

Commodity Futures Archive - Selected materials, CFTC Interpretative Letter No. 75-20 (Registration of Futures Commission Merchants and Associated Persons Holding Proprietary Accounts), ¶20,119, Commodity Futures Trading Commission, (Dec. 5, 1975)

¶20,119. Commodity Futures Trading Commission, Office of the General Counsel, Trading and Markets. December 5, 1975. Staff reply in full text.

Registration: Futures Commission Merchants: Proprietary Accounts Trading Exemption: Common Corporate Control.— A futures commission merchant established solely to execute futures transactions for two business affiliates is not required to register under Section 4d of the Commodity Exchange Act. Reg. §1.7 (at ¶2134) of the Commodity Futures Trading Commission exempts from registration those futures commission merchants whose trading activity is limited exclusively to proprietary accounts. These accounts are defined in Reg. §1.3(y) (at ¶2128) as including accounts of business affiliates who along with the futures commission merchant are under common corporate control.

The CFTC staff, responding to an inquiry, found a corporate relationship wherein various foreign and domestic bank holding companies acted to exert direct and indirect control over the two entities seeking to trade futures contracts and the futures commission merchant set up to execute those trades.

Along with its decision not to recommend enforcement action for failure to register, the staff noted that all other Commission requirements apply to the registration-exempt futures commission merchant, especially recordkeeping. See ¶7025, "Registration" division.

Registration: Associated Persons: Proprietary Account Exemption for Futures Commission Merchant Extended.— Associated persons needed not register under Section 4k of the Commodity Exchange Act if their futures commission merchant is exempt from registration because of an exclusivity of trading in proprietary accounts of business affiliates.

The Commodity Futures Trading Commission staff stressed that the mere absence of registration of a futures commission merchant by reason of exemption does not excuse associated persons from their own registration. However, in this case where the officers of the futures commission merchant would deal solely with two proprietary accounts, the staff concluded that it would not recommend enforcement action.

See ¶7425, "Registration" division.

[CFTC Staff Reply]

This is in response to your letter to this Office dated August 8, 1975, concerning sections 4d and 4k of the Commodity Exchange Act, as amended ("Act"), as they apply to (ABC, Inc.) ("ABC") and certain of its officers. You have requested that this Office advise you of its position should (ABC) and certain of its officers not register under the Act as a futures commission merchant and associated persons, respectively.

Based upon your letter and your telephone conversation with this Office on August 15, 1975, we understand the facts to be as follows: (ABC) was formed in , 197 and is a wholly-owned subsidiary of (DEF, Inc.) ("DEF"), whose stock is listed on the American Stock Exchange and The London Stock Exchange. (DEF) owns all the outstanding shares (except directors' qualifying shares) of (GHI, Inc.) ("GHI"), a national banking association, as a result of which (DEF) is a bank holding company registered under the Bank Holding Company Act of 1956 ("Bank Act"). Approximately 29.6% of (DEF's) shares are owned by (JKL, Inc.) ("JKL"), a Swiss banking corporation, which is also a bank holding company registered under the Bank Act. All of (JKL's) outstanding shares are owned by (MNO, Inc.) ("MNO"), a foreign bank holding company which is also registered under the Bank Act. The stock of (MNO) is listed on The London Stock Exchange and the Luxembourg Stock Exchange. By virtue of its ownership of all of (JKL's) outstanding shares, (MNO) indirectly owns the 29.6% of (DEF's) outstanding shares directly owned by (JKL). (MNO) also owns directly, and indirectly through its ownership of all of the outstanding shares of two foreign companies, an aggregate of an addition 29.2% of (DEF's) outstanding shares. Accordingly, (MNO) directly and indirectly owns 58.8% of (DEF's) outstanding shares.

(ABC) was formed to undertake to become a member of various commodity exchanges in order to act on behalf of (GHI) and (JKL) in executing transactions on such exchanges. At the present time (ABC) has become or is approved to become, and is applying to become, a member of certain contract markets regulated by the Commission. (ABC) intends to obtain corporate membership privileges on each contract market through one of its officers who will become an individual member of such contract market. (ABC), acting through this officer, will accept and place orders for the

purchase and sale of commodity futures contracts solely from (GHI) and (JKL). Certain other officers of (ABC) will be responsible for supervising this officer's activities.

(GHI) and (JKL) have been active as dealers and traders in foreign exchange, gold and silver bullion, gold coins and United States silver coins for many years. A substantial portion of this activity includes the purchase and sale of contracts for future delivery of these commodities executed on various commodity exchanges. It is anticipated that (GHI) and (JKL) will place orders for the purchase and sale of such commodity futures contracts with (ABC). (GHI) and (JKL) will place such orders with (ABC) exclusively for their own respective beneficial account and will not solicit or accept such orders from any other person. For the purposes of engaging in commodity futures transactions, (GHI) and (JKL) will utilize their own respective general corporate funds. The sources of such funds will derive principally from (GHI) and (JKL's) equity and long-term debt capital fund, their deposits and, for (GHI), Federal funds purchased. Should a customer of (GHI) or (JKL) want to place an order with (GHI) or (JKL) to purchase or sell a commodity futures contract, (GHI) and (JKL) will not place such order with (ABC); rather (GHI) and (JKL) will refer the customer to a futures commission merchant which is registered with the Commission and which is not affiliated with (GHI) or (JKL).

Section 4d of the Act provides in part that it is unlawful for any person to engage as a futures commission merchant in soliciting orders or accepting orders for the purchase or sale of any commodity for future delivery on or subject to the rules of any contract market unless such person is registered with the Commission as a futures commission merchant. For purposes of your letter you have assumed that (ABC) will be acting for (JKL) and (GHI) as a futures commission merchant as defined in section 2(a)(1) of the Act. You refer, however, to section 1.7 of the regulations promulgated under the Act, which exempts from the Act's registration requirements those futures commission merchants who trade solely for proprietary accounts within the meaning of section 1.3(y) of the regulations promulgated under the Act.

Section 1.7 was amended and paragraph (y) of section 1.3 was added to the regulations in 1974 to exempt futures commission merchants, trading *solely* for proprietary accounts, from the registration requirements of section 4d of the Act because, in the view of the Commodity Exchange Authority, predecessor to the Commission, requiring the registration of such persons would not serve any useful purpose.¹ Section 1.3(y) defines a "proprietary account" to include a commodity futures trading account carried on the books and records of a corporation for "(vii) [a] business affiliate that directly or indirectly controls such ... corporation ..." or "(viii) [a] business affiliate that, directly or indirectly is controlled by or is under common control with, such ... corporation...."

With respect to (ABC's) trading for (GHI) you are of the view that "since both (GHI) and (ABC) are under the direct common control of (DEF)," (GHI's) account with (ABC) will represent a proprietary account of (ABC) within the meaning of section 1.3(y)(viii). With respect to (ABC's) trading for (JKL) you are of the view that "since ... (JKL) indirectly controls (ABC) through its 29.6% stock interest in (DEF)" and "(ABC) and (JKL) are directly and indirectly under the common control of (MNO)," (JKL's) account with (ABC) will also represent a proprietary account of (ABC) within the meaning of paragraphs (vii) and (viii) of section 1.3(y). You also maintain that since (ABC's) (JKL) and (GHI) accounts are proprietary accounts within the meaning of regulation 1.3(y) and since (ABC) will be trading solely for these accounts, (ABC) is exempt under section 1.7 from registering as a futures commission merchant.

Based upon the facts and your representations as to the control relationships referred to above and the provisions of sections 1.7 and 1.3(y) of the regulations cited above, this Office will not recommend any enforcement action to the Commission, based solely on the failure of (ABC) to register as a futures commission merchant under section 4d of the Act. We point out, however, that any different, changed, or omitted facts or representations might require a different conclusion. Furthermore, we remind you that section 1.7 exempts certain futures commission merchants from the registration requirements of the Act only and that a futures commission merchant so exempted remains subject to all other provisions of the Act and the rules and regulations promulgated thereunder, including particularly in this case, the recordkeeping requirements of the Act.

In your letter you maintain that if (ABC) is exempt from registering as a futures commission merchant by virtue of section 1.7 of the regulations, the officers of (ABC) engaged in the solicitation or acceptance of orders for (JKL) and (GHI), or in the supervision of persons so engaged, should not be required to register under section 4k of the Act as persons associated with a futures commission merchant.²

We wish to point out that section 4k of the Act requires the registration of all associated persons (other than registered floor brokers), regardless of whether their employing futures commission merchant is registered under the Act or is exempt from registration by virtue of section 1.7 of the regulations. However, based upon our understanding that the officers of (ABC), who are associated persons as described in section 4k of the Act, will be acting in such capacity solely for (ABC) with respect to its trading for (JKL) and (GHI), and based upon our position set forth above with respect to the registration of (ABC) as a futures commission merchant, this Office will not recommend any enforcement

action to the Commission based solely on the failure of such officers of (ABC) to register as associated persons under section 4k of the Act. We point out, however, that any different, changed, or omitted facts or conditions contrary to our understanding might require a different conclusion.

Footnotes

1 See 39 Fed. Reg. 28618 (August 9, 1974).

2 Section 4k of the Act provides in relevant part that:

It shall be unlawful for any person to be associated with any futures commission merchant ... as a partner, officer, or employee ..., in any capacity which involves (i) the solicitation or acceptance of customers' orders ... or (ii) the supervision of any person or persons so engaged, unless such person shall have registered under this Act, with the Commission ... and it shall be unlawful for any futures commission merchant ... to permit such a person to become or remain associated with him in any such capacity if such futures commission merchant ... knew or should have known that such person was not so registered....