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COMMENT

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Received CFTC
Records Section
8/1/06

Brussels, 1 August 2006

Response to the Request for Comment of

the Commodity Futures Trading Commission (CFTC):

"What Constitutes a Board of Trade Located Outside the United States"

I. Introduction

1. The Federation of European Securities Exchanges (FESE) represents operators of the European regulated markets and other market segments, comprising the markets for not only stocks, but also financial, energy and commodity derivatives. Established in 1974 as a small forum of stock exchanges in Europe, FESE today has 24 full members representing close to 40 securities exchanges from all the countries of the European Union (EU) and Iceland, Norway, and Switzerland, as well as several corresponding members from other non-EU countries.

2. FESE welcomes the opportunity to respond to the CFTC's Request For Comment related to the definition of a "board of trade, exchange, or market located outside the United States" as that phrase is used in Section 4(a) of the Commodity Exchange Act (CEA), which has been the basis of the practice of "no-action" letters allowing such entities to make their products available in the US by permitting direct access to their electronic systems without becoming registered as a designated contract market or a derivatives transaction execution facility.

3. Several members of FESE are responding to this Request for Comment directly. **FESE as a whole fully supports the broad thrust of the views put forth in these responses**. The purpose of the current response is to express this support and at the same time to underline the key principles from these responses that are of particular concern to FESE's broader membership.

II. Key Elements of Our Response to the CFTC's Request for Comment

4. FESE's response to the Request for Comment is based on the experience of several of its members which have received the no-action letters in the past, as well as its members' broader involvement and interest in offering a range of their services internationally, including in the US. FESE's main concern with respect to the issues at hand is fostering an **open and competitive environment** in which to engage in an **innovative** and **adequately regulated and supervised** derivatives business across the Atlantic.

5. Thus FESE appreciates that the CFTC's Request for Comment is informed by its mandate given by Congress and in particular its principal goals of safeguarding market integrity and investor protection. At the same time, FESE is pleased to see that the CFTC recognizes its duty to foster competition and to facilitate international trade in financial products. In particular, we support the CFTC's statement on page 9 of the Request for Comment that it will "strive to ensure

that it neither inhibits cross-border trading nor imposes unnecessary regulatory burdens".

6. In this context, we consider the CFTC's practice of issuing no-action letters to allow foreign boards of trade (FBOTs) to make their products available in the US as **very successful**. This regime is consistent with and complements another successful policy of the CFTC, that of its Part 30 regime for the foreign intermediaries. Both policies are based on the principle of mutual recognition and equivalence which have made the CFTC a true leader in bringing the long-term agenda of fostering competition and integrating the global derivatives markets forward.

7. The arrangements built around the no-action letters used by the CFTC – including the comprehensive reviews of the FBOT as well as of its supervisory environment - have served the CFTC's objectives very well. As explained on page 7 of the Request for Comment and also described by the FESE members present at the June Hearing, each request for terminal placement non-action relief involves a thorough analysis on the part of the CFTC of the factors its considers most important and relevant to each case in assessing the bona fide foreign nature of the FBOT. Moreover, this process also involves an intense dialogue with the foreign supervisor in question which lays the groundwork for long-term cooperation throughout the life of the activities of the FBOT under the no-action letter. It is also noteworthy that each letter is tailored to the specific circumstances of the request and gives the CFTC the opportunity to introduce special conditions which it feels are necessary to achieve its objectives.

8. Moreover, we also note the recent amendment of the no-action letter procedure dated April 2006 which requires a longer period of notice to the CFTC in respect of new contract listings. Overall, these arrangements provide the necessary flexibility to deal with a complex set of dynamic factors that the US regulators have to take into account in a market that changes very fast and to react in conjunction with other regulators.

9. In its essence, this practice is fully consistent with the **principles-based approach** established by the Commodity Futures Modernization Act (CFMA) – an approach that we particularly value in Europe, where the legislative reform launched through the Lamfalussy process over the last five years is also based on this key regulatory principle. The legislative reform was accompanied by an overhaul of the EU's financial sector framework to introduce high standards of investor protection and safeguards for market integrity and market stability. This process has also been accompanied by an increasingly intense collaboration between the capital markets regulators in the EU and the US, of which the CFTC-CESR joint work is probably the best example. Thus we consider the supervisors of the FBOTs established in the European Single Market as particularly good partners for the CFTC in its continued policy of international cooperation to ensure an adequate level of supervision of the FBOTs.

10. As for markets beyond the borders of the EU Single Market, we view the IOSCO principles for screen-based trading in derivatives markets in particular, and the various avenues of cooperation and regulatory convergence that exist today more generally, as sufficient factors that will guarantee that the CFTC can rely on its partner supervisors. In this context, we would especially like to draw attention to the IOSCO Multilateral Memorandum of Understanding (MoU) Concerning Consultation and Cooperation and the Exchange of Information of 2002, of which

the CFTC is a signatory. Thus the CFTC already has the basis for an extensive exchange of information with all the signatories of this MoU.

11. Considering all the factors above, and the more than satisfactory track record of the current arrangements, we would caution against any change of the current regime, especially in the absence of positive evidence that alternative arrangements will: (i) achieve the CFTC's goals; and (ii) do so in a more effective way than the existing no-action regime.

12. In this context, while referring the CFTC to the **more detailed responses of our members**, we would like to highlight a couple of the **most important problems** we have identified with the alternative arrangements proposed in the Request for Comment.

13. First and foremost, we see more potential harm than good in "codifying" the practice of no-action letters. In fact, we fundamentally challenge the view that it needs to be "codified" since we find that the practice already constitutes a clear and transparent policy of the CFTC. Its time-tested success clearly shows that, although implemented on the basis of ad hoc requests, it constitutes a coherent approach that is well designed to address the CFTC's concerns effectively and is well understood by the industry as well as the international regulatory community. As the June Hearing shows, all of the users and the majority of the observers of the practice appear to find that it is consistently implemented and transparently communicated.

14. While such a "codification" falls far short of being demonstrably beneficial, it is very likely to lead to great potential damage to the functioning of the markets by inhibiting cross-border trading, imposing unnecessary regulatory burdens, and undermining innovation. Most of the alternative arrangements considered in the Request for Comment and the Hearing seem to us to lead to a rigid and technically inadequate formula that would create duplicative regulation, confusion, and unjustified burdens for the FBOTs. Such an outcome would not only harm the entities providing access to their services from the US, but also the US investors, traders, and other end users of these markets.

15. To the extent that the CFTC sees it as necessary to formalize its practice of no-action letters, **only the very minimum changes that would retain the flexibility of the current regime should be considered, if any at all**. In fact, the main difficulty with finding satisfactory alternative arrangements, such as quantitative thresholds, demonstrates the strength of the current regime, which takes into account the **totality of the circumstances rather than one single element or one single measure**. The proposal of fixed definitions relying on quantitative thresholds in particular would take away this flexibility and at the same time place undue burdens on the foreign exchanges due to the technical difficulties in implementing such a regime (as described in more detail by our members in the Hearing and in their subsequent submissions).

16. In our view, the definition of **a foreign board** has to take into account the totality of circumstances (such as where the entity is located; where it is regulated; and where its decisions are made) with an emphasis on those criteria of most significance from the supervisory/regulatory standpoint. By contrast, alternative factors such as where the operations of the entity are carried out and where its trading volume is derived are largely irrelevant in most cases and problematic to measure and to implement. It is important to remember that the current review involved in each no-action letter allows the CFTC to take into

account any factor that it sees as relevant, which would be difficult to achieve in an alternative regime that is fixed around given parameters.

17. A final point we would like to comment on is the concern for a level playing field expressed by some of the participants in the Hearing. As the above discussion demonstrates, we fully support the principle of a level playing field between competitors and in fact see it as potentially endangered by an unjustified duplicative imposition of jurisdiction on FBOTs who operate under the no-action letters. In fact, for an FBOT to qualify for a no-action letter, the CFTC has to be fully satisfied that its home supervision is equivalent to that of the CFTC in every tangible area affecting the US operations. As in any other case of the evaluation of equivalence, one needs to look at the totality of principles and rules to which the entity is subject.

18. In this sense, we fully support the views expressed by many participants in the Hearing concerning the need to look at the totality of the rules of the foreign jurisdiction, and not to focus on a few of the areas in which the foreign jurisdiction may seem to be more lenient, which will no doubt be counterbalanced by other areas where the rules might be more stringent, if the overall effect is to be equivalent. Thus we see no risks to the level playing field for the US exchanges at all from the imposition of different rules in the foreign jurisdiction as long as the CFTC and the foreign supervisor are able to come to an agreement on the ultimate policy objectives and the desired outcomes and, further, can agree that their respective regulatory regimes are equivalent.

III. Conclusion

19. For all the reasons described above, **we fully support the continuation of the existing arrangements used by the CFTC in allowing the FBOTs access to the US market**. These arrangements constitute a coherent and transparent policy, which serves all of the policy goals of the CFTC well, ensures proportionality and efficiency, and is seen by the industry and regulatory community around the world as a very positive example of regulatory collaboration.

20. Above all it should be kept in mind that the existing regime offers the ability for the CFTC to impose additional requirements on a case-by-case basis as necessary. As FESE, we are of the opinion that any changes to the current procedures and policies that underlie them should be made only as a last resort, once all remedies available under the no-action regime have been exhausted.

21. We have full confidence that a review that focuses above all on **the interests of the US investors, traders and economy as whole** in **an open and well-supervised global derivatives market** will lead to the continuation of the uniquely successful no-action letters of the CFTC which have directly and tangibly contributed to the development of this market over the past ten years they have been in existence.