



COMMODITY FUTURES TRADING COMMISSION
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Mary L. Schapiro
Chairman

March 24, 1995

Mr. R. K. Bagri, Chairman
London Metal Exchange Limited
56 Leadenhall St.
London, England EC3A2J

Dear Mr. Bagri:

I understand from our meeting on March 17, and various reports in the press that the London Metal Exchange ("LME") plans to permit delivery on its copper contract through United States warehouses, beginning in April 1995. This development raises certain issues relating to the interrelationship between trading on the LME contract and the U.S. copper market. Of course, inclusion of a U.S. delivery point would not change the applicable requirements under U.S. law regarding transactions by U.S. persons in the LME copper contract.

Several sections of the Commodity Exchange Act, as amended, 7 U.S.C. §1, et seq., which is administered and enforced by the Commission, broadly apply to transactions involving any commodity in interstate commerce. For example, Section 4c of the Act, 7 U.S.C. §6c, provides, in part, that:

It shall be unlawful for any person to offer to enter into, enter into, or confirm the execution of, any transaction involving any commodity, which is or may be used for . . .
(3) delivering any such commodity sold shipped, or received in interstate commerce for the fulfillment thereof--

(A) if such transaction is, is of the character of, or is commonly known to the trade as, a "wash sale," "cross trade," or "accommodation trade," or is a fictitious sale, or

(B) if such transaction is used to cause any price to be reported, registered or recorded which is not a true and bona fide price.

Similarly, Sections 6(c) and 6(d) of the Act, 7 U.S.C. §§9 and 13,

prohibit any person from "manipulating or attempting to manipulate . . . the market price of any commodity, in interstate commerce"

Although the LME and other foreign exchanges have U.S. delivery points on several other contracts, the proposed U.S. delivery point for LME copper is the first instance where the deliverable commodity is also the subject of a substantially similar, actively-traded U.S. futures contract. Because the Commission's authority extends to the integrity of related cash markets, and because the U.S. delivery facilities of the LME might be implicated in a market manipulation or other trading anomaly occurring in foreign markets, a United States regulatory interest is invoked. In this regard, in view of the arbitrage relationship which exists between the London and United States copper markets, the Commission would appreciate an analysis from the LME on the potential impact the addition of a United States delivery point on the LME copper contract might have on the U.S. copper market. In particular, the Commission would appreciate receiving the LME's views regarding the pricing relationship between its London and proposed U.S. delivery facilities and the larger U.S. market in copper, and the relative stability of that pricing relationship during times of market stress.

Moreover, the recent collapse of Barings PLC underscores the importance that the LME and its U.K. regulators assure the Commission that adequate arrangements are in place to inform the Commission of actions which may be taken by the LME or the U.K. regulators to address various types of potential market disruptions. In addition, the LME must assure the Commission of its ability to address the Commission's needs for information regarding the potential impact of any such market disruptions on U.S. deliverable supplies of copper and on the U.S. copper futures contract. In this regard, senior Commission staff will be in London, before the delivery of copper on the LME contract through U.S. warehouses becomes effective, during the last week of March 1995, and will be available to meet with you to discuss these issues.

Finally, the inclusion of a U.S. delivery point in copper, coupled with issues raised by the Barings collapse and the clear difference in practice regarding trading rules and the methods of ensuring financial prudence, further emphasizes the need for greater international harmonization of rules and procedures relating to customer protection and prudential regulation. Commission concern relating to the protection of U.S. participants trading on foreign markets and the impact of foreign futures markets on the operation of U.S. cash markets will become heightened to the degree that foreign markets become more linked to

domestic U.S. markets through arrangements such as these. The Commission would like to explore further these issues with both the LME and its U.K. regulators.

Sincerely,

Mary L. Schapiro

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Chairman