

CFTC Letter No. 98-76**November 18, 1998****Division of Trading & Markets**

November 18, 1998

Re: Sections 4m(1) and 4d(1) – Request for an Interpretation or No-Action Position
Regarding Commodity Trading Advisor and Introducing Broker Registration

Dear :

This is in response to your letter dated June 23, 1998, to the Division of Trading and Markets (“Division”) of the Commodity Futures Trading Commission (“Commission”), as supplemented by your letter dated September 30, 1998 and telephone conversations with Division staff. By this correspondence, as supplemented, you request, on behalf of “X”, that the Division issue an interpretative letter regarding “X’s” obligation to register as a commodity trading advisor (“CTA”) and introducing broker (“IB”) under Sections 4m(1) and 4d(1) of the Commodity Exchange Act (“Act”)¹, respectively, or, in the alternative, take a “no-action” position with respect to “X’s” obligation to register as a CTA and IB, in connection with its customer referral service (“Service”).

To date, you have given us only a very cursory description of your clients’ proposed activities. However, based upon the representations made in your correspondence, we understand the facts to be as follows. “X” is an Illinois corporation with its principal place of business located in Illinois. “A”, a registered associated person (“AP”) of a futures commission merchant (“FCM”), is the sole principal and stockholder of “X”. “X” proposes to operate the Service in which members of the public seeking the services of a registered AP can be referred to an AP that advertises an expertise in the particular markets in which the customer intends to invest. Referrals will be made utilizing a database constructed and maintained by “X”. “X” intends to construct a database using information provided by registered APs who agree to advertise through “X” and pay an annual \$500 fee to “X”. The Service will work as follows: (1) customers contact “X” to request the names of APs located in their geographical area; (2) if a customer decides to use “X’s” Service, the customer pays a one-time fee of \$40 to “X”, provides “X” with some basic personal information such as name, address and phone number, and instructs “X” as to the type of trading he or she is interested in and the services he or she is seeking from an AP; (3) “X” searches its database in order to match the customer’s preferences with APs offering similar services; (4) if matches are found, “X” then forwards to the customer an informational sheet discussing each matched AP’s market expertise, limited biographical and employment histories, registration status and contact information and, in addition, informs each AP that his or her name has been given out to a prospective customer by forwarding the customer’s name and contact information to the AP; and (5) finally, either

the customer or the AP may contact one another, if he or she so desires, in order to establish a business relationship. If a customer does not receive a referral within 15 days of signing up for the Service, the customer will receive a full refund. However, "X" keeps the entire customer fee if any referral is made, whether or not the customer accepts the services of the referred AP. Likewise, if "X" does not make one referral to a participating AP within twelve months of the AP listing with "X", the AP is given the opportunity to withdraw its listing and receive a full refund of the annual fee paid to "X". In addition, you state that "X" plans to advertise the Service through advertisements in various financial print media and appearances by "X" representatives at financial services industry trade shows.

In support of your request, you represent that "X" will review each AP prior to listing the AP in the database. This review will consist of a search of the Commission's and the National Futures Association's registration and disciplinary records for references to the AP. "X" will also contact the current and prior employer, if applicable, of any AP seeking inclusion in the database for a reference. On occasion, "A" may also research the records of applicable contract markets, state regulatory agencies and the Central Registration Depository maintained by the National Association of Securities Dealers for references to the APs seeking inclusion in the database. In addition, you represent that neither "X" nor "A" will advise any person or entity as to the value of any commodity or as to the advisability of trading in any commodity or commodity interest contract in general. Finally, neither "X" nor "A" will hold themselves out to the public as either a CTA or an IB.

IB Registration>

Section 1a(14)² of the Act defines an IB as:

any person (except an individual who elects to be and is registered as an associated person of a futures commission merchant) engaged in soliciting or in accepting orders for the purchase or sale of any commodity for future delivery on or subject to the rules of any contract market who does not accept any money, securities, or property (or extend credit in lieu thereof) to margin, guarantee, or secure any trades or contracts that result or may result therefrom.

In addition, Commission Rule 1.3(mm)(1)³ further defines an IB as:

(1) Any person who, ***for compensation or profit, whether direct or indirect***, is engaged in soliciting or in accepting orders (other than in a clerical capacity) for the purchase or sale of any commodity for future delivery on or subject to the rules of any contract market who does not accept any money, securities, or property (or extend credit in lieu thereof) to margin, guarantee, or secure any trades or contracts that result or may result therefrom; . . . (*Emphasis added*)

Section 4d(1) of the Act generally requires registration of each person who comes within the IB definition. “X” seeks an interpretation or “no-action” position with respect to the IB registration requirements of Section 4d(1) based on the belief that its activities do not come within the statutory definition of an IB as defined in Section 1a(14) of the Act and Commission Rule 1.3(mm)(1). You claim that “X”, although operating the Service by which customers are referred to APs, does not solicit or accept orders for the purchase or sale of commodity interest contracts and therefore is not acting as an IB.

Generally, persons who, for compensation, refer potential customers to Commission registrants are required to register under the Act.⁴ This registration requirement serves to screen unfit persons from dealings with customers and thus represents an important customer safeguard. The registration requirement has been construed flexibly to require the registration of persons who participate even indirectly in such solicitations.⁵ The Division has stated in prior interpretative letters that “soliciting or accepting orders . . . must be construed to encompass not just the literal solicitation of customers’ orders, but also the solicitation of customers . . . for referral to an FCM for the institution of a trading relationship and the execution of those orders.”⁶ In CFTC Interpretative Letter No. 90-8, [1990-92 *Transfer Binder*] *Comm. Fut. L. Rep. (CCH)* ¶ 24,831 (May 7, 1990), the Division required a telecommunications company that was conducting a survey on behalf of a registered FCM to register as an IB since the objective of the tele-communications company’s efforts was not to conduct a survey among the general public of attitudes concerning financial markets, but rather to develop futures market clients from an identified target audience. Furthermore, the Division stated that the telecommunications company would be operating on a regular basis in the nature of a finder of such clients (in an agency capacity) for the FCM.

In CFTC Interpretative Letter No. 95-51, [1994-96 *Transfer Binder*] *Comm. Fut. L. Rep. (CCH)* ¶ 26,420 (May 1, 1995), the Division stated that “any contact initiated by a party that is intended to establish or to culminate in a customer relationship is conduct that entails the solicitation of customers, and may be characterized as indirect solicitation of customer orders, even though customers are under no obligation to open accounts with an FCM.” The Division believes that “X”, through its operation of the Service, is soliciting for compensation since “X’s” ultimate goal is to introduce members of the public to Commission registrants for the purpose of instituting a trading relationship. Therefore, since “X” appears to be acting as an IB, it would be required to register pursuant to Section 4d(1) of the Act.

Based upon the information provided in your correspondence, we do not find that your situation presents facts upon which the Division can grant relief from the Act’s IB registration requirement. Thus, we are declining to provide the relief you have requested with respect to IB registration. In addition, since “X” will be prohibited from operating the Service absent registration as an IB, we are declining to consider your request for CTA relief at this time.

If you have any questions regarding this correspondence, please contact me, or Charles T. O’Brien, an attorney on my staff, at (202) 418-5450.

Sincerely,

I. Michael Greenberger

Director

¹ 7 U.S.C. §§ 6m(1) and 6d(1) (1994).

² 7 U.S.C. § 1a(14) (1994).

³ Commission rules referred to herein are found at 17 C.F.R. Ch. I (1998).

⁴ *See, e.g.*, CFTC Interpretative Letter No. 96-45, [1994-96 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,715 (May 8, 1996).

⁵ *See, e.g.*, Subcommittee on Special Small Business Problems of the House Permanent Select Committee on Small Business, H.R. Rep. No. 963, 93rd Cong., 2d Sess. at 36-37 (1974) (discussing Congressional intent that “registration requirements and fitness checks should be imposed on commodity solicitors, advisors, and all other individuals who are involved either directly or indirectly in influencing or advising the investment of customers’ funds”).

⁶ *See, e.g.*, CFTC Interpretative Letter No. 97-44, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,084 (June 9, 1997) citing 48 Fed. Reg. 35248, 35250 (August 3, 1983).

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