

CFTC Letter No. 98-73**October 8, 1998****Division of Trading & Markets****Re: Applicability of the Commodity Exchange Act to Transactions
Involving the Purchase or Sale of Gold Coins and Silver Bars**

Dear :

This is in response to your letter dated July 22, 1998 to the Office of the General Counsel of the Commodity Futures Trading Commission ("Commission"). Your letter was forwarded to the Division of Trading and Markets ("Division") for reply. By your letter, you requested the issuance by the Commission of a "no-action letter" with regard to a failure by "A" to register as a futures commission merchant ("FCM") under Section 4d of the Commodity Exchange Act ("Act")¹ if "A" undertakes to buy and sell gold coins and silver bars with members of the general public (the "Transactions"). As is set forth more fully below, the Transactions may implicate more than just the FCM registration provisions of the Act. Accordingly, by this letter the Division is providing you with general guidance concerning the application of the Act and the Commission's regulations issued thereunder to "A" and the Transactions.

The Act provides the Commission with "exclusive jurisdiction" with respect to "any transaction which is of the character of, or is commonly known to the trade as, an `option', `privilege', `indemnity', `bid', `offer', `put', `call', `advance guaranty', or `decline guaranty'" and "transactions involving contracts of sale of a commodity for future delivery . . .," which are more commonly known as "futures contracts."² If the Transactions are futures or commodity option contracts, the Act and the Commission's regulations require, with few exceptions, that the transactions be conducted on a regulated futures exchange and in accordance with the regulatory structure established by the Act and administered by the Commission.³ As discussed more fully below, this regulatory scheme includes requirements that persons who are involved in the offer, sale and execution of futures or option contracts generally register with the Commission in an appropriate category.

Neither the Act nor the Commission's regulations specifically define the phrase "contracts of sale of a commodity for future delivery," although the Act does state that the "term `future delivery' does not include any sale of any cash commodity for deferred shipment."⁴ In determining whether a specific transaction constitutes a commodity futures contract, the Commission and the courts have assessed the transaction as a whole with an eye toward its underlying purpose.⁵ While neither the courts nor the Commission has identified an exclusive list of factors that define a futures contract, they have identified

certain characteristics that are common to most futures contracts. These characteristics include that futures contracts are contracts for the purchase or sale of a commodity in the future at a price agreed upon at the time the contract is entered into; the futures contract may be satisfied either by entering into an offsetting transaction prior to maturity of the contract or making or taking delivery of the specified quantity of the underlying commodity; and the purpose of the contract is to provide participants with an opportunity to assume or shift commodity price risks without ultimately acquiring or disposing of the commodity through delivery pursuant to the contract terms.⁶ The Commission has emphasized that these elements are not an "exhaustive catalogue of factors" to be used in identifying a futures contract and that it "will look at each operation in context and will not hesitate to look behind whatever label the parties may give to the instrument" when it analyzes whether a transaction is a futures contract.⁷

Various provisions of the Act and the Commission's regulations require registration of persons who perform certain specified functions in connection with futures or commodity option trades. For example, persons or entities who engage in the solicitation or acceptance of orders for the purchase of a futures contract and accept money, securities or property to margin, guarantee or secure any resulting trades must register as an FCM.⁸ Similarly, persons or entities who engage in the solicitation or acceptance of orders for the purchase of a futures contracts but do not accept money, securities or property to margin, guarantee or secure any resulting trades must register as an introducing broker.⁹ In addition, natural persons who solicit customers on behalf of registrants or supervise persons engaged in such solicitation generally are required to register as associated persons of the registrant.¹⁰ Additional registration requirements may apply to other activities or services undertaken on behalf of or provided to persons trading commodity futures or option contracts.

The Act does not provide the Commission with jurisdiction over true "spot" transactions. In a spot transaction, immediate delivery of the product and immediate payment for the products are expected on or within a few days of the trade date.¹¹ However, we again emphasize that when assessing whether a transaction constitutes a commodity futures or option contract, the Commission and the courts have looked beyond appearances created by marketing materials concerning the transaction to the underlying economic reality of the transaction itself, as reflected in the actual day-to-day operations of those engaged in the trades in question.

In light of the breadth of issues that the Transactions raise, the Division is unable to provide you with the FCM registration no-action position that you have requested. Moreover, by this letter, the Division is not offering an opinion as to the nature or the legality of the Transactions or as to whether, and to what extent, "A" and the Transactions are subject to the Act and the Commission's regulations issued thereunder.¹² Rather, we

recommend that you carefully review with knowledgeable private counsel all of the facts and circumstances relating to the Transactions in order to obtain an opinion as to whether "A" and the Transactions may be subject to the Act and the Commission's regulations, or other applicable laws and regulations.

The views expressed herein are those of the Division only and do 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 Thomas E. Joseph, an attorney on my staff at (202) 418-5430.

Very truly yours,

I. Michael Greenberger

Director

¹ 7 U.S.C. § 6d (1994).

² Section 2(a)(1)(A)(i) of the Act, 7 U.S.C. § 2(i)(1994). The Act also sets forth certain exclusions from Commission jurisdiction. *See, e.g.*, Section 2(a)(1)(A)(ii) of the Act, 7 U.S.C. § 2(ii)(1994). The term "commodity" is defined by the Act to include certain enumerated agricultural goods and "all other goods and articles, except onions . . . and all services, rights and interests in which contracts for future delivery are presently or in the future dealt in." Section 1a(3) of the Act, 7 U.S.C. § 1a(3) (1994). Thus, the Transactions could involve "commodities" as defined by the Act.

³ Section 4(a) of the Act, 7 U.S.C. § 6(a)(1994), renders it "unlawful for any person to offer to enter into, to enter into, to execute, to confirm the execution of or to conduct any office or business anywhere in the United States . . . for the purpose of soliciting, or accepting any order for, or otherwise dealing in, any transaction in, or in connection with, a contract for the purchase or sale of a commodity for future delivery . . . unless such transaction is [among other requirements] conducted on a board which has been designated by the Commission as a 'contract market' for such commodity." In addition, except as provided elsewhere in Commission regulations, Commission Rule 33.3, 17 C.F.R. § 33.3 (1998), prohibits the offer or execution of any commodity option which is not traded on or subject to the rules of a contract market designated to trade such option by the Commission. Rule 33.3 was adopted, in part, pursuant to authority in Section 4c(b) of the Act, 7 U.S.C. 6c(b)(1994), which states that "[n]o person shall offer to enter into, enter into or confirm the execution of, any transaction involving any commodity regulated under this Act which is of the character of or is commonly known to the trade as, an 'option' . . . contrary to any rule, regulation or order of the Commission prohibiting any such transaction or allowing such transaction under such terms and conditions as the Commission shall prescribe."

⁴ Section 1a(11) of the Act, 7 U.S.C. § 1a(11)(1994). While the Act provides the Commission with exclusive jurisdiction over "any transaction which is of the character of, or is commonly known to the

trade as, an `option', `privilege', `indemnity', `bid', `offer', `put', `call', `advance guaranty', or `decline guaranty'," it does not further define these terms.

⁵ See, e.g., *CFTC v. CoPetro Marketing Group Inc.*, 680 F.2d 573 (9th Cir. 1982)(finding transactions to be illegal off-exchange futures contracts); and *In Re Stovall*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 (CFTC 1989)(finding transactions to be illegal off-exchange futures contracts).

⁶ See, e.g., *In the Matter of First National Monetary Corp.*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. ¶ 21,707 at p. 26,744 (CFTC 1983).

⁷ *In Re Stovall* at p. 23,779.

⁸ See Sections 1a(12) and 4d of the Act, 7 U.S.C §§ 1a(12) and 6d (1994).

⁹ See Sections 1a(14) and 4d of the Act, 7 U.S.C. §§ 1a(14) and 6d (1994).

¹⁰ See Section 4(k) of the Act, 7 U.S.C § 6(k)(1994), and Commission Rule 1.3(aa), 17 C.F.R. § 1.3(aa) (1998).

¹¹ See CFTC Interpretative Letter No. 97-01, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,937 at p. 44,520 (December 12, 1996)(citing Timothy J. Snider, *Regulation of the Commodities Futures and Options Markets*, Vol. 1, § 9.01 (2ed. 1995).

¹² In addition, the Division is not providing any opinion as to the applicability of any state or federal laws administered by other regulatory agencies, including securities laws, to "A" and the Transactions.