



U.S. COMMODITY FUTURES TRADING COMMISSION

Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581
Telephone: (202) 418-5977
Facsimile: (202) 418-5407
gbarnett@cftc.gov

Division of Swap Dealer and
Intermediary Oversight

Gary Barnett
Director

CFTC Letter No. 13-72
No-Action
December 18, 2013
Division of Swap Dealer and Intermediary Oversight

Charles F. Conner
President & CEO
National Council of Farmer Cooperatives
50 F Street, NW
Suite 900
Washington, DC 20001

**Re: No-Action Relief: Oral Recordkeeping at Certain Futures Commission Merchant
Agricultural Cooperative Branch Offices**

Ladies and Gentlemen:

This letter is in response to a November 27, 2013 letter received by the Division of Swap Dealer and Intermediary Oversight (“**Division**”) of the Commodity Futures Trading Commission (“**Commission**”) from the National Council of Farmer Cooperatives (“**NCFC**”) on behalf of two of its members, CHS Hedging, Inc. (“**CHS**”) and MID-CO Commodities, Inc. (“**MID-CO**”), both registered futures commission merchants (“**FCMs**”).

CHS and MID-CO serve a customer base comprised largely of physical commodity hedgers. As part of servicing their customers, they each have a network of branch offices embedded in locations such as cooperatively-owned grain elevators (“**co-ops**”), whose primary business is buying grain produced by their farmer customers. Each branch operation has a person who is an employee of the co-op, but is also registered as a branch manager and associated person (“**AP**”) of the FCM for the purpose of providing ancillary risk management services to the co-op’s local farmer customers.¹ When a member of the co-op decides to enter into a futures or options transaction, the local AP takes the order over the telephone or in person, creates a written record of the order, and relays it to the main office via the telephone or electronic order entry. Customer funds supporting the trade are sent to the main office, which is responsible for handling the customer funds, accounting, and other back office functions. If additional margin is required to cover a position at any particular time, the customer sends the funds directly to the main office. Telephone calls between the branch AP and the main office are

¹ These branch operations also include farm supply or marketing cooperatives. CHS’s branch office network currently consists of APs in 66 facilities located in 16 states. MID-CO has APs at 27 facilities in two states.

recorded by equipment installed at the main office, but calls between the branch AP and the customer are not recorded.²

Commission Regulation 1.35(a)(1) requires FCMs to record, among other things, all oral communications “provided or received concerning quotes, solicitations, bids, offers, instructions, trading, and prices that lead to the execution of a transaction in a commodity interest.”³ In response to comments asserting that the cost of implementing and maintaining an oral communication recording system would be overly burdensome for small entities, the Commission excluded from this requirement oral communications provided or received by a small introducing broker (“**Small IB**”), defined as an IB that has generated \$5 million or less in aggregate gross revenues from its activities as an IB over the preceding three years.⁴ In adopting this exclusion, the Commission recognized that, while Small IBs take customer orders, they lack a direct market interface that could affect market integrity and are unlikely to generate the volume of market activity that the Commission would expect could affect market integrity.⁵ The Commission did not exempt Small IBs from keeping written records of covered information given or received by telephone. For example, when a Small IB takes an order from a customer over the telephone, the Small IB is not required to record the call, but it is required to keep a written record of the order under Regulation 1.35(a)’s requirement to keep and maintain records of “all orders (filled, unfilled, or cancelled)” and “instructions” to place orders.⁶

NCFC states that the risk management services provided by the CHS and MID-CO branch operations account for a small percentage of the revenue generated by the local co-ops’ primary function of buying grain. Each branch office generates, on a yearly basis, gross revenues from its ancillary brokerage services ranging from less than \$1,000 per location to \$250,000 per location, with an average of \$20,000.⁷ NCFC represents that although the respective headquarters offices of CHS and MID-CO and certain of their branch offices record and retain oral communications in accordance with Regulation 1.35(a), certain of their branch offices do not record such oral communications (“**Non-Recording Branches**”). NCFC further represents that, given the low volume of the futures and options transactions handled by the Non-Recording Branches, the cost of installing and maintaining the equipment necessary to comply

² CHS is headquartered in Inver Grove Heights, MN and has offices in Kansas City, MO and Indianapolis, IN that service commercial clients in addition to farmers. Those offices, as well as the main office, record telephone conversations. MID-CO is headquartered in Bloomington, IL and has an office in Urbandale, IA that services commercial grain facility customers. Both the Bloomington and Urbandale offices record telephone conversations.

³ 17 CFR 1.35(a)(1).

⁴ 17 CFR 1.35(a)(1)(iii).

⁵ 77 Fed. Reg. 75523, 75529 (Dec. 21, 2012).

⁶ *Id.*

⁷ Given the ancillary nature of the brokerage services, each branch office generally has just one, and no more than two, registered APs, who are compensated directly by the FCM in the form of commissions split between the FCM and the branch office.

with the oral recording requirements at those locations is not economically feasible. NCFC therefore asks the Division to grant relief from Regulation 1.35(a)'s oral recording requirements for the Non-Recording Branches of CHS and MID-CO, where the aggregate gross revenues from their activities as APs fall within the Small IB exclusion, i.e., where such activities have generated \$5 million or less in aggregate gross revenues over the preceding three years. NCFC understands that an exclusion from the oral recording requirements would not exclude Non-Recording Branches from the other recordkeeping requirements of the Regulation, such as the requirements to keep and maintain written records of all orders and instructions to place orders. NCFC represents that, absent relief, risk management options for farmers and ranchers serviced by the branch locations will be reduced.

Based upon the representations made by NCFC, the Division believes that no-action relief is warranted. Accordingly, the Division will not recommend that the Commission take enforcement action against CHS or MID-CO, respectively, or against their respective Non-Recording Branches, for failure to comply with the oral recording requirements of Regulation 1.35(a)(1), provided that the following conditions are met:

- Each Non-Recording Branch has no more than two persons who are registered, or are required to be registered, as APs;
- All APs of the Non-Recording Branches are employees of the co-op;
- With respect to oral communications between each Non-Recording Branch and the headquarters office of the FCM, the FCM fully complies with the requirements of Regulation 1.35(a)(1);
- Each Non-Recording Branch complies with all other recordkeeping requirements of Regulation 1.35(a)(1);
- The headquarters office of the FCM handles all customer funds, accounting, and other back office functions; and
- The aggregate gross revenues over the preceding three years that are generated by all Non-Recording Branches from their activities as branch offices of the FCM do not exceed \$5 million in total.

This letter, and the positions taken herein, represent the view of the Division only, and do not necessarily represent the position or view of the Commission or of any other office or division of the Commission. As with all no-action letters, the relief issued by this letter does not excuse the affected persons from compliance with any other applicable requirements contained in the Act or in the Regulations issued thereunder. Further, this letter, and the relief contained herein, is based upon the information made available to the Division. Any different, changed or omitted material facts or circumstances might render this no-action relief void.

CHS and MID-CO

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Should you have any questions, please do not hesitate to contact the undersigned, or Frank Fisanich, Chief Counsel, at 202-418-5949, Ward Griffin, Associate Chief Counsel, at (202) 418-5425, or Marcia Blase, Special Counsel, at 202-418-5138, of my staff.

Very truly yours,

Gary Barnett
Director
Division of Swap Dealer and Intermediary Oversight

cc: Regina Thoele, Compliance
National Futures Association, Chicago

Jamila A. Piracci, OTC Derivatives
National Futures Association, New York