

CFTC Letter No. 98-57**June 12, 1998****Division of Trading & Markets****Re: Section 4d: Request for IB Registration No-Action Position**

Dear :

This is in response to a letter from "A" dated January 16, 1996 to the Division of Trading and Markets ("Division") of the Commodity Futures Trading Commission ("Commission"), as supplemented by letters dated January 26, 1996, February 12, 1996, March 1, 1996, March 21, 1996, April 25, 1996, September 18, 1996, March 9, 1998, and May 22, 1998, as well as telephone conversations with Division staff. By "A's" letter, as supplemented, a request was made on behalf of "T", a registered introducing broker ("IB"), and certain agricultural elevator cooperatives ("Elevators"), for relief from the registration requirements of the Commodity Exchange Act ("Act").¹ This exemption is sought in order to allow the Elevators, without registering as IBs, to receive a share of commissions from "T" and related compensation based upon futures transactions effected through "T" branch offices located at the Elevators and staffed by associated persons ("APs") of "T" who are employees of the Elevators.

Based upon the representations made in "A's" letter, as supplemented, we understand that the relevant facts are as follows. "T" is an independent IB.² "T" is an "X" wholly-owned by "U", also an "X" and a member/farmer owned cooperative.³ "T" provides futures trading services for approximately 200 grain elevators throughout the Midwest.

"T" seeks to establish IB branch offices at three participating Elevators, located in the Midwest.⁴ Each of the Elevators is an entity incorporated separately from "T". All of the Elevators for which relief is sought are members of "U", and thus all of the Elevators have an indirect interest in "T". It has been represented that each Elevator/branch office would employ at least one individual registered with the Commission as an AP of "T" and that this individual, or another employee of each Elevator who would be a Commission registrant, would meet the Commission's and the National Futures Association's requirements for branch managers.⁵

It has been further represented that the futures-related business transacted at each "T" branch office would be incidental to the Elevator's other agricultural cooperative business with producers/customers and that the commissions generated by each branch office would represent a small percentage (between 0.5% and 2%) of the respective Elevator's

total revenues. It is anticipated that in most cases each AP would be accepting orders for a total of between 10 to 30 contracts per month, and the largest branch offices would trade approximately 50 contracts per month.⁶

The provisions of the Futures Trading Act of 1982, which created the IB category of registrant and eliminated the former category of agents of FCMs, contemplated the separate existence and business identity of IBs and required that a separately incorporated branch office of an FCM register with the Commission as an IB. Thus, persons who previously operated as agents of an FCM must elect either to operate as an IB or as a branch office of an FCM. Similarly, each branch office that previously maintained a separate legal existence, *i.e.*, a "non-proprietary" branch office, must elect to operate as an IB or forsake its separate identity and become a "proprietary" branch office of the FCM. See Interpretative Letter No. 84-10, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22, 252 (May 29, 1984). Upon request for reconsideration of Interpretative Letter No. 84-10, the Commission reiterated the policies set forth above and made clear that a non-proprietary branch office of any registrant that is a separate legal person from the registrant must itself be registered with the Commission in an appropriate capacity. [Emphasis added.] See Interpretative Letter No. 84-26, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22, 472, at 30, 097 (Dec. 6, 1984). Thus, a separately incorporated branch office of an IB generally must register with the Commission in an appropriate capacity.

An IB's duty to supervise under Commission Rule 166.3 extends to the performance by its agents of any activities relating to its business as a registrant, whether or not the agents are actual employees of the IB.⁷ The Division is concerned about the ability of "T" officials in "Y" to establish and to maintain an adequate level of supervision over the handling of customer accounts by APs who work at and are employed by grain elevators located elsewhere in "Z" or throughout the Midwest.

Although, as the Commission has noted, the Division is willing to entertain specific requests for relief from compliance with the registration requirements when circumstances warrant, the Division believes that based upon the facts presented herein, "T" has not shown that it would be an unwarranted hardship to require separate registration of the Elevators. Accordingly, the Division must deny your request for a no-action position.

If you have any questions concerning this correspondence, please contact me or Thomas E. Joseph, an attorney on my staff, at (202) 418-5450.

Very truly yours,

I. Michael Greenberger

Director

¹ 7 U.S.C. § 1 et seq. (1994). "A" ceased his representation of "T" in this matter during 1996 and Division staff had several conversations with "B" of "T" about this matter before and after "A's" involvement ended. You informed us that you had been retained in this matter in the March 9, 1998 letter referred to above.

² When this request was first submitted, "T" was guaranteed by "V", a registered futures commission merchant ("FCM").

³ "U" is the acronym for "W", which is listed as a principal of "T".

⁴ "T" initially requested relief such that it could establish IB branch offices at between five and fifteen participating Elevators. "T" amended its request to limit the number of proposed branch offices to three, with the proviso that it may subsequently request relief to establish additional branch offices at participating Elevators.

⁵ See, e.g., Commission Rule 166.3.

⁶ With respect to commissions on commodity interest transactions, "T" intends to pay each Elevator an estimated flat fee of \$25.00 per round turn on each trade generated by a branch office and \$12.50 for each side of an option contract traded by the branch office's customers, with no charge on options expiring worthless. You indicated in your March 9, 1998 letter that "T" would charge customers \$65.00 per round turn.

⁷ *Lobb v. J.T. McKerr & Co.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,568 at 36,444 (CFTC Dec. 14, 1989).