

CFTC Letter No. 04-18**July 8, 2004****Interpretation****Division of Clearing and Intermediary Oversight**Re: Interpretation of Rule 1.35(a-1)(5)

Dear :

This is in response to your May 13, 2004 letter to the Division of Trading and Markets (“Commission”) of the Commodity Futures Trading Commission.^[1] By your correspondence, you requested an interpretation of Commission Rule 1.35(a-1)(5)(i)^[2] (“Rule 1.35(a-1)”), which governs post-trade allocation of bunched orders. In your letter and subsequent phone conversations, you stated that you have an employee, “A”, that is registered as an Associated Person (“AP”) of “B”, an Introducing Broker (“IB”). In addition to your employee’s position at “B”, your employee is also an exempt Commodity Trade Advisor (“CTA”), pursuant to Rule 4.14(a)(5) and 4.14(a)(10), to four exempt commodity pools.^[3] As an exempt CTA, your employee wishes to bunch orders and allocate trades at the end of the day. Therefore, you asked whether Rule 1.35 allows CTAs who are exempt from registration pursuant to Rule 4.14(a)(5) and (a)(10) to allocate bunched orders on a post-trade basis.

Commission Rule 1.35(a-1) allows bunched orders for eligible customers to be placed on a contract market without specific customer account identification either at the time of order placement or at the time of report of execution. On June 11, 2003, the Commission amended the rule to expand the availability of bunching, simplify the process, and clarify the respective responsibilities of account managers and FCMs.^[4] To expand the availability of bunching, the Commission amended Rule 1.35 to expand the class of account managers permitted to bunch orders. Specifically, the Commission expanded the definition to include CTAs who are exempt from registration or are excluded from registration by operation of law or rule.^[5] When the Commission announced the amendments to Rule 1.35, it stated that these CTAs exclusively service sophisticated customers and are thus are exempt from Commission registration. The Commission further stated in the release that associated persons and introducing brokers exempt from Commission registration pursuant to Rule 4.14(a)(3) and (6) were not “eligible account managers” allowed to allocate, post-execution, bunched orders.

As stated above, your employee is exempt from registration pursuant to Rule 4.14(a)(5) and Rule 4.14(a)(10). You have stated that your employee has not advised more than 15 persons during the preceding 12 months and has not held himself out generally to the public at a CTA. Rule 1.35(a-1)(5) includes as “eligible account managers”: “[a] commodity trading advisor registered with the Commission...or exempt from registration under the Act....” Thus, you have submitted that your employee is an “eligible

account manager” because the employee is an exempt CTA and an exempt CPO.

The Commission, in adopting Rule 1.35(a-1)(5), decided not to allow APs to be “eligible account managers.”^[6] However, as stated above, your AP is operating in his capacity as an exempt CTA, not as an AP. Therefore, he is an “eligible account manager” for the purposes of Rule 1.35(a-1).

This letter, and the interpretation provided herein, are based upon the representations that you have made to us. Any different, changed or omitted material facts or circumstances might render this interpretation void. The position taken in this letter does not excuse from compliance with any other requirements contained in the Act or Commission regulations promulgated thereunder, and in particular, the remaining provisions of Rule 1.35(a-1) and all applicable antifraud provisions of the Act and Commission regulations.

If you have any questions concerning this correspondence, please contact Lawrence B. Patent, Deputy Director of the Division of Clearing and Intermediary Oversight, at (202) 418-5439.

Very truly yours,

James L. Carley
Director

^[1] Your letter was addressed to the Division of Trading and Markets. The Commission reorganized in 2002 and the functions formerly performed by the Division of Trading and Markets, which has been eliminated, are now performed by two new Divisions, the Division of Clearing and Intermediary Oversight and the Division of Market Oversight.

^[2] 17 C.F.R. 1.35(a-1)(5) (2003).

^[3] Rule 4.14 provides several exemptions from registration as a CTA. Paragraph (a)(5) provides an exemption from registration as a CTA to a person exempt from registration as a commodity pool operator (“CPO”) who solely advises pools for which the person is exempt from CPO registration. Paragraph (a)(10) tracks the statutory exemption in Section 4m(1) of the Commodity Exchange Act and provides an exemption from CTA registration if a person has not advised more than 15 persons during the preceding 12 months and has not held himself out generally to the public at a CTA. One of the pools in question is managed by your employee acting in the capacity of a CPO and the appropriate Notice of Eligibility for CPO exemption has been filed, and the rest he advises solely as an exempt CTA. Based upon your correspondence, the members of the commodity pools are long-time acquaintances of your employee and are Qualified Eligible Persons under Commission Rule 4.7 (*see*, 17 C.F.R. §4.7(a)(1) (2003)). In addition, your employee has never held himself out generally to the public to be a CTA.

[\[4\]](#) 68 Fed. Reg. 34790 (June 11, 2003).

[\[5\]](#) *Id.* at 34791.

[\[6\]](#) IBs are allowed to bunch orders pursuant to a pre-execution or contemporaneous execution allocation scheme. *See*, 17 CFR Part 1, Appendix C (2002), 62 Fed. Reg. 25470 (May 8, 1997).