## U.S. COMMODITY FUTURES TRADING COMMISSION



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CFTC letter No. 07-13 June 12, 2007 Exemption Division of Clearing and Intermediary Oversight

Re: Request for Exemption from Regulation 155.3(c)(3)

Dear :

This is in response to your letter dated April 13, 2007, to the Division of Clearing and Intermediary Oversight ("Division")<sup>1</sup>, in which you request, on behalf of (the "Company"), a registered futures commission merchant ("FCM"), an exemption from Commission Regulation 155.3(c)(3),<sup>2</sup> which requires an FCM that handles the account of an associated person ("AP") of another FCM, or introducing broker ("IB"), to send to the other FCM or IB certain account statements and written records relating to the AP's account (the "Order Data")<sup>3</sup>. Specifically, you request that the Company be relieved from the requirement that an FCM transmit to an IB the written records specified in Regulation 155.3(c)(3) where the IB has been provided electronic access to the information required to be transmitted.

Based upon the representations made in your letter, we understand the relevant facts to be as follows. The Company is a registered FCM, which acts as a clearing broker for several IBs. You state that the Company intends to allow the APs of a certain IB (the "Employing IB") to trade futures through an automated order routing system ("AORS"), which will then be submitted for clearing by the Company. The Company will enable such AP to trade through the AORS after receiving written authorization from the Employing IB to open an AP's account. As part of its written authorization, the Employing IB will acknowledge that it understands how to access the Order Data from the Company's computer system, so that the IB will have constant access to the data. The Company will provide the Order Data in hardcopy format at the Employing IB's request. If the AP executes trades without using the AORS, then the

We note that while your letter was addressed to the Director of the Division, Regulation 155.10 gives the Commission the authority to grant an exemption from Part 155. This authority has not been specifically delegated to the Division and, consequently, the Commission rather than the Division responds to your request.

<sup>&</sup>lt;sup>2</sup> Commission regulations referred to in this letter are found at 17 C.F.R. Ch. I (2006).

The Order Data will include an account identifier, order number, and the date and time the order is received, as required by Regulation 155.3(c)(2).

requirement of Regulation 155.3(c)(3) to transmit hardcopies of the Order Data to the Employing IB would still apply.

As you are aware, Regulation 155.3(c)(3) requires any FCM that handles the account of an AP of another FCM, or an AP of an IB, to transmit on a regular basis to such other FCM or IB "copies of all statements of such account and of *all written records* prepared upon receipt of the orders for such account . . . ." (emphasis added). Paragraph (c) was "designed to assist FCMs in supervising the trading activities of their affiliated persons by providing them with notification of and information concerning the accounts maintained by their affiliated persons with other FCMs." The Commission, in adopting the Part 155 regulations, expressed the view that information pertaining to the time and sequence of transactions is essential for contract markets to be able to reconstruct trading on any given day. Such information also assists FCMs in carrying out the public protection function of the trading standards regulations, *i.e.*, to ensure "that FCMs and their employees do not take advantage of their relationship with customers by using their knowledge of customer orders to trade ahead of or against the interests of such customers for their own benefit or that of their preferred customers."

Because of the trend towards greater electronic trading and the ability to store or transmit certain required documents electronically, the Commission has previously made allowances and provided guidance for the electronic storage and delivery of certain required documents. For instance, the Commission permits the electronic delivery and retention of customer account statements, including monthly, confirmation, and purchase-and-sale statements, by FCMs. <sup>6</sup>

The Commission has considered requests for relief from Regulation 155.3(c) in Commission Letter 92-21 (December 21, 1992), and in Commission Letter 99-18 (March 23, 1999). In Commission Letter 99-18, the request was on behalf of an FCM that wished to have one of its APs trade through another FCM with whom the AP had a longstanding relationship and from whom the AP would receive a discount on his trades. The stated reason for the arrangement was to keep the AP's trades confidential from his fellow employees. Relief was requested because transmitting copies of the required documents would not be feasible at the discounted trade price. In that instance, the relief was denied. In Commission Letter 92-21, the Commission granted relief where an FCM with numerous IBs requested relief from providing its

<sup>&</sup>lt;sup>4</sup> 41 Fed. Reg. 56134, 56139 (December 23, 1976). This followed a recommendation from the Commission's Advisory Committee on Commodity Futures Trading Professionals ("Martin Committee") that "[t]he trading of futures by associated persons for their own accounts should be closely supervised by the employing FCM." Martin Committee Report at 20 (August 1976).

<sup>&</sup>lt;sup>5</sup> 41 Fed. Reg. 56134, 56139 n.18; see also United States v. Dial, 757 F.2d 163 (7th Cir. 1985) (affirming criminal conviction of brokers for trading ahead of customer orders).

<sup>&</sup>lt;sup>6</sup> See 62 Fed. Reg. 31507, June 10, 1997.

IBs with copies of all floor and office order tickets. The IBs and FCM agreed that the required floor and office order tickets would be available upon request and that the IBs and FCM would execute a written agreement in which the Employing IB would agree to the arrangement.

Based on the foregoing, the Commission has determined that granting the Company's request for relief from the requirements of Regulation 155.3(c)(3) would not be contrary to the public interest and the purpose of the rule from which relief is sought. Accordingly, the Commission hereby exempts the Company from Regulation 155.3(c)(3) insofar as it requires that the Company send to the Employing IB copies of all order tickets prepared with respect to the accounts of the Employing IB's APs. This exemption is, however, subject to the conditions that the Company: (1) receive a written statement from the Employing IB in which such Employing IB acknowledges and agrees to the foregoing arrangement; and (2) promptly furnish to the Employing IB, upon its request, floor and office order tickets related to trading of the Employing IB's APs.

The relief granted herein does not diminish the Employing IB's affirmative obligation to supervise its APs' activities under Commission Regulation 166.3 or to establish and enforce internal rules, procedures and controls to insure, to the extent possible, that customer orders are transmitted to the floor or entered into an AORS prior to any order for the same commodity for any proprietary account, any account in which an affiliated person has an interest, or any account for which an affiliated person may originate orders without the prior consent of the owner in the circumstances addressed in Regulation 155.3. To fulfill these obligations, the Employing IB, of course, continues to retain its right to impose restrictions on its APs' trading activities. For example, the Employing IB may prohibit its APs either from trading for their own accounts, or from establishing accounts with any IB or FCM other than the Employing IB. If the Employing IB chooses not to restrict the trading activities of its APs as mentioned above, and further acknowledges and agrees to the arrangement the Company proposes, the Employing IB would have an affirmative duty to request and analyze the order tickets regarding the accounts of its APs whenever the circumstances warrant. This duty would arise, for example, in those cases when a review of the daily confirmations and/or monthly statements of the Employing IB's APs the possibility that a trade by an AP occurred in violation of the AP's or Employing IB's duty to a customer.

The relief granted by this letter is based on the representations you have made to us and is subject to the conditions stated above. The relief granted by this letter does not excuse the Company from compliance with any other applicable requirements contained in the Act or the Commission's regulations thereunder, such as the supervision requirements in Regulation 166.3. Any different, changed or omitted facts or conditions might require us to reach a different conclusion. In this regard, we request that you notify us immediately in the event the facts presented change in any way from those represented to us.

If you have any questions concerning this correspondence, please contact Deputy Director, Lawrence B. Patent at (202) 418-5439, or Special Counsel, Peter Sanchez at (202) 418-5237.

Very truly yours,

Eileen Donovan, Acting Secretary of the Commission