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## SECURITIES AND EXCHANGE COMMISSION

### 17 CFR Part 240

[Release No. 34-36580, International Series Release No. 900, File No. S7-34-95]

RIN 3235-AG68

#### Exemption of the Securities of the Federative Republic of Brazil, the Republic of Argentina, and the Republic of Venezuela Under the Securities Exchange Act of 1934 for Purposes of Trading Futures Contracts on Those Securities

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Proposed rule amendment and solicitation of public comments.

**SUMMARY:** The Commission proposes for comment an amendment to Rule 3a12-8 ("Rule") that would designate debt obligations issued by the Federative Republic of Brazil ("Brazil"), the Republic of Argentina ("Argentina"), and the Republic of Venezuela ("Venezuela") (collectively the "Proposed Countries") as "exempted securities" for the purpose of marketing and trading of futures contracts on those securities in the United States. The amendment is intended to permit futures trading on the sovereign debt of the Proposed Countries. This change is not intended to have any substantive effect on the operation of the Rule.

**DATES:** Comments should be submitted by January 19, 1996.

**ADDRESSES:** All comments should be submitted in triplicate and addressed to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. All comments should refer to File No. S7-34-95, and will be available for public inspection and copying at the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C.

**FOR FURTHER INFORMATION CONTACT:** James T. McHale, Attorney, Office of Market Supervision ("OMS"), Division of Market Regulation ("Division"), Securities and Exchange Commission (Mail Stop 5-1), 450 Fifth Street, N.W., Washington, D.C. 20549, at 202/942-0190.

## SUPPLEMENTARY INFORMATION:

### I. Introduction

Under the Commodity Exchange Act ("CEA"), it is unlawful to trade a futures contract on any individual security unless the security in question is an exempted security (other than a municipal security) under the Securities Act of 1933 ("Securities Act") or the Securities Exchange Act of 1934 ("Exchange Act"). Debt obligations of foreign governments are not exempted securities under either of these statutes. The Securities and Exchange Commission ("SEC" or "Commission"), however, has adopted Rule 3a12-8 under the Exchange Act to designate debt obligations issued by certain foreign governments as exempted securities under the Exchange Act solely for the purpose of marketing and trading futures contracts on those securities in the United States. As amended, the foreign governments currently designated in the Rule are Great Britain, Canada, Japan, Australia, France, New Zealand, Austria, Denmark, Finland, The Netherlands, Switzerland, Germany, the Republic of Ireland, Italy, Spain, and Mexico (the "Designated Foreign Governments"). As a result, futures contracts on the debt obligations of these countries may be sold in the United States, as long as the other terms of the Rule are satisfied.

The Commission today is soliciting comments on a proposal to amend Rule 3a12-8 (17 CFR 240.3a12-8) to add the debt obligations of Brazil, Argentina, and Venezuela to the list of Designated Foreign Government securities that are exempted by Rule 3a12-8. To qualify for the exemption, futures contracts on debt obligations of the Proposed Countries would have to meet all the other existing requirements of the Rule.

### II. Background

Rule 3a12-8 was adopted in 1984<sup>1</sup> pursuant to the exemptive authority in Section 3(a)(12) of the Exchange Act in order to provide a limited exception from the CEA's prohibition on futures overlying individual securities.<sup>2</sup> As

<sup>1</sup> See Securities Exchange Act Release Nos. 20708 ("Original Adopting Release") (March 2, 1984), 49 FR 8595 (March 8, 1984) and 19811 ("Original Proposing Release") (May 25, 1983), 48 FR 24725 (June 2, 1983).

<sup>2</sup> In approving the Futures Trading Act of 1982, Congress expressed its understanding that neither the SEC nor the Commodity Futures Trading Commission ("CFTC") had intended to bar the sale of futures on debt obligations of the United Kingdom of Great Britain and Northern Ireland to U.S. persons, and its expectation that administrative action would be taken to allow the sale of such futures contracts in the United States. See Original Proposing Release, *supra* note 1, 48 FR at 24725 (citing 128 Cong. Rec. H7492 (daily ed.

originally adopted, the Rule provided that the debt obligations of Great Britain and Canada would be deemed to be exempted securities, solely for the purpose of permitting the offer, sale, and confirmation of "qualifying foreign futures contracts" on such securities. The securities in question were not eligible for the exemption if they were registered under the Securities Act or were the subject of any American depositary receipt so registered. A futures contract on such a debt obligation is deemed under the Rule to be a "qualifying foreign futures contract" if the contract is deliverable outside the United States and is traded on a board of trade.<sup>3</sup>

The conditions imposed by the Rule were intended to facilitate the trading of futures contracts on foreign government securities in the United States while requiring offerings of foreign government securities to comply with the federal securities laws. Accordingly, the conditions set forth in the Rule were designed to ensure that, absent registration, a domestic market in unregistered foreign government securities would not develop, and that markets for futures on these instruments would not be used to avoid the securities law registration requirements. In particular, the Rule was intended to ensure that futures on exempted sovereign debt did not operate as a surrogate means of trading the unregistered debt.

Subsequently, the Commission amended the Rule to include the debt securities issued by Japan, Australia, France, New Zealand, Austria, Denmark, Finland, the Netherlands, Switzerland, Germany, Ireland, Italy, Spain, and, most recently, Mexico.<sup>4</sup>

September 23, 1982) (statements of Representatives Daschle and Wirth)).

<sup>3</sup> As originally adopted, the Rule required that the board of trade be located in the country that issued the underlying securities. This requirement was eliminated in 1987. See Securities Exchange Act Release No. 24209 (March 12, 1987), 52 FR 8875 (March 20, 1987).

<sup>4</sup> As originally adopted, the Rule applied only to British and Canadian government securities. See Original Adopting Release, *supra* note 1. In 1986, the Rule was amended to include Japanese government securities. See Securities Exchange Act Release No. 23423 (July 11, 1986), 51 FR 25996 (July 18, 1986). In 1987, the Rule was amended to include debt securities issued by Australia, France and New Zealand. See Securities Exchange Act Release No. 25072 (October 29, 1987), 52 FR 42277 (November 4, 1987). In 1988, the Rule was amended to include debt securities issued by Austria, Denmark, Finland, the Netherlands, Switzerland, and West Germany. See Securities Exchange Act Release No. 26217 (October 26, 1988), 53 FR 43860 (October 31, 1988). In 1992 the Rule was again amended to (1) include debt securities offered by the Republic of Ireland and Italy, (2) change the country designation of "West Germany" to the

Continued

### III. Discussion

The Chicago Mercantile Exchange ("CME") has proposed that the Commission amend Rule 3a12-8 to include the sovereign debt of the Proposed Countries.<sup>5</sup> The CME intends to develop a futures contract market in Brady bonds issued by the Proposed Countries.<sup>6</sup> Brady bonds are issued pursuant to the Brady plan which allows developing countries to restructure their commercial bank debt by issuing long-term dollar denominated bonds.<sup>7</sup> The Commission understands that Brady bonds issued by the Proposed Countries are currently traded primarily in the over-the-counter market in the United States.

Under the proposed amendment, the existing conditions set forth in the Rule (*i.e.*, that the underlying securities not be registered in the United States,<sup>8</sup> the futures contracts require delivery

"Federal Republic of Germany," and (3) replace all references to the informal names of the countries listed in the Rule with references to their official names. See Securities Exchange Act Release No. 30166 (January 6, 1992), 57 FR 1375 (January 14, 1992). In 1994, the Rule was amended to include debt securities issued by the Kingdom of Spain. See Securities Exchange Act Release No. 34908 (October 27, 1994), 59 FR 54812 (November 2, 1994). Finally, the Rule was amended to include the debt securities of Mexico. See Securities Exchange Act Release No. 36530 (November 30, 1995), 60 FR 62323 (December 6, 1995) ("Mexico Adopting Release").

<sup>5</sup> See Letter from William J. Brodsky, President and Chief Executive Officer, CME, to Arthur Levitt, Jr., Chairman, Commission, dated November 10, 1995 ("CME petition").

<sup>6</sup> The marketing and trading of foreign futures contracts is subject to regulation by the CFTC. In particular, Section 4b of the CEA authorizes the CFTC to regulate the offer and sale of foreign futures contracts to U.S. residents, and Rule 9 (17 CFR 30.9), promulgated under Section 2(a)(1)(A) of the CEA, is intended to prohibit fraud in connection with the offer and sale of futures contracts executed on foreign exchanges. Additional rules promulgated under 2(a)(1)(A) of the CEA govern the domestic offer and sale of futures and options contracts traded on foreign boards of trade. These rules require, among other things, that the domestic offer and sale of foreign futures be effected through the CFTC registrants or through entities subject to a foreign regulatory framework comparable to that governing domestic futures trading. See 17 CFR 30.3, 30.4, and 30.5 (1991).

<sup>7</sup> There are several types of Brady bonds, but "Par Bradys" and "Discount Bradys" represent the great majority of issues in the Brady bond market. In general, both Par Bradys and Discount Bradys are secured as to principal at maturity by U.S. Treasury zero-coupon bonds. Additionally, usually 12 to 18 months of interest payments are also secured in the form of a cash collateral account, which is maintained to pay interest in the event that the sovereign debtor misses an interest payment.

<sup>8</sup> The Commission notes that while no Brady bonds of Proposed Countries have been registered in the United States, certain sovereign debt issues of Argentina and Venezuela have been so registered. The trading of futures on U.S.-registered debt securities of Argentina and Venezuela would not be exempted under Rule 3a12-8 from the CEA's general prohibition on futures overlying individual securities.

outside the United States,<sup>9</sup> and the contracts be traded on a board of trade) would continue to apply.

In determining whether to amend the Rule to add new countries, the Commission has considered whether there is an active and liquid secondary trading market in the particular sovereign debt. There appears to be an active and liquid market in the debt instruments of the Proposed Countries. According to the CME, as of December 31, 1993, the total public and publicly guaranteed debt<sup>10</sup> of Brazil, Argentina, and Venezuela was approximately US\$86 billion, US\$55 billion, and US\$74 billion, respectively.<sup>11</sup> Moreover, the cash market for Brady bonds issued by the Proposed Countries evidences relatively active trading. Based on data provided by the CME, the total 1994 trading volume in the Brady bonds of Brazil, Argentina, and Venezuela was approximately US\$371 billion, US\$360 billion, and US\$320 billion, respectively.<sup>12</sup>

In light of the above data, the Commission believes preliminarily that the debt obligations of the Proposed Countries should be subject to the same regulatory treatment under the Rule as the debt obligations of the Designated Foreign Governments. Moreover, the trading of futures on the sovereign debt of Brazil, Argentina, and Venezuela should provide U.S. investors with a vehicle for hedging the risks involved in the trading of the underlying sovereign debt of the Proposed Countries.

In addition, the Commission preliminarily believes that the proposed amendment offers potential benefits for U.S. investors. If adopted, the proposed amendment would allow U.S. boards of trade to offer in the United States, and U.S. investors to trade, a greater range

<sup>9</sup> The CME's proposed futures contracts will be cash-settled (*i.e.*, settlement of the futures contracts will not entail delivery of the underlying securities). The Commission has recognized that a cash-settled futures contract is consistent with the requirement of the Rule that delivery must be made outside the United States. See Securities Exchange Act Release No. 25072 (October 29, 1987), 52 FR 42277 (November 4, 1987).

<sup>10</sup> Public debt is an external obligation of a public debtor, including the national government, a political subdivision (or any agency of either) and autonomous public bodies. Publicly guaranteed debt is an external obligation of a private debtor that is guaranteed for repayment by a public entity.

<sup>11</sup> See Letter from Carl A. Royal, Senior Vice President and Special Counsel, CME, to James T. McHale, Attorney, OMS, Division, Commission, dated November 30, 1995 (citing the World Bank's 1995 World Debt Tables as the source for this information) ("November 30 letter").

<sup>12</sup> See November 30 letter, *supra* note 11. As mentioned earlier, the Commission recently amended the Rule to include the debt securities of Mexico. The total 1994 trading volume in Mexican Brady bonds was approximately US\$282.3 billion. See Mexico Adopting Release, *supra* note 4.

of futures contracts on foreign government debt obligations. The Commission does not anticipate that the proposed amendment would result in any direct cost for U.S. investors or others. The proposed amendment would impose no recordkeeping or compliance burdens, and merely would provide a limited purpose exemption under the federal securities laws. The restrictions imposed under the proposed amendment are identical to the restrictions currently imposed under the terms of the Rule and are designed to protect U.S. investors.

Section 23(a)(2) of the Exchange Act requires the Commission in amending rules to consider potential impact on competition. Because the proposal is intended to expand the range of financial products available in the United States, the Commission preliminarily believes that the proposed amendment to the Rule will not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

### IV. Request for Comments

The Commission seeks comments on the desirability of designating the debt securities of the Proposed Countries as exempted securities under Rule 3a12-8. Comments should address whether the trading or other characteristics of the Proposed Countries' debt warrant an exemption for purposes of futures trading. Commentators may wish to discuss whether there are any legal or policy reasons for distinguishing between the Proposed Countries and the Designated Foreign Governments for purposes of the Rule. The Commission also solicits comments on the costs and benefits of the proposed amendment to Rule 3a12-8. Specifically, the Commission requests commentators to address whether the proposed amendment would generate the anticipated benefits, or impose any costs on U.S. investors or others. Finally, the Commission seeks comment on the general application and operation of the Rule given the increased globalization of the securities markets since the Rule was adopted.

### V. Regulatory Flexibility Act Certification

Pursuant to Section 605(b) of the Regulatory Flexibility Act, 5 U.S.C. § 605(b), the Chairman of the Commission has certified that the amendment proposed herein would not, if adopted, have a significant economic impact on a substantial number of small entities. This certification, including the reasons therefor, is attached to this release as Appendix A.

**VI. Statutory Basis**

The amendment to Rule 3a12-8 is being proposed pursuant to 15 U.S.C. §§ 78a et seq., particularly Sections 3(a)(12) and 23(a), 15 U.S.C. §§ 78c(a)(12) and 78w(a).

**List of Subjects in 17 CFR Part 240**

Reporting and recordkeeping requirements, Securities.

**VII. Text of the Proposed Amendment**

For the reasons set forth in the preamble, the Commission is proposing to amend Part 240 of Chapter II, Title 17 of the Code of Federal Regulations as follows:

**PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934**

1. The authority citation for part 240 continues to read in part as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78i, 78j, 78l, 78m, 78n, 78o, 78p, 78q, 78s, 78w, 78x, 78ll(d), 79q, 79t, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4 and 80b-11, unless otherwise noted.

\* \* \* \* \*

2. Section 240.3a12-8 is amended by removing the word "or" at the end of paragraph (a)(1)(xv), removing the "period" at the end of paragraph (a)(1)(xvi) and adding "; or" in its place, and adding paragraph (a)(1)(xvii), paragraph (a)(1)(xviii), and paragraph (a)(1)(xix) to read as follows:

**§ 240.3a12-8 Exemption for designated foreign government securities for purposes of futures trading.**

- (a) \* \* \*
- (1) \* \* \*
- (xvii) the Federative Republic of Brazil;
- (xviii) the Republic of Argentina; or
- (xix) the Republic of Venezuela.

\* \* \* \* \*

By the Commission.  
Dated: December 13, 1995.

Jonathan G. Katz,  
*Secretary.*

Note: Appendix A to the Preamble will not appear in the Code of Federal Regulations.

**Appendix A—Regulatory Flexibility Act Certification**

I, Arthur Levitt, Jr., Chairman of the Securities and Exchange Commission, hereby certify, pursuant to 5 U.S.C. 605(b), that the proposed amendment to Rule 3a12-8 ("Rule") under the Securities Exchange Act of 1934 ("Exchange Act") set forth in Securities Exchange Act Release No. 36580, which would define government debt securities of Brazil, Argentina and Venezuela (collectively the "Proposed Countries") as exempted securities under the Exchange Act

for the purpose of trading futures on such securities, will not have a significant economic impact on a substantial number of small entities for the following reasons. First, the proposed amendment imposes no record-keeping or compliance burden in itself and merely allows, in effect, the marketing and trading in the United States of futures contracts overlying the government debt securities of the Proposed Countries. Second, because futures contracts on the sixteen countries whose debt obligations are designated as "exempted securities" under the Rule, which already can be traded and marketed in the U.S., still will be eligible for trading under the proposed amendment, the proposal will not affect any entity currently engaged in trading such futures contracts. Third, because the level of interest presently evident in this country in the futures trading covered by the proposed rule amendment is modest and those primarily interested are large, institutional investors, neither the availability nor the unavailability of these futures products will have a significant economic impact on a substantial number of small entities, as that term is defined for broker-dealers in 27 CFR 240.0-10 and to the extent that it is defined for futures market participants in the Commodity Futures Trading Commission's "Policy Statement and Establishment of Definitions of 'Small Entities' for Purposes of the Regulatory Flexibility Act."<sup>1</sup>

Dated: December 13, 1995.  
Arthur Levitt, Jr.,  
*Chairman.*  
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**DEPARTMENT OF STATE**

**22 CFR Part 89**

**Bureau of Economic and Business Affairs; Foreign Prohibitions on Longshore Work by U.S. Nationals**

[Public Notice No. 2314]

AGENCY: Department of State.  
ACTION: Proposed rule; extension of Comment Period.

**SUMMARY:** On November 24, 1995, the Department of State issued a proposed rulemaking regarding longshore work by foreign nationals in U.S. ports and waters. In response to requests from several interested parties, the Department is extending the deadline for comments by 30 days, from December 26, 1995 to January 26, 1996.

**DATES:** Interested parties are invited to submit comments in triplicate no later than January 26, 1996.

**ADDRESSES:** Comments may be mailed to the Office of Maritime and Land Transport (EB/TRA/MA), Room 5828,

<sup>1</sup>45 FR 18618 (April 30, 1982).

Department of State, Washington, D.C. 20520-5816.

**FOR FURTHER INFORMATION CONTACT:** Richard T. Miller, Office of Maritime and Land Transport, Department of State, (202) 647-6961.

**SUPPLEMENTARY INFORMATION:** On November 24, 1995, the Department of State issued a proposed rulemaking (60 FR 58026) updating the list of longshore work by particular activity, of countries where performance of such a particular activity by crewmembers aboard United States vessels is prohibited by law, regulation, or in practice in the country. The crews of ships registered in or owned by nationals of the countries on the list may not perform the activities enumerated on the list. Citing the need for more time to assess the full effects of the proposed rule, a number of parties have requested an extension of the comment period. Consequently, the Department will extend the deadline by 30 days, from December 26, 1995 to January 26, 1996.

(8 U.S.C. 1288, Pub. L. 010-649, 104 Stat. 4878)

Dated: December 14, 1995.  
Daniel K. Tarullo,  
*Assistant Secretary, Economic and Business Affairs, Department of State.*  
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**DEPARTMENT OF LABOR**

**Mine Safety and Health Administration**

**30 CFR Parts 18 and 75**

RIN 1219-AA65

**Requirements for Approval of Flame-Resistant Conveyor Belts**

AGENCY: Mine Safety and Health Administration, Labor.

ACTION: Proposed Rule; extension of comment period.

**SUMMARY:** In response to requests from the mining community for additional time in which to prepare comments, the Mine Safety and Health Administration (MSHA) is extending the period for public comment on its proposed rule addressing the requirements for approval of flame-resistant conveyor belts to be used in underground mines.

**DATES:** Written comments must be received on or before February 5, 1996.

**ADDRESSES:** Send comments to the Office of Standards, Regulations, and Variances, MSHA, Room 631, 4015 Wilson Boulevard, Arlington, Virginia 22203.