

Public Law 97-303
97th Congress

An Act

To clarify the jurisdiction of the Securities and Exchange Commission and the definition of security, and for other purposes.

Oct. 13, 1982
[H.R. 6156]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. Section 2(1) of the Securities Act of 1933 (15 U.S.C. 77b(1)) is amended by inserting after “mineral rights,” the following: “any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency.”

Securities and Exchange
Commission,
jurisdiction clarification.

SEC. 2. Section 3(a)(10) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(10)) is amended by inserting after “for a security,” the following: “any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency.”

SEC. 3. Section 9 of the Securities Exchange Act of 1934 (15 U.S.C. 78i) is amended—

(1) by striking out “this section” in subsection (f) and inserting in lieu thereof “subsection (a)”; and

(2) by inserting after subsection (f) the following new subsection:

Authority to regulate
trading.

“(g) Notwithstanding any other provision of law, the Commission shall have the authority to regulate the trading of any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency (but not, with respect to any of the foregoing, an option on a contract for future delivery).”

SEC. 4. Section 28(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78bb(a)) is amended by adding at the end thereof the following new sentence: “No State law which prohibits or regulates the making or promoting of wagering or gaming contracts, or the operation of ‘bucket shops’ or other similar or related activities, shall invalidate any put, call, straddle, option, privilege, or other security, or apply to any activity which is incidental or related to the offer, purchase, sale, exercise, settlement, or closeout of any such instrument, if such instrument is traded pursuant to rules and regulations of a self-regulatory organization that are filed with the Commission pursuant to section 19(b) of this Act.”

15 USC 79s

SEC. 5. Section 2(a)(36) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(36)) is amended by inserting after “mineral rights,” the following: “any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value

thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency.”.

SEC. 6. Section 202(a)(18) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(18)) is amended by inserting after “mineral rights,” the following: “any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency,”.

15 USC 7811l.

SEC. 7. Section 16(14) of the Securities Investor Protection Act (15 U.S.C. 7811l(14)) is amended—

(1) by inserting after “Securities Act of 1933),” the following: “any put, call, straddle, option, or privilege on any security, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency,”; and

(2) by striking out “The” in the last sentence and inserting in lieu thereof “Except as specifically provided above, the”.

Approved October 13, 1982.

LEGISLATIVE HISTORY—H.R. 6156 (S. 2260):

HOUSE REPORTS: No. 97-626 Pt. I (Comm. on Energy and Commerce), Pt. II (Comm. on Agriculture).
SENATE REPORT No. 97-390 accompanying S. 2260 (Comm. on Banking, Housing, and Urban Affairs).
CONGRESSIONAL RECORD, Vol. 128 (1982):

Sept. 23, considered and passed House.

Oct. 1, considered and passed Senate.

SECURITIES—COMMODITIES ACCORD
AMENDMENTS OF 1982

REPORT

OF THE

COMMITTEE ON BANKING, HOUSING,
AND URBAN AFFAIRS
UNITED STATES SENATE

TO ACCOMPANY

S. 2260

MAY 12 (legislative day, MAY 11), 1982.—Ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON: 1982

89-010 O

In view of the SEC's strong regulatory interest in the trading of securities which may be components of stock groups or indices, as well as Congressional interest in assuring coordination between the activities of the two agencies, amendments to the CEA contained in S. 2109 would provide the SEC with an explicit role in the CFTC's administrative process of designating contract markets for the trading of futures contracts on stock groups and indices. S. 2109 would create a more extensive role for the SEC that the role now provided for the Department of the Treasury and the Federal Reserve Board in connection with contracts relating to government securities. In addition, in order to facilitate cooperation between the SEC and the CFTC and the entities they regulate in conducting surveillance, S. 2109 would amend the CEA to remove existing statutory impediments to transmission by the CFTC of trade information to securities self-regulatory organizations and to registered futures associations.

Commodity pools

While the CFTC has adopted regulations governing the activities of commodity pool operators and has exclusive jurisdiction with respect to "accounts * * * involving" futures, uncertainty has existed with respect to the extent to which the activities of a commodity pool as a company, e.g., its formation, capital-raising, and periodic disclosure, are subject to the federal securities laws. Proposed amendments to the CEA in S. 2109 would clarify the applicability of the Securities Act and the Securities Exchange Act to securities issued by commodity pools and transactions in such securities. Moreover, in appropriate circumstances, commodity pools and persons managing them may be subject to the Investment Advisers Act and, if a pool also acts as an investment company, to the Investment Company Act.

SECTION-BY-SECTION ANALYSIS OF S. 2260

To accomplish the purposes discussed above, S. 2260 would amend the Securities Act, the Securities Exchange Act, the Investment Company Act, and the Investment Adviser Act.

Section 2

This section of the bill would amend Section 2 (1) of the Securities Act of 1933 (15 U.S.C. 77b(1)), which defines the term "security", to include among the instruments specifically enumerated "any put, call, straddle, option, or privilege on any security." This amendment would make clear that such instruments are themselves separate securities. In addition, the amended definition would make clear that options on groups and indices of securities, options on certificates of deposit and, when traded on a national securities exchange, options on foreign currency are securities. The proposed treatment of options on certificates of deposit under the Securities Act is not intended to affect existing law governing the circumstances under which certificates of deposit may be securities.

Section 3

This section of the bill would amend Section 3(a) (10) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a) (10)), which defines the term "security," to make changes identical to those made in the defini-

tion of the term “security” in the Securities Act. The amendment would make clear that an option on an exempted security is a separate security. Accordingly, a person in the business of effecting transactions in such instruments would, absent an applicable exemption, be required, pursuant to Section 15 of the Securities Exchange Act, to register with the SEC as a broker or dealer. To the extent, however, that such a requirement would impose an unnecessary burden on certain entities, including government securities dealers, involved in effecting transactions in options on government securities, the Committee anticipates that the SEC would exercise its authority to grant administrative exemptions.

Section 4

This section of the bill would amend Section 9 of the Securities Exchange Act (15 U.S.C. 78i) to make it clear that the SEC’s plenary authority over options trading on national securities exchanges extends to options on securities, securities groups and indices, certificates of deposit, and, when traded on a national securities exchange, options on foreign currency.

Section 5

This section of the bill amends Section 2 (a) (36) of the Investment Company Act of 1940 (15 U.S.C. 80a-2 (a) (36)), which defines the term “security,” to make explicit that the term includes “any put, call, straddle, option or privilege on any security including a certificate of deposit, or any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option or privilege entered into on a national securities exchange relating to foreign currency.” The proposed treatment of options on certificates of deposits in the Investment Company Act would recognize that the underlying certificates of deposit clearly are securities for the purpose of the Investment Company Act.

Section 6

This section of the bill amends Section 202(a) (18) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a) (18)), which defines the term “security,” to make changes identical to those made in the definition of “security” in the Investment Company Act.

FISCAL IMPACT STATEMENT

No provision in S. 2260 is intended by the Committee to authorize new budget authority.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, D.C., May 11, 1982.

Hon. JAKE GARN,
*Chairman, Committee on Banking, Housing and Urban Affairs, U.S. Senate,
Dirksen Senate Office Building, Washington, D.C.*

DEAR MR. CHAIRMAN: Pursuant to Section 403 of the Congressional Budget Act of 1974, the Congressional Budget Office has reviewed S. 2260, Securities—Commodities Accord Amendments of 1982, as ordered reported by the Senate Committee on Banking, Housing and Urban Affairs, May 10, 1982.

CLARIFYING THE JURISDICTION OF THE SECURITIES AND
EXCHANGE COMMISSION AND THE DEFINITION OF SECURITY

JUNE 24, 1982.—Ordered to be printed

Mr. DINGELI, from the Committee on Energy and Commerce,
submitted the following

R E P O R T

[To accompany H.R. 6156]

[Including cost estimate of the Congressional Budget Office]

The Committee on Energy and Commerce, to whom was referred the bill (H.R. 6156) to clarify the jurisdiction of the Securities and Exchange Commission and the definition of security, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. Section 2(1) of the Securities Act of 1933 (15 U.S.C. 77b(1)) is amended by inserting after "mineral rights," the following: "any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency,".

SEC. 2. Section 3(a) (10) of the Securities Exchange Act of 1934 (15 U.S.C. 78c (a) (10)) is amended by inserting after "for a security," the following: "any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency,".

SEC. 3. Section 9 of the Securities Exchange Act of 1934 (15 U.S.C. 781) is amended—

(1) by striking out "this section" in subsection (f) and inserting in lieu thereof "subsection (a)"; and

(2) by inserting after subsection (f) the following new subsection:

"(g) Notwithstanding any other provisions of law, the Commission shall have the authority to regulate the trading of any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency.".

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SEC. 4. Section 28(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78bb(a)) is amended by adding at the end thereof the following new sentence: "No State law which prohibits or regulates the making or promoting of wagering or gaming contracts, or the operation of 'bucket shops' or other similar or related activities, shall invalidate any put, call, straddle, option, privilege, or other security, or apply (except for purposes of chapter 96 of title 18, United States Code) to any activity which is incidental or related to the offer, purchase, sale, exercise, settlement, or closeout of any such instrument, if such instrument is traded pursuant to rules and regulations of a self-regulatory organization that are filed with the Commission pursuant to section 19(b) of this Act."

SEC. 5. Section 2(a) (36) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a) (36)) is amended by inserting after "mineral rights," the following: "any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency,".

SEC. 6. Section 202(a) (18) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a) (18)) is amended by inserting after "mineral rights," the following: "any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency,".

PURPOSE AND SUMMARY

The purpose of H.R. 6156 is to amend the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940 and the Investment Advisers Act of 1940 to expressly include options on securities within the definition of "security" and to clarify the jurisdiction of the Securities and Exchange Commission over options on securities and for certain other purposes.

BACKGROUND

INTRODUCTION

In recent years, the United States financial markets have undergone dramatic and rapid changes. Inflation, high interest rates, a volatile stock market and economic uncertainty have fueled the growth of a number of investment and trading instruments that were either nonexistent or seldom used before the decade of the 1970s. Financial instruments designed to speculate on, or hedge against, fluctuations in interest rates and exchange rates, as well as stock market movements and other economic changes, have proliferated. With the development of innovative financial instruments, the previously drawn lines of regulatory responsibility for these instruments and the markets on which they are traded has become confused. As a result, recently, the SEC's long-standing authority to regulate options on securities and other instruments traded on national securities exchanges has been challenged. Without clarification and confirmation of its authority, the SEC's regulation of the securities and options markets and the SEC's historic mandate to foster the integrity of the markets, protect investors and maintain investor confidence in the markets may be undermined. Thus, capital formation in the form of investments in the U.S. securities markets, may be seriously threatened.

instruments stated under the definition of “security” as amended by this bill.

Section 5 amends Section 2(a) (36) of the Investment Company Act [15 U.S.C. 80a-2(a) (36)], which defines the term “security,” to make it explicit that the term includes “any put, call, straddle, option or privilege on any security including a certificate of deposit, or any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option or privilege entered into on a national securities exchange relating to foreign currency.” The language “any security including a certificate of deposit” recognizes that certificates of deposit have been consistently considered “securities” for the purposes of the Investment Company Act.

Section 6 amends Section 202(a) (18) of the Investment Advisers Act [15 U.S.C. 80b-2(a) (18)], which defines the term “security” to make changes identical to those made in the definition of “security” in the Investment Company Act.

AGENCY VIEWS

The Securities and Exchange Commission testified in support of H.R. 6156 at the hearing on April 23, 1982. The views of the SEC are expressed in the agency’s written statement, which is included in its entirety in the record of those proceedings.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, as shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed in shown in roman):

SECTION 2 OF THE SECURITIES ACT OF 1933

DEFINITIONS

SEC. 2. When used in this title, unless the context otherwise requires—

(1) The term “security” means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for security, fractional undivided interest in oil, gas, or other mineral rights, *any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option or privilege entered into on a national securities exchange relating to foreign currency,* or, in general, any interest or instrument commonly known as a “security”, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

* * * * *

any security or any person insofar as it does not conflict with the provisions of this title or the rules and regulations thereunder. *No State law which prohibits or regulates the making or promoting of wagering or gaming contracts, or the operation of "bucket shops" or other similar or related activities, shall invalidate any put, call, straddle, option, privilege, or other security or apply (except for purposes of chapter 96 of title 18, United States Code) to any activity which is incidental or related to the offer, purchase, sale, exercise, settlement, or closeout of any such instrument, if such instrument is traded pursuant to rules and regulations of a self-regulatory organization that are filed with the Commission pursuant to section 19 (b) of this Act.*

* * * * *

SECTION 2 OF THE INVESTMENT COMPANY ACT OF 1940

GENERAL DEFINITIONS

SEC. 2. (a) When used in this title, unless the context other wise requires—

(1) * * *

* * * * *

(36) "Security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas or other mineral rights, *any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency,* or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

* * * * *

SECTION 202 OF THE INVESTMENT ADVISERS ACT OF 1940

DEFINITIONS

SEC. 202. (a) When used in this title, unless the context otherwise requires—

(1) * * *

* * * * *

(18) "Security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or par-

participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract; voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, *any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency*, or, in general, any interest or instrument commonly known as a “security”, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guaranty of, or warrant or right to subscribe to or purchase any of the foregoing.

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CLARIFYING THE JURISDICTION OF THE SECURITIES AND
EXCHANGE COMMISSION AND THE DEFINITION OF SECURITY

JULY 30, 1982.—Committed to the Committee of the Whole House on the
State of the Union and ordered to be printed

Mr. DE LA GARZA, from the Committee on Agriculture,
submitted the following

R E P O R T

[To accompany H.R. 6156]

[Including Congressional Budget Office cost estimate]

The Committee on Agriculture, to whom was referred the bill (H.R. 6156) to clarify the jurisdiction of the Securities and Exchange Commission and the definition of security, and for other purposes, having considered the same, reports favorably thereon with an amendment and recommends that the bill as amended do pass.

The amendment (stated in terms of the page and line number of the bill as reported by the Committee on Energy and Commerce) is as follows:

Page 4, line 15, after the word “currency” insert the following: “(but not, with respect to any of the foregoing, an option on a contract for future delivery)”.

PURPOSE AND NEED FOR THE LEGISLATION

H.R. 6156 amends the Federal securities laws to provide for jurisdiction of the Securities and Exchange Commission to cover options on exempt securities, stock indexes, certificates of deposit and when traded on national securities exchanges, foreign currencies. The Committee on Agriculture has amended the bill reported by the Committee on Energy and Commerce to specifically exclude from SEC jurisdiction options on any of these contracts for future delivery.

H.R. 6156 is a response to the joint recommendations of SEC and CFTC to resolve disputes that had arisen regarding the jurisdiction of the two agencies. Other proposals recommended by these agencies related to amendments to the Commodity Exchange Act regarding the jurisdiction of the CFTC. Under their joint proposal the CFTC

Section 3 amends section 9 of the Securities Exchange Act (15 U.S.C. 78i) to provide that the SEC's authority over options trading on national securities exchanges extends to options on exempted securities, options on groups and indices of securities, options on certificates of deposit, and, when traded on a national securities exchange, options on foreign currency. It also explicitly provides under an amendment made by this Committee that the SEC has no authority with respect to an option on any such contract for future delivery. Trading in options on contracts for future delivery are governed by the provisions of the Commodity Exchange Act.

Section 4 amends section 28(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78bb(a)) by providing that no state law prohibiting or regulating wagering or gaming contracts or the operation of "bucket shops" or similar activities shall invalidate any "put, call, straddle, option or privilege or other security" or apply (except for purposes of chapter 96 of title 18, United States Code) to any activity related to the offer, purchase, sale, exercise, settlement or closeout of any such instrument if such instrument is approved by the SEC for trading pursuant to the rules of a securities self-regulatory organization. As used in this section, the term "security" would include all instruments stated under the definition of "security" as amended by this bill.

Section 5 amends section 2(a) (36) of the Investment Company Act (15 U.S.C. 80a-2(a) (36)), which defines the term "security," to provide that the term include "any put, call, straddle, option or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option or privilege entered into on a national securities exchange relating to foreign currency."

Section 6 amends section 202(a) (18) of the Investment Advisers Act (15 U.S.C. 80b-2(a) (18)), which defines the term "security" to make changes identical to those made in the definition of "security" in the Investment Company Act.

COMMITTEE CONSIDERATION

A. HEARINGS

The Subcommittee on Conservation, Credit, and Rural Development held a hearing on July 15 to hear testimony on H.R. 6156, a bill to clarify the jurisdiction of the Securities and Exchange Commission and the definition of "security." Witnesses were Representatives Tim Wirth of Colorado and Edward Madigan of Illinois, John Shad, Chairman of the Securities and Exchange Commission, and Phil Johnson, Chairman of the Commodity Futures Trading Commission. Representative Matthew J. Rinaldo of New Jersey also submitted a statement for the record. Representative Berkley Bedell presided over the hearing in the absence of Subcommittee Chairman Ed Jones.

Representative Wirth, Chairman of the Subcommittee on Telecommunications, Consumer Protection, and Finance of the House Energy and Commerce Committee and a cosponsor of H.R. 6156, addressed his comments to both H.R. 6156 and H.R. 5447, which contains the CFTC portion of the joint agency jurisdictional accord. Representative Wirth noted that he had several concerns over that portion of the

the Committee amendment to H.R. 6156. Their testimony is summarized in the committee consideration portion of this report. The joint communication from the Securities and Exchange Commission and the Commodity Futures Trading Commission proposing amendments to the Federal securities and commodities laws to clarify their respective jurisdiction is set forth below:

SECURITIES AND EXCHANGE COMMISSION,
Washington, D.C., February 24, 1982.

Hon. THOMAS P. O'NEILL, Jr.,
Speaker of the House,
U.S. House of Representatives,
Washington, D.C.

DEAR MR. SPEAKER: As you may know, the Securities and Exchange Commission and the Commodity Futures Trading Commission announced on December 7, 1981, that they intended to propose amendments to the federal securities and commodity laws so as to clarify their respective jurisdictions. I am pleased to transmit, on behalf of the Securities and Exchange Commission, the portion of those legislative proposals amending the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, and the Investment Advisers Act of 1940. Attached are a joint explanatory statement and legislative proposals to implement this agreement. We have also furnished copies of these materials to our oversight committee, the House Committee on Energy and Commerce; and we understand that the C.F.T.C. has furnished their portion of the proposal to the House Agriculture Committee.

The views expressed in the accompanying materials are those of the two Commissions and do not necessarily represent the views of the President. These materials are being simultaneously submitted to the Office of Management and Budget. We will inform you of any advice received from that office concerning the relationship of these materials to the program of the Administration.

Sincerely,

JOHN S. R. SHAD.

Enclosures.

[C.F.T.C. Release No. 883-82, S.E.C. Release No. 82-9]

News from the—United States Securities and Exchange
Commission, United States Commodity Futures Trading
Commission

SEC AND CFTC JURISDICTIONAL AGREEMENT: PROPOSED
LEGISLATION

For Release: Tuesday, February 2, 1982.

For Further Information Contact: Andrew Rothman (S.E.C.).
Laurie Buchanan (C.F.T.C.).

The Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC) announced today that they have agreed on proposed legislation to codify the previously announced agreement on the range of

issues regarding the jurisdiction of so-called financial instruments and various related matters.

On December 7, 1981, the two agencies announced that following discussions between SEC Chairman John S.R. Shad and CFTC Chairman Philip McB. Johnson, the Commissions had agreed to certain jurisdictional proposals on their respective regulatory responsibilities and would seek to codify that agreement formally. Since that time each agency has prepared legislative amendments to the affected statutes. Each agency has submitted the draft legislative proposals (a copy of which is attached) to their respective Congressional oversight committees.

Attachment.

JOINT EXPLANATORY STATEMENT OF COMMODITY FUTURES TRADING COMMISSION AND SECURITIES AND EXCHANGE COMMISSION

As announced on December 7, 1981, the Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") have come to an agreement on a range of issues regarding their respective jurisdictions. In connection with this effort, the agencies have prepared draft legislation which, among other things, would clarify the statutes administered by the two agencies. The CFTC and the SEC are transmitting the draft legislative proposals to their respective Congressional committees, with this Statement, which explains a number of issues relating to the agreement. The two agencies urge that these statutory changes be enacted as promptly as possible.

The desirability of a resolution by the two agencies of the issues between them has become increasingly clear. The growing demand for new products related to securities or financial instruments, either as investments or as price hedging tools, has magnified the importance of removing the jurisdictional confusion that has hampered the development of the markets for such instruments. The confusion is a result essentially of amendments in 1974 to the Commodity Exchange Act (the "CEA") that (1) expanded the definition of "commodity" to embrace not only tangible goods but to reach intangible rights and interests, (2) gave the CFTC "exclusive jurisdiction" over agreements and transactions "involving" futures trading in commodities, and (3) inserted in the CEA a qualified proviso to preserve the SEC's preexisting authority over securities trading and the securities markets.

SUMMARY

The two agencies have agreed that the SEC will regulate options on securities and on certificates of deposit (and on all groups or indices of securities or certificates of deposit) and the CFTC will regulate futures contracts on exempted securities (other than municipal securities) and on broad-based groups or indices of any securities, as well as options

on any such futures contracts. No futures contracts (or options on futures contracts) on individual corporate and municipal securities will be permitted to trade. The SEC may also allow options on foreign currency to trade on national securities exchanges, while the CFTC will have jurisdiction to regulate the trading of options on foreign currency in the commodities markets. The attached legislative proposals would specifically codify the agreement of the two agencies by clarifying current law in certain areas.

OPTIONS ON SECURITIES

Since 1973, national securities exchanges have traded options on securities under the regulatory structure administered by the SEC. The proposals to amend the federal securities laws would relate to the SEC's authority to regulate trading in options on securities. The SEC's authority over such trading on exempted securities has been challenged in the United States Court of Appeals for the Seventh Circuit.¹ Thus, one proposal would clarify the definition of "security" in the federal securities laws to include explicitly any option on a security.² In addition, options on foreign currency traded on a national securities exchange and options on certificates of deposit³ would be included within that definition. Under the proposals, the SEC's authority over the trading of securities options also would be clarified by an amendment to Section 9(f) to establish specifically that the SEC's plenary options authority in Section 9(b) of the Exchange Act extends to options on exempted securities and by the addition of Section 9(g) which confirms that SEC's authority to regulate the trading of options on all securities and on certificates of deposit. The same legislative proposal would provide that only the SEC, and not the CFTC, has authority with respect to options directly on underlying securities and securities groups or indices.

Under a series of proposed amendments to the Federal commodity laws, the CEA would not apply to options on securities or securities aggregates, and the CFTC would not be

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¹ *Board of Trade of the City of Chicago v. Securities and Exchange Commission, et al.*, No. 81-1660 (7th Cir., petition for review filed April 24, 1981). (No. 81-2587 (7th Cir., petition for review filed October 5, 1981); and No. 82-1097 (7th Cir., petition for review filed January 21, 1982.

² As a result, an option on an exempted security would expressly be a separate, nonexempted security. Accordingly, a person in the business of effecting transactions in such instruments would, absent an applicable exemption, be required, pursuant to Section 15 of the Securities Exchange Act of 1934 (the "Exchange Act"), to register with the SEC as a broker or dealer. Too [sic] the extent, however, that such a requirement would impose an unnecessary burden on government securities dealers effecting transactions in options on government securities, the SEC has the authority administratively to provide an exemption from that requirement and currently intends to do so.

³ Although the status of certificates of deposit as securities under the Securities Act of 1933 (the "Securities Act") and the Exchange Act is not free from doubt, certificates of deposit have consistently been considered "securities" for the purposes of the Investment Company Act of 1940. In order to emphasize that no change in current law is contemplated, the legislative language used in the two circumstances differs. Thus, for investment company purposes, the relevant portion of the definition of security would read " * * * option * * * on any security including a certificate of deposit," while the corresponding language proposed in the Securities and Exchange Act would read " * * * option * * * on any security, or certificate of deposit * * *."

permitted to designate a board of trade as a contract market for the trading of such instruments. Nevertheless, the CFTC would have exclusive jurisdiction over all permissible futures contracts as well as options on those futures contracts, and would regulate options directly on foreign currencies traded in the commodity markets (but not on a national securities exchange).

FUTURES ON INDIVIDUAL CORPORATE OR MUNICIPAL SECURITIES

Pending further review of appropriate regulatory systems for trading in such futures, the legislative proposal would foreclose the trading of futures (and options on futures) on individual corporate or municipal securities, or contracts based on the value of such a security. Nevertheless, the two agencies intend to study further the issues raised by such trading with a view toward a future recommendation to lift this restriction. This temporary foreclosure of trading does not apply to futures (or options on futures) on exempted securities, except municipal securities.

FUTURES ON SECURITIES INDICES

The CFTC would be permitted under proposed amendments to the CEA to designate a board of trade as a contract market for contracts (or options on such contracts) of sale for future delivery of a securities group or index, but only if the contract (or option on such contract) meets certain specific minimum requirements set forth in the draft legislation as well as other requirements currently in the CEA.

With respect to a futures contract on a securities group or index (or option on such contract), settlement must be effected in cash or by means other than a security on which a futures contract could not be authorized. That is, such a contract could be settled by delivery of an exempted security, such as a security issued or guaranteed by the United States Government, but could not be settled by the transfer or receipt of a corporate or municipal security.

Separate and apart from the present statutory requirement that any contract market have rules to prevent manipulation, the CFTC also would be required to find that trading in the contract under consideration would not be likely to produce manipulation in the futures markets or in related markets, *i.e.*, those for any underlying security, option on such security, or option on a group or index including such securities.⁴

A securities group or index underlying a futures contract must be predominantly composed of the securities of unaffiliated issuers and, in addition, would be required to be a widely published measure of, and to reflect, the market for all

⁴ In order to address concerns relating to the general possibility of inter-market manipulation, the agencies have recommended the CEA be amended to authorize the CFTC to provide trade information to securities self-regulatory organizations and to registered futures associations, as well as to contract markets.

publicly-traded equity or debt securities or a substantial segment of such market, or be comparable to such a measure. This standard is intended to provide adequate flexibility for the market to respond to the needs of participants, while assuring that only broad-based securities index futures contracts that are not conducive to manipulation could be authorized.⁵

In view of the SEC's strong regulatory concern with respect to the trading of futures on securities groups and indices, that agency would be provided a specific role in the process of CFTC designation of a contract market for the trading of such instruments.⁶ The CFTC would be required to consult with the SEC with respect to designation of any board of trade as a contract market for any futures contract involving a securities group or index. Following a mandatory public comment period, the SEC would be provided with a specific time period during which it could object to the designation on the ground that any minimum requirement was not met. If the SEC objected, the CFTC would, if the SEC requested, afford it an opportunity, after the public comment period, for an oral hearing prior to action upon the designation. After the oral hearing, if the SEC continued to maintain its objections, the CFTC would be required to give appropriate weight to the SEC's views in deciding whether to authorize the contract. If, nonetheless, the CFTC designated a board of trade as a contract market for such a futures contract,⁷ the SEC would have the right to judicial review of such order, at which time the court would consider the CFTC's action and the SEC's views. In reviewing the CFTC action, the court would be required to determine, in accordance with the standards of Section 6(b) of the CEA, whether the agency action was supported by the weight of the evidence.

COMMODITY POOLS

While the CFTC has adopted extensive regulations governing the activities of commodity pool operators and has

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⁵ In practice, the two agencies believe that these standards will raise few substantial questions with respect to trading futures on established, widely-used indices containing a number of securities sufficient so that the indices will not be subject to manipulation. As one example, an index of most of the securities traded on a major national securities exchange would appear unlikely to present difficulties. Such indices also would seem more likely to be useful to the marketplace, since they would permit persons such as underwriters or portfolio managers to hedge the risk of overall market movements. However, it appears unlikely that indices not now in existence, based on bonds issued by a group of affiliated companies or on small industry groups, would meet such standards.

⁶ Section 2(a) (8) of the CEA provides a procedure for CFTC solicitation of comments from the U.S. Department of the Treasury and the Board of Governors of the Federal Reserve System ("FRB") with respect to futures contracts involving securities issued or guaranteed by the U.S. government. As agencies concerned with the issuance of such securities and with monetary policy and debt management, the Treasury Department and the FRB clearly have an interest in the CFTC's designation of a market for futures on such instruments. Nevertheless, the SEC, as the regulator of trading markets in municipal and corporate securities, has an even more direct interest in the authorization of a related futures market. Thus, the involvement of the SEC in the designation process is intended to go beyond the relatively informal communications procedure established for the Treasury Department and the FRB.

⁷ If the CFTC refused to grant the application for designation and, pursuant to the CEA, afforded the board of trade an opportunity for a hearing on the record, the SEC would have the right to participate in that hearing as an interested party. Thus, the SEC would be permitted to present evidence and its views and to challenge the arguments advanced by the board of trade in support of its application.

exclusive jurisdiction with respect to “accounts * * * involving” futures, the SEC has taken the position that the activities of a commodity pool as a company, i.e., its formation, capital-raising, and continued corporate existence, are subject to the federal securities laws. The draft legislative language would make this result explicit by stating that nothing in the CEA affects the applicability of the Securities Act and the Exchange Act with respect to securities issued by commodity pools and transactions therein. Of course, the proposed language would not affect the exclusive jurisdiction granted by the CEA with respect to state regulation. Moreover, in appropriate circumstances, commodity pools and persons managing them may be subject to the Investment Advisers Act of 1940 and, if a pool conducts not only a commodities business but also acts as an investment company, the Investment Company Act of 1940.

AMENDMENTS TO THE SECURITIES LAWS, FEBRUARY 1, 1982

SECURITIES ACT OF 1933

Section 2

(1) The term “security” means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, *any put, call, straddle, option, or privilege on any security or certificate of deposit or any put, call, straddle, option or privilege entered into on a national securities exchange relating to foreign currency*, or, in general, any interest or instrument commonly known as a “security”, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase any of the foregoing.

SECURITIES EXCHANGE ACT OF 1934

Section 3 (a)

(10) The term “security” means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit, for a security, *any put, call, straddle, option, or privilege on any security, or certificate of deposit, or any put, call, straddle, option or privilege entered into on a national securities exchange relating to foreign currency* or, in general, any instrument commonly known as a “security”; or any certificate of interest or participation in, temporary or interim

certificate for, receipt for, warrant or right to subscribe to or purchase any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited.

Section 9

(f) The provisions of [this section] *subsection (a)* shall not apply to an exempted security.

(g) *Notwithstanding any other provision of law the Commission shall have the authority to regulate the trading of any option on a security or on a certificate of deposit (but not an option on a contract for future delivery).*

INVESTMENT COMPANY ACT OF 1949

Section 2(a)

(36) "Security" means any note, stock treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, *any put, call, straddle, option, or privilege on any security including a certificate of deposit, or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency*, or, in general, any interest or instrument commonly known as a "security", certificate or interest or participation in, temporary or interim certificate for, receipt for, guarantee of, warrant or right to subscribe to or purchase any of the foregoing.

INVESTMENT ADVISERS ACT OF 1940

Section 202(a)

(19) "Security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, *any put, call, straddle, option, or privilege on any security including a certificate of deposit or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to a foreign currency*, or, in general, any interest or instrument commonly known as a "security", certificate or interest or participation in, temporary or interim certificate for, receipt for, guarantee of, warrant or right to subscribe to or purchase any of the foregoing.

(36) "Security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, *any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency*, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, warrant or right to subscribe to or purchase, any of the foregoing.

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SECTION 202 OF THE INVESTMENT ADVISERS ACT OF 1940

DEFINITIONS

SEC. 202. (a) When used in this title, unless the context otherwise requires—

(1) * * *

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(18) "Security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract; voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, *any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency*, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guaranty of, or warrant or right to subscribe to or purchase any of the foregoing.

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