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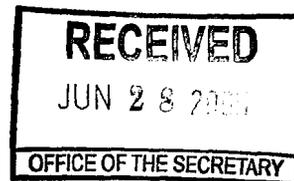
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June 28, 2005

4-505

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549



RE: Petition to Amend Rule 3a12-8 to Add the Republic of Korea

Dear Mr. Katz:

Please accept this letter and the attached draft of *Federal Register* notice as a petition under Rule of Practice 192 of the Securities and Exchange Commission to amend Rule 3a12-8 under the Securities Exchange Act of 1934 to include within its exemption the sovereign debt of the Republic of Korea, which is listed and traded as a futures contract on the Korea Exchange (KRX).

We have included with Ms. King's and Ms. Fraticelli's copy certain pertinent trading statistics. We, as a surrogate for KRX, stand ready to provide such additional information or explanation as the Commission may find of value.

Sincerely,

A handwritten signature in black ink, appearing to read "Philip McBride Johnson". The signature is fluid and cursive, with a long horizontal line extending to the right.

Philip McBride Johnson

cc: Elizabeth King, Esq.
Yvonne Fraticelli, Esq.
Division of Market Regulation

DRAFT FEDERAL REGISTER

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 34-_____, International Series Release No. _____, File No. [_____]]

RIN [_____]

Exemption of the Securities of the Republic of Korea under the Securities Exchange Act of 1934 for Purposes of Trading Futures Contracts on Those Securities

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission proposes for comment an amendment to Rule 3a12-8 that would designate debt obligations issued by the Republic of Korea as "exempted securities" for the purpose of marketing and trading futures contracts on those securities in the United States. The amendment is intended to permit futures trading on the sovereign debt of the Republic of Korea.

DATES: Comments should be submitted on or before [insert date thirty days after publication in Federal Register].

ADDRESSES: Comments may be submitted electronically or by paper. Electronic comments may be submitted by: (1) electronic form on the SEC website (<http://www.sec.gov>) or (2) e-mail to rule-comments@sec.gov. Mail paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549. All submissions should refer to file number []; this file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The

Commission will post all comments on the Commission's internet website (<http://www.sec.gov>). Comments are also available for public inspection and copying in the Commission's Public Reference Room, 100 F Street, N.E., Washington, DC 20549. We do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

FOR FURTHER INFORMATION CONTACT: Elizabeth King or Yvonne Fraticelli, Division of Market Regulation ("Division"), Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549, at 202/551-5600 and 202/942-0197, respectively.

SUPPLEMENTARY INFORMATION:

I. Introduction

Under the Commodity Exchange Act (CEA),¹ it is unlawful (absent compliance with section 2(a)(1)(D) thereof) 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)² or the Securities Exchange Act of 1934 (Exchange Act)³. 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 3a12-8⁴ (Rule) under the Exchange Act to designate debt obligations issued by certain foreign governments as exempted securities under the Exchange Act solely for

¹ 7 U.S.C. 1 et seq.

² 15 U.S.C. 77a et seq.

³ 15 U.S.C. 78a et seq.

⁴ 17 CFR 240.3a12-8.

the purpose of marketing and trading futures contracts on those securities in the United States. The foreign governments currently designated in the Rule are the United Kingdom of Great Britain and Northern Ireland, Canada, Japan, Australia, France, New Zealand, Austria, Denmark, Finland, the Netherlands, Switzerland, Germany, the Republic of Ireland, Italy, Spain, Mexico, Brazil, Argentina, Venezuela, Belgium, and, most recently, the Kingdom of Sweden (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 is soliciting comments on a proposal to amend Rule 3a12-8 to add the debt obligations of the Republic of Korea (Korea) to the list of Designated Foreign Governments whose debt obligations are exempted by Rule 3a12-8. To qualify for the exemption, futures contracts on the debt obligations of Korea would have to meet all the other existing requirements of the Rule.

II. Background

Adopted in 1984 pursuant to exemptive authority contained in Section 3(a)(12) of the Exchange Act,⁵ Rule 3a12-8 provides a limited exception from the CEA's prohibition (absent compliance with section 2(a)(1)(D) thereof) on futures overlying individual securities.⁶ As originally adopted, the Rule provided that the debt obligations of the

⁵ See Securities Exchange Act Release No. 20708 (Original Adopting Release) (March 2, 1984), 49 FR 8595 (March 8, 1984); Securities Exchange Act Release No. 19811 (Original Proposing Release) (May 25, 1983), 48 FR 24725 (June 2, 1983).

⁶ 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

United Kingdom of Great Britain and Northern Ireland 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 the covered debt obligation under the Rule is deemed to be a "qualifying foreign futures contract" if the contract is deliverable outside the United States and is traded on a board of trade.⁷

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.⁸

Original Proposing Release, *supra* note 5, 48 FR at 24725 (citing 128 Cong. Rec. H7492 (daily ed. September 23, 1982) (statements of Representatives Daschle and Wirth)).

⁷ 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).

⁸ The CFTC regulates the marketing and trading of foreign futures contracts. CFTC rules provide that any person who offers or sells a foreign futures contract to a U.S. customer must be registered under the CEA, unless otherwise specifically exempted.

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, Mexico, Brazil, Argentina, Venezuela, Belgium and, most recently, the Kingdom of Sweden.⁹

III. Discussion

The Korea Exchange (KRX) has proposed that the Commission amend Rule 3a12-8 to include the sovereign debt of the Republic of Korea. The Applicant has stated that futures contracts on Korean Treasury Bonds (KTB) have traded since 1999 (3-year KTB) and 2003 (5-year KTB), respectively, and that its Petition for Rulemaking to amend Rule 3a12-8 is made principally to permit the lawful marketing of those contracts

⁹ 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 "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 8, 1992), 57 FR 1375 (January 14, 1992). In 1994, the Rule was amended to include debt securities issued by Spain. See Securities Exchange Act Release No. 34908 (October 27, 1994), 59 FR 54812 (November 2, 1994). In 1995, 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). In 1996, the Rule was amended to include debt securities issued by Brazil, Argentina, and Venezuela. See Securities Exchange Act Release No. 36940 (March 7, 1996), 61 FR 10271 (March 13, 1996). In 1999, the Rule was amended to include debt securities issued by Belgium and the Kingdom of Sweden. See Securities Exchange Act Release No. 41116 (February 26, 1999), 64 FR 10564 (March 5, 1999); Securities Exchange Act Release No. 41453 (May 26, 1999), 64 FR 29550 (June 2, 1999).

to U.S. investors. The Applicant further represents that the Treasury Bureau of the Ministry of Finance and Economy - a government office authorized by the law to issue and manage government debt – agrees to the Applicant's request for the amendment of Rule 3a12-8.

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, were delivery to occur it would take place outside the United States,¹⁰ and the contracts be traded on a board of trade) would continue to apply. The Applicant has represented that the securities underlying the futures contracts it intends to list are not registered in the United States, that delivery of KTB is not permissible under the futures contracts (cash settlement is substituted), and that the KRX is a "board of trade" as defined by the CEA.

When amending the Rule to include Belgium, the Commission stated that it would consider two types of evidence about whether there was an active and liquid secondary trading market for the security -- credit rating (as indirect evidence) and trading data.¹¹ Earlier, when amending the Rule to include Mexico, Brazil, Argentina, and Venezuela, the Commission considered primarily whether market evidence indicated that an active and liquid secondary trading market exists for the sovereign debt of those countries.¹² Prior to the addition of those countries to the Rule, the Commission

¹⁰ A number of Korean government debt securities have been registered under the Securities Act. The Rule does not exempt futures contracts on those securities.

¹¹ See Securities Exchange Act Release No. 41116 (February 26, 1999) 64 FR 10564 (March 5, 1999).

¹² See, e.g., Securities Exchange Act Release No. 36530 (November 30, 1995) 60 FR 62323 (December 6, 1995) (amending the Rule to add Mexico because the Commission believed that as a whole, the market for Mexican sovereign debt was sufficiently liquid and deep for the purposes of the Rule); Securities Exchange Act Release No. 36940

considered principally whether the particular sovereign debt had been rated in one of the two highest rating categories¹³ by at least two nationally recognized statistical rating organizations (NRSROs).¹⁴

The Commission has been advised that Korea does not presently satisfy the credit rating standard.¹⁵ However, the Commission also observes that market data indicates that there exists an active and liquid secondary trading market for the sovereign debt of the Republic of Korea (the "Relevant Bonds").¹⁶ At the end of 2002, total Relevant Bonds

(March 7, 1996) 61 FR 10271 (March 13, 1996) (amending the Rule to add Brazil, Argentina and Venezuela because the Commission believed that the market for the sovereign debt of those countries was sufficiently liquid and deep for the purposes of the Rule).

¹³ The two highest categories used by Moody's Investor Services (Moody's) for long-term debt are "Aaa" and "Aa." The two highest categories used by Standard and Poor's (S&P) for long-term debt are "AAA" and "AA."

¹⁴ See, e.g., Securities Exchange Act Release No. 30166 (January 6, 1992) 57 FR 1375 (January 14, 1992) (amending the Rule to include debt securities issued by Ireland and Italy -- Ireland's long-term sovereign debt was rated Aa3 by Moody's and AA- by S&P, and Italy's long-term sovereign debt was rated Aaa by Moody's and AA+ by S&P); and Securities Exchange Act Release No. 34908 (October 27, 1994) 59 FR 54812 (November 2, 1994) (amending the Rule to include Spain, which had long-term debt ratings of Aa2 from Moody's and AA from S&P); see also Securities Exchange Act Release No. 36213 (September 11, 1995) 60 FR 48078 (September 18, 1995) (proposal to add Mexico to list of countries encompassed by the Rule); Securities Exchange Act Release No. 24428 (May 5, 1987) 52 FR 18237 (May 14, 1987) (proposed amendment, which was not implemented, that would have extended the Rule to encompass all countries rated in one of the two highest categories by at least two NRSROs).

¹⁵ Applicants state that Relevant Bonds are rated by Moody's at A3 for long-term local currency bonds and A3 for long-term foreign currency bonds, while they are rated by Standard & Poor's at A+ and A- respectively.

¹⁶ The Commission is advised by the KRX that KTBs accounted for 89%, 88% and 95% of all Korean government bond trading (by US\$ value) in the years 2002, 2003 and 2004, respectively.

outstanding were equivalent to approximately US\$ 56 billion.¹⁷ At the end of 2003 and 2004, Relevant Bonds outstanding were US\$ 81 billion and US\$ 123 billion, respectively. The number of Relevant Bond transactions exceeded 83,400 (in 2002), 138,700 (in 2003) and 236,100 (in 2004).

The KRX has also provided the Commission with the following turn-over statistics. The average daily trading volume in Relevant Bonds was US\$ 2.95 billion in 2002, US\$ 5.01 billion in 2003, and US\$ 8.47 billion for 2004. The Applicant adds that there were \$721 billion in Relevant Bond volume in 2002, \$1,238 billion in 2003, and \$2,110 billion in 2004.

In light of the above data, the Commission preliminarily believes that Korea's sovereign debt should be subject to the same regulatory treatment under the Rule as the debt obligations of the Designated Foreign Governments.

IV. General Request for Comments

The Commission seeks comments on the desirability of designating the debt securities of Korea as exempted securities under Rule 3a12-8. Comments should address whether the trading or other characteristics of Korea's sovereign 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 Korea and the Designated Foreign Governments for purposes of the Rule. The Commission also requests information regarding the potential impact of the proposed rule on the U.S. economy on an annual basis. If possible, commenters should provide empirical data to support their views. The Commission also seeks comments on the general application and operation of

¹⁷ The rate of exchange used to calculate values was 1,001.8 Korean won for each U.S. dollar, as in effect on April 30, 2005.

the Rule given the increased globalization of the securities markets since the Rule was adopted.

V. Costs and Benefits of the Proposed Amendments

The Commission has considered the costs and benefits of the proposed amendment to the Rule and preliminarily believes that the proposed amendment offers potential benefits for U.S. investors, with no direct costs. If adopted, the proposed amendment would allow U.S. and foreign boards of trade to offer in the United States, and U.S. investors to trade, a greater range of futures contracts on foreign government debt obligations. Consistent with Congressional support for futures on foreign sovereign debt securities, the trading of futures on the sovereign debt of Korea should provide U.S. investors with a vehicle for hedging the risks involved in the trading of the underlying sovereign debt of Korea. The Commission does not anticipate that the proposed amendment would result in any direct cost for U.S. investors or others because the proposed amendment would impose no record-keeping 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. The Commission requests comments on the costs and benefits of the proposed amendment to Rule 3a12-8. In particular, 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.

VI. Effect of the Proposed Amendment on Competition, Efficiency and Capital Formation

Section 23(a)(2) of the Exchange Act¹⁸ requires the Commission, in adopting rules under the Exchange Act, to consider the competitive effect of such rules, if any, and to refrain from adopting a rule that would impose a burden on competition not necessary or appropriate in furthering the purposes of the Exchange Act. Moreover, Section 3 of the Exchange Act,¹⁹ as amended by the National Securities Markets Improvement Act of 1996,²⁰ provides that whenever the Commission is engaged in a rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission must consider, in addition to the protection of investors, whether the action will promote efficiency, competition and capital formation.

In light of the standards cited in Sections 3 and 23(a)(2) of the Exchange Act, the Commission preliminarily believes that the proposed amendment to the Rule will promote efficiency, competition and capital formation. The proposal is intended to expand the range of financial products available in the United States, and will make available to U.S. investors an additional product to use to hedge the risks associated with the trading of the underlying sovereign debt of Korea. Insofar as the proposed amendment contains limitations, they are designed to promote the purposes of the Exchange Act by ensuring that futures trading on government securities of Korea is consistent with the goals and purposes of the federal securities laws by minimizing the impact of the Rule on securities trading and distribution in the United States.

¹⁸ 15 U.S.C. 78w(a)(2).

¹⁹ 15 U.S.C. 78c.

²⁰ Pub. L. No. 104-290, 110 Stat. 3416 (1996).

The Commission requests comments as to whether the amendment to the Rule will have any anti-competitive effects.

VII. Administrative Requirements

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. We encourage written comments on the Certification. Commentators are asked to describe the nature of any impact on small entities and provide empirical data to support the extent of the impact.

The Paperwork Reduction Act does not apply because the proposed amendment does not impose recordkeeping or information collection requirements, or other collections of information that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, et seq.

VIII. 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.

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, 77z-2, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78f, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78o, 78p, 78q, 78s, 78u-5, 78w, 78x, 78ll(d), 78mm, 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)(xx), removing the period at the end of paragraph (a)(1)(xxi) and adding "; or" in its place, and adding paragraph (a)(1)(xxii), to read as follows:

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

(a) * * *

(1) * * *

(xxii) the Republic of Korea.

* * * * *

Jonathan G. Katz

Secretary

Dated: _____

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

Appendix A

Regulatory Flexibility Act Certification

I, William H. Donaldson, 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), which would define the government debt securities of the Republic of Korea (Korea) 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 Korea. Second, because futures contracts on the twenty-one countries whose debt obligations are designated as "exempted securities" under the Rule, which already can be traded and marketed in the United States, 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 those primarily interested in trading such futures contracts 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 17 CFR 240.0-10.

William H. Donaldson

Chairman

Dated: _____