

**Commodity Futures Archive - Selected materials, CFTC Interpretative Letter No. 76-13A (Registration of FCM's Trading London Options as Commodity Trading Advisors), ¶20,206, Commodity Futures Trading Commission, (Sep. 9, 1976)**

¶20,206. Commodity Futures Trading Commission, Office of General Counsel. (Released September 9, 1976).  
Correspondence in full text.

**Registration: Commodity Trading Advisor: Futures Commission Merchant Trading London Options: Reaffirmation of Position that Public Interest is Served by Requiring Registration.**— Trading in London options is not solely incidental to the business of a futures commission merchant and since the Commodity Futures Trading Commission requires options traders to register as commodity trading advisors, then an FCM trading options must register as an advisor. The Office of General Counsel reaffirmed its position that the public interest was served by requiring this registration for FCM's, particularly in the detection of fraudulent and deceptive practices.

See ¶4375, "Definitions" division; and ¶7625, "Registration" division.

**Commodity Trading Advisors: Disclosure of Futures Positions: FCM's Trading Options Registered as Advisors: No-Action Position on Disclosures.**— The CFTC Office of General Counsel will not recommend that action be taken against futures commission merchants registered as trading advisors because of their dealing in London options who do not disclose the futures positions of principals. It is believed that it is not currently in the public interest to require FCM's registered as advisors to disclose to their customers the futures positions of principals, especially where all other FCM's are not subject to such a requirement, and the exact form and content of such disclosures has not yet been promulgated by the Commission.

See ¶8575, "Reports—Records" division.

Re: Registration of Futures Commission Merchants as Commodity Trading Advisors—CFTC Interpretative Letter 76-13A

Dear [Sir]:

Reference is made to your letter of July 20, 1976, in which you request that this Office reconsider the views which it expressed in its Interpretative Letter 76-13, dated June 21, 1976 [see ¶20,174. CCH.], to the effect that your client, a registered futures commission merchant ("FCM"), which offers to its customers commodity options traded on a London commodity exchange cleared through ICCH, is a commodity trading advisor required to register under the Commodity Exchange Act, as amended ("Act"), 7 U. S. C. 1, *et seq.* We have reviewed your letter and letters and comments submitted by other interested persons in response to the published version of our letter (which did not identify your client).

This Office has re-examined its interpretation in light of your letter and those letters and comments. We wish to advise you that, except for the no action position taken with respect to commodity trading advisor disclosure requirements, as hereinafter set forth, we reaffirm our interpretation of June 21, 1976.

In reviewing the comments on our interpretation, we noted that several persons asserted that no additional public interest would be served by requiring an FCM to register as a commodity trading advisor. As we indicated in our letter, in Section 2(a)(1) of the Act, 7 U. S. C. §2 (Supp. IV, 1974), Congress did not grant FCMs an automatic exclusion from the commodity trading advisor definition; rather, it expressly provided that the exclusion would not apply if the services were rendered on a basis not solely incidental to the conduct of the FCM's business. While we fully comprehend the argument made that FCMs deal in various commodity related businesses on behalf of customers, for the reasons stated in our June 21, 1976 letter, we do not believe that the definition of an FCM contemplates, as an incidental part thereof, the options business. We find this particularly so in light of the express prohibition on options transactions contained in the Act prior to the 1974 Amendments, the Commission's authority granted by those amendments to prohibit or to condition commodity options transactions, and the provisions of Regulation 1.19 (which has not been repealed) which prohibit an FCM from underwriting commodity options.

Moreover, at least for the present, we believe that there is a public interest to be served by requiring FCMs which deal in options to register as commodity trading advisors. Section 4n(4)(A) of the Act, 7 U. S. C. 6n(4)(A) (Supp. IV, 1974), requires registered commodity trading advisors, upon request by the Commission, to submit samples or copies of their advice, publications, writings, reports and other similar materials distributed to clients and subscribers; a requirement not otherwise imposed on FCMs, even in light of Regulation 1.40. The Section 4n(4)(A) requirement, of course, assists

the Commission in the detection of fraudulent or deceptive practices prohibited by Section 4 of the Act, 7 U. S. C. 6 of (Supp. IV, 1974) and Regulation 30.01. Accordingly, since we believe that FCMs conducting an options business do not qualify for the statutory exclusion from the definition of commodity trading advisor contained in Section 2(a)(1), the public interest considerations set forth in Section 4n(4)(A) apply to these FCMs.

We have also evaluated the comments by various persons regarding the burdens which registration as a commodity trading advisor would impose on an FCM. In particular, we have examined the requirement of Section 4n(4)(B) of the Act, 7 U. S. C. 6n(4)(B) (Supp. IV, 1974), that all commodity trading advisors make full and complete disclosure to their subscribers and clients of all futures market positions taken or held by the individual principals of their organization. Several FCMs, with principals engaged in substantial hedging transactions in the market, cited the potential adverse consequences which disclosure of market positions in these circumstances would create. We find those comments convincing, particularly in light of our confidentiality responsibilities under Section 8 of the Act, 7 U. S. C. §12 (Supp. IV, 1974). As a result, we have decided to take a no action position on disclosure by FCMs which fall into the commodity trading advisor category.

This decision results in part from a recognition that the Act and the regulations thereunder do not presently require that an FCM which is not a commodity trading advisor make such disclosure to its customers and we do not believe such disclosure by FCMs to be in the public interest at this time. Moreover, uncertainty would be created by any other result since the Commission has not yet promulgated rules regarding the frequency, form and content of the disclosure required by Section 4n(4)(B).

You are aware that, apart from its general antifraud rule (17 C. F. R. 30.01), the Commission has not yet adopted rules or regulations as to whether it will prohibit, or the terms and conditions under which it will permit, the offer or sale of commodity option transactions specified in Section 4c(b) of the Act, 7 U. S. C. 6c(b) (Supp. IV, 1974). We are not unmindful that the Commission's Advisory Committee on Market Instruments has recommended that FCMs dealing in commodity options need not register in any other category with the Commission. However, this position was taken by the Advisory Committee in the context of full and complete regulation of the commodity options business by the Commission.

As the result of the foregoing, this Office has determined that (1) an FCM which engages in an options business should register as a commodity trading advisor and (2) pending the Commission's adoption of regulations under Section 4n(4)(B) and 4c(b) dealing with the issues referred to herein this Office will not recommend enforcement action to the Commission, based solely on the failure of an FCM which is registered as a commodity trading advisor under the Act to make the disclosures required by Section 4n(4)(B).

This position is, of course, an interim position, pending the Commission's adoption of options and commodity trading advisor regulations. At least two of the issues for Commission determination in adopting such regulations will be FCM registration in other categories and concomitant requirements for disclosure.

**[ Letter of Inquiry ]**

ATTENTION: Howard Schneider General Counsel

RE: Commodity Trading Advisors; Section 2(a)(1) of the Commodity Exchange Act, As Amended—Staff Interpretative Letter Number 76-13

Gentlemen:

Reference is made to your letter to this firm dated June 1, 1976 stating that you are of the opinion that our client, ..... (the "Company") is a commodity trading advisor required to register as such under the Commodity Exchange Act, as amended (the "Act"). On behalf of the Company, we hereby request that you reconsider your opinion as set forth in your June 21, 1976 letter. In this connection, we wish to state the following:

As you know, we are aware that the Commission has expressed the view that, generally, persons who are offering commodity options to the public are required to register with the Commission as commodity trading advisors. We are further aware that this view is based upon the Commission's presumption that "in connection with the offer and sale of a commodity option, such persons presumably will render advice or analyses with respect to the advisability of trading in a futures contract traded on a contract market and/or with respect to the "value of" or "concerning" the commodity underlying a cash commodity option or underlying the foreign futures contract which is the subject of the option." It is clear that were such advice or analyses rendered by an FCM "solely incidental to the conduct" of its business as such, such FCM would be exempt from registration under Section 4m by reason of the exclusionary language in Section 2(a)(1) of the Act. It is the position of the Company, a position in which we concur, that any rendering of advice or analyses by the Company in connection with its agency foreign commodity option business is, likewise, solely

incidental to the soliciting and accepting of orders for the purchase or sale of such commodity options.

We recognize that Section 2(a)(1) of the Act defines an FCM as a person engaged in certain activities on or subject to the rules of any contract market and that the foreign commodity exchanges or clearing houses involved, having not been designated by the Commission, do not come within the regulatory definition of "contract market". However, we believe that the statutory use of the limiting phrase "on or subject to the rules of any contract market" was inserted so as to limit the affirmative jurisdiction of the Commission. In other words, by reason of this statutory limitation, the Commission is precluded from imposing its jurisdiction over FCMs against persons engaged in soliciting or in accepting orders for the purchase or sale of any commodity for future delivery not on or subject to the rules of any contract market. However, should such a person in this latter category, for whatever reason, wish to register as an FCM and subject himself to all of the financial and other requirements and obligations of FCMs as provided in the Act and the rules and regulations promulgated thereunder, we do not believe that the Commission would deny such registration as an FCM solely by reason of the lack of contacts of such person with a contract market designated by the Commission. Thus, for example, should a member of a foreign board of trade determine to register with the Commission as an FCM and not as a commodity trading advisor, the result of which would be to impose substantially greater obligations on such person as an FCM as opposed to a commodity trading advisor, we believe that the Commission may well be constrained to grant such registration as an FCM, provided, of course, that such person met all other FCM requirements.

We believe that, a fortiori, the above reasoning applies to the instant case. Clearly, the Commission's view that, generally, persons who are offering commodity options to the public are required to register as commodity trading advisors, is premised upon the Commission's proper desire to subject such persons, who are not otherwise registered with the Commission, to be so registered in the public interest. The reason underlying the Commission's general view, we believe, is an attempt to secure regulation over such persons pending the adoption of definitive regulations dealing directly with persons engaged in the commodity options business. It is our view that the Commission's more basic intent to subject persons in the commodity options business to regulation might be better served were the Commission in a position to require all such persons to register as FCMs. Unfortunately, the present state of the law and regulations precludes the Commission from placing such an onerous burden upon persons engaged solely in commodity options business and, at the present time at least, requiring, generally, registration of such persons as commodity trading advisors is a viable alternative. In the instant case, the better satisfaction, in our opinion, of the Commission's underlying policy is available. In effect, the Company is willing to be "registered" as an FCM with respect to its agency commodity option, business. Such business is conducted in substantially the same manner as the Company conducts its agency business on contract markets. The benefits to the public, which are the foundations to the Act and the rules and regulations promulgated thereunder, which accrue by reason of the Company being registered as an FCM and a clearing member of principal contract markets may well be substantially in excess of any benefits to the public which would accrue merely by simple registration as a commodity trading advisor.

Since the "public interest" is the basis upon which the Act and the rules and regulations rest, the Company believes that its additional registration as a commodity trading advisor would serve no additional public interest purpose. The Company is already fully subject to the jurisdiction of the Commission and an additional denomination of the Company as a commodity trading advisor would protect the public no further than it is already protected by the Company's registration as an FCM.

We note, further, in line with our reasoning that the agency commodity options business transacted by the Company is essentially that of an FCM, but for not being on or subject to the rules of a contract market designated by the Commission, even looking at Section 4m of the Act, the Company does not in any manner hold itself out to the public as a trading advisor (except in the sense of such activities being solely incidental to its executing and accepting orders for customers and the like) and that the Company has no advisory clients, on the same basis. Accordingly, we believe that the exemptions set forth in Section 4m of the Act could very well be deemed applicable to the instant situation.

In light of the foregoing, we would appreciate your reconsidering the position taken in your June 21, 1976 letter. The Company believes that there are many FCMs in the United States which may be engaged in the foreign commodity option business and believes, further, that it would be unfair of the Commission to require the Company to register as a commodity trading advisor while not requiring similar registrations from other FCMs. We believe that the Company's position is fully consonant with the public interest and the regulatory framework which the Commission administers.

Should you have any further questions or comments on this matter, please do not hesitate to contact this office.