Futures Markets

Commodity Exchange Act and Commodity Exchange Authority

Leaflet No. 330

U. S. Department of Agriculture

Leading Commodities Covered

- Wheat
- Corn
- Oats
- Rye
- Soybeans
- Grain Sorghums
- Butter
- Eggs
- Potatoes
- Cotton
- Wool Tops
- Cottonseed Oil
- Soybean Oil
- Lard
- Cottonseed Meal
- Soybean Meal
- Bran
- Shorts

Contract Markets

- Chicago Board of Trade
- Chicago Mercantile Exchange
- Chicago Open Board of Trade
- Duluth Board of Trade
- Kansas City Board of Trade
- Los Angeles Grain Exchange
- Memphis Merchants Exchange Clearing Association
- Milwaukee Grain Exchange
- Minneapolis Grain Exchange
- New Orleans Cotton Exchange
- New York Cotton Exchange
- New York Mercantile Exchange
- New York Produce Exchange
- Portland Grain Exchange
- San Francisco Grain Exchange
- Seattle Grain Exchange
- St. Louis Merchants' Exchange
- Wool Associates of the New York Cotton Exchange, Inc.

Issued August 1952

The Commodity Exchange Act

THIS is the Federal law which regulates futures trading in agricultural commodities on the Chicago Board of Trade, the New York Cotton Exchange, and 16 other commodity futures markets.

The original act was the Grain Futures Act of 1922. In 1936 the law was strengthened and amended to include other commodities than grain, and its short title was changed to Commodity Exchange Act. In 1938 and 1940 additional commodities were added by amendments to the law.

The act is based upon the power of Congress to regulate interstate commerce. Its constitutionality was upheld by the United States Supreme Court in 1923.

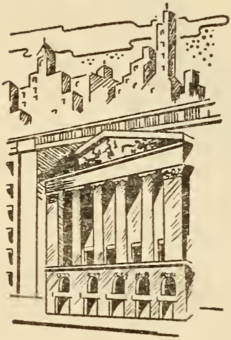
In effect, the law provides that all futures transactions in commodities covered by the act must be made on an exchange designated as a contract market.

The act prohibits undesirable practices and transactions, such as:

- Price manipulation and cornering of a commodity.
- Cheating or defrauding of customers.
- Making false reports to customers.
- Disseminating false crop or market information.
- "Bucketing" of orders, and bucket shops.
- "Wash" sales and other fictitious transactions.
- "Puts," "calls," or "privileges."

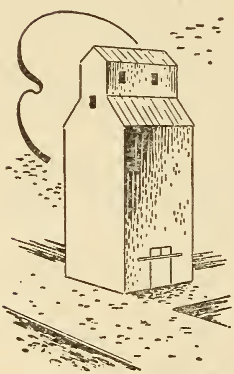
The Commodity Exchange Act

Requires Exchanges To Be Designated as "Contract Markets"



Any exchange or board of trade desiring to conduct a futures market in any commodity named in the act must first be designated by the Secretary of Agriculture as a "contract market," and must conform with requirements specified in the act.

An exchange, to be designated as a contract market, must meet certain conditions, including:



Location at a terminal market, with sufficient cash sales to reflect values, and official inspection service approved by the Secretary of Agriculture.[1]

Provision for keeping records and filing reports prescribed by the Secretary.

Provision for prevention of price manipulation and cornering and the sending out of false or misleading crop or market information by the exchange or its members.

Admission of cooperatives to membership on equal terms with others.

---

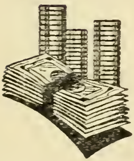
[1] An exchange located elsewhere is eligible if it provides for deliveries of commodities at a delivery point or points and on conditions approved by the Secretary of Agriculture.

Requires Futures Commission Merchants and Floor Brokers To Be Registered

All persons who handle or execute orders for others must register each year with the Secretary of Agriculture. This covers:

Futures Commission Merchants (commonly referred to as brokerage firms), including individuals, associations, partnerships, corporations, and trusts engaged in soliciting or in accepting orders to buy or sell commodity futures, and

Floor Brokers, who execute orders for others in the trading "pit" or "ring" on an exchange floor.



Provides for Protection of Customers' Funds

A futures commission merchant must keep customers' funds separate from his own capital.

He may not use customers' funds in his own business.

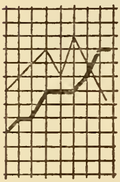
He may not use funds belonging to one customer to finance the trades of another customer.

He may deposit customers' funds in a bank or invest them in certain kinds of securities.

Specifies the Commodities Covered

The act defines "commodity" to mean wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, Solanum tuberosum (Irish potatoes), wool tops, fats and oils (including lard, tallow, cottonseed oil, peanut oil, soybean oil, and all other fats and oils), cottonseed meal, cottonseed, peanuts, soybeans and soybean meal.

Commodity Exchange Act



Limits Large-Scale Speculation

The act authorizes the fixing of limits on the amount of speculative purchases or sales by a person on one day and the amount of his speculative holdings of futures.

Provides Two Means of Dealing With Violations

Criminal proceedings: Violations of certain sections of the Commodity Exchange Act are criminal offenses, and proceedings may be instituted in a United States District Court. Upon conviction, a person may be fined not more than $10,000 and imprisoned for not more than 1 year, or both.

Administrative proceedings before the Secretary of Agriculture: Any person who is found, after hearings, to have violated any provision of the act may be denied trading privileges on all contract markets by the Secretary of Agriculture. The Secretary may also suspend or revoke the registration of futures commission merchants or floor brokers found guilty of violating the act. Orders of the Secretary may be appealed to a United States Court of Appeals.

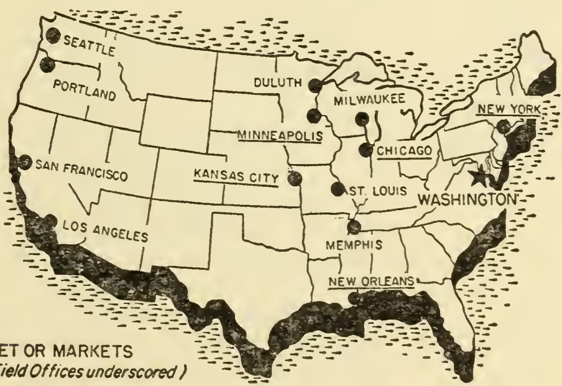
The Commodity Exchange Authority

of the United States Department of Agriculture

The Commodity Exchange Authority is the agency of the U. S. Department of Agriculture acting for the Secretary of Agriculture in the administration and enforcement of the Commodity Exchange Act. The act confers upon the Secretary of Agriculture the principal powers for enforcement of the law, including authority to issue rules and regulations to carry out its provisions.

The Commodity Exchange Authority also acts for the Commodity Exchange Commission, consisting of the Secretary of Agriculture, the Secretary of Commerce, and the Attorney General, which has certain responsibilities under the act, principally with respect to fixing of limits on speculative trading by any person and to violations of the law by contract markets.

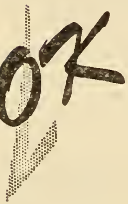
The Commodity Exchange Authority has approximately 120 employees. Its headquarters are in Washington, D. C., and it has field offices in Chicago, New York, New Orleans, Kansas City, and Minneapolis. The map below shows the location of the CEA field offices and the cities with one or more contract markets (see list inside front cover).



● CONTRACT MARKET OR MARKETS
(Cities with CEA Field Offices underscored)

Enforcement of the Commodity Exchange Act involves five principal kinds of work.

1. Contract Market Designation and Broker Registration



An exchange wishing to conduct futures trading in a commodity must make an application. This is reviewed to insure conformity with the act before the exchange is designated as a contract market for the commodity.

All new or proposed rules, regulations, and bylaws of contract markets are examined to see that they are not contrary to the act.

Each year applications of futures commission merchants and floor brokers are received and registrations issued. As of June 30, 1951, 762 floor brokers and 578 futures commission merchants were registered. The latter had 1780 principal and branch offices located in the United States and 12 foreign countries.

2. Audits of Brokerage Firms

To prevent misuse of customers' funds and see that separate accounting records are kept and the funds segregated, accountants of the Commodity Exchange Authority make audits of the books of futures commission merchants.

In the year ended June 30, 1951, the audits numbered 641. The accounts examined totaled 25,787. The amount of customers' funds was $145,602,818.

Generally the audits show that most futures commission merchants are complying with the requirements of the act. In some instances, however, audits show that all customers' funds are not segregated, or that customers' funds are improperly transferred or mixed with those of the brokerage firm. The audits also uncover other types of violations.

Many such instances are the result of carelessness or misunderstanding, and are promptly corrected. In more serious cases, the necessary procedures are used to obtain compliance with the law.

3. Dealing With Questionable Practices and Violations of the Act

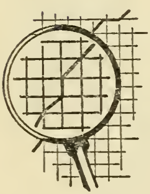
Instances occur in which customers are cheated or defrauded, and there are some cases of bucketing of customers' orders, "wash" or fictitious trades, or other illegal practices.

There are attempts by traders to manipulate or move futures prices up or down artificially to their own advantage, or to corner the market.

Transactions or practices which appear to be in violation of the act are brought to light in various ways—through complaints, audits of books and records, examination of reports, special trade practice surveys of exchange trading, and other means.

The CEA has investigators and accountants who examine records and talk with persons involved, to bring out the actual facts in each instance, and determine whether there has been a violation of the law. In this way evidence is brought together and, where justified, administrative or criminal proceedings are instituted.

4. Supervision Over Daily Trading



Constant watch is kept over operations and conditions in the futures markets to preserve their open competitive status. This constant watch is a way of learning quickly about unusual market conditions. It reveals from the early stages, for example, the build-up of large traders' positions, which unchecked may result in price manipulation, corners or "squeezes."

As one means of knowing what is happening in the markets, employees of the CEA are frequently on the floors of the principal exchanges while trading is going on and field office supervisors are in contact with officers and committees of exchanges.

Another means is the system of required reports. Daily reports by futures commission merchants give the total amount or volume of trading and the open contracts in each future and commodity. Reports by large traders give detailed facts on their operations. Figures on prices, deliveries on futures contracts, stocks of cash commodities, and other basic facts affecting the futures market are brought together.

To get the most value from these daily reports quickly, tabulations are made by electric tabulating equipment in the larger field offices. Trading analysts of the CEA examine the reports and summary figures to see whether there are artificial forces in the markets and discover possible violations of the act.

This system of reports is the basis for the release of factual data on futures trading. Such data were not available to the public until Federal regulation began. Releases are issued daily giving the figures on volume of trading and open contracts. These are carried regularly by wire services and newspapers.

5. Limits on Speculation by Large Traders

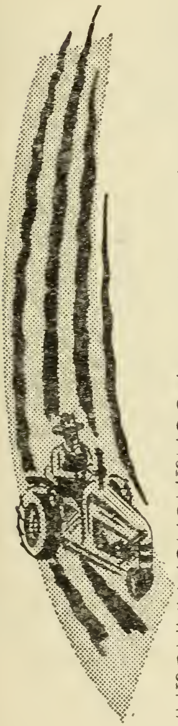
The history of futures markets has been highlighted with cases of big speculators manipulating prices up or down by the size of their trading. The Hutchinson, Leiter, and Cutten cornering operations involving millions of bushels of grain futures on the Chicago Board of Trade, and the Patton corner in cotton futures on the New York Cotton Exchange, are bywords in the earlier story of the futures markets.

As one means of preventing large-scale operations by market "plungers," the Commodity Exchange Act amendments of 1936 authorize the Commodity Exchange Commission to fix limits on the amount of any person's speculative trading and open contracts. In the following years evidence prepared by economists and trading analysts of the Commodity Exchange Authority on the effects of large-scale trading in various commodities upon prices was given at public hearings of the Commodity Exchange Commission.

In 1951, limits were in effect on speculative transactions in grain, soybean, cotton, and egg futures. Existing limits may be changed after hearings before the Commission, and limits may be placed on other commodities. The limits, specifying fixed amounts in bushels, bales, or carlots, in general prevent an individual trader from having trades or positions amounting to more than 2 or 3 percent of all open contracts.

To see that traders do not exceed the limits, the Commodity Exchange Authority keeps constant watch over large operators in the markets. Regular and systematic scrutiny of daily reports required from large traders, examination of brokerage-firm records, and other means, are used for enforcement of the limits on speculative trading.

Value and Volume of Trading

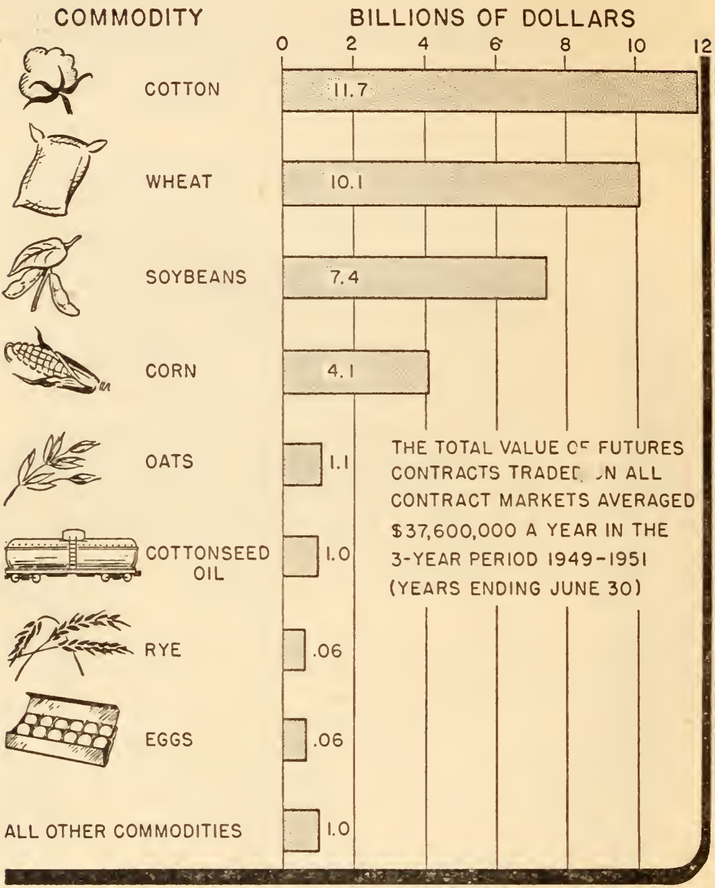


The total dollar value of futures trading in commodities regulated under the Commodity Exchange Act was approximately 47 billion dollars in the year ended June 30, 1951. The leading commodity in that year was cotton, in which futures trading had an estimated value of 16.7 billion dollars. Futures trading in wheat ranked second, with 11.1 billion dollars, and soybean trading was third with 8.9 billions.

The table below gives the volume of trading in the year ended June 30, 1951, in terms of physical quantities, for all commodities and contract markets under the Commodity Exchange Act.

Commodity	*Unit*	*Volume of trading*
Wheat	1,000 bushels	4, 675, 715
Corn	do	2, 236, 588
Oats	do	1, 617, 253
Rye	do	576, 216
Soybeans	do	2, 952, 610
Flaxseed	do	5, 607
Grain sorghums	do	41, 225
Rice	1,000 pounds	2, 880
Cotton	1,000 bales	79, 067
Wool tops	1,000 pounds	82, 780
Butter	Carlots	3, 236
Eggs	do	148, 811
Potatoes	do	2, 627
Cottonseed oil	1,000 pounds	7, 331, 700
Soybean oil	do	3, 532, 620
Lard	do	2, 213, 080
Bran	Tons	406, 800
Shorts	do	173, 670
Cottonseed meal	do	586, 800
Soybean meal	do	2, 292, 000

VALUE OF FUTURES TRADING SUPERVISED BY THE COMMODITY EXCHANGE AUTHORITY OVER $37 BILLION ANNUALLY



U. S. GOVERNMENT PRINTING OFFICE: 1952

For sale by the Superintendent of Documents, U. S. Government Printing Office
Washington 25, D. C. - Price 5 cents