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The American Stock Exchange®
An NASD Company

Michael J. Ryan, Jr.
Executive Vice President
and General Counsel

COMMENT

August 31, 2001

Via Overnight Delivery
Ms. Jean Webb, Secretary
Office of the Secretary
Commodity Futures Trading Commission
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Listing Standards and Conditions for Trading Security Futures Products, 17 Part 41, 66 FR 37932 (July 20, 2001)

Dear Ms. Webb:

The American Stock Exchange LLC ("Amex" or "Exchange")[1] is pleased to submit this comment letter in connection with the Commodity Futures Trading Commission's ("CFTC" or "Commission") proposal captioned "Listing Standards and Conditions for Trading Security Futures Products."[2] Although we generally agree with the Commission's proposal, the Amex believes that the three (3) issues identified below must be addressed prior to the Commission adopting the final rules. First, we believe that initial and maintenance listing standards for security futures products set forth in Proposed Rule 41.21 must be uniform among the various exchanges, registered designated contract markets and/or registered derivatives trading execution facilities ("DTEFs"). Second, we assert that the Commodity Exchange Act ("CEA") through the Commodity Futures Modernization Act of 2000 ("CFMA") does not provide the CFTC with the authority to mandate full Intermarket Surveillance Group ("ISG") membership for boards of trade that trade security futures products. Third, we believe that the speculative position limit and position accountability provision in Proposed Rule 41.25 should be made consistent for both options and security futures products.

Proposed Rule 41.21

We reiterate our position set forth in our prior letter dated June 14, 2001 distributed to the CFTC and SEC. A copy is attached hereto as Exhibit A. Accordingly, we believe that shares of exchange-traded funds ("ETFs"), trust issued receipts ("TIRs"), American Depositary Receipts ("ADRs")(including such similar securities as American Depositary Shares, Global Depositary Receipts and Global Depositary Shares), and closed-end registered investment companies (collectively referred to a the "subject securities") are *single securities* for purposes of the CFMA's "security future" definition and should be permitted to overlie a security futures product.[3] Based on the purpose of the CFMA to

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1 The Amex is a national securities exchange registered with the Securities and Exchange Commission ("SEC") pursuant to Section 6 of the Securities Exchange Act of 1934, as amended (the "1934 Act").

2 *See* 17 CFR Part 41 [RIN 3038-AB73], 66 FR 37932 (July 20, 2001)(the "Proposing Release").

3 Section 1a(31) of the CEA defines "security future" as any "contract of sale for future delivery of a single security or of a narrow-based security index ...." (collectively "narrow-based products"). Section 1a(32) defines "security futures product" as a security future or any put, call, straddle, option or privilege on any security future.

provide legal certainty, we believe that issuers, market participants and exchanges would benefit from confirmation of this matter by the CFTC and SEC.

Section 2(a)(1)(D) of the CEA and Section 6(h) of the 1934 Act as amended by the CFMA also require that boards of trade and national securities exchanges establish listing standards for the trading of security futures products. Among other things, these listing requirements require that the underlying security or securities must be registered pursuant to Section 12 of the 1934 Act and be based upon common stock or such other equity securities as the CFTC and SEC jointly determine appropriate.[4] For the purpose of minimizing competitive disparity between trading markets based on regulatory requirements, the CFMA requires that listing standards for security future products be no less restrictive than comparable listing standards for security options. This provision coupled with the harmonization of certain market trading rules, such as margin, suitability, sales practices and transaction fees, between options and futures markets is intended to prevent potential advantage to either regulatory regime (SEC regulated or CFTC-regulated), and, accordingly, preclude "regulatory arbitrage" on the part of market participants.

A security futures product based on a *single security* may be listed and traded on a national securities exchange or national securities association by notice-filing as a designated contract market as follows: (1) the underlying security is registered pursuant to Section 12 of the 1934 Act; (2) the underlying security is common stock or other equity security as the CFTC and SEC jointly determine appropriate; and (3) the security meets the listing standards required by the SEC pursuant to Section 6(h) of the 1934 Act. Similarly, a security futures product based on an *index composed of two or more securities* may be listed and traded on a national securities exchange or national securities association by notice-filing as a designated contract market as follows: (1) the index meets the narrow-based definition found in Section 1a(25) of the CEA; (2) the securities are registered pursuant to Section 12 of the 1934 Act; (3) the securities are common stock or other equity securities as the CFTC and SEC jointly determine appropriate; and (4) the securities meet the listing standards required by the SEC pursuant to Section 6(h) of the 1934 Act.

In addition to conventional common stock, we believe there are a number of other kinds of equity securities that are appropriate to underlie security futures products. In each case, the subject securities are either registered or exempt[5] from registration under Section 12 of the 1934 Act. In each instance, the subject securities are functionally comparable to, or represent investment interests in, one or more common stock. The subject securities have trading and market characteristics substantially similar to traditional common stock listed and traded on national securities exchanges.

With respect to the provision of the CFMA that requires a security futures product to be based on "common stock," such term is not defined in the CFMA, CEA or federal securities laws. Congress did not fully appreciate or intend the disparate treatment for certain equity securities based solely on the status or formation of the legal entity itself rather than on the economic substance of the particular product. Therefore, we submit that security futures based on ETFs, TIRs, ADRs (and like securities), and closed-end registered investment companies should be included as part of any package of listing standards.

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[4] These listing standards also relate to rules regarding settlement; who may deal in security futures products; prohibitions on dual trading; the prevention of price manipulation; and rules governing surveillance, audit trails, trading halts, and margin requirements.

[5] ADRs are provided an exemption from the registration and reporting requirements of Section 12 of the 1934 Act by Rule 12g3-2 thereunder. However, ADRs are generally registered for purposes of the Securities Act of 1933, as amended, on Form F-6. The underlying common stock of an ADR is not similarly exempt from registration.

Mandatory Full ISG Membership

Although we support and encourage information sharing for the purpose of fulfilling coordinated surveillance envisioned by the CFMA, we believe that the Commission has overstepped its authority with respect to the proposal found in Proposed Rule 41.22 that would mandate full ISG membership for boards of trade that trade security futures. We also believe that the Commission's proposal, if adopted, may actually delay the introduction of trading security futures.

The ISG was created in 1983 by the major U.S. securities exchanges and the National Association of Securities Dealers, Inc. ("NASD") in response to the growing need to share regulatory information related to the conduct of effective market surveillance. In 1990 in response to the growing market for derivative products and internationalization, an affiliate category of ISG membership was created to allow futures exchanges and non-U.S. organizations into the ISG to facilitate information sharing. The ISG, however, is not a separate legal entity and is not subject to the direct regulatory oversight of the SEC or any other regulator. In effect, the ISG is a cooperative group formed by contract to facilitate the performance of certain regulatory responsibilities of its members. Currently, the "full" members of ISG are the Amex, Boston Stock Exchange, Chicago Board Options Exchange, Chicago Stock Exchange, Cincinnati Stock Exchange, International Securities Exchange, NASD, New York Stock Exchange, Pacific Stock Exchange and Philadelphia Stock Exchange.

The plain language and intent of the CFMA does not mandate that boards of trade become full members of the ISG. Without clear Congressional directive and intent to require boards of trade to be full members of ISG, and, therefore, impose additional regulatory burdens and oversight on the members of ISG, the Amex submits that the Commission's proposal as a matter of law is not justified.

We generally support using ISG and its mechanisms to ensure coordinated surveillance between markets that trade security futures products and those markets that trade the underlying securities and securities options. Implementing automated systems for the daily exchange of market surveillance information will require time, however. Admission to "full" membership status will also require the unanimous vote of all current full ISG members, the majority of which have expressed no intention to trade securities futures and thus are likely to remain outside the Commission's jurisdiction. It would seem to us inconsistent with the clear intent of Congress to permit trading in securities futures to commence by certain dates to make the commencement of trading dependent on the unanimous vote of a group of securities markets some of which may have no interest in expediting the introduction of securities futures. The proposed Commission rulemaking, accordingly, is not a useful or appropriate vehicle for changing the membership status of boards of trade within the ISG.

Speculative Position Limits

The Amex believes that the CFMA requires consistency between CFTC and SEC-regulated markets trading security futures products and between the regulation of these products and the underlying securities and related security options, so that none of these marketplaces has a competitive advantage through regulation. Therefore, it is essential that the proposed speculative position limit and position accountability rule should be coordinated between the SEC and CFTC. For example, position limits in the options markets should not be placed at a competitive disadvantage in relation to the speculative position limits and/or position accountability rule adopted for security futures products.

At the Amex, position limits restrict the number of options contracts that an investor, or a group of investors acting in concert, may own or control on the same side of the market (long calls and short puts are aggregated; as are short calls and long puts). Similarly, exercise limits prohibit the

exercise of more than a specified number of contracts on a particular instrument within five (5) business days. The actual limits set by the Exchange are 13,500, 22,500, 31,500, 60,000, or 75,000 based on actual trading volumes.[6] With respect to narrow-based options contracts, the position limits are 18,000, 24,000 and 30,000 contracts on the same side of the market based on index composition.[7] These are gross, not net limits (*i.e.* long call/short put positions are not offset by short call/long put positions).

Proposed Rule 41.25(a)(3) provides that designated contract markets or DTEFs must establish position limit and/or position accountability rules for the expiring month of a security futures contract. In particular, the proposal calls for either a limit of 13,500 contracts or 22,500 contracts held during the last 5 days of trading. To receive the upper limit of 22,500 contracts, the average daily trading volume ("ADTV") in the underlying security must exceed 20 million shares or exceed 15 million shares and have more than 40 million shares outstanding. In addition, a designated contract market or DTEF may adopt a position accountability rule if the ADTV exceeds 20 million shares and there are more than 40 million outstanding shares in the underlying. The position accountability rule permits traders to be free from these speculative position limits and provides that traders with a net position of greater than 22,500 contracts, or such lower level established by the designated contract market or DTEF, are required to provide position information and consent to stop increasing positions if ordered to do so.

Consistent with the comment of Chicago Mercantile Exchange in its letter dated August 20, 2001, we also believe that the Commission's Proposed Rule 41.25(a)(3)(ii) should be revised to reflect a minimum average trading volume standard rather than the proposed standard of "least liquid security" for purposes of speculative position limits and the position accountability rule for narrow-based security indexes.

As the above descriptions demonstrate, the methodology used to develop and apply position limits for security futures products differ substantially from that in place for security options. The levels of the proposed limits for security futures products are actually lower than security options, at least for those overlying the largest and most active underlying stocks. But they are net limits allowing positions of effectively unlimited size in different contract months, whereas the security options limits impose caps on maximum positions on either side of the market. Moreover, the proposed exemption for traders eliminating any limit at all has no counterpart for security options. Clearly, the disparate treatment of position limits for security options and security futures products under this proposal likely will result in benefits to security futures products solely based on the regulatory environment. We believe the CFTC and SEC jointly should provide uniform position limits across the markets for security options and security futures products so that the trading markets for these products are on an equal footing.

The Amex, based on the purpose and intent of the CFMA, believes that position limits for security products and security options should be uniform. Although we are not particularly concerned whether the existing security options approach or proposed security futures approach is ultimately adopted, it should be consistent across related markets. Given the fact that position limits have been imposed on security options since the introduction of standardized options trading in 1973, we submit that the instant proposal provides a unique opportunity for the SEC together with the input of the CFTC to evaluate whether or not position limits in either context are necessary to foster market integrity and protect investors. Above all, it is imperative that the limits as adopted by the Commissions be uniform and consistent among SEC and CFTC-regulated markets.

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[6] *See* Amex Rule 904, Commentary .07 and .09.
[7] *See* Amex Rule 904C(c) and Commentary .01.

We also note that Proposed Rule 41.25(a) requires designated contract markets and DTEFs to comply with the daily reporting requirements of Chapter 16 of the Commission's regulations. This proposal, however, fails to distinguish those notice-registered designated contract markets and DTEFs that are primarily regulated by the SEC, and, therefore, already provide comparable information to the SEC. Accordingly, we believe that notice-registered markets with the Commission should be exempt from the provisions of Proposed Rule 41.25(a) if comparable information is provided to the SEC.

Thank you for this opportunity to comment on the Proposing Release. If there are any questions or comments regarding this letter and related matters, please contact me at (212) 306-1200 or Jeffrey P. Burns at (212) 306-1822.

Sincerely,

Michael J. Ryan, Jr.
Executive Vice President and General Counsel

cc: Elizabeth L. R. Fox, Acting Deputy General Counsel, CFTC
Richard A. Shilts, Acting Director, Division of Economic Analysis, CFTC
Thomas M. Leahy, Jr., Chief, Financial Instruments Unit, Division of Economic Analysis, CFTC
Annette L. Nazareth, Director, Division of Market Regulation, SEC
Elizabeth King, Associate Director, Division of Market Regulation, SEC

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Exhibit A

June 14, 2001

Via Overnight Delivery
Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Ms. Jean Webb
Secretary
Commodity Futures Trading Commission
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Method for Determining Market Capitalizations and
Dollar Value of Average Daily Trading Volume;
Application of the Definition of Narrow-Based Security Index
SEC Release No. 34-44288; File No. S7-11-01

Dear Ladies and Gentlemen:

The American Stock Exchange LLC ("Amex" or "Exchange")[1] is pleased to submit this comment letter in connection with the joint release of the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC"): "Method for Determining Market Capitalizations and Dollar Value of Average Daily Trading Volume; Application of the Definition of Narrow-Based Security Index" (the "Joint Release").[2] First, although not specifically covered in the Joint Release, we believe the release provides the opportunity for the Commissions to provide clarification of the term "single stock future" as it applies to futures contracts on shares of exchange-traded funds ("ETFs")[3] and trust-issued receipts ("TIRs")[4] under The Commodity Futures Modernization Act of 2000 (the "CFMA").[5] Second, we believe that proposed CFTC Rule 41.14 should be revised to permit a "grace period" of not less than nine (9) months, with extensions possible, and to allow trading other than "liquidation only" transactions during the wind-down period, for cases where a securities index future ceases to meet the "narrow-based" definition.

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1 The Amex is a national securities exchange registered with the SEC pursuant to Section 6 of the Securities Exchange Act of 1934, as amended (the "1934 Act").

2 *See* Securities Exchange Act Release No. 44288 (May 9, 2001), File No. S7-11-01 [RIN 3235-AH13], 17 CFR Part 240; CFTC, 17 CFR Part 41 [RIN 3038-AB77].

3 Currently, the Amex lists and trades eighty-three (83) ETFs.

4 Currently, the Amex lists and trades 17 HOLDRS products listed under our TIR standards.

5 *See* Section 222 of the CFMA [Section 5 of the Commodity Exchange Act, as amended ("CEA")].

Statutory Background

The CMFA by its amendment to the Commodity Exchange Act ("CEA") and the Securities Exchange Act of 1934 ("1934 Act") and other federal securities laws establishes a divided regulatory jurisdiction over securities related futures contracts. Jurisdiction over any "security future," which is defined to mean any "contract of sale for future delivery of a single security or of a narrow-based security index ..." (collectively "narrow-based products") is assigned jointly to the SEC and the CFTC.[1] The CFTC is given exclusive jurisdiction over any futures contract on any "group or index of securities" that does "not constitute a narrow-based security index."[2] If a product is jointly regulated, it may be traded on either a SEC or CFTC regulated market which complies with the requirements of its principal regulator and makes a "notice" filing allowing it to be a limited purpose market place for purposes of the other commission's jurisdiction. Thus, to trade "narrow-based" products, a national securities exchange, such as the Amex, would be required to satisfy SEC listing requirements as well as become a limited purpose designated contract market by making a notice filing with the CFTC. In contrast, if a product is not narrow-based (i.e. deemed to provide for future delivery of a broad-based index), the CFTC would have sole jurisdiction and a national securities exchange would be able to trade in it only if the exchange went through the full CFTC application and review process to become a designated contract market or a derivative transaction execution facility ("DTEF"). Furthermore, as pointed out by the Joint Release, this procedure would apply if the product, although initially a "narrow-based" were to later fail to meet the "narrow-based" definition.

Single Security Futures

One of the often cited purposes of the CFMA is to provide legal certainty. This purpose would be furthered by the Commissions clarifying that certain instruments, particularly shares of ETFs and TIRs are single securities for purposes of the CFMA's "narrow-based products" definition. We believe that issuers, market participants and exchanges would benefit from the certainty that would be provided by a confirmation of this matter by the two Commissions.

An ETF refers to an investment company registered under the Investment Company Act of 1940, as amended (the "1940 Act"), that has its shares traded on a national securities exchange. Currently, ETFs are structured to track the yield and price performance of certain securities indexes, although in the future, ETFs may also be actively-managed. The majority of ETFs are registered under the 1940 Act either as unit investment trusts ("UITs") or open-end management investment companies (UITs and open-end management investment companies are collectively referred to as a "fund" or "funds"). Each such fund continuously offers and redeems shares in large aggregation amounts (50,000 shares) called Creation Units at a price established at the end of each business day based on the net asset value ("NAV") of its portfolio. The individual shares of the fund are listed and traded in a secondary trading market on a national securities exchange. These shares are separate securities registered under Section 12(b) of the 1934 Act and are subject to applicable exchange listing standards.[3] Accordingly, a fund share is traded like any other single security listed for trading on a national securities exchange.

[1] CEA §2(a)(1)(D)(i).

[2] CEA §2(a)(1)(c)(ii)(III).

[3] *See* Amex Rules 1000 *et. seq.* (Portfolio Depository Receipts) and 1000A *et. seq.* (Index Fund Shares).

TIRs are issued by a trust formed for the specific purpose of holding deposited shares for the benefit of its owners. For example, Holding Company Depository Receipts or "HOLDRS" are issued by a trust formed specifically for the purpose of issuing HOLDRS (the "HOLDRS Trust") and listed on the Amex under the TIR Rules.[4] As a result of no-action relief granted by the SEC's Division of Investment Management, the HOLDRS Trust is not a registered investment company under the 1940 Act.[5] Although investors in HOLDRS have many of the same rights as the owners of the underlying securities in the relevant HOLDRS Trust,[6] HOLDRS are separate securities registered under Section 12(b) of the 1934 Act and subject to applicable exchange listing standards. Consequently, HOLDRS and other TIRs, trade like any other single security listed for trading on a national securities exchange. Further, HOLDRS may trade at a discount in the secondary market at prices lower than the net asset value of the underlying group of securities.

ETF shares and TIRs are each regulated and traded as single securities, and therefore, we submit, come within the definition of a "security future," and are *not* contracts for delivery of a securities index. ETFs are registered as management investment companies or UITs under the 1940 Act with their securities separately registered under Section 12(b) of the 1934 Act and subject to exchange listing standards. ETF shares do not represent a direct ownership interest of the underlying securities, but instead, are separately registered and traded shares in a single fund representing a direct ownership interest in the fund (ETF). Like mutual funds, an ETF holder cannot vote the underlying shares held by such ETF and may receive capital gain distributions, potentially resulting in economic results quite different than directly holding the actual underlying portfolio. Furthermore, with respect to ETFs, ownership of an ETF is not the same as ownership of the benchmark index. For example, a S&P Depository Receipt ("SPDR") is a separate security that tracks the performance of the Standard & Poor's 500 Index but is not the index itself.[7]

Similarly, TIR shares generally and, in particular, HOLDRS, are single, separate securities registered under Section 12(b) of the 1934 Act and also subject to exchange listing standards. The Amex, in particular, has adopted separate listing standards for HOLDRS through adoption of the TIR rules.[8] An investor in a HOLDR has an ownership interest in the underlying securities held by the HOLDRS Trust, however, that ownership is indirect and undivided, and

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[4] The HOLDRS Trust is created by a depository trust agreement with a trustee, Merrill Lynch, Pierce, Fenner & Smith Incorporated (Initial Depositor) and other depositors and owners of the HOLDRS. *See* SEC No-Action Letter to Merrill, Lynch, Pierce, Fenner & Smith Incorporated dated September 3, 1999 (Merrill Lynch No-Action Ltr.").

[5] *Id*

[6] HOLDRS are issued by the trust and represent a beneficial ownership interest in the common stock of the specified underlying securities of the particular HOLDRS Trust. Beneficial owners have many of the same rights as they would have if they owned the underlying securities outside of the HOLDRS Trust. These rights include but are not limited to, the right to vote the common stock and receive dividends and other distributions on the underlying securities as well as receipt of all communications, proxy statements and other materials from the issuers of the underlying securities. However, an investor in HOLDRS is not free to receive or transfer the underlying securities. Rather the investor can gain access to the underlying securities only after cancellation of the related HOLDR, which requires surrender of the HOLDR during the trustee's normal business hours and payment of applicable fees, taxes or governmental charges, if any. Receipt of the underlying securities will occur within one (1) business day after the trustee receives the cancellation request.

[7] Although investment in an ETF may generally correspond to the price and yield performance of the underlying index or portfolio of securities, it is not the same as purchasing the underlying index or portfolio of securities. ETFs do not replicate the underlying benchmark index or group of securities, but instead, are initially set on a per share basis at a percentage of the underlying index or portfolio of securities. For example, SPDRs are $1/10^{th}$ the value of the S&P 500 Index while the QQQ (Nasdaq-100 Index Tracking Stock) is $1/40^{th}$ of the value of the Nasdaq-100. As of March 30, 2001, the "tracking error" as compared to the S&P 500 Index and Nasdaq-100 Index for SPDRs and QQQs was 0.01% and 0.02%, respectively. Therefore, owning the particular ETF is not the same as owning the underlying benchmark index or portfolio of securities.

[8] *See* Amex Rules 1200-1202.

therefore, economically distinct as evidenced by the HOLDRS constitutive documents, [9] and by the fact that HOLDRS prices may vary from the value of shares held in the HOLDRS Trust. Further, HOLDRS are margined like individual stocks for customer accounts.

As a practical matter, the market has treated ETF shares and HOLDRS as separate securities for some time and each are actively traded as separate securities on national securities exchanges. For example, as of April 30, 2001, year-to-date average daily trading volumes for shares of the two most active ETFs – SPDRs and QQQs -- and aggregate HOLDRS were 11.3 million, 70.5 million and 5.11 million shares, respectively. Clearly, ETFs and HOLDRS function as separate securities with distinct and active trading markets. In addition, equity options are traded on shares of various ETFs and HOLDRS while a futures contract has yet to be developed on these securities. Of particular note is the absence of a futures contract based on SPDRs or QQQs. The lack of a futures contract on a variety of ETFs and HOLDRS suggests that the futures exchanges and related market participants have understood that shares of ETF and HOLDRS are separate securities.

The holder of an ETF contract also bears a risk that achieved performance of the ETF fund may not mimic exactly the performance of the benchmark index. As a security, ETF shares do not provide for "delivery" of the benchmark index, but reflect the shares of the underlying fund, which in turn is ultimately tied in value to the fund's specific securities holdings, not the value of an index. Therefore, a HOLDR has even less of a connection than an ETF to a securities index. In addition, each HOLDR has its own separate pricing and trading characteristics apart from the underlying basket of securities held by the HOLDR Trust. The basket of securities, in turn, is completely distinct from *any* securities index (including an index that could in the future be conceived of) that happened to be comprised of the securities in the basket.

For all these reasons, we request that the Commissions confirm that shares of ETFs and TIRs (*i.e.* HOLDRS) which we registered as single securities under the 1934 Act, will also be classified as a single security for purposes of Section 3(a)(55) of the 1934 Act.

Narrow-Based Index Reclassification

The Joint Release, in addition to proposing rules for determining market capitalization and dollar value of trading volume for purposes of applying the definition of "narrow-based" security index, also proposes a procedure for closing down markets when such an index ceases to be "narrow-based." This procedure has application to a national securities exchange that has become a limited purpose designated contract market by notice filing with the CFTC. Proposed CFTC Rule 41.14 provides that an index is "narrow-based" as long as it meets that definition for 45 days in any consecutive three (3) calendar months. However, if an index that was previously "narrow-based" ceases to be "narrow-based" (and is therefore "broad-based") for more than 45 days in the 3-month period, it would be deemed "broad-based" under the proposed Rule. After a "grace period" of three (3) months in which the index would continue to be deemed to be "narrow-based," the securities futures contract would be required to be wound down. Accordingly, the listing of new contract months would be prohibited with trading limited to liquidating only transactions.

We believe that the proposed Rule, if left unmodified, risks undue disruption and injury to investors and to any national securities exchange trading securities futures on an index that, may, due to no fault of the investors or the exchange ceases to be narrow-based.[10] More importantly, the

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[9] *See* Merrill Lynch No-Action Letter, supra note 9.

[10] In contrast, a broad-based securities index future that becomes narrow-based after at least 30 days of trading is provided a 3-month grace period where in order to remain solely regulated by the CFTC, such designated contract market, DTEF or foreign board of trade would be required to change the composition of, or weightings of,

proposal by providing an unreasonably short grace period and then limiting trading by all market participants (including specialists and market makers who provide market liquidity) to liquidating only transactions would reduce the liquidity of the securities futures contract market, and thereby, directly impose potentially significant costs on investors seeking to close positions. The mere risk that such an event could occur would impair the attractiveness of a narrow-based securities index futures contract. Depending on the particular index, a national securities exchange such as the Amex, may also have very little influence or power to change or modify the composition of an index in order for it to remain narrow-based. Accordingly, we believe that a national securities exchange trading a narrow-based securities index futures contract should not be materially disadvantaged by a subsequent change in the index's classification to broad-based.

While CEA section 2(a)(1)(c)(iii) grants the CFTC discretion to determine that a stock index futures contract, although not conforming to the "narrow-based" definition, should be treated as a security future, we believe that this discretionary authority would not cure the identified inadequacies in the proposed Rule. Both investor protection and exchange business requirements call for the legal certainty of a well-crafted rule on this subject. We therefore urge both the SEC and CFTC to incorporate the following modifications into the final Rule. With respect to the "grace period," if an underlying index had been the narrow based for at least 6 consecutive months prior to the initial trading in the related securities futures contract, we believe that there exists a strong presumption that the contract was listed in good faith and not in an attempt to evade CFTC jurisdiction. In such case, a grace period of at least 9 months should be allowed for a more orderly wind-down to trading or to permit the exchange to seek to qualify as a designated contract market so that the futures contract could continue trading. Furthermore, we also believe that it would be appropriate for the CFTC to give itself the flexibility to extend the grace period, particularly when an application for designation as a contract market is pending. We also assert that the "liquidating only" limitation on trading should be eliminated from the proposed Rule. At the very least, it is essential that professional liquidity providers, such as specialists and market makers, be allowed to continue to effect opening transactions through the remaining life of the contract, to foster liquidity and avoid harming investors who hold positions in the expiring contract. Otherwise, specialists and market makers will quickly flatten out their positions. Therefore, public customers would only be able to liquidate their positions in the unlikely event that another public customer with an opposing position were seeking to close-out their position at the same time.

Thank you for this opportunity to comment on the Joint Release. If there are any questions or comments regarding this letter and related matters, please contact the undersigned at (212) 306-1200 or Jeffrey P. Burns at (212) 306-1822.

Sincerely,

Michael J. Ryan, Jr.
Executive Vice President and General Counsel

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securities in the index so that it is not narrow-based. Alternatively, such markets could notice register as a securities futures product exchange under Section 6(g) of the 1934 Act. *See* Section 202 of the CFMA. In cases where the broad-based securities index future has traded for less than 30 days, the proposed Rule calls for an exclusion from the definition of narrow-based security index if such index for an uninterrupted period of 6 months prior to the first day of trading would not have been narrow-based.

cc: Hon. Laura S. Unger, Acting Chairman, SEC
Hon. Isaac C. Hunt, Jr., Commissioner, SEC
Hon. Paul R. Carey, Commissioner, SEC
Annette Nazareth, Director, Division of Market Regulation, SEC
Robert L. D. Colby, Deputy Director, Division of Market Regulation, SEC
Elizabeth K. King, Associate Director, Division of Market Regulation, SEC
Nancy J. Sanow, Assistant Director, Division of Market Regulation, SEC

Hon. James E. Newsome, Acting Chairman, CFTC
Hon. David D. Spears, Commissioner, CFTC
Hon. Barbara Pedersen Holum, Commissioner, CFTC
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Elizabeth L. R. Fox, Acting Deputy General Counsel, CFTC
De'Anna Dow, Acting Director, Division of Trading and Markets
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