cases, in the absence of such a comprehensive surveillance sharing agreement, the Commission believes that it would be difficult to conclude that an exchange listing a derivative product, such as a DAX Index warrant, would be able to monitor effectively trading involving the derivative product. Indeed, in commenting on the DTB's application to offer and sell DAX Index futures to U.S. persons, the Commission relied, in part, on the existence of a surveillance sharing agreement between the FSE and the DTB.²⁴

With regard to the Amex and CBOE proposals, the Commission would prefer that comprehensive surveillance agreements be in place, and believes that such agreements play a particularly important role in ensuring the integrity of global securities markets. The Deutsche Börse AG, however, terminated license and market surveillance agreements between the FSE and the Exchanges as part of a now completed strategic review relating to competitive concerns surrounding the trading of the DAX Index products by the Exchanges.²⁵ Since completion of the strategic review, the Deutsche Börse AG has decided to commence active negotiations with the Exchanges regarding their listing and trading of DAX Index warrants and for the purpose of entering into new market surveillance sharing agreements.²⁶ The Commission views these new efforts favorably, and believes that a major market such as the FSE should readily enter into comprehensive surveillance sharing agreements.²⁷ Even in the absence of such agreements, however, the Commission does not believe that the Exchanges' proposals should continue to be detained pending the conclusion of these negotiations when an alternative with respect to obtaining

²⁵ See July 19 Letter, *supra* note 4. The commenters stated that ''[b]ecause of the amount of work and discretion involved in maintaining the DAX Index, under both federal and state law, [the FSE] has a proprietary interest in its Index, which vests it with the exclusive right to license its use for trading in stock index products.'' *See* Comment Letters, *supra* note 4.

²⁶ See July 19 Letter, supra note 4.

²⁷ Ideally, such agreements should be broad in nature rather than designed to cover a specific product, such as DAX Index warrants. The absence of broad surveillance agreements slows down the introduction of new international products by forcing the relevant exchanges to amend productspecific surveillance sharing agreements every time a new product is introduced.

surveillance information exists for the DAX Index products. Specifically, the U.S. Department of State and the German Foreign Office have exchanged Diplomatic Notes that provide a framework for mutual assistance in investigatory and regulatory matters ("Diplomatic Notes").28 The Diplomatic Notes confirm that the Commission is qualified to obtain assistance through the German Ministry of Justice under German law. Based on the existence of the Diplomatic Notes, the Commission believes that the German governmental authorities are committed to assistance in addressing cross-border fraud. In addition, the Commission could obtain from the German Ministry of Justice (and vice versa) information similar to that which would be available in the event that a comprehensive surveillance sharing agreement were executed between the FSE and the Amex and the CBOE with respect to transactions in FSE-traded stocks related to DAX Index warrant transactions on the Amex and the CBOE.29 While this arrangement would certainly be enhanced by the existence of comprehensive surveillance sharing agreements, it is nonetheless consistent with other instances where the Commission has explored alternatives to direct exchange-toexchange surveillance sharing agreements where the relevant foreign exchange was unwilling or unable to enter into a comprehensive surveillance sharing agreement.30

In addition, the Commission notes that there are factors relating to the computation of the DAX Index that further support reliance on arrangements other than direct exchange-to-exchange surveillance agreements. Specifically, the size of the market for the securities underlying the DAX Index makes it less likely that the proposed Index warrants are readily susceptible to manipulation.³¹ For

³⁰ See, e.g., Letter to David R. Merrill, Deputy General Counsel, CFTC, from Brandon Becker, Director, Division, Commission, dated April 20, 1994 (Commission comment letter to the CFTC regarding the offer by the Osaka Securities Exchange of futures contracts based on the Nikkei 300 Index to U.S. persons), and letter to Joanne T. Medero, General Counsel, CFTC, from William H. Heyman, Director, Division, Commission, dated January 16, 1992 (Commission comment letter to the CFTC regarding the offers by the Osaka Stock Exchange and the Tokyo Stock Exchange of futures contracts based on the Nikkei 225 and TOPIX Indexes to U.S. persons).

³¹ In evaluating the manipulative potential of a proposed index derivative product, as it relates to

example, as of December 2, 1994, the market capitalization of the securities in the Index ranged from a low of approximately U.S. \$841 million to a high of approximately U.S. \$36 billion, and the average trading volume for individual Index component securities during the period from June 1, 1994, through November 30, 1994, ranged from a low of 59,408 shares per day to a high of over one million shares per day.

day. The Commission continues to believe strongly that the existence of comprehensive surveillance sharing agreements between the appropriate German entity(ies) 32 and each of the Exchanges would be important measures to deter and detect potential manipulations or other improper or illegal trading involving DAX Index warrants. Accordingly, the Commission urges the German parties and the Exchanges to continue in their present negotiations with the goal of finalizing formal comprehensive surveillance sharing agreements covering DAX Index warrants and the securities contained in the DAX Index as soon as practicable.33

D. Commission Response to Comment Letters

The comment letters received by the Commission in response to the proposed rule changes raise two issues—one concerning the potential for manipulation as a result of the lack of surveillance sharing agreements between the American and German exchanges, and the other concerning the FSE's intellectual property rights in the DAX Index and the DAX name.³⁴

As stated above, the Commission believes that, even though new surveillance sharing agreements between the Deutsche Börse AG and the Exchanges have not yet been finalized, the Diplomatic Notes provide, in the interim, both the Commission and the German Ministry of Justice with the ability to obtain and share information necessary, among other things, to investigate suspected attempts at manipulation of the trading of DAX

³² This would probably be the FSE and/or the Deutsche Börse AG. See July 19 Letter, supra note 4

³³ See supra notes 23 and 27.

including, among other things, the identity of the ultimate purchasers and sellers of securities.

²⁴ See Letter to Elisse B. Walter, General Counsel, Commodity Futures Trading Commission ("CFTC"), from Brandon Becker, Director, Division of Market Regulation ("Division"), Commission, dated November 21, 1994.

²⁸ See International Series Release No. 691, 1994 SEC LEXIS 2324 (July 22, 1994).

²⁹ It is the Commission's expectation that this information would include transaction, clearing, and customer information necessary to conduct an investigation relating to trading in DAX Index warrants or components of the DAX Index.

the securities that comprise the index and the index product itself, the Commission has considered several factors, including, among others, (1) the number of securities contained in the index or group, (2) the capitalizations of those securities, (3) the depth and liquidity of the group or index, (4) the diversification of the group or index, (5) the manner in which the index or group is weighted, and (6) the ability to conduct surveillance on the product. *See* Securities Exchange Act Release No. 31016 (August 11, 1992), 57 FR 37012 (August 17, 1992).

³⁴ See Section III, supra.