CFTC letter No. 04-02
January 21, 2004
No-Action
Office of General Counsel

Mr. Benjamin Foo
Senior Vice President
Singapore Exchange Derivatives Trading Limited
2 Shenton Way, #19-00,
SGX Centre 1
Singapore 068804

Re: Singapore Exchange Derivatives Trading Limited's Request for No-Action Relief in Connection with the Offer and Sale of its Futures Contract Based on the Standard & Poors CNX Nifty Index in the United States

Dear Mr. Foo:

This is in response to letters, attachments, facsimiles and electronic mail dated from December 13, 2000 to April 3, 2003, requesting that the Office of General Counsel ("Office") of the Commodity Futures Trading Commission ("Commission" or "CFTC") issue to the Singapore Exchange Derivatives Trading Limited ("SGX-DT"), a "no-action" letter concerning the offer and sale in the United States ("U.S.") of SGX-DT's futures contract based on the Standard & Poors CNX Nifty Index ("S&P CNX Nifty" or "Index").[1].

We understand the facts to be as follows. SGX-DT, a wholly-owned subsidiary of Singapore Exchange, Limited ("SGX"), is a futures and options exchange located in Singapore.[2] SGX-DT and its parent company are both regulated by the Monetary Authority of Singapore ("MAS"), an independent governmental authority established under the Monetary Authority of Singapore Act. MAS is charged with, among other things, protecting customers and the integrity of Singapore's securities and futures markets.

The S&P CNX Nifty is designed to be a benchmark index for the Indian stock market. The Index is owned and managed by India Index Services and Products, Ltd. ("IISL"), a joint venture between the National Stock Exchange of India, Limited ("NSE") and Credit Rating Information Services of India, Limited.[3] The Index is a broad-based, capitalization-weighted composite security index composed of 50 of the largest stocks, in terms of market capitalization, and the most liquid stocks, in terms of market impact cost, traded in India on the NSE. Based on data supplied by NSE, the total market capitalization of the S&P CNX Nifty was U.S. $66.3 billion as of March 31, 2003.[4] Also as of that date, the largest single stock by weight represented 12.26%, and the five most heavily weighted stocks represented

45.01%, of the S&P CNX Nifty.[5] The stocks comprising the lowest 25% of the S&P CNX Nifty had a six-month aggregate dollar value of average daily trading volume in excess of U.S. $30 million: approximately U.S. $96.9 million for the 6-month period ending March 2003.[6] The S&P CNX Nifty is calculated in real time and is disseminated by electronic means through major data vendors, such as Bloomberg and Reuters.[7]

SGX-DT's futures contract on the S&P CNX Nifty provides for cash settlement in U.S. dollars ("U.S. $"). Prices are quoted in Index points with each Index point equal to U.S.$20 per contract. The minimum price fluctuation is 0.5 Index point, equal to U.S.$10 per contract. SGX-DT lists for trading four quarterly contract months (March, June, September and December), plus two nearest serial months. The contract is listed for trading from 12:15 p.m. to 6:15 p.m. Singapore time, Monday through Friday. The last trading day is the last Thursday of the contract month. The final settlement price for the contract is the closing spot Index on the last day of trading, rounded to two decimal places. The spot Index level is based on the weighted average prices of the component stocks during the last 30 minutes of trading.[8]

The Commodity Exchange Act ("CEA"),[9] as amended by the Commodity Futures Modernization Act of 2000 ("CFMA"),[10] provides that the offer or sale in the U.S. of futures contracts based on a group or index of securities, including those contracts traded on or subject to the rules of a foreign board of trade, is subject to the Commission's exclusive jurisdiction,[11] with the exception of security futures products,[12] over which the Commission shares jurisdiction with the Securities and Exchange Commission ("SEC").[13] Thus, the Commission's jurisdiction remains exclusive with regard to futures contracts on a group or index of securities that are broad-based pursuant to CEA Section 1a(25).[14]

CEA Section 2(a)(1)(C)(iv) generally prohibits any person from offering or selling a futures contract based on a security index in the United States, except as permitted under CEA Section 2(a)(1)(C)(ii) or CEA Section 2(a)(1)(D).[15] By its terms, CEA Section 2(a)(1)(C)(iv) applies to futures contracts on security indices traded on both domestic and foreign boards of trade. CEA Section 2(a)(1)(C)(ii) sets forth three criteria to govern the trading of futures contracts on a group or index of securities on designated contract markets and registered derivatives transaction execution facilities ("DTEFs"):

(1) the contract must provide for cash settlement;

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

(3) the group or index of securities must not constitute a narrow-based security index.[16]

While Section 2(a)(1)(C)(ii) provides that no board of trade or DTEF may trade a security index futures contract unless it meets the three criteria noted above, it does not explicitly address the standards to be applied to a foreign security index futures contract traded on a foreign board of trade. This Office has applied those same three criteria in evaluating requests by foreign boards of trade to allow the offer and sale within the U.S. of their foreign security index futures contracts when those foreign boards of trade do not seek designation as a contract market or registration as a DTEF to trade those products.[17]

Accordingly, this Office has examined the S&P CNX Nifty and SGX-DT's futures contract based thereon to determine whether the Index and the futures contract meet the requirements enumerated in CEA Section 2(a)(1)(C)(ii). Based on the information noted herein and as set forth in the letters, attachments, facsimiles and electronic mail noted above, we have determined that the S&P CNX Nifty and SGX-DT's futures contract based thereon conform to these requirements.[18]

In determining whether a foreign futures contract based on a foreign security index is not readily susceptible to manipulation or being used to manipulate any underlying security, one preliminary consideration is the requesting exchange's ability to access information regarding the securities underlying the index. SGX-DT has an information-sharing arrangement with NSE, pursuant to which SGX-DT and NSE have agreed to cooperate in areas relating to derivatives trading, market-information sharing (including surveillance data), staff training and technical assistance.[19] For the reasons mentioned in our letter to NSE, NSE should have access to information necessary to detect and deter manipulation with respect to the securities underlying the Index, which should be available to SGX-DT pursuant to its MOU with NSE. In the event that SGX-DT is unable to obtain access to adequate surveillance data in this regard, or is unable to share such data with the CFTC, this Office reserves the right to reconsider the position we have taken herein.[20]

In light of the foregoing, this Office will not recommend any enforcement action to the Commission based on Sections 2(a)(1)(C)(iv), 4(a), or 12(e) of the CEA, as amended, if SGX-DT's S&P CNX Nifty futures contract is offered or sold in the U.S. Because this position is based upon facts and representations contained in the letters, attachments, facsimiles and electronic mail cited above, it should be noted that any different, omitted or changed facts or conditions might require a different conclusion. This position also is contingent on the continued compliance by SGX-DT with all regulatory requirements imposed by MAS, and the applicable laws and regulations of Singapore. In addition, this position may be affected by any rules that the Commission may adopt regarding futures contracts based on non-narrow-based security indices.

The offer and sale in the U.S. of SGX-DT's S&P CNX Nifty futures contract is, of course, subject to Part 30 of the Commission's regulations, which govern the offer and sale of foreign futures and foreign option contracts in the U.S.[21]

Sincerely,

Patrick J. McCarty
General Counsel

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[1]This Office also received a request from the National Stock Exchange of India, Limited ("NSE") for a no-action letter to permit the offer and sale of NSE's futures contract on the same Index in the U.S. We recently issued a no-action letter to NSE, *see* CFTC Letter No. 03-35 (October 17, 2003).

[2]For a description of the formation of SGX and its subsidiaries, *see* CFTC Letter No. 00-77, [1999-2000 Transfer Binder] Comm. Fut. L Rep. (CCH) ¶ 28,182 (June 21, 2000).

[3]IISL has a consulting and licensing agreement with S&P, for co-branding equity indices of IISL, including the S&P CNX Nifty. SGX-DT has entered into a licensing agreement with IISL for listing futures contracts on the S&P CNX Nifty. *See* letter from Jimmy Ang, Executive Vice President, SGX-DT to C. Robert Paul, General Counsel, CFTC, dated December 13, 2000.

[4]*See* electronic mail from R. Sundararaman, Assistant Vice President, NSE, to Patrick J. McCarty, General Counsel, CFTC, dated April 9, 2003 (Annexure 1, Table 1).

[5]*Id.*

[6]*See id.* (Annexure B) and letter from R. Sundararaman, Assistant Vice President, NSE to Julian E. Hammar, Counsel, CFTC, dated May 19, 2003.

[7]*See* electronic mail from Mr. Sundararaman to Mr. McCarty, dated April 9, 2003.

[8]*See* letter from Mr. Ang to Mr. Paul, dated December 13, 2000. Information on contract specifications is available on SGX's website, <http://www.sgx.com>.

[9]7 U.S.C. § 1 *et seq.*

[10]Appendix E of Pub. L. No. 106-554, 114 Stat. 2763 (2000).

[11]*See* CEA Section 2(a)(1)(C)(ii).

[12]Security futures products are defined as a security future or any put, call, straddle, option, or

privilege on any security future. *See* CEA Section 1a(32). A security future is defined as a contract of sale for future delivery of a single security or of a narrow-based security index, including any interest therein or based on the value thereof, with certain exceptions. *See* CEA Section 1a(31).

[13] *See* CEA Section 2(a)(1)(D).

[14] *See* CEA Section 2(a)(1)(C)(ii).

[15] CEA Section 2(a)(1)(D) governs the offer and sale of security futures products.

[16] The first two criteria under CEA Section 2(a)(1)(C)(ii) were unchanged by the CFMA. With regard to the third criterion, an index is a "narrow-based security index" under both the CEA and the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78a *et seq.*, if it has any one of the following four characteristics: (1) it has nine or fewer component securities; (2) any one of its component securities comprises more than 30% of its weighting; (3) the five highest weighted component securities in the aggregate comprise more than 60% of the index's weighting; or (4) the lowest weighted component securities comprising, in the aggregate, 25% of the index's weighting, have an aggregate dollar value of average daily trading volume of less than $50 million (or in the case of an index with 15 or more component securities, $30 million). *See* CEA Section 1a(25)(A)(i)-(iv); Exchange Act Section 3(a)(55)(B)(i)-(iv). Thus, an index that does not have any of these elements is not a narrow-based security index for purposes of CEA Section 2(a)(1)(C)(ii). *See also* CEA Section 1a(25)(B); Exchange Act Section 3(a)(55)(C).

[17] With regard to the third criterion, the CFTC and SEC jointly promulgated Rule 41.13 under the CEA and Rule 3a55-3 under the Exchange Act, governing security index futures contracts traded on foreign boards of trade. These rules provide that "[w]hen a contract of sale for future delivery on a security index is traded on or subject to the rules of a foreign board of trade, such index shall not be a narrow-based security index if it would not be a narrow-based security index if a futures contract on such index were traded on a designated contract market or registered derivatives transaction execution facility." CFTC Rule 41.13, 17 C.F.R. § 41.13; Exchange Act Rule 3a55-3, 17 C.F.R. § 240.3a55-3.

[18] In making this determination, the Commission staff has concluded that the S&P CNX Nifty does not have any of the elements of a narrow-based security index as enumerated in CEA Section 1a(25)(A), and accordingly the Index would not be a narrow-based security index if traded on a designated contract market or DTEF.

[19] *See* letter from Jimmy Ang, Executive Vice President, SGX-DT to C. Robert Paul, General Counsel, CFTC, dated December 13, 2000. SGX-DT represents that under the terms of the MOU with NSE, information relating to market surveillance, which may include information on futures contracts or options on futures contracts based on the S&P CNX Nifty, may be exchanged on a reciprocal basis. *See*

letter from Jimmy Ang, Executive Vice President, SGX-DT to David R. Merrill, Deputy General Counsel, CFTC, dated May 24, 2001. Information that may facilitate the detection or prevention of market manipulation in such contracts or securities underlying the Index may also be shared. *Id.* This information may include, but is not limited to, transactions on trade prices and clearing data and the identity of the ultimate customer to a transaction. *See id.* and electronic mail from Benjamin Foo, Senior Vice President, SGX-DT to Julian E. Hammar, Counsel, CFTC, dated July 13, 2001.

[20]SGX-DT has confirmed that it would cooperate with the Commission in any inquiry, investigation, and/or enforcement proceeding relating to the offer and sale of its futures contract on the S&P CNX Nifty in the U.S. *See* letter from Mr. Ang to Mr. Paul, dated December 13, 2000. In addition, the CFTC has granted Regulation 30.10 relief to SIMEX, SGX-DT's predecessor. *See* Appendix C to Commission Regulation 30.10, 17 C.F.R. § 30.10. Further, SGX-DT is a signatory to the International Information Sharing Memorandum of Understanding and Agreement signed on March 15, 1996, at Boca Raton, Florida.

On May 16, 2000, a Memorandum of Understanding ("MOU") was entered into by SGX-DT's regulator, the MAS, and the U.S. CFTC and SEC with respect to the sharing of confidential information among agencies and mutual assistance in investigation and enforcement matters. Moreover, MAS is a signatory to the Declaration on Cooperation and Supervision of International Futures Markets and Clearing Organizations, signed on March 15, 1996, at Boca Raton, Florida.

[21]*See* 17 C.F.R. Part 30.