

CFTC Letter No. 97-43**June 9, 1997****Division of Trading & Markets**

Re: Rule 4.14(a)(6): Applicability To Introducing Brokers Who Trade Customer Commodity Interest Accounts Pursuant to Third-Party Trading Systems

Dear :

This is in response to your letter dated November 7, 1996 to the Division of Trading and Markets ("Division") of the Commodity Futures Trading Commission ("Commission"). In your letter, you request the Division's opinion as to the availability of the Rule 4.14(a)(6)¹ exemption from commodity trading advisor ("CTA") registration to your client, an introducing broker ("IB") who trades customer commodity interest accounts pursuant to signals generated by a commodity trading system developed and sold by a third party ("Third Party Advisor"). You contend that the registration status of the Third Party Advisor should not be relevant to the determination of whether the Rule 4.14(a)(6) exemption is available to a registered IB.

We believe the registration status of the Third Party Advisor is a relevant factor to consider in making a determination under Rule 4.14(a)(6). As the Division has stated, in making a determination under Rule 4.14(a)(6) it will consider all relevant facts in the context of the specific business concerned.²

Moreover, the Division believes that given the facts presented in your letter, it is unnecessary to determine the applicability of Rule 4.14(a)(6) since, in the circumstances you posit, the registered IB is likely to be acting in violation of the Commodity Exchange Act.³ Persons who develop and sell commodity trading systems are engaged in activities within the statutory definition of CTA.⁴ Thus, these persons will generally be required to register as CTAs unless they qualify for an exemption from the registration requirement. Persons who willfully aid or abet participation by unregistered persons in activities that require registration under the Act or who act in combination or concert with another person in such a violation may be held liable for resulting violations under Section 13(a) of the Act.⁵ In addition, an IB who fails to fully inform its customer that the Third Party Advisor with whom the customer is dealing is required to be registered but is not so registered may be violating the antifraud provisions of Sections 4b and 4o of the Act.⁶

This letter provides general guidance only. It is based upon the representations that you

have made to us. Any different, changed or omitted conditions might require us to reach different conclusions. The views expressed herein are those of the Division of Trading and Markets only and do not represent the views of the Commission or of any other office or division of the Commission. If you have any questions concerning this correspondence, please do not hesitate to contact me or Thomas E. Joseph, an attorney on my staff, at (202) 418-5430.

Very truly yours,

Susan C. Ervin

Chief Counsel

¹ Commission rules referred to herein are found at 17 C.F.R. Ch. I (1996). Rule 4.14(a)(6) exempts a person who is registered with the Commission as an IB from also registering as a CTA if such person's trading advice is "solely in connection with its business as an [IB]."

² See, e.g., CFTC Interpretative Letter No. 95-85, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,540, (October 12, 1995).

³ 7 U.S.C. § 1 et seq. (1994).

⁴ See, CFTC Interpretative Letter No. 95-68, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,498 at 43,232 (August 10, 1995)(persons who develop or sell commodity trading systems must register as a CTA).

⁵ See, In re Richardson Securities, Inc., [1980-1982 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,145 at 24,646 (CFTC Jan. 27, 1981) ("in order to violate § 13(a) . . . one must knowingly associate himself with an unlawful venture, participate in it as something he wishes to bring about and seek by his action to make it succeed.").

Depending upon the nature of the business relationship between an IB and an unregistered Third Party Advisor, the IB's dealings with the Third Party Advisor may also violate National Futures Association's Bylaw 1101. Bylaw 1101 states, in relevant part, that:

No Member may carry an account, accept an order or handle a transaction in commodity futures contracts for or on behalf of any non-Member of NFA, that is required to be registered with the Commission as an FCM, IB, CPO, CTA or LTM, and that is acting in respect to the account, order or transaction for a customer, a commodity pool or participant therein, a client of a commodity trading advisor, or any other person

6 7 U.S.C. §§ 6b and 6o (1994).

See, CFTC Interpretative Letter No. 96-77, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,821 (October 26, 1996) (registration status of parties with whom customers deal is a material fact and registrant may violate antifraud provisions of Act if it fails to inform customers that an unregistered third party with whom a customer is dealing is required to be registered).