

COMMODITY FUTURES TRADING COMMISSION

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-)

Joint Order Granting the Modification of Listing Standards Requirements under Section 6(h) of the Securities Exchange Act of 1934 and the Criteria under Section 2(a)(1) of the Commodity Exchange Act

August 20, 2001

The Commodity Futures Modernization Act of 2000¹ (“CFMA”), which became law on December 21, 2000, lifted the ban on the trading of futures on single securities and on narrow-based security indexes (“security futures”)² in the United States. In addition, the CFMA established a framework for the joint regulation of these newly-permissible security futures products by the Commodity Futures Trading Commission (“CFTC”) and the Securities and Exchange Commission (“SEC”) (jointly, the “Commissions”). Under the CFMA, national securities exchanges and national securities associations may trade security futures products if they register with the CFTC and comply with certain requirements of the CEA. Likewise, designated contract markets and registered derivatives transaction execution facilities (“DTEFs”) may trade security futures products if they register with the SEC and comply with certain other requirements of the Exchange Act.

As part of this new regulatory framework, the CFMA amended the Securities Exchange Act of 1934 (“Exchange Act”) and the Commodity Exchange Act (“CEA”) by, among other things, establishing the criteria and requirements for listing standards

¹ P.L. 106-554, 114 Stat. 2763 (2000).

² Section 6(h)(6) of the Exchange Act provides that options on security futures (“security futures products”) may not be traded until three years after the enactment of the CFMA and the determination

regarding the category of securities on which security futures products can be based. The Exchange Act³ provides that it is unlawful for any person to effect transactions in security futures products that are not listed on a national securities exchange or a national securities association registered pursuant to Section 15A(a) of the Exchange Act.⁴ The Exchange Act⁵ further provides that such exchange or association is permitted to trade only security futures products that conform with listing standards filed with the SEC and that meet the criteria specified in Section 2(a)(1)(D)(i) of the CEA. Section 2(a)(1)(D)(i) of the CEA states that no board of trade shall be designated as a contract market with respect to, or registered as a DTEF for, any contracts of sale for future delivery of a security futures product unless the board of trade and the applicable contract meet the criteria specified in that section.⁶ Similarly, the Exchange Act requires that the listing standards filed with the SEC by an exchange or association meet specified requirements.⁷

In particular, the Exchange Act⁸ and the CEA⁹ state that, except as otherwise provided in a rule, regulation, or order, any security underlying the security future, including each component security of a narrow-based security index, is required to be

jointly by the Securities and Exchange Commission and Commodity Futures Trading Commission to permit options on such futures. 15 U.S.C. 78f(h)(6).

³ Section 6(h)(1) of the Exchange Act, 15 U.S.C. 78f(h)(1).

⁴ 15 U.S.C. 78a et seq.

⁵ Section 6(h)(2) of the Exchange Act, 15 U.S.C. 78f(h)(2).

⁶ 7 U.S.C. 2(a)(1)(D)(i).

⁷ Section 6(h)(3) of the Exchange Act, 15 U.S.C. 78f(h)(3).

⁸ Section 6(h)(3)(A) of the Exchange Act, 15 U.S.C. 78f(h)(3)(A).

⁹ Section 2(a)(1)(D)(i)(I) of the CEA, 7 U.S.C. 2(a)(1)(D)(i)(I).

registered under Section 12 of the Exchange Act.¹⁰ The Exchange Act¹¹ and the CEA¹² also require that, except as otherwise provided in a rule, regulation, or order, security futures must be based upon common stock¹³ and such other equity securities as the Commissions jointly determine appropriate.

Accordingly, without modification of the statutory listing requirements, a national securities exchange, national securities association, designated contract market, or registered DTEF may not list and trade a security future on a depositary share or on a narrow-based security index that includes as one of its component securities a depositary share.¹⁴ Although the security underlying a depositary share may be registered pursuant to Section 12 of the Exchange Act, the depositary share itself is not so registered. In addition, although the depositary share may represent the common stock of an issuer, the depositary share itself is not common stock. As a consequence, the requirements specified in Sections 6(h)(3)(A) and (D) of the Exchange Act and the criteria specified in Sections 2(a)(1)(D)(i)(I) and (III) of the CEA are not satisfied.

Section 6(h)(4) of the Exchange Act¹⁵ and Section 2(a)(1)(D)(v)(I) of the CEA¹⁶ provide that the Commissions, by rule, regulation, or order may jointly modify the listing standards requirements specified in Sections 6(h)(3)(A) and (D) of the Exchange Act, and

¹⁰ 15 U.S.C. 78l.

¹¹ Section 6(h)(3)(D), 15 U.S.C. 78f(h)(3)(D).

¹² Section 2(a)(1)(D)(i)(III) of the CEA, 7 U.S.C. 2(a)(1)(D)(i)(III).

¹³ For purposes of Section 6(h)(3) of the Exchange Act and Section 2(a)(1)(D)(i) of the CEA, the term common stock includes ordinary shares.

¹⁴ A depositary share is defined as a security evidenced by an American Depositary Receipt that represents a foreign security or a multiple or fraction thereof. See 17 CFR 240.12b-2.

¹⁵ 15 U.S.C. 78f(h)(4).

the criteria specified in Sections 2(a)(1)(D)(i)(I) and (III) of the CEA, respectively, to the extent such modification fosters the development of fair and orderly markets in security futures products, is necessary or appropriate in the public interest, and is consistent with the protection of investors. Because a depositary share is a security that represents the underlying common stock, the Commissions believe that a future based on a depositary share that represents a particular common stock is fundamentally equivalent to a future based on such common stock. In addition, although a depositary share itself is not registered pursuant to Section 12 of the Exchange Act, if the security represented by that depositary share is registered under Section 12, an investor effecting a transaction in the depositary share would have publicly available information about the company prior to making an investment decision. Moreover, permitting futures on ADRs makes available additional products to market participants.

Therefore, the Commissions believe that it would foster the development of fair and orderly markets, would be necessary or appropriate in the public interest, and would be consistent with the protection of investors to modify by joint order the listing standards requirements specified in subparagraphs (A) and (D) of Exchange Act Section 6(h)(3) and subclause (I) and (III) of Section 2(a)(1)(D)(i) of the CEA, to permit, in certain specified circumstances, a national securities exchange, national securities association, designated contract market, or registered DTEF to list and trade security futures products when a depositary share is underlying the security future or is a component security of a narrow-based security index underlying the security future.¹⁷

¹⁶ 7 U.S.C. 2(a)(1)(D)(v)(I).

¹⁷ A national securities exchange, national securities association, designated contract market or registered DTEF that relies on this order to list and trade a security futures product when a depositary share is underlying the security future, or is a component security of a narrow-based security index underlying

For these reasons, the Commissions by order are jointly modifying the requirements specified in subparagraphs Sections 6(h)(3)(A) and (D) of the Exchange Act and the criteria specified in Sections 2(a)(1)(D)(i)(I) and (III) of the CEA to permit a depositary share, as defined in Exchange Act Rule 12b-2, to underlie a security future, and be a component security of a narrow-based security index, provided that:

- (1) the deposited securities represented by such depositary share are common stock or ordinary shares registered pursuant to Section 12 of the Exchange Act; and
- (2) the depositary shares were registered under the Securities Act of 1933 on Form F-6.

Accordingly,

IT IS ORDERED, pursuant to Section 6(h)(4) of the Exchange Act and Section 2(a)(1)(D)(v)(I) of the CEA, that the requirements specified in Sections 6(h)(3)(A) and

the security future, must comply with the other requirements and criteria specified in the Exchange Act and the CEA, respectively, and the listing standards requirements of the national securities exchange or national securities association.

(D) of the Exchange Act and the criteria specified in Sections 2(a)(1)(D)(i)(I) and (III) are modified, subject to the conditions set forth above.

By the Commodity Futures Trading Commission.

Catherine D. Dixon
Assistant Secretary

August 20, 2001

By the Securities and Exchange Commission.¹⁸

Jonathan G. Katz
Secretary

August 20, 2001

¹⁸ Chairman Pitt did not participate in this matter.