale of futures contracts in the United States traded on or subject to the rules of a foreign exchange is subject to the Commission's exclusive jurisdiction.[6] Section 2(a)(1)(A), 7 U.S.C. § 2 (1988); 120 Cong. Rec. 34497 (1974) (statement of Senator Talmadge) (the terms "any other board of trade, exchange, or market" in Section 2(a)(1)(A)(i) make clear the Commission's exclusive jurisdiction includes futures contracts executed on a foreign board of trade, exchange or market.)[7] Section 2(a)(1)(B)(v) of the Act, 7 U.S.C. § 2a(v), generally prohibits any person from offering or selling a futures contract based on a securities index in the United States except as permitted under Section 2(a)(1)(B)(ii), 7 U.S.C. § 2a(ii) (1994). In turn, Section 2(a)(1)(B)(ii) sets forth three criteria to govern Commission designation of futures contracts in a group or index of securities:

(1) the contract must provide for cash settlement;

(2) the proposed contract must not be readily susceptible to manipulation nor to being used to manipulate any underlying security; and

(3) the index is predominately composed of the securities of unaffiliated issuers and reflects the market for all publicly traded securities or a substantial segment thereof.

See H.R. Rep. No. 565, Part 1, 97th Cong., 2d Sess. 39 (1982).

Section 2(a)(1)(B)(ii) provides that the Commission shall not designate a board of trade as a contract market unless the Commission finds that the board of trade meets the enumerated criteria. As noted above, we understand that the Simex does not seek designation as a contract market. However, Congress understood that a foreign exchange might lawfully offer futures contracts on stock indices absent designation. Thus, the House Committee on Agriculture suggested that a foreign board of trade could apply for "certification" that its stock index contract met all applicable Commission requirements. H.R. Rep. No. 565, Part 1, 97th Cong., 2d Sess. 85 (1982). The Commission has not

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[6]Section 12(e) of the Commodity Exchange Act prohibits the application of any federal or state statute to a transaction that is conducted on or subject to the rules of a foreign exchange "except as otherwise specified by the Commission by rule or regulation." 7 U.S.C. § 16(e) (1994). The Commission has authorized the application of state law to "any person required to be registered under . . . [Part 30] who solicits foreign futures and foreign options customers and who shall fail or refuse to obtain such registration, unless such person is exempt from such registration . . . ." 17 C.F.R. § 30.11 (1997).

[7]In this regard, pursuant to the authority in, among other provisions, Section 4(b) of the Act, the Commission has promulgated rules to regulate the offer and sale in the United States of foreign futures and options contracts. See 17 C.F.R. Part 30 (1997).

established criteria for certification of foreign futures contracts. However, the House Committee on Agriculture explained that a foreign exchange seeking certification for a futures contract based upon an index of American securities must demonstrate that the proposed futures contract meets the requirements set forth in Section 2(a)(1)(B)(ii). Id.

We understand that the securities in the Taiwan Index are issued by companies located in Taiwan. The House Committee suggests that the Commission may use such criteria as it deems appropriate in evaluating a foreign stock index contract based on "foreign securities." Id. The requirements of Section 2(a)(1)(B)(ii) of the Act were designed to permit innovative financial instruments "while at the same time [assuring] that futures trading is limited to broad-based . . . indices that are not conducive to manipulation or disruption of the market for the underlying securities." S. Rep. No. 390, 97th Cong., 2d Sess. 6 (1982). See also H.R. Rep. No. 565, Part 1, 97th Cong., 2d Sess. at 39. As a result, we would recommend that the Commission use the criteria set forth in Section 2(a)(1)(B)(ii) in establishing any certification procedures for the MSCI Taiwan Index futures contract. Accordingly, the staff has examined the Simex MSCI Taiwan Index futures contract in light of these criteria.[8]

Based on the information set forth above, this Office will not recommend any enforcement action to the Commission based on Sections 2(a)(1)(B)(v), 4(a) or 12(e) of the Commodity Exchange Act, as amended, if the MSCI Taiwan Index futures contract traded on the Simex is offered and sold in the United States. Because this position is based upon facts and representations contained in the above-noted letters and attachments and numerous communications from the MAS regarding information sharing, it should be noted that any different, omitted or changed facts or conditions might require a different conclusion.[9] This position also is contingent on the Singapore International Monetary Ex-

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[8]We also have sought the opinion of the staff of the Securities and Exchange Commission which informs us that they would have no objection to the offer and sale of this futures contract in the United States.

[9]The Simex has represented that it will cooperate with the Commission in inquiries, investigations and enforcement proceedings relating to the offer and sale in the United States of the Simex futures contract on the MSCI Taiwan Index. Simex also has confirmed that its agreement to share information, in conjunction with the Commission's grant of regulation 30.10 relief to Simex, is equally applicable to data pertaining to the MSCI Taiwan Index futures contracts. See December 12, 1996 letter to Daniel R. Waldman, General Counsel, Commodity Futures Trading Commission, from Philip McBride Johnson, Skadden, Arps, Slate, Meagher & Flom LLP. The MAS has confirmed that there are no constraints under the Singapore Futures Trading Act for Simex to provide information in their possession to overseas regulators. However, MAS authorization is required but the MAS represents that it does not envisage that there would be any reason for MAS not to give

change's continued compliance with all regulatory requirements imposed by the Monetary Authority of Singapore and the applicable statutes of Singapore.

As you are aware, the Commission has adopted rules governing the offer and sale of foreign futures and foreign option contracts in the United States. See 17 C.F.R. Part 30.

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such authorization pursuant to a legitimate request. See letter from Koh Beng Seng, MAS, to Paul Leder, SEC, dated July 4, 1997.

The MAS has confirmed that it will continue to cooperate with the Commission with respect to the Simex MSCI Taiwan Index futures contract. See January 27, 1997 letter from Koh Beng Seng, Deputy Managing Director, Banking & Financial Institutions Group, MAS, to Andrea Corcoran, Director, Division of Trading and Markets, Commodity Futures Trading Commission. The MAS has signed a Memorandum of Understanding ("MOU") with the Securities and Exchange Commission of Taiwan and has represented that it will endeavor to cooperate with the CFTC on a best efforts basis to share information received from the Taiwan Securities and Exchange Commission with the Commodity Futures Trading Commission to the extent which the MOU between MAS and the Taiwan Securities and Exchange Commission permits. Id. See also, February 19, 1997 letter from Koh Beng Seng, Deputy Managing Director, Banking & Financial Institutions Group, MAS, to Andrea M. Corcoran, Director, Division of Trading and Markets, Commodity Futures Trading Commission. The Commission and the Taiwan Securities and Exchange Commission, through representative agencies, have entered into a MOU for the sharing of information. See Memorandum of Understanding between the American Institute in Taiwan and the Coordination Council for North American Affairs (now Taipei Eonomic Cultural Representative Office) on the Exchange of Information Concerning Commodity Futures and Options Matters dated January 11, 1993.

In evaluating requests for no-action relief with regard to foreign futures contracts based on foreign stock indices, this Office generally examines whether a surveillance sharing arrangement exists between the futures exchange and the securities exchange on which the underlying stocks are traded. While there is no surveillance sharing arrangement between the Simex and the Taiwan Stock Exchange with regard to the MSCI Taiwan Index futures contracts, several counterbalancing factors provide this Office with sufficient assurances that necessary information will be available to detect potential manipulations. See, e.g., July 30, 1997 letter from Howard L. Kramer, Senior Associate Director, Division of Market Regulation, Securities and Exchange Commission, to David R. Merrill, Deputy General Counsel, Office of the General Counsel, Commodity Futures Trading Commission.

The offer and sale in the United States of the Simex MSCI Taiwan Index futures contract is, of course, governed by these regulations.

Sincerely,

Daniel R. Waldman
General Counsel

cc: Howard L. Kramer
Senior Associate Director
Division of Market Regulation
Securities and Exchange Commission