U.S. COMMODITY FUTURES TRADING COMMISSION
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Division of
Market Oversight

Vincent McGonagle
Director

Mr. Hyojae Cho
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Korea Exchange, Inc.
40 Munhyeongeumyung-ro
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Re: Request for No-Action Letter Under Section 2(a)(1)(C)(ii) and (iv) of the Commodity Exchange Act and CFTC Regulation 30.13

Dear Mr. Cho,

The Division of Market Oversight ("DMO") of the Commodity Futures Trading Commission (the "Commission" or "CFTC") is issuing this letter in response to a request received from the Korea Exchange, Inc. ("KRX") pursuant to Commission Regulation 140.99(a)(2).[1] In the letter, KRX requested assurance that DMO will not recommend enforcement action against KRX with respect to the offer or sale to persons located within the United States who are Qualified Institutional Buyers ("QIBs")[2] of Korea Composite Stock Price Index ("KOSPI") 200 Futures contracts or Mini KOSPI 200 Futures contracts (the "Contracts"). KRX requests that this no-action letter take effect on October 24, 2022, and continue until the earliest of: 1) when the Contracts are deemed certified pursuant to Commission Regulation 30.13; 2) when the Commission terminates its review or denies certification of the Contracts pursuant to Commission Regulation 30.13; or 3) November 24, 2023, (Korea time).

I. Background

KRX is the sole securities and derivatives exchange operating in the Republic of Korea. It also serves as the central counterparty for the futures and securities products KRX offers as well as certain swaps.[3] KRX's derivatives market offers twenty-six futures and options contracts,

[1] 17 C.F.R. § 140.99(a)(2) (governing requests for no-action letters).

[2] As defined in Rule 144A under the Securities Act of 1933.

[3] KRX is an exempt derivative clearing organization for the purpose of clearing certain swap transactions. *See* In the Matter of the Petition of Korea Exchange, Inc., For Exemption from Registration as a Derivatives Clearing Organization, Order of Exemption From Registration (Oct. 26, 2015), *available at* https://www.cftc.gov/PressRoom/PressReleases/7270-15.

including the Contracts. Specifications for the Contracts are attached to this letter as Appendix A. The KOSPI 200 Index is a capitalization-weighted securities index of 200 Korean stocks trading on KRX's securities market.

II. Governing Law

The Commodity Exchange Act ("CEA" or the "Act") section 2(a)(1)(C)(iv) generally prohibits any person from offering or selling a futures contract based on a security index in the U.S., except as permitted under CEA section 2(a)(1)(C)(ii) or CEA section 2(a)(1)(D).[4] CEA section 2(a)(1)(C)(ii) grants the CFTC "exclusive jurisdiction with respect to accounts, agreements . . . and transactions involving . . . [futures] contracts [on] a group or index of securities (or any interest therein or based upon the value thereof) . . ." subject to three conditions. Specifically, Congress authorized the CFTC to regulate a futures contract on a security index where:

(1) the contract is cash-settled;

(2) trading of the contract is not readily susceptible to manipulation; and

(3) such group or index of securities does not constitute a narrow-based security index.[5]

Commission Regulation 41.1(c) defines a broad-based security index as any index of securities that does not meet the definition of a narrow-based security index.[6] CEA section 1a(35)(A) defines a narrow-based security index as an index:

- That has 9 or fewer component securities;
- In which a component security comprises more than 30% of the index's weighting;
- In which the five highest weighted securities in aggregate comprise more than 60 percent of the index's weighting; or
- In which 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 $50,000,000 (or in the case of an index with 15 or more component securities, $30,000,000). . ..[7]

Upon request, the Commission may certify that a futures contract on a broad-based security index trading on a foreign board of trade conforms with CEA section 2(a)(1)(C)(ii).[8] Commission

[4] 7 U.S.C. § 2(a)(1)(C)(iv). CEA section 2(a)(1)(D) governs the offer and sale of security futures products, which are defined by CEA section 1a(44) as based on a "single security or narrow-based security index," and is not applicable to the extent the Contracts involve a broad-based security index. 7 U.S.C. § 2(a)(1)(D); 7 U.S.C. § 1a(44). By its terms, section 2(a)(1)(C)(iv) applies to security index futures contracts traded on both domestic and foreign boards of trade.

[5] 7 U.S.C. § 2(a)(1)(C)(ii).

[6] 17 C.F.R. § 41.1(c) ("[b]road-based security index means a group or index of securities that does not constitute a narrow-based security index"); 17 C.F.R. § 41.1(e) ("[n]arrow-based security index has the same meaning as in section 1a(35) of the Commodity Exchange Act").

[7] 7 U.S.C. § 1a(35)(A). CEA section 1a(35)(B) sets forth several exclusions from the definition of narrow-based security index, none of which are relevant here. 7 U.S.C. § 1a(35)(B).

[8] 17 C.F.R. § 30.13(a).

Regulation 30.13 sets forth the process for seeking such certification.[9] A submission seeking certification must include data, information, facts, and statements confirming that the subject contract conforms with section 2(a)(1)(C)(ii) of the Act.[10]

Commission Regulation 30.13 places no time limit on the Commission's standard certification review procedure. Under certain circumstances, however, a contract may be eligible for expedited review pursuant to Commission Regulation 30.13(e)-(f).[11] The expedited review procedure takes place over 45 days unless the Commission elects to extend its review for an additional 45 days where the request raises novel or complex issues that require additional time for review.[12] The submitting foreign board of trade may also request an extension of the review period.[13]

Indexes do not necessarily remain broad or narrow-based permanently – they may transition from narrow-based to broad-based and then back to narrow-based. Pursuant to Commission Regulation 41.14(b), "an index that is a narrow-based security index that becomes a broad-based security index for more than 45 business days over 3 consecutive calendar months shall continue to be a narrow-based index for the following 3 calendar months," providing market participants with time to adjust to applicable CFTC regulations.[14] Following this 3-month transition period, the index becomes broad-based, and "a national securities exchange may continue to trade only in those months in the security futures product that had open interest on the date the transition period ended."[15] As noted above, pursuant to Commission Regulation 30.13, products based on a broad-based security index trading on a foreign board of trade may receive Commission certification, and the Commission withdraws such certification when the underlying index becomes narrow-based.[16]

III. The KOSPI 200 Index

Staff granted KRX a no-action letter on November 26, 2008, with respect to the offer and sale of KOSPI 200 index futures contracts to persons within the United States.[17] The Commission certified the Mini KOSPI 200 futures contract under Commission Regulation 30.13(m) on August 1, 2017.[18] At the time that staff issued such no-action letter, as well as at the time that the Commission made such certification, the KOSPI 200 was a broad-based security index.

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[9] 17 C.F.R. § 30.13.

[10] 17 C.F.R. § 30.13(a)(2).

[11] 17 C.F.R. § 30.13(e)-(f).

[12] 17 C.F.R. § 30.13(g)-(h).

[13] 17 C.F.R. § 30.13(h)(2).

[14] 17 C.F.R. § 41.14(b)

[15] *Id*.

[16] 17 C.F.R. § 30.13(a).

[17] CFTC Staff Letter No. 08-20 (November 26, 2008), *available at* https://www.cftc.gov/LawRegulation/CFTCStaffLetters/letters.htm.

[18] Prior to the adoption of Commission Regulation 30.13, Commission staff provided foreign boards of trade a staff no-action letter confirming that a contract complied with CEA section 2(a)(1)(C)(ii). The substantive review under Commission Regulation 30.13 is the same as the prior no-action process. Foreign Futures and Options Contracts on a Non-Narrow-Based Security Index; Commission Certification Procedures, 76 Fed.Reg. 59241, 59242 (September 26, 2011).

The KOSPI 200 has transitioned between a narrow and broad-based security index on several occasions beginning in 2020. Specifically, the KOSPI 200 became a narrow-based security index on April 1, 2020. At that point, staff revoked its no-action letter, and the Commission revoked its certification. The KOSPI 200 became broad-based again, and KRX filed a request for expedited certification pursuant to Commission Regulation 30.13(e) on December 1, 2021. DMO staff issued no action relief to KRX during the pendency of its requests for certification of the KOSPI 200 Futures and Mini KOSPI 200 Futures contracts, and the contracts were deemed certified on January 18, 2022.

Most recently, the KOSPI 200 was recharacterized as a narrow-based security index on May 18, 2022. As a result, the Commission withdrew its existing certifications of the Contracts, and products based on the KOSPI 200 became subject to joint regulation by the CFTC and the Securities and Exchange Commission ("SEC") as foreign security futures products. Pursuant to an SEC Order[19] and related CFTC Advisory,[20] the only persons located within the United States permitted to trade the Contracts as foreign security futures products are QIBs.

KRX has represented to staff that the KOSPI 200 met the definition of a broad-based security index for greater than 45 days over three consecutive calendar months as of July 21, 2022, triggering a 3-month transition period pursuant to Commission Regulation 41.14(b) beginning on July 22, 2022.[21] The transition period ends on October 21, 222, and the KOSPI 200 is set to become a broad-based security index pursuant to Commission Regulation 41.14(b) on October 22, 2022. Because October 22, 2022, is a Saturday, October 24, 2022, is the first trading day following the KOSPI 200's recharacterization.

IV. Requested No-Action Letter

KRX has noted that a lag may exist between expiration of the requisite transition period under Commission Regulation 41.14(b) and when KRX secures certification of the Contracts pursuant to Commission Regulation 30.13. KRX has submitted this request for no-action to cover the period beginning on October 24, 2022, the first trading day after the KOSPI 200 is set to become a broad-based security index, until the Contracts are deemed certified.

KRX has requested a no-action letter as follows:

- Effective October 24, 2022 (Korea time), all KOSPI 200 futures contracts and Mini KOSPI 200 futures contracts (regardless of contract month, including all contract

[19] Order under section 36 of the Securities Exchange Act of 1934 Granting an Exemption from Exchange Act Section 6(h)(1) for Certain Persons Effecting Transactions in Foreign Security Futures and under Exchange Act Section 15(a)(2) and Section 36 Granting Exemptions from Exchange Act Section 15(a)(1) and Certain Other Requirements, (Release No. 34-60194; International Series Release No. 1311) (June 30, 2009), *available at* https://www.sec.gov/rules/exorders/2009/34-60194.pdf.

[20] Division of Clearing and Intermediary Oversight Advisory Concerning the Offer and Sale of Foreign Security Futures Products to Customers Located in the U.S. (June 8, 2010), *available at* https://www.cftc.gov/sites/default/files/idc/groups/public/@internationalaffairs/documents/ssproject/fsfpadvisory.pdf.

[21] 17 C.F.R. § 41.14(b).

months listed before or after October 24, 2022) may be offered or sold to U.S. persons that are QIBs while the certification is pending at the Commission. [22]

- The relief would expire upon the earlier of: (a) the Commission issuing a notice of certification of the KOSPI 200 Futures contracts and the Mini KOSPI 200 Futures contracts as being based upon a non-narrow based index (which certification would allow the offer and sale of KOSPI 200 Futures contracts and Mini KOSPI 200 Futures contracts to all U.S. persons (not just QIBs)); (b) a determination by the Commission to terminate its review of or deny the request for certification of the Contracts pursuant to Commission regulation 30.13; or (c) November 24, 2023 (Korea Time).

As a condition of receiving the letter, KRX represents as follows:

- KRX will submit its request for expedited review and certification to the CFTC pursuant to CFTC Regulation 30.13(e) on or around October 24, 2022. KRX will promptly respond to Division or Commission requests for additional information regarding the Contracts.

- KRX will abide by all provisions of Commission Regulation 30.13 during the pendency of its requests for certification, including, but not limited to, informing Division staff of any changes in the material facts and representations provided in the request for certification pursuant to Commission Regulation 30.13(l).

V. No-Action Letter

Based on the representations presented by KRX to DMO as discussed above, DMO will not recommend that the Commission take enforcement action against KRX with respect to the offer or sale of the Contracts to persons located within the United States[23] while the Commission's review of KRX's forthcoming request for certification of the Contracts pursuant to Commission Regulation 30.13 is pending. This no-action letter is subject to the following conditions:

- KRX must submit a materially complete request for certification under Commission Regulation 30.13 for the Contracts on October 24, 2022.[24]

- KRX must promptly respond to DMO or Commission requests for additional information regarding the Contracts.

[22] For avoidance of doubt, DMO understands this relief to include continued trading in contract months that had open interest before October 22, 2022.

[23] For avoidance of doubt, this letter extends to persons located within the United States and is not limited to QIBs located within the United States.

[24] For avoidance of doubt, this letter requires KRX to submit its materially complete request for certification pursuant to Commission Regulation 30.13 on or before October 24, 2022 absent exigent circumstances communicated to DMO staff prior to October 24, 2022.

- KRX will abide by all provisions of Commission Regulation 30.13 during the pendency of its requests for certification, including, but not limited to, informing DMO staff of any changes in the material facts and representations provided in the request for certification pursuant to Commission Regulation 30.13(l).[25]

This letter will become effective on October 24, 2022.

This letter will remain in effect with respect to the Contracts during the pendency of certification procedures under Commission Regulation 30.13, including any extensions of review under Commission Regulation 30.13(h), until the earliest of the following events:

- The Contracts are certified pursuant to Commission Regulation 30.13(d) or (g);
- The Commission terminates its review of the request for certification of the Contracts pursuant to Commission Regulation 30.13(b) or (i);
- The Commission denies the request for certification of the Contracts pursuant to Commission Regulation 30.13(j); or
- April 24, 2023 (Korea time).

VI. Conclusion

This letter, and the positions taken herein, represent only the views of DMO staff, and do not necessarily represent the positions or views of the Commission or of any other office or division of the Commission. This letter and the no-action positions taken herein are not binding on the Commission.[26] The positions provided in this letter do not excuse persons relying on it from compliance with any other applicable requirements contained in the CEA, Commission regulations, or any other applicable laws (*i.e.*, securities laws). Further, this letter, and the positions taken herein, are based upon the facts and circumstances presented to DMO staff. Any different, changed, or omitted material facts or circumstances might render this letter void.

Finally, as with all staff letters, DMO retains the authority to condition further, modify, suspend, terminate, or otherwise restrict the terms provided herein, in its discretion.

If you have any questions concerning this correspondence, please contact Grey Tanzi, Assistant Chief Counsel, DMO, at (312) 596-0635 or gtanzi@cftc.gov; or Sebastian Pujol Schott, Senior Counsel and Policy Advisor to the Director, DMO, at (202) 418-5641 or sps@cftc.gov.

[25] 17 C.F.R. § 30.13(l).

[26] *See* 17 CFR § 140.99(a)(2) ("A no-action letter binds only the issuing Division… and not the Commission or other Commission staff.").

Sincerely,

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Vincent McGonagle
Director
Division of Market Oversight