

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-44731 / August 21, 2001]

Order Granting Temporary Exemption of Certain Futures Commission Merchants and Introducing Brokers from the Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934

The Commodity Futures Modernization Act of 2000 (“CFMA”) permits the trading of security futures, *i.e.*, futures contracts on individual securities and on narrow-based security indexes.¹ The CFMA regulates security futures both as “securities” under the federal securities laws,² and as futures contracts for purposes of the Commodity Exchange Act (“CEA”).³ As a result, the Securities and Exchange Commission (“Commission”) and the Commodity Futures Trading Commission (“CFTC”) have joint jurisdiction over security futures products. To avoid duplicative regulation, the CFMA established a system of notice registration under which trading facilities and intermediaries that are already registered with either the Commission or the CFTC may register with the other agency on an expedited basis for the limited purpose of trading

¹ Pub. L. No. 106-554, 114 Stat. 2763. Under Section 3(a)(55)(A) of the Securities Exchange Act of 1934 (“Exchange Act”), the term “security future” is defined as a contract of sale for future delivery of a single security or of a narrow-based security index. 15 U.S.C. 78c(a)(55)(A). Under Exchange Act Section 3(a)(56), the term “security futures product” is defined as a security future or an option on a security future. 15 U.S.C. 78c(a)(56).

² See, e.g., Exchange Act Section 3(a)(10), 15 U.S.C. 78c(a)(10).

³ The term “security future” is defined in CEA Section 1a(31) (7 U.S.C. 1a(31)) as a contract of sale for future delivery of a single security or of a narrow-based security index. Under CEA Section 1a(33) (7 U.S.C. 1a(33)), the term “security futures product” is defined as a security future or an option on a security future.

security futures products. Section 6(g)(5)(B) of the Exchange Act⁴ provides that trading in security futures products may begin on a limited basis on August 21, 2001.

For purposes of the Exchange Act, any person who is engaged in the business of effecting transactions in security futures products for the account of another is a broker.⁵ Similarly, any person who is engaged in the business of buying and selling security futures products for the person's own account is a dealer.⁶ With limited exceptions, brokers and dealers are required by Exchange Act Section 15(a) to register with the Commission.⁷ However, Section 15(b)(11) of the Exchange Act⁸ permits futures commission merchants and introducing brokers⁹ that are registered with the CFTC to register with the Commission as broker-dealers for the limited purpose of effecting transactions in certain security futures products by filing a written notice that is effective upon filing.

The Commission is adopting rules today to implement Section 15(b)(11) and to provide the procedure for futures commission merchants and introducing brokers to register by notice as broker-dealers.¹⁰ Specifically, Rule 15b11-1 under the Exchange

⁴ 15 U.S.C. 78f(g)(5)(B).

⁵ See Exchange Act Section 3(a)(4), 15 U.S.C. 78c(a)(4).

⁶ See Exchange Act Section 3(a)(5), 15 U.S.C. 78c(a)(5).

⁷ 15 U.S.C. 78o(a).

⁸ 15 U.S.C. 78o(b)(11).

⁹ As used in this order, the terms "futures commission merchant" and "introducing broker" have the meanings given in Sections 1a(20) and 1a(23) of the CEA (7 U.S.C. 1a(20) and 1a(23)).

¹⁰ Securities Exchange Act Release No. 44730 (August 21, 2001).

Act¹¹ requires futures commission merchants and introducing brokers to file new Form BD-N as the form of notice required by Section 15(b)(11). Form BD-N requires a registrant to provide basic identification information and to indicate that it meets the requirements for notice registration under Section 15(b)(11). The Commission recognizes that futures commission merchants and introducing brokers that want to trade security futures products may not have sufficient time to complete the notice registration process before limited trading in the products is permitted to begin on August 21, 2001.

The Commission appreciates the importance of Congress' determination to provide investors with the ability to trade security futures products and is committed to ensuring that the necessary regulatory infrastructure is in place to enable the development of, and trading in, security futures products within the timeframes established in the CFMA.

With limited exceptions, Section 6(g)(5) of the Exchange Act permits futures commission merchants and introducing brokers to trade security futures products only for their own accounts. Futures commission merchants and introducing brokers may not trade security futures products on behalf of customers until December 21, 2001, or such later date by which a limited purpose national securities association has satisfied the requirements of Exchange Act Section 15A(k)(2). We do not believe that principal-to-principal trading of security futures products alone will raise the same investor protection concerns as will arise when trading in security futures products is also permitted on behalf of customers. Moreover, the National Futures Association has informally committed to the Commission staff that it will provide the Commission with access to its

¹¹ 17 CFR 240.15b11-1.

membership database. As a result, during the period of the exemption provided by this order the Commission will have full access to disclosure information that futures commission merchants and introducing brokers file with the CFTC, even in the absence of the identification information that the Commission will receive through Form BD-N.

The Commission therefore believes that it is consistent with the public interest and the protection of investors to temporarily exempt from the registration requirements of Section 15(a)(1) futures commission merchants and introducing brokers that meet the requirements for use of a notice filed under Section 15(b)(11) for the limited trading permitted by Section 6(g)(5)(B) of the Exchange Act.¹²

Accordingly, pursuant to Section 15(a)(2) of the Exchange Act,¹³

IT IS HEREBY ORDERED that futures commission merchants and introducing brokers are exempted from the registration requirements of Section 15(a)(1) of the Exchange Act¹⁴ until October 21, 2001 with respect to any transaction in security futures products permitted by Section 6(g)(5)(B) of the Exchange Act, provided that a futures commission merchant or introducing broker that relies on this exemption must be: (1)

¹² Section 6(g)(5)(B)(i) of the Exchange Act permits security futures product transactions entered into:

(I) on a principal-to-principal basis between parties trading for their own accounts or as described in section 1a(12)(B)(ii) of the Commodity Exchange Act; and

(II) only between eligible contract participants (as defined in subparagraphs (A), (B)(ii), and (C) of such section 1a(12)) at the time at which the persons enter into the agreement, contract, or transaction

¹³ 15 U.S.C. 78o(a)(2).

¹⁴ 15 U.S.C. 78o(a)(1).

registered with the CFTC; and (2) a member of the National Futures Association or another national securities association registered pursuant to Exchange Act Section 15A(k).¹⁵

By the Commission.¹⁶

Jonathan G. Katz
Secretary

August 21, 2001

¹⁵ 15 U.S.C. 78o(a)(2).

¹⁶ Chairman Pitt did not participate in this matter.