

CFTC Letter No. 01-20

March 26, 2001

No-Action

Division of Trading and Markets

Re: Rule 1.57 Request for No-Action Relief for IB Carrying Accounts with Non-Guarantor FCM

Dear:

This is in response to your letter dated February 21, 2001, to the Division of Trading and Markets ("Division") of the Commodity Futures Trading Commission ("Commission"). You request, on behalf of "X", a guaranteed introducing broker ("IB") of "Y", a registered futures commission merchant ("FCM"), relief permitting "Y" to provide execution but not clearing services for certain customers introduced by "X".

Based upon your representations, we understand the relevant facts to be as follows. "X", as "Y's" IB, introduces certain customers, all of whom are "Eligible Contract Participants,"¹ to "Y". Although "Y" will be providing execution services for these customers, it will not be clearing all such trades. "Y" will "give up" a large percentage of these trades to FCMs chosen by "X" customers. You represented that "X" will not receive any compensation from the other FCMs through which the transactions are cleared. In addition, "Y" is substantially capitalized and will have sufficient net capital to meet any obligations it may have to "X's" customers. Specifically, you represented that as of December 31, 2000, "Y" had net capital of \$107.4 million and excess net capital of \$69.6 million. Further, you note that the guarantee agreement "Y" has executed with "X" provides that "Y" accepts joint and several liability for all obligations under the Commodity Exchange Act (the "Act")² and the regulations thereunder with respect to the solicitation of, and transactions involving, all customer accounts of "X".

Commission Rule 1.57(a)(1)³ provides that an IB that has entered into a guarantee agreement with an FCM must open and carry customer accounts with such guarantor FCM on a fully-disclosed basis. Accordingly, in order to protect the customers of the IB, an FCM that has entered into a guarantee agreement with an IB must carry all of the customer accounts introduced by the IB.⁴

Based upon the foregoing, and consistent with prior positions taken by the Division in this area, the Division believes that granting your request would not be contrary to the "customer protection" objective of Rule 1.57(a)(1).⁵ This is based principally upon your representations as to the substantial capital held by "Y" and that the customers being referred are Eligible Contract Participants who have requested their trades be cleared by FCMs other than "Y".

Accordingly, based upon the above representations, the Division will not recommend that the

Commission take any enforcement action under rule 1.57(a)(1) against "X" or "Y" if "X" introduces to "Y" certain customers who employ "Y's" execution services but choose to clear their transactions through another FCM.

This letter, and the relief issued herein, is based upon the representations that have been made to us. Any different, changed, or omitted facts or conditions might render this letter void. In this regard, you must notify the Division immediately in the event the operations or activities of "X" or "Y" change in any material way from those represented to us. Further, this letter represents the position of this Division only and does not necessarily reflect the views of the Commission or any other division or office of the Commission.

If you have any questions concerning this correspondence, please contact Michael A.Piracci, an attorney on my staff, at (202) 418-5430.

Very truly yours,

John C. Lawton
Acting Director

¹ See Section 1a(12) of the Commodity Exchange Act for a definition of Eligible Contract Participants. 7 U.S.C. § 1a(12), *as amended by* Pub. L. No. 106-554, 114 Stat.2763.

² 7 U.S.C. § 1 *et seq.* (1994), *as amended by* Pub. L. No. 106-554, 114 Stat.2763.

³ 17 C.F.R. § 1.57(a)(1). Commission rules referred to herein are found at 17 C.F.R. Ch.1 (2000).

⁴ See 57 Fed. Reg. 23136, 23137 (June 2, 1992).

⁵ See, e.g., CFTC Interpretative Letter No. 96-7, [1994-1996 Transfer Binder] Comm. Fut. L. rep. (CCH) ¶ 26,609 (December 18, 1995).