CFTC Letter No. 02-90
July 22, 2002
Interpretation
Division of Clearing and Intermediary Oversight

Re: "Y"

Dear :

This is in response to your letter dated July 1, 2002, to the Division of Trading and Markets (the "Division")[1] of the Commodity Futures Trading Commission (the "Commission" or "CFTC"), as supplemented by telephone conversations with Division staff. By your correspondence, you request, on behalf of "X", that the Division confirm that registered securities broker-dealers ("BDs") and their registered representatives ("RRs") who offer and sell security futures products ("SFPs") are not by that fact precluded from offering and selling "Y" on behalf of non-institutional customers.

By letter dated July 11, 2001 (the "July 11, 2001 letter"), the Division issued a no-action position with respect to the offer and sale by BDs and RRs of "Y"subject to the conditions that such BDs and RRs comply with notice-registration procedures (as FCMs and APs, respectively) outlined in the July 11, 2001 Letter, and that the BDs and RRs "restrict their Commission-regulated activities to the offer and sale of "Y"." In your correspondence, you call the Division's attention to this fact as well as to Section 252(b) of the Commodity Futures Modernization Act of 2000 (the "CFMA"), which states, in relevant part:

[A]ny broker or dealer that is registered with the Securities and Exchange Commission ["SEC"] shall be registered as a futures commission merchant or introducing broker, as applicable, if . . . the broker or dealer limits its solicitation of orders, acceptance of orders, or execution of orders, or placing of orders on behalf of others involving contracts of sale of any commodity for future delivery, on or subject to the rules of any contract market or registered derivatives transaction execution facility to security futures products."[2]

You are concerned that, absent the requested confirmation from the Division, BDs and RRs who offer and sell SFPs may be (or may conclude that they are) precluded from also offering and selling "Y". You argue that permitting BDs who offer and sell SFPs also to offer and sell "Y" is consistent with the relief granted in the July 11, 2001 Letter and with the intent of the CFMA.

The Division recognizes that SFPs and "Y" are unique products. SFPs are considered to be both securities and futures contracts (or options thereon), subject to the joint jurisdiction of the CFTC and the SEC. "Y" are futures contracts subject to the exclusive jurisdiction of the CFTC, but they were developed in such a way as to appeal to securities customers, and they were intended to be offered and sold by BDs and RRs to retail customers, generally complying with the securities regulatory framework

in lieu of the futures regulatory framework, in accordance with the July 11, 2001 Letter. Clearly, when the CFMA was enacted, the existence of the "Y" concept was not widely known. The Division was, however, aware of the CFMA when it issued the July 11, 2001 Letter and did not intend that those taking advantage of the July 11, 2001 Letter would be barred from SFP transactions. In light of these factors, the Division does not believe that the intent of the CFMA was to require BDs and RRs that were not otherwise involved with futures transactions to choose between conducting business involving SFPs or "Y".

Accordingly, the Division will not recommend that the Commission commence any enforcement action against a BD or RR that is notice-registered with the Commission for the purpose of offering and selling SFPs based solely upon the BD or RR also offering and selling "Y". This position is conditioned upon simultaneous compliance by such BD or RR with the provisions of the Act and Commission rules applicable to persons notice-registered with the Commission under Section 4f(a)(2) of the Act with respect to the offer and sale of SFPs, and with the terms and conditions set forth in the July 11, 2001 letter with respect to the offer and sale of "Y". For example, BDs and RRs conducting both SFP and "Y" business must comply with the notice registration requirements of CFTC Rule 3.10(a)(3)[3] and separately with such procedures as are established by NFA applicable to persons offering and/or selling "Y". Compliance with one of these regimes will not by itself allow a person to conduct business in the other product.

This letter does not excuse "X", or any BD or RR offering or selling SFPs or "Y", from compliance with any other applicable requirements contained in the Act or in the Commission's rules issued thereunder. For example, each remains subject to the relevant antifraud provisions of the Act and Commission rules. This letter is applicable to "X", BDs and RRs solely in connection with the activities described above.

The no-action position taken in this letter represents the views of this Division only and does not necessarily 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 contact me or Christopher W. Cummings, an attorney on my staff, at (202) 418-5445.

Very truly yours,

Jane Kang Thorpe
Director

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[1] As of July 1, 2002, a reorganization of Commission staff became effective. The responsibility for addressing requests for interpretative, no-action and exemptive letters is now with the Division of Clearing and Intermediary Oversight. Accordingly, for purposes of this letter, the term "Division" includes the Division of Clearing and Intermediary Oversight and its predecessor, the Division of

Trading and Markets, as the context requires.

[2] Codified at Section 4f(a)(2) of the Commodity Exchange Act (the "Act"), 7 U.S.C. §6f(a)(2) (1994).

[3] Commission rules referred to herein are found at 17 C.F.R. Ch. I (2002).