

Page 1 of \* 175

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
Form 19b-7

File No.\* SR - 2014 - \* 001

Amendment No. (req. for Amendments \*)

**Proposed Rule Change by \* CBOE Futures Exchange**

Pursuant to Rule 19b-7 under the Securities Exchange Act of 1934

Initial \*

Amendment \*

Withdrawal

Exhibit 2 Sent As Paper Document

Exhibit 3 Sent As Paper Document

**Description**

Provide a brief description of the proposed rule change (limit 250 characters, required when Initial is checked \*).

Proposed rule change relating to certain customer protection and financial rules.

**Contact Information**

Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name \*

Eric

Last Name \*

Seinsheimer

Title \*

Assistant Secretary

E-mail \*

seinsheimer@cboe.com

Telephone \*

(312) 786-8740

Fax

(312) 786-7919

**SRO Governing Body Action**

Describe action on the proposed rule change taken by the members or board of directors or other governing body of the SRO (limit 250 characters, required \*).

CFE's Senior Managing Director approved the proposed rule change on April 11, 2014 pursuant to delegated authority.

**Signature**

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized officer.

Date

04/11/2014

Assistant Secretary

By

Jenny L. Golding

(Name \*)

(Title \*)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Persona Not Validated - 1382733830495,

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-7 instructions please refer to the EFFS website.

**Exhibit 1- Notice of Proposed Rule Change (required when Initial)**

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal.

The Notice section of this Form 19b-7 must comply with the guidelines for publication in the Federal Register, as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC and CFTC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases and Commodities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2- Notices, Written Comments, Transcripts, Other Communications**

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction E, they shall be filed in accordance with Instruction F.

Exhibit Sent As Paper Document



**Exhibit 3 - Form, Report, or Questionnaire**

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Exhibit Sent As Paper Document



Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change. If such documents cannot be filed electronically in accordance with Instruction E, they shall be filed in accordance with Instruction F.

**Exhibit 4 - Proposed Rule Text**

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The self-regulatory organization must attach as Exhibit 4 proposed changes to rule text. Exhibit 4 shall be considered part of the proposed rule change.

**Exhibit 5 - Date of Effectiveness of Proposed Rule Change (required when Initial)**

The self-regulatory organization must attach one of the following:

- CFTC Certification
- CFTC Request that Review of Proposed Rule Change is not Necessary
- Request for CFTC Approval of Proposed Rule Change
- CFTC Determination that Review of Proposed Rule Change is not Necessary
- Indication of CFTC Approval of Proposed Rule Change

CFTC Certification: Attach a copy of the certification submitted to the CFTC pursuant to section 5c(c) of the Commodity Exchange Act.

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Exhibit Sent As Paper Document



**Partial Amendment**

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission staff's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

Exhibit 1

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34- ; File No. SR-CFE-2014-001)

Self-Regulatory Organizations; CBOE Futures Exchange, LLC; Proposed Rule Change to Adopt and Amend Certain Customer Protection and Financial Rules

Pursuant to Section 19(b)(7) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> notice is hereby given that on April 11, 2014 CBOE Futures Exchange, LLC (“CFE” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change described in Items I, II, and III below, which Items have been prepared by CFE. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons. CFE also has filed this proposed rule change with the Commodity Futures Trading Commission (“CFTC”). CFE filed a written certification with the CFTC under Section 5c(c) of the Commodity Exchange Act (“CEA”)<sup>2</sup> on April 11, 2014.

I. Self-Regulatory Organization's Description of the Proposed Rule Change

The Exchange proposes to adopt and amend certain customer protection and financial rules that are applicable to security futures traded on CFE. The only security futures currently traded on CFE are traded under Chapter 16 of CFE's Rulebook which is applicable to Individual Stock Based and Exchange-Traded Fund Based Volatility Index security futures. The rule amendments included as part of this rule change relate generally to amending CFE Rules to incorporate new and amended CFTC regulations concerning customer protection and the financial surveillance of futures commission merchants (“FCMs”). The text of the proposed rule change is attached as Exhibit 4.

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<sup>1</sup> 15 U.S.C. 78s(b)(7).

<sup>2</sup> 7 U.S.C. 7a-2(c).

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, CFE included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. CFE has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, Proposed Rule Change

1. Purpose

The purpose of the proposed CFE rule amendments included as part of this rule change is to amend CFE rules (i) to incorporate the final regulations adopted by the CFTC under the caption Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations ("CFTC Rulemaking")<sup>3</sup> and (ii) to enhance the financial surveillance of FCMs that are Trading Privilege Holders ("TPHs"). The rule amendments included as part of this rule change are to apply to all products traded on CFE, including both non-security futures and security futures. CFE is making these rule amendments in conjunction with other rule amendments being made by CFE consistent with the CFTC Rulemaking that are not required to be submitted to the Commission pursuant to Section 19(b)(7) of the Act<sup>4</sup> and thus are not included as part of this rule change.

CFE has incorporated into Appendix to Chapter 5 of its Rulebook certain CFTC regulations relating to customer protection, recordkeeping, and reporting and has

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<sup>3</sup> 78 FR 68506 (Nov. 14, 2013).

<sup>4</sup> 15 U.S.C. 78s(b)(7).

provided that a violation of any of those regulations shall be deemed a violation of a specific CFE Rule. With the exception of the amendments to CFE Rule 503A, all other amendments to CFE Rules contained in this filing are proposed to change the CFE Rules in the Appendix to Chapter 5 of the CFE Rulebook to make their language consistent with the language in the CFTC regulations that was amended by the CFTC Rulemaking.

CFE already requires that its FCMs that are TPHs comply with all CFTC regulations. For example, CFE Rule 604 prohibits TPHs and their Related Parties from engaging in conduct in violation of Applicable Law (which includes, among other things, the CEA<sup>5</sup> and CFTC regulations). CFE Rule 505 specifically requires TPHs to comply with CFTC regulations relating to the treatment of Customer funds and the maintenance of related books and records. CFE Rule 518 specifically requires TPHs to comply with CFTC regulations relating to minimum financial requirements, financial reporting requirements, and protection of customer funds that are set forth in the Appendix to Chapter 5 of the CFE Rulebook. The purpose of these proposed rule amendments is to make the CFTC regulations that were added or amended by the CFTC Rulemaking even more explicit.

#### Risk Management Program for FCMs

CFE is proposing to add to its Rules new Rule 520 (and renumber all subsequent Rules in the Chapter) to require that FCMs comply with the risk management requirements set forth in CFTC Regulation 1.11: *Risk Management Program for futures commission merchants*.<sup>6</sup> As a result of the CFTC Rulemaking, CFTC Regulation 1.52(b)(2) requires that all self-regulatory organizations (“SROs”) (defined as designated

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<sup>5</sup> 7 U.S.C. 1 *et seq.*

<sup>6</sup> 17 CFR 1.11.

contract markets and registered futures associations in CFTC Regulation 1.52(a)(2)) adopt rules prescribing risk management requirements for FCM member registrants that are at least as stringent as the requirements contained in CFTC Regulation 1.11.<sup>7</sup> CFTC Regulation 1.11 imposes, among other things, both recordkeeping and reporting requirements on FCMs. Specifically, FCMs must maintain their risk management policies and procedures, all written approvals, and all records and reports required under the Regulation.<sup>8</sup> In addition, FCMs must furnish a copy of their risk management policies and procedures to the CFTC and its designated SRO upon application for registration and thereafter upon request, as well as furnish copies of Risk Exposure Reports to the CFTC.<sup>9</sup> Although all FCMs that are TPHs must already comply with all CFTC Regulations, new CFE Rule 520 is proposed specifically to follow the CFTC Rulemaking's directive with respect to CFTC Regulation 1.11.

#### Recordkeeping

The recordkeeping amendments proposed to be included in the Appendix to Chapter 5 of the CFE Rulebook would impose requirements that generally already exist under CFE Rules 505, 518, and 604, which, as discussed, require adherence to CFTC regulations. The amendments to certain CFTC regulations by the CFTC Rulemaking will now be specifically incorporated into CFE's rules. In particular, CFE is proposing to amend CFE Rule 521 which incorporates into CFE's Rulebook CFTC Regulation 1.18 (Minimum Financial Requirements for Futures Commission Merchants and Introducing Brokers),<sup>10</sup> CFE Rule 523 which incorporates into CFE's Rulebook CFTC Regulation

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<sup>7</sup> 17 CFR 1.52.

<sup>8</sup> 17 C.F.R. 1.11(c)(2), (h).

<sup>9</sup> 17 C.F.R. 1.11(c)(4), (e)(2)(ii).

<sup>10</sup> 17 CFR 1.18.

1.20 (Futures Customer Funds to be Segregated and Separately Accounted for),<sup>11</sup> CFE Rule 526 which incorporates into CFE's Rulebook CFTC Regulation 1.23 (Interest of Futures Commission Merchants in Segregated Futures Customer Funds; Additions and Withdrawals),<sup>12</sup> CFE Rule 528 which incorporates into CFE's Rulebook CFTC Regulation 1.25 (Investment of Customer Funds),<sup>13</sup> CFE Rule 529 which incorporates into CFE's Rulebook CFTC Regulation 1.26 (Deposit of Instruments Purchased with Futures Customer Funds),<sup>14</sup> and CFE Rule 535 which incorporates into CFE's Rulebook CFTC Regulation 1.32 (Reporting of Segregated Account Computation and Details Regarding the Holding of Futures Customer Funds).<sup>15</sup>

### Reporting

As CFE is proposing to do with various recordkeeping requirements, CFE is also proposing to specifically incorporate into the Appendix to Chapter 5 of its Rulebook the CFTC Rulemaking's amendments to CFTC regulations relating to reporting. Like with the foregoing amended recordkeeping requirements, the reporting amendments to this regulation would impose requirements that generally already exist under CFE Rules 505, 518, and 604, which, as discussed, require adherence to CFTC regulations. These amendments by the CFTC Rulemaking will now be specifically incorporated into CFE's rules. In particular, CFE is proposing to amend CFE Rule 519 which incorporates into CFE's Rulebook CFTC Regulation 1.10 (Financial Reports of Futures Commission

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<sup>11</sup> 17 CFR 1.20.

<sup>12</sup> 17 CFR 1.23.

<sup>13</sup> 17 CFR 1.25.

<sup>14</sup> 17 CFR 1.26.

<sup>15</sup> 17 CFR 1.32. CFE notes that certain of these amendments relate to both recordkeeping and reporting (discussed in the next section) but is only including discussion of them in this section to avoid duplicative mention.

Merchants and Introducing Brokers)<sup>16</sup> and CFE Rule 520 which incorporates into CFE's Rulebook CFTC Regulation 1.12 (Maintenance of Minimum Financial Requirements by Futures Commission Merchants and Introducing Brokers).<sup>17</sup>

In addition to the foregoing amendments that incorporate the CFTC Rulemaking, CFE is proposing amendments to CFE Rule 503A, which relate to reporting obligations on FCMs and are not related to the CFTC Rulemaking. CFE Rule 503A, which presently imposes reporting obligations on FCMs that are TPHs, is proposed to be amended to require these FCMs to file financial documentation with CFE in addition to the documentation the Rule already requires. First, each TPH that is an FCM would be required, in a form and manner prescribed by the Exchange, to concurrently file with the Exchange all FOCUS Report Part III submissions as well as any attachments or related submissions to all Form 1-FR-FCM, Form 1-FR-IB, or FOCUS Report Part II, Part IIA or Part II CSE and Part III submissions. Second, each TPH that is an FCM would be required, in a form and manner prescribed by the Exchange, to concurrently file with the Exchange a copy of any daily Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges filed with the CFTC pursuant to CFTC Regulation 1.32. Third, each TPH that is an FCM would be required, in a form and manner prescribed by the Exchange, to concurrently file with the Exchange a copy of any daily net capital filings submitted by the TPH to its Designated Self-Regulatory Organization. Fourth, each TPH that is an FCM would be required, in a form and manner prescribed by the Exchange, to concurrently file with the Exchange a copy of

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<sup>16</sup> 17 CFR 1.10.

<sup>17</sup> 17 CFR 1.12.

any notice that is filed with the CFTC pursuant to CFTC Regulation 1.23. The receipt of this information will enhance CFE's financial surveillance of FCMs.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,<sup>18</sup> in general, and furthers the objectives of Section 6(b)(5)<sup>19</sup> in particular in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanism of a free and open market and a national market system, and in general, to protect investors and the public interest.

The addition of new CFE Rule 520, which requires FCMs to establish risk management programs that comply with CFTC Regulation 1.11, will enhance CFE's ability to protect investors and the public interest and to enforce CFE Rules that prohibit fraudulent and manipulative acts and conduct inconsistent with just and equitable principles of trade. By specifically requiring that FCMs that are TPHs establish risk management programs that comply with CFTC Regulation 1.11, CFE further protects FCM customers.

The recordkeeping amendments to CFE Rules 521, 523, 526, 528, 529, and 535 and the reporting amendments to CFE Rules 503A, 519, and 520 will also enhance CFE's ability to protect investors and the public interest and to enforce CFE Rules that prohibit fraudulent and manipulative acts and conduct inconsistent with just and equitable principles of trade. These recordkeeping requirements are designed to ensure that TPHs

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<sup>18</sup> 15 U.S.C. 78f(b).

<sup>19</sup> 15 U.S.C. 78f(b)(5).

maintain records that enable CFE and/or other regulators to investigate whether TPHs are complying with applicable rules and regulations by requiring the maintenance of information that may be reviewed to determine whether or not a TPH is complying with applicable regulatory requirements. Similarly, these reporting requirements are designed to enable CFE to receive and request information that allows CFE to monitor for compliance with rules and regulations, to investigate for noncompliance when appropriate, and to conduct financial monitoring with regard to TPHs that are FCMs.

**B. Self-Regulatory Organization's Statement on Burden on Competition**

CFE does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act, in that the rule change makes enhancements to CFE's financial surveillance of FCMs and requires TPHs to comply with the amendments set forth in the CFTC Rulemaking. The Exchange believes that the proposed rule change is equitable and not unfairly discriminatory because all of the amended Rules would apply equally to all TPHs that are subject to the applicable requirements, and the Amendment is expressly consistent with the CFTC Rulemaking.

**C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

No written comments were solicited or received with respect to the proposed rule change.

**III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

The proposed rule change will become effective on April 28, 2014.

At any time within 60 days of the date of effectiveness of the proposed rule change, the Commission, after consultation with the CFTC, may summarily abrogate the

proposed rule change and require that the proposed rule change be refiled in accordance with the provisions of Section 19(b)(1) of the Act.<sup>20</sup>

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic comments:

- Use the Commission's Internet comment form  
<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-CFE-2014-001 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-CFE-2014-001. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for

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<sup>20</sup> 15 U.S.C. 78s(b)(1).

inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. Copies of such filing also will be available for inspection and copying at the principal office of CBOE Futures Exchange, LLC. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-CFE-2014-001 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>21</sup>

Secretary

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<sup>21</sup> 17 CFR 200.30-3(a)(73).

**Exhibit 4**

Set forth below are proposed changes to the rule text, with additions represented by underscoring and deletions represented by [bracketing].

### **CBOE Futures Exchange, LLC Rules**

#### **503A. Reporting by Futures Commission Merchants and Introducing Brokers**

- (a) Each Trading Privilege Holder that is a Futures Commission Merchant or Introducing Broker shall, in a form and manner prescribed by the Exchange, concurrently file with the Exchange a copy of all Form 1-FR-FCM, Form 1-FR-IB or FOCUS Report Part II, Part IIA or Part II CSE and Part III submissions (including any attachments or related submissions), as applicable, made by the Trading Privilege Holder.
- (b) Each Trading Privilege Holder that is a Futures Commission Merchant shall, in a form and manner prescribed by the Exchange, concurrently file with the Exchange a copy of any daily Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges filed with the Commission pursuant to Commission Regulation § 1.32.
- (c) Each Trading Privilege Holder that is a Futures Commission Merchant shall, in a form and manner prescribed by the Exchange, concurrently file with the Exchange a copy of any daily net capital filings submitted by the Trading Privilege Holder to its Designated Self-Regulatory Organization.
- ([b]d) Each Trading Privilege Holder that is a Futures Commission Merchant and (i) is not Clearing Member or (ii) is a Clearing Member that utilizes another Clearing Member for purposes of clearing Exchange Contracts shall, in a form and manner prescribed by the Exchange, provide a report to the Exchange on a daily basis which sets forth the positions, if any, in Exchange Contracts of the Trading Privilege Holder's customers held by any Clearing Member in the customer range at the Clearing Corporation.
- (e) Each Trading Privilege Holder that is a Futures Commission Merchant shall, in a form and manner prescribed by the Exchange, concurrently file with the Exchange a copy of any notice that is filed with the Commission pursuant to Commission Regulation § 1.23.

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#### **519. Compliance with Commission Regulation 1.10 – Financial Reports of Futures Commission Merchants and Introducing Brokers**

Any Trading Privilege Holder subject to Commission Regulation 1.10 that violates Commission Regulation 1.10 shall be deemed to have violated this Rule 519. Commission Regulation 1.10 is set forth below and incorporated into this Rule 519.

Commission Regulation 1.10 - Financial reports of futures commission merchants and introducing brokers.

(a) *Application for registration.* (1) Except as otherwise provided, a futures commission merchant or an applicant for registration as a futures commission merchant, in order to satisfy any requirement in this part that it file a Form 1-FR, must file a Form 1-FR-FCM, and any reference in this part to Form 1-FR with respect to a futures commission merchant or applicant therefor shall be deemed to be a reference to Form 1-FR-FCM. Except as otherwise provided, an introducing broker or an applicant for registration as an introducing broker, in order to satisfy any requirement in this part that it file a Form 1-FR, must file a Form 1-FR-IB, and any reference in this part to Form 1-FR with respect to an introducing broker or applicant therefor shall be deemed to be a reference to Form 1-FR-IB.

(2) (i) (A) Except as provided in paragraphs (a)(3) and (h) of this section, each person who files an application for registration as a futures commission merchant and who is not so registered at the time of such filing, must, concurrently with the filing of such application, file either:

(1) A Form 1-FR-FCM certified by an independent public accountant in accordance with §1.16 as of a date not more than 45 days prior to the date on which such report is filed; or

(2) A Form 1-FR-FCM as of a date not more than 17 business days prior to the date on which such report is filed and a Form 1-FR-FCM certified by an independent public accountant in accordance with §1.16 as of a date not more than one year prior to the date on which such report is filed.

(B) Each such person must include with such financial report a statement describing the source of his current assets and representing that his capital has been contributed for the purpose of operating his business and will continue to be used for such purpose.

(ii) (A) Except as provided in paragraphs (a)(3) and (h) of this section, each person who files an application for registration as an introducing broker and who is not so registered at the time of such filing, must, concurrently with the filing of such application, file either:

(1) A Form 1-FR-IB certified by an independent public accountant in accordance with §1.16 as of a date not more than 45 days prior to the date on which such report is filed;

(2) A Form 1-FR-IB as of a date not more than 17 business days prior to the date on which such report is filed and a Form 1-FR-IB certified by an independent public accountant in accordance with §1.16 as of a date not more than one year prior to the date on which such report is filed;

(3) A Form 1-FR-IB as of a date not more than 17 business days prior to the date on which such report is filed, *Provided, however,* that such applicant shall be subject to a review by the applicant's designated self-regulatory organization within six months of registration; or

(4) A guarantee agreement.

(B) Each person filing in accordance with paragraphs (a)(2)(ii)(A) (1), (2) or (3) of this section must include with such financial report a statement describing the source of his current assets

and representing that his capital has been contributed for the purpose of operating his business and will continue to be used for such purpose.

(3)(i) The provisions of paragraph (a)(2) of this section do not apply to any person succeeding to and continuing the business of another futures commission merchant. Each such person who files an application for registration as a futures commission merchant and who is not so registered in that capacity at the time of such filing must file a Form 1-FR-FCM as of the first month end following the date on which his registration is approved. Such report must be filed with the National Futures Association, the Commission and the designated self-regulatory organization, if any, not more than 17 business days after the date for which the report is made.

(ii) The provisions of paragraph (a)(2) of this section do not apply to any person succeeding to and continuing the business of another introducing broker.

(A) Each such person who succeeds to and continues the business of an introducing broker which was not operating pursuant to a guarantee agreement, or which was operating pursuant to a guarantee agreement and was also a securities broker or dealer at the time of succession, who files an application for registration as an introducing broker, and who is not so registered in that capacity at the time of such filing, must file with the National Futures Association either a guarantee agreement with his application for registration or a Form 1-FR-IB as of the first month end following the date on which his registration is approved. Such Form 1-FR-IB must be filed not more than 17 business days after the date for which the report is made.

(B) Each such person who succeeds to and continues the business of an introducing broker which was operating pursuant to a guarantee agreement and which was not also a securities broker or dealer at the time of succession, who files an application for registration as an introducing broker, and who is not so registered in that capacity at the time of such filing, must file with the National Futures Association either a guarantee agreement or a Form 1-FR-IB with his application for registration. If such person files a Form 1-FR-IB with his application for registration, such person must also file a Form 1-FR-IB, certified by an independent public accountant, as of a date no later than the end of the month registration is granted. The Form 1-FR-IB certified by an independent public accountant must be filed with the National Futures Association not more than 45 days after the date for which the report is made.

(b) *Filing of financial reports.* (1)(i) Except as provided in paragraphs (b)(3) and (h) of this section, each person registered as a futures commission merchant must file a Form 1-FR-FCM as of the close of business each month. Each Form 1-FR-FCM must be filed no later than 17 business days after the date for which the report is made.

(ii) In addition to the monthly financial reports required by paragraph (b)(1)(i) of this section, each person registered as a futures commission merchant must file a Form 1-FR-FCM as of the close of its fiscal year, which must be certified by an independent public accountant in accordance with §1.16, and must be filed no later than [90] 60 days after the close of the futures commission merchant's fiscal year: *Provided, however,* that a registrant which is registered with the Securities and Exchange Commission as a securities broker or dealer must file this report not later than the time permitted for filing an annual audit report under §240.17a-5(d)(5) of this title.

(2)(i) Except as provided in paragraphs (b)(3) and (h) of this section, and except for an introducing broker operating pursuant to a guarantee agreement which is not also a securities broker or dealer, each person registered as an introducing broker must file a Form 1-FR-IB semiannually as of the middle and the close of each fiscal year. Each Form 1-FR-IB must be filed no later than 17 business days after the date for which the report is made.

(ii)(A) In addition to the financial reports required by paragraph (b)(2)(i) of this section, each person registered as an introducing broker must file a Form 1-FR-IB as of the close of its fiscal year which must be certified by an independent public accountant in accordance with §1.16 no

later than 90 days after the close of each introducing broker's fiscal year: *Provided, however,* that a registrant which is registered with the Securities and Exchange Commission as a securities broker or dealer must file this report not later than the time permitted for filing an annual audit report under §240.17a-5(d)(5) of this title.

(B) If an introducing broker has filed previously a Form 1-FR-IB, certified by an independent public accountant in accordance with the provisions of paragraphs (a)(2)(ii) or (j)(8) of this section and §1.16 of this part, as of a date not more than one year prior to the close of such introducing broker's fiscal year, it need not have certified by an independent public accountant the Form 1-FR-IB filed as of the introducing broker's first fiscal year-end following the as of date of its initial certified Form 1-FR-IB. In such a case, the introducing broker's Form 1-FR-IB filed as of the close of the second fiscal year-end following the as of date of its initial certified Form 1-FR-IB must cover the period of time between those two dates and must be certified by an independent public accountant in accordance with §1.16 of this part.

(3) The provisions of paragraphs (b)(1) and (b)(2) of this section may be met by any person registered as a futures commission merchant or as an introducing broker who is a member of a designated self-regulatory organization and conforms to minimum financial standards and related reporting requirements set by such designated self-regulatory organization in its bylaws, rules, regulations, or resolutions and approved by the Commission pursuant to Section 4f(b) of the Act and §1.52: *Provided, however,* That each such registrant shall promptly file with the Commission a true and exact copy of each financial report which it files with such designated self-regulatory organization.

(4) Upon receiving written notice from any representative of the National Futures Association, the Commission or any self-regulatory organization of which it is a member, an applicant or registrant, except an applicant for registration as an introducing broker which has filed concurrently with its application for registration a guarantee agreement and which is not also a securities broker or dealer, must, monthly or at such times as specified, furnish the National Futures Association, the Commission or the self-regulatory organization requesting such information a Form 1-FR or such other financial information as requested by the National Futures Association, the Commission or the self-regulatory organization. Each such Form 1-FR or such other information must be furnished within the time period specified in the written notice, and in accordance with the provisions of paragraph (c) of this section.

(5) Each futures commission merchant must file with the Commission the measure of the future commission merchant's leverage as of the close of the business each month. For purpose of this section, the term "leverage" shall be defined by a registered futures association of which the futures commission merchant is a member. The futures commission merchant is required to file the leverage information with the Commission within 17 business days of the close of the futures commission merchant's month end.

(c) *Where to file reports.* (1) Form 1-FR filed by an introducing broker pursuant to paragraph (b)(2) of this section need be filed only with, and will be considered filed when received by, the National Futures Association. Other reports or information provided for in this section will be considered filed when received by the [regional] Regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located (as set forth in §140.02 of this chapter) and by the designated self-regulatory organization, if any; and reports or other information required to be filed by this section by an applicant for registration will be considered filed when received by the National Futures Association. Any report or information filed with the National Futures Association pursuant to this paragraph shall be deemed for all purposes to be filed with, and to be the official record of, the Commission.

(2)(i) [Except as provided in the last sentence of this subparagraph, all] All filings or other notices prepared by a futures commission merchant pursuant to this section [may] must be submitted to the Commission in electronic form using a form of user authentication assigned in accordance

with procedures established by or approved by the Commission, and otherwise in accordance with instructions issued by or approved by the Commission, if the futures commission merchant or a designated self-regulatory organization has provided the Commission with the means necessary to read and to process the information contained in such report. A Form 1–FR required to be certified by an independent public accountant in accordance with §1.16 which is filed by a futures commission merchant must be filed [in paper form and may not be filed] electronically.

(ii) Except as provided in paragraph (h) of this section, all filings or other notices or applications prepared by an introducing broker or applicant for registration as an introducing broker or futures commission merchant pursuant to this section must be filed electronically in accordance with electronic filing procedures established by the National Futures Association. In the case of a Form 1–FR–IB that is required to be certified by an independent public accountant in accordance with §1.16, a paper copy of any such filing with the original manually signed certification must be maintained by the introducing broker or applicant for registration as an introducing broker in accordance with §1.31.

(3) Any information required of a registrant by a self-regulatory organization pursuant to paragraph (b)(4) of this section need be furnished only to such self-regulatory organization and the Commission, and any information required of an applicant by the National Futures Association pursuant to paragraph (b)(4) of this section need be furnished only to the National Futures Association and the Commission.

(4) Any guarantee agreement entered into between a futures commission merchant and an introducing broker in accordance with the provisions of this section need be filed only with, and will be considered filed when received by, the National Futures Association.

(d) *Contents of financial reports.* (1) Each Form 1–FR filed pursuant to this §1.10 which is not required to be certified by an independent public accountant must be completed in accordance with the instructions to the form and contain:

(i) A statement of financial condition as of the date for which the report is made;

(ii) Statements of income (loss) and a statement of changes in ownership equity for the period between the date of the most recent statement of financial condition filed with the Commission and the date for which the report is made;

(iii) A statement of changes in liabilities subordinated to claims of general creditors for the period between the date of the most recent statement of financial condition filed with the Commission and the date for which the report is made;

(iv) A statement of the computation of the minimum capital requirements pursuant to §1.17 as of the date for which the report is made;

(v) For a futures commission merchant only, the statements of segregation requirements and funds in segregation for customers trading on U.S. commodity exchanges and for customers' dealer options accounts, [and] the statement of secured amounts and funds held in separate accounts for [foreign futures and foreign options] 30.7 customers (as defined in §30.1 of this chapter) in accordance with §30.7 of this chapter, and the statement of cleared swaps customer segregation requirements and funds in cleared swaps customer accounts under section 4d(f) of the Act as of the date for which the report is made; and

(vi) In addition to the information expressly required, such [father] further material information as may be necessary to make the required statements and schedules not misleading.

(2) Each Form 1–FR filed pursuant to this §1.10 which is required to be certified by an independent public accountant must be completed in accordance with the instructions to the form and contain:

- (i) A statement of financial condition as of the date for which the report is made;
- (ii) Statements of income (loss), cash flows, changes in ownership equity, and changes in liabilities subordinated to claims of general creditors, for the period between the date of the most recent certified statement of financial condition filed with the Commission and the date for which the report is made: *Provided*, That for an applicant filing pursuant to paragraph (a)(2) of this section the period must be the year ending as of the date of the statement of financial condition;
- (iii) A statement of the computation of the minimum capital requirements pursuant to §1.17 as of the date for which the report is made;
- (iv) For a futures commission merchant only, the statements of segregation requirements and funds in segregation for customers trading on U.S. commodity exchanges and for customers' dealer options accounts, [and] the statement of secured amounts and funds held in separate accounts for [foreign futures and foreign options] 30.7 customers (as defined in §30.1 of this chapter) in accordance with §30.7 of [this chapter] the chapter, and the statement of cleared swaps customers segregation requirements and funds in cleared swaps customer accounts under section 4d(f) of the Act as of the date for which the report is made;
- (v) Appropriate footnote disclosures;
- (vi) A reconciliation, including appropriate explanations, of the statement of the computation of the minimum capital requirements pursuant to §1.17 and, for a futures commission merchant only, the statements of segregation requirements and funds in segregation for customers trading on U.S. commodity exchanges and for customers' dealer option accounts, [and] the statement of secured amounts and funds held in separate accounts for [foreign futures and foreign options] 30.7 customers (as defined in §30.1 of this chapter) in accordance with §30.7 of this chapter, and the statement of cleared swaps customer segregation requirements and funds in cleared swaps customer accounts under section 4d(f) of the Act, in the certified Form 1–FR with the applicant's or registrant's corresponding uncertified most recent Form 1–FR filing when material differences exist or, if no material differences exist, a statement so indicating; and
- (vii) In addition to the information expressly required, such further material information as may be necessary to make the required statements not misleading.

(3) The statements required by paragraphs (d)(2)(i) and (d)(2)(ii) of this section may be presented in accordance with generally accepted accounting principles in the certified reports filed as of the close of the registrant's fiscal year pursuant to paragraphs (b)(1)(ii) or (b)(2)(ii) of this section or accompanying the application for registration pursuant to paragraph (a)(2) of this section, rather than in the format specifically prescribed by these regulations: *Provided*, the statement of financial condition is presented in a format as consistent as possible with the Form 1–FR and a reconciliation is provided reconciling such statement of financial condition to the statement of the computation of the minimum capital requirements pursuant to §1.17. Such reconciliation must be certified by an independent public accountant in accordance with §1.16.

(4) Attached to each Form 1–FR filed pursuant to this section must be an oath or affirmation that to the best knowledge and belief of the individual making such oath or affirmation the information contained in the Form 1–FR is true and correct. The individual making such oath or affirmation must be:

(i) If the registrant or applicant is a sole proprietorship, the proprietor; if a partnership, any general partner; if a corporation, the chief executive officer or chief financial officer; and, if a limited liability company or limited liability partnership, the chief executive officer, the chief financial officer, the manager, the managing member, or those members vested with the management authority for the limited liability company or limited liability partnership; or

(ii) If the registrant or applicant is registered with the Securities and Exchange Commission as a securities broker or dealer, the representative authorized under §240.17a-5 of this title to file for the securities broker or dealer its Financial and Operational Combined Uniform Single Report under the Securities Exchange Act of 1934, part II, part IIA, or part II CSE.

(iii) In the case of a Form 1-FR filed via electronic transmission in accordance with procedures established by or approved by the Commission, such transmission must be accompanied by the user authentication assigned to the authorized signer under such procedures, and the use of such user authentication will constitute and become a substitute for the manual signature of the authorized signer for the purpose of making the oath or affirmation referred to in this paragraph.

(e) *Election of fiscal year.* (1) An applicant wishing to establish a fiscal year other than the calendar year may do so by notifying the National Futures Association of its election of such fiscal year, in writing, concurrently with the filing of the Form 1-FR pursuant to paragraph (a)(2) of this section, but in no event may such fiscal year end more than one year from the date of the Form 1-FR filed pursuant to paragraph (a)(2) of this section. An applicant that does not so notify the National Futures Association will be deemed to have elected the calendar year as its fiscal year.

(2) (i) A registrant must continue to use its elected fiscal year, calendar or otherwise, unless a change in such fiscal year has been approved pursuant to this paragraph (e)(2).

(ii) *Futures commission merchant registrants.* (A) A futures commission merchant may file with its designated self-regulatory organization an application to change its fiscal year, a copy of which the registrant must file with the Commission. The application shall be approved or denied in writing by the designated self-regulatory organization. The registrant must file immediately with the Commission a copy of any notice it receives from the designated self-regulatory organization to approve or deny the registrant's application to change its fiscal year. A written notice of approval shall become effective upon the filing by the registrant of a copy with the Commission, and a written notice of denial shall be effective as of the date of the notice.

(B) A futures commission merchant that is registered with the Securities and Exchange Commission as a securities broker or dealer may file with its designated self-regulatory organization copies of any notice or application filed with its designated examining authority, pursuant to §240.17a-5(d)(1)(i) of this title, for a change in fiscal year or "as of" date for its annual audited financial statement. The registrant must also file immediately with the designated self-regulatory organization and the Commission copies of any notice it receives from its designated examining authority to approve or deny the registrant's request for change in fiscal year or "as of" date. Upon the receipt by the designated self-regulatory organization and the Commission of copies of any such notice of approval, the change in fiscal year or "as of" date referenced in the notice shall be deemed approved under this paragraph (e)(2).

(C) Any copy that under this paragraph (e)(2) is required to be filed with the Commission shall be filed with the regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located, and any copy or application to be filed with the designated self-regulatory organization shall be filed at its principal place of business.

(iii) *Introducing broker registrants.* (A) An introducing broker may file with the National Futures Association an application to change its fiscal year, which shall be approved or denied in writing.

(B) An introducing broker that is registered with the Securities and Exchange Commission as a securities broker or dealer may file with the National Futures Association copies of any notice or application filed with its designated examining authority, pursuant to §240.17a-5(d)(1)(i) of this title, for a change in fiscal year or "as of" date for its annual audited financial statement. The registrant must also file immediately with the National Futures Association copies of any notice it receives from its designated examining authority to approve or deny the registrant's request for change in fiscal year or "as of" date. Upon the receipt by the National Futures Association of copies of any such notice of approval, the change in fiscal year or "as of" date referenced in the notice shall be deemed approved under this paragraph (e)(2).

(f) *Extension of time for filing uncertified reports.* (1) In the event a registrant finds that it cannot file its Form 1-FR, or, in accordance with paragraph (h) of this section, its Financial and Operational Combined Uniform Single Report under the Securities Exchange Act of 1934, part II, part IIA, or part II CSE (FOCUS report), for any period within the time specified in paragraphs (b)(1)(i) or (b)(2)(i) of this section without substantial undue hardship, it may request approval for an extension of time, as follows:

(i) *Futures commission merchant registrants.* (A) A futures commission merchant may file with its designated self-regulatory organization an application for extension of time, a copy of which the registrant must file with the Commission. The application shall be approved or denied in writing by the designated self-regulatory organization. The registrant must file immediately with the Commission a copy of any notice it receives from the designated self-regulatory organization to approve or deny the registrant's request for extension of time. A written notice of approval shall become effective upon the filing by the registrant of a copy with the Commission, and a written notice of denial shall be effective as of the date of the notice.

(B) A futures commission merchant that is registered with the Securities and Exchange Commission as a securities broker or dealer may file with its designated self-regulatory organization a copy of any application that the registrant has filed with its designated examining authority, pursuant to §240.17-a5(l)(5) of this title, for an extension of time to file its FOCUS report. The registrant must also file immediately with the designated self-regulatory organization and the Commission copies of any notice it receives from its designated examining authority to approve or deny the requested extension of time. Upon receipt by the designated self-regulatory organization and the Commission of copies of any such notice of approval, the requested extension of time referenced in the notice shall be deemed approved under this paragraph (f)(1).

(C) Any copy that under this subparagraph (f)(1)(i) is required to be filed with the Commission shall be filed with the regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located.

(ii) *Introducing broker registrants.* (A) An introducing broker may file with the National Futures Association an application for extension of the time, which shall be approved or denied in writing.

(B) An introducing broker that is registered with the Securities and Exchange Commission as a securities broker or dealer may file with the National Futures Association copies of any application that the registrant has filed with its designated examining authority, pursuant to §240.17-a5(l)(5) of this title, for an extension of time to file its FOCUS report. The registrant must also file immediately with the National Futures Association copies of any notice it receives from its designated examining authority to approve or deny the requested extension of time. Upon the receipt by the National Futures Association of a copy of any such notice of approval, the requested extension of time referenced in the notice shall be deemed approved under this paragraph (f)(1)(ii).

(2) In the event an applicant finds that it cannot file its report for any period within the time specified in paragraph (b)(4) of this section without substantial undue hardship, it may file with the National Futures Association an application for an extension of time to a specified date which

may not be more than 90 days after the date as of which the financial statements were to have been filed. The application must state the reasons for the requested extension and must contain an agreement to file the report on or before the specified date. The application must be received by the National Futures Association before the time specified in paragraph (b)(4) of this section for filing the report. Notice of such application must be filed with the regional office of the Commission with jurisdiction over the state in which the applicant's principal place of business is located concurrently with the filing of such application with the National Futures Association. Within ten calendar days after receipt of the application for an extension of time, the National Futures Association shall:

- (i) Notify the applicant of the grant or denial of the requested extension; or
  - (ii) Indicate to the applicant that additional time is required to analyze the request, in which case the amount of time needed will be specified.
- (g) *Public availability of reports.* (1) Forms 1–FR filed pursuant to this section, and FOCUS reports filed in lieu of Forms 1–FR pursuant to paragraph (h) of this section, will be treated as exempt from mandatory public disclosure for purposes of the Freedom of Information Act and the Government in the Sunshine Act and parts 145 and 147 of this chapter, except for the information described in paragraph (g)(2) of this section.
- (2) The following information in Forms 1–FR, and the same or equivalent information in FOCUS reports filed in lieu of Forms 1–FR, will be publicly available:
- (i) The amount of the applicant's or registrant's adjusted net capital; the amount of its minimum net capital requirement under §1.17 of this chapter; and the amount of its adjusted net capital in excess of its minimum net capital requirement; and
  - (ii) The following statements and footnote disclosures thereof: the Statement of Financial Condition in the certified annual financial reports of futures commission merchants and introducing brokers; the Statements (to be filed by a futures commission merchant only) of Segregation Requirements and Funds in Segregation for customers trading on U.S. commodity exchanges and for customers' dealer options accounts, [and] the Statement (to be filed by a futures commission merchant only) of Secured Amounts and Funds held in Separate Accounts for [foreign futures and foreign options customers] 30.7 Customers (as defined in §30.1 of this chapter) in accordance with §30.7 of this chapter, and the Statement (to be filed by futures commission merchants only) of Cleared Swaps Customer Segregation Requirements and Funds in Cleared Swaps Customer Accounts under section 4d(f) of the Act.

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## **520. Compliance with Commission Regulation 1.11 – Risk Management Program for Futures Commission Merchants.**

Any Trading Privilege Holder subject to Commission Regulation 1.11 that violates Commission Regulation 1.11 shall be deemed to have violated this Rule 520. Commission Regulation 1.11 is set forth below and incorporated into this Rule 520.

Commission Regulation 1.11 - Risk management program for futures commission merchants.

(a) Applicability. Nothing in this section shall apply to a futures commission merchant that does not accept any money, securities, or property (or extend credit in lieu thereof) to margin.

guarantee, or secure any trades or contracts that result from soliciting or accepting orders for the purchase or sale of any commodity interest.

(b) Definitions. For purposes of this section:

(1) Business unit means any department, division, group, or personnel of a futures commission merchant or any of its affiliates, whether or not identified as such that:

(i) Engages in soliciting or in accepting orders for the purchase or sale of any commodity interest and that, in or in connection with such solicitation or acceptance of orders, accepts any money, securities, or property (or extends credit in lieu thereof) to margin, guarantee, or secure any trades or contracts that result or may result therefrom; or

(ii) Otherwise handles segregated funds, including managing, investing, and overseeing the custody of segregated funds, or any documentation in connection therewith, other than for risk management purposes; and

(iii) Any personnel exercising direct supervisory authority of the performance of the activities described in paragraph (b)(1)(i) or (ii) of this section.

(2) Customer means a futures customer as defined in §1.3, Cleared Swaps Customer as defined in §22.1 of this chapter, and 30.7 customer as defined in §30.1 of this chapter.

(3) Governing body means the proprietor, if the futures commission merchant is a sole proprietorship; a general partner, if the futures commission merchant is a partnership; the board of directors if the futures commission merchant is a corporation; the chief executive officer, the chief financial officer, the manager, the managing member, or those members vested with the management authority if the futures commission merchant is a limited liability company or limited liability partnership.

(4) Segregated funds means money, securities, or other property held by a futures commission merchant in separate accounts pursuant to §1.20 for futures customers, pursuant to §22.2 of this chapter for Cleared Swaps Customers, and pursuant to §30.7 of this chapter for 30.7 customers.

(5) Senior management means, any officer or officers specifically granted the authority and responsibility to fulfill the requirements of senior management by the governing body.

(c) Risk Management Program. (1) Each futures commission merchant shall establish, maintain, and enforce a system of risk management policies and procedures designed to monitor and manage the risks associated with the activities of the futures commission merchant as such. For purposes of this section, such policies and procedures shall be referred to collectively as a "Risk Management Program."

(2) Each futures commission merchant shall maintain written policies and procedures that describe the Risk Management Program of the futures commission merchant.

(3) The Risk Management Program and the written risk management policies and procedures, and any material changes thereto, shall be approved in writing by the governing body of the futures commission merchant.

(4) Each futures commission merchant shall furnish a copy of its written risk management policies and procedures to the Commission and its designated self-regulatory organization upon application for registration and thereafter upon request.

(d) Risk management unit. As part of the Risk Management Program, each futures commission merchant shall establish and maintain a risk management unit with sufficient authority; qualified personnel; and financial, operational, and other resources to carry out the risk management program established pursuant to this section. The risk management unit shall report directly to senior management and shall be independent from the business unit.

(e) Elements of the Risk Management Program. The Risk Management Program of each futures commission merchant shall include, at a minimum, the following elements:

(1) Identification of risks and risk tolerance limits. (i) The Risk Management Program shall take into account market, credit, liquidity, foreign currency, legal, operational, settlement, segregation, technological, capital, and any other applicable risks together with a description of the risk tolerance limits set by the futures commission merchant and the underlying methodology in the written policies and procedures. The risk tolerance limits shall be reviewed and approved quarterly by senior management and annually by the governing body. Exceptions to risk tolerance limits shall be subject to written policies and procedures.

(ii) The Risk Management Program shall take into account risks posed by affiliates, all lines of business of the futures commission merchant, and all other trading activity engaged in by the futures commission merchant. The Risk Management Program shall be integrated into risk management at the consolidated entity level.

(iii) The Risk Management Program shall include policies and procedures for detecting breaches of risk tolerance limits set by the futures commission merchant, and alerting supervisors within the risk management unit and senior management, as appropriate.

(2) Periodic Risk Exposure Reports. (i) The risk management unit of each futures commission merchant shall provide to senior management and to its governing body quarterly written reports setting forth all applicable risk exposures of the futures commission merchant; any recommended or completed changes to the Risk Management Program; the recommended time frame for implementing recommended changes; and the status of any incomplete implementation of previously recommended changes to the Risk Management Program. For purposes of this section, such reports shall be referred to as "Risk Exposure Reports." The Risk Exposure Reports also shall be provided to the senior management and the governing body immediately upon detection of any material change in the risk exposure of the futures commission merchant.

(ii) Furnishing to the Commission. Each futures commission merchant shall furnish copies of its Risk Exposure Reports to the Commission within five (5) business days of providing such reports to its senior management.

(3) Specific risk management considerations. The Risk Management Program of each futures commission merchant shall include, but not be limited to, policies and procedures necessary to monitor and manage the following risks:

(i) Segregation risk. The written policies and procedures shall be reasonably designed to ensure that segregated funds are separately accounted for and segregated or secured as belonging to customers as required by the Act and Commission regulations and must, at a minimum, include or address the following:

(A) A process for the evaluation of depositories of segregated funds, including, at a minimum, documented criteria that any depository that will hold segregated funds, including an entity affiliated with the futures commission merchant, must meet, including criteria addressing the depository's capitalization, creditworthiness, operational reliability, and access to liquidity. The criteria should further consider the extent to which segregated funds are concentrated with any

depository or group of depositories. The criteria also should include the availability of deposit insurance and the extent of the regulation and supervision of the depository;

(B) A program to monitor an approved depository on an ongoing basis to assess its continued satisfaction of the futures commission merchant's established criteria, including a thorough due diligence review of each depository at least annually;

(C) An account opening process for depositories, including documented authorization requirements, procedures that ensure that segregated funds are not deposited with a depository prior to the futures commission merchant receiving the acknowledgment letter required from such depository pursuant to §1.20, and §§22.2 and 30.7 of this chapter, and procedures that ensure that such account is properly titled to reflect that it is holding segregated funds pursuant to the Act and Commission regulations;

(D) A process for establishing a targeted amount of residual interest that the futures commission merchant seeks to maintain as its residual interest in the segregated funds accounts and such process must be designed to reasonably ensure that the futures commission merchant maintains the targeted residual amounts and remains in compliance with the segregated funds requirements at all times. The policies and procedures must require that senior management, in establishing the total amount of the targeted residual interest in the segregated funds accounts, perform appropriate due diligence and consider various factors, as applicable, relating to the nature of the futures commission merchant's business including, but not limited to, the composition of the futures commission merchant's customer base, the general creditworthiness of the customer base, the general trading activity of the customers, the types of markets and products traded by the customers, the proprietary trading of the futures commission merchant, the general volatility and liquidity of the markets and products traded by customers, the futures commission merchant's own liquidity and capital needs, and the historical trends in customer segregated fund balances, including undermarginated amounts and net deficit balances in customers' accounts. The analysis and calculation of the targeted amount of the future commission merchant's residual interest must be described in writing with the specificity necessary to allow the Commission and the futures commission merchant's designated self-regulatory organization to duplicate the analysis and calculation and test the assumptions made by the futures commission merchant. The adequacy of the targeted residual interest and the process for establishing the targeted residual interest must be reassessed periodically by Senior Management and revised as necessary;

(E) A process for the withdrawal of cash, securities, or other property from accounts holding segregated funds, where the withdrawal is not for the purpose of payments to or on behalf of the futures commission merchant's customers. Such policies and procedures must satisfy the requirements of §1.23, §22.17 of this chapter, or §30.7 of this chapter, as applicable;

(F) A process for assessing the appropriateness of specific investments of segregated funds in permitted investments in accordance with §1.25. Such policies and procedures must take into consideration the market, credit, counterparty, operational, and liquidity risks associated with such investments, and assess whether such investments comply with the requirements in §1.25 including that the futures commission merchant manage the permitted investments consistent with the objectives of preserving principal and maintaining liquidity;

(G) Procedures requiring the appropriate separation of duties among individuals responsible for compliance with the Act and Commission regulations relating to the protection and financial reporting of segregated funds, including the separation of duties among personnel that are responsible for advising customers on trading activities, approving or overseeing cash receipts and disbursements (including investment operations), and recording and reporting financial transactions. The policies and procedures must require that any movement of funds to affiliated companies and parties are properly approved and documented;

(H) A process for the timely recording of all transactions, including transactions impacting customers' accounts, in the firm's books of record;

(I) A program for conducting annual training of all finance, treasury, operations, regulatory, compliance, settlement, and other relevant officers and employees regarding the segregation requirements for segregated funds required by the Act and regulations, the requirements for notices under §1.12, procedures for reporting suspected breaches of the policies and procedures required by this section to the chief compliance officer, without fear of retaliation, and the consequences of failing to comply with the segregation requirements of the Act and regulations; and

(J) Policies and procedures for assessing the liquidity, marketability and mark-to-market valuation of all securities or other non-cash assets held as segregated funds, including permitted investments under §1.25, to ensure that all non-cash assets held in the customer segregated accounts, both customer-owned securities and investments in accordance with §1.25, are readily marketable and highly liquid. Such policies and procedures must require daily measurement of liquidity needs with respect to customers; assessment of procedures to liquidate all non-cash collateral in a timely manner and without significant effect on price; and application of appropriate collateral haircuts that accurately reflect market and credit risk.

(ii) Operational risk. The Risk Management Program shall include automated financial risk management controls reasonably designed to prevent the placing of erroneous orders, including those that exceed pre-set capital, credit, or volume thresholds. The Risk Management Program shall ensure that the use of automated trading programs is subject to policies and procedures governing the use, supervision, maintenance, testing, and inspection of such programs.

(iii) Capital risk. The written policies and procedures shall be reasonably designed to ensure that the futures commission merchant has sufficient capital to be in compliance with the Act and the regulations, and sufficient capital and liquidity to meet the reasonably foreseeable needs of the futures commission merchant.

(4) Supervision of the Risk Management Program. The Risk Management Program shall include a supervisory system that is reasonably designed to ensure that the policies and procedures required by this section are diligently followed.

(f) Review and testing. (1) The Risk Management Program of each futures commission merchant shall be reviewed and tested on at least an annual basis, or upon any material change in the business of the futures commission merchant that is reasonably likely to alter the risk profile of the futures commission merchant.

(2) The annual reviews of the Risk Management Program shall include an analysis of adherence to, and the effectiveness of, the risk management policies and procedures, and any recommendations for modifications to the Risk Management Program. The annual testing shall be performed by qualified internal audit staff that are independent of the business unit, or by a qualified third party audit service reporting to staff that are independent of the business unit. The results of the annual review of the Risk Management Program shall be promptly reported to and reviewed by the chief compliance officer, senior management, and governing body of the futures commission merchant.

(3) Each futures commission merchant shall document all internal and external reviews and testing of its Risk Management Program and written risk management policies and procedures including the date of the review or test; the results; any deficiencies identified; the corrective action taken; and the date that corrective action was taken. Such documentation shall be provided to Commission staff, upon request.

(g) Distribution of risk management policies and procedures. The Risk Management Program shall include procedures for the timely distribution of its written risk management policies and procedures to relevant supervisory personnel. Each futures commission merchant shall maintain records of the persons to whom the risk management policies and procedures were distributed and when they were distributed.

(h) Recordkeeping. (1) Each futures commission merchant shall maintain copies of all written approvals required by this section.

(2) All records or reports, including, but not limited to, the written policies and procedures and any changes thereto that a futures commission merchant is required to maintain pursuant to this regulation shall be maintained in accordance with §1.31 and shall be made available promptly upon request to representatives of the Commission.

**[520] 521. Compliance with Commission Regulation 1.12 – Maintenance of Minimum Financial Requirements by Futures Commission Merchants and Introducing Brokers.**

Any Trading Privilege Holder subject to Commission Regulation 1.12 that violates Commission Regulation 1.12 shall be deemed to have violated this Rule [520] 521. Commission Regulation 1.12 is set forth below and incorporated into this Rule [520] 521.

Commission Regulation 1.12 - Maintenance of minimum financial requirements by futures commission merchants and introducing brokers.

(a) Each person registered as a futures commission merchant or who files an application for registration as a futures commission merchant, and each person registered as an introducing broker or who files an application for registration as an introducing broker (except for an introducing broker or applicant for registration as an introducing broker operating pursuant to, or who has filed concurrently with its application for registration, a guarantee agreement and who is not also a securities broker or dealer), who knows or should have known that its adjusted net capital at any time is less than the minimum required by §1.17 or by the capital rule of any self-regulatory organization to which such person is subject, if any, must:

(1) Give [telephonic notice, to be confirmed in writing by facsimile] notice, as set forth in paragraph ([i]n) of this section that the applicant's or registrant's adjusted net capital is less than required by §1.17 or by other capital rule, identifying the applicable capital rule. The notice must be given immediately after the applicant or registrant knows or should [know] have known that its adjusted net capital is less than required by any of the aforesaid rules to which the applicant or registrant is subject; and

(2) Provide together with such notice documentation in such form as necessary to adequately reflect the applicant's or registrant's capital condition as of any date on which such person's adjusted net capital is less than the minimum required; Provided, however, that if the applicant or registrant cannot calculate or otherwise immediately determine its financial condition, it must provide the notice required by paragraph (a)(1) of this section and include in such notice a statement that the entity cannot presently calculate its financial condition. The applicant or registrant must provide similar documentation of its financial condition for other days as the Commission may request.

(b) Each person registered as a futures commission merchant, or who files an application for registration as a futures commission merchant, who knows or should have known that its adjusted net capital at any time is less than the greatest of:

- (1) 150 percent of the minimum dollar amount required by §1.17(a)(1)(i)(A);
  - (2) 110 percent of the amount required by §1.17(a)(1)(i)(B);
  - (3) 150 percent of the amount of adjusted net capital required by a registered futures association of which it is a member, unless such amount has been determined by a margin-based capital computation set forth in the rules of the registered futures association, and such amount meets or exceeds the amount of adjusted net capital required under the margin-based capital computation set forth in §1.17(a)(1)(i)(B), in which case the required percentage is 110 percent, or
  - (4) For securities brokers or dealers, the amount of net capital specified in Rule 17a-11(c) of the Securities and Exchange Commission (17 CFR 240.17a-11(c)), must file [written] notice to that effect, as set forth in paragraph ([i]n) of this section [within] , as soon as possible and no later than twenty-four (24) hours of such event.
- (c) If an applicant or registrant at any time fails to make or keep current the books and records required by these regulations, such applicant or registrant must, on the same day such event occurs, provide [facsimile] notice of such fact as specified in paragraph (n) of this section, specifying the books and records which have not been made or which are not current, and [within] as soon as possible, but not later than forty-eight (48) hours after giving such notice file a [written] report as required by paragraph (n) of this section stating what steps have been and are being taken to correct the situation.
- (d) Whenever any applicant or registrant discovers or is notified by an independent public accountant, pursuant to §1.16(e)(2) [of this chapter], of the existence of any material inadequacy, as specified in §1.16(d)(2) [of this chapter], such applicant or registrant must give [facsimile] notice of such material inadequacy [within twenty-four (24) hours, and within forty-eight (48) hours after giving such notice file a written] , as provided in paragraph (n) of this section, as soon as possible but not later than twenty-four (24) hours of discovering or being notified of the material inadequacy. The applicant or registrant must file, in the manner provided for under paragraph (n) of this section, a report stating what steps have been and are being taken to correct the material inadequacy within forty-eight (48) hours of filing its notice of the material inadequacy.
- (e) Whenever any self-regulatory organization learns that a member registrant has failed to file a notice or [written] report as required by [§1.12] this section, that self-regulatory organization must immediately report this failure by [telephone, confirmed in writing immediately by facsimile] notice, as provided in paragraph ([i]n) of this section.

(f)(1) [Reserved]

(2) Whenever a registered futures commission merchant determines that any position it carries for another registered futures commission merchant or for a registered leverage transaction merchant must be liquidated immediately, transferred immediately or that the trading of any account of such futures commission merchant or leverage transaction merchant shall be only for purposes of liquidation, because the other futures commission merchant or the leverage transaction merchant has failed to meet a call for margin or to make other required deposits, the carrying futures commission merchant must immediately give [telephonic notice, confirmed in writing immediately by facsimile notice] notice, as provided in paragraph (n) of this section, of such a determination [to the principal office of the Commission at Washington, DC].

(3) Whenever a registered futures commission merchant determines that an account which it is carrying is undermargined by an amount which exceeds the futures commission merchant's adjusted net capital determined in accordance with §1.17, the futures commission merchant must immediately [give telephonic notice, confirmed in writing immediately by facsimile notice] provide notice, as provided in paragraph (n) of this section, of such a determination to the designated self-regulatory organization and the [principal office of the] Commission [at Washington, DC]. This paragraph (f)(3) shall apply to any account carried by the futures commission merchant, whether a customer, noncustomer, omnibus or proprietary account. For purposes of this paragraph [(f)(3)], if any person has an interest of 10 percent or more in ownership or equity in, or guarantees, more than one account, or has guaranteed an account in addition to [his] its own account, all such accounts shall be combined. [A designated self-regulatory organization may grant an exemption from the provisions of this paragraph to a futures commission merchant with respect to any particular account on a continuous basis provided the designated self-regulatory organization documents the reasons for granting such an exemption and continues to monitor any such account.]

(4) A futures commission merchant shall [report immediately by telephone, confirmed immediately in writing by facsimile notice] provide immediate notice, as provided in paragraph (n) of this section, whenever any commodity interest account it carries is subject to a margin call, or call for other deposits required by the futures commission merchant, that exceeds the futures commission merchant's excess adjusted net capital, determined in accordance with §1.17, and such call has not been answered by the close of business on the day following the issuance of the call. This applies to all accounts carried by the futures commission merchant, whether customer, noncustomer, or omnibus, that are subject to margining, including commodity futures, cleared swaps, and options. In addition to actual margin deposits by an account owner, a futures commission merchant may also take account of favorable market moves in determining whether the margin call is required to be reported under this paragraph.

(5)(i) A futures commission merchant shall [report immediately by telephone, confirmed immediately in writing by facsimile notice] provide immediate notice, as provided in paragraph (n) of this section, whenever its excess adjusted net capital is less than six percent of the maintenance margin required by the futures commission merchant on all positions held in accounts of a noncustomer other than a noncustomer who is subject to the minimum financial requirements of:

(A) A futures commission merchant, or

(B) The Securities and Exchange Commission for a securities broker [and] or dealer.

(ii) For purposes of paragraph (f)(5)(i) of this section, maintenance margin shall include all deposits which the futures commission merchant requires the noncustomer to maintain in order to carry its positions at the futures commission merchant.

(g) A futures commission merchant shall provide [written] notice, as provided in paragraph (n) of this section, of a substantial reduction in capital as compared to that last reported in a financial report filed with the Commission pursuant to §1.10. This notice shall be provided as follows:

(1) If any event or series of events, including any withdrawal, advance, loan or loss cause, on a net basis, a reduction in net capital (or, if the futures commission merchant is qualified to use the filing option available under §1.10(h), tentative net capital as defined in the rules of the Securities and Exchange Commission) of 20 percent or more, notice must be provided as provided in paragraph (n) of this section within two business days of the event or series of events causing the reduction stating the reason for the reduction and steps the futures commission merchant will be taking to ensure an appropriate level of net capital is maintained by the futures commission merchant; and

(2) If equity capital of the futures commission merchant or a subsidiary or affiliate of the futures commission merchant consolidated pursuant to §1.17(f) (or 17 CFR 240.15c3-1e) would be withdrawn by action of a stockholder or a partner or a limited liability company member or by redemption or repurchase of shares of stock by any of the consolidated entities or through the payment of dividends or any similar distribution, or an unsecured advance or loan would be made to a stockholder, partner, sole proprietor, limited liability company member, employee or affiliate, such that the withdrawal, advance or loan would cause, on a net basis, a reduction in excess adjusted net capital (or, if the futures commission merchant is qualified to use the filing option available under §1.10(h), excess net capital as defined in the rules of the Securities and Exchange Commission) of 30 percent or more, notice must be provided as provided in paragraph (n) of this section at least two business days prior to the withdrawal, advance or loan that would cause the reduction: *Provided, however,* That the provisions of paragraphs (g)(1) and (g)(2) of this section do not apply to any futures or securities transaction in the ordinary course of business between a futures commission merchant and any affiliate where the futures commission merchant makes payment to or on behalf of such affiliate for such transaction and then receives payment from such affiliate for such transaction within two business days from the date of the transaction.

(3) Upon receipt of such notice from a futures commission merchant, or upon a reasonable belief that a substantial reduction in capital has occurred or will occur, the Director of the Division of [Clearing] Swap Dealer and Intermediary Oversight or the Director's designee may require that the futures commission merchant provide or cause a Material Affiliated Person (as that term is defined in §1.14(a)(2)) to provide, within three business days from the date of request or such shorter period as the Division Director or designee may specify, such other information as the Division Director or designee determines to be necessary based upon market conditions, reports provided by the futures commission merchant, or other available information.

(h) Whenever a person registered as a futures commission merchant knows or should know that the total amount of its funds on deposit in segregated accounts on behalf of customers[, or that trading on designated contract markets, or the amount of funds on deposit in segregated accounts for customers transacting in Cleared Swaps under part 22 of this chapter, or the total amount set aside on behalf of customers trading on non-United States markets under part 30 of this chapter], is less than the total amount of such funds required by the Act and the [Commission's rules] regulations to be on deposit in segregated or secured amount accounts on behalf of such customers, the registrant must report such deficiency immediately by [telephone notice, confirmed immediately in writing by facsimile notice,] notice to the registrant's designated self-regulatory organization and the [principal office of the Commission in Washington, DC, to the attention of the Director and the Chief Accountant of the Division of Clearing and Intermediary Oversight] Commission, as provided in paragraph (n) of this section.

(i) A futures commission merchant must provide immediate notice, as set forth in paragraph (n) of this section, whenever it discovers or is informed that it has invested funds held for futures customers trading on designated contract markets pursuant to §1.20, Cleared Swaps Customer Collateral, as defined in §22.1 of this chapter, or 30.7 customer funds, as defined in §30.1 of this chapter, in instruments that are not permitted investments under §1.25, or has otherwise violated the requirements governing the investment of funds belonging to customers under §1.25.

(j) A futures commission merchant must provide immediate notice, as provided in paragraph (n) of this section, whenever the futures commission merchant does not hold a sufficient amount of funds in segregated accounts for futures customers under §1.20, in segregated accounts for Cleared Swaps Customers under part 22 of this chapter, or in secured amount accounts for customers trading on foreign markets under part 30 of this chapter to meet the futures commission merchant's targeted residual interest in the segregated or secured amount accounts pursuant to its policies and procedures required under §1.11, or whenever the futures commission merchant's amount of residual interest is less than the sum of the undermargined amounts in its customer accounts as determined at the point in time that the firm is required to maintain the undermargined amounts under §1.22, and §§22.2 and 30.7 of this chapter.

(k) A futures commission merchant must provide immediate notice, as provided in paragraph (n) of this section, whenever the futures commission merchant, or the futures commission merchant's parent or material affiliate, experiences a material adverse impact to its creditworthiness or ability to fund its obligations, including any change that could adversely impact the firm's liquidity resources.

(l) A futures commission merchant must provide prompt notice, but in no event later than 24 hours, as provided in paragraph (n) of this section, whenever the futures commission merchant experiences a material change in its operations or risk profile, including a change in the senior management of the futures commission merchant, the establishment or termination of a line of business, or a material adverse change in the futures commission merchant's clearing arrangements.

(m) A futures commission merchant must provide notice, if the futures commission merchant has been notified by the Securities and Exchange Commission, a securities self-regulatory organization, or a futures self-regulatory organization, that it is the subject of a formal investigation. A futures commission merchant must provide a copy of any examination report issued to the futures commission merchant by the Securities and Exchange Commission or a securities self-regulatory organization. A futures commission merchant must provide the Commission with notice of any correspondence received from the Securities and Exchange Commission or a securities self-regulatory organization that raises issues with the adequacy of the futures commission merchant's capital position, liquidity to meet its obligations or otherwise operate its business, or internal controls. The notices and examination reports required by this section must be filed in a prompt manner, but in no event later than 24 hours of the reportable event, and must be filed in accordance with paragraph (n) of the section; Provided, however, that a futures commission merchant is not required to file a notice or copy of an examination report with the Securities and Exchange Commission, a securities self-regulatory organization, or a futures self-regulatory organization if such entity originally provided the communication or report to the futures commission merchant.

(n) Notice. (1) Every notice and [written] report required to be [given or] filed by this section [(except for notices required by paragraph (f) of this section)] by a futures commission merchant or a self-regulatory organization must be filed with the [regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located, with the principal office of the Commission in Washington, DC] Commission, with the designated self-regulatory organization, if any[;], and with the Securities and Exchange Commission, if such registrant is a securities broker or dealer. Every notice and [written] report required to be [given or] filed by this section by an applicant for registration as a futures commission merchant must be filed with the National Futures Association (on behalf of the Commission), with the designated self-regulatory organization, if any, and with the Securities and Exchange Commission, if such applicant is a securities broker or dealer. [Any notice or report filed with the National Futures Association pursuant to this paragraph shall be deemed for all purposes to be filed with, and to be the official record of, the Commission] Every notice or report that is required to be filed by this section by a futures commission merchant or a self-regulatory organization must include a discussion of how the reporting event originated and what steps have been, or are being taken, to address the reporting event.

(2) Every notice and [written] report which an introducing broker or applicant for registration as an introducing broker is required to [give or] file by paragraphs (a), (c) and (d) of this section must be filed with the National Futures Association (on behalf of the Commission), with the designated self-regulatory organization, if any, and with every futures commission merchant carrying or intending to carry customer accounts for the introducing broker or applicant for registration as an introducing broker. Any notice or report filed with the National Futures Association pursuant to this paragraph shall be deemed for all purposes to be filed with, and to be the official record of, the Commission. Every notice or report that is required to be filed by this section by an introducing broker or applicant for registration as an introducing broker must include a discussion

of how the reporting event originated and what steps have been, or are being taken, to address the reporting event.

(3) Every notice or report that is required to be [provided in writing to] filed by a futures commission merchant with the Commission or with a designated self-regulatory organization under this section [may, in lieu of facsimile,] must be in writing and must be filed via electronic transmission using a form of user authentication assigned in accordance with procedures established by or approved by the Commission, and otherwise in accordance with instructions issued by or approved by the Commission; Provided, however, that if the registered futures commission merchant cannot file the notice or report using the electronic transmission approved by the Commission due to a transmission or systems failure, the futures commission merchant must immediately contact the Commission's regional office with jurisdiction over the futures commission merchant as provided in §140.02 of this chapter, and by email to FCMNotice@CFTC.gov. Any such electronic submission must clearly indicate the [registrant or applicant] futures commission merchant on whose behalf such filing is made and the use of such user authentication in submitting such filing will constitute and become a substitute for the manual signature of the authorized signer.

**[521] 522. Compliance with Commission Regulation 1.17  
- Minimum Financial Requirements for Futures  
Commission Merchants and Introducing Brokers**

Any Trading Privilege Holder subject to Commission Regulation 1.17 that violates Commission Regulation 1.17 shall be deemed to have violated this Rule [521] 522. Commission Regulation 1.17 is set forth below and incorporated into this Rule [521] 522.

Commission Regulation 1.17 - Minimum financial requirements for futures commission merchants and [Introducing] introducing brokers.

(a)(1)(i) Except as provided in paragraph (a)(2)(i) of this section, each person registered as a futures commission merchant must maintain adjusted net capital equal to or in excess of the greatest of:

(A) \$1,000,000;

(B) The futures commission merchant's risk-based capital requirement, computed as eight percent of the total risk margin requirement for positions carried by the futures commission merchant in customer accounts and noncustomer accounts.

(C) The amount of adjusted net capital required by a registered futures association of which it is a member; or

(D) For securities brokers and dealers, the amount of net capital required by Rule 15c3-1(a) of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

(ii) [Each person registered as a futures commission merchant engaged in soliciting or accepting orders and customer funds related thereto for the purchase or sale of any commodity for future delivery or any commodity option on or subject to the rules of a registered derivatives transaction execution facility from any customer who does not qualify as an "institutional customer" as defined in §1.3(g) must:] Reserved

[(A) Be a clearing member of a derivatives clearing organization and maintain net capital in the amount of the greater of \$20,000,000 or the amounts otherwise specified in paragraph (a)(1)(i) of this section; or

(B) Receive orders on behalf of the customer from a commodity trading advisor acting in accordance with §4.32 of this chapter.]

(iii) Except as provided in paragraph (a)(2) of this section, each person registered as an introducing broker must maintain adjusted net capital equal to or in excess of the greatest of:

(A) \$45,000;

(B) The amount of adjusted net capital required by a registered futures association of which it is a member; or

(C) For securities brokers and dealers, the amount of net capital required by Rule 15c3-1(a) of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

(2)(i) The requirements of paragraph (a)(1) of this section shall not be applicable if the registrant is a member of a designated self-regulatory organization and conforms to minimum financial standards and related reporting requirements set by such designated self-regulatory organization in its bylaws, rules, regulations or resolutions approved by the Commission pursuant to section 4f(b) of the Act and §1.52.

(ii) The minimum requirements of paragraph (a)(1)(iii) of this section shall not be applicable to an introducing broker which elects to meet the alternative adjusted net capital requirement for introducing brokers by operation pursuant to a guarantee agreement which meets the requirements set forth in §1.10(j). Such an introducing broker shall be deemed to meet the adjusted net capital requirement under this section so long as such agreement is binding and in full force and effect, and, if the introducing broker is also a securities broker or dealer, it maintains the amount of net capital required by Rule 15c3-1(a) of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

(3) No person applying for registration as a futures commission merchant or as an introducing broker shall be so registered unless such person affirmatively demonstrates to the satisfaction of the National Futures Association that it complies with the financial requirements of this section. Each registrant must be in compliance with this section at all times and must be able to demonstrate such compliance to the satisfaction of the Commission or the designated self-regulatory organization.

(4) A futures commission merchant who is not in compliance with this section, or is unable to demonstrate such compliance as required by paragraph (a)(3) of this section, or who cannot certify to the Commission immediately upon request and demonstrate with verifiable evidence that it has sufficient access to liquidity to continue operating as a going concern, must transfer all customer accounts and immediately cease doing business as a futures commission merchant until such time as the firm is able to demonstrate such compliance[:]; *Provided, however,* The registrant may trade for liquidation purposes only unless otherwise directed by the Commission and/or the designated self-regulatory organization[:]; *And, Provided further,* That if such registrant immediately demonstrates to the satisfaction of the Commission or the designated self-regulatory organization the ability to achieve compliance, the Commission or the designated self-regulatory organization may in its discretion allow such registrant up to a maximum of 10 business days in which to achieve compliance without having to transfer accounts and cease doing business as required above. Nothing in this paragraph [(a)(4)] shall be construed as preventing the Commission or the designated self-regulatory organization from taking action against a registrant for non-compliance with any of the provisions of this section.

(5) An introducing broker who is not in compliance with this section, or is unable to demonstrate such compliance as required by paragraph (a)(3) of this section, must immediately cease doing business as an introducing broker until such time as the registrant is able to demonstrate such compliance: *Provided, however,* That if such registrant immediately demonstrates to the satisfaction of the Commission or the designated self-regulatory organization the ability to achieve compliance, the Commission or the designated self-regulatory organization may in its discretion allow such registrant up to a maximum of 10 business days in which to achieve compliance without having to cease doing business as required above. If the introducing broker is required to cease doing business in accordance with this paragraph (a)(5), the introducing broker must immediately notify each of its customers and the futures commission merchants carrying the account of each customer that it has ceased doing business. Nothing in this paragraph (a)(5) shall be construed as preventing the Commission or the designated self-regulatory organization from taking action against a registrant for non-compliance with any of the provisions of this section.

(b) For the purposes of this section:

(1) Where the applicant or registrant has an asset or liability which is defined in Securities Exchange Act Rule 15c3-1 (§240.15c3-1 of this title) the inclusion or exclusion of all or part of such asset or liability for the computation of adjusted net capital shall be in accordance with §240.15c3-1 of this title, unless specifically stated otherwise in this section.

(2) *Customer.* This term means a futures customer [(as defined in §[1.3(k))], option customer (as defined in §1.3(jj) and in §32.1(c) of this chapter),] 1.3, a cleared over the counter customer [(as defined in [§1.17] paragraph (b)(10)[]) of this section, and [includes a foreign futures, foreign options] a 30.7 customer [(as defined in §30.1[(c)] of this chapter)].

(3) *Proprietary account* means an account in which commodity futures, options or cleared over the counter derivative positions are carried on the books of the applicant or registrant for the applicant or registrant itself, or for general partners in the applicant or registrant.

(4) *Noncustomer account* means an account in which commodity futures, options or cleared over the counter derivative positions are carried on the books of the applicant or registrant which is either:

(i) An account that is not included in the definition of customer (as defined in §1.17(b)(2)) or proprietary account (as defined in §1.17(b)(3)), or

(ii) An account for a foreign-domiciled person trading futures or options on a foreign board of trade, and such account is a proprietary account as defined in §1.3(y) of this title, but is not a proprietary account as defined in §1.17(b)(3).

(5) *Clearing organization* means clearing organization (as defined in §1.3(d)) and includes a clearing organization of any board of trade.

(6) *Business day* means any day other than a Sunday, Saturday, or holiday.

(7) *Customer account.* This term means an account in which commodity futures, options or cleared over the counter derivative positions are carried on the books of the applicant or registrant which is [either:]

[(i) An] an account that is included in the definition of customer [(as defined in §1.17(b)(2)[)], or

(ii) An account for a foreign-domiciled person trading on a foreign board of trade, where such account for the foreign-domiciled person is not a proprietary account (as defined in §1.17(b)(3)) or a noncustomer account (as defined in §1.17(b)(4)(ii)].

(8) *Risk margin* for an account means the level of maintenance margin or performance bond required for the customer or noncustomer positions by the applicable exchanges or clearing organizations, and, where margin or performance bond is required only for accounts at the clearing organization, for purposes of the FCM's risk-based capital calculations applying the same margin or performance bond requirements to customer and noncustomer positions in accounts carried by the FCM, subject to the following.

(i) Risk margin does not include the equity component of short or long option positions maintained in an account;

(ii) The maintenance margin or performance bond requirement associated with a long option position may be excluded from risk margin to the extent that the value of such long option position does not reduce the total risk maintenance or performance bond requirement of the account that holds the long option position;

(iii) The risk margin for an account carried by a futures commission merchant which is not a member of the exchange or the clearing organization that requires collection of such margin should be calculated as if the futures commission merchant were such a member; and

(iv) If a futures commission merchant does not possess sufficient information to determine what portion of an account's total margin requirement represents risk margin, all of the margin required by the exchange or the clearing organization that requires collection of such margin for that account, shall be treated as risk margin.

(9) *Cleared over the counter derivative positions* means "over the counter derivative instrument" (as defined in 12 U.S.C. 4421) positions of any person in accounts carried on the books of the futures commission merchant and cleared by any organization permitted to clear such instruments under the laws of the relevant jurisdiction.

(10) *Cleared over the counter customer* means any person that is not a proprietary person as defined in §1.3(y) and for whom the futures commission merchant carries on its books one or more accounts for the over the counter-cleared derivative positions of such person.

(c) Definitions: For the purposes of this section:

(1) *Net capital* means the amount by which current assets exceed liabilities. In determining "net capital":

(i) Unrealized profits shall be added and unrealized losses shall be deducted in the accounts of the applicant or registrant, including unrealized profits and losses on fixed price commitments and forward contracts;

(ii) All long and all short positions in commodity options which are traded on a contract market and listed security options shall be marked to their market value and all long and all short securities and commodities positions shall be marked to their market value;

(iii) The value attributed to any commodity option which is not traded on a contract market shall be the difference between the option's strike price and the market value for the [physical] commodity or futures contract which is the subject of the option. In the case of a call commodity option which is not traded on a contract market, if the market value for the [physical] commodity or futures contract which is the subject of the option is less than the strike price of the option, it

shall be given no value. In the case of a put commodity option which is not traded on a contract market, if the market value for the [physical] commodity or futures contract which is the subject of the option is more than the strike price of the option, it shall be given no value; and

(iv) The value attributed to any unlisted security option shall be the difference between the option's exercise value or striking value and the market value of the underlying security. In the case of an unlisted call, if the market value of the underlying security is less than the exercise value or striking value of such call, it shall be given no value; and, in the case of an unlisted put, if the market value of the underlying security is more than the exercise value or striking value of the unlisted put, it shall be given no value.

(2) The term *current assets* means cash and other assets or resources commonly identified as those which are reasonably expected to be realized in cash or sold during the next 12 months. "Current assets" shall:

(i) Exclude any unsecured commodity futures or option account containing a ledger balance and open trades, the combination of which liquidates to a deficit or containing a debit ledger balance only: *Provided, however,* Deficits or debit ledger balances in unsecured customers', non-customers', and proprietary accounts, which are the subject of calls for margin or other required deposits may be included in current assets until the close of business on the business day following the date on which such deficit or debit ledger balance originated providing that the account had timely satisfied, through the deposit of new funds, the previous day's debit or deficits, if any, in its entirety.

(ii) Exclude all unsecured receivables, advances and loans except for:

(A) Receivables resulting from the marketing of inventories commonly associated with the business activities of the applicant or registrant and advances on fixed price purchases commitments: *Provided,* Such receivables or advances are outstanding no longer than 3 calendar months from the date that they are accrued;

(B) Interest receivable, floor brokerage receivable, commissions receivable from other brokers or dealers (other than syndicate profits), mutual fund concessions receivable and management fees receivable from registered investment companies and commodity pools: *Provided,* Such receivables are outstanding no longer than thirty (30) days from the date they are due; and dividends receivable outstanding no longer than thirty (30) days from the payable date;

(C) Receivables from clearing organizations and securities clearing organizations;

(D) Receivables from registered futures commission merchants or brokers, resulting from commodity futures or option transactions, except those specifically excluded under paragraph (c)(2)(i) of this section;

(E) Insurance claims which arise from a reportable segment of the applicant's or registrant's overall business activities, as defined in generally accepted accounting principles, other than in the commodity futures, commodity option, security and security option segments of the applicant's or registrant's business activities which are not outstanding more than 3 calendar months after the date they are recorded as a receivable;

(F) All other insurance claims not subject to paragraph (c)(2)(ii)(E) of this section, which are not older than seven (7) business days from the date the loss giving rise to the claim is discovered; insurance claims which are not older than twenty (20) business days from the date the loss giving rise to the claim is discovered and which are covered by an option of outside counsel that the claim is valid and is covered by insurance policies presently in effect; insurance claims which are older than twenty (20) business days from the date the loss giving rise to the claim is discovered

and which are covered by an opinion of outside counsel that the claim is valid and is covered by insurance policies presently in effect and which have been acknowledged in writing by the insurance carrier as due and payable: *Provided*, Such claims are not outstanding longer than twenty (20) business days from the date they are so acknowledged by the carrier;

(iii) Exclude all prepaid expenses and deferred charges;

(iv) Exclude all inventories except for:

(A) Readily marketable spot commodities; or spot commodities which "adequately collateralize" indebtedness under paragraph (c)(7) of this section;

(B) Securities which are considered "readily marketable" (as defined in §240.15c3-1(c)(11) of this title) or which "adequately collateralize" indebtedness under paragraph (c)(7) of this section;

(C) Work in process and finished goods which result from the processing of commodities at market value;

(D) Raw materials at market value which will be combined with spot commodities to produce a finished processed commodity; and

(E) Inventories held for resale commonly associated with the business activities of the applicant or registrant;

(v) Include fixed assets and assets which otherwise would be considered noncurrent to the extent of any long-term debt adequately collateralized by assets acquired for use in the ordinary course of the trade or business of an applicant or registrant and any other long-term debt adequately collateralized by assets of the applicant or registrant if the sole recourse of the creditor for nonpayment of such liability is to such asset: *Provided*, Such liabilities are not excluded from liabilities in the computation of net capital under paragraph (c)(4)(vi) of this section;

(vi) Exclude all assets doubtful of collection or realization less any reserves established therefor;

(vii) Include, in the case of future income tax benefits arising as a result of unrealized losses, the amount of such benefits not exceeding the amount of income tax liabilities accrued on the books and records of the applicant or registrant, but only to the extent such benefits could have been applied to reduce accrued tax liabilities on the date of the capital computation, had the related unrealized losses been realized on that date;

(viii) Include guarantee deposits with clearing organizations and stock in clearing organizations to the extent of its margin value;

(ix) In the case of an introducing broker or an applicant for registration as an introducing broker, include 50 percent of the value of a guarantee or security deposit with a futures commission merchant which carries or intends to carry accounts for the customers of the introducing broker; and

(x) Exclude exchange memberships.

(3) A loan or advance or any other form of receivable shall not be considered "secured" for the purposes of paragraph (c)(2) of this section unless the following conditions exist:

(i) The receivable is secured by readily marketable collateral which is otherwise unencumbered and which can be readily converted into cash: *Provided, however*, That the receivable will be

considered secured only to the extent of the market value of such collateral after application of the percentage deductions specified in paragraph (c)(5) of this section; and

(ii)(A) The readily marketable collateral is in the possession or control of the applicant or registrant; or

(B) The applicant or registrant has a legally enforceable, written security agreement, signed by the debtor, and has a perfected security interest in the readily marketable collateral within the meaning of the laws of the State in which the readily marketable collateral is located.

(4) The term *liabilities* means the total money liabilities of an applicant or registrant arising in connection with any transaction whatsoever, including economic obligations of an applicant or registrant that are recognized and measured in conformity with generally accepted accounting principles. "Liabilities" also include certain deferred credits that are not obligations but that are recognized and measured in conformity with generally accepted accounting principles. For the purposes of computing "net capital", the term "liabilities":

(i) Excludes liabilities of an applicant or registrant which are subordinated to the claims of all general creditors of the applicant or registrant pursuant to a satisfactory subordination agreement, as defined in paragraph (h) of this section;

(ii) Excludes, in the case of a futures commission merchant, the amount of money, securities and property due to commodity futures or option customers which is held in segregated accounts in compliance with the requirements of the Act and these regulations: *Provided, however,* That such exclusion may be taken only if such money, securities and property held in segregated accounts have been excluded from current assets in computing net capital;

(iii) Includes, in the case of an applicant or registrant who is a sole proprietor, the excess of liabilities which have not been incurred in the course of business as a futures commission merchant or as an introducing broker over assets not used in the business;

(iv) Excludes the lesser of any deferred income tax liability related to the items in paragraphs (c)(4)(i) (A), (B), and (C) below, or the sum of paragraphs (c)(4)(i) (A), (B), and (C) below:

(A) The aggregate amount resulting from applying to the amount of the deductions computed in accordance with paragraph (c)(5) of this section the appropriate Federal and State tax rate(s) applicable to any unrealized gain on the asset on which the deduction was computed;

(B) Any deferred tax liability related to income accrued which is directly related to an asset otherwise deducted pursuant to this section;

(C) Any deferred tax liability related to unrealized appreciation in value of any asset(s) which has been otherwise excluded from current assets in accordance with the provisions of this section;

(v) Excludes any current tax liability related to income accrued which is directly related to an asset otherwise deducted pursuant to this section; and

(vi) Excludes liabilities which would be classified as long term in accordance with generally accepted accounting principles to the extent of the net book value of plant, property and equipment which is used in the ordinary course of any trade or business of the applicant or registrant which is a reportable segment of the applicant's or registrant's overall business activities, as defined in generally accepted accounting principles, other than in the commodity futures, commodity option, security and security option segments of the applicant's or registrant's business activities: *Provided,* That such plant, property and equipment is not included in current assets pursuant to paragraph (c)(2)(v) of this section.

(5) The term *adjusted net capital* means net capital less:

(i) The amount by which any advances paid by the applicant or registrant on cash commodity contracts and used in computing net capital exceeds 95 percent of the market value of the commodities covered by such contracts;

(ii) In the case of all inventory, fixed price commitments and forward contracts, the applicable percentage of the net position specified below:

(A) Inventory which is currently registered as deliverable on a contract market and covered by an open futures contract or by a commodity option on a physical[.] commodity—No charge.

(B) Inventory which is covered by an open futures contract or commodity option.—5 percent of the market value.

(C) Inventory which is not covered.—20 percent of the market value.

(D) Inventory and forward contracts in those foreign currencies that are purchased or sold for future delivery on or subject to the rules of a contract market, and which are covered by an open futures contract.—No charge

(E) Inventory and forward contracts in euros, British pounds, Canadian dollars, Japanese yen, or Swiss francs, and which are not covered by an open futures contract or commodity option.—6 percent of the market value.

(F) Fixed price commitments (open purchases and sales) and forward contracts which are covered by an open futures contract or commodity option.—10 percent of the market value.

(G) Fixed price commitments (open purchases and sales) and forward contracts which are not covered by an open futures contract or commodity option.—20 percent of the market value.

(iii)—(iv) [Reserved]

(v) In the case of securities and obligations used by the applicant or registrant in computing net capital, and in the case of a futures commission merchant [with securities in segregation pursuant to section 4d(2) of the Act and the regulations in this chapter which were not] that invests funds deposited by futures customers[, the] as defined in §1.3, Cleared Swaps Customers as defined in §22.1 of this chapter, and 30.7 customers as defined in §30.1 of this chapter in securities as permitted investments under §1.25, the deductions specified in Rule 240.15c3-1(c)(2)(vi) or Rule 240.15c3-1(c)(2)(vii) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vi) and 17 CFR 240.15c3-1(c)(2)(vii)) ("securities haircuts"). Futures commission merchants that establish and enforce written policies and procedures to assess the credit risk of commercial paper, convertible debt instruments, or nonconvertible debt instruments in accordance with Rule 240.15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vi)) may apply the lower haircut percentages specified in Rule 240.15c3[-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vi)) ("securities haircuts") and 100 percent of the value of "nonmarketable securities" as specified in Rule 240.15c3-1(c)(2)(vii) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vii));]-1(c)(2)(vi) for such commercial paper, convertible debt instruments and nonconvertible debt instruments. Futures commission merchants must maintain their written policies and procedures in accordance with §1.31;

(vi) In the case of securities options and/or other options for which a haircut has been specified for the option or for the underlying instrument in §240.15c3-1 appendix A of this title, the

treatment specified in, or under, §240.15c3-1 appendix A, after effecting certain adjustments to net capital for listed and unlisted options as set forth in such appendix;

(vii) In the case of an applicant or registrant who has open contractual commitments, as hereinafter defined, the deductions specified in §240.15c3-1(c)(2)(viii) of this title;

(viii) In the case of a futures commission merchant, for undermargined customer commodity futures accounts and commodity option customer accounts the amount of funds required in each such account to meet maintenance margin requirements of the applicable board of trade or if there are no such maintenance margin requirements, clearing organization margin requirements applicable to such positions, after application of calls for margin or other required deposits which are outstanding [three] no more than one business [days or less] day. If there are no such maintenance margin requirements or clearing organization margin requirements, then the amount of funds required to provide margin equal to the amount necessary after application of calls for margin or other required deposits outstanding [three] no more than one business [days or less] day to restore original margin when the original margin has been depleted by 50 percent or more: *Provided*, To the extent a deficit is excluded from current assets in accordance with paragraph (c)(2)(i) of this section such amount shall not also be deducted under this paragraph [(c)(5)(viii)]. In the event that an owner of a customer account has deposited an asset other than cash to margin, guarantee or secure his account, the value attributable to such asset for purposes of this subparagraph shall be the lesser of (A) [the] The value attributable to the asset pursuant to the margin rules of the applicable board of trade, or (B) [the] The market value of the asset after application of the percentage deductions specified in [this] paragraph (c)(5) of this section;

(ix) In the case of a futures commission merchant, for undermargined commodity futures and commodity option noncustomer and omnibus accounts the amount of funds required in each such account to meet maintenance margin requirements of the applicable board of trade or if there are no such maintenance margin requirements, clearing organization margin requirements applicable to such positions, after application of calls for margin or other required deposits which are outstanding [two] no more than one business [days or less] day. If there are no such maintenance margin requirements or clearing organization margin requirements, then the amount of funds required to provide margin equal to the amount necessary after application of calls for margin or other required deposits outstanding [two] no more than one business [days or less] day to restore original margin when the original margin has been depleted by 50 percent or more: *Provided*, To the extent a deficit is excluded from current assets in accordance with paragraph (c)(2)(i) of this section such amount shall not also be deducted under this paragraph [(c)(5)(ix)]. In the event that an owner of a noncustomer or omnibus account has deposited an asset other than cash to margin, guarantee or secure his account the value attributable to such asset for purposes of this [subparagraph] paragraph shall be the lesser of [(A)] the value attributable to such asset pursuant to the margin rules of the applicable board of trade, or [(B)] the market value of such asset after application of the percentage deductions specified in [this] paragraph (c)(5) of this section;

(x) In the case of open futures contracts or cleared OTC derivative positions and granted (sold) commodity options held in proprietary accounts carried by the applicant or registrant which are not covered by a position held by the applicant or registrant or which are not the result of a "changer trade" made in accordance with the rules of a contract market:

(A) For an applicant or registrant which is a clearing member of a clearing organization for the positions cleared by such member, the applicable margin requirement of the applicable clearing organization;

(B) For an applicant or registrant which is a member of a self-regulatory organization 150 percent of the applicable maintenance margin requirement of the applicable board of trade, or clearing organization, whichever is greater;

(C) For all other applicants or registrants, 200 percent of the applicable maintenance margin requirements of the applicable board of trade or clearing organization, whichever is greater; or

(D) For open contracts or granted (sold) commodity options for which there are no applicable maintenance margin requirements, 200 percent of the applicable initial margin requirement: *Provided*, The equity in any such proprietary account shall reduce the deduction required by this paragraph (c)(5)(x) if such equity is not otherwise includable in adjusted net capital;

(xi) In the case of an applicant or registrant which is a purchaser of a commodity option not traded on a contract market which has value and such value is used to increase adjusted net capital, ten percent of the market value of the [physical] commodity or futures contract which is the subject of such option but in no event more than the value attributed to such option;

(xii) In the case of an applicant or registrant which is a purchaser of a commodity option which is traded on a contract market the same safety factor as if the applicant or registrant were the grantor of such option in accordance with paragraph (c)(5)(x) of this section, but in no event shall the safety factor be greater than the market value attributed to such option;

(xiii) Five percent of all unsecured receivables includable under paragraph (c)(2)(ii)(D) of this section used by the applicant or registrant in computing "net capital" and which are not due from:

(A) A registered futures commission merchant;

(B) A broker or dealer that is registered as such with the Securities and Exchange Commission; or

(C) A foreign broker that has been granted comparability relief pursuant to §30.10 of this chapter, *Provided, however*, that the amount of the unsecured receivable not subject to the five percent capital charge is no greater than 150 percent of the current amount required to maintain futures and [option] options positions in accounts with the foreign broker, or 100 percent of such greater amount required to maintain futures and option positions in the accounts at any time during the previous six-month period, and *Provided, that*, in the case of [customer funds] the foreign futures or foreign options secured amount, as §1.3(rr) defines such term, such account is treated in accordance with the special requirements of the applicable Commission order issued under §30.10 of this chapter.

(xiv) For securities brokers and dealers, all other deductions specified in §240.15c3–1 of this title.

(6) Election of alternative capital deductions that have received approval of Securities and Exchange Commission pursuant to §240.15c3–1(a)(7) of this title.

(i) Any futures commission merchant that is also registered with the Securities and Exchange Commission as a securities broker or dealer, and who also satisfies the other requirements of this paragraph (c)(6), may elect to compute its adjusted net capital using the alternative capital deductions that, under §240.15c3–1(a)(7) of this title, the Securities and Exchange Commission has approved by written order. To the extent that a futures commission merchant is permitted by the Securities and Exchange Commission to use alternative capital deductions for its unsecured receivables from over-the-counter transactions in derivatives, or for its proprietary positions in securities, forward contracts, or futures contracts, the futures commission merchant may use these same alternative capital deductions when computing its adjusted net capital, in lieu of the deductions that would otherwise be required by paragraph (c)(2)(ii) of this section for its unsecured receivables from over-the-counter derivatives transactions; by paragraph (c)(5)(ii) of this section for its proprietary positions in forward contracts; by paragraph (c)(5)(v) of this section for its proprietary positions in securities; and by paragraph (c)(5)(x) of this section for its proprietary positions in futures contracts.

(ii) *Notifications of election or of changes to election.* (A) No election to use the alternative market risk and credit risk deductions referenced in paragraph (c)(6)(i) of this section shall be effective unless and until the futures commission merchant has filed with the Commission, addressed to the Director of the Division of [Clearing] Swap Dealer and Intermediary Oversight, a notice that is to include a copy of the approval order of the Securities and Exchange Commission referenced in paragraph (c)(6)(i) of this section, and to include also a statement that identifies the amount of tentative net capital below which the futures commission merchant is required to provide notice to the Securities and Exchange Commission, and which also provides the following information: a list of the categories of positions that the futures commission merchant holds in its proprietary accounts, and, for each such category, a description of the methods that the futures commission merchant will use to calculate its deductions for market risk and credit risk, and also, if calculated separately, deductions for specific risk; a description of the value at risk (VaR) models to be used for its market risk and credit risk deductions, and an overview of the integration of the models into the internal risk management control system of the futures commission merchant; a description of how the futures commission merchant will calculate current exposure and maximum potential exposure for its deductions for credit risk; a description of how the futures commission merchant will determine internal credit ratings of counterparties and internal credit risk weights of counterparties, if applicable; and a description of the estimated effect of the alternative market risk and credit risk deductions on the amounts reported by the futures commission merchant as net capital and adjusted net capital.

(B) A futures commission merchant must also, upon the request of the Commission at any time, supplement the statement described in paragraph (c)(6)(ii)(A) of this section, by providing any other explanatory information regarding the computation of its alternative market risk and credit risk deductions as the Commission may require at its discretion.

(C) A futures commission merchant must also file the following supplemental notices with the Director of the Division and Clearing and Intermediary Oversight:

(1) A notice advising that the Securities and Exchange Commission has imposed additional or revised conditions for the approval evidenced by the order referenced in paragraph (c)(6)(i) of this section, and which describes the new or revised conditions in full, and

(2) A notice which attaches a copy of any approval by the Securities and Exchange Commission of amendments that a futures commission merchant has requested for its application, filed under 17 CFR 240.15c3-1e, to use alternative market risk and credit risk deductions approved by the Securities and Exchange Commission.

(D) A futures commission merchant may voluntarily change its election to use the alternative market risk and credit risk deductions referenced in paragraph (c)(6)(i) of this section, by filing with the Director of the Division of [Clearing] Swap Dealer and Intermediary Oversight a written notice specifying a future date as of which it will no longer use the alternative market risk and credit risk deductions, and will instead compute such deductions in accordance with the requirements otherwise applicable under paragraph (c)(2)(ii) of this section for unsecured receivables from over-the-counter derivatives transactions; by paragraph (c)(5)(ii) of this section for proprietary positions in forward contracts; by paragraph (c)(5)(v) of this section for proprietary positions in securities; and by paragraph (c)(5)(x) of this section for proprietary positions in futures contracts.

(iii) *Conditions under which election terminated.* A futures commission merchant may no longer elect to use the alternative market risk and credit risk deductions referenced in paragraph (c)(6)(i) of this section, and shall instead compute the deductions otherwise required under paragraph (c)(2)(ii) of this section for unsecured receivables from over-the-counter derivatives transactions; by paragraph (c)(5)(ii) of this section for proprietary positions in forward contracts; by paragraph (c)(5)(v) of this section for proprietary positions in securities; and by paragraph (c)(5)(x) of this section for proprietary positions in futures contracts, upon the occurrence of any of the following:

(A) The Securities and Exchange Commission revokes its approval of the market risk and credit risk deductions for such futures commission merchant;

(B) A futures commission merchant fails to come into compliance with its filing requirements under this paragraph (c)(6), after having received from the Director of the Division of [Clearing] Swap Dealer and Intermediary Oversight written notification that the firm is not in compliance with its filing requirements, and must cease using alternative capital deductions permitted under this paragraph (c)(6) if it has not come into compliance by a date specified in the notice; or

(C) The Commission by written order finds that permitting the futures commission merchant to continue to use such alternative market risk and credit risk deductions is no longer necessary or appropriate for the protection of customers of the futures commission merchant or of the integrity of the futures or options markets.

(iv) *Additional filing requirements.* Any futures commission merchant that elects to use the alternative market risk and credit risk deductions referenced in paragraph (c)(6)(i) of this section must file with the Commission, in addition to the filings required by paragraph (c)(6)(ii) of this section, copies of any and all of the following documents, at such time as the originals are filed with the Securities and Exchange Commission:

(A) Information that the futures commission merchant files on a monthly basis with its designated examining authority or the Securities and Exchange Commission, whether by way of schedules to its FOCUS reports or by other filings, in satisfaction of 17 CFR 240.17a-5(a)(5)(i);

(B) The quarterly reports required by 17 CFR 240.17a-5(a)(5)(ii);

(C) The supplemental annual filings as required by 17 CFR 240.17a-5(k);

(D) Any notification to the Securities and Exchange Commission or the futures commission merchant's designated examining authority of planned withdrawals of excess net capital; and

(E) Any notification that the futures commission merchant is required to file with the Securities and Exchange Commission when its tentative net capital is below an amount specified by the Securities and Exchange Commission.

(7) *Liabilities* are "adequately collateralized" when, pursuant to a legally enforceable written instrument, such liabilities are secured by identified assets that are otherwise unencumbered and the market value of which exceeds the amount of such liabilities.

(8) The term *contractual commitments* shall include underwriting, when issued, when distributed, and delayed delivery contracts; and the writing or endorsement of security puts and calls and combinations thereof; but shall not include uncleared regular way purchases and sales of securities. A series of contracts of purchase or sale of the same security, conditioned, if at all, only upon issuance, may be treated as an individual commitment.

(d) Each applicant or registrant shall have equity capital (inclusive of satisfactory subordination agreements which qualify under this paragraph (d) as equity capital) of not less than 30 percent of the debt-equity total, provided, an applicant or registrant may be exempted from the provisions of this paragraph (d) for a period not to exceed 90 days or for such longer period which the Commission may, upon application of the applicant or registrant, grant in the public interest or for the protection of investors. For the purposes of this paragraph (d):

(1) Equity capital means a satisfactory subordination agreement entered into by a partner or stockholder or limited liability company member which has an initial term of at least 3 years and has a remaining term of not less than 12 months if:

(i) It does not have any of the provisions for accelerated maturity provided for by paragraphs (h)(2) (ix)(A), (x)(A), or (x)(B) of this section, or the provisions allowing for special prepayment provided for by paragraph (h)(2)(vii)(B) of this section, and is maintained as capital subject to the provisions restricting the withdrawal thereof required by paragraph (e) of this section; or

(ii) The partnership agreement provides that capital contributed pursuant to a satisfactory subordination agreement as defined in paragraph (h) of this section shall in all respects be partnership capital subject to the provisions restricting the withdrawal thereof required by paragraph (e) of this section, and

(A) In the case of a corporation, the sum of its par or stated value of capital stock, paid in capital in excess of par, retained earnings, unrealized profit and loss, and other capital accounts.

(B) In the case of a partnership, the sum of its capital accounts of partners (inclusive of such partners' commodities, options and securities accounts subject to the provisions of paragraph (e) of this section), and unrealized profit and loss.

(C) In the case of a sole proprietorship, the sum of its capital accounts of the sole proprietorship and unrealized profit and loss.

(D) In the case of a limited liability company, the sum of its capital accounts of limited liability company members, and unrealized profit and loss.

(2) Debt-equity total means equity capital as defined in paragraph (d)(1) of this section plus the outstanding principal amount of satisfactory subordination agreements.

(e) No equity capital of the applicant or registrant or a subsidiary's or affiliate's equity capital consolidated pursuant to paragraph (f) of this section, whether in the form of capital contributions by partners (including amounts in the commodities, options and securities trading accounts of partners which are treated as equity capital but excluding amounts in such trading accounts which are not equity capital and excluding balances in limited partners' capital accounts in excess of their stated capital contributions), par or stated value of capital stock, paid-in capital in excess of par or stated value, retained earnings or other capital accounts, may be withdrawn by action of a stockholder or partner or limited liability company member or by redemption or repurchase of shares of stock by any of the consolidated entities or through the payment of dividends or any similar distribution, nor may any unsecured advance or loan be made to a stockholder, partner, sole proprietor, limited liability company member, or employee if, after giving effect thereto and to any other such withdrawals, advances, or loans and any payments of payment obligations (as defined in paragraph (h) of this section) under satisfactory subordination agreements and any payments of liabilities excluded pursuant to paragraph (c)(4)(vi) of this section which are scheduled to occur within six months following such withdrawal, advance or loan:

(1) Either adjusted net capital of any of the consolidated entities would be less than the greatest of:

(i) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

(ii) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

(iii) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

(iv) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1(e) of the Securities and Exchange Commission (17 CFR 240.15c3-1(e)); or

(2) In the case of any applicant or registrant included within such consolidation, if equity capital of the applicant or registrant (inclusive of satisfactory subordination agreements which qualify as equity under paragraph (d) of this section) would be less than 30 percent of the required debt-equity total as defined in paragraph (d) of this section.

*Provided*, That this paragraph (e) shall not preclude an applicant or registrant from making required tax payments or preclude the payment to partners of reasonable compensation. The Commission may, upon application of the applicant or registrant, grant relief from this paragraph (e) if the Commission deems it to be in the public interest or for the protection of nonproprietary accounts.

(f)(1) Every applicant or registrant, in computing its net capital pursuant to this section must, subject to the provisions of paragraphs (f)(2) and (f)(4) of this section, consolidate in a single computation, assets and liabilities of any subsidiary or affiliate for which it guarantees, endorses, or assumes directly or indirectly the obligations or liabilities. The assets and liabilities of a subsidiary or affiliate whose liabilities and obligations have not been guaranteed, endorsed, or assumed directly or indirectly by the applicant or registrant may also be so consolidated if an opinion of counsel is obtained as provided for in paragraph (f)(2) of this section.

(2)(i) If the consolidation, provided for in paragraph (f)(1) of this section, of any such subsidiary or affiliate results in the increase of the applicant's or registrant's adjusted net capital or decreases the minimum adjusted net capital requirement, and an opinion of counsel called for in paragraph (f)(2)(ii) of this section has not been obtained, such benefits shall not be recognized in the applicant's or registrant's computation required by this section.

(ii) Except as provided for in paragraph (f)(2)(i) of this section, consolidation shall be permitted with respect to any subsidiaries or affiliates which are majority owned and controlled by the applicant or registrant, and for which the applicant can demonstrate to the satisfaction of the National Futures Association, or for which the registrant can demonstrate to the satisfaction of the Commission and the designated self-regulatory organization, if any, by an opinion of counsel, that the net asset values or the portion thereof related to the parent's ownership interest in the subsidiary or affiliate, may be caused by the applicant or registrant or an appointed trustee to be distributed to the applicant or registrant within 30 calendar days. Such opinion must also set forth the actions necessary to cause such a distribution to be made, identify the parties having the authority to take such actions, identify and describe the rights of other parties or classes of parties, including but not limited to customers, general creditors, subordinated lenders, minority shareholders, employees, litigants, and governmental or regulatory authorities, who may delay or prevent such a distribution and such other assurances as the National Futures Association, the Commission or the designated self-regulatory organization by rule or interpretation may require. Such opinion must be current and periodically renewed in connection with the applicant's or registrant's annual audit pursuant to §1.10 or upon any material change in circumstances.

(3) In preparing a consolidated computation of adjusted net capital pursuant to this section, the following minimum and non-exclusive requirements shall be observed;

(i) Consolidated adjusted net capital shall be reduced by the estimated amount of any tax reasonably anticipated to be incurred upon distribution of the assets of the subsidiary or affiliate.

(ii) Liabilities of a consolidated subsidiary or affiliate which are subordinated to the claims of present and future creditors pursuant to a satisfactory subordination agreement shall be deducted from consolidated adjusted net capital unless such subordination extends also to the claims of present or future creditors of the parent applicant or registrant and all consolidated subsidiaries.

(iii) Subordinated liabilities of a consolidated subsidiary or affiliate which are consolidated in accordance with paragraph (f)(3)(ii) of this section may not be prepaid, repaid, or accelerated if any of the entities included in such consolidation would otherwise be unable to comply with the provisions of paragraph (h) of this section.

(iv) Each applicant or registrant included within the consolidation shall at all times be in compliance with the adjusted net capital requirement to which it is subject.

(4) No applicant or registrant shall guarantee, endorse, or assume directly or indirectly any obligation or liability of a subsidiary or affiliate unless the obligation or liability is reflected in the computation of adjusted net capital pursuant to this section except as provided in paragraph (f)(2)(i) of this section.

(g)(1) The Commission may by order restrict, for a period up to twenty business days, any withdrawal by a futures commission merchant of equity capital, or any unsecured advance or loan to a stockholder, partner, limited liability company member, sole proprietor, employee or affiliate, if:

(i) Such withdrawal, advance or loan would cause, when aggregated with all other withdrawals, advances or loans during a 30 calendar day period from the futures commission merchant or a subsidiary or affiliate of the futures commission merchant consolidated pursuant to §1.17(f) (or 17 CFR 240.15c3–1e), a net reduction in excess adjusted net capital (or, if the futures commission merchant is qualified to use the filing option available under §1.10(h), excess net capital as defined in the rules of the Securities and Exchange Commission) of 30 percent or more, and

(ii) The Commission, based on the facts and information available, concludes that any such withdrawal, advance or loan may be detrimental to the financial integrity of the futures commission merchant, or may unduly jeopardize its ability to meet customer obligations or other liabilities that may cause a significant impact on the markets.

(2) The futures commission merchant may file with the Secretary of the Commission a written petition to request rescission of the order issued under paragraph (g)(1) of this section. The petition filed by the futures commission merchant must specify the facts and circumstances supporting its request for rescission. The Commission shall respond in writing to deny the futures commission merchant's petition for rescission, or, if the Commission determines that the order issued under paragraph (g)(1) of this section should not remain in effect, the order shall be rescinded.

(h) The term *satisfactory subordination agreement* ("subordination agreement") means an agreement which contains the minimum and nonexclusive requirements set forth below.

(1) Certain definitions for purposes of this section:

(i) A subordination agreement may be either a subordinated loan agreement or a secured demand note agreement.

(ii) The term *subordinated loan agreement* means the agreement or agreements evidencing or governing a subordinated borrowing of cash.

(iii) The term "collateral value" of any securities pledged to secure a secured demand note means the market value of such securities after giving effect to the percentage deductions specified in Rule 240.15c3–1d(a)(2)(iii) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(a)(2)(iii)).

(iv) The term *payment obligation* means the obligation of an applicant or registrant in respect to any subordination agreement:

(A) To repay cash loaned to the applicant or registrant pursuant to a subordinated loan agreement; or

(B) To return a secured demand note contributed to the applicant or registrant or to reduce the unpaid principal amount thereof and to return cash or securities pledged as collateral to secure the secured demand note; and (C) "payment" shall mean the performance by an applicant or registrant of a payment obligation.

(v)(A) The term *secured demand note agreement* means an agreement (including the related secured demand note) evidencing or governing the contribution of a secured demand note to an applicant or registrant and the pledge of securities and/or cash with the applicant or registrant as collateral to secure payment of such secured demand note. The secured demand note agreement may provide that neither the lender, his heirs, executors, administrators, or assigns shall be personally liable on such note and that in the event of default the applicant or registrant shall look for payment of such note solely to the collateral then pledged to secure the same.

(B) The secured demand note shall be a promissory note executed by the lender and shall be payable on the demand of the applicant or registrant to which it is contributed: *Provided, however,* That the making of such demand may be conditioned upon the occurrence of any of certain events which are acceptable to the designated self-regulatory organization and the Commission.

(C) If such note is not paid upon presentment and demand as provided for therein, the applicant or registrant shall have the right to liquidate all or any part of the securities then pledged as collateral to secure payment of the same and to apply the net proceeds of such liquidation, together with any cash then included in the collateral, in payment of such note. Subject to the prior rights of the applicant or registrant as pledgee, the lender, as defined in paragraph (h)(i)(v)(F) of this section may retain ownership of the collateral and have the benefit of any increases and bear the risks of any decreases in the value of the collateral and may retain the right to vote securities contained within the collateral and any right to income therefrom or distributions thereon, except the applicant or registrant shall have the right to receive and hold as pledgee all dividends payable in securities and all partial and complete liquidating dividends.

(D) Subject to the prior rights of the applicant or registrant as pledgee, the lender may have the right to direct the sale of any securities included in the collateral, to direct the purchase of securities with any cash included therein, to withdraw excess collateral or to substitute cash or other securities as collateral: *Provided,* That the net proceeds of any such sale and the cash so substituted and the securities so purchased or substituted are held by the applicant or registrant as pledgee, and are included within the collateral to secure payment of the secured demand note: *And provided further,* That no such transaction shall be permitted, if, after giving effect thereto, the sum of the amount of any cash, plus the collateral value of the securities, then pledged as collateral to secure the secured demand note would be less than the unpaid principal amount of the secured demand note.

(E) Upon payment by the lender, as distinguished from a reduction by the lender which is provided for in paragraph (h)(2)(vi)(C) of this section or reduction by the applicant or registrant as provided for in paragraph (h)(2)(vii) of this section, of all or any part of the unpaid principal amount of the secured demand note, the applicant or registrant shall issue to the lender a subordinated loan agreement in the amount of such payment (or in the case of an applicant or registrant that is a partnership, credit a capital account of the lender), or issue preferred or common stock of the applicant or registrant in the amount of such payment, or any combination of the foregoing, as provided for in the secured demand note agreement.

(F) The term *lender* means the person who lends cash to an applicant or registrant pursuant to a subordinated loan agreement and the person who contributes a secured demand note to an applicant or registrant pursuant to a secured demand note agreement.

(2) Minimum requirements for subordination agreements:

(i) Subject to paragraph (h)(1) of this section, a subordination agreement shall mean a written agreement between the applicant or registrant and the lender, which:

(A) Has a minimum term of 1 year, except for temporary subordination agreements provided for in paragraph (h)(3)(v) of this section, and

(B) Is a valid and binding obligation enforceable in accordance with its terms (subject as to enforcement to applicable bankruptcy, insolvency, reorganization, moratorium, and other similar laws) against the applicant or registrant and the lender and their respective heirs, executors, administrators, successors, and assigns.

(ii) *Specific amount.* All subordination agreements shall be for a specific dollar amount which shall not be reduced for the duration of the agreement except by installments as specifically provided for therein and except as otherwise provided in this paragraph (h)(2) of this section.

(iii) *Effective subordination.* The subordination agreement shall effectively subordinate any right of the lender to receive any payment with respect thereto, together with accrued interest or compensation, to the prior payment or provision for payment in full of all claims of all present and future creditors of the applicant or registrant arising out of any matter occurring prior to the date on which the related payment obligation matures, except for claims which are the subject of subordination agreements which rank on the same priority as or junior to the claim of the lender under such subordination agreements.

(iv) *Proceeds of subordinated loan agreements.* The subordinated loan agreement shall provide that the cash proceeds thereof shall be used and dealt with by the applicant or registrant as part of its capital and shall be subject to the risks of the business.

(v) *Certain rights of the borrower.* The subordination agreement shall provide that the applicant or registrant shall have the right to:

(A) Deposit any cash proceeds of a subordinated loan agreement and any cash pledged as collateral to secure a secured demand note in an account or accounts in its own name in any bank or trust company;

(B) Pledge, repledge, hypothecate and rehypothecate, any or all of the securities pledged as collateral to secure a secured demand note, without notice, separately or in common with other securities or property for the purpose of securing any indebtedness of the applicant or registrant; and

(C) Lend to itself or others any or all of the securities and cash pledged as collateral to secure a secured demand note.

(vi) *Collateral for secured demand notes.* Only cash and securities which are fully paid for and which may be publicly offered or sold without registration under the Securities Act of 1933, and the offer, sale, and transfer of which are not otherwise restricted, may be pledged as collateral to secure a secured demand note. The secured demand note agreement shall provide that if at any time the sum of the amount of any cash, plus the collateral value of any securities, then pledged as collateral to secure the secured demand note is less than the unpaid principal amount of the secured demand note, the applicant or registrant must immediately transmit written notice to that

effect to the lender. The secured demand note agreement shall also provide that if the borrower is an applicant, such notice must also be transmitted immediately to the National Futures Association, and if the borrower is a registrant, such notice must also be transmitted immediately to the designated self-regulatory organization, if any, and the Commission. The secured demand note agreement shall also require that following such transmittal:

(A) The lender, prior to noon of the business day next succeeding the transmittal of such notice, may pledge as collateral additional cash or securities sufficient, after giving effect to such pledge, to bring the sum of the amount of any cash plus the collateral value of any securities, then pledged as collateral to secure the secured demand note, up to an amount not less than the unpaid principal amount of the secured demand note; and

(B) Unless additional cash or securities are pledged by the lender as provided in paragraph (h)(2)(vi)(A) above, the applicant or registrant at noon on the business day next succeeding the transmittal of notice to the lender must commence sale, for the account of the lender, of such of the securities then pledged as collateral to secure the secured demand note and apply so much of the net proceeds thereof, together with such of the cash then pledged as collateral to secure the secured demand note as may be necessary to eliminate the unpaid principal amount of the secured demand note: *Provided, however,* That the unpaid principal amount of the secured demand note need not be reduced below the sum of the amount of any remaining cash, plus the collateral value of the remaining securities, then pledged as collateral to secure the secured demand note. The applicant or registrant may not purchase for its own account any securities subject to such a sale; and

(C) The secured demand note agreement may also provide that, in lieu of the procedures specified in the provisions required by paragraph (h)(2)(vi)(B) of this section, the lender, with the prior written consent of the applicant and the National Futures Association, or with the prior written consent of the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory organization, the Commission, may reduce the unpaid principal amount of the secured demand note: *Provided,* That after giving effect to such reduction the adjusted net capital of the applicant or registrant would not be less than the greatest of:

(1) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

(2) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

(3) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

(4) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(b)(6)(iii) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(b)(6)(iii)): *Provided, further,* That no single secured demand note shall be permitted to be reduced by more than 15 percent of its original principal amount and after such reduction no excess collateral may be withdrawn.

(vii) *Permissive prepayments and special prepayments.* (A) An applicant or registrant at its option, but not at the option of the lender, may, if the subordination agreement so provides, make a payment of all or any portion of the payment obligation thereunder prior to the scheduled maturity date of such payment obligation (hereinafter referred to as a "prepayment"), but in no event may any prepayment be made before the expiration of one year from the date such subordination agreement became effective: *Provided, however,* That the foregoing restriction shall not apply to temporary subordination agreements which comply with the provisions of paragraph (h)(3)(v) of this section nor shall it apply to "special prepayments" made in accordance with the provisions of

paragraph (h)(2)(vii)(B) of this section. No prepayment shall be made if, after giving effect thereto (and to all payments of payment obligations under any other subordination agreements then outstanding, the maturity or accelerated maturities of which are scheduled to fall due within six months after the date such prepayment is to occur pursuant to this provision, or on or prior to the date on which the payment obligation in respect to such prepayment is scheduled to mature disregarding this provision, whichever date is earlier) without reference to any projected profit or loss of the applicant or registrant, the adjusted net capital of the applicant or registrant is less than the greatest of:

(1) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

(2) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

(3) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

(4) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(b)(7) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(b)(7)).

(B) An applicant or registrant at its option, but not at the option of the lender, may, if the subordination agreement so provides, make a payment at any time of all or any portion of the payment obligation thereunder prior to the scheduled maturity date of such payment obligation (hereinafter referred to as a "special prepayment"). No special prepayment shall be made if, after giving effect thereto (and to all payments of payment obligations under any other subordination agreements then outstanding, the maturity or accelerated maturities of which are scheduled to fall due within six months after the date such special prepayment is to occur pursuant to this provision, or on or prior to the date on which the payment obligation in respect to such special prepayment is scheduled to mature disregarding this provision, whichever date is earlier) without reference to any projected profit or loss of the applicant or registrant, the adjusted net capital of the applicant or registrant is less than the greatest of:

(1) 200 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

(2) For a futures commission merchant or applicant therefor, 125 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

(3) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

(4) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(c)(5)(ii) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(c)(5)(ii)): *Provided, however,* That no special prepayment shall be made if pre-tax losses during the latest three-month period were greater than 15 percent of current excess adjusted net capital.

(C)(1) Notwithstanding the provisions of paragraphs (h)(2)(vii)(A) and (h)(2)(vii)(B) of this section, in the case of an applicant, no prepayment or special prepayment shall occur without the prior written approval of the National Futures Association; in the case of a registrant, no prepayment or special prepayment shall occur without the prior written approval of the designated self-regulatory organization, if any, or of the Commission if the registrant is not a member of a self-regulatory organization.

(2) A registrant may make a prepayment or special prepayment without the prior written approval of the designated self-regulatory organization: Provided, That the registrant: Is a securities broker or dealer registered with the Securities and Exchange Commission; files a request to make a prepayment or special prepayment with its applicable securities designated examining authority, as defined in Rule 15c3-1(c)(12) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(12)), in the form and manner prescribed by the designated examining authority; files a copy of the prepayment request or special prepayment request with the designated self-regulatory organization at the time it files such request with the designated examining authority in the form and manner prescribed by the designated self-regulatory organization; and files a copy of the designated examining authority's approval of the prepayment or special prepayment with the designated self-regulatory organization immediately upon receipt of such approval. The approval of the prepayment or special prepayment by the designated examining authority will be deemed approval by the designated self-regulatory organization, unless the designated self-regulatory organization notifies the registrant that the designated examining authority's approval shall not constitute designated self-regulatory organization approval.

(3) The designated self-regulatory organization shall immediately provide the Commission with a copy of any notice of approval issued where the requested prepayment or special prepayment will result in the reduction of the registrant's net capital by 20 percent or more or the registrant's excess adjusted net capital by 30 percent or more.

(viii) *Suspended repayment.* (A) The payment obligation of the applicant or registrant in respect of any subordination agreement shall be suspended and shall not mature if, after giving effect to payment of such payment obligation (and to all payments of payment obligations of the applicant or registrant under any other subordination agreement(s) then outstanding which are scheduled to mature on or before such payment obligation), the adjusted net capital of the applicant or registrant would be less than the greatest of:

(1) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

(2) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

(3) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

(4) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(b)(8)(i) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(b)(8)(i)): *Provided,* That the subordination agreement may provide that if the payment obligation of the applicant or registrant thereunder does not mature and is suspended as a result of the requirement of this paragraph (h)(2)(viii) for a period of not less than six months, the applicant or registrant shall then commence the rapid and orderly liquidation of its business, but the right of the lender to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of this section.

(B) [Reserved]

(ix) *Accelerated maturity.* Obligation to repay to remain subordinate:

(A) Subject to the provisions of paragraph (h)(2)(viii) of this section, a subordination agreement may provide that the lender may, upon prior written notice to the applicant and the National Futures Association, or upon prior written notice to the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory

organization, the Commission, given not earlier than six months after the effective date of such subordination agreement, accelerate the date on which the payment obligation of the borrower, together with accrued interest or compensation, is scheduled to mature to a date not earlier than six months after giving of such notice, but the right of the lender to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of this paragraph (h)(2) of this section.

(B) Notwithstanding the provisions of paragraph (h)(2)(vii) of this section, the payment obligation of the applicant or registrant with respect to a subordination agreement, together with accrued interest and compensation, shall mature in the event of any receivership, insolvency, liquidation pursuant to the Securities Investor Protection Act of 1970 or otherwise, bankruptcy, assignment for the benefit of creditors, reorganization whether or not pursuant to the bankruptcy laws, or any other marshalling of the assets and liabilities of the applicant or registrant, but the right of the lender to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of paragraph (h)(2) of this section.

(x) *Accelerated maturity of subordination agreements on event of default and event of acceleration.* Obligation to repay to remain subordinate:

(A) A subordination agreement may provide that the lender may, upon prior written notice to the applicant and the National Futures Association, or upon prior written notice to the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory organization, the Commission, of the occurrence of any event of acceleration (as hereinafter defined) given no sooner than six months after the effective date of such subordination agreement, accelerate the date on which the payment obligation of the applicant or registrant, together with accrued interest or compensation, is scheduled to mature, to the last business day of a calendar month which is not less than six months after notice of acceleration is received by the applicant and by the National Futures Association, or by the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory organization, the Commission. Any subordination agreement containing such events of acceleration may also provide that, if upon such accelerated maturity date the payment obligation of the applicant or registrant is suspended as required by paragraph (h)(2)(viii) of this section and liquidation of the applicant or registrant has not commenced on or prior to such accelerated maturity date, notwithstanding paragraph (h)(2)(viii) of this section, the payment obligation of the applicant or registrant with respect to such subordination agreement shall mature on the day immediately following such accelerated maturity date and in any such event the payment obligations of the applicant or registrant with respect to all other subordination agreements then outstanding shall also mature at the same time but the rights of the respective lenders to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of paragraph (h)(2) of this section. Events of acceleration which may be included in a subordination agreement complying with this paragraph (h)(2)(x) of this section shall be limited to:

( 1 ) Failure to pay interest or any installment of principal on a subordination agreement as scheduled;

( 2 ) Failure to pay when due other money obligations of a specified material amount;

( 3 ) Discovery that any material, specified representation or warranty of the applicant or registrant which is included in the subordination agreement and on which the subordination agreement was based or continued was inaccurate in a material respect at the time made;

( 4 ) Any specified and clearly measurable event which is included in the subordination agreement and which the lender and the applicant or registrant agree, (a) is a significant indication that the financial position of the applicant or registrant has changed materially and adversely from agreed upon specified norms; or (b) could materially and adversely affect the

ability of the applicant or registrant to conduct its business as conducted on the date the subordination agreement was made; or (c) is a significant change in the senior management of the applicant or registrant or in the general business conducted by the applicant or registrant from that which obtained on the date the subordination agreement became effective;

(5) Any continued failure to perform agreed covenants included in the subordination agreement relating to the conduct of the business of the applicant or registrant or relating to the maintenance and reporting of its financial position; and

(B) Notwithstanding the provisions of paragraph (h)(2)(viii) of this section, a subordination agreement may provide that, if liquidation of the business of the applicant or registrant has not already commenced, the payment obligation of the applicant or registrant shall mature, together with accrued interest or compensation, upon the occurrence of an event of default (as hereinafter defined). Such agreement may also provide that, if liquidation of the business of the applicant or registrant has not already commenced, the rapid and orderly liquidation of the business of the applicant or registrant shall then commence upon the happening of an event of default. Any subordination agreement which so provides for maturity of the payment obligation upon the occurrence of an event of default shall also provide that the date on which such event of default occurs shall, if liquidation of the applicant or registrant has not already commenced, be the date on which the payment obligation of the applicant or registrant with respect to all other subordination agreements then outstanding shall mature but the rights of the respective lenders to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of paragraph (h)(2) of this section. Events of default which may be included in a subordination agreement shall be limited to:

(1) The making of an application by the Securities Investor Protection Corporation for a decree adjudicating that customers of the applicant or registrant are in need of protection under the Securities Investor Protection Act of 1970 and the failure of the applicant or registrant to obtain the dismissal of such application within 30 days;

(2) Failure to meet the minimum capital requirements of the designated self-regulatory organization, or of the Commission, throughout a period of 15 consecutive business days, commencing on the day the borrower first determines and notifies the designated self-regulatory organization, if any, of which he is a member and the Commission, in the case of a registrant, or the National Futures Association, in the case of an applicant, or commencing on the day any self-regulatory organization, the Commission or the National Futures Association first determines and notifies the applicant or registrant of such fact;

(3) The Commission shall revoke the registration of the applicant or registrant;

(4) The self-regulatory organization shall suspend (and not reinstate within 10 days) or revoke the applicant or registrant's status as a member thereof;

(5) Any receivership, insolvency, liquidation pursuant to the Securities Investor Protection Act of 1970 or otherwise, bankruptcy, assignment for the benefit of creditors, reorganization whether or not pursuant to bankruptcy laws, or any other marshalling of the assets and liabilities of the applicant or registrant. A subordination agreement which contains any of the provisions permitted by this subparagraph (2)(x) shall not contain the provision otherwise permitted by paragraph (h)(2)(ix)(A) of this section.

(3) *Miscellaneous provisions—(i) Prohibited cancellation.* The subordination agreement shall not be subject to cancellation by either party; no payment shall be made with respect thereto and the agreement shall not be terminated, rescinded or modified by mutual consent or otherwise if the effect thereof would be inconsistent with the requirements of paragraph (h) of this section.

(ii) *Notice of maturity or accelerated maturity.* Every applicant or registrant shall immediately notify the National Futures Association, and the registrant shall immediately notify the designated self-regulatory organization, if any, and the Commission if, after giving effect to all payments of payment obligations under subordination agreements then outstanding which are then due or mature within the following six months without reference to any projected profit or loss of the applicant or registrant, its adjusted net capital would be less than:

- (A) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;
- (B) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;
- (C) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or
- (D) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(c)(2) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(c)(2)).

(iii) *Certain legends.* If all the provisions of a satisfactory subordination agreement do not appear in a single instrument, then the debenture or other evidence of indebtedness shall bear on its face an appropriate legend stating that it is issued subject to the provisions of a satisfactory subordination agreement which shall be adequately referred to and incorporated by reference.

(iv) *Legal title to securities.* All securities pledged as collateral to secure a secured demand note must be in bearer form, or registered in the name of the applicant or registrant or the name of its nominee or custodian.

(v) *Temporary subordinations.* To enable an applicant or registrant to participate as an underwriter of securities or undertake other extraordinary activities and remain in compliance with the adjusted net capital requirements of this section, an applicant or registrant shall be permitted, on no more than three occasions in any 12-month period, to enter into a subordination agreement on a temporary basis which has a stated term of no more than 45 days from the date the subordination agreement became effective: *Provided*, That this temporary relief shall not apply to any applicant or registrant if the adjusted net capital of the applicant or registrant is less than the greatest of:

- (A) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;
- (B) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;
- (C) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member;
- (D) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(c)(5)(i) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(c)(5)(i)); or
- (E) The amount of equity capital as defined in paragraph (d) of this section is less than the limits specified in paragraph (d) of this section. Such temporary subordination agreement shall be subject to all the other provisions of this section.

(vi) *Filing.* An applicant shall file a signed copy of any proposed subordination agreement (including nonconforming subordination agreements) with the National Futures Association at least ten days prior to the proposed effective date of the agreement or at such other time as the National Futures Association for good cause shall accept such filing. A registrant that is not a member of any designated self-regulatory organization shall file two signed copies of any proposed subordination agreement (including nonconforming subordination agreements) with the regional office of the Commission nearest the principal place of business of the registrant at least ten days prior to the proposed effective date of the agreement or at such other time as the Commission for good cause shall accept such filing. A registrant that is a member of a designated self-regulatory organization shall file signed copies of any proposed subordination agreement (including nonconforming subordination agreements) with the designated self-regulatory organization in such quantities and at such time as the designated self-regulatory organization may require prior to the effective date. The applicant or registrant shall also file with said parties a statement setting forth the name and address of the lender, the business relationship of the lender to the applicant or registrant and whether the applicant or registrant carried funds or securities for the lender at or about the time the proposed agreement was so filed. A proposed agreement filed by an applicant with the National Futures Association shall be reviewed by the National Futures Association, and no such agreement shall be a satisfactory subordination agreement for the purposes of this section unless and until the National Futures Association has found the agreement acceptable and such agreement has become effective in the form found acceptable. A proposed agreement filed by a registrant shall be reviewed by the designated self-regulatory organization with whom such an agreement is required to be filed prior to its becoming effective or, if the registrant is not a member of any designated self-regulatory organization, by the regional office of the Commission where the agreement is required to be filed prior to its becoming effective. No proposed agreement shall be a satisfactory subordination agreement for the purposes of this section unless and until the designated self-regulatory organization or, if a registrant is not a member of any designated self-regulatory organization, the Commission, has found the agreement acceptable and such agreement has become effective in the form found acceptable: Provided, however, That a proposed agreement shall be a satisfactory subordination agreement for purpose of this section if the registrant: is a securities broker or dealer registered with the Securities and Exchange Commission; files signed copies of the proposed subordination agreement with the applicable securities designated examining authority, as defined in Rule 15c3-1(c)(12) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(12)), in the form and manner prescribed by the designated examining authority; files signed copies of the proposed subordination agreement with the designated self-regulatory organization at the time it files such copies with the designated examining authority in the form and manner prescribed by the designated self-regulatory organization; and files a copy of the designated examining authority's approval of the proposed subordination agreement with the designated self-regulatory organization immediately upon receipt of such approval. The designated examining authority's determination that the proposed subordination agreement satisfies the requirements for a satisfactory subordination agreement will be deemed a like finding by the designated self-regulatory organization, unless the designated self-regulatory organization notifies the registrant that the designated examining authority's determination shall not constitute a like finding by the designated self-regulatory organization.

(vii) *Subordination agreements that incorporate adjusted net capital requirements in effect prior to September 30, 2004.* Any subordination agreement that incorporates the adjusted net capital requirements in paragraphs (h)(2)(vi)(C)( 2 ), (h)(2)(vii)(A)( 2 ) and (B)( 2 ), (h)(2)(viii)(A)( 2 ), (h)(3)(ii)(B), and (h)(3)(v)(B) of this section, as in effect prior to September 30, 2004, and which has been deemed to be satisfactorily subordinated pursuant to this section prior to September 30, 2004, shall continue to be deemed a satisfactory subordination agreement until the maturity of such agreement. In the event, however, that such agreement is amended or renewed for any reason, then such agreement shall not be deemed a satisfactory subordination agreement unless the amended or renewed agreement meets the requirements of this section.

(4) A designated self-regulatory organization and the Commission may allow debt with a maturity date of 1 year or more to be treated as meeting the provisions of this paragraph (h): *Provided, (i)*

Such exemption shall only be given when the registrant's adjusted net capital is less than the minimum required by this section or by the capital rule of the designated self-regulatory organization to which such registrant is subject;

- (ii) That such debt did not exist prior to its use under this paragraph (h)(4);
- (iii) Such exemption shall be for a period of 30 days or such lesser period as the designated self-regulatory organization and the Commission may determine;
- (iv) Such exemption shall not be allowed more than once in any 12 month period; and
- (v) At all times during such exemption the registrant shall make a good faith effort to comply with the provisions of this section or the capital rule of the designated self-regulatory organization to which such registrant is subject exclusive of any benefits derived from this paragraph (h)(4).

(i) [Reserved]

(j) For the purposes of this section *cover* is defined as follows:

(1) *General definition.* Cover shall mean transactions or positions in a contract for future delivery on a board of trade or a commodity option where such transactions or positions normally represent a substitute for transactions to be made or positions to be taken at a later time in a physical marketing channel, and where they are economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise, and where they arise from:

- (i) The potential change in the value of assets which a person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising.
- (ii) The potential change in the value of liabilities which a person owes or anticipates incurring, or
- (iii) The potential change in the value of services which a person provides, purchases or anticipates providing or purchasing. Notwithstanding the foregoing, no transactions or positions shall be classified as cover for the purposes of this section unless their purpose is to offset price risks incidental to commercial cash or spot operations and such positions are established and liquidated in accordance with sound commercial practices and unless the provisions of paragraphs (j) (2) and (3) of this section have been satisfied.

(2) *Enumerated cover transactions.* The definition of covered transactions and positions in paragraph (j)(1) of this section includes, but is not limited to, the following specific transactions and positions:

- (i) Ownership or fixed-price purchase of any commodity which does not exceed in quantity (A) the sales of the same commodity for future delivery on a board of trade or (B) the purchase of a put commodity option of the same commodity for which the market value for the actual commodity or futures contract which is the subject of the option is less than the strike price of the option or (C) the ownership of a commodity option position established by the sale (grant) of a call commodity option of the same commodity for which the market value for the actual commodity or futures contract which is the subject of the option is more than the strike price of the option: *Provided,* That for purposes of paragraph (c)(5)(x) of this section the market value for the actual commodity or futures contract which is the subject of such option need not be more than the strike price of that option;
- (ii) Fixed-price sale of any commodity which does not exceed in quantity (A) the purchase of the same commodity for future delivery on a board of trade or (B) the purchase of a call commodity

option of the same commodity for which the market value for the actual commodity or futures contract which is the subject of such option is more than the strike price of the option or (C) ownership of a commodity option position established by the sale (grant) of a put commodity option of the same commodity for which the market value for the actual commodity or futures contract which is the subject of the option is less than the strike price of the option: *Provided*, That for purposes of paragraph (c)(5)(x) of this section the market value for the actual commodity or futures contract which is the subject of such option need not be less than the strike price of that option; and

(iii) Ownership or fixed-price contracts of a commodity described in paragraphs (j)(2)(i) and (j)(2)(ii) of this section may also be covered other than by the same quantity of the same cash commodity, provided that the fluctuations in value of the position for future delivery or commodity option are substantially related to the fluctuations in value of the actual cash position.

(3) *Nonenumerated cases*. Upon specific request, the Commission may recognize transactions and positions other than those enumerated in paragraph (j)(2) of this section as cover in amounts and under the terms and conditions as it may specify. Any applicant or registrant who wishes to avail itself of the provisions of this paragraph (j)(3) must apply to the Commission in writing at its principal office in Washington, DC giving full details of the transaction including detailed information which will demonstrate that the transaction is economically appropriate to the reduction of risk exposure attendant to the conduct and management of a commercial enterprise.

**[522] 523. Compliance with Commission Regulation 1.18  
- Records for and relating to Financial Reporting and  
Monthly Computation by Futures Commission  
Merchants and Introducing Brokers**

Any Trading Privilege Holder subject to Commission Regulation 1.18 that violates Commission Regulation 1.18 shall be deemed to have violated this Rule [522] 523. Commission Regulation 1.20 is set forth below and incorporated into this Rule [522] 523.

\* \* \* \* \*

**[523] 524. Compliance with Commission Regulation 1.20  
– Futures Customer Funds to Be Segregated and  
Separately Accounted For**

Any Trading Privilege Holder subject to Commission Regulation 1.20 that violates Commission Regulation 1.20 shall be deemed to have violated this Rule [523] 524. Commission Regulation 1.20 is set forth below and incorporated into this Rule [523] 524.

Commission Regulation 1.20 – [Customer] Futures customer funds to be segregated and separately accounted for[.]

[(a) All customer funds shall be separately accounted for and segregated as belonging to commodity or option customers. Such customer funds when deposited with any bank, trust company, clearing organization or another futures commission merchant shall be deposited under an account name which clearly identifies them as such and shows that they are segregated as required by the Act and this part. Each registrant shall obtain and retain in its files for the period provided in §1.31 a written acknowledgment from such bank, trust company, clearing organization, or futures commission merchant, that it was informed that the customer funds

deposited therein are those of commodity or option customers and are being held in accordance with the provisions of the Act and this part: *Provided, however,* that an acknowledgment need not be obtained from a clearing organization that has adopted and submitted to the Commission rules that provide for the segregation as customer funds, in accordance with all relevant provisions of the Act and the rules and orders promulgated thereunder, of all funds held on behalf of customers. Under no circumstances shall any portion of customer funds be obligated to a clearing organization, any member of a contract market, a futures commission merchant, or any depository except to purchase, margin, guarantee, secure, transfer, adjust or settle trades, contracts or commodity option transactions of commodity or option customers. No person, including any clearing organization or any depository, that has received customer funds for deposit in a segregated account, as provided in this section, may hold, dispose of, or use any such funds as belonging to any person other than the option or commodity customers of the futures commission merchant which deposited such funds.

(b) All customer funds received by a clearing organization from a member of the clearing organization to purchase, margin, guarantee, secure or settle the trades, contracts or commodity options of the clearing member's commodity or option customers and all money accruing to such commodity or option customers as the result of trades, contracts or commodity options so carried shall be separately accounted for and segregated as belonging to such commodity or option customers, and a clearing organization shall not hold, use or dispose of such customer funds except as belonging to such commodity or option customers. Such customer funds when deposited in a bank or trust company shall be deposited under an account name which clearly shows that they are the customer funds of the commodity or option customers of clearing members, segregated as required by the Act and these regulations. The clearing organization shall obtain and retain in its files for the period provided by §1.31 an acknowledgment from such bank or trust company that it was informed that the customer funds deposited therein are those of commodity or option customers of its clearing members and are being held in accordance with the provisions of the Act and these regulations.

(c) Each futures commission merchant shall treat and deal with the customer funds of a commodity customer or of an option customer as belonging to such commodity or option customer. All customer funds shall be separately accounted for, and shall not be commingled with the money, securities or property of a futures commission merchant or of any other person, or be used to secure or guarantee the trades, contracts or commodity options, or to secure or extend the credit, of any person other than the one for whom the same are held: *Provided, however,* That customer funds treated as belonging to the commodity or option customers of a futures commission merchant may for convenience be commingled and deposited in the same account or accounts with any bank or trust company, with another person registered as a futures commission merchant, or with a clearing organization, and that such share thereof as in the normal course of business is necessary to purchase, margin, guarantee, secure, transfer, adjust, or settle the trades, contracts or commodity options of such commodity or option customers or resulting market positions, with the clearing organization or with any other person registered as a futures commission merchant, may be withdrawn and applied to such purposes, including the payment of premiums to option grantors, commissions, brokerage, interest, taxes, storage and other fees and charges, lawfully accruing in connection with such trades, contracts or commodity options: *Provided, further,* That customer funds may be invested in instruments described in §1.25.]

(a) General. A futures commission merchant must separately account for all futures customer funds and segregate such funds as belonging to its futures customers. A futures commission merchant shall deposit futures customer funds under an account name that clearly identifies them as futures customer funds and shows that such funds are segregated as required by sections 4d(a) and 4d(b) of the Act and by this part. A futures commission merchant must at all times maintain in the separate account or accounts money, securities and property in an amount at least sufficient in the aggregate to cover its total obligations to all futures customers as computed under paragraph (i) of this section. The futures commission merchant must perform appropriate due diligence as required by §1.11 on any and all locations of futures customer funds,

as specified in paragraph (b) of this section, to ensure that the location in which the futures commission merchant has deposited such funds is a financially sound entity.

(b) Location of futures customer funds. A futures commission merchant may deposit futures customer funds, subject to the risk management policies and procedures of the futures commission merchant required by §1.11, with the following depositories:

- (1) A bank or trust company;
- (2) A derivatives clearing organization; or
- (3) Another futures commission merchant.

(c) Limitation on the holding of futures customer funds outside of the United States. A futures commission merchant may hold futures customer funds with a depository outside of the United States only in accordance with §1.49.

(d) Written acknowledgment from depositories. (1) A futures commission merchant must obtain a written acknowledgment from each bank, trust company, derivatives clearing organization, or futures commission merchant prior to or contemporaneously with the opening of an account by the futures commission merchant with such depositories; provided, however, that a written acknowledgment need not be obtained from a derivatives clearing organization that has adopted and submitted to the Commission rules that provide for the segregation of futures customer funds in accordance with all relevant provisions of the Act and the rules and orders promulgated thereunder.

(2) The written acknowledgment must be in the form as set out in Appendix A to this part.

(3)(i) A futures commission merchant shall deposit futures customer funds only with a depository that agrees to provide the director of the Division of Swap Dealer and Intermediary Oversight, or any successor division, or such director's designees, with direct, read-only electronic access to transaction and account balance information for futures customer accounts.

(ii) The written acknowledgment must contain the futures commission merchant's authorization to the depository to provide direct, read-only electronic access to futures customer account transaction and account balance information to the director of the Division of Swap Dealer and Intermediary Oversight, or any successor division, or such director's designees, without further notice to or consent from the futures commission merchant.

(4) A futures commission merchant shall deposit futures customer funds only with a depository that agrees to provide the Commission and the futures commission merchant's designated self-regulatory organization with a copy of the executed written acknowledgment no later than three business days after the opening of the account or the execution of a new written acknowledgment for an existing account, as applicable. The Commission must receive the written acknowledgment from the depository via electronic means, in a format and manner determined by the Commission. The written acknowledgment must contain the futures commission merchant's authorization to the depository to provide the written acknowledgment to the Commission and to the futures commission merchant's designated self-regulatory organization without further notice to or consent from the futures commission merchant.

(5) A futures commission merchant shall deposit futures customer funds only with a depository that agrees that accounts containing customer funds may be examined at any reasonable time by the director of the Division of Swap Dealer and Intermediary Oversight or the director of the Division of Clearing and Risk, or any successor divisions, or such directors' designees, or an appropriate officer, agent or employee of the futures commission merchant's

designated self-regulatory organization. The written acknowledgment must contain the futures commission merchant's authorization to the depository to permit any such examination to take place without further notice to or consent from the futures commission merchant.

(6) A futures commission merchant shall deposit futures customer funds only with a depository that agrees to reply promptly and directly to any request from the director of the Division of Swap Dealer and Intermediary Oversight or the director of the Division of Clearing and Risk, or any successor divisions, or such directors' designees, or an appropriate officer, agent or employee of the futures commission merchant's designated self-regulatory organization for confirmation of account balances or provision of any other information regarding or related to an account. The written acknowledgment must contain the futures commission merchant's authorization to the depository to reply promptly and directly as required by this paragraph without further notice to or consent from the futures commission merchant.

(7) The futures commission merchant shall promptly file a copy of the written acknowledgment with the Commission in the format and manner specified by the Commission no later than three business days after the opening of the account or the execution of a new written acknowledgment for an existing account, as applicable.

(8) A futures commission merchant shall obtain a new written acknowledgment within 120 days of any changes in the following:

- (i) The name or business address of the futures commission merchant;
- (ii) The name or business address of the bank, trust company, derivatives clearing organization or futures commission merchant receiving futures customer funds; or
- (iii) The account number(s) under which futures customer funds are held.

(9) A futures commission merchant shall maintain each written acknowledgment readily accessible in its files in accordance with §1.31, for as long as the account remains open, and thereafter for the period provided in §1.31.

(e) *Commingling.* (1) A futures commission merchant may for convenience commingle the futures customer funds that it receives from, or on behalf of, multiple futures customers in a single account or multiple accounts with one or more of the depositories listed in paragraph (b) of this section.

(2) A futures commission merchant shall not commingle futures customer funds with the money, securities or property of such futures commission merchant, or with any proprietary account of such futures commission merchant, or use such funds to secure or guarantee the obligation of, or extend credit to, such futures commission merchant or any proprietary account of such futures commission merchant; *provided, however,* a futures commission merchant may deposit proprietary funds in segregated accounts as permitted under §1.23.

(3) A futures commission merchant may not commingle futures customer funds with funds deposited by 30.7 customers as defined in §30.1 of this chapter and set aside in separate accounts as required by part 30 of this chapter, or with funds deposited by Cleared Swaps Customers as defined in §22.1 of this chapter and held in segregated accounts pursuant to section 4d(f) of the Act; *provided, however,* that a futures commission merchant may commingle futures customer funds with funds deposited by 30.7 customers or Cleared Swaps Customers if expressly permitted by a Commission regulation or order, or by a derivatives clearing organization rule approved in accordance with §39.15(b)(2) of this chapter.

(f) Limitation on use of futures customer funds. (1) A futures commission merchant shall treat and deal with the funds of a futures customer as belonging to such futures customer. A futures commission merchant shall not use the funds of a futures customer to secure or guarantee the commodity interests, or to secure or extend the credit, of any person other than the futures customer for whom the funds are held.

(2) A futures commission merchant shall obligate futures customer funds to a derivatives clearing organization, a futures commission merchant, or any depository solely to purchase, margin, guarantee, secure, transfer, adjust or settle trades, contracts or commodity option transactions of futures customers; *provided, however,* that a futures commission merchant is permitted to use the funds belonging to a futures customer that are necessary in the normal course of business to pay lawfully accruing fees or expenses on behalf of the futures customer's positions including commissions, brokerage, interest, taxes, storage and other fees and charges.

(3) No person, including any derivatives clearing organization or any depository, that has received futures customer funds for deposit in a segregated account, as provided in this section, may hold, dispose of, or use any such funds as belonging to any person other than the futures customers of the futures commission merchant which deposited such funds.

(g) Derivatives clearing organizations—(1) General. All futures customer funds received by a derivatives clearing organization from a member to purchase, margin, guarantee, secure or settle the trades, contracts or commodity options of the clearing member's futures customers and all money accruing to such futures customers as the result of trades, contracts or commodity options so carried shall be separately accounted for and segregated as belonging to such futures customers, and a derivatives clearing organization shall not hold, use or dispose of such futures customer funds except as belonging to such futures customers. A derivatives clearing organization shall deposit futures customer funds under an account name that clearly identifies them as futures customer funds and shows that such funds are segregated as required by sections 4d(a) and 4d(b) of the Act and by this part.

(2) Location of futures customer funds. A derivatives clearing organization may deposit futures customer funds with a bank or trust company, which may include a Federal Reserve Bank with respect to deposits of a derivatives clearing organization that is designated by the Financial Stability Oversight Council to be systemically important.

(3) Limitation on the holding of futures customer funds outside of the United States. A derivatives clearing organization may hold futures customer funds with a depository outside of the United States only in accordance with §1.49.

(4) Written acknowledgment from depositories. (i) A derivatives clearing organization must obtain a written acknowledgment from each depository prior to or contemporaneously with the opening of a futures customer funds account.

(ii) The written acknowledgment must be in the form as set out in Appendix B to this part; *provided, however,* that a derivatives clearing organization shall obtain from a Federal Reserve Bank only a written acknowledgment that:

(A) The Federal Reserve Bank was informed that the customer funds deposited therein are those of customers who trade commodities, options, swaps, and other products and are being held in accordance with the provisions of section 4d of the Act and Commission regulations thereunder; and

(B) The Federal Reserve Bank agrees to reply promptly and directly to any request from the director of the Division of Clearing and Risk or the director of the Division of Swap Dealer and

Intermediary Oversight, or any successor divisions, or such directors' designees, for confirmation of account balances or provision of any other information regarding or related to an account.

(iii) A derivatives clearing organization shall deposit futures customer funds only with a depository that agrees to provide the Commission with a copy of the executed written acknowledgment no later than three business days after the opening of the account or the execution of a new written acknowledgment for an existing account, as applicable. The Commission must receive the written acknowledgment from the depository via electronic means, in a format and manner determined by the Commission. The written acknowledgment must contain the derivatives clearing organization's authorization to the depository to provide the written acknowledgment to the Commission without further notice to or consent from the derivatives clearing organization.

(iv) A derivatives clearing organization shall deposit futures customer funds only with a depository that agrees to reply promptly and directly to any request from the director of the Division of Clearing and Risk or the director of the Division of Swap Dealer and Intermediary Oversight, or any successor divisions, or such directors' designees, for confirmation of account balances or provision of any other information regarding or related to an account. The written acknowledgment must contain the derivatives clearing organization's authorization to the depository to reply promptly and directly as required by this paragraph without further notice to or consent from the derivatives clearing organization.

(v) A derivatives clearing organization shall promptly file a copy of the written acknowledgment with the Commission in the format and manner specified by the Commission no later than three business days after the opening of the account or the execution of a new written acknowledgment for an existing account, as applicable.

(vi) A derivatives clearing organization shall obtain a new written acknowledgment within 120 days of any changes in the following:

(A) The name or business address of the derivatives clearing organization;

(B) The name or business address of the depository receiving futures customer funds; or

(C) The account number(s) under which futures customer funds are held.

(vii) A derivatives clearing organization shall maintain each written acknowledgment readily accessible in its files in accordance with §1.31, for as long as the account remains open, and thereafter for the period provided in §1.31.

(5) *Commingling.* (i) A derivatives clearing organization may for convenience commingle the futures customer funds that it receives from, or on behalf of, multiple futures commission merchants in a single account or multiple accounts with one or more of the depositories listed in paragraph (g)(2) of this section.

(ii) A derivatives clearing organization shall not commingle futures customer funds with the money, securities or property of such derivatives clearing organization or with any proprietary account of any of its clearing members, or use such funds to secure or guarantee the obligations of, or extend credit to, such derivatives clearing organization or any proprietary account of any of its clearing members.

(iii) A derivatives clearing organization may not commingle funds held for futures customers with funds deposited by clearing members on behalf of their 30.7 customers as defined in §30.1 of this chapter and set aside in separate accounts as required by part 30 of this chapter, or with funds deposited by clearing members on behalf of their Cleared Swaps Customers as defined in

§22.1 of this chapter and held in segregated accounts pursuant section 4d(f) of the Act; provided, however, that a derivatives clearing organization may commingle futures customer funds with funds deposited by clearing members on behalf of their 30.7 customers or Cleared Swaps Customers if expressly permitted by a Commission regulation or order, or by a derivatives clearing organization rule approved in accordance with §39.15(b)(2) of this chapter.

(h) Immediate availability of bank and trust company deposits. All futures customer funds deposited by a futures commission merchant or a derivatives clearing organization with a bank or trust company must be immediately available for withdrawal upon the demand of the futures commission merchant or derivatives clearing organization.

(i) Requirements as to amount. (1) For purposes of this paragraph (i), the term "account" shall mean the entries on the books and records of a futures commission merchant pertaining to the futures customer funds of a particular futures customer.

(2) The futures commission merchant must reflect in the account that it maintains for each futures customer the net liquidating equity for each such customer, calculated as follows: The market value of any futures customer funds that it receives from such customer, as adjusted by:

(i) Any uses permitted under paragraph (f) of this section;

(ii) Any accruals on permitted investments of such collateral under \$1.25 that, pursuant to the futures commission merchant's customer agreement with that customer, are creditable to such customer;

(iii) Any gains and losses with respect to contracts for the purchase or sale of a commodity for future delivery and any options on such contracts;

(iv) Any charges lawfully accruing to the futures customer, including any commission, brokerage fee, interest, tax, or storage fee; and

(v) Any appropriately authorized distribution or transfer of such collateral.

(3) If the market value of futures customer funds in the account of a futures customer is positive after adjustments, then that account has a credit balance. If the market value of futures customer funds in the account of a futures customer is negative after adjustments, then that account has a debit balance.

(4) The futures commission merchant must maintain in segregation an amount equal to the sum of any credit balances that the futures customers of the futures commission merchant have in their accounts. This balance may not be reduced by any debit balances that the futures customers of the futures commission merchants have in their accounts.

APPENDIX A TO §1.20—FUTURES COMMISSION MERCHANT ACKNOWLEDGMENT LETTER FOR CFTC REGULATION 1.20 CUSTOMER SEGREGATED ACCOUNT

[Date]

[Name and Address of Bank, Trust Company, Derivatives Clearing Organization or Futures Commission Merchant]

We refer to the Segregated Account(s) which [Name of Futures Commission Merchant] ("we" or "our") have opened or will open with [Name of Bank, Trust Company, Derivatives Clearing Organization or Futures Commission Merchant] ("you" or "your") entitled:

[Name of Futures Commission Merchant] [if applicable, add "FCM Customer Omnibus Account"] CFTC Regulation 1.20 Customer Segregated Account under Sections 4d(a) and 4d(b) of the Commodity Exchange Act [and, if applicable, ", Abbreviated as [short title reflected in the depository's electronic system]]"

Account Number(s): [ ]

(collectively, the "Account(s)").

You acknowledge that we have opened or will open the above-referenced Account(s) for the purpose of depositing, as applicable, money, securities and other property (collectively the "Funds") of customers who trade commodities, options, swaps, and other products, as required by Commodity Futures Trading Commission ("CFTC") Regulations, including Regulation 1.20, as amended; that the Funds held by you, hereafter deposited in the Account(s) or accruing to the credit of the Account(s), will be separately accounted for and segregated on your books from our own funds and from any other funds or accounts held by us in accordance with the provisions of the Commodity Exchange Act, as amended (the "Act"), and Part 1 of the CFTC's regulations, as amended; and that the Funds must otherwise be treated in accordance with the provisions of Section 4d of the Act and CFTC regulations thereunder.

Furthermore, you acknowledge and agree that such Funds may not be used by you or by us to secure or guarantee any obligations that we might owe to you, and they may not be used by us to secure or obtain credit from you. You further acknowledge and agree that the Funds in the Account(s) shall not be subject to any right of offset or lien for or on account of any indebtedness, obligations or liabilities we may now or in the future have owing to you. This prohibition does not affect your right to recover funds advanced in the form of cash transfers, lines of credit, repurchase agreements or other similar liquidity arrangements you make in lieu of liquidating non-cash assets held in the Account(s) or in lieu of converting cash held in the Account(s) to cash in a different currency.

In addition, you agree that the Account(s) may be examined at any reasonable time by the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent or employee of our designated self-regulatory organization ("DSRO"), [Name of DSRO], and this letter constitutes the authorization and direction of the undersigned on our behalf to permit any such examination to take place without further notice to or consent from us.

You agree to reply promptly and directly to any request for confirmation of account balances or provision of any other information regarding or related to the Account(s) from the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent, or employee of [Name of DSRO], acting in its capacity as our DSRO, and this letter constitutes the authorization and direction of the undersigned on our behalf to release the requested information without further notice to or consent from us.

You further acknowledge and agree that, pursuant to authorization granted by us to you previously or herein, you have provided, or will promptly provide following the opening of the Account(s), the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor division, or such director's designees, with technological connectivity, which may include provision of hardware, software, and related technology and protocol support, to facilitate direct, read-only electronic access to transaction and account balance information for the Account(s). This letter constitutes the authorization and direction of the undersigned on our behalf for you to establish this connectivity and access if not previously established, without further notice to or consent from us.

The parties agree that all actions on your part to respond to the above information and access requests will be made in accordance with, and subject to, such usual and customary authorization verification and authentication policies and procedures as may be employed by you to verify the authority of, and authenticate the identity of, the individual making any such information or access request, in order to provide for the secure transmission and delivery of the requested information or access to the appropriate recipient(s). We will not hold you responsible for acting pursuant to any information or access request from the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent, or employee of [Name of DSRO], acting in its capacity as our DSRO, upon which

you have relied after having taken measures in accordance with your applicable policies and procedures to assure that such request was provided to you by an individual authorized to make such a request.

In the event that we become subject to either a voluntary or involuntary petition for relief under the U.S. Bankruptcy Code, we acknowledge that you will have no obligation to release the Funds held in the Account(s), except upon instruction of the Trustee in Bankruptcy or pursuant to the Order of the respective U.S. Bankruptcy Court.

Notwithstanding anything in the foregoing to the contrary, nothing contained herein shall be construed as limiting your right to assert any right of offset or lien on assets that are not Funds maintained in the Account(s), or to impose such charges against us or any proprietary account maintained by us with you. Further, it is understood that amounts represented by checks, drafts or other items shall not be considered to be part of the Account(s) until finally collected. Accordingly, checks, drafts and other items credited to the Account(s) and subsequently dishonored or otherwise returned to you or reversed, for any reason, and any claims relating thereto, including but not limited to claims of alteration or forgery, may be charged back to the Account(s), and we shall be responsible to you as a general endorser of all such items whether or not actually so endorsed.

You may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry, provided that, in the ordinary course of your business as a depository, you have no notice of or actual knowledge of a potential violation by us of any provision of the Act or the CFTC regulations that relates to the segregation of customer funds; and you shall not in any manner not expressly agreed to herein be responsible to us for ensuring compliance by us with such provisions of the Act and CFTC regulations; however, the aforementioned presumption does not affect any obligation you may otherwise have under the Act or CFTC regulations.

You may, and are hereby authorized to, obey the order, judgment, decree or levy of any court of competent jurisdiction or any governmental agency with jurisdiction, which order, judgment, decree or levy relates in whole or in part to the Account(s). In any event, you shall not be liable by reason of any action or omission to act pursuant to any such order, judgment, decree or levy, to us or to any other person, firm, association or corporation even if thereafter any such order, decree, judgment or levy shall be reversed, modified, set aside or vacated.

The terms of this letter agreement shall remain binding upon the parties, their successors and assigns and, for the avoidance of doubt, regardless of a change in the name of either party. This letter agreement supersedes and replaces any prior agreement between the parties in connection with the Account(s), including but not limited to any prior acknowledgment letter agreement, to the extent that such prior agreement is inconsistent with the terms hereof. In the event of any conflict between this letter agreement and any other agreement between the parties in connection with the Account(s), this letter agreement shall govern with respect to matters specific to Section 4d of the Act and the CFTC's regulations thereunder, as amended.

This letter agreement shall be governed by and construed in accordance with the laws of [Insert governing law] without regard to the principles of choice of law.

Please acknowledge that you agree to abide by the requirements and conditions set forth above by signing and returning to us the enclosed copy of this letter agreement, and that you further agree to provide a copy of this fully executed letter agreement directly to the CFTC (via electronic means in a format and manner determined by the CFTC) and to [Name of DSRO], acting in its capacity as our DSRO. We hereby authorize and direct you to provide such copies without further notice to or consent from us, no later than three business days after opening the Account(s) or revising this letter agreement, as applicable.

[Name of Futures Commission Merchant]

By:

Print Name:

Title:

ACKNOWLEDGED AND AGREED:

[Name of Bank, Trust Company, Derivatives Clearing Organization or Futures Commission Merchant]

By:

Print Name:

Title:

Contact Information: [Insert phone number and email address]

DATE:

APPENDIX B TO §1.20—DERIVATIVES CLEARING ORGANIZATION ACKNOWLEDGMENT LETTER FOR CFTC REGULATION 1.20 CUSTOMER SEGREGATED ACCOUNT

[Date]

[Name and Address of Bank or Trust Company]

We refer to the Segregated Account(s) which [Name of Derivatives Clearing Organization] ("we" or "our") have opened or will open with [Name of Bank or Trust Company] ("you" or "your") entitled:

[Name of Derivatives Clearing Organization] Futures Customer Omnibus Account, CFTC Regulation 1.20 Customer Segregated Account under Sections 4d(a) and 4d(b) of the Commodity Exchange Act [and, if applicable, "Abbreviated as [short title reflected in the depository's electronic system]"]

Account Number(s): [ ]

(collectively, the "Account(s)").

You acknowledge that we have opened or will open the above-referenced Account(s) for the purpose of depositing, as applicable, money, securities and other property (collectively the "Funds") of customers who trade commodities, options, swaps, and other products, as required by Commodity Futures Trading Commission ("CFTC") Regulations, including Regulation 1.20, as amended; that the Funds held by you, hereafter deposited in the Account(s) or accruing to the credit of the Account(s), will be separately accounted for and segregated on your books from our own funds and from any other funds or accounts held by us in accordance with the provisions of the Commodity Exchange Act, as amended (the "Act"), and Part 1 of the CFTC's regulations, as amended; and that the Funds must otherwise be treated in accordance with the provisions of Section 4d of the Act and CFTC regulations thereunder.

Furthermore, you acknowledge and agree that such Funds may not be used by you or by us to secure or guarantee any obligations that we might owe to you, and they may not be used by us to secure or obtain credit from you. You further acknowledge and agree that the Funds in the Account(s) shall not be subject to any right of offset or lien for or on account of any indebtedness, obligations or liabilities we may now or in the future have owing to you. This prohibition does not affect your right to recover funds advanced in the form of cash transfers, lines of credit, repurchase agreements or other similar liquidity arrangements you make in lieu of liquidating non-cash assets held in the Account(s) or in lieu of converting cash held in the Account(s) to cash in a different currency.

You agree to reply promptly and directly to any request for confirmation of account balances or provision of any other information regarding or related to the Account(s) from the director of the Division of Clearing and Risk of the CFTC or the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor divisions, or such directors' designees, and this letter constitutes the authorization and direction of the undersigned on our behalf to release the requested information without further notice to or consent from us.

The parties agree that all actions on your part to respond to the above information requests will be made in accordance with, and subject to, such usual and customary authorization verification and authentication policies and procedures as may be employed by you to verify the authority of, and authenticate the identity of, the individual making any such information request, in order to provide for the

secure transmission and delivery of the requested information to the appropriate recipient(s). We will not hold you responsible for acting pursuant to any information request from the director of the Division of Clearing and Risk of the CFTC or the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor divisions, or such directors' designees, upon which you have relied after having taken measures in accordance with your applicable policies and procedures to assure that such request was provided to you by an individual authorized to make such a request.

In the event that we or any of our futures commission merchant clearing members become(s) subject to either a voluntary or involuntary petition for relief under the U.S. Bankruptcy Code, we acknowledge that you will have no obligation to release the Funds held in the Account(s), except upon instruction of the Trustee in Bankruptcy or pursuant to the Order of the respective U.S. Bankruptcy Court.

Notwithstanding anything in the foregoing to the contrary, nothing contained herein shall be construed as limiting your right to assert any right of offset or lien on assets that are not Funds maintained in the Account(s), or to impose such charges against us or any proprietary account maintained by us with you. Further, it is understood that amounts represented by checks, drafts or other items shall not be considered to be part of the Account(s) until finally collected. Accordingly, checks, drafts and other items credited to the Account(s) and subsequently dishonored or otherwise returned to you or reversed, for any reason, and any claims relating thereto, including but not limited to claims of alteration or forgery, may be charged back to the Account(s), and we shall be responsible to you as a general endorser of all such items whether or not actually so endorsed.

You may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry, provided that, in the ordinary course of your business as a depository, you have no notice of or actual knowledge of a potential violation by us of any provision of the Act or the CFTC regulations that relates to the segregation of customer funds; and you shall not in any manner not expressly agreed to herein be responsible to us for ensuring compliance by us with such provisions of the Act and CFTC regulations; however, the aforementioned presumption does not affect any obligation you may otherwise have under the Act or CFTC regulations.

You may, and are hereby authorized to, obey the order, judgment, decree or levy of any court of competent jurisdiction or any governmental agency with jurisdiction, which order, judgment, decree or levy relates in whole or in part to the Account(s). In any event, you shall not be liable by reason of any action or omission to act pursuant to any such order, judgment, decree or levy, to us or to any other person, firm, association or corporation even if thereafter any such order, decree, judgment or levy shall be reversed, modified, set aside or vacated.

The terms of this letter agreement shall remain binding upon the parties, their successors and assigns and, for the avoidance of doubt, regardless of a change in the name of either party. This letter agreement supersedes and replaces any prior agreement between the parties in connection with the Account(s), including but not limited to any prior acknowledgment letter agreement, to the extent that such prior agreement is inconsistent with the terms hereof. In the event of any conflict between this letter agreement and any other agreement between the parties in connection with the Account(s), this letter agreement shall govern with respect to matters specific to Section 4d of the Act and the CFTC's regulations thereunder, as amended.

This letter agreement shall be governed by and construed in accordance with the laws of [Insert governing law] without regard to the principles of choice of law.

Please acknowledge that you agree to abide by the requirements and conditions set forth above by signing and returning to us the enclosed copy of this letter agreement, and that you further agree to provide a copy of this fully executed letter agreement directly to the CFTC (via electronic means in a format and manner determined by the CFTC). We hereby authorize and direct you to provide such copy without further notice to or consent from us, no later than three business days after opening the Account(s) or revising this letter agreement, as applicable.

[Name of Derivatives Clearing Organization]

By:

Print Name:

Title:

ACKNOWLEDGED AND AGREED:

[Name of Bank or Trust Company]

By:

Print Name:

Title:

Contact Information: [Insert phone number and email address]

DATE:

**[524] 525. Compliance with Commission Regulation 1.21  
- Care of Money and Equities Accruing to Customers**

Any Trading Privilege Holder subject to Commission Regulation 1.21 that violates Commission Regulation 1.21 shall be deemed to have violated this Rule [524] 525. Commission Regulation 1.21 is set forth below and incorporated into this Rule [524] 525.

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**[525] 526. Compliance with Commission Regulation 1.22  
- Use of Futures Customer Funds Restricted**

Any Trading Privilege Holder subject to Commission Regulation 1.22 that violates Commission Regulation 1.22 shall be deemed to have violated this Rule [525] 526. Commission Regulation 1.22 is set forth below and incorporated into this Rule [525] 526.

Commission Regulation 1.22 - Use of futures customer funds restricted.

[No futures commission merchant shall use, or permit the use of, the customer funds of one commodity and/or option customer to purchase, margin, or settle the trades, contracts, or commodity options of, or to secure or extend the credit of, any person other than such customer or option customer. Customer funds shall not be used to carry trades or positions of the same commodity and/or option customer other than in commodities or commodity options traded through the facilities of a contract market.]

(a) No futures commission merchant shall use, or permit the use of, the futures customer funds of one futures customer to purchase, margin, or settle the trades, contracts, or commodity options of, or to secure or extend the credit of, any person other than such futures customer.

(b) Futures customer funds shall not be used to carry trades or positions of the same futures customer other than in contracts for the purchase or sale of any commodity for future delivery or for options thereon traded through the facilities of a designated contract market.

(c)(1) The undermargin amount for a futures customer's account is the amount, if any, by which:

(i) The total amount of collateral required for that futures customer's positions in that account, at the time or times referred to in paragraph (c)(2) of this section, exceeds

(ii) The value of the futures customer funds for that account, as calculated in §1.20(i)(2).

(2) Each futures commission merchant must compute, based on the information available to the futures commission merchant as of the close of each business day,

(i) The undermargined amounts, based on the clearing initial margin that will be required to be maintained by that futures commission merchant for its futures customers, at each derivatives clearing organization of which the futures commission merchant is a member, at the point of the daily settlement (as described in §39.14 of this chapter) that will complete during the following business day for each such derivatives clearing organization less

(ii) Any debit balances referred to in §1.20(i)(4) included in such undermargined amounts.

(3)(i) Prior to the Residual Interest Deadline, such futures commission merchant must maintain residual interest in segregated funds that is at least equal to the computation set forth in paragraph (c)(2) of this section. Where a futures commission merchant is subject to multiple Residual Interest Deadlines, prior to each Residual Interest Deadline, such futures commission merchant must maintain residual interest in segregated funds that is at least equal to the portion of the computation set forth in paragraph (c)(2) of this section attributable to the clearing initial margin required by the derivatives clearing organization making such settlement.

(ii) A futures commission merchant may reduce the amount of residual interest required in paragraph (c)(3)(i) of this section to account for payments received from or on behalf of undermargined futures customers (less the sum of any disbursements made to or on behalf of such customers) between the close of the previous business day and the Residual Interest Deadline.

(4) For purposes of paragraph (c)(2) of this section, a futures commission merchant should include, as clearing initial margin, customer initial margin that the futures commission merchant will be required to maintain, for that futures commission merchant's futures customers, at another futures commission merchant.

(5) *Residual Interest Deadline defined.* (i) Except as provided in paragraph (c)(5)(ii) of this section, the Residual Interest Deadline shall be the time of the settlement referenced in paragraph (c)(2)(i) or, as appropriate, (c)(4), of this section.

(ii) Starting on November 14, 2014 and during the phase-in period described in paragraph (c)(5)(iii) of this section, the Residual Interest Deadline shall be 6:00 p.m. Eastern Time on the date of the settlement referenced in paragraph (c)(2)(i) or, as appropriate, (c)(4), of this section.

(iii)(A) No later than May 16, 2016, the staff of the Commission shall complete and publish for public comment a report addressing, to the extent information is practically available, the practicability (for both futures commission merchants and customers) of moving that deadline from 6:00 p.m. Eastern Time on the date of the settlement referenced in paragraph (c)(2)(i) or, as appropriate, (c)(4), of this section to the time of that settlement (or to some other time of day), including whether and on what schedule it would be feasible to do so, and the costs and benefits of such potential requirements. Staff shall, using the Commission's Web site, solicit public comment and shall conduct a public roundtable regarding specific issues to be covered by such report.

(B) Nine months after publication of the report required by paragraph (c)(5)(iii)(A) of this section, the Commission may (but shall not be required to) do either or both of the following:

(1) Terminate the phase-in period, in which case the phase-in period shall end as of a date established by order published in the FEDERAL REGISTER, which date shall be no less than one year after the date such order is published; or

(2) Determine that it is necessary or appropriate in the public interest to propose through rulemaking a different Residual Interest Deadline. In that event, the Commission shall establish, by order published in the FEDERAL REGISTER, a phase-in schedule.

(C) If the phase-in schedule has not been amended pursuant to paragraph (c)(5)(iii)(B) of this section, then the phase-in period shall end on December 31, 2018.

**[526] 527. Compliance with Commission Regulation 1.23  
- Interest of Futures Commission Merchants in  
Segregated Futures Customer Funds; Additions and  
Withdrawals**

Any Trading Privilege Holder subject to Commission Regulation 1.23 that violates Commission Regulation 1.23 shall be deemed to have violated this Rule [526] 527. Commission Regulation 1.23 is set forth below and incorporated into this Rule [526] 527.

Commission Regulation 1.23 - Interest of futures commission merchant in segregated futures customer funds; additions and withdrawals.

[The provision in section 4d(a)(2) of the Act and the provision in §1.20(c), which prohibit the commingling of customer funds with the funds of a futures commission merchant, shall not be construed to prevent a futures commission merchant from having a residual financial interest in the customer funds, segregated as required by the Act and the rules in this part and set apart for the benefit of commodity or option customers; nor shall such provisions be construed to prevent a futures commission merchant from adding to such segregated customer funds such amount or amounts of money, from its own funds or unencumbered securities from its own inventory, of the type set forth in §1.25, as it may deem necessary to ensure any and all commodity or option customers' accounts from becoming undersegregated at any time. The books and records of a futures commission merchant shall at all times accurately reflect its interest in the segregated funds. A futures commission merchant may draw upon such segregated funds to its own order, to the extent of its actual interest therein, including the withdrawal of securities held in segregated safekeeping accounts held by a bank, trust company, contract market clearing organization or other futures commission merchant. Such withdrawal shall not result in the funds of one commodity and/or option customer being used to purchase, margin or carry the trades, contracts or commodity options, or extend the credit of any other commodity customer, option customer or other person.]

(a)(1) The provision in sections 4d(a)(2) and 4d(b) of the Act and the provision in §1.20 that prohibit the commingling of futures customer funds with the funds of a futures commission merchant, shall not be construed to prevent a futures commission merchant from having a residual financial interest in the futures customer funds segregated as required by the Act and the regulations in this part and set apart for the benefit of futures customers; nor shall such provisions be construed to prevent a futures commission merchant from adding to such segregated futures customer funds such amount or amounts of money, from its own funds or unencumbered securities from its own inventory, of the type set forth in §1.25 of this part, as it may deem necessary to ensure any and all futures customers' accounts from becoming undersegregated at any time.

(2) If a futures commission merchant discovers at any time that it is holding insufficient funds in segregated accounts to meet its obligations under §§1.20 and 1.22, the futures commission merchant shall immediately deposit sufficient funds into segregation to bring the account into compliance.

(b) A futures commission merchant may not withdraw funds, except withdrawals that are made to or for the benefit of futures customers, from an account or accounts holding futures customer funds unless the futures commission merchant has prepared the daily segregation calculation required by §1.32 as of the close of business on the previous business day. A futures commission merchant that has completed its daily segregation calculation may make withdrawals, in addition to withdrawals that are made to or for the benefit of futures customers, to the extent of its actual residual financial interest in funds held in segregated futures accounts, adjusted to reflect market activity and other events that may have decreased the amount of the firm's residual financial interest since the close of business on the previous business day, including the withdrawal of securities held in segregated safekeeping accounts held by a bank, trust company, derivatives clearing organization or other futures commission merchant. Such withdrawal(s), however, shall not result in the funds of one futures customer being used to purchase, margin or carry the trades, contracts or commodity options, or extend the credit of any other futures customer or other person.

(c) Notwithstanding paragraphs (a) and (b) of this section, each futures commission merchant shall establish a targeted residual interest (i.e., excess funds) that is in an amount that, when maintained as its residual interest in the segregated funds accounts, reasonably ensures that the futures commission merchant shall remain in compliance with the segregated funds requirements at all times. Each futures commission merchant shall establish policies and procedures designed to reasonably ensure that the futures commission merchant maintains the targeted residual amounts in segregated funds at all times. The futures commission merchant shall maintain sufficient capital and liquidity, and take such other appropriate steps as are necessary, to reasonably ensure that such amount of targeted residual interest is maintained as the futures commission merchant's residual interest in the segregated funds accounts at all times. In determining the amount of the targeted residual interest, the futures commission merchant shall analyze all relevant factors affecting the amounts in segregated funds from time to time, including without limitation various factors, as applicable, relating to the nature of the futures commission merchant's business including, but not limited to, the composition of the futures commission merchant's customer base, the general creditworthiness of the customer base, the general trading activity of the customers, the types of markets and products traded by the customers, the proprietary trading of the futures commission merchant, the general volatility and liquidity of the markets and products traded by customers, the futures commission merchant's own liquidity and capital needs, and the historical trends in customer segregated fund balances and debit balances in customers' and undermargined accounts. The analysis and calculation of the targeted amount of the future commission merchant's residual interest must be described in writing with the specificity necessary to allow the Commission and the futures commission merchant's designated self-regulatory organization to duplicate the analysis and calculation and test the assumptions made by the futures commission merchant. The adequacy of the targeted residual interest and the process for establishing the targeted residual interest must be reassessed periodically by the futures commission merchant and revised as necessary.

(d) Notwithstanding any other paragraph of this section, a futures commission merchant may not withdraw funds, in a single transaction or a series of transactions, that are not made to or for the benefit of futures customers from futures accounts if such withdrawal(s) would exceed 25 percent of the futures commission merchant's residual interest in such accounts as reported on the daily segregation calculation required by §1.32 and computed as of the close of business on the previous business day, unless:

(1) The futures commission merchant's chief executive officer, chief finance officer or other senior official that is listed as a principal of the futures commission merchant on its Form 7-R and is

knowledgeable about the futures commission merchant's financial requirements and financial position pre-approves in writing the withdrawal, or series of withdrawals;

(2) The futures commission merchant files written notice of the withdrawal or series of withdrawals, with the Commission and with its designated self-regulatory organization immediately after the chief executive officer, chief finance officer or other senior official as described in paragraph (c)(1) of this section pre-approves the withdrawal or series of withdrawals. The written notice must:

(i) Be signed by the chief executive officer, chief finance officer or other senior official as described in paragraph (c)(1) of this section that pre-approved the withdrawal, and give notice that the futures commission merchant has withdrawn or intends to withdraw more than 25 percent of its residual interest in segregated accounts holding futures customer funds;

(ii) Include a description of the reasons for the withdrawal or series of withdrawals;

(iii) List the amount of funds provided to each recipient and each recipient's name;

(iv) Include the current estimate of the amount of the futures commission merchant's residual interest in the futures accounts after the withdrawal;

(v) Contain a representation by the chief executive officer, chief finance officer or other senior official as described in paragraph (c)(1) of this section that pre-approved the withdrawal, or series of withdrawals, that, after due diligence, to such person's knowledge and reasonable belief, the futures commission merchant remains in compliance with the segregation requirements after the withdrawal. The chief executive officer, chief finance officer or other senior official as described in paragraph (c)(1) of this section must consider the daily segregation calculation as of the close of business on the previous business day and any other factors that may cause a material change in the futures commission merchant's residual interest since the close of business the previous business day, including known unsecured futures customer debits or deficits, current day market activity and any other withdrawals made from the futures accounts; and

(vi) Any such written notice filed with the Commission must be filed via electronic transmission using a form of user authentication assigned in accordance with procedures established by or approved by the Commission, and otherwise in accordance with instruction issued by or approved by the Commission. Any such electronic submission must clearly indicate the registrant on whose behalf such filing is made and the use of such user authentication in submitting such filing will constitute and become a substitute for the manual signature of the authorized signer. Any written notice filed must be followed up with direct communication to the Regional office of the Commission that has supervisory authority over the futures commission merchant whereby the Commission acknowledges receipt of the notice; and

(3) After making a withdrawal requiring the approval and notice required in paragraphs (c)(1) and (2) of this section, and before the completion of its next daily segregated funds calculation, no futures commission merchant may make any further withdrawals from accounts holding futures customer funds, except to or for the benefit of futures customers, without, for each withdrawal, obtaining the approval required under paragraph (c)(1) of this section and filing a written notice in the manner specified under paragraph (c)(2) of this section with the Commission and its designated self-regulatory organization signed by the chief executive officer, chief finance officer, or other senior official. The written notice must:

(i) List the amount of funds provided to each recipient and each recipient's name;

(ii) Disclose the reason for each withdrawal;

(iii) Confirm that the chief executive officer, chief finance officer, or other senior official (and identify of the person if different from the person who signed the notice) pre-approved the withdrawal in writing;

(iv) Disclose the current estimate of the futures commission merchant's remaining total residual interest in the segregated accounts holding futures customer funds after the withdrawal; and

(v) Include a representation that, after due diligence, to the best of the notice signatory's knowledge and reasonable belief the futures commission merchant remains in compliance with the segregation requirements after the withdrawal.

(e) If a futures commission merchant withdraws funds from futures accounts that are not made to or for the benefit of futures customers, and the withdrawal causes the futures commission merchant to not hold sufficient funds in the futures accounts to meet its targeted residual interest, as required to be computed under §1.11, the futures commission merchant should deposit its own funds into the futures accounts to restore the account balance to the targeted residual interest amount by the close of business on the next business day, or, if appropriate, revise the futures commission merchant's targeted amount of residual interest pursuant to the policies and procedures required by §1.11. Notwithstanding the foregoing, if a the futures commission merchant's residual interest in customer accounts is less than the amount required by §1.22 at any particular point in time, the futures commission merchant must immediately restore the residual interest to exceed the sum of such amounts. Any proprietary funds deposited in the futures accounts must be unencumbered and otherwise compliant with §1.25, as applicable.

**[527] 528. Compliance with Commission Regulation 1.24  
- Segregated Funds; Exclusions Therefrom**

Any Trading Privilege Holder subject to Commission Regulation 1.24 that violates Commission Regulation 1.24 shall be deemed to have violated this Rule [527] 528. Commission Regulation 1.24 is set forth below and incorporated into this Rule [527] 528.

\* \* \* \* \*

**[528] 529. Compliance with Commission Regulation 1.25  
- Investment of Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.25 that violates Commission Regulation 1.25 shall be deemed to have violated this Rule [528] 529. Commission Regulation 1.25 is set forth below and incorporated into this Rule [528] 529.

Commission Regulation 1.25 - Investment of customer funds.

(a) *Permitted investments.* (1) Subject to the terms and conditions set forth in this section, a futures commission merchant or a derivatives clearing organization may invest customer money in the following instruments (permitted investments):

(i) Obligations of the United States and obligations fully guaranteed as to principal and interest by the United States (U.S. government securities);

(ii) General obligations of any State or of any political subdivision thereof (municipal securities);

- (iii) Obligations of any United States government corporation or enterprise sponsored by the United States government (U.S. agency obligations);
- (iv) Certificates of deposit issued by a bank (certificates of deposit) as defined in section 3(a)(6) of the Securities Exchange Act of 1934, or a domestic branch of a foreign bank that carries deposits insured by the Federal Deposit Insurance Corporation;
- (v) Commercial paper fully guaranteed as to principal and interest by the United States under the Temporary Liquidity Guarantee Program as administered by the Federal Deposit Insurance Corporation (commercial paper);
- (vi) Corporate notes or bonds fully guaranteed as to principal and interest by the United States under the Temporary Liquidity Guarantee Program as administered by the Federal Deposit Insurance Corporation (corporate notes or bonds); and
- (vii) Interests in money market mutual funds.

(2)(i) In addition, a futures commission merchant or derivatives clearing organization may buy and sell the permitted investments listed in paragraphs (a)(1)(i) through (vii) of this section pursuant to agreements for resale or repurchase of the instruments, in accordance with the provisions of paragraph (d) of this section.

(ii) A futures commission merchant or a derivatives clearing organization may sell securities deposited by customers as margin pursuant to agreements to repurchase subject to the following:

- (A) Securities subject to such repurchase agreements must be "highly liquid" as defined in paragraph (b)(1) of this section.
- (B) Securities subject to such repurchase agreements must not be "specifically identifiable property" as defined in §190.01(kk) of this chapter.
- (C) The terms and conditions of such an agreement to repurchase must be in accordance with the provisions of paragraph (d) of this section.
- (D) Upon the default by a counterparty to a repurchase agreement, the futures commission merchant or derivatives clearing organization shall act promptly to ensure that the default does not result in any direct or indirect cost or expense to the customer.

(3) Obligations issued by the Federal National Mortgage Association or the Federal Home Loan Mortgage Association are permitted while these entities operate under the conservatorship or receivership of the Federal Housing Finance Authority with capital support from the United States.

(b) *General terms and conditions.* A futures commission merchant or a derivatives clearing organization is required to manage the permitted investments consistent with the objectives of preserving principal and maintaining liquidity and according to the following specific requirements:

- (1) *Liquidity.* Investments must be "highly liquid" such that they have the ability to be converted into cash within one business day without material discount in value.
- (2) *Restrictions on instrument features.* (i) With the exception of money market mutual funds, no permitted investment may contain an embedded derivative of any kind, except as follows:
  - (A) The issuer of an instrument otherwise permitted by this section may have an option to call, in whole or in part, at par, the principal amount of the instrument before its stated maturity date; or

(B) An instrument that meets the requirements of paragraph (b)(2)(iv) of this section may provide for a cap, floor, or collar on the interest paid; *provided, however,* that the terms of such instrument obligate the issuer to repay the principal amount of the instrument at not less than par value upon maturity.

(ii) No instrument may contain interest-only payment features.

(iii) No instrument may provide payments linked to a commodity, currency, reference instrument, index, or benchmark except as provided in paragraph (b)(2)(iv) of this section, and it may not otherwise constitute a derivative instrument.

(iv)(A) Adjustable rate securities are permitted, subject to the following requirements:

( 1 ) The interest payments on variable rate securities must correlate closely and on an unleveraged basis to a benchmark of either the Federal Funds target or effective rate, the prime rate, the three-month Treasury Bill rate, the one-month or three-month LIBOR rate, or the interest rate of any fixed rate instrument that is a permitted investment listed in paragraph (a)(1) of this section;

( 2 ) The interest payment, in any period, on floating rate securities must be determined solely by reference, on an unleveraged basis, to a benchmark of either the Federal Funds target or effective rate, the prime rate, the three-month Treasury Bill rate, the one-month or three-month LIBOR rate, or the interest rate of any fixed rate instrument that is a permitted investment listed in paragraph (a)(1) of this section;

( 3 ) Benchmark rates must be expressed in the same currency as the adjustable rate securities that reference them; and

( 4 ) No interest payment on an adjustable rate security, in any period, can be a negative amount.

(B) For purposes of this paragraph, the following definitions shall apply:

( 1 ) The term *adjustable rate security* means, a floating rate security, a variable rate security, or both.

( 2 ) The term *floating rate security* means a security, the terms of which provide for the adjustment of its interest rate whenever a specified interest rate changes and that, at any time until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have market value that approximates its amortized cost.

( 3 ) The term *variable rate security* means a security, the terms of which provide for the adjustment of its interest rate on set dates (such as the last day of a month or calendar quarter) and that, upon each adjustment until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have a market value that approximates its amortized cost.

(v) Certificates of deposit must be redeemable at the issuing bank within one business day, with any penalty for early withdrawal limited to any accrued interest earned according to its written terms.

(vi) Commercial paper and corporate notes or bonds must meet the following criteria:

(A) The size of the issuance must be greater than \$1 billion;

- (B) The instrument must be denominated in U.S. dollars; and
  - (C) The instrument must be fully guaranteed as to principal and interest by the United States for its entire term.
- (3) *Concentration* —(i) *Asset-based concentration limits for direct investments.* (A) Investments in U.S. government securities shall not be subject to a concentration limit.
- (B) Investments in U.S. agency obligations may not exceed 50 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.
  - (C) Investments in each of commercial paper, corporate notes or bonds and certificates of deposit may not exceed 25 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.
  - (D) Investments in municipal securities may not exceed 10 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.
  - (E) Subject to paragraph (b)(3)(i)(G) of this section, investments in money market mutual funds comprising only U.S. government securities shall not be subject to a concentration limit.
  - (F) Subject to paragraph (b)(3)(i)(G) of this section, investments in money market mutual funds, other than those described in paragraph (b)(3)(i)(E) of this section, may not exceed 50 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.
  - (G) Investments in money market mutual funds comprising less than \$1 billion in assets and/or which have a management company comprising less than \$25 billion in assets, may not exceed 10 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.
- (ii) *Issuer-based concentration limits for direct investments.* (A) Securities of any single issuer of U.S. agency obligations held by a futures commission merchant or derivatives clearing organization may not exceed 25 percent of total assets held in segregation by the futures commission merchant or derivatives clearing organization.
- (B) Securities of any single issuer of municipal securities, certificates of deposit, commercial paper, or corporate notes or bonds held by a futures commission merchant or derivatives clearing organization may not exceed 5 percent of total assets held in segregation by the futures commission merchant or derivatives clearing organization.
  - (C) Interests in any single family of money market mutual funds described in paragraph (b)(3)(i)(F) of this section may not exceed 25 percent of total assets held in segregation by the futures commission merchant or derivatives clearing organization.
  - (D) Interests in any individual money market mutual fund described in paragraph (b)(3)(i)(F) of this section may not exceed 10 percent of total assets held in segregation by the futures commission merchant or derivatives clearing organization.
  - (E) For purposes of determining compliance with the issuer-based concentration limits set forth in this section, securities issued by entities that are affiliated, as defined in paragraph (b)(5) of this section, shall be aggregated and deemed the securities of a single issuer. An interest in a permitted money market mutual fund is not deemed to be a security issued by its sponsoring entity.

(iii) *Concentration limits for agreements to repurchase* —(A) *Repurchase agreements*. For purposes of determining compliance with the asset-based and issuer-based concentration limits set forth in this section, securities sold by a futures commission merchant or derivatives clearing organization subject to agreements to repurchase shall be combined with securities held by the futures commission merchant or derivatives clearing organization as direct investments.

(B) *Reverse repurchase agreements*. For purposes of determining compliance with the asset-based and issuer-based concentration limits set forth in this section, securities purchased by a futures commission merchant or derivatives clearing organization subject to agreements to resell shall be combined with securities held by the futures commission merchant or derivatives clearing organization as direct investments.

(iv) *Treatment of customer-owned securities*. For purposes of determining compliance with the asset-based and issuer-based concentration limits set forth in this section, securities owned by the customers of a futures commission merchant and posted as margin collateral are not included in total assets held in segregation by the futures commission merchant, and securities posted by a futures commission merchant with a derivatives clearing organization are not included in total assets held in segregation by the derivatives clearing organization.

(v) *Counterparty concentration limits*. Securities purchased by a futures commission merchant or derivatives clearing organization from a single counterparty, or from one or more counterparties under common ownership or control, subject to an agreement to resell the securities to [that] the counterparty or counterparties, shall not exceed 25 percent of total assets held in segregation or under §30.7 of this chapter by the futures commission merchant or derivatives clearing organization.

(4) *Time-to-maturity*. (i) Except for investments in money market mutual funds, the dollar-weighted average of the time-to-maturity of the portfolio, as that average is computed pursuant to §270.2a-7 of this title, may not exceed 24 months.

(ii) For purposes of determining the time-to-maturity of the portfolio, an instrument that is set forth in paragraphs (a)(1)(i) through (vii) of this section may be treated as having a one-day time-to-maturity if the following terms and conditions are satisfied:

(A) The instrument is deposited solely on an overnight basis with a derivatives clearing organization pursuant to the terms and conditions of a collateral management program that has become effective in accordance with §39.4 of this chapter;

(B) The instrument is one that the futures commission merchant owns or has an unqualified right to pledge, is not subject to any lien, and is deposited by the futures commission merchant into a segregated account at a derivatives clearing organization;

(C) The derivatives clearing organization prices the instrument each day based on the current mark-to-market value; and

(D) The derivatives clearing organization reduces the assigned value of the instrument each day by a haircut of at least 2 percent.

(5) *Investments in instruments issued by affiliates*. (i) A futures commission merchant shall not invest customer funds in obligations of an entity affiliated with the futures commission merchant, and a derivatives clearing organization shall not invest customer funds in obligations of an entity affiliated with the derivatives clearing organization. An affiliate includes parent companies, including all entities through the ultimate holding company, subsidiaries to the lowest level, and companies under common ownership of such parent company or affiliates.

(ii) A futures commission merchant or derivatives clearing organization may invest customer funds in a fund affiliated with that futures commission merchant or derivatives clearing organization.

[(6) *Recordkeeping*. A futures commission merchant and a derivatives clearing organization shall prepare and maintain a record that will show for each business day with respect to each type of investment made pursuant to this section, the following information:

- (i) The type of instruments in which customer funds have been invested;
- (ii) The original cost of the instruments; and
- (iii) The current market value of the instruments.]

(c) *Money market mutual funds*. The following provisions will apply to the investment of customer funds in money market mutual funds (the fund).

(1) The fund must be an investment company that is registered under the Investment Company Act of 1940 with the Securities and Exchange Commission and that holds itself out to investors as a money market fund, in accordance with §270.2a–7 of this title.

(2) The fund must be sponsored by a federally-regulated financial institution, a bank as defined in section 3(a)(6) of the Securities Exchange Act of 1934, an investment adviser registered under the Investment Advisers Act of 1940, or a domestic branch of a foreign bank insured by the Federal Deposit Insurance Corporation.

(3) A futures commission merchant or derivatives clearing organization shall maintain the confirmation relating to the purchase in its records in accordance with §1.31 and note the ownership of fund shares (by book-entry or otherwise) in a custody account of the futures commission merchant or derivatives clearing organization in accordance with §1.26. The futures commission merchant or the derivatives clearing organization shall obtain the acknowledgment letter required by §1.26 from an entity that has substantial control over the fund shares purchased with customer [segregated] funds and has the knowledge and authority to facilitate redemption and payment or transfer of the customer [segregated] funds. Such entity may include the fund sponsor or depository acting as custodian for fund shares.

(4) The net asset value of the fund must be computed by 9 a.m. of the business day following each business day and made available to the futures commission merchant or derivatives clearing organization by that time.

(5)(i) General requirement for redemption of interests. A fund shall be legally obligated to redeem an interest and to make payment in satisfaction thereof by the business day following a redemption request, and the futures commission merchant or derivatives clearing organization shall retain documentation demonstrating compliance with this requirement.

(ii) Exception. A fund may provide for the postponement of redemption and payment due to any of the following circumstances:

(A) For any period during which there is a non-routine closure of the Fedwire or applicable Federal Reserve Banks;

(B) For any period:

(1) During which the New York Stock Exchange is closed other than customary week-end and holiday closings; or

(2) During which trading on the New York Stock Exchange is restricted;

(C) For any period during which an emergency exists as a result of which:

(1) Disposal by the company of securities owned by it is not reasonably practicable; or

(2) It is not reasonably practicable for such company fairly to determine the value of its net assets;

(D) For any period as the Securities and Exchange Commission may by order permit for the protection of security holders of the company;

(E) For any period during which the Securities and Exchange Commission has, by rule or regulation, deemed that:

(1) Trading shall be restricted; or

(2) An emergency exists; or

(F) For any period during which each of the conditions of §270.22e-3(a)(1) through (3) of this title are met.

(6) The agreement pursuant to which the futures commission merchant or derivatives clearing organization has acquired and is holding its interest in a fund must contain no provision that would prevent the pledging or transferring of shares.

(7) The appendix to this section sets forth language that will satisfy the requirements of paragraph (c)(5) of this section.

(d) *Repurchase and reverse repurchase agreements.* A futures commission merchant or derivatives clearing organization may buy and sell the permitted investments listed in paragraphs (a)(1)(i) through (vii) of this section pursuant to agreements for resale or repurchase of the securities (agreements to repurchase or resell), provided the agreements to repurchase or resell conform to the following requirements:

(1) The securities are specifically identified by coupon rate, par amount, market value, maturity date, and CUSIP or ISIN number.

(2) Permitted counterparties are limited to a bank as defined in section 3(a)(6) of the Securities Exchange Act of 1934, a domestic branch of a foreign bank insured by the Federal Deposit Insurance Corporation, a securities broker or dealer, or a government securities broker or government securities dealer registered with the Securities and Exchange Commission or which has filed notice pursuant to section 15C(a) of the Government Securities Act of 1986.

(3) A futures commission merchant or derivatives clearing organization shall not enter into an agreement to repurchase or resell with a counterparty that is an affiliate of the futures commission merchant or derivatives clearing organization, respectively. An affiliate includes parent companies, including all entities through the ultimate holding company, subsidiaries to the lowest level, and companies under common ownership of such parent company or affiliates.

(4) The transaction is executed in compliance with the concentration limit requirements applicable to the securities transferred to the customer segregated custodial account in connection with the agreements to repurchase referred to in paragraphs (b)(3)(iii)(A) and (B) of this section.

(5) The transaction is made pursuant to a written agreement signed by the parties to the agreement, which is consistent with the conditions set forth in paragraphs (d)(1) through (13) of this section and which states that the parties thereto intend the transaction to be treated as a purchase and sale of securities.

(6) The term of the agreement is no more than one business day, or reversal of the transaction is possible on demand.

(7) Securities transferred to the futures commission merchant or derivatives clearing organization under the agreement are held in a safekeeping account with a bank as referred to in paragraph (d)(2) of this section, a Federal Reserve Bank, a derivatives clearing organization, or the Depository Trust Company in an account that complies with the requirements of §1.26.

(8) The futures commission merchant or the derivatives clearing organization may not use securities received under the agreement in another similar transaction and may not otherwise hypothecate or pledge such securities, except securities may be pledged on behalf of customers at another futures commission merchant or derivatives clearing organization. Substitution of securities is allowed, *provided, however,* that:

(i) The qualifying securities being substituted and original securities are specifically identified by date of substitution, market values substituted, coupon rates, par amounts, maturity dates and CUSIP or ISIN numbers;

(ii) Substitution is made on a "delivery versus delivery" basis; and

(iii) The market value of the substituted securities is at least equal to that of the original securities.

(9) The transfer of securities to the customer segregated custodial account is made on a delivery versus payment basis in immediately available funds. The transfer of funds to the customer segregated cash account is made on a payment versus delivery basis. The transfer is not recognized as accomplished until the funds and/or securities are actually received by the custodian of the futures commission merchant's or derivatives clearing organization's customer funds or securities purchased on behalf of customers. The transfer or credit of securities covered by the agreement to the futures commission merchant's or derivatives clearing organization's customer segregated custodial account is made simultaneously with the disbursement of funds from the futures commission merchant's or derivatives clearing organization's customer segregated cash account at the custodian bank. On the sale or resale of securities, the futures commission merchant's or derivatives clearing organization's customer segregated cash account at the custodian bank must receive same-day funds credited to such segregated account simultaneously with the delivery or transfer of securities from the customer segregated custodial account.

(10) A written confirmation to the futures commission merchant or derivatives clearing organization specifying the terms of the agreement and a safekeeping receipt are issued immediately upon entering into the transaction and a confirmation to the futures commission merchant or derivatives clearing organization is issued once the transaction is reversed.

(11) The transactions effecting the agreement are recorded in the record required to be maintained under §1.27 of investments of customer funds, and the securities subject to such transactions are specifically identified in such record as described in paragraph (d)(1) of this

section and further identified in such record as being subject to repurchase and reverse repurchase agreements.

(12) An actual transfer of securities to the customer segregated custodial account by book entry is made consistent with Federal or State commercial law, as applicable. At all times, securities received subject to an agreement are reflected as "customer property."

(13) The agreement makes clear that, in the event of the bankruptcy of the futures commission merchant or derivatives clearing organization, any securities purchased with customer funds that are subject to an agreement may be immediately transferred. The agreement also makes clear that, in the event of a futures commission merchant or derivatives clearing organization bankruptcy, the counterparty has no right to compel liquidation of securities subject to an agreement or to make a priority claim for the difference between current market value of the securities and the price agreed upon for resale of the securities to the counterparty, if the former exceeds the latter.

(e) *Deposit of firm-owned securities into segregation.* A futures commission merchant [shall not be prohibited from directly depositing] may deposit unencumbered securities of the type specified in this section, which it owns for its own account, into a [segregated safekeeping account or from transferring any such securities from a segregated account to its own account, up to the extent of its residual financial interest in customers' segregated funds; provided, however, that such investments] customer account. A futures commission merchant must include such securities, transfers of securities, and disposition of proceeds from the sale or maturity of such securities [are recorded] in the record of investments required to be maintained by §1.27. All such securities may be segregated in safekeeping only with a bank, trust company, derivatives clearing organization, or other registered futures commission merchant[. Furthermore, for] in accordance with the provisions of §1.20 part. For purposes of this section and §§[1.25, 1.26,] 1.27, 1.28, [and 1.29, investments permitted by §1.25] 1.29, and 1.32, securities of the type specified by this section that are owned by the futures commission merchant and deposited into [such a segregated] a customer account shall be considered customer funds until such investments are withdrawn from segregation in accordance with the provisions of §1.23. Investments permitted by §1.25 that are owned by the futures commission merchant and deposited into a futures customer account pursuant to §1.26 shall be considered futures customer funds until such investments are withdrawn from segregation in accordance with §1.23. Investments permitted by §1.25 that are owned by the futures commission merchant and deposited into a Cleared Swaps Customer Account, as defined in §22.1 of this chapter, shall be considered Cleared Swaps Customer Collateral, as defined in §22.1 of this chapter, until such investments are withdrawn from segregation in accordance with §22.17 of this chapter.

Appendix to §1.25 - Money Market Mutual Fund Prospectus Provisions Acceptable for Compliance With Section 1.25(c)(5)

Upon receipt of a proper redemption request submitted in a timely manner and otherwise in accordance with the redemption procedures set forth in this prospectus, the [Name of Fund] will redeem the requested shares and make a payment to you in satisfaction thereof no later than the business day following the redemption request. The [Name of Fund] may postpone and/or suspend redemption and payment beyond one business day only as follows:

- a. For any period during which there is a non-routine closure of the Fedwire or applicable Federal Reserve Banks;
- b. For any period (1) during which the New York Stock Exchange is closed other than customary week-end and holiday closings or (2) during which trading on the New York Stock Exchange is restricted;

- c. For any period during which an emergency exists as a result of which (1) disposal of securities owned by the [Name of Fund] is not reasonably practicable or (2) it is not reasonably practicable for the [Name of Fund] to fairly determine the net asset value of shares of the [Name of Fund];
- d. For any period during which the Securities and Exchange Commission has, by rule or regulation, deemed that (1) trading shall be restricted or (2) an emergency exists;
- e. For any period that the Securities and Exchange Commission, may by order permit for your protection; or
- f. For any period during which the [Name of Fund,] as part of a necessary liquidation of the fund, has properly postponed and/or suspended redemption of shares and payment in accordance with federal securities laws.

**[529] 530. Compliance with Commission Regulation 1.26  
- Deposit of Instruments Purchased with Futures  
Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.26 that violates Commission Regulation 1.26 shall be deemed to have violated this Rule [529] 530. Commission Regulation 1.26 is set forth below and incorporated into this Rule [529] 530.

Commission Regulation 1.26 - Deposit of instruments purchased with futures customer funds.

[(a) Each futures commission merchant who invests customer funds in instruments described in §1.25 shall separately account for such instruments and segregate such instruments as belonging to such commodity or option customers. Such instruments, when deposited with a bank, trust company, clearing organization or another futures commission merchant, shall be deposited under an account name which clearly shows that they belong to commodity or option customers and are segregated as required by the Act and this part. Each futures commission merchant upon opening such an account shall obtain and retain in its files an acknowledgment from such bank, trust company, clearing organization or other futures commission merchant that it was informed that the instruments belong to commodity or option customers and are being held in accordance with the provisions of the Act and this part. *Provided, however,* that an acknowledgment need not be obtained from a clearing organization that has adopted and submitted to the Commission rules that provide for the segregation as customer funds, in accordance with all relevant provisions of the Act and the rules and orders promulgated thereunder, of all funds held on behalf of customers and all instruments purchased with customer funds. Such acknowledgment shall be retained in accordance with §1.31. Such bank, trust company, clearing organization or other futures commission merchant shall allow inspection of such obligations at any reasonable time by representatives of the Commission.

(b) Each clearing organization which invests money belonging or accruing to commodity or option customers of its clearing members in instruments described in §1.25 shall separately account for such instruments and segregate such instruments as belonging to such commodity or option customers. Such instruments, when deposited with a bank or trust company, shall be deposited under an account name which will clearly show that they belong to commodity or option customers and are segregated as required by the Act and this part. Each clearing organization upon opening such an account shall obtain and retain in its files a written acknowledgment from such bank or trust company that it was informed that the instruments belong to commodity or option customers of clearing members and are being held in accordance with the provisions of

the Act and this part. Such acknowledgment shall be retained in accordance with §1.31. Such bank or trust company shall allow inspection of such instruments at any reasonable time by representatives of the Commission.]

(a) Each futures commission merchant who invests futures customer funds in instruments described in §1.25, except for investments in money market mutual funds, shall separately account for such instruments as futures customer funds and segregate such instruments as funds belonging to such futures customers in accordance with the requirements of §1.20. Each derivatives clearing organization which invests money belonging or accruing to futures customers of its clearing members in instruments described in §1.25, except for investments in money market mutual funds, shall separately account for such instruments as customer funds and segregate such instruments as customer funds belonging to such futures customers in accordance with §1.20.

(b) Each futures commission merchant or derivatives clearing organization which invests futures customer funds in money market mutual funds, as permitted by §1.25, shall separately account for such funds and segregate such funds as belonging to such futures customers. Such funds shall be deposited under an account name that clearly shows that they belong to futures customers and are segregated as required by sections 4d(a) and 4d(b) of the Act and by this part. Each futures commission merchant or derivatives clearing organization, upon opening such an account, shall obtain and maintain readily accessible in its files in accordance with §1.31, for as long as the account remains open, and thereafter for the period provided in §1.31, a written acknowledgment and shall file such acknowledgment in accordance with the requirements of §1.20. In the event such funds are held directly with the money market mutual fund or its affiliate, the written acknowledgment shall be in the form as set out in Appendix A or B to this section. In the event such funds are held with a depository, the written acknowledgment shall be in the form as set out in Appendix A or B to §1.20. In either case, the written acknowledgment shall be obtained, provided to the Commission and designated self-regulatory organizations, and retained as required under §1.20.

APPENDIX A TO §1.26—FUTURES COMMISSION MERCHANT ACKNOWLEDGMENT LETTER FOR CFTC REGULATION 1.26 CUSTOMER SEGREGATED MONEY MARKET MUTUAL FUND ACCOUNT

[Date]

Name and Address of Money Market Mutual Fund

We propose to invest funds held by [Name of Futures Commission Merchant] ("we" or "our") on behalf of our customers in shares of [Name of Money Market Mutual Fund] ("you" or "your") under account(s) entitled (or shares issued to):

[Name of Futures Commission Merchant] [if applicable, add "FCM Customer Omnibus Account"] CFTC Regulation 1.26 Customer Segregated Money Market Mutual Fund Account under Sections 4d(a) and 4d(b) of the Commodity Exchange Act [and, if applicable, ", Abbreviated as [short title reflected in the depository's electronic system]]"

Account Number(s): []

(collectively, the "Account(s)").

You acknowledge that we are holding these funds, including any shares issued and amounts accruing in connection therewith (collectively, the "Shares"), for the benefit of customers who trade commodities, options, swaps and other products ("Commodity Customers"), as required by Commodity Futures Trading Commission ("CFTC") Regulation 1.26, as amended; that the Shares held by you, hereafter deposited in the Account(s) or accruing to the credit of the Account(s), will be separately accounted for and segregated on your books from our own funds and from any other funds or accounts held by us in accordance with the provisions of the Commodity Exchange Act, as amended (the "Act"), and part 1 of the CFTC's regulations,

as amended; and that the Shares must otherwise be treated in accordance with the provisions of Section 4d of the Act and CFTC regulations thereunder.

Furthermore, you acknowledge and agree that such Shares may not be used by you or by us to secure or guarantee any obligations that we might owe to you, and they may not be used by us to secure or obtain credit from you. You further acknowledge and agree that the Shares in the Account(s) shall not be subject to any right of offset or lien for or on account of any indebtedness, obligations or liabilities we may now or in the future have owing to you.

In addition, you agree that the Account(s) may be examined at any reasonable time by the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent or employee of our designated self-regulatory organization ("DSRO"), [Name of DSRO], and this letter constitutes the authorization and direction of the undersigned on our behalf to permit any such examination to take place without further notice to or consent from us.

You agree to reply promptly and directly to any request for confirmation of account balances or provision of any other account information regarding or related to the Account(s) from the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent, or employee of [Name of DSRO], acting in its capacity as our DSRO, and this letter constitutes the authorization and direction of the undersigned on our behalf to release the requested information without further notice to or consent from us.

You further acknowledge and agree that, pursuant to the authorization granted by us to you previously or herein, you have provided, or will provide following the opening of the Account(s), the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor division, or such director's designees, with technological connectivity, which may include provision of hardware, software, and related technology and protocol support, to facilitate direct, read-only electronic access to transaction and account balance information for the Account(s). This letter constitutes the authorization and direction of the undersigned on our behalf for you to establish this connectivity and access if not previously established, without further notice to or consent from us.

The parties agree that all actions on your part to respond to the above information and access requests will be made in accordance with, and subject to, such usual and customary authorization verification and authentication policies and procedures as may be employed by you to verify the authority of, and authenticate the identity of, the individual making any such information or access request, in order to provide for the secure transmission and delivery of the requested information or access to the appropriate recipient(s).

We will not hold you responsible for acting pursuant to any information or access request from the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent, or employee of [Name of DSRO], acting in its capacity as our DSRO, upon which you have relied after having taken measures in accordance with your applicable policies and procedures to assure that such request was provided to you by an individual authorized to make such a request.

In the event we become subject to either a voluntary or involuntary petition for relief under the U.S. Bankruptcy Code, we acknowledge that you will have no obligation to release the Shares held in the Account(s), except upon instruction of the Trustee in Bankruptcy or pursuant to the Order of the respective U.S. Bankruptcy Court.

Notwithstanding anything in the foregoing to the contrary, nothing contained herein shall be construed as limiting your right to assert any right of offset or lien on assets that are not Shares maintained in the Account(s), or to impose such charges against us or any proprietary account maintained by us with you. Further, it is understood that amounts represented by checks, drafts or other items shall not be considered to be part of the Account(s) until finally collected. Accordingly, checks, drafts and other items credited to the Account(s) and subsequently dishonored or otherwise returned to you or reversed, for any reason and any claims relating thereto, including but not limited to claims of alteration or forgery, may be charged back to the Account(s), and we shall be responsible to you as a general endorser of all such items whether or not actually so endorsed.

You may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry, provided that, in the ordinary course of your business as a depository, you have no notice of or actual knowledge of a potential violation by us of any provision of the Act or the CFTC regulations that relates to the segregation of customer funds; and you shall not in any manner not expressly agreed to herein be responsible to us for ensuring compliance by us with such provisions of the Act and CFTC regulations; however, the aforementioned presumption does not affect any obligation you may otherwise have under the Act or CFTC regulations.

You may, and are hereby authorized to, obey the order, judgment, decree or levy of any court of competent jurisdiction or any governmental agency with jurisdiction, which order, judgment, decree or levy relates in whole or in part to the Account(s). In any event, you shall not be liable by reason of any action or omission to act pursuant to such order, judgment, decree or levy, to us or to any other person, firm, association or corporation even if thereafter any such order, decree, judgment or levy shall be reversed, modified, set aside or vacated.

We are permitted to invest customers' funds in money market mutual funds pursuant to CFTC Regulation 1.25. That rule sets forth the following conditions, among others, with respect to any investment in a money market mutual fund:

- (1) The net asset value of the fund must be computed by 9:00 a.m. of the business day following each business day and be made available to us by that time;
- (2) The fund must be legally obligated to redeem an interest in the fund and make payment in satisfaction thereof by the close of the business day following the day on which we make a redemption request except as otherwise specified in CFTC Regulation 1.25(c)(5)(ii); and,
- (3) The agreement under which we invest customers' funds must not contain any provision that would prevent us from pledging or transferring fund shares.

The terms of this letter agreement shall remain binding upon the parties, their successors and assigns, and for the avoidance of doubt, regardless of a change in the name of either party. This letter agreement supersedes and replaces any prior agreement between the parties in connection with the Account(s), including but not limited to any prior acknowledgment letter agreement, to the extent that such prior agreement is inconsistent with the terms hereof. In the event of any conflict between this letter agreement and any other agreement between the parties in connection with the Account(s), this letter agreement shall govern with respect to matters specific to Section 4d of the Act and the CFTC's regulations thereunder, as amended.

This letter agreement shall be governed by and construed in accordance with the laws of [Insert governing law] without regard to the principles of choice of law.

Please acknowledge that you agree to abide by the requirements and conditions set forth above by signing and returning to us the enclosed copy of this letter agreement, and that you further agree to provide a copy of this fully executed letter agreement directly to the CFTC (via electronic means in a format and manner determined by the CFTC) and to [Name of DSRO], acting in its capacity as our DSRO, in accordance with CFTC Regulation 1.20. We hereby authorize and direct you to provide such copies without further notice to or consent from us, no later than three business days after opening the Account(s) or revising this letter agreement, as applicable.

[Name of Futures Commission Merchant]

By:

Print Name:

Title:

ACKNOWLEDGED AND AGREED:

[Name of Money Market Mutual Fund]

By:

Print Name:

Title:

Contact Information: [Insert phone number and email address]

Date:

**APPENDIX B TO §1.26—DERIVATIVES CLEARING ORGANIZATION ACKNOWLEDGMENT LETTER FOR CFTC REGULATION 1.26 CUSTOMER SEGREGATED MONEY MARKET MUTUAL FUND ACCOUNT**

[Date]

[Name and Address of Money Market Mutual Fund]

We propose to invest funds held by [Name of Derivatives Clearing Organization] ("we" or "our") on behalf of customers in shares of [Name of Money Market Mutual Fund] ("you" or "your") under account(s) entitled (or shares issued to):

[Name of Derivatives Clearing Organization] Futures Customer Omnibus Account, CFTC Regulation 1.26 Customer Segregated Money Market Mutual Fund Account under Sections 4d(a) and 4d(b) of the Commodity Exchange Act [and, if applicable, " Abbreviated as [short title reflected in the depository's electronic system]" ]

Account Number(s): [ ]

(collectively, the "Account(s)").

You acknowledge that we are holding these funds, including any shares issued and amounts accruing in connection therewith (collectively, the "Shares"), for the benefit of customers who trade commodities, options, swaps and other products, as required by Commodity Futures Trading Commission ("CFTC") Regulation 1.26, as amended; that the Shares held by you, hereafter deposited in the Account(s) or accruing to the credit of the Account(s), will be separately accounted for and segregated on your books from our own funds and from any other funds or accounts held by us in accordance with the provisions of the Commodity Exchange Act, as amended (the "Act"), and part 1 of the CFTC's regulations, as amended; and that the Shares must otherwise be treated in accordance with the provisions of Section 4d of the Act and CFTC regulations thereunder.

Furthermore, you acknowledge and agree that such Shares may not be used by you or by us to secure or guarantee any obligations that we might owe to you, and they may not be used by us to secure or obtain credit from you. You further acknowledge and agree that the Shares in the Account(s) shall not be subject to any right of offset or lien for or on account of any indebtedness, obligations or liabilities we may now or in the future have owing to you.

You agree to reply promptly and directly to any request for confirmation of account balances or provision of any other account information regarding or related to the Account(s) from the director of the Division of Clearing and Risk of the CFTC or the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor divisions, or such directors' designees, and this letter constitutes the authorization and direction of the undersigned on our behalf to release the requested information without further notice to or consent from us.

The parties agree that all actions on your part to respond to the above information requests will be made in accordance with, and subject to, such usual and customary authorization verification and authentication policies and procedures as may be employed by you to verify the authority of, and authenticate the identity of, the individual making any such information request, in order to provide for the secure transmission and delivery of the requested information to the appropriate recipient(s).

We will not hold you responsible for acting pursuant to any information request from the director of the Division of Clearing and Risk of the CFTC or the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor divisions, or such directors' designees, upon which you have relied after having taken measures in accordance with your applicable policies and procedures to assure that such request was provided to you by an individual authorized to make such a request.

In the event that we or any of our futures commission merchant clearing members become(s) subject to either a voluntary or involuntary petition for relief under the U.S. Bankruptcy Code, we acknowledge that you will have no obligation to release the Shares held in the Account(s), except upon instruction of the Trustee in Bankruptcy or pursuant to the Order of the respective U.S. Bankruptcy Court.

Notwithstanding anything in the foregoing to the contrary, nothing contained herein shall be construed as limiting your right to assert any right of offset or lien on assets that are not Shares maintained in the Account(s), or to impose such charges against us or any proprietary account maintained by us with you. Further, it is understood that amounts represented by checks, drafts or other items shall not be considered to be part of the Account(s) until finally collected. Accordingly, checks, drafts and other items credited to the Account(s) and subsequently dishonored or otherwise returned to you, or reversed, for any reason and any claims relating thereto, including but not limited to claims of alteration or forgery, may be charged back to the Account(s), and we shall be responsible to you as a general endorser of all such items whether or not actually so endorsed.

You may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry, provided that, in the ordinary course of your business as a depository, you have no notice of or actual knowledge of a potential violation by us of any provision of the Act or the CFTC regulations that relates to the segregation of customer funds; and you shall not in any manner not expressly agreed to herein be responsible to us for ensuring compliance by us with such provisions of the Act and CFTC regulations; however, the aforementioned presumption does not affect any obligation you may otherwise have under the Act or CFTC regulations.

You may, and are hereby authorized to, obey the order, judgment, decree or levy of any court of competent jurisdiction or any governmental agency with jurisdiction, which order, judgment, decree or levy relates in whole or in part to the Account(s). In any event, you shall not be liable by reason of any action or omission to act pursuant to any such order, judgment, decree or levy, to us or to any other person, firm, association or corporation even if thereafter any such order, decree, judgment or levy shall be reversed, modified, set aside or vacated.

We are permitted to invest customers' funds in money market mutual funds pursuant to CFTC Regulation 1.25. That rule sets forth the following conditions, among others, with respect to any investment in a money market mutual fund:

(1) The net asset value of the fund must be computed by 9:00 a.m. of the business day following each business day and be made available to us by that time;

(2) The fund must be legally obligated to redeem an interest in the fund and make payment in satisfaction thereof by the close of the business day following the day on which we make a redemption request except as otherwise specified in CFTC Regulation 1.25(c)(5)(ii); and,

(3) The agreement under which we invest customers' funds must not contain any provision that would prevent us from pledging or transferring fund shares.

The terms of this letter agreement shall remain binding upon the parties, their successors and assigns, and for the avoidance of doubt, regardless of a change in the name of either party. This letter agreement supersedes and replaces any prior agreement between the parties in connection with the Account(s), including but not limited to any prior acknowledgment letter agreement, to the extent that such prior agreement is inconsistent with the terms hereof. In the event of any conflict between this letter agreement and any other agreement between the parties in connection with the Account(s), this letter agreement shall govern with respect to matters specific to Section 4d of the Act and the CFTC's regulations thereunder, as amended.

This letter agreement shall be governed by and construed in accordance with the laws of [Insert governing law] without regard to the principles of choice of law.

Please acknowledge that you agree to abide by the requirements and conditions set forth above by signing and returning to us the enclosed copy of this letter agreement, and you further agree to provide a copy of this fully executed letter agreement directly to the CFTC (via electronic means in a format and manner determined by the CFTC) in accordance with CFTC Regulation 1.20. We hereby authorize and direct you to provide such copies without further notice to or consent from us, no later than three business days after opening the Account(s) or revising this letter agreement, as applicable.

[Name of Derivatives Clearing Organization]

By:

Print Name:

Title:

ACKNOWLEDGED AND AGREED:

[Name of Money Market Mutual Fund]

By:

Print Name:

Title:

Contact Information: [Insert phone number and email address]

Date:

**[530] 531. Compliance with Commission Regulation 1.27  
- Record of Investments**

Any Trading Privilege Holder subject to Commission Regulation 1.27 that violates Commission Regulation 1.27 shall be deemed to have violated this Rule [530] 531. Commission Regulation 1.27 is set forth below and incorporated into this Rule [530] 531.

\* \* \* \* \*

**[531] 532. Compliance with Commission Regulation 1.28  
- Appraisal of Instruments Purchased with Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.28 that violates Commission Regulation 1.28 shall be deemed to have violated this Rule [531] 532. Commission Regulation 1.28 is set forth below and incorporated into this Rule [531] 532.

\* \* \* \* \*

**[532] 533. Compliance with Commission Regulation 1.29  
- [Increment of Interest] Gains and Losses Resulting  
from Investment of Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.29 that violates Commission Regulation 1.29 shall be deemed to have violated this Rule [532] 533. Commission Regulation 1.29 is set forth below and incorporated into this Rule [532] 533.

Commission Regulation 1.29 – [Increment of interest] Gains and losses resulting from investment of customer funds.

(a) The investment of customer funds in instruments described in §1.25 shall not prevent the futures commission merchant or derivatives clearing organization so investing such funds from receiving and retaining as its own any [increment] incremental income or interest income resulting therefrom.

(b) The futures commission merchant or derivatives clearing organization, as applicable, shall bear sole responsibility for any losses resulting from the investment of customer funds in instruments described in §1.25. No investment losses shall be borne or otherwise allocated to the customers of the futures commission merchant and, if customer funds are invested by a derivatives clearing organization in its discretion, to the futures commission merchant.

**[533] 534. Compliance with Commission Regulation 1.30  
- Loans by Futures Commission Merchants; Treatment  
of Proceeds**

Any Trading Privilege Holder subject to Commission Regulation 1.30 that violates Commission Regulation 1.30 shall be deemed to have violated this Rule [533] 534. Commission Regulation 1.30 is set forth below and incorporated into this Rule [533] 534.

Commission Regulation 1.30 - Loans by futures commission merchants; treatment of proceeds.

Nothing in [these] the regulations in this chapter shall prevent a futures commission merchant from lending its own funds to [commodity or option] customers on securities and property pledged by such [commodity or option] customers, or from repledging or selling such securities and property pursuant to specific written agreement with such [commodity or option] customers. The proceeds of such loans used to purchase, margin, guarantee, or secure the trades, contracts, or commodity options of [commodity or option] customers shall be treated and dealt with by a futures commission merchant as belonging to such [commodity or option] customers, in accordance with and subject to the provisions of [section 4d(a)(2) of] the Act and these regulations. A futures commission merchant may not loan funds on an unsecured basis to finance customers' trading, nor may a futures commission merchant loan funds to customers secured by the customer accounts of such customers.

**[534] 535. Compliance with Commission Regulation 1.31  
- Books and Records; Keeping and Inspection**

Any Trading Privilege Holder subject to Commission Regulation 1.31 that violates Commission Regulation 1.31 shall be deemed to have violated

this Rule [534] 535. Commission Regulation 1.31 is set forth below and incorporated into this Rule [534] 535.

\* \* \* \* \*

**[535] 536. Compliance with Commission Regulation 1.32 – [Segregated Account; Daily Computation and Record]**  
**Reporting of Segregated Account Computation and Details Regarding the Holding of Futures Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.32 that violates Commission Regulation 1.32 shall be deemed to have violated this Rule [535] 536. Commission Regulation 1.32 is set forth below and incorporated into this Rule [535] 536.

[Commission Regulation 1.32 - Segregated account; daily computation and record.

(a) Each futures commission merchant must compute as of the close of each business day, on a currency-by-currency basis:

(1) The total amount of customer funds on deposit in segregated accounts on behalf of commodity and option customers;

(2) the amount of such customer funds required by the Act and these regulations to be on deposit in segregated accounts on behalf of such commodity and option customers; and

(3) the amount of the futures commission merchant's residual interest in such customer funds.

(b) In computing the amount of funds required to be in segregated accounts, a futures commission merchant may offset any net deficit in a particular customer's account against the current market value of readily marketable securities, less applicable percentage deductions (*i.e.*, "securities haircuts") as set forth in Rule 15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 241.15c3-1(c)(2)(vi)), held for the same customer's account. The futures commission merchant must maintain a security interest in the securities, including a written authorization to liquidate the securities at the futures commission merchant's discretion, and must segregate the securities in a safekeeping account with a bank, trust company, clearing organization of a contract market, or another futures commission merchant. For purposes of this section, a security will be considered readily marketable if it is traded on a "ready market" as defined in Rule 15c3-1(c)(11)(i) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(11)(i)).

(c) The daily computations required by this section must be completed by the futures commission merchant prior to noon on the next business day and must be kept, together with all supporting data, in accordance with the requirements of §1.31.]

Commission Regulation 1.32 – Reporting of segregated account computation and details regarding the holding of futures customer funds

(a) Each futures commission merchant must compute as of the close of each business day, on a currency-by-currency basis:

(1) The total amount of futures customer funds on deposit in segregated accounts on behalf of futures customers;

(2) The amount of such futures customer funds required by the Act and these regulations to be on deposit in segregated accounts on behalf of such futures customers; and

(3) The amount of the futures commission merchant's residual interest in such futures customer funds.

(b) In computing the amount of futures customer funds required to be in segregated accounts, a futures commission merchant may offset any net deficit in a particular futures customer's account against the current market value of readily marketable securities, less applicable deductions (i.e., "securities haircuts") as set forth in Rule 15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 241.15c3-1(c)(2)(vi)), held for the same futures customer's account. Futures commission merchants that establish and enforce written policies and procedures to assess the credit risk of commercial paper, convertible debt instruments, or nonconvertible debt instruments in accordance with Rule 240.15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vi)) may apply the lower haircut percentages specified in Rule 240.15c3-1(c)(2)(vi) for such commercial paper, convertible debt instruments and nonconvertible debt instruments. The futures commission merchant must maintain a security interest in the securities, including a written authorization to liquidate the securities at the futures commission merchant's discretion, and must segregate the securities in a safekeeping account with a bank, trust company, derivatives clearing organization, or another futures commission merchant. For purposes of this section, a security will be considered readily marketable if it is traded on a "ready market" as defined in Rule 15c3-1(c)(11)(i) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(11)(i)).

(c) Each futures commission merchant is required to document its segregation computation required by paragraph (a) of this section by preparing a Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges contained in the Form 1-FR-FCM as of the close of each business day. Nothing in this paragraph shall affect the requirement that a futures commission merchant at all times maintain sufficient money, securities and property to cover its total obligations to all futures customers, in accordance with §1.20.

(d) Each futures commission merchant is required to submit to the Commission and to the firm's designated self-regulatory organization the daily Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges required by paragraph (c) of this section by noon the following business day.

(e) Each futures commission merchant shall file the Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges required by paragraph (c) of this section in an electronic format using a form of user authentication assigned in accordance with procedures established or approved by the Commission.

(f) Each futures commission merchant is required to submit to the Commission and to the firm's designated self-regulatory organization a report listing the names of all banks, trust companies, futures commission merchants, derivatives clearing organizations, or any other depository or custodian holding futures customer funds as of the fifteenth day of the month, or the first business day thereafter, and the last business day of each month. This report must include:

(1) The name and location of each entity holding futures customer funds;

(2) The total amount of futures customer funds held by each entity listed in paragraph (f)(1) of this section; and

(3) The total amount of cash and investments that each entity listed in paragraph (f)(1) of this section holds for the futures commission merchant. The futures commission merchant must report the following investments:

- (i) Obligations of the United States and obligations fully guaranteed as to principal and interest by the United States (U.S. government securities);
  - (ii) General obligations of any State or of any political subdivision of a State (municipal securities);
  - (iii) General obligation issued by any enterprise sponsored by the United States (government sponsored enterprise securities);
  - (iv) Certificates of deposit issued by a bank;
  - (v) Commercial paper fully guaranteed as to principal and interest by the United States under the Temporary Liquidity Guarantee Program as administered by the Federal Deposit Insurance Corporation;
  - (vi) Corporate notes or bonds fully guaranteed as to principal and interest by the United States under the Temporary Liquidity Guarantee Program as administered by the Federal Deposit Insurance Corporation; and
  - (vii) Interests in money market mutual funds.
- (g) Each futures commission merchant must report the total amount of futures customer-owned securities held by the futures commission merchant as margin collateral and must list the names and locations of the depositories holding such margin collateral.
- (h) Each futures commission merchant must report the total amount of futures customer funds that have been used to purchase securities under agreements to resell the securities (reverse repurchase transactions).
- (i) Each futures commission merchant must report which, if any, of the depositories holding futures customer funds under paragraph (f)(1) of this section are affiliated with the futures commission merchant.
- (j) Each futures commission merchant shall file the detailed list of depositories required by paragraph (f) of this section by 11:59 p.m. the next business day in an electronic format using a form of user authentication assigned in accordance with procedures established or approved by the Commission.
- (k) Each futures commission merchant shall retain its daily segregation computation and the Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges required by paragraph (c) of this section, and its detailed list of depositories required by paragraph (f) of this section, together with all supporting documentation, in accordance with the requirements of §1.31.

**[536] 537. Compliance with Commission Regulation 1.36  
- Record of Securities and Property Received from  
Customers and Options Customers**

Any Trading Privilege Holder subject to Commission Regulation 1.36 that violates Commission Regulation 1.36 shall be deemed to have violated this Rule [536] 537. Commission Regulation 1.36 is set forth below and incorporated into this Rule [536] 537.

Exhibit 5

A copy of the certification submitted to the CFTC pursuant to Section 5c(c) of the Commodity Exchange Act with respect to the proposed rule change.



April 11, 2014

**Via Electronic Mail**

Ms. Melissa Jurgens  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, N.W.  
Washington, D.C. 20581

Re: CBOE Futures Exchange, LLC Rule Certification  
Submission Number CFE-2014-07

Dear Ms. Jurgens:

Pursuant to Section 5c(c)(1) of the Commodity Exchange Act, as amended ("Act"), and §40.6(a) of the regulations promulgated by the Commodity Futures Trading Commission ("CFTC" or "Commission") under the Act, CBOE Futures Exchange, LLC ("CFE" or "Exchange") hereby submits a CFE rule amendment ("Amendment") to amend CFE rules (i) to enhance the financial surveillance and financial integrity of futures commission merchants ("FCMs") that are Trading Privilege Holders ("TPHs") and (ii) to reflect the Final Rule adopted by the Commission under the caption Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations ("Customer Protection Rule").<sup>1</sup> The Amendment will become effective on April 28, 2014.

CFE is amending Rule 503A, which, in part, imposes reporting obligations on FCMs that are TPHs, to require these FCMs to file additional financial documentation with CFE relating to segregation requirements and funds in segregation for customers, net capital, and notices filed with the Commission. Requiring its FCMs that are TPHs to report additional financial documentation enhances CFE's financial surveillance of FCMs.

CFE is adding new Rule 520 to the Appendix to Chapter 5 of the CFE Rulebook to require that FCMs comply with the risk management requirements set forth in CFTC Regulation 1.11: *Risk Management Program for futures commission merchants*. CFTC Regulation 1.52(b)(2) requires that all self-regulatory organizations ("SROs") (defined as DCMs and registered futures associations in CFTC Regulation 1.52(a)(2)) adopt rules prescribing risk management requirements for FCM member registrants that are at least as stringent as the requirements contained in CFTC Regulation 1.11.

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<sup>1</sup> 78 FR 68506 (Nov. 14, 2013).

CFE is amending presently numbered Rules 519, 520, 521, 523, 525, 526, 528, 529, 532, 533, and 535 in the Appendix to Chapter 5 of the CFE Rulebook to reflect the Customer Protection Rule's changes to the respective language in CFTC Regulations 1.10, 1.12, 1.17, 1.20, 1.22, 1.23, 1.25, 1.26, 1.29, 1.30, and 1.32. Lastly, CFE is renumbering presently numbered Rule 520 and all subsequent Rules in the Appendix to accommodate the addition of new Rule 520. CFE notes that it already requires that its FCMs that are TPHs comply with all CFTC Regulations. For example, CFE Rule 604 prohibits TPHs and their Related Parties from engaging in conduct in violation of Applicable Law (which includes, among other things, the Act and CFTC regulations), and CFE Rule 505 specifically requires TPHs to comply with CFTC Regulations relating to the treatment of Customer funds and the maintenance of related books and records. CFE believes that the addition of new Rule 520 and modifications to the Rules listed above will make this requirement even more explicit in light of the Customer Protection Rule.

CFE believes that the Amendment complies with DCM Core Principle 11 (Financial Integrity of Transactions) under Section 5 of the Act. Specifically, amended Rule 503A provides CFE with additional financial information concerning FCMs that are TPHs and enhances CFE's monitoring of them. New Rule 520 increases the general financial integrity of the Exchange's FCMs that are TPHs by implementing new standards for risk management programs including policies that address, among other things, segregation risk, operational risk, and capital risk in conformance with CFTC Regulation 1.11. Amended Rules 519, 520, 521, 523, 525, 526, 528, 529, 532, 533, and 535 will be consistent with the respective, new language in the Customer Protection Rule. Lastly, the Amendment enhances the general financial integrity of CFE's FCMs that are TPHs pursuant to CFTC Regulation 38.602.

CFE believes that the impact of the Amendment will be beneficial to the public and market participants. CFE is not aware of any substantive opposing views to the Amendment. CFE hereby certifies that the Amendment complies with the Act and the regulations thereunder. CFE further certifies that CFE has posted a notice of pending certification with the Commission and a copy of this submission on CFE's Web site (<http://cfe.cboe.com/aboutcfe/rules.aspx>) concurrent with the filing of this submission with the Commission.

CFE intends to file portions of the Amendment as they may relate to security futures with the Securities and Exchange Commission pursuant to Section 19b-7 of the Securities Exchange Act of 1934.

The Amendment, marked to show additions in underlined text and deletions in [bracketed] text, consists of the following:

\* \* \* \* \*

## **CBOE Futures Exchange, LLC Rules**

### **503A. Reporting by Futures Commission Merchants and Introducing Brokers**

- (a) Each Trading Privilege Holder that is a Futures Commission Merchant or Introducing Broker shall, in a form and manner prescribed by the Exchange, concurrently file with the Exchange a copy of all Form 1-FR-FCM, Form 1-FR-IB or FOCUS Report Part II, Part IIA or Part II CSE and Part III submissions

(including any attachments or related submissions), as applicable, made by the Trading Privilege Holder.

(b) Each Trading Privilege Holder that is a Futures Commission Merchant shall, in a form and manner prescribed by the Exchange, concurrently file with the Exchange a copy of any daily Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges filed with the Commission pursuant to Commission Regulation § 1.32.

(c) Each Trading Privilege Holder that is a Futures Commission Merchant shall, in a form and manner prescribed by the Exchange, concurrently file with the Exchange a copy of any daily net capital filings submitted by the Trading Privilege Holder to its Designated Self-Regulatory Organization.

([b]d) Each Trading Privilege Holder that is a Futures Commission Merchant and (i) is not Clearing Member or (ii) is a Clearing Member that utilizes another Clearing Member for purposes of clearing Exchange Contracts shall, in a form and manner prescribed by the Exchange, provide a report to the Exchange on a daily basis which sets forth the positions, if any, in Exchange Contracts of the Trading Privilege Holder's customers held by any Clearing Member in the customer range at the Clearing Corporation.

(e) Each Trading Privilege Holder that is a Futures Commission Merchant shall, in a form and manner prescribed by the Exchange, concurrently file with the Exchange a copy of any notice that is filed with the Commission pursuant to Commission Regulation § 1.23.

\* \* \* \* \*

### **519. Compliance with Commission Regulation 1.10 – Financial Reports of Futures Commission Merchants and Introducing Brokers**

Any Trading Privilege Holder subject to Commission Regulation 1.10 that violates Commission Regulation 1.10 shall be deemed to have violated this Rule 519. Commission Regulation 1.10 is set forth below and incorporated into this Rule 519.

Commission Regulation 1.10 - Financial reports of futures commission merchants and introducing brokers.

(a) *Application for registration.* (1) Except as otherwise provided, a futures commission merchant or an applicant for registration as a futures commission merchant, in order to satisfy any requirement in this part that it file a Form 1-FR, must file a Form 1-FR-FCM, and any reference in this part to Form 1-FR with respect to a futures commission merchant or applicant therefor shall be deemed to be a reference to Form 1-FR-FCM. Except as otherwise provided, an introducing broker or an applicant for registration as an introducing broker, in order to satisfy any requirement in this part that it file a Form 1-FR, must file a Form 1-FR-IB, and any reference in this part to Form 1-FR with

respect to an introducing broker or applicant therefor shall be deemed to be a reference to Form 1-FR-IB.

(2) (i) (A) Except as provided in paragraphs (a)(3) and (h) of this section, each person who files an application for registration as a futures commission merchant and who is not so registered at the time of such filing, must, concurrently with the filing of such application, file either:

(1) A Form 1-FR-FCM certified by an independent public accountant in accordance with §1.16 as of a date not more than 45 days prior to the date on which such report is filed; or

(2) A Form 1-FR-FCM as of a date not more than 17 business days prior to the date on which such report is filed and a Form 1-FR-FCM certified by an independent public accountant in accordance with §1.16 as of a date not more than one year prior to the date on which such report is filed.

(B) Each such person must include with such financial report a statement describing the source of his current assets and representing that his capital has been contributed for the purpose of operating his business and will continue to be used for such purpose.

(ii) (A) Except as provided in paragraphs (a)(3) and (h) of this section, each person who files an application for registration as an introducing broker and who is not so registered at the time of such filing, must, concurrently with the filing of such application, file either:

(1) A Form 1-FR-IB certified by an independent public accountant in accordance with §1.16 as of a date not more than 45 days prior to the date on which such report is filed;

(2) A Form 1-FR-IB as of a date not more than 17 business days prior to the date on which such report is filed and a Form 1-FR-IB certified by an independent public accountant in accordance with §1.16 as of a date not more than one year prior to the date on which such report is filed;

(3) A Form 1-FR-IB as of a date not more than 17 business days prior to the date on which such report is filed, *Provided, however,* that such applicant shall be subject to a review by the applicant's designated self-regulatory organization within six months of registration; or

(4) A guarantee agreement.

(B) Each person filing in accordance with paragraphs (a)(2)(ii)(A) (1), (2) or (3) of this section must include with such financial report a statement describing the source of his current assets and representing that his capital has been contributed for the purpose of operating his business and will continue to be used for such purpose.

(3)(i) The provisions of paragraph (a)(2) of this section do not apply to any person succeeding to and continuing the business of another futures commission merchant. Each such person who files an application for registration as a futures commission merchant and who is not so registered in that capacity at the time of such filing must file a Form 1-FR-FCM as of the first month end following the date on which his registration is approved. Such report must be filed with the National Futures Association, the Commission and the designated self-regulatory organization, if any, not more than 17 business days after the date for which the report is made.

(ii) The provisions of paragraph (a)(2) of this section do not apply to any person succeeding to and continuing the business of another introducing broker.

(A) Each such person who succeeds to and continues the business of an introducing broker which was not operating pursuant to a guarantee agreement, or which was operating pursuant to a guarantee agreement and was also a securities broker or dealer at the time of succession, who files an application for registration as an introducing broker, and who is not so registered in that capacity at the time of such filing, must file with the National Futures Association either a guarantee agreement with his application for registration or a Form 1-FR-IB as of the first month end following the date on which his registration is approved. Such Form 1-FR-IB must be filed not more than 17 business days after the date for which the report is made.

(B) Each such person who succeeds to and continues the business of an introducing broker which was operating pursuant to a guarantee agreement and which was not also a securities broker or dealer at the time of succession, who files an application for registration as an introducing broker, and who is not so registered in that capacity at the time of such filing, must file with the National Futures Association either a guarantee agreement or a Form 1-FR-IB with his application for registration. If such person files a Form 1-FR-IB with his application for registration, such person must also file a Form 1-FR-IB, certified by an independent public accountant, as of a date no later than the end of the month registration is granted. The Form 1-FR-IB certified by an independent public accountant must be filed with the National Futures Association not more than 45 days after the date for which the report is made.

(b) *Filing of financial reports.* (1)(i) Except as provided in paragraphs (b)(3) and (h) of this section, each person registered as a futures commission merchant must file a Form 1-FR-FCM as of the close of business each month. Each Form 1-FR-FCM must be filed no later than 17 business days after the date for which the report is made.

(ii) In addition to the monthly financial reports required by paragraph (b)(1)(i) of this section, each person registered as a futures commission merchant must file a Form 1-FR-FCM as of the close of its fiscal year, which must be certified by an independent public accountant in accordance with §1.16, and must be filed no later than [90] 60 days after the close of the futures commission merchant's fiscal year: *Provided, however,* that a registrant which is registered with the Securities and Exchange Commission as a securities broker or dealer must file this report not later than the time permitted for filing an annual audit report under §240.17a-5(d)(5) of this title.

(2)(i) Except as provided in paragraphs (b)(3) and (h) of this section, and except for an introducing broker operating pursuant to a guarantee agreement which is not also a securities broker or dealer, each person registered as an introducing broker must file a Form 1-FR-IB semiannually as of the middle and the close of each fiscal year. Each Form 1-FR-IB must be filed no later than 17 business days after the date for which the report is made.

(ii)(A) In addition to the financial reports required by paragraph (b)(2)(i) of this section, each person registered as an introducing broker must file a Form 1-FR-IB as of the close of its fiscal year which must be certified by an independent public accountant in accordance with §1.16 no later than 90 days after the close of each introducing broker's fiscal year: *Provided, however,* that a registrant which is registered with the Securities and Exchange Commission as a securities broker or dealer must file this report not later than the time permitted for filing an annual audit report under §240.17a-5(d)(5) of this title.

(B) If an introducing broker has filed previously a Form 1-FR-IB, certified by an independent public accountant in accordance with the provisions of paragraphs (a)(2)(ii) or (j)(8) of this section and §1.16 of this part, as of a date not more than one year prior to the close of such introducing broker's fiscal year, it need not have certified by an independent public accountant the Form 1-FR-IB filed as of the introducing broker's first fiscal year-end following the as of date of its initial certified Form 1-FR-IB. In such a case, the introducing broker's Form 1-FR-IB filed as of the close of the second fiscal year-end following the as of date of its initial certified Form 1-FR-IB must cover

the period of time between those two dates and must be certified by an independent public accountant in accordance with §1.16 of this part.

(3) The provisions of paragraphs (b)(1) and (b)(2) of this section may be met by any person registered as a futures commission merchant or as an introducing broker who is a member of a designated self-regulatory organization and conforms to minimum financial standards and related reporting requirements set by such designated self-regulatory organization in its bylaws, rules, regulations, or resolutions and approved by the Commission pursuant to Section 4f(b) of the Act and §1.52: *Provided, however,* That each such registrant shall promptly file with the Commission a true and exact copy of each financial report which it files with such designated self-regulatory organization.

(4) Upon receiving written notice from any representative of the National Futures Association, the Commission or any self-regulatory organization of which it is a member, an applicant or registrant, except an applicant for registration as an introducing broker which has filed concurrently with its application for registration a guarantee agreement and which is not also a securities broker or dealer, must, monthly or at such times as specified, furnish the National Futures Association, the Commission or the self-regulatory organization requesting such information a Form 1–FR or such other financial information as requested by the National Futures Association, the Commission or the self-regulatory organization. Each such Form 1–FR or such other information must be furnished within the time period specified in the written notice, and in accordance with the provisions of paragraph (c) of this section.

(5) Each futures commission merchant must file with the Commission the measure of the future commission merchant's leverage as of the close of the business each month. For purpose of this section, the term "leverage" shall be defined by a registered futures association of which the futures commission merchant is a member. The futures commission merchant is required to file the leverage information with the Commission within 17 business days of the close of the futures commission merchant's month end.

(c) *Where to file reports.* (1) Form 1–FR filed by an introducing broker pursuant to paragraph (b)(2) of this section need be filed only with, and will be considered filed when received by, the National Futures Association. Other reports or information provided for in this section will be considered filed when received by the [regional] Regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located (as set forth in §140.02 of this chapter) and by the designated self-regulatory organization, if any; and reports or other information required to be filed by this section by an applicant for registration will be considered filed when received by the National Futures Association. Any report or information filed with the National Futures Association pursuant to this paragraph shall be deemed for all purposes to be filed with, and to be the official record of, the Commission.

(2)(i) [Except as provided in the last sentence of this subparagraph, all] All filings or other notices prepared by a futures commission merchant pursuant to this section [may] must be submitted to the Commission in electronic form using a form of user authentication assigned in accordance with procedures established by or approved by the Commission, and otherwise in accordance with instructions issued by or approved by the Commission, if the futures commission merchant or a designated self-regulatory organization has provided the Commission with the means necessary to read and to process the information contained in such report. A Form 1–FR required to be certified by an independent public accountant in accordance with §1.16 which is filed by a futures commission merchant must be filed [in paper form and may not be filed] electronically.

(ii) Except as provided in paragraph (h) of this section, all filings or other notices or applications prepared by an introducing broker or applicant for registration as an introducing broker or futures commission merchant pursuant to this section must be filed electronically in accordance with electronic filing procedures established by the National Futures Association. In the case of a Form

1–FR–IB that is required to be certified by an independent public accountant in accordance with §1.16, a paper copy of any such filing with the original manually signed certification must be maintained by the introducing broker or applicant for registration as an introducing broker in accordance with §1.31.

(3) Any information required of a registrant by a self-regulatory organization pursuant to paragraph (b)(4) of this section need be furnished only to such self-regulatory organization and the Commission, and any information required of an applicant by the National Futures Association pursuant to paragraph (b)(4) of this section need be furnished only to the National Futures Association and the Commission.

(4) Any guarantee agreement entered into between a futures commission merchant and an introducing broker in accordance with the provisions of this section need be filed only with, and will be considered filed when received by, the National Futures Association.

(d) *Contents of financial reports.* (1) Each Form 1–FR filed pursuant to this §1.10 which is not required to be certified by an independent public accountant must be completed in accordance with the instructions to the form and contain:

(i) A statement of financial condition as of the date for which the report is made;

(ii) Statements of income (loss) and a statement of changes in ownership equity for the period between the date of the most recent statement of financial condition filed with the Commission and the date for which the report is made;

(iii) A statement of changes in liabilities subordinated to claims of general creditors for the period between the date of the most recent statement of financial condition filed with the Commission and the date for which the report is made;

(iv) A statement of the computation of the minimum capital requirements pursuant to §1.17 as of the date for which the report is made;

(v) For a futures commission merchant only, the statements of segregation requirements and funds in segregation for customers trading on U.S. commodity exchanges and for customers' dealer options accounts, [and] the statement of secured amounts and funds held in separate accounts for [foreign futures and foreign options] 30.7 customers (as defined in §30.1 of this chapter) in accordance with §30.7 of this chapter, and the statement of cleared swaps customer segregation requirements and funds in cleared swaps customer accounts under section 4d(f) of the Act as of the date for which the report is made; and

(vi) In addition to the information expressly required, such [father] further material information as may be necessary to make the required statements and schedules not misleading.

(2) Each Form 1–FR filed pursuant to this §1.10 which is required to be certified by an independent public accountant must be completed in accordance with the instructions to the form and contain:

(i) A statement of financial condition as of the date for which the report is made;

(ii) Statements of income (loss), cash flows, changes in ownership equity, and changes in liabilities subordinated to claims of general creditors, for the period between the date of the most recent certified statement of financial condition filed with the Commission and the date for which the report is made: *Provided*, That for an applicant filing pursuant to paragraph (a)(2) of this section the period must be the year ending as of the date of the statement of financial condition;

(iii) A statement of the computation of the minimum capital requirements pursuant to §1.17 as of the date for which the report is made;

(iv) For a futures commission merchant only, the statements of segregation requirements and funds in segregation for customers trading on U.S. commodity exchanges and for customers' dealer options accounts, [and] the statement of secured amounts and funds held in separate accounts for [foreign futures and foreign options] 30.7 customers (as defined in §30.1 of this chapter) in accordance with §30.7 of [this chapter] the chapter, and the statement of cleared swaps customers segregation requirements and funds in cleared swaps customer accounts under section 4d(f) of the Act as of the date for which the report is made;

(v) Appropriate footnote disclosures;

(vi) A reconciliation, including appropriate explanations, of the statement of the computation of the minimum capital requirements pursuant to §1.17 and, for a futures commission merchant only, the statements of segregation requirements and funds in segregation for customers trading on U.S. commodity exchanges and for customers' dealer option accounts, [and] the statement of secured amounts and funds held in separate accounts for [foreign futures and foreign options] 30.7 customers (as defined in §30.1 of this chapter) in accordance with §30.7 of this chapter, and the statement of cleared swaps customer segregation requirements and funds in cleared swaps customer accounts under section 4d(f) of the Act, in the certified Form 1-FR with the applicant's or registrant's corresponding uncertified most recent Form 1-FR filing when material differences exist or, if no material differences exist, a statement so indicating; and

(vii) In addition to the information expressly required, such further material information as may be necessary to make the required statements not misleading.

(3) The statements required by paragraphs (d)(2)(i) and (d)(2)(ii) of this section may be presented in accordance with generally accepted accounting principles in the certified reports filed as of the close of the registrant's fiscal year pursuant to paragraphs (b)(1)(ii) or (b)(2)(ii) of this section or accompanying the application for registration pursuant to paragraph (a)(2) of this section, rather than in the format specifically prescribed by these regulations: *Provided*, the statement of financial condition is presented in a format as consistent as possible with the Form 1-FR and a reconciliation is provided reconciling such statement of financial condition to the statement of the computation of the minimum capital requirements pursuant to §1.17. Such reconciliation must be certified by an independent public accountant in accordance with §1.16.

(4) Attached to each Form 1-FR filed pursuant to this section must be an oath or affirmation that to the best knowledge and belief of the individual making such oath or affirmation the information contained in the Form 1-FR is true and correct. The individual making such oath or affirmation must be:

(i) If the registrant or applicant is a sole proprietorship, the proprietor; if a partnership, any general partner; if a corporation, the chief executive officer or chief financial officer; and, if a limited liability company or limited liability partnership, the chief executive officer, the chief financial officer, the manager, the managing member, or those members vested with the management authority for the limited liability company or limited liability partnership; or

(ii) If the registrant or applicant is registered with the Securities and Exchange Commission as a securities broker or dealer, the representative authorized under §240.17a-5 of this title to file for the securities broker or dealer its Financial and Operational Combined Uniform Single Report under the Securities Exchange Act of 1934, part II, part IIA, or part II CSE.

(iii) In the case of a Form 1–FR filed via electronic transmission in accordance with procedures established by or approved by the Commission, such transmission must be accompanied by the user authentication assigned to the authorized signer under such procedures, and the use of such user authentication will constitute and become a substitute for the manual signature of the authorized signer for the purpose of making the oath or affirmation referred to in this paragraph.

(e) *Election of fiscal year.* (1) An applicant wishing to establish a fiscal year other than the calendar year may do so by notifying the National Futures Association of its election of such fiscal year, in writing, concurrently with the filing of the Form 1–FR pursuant to paragraph (a)(2) of this section, but in no event may such fiscal year end more than one year from the date of the Form 1–FR filed pursuant to paragraph (a)(2) of this section. An applicant that does not so notify the National Futures Association will be deemed to have elected the calendar year as its fiscal year.

(2) (i) A registrant must continue to use its elected fiscal year, calendar or otherwise, unless a change in such fiscal year has been approved pursuant to this paragraph (e)(2).

(ii) *Futures commission merchant registrants.* (A) A futures commission merchant may file with its designated self-regulatory organization an application to change its fiscal year, a copy of which the registrant must file with the Commission. The application shall be approved or denied in writing by the designated self-regulatory organization. The registrant must file immediately with the Commission a copy of any notice it receives from the designated self-regulatory organization to approve or deny the registrant's application to change its fiscal year. A written notice of approval shall become effective upon the filing by the registrant of a copy with the Commission, and a written notice of denial shall be effective as of the date of the notice.

(B) A futures commission merchant that is registered with the Securities and Exchange Commission as a securities broker or dealer may file with its designated self-regulatory organization copies of any notice or application filed with its designated examining authority, pursuant to §240.17a–5(d)(1)(i) of this title, for a change in fiscal year or "as of" date for its annual audited financial statement. The registrant must also file immediately with the designated self-regulatory organization and the Commission copies of any notice it receives from its designated examining authority to approve or deny the registrant's request for change in fiscal year or "as of" date. Upon the receipt by the designated self-regulatory organization and the Commission of copies of any such notice of approval, the change in fiscal year or "as of" date referenced in the notice shall be deemed approved under this paragraph (e)(2).

(C) Any copy that under this paragraph (e)(2) is required to be filed with the Commission shall be filed with the regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located, and any copy or application to be filed with the designated self-regulatory organization shall be filed at its principal place of business.

(iii) *Introducing broker registrants.* (A) An introducing broker may file with the National Futures Association an application to change its fiscal year, which shall be approved or denied in writing.

(B) An introducing broker that is registered with the Securities and Exchange Commission as a securities broker or dealer may file with the National Futures Association copies of any notice or application filed with its designated examining authority, pursuant to §240.17a–5(d)(1)(i) of this title, for a change in fiscal year or "as of" date for its annual audited financial statement. The registrant must also file immediately with the National Futures Association copies of any notice it receives from its designated examining authority to approve or deny the registrant's request for change in fiscal year or "as of" date. Upon the receipt by the National Futures Association of copies of any such notice of approval, the change in fiscal year or "as of" date referenced in the notice shall be deemed approved under this paragraph (e)(2).

(f) *Extension of time for filing uncertified reports.* (1) In the event a registrant finds that it cannot file its Form 1-FR, or, in accordance with paragraph (h) of this section, its Financial and Operational Combined Uniform Single Report under the Securities Exchange Act of 1934, part II, part IIA, or part II CSE (FOCUS report), for any period within the time specified in paragraphs (b)(1)(i) or (b)(2)(i) of this section without substantial undue hardship, it may request approval for an extension of time, as follows:

(i) *Futures commission merchant registrants.* (A) A futures commission merchant may file with its designated self-regulatory organization an application for extension of time, a copy of which the registrant must file with the Commission. The application shall be approved or denied in writing by the designated self-regulatory organization. The registrant must file immediately with the Commission a copy of any notice it receives from the designated self-regulatory organization to approve or deny the registrant's request for extension of time. A written notice of approval shall become effective upon the filing by the registrant of a copy with the Commission, and a written notice of denial shall be effective as of the date of the notice.

(B) A futures commission merchant that is registered with the Securities and Exchange Commission as a securities broker or dealer may file with its designated self-regulatory organization a copy of any application that the registrant has filed with its designated examining authority, pursuant to §240.17-a5(l)(5) of this title, for an extension of time to file its FOCUS report. The registrant must also file immediately with the designated self-regulatory organization and the Commission copies of any notice it receives from its designated examining authority to approve or deny the requested extension of time. Upon receipt by the designated self-regulatory organization and the Commission of copies of any such notice of approval, the requested extension of time referenced in the notice shall be deemed approved under this paragraph (f)(1).

(C) Any copy that under this subparagraph (f)(1)(i) is required to be filed with the Commission shall be filed with the regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located.

(ii) *Introducing broker registrants.* (A) An introducing broker may file with the National Futures Association an application for extension of the time, which shall be approved or denied in writing.

(B) An introducing broker that is registered with the Securities and Exchange Commission as a securities broker or dealer may file with the National Futures Association copies of any application that the registrant has filed with its designated examining authority, pursuant to §240.17-a5(l)(5) of this title, for an extension of time to file its FOCUS report. The registrant must also file immediately with the National Futures Association copies of any notice it receives from its designated examining authority to approve or deny the requested extension of time. Upon the receipt by the National Futures Association of a copy of any such notice of approval, the requested extension of time referenced in the notice shall be deemed approved under this paragraph (f)(1)(ii).

(2) In the event an applicant finds that it cannot file its report for any period within the time specified in paragraph (b)(4) of this section without substantial undue hardship, it may file with the National Futures Association an application for an extension of time to a specified date which may not be more than 90 days after the date as of which the financial statements were to have been filed. The application must state the reasons for the requested extension and must contain an agreement to file the report on or before the specified date. The application must be received by the National Futures Association before the time specified in paragraph (b)(4) of this section for filing the report. Notice of such application must be filed with the regional office of the Commission with jurisdiction over the state in which the applicant's principal place of business is located concurrently with the filing of such application with the National Futures Association. Within ten calendar days after receipt of the application for an extension of time, the National Futures Association shall:

- (i) Notify the applicant of the grant or denial of the requested extension; or
  - (ii) Indicate to the applicant that additional time is required to analyze the request, in which case the amount of time needed will be specified.
- (g) *Public availability of reports.* (1) Forms 1–FR filed pursuant to this section, and FOCUS reports filed in lieu of Forms 1–FR pursuant to paragraph (h) of this section, will be treated as exempt from mandatory public disclosure for purposes of the Freedom of Information Act and the Government in the Sunshine Act and parts 145 and 147 of this chapter, except for the information described in paragraph (g)(2) of this section.
- (2) The following information in Forms 1–FR, and the same or equivalent information in FOCUS reports filed in lieu of Forms 1–FR, will be publicly available:
- (i) The amount of the applicant's or registrant's adjusted net capital; the amount of its minimum net capital requirement under §1.17 of this chapter; and the amount of its adjusted net capital in excess of its minimum net capital requirement; and
  - (ii) The following statements and footnote disclosures thereof: the Statement of Financial Condition in the certified annual financial reports of futures commission merchants and introducing brokers; the Statements (to be filed by a futures commission merchant only) of Segregation Requirements and Funds in Segregation for customers trading on U.S. commodity exchanges and for customers' dealer options accounts, [and] the Statement (to be filed by a futures commission merchant only) of Secured Amounts and Funds held in Separate Accounts for [foreign futures and foreign options customers] 30.7 Customers (as defined in §30.1 of this chapter) in accordance with §30.7 of this chapter, and the Statement (to be filed by futures commission merchants only) of Cleared Swaps Customer Segregation Requirements and Funds in Cleared Swaps Customer Accounts under section 4d(f) of the Act.

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## **520. Compliance with Commission Regulation 1.11 – Risk Management Program for Futures Commission Merchants.**

Any Trading Privilege Holder subject to Commission Regulation 1.11 that violates Commission Regulation 1.11 shall be deemed to have violated this Rule 520. Commission Regulation 1.11 is set forth below and incorporated into this Rule 520.

Commission Regulation 1.11 - Risk management program for futures commission merchants.

(a) Applicability. Nothing in this section shall apply to a futures commission merchant that does not accept any money, securities, or property (or extend credit in lieu thereof) to margin, guarantee, or secure any trades or contracts that result from soliciting or accepting orders for the purchase or sale of any commodity interest.

(b) Definitions. For purposes of this section:

(1) Business unit means any department, division, group, or personnel of a futures commission merchant or any of its affiliates, whether or not identified as such that:

(i) Engages in soliciting or in accepting orders for the purchase or sale of any commodity interest and that, in or in connection with such solicitation or acceptance of orders, accepts any money, securities, or property (or extends credit in lieu thereof) to margin, guarantee, or secure any trades or contracts that result or may result therefrom; or

(ii) Otherwise handles segregated funds, including managing, investing, and overseeing the custody of segregated funds, or any documentation in connection therewith, other than for risk management purposes; and

(iii) Any personnel exercising direct supervisory authority of the performance of the activities described in paragraph (b)(1)(i) or (ii) of this section.

(2) *Customer* means a futures customer as defined in §1.3, Cleared Swaps Customer as defined in §22.1 of this chapter, and 30.7 customer as defined in §30.1 of this chapter.

(3) *Governing body* means the proprietor, if the futures commission merchant is a sole proprietorship; a general partner, if the futures commission merchant is a partnership; the board of directors if the futures commission merchant is a corporation; the chief executive officer, the chief financial officer, the manager, the managing member, or those members vested with the management authority if the futures commission merchant is a limited liability company or limited liability partnership.

(4) *Segregated funds* means money, securities, or other property held by a futures commission merchant in separate accounts pursuant to §1.20 for futures customers, pursuant to §22.2 of this chapter for Cleared Swaps Customers, and pursuant to §30.7 of this chapter for 30.7 customers.

(5) *Senior management* means, any officer or officers specifically granted the authority and responsibility to fulfill the requirements of senior management by the governing body.

(c) *Risk Management Program.* (1) Each futures commission merchant shall establish, maintain, and enforce a system of risk management policies and procedures designed to monitor and manage the risks associated with the activities of the futures commission merchant as such. For purposes of this section, such policies and procedures shall be referred to collectively as a "Risk Management Program."

(2) Each futures commission merchant shall maintain written policies and procedures that describe the Risk Management Program of the futures commission merchant.

(3) The Risk Management Program and the written risk management policies and procedures, and any material changes thereto, shall be approved in writing by the governing body of the futures commission merchant.

(4) Each futures commission merchant shall furnish a copy of its written risk management policies and procedures to the Commission and its designated self-regulatory organization upon application for registration and thereafter upon request.

(d) *Risk management unit.* As part of the Risk Management Program, each futures commission merchant shall establish and maintain a risk management unit with sufficient authority; qualified personnel; and financial, operational, and other resources to carry out the risk management program established pursuant to this section. The risk management unit shall report directly to senior management and shall be independent from the business unit.

(e) Elements of the Risk Management Program. The Risk Management Program of each futures commission merchant shall include, at a minimum, the following elements:

(1) Identification of risks and risk tolerance limits. (i) The Risk Management Program shall take into account market, credit, liquidity, foreign currency, legal, operational, settlement, segregation, technological, capital, and any other applicable risks together with a description of the risk tolerance limits set by the futures commission merchant and the underlying methodology in the written policies and procedures. The risk tolerance limits shall be reviewed and approved quarterly by senior management and annually by the governing body. Exceptions to risk tolerance limits shall be subject to written policies and procedures.

(ii) The Risk Management Program shall take into account risks posed by affiliates, all lines of business of the futures commission merchant, and all other trading activity engaged in by the futures commission merchant. The Risk Management Program shall be integrated into risk management at the consolidated entity level.

(iii) The Risk Management Program shall include policies and procedures for detecting breaches of risk tolerance limits set by the futures commission merchant, and alerting supervisors within the risk management unit and senior management, as appropriate.

(2) Periodic Risk Exposure Reports. (i) The risk management unit of each futures commission merchant shall provide to senior management and to its governing body quarterly written reports setting forth all applicable risk exposures of the futures commission merchant; any recommended or completed changes to the Risk Management Program; the recommended time frame for implementing recommended changes; and the status of any incomplete implementation of previously recommended changes to the Risk Management Program. For purposes of this section, such reports shall be referred to as "Risk Exposure Reports." The Risk Exposure Reports also shall be provided to the senior management and the governing body immediately upon detection of any material change in the risk exposure of the futures commission merchant.

(ii) Furnishing to the Commission. Each futures commission merchant shall furnish copies of its Risk Exposure Reports to the Commission within five (5) business days of providing such reports to its senior management.

(3) Specific risk management considerations. The Risk Management Program of each futures commission merchant shall include, but not be limited to, policies and procedures necessary to monitor and manage the following risks:

(i) Segregation risk. The written policies and procedures shall be reasonably designed to ensure that segregated funds are separately accounted for and segregated or secured as belonging to customers as required by the Act and Commission regulations and must, at a minimum, include or address the following:

(A) A process for the evaluation of depositories of segregated funds, including, at a minimum, documented criteria that any depository that will hold segregated funds, including an entity affiliated with the futures commission merchant, must meet, including criteria addressing the depository's capitalization, creditworthiness, operational reliability, and access to liquidity. The criteria should further consider the extent to which segregated funds are concentrated with any depository or group of depositories. The criteria also should include the availability of deposit insurance and the extent of the regulation and supervision of the depository;

(B) A program to monitor an approved depository on an ongoing basis to assess its continued satisfaction of the futures commission merchant's established criteria, including a thorough due diligence review of each depository at least annually;

(C) An account opening process for depositories, including documented authorization requirements, procedures that ensure that segregated funds are not deposited with a depository prior to the futures commission merchant receiving the acknowledgment letter required from such depository pursuant to §1.20, and §§22.2 and 30.7 of this chapter, and procedures that ensure that such account is properly titled to reflect that it is holding segregated funds pursuant to the Act and Commission regulations;

(D) A process for establishing a targeted amount of residual interest that the futures commission merchant seeks to maintain as its residual interest in the segregated funds accounts and such process must be designed to reasonably ensure that the futures commission merchant maintains the targeted residual amounts and remains in compliance with the segregated funds requirements at all times. The policies and procedures must require that senior management, in establishing the total amount of the targeted residual interest in the segregated funds accounts, perform appropriate due diligence and consider various factors, as applicable, relating to the nature of the futures commission merchant's business including, but not limited to, the composition of the futures commission merchant's customer base, the general creditworthiness of the customer base, the general trading activity of the customers, the types of markets and products traded by the customers, the proprietary trading of the futures commission merchant, the general volatility and liquidity of the markets and products traded by customers, the futures commission merchant's own liquidity and capital needs, and the historical trends in customer segregated fund balances, including undermargined amounts and net deficit balances in customers' accounts. The analysis and calculation of the targeted amount of the future commission merchant's residual interest must be described in writing with the specificity necessary to allow the Commission and the futures commission merchant's designated self-regulatory organization to duplicate the analysis and calculation and test the assumptions made by the futures commission merchant. The adequacy of the targeted residual interest and the process for establishing the targeted residual interest must be reassessed periodically by Senior Management and revised as necessary;

(E) A process for the withdrawal of cash, securities, or other property from accounts holding segregated funds, where the withdrawal is not for the purpose of payments to or on behalf of the futures commission merchant's customers. Such policies and procedures must satisfy the requirements of §1.23, §22.17 of this chapter, or §30.7 of this chapter, as applicable;

(F) A process for assessing the appropriateness of specific investments of segregated funds in permitted investments in accordance with §1.25. Such policies and procedures must take into consideration the market, credit, counterparty, operational, and liquidity risks associated with such investments, and assess whether such investments comply with the requirements in §1.25 including that the futures commission merchant manage the permitted investments consistent with the objectives of preserving principal and maintaining liquidity;

(G) Procedures requiring the appropriate separation of duties among individuals responsible for compliance with the Act and Commission regulations relating to the protection and financial reporting of segregated funds, including the separation of duties among personnel that are responsible for advising customers on trading activities, approving or overseeing cash receipts and disbursements (including investment operations), and recording and reporting financial transactions. The policies and procedures must require that any movement of funds to affiliated companies and parties are properly approved and documented;

(H) A process for the timely recording of all transactions, including transactions impacting customers' accounts, in the firm's books of record;

(I) A program for conducting annual training of all finance, treasury, operations, regulatory, compliance, settlement, and other relevant officers and employees regarding the segregation requirements for segregated funds required by the Act and regulations, the requirements for notices under §1.12, procedures for reporting suspected breaches of the policies and procedures

required by this section to the chief compliance officer, without fear of retaliation, and the consequences of failing to comply with the segregation requirements of the Act and regulations; and

(J) Policies and procedures for assessing the liquidity, marketability and mark-to-market valuation of all securities or other non-cash assets held as segregated funds, including permitted investments under §1.25, to ensure that all non-cash assets held in the customer segregated accounts, both customer-owned securities and investments in accordance with §1.25, are readily marketable and highly liquid. Such policies and procedures must require daily measurement of liquidity needs with respect to customers; assessment of procedures to liquidate all non-cash collateral in a timely manner and without significant effect on price; and application of appropriate collateral haircuts that accurately reflect market and credit risk.

(ii) Operational risk. The Risk Management Program shall include automated financial risk management controls reasonably designed to prevent the placing of erroneous orders, including those that exceed pre-set capital, credit, or volume thresholds. The Risk Management Program shall ensure that the use of automated trading programs is subject to policies and procedures governing the use, supervision, maintenance, testing, and inspection of such programs.

(iii) Capital risk. The written policies and procedures shall be reasonably designed to ensure that the futures commission merchant has sufficient capital to be in compliance with the Act and the regulations, and sufficient capital and liquidity to meet the reasonably foreseeable needs of the futures commission merchant.

(4) Supervision of the Risk Management Program. The Risk Management Program shall include a supervisory system that is reasonably designed to ensure that the policies and procedures required by this section are diligently followed.

(f) Review and testing. (1) The Risk Management Program of each futures commission merchant shall be reviewed and tested on at least an annual basis, or upon any material change in the business of the futures commission merchant that is reasonably likely to alter the risk profile of the futures commission merchant.

(2) The annual reviews of the Risk Management Program shall include an analysis of adherence to, and the effectiveness of, the risk management policies and procedures, and any recommendations for modifications to the Risk Management Program. The annual testing shall be performed by qualified internal audit staff that are independent of the business unit, or by a qualified third party audit service reporting to staff that are independent of the business unit. The results of the annual review of the Risk Management Program shall be promptly reported to and reviewed by the chief compliance officer, senior management, and governing body of the futures commission merchant.

(3) Each futures commission merchant shall document all internal and external reviews and testing of its Risk Management Program and written risk management policies and procedures including the date of the review or test; the results; any deficiencies identified; the corrective action taken; and the date that corrective action was taken. Such documentation shall be provided to Commission staff, upon request.

(g) Distribution of risk management policies and procedures. The Risk Management Program shall include procedures for the timely distribution of its written risk management policies and procedures to relevant supervisory personnel. Each futures commission merchant shall maintain records of the persons to whom the risk management policies and procedures were distributed and when they were distributed.

(h) Recordkeeping. (1) Each futures commission merchant shall maintain copies of all written approvals required by this section.

(2) All records or reports, including, but not limited to, the written policies and procedures and any changes thereto that a futures commission merchant is required to maintain pursuant to this regulation shall be maintained in accordance with §1.31 and shall be made available promptly upon request to representatives of the Commission.

**[520] 521. Compliance with Commission Regulation 1.12  
– Maintenance of Minimum Financial Requirements by  
Futures Commission Merchants and Introducing Brokers.**

Any Trading Privilege Holder subject to Commission Regulation 1.12 that violates Commission Regulation 1.12 shall be deemed to have violated this Rule [520] 521. Commission Regulation 1.12 is set forth below and incorporated into this Rule [520] 521.

Commission Regulation 1.12 - Maintenance of minimum financial requirements by futures commission merchants and introducing brokers.

(a) Each person registered as a futures commission merchant or who files an application for registration as a futures commission merchant, and each person registered as an introducing broker or who files an application for registration as an introducing broker (except for an introducing broker or applicant for registration as an introducing broker operating pursuant to, or who has filed concurrently with its application for registration, a guarantee agreement and who is not also a securities broker or dealer), who knows or should have known that its adjusted net capital at any time is less than the minimum required by §1.17 or by the capital rule of any self-regulatory organization to which such person is subject, if any, must:

(1) Give [telephonic notice, to be confirmed in writing by facsimile] notice, as set forth in paragraph ([i][n]) of this section that the applicant's or registrant's adjusted net capital is less than required by §1.17 or by other capital rule, identifying the applicable capital rule. The notice must be given immediately after the applicant or registrant knows or should [know] have known that its adjusted net capital is less than required by any of the aforesaid rules to which the applicant or registrant is subject; and

(2) Provide together with such notice documentation in such form as necessary to adequately reflect the applicant's or registrant's capital condition as of any date on which such person's adjusted net capital is less than the minimum required; Provided, however, that if the applicant or registrant cannot calculate or otherwise immediately determine its financial condition, it must provide the notice required by paragraph (a)(1) of this section and include in such notice a statement that the entity cannot presently calculate its financial condition. The applicant or registrant must provide similar documentation of its financial condition for other days as the Commission may request.

(b) Each person registered as a futures commission merchant, or who files an application for registration as a futures commission merchant, who knows or should have known that its adjusted net capital at any time is less than the greatest of:

(1) 150 percent of the minimum dollar amount required by §1.17(a)(1)(i)(A);

(2) 110 percent of the amount required by §1.17(a)(1)(i)(B);

(3) 150 percent of the amount of adjusted net capital required by a registered futures association of which it is a member, unless such amount has been determined by a margin-based capital computation set forth in the rules of the registered futures association, and such amount meets or exceeds the amount of adjusted net capital required under the margin-based capital computation set forth in §1.17(a)(1)(i)(B), in which case the required percentage is 110 percent, or

(4) For securities brokers or dealers, the amount of net capital specified in Rule 17a-11(c) of the Securities and Exchange Commission (17 CFR 240.17a-11(c)), must file [written] notice to that effect, as set forth in paragraph ([i]n) of this section [within], as soon as possible and no later than twenty-four (24) hours of such event.

(c) If an applicant or registrant at any time fails to make or keep current the books and records required by these regulations, such applicant or registrant must, on the same day such event occurs, provide [facsimile] notice of such fact as specified in paragraph (n) of this section, specifying the books and records which have not been made or which are not current, and [within] as soon as possible, but not later than forty-eight (48) hours after giving such notice file a [written] report as required by paragraph (n) of this section stating what steps have been and are being taken to correct the situation.

(d) Whenever any applicant or registrant discovers or is notified by an independent public accountant, pursuant to §1.16(e)(2) [of this chapter], of the existence of any material inadequacy, as specified in §1.16(d)(2) [of this chapter], such applicant or registrant must give [facsimile] notice of such material inadequacy [within twenty-four (24) hours, and within forty-eight (48) hours after giving such notice file a written] , as provided in paragraph (n) of this section, as soon as possible but not later than twenty-four (24) hours of discovering or being notified of the material inadequacy. The applicant or registrant must file, in the manner provided for under paragraph (n) of this section, a report stating what steps have been and are being taken to correct the material inadequacy within forty-eight (48) hours of filing its notice of the material inadequacy.

(e) Whenever any self-regulatory organization learns that a member registrant has failed to file a notice or [written] report as required by [§1.12] this section, that self-regulatory organization must immediately report this failure by [telephone, confirmed in writing immediately by facsimile] notice, as provided in paragraph ([i]n) of this section.

(f)(1) [Reserved]

(2) Whenever a registered futures commission merchant determines that any position it carries for another registered futures commission merchant or for a registered leverage transaction merchant must be liquidated immediately, transferred immediately or that the trading of any account of such futures commission merchant or leverage transaction merchant shall be only for purposes of liquidation, because the other futures commission merchant or the leverage transaction merchant has failed to meet a call for margin or to make other required deposits, the carrying futures commission merchant must immediately give [telephonic notice, confirmed in writing immediately by facsimile notice] as provided in paragraph (n) of this section, of such a determination [to the principal office of the Commission at Washington, DC].

(3) Whenever a registered futures commission merchant determines that an account which it is carrying is undermargined by an amount which exceeds the futures commission merchant's adjusted net capital determined in accordance with §1.17, the futures commission merchant must immediately [give telephonic notice, confirmed in writing immediately by facsimile notice] provide notice, as provided in paragraph (n) of this section, of such a determination to the designated self-regulatory organization and the [principal office of the] Commission [at Washington, DC]. This paragraph (f)(3) shall apply to any account carried by the futures commission merchant, whether a customer, noncustomer, omnibus or proprietary account. For purposes of this paragraph [(f)(3)], if

any person has an interest of 10 percent or more in ownership or equity in, or guarantees, more than one account, or has guaranteed an account in addition to [his] its own account, all such accounts shall be combined. [A designated self-regulatory organization may grant an exemption from the provisions of this paragraph to a futures commission merchant with respect to any particular account on a continuous basis provided the designated self-regulatory organization documents the reasons for granting such an exemption and continues to monitor any such account.]

(4) A futures commission merchant shall [report immediately by telephone, confirmed immediately in writing by facsimile notice] provide immediate notice, as provided in paragraph (n) of this section, whenever any commodity interest account it carries is subject to a margin call, or call for other deposits required by the futures commission merchant, that exceeds the futures commission merchant's excess adjusted net capital, determined in accordance with §1.17, and such call has not been answered by the close of business on the day following the issuance of the call. This applies to all accounts carried by the futures commission merchant, whether customer, noncustomer, or omnibus, that are subject to margining, including commodity futures, cleared swaps, and options. In addition to actual margin deposits by an account owner, a futures commission merchant may also take account of favorable market moves in determining whether the margin call is required to be reported under this paragraph.

(5)(i) A futures commission merchant shall [report immediately by telephone, confirmed immediately in writing by facsimile notice] provide immediate notice, as provided in paragraph (n) of this section, whenever its excess adjusted net capital is less than six percent of the maintenance margin required by the futures commission merchant on all positions held in accounts of a noncustomer other than a noncustomer who is subject to the minimum financial requirements of:

(A) A futures commission merchant, or

(B) The Securities and Exchange Commission for a securities broker [and] or dealer.

(ii) For purposes of paragraph (f)(5)(i) of this section, maintenance margin shall include all deposits which the futures commission merchant requires the noncustomer to maintain in order to carry its positions at the futures commission merchant.

(g) A futures commission merchant shall provide [written] notice, as provided in paragraph (n) of this section, of a substantial reduction in capital as compared to that last reported in a financial report filed with the Commission pursuant to §1.10. This notice shall be provided as follows:

(1) If any event or series of events, including any withdrawal, advance, loan or loss cause, on a net basis, a reduction in net capital (or, if the futures commission merchant is qualified to use the filing option available under §1.10(h), tentative net capital as defined in the rules of the Securities and Exchange Commission) of 20 percent or more, notice must be provided as provided in paragraph (n) of this section within two business days of the event or series of events causing the reduction stating the reason for the reduction and steps the futures commission merchant will be taking to ensure an appropriate level of net capital is maintained by the futures commission merchant; and

(2) If equity capital of the futures commission merchant or a subsidiary or affiliate of the futures commission merchant consolidated pursuant to §1.17(f) (or 17 CFR 240.15c3-1e) would be withdrawn by action of a stockholder or a partner or a limited liability company member or by redemption or repurchase of shares of stock by any of the consolidated entities or through the payment of dividends or any similar distribution, or an unsecured advance or loan would be made to a stockholder, partner, sole proprietor, limited liability company member, employee or affiliate, such that the withdrawal, advance or loan would cause, on a net basis, a reduction in excess adjusted net capital (or, if the futures commission merchant is qualified to use the filing option

available under §1.10(h), excess net capital as defined in the rules of the Securities and Exchange Commission) of 30 percent or more, notice must be provided as provided in paragraph (n) of this section at least two business days prior to the withdrawal, advance or loan that would cause the reduction: *Provided, however,* That the provisions of paragraphs (g)(1) and (g)(2) of this section do not apply to any futures or securities transaction in the ordinary course of business between a futures commission merchant and any affiliate where the futures commission merchant makes payment to or on behalf of such affiliate for such transaction and then receives payment from such affiliate for such transaction within two business days from the date of the transaction.

(3) Upon receipt of such notice from a futures commission merchant, or upon a reasonable belief that a substantial reduction in capital has occurred or will occur, the Director of the Division of [Clearing] Swap Dealer and Intermediary Oversight or the Director's designee may require that the futures commission merchant provide or cause a Material Affiliated Person (as that term is defined in §1.14(a)(2)) to provide, within three business days from the date of request or such shorter period as the Division Director or designee may specify, such other information as the Division Director or designee determines to be necessary based upon market conditions, reports provided by the futures commission merchant, or other available information.

(h) Whenever a person registered as a futures commission merchant knows or should know that the total amount of its funds on deposit in segregated accounts on behalf of customers[, or that] trading on designated contract markets, or the amount of funds on deposit in segregated accounts for customers transacting in Cleared Swaps under part 22 of this chapter, or the total amount set aside on behalf of customers trading on non-United States markets under part 30 of this chapter, is less than the total amount of such funds required by the Act and the [Commission's rules] regulations to be on deposit in segregated or secured amount accounts on behalf of such customers, the registrant must report such deficiency immediately by [telephone notice, confirmed immediately in writing by facsimile notice,] notice to the registrant's designated self-regulatory organization and the [principal office of the Commission in Washington, DC, to the attention of the Director and the Chief Accountant of the Division of Clearing and Intermediary Oversight] Commission, as provided in paragraph (n) of this section.

(i) A futures commission merchant must provide immediate notice, as set forth in paragraph (n) of this section, whenever it discovers or is informed that it has invested funds held for futures customers trading on designated contract markets pursuant to §1.20, Cleared Swaps Customer Collateral, as defined in §22.1 of this chapter, or 30.7 customer funds, as defined in §30.1 of this chapter, in instruments that are not permitted investments under §1.25, or has otherwise violated the requirements governing the investment of funds belonging to customers under §1.25.

(j) A futures commission merchant must provide immediate notice, as provided in paragraph (n) of this section, whenever the futures commission merchant does not hold a sufficient amount of funds in segregated accounts for futures customers under §1.20, in segregated accounts for Cleared Swaps Customers under part 22 of this chapter, or in secured amount accounts for customers trading on foreign markets under part 30 of this chapter to meet the futures commission merchant's targeted residual interest in the segregated or secured amount accounts pursuant to its policies and procedures required under §1.11, or whenever the futures commission merchant's amount of residual interest is less than the sum of the undermargined amounts in its customer accounts as determined at the point in time that the firm is required to maintain the undermargined amounts under §1.22, and §§22.2 and 30.7 of this chapter.

(k) A futures commission merchant must provide immediate notice, as provided in paragraph (n) of this section, whenever the futures commission merchant, or the futures commission merchant's parent or material affiliate, experiences a material adverse impact to its creditworthiness or ability to fund its obligations, including any change that could adversely impact the firm's liquidity resources.

(l) A futures commission merchant must provide prompt notice, but in no event later than 24 hours, as provided in paragraph (n) of this section, whenever the futures commission merchant experiences a material change in its operations or risk profile, including a change in the senior management of the futures commission merchant, the establishment or termination of a line of business, or a material adverse change in the futures commission merchant's clearing arrangements.

(m) A futures commission merchant must provide notice, if the futures commission merchant has been notified by the Securities and Exchange Commission, a securities self-regulatory organization, or a futures self-regulatory organization, that it is the subject of a formal investigation. A futures commission merchant must provide a copy of any examination report issued to the futures commission merchant by the Securities and Exchange Commission or a securities self-regulatory organization. A futures commission merchant must provide the Commission with notice of any correspondence received from the Securities and Exchange Commission or a securities self-regulatory organization that raises issues with the adequacy of the futures commission merchant's capital position, liquidity to meet its obligations or otherwise operate its business, or internal controls. The notices and examination reports required by this section must be filed in a prompt manner, but in no event later than 24 hours of the reportable event, and must be filed in accordance with paragraph (n) of the section; Provided, however, that a futures commission merchant is not required to file a notice or copy of an examination report with the Securities and Exchange Commission, a securities self-regulatory organization, or a futures self-regulatory organization if such entity originally provided the communication or report to the futures commission merchant.

(n) Notice. (1) Every notice and [written] report required to be [given or] filed by this section [(except for notices required by paragraph (f) of this section)] by a futures commission merchant or a self-regulatory organization must be filed with the [regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located, with the principal office of the Commission in Washington, DC] Commission, with the designated self-regulatory organization, if any[;], and with the Securities and Exchange Commission, if such registrant is a securities broker or dealer. Every notice and [written] report required to be [given or] filed by this section by an applicant for registration as a futures commission merchant must be filed with the National Futures Association (on behalf of the Commission), with the designated self-regulatory organization, if any, and with the Securities and Exchange Commission, if such applicant is a securities broker or dealer. [Any notice or report filed with the National Futures Association pursuant to this paragraph shall be deemed for all purposes to be filed with, and to be the official record of, the Commission] Every notice or report that is required to be filed by this section by a futures commission merchant or a self-regulatory organization must include a discussion of how the reporting event originated and what steps have been, or are being taken, to address the reporting event.

(2) Every notice and [written] report which an introducing broker or applicant for registration as an introducing broker is required to [give or] file by paragraphs (a), (c) and (d) of this section must be filed with the National Futures Association (on behalf of the Commission), with the designated self-regulatory organization, if any, and with every futures commission merchant carrying or intending to carry customer accounts for the introducing broker or applicant for registration as an introducing broker. Any notice or report filed with the National Futures Association pursuant to this paragraph shall be deemed for all purposes to be filed with, and to be the official record of, the Commission. Every notice or report that is required to be filed by this section by an introducing broker or applicant for registration as an introducing broker must include a discussion of how the reporting event originated and what steps have been, or are being taken, to address the reporting event.

(3) Every notice or report that is required to be [provided in writing to] filed by a futures commission merchant with the Commission or with a designated self-regulatory organization under this section [may, in lieu of facsimile,] must be in writing and must be filed via electronic transmission using a

form of user authentication assigned in accordance with procedures established by or approved by the Commission, and otherwise in accordance with instructions issued by or approved by the Commission; Provided, however, that if the registered futures commission merchant cannot file the notice or report using the electronic transmission approved by the Commission due to a transmission or systems failure, the futures commission merchant must immediately contact the Commission's regional office with jurisdiction over the futures commission merchant as provided in §140.02 of this chapter, and by email to FCMNotice@CFTC.gov. Any such electronic submission must clearly indicate the [registrant or applicant] futures commission merchant on whose behalf such filing is made and the use of such user authentication in submitting such filing will constitute and become a substitute for the manual signature of the authorized signer.

**[521] 522. Compliance with Commission Regulation 1.17 - Minimum Financial Requirements for Futures Commission Merchants and Introducing Brokers**

Any Trading Privilege Holder subject to Commission Regulation 1.17 that violates Commission Regulation 1.17 shall be deemed to have violated this Rule [521] 522. Commission Regulation 1.17 is set forth below and incorporated into this Rule [521] 522.

Commission Regulation 1.17 - Minimum financial requirements for futures commission merchants and [Introducing] introducing brokers.

(a)(1)(i) Except as provided in paragraph (a)(2)(i) of this section, each person registered as a futures commission merchant must maintain adjusted net capital equal to or in excess of the greatest of:

(A) \$1,000,000;

(B) The futures commission merchant's risk-based capital requirement, computed as eight percent of the total risk margin requirement for positions carried by the futures commission merchant in customer accounts and noncustomer accounts.

(C) The amount of adjusted net capital required by a registered futures association of which it is a member; or

(D) For securities brokers and dealers, the amount of net capital required by Rule 15c3-1(a) of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

(ii) [Each person registered as a futures commission merchant engaged in soliciting or accepting orders and customer funds related thereto for the purchase or sale of any commodity for future delivery or any commodity option on or subject to the rules of a registered derivatives transaction execution facility from any customer who does not qualify as an "institutional customer" as defined in §1.3(g) must:] Reserved

[(A) Be a clearing member of a derivatives clearing organization and maintain net capital in the amount of the greater of \$20,000,000 or the amounts otherwise specified in paragraph (a)(1)(i) of this section; or

(B) Receive orders on behalf of the customer from a commodity trading advisor acting in accordance with §4.32 of this chapter.]

(iii) Except as provided in paragraph (a)(2) of this section, each person registered as an introducing broker must maintain adjusted net capital equal to or in excess of the greatest of:

(A) \$45,000;

(B) The amount of adjusted net capital required by a registered futures association of which it is a member; or

(C) For securities brokers and dealers, the amount of net capital required by Rule 15c3-1(a) of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

(2)(i) The requirements of paragraph (a)(1) of this section shall not be applicable if the registrant is a member of a designated self-regulatory organization and conforms to minimum financial standards and related reporting requirements set by such designated self-regulatory organization in its bylaws, rules, regulations or resolutions approved by the Commission pursuant to section 4f(b) of the Act and §1.52.

(ii) The minimum requirements of paragraph (a)(1)(iii) of this section shall not be applicable to an introducing broker which elects to meet the alternative adjusted net capital requirement for introducing brokers by operation pursuant to a guarantee agreement which meets the requirements set forth in §1.10(j). Such an introducing broker shall be deemed to meet the adjusted net capital requirement under this section so long as such agreement is binding and in full force and effect, and, if the introducing broker is also a securities broker or dealer, it maintains the amount of net capital required by Rule 15c3-1(a) of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

(3) No person applying for registration as a futures commission merchant or as an introducing broker shall be so registered unless such person affirmatively demonstrates to the satisfaction of the National Futures Association that it complies with the financial requirements of this section. Each registrant must be in compliance with this section at all times and must be able to demonstrate such compliance to the satisfaction of the Commission or the designated self-regulatory organization.

(4) A futures commission merchant who is not in compliance with this section, or is unable to demonstrate such compliance as required by paragraph (a)(3) of this section, or who cannot certify to the Commission immediately upon request and demonstrate with verifiable evidence that it has sufficient access to liquidity to continue operating as a going concern, must transfer all customer accounts and immediately cease doing business as a futures commission merchant until such time as the firm is able to demonstrate such compliance[:]; *Provided, however,* The registrant may trade for liquidation purposes only unless otherwise directed by the Commission and/or the designated self-regulatory organization[:]; *And, Provided further,* That if such registrant immediately demonstrates to the satisfaction of the Commission or the designated self-regulatory organization the ability to achieve compliance, the Commission or the designated self-regulatory organization may in its discretion allow such registrant up to a maximum of 10 business days in which to achieve compliance without having to transfer accounts and cease doing business as required above. Nothing in this paragraph [(a)(4)] shall be construed as preventing the Commission or the designated self-regulatory organization from taking action against a registrant for non-compliance with any of the provisions of this section.

(5) An introducing broker who is not in compliance with this section, or is unable to demonstrate such compliance as required by paragraph (a)(3) of this section, must immediately cease doing business as an introducing broker until such time as the registrant is able to demonstrate such compliance: *Provided, however,* That if such registrant immediately demonstrates to the satisfaction of the Commission or the designated self-regulatory organization the ability to achieve

compliance, the Commission or the designated self-regulatory organization may in its discretion allow such registrant up to a maximum of 10 business days in which to achieve compliance without having to cease doing business as required above. If the introducing broker is required to cease doing business in accordance with this paragraph (a)(5), the introducing broker must immediately notify each of its customers and the futures commission merchants carrying the account of each customer that it has ceased doing business. Nothing in this paragraph (a)(5) shall be construed as preventing the Commission or the designated self-regulatory organization from taking action against a registrant for non-compliance with any of the provisions of this section.

(b) For the purposes of this section:

(1) Where the applicant or registrant has an asset or liability which is defined in Securities Exchange Act Rule 15c3-1 (§240.15c3-1 of this title) the inclusion or exclusion of all or part of such asset or liability for the computation of adjusted net capital shall be in accordance with §240.15c3-1 of this title, unless specifically stated otherwise in this section.

(2) *Customer.* This term means a futures customer [(as defined in §1.3(k)), option customer (as defined in §1.3(jj) and in §32.1(c) of this chapter),] 1.3, a cleared over the counter customer [(as defined in [§1.17] paragraph (b)(10)]) of this section, and [includes a foreign futures, foreign options] a 30.7 customer [(as defined in §30.1(c) of this chapter)].

(3) *Proprietary account* means an account in which commodity futures, options or cleared over the counter derivative positions are carried on the books of the applicant or registrant for the applicant or registrant itself, or for general partners in the applicant or registrant.

(4) *Noncustomer account* means an account in which commodity futures, options or cleared over the counter derivative positions are carried on the books of the applicant or registrant which is either:

(i) An account that is not included in the definition of customer (as defined in §1.17(b)(2)) or proprietary account (as defined in §1.17(b)(3)), or

(ii) An account for a foreign-domiciled person trading futures or options on a foreign board of trade, and such account is a proprietary account as defined in §1.3(y) of this title, but is not a proprietary account as defined in §1.17(b)(3).

(5) *Clearing organization* means clearing organization (as defined in §1.3(d)) and includes a clearing organization of any board of trade.

(6) *Business day* means any day other than a Sunday, Saturday, or holiday.

(7) *Customer account.* This term means an account in which commodity futures, options or cleared over the counter derivative positions are carried on the books of the applicant or registrant which is [either:]

[(i) An] an account that is included in the definition of customer [(as defined in §1.17(b)(2)], or

(ii) An account for a foreign-domiciled person trading on a foreign board of trade, where such account for the foreign-domiciled person is not a proprietary account (as defined in §1.17(b)(3)) or a noncustomer account (as defined in §1.17(b)(4)(ii)).

(8) *Risk margin* for an account means the level of maintenance margin or performance bond required for the customer or noncustomer positions by the applicable exchanges or clearing

organizations, and, where margin or performance bond is required only for accounts at the clearing organization, for purposes of the FCM's risk-based capital calculations applying the same margin or performance bond requirements to customer and noncustomer positions in accounts carried by the FCM, subject to the following.

- (i) Risk margin does not include the equity component of short or long option positions maintained in an account;
- (ii) The maintenance margin or performance bond requirement associated with a long option position may be excluded from risk margin to the extent that the value of such long option position does not reduce the total risk maintenance or performance bond requirement of the account that holds the long option position;
- (iii) The risk margin for an account carried by a futures commission merchant which is not a member of the exchange or the clearing organization that requires collection of such margin should be calculated as if the futures commission merchant were such a member; and
- (iv) If a futures commission merchant does not possess sufficient information to determine what portion of an account's total margin requirement represents risk margin, all of the margin required by the exchange or the clearing organization that requires collection of such margin for that account, shall be treated as risk margin.

(9) *Cleared over the counter derivative positions* means "over the counter derivative instrument" (as defined in 12 U.S.C. 4421) positions of any person in accounts carried on the books of the futures commission merchant and cleared by any organization permitted to clear such instruments under the laws of the relevant jurisdiction.

(10) *Cleared over the counter customer* means any person that is not a proprietary person as defined in §1.3(y) and for whom the futures commission merchant carries on its books one or more accounts for the over the counter-cleared derivative positions of such person.

(c) Definitions: For the purposes of this section:

(1) *Net capital* means the amount by which current assets exceed liabilities. In determining "net capital":

- (i) Unrealized profits shall be added and unrealized losses shall be deducted in the accounts of the applicant or registrant, including unrealized profits and losses on fixed price commitments and forward contracts;
- (ii) All long and all short positions in commodity options which are traded on a contract market and listed security options shall be marked to their market value and all long and all short securities and commodities positions shall be marked to their market value;
- (iii) The value attributed to any commodity option which is not traded on a contract market shall be the difference between the option's strike price and the market value for the [physical] commodity or futures contract which is the subject of the option. In the case of a call commodity option which is not traded on a contract market, if the market value for the [physical] commodity or futures contract which is the subject of the option is less than the strike price of the option, it shall be given no value. In the case of a put commodity option which is not traded on a contract market, if the market value for the [physical] commodity or futures contract which is the subject of the option is more than the strike price of the option, it shall be given no value; and

(iv) The value attributed to any unlisted security option shall be the difference between the option's exercise value or striking value and the market value of the underlying security. In the case of an unlisted call, if the market value of the underlying security is less than the exercise value or striking value of such call, it shall be given no value; and, in the case of an unlisted put, if the market value of the underlying security is more than the exercise value or striking value of the unlisted put, it shall be given no value.

(2) The term *current assets* means cash and other assets or resources commonly identified as those which are reasonably expected to be realized in cash or sold during the next 12 months. "Current assets" shall:

(i) Exclude any unsecured commodity futures or option account containing a ledger balance and open trades, the combination of which liquidates to a deficit or containing a debit ledger balance only: *Provided, however,* Deficits or debit ledger balances in unsecured customers', non-customers', and proprietary accounts, which are the subject of calls for margin or other required deposits may be included in current assets until the close of business on the business day following the date on which such deficit or debit ledger balance originated providing that the account had timely satisfied, through the deposit of new funds, the previous day's debit or deficits, if any, in its entirety.

(ii) Exclude all unsecured receivables, advances and loans except for:

(A) Receivables resulting from the marketing of inventories commonly associated with the business activities of the applicant or registrant and advances on fixed price purchases commitments: *Provided,* Such receivables or advances are outstanding no longer than 3 calendar months from the date that they are accrued;

(B) Interest receivable, floor brokerage receivable, commissions receivable from other brokers or dealers (other than syndicate profits), mutual fund concessions receivable and management fees receivable from registered investment companies and commodity pools: *Provided,* Such receivables are outstanding no longer than thirty (30) days from the date they are due; and dividends receivable outstanding no longer than thirty (30) days from the payable date;

(C) Receivables from clearing organizations and securities clearing organizations;

(D) Receivables from registered futures commission merchants or brokers, resulting from commodity futures or option transactions, except those specifically excluded under paragraph (c)(2)(i) of this section;

(E) Insurance claims which arise from a reportable segment of the applicant's or registrant's overall business activities, as defined in generally accepted accounting principles, other than in the commodity futures, commodity option, security and security option segments of the applicant's or registrant's business activities which are not outstanding more than 3 calendar months after the date they are recorded as a receivable;

(F) All other insurance claims not subject to paragraph (c)(2)(ii)(E) of this section, which are not older than seven (7) business days from the date the loss giving rise to the claim is discovered; insurance claims which are not older than twenty (20) business days from the date the loss giving rise to the claim is discovered and which are covered by an opinion of outside counsel that the claim is valid and is covered by insurance policies presently in effect; insurance claims which are older than twenty (20) business days from the date the loss giving rise to the claim is discovered and which are covered by an opinion of outside counsel that the claim is valid and is covered by insurance policies presently in effect and which have been acknowledged in writing by the

insurance carrier as due and payable: *Provided*, Such claims are not outstanding longer than twenty (20) business days from the date they are so acknowledged by the carrier;

(iii) Exclude all prepaid expenses and deferred charges;

(iv) Exclude all inventories except for:

(A) Readily marketable spot commodities; or spot commodities which "adequately collateralize" indebtedness under paragraph (c)(7) of this section;

(B) Securities which are considered "readily marketable" (as defined in §240.15c3-1(c)(11) of this title) or which "adequately collateralize" indebtedness under paragraph (c)(7) of this section;

(C) Work in process and finished goods which result from the processing of commodities at market value;

(D) Raw materials at market value which will be combined with spot commodities to produce a finished processed commodity; and

(E) Inventories held for resale commonly associated with the business activities of the applicant or registrant;

(v) Include fixed assets and assets which otherwise would be considered noncurrent to the extent of any long-term debt adequately collateralized by assets acquired for use in the ordinary course of the trade or business of an applicant or registrant and any other long-term debt adequately collateralized by assets of the applicant or registrant if the sole recourse of the creditor for nonpayment of such liability is to such asset: *Provided*, Such liabilities are not excluded from liabilities in the computation of net capital under paragraph (c)(4)(vi) of this section;

(vi) Exclude all assets doubtful of collection or realization less any reserves established therefor;

(vii) Include, in the case of future income tax benefits arising as a result of unrealized losses, the amount of such benefits not exceeding the amount of income tax liabilities accrued on the books and records of the applicant or registrant, but only to the extent such benefits could have been applied to reduce accrued tax liabilities on the date of the capital computation, had the related unrealized losses been realized on that date;

(viii) Include guarantee deposits with clearing organizations and stock in clearing organizations to the extent of its margin value;

(ix) In the case of an introducing broker or an applicant for registration as an introducing broker, include 50 percent of the value of a guarantee or security deposit with a futures commission merchant which carries or intends to carry accounts for the customers of the introducing broker; and

(x) Exclude exchange memberships.

(3) A loan or advance or any other form of receivable shall not be considered "secured" for the purposes of paragraph (c)(2) of this section unless the following conditions exist:

(i) The receivable is secured by readily marketable collateral which is otherwise unencumbered and which can be readily converted into cash: *Provided, however*, That the receivable will be

considered secured only to the extent of the market value of such collateral after application of the percentage deductions specified in paragraph (c)(5) of this section; and

(ii)(A) The readily marketable collateral is in the possession or control of the applicant or registrant; or

(B) The applicant or registrant has a legally enforceable, written security agreement, signed by the debtor, and has a perfected security interest in the readily marketable collateral within the meaning of the laws of the State in which the readily marketable collateral is located.

(4) The term *liabilities* means the total money liabilities of an applicant or registrant arising in connection with any transaction whatsoever, including economic obligations of an applicant or registrant that are recognized and measured in conformity with generally accepted accounting principles. "Liabilities" also include certain deferred credits that are not obligations but that are recognized and measured in conformity with generally accepted accounting principles. For the purposes of computing "net capital", the term "liabilities":

(i) Excludes liabilities of an applicant or registrant which are subordinated to the claims of all general creditors of the applicant or registrant pursuant to a satisfactory subordination agreement, as defined in paragraph (h) of this section;

(ii) Excludes, in the case of a futures commission merchant, the amount of money, securities and property due to commodity futures or option customers which is held in segregated accounts in compliance with the requirements of the Act and these regulations: *Provided, however,* That such exclusion may be taken only if such money, securities and property held in segregated accounts have been excluded from current assets in computing net capital;

(iii) Includes, in the case of an applicant or registrant who is a sole proprietor, the excess of liabilities which have not been incurred in the course of business as a futures commission merchant or as an introducing broker over assets not used in the business;

(iv) Excludes the lesser of any deferred income tax liability related to the items in paragraphs (c)(4)(i) (A), (B), and (C) below, or the sum of paragraphs (c)(4)(i) (A), (B), and (C) below:

(A) The aggregate amount resulting from applying to the amount of the deductions computed in accordance with paragraph (c)(5) of this section the appropriate Federal and State tax rate(s) applicable to any unrealized gain on the asset on which the deduction was computed;

(B) Any deferred tax liability related to income accrued which is directly related to an asset otherwise deducted pursuant to this section;

(C) Any deferred tax liability related to unrealized appreciation in value of any asset(s) which has been otherwise excluded from current assets in accordance with the provisions of this section;

(v) Excludes any current tax liability related to income accrued which is directly related to an asset otherwise deducted pursuant to this section; and

(vi) Excludes liabilities which would be classified as long term in accordance with generally accepted accounting principles to the extent of the net book value of plant, property and equipment which is used in the ordinary course of any trade or business of the applicant or registrant which is a reportable segment of the applicant's or registrant's overall business activities, as defined in generally accepted accounting principles, other than in the commodity futures, commodity option, security and security option segments of the applicant's or registrant's business activities: *Provided,*

That such plant, property and equipment is not included in current assets pursuant to paragraph (c)(2)(v) of this section.

(5) The term *adjusted net capital* means net capital less:

(i) The amount by which any advances paid by the applicant or registrant on cash commodity contracts and used in computing net capital exceeds 95 percent of the market value of the commodities covered by such contracts;

(ii) In the case of all inventory, fixed price commitments and forward contracts, the applicable percentage of the net position specified below:

(A) Inventory which is currently registered as deliverable on a contract market and covered by an open futures contract or by a commodity option on a physical[.] commodity—No charge.

(B) Inventory which is covered by an open futures contract or commodity option.—5 percent of the market value.

(C) Inventory which is not covered.—20 percent of the market value.

(D) Inventory and forward contracts in those foreign currencies that are purchased or sold for future delivery on or subject to the rules of a contract market, and which are covered by an open futures contract.—No charge

(E) Inventory and forward contracts in euros, British pounds, Canadian dollars, Japanese yen, or Swiss francs, and which are not covered by an open futures contract or commodity option.—6 percent of the market value.

(F) Fixed price commitments (open purchases and sales) and forward contracts which are covered by an open futures contract or commodity option.—10 percent of the market value.

(G) Fixed price commitments (open purchases and sales) and forward contracts which are not covered by an open futures contract or commodity option.—20 percent of the market value.

(iii)—(iv) [Reserved]

(v) In the case of securities and obligations used by the applicant or registrant in computing net capital, and in the case of a futures commission merchant [with securities in segregation pursuant to section 4d(2) of the Act and the regulations in this chapter which were not] that invests funds deposited by futures customers[, the] as defined in §1.3, Cleared Swaps Customers as defined in §22.1 of this chapter, and 30.7 customers as defined in §30.1 of this chapter in securities as permitted investments under §1.25, the deductions specified in Rule 240.15c3-1(c)(2)(vi) or Rule 240.15c3-1(c)(2)(vii) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vi) and 17 CFR 240.15c3-1(c)(2)(vii)) ("securities haircuts"). Futures commission merchants that establish and enforce written policies and procedures to assess the credit risk of commercial paper, convertible debt instruments, or nonconvertible debt instruments in accordance with Rule 240.15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vi)) may apply the lower haircut percentages specified in Rule 240.15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vi)) ("securities haircuts") and 100 percent of the value of "nonmarketable securities" as specified in Rule 240.15c3-1(c)(2)(vii) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vii);]-1(c)(2)(vi) for such commercial paper, convertible debt instruments and nonconvertible debt instruments. Futures

commission merchants must maintain their written policies and procedures in accordance with §1.31;

(vi) In the case of securities options and/or other options for which a haircut has been specified for the option or for the underlying instrument in §240.15c3–1 appendix A of this title, the treatment specified in, or under, §240.15c3–1 appendix A, after effecting certain adjustments to net capital for listed and unlisted options as set forth in such appendix;

(vii) In the case of an applicant or registrant who has open contractual commitments, as hereinafter defined, the deductions specified in §240.15c3–1(c)(2)(viii) of this title;

(viii) In the case of a futures commission merchant, for undermargined customer commodity futures accounts and commodity option customer accounts the amount of funds required in each such account to meet maintenance margin requirements of the applicable board of trade or if there are no such maintenance margin requirements, clearing organization margin requirements applicable to such positions, after application of calls for margin or other required deposits which are outstanding [three] no more than one business [days or less] day. If there are no such maintenance margin requirements or clearing organization margin requirements, then the amount of funds required to provide margin equal to the amount necessary after application of calls for margin or other required deposits outstanding [three] no more than one business [days or less] day to restore original margin when the original margin has been depleted by 50 percent or more: *Provided*, To the extent a deficit is excluded from current assets in accordance with paragraph (c)(2)(i) of this section such amount shall not also be deducted under this paragraph [(c)(5)(viii)]. In the event that an owner of a customer account has deposited an asset other than cash to margin, guarantee or secure his account, the value attributable to such asset for purposes of this subparagraph shall be the lesser of (A) [the] The value attributable to the asset pursuant to the margin rules of the applicable board of trade, or (B) [the] The market value of the asset after application of the percentage deductions specified in [this] paragraph (c)(5) of this section;

(ix) In the case of a futures commission merchant, for undermargined commodity futures and commodity option noncustomer and omnibus accounts the amount of funds required in each such account to meet maintenance margin requirements of the applicable board of trade or if there are no such maintenance margin requirements, clearing organization margin requirements applicable to such positions, after application of calls for margin or other required deposits which are outstanding [two] no more than one business [days or less] day. If there are no such maintenance margin requirements or clearing organization margin requirements, then the amount of funds required to provide margin equal to the amount necessary after application of calls for margin or other required deposits outstanding [two] no more than one business [days or less] day to restore original margin when the original margin has been depleted by 50 percent or more: *Provided*, To the extent a deficit is excluded from current assets in accordance with paragraph (c)(2)(i) of this section such amount shall not also be deducted under this paragraph [(c)(5)(ix)]. In the event that an owner of a noncustomer or omnibus account has deposited an asset other than cash to margin, guarantee or secure his account the value attributable to such asset for purposes of this [subparagraph] paragraph shall be the lesser of [(A)] the value attributable to such asset pursuant to the margin rules of the applicable board of trade, or [(B)] the market value of such asset after application of the percentage deductions specified in [this] paragraph (c)(5) of this section;

(x) In the case of open futures contracts or cleared OTC derivative positions and granted (sold) commodity options held in proprietary accounts carried by the applicant or registrant which are not covered by a position held by the applicant or registrant or which are not the result of a “changer trade” made in accordance with the rules of a contract market:

(A) For an applicant or registrant which is a clearing member of a clearing organization for the positions cleared by such member, the applicable margin requirement of the applicable clearing organization;

(B) For an applicant or registrant which is a member of a self-regulatory organization 150 percent of the applicable maintenance margin requirement of the applicable board of trade, or clearing organization, whichever is greater;

(C) For all other applicants or registrants, 200 percent of the applicable maintenance margin requirements of the applicable board of trade or clearing organization, whichever is greater; or

(D) For open contracts or granted (sold) commodity options for which there are no applicable maintenance margin requirements, 200 percent of the applicable initial margin requirement: *Provided*, The equity in any such proprietary account shall reduce the deduction required by this paragraph (c)(5)(x) if such equity is not otherwise includable in adjusted net capital;

(xi) In the case of an applicant or registrant which is a purchaser of a commodity option not traded on a contract market which has value and such value is used to increase adjusted net capital, ten percent of the market value of the [physical] commodity or futures contract which is the subject of such option but in no event more than the value attributed to such option;

(xii) In the case of an applicant or registrant which is a purchaser of a commodity option which is traded on a contract market the same safety factor as if the applicant or registrant were the grantor of such option in accordance with paragraph (c)(5)(x) of this section, but in no event shall the safety factor be greater than the market value attributed to such option;

(xiii) Five percent of all unsecured receivables includable under paragraph (c)(2)(ii)(D) of this section used by the applicant or registrant in computing "net capital" and which are not due from:

(A) A registered futures commission merchant;

(B) A broker or dealer that is registered as such with the Securities and Exchange Commission; or

(C) A foreign broker that has been granted comparability relief pursuant to §30.10 of this chapter, *Provided, however*, that the amount of the unsecured receivable not subject to the five percent capital charge is no greater than 150 percent of the current amount required to maintain futures and [option] options positions in accounts with the foreign broker, or 100 percent of such greater amount required to maintain futures and option positions in the accounts at any time during the previous six-month period, and *Provided, that*, in the case of [customer funds] the foreign futures or foreign options secured amount, as §1.3(rr) defines such term, such account is treated in accordance with the special requirements of the applicable Commission order issued under §30.10 of this chapter.

(xiv) For securities brokers and dealers, all other deductions specified in §240.15c3–1 of this title.

(6) Election of alternative capital deductions that have received approval of Securities and Exchange Commission pursuant to §240.15c3–1(a)(7) of this title.

(i) Any futures commission merchant that is also registered with the Securities and Exchange Commission as a securities broker or dealer, and who also satisfies the other requirements of this paragraph (c)(6), may elect to compute its adjusted net capital using the alternative capital deductions that, under §240.15c3–1(a)(7) of this title, the Securities and Exchange Commission has approved by written order. To the extent that a futures commission merchant is permitted by the Securities and Exchange Commission to use alternative capital deductions for its unsecured receivables from over-the-counter transactions in derivatives, or for its proprietary positions in securities, forward contracts, or futures contracts, the futures commission merchant may use these same alternative capital deductions when computing its adjusted net capital, in lieu of the

deductions that would otherwise be required by paragraph (c)(2)(ii) of this section for its unsecured receivables from over-the-counter derivatives transactions; by paragraph (c)(5)(ii) of this section for its proprietary positions in forward contracts; by paragraph (c)(5)(v) of this section for its proprietary positions in securities; and by paragraph (c)(5)(x) of this section for its proprietary positions in futures contracts.

(ii) *Notifications of election or of changes to election.* (A) No election to use the alternative market risk and credit risk deductions referenced in paragraph (c)(6)(i) of this section shall be effective unless and until the futures commission merchant has filed with the Commission, addressed to the Director of the Division of [Clearing] Swap Dealer and Intermediary Oversight, a notice that is to include a copy of the approval order of the Securities and Exchange Commission referenced in paragraph (c)(6)(i) of this section, and to include also a statement that identifies the amount of tentative net capital below which the futures commission merchant is required to provide notice to the Securities and Exchange Commission, and which also provides the following information: a list of the categories of positions that the futures commission merchant holds in its proprietary accounts, and, for each such category, a description of the methods that the futures commission merchant will use to calculate its deductions for market risk and credit risk, and also, if calculated separately, deductions for specific risk; a description of the value at risk (VaR) models to be used for its market risk and credit risk deductions, and an overview of the integration of the models into the internal risk management control system of the futures commission merchant; a description of how the futures commission merchant will calculate current exposure and maximum potential exposure for its deductions for credit risk; a description of how the futures commission merchant will determine internal credit ratings of counterparties and internal credit risk weights of counterparties, if applicable; and a description of the estimated effect of the alternative market risk and credit risk deductions on the amounts reported by the futures commission merchant as net capital and adjusted net capital.

(B) A futures commission merchant must also, upon the request of the Commission at any time, supplement the statement described in paragraph (c)(6)(ii)(A) of this section, by providing any other explanatory information regarding the computation of its alternative market risk and credit risk deductions as the Commission may require at its discretion.

(C) A futures commission merchant must also file the following supplemental notices with the Director of the Division and Clearing and Intermediary Oversight:

(1) A notice advising that the Securities and Exchange Commission has imposed additional or revised conditions for the approval evidenced by the order referenced in paragraph (c)(6)(i) of this section, and which describes the new or revised conditions in full, and

(2) A notice which attaches a copy of any approval by the Securities and Exchange Commission of amendments that a futures commission merchant has requested for its application, filed under 17 CFR 240.15c3-1e, to use alternative market risk and credit risk deductions approved by the Securities and Exchange Commission.

(D) A futures commission merchant may voluntarily change its election to use the alternative market risk and credit risk deductions referenced in paragraph (c)(6)(i) of this section, by filing with the Director of the Division of [Clearing] Swap Dealer and Intermediary Oversight a written notice specifying a future date as of which it will no longer use the alternative market risk and credit risk deductions, and will instead compute such deductions in accordance with the requirements otherwise applicable under paragraph (c)(2)(ii) of this section for unsecured receivables from over-the-counter derivatives transactions; by paragraph (c)(5)(ii) of this section for proprietary positions in forward contracts; by paragraph (c)(5)(v) of this section for proprietary positions in securities; and by paragraph (c)(5)(x) of this section for proprietary positions in futures contracts.

(iii) *Conditions under which election terminated.* A futures commission merchant may no longer elect to use the alternative market risk and credit risk deductions referenced in paragraph (c)(6)(i) of this section, and shall instead compute the deductions otherwise required under paragraph (c)(2)(ii) of this section for unsecured receivables from over-the-counter derivatives transactions; by paragraph (c)(5)(ii) of this section for proprietary positions in forward contracts; by paragraph (c)(5)(v) of this section for proprietary positions in securities; and by paragraph (c)(5)(x) of this section for proprietary positions in futures contracts, upon the occurrence of any of the following:

- (A) The Securities and Exchange Commission revokes its approval of the market risk and credit risk deductions for such futures commission merchant;
- (B) A futures commission merchant fails to come into compliance with its filing requirements under this paragraph (c)(6), after having received from the Director of the Division of [Clearing] Swap Dealer and Intermediary Oversight written notification that the firm is not in compliance with its filing requirements, and must cease using alternative capital deductions permitted under this paragraph (c)(6) if it has not come into compliance by a date specified in the notice; or
- (C) The Commission by written order finds that permitting the futures commission merchant to continue to use such alternative market risk and credit risk deductions is no longer necessary or appropriate for the protection of customers of the futures commission merchant or of the integrity of the futures or options markets.

(iv) *Additional filing requirements.* Any futures commission merchant that elects to use the alternative market risk and credit risk deductions referenced in paragraph (c)(6)(i) of this section must file with the Commission, in addition to the filings required by paragraph (c)(6)(ii) of this section, copies of any and all of the following documents, at such time as the originals are filed with the Securities and Exchange Commission:

- (A) Information that the futures commission merchant files on a monthly basis with its designated examining authority or the Securities and Exchange Commission, whether by way of schedules to its FOCUS reports or by other filings, in satisfaction of 17 CFR 240.17a-5(a)(5)(i);
- (B) The quarterly reports required by 17 CFR 240.17a-5(a)(5)(ii);
- (C) The supplemental annual filings as required by 17 CFR 240.17a-5(k);
- (D) Any notification to the Securities and Exchange Commission or the futures commission merchant's designated examining authority of planned withdrawals of excess net capital; and
- (E) Any notification that the futures commission merchant is required to file with the Securities and Exchange Commission when its tentative net capital is below an amount specified by the Securities and Exchange Commission.

(7) *Liabilities* are "adequately collateralized" when, pursuant to a legally enforceable written instrument, such liabilities are secured by identified assets that are otherwise unencumbered and the market value of which exceeds the amount of such liabilities.

(8) The term *contractual commitments* shall include underwriting, when issued, when distributed, and delayed delivery contracts; and the writing or endorsement of security puts and calls and combinations thereof; but shall not include uncleared regular way purchases and sales of securities. A series of contracts of purchase or sale of the same security, conditioned, if at all, only upon issuance, may be treated as an individual commitment.

(d) Each applicant or registrant shall have equity capital (inclusive of satisfactory subordination agreements which qualify under this paragraph (d) as equity capital) of not less than 30 percent of the debt-equity total, provided, an applicant or registrant may be exempted from the provisions of this paragraph (d) for a period not to exceed 90 days or for such longer period which the Commission may, upon application of the applicant or registrant, grant in the public interest or for the protection of investors. For the purposes of this paragraph (d):

(1) Equity capital means a satisfactory subordination agreement entered into by a partner or stockholder or limited liability company member which has an initial term of at least 3 years and has a remaining term of not less than 12 months if:

(i) It does not have any of the provisions for accelerated maturity provided for by paragraphs (h)(2)(ix)(A), (x)(A), or (x)(B) of this section, or the provisions allowing for special prepayment provided for by paragraph (h)(2)(vii)(B) of this section, and is maintained as capital subject to the provisions restricting the withdrawal thereof required by paragraph (e) of this section; or

(ii) The partnership agreement provides that capital contributed pursuant to a satisfactory subordination agreement as defined in paragraph (h) of this section shall in all respects be partnership capital subject to the provisions restricting the withdrawal thereof required by paragraph (e) of this section, and

(A) In the case of a corporation, the sum of its par or stated value of capital stock, paid-in capital in excess of par, retained earnings, unrealized profit and loss, and other capital accounts.

(B) In the case of a partnership, the sum of its capital accounts of partners (inclusive of such partners' commodities, options and securities accounts subject to the provisions of paragraph (e) of this section), and unrealized profit and loss.

(C) In the case of a sole proprietorship, the sum of its capital accounts of the sole proprietorship and unrealized profit and loss.

(D) In the case of a limited liability company, the sum of its capital accounts of limited liability company members, and unrealized profit and loss.

(2) Debt-equity total means equity capital as defined in paragraph (d)(1) of this section plus the outstanding principal amount of satisfactory subordination agreements.

(e) No equity capital of the applicant or registrant or a subsidiary's or affiliate's equity capital consolidated pursuant to paragraph (f) of this section, whether in the form of capital contributions by partners (including amounts in the commodities, options and securities trading accounts of partners which are treated as equity capital but excluding amounts in such trading accounts which are not equity capital and excluding balances in limited partners' capital accounts in excess of their stated capital contributions), par or stated value of capital stock, paid-in capital in excess of par or stated value, retained earnings or other capital accounts, may be withdrawn by action of a stockholder or partner or limited liability company member or by redemption or repurchase of shares of stock by any of the consolidated entities or through the payment of dividends or any similar distribution, nor may any unsecured advance or loan be made to a stockholder, partner, sole proprietor, limited liability company member, or employee if, after giving effect thereto and to any other such withdrawals, advances, or loans and any payments of payment obligations (as defined in paragraph (h) of this section) under satisfactory subordination agreements and any payments of liabilities excluded pursuant to paragraph (c)(4)(vi) of this section which are scheduled to occur within six months following such withdrawal, advance or loan:

(1) Either adjusted net capital of any of the consolidated entities would be less than the greatest of:

- (i) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;
  - (ii) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;
  - (iii) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or
  - (iv) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1(e) of the Securities and Exchange Commission (17 CFR 240.15c3-1(e)); or
- (2) In the case of any applicant or registrant included within such consolidation, if equity capital of the applicant or registrant (inclusive of satisfactory subordination agreements which qualify as equity under paragraph (d) of this section) would be less than 30 percent of the required debt-equity total as defined in paragraph (d) of this section.

*Provided*, That this paragraph (e) shall not preclude an applicant or registrant from making required tax payments or preclude the payment to partners of reasonable compensation. The Commission may, upon application of the applicant or registrant, grant relief from this paragraph (e) if the Commission deems it to be in the public interest or for the protection of nonproprietary accounts.

(f)(1) Every applicant or registrant, in computing its net capital pursuant to this section must, subject to the provisions of paragraphs (f)(2) and (f)(4) of this section, consolidate in a single computation, assets and liabilities of any subsidiary or affiliate for which it guarantees, endorses, or assumes directly or indirectly the obligations or liabilities. The assets and liabilities of a subsidiary or affiliate whose liabilities and obligations have not been guaranteed, endorsed, or assumed directly or indirectly by the applicant or registrant may also be so consolidated if an opinion of counsel is obtained as provided for in paragraph (f)(2) of this section.

(2)(i) If the consolidation, provided for in paragraph (f)(1) of this section, of any such subsidiary or affiliate results in the increase of the applicant's or registrant's adjusted net capital or decreases the minimum adjusted net capital requirement, and an opinion of counsel called for in paragraph (f)(2)(ii) of this section has not been obtained, such benefits shall not be recognized in the applicant's or registrant's computation required by this section.

(ii) Except as provided for in paragraph (f)(2)(i) of this section, consolidation shall be permitted with respect to any subsidiaries or affiliates which are majority owned and controlled by the applicant or registrant, and for which the applicant can demonstrate to the satisfaction of the National Futures Association, or for which the registrant can demonstrate to the satisfaction of the Commission and the designated self-regulatory organization, if any, by an opinion of counsel, that the net asset values or the portion thereof related to the parent's ownership interest in the subsidiary or affiliate, may be caused by the applicant or registrant or an appointed trustee to be distributed to the applicant or registrant within 30 calendar days. Such opinion must also set forth the actions necessary to cause such a distribution to be made, identify the parties having the authority to take such actions, identify and describe the rights of other parties or classes of parties, including but not limited to customers, general creditors, subordinated lenders, minority shareholders, employees, litigants, and governmental or regulatory authorities, who may delay or prevent such a distribution and such other assurances as the National Futures Association, the Commission or the designated self-regulatory organization by rule or interpretation may require. Such opinion must be current and periodically renewed in connection with the applicant's or registrant's annual audit pursuant to §1.10 or upon any material change in circumstances.

(3) In preparing a consolidated computation of adjusted net capital pursuant to this section, the following minimum and non-exclusive requirements shall be observed;

(i) Consolidated adjusted net capital shall be reduced by the estimated amount of any tax reasonably anticipated to be incurred upon distribution of the assets of the subsidiary or affiliate.

(ii) Liabilities of a consolidated subsidiary or affiliate which are subordinated to the claims of present and future creditors pursuant to a satisfactory subordination agreement shall be deducted from consolidated adjusted net capital unless such subordination extends also to the claims of present or future creditors of the parent applicant or registrant and all consolidated subsidiaries.

(iii) Subordinated liabilities of a consolidated subsidiary or affiliate which are consolidated in accordance with paragraph (f)(3)(ii) of this section may not be prepaid, repaid, or accelerated if any of the entities included in such consolidation would otherwise be unable to comply with the provisions of paragraph (h) of this section.

(iv) Each applicant or registrant included within the consolidation shall at all times be in compliance with the adjusted net capital requirement to which it is subject.

(4) No applicant or registrant shall guarantee, endorse, or assume directly or indirectly any obligation or liability of a subsidiary or affiliate unless the obligation or liability is reflected in the computation of adjusted net capital pursuant to this section except as provided in paragraph (f)(2)(i) of this section.

(g)(1) The Commission may by order restrict, for a period up to twenty business days, any withdrawal by a futures commission merchant of equity capital, or any unsecured advance or loan to a stockholder, partner, limited liability company member, sole proprietor, employee or affiliate, if:

(i) Such withdrawal, advance or loan would cause, when aggregated with all other withdrawals, advances or loans during a 30 calendar day period from the futures commission merchant or a subsidiary or affiliate of the futures commission merchant consolidated pursuant to §1.17(f) (or 17 CFR 240.15c3-1e), a net reduction in excess adjusted net capital (or, if the futures commission merchant is qualified to use the filing option available under §1.10(h), excess net capital as defined in the rules of the Securities and Exchange Commission) of 30 percent or more, and

(ii) The Commission, based on the facts and information available, concludes that any such withdrawal, advance or loan may be detrimental to the financial integrity of the futures commission merchant, or may unduly jeopardize its ability to meet customer obligations or other liabilities that may cause a significant impact on the markets.

(2) The futures commission merchant may file with the Secretary of the Commission a written petition to request rescission of the order issued under paragraph (g)(1) of this section. The petition filed by the futures commission merchant must specify the facts and circumstances supporting its request for rescission. The Commission shall respond in writing to deny the futures commission merchant's petition for rescission, or, if the Commission determines that the order issued under paragraph (g)(1) of this section should not remain in effect, the order shall be rescinded.

(h) The term *satisfactory subordination agreement* ("subordination agreement") means an agreement which contains the minimum and nonexclusive requirements set forth below.

(1) Certain definitions for purposes of this section:

(i) A subordination agreement may be either a subordinated loan agreement or a secured demand note agreement.

(ii) The term *subordinated loan agreement* means the agreement or agreements evidencing or governing a subordinated borrowing of cash.

(iii) The term "collateral value" of any securities pledged to secure a secured demand note means the market value of such securities after giving effect to the percentage deductions specified in Rule 240.15c3–1d(a)(2)(iii) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(a)(2)(iii)).

(iv) The term *payment obligation* means the obligation of an applicant or registrant in respect to any subordination agreement:

(A) To repay cash loaned to the applicant or registrant pursuant to a subordinated loan agreement; or

(B) To return a secured demand note contributed to the applicant or registrant or to reduce the unpaid principal amount thereof and to return cash or securities pledged as collateral to secure the secured demand note; and (C) "payment" shall mean the performance by an applicant or registrant of a payment obligation.

(v)(A) The term *secured demand note agreement* means an agreement (including the related secured demand note) evidencing or governing the contribution of a secured demand note to an applicant or registrant and the pledge of securities and/or cash with the applicant or registrant as collateral to secure payment of such secured demand note. The secured demand note agreement may provide that neither the lender, his heirs, executors, administrators, or assigns shall be personally liable on such note and that in the event of default the applicant or registrant shall look for payment of such note solely to the collateral then pledged to secure the same.

(B) The secured demand note shall be a promissory note executed by the lender and shall be payable on the demand of the applicant or registrant to which it is contributed: *Provided, however,* That the making of such demand may be conditioned upon the occurrence of any of certain events which are acceptable to the designated self-regulatory organization and the Commission.

(C) If such note is not paid upon presentment and demand as provided for therein, the applicant or registrant shall have the right to liquidate all or any part of the securities then pledged as collateral to secure payment of the same and to apply the net proceeds of such liquidation, together with any cash then included in the collateral, in payment of such note. Subject to the prior rights of the applicant or registrant as pledgee, the lender, as defined in paragraph (h)(i)(v)(F) of this section may retain ownership of the collateral and have the benefit of any increases and bear the risks of any decreases in the value of the collateral and may retain the right to vote securities contained within the collateral and any right to income therefrom or distributions thereon, except the applicant or registrant shall have the right to receive and hold as pledgee all dividends payable in securities and all partial and complete liquidating dividends.

(D) Subject to the prior rights of the applicant or registrant as pledgee, the lender may have the right to direct the sale of any securities included in the collateral, to direct the purchase of securities with any cash included therein, to withdraw excess collateral or to substitute cash or other securities as collateral: *Provided,* That the net proceeds of any such sale and the cash so substituted and the securities so purchased or substituted are held by the applicant or registrant as pledgee, and are included within the collateral to secure payment of the secured demand note: *And provided further,* That no such transaction shall be permitted, if, after giving effect thereto, the sum of the amount of any cash, plus the collateral value of the securities, then pledged as collateral to

secure the secured demand note would be less than the unpaid principal amount of the secured demand note.

(E) Upon payment by the lender, as distinguished from a reduction by the lender which is provided for in paragraph (h)(2)(vi)(C) of this section or reduction by the applicant or registrant as provided for in paragraph (h)(2)(vii) of this section, of all or any part of the unpaid principal amount of the secured demand note, the applicant or registrant shall issue to the lender a subordinated loan agreement in the amount of such payment (or in the case of an applicant or registrant that is a partnership, credit a capital account of the lender), or issue preferred or common stock of the applicant or registrant in the amount of such payment, or any combination of the foregoing, as provided for in the secured demand note agreement.

(F) The term *lender* means the person who lends cash to an applicant or registrant pursuant to a subordinated loan agreement and the person who contributes a secured demand note to an applicant or registrant pursuant to a secured demand note agreement.

(2) Minimum requirements for subordination agreements:

(i) Subject to paragraph (h)(1) of this section, a subordination agreement shall mean a written agreement between the applicant or registrant and the lender, which:

(A) Has a minimum term of 1 year, except for temporary subordination agreements provided for in paragraph (h)(3)(v) of this section, and

(B) Is a valid and binding obligation enforceable in accordance with its terms (subject as to enforcement to applicable bankruptcy, insolvency, reorganization, moratorium, and other similar laws) against the applicant or registrant and the lender and their respective heirs, executors, administrators, successors, and assigns.

(ii) *Specific amount.* All subordination agreements shall be for a specific dollar amount which shall not be reduced for the duration of the agreement except by installments as specifically provided for therein and except as otherwise provided in this paragraph (h)(2) of this section.

(iii) *Effective subordination.* The subordination agreement shall effectively subordinate any right of the lender to receive any payment with respect thereto, together with accrued interest or compensation, to the prior payment or provision for payment in full of all claims of all present and future creditors of the applicant or registrant arising out of any matter occurring prior to the date on which the related payment obligation matures, except for claims which are the subject of subordination agreements which rank on the same priority as or junior to the claim of the lender under such subordination agreements.

(iv) *Proceeds of subordinated loan agreements.* The subordinated loan agreement shall provide that the cash proceeds thereof shall be used and dealt with by the applicant or registrant as part of its capital and shall be subject to the risks of the business.

(v) *Certain rights of the borrower.* The subordination agreement shall provide that the applicant or registrant shall have the right to:

(A) Deposit any cash proceeds of a subordinated loan agreement and any cash pledged as collateral to secure a secured demand note in an account or accounts in its own name in any bank or trust company;

(B) Pledge, repledge, hypothecate and rehypothecate, any or all of the securities pledged as collateral to secure a secured demand note, without notice, separately or in common with other securities or property for the purpose of securing any indebtedness of the applicant or registrant; and

(C) Lend to itself or others any or all of the securities and cash pledged as collateral to secure a secured demand note.

(vi) *Collateral for secured demand notes.* Only cash and securities which are fully paid for and which may be publicly offered or sold without registration under the Securities Act of 1933, and the offer, sale, and transfer of which are not otherwise restricted, may be pledged as collateral to secure a secured demand note. The secured demand note agreement shall provide that if at any time the sum of the amount of any cash, plus the collateral value of any securities, then pledged as collateral to secure the secured demand note is less than the unpaid principal amount of the secured demand note, the applicant or registrant must immediately transmit written notice to that effect to the lender. The secured demand note agreement shall also provide that if the borrower is an applicant, such notice must also be transmitted immediately to the National Futures Association, and if the borrower is a registrant, such notice must also be transmitted immediately to the designated self-regulatory organization, if any, and the Commission. The secured demand note agreement shall also require that following such transmittal:

(A) The lender, prior to noon of the business day next succeeding the transmittal of such notice, may pledge as collateral additional cash or securities sufficient, after giving effect to such pledge, to bring the sum of the amount of any cash plus the collateral value of any securities, then pledged as collateral to secure the secured demand note, up to an amount not less than the unpaid principal amount of the secured demand note; and

(B) Unless additional cash or securities are pledged by the lender as provided in paragraph (h)(2)(vi)(A) above, the applicant or registrant at noon on the business day next succeeding the transmittal of notice to the lender must commence sale, for the account of the lender, of such of the securities then pledged as collateral to secure the secured demand note and apply so much of the net proceeds thereof, together with such of the cash then pledged as collateral to secure the secured demand note as may be necessary to eliminate the unpaid principal amount of the secured demand note: *Provided, however,* That the unpaid principal amount of the secured demand note need not be reduced below the sum of the amount of any remaining cash, plus the collateral value of the remaining securities, then pledged as collateral to secure the secured demand note. The applicant or registrant may not purchase for its own account any securities subject to such a sale; and

(C) The secured demand note agreement may also provide that, in lieu of the procedures specified in the provisions required by paragraph (h)(2)(vi)(B) of this section, the lender, with the prior written consent of the applicant and the National Futures Association, or with the prior written consent of the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory organization, the Commission, may reduce the unpaid principal amount of the secured demand note: *Provided,* That after giving effect to such reduction the adjusted net capital of the applicant or registrant would not be less than the greatest of:

(1) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

(2) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

( 3 ) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

( 4 ) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(b)(6)(iii) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(b)(6)(iii)): *Provided, further,* That no single secured demand note shall be permitted to be reduced by more than 15 percent of its original principal amount and after such reduction no excess collateral may be withdrawn.

(vii) *Permissive prepayments and special prepayments.* (A) An applicant or registrant at its option, but not at the option of the lender, may, if the subordination agreement so provides, make a payment of all or any portion of the payment obligation thereunder prior to the scheduled maturity date of such payment obligation (hereinafter referred to as a "prepayment"), but in no event may any prepayment be made before the expiration of one year from the date such subordination agreement became effective: *Provided, however,* That the foregoing restriction shall not apply to temporary subordination agreements which comply with the provisions of paragraph (h)(3)(v) of this section nor shall it apply to "special prepayments" made in accordance with the provisions of paragraph (h)(2)(vii)(B) of this section. No prepayment shall be made if, after giving effect thereto (and to all payments of payment obligations under any other subordination agreements then outstanding, the maturity or accelerated maturities of which are scheduled to fall due within six months after the date such prepayment is to occur pursuant to this provision, or on or prior to the date on which the payment obligation in respect to such prepayment is scheduled to mature disregarding this provision, whichever date is earlier) without reference to any projected profit or loss of the applicant or registrant, the adjusted net capital of the applicant or registrant is less than the greatest of:

( 1 ) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

( 2 ) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

( 3 ) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

( 4 ) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(b)(7) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(b)(7)).

(B) An applicant or registrant at its option, but not at the option of the lender, may, if the subordination agreement so provides, make a payment at any time of all or any portion of the payment obligation thereunder prior to the scheduled maturity date of such payment obligation (hereinafter referred to as a "special prepayment"). No special prepayment shall be made if, after giving effect thereto (and to all payments of payment obligations under any other subordination agreements then outstanding, the maturity or accelerated maturities of which are scheduled to fall due within six months after the date such special prepayment is to occur pursuant to this provision, or on or prior to the date on which the payment obligation in respect to such special prepayment is scheduled to mature disregarding this provision, whichever date is earlier) without reference to any projected profit or loss of the applicant or registrant, the adjusted net capital of the applicant or registrant is less than the greatest of:

( 1 ) 200 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

( 2 ) For a futures commission merchant or applicant therefor, 125 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

( 3 ) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

( 4 ) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(c)(5)(ii) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(c)(5)(ii)): *Provided, however,* That no special prepayment shall be made if pre-tax losses during the latest three-month period were greater than 15 percent of current excess adjusted net capital.

(C)( 1 ) Notwithstanding the provisions of paragraphs (h)(2)(vii)(A) and (h)(2)(vii)(B) of this section, in the case of an applicant, no prepayment or special prepayment shall occur without the prior written approval of the National Futures Association; in the case of a registrant, no prepayment or special prepayment shall occur without the prior written approval of the designated self-regulatory organization, if any, or of the Commission if the registrant is not a member of a self-regulatory organization.

( 2 ) A registrant may make a prepayment or special prepayment without the prior written approval of the designated self-regulatory organization: *Provided, That the registrant:* Is a securities broker or dealer registered with the Securities and Exchange Commission; files a request to make a prepayment or special prepayment with its applicable securities designated examining authority, as defined in Rule 15c3-1(c)(12) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(12)), in the form and manner prescribed by the designated examining authority; files a copy of the prepayment request or special prepayment request with the designated self-regulatory organization at the time it files such request with the designated examining authority in the form and manner prescribed by the designated self-regulatory organization; and files a copy of the designated examining authority's approval of the prepayment or special prepayment with the designated self-regulatory organization immediately upon receipt of such approval. The approval of the prepayment or special prepayment by the designated examining authority will be deemed approval by the designated self-regulatory organization, unless the designated self-regulatory organization notifies the registrant that the designated examining authority's approval shall not constitute designated self-regulatory organization approval.

( 3 ) The designated self-regulatory organization shall immediately provide the Commission with a copy of any notice of approval issued where the requested prepayment or special prepayment will result in the reduction of the registrant's net capital by 20 percent or more or the registrant's excess adjusted net capital by 30 percent or more.

(viii) *Suspended repayment.* (A) The payment obligation of the applicant or registrant in respect of any subordination agreement shall be suspended and shall not mature if, after giving effect to payment of such payment obligation (and to all payments of payment obligations of the applicant or registrant under any other subordination agreement(s) then outstanding which are scheduled to mature on or before such payment obligation), the adjusted net capital of the applicant or registrant would be less than the greatest of:

( 1 ) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;

( 2 ) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;

(3) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

(4) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(b)(8)(i) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(b)(8)(i)): *Provided*, That the subordination agreement may provide that if the payment obligation of the applicant or registrant thereunder does not mature and is suspended as a result of the requirement of this paragraph (h)(2)(viii) for a period of not less than six months, the applicant or registrant shall then commence the rapid and orderly liquidation of its business, but the right of the lender to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of this section.

(B) [Reserved]

(ix) *Accelerated maturity. Obligation to repay to remain subordinate:*

(A) Subject to the provisions of paragraph (h)(2)(viii) of this section, a subordination agreement may provide that the lender may, upon prior written notice to the applicant and the National Futures Association, or upon prior written notice to the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory organization, the Commission, given not earlier than six months after the effective date of such subordination agreement, accelerate the date on which the payment obligation of the borrower, together with accrued interest or compensation, is scheduled to mature to a date not earlier than six months after giving of such notice, but the right of the lender to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of this paragraph (h)(2) of this section.

(B) Notwithstanding the provisions of paragraph (h)(2)(viii) of this section, the payment obligation of the applicant or registrant with respect to a subordination agreement, together with accrued interest and compensation, shall mature in the event of any receivership, insolvency, liquidation pursuant to the Securities Investor Protection Act of 1970 or otherwise, bankruptcy, assignment for the benefit of creditors, reorganization whether or not pursuant to the bankruptcy laws, or any other marshalling of the assets and liabilities of the applicant or registrant, but the right of the lender to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of paragraph (h)(2) of this section.

(x) *Accelerated maturity of subordination agreements on event of default and event of acceleration. Obligation to repay to remain subordinate:*

(A) A subordination agreement may provide that the lender may, upon prior written notice to the applicant and the National Futures Association, or upon prior written notice to the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory organization, the Commission, of the occurrence of any event of acceleration (as hereinafter defined) given no sooner than six months after the effective date of such subordination agreement, accelerate the date on which the payment obligation of the applicant or registrant, together with accrued interest or compensation, is scheduled to mature, to the last business day of a calendar month which is not less than six months after notice of acceleration is received by the applicant and by the National Futures Association, or by the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory organization, the Commission. Any subordination agreement containing such events of acceleration may also provide that, if upon such accelerated maturity date the payment obligation of the applicant or registrant is suspended as required by paragraph (h)(2)(viii) of this section and liquidation of the applicant or registrant has not commenced on or prior to such accelerated maturity date, notwithstanding paragraph (h)(2)(viii) of this section, the payment obligation of the

applicant or registrant with respect to such subordination agreement shall mature on the day immediately following such accelerated maturity date and in any such event the payment obligations of the applicant or registrant with respect to all other subordination agreements then outstanding shall also mature at the same time but the rights of the respective lenders to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of paragraph (h)(2) of this section. Events of acceleration which may be included in a subordination agreement complying with this paragraph (h)(2)(x) of this section shall be limited to:

- ( 1 ) Failure to pay interest or any installment of principal on a subordination agreement as scheduled;
- ( 2 ) Failure to pay when due other money obligations of a specified material amount;
- ( 3 ) Discovery that any material, specified representation or warranty of the applicant or registrant which is included in the subordination agreement and on which the subordination agreement was based or continued was inaccurate in a material respect at the time made;
- ( 4 ) Any specified and clearly measurable event which is included in the subordination agreement and which the lender and the applicant or registrant agree, (a) is a significant indication that the financial position of the applicant or registrant has changed materially and adversely from agreed upon specified norms; or (b) could materially and adversely affect the ability of the applicant or registrant to conduct its business as conducted on the date the subordination agreement was made; or (c) is a significant change in the senior management of the applicant or registrant or in the general business conducted by the applicant or registrant from that which obtained on the date the subordination agreement became effective;
- ( 5 ) Any continued failure to perform agreed covenants included in the subordination agreement relating to the conduct of the business of the applicant or registrant or relating to the maintenance and reporting of its financial position; and

(B) Notwithstanding the provisions of paragraph (h)(2)(viii) of this section, a subordination agreement may provide that, if liquidation of the business of the applicant or registrant has not already commenced, the payment obligation of the applicant or registrant shall mature, together with accrued interest or compensation, upon the occurrence of an event of default (as hereinafter defined). Such agreement may also provide that, if liquidation of the business of the applicant or registrant has not already commenced, the rapid and orderly liquidation of the business of the applicant or registrant shall then commence upon the happening of an event of default. Any subordination agreement which so provides for maturity of the payment obligation upon the occurrence of an event of default shall also provide that the date on which such event of default occurs shall, if liquidation of the applicant or registrant has not already commenced, be the date on which the payment obligation of the applicant or registrant with respect to all other subordination agreements then outstanding shall mature but the rights of the respective lenders to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of paragraph (h)(2) of this section. Events of default which may be included in a subordination agreement shall be limited to:

- ( 1 ) The making of an application by the Securities Investor Protection Corporation for a decree adjudicating that customers of the applicant or registrant are in need of protection under the Securities Investor Protection Act of 1970 and the failure of the applicant or registrant to obtain the dismissal of such application within 30 days;
- ( 2 ) Failure to meet the minimum capital requirements of the designated self-regulatory organization, or of the Commission, throughout a period of 15 consecutive business days, commencing on the day the borrower first determines and notifies the designated self-regulatory

organization, if any, of which he is a member and the Commission, in the case of a registrant, or the National Futures Association, in the case of an applicant, or commencing on the day any self-regulatory organization, the Commission or the National Futures Association first determines and notifies the applicant or registrant of such fact;

- (3) The Commission shall revoke the registration of the applicant or registrant;
  - (4) The self-regulatory organization shall suspend (and not reinstate within 10 days) or revoke the applicant or registrant's status as a member thereof;
  - (5) Any receivership, insolvency, liquidation pursuant to the Securities Investor Protection Act of 1970 or otherwise, bankruptcy, assignment for the benefit of creditors, reorganization whether or not pursuant to bankruptcy laws, or any other marshalling of the assets and liabilities of the applicant or registrant. A subordination agreement which contains any of the provisions permitted by this subparagraph (2)(x) shall not contain the provision otherwise permitted by paragraph (h)(2)(ix)(A) of this section.
- (3) *Miscellaneous provisions*— (i) *Prohibited cancellation*. The subordination agreement shall not be subject to cancellation by either party; no payment shall be made with respect thereto and the agreement shall not be terminated, rescinded or modified by mutual consent or otherwise if the effect thereof would be inconsistent with the requirements of paragraph (h) of this section.
- (ii) *Notice of maturity or accelerated maturity*. Every applicant or registrant shall immediately notify the National Futures Association, and the registrant shall immediately notify the designated self-regulatory organization, if any, and the Commission if, after giving effect to all payments of payment obligations under subordination agreements then outstanding which are then due or mature within the following six months without reference to any projected profit or loss of the applicant or registrant, its adjusted net capital would be less than:
- (A) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;
  - (B) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;
  - (C) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or
  - (D) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(c)(2) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(c)(2)).
- (iii) *Certain legends*. If all the provisions of a satisfactory subordination agreement do not appear in a single instrument, then the debenture or other evidence of indebtedness shall bear on its face an appropriate legend stating that it is issued subject to the provisions of a satisfactory subordination agreement which shall be adequately referred to and incorporated by reference.
- (iv) *Legal title to securities*. All securities pledged as collateral to secure a secured demand note must be in bearer form, or registered in the name of the applicant or registrant or the name of its nominee or custodian.
- (v) *Temporary subordinations*. To enable an applicant or registrant to participate as an underwriter of securities or undertake other extraordinary activities and remain in compliance with the adjusted

net capital requirements of this section, an applicant or registrant shall be permitted, on no more than three occasions in any 12-month period, to enter into a subordination agreement on a temporary basis which has a stated term of no more than 45 days from the date the subordination agreement became effective: *Provided*, That this temporary relief shall not apply to any applicant or registrant if the adjusted net capital of the applicant or registrant is less than the greatest of:

- (A) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(iii)(A) of this section;
- (B) For a futures commission merchant or applicant therefor, 120 percent of the amount required by paragraph (a)(1)(i)(B) of this section;
- (C) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member;
- (D) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(c)(5)(i) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(c)(5)(i)); or
- (E) The amount of equity capital as defined in paragraph (d) of this section is less than the limits specified in paragraph (d) of this section. Such temporary subordination agreement shall be subject to all the other provisions of this section.

(vi) *Filing*. An applicant shall file a signed copy of any proposed subordination agreement (including nonconforming subordination agreements) with the National Futures Association at least ten days prior to the proposed effective date of the agreement or at such other time as the National Futures Association for good cause shall accept such filing. A registrant that is not a member of any designated self-regulatory organization shall file two signed copies of any proposed subordination agreement (including nonconforming subordination agreements) with the regional office of the Commission nearest the principal place of business of the registrant at least ten days prior to the proposed effective date of the agreement or at such other time as the Commission for good cause shall accept such filing. A registrant that is a member of a designated self-regulatory organization shall file signed copies of any proposed subordination agreement (including nonconforming subordination agreements) with the designated self-regulatory organization in such quantities and at such time as the designated self-regulatory organization may require prior to the effective date. The applicant or registrant shall also file with said parties a statement setting forth the name and address of the lender, the business relationship of the lender to the applicant or registrant and whether the applicant or registrant carried funds or securities for the lender at or about the time the proposed agreement was so filed. A proposed agreement filed by an applicant with the National Futures Association shall be reviewed by the National Futures Association, and no such agreement shall be a satisfactory subordination agreement for the purposes of this section unless and until the National Futures Association has found the agreement acceptable and such agreement has become effective in the form found acceptable. A proposed agreement filed by a registrant shall be reviewed by the designated self-regulatory organization with whom such an agreement is required to be filed prior to its becoming effective or, if the registrant is not a member of any designated self-regulatory organization, by the regional office of the Commission where the agreement is required to be filed prior to its becoming effective. No proposed agreement shall be a satisfactory subordination agreement for the purposes of this section unless and until the designated self-regulatory organization or, if a registrant is not a member of any designated self-regulatory organization, the Commission, has found the agreement acceptable and such agreement has become effective in the form found acceptable: *Provided*, however, That a proposed agreement shall be a satisfactory subordination agreement for purpose of this section if the registrant: is a securities broker or dealer registered with the Securities and Exchange Commission; files signed copies of the proposed subordination agreement with the applicable securities designated examining authority, as defined in Rule 15c3-1(c)(12) of the Securities and Exchange Commission

(17 CFR 240.15c3–1(c)(12)), in the form and manner prescribed by the designated examining authority; files signed copies of the proposed subordination agreement with the designated self-regulatory organization at the time it files such copies with the designated examining authority in the form and manner prescribed by the designated self-regulatory organization; and files a copy of the designated examining authority's approval of the proposed subordination agreement with the designated self-regulatory organization immediately upon receipt of such approval. The designated examining authority's determination that the proposed subordination agreement satisfies the requirements for a satisfactory subordination agreement will be deemed a like finding by the designated self-regulatory organization, unless the designated self-regulatory organization notifies the registrant that the designated examining authority's determination shall not constitute a like finding by the designated self-regulatory organization.

(vii) *Subordination agreements that incorporate adjusted net capital requirements in effect prior to September 30, 2004.* Any subordination agreement that incorporates the adjusted net capital requirements in paragraphs (h)(2)(vi)(C)( 2 ), (h)(2)(vii)(A)( 2 ) and (B)( 2 ), (h)(2)(viii)(A)( 2 ), (h)(3)(ii)(B), and (h)(3)(v)(B) of this section, as in effect prior to September 30, 2004, and which has been deemed to be satisfactorily subordinated pursuant to this section prior to September 30, 2004, shall continue to be deemed a satisfactory subordination agreement until the maturity of such agreement. In the event, however, that such agreement is amended or renewed for any reason, then such agreement shall not be deemed a satisfactory subordination agreement unless the amended or renewed agreement meets the requirements of this section.

(4) A designated self-regulatory organization and the Commission may allow debt with a maturity date of 1 year or more to be treated as meeting the provisions of this paragraph (h): *Provided,* (i) Such exemption shall only be given when the registrant's adjusted net capital is less than the minimum required by this section or by the capital rule of the designated self-regulatory organization to which such registrant is subject;

(ii) That such debt did not exist prior to its use under this paragraph (h)(4);

(iii) Such exemption shall be for a period of 30 days or such lesser period as the designated self-regulatory organization and the Commission may determine;

(iv) Such exemption shall not be allowed more than once in any 12 month period; and

(v) At all times during such exemption the registrant shall make a good faith effort to comply with the provisions of this section or the capital rule of the designated self-regulatory organization to which such registrant is subject exclusive of any benefits derived from this paragraph (h)(4).

(i) [Reserved]

(j) For the purposes of this section *cover* is defined as follows:

(1) *General definition.* Cover shall mean transactions or positions in a contract for future delivery on a board of trade or a commodity option where such transactions or positions normally represent a substitute for transactions to be made or positions to be taken at a later time in a physical marketing channel, and where they are economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise, and where they arise from:

(i) The potential change in the value of assets which a person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising.

- (ii) The potential change in the value of liabilities which a person owes or anticipates incurring, or
- (iii) The potential change in the value of services which a person provides, purchases or anticipates providing or purchasing. Notwithstanding the foregoing, no transactions or positions shall be classified as cover for the purposes of this section unless their purpose is to offset price risks incidental to commercial cash or spot operations and such positions are established and liquidated in accordance with sound commercial practices and unless the provisions of paragraphs (j) (2) and (3) of this section have been satisfied.

(2) *Enumerated cover transactions.* The definition of covered transactions and positions in paragraph (j)(1) of this section includes, but is not limited to, the following specific transactions and positions:

- (i) Ownership or fixed-price purchase of any commodity which does not exceed in quantity (A) the sales of the same commodity for future delivery on a board of trade or (B) the purchase of a put commodity option of the same commodity for which the market value for the actual commodity or futures contract which is the subject of the option is less than the strike price of the option or (C) the ownership of a commodity option position established by the sale (grant) of a call commodity option of the same commodity for which the market value for the actual commodity or futures contract which is the subject of the option is more than the strike price of the option: *Provided*, That for purposes of paragraph (c)(5)(x) of this section the market value for the actual commodity or futures contract which is the subject of such option need not be more than the strike price of that option;
- (ii) Fixed-price sale of any commodity which does not exceed in quantity (A) the purchase of the same commodity for future delivery on a board of trade or (B) the purchase of a call commodity option of the same commodity for which the market value for the actual commodity or futures contract which is the subject of such option is more than the strike price of the option or (C) ownership of a commodity option position established by the sale (grant) of a put commodity option of the same commodity for which the market value for the actual commodity or futures contract which is the subject of the option is less than the strike price of the option: *Provided*, That for purposes of paragraph (c)(5)(x) of this section the market value for the actual commodity or futures contract which is the subject of such option need not be less than the strike price of that option; and
- (iii) Ownership or fixed-price contracts of a commodity described in paragraphs (j)(2)(i) and (j)(2)(ii) of this section may also be covered other than by the same quantity of the same cash commodity, provided that the fluctuations in value of the position for future delivery or commodity option are substantially related to the fluctuations in value of the actual cash position.

(3) *Nonenumerated cases.* Upon specific request, the Commission may recognize transactions and positions other than those enumerated in paragraph (j)(2) of this section as cover in amounts and under the terms and conditions as it may specify. Any applicant or registrant who wishes to avail itself of the provisions of this paragraph (j)(3) must apply to the Commission in writing at its principal office in Washington, DC giving full details of the transaction including detailed information which will demonstrate that the transaction is economically appropriate to the reduction of risk exposure attendant to the conduct and management of a commercial enterprise.

**[522] 523. Compliance with Commission Regulation 1.18 -  
Records for and relating to Financial Reporting and  
Monthly Computation by Futures Commission Merchants  
and Introducing Brokers**

Any Trading Privilege Holder subject to Commission Regulation 1.18 that violates Commission Regulation 1.18 shall be deemed to have violated this Rule [522] 523. Commission Regulation 1.20 is set forth below and incorporated into this Rule [522] 523.

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**[523] 524. Compliance with Commission Regulation 1.20  
– Futures Customer Funds to Be Segregated and  
Separately Accounted For**

Any Trading Privilege Holder subject to Commission Regulation 1.20 that violates Commission Regulation 1.20 shall be deemed to have violated this Rule [523] 524. Commission Regulation 1.20 is set forth below and incorporated into this Rule [523] 524.

Commission Regulation 1.20 – [Customer] Futures customer funds to be segregated and separately accounted for[.]

[(a) All customer funds shall be separately accounted for and segregated as belonging to commodity or option customers. Such customer funds when deposited with any bank, trust company, clearing organization or another futures commission merchant shall be deposited under an account name which clearly identifies them as such and shows that they are segregated as required by the Act and this part. Each registrant shall obtain and retain in its files for the period provided in §1.31 a written acknowledgment from such bank, trust company, clearing organization, or futures commission merchant, that it was informed that the customer funds deposited therein are those of commodity or option customers and are being held in accordance with the provisions of the Act and this part: *Provided, however,* that an acknowledgment need not be obtained from a clearing organization that has adopted and submitted to the Commission rules that provide for the segregation as customer funds, in accordance with all relevant provisions of the Act and the rules and orders promulgated thereunder, of all funds held on behalf of customers. Under no circumstances shall any portion of customer funds be obligated to a clearing organization, any member of a contract market, a futures commission merchant, or any depository except to purchase, margin, guarantee, secure, transfer, adjust or settle trades, contracts or commodity option transactions of commodity or option customers. No person, including any clearing organization or any depository, that has received customer funds for deposit in a segregated account, as provided in this section, may hold, dispose of, or use any such funds as belonging to any person other than the option or commodity customers of the futures commission merchant which deposited such funds.

(b) All customer funds received by a clearing organization from a member of the clearing organization to purchase, margin, guarantee, secure or settle the trades, contracts or commodity options of the clearing member's commodity or option customers and all money accruing to such commodity or option customers as the result of trades, contracts or commodity options so carried shall be separately accounted for and segregated as belonging to such commodity or option customers, and a clearing organization shall not hold, use or dispose of such customer funds except as belonging to such commodity or option customers. Such customer funds when deposited

in a bank or trust company shall be deposited under an account name which clearly shows that they are the customer funds of the commodity or option customers of clearing members, segregated as required by the Act and these regulations. The clearing organization shall obtain and retain in its files for the period provided by §1.31 an acknowledgment from such bank or trust company that it was informed that the customer funds deposited therein are those of commodity or option customers of its clearing members and are being held in accordance with the provisions of the Act and these regulations.

(c) Each futures commission merchant shall treat and deal with the customer funds of a commodity customer or of an option customer as belonging to such commodity or option customer. All customer funds shall be separately accounted for, and shall not be commingled with the money, securities or property of a futures commission merchant or of any other person, or be used to secure or guarantee the trades, contracts or commodity options, or to secure or extend the credit, of any person other than the one for whom the same are held: *Provided, however,* That customer funds treated as belonging to the commodity or option customers of a futures commission merchant may for convenience be commingled and deposited in the same account or accounts with any bank or trust company, with another person registered as a futures commission merchant, or with a clearing organization, and that such share thereof as in the normal course of business is necessary to purchase, margin, guarantee, secure, transfer, adjust, or settle the trades, contracts or commodity options of such commodity or option customers or resulting market positions, with the clearing organization or with any other person registered as a futures commission merchant, may be withdrawn and applied to such purposes, including the payment of premiums to option grantors, commissions, brokerage, interest, taxes, storage and other fees and charges, lawfully accruing in connection with such trades, contracts or commodity options: *Provided, further,* That customer funds may be invested in instruments described in §1.25.]

(a) General. A futures commission merchant must separately account for all futures customer funds and segregate such funds as belonging to its futures customers. A futures commission merchant shall deposit futures customer funds under an account name that clearly identifies them as futures customer funds and shows that such funds are segregated as required by sections 4d(a) and 4d(b) of the Act and by this part. A futures commission merchant must at all times maintain in the separate account or accounts money, securities and property in an amount at least sufficient in the aggregate to cover its total obligations to all futures customers as computed under paragraph (i) of this section. The futures commission merchant must perform appropriate due diligence as required by §1.11 on any and all locations of futures customer funds, as specified in paragraph (b) of this section, to ensure that the location in which the futures commission merchant has deposited such funds is a financially sound entity.

(b) Location of futures customer funds. A futures commission merchant may deposit futures customer funds, subject to the risk management policies and procedures of the futures commission merchant required by §1.11, with the following depositories:

- (1) A bank or trust company;
- (2) A derivatives clearing organization; or
- (3) Another futures commission merchant.

(c) Limitation on the holding of futures customer funds outside of the United States. A futures commission merchant may hold futures customer funds with a depository outside of the United States only in accordance with §1.49.

(d) Written acknowledgment from depositories. (1) A futures commission merchant must obtain a written acknowledgment from each bank, trust company, derivatives clearing organization,

or futures commission merchant prior to or contemporaneously with the opening of an account by the futures commission merchant with such depositories; provided, however, that a written acknowledgment need not be obtained from a derivatives clearing organization that has adopted and submitted to the Commission rules that provide for the segregation of futures customer funds in accordance with all relevant provisions of the Act and the rules and orders promulgated thereunder.

(2) The written acknowledgment must be in the form as set out in Appendix A to this part.

(3)(i) A futures commission merchant shall deposit futures customer funds only with a depository that agrees to provide the director of the Division of Swap Dealer and Intermediary Oversight, or any successor division, or such director's designees, with direct, read-only electronic access to transaction and account balance information for futures customer accounts.

(ii) The written acknowledgment must contain the futures commission merchant's authorization to the depository to provide direct, read-only electronic access to futures customer account transaction and account balance information to the director of the Division of Swap Dealer and Intermediary Oversight, or any successor division, or such director's designees, without further notice to or consent from the futures commission merchant.

(4) A futures commission merchant shall deposit futures customer funds only with a depository that agrees to provide the Commission and the futures commission merchant's designated self-regulatory organization with a copy of the executed written acknowledgment no later than three business days after the opening of the account or the execution of a new written acknowledgment for an existing account, as applicable. The Commission must receive the written acknowledgment from the depository via electronic means, in a format and manner determined by the Commission. The written acknowledgment must contain the futures commission merchant's authorization to the depository to provide the written acknowledgment to the Commission and to the futures commission merchant's designated self-regulatory organization without further notice to or consent from the futures commission merchant.

(5) A futures commission merchant shall deposit futures customer funds only with a depository that agrees that accounts containing customer funds may be examined at any reasonable time by the director of the Division of Swap Dealer and Intermediary Oversight or the director of the Division of Clearing and Risk, or any successor divisions, or such directors' designees, or an appropriate officer, agent or employee of the futures commission merchant's designated self-regulatory organization. The written acknowledgment must contain the futures commission merchant's authorization to the depository to permit any such examination to take place without further notice to or consent from the futures commission merchant.

(6) A futures commission merchant shall deposit futures customer funds only with a depository that agrees to reply promptly and directly to any request from the director of the Division of Swap Dealer and Intermediary Oversight or the director of the Division of Clearing and Risk, or any successor divisions, or such directors' designees, or an appropriate officer, agent or employee of the futures commission merchant's designated self-regulatory organization for confirmation of account balances or provision of any other information regarding or related to an account. The written acknowledgment must contain the futures commission merchant's authorization to the depository to reply promptly and directly as required by this paragraph without further notice to or consent from the futures commission merchant.

(7) The futures commission merchant shall promptly file a copy of the written acknowledgment with the Commission in the format and manner specified by the Commission no later than three business days after the opening of the account or the execution of a new written acknowledgment for an existing account, as applicable.

(8) A futures commission merchant shall obtain a new written acknowledgment within 120 days of any changes in the following:

- (i) The name or business address of the futures commission merchant;
- (ii) The name or business address of the bank, trust company, derivatives clearing organization or futures commission merchant receiving futures customer funds; or
- (iii) The account number(s) under which futures customer funds are held.

(9) A futures commission merchant shall maintain each written acknowledgment readily accessible in its files in accordance with §1.31, for as long as the account remains open, and thereafter for the period provided in §1.31.

(e) *Commingling.* (1) A futures commission merchant may for convenience commingle the futures customer funds that it receives from, or on behalf of, multiple futures customers in a single account or multiple accounts with one or more of the depositories listed in paragraph (b) of this section.

(2) A futures commission merchant shall not commingle futures customer funds with the money, securities or property of such futures commission merchant, or with any proprietary account of such futures commission merchant, or use such funds to secure or guarantee the obligation of, or extend credit to, such futures commission merchant or any proprietary account of such futures commission merchant; provided, however, a futures commission merchant may deposit proprietary funds in segregated accounts as permitted under §1.23.

(3) A futures commission merchant may not commingle futures customer funds with funds deposited by 30.7 customers as defined in §30.1 of this chapter and set aside in separate accounts as required by part 30 of this chapter, or with funds deposited by Cleared Swaps Customers as defined in §22.1 of this chapter and held in segregated accounts pursuant to section 4d(f) of the Act; provided, however, that a futures commission merchant may commingle futures customer funds with funds deposited by 30.7 customers or Cleared Swaps Customers if expressly permitted by a Commission regulation or order, or by a derivatives clearing organization rule approved in accordance with §39.15(b)(2) of this chapter.

(f) *Limitation on use of futures customer funds.* (1) A futures commission merchant shall treat and deal with the funds of a futures customer as belonging to such futures customer. A futures commission merchant shall not use the funds of a futures customer to secure or guarantee the commodity interests, or to secure or extend the credit, of any person other than the futures customer for whom the funds are held.

(2) A futures commission merchant shall obligate futures customer funds to a derivatives clearing organization, a futures commission merchant, or any depository solely to purchase, margin, guarantee, secure, transfer, adjust or settle trades, contracts or commodity option transactions of futures customers; provided, however, that a futures commission merchant is permitted to use the funds belonging to a futures customer that are necessary in the normal course of business to pay lawfully accruing fees or expenses on behalf of the futures customer's positions including commissions, brokerage, interest, taxes, storage and other fees and charges.

(3) No person, including any derivatives clearing organization or any depository, that has received futures customer funds for deposit in a segregated account, as provided in this section, may hold, dispose of, or use any such funds as belonging to any person other than the futures customers of the futures commission merchant which deposited such funds.

(g) *Derivatives clearing organizations—(1) General.* All futures customer funds received by a derivatives clearing organization from a member to purchase, margin, guarantee, secure or settle the trades, contracts or commodity options of the clearing member's futures customers and all money accruing to such futures customers as the result of trades, contracts or commodity options so carried shall be separately accounted for and segregated as belonging to such futures customers, and a derivatives clearing organization shall not hold, use or dispose of such futures customer funds except as belonging to such futures customers. A derivatives clearing organization shall deposit futures customer funds under an account name that clearly identifies them as futures customer funds and shows that such funds are segregated as required by sections 4d(a) and 4d(b) of the Act and by this part.

(2) *Location of futures customer funds.* A derivatives clearing organization may deposit futures customer funds with a bank or trust company, which may include a Federal Reserve Bank with respect to deposits of a derivatives clearing organization that is designated by the Financial Stability Oversight Council to be systemically important.

(3) *Limitation on the holding of futures customer funds outside of the United States.* A derivatives clearing organization may hold futures customer funds with a depository outside of the United States only in accordance with \$1.49.

(4) *Written acknowledgment from depositories.* (i) A derivatives clearing organization must obtain a written acknowledgment from each depository prior to or contemporaneously with the opening of a futures customer funds account.

(ii) The written acknowledgment must be in the form as set out in Appendix B to this part; provided, however, that a derivatives clearing organization shall obtain from a Federal Reserve Bank only a written acknowledgment that:

(A) The Federal Reserve Bank was informed that the customer funds deposited therein are those of customers who trade commodities, options, swaps, and other products and are being held in accordance with the provisions of section 4d of the Act and Commission regulations thereunder; and

(B) The Federal Reserve Bank agrees to reply promptly and directly to any request from the director of the Division of Clearing and Risk or the director of the Division of Swap Dealer and Intermediary Oversight, or any successor divisions, or such directors' designees, for confirmation of account balances or provision of any other information regarding or related to an account.

(iii) A derivatives clearing organization shall deposit futures customer funds only with a depository that agrees to provide the Commission with a copy of the executed written acknowledgment no later than three business days after the opening of the account or the execution of a new written acknowledgment for an existing account, as applicable. The Commission must receive the written acknowledgment from the depository via electronic means, in a format and manner determined by the Commission. The written acknowledgment must contain the derivatives clearing organization's authorization to the depository to provide the written acknowledgment to the Commission without further notice to or consent from the derivatives clearing organization.

(iv) A derivatives clearing organization shall deposit futures customer funds only with a depository that agrees to reply promptly and directly to any request from the director of the Division of Clearing and Risk or the director of the Division of Swap Dealer and Intermediary Oversight, or any successor divisions, or such directors' designees, for confirmation of account balances or provision of any other information regarding or related to an account. The written acknowledgment must contain the derivatives clearing organization's authorization to the depository to reply

promptly and directly as required by this paragraph without further notice to or consent from the derivatives clearing organization.

(v) A derivatives clearing organization shall promptly file a copy of the written acknowledgment with the Commission in the format and manner specified by the Commission no later than three business days after the opening of the account or the execution of a new written acknowledgment for an existing account, as applicable.

(vi) A derivatives clearing organization shall obtain a new written acknowledgment within 120 days of any changes in the following:

(A) The name or business address of the derivatives clearing organization;

(B) The name or business address of the depository receiving futures customer funds; or

(C) The account number(s) under which futures customer funds are held.

(vii) A derivatives clearing organization shall maintain each written acknowledgment readily accessible in its files in accordance with §1.31, for as long as the account remains open, and thereafter for the period provided in §1.31.

(5) *Commingling.* (i) A derivatives clearing organization may for convenience commingle the futures customer funds that it receives from, or on behalf of, multiple futures commission merchants in a single account or multiple accounts with one or more of the depositories listed in paragraph (g)(2) of this section.

(ii) A derivatives clearing organization shall not commingle futures customer funds with the money, securities or property of such derivatives clearing organization or with any proprietary account of any of its clearing members, or use such funds to secure or guarantee the obligations of, or extend credit to, such derivatives clearing organization or any proprietary account of any of its clearing members.

(iii) A derivatives clearing organization may not commingle funds held for futures customers with funds deposited by clearing members on behalf of their 30.7 customers as defined in §30.1 of this chapter and set aside in separate accounts as required by part 30 of this chapter, or with funds deposited by clearing members on behalf of their Cleared Swaps Customers as defined in §22.1 of this chapter and held in segregated accounts pursuant section 4d(f) of the Act; provided, however, that a derivatives clearing organization may commingle futures customer funds with funds deposited by clearing members on behalf of their 30.7 customers or Cleared Swaps Customers if expressly permitted by a Commission regulation or order, or by a derivatives clearing organization rule approved in accordance with §39.15(b)(2) of this chapter.

(h) *Immediate availability of bank and trust company deposits.* All futures customer funds deposited by a futures commission merchant or a derivatives clearing organization with a bank or trust company must be immediately available for withdrawal upon the demand of the futures commission merchant or derivatives clearing organization.

(i) *Requirements as to amount.* (1) For purposes of this paragraph (i), the term "account" shall mean the entries on the books and records of a futures commission merchant pertaining to the futures customer funds of a particular futures customer.

(2) The futures commission merchant must reflect in the account that it maintains for each futures customer the net liquidating equity for each such customer, calculated as follows: The market value of any futures customer funds that it receives from such customer, as adjusted by:

- (i) Any uses permitted under paragraph (f) of this section;
- (ii) Any accruals on permitted investments of such collateral under §1.25 that, pursuant to the futures commission merchant's customer agreement with that customer, are creditable to such customer;
- (iii) Any gains and losses with respect to contracts for the purchase or sale of a commodity for future delivery and any options on such contracts;
- (iv) Any charges lawfully accruing to the futures customer, including any commission, brokerage fee, interest, tax, or storage fee; and
- (v) Any appropriately authorized distribution or transfer of such collateral.

(3) If the market value of futures customer funds in the account of a futures customer is positive after adjustments, then that account has a credit balance. If the market value of futures customer funds in the account of a futures customer is negative after adjustments, then that account has a debit balance.

(4) The futures commission merchant must maintain in segregation an amount equal to the sum of any credit balances that the futures customers of the futures commission merchant have in their accounts. This balance may not be reduced by any debit balances that the futures customers of the futures commission merchants have in their accounts.

APPENDIX A TO §1.20—FUTURES COMMISSION MERCHANT ACKNOWLEDGMENT LETTER FOR CFTC REGULATION 1.20 CUSTOMER SEGREGATED ACCOUNT

[Date]

Name and Address of Bank, Trust Company, Derivatives Clearing Organization or Futures Commission Merchant]

We refer to the Segregated Account(s) which [Name of Futures Commission Merchant] ("we" or "our") have opened or will open with [Name of Bank, Trust Company, Derivatives Clearing Organization or Futures Commission Merchant] ("you" or "your") entitled:

[Name of Futures Commission Merchant] [if applicable, add "FCM Customer Omnibus Account"] CFTC Regulation 1.20 Customer Segregated Account under Sections 4d(a) and 4d(b) of the Commodity Exchange Act [and, if applicable, ", Abbreviated as [short title reflected in the depository's electronic system]]"

Account Number(s): []

(collectively, the "Account(s)").

You acknowledge that we have opened or will open the above-referenced Account(s) for the purpose of depositing, as applicable, money, securities and other property (collectively the "Funds") of customers who trade commodities, options, swaps, and other products, as required by Commodity Futures Trading Commission ("CFTC") Regulations, including Regulation 1.20, as amended; that the Funds held by you, hereafter deposited in the Account(s) or accruing to the credit of the Account(s), will be separately accounted for and segregated on your books from our own funds and from any other funds or accounts held by us in accordance with the provisions of the Commodity Exchange Act, as amended (the "Act"), and Part 1 of the

CFTC's regulations, as amended; and that the Funds must otherwise be treated in accordance with the provisions of Section 4d of the Act and CFTC regulations thereunder.

Furthermore, you acknowledge and agree that such Funds may not be used by you or by us to secure or guarantee any obligations that we might owe to you, and they may not be used by us to secure or obtain credit from you. You further acknowledge and agree that the Funds in the Account(s) shall not be subject to any right of offset or lien for or on account of any indebtedness, obligations or liabilities we may now or in the future have owing to you. This prohibition does not affect your right to recover funds advanced in the form of cash transfers, lines of credit, repurchase agreements or other similar liquidity arrangements you make in lieu of liquidating non-cash assets held in the Account(s) or in lieu of converting cash held in the Account(s) to cash in a different currency.

In addition, you agree that the Account(s) may be examined at any reasonable time by the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent or employee of our designated self-regulatory organization ("DSRO"), [Name of DSRO], and this letter constitutes the authorization and direction of the undersigned on our behalf to permit any such examination to take place without further notice to or consent from us.

You agree to reply promptly and directly to any request for confirmation of account balances or provision of any other information regarding or related to the Account(s) from the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent, or employee of [Name of DSRO], acting in its capacity as our DSRO, and this letter constitutes the authorization and direction of the undersigned on our behalf to release the requested information without further notice to or consent from us.

You further acknowledge and agree that, pursuant to authorization granted by us to you previously or herein, you have provided, or will promptly provide following the opening of the Account(s), the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor division, or such director's designees, with technological connectivity, which may include provision of hardware, software, and related technology and protocol support, to facilitate direct, read-only electronic access to transaction and account balance information for the Account(s). This letter constitutes the authorization and direction of the undersigned on our behalf for you to establish this connectivity and access if not previously established, without further notice to or consent from us.

The parties agree that all actions on your part to respond to the above information and access requests will be made in accordance with, and subject to, such usual and customary authorization verification and authentication policies and procedures as may be employed by you to verify the authority of, and authenticate the identity of, the individual making any such information or access request, in order to provide for the secure transmission and delivery of the requested information or access to the appropriate recipient(s). We will not hold you responsible for acting pursuant to any information or access request from the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent, or employee of [Name of DSRO], acting in its capacity as our DSRO, upon which you have relied after having taken measures in accordance with your applicable policies and procedures to assure that such request was provided to you by an individual authorized to make such a request.

In the event that we become subject to either a voluntary or involuntary petition for relief under the U.S. Bankruptcy Code, we acknowledge that you will have no obligation to release the Funds held in the Account(s), except upon instruction of the Trustee in Bankruptcy or pursuant to the Order of the respective U.S. Bankruptcy Court.

Notwithstanding anything in the foregoing to the contrary, nothing contained herein shall be construed as limiting your right to assert any right of offset or lien on assets that are not Funds maintained in the Account(s), or to impose such charges against us or any proprietary account maintained by us with you. Further, it is understood that amounts represented by checks, drafts or other items shall not be considered to be part of the Account(s) until finally collected. Accordingly, checks, drafts and other items credited to the Account(s) and subsequently dishonored or otherwise returned to you or reversed, for any reason, and any claims relating thereto, including but not limited to claims of alteration or forgery, may be charged back to the

Account(s), and we shall be responsible to you as a general endorser of all such items whether or not actually so endorsed.

You may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry, provided that, in the ordinary course of your business as a depository, you have no notice of or actual knowledge of a potential violation by us of any provision of the Act or the CFTC regulations that relates to the segregation of customer funds; and you shall not in any manner not expressly agreed to herein be responsible to us for ensuring compliance by us with such provisions of the Act and CFTC regulations; however, the aforementioned presumption does not affect any obligation you may otherwise have under the Act or CFTC regulations.

You may, and are hereby authorized to, obey the order, judgment, decree or levy of any court of competent jurisdiction or any governmental agency with jurisdiction, which order, judgment, decree or levy relates in whole or in part to the Account(s). In any event, you shall not be liable by reason of any action or omission to act pursuant to any such order, judgment, decree or levy, to us or to any other person, firm, association or corporation even if thereafter any such order, decree, judgment or levy shall be reversed, modified, set aside or vacated.

The terms of this letter agreement shall remain binding upon the parties, their successors and assigns and, for the avoidance of doubt, regardless of a change in the name of either party. This letter agreement supersedes and replaces any prior agreement between the parties in connection with the Account(s), including but not limited to any prior acknowledgment letter agreement, to the extent that such prior agreement is inconsistent with the terms hereof. In the event of any conflict between this letter agreement and any other agreement between the parties in connection with the Account(s), this letter agreement shall govern with respect to matters specific to Section 4d of the Act and the CFTC's regulations thereunder, as amended.

This letter agreement shall be governed by and construed in accordance with the laws of [Insert governing law] without regard to the principles of choice of law.

Please acknowledge that you agree to abide by the requirements and conditions set forth above by signing and returning to us the enclosed copy of this letter agreement, and that you further agree to provide a copy of this fully executed letter agreement directly to the CFTC (via electronic means in a format and manner determined by the CFTC) and to [Name of DSRO], acting in its capacity as our DSRO. We hereby authorize and direct you to provide such copies without further notice to or consent from us, no later than three business days after opening the Account(s) or revising this letter agreement, as applicable.

[Name of Futures Commission Merchant]

By:

Print Name:

Title:

ACKNOWLEDGED AND AGREED:

[Name of Bank, Trust Company, Derivatives Clearing Organization or Futures Commission Merchant]

By:

Print Name:

Title:

Contact Information: [Insert phone number and email address]

DATE:

APPENDIX B TO §1.20—DERIVATIVES CLEARING ORGANIZATION ACKNOWLEDGMENT LETTER FOR CFTC REGULATION 1.20 CUSTOMER SEGREGATED ACCOUNT

[Date]

[Name and Address of Bank or Trust Company]

We refer to the Segregated Account(s) which [Name of Derivatives Clearing Organization] ("we" or "our") have opened or will open with [Name of Bank or Trust Company] ("you" or "your") entitled:

[Name of Derivatives Clearing Organization] Futures Customer Omnibus Account, CFTC Regulation 1.20 Customer Segregated Account under Sections 4d(a) and 4d(b) of the Commodity Exchange Act [and, if applicable, "Abbreviated as [short title reflected in the depository's electronic system]"']

Account Number(s): []

(collectively, the "Account(s)").

You acknowledge that we have opened or will open the above-referenced Account(s) for the purpose of depositing, as applicable, money, securities and other property (collectively the "Funds") of customers who trade commodities, options, swaps, and other products, as required by Commodity Futures Trading Commission ("CFTC") Regulations, including Regulation 1.20, as amended; that the Funds held by you, hereafter deposited in the Account(s) or accruing to the credit of the Account(s), will be separately accounted for and segregated on your books from our own funds and from any other funds or accounts held by us in accordance with the provisions of the Commodity Exchange Act, as amended (the "Act"), and Part 1 of the CFTC's regulations, as amended; and that the Funds must otherwise be treated in accordance with the provisions of Section 4d of the Act and CFTC regulations thereunder.

Furthermore, you acknowledge and agree that such Funds may not be used by you or by us to secure or guarantee any obligations that we might owe to you, and they may not be used by us to secure or obtain credit from you. You further acknowledge and agree that the Funds in the Account(s) shall not be subject to any right of offset or lien for or on account of any indebtedness, obligations or liabilities we may now or in the future have owing to you. This prohibition does not affect your right to recover funds advanced in the form of cash transfers, lines of credit, repurchase agreements or other similar liquidity arrangements you make in lieu of liquidating non-cash assets held in the Account(s) or in lieu of converting cash held in the Account(s) to cash in a different currency.

You agree to reply promptly and directly to any request for confirmation of account balances or provision of any other information regarding or related to the Account(s) from the director of the Division of Clearing and Risk of the CFTC or the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor divisions, or such directors' designees, and this letter constitutes the authorization and direction of the undersigned on our behalf to release the requested information without further notice to or consent from us.

The parties agree that all actions on your part to respond to the above information requests will be made in accordance with, and subject to, such usual and customary authorization verification and authentication policies and procedures as may be employed by you to verify the authority of, and authenticate the identity of, the individual making any such information request, in order to provide for the secure transmission and delivery of the requested information to the appropriate recipient(s). We will not hold you responsible for acting pursuant to any information request from the director of the Division of Clearing and Risk of the CFTC or the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor divisions, or such directors' designees, upon which you have relied after having taken measures in accordance with your applicable policies and procedures to assure that such request was provided to you by an individual authorized to make such a request.

In the event that we or any of our futures commission merchant clearing members become(s) subject to either a voluntary or involuntary petition for relief under the U.S. Bankruptcy Code, we acknowledge that you will have no obligation to release the Funds held in the Account(s), except upon instruction of the Trustee in Bankruptcy or pursuant to the Order of the respective U.S. Bankruptcy Court.

Notwithstanding anything in the foregoing to the contrary, nothing contained herein shall be construed as limiting your right to assert any right of offset or lien on assets that are not Funds maintained in the

Account(s), or to impose such charges against us or any proprietary account maintained by us with you. Further, it is understood that amounts represented by checks, drafts or other items shall not be considered to be part of the Account(s) until finally collected. Accordingly, checks, drafts and other items credited to the Account(s) and subsequently dishonored or otherwise returned to you or reversed, for any reason, and any claims relating thereto, including but not limited to claims of alteration or forgery, may be charged back to the Account(s), and we shall be responsible to you as a general endorser of all such items whether or not actually so endorsed.

You may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry, provided that, in the ordinary course of your business as a depository, you have no notice of or actual knowledge of a potential violation by us of any provision of the Act or the CFTC regulations that relates to the segregation of customer funds; and you shall not in any manner not expressly agreed to herein be responsible to us for ensuring compliance by us with such provisions of the Act and CFTC regulations; however, the aforementioned presumption does not affect any obligation you may otherwise have under the Act or CFTC regulations.

You may, and are hereby authorized to, obey the order, judgment, decree or levy of any court of competent jurisdiction or any governmental agency with jurisdiction, which order, judgment, decree or levy relates in whole or in part to the Account(s). In any event, you shall not be liable by reason of any action or omission to act pursuant to any such order, judgment, decree or levy, to us or to any other person, firm, association or corporation even if thereafter any such order, decree, judgment or levy shall be reversed, modified, set aside or vacated.

The terms of this letter agreement shall remain binding upon the parties, their successors and assigns and, for the avoidance of doubt, regardless of a change in the name of either party. This letter agreement supersedes and replaces any prior agreement between the parties in connection with the Account(s), including but not limited to any prior acknowledgment letter agreement, to the extent that such prior agreement is inconsistent with the terms hereof. In the event of any conflict between this letter agreement and any other agreement between the parties in connection with the Account(s), this letter agreement shall govern with respect to matters specific to Section 4d of the Act and the CFTC's regulations thereunder, as amended.

This letter agreement shall be governed by and construed in accordance with the laws of [Insert governing law] without regard to the principles of choice of law.

Please acknowledge that you agree to abide by the requirements and conditions set forth above by signing and returning to us the enclosed copy of this letter agreement, and that you further agree to provide a copy of this fully executed letter agreement directly to the CFTC (via electronic means in a format and manner determined by the CFTC). We hereby authorize and direct you to provide such copy without further notice to or consent from us, no later than three business days after opening the Account(s) or revising this letter agreement, as applicable.

[Name of Derivatives Clearing Organization]

By:

Print Name:

Title:

ACKNOWLEDGED AND AGREED:

[Name of Bank or Trust Company]

By:

Print Name:

Title:

Contact Information: [Insert phone number and email address]

DATE:

**[524] 525. Compliance with Commission Regulation 1.21 - Care of Money and Equities Accruing to Customers**

Any Trading Privilege Holder subject to Commission Regulation 1.21 that violates Commission Regulation 1.21 shall be deemed to have violated this Rule [524] 525. Commission Regulation 1.21 is set forth below and incorporated into this Rule [524] 525.

\* \* \* \* \*

**[525] 526. Compliance with Commission Regulation 1.22 - Use of Futures Customer Funds Restricted**

Any Trading Privilege Holder subject to Commission Regulation 1.22 that violates Commission Regulation 1.22 shall be deemed to have violated this Rule [525] 526. Commission Regulation 1.22 is set forth below and incorporated into this Rule [525] 526.

Commission Regulation 1.22 - Use of futures customer funds restricted.

[No futures commission merchant shall use, or permit the use of, the customer funds of one commodity and/or option customer to purchase, margin, or settle the trades, contracts, or commodity options of, or to secure or extend the credit of, any person other than such customer or option customer. Customer funds shall not be used to carry trades or positions of the same commodity and/or option customer other than in commodities or commodity options traded through the facilities of a contract market.]

(a) No futures commission merchant shall use, or permit the use of, the futures customer funds of one futures customer to purchase, margin, or settle the trades, contracts, or commodity options of, or to secure or extend the credit of, any person other than such futures customer.

(b) Futures customer funds shall not be used to carry trades or positions of the same futures customer other than in contracts for the purchase or sale of any commodity for future delivery or for options thereon traded through the facilities of a designated contract market.

(c)(1) The undermargined amount for a futures customer's account is the amount, if any, by which:

(i) The total amount of collateral required for that futures customer's positions in that account, at the time or times referred to in paragraph (c)(2) of this section, exceeds

(ii) The value of the futures customer funds for that account, as calculated in §1.20(i)(2).

(2) Each futures commission merchant must compute, based on the information available to the futures commission merchant as of the close of each business day,

(i) The undermargined amounts, based on the clearing initial margin that will be required to be maintained by that futures commission merchant for its futures customers, at each derivatives clearing organization of which the futures commission merchant is a member, at the point of the

daily settlement (as described in §39.14 of this chapter) that will complete during the following business day for each such derivatives clearing organization less

(ii) Any debit balances referred to in §1.20(i)(4) included in such undermargined amounts.

(3)(i) Prior to the Residual Interest Deadline, such futures commission merchant must maintain residual interest in segregated funds that is at least equal to the computation set forth in paragraph (c)(2) of this section. Where a futures commission merchant is subject to multiple Residual Interest Deadlines, prior to each Residual Interest Deadline, such futures commission merchant must maintain residual interest in segregated funds that is at least equal to the portion of the computation set forth in paragraph (c)(2) of this section attributable to the clearing initial margin required by the derivatives clearing organization making such settlement.

(ii) A futures commission merchant may reduce the amount of residual interest required in paragraph (c)(3)(i) of this section to account for payments received from or on behalf of undermargined futures customers (less the sum of any disbursements made to or on behalf of such customers) between the close of the previous business day and the Residual Interest Deadline.

(4) For purposes of paragraph (c)(2) of this section, a futures commission merchant should include, as clearing initial margin, customer initial margin that the futures commission merchant will be required to maintain, for that futures commission merchant's futures customers, at another futures commission merchant.

(5) *Residual Interest Deadline defined.* (i) Except as provided in paragraph (c)(5)(ii) of this section, the Residual Interest Deadline shall be the time of the settlement referenced in paragraph (c)(2)(i) or, as appropriate, (c)(4), of this section.

(ii) Starting on November 14, 2014 and during the phase-in period described in paragraph (c)(5)(iii) of this section, the Residual Interest Deadline shall be 6:00 p.m. Eastern Time on the date of the settlement referenced in paragraph (c)(2)(i) or, as appropriate, (c)(4), of this section.

(iii)(A) No later than May 16, 2016, the staff of the Commission shall complete and publish for public comment a report addressing, to the extent information is practically available, the practicability (for both futures commission merchants and customers) of moving that deadline from 6:00 p.m. Eastern Time on the date of the settlement referenced in paragraph (c)(2)(i) or, as appropriate, (c)(4), of this section to the time of that settlement (or to some other time of day), including whether and on what schedule it would be feasible to do so, and the costs and benefits of such potential requirements. Staff shall, using the Commission's Web site, solicit public comment and shall conduct a public roundtable regarding specific issues to be covered by such report.

(B) Nine months after publication of the report required by paragraph (c)(5)(iii)(A) of this section, the Commission may (but shall not be required to) do either or both of the following:

(1) Terminate the phase-in period, in which case the phase-in period shall end as of a date established by order published in the FEDERAL REGISTER, which date shall be no less than one year after the date such order is published; or

(2) Determine that it is necessary or appropriate in the public interest to propose through rulemaking a different Residual Interest Deadline. In that event, the Commission shall establish, by order published in the FEDERAL REGISTER, a phase-in schedule.

(C) If the phase-in schedule has not been amended pursuant to paragraph (c)(5)(iii)(B) of this section, then the phase-in period shall end on December 31, 2018.

**[526] 527. Compliance with Commission Regulation 1.23 - Interest of Futures Commission Merchants in Segregated Futures Customer Funds; Additions and Withdrawals**

Any Trading Privilege Holder subject to Commission Regulation 1.23 that violates Commission Regulation 1.23 shall be deemed to have violated this Rule [526] 527. Commission Regulation 1.23 is set forth below and incorporated into this Rule [526] 527.

Commission Regulation 1.23 - Interest of futures commission merchant in segregated futures customer funds; additions and withdrawals.

[The provision in section 4d(a)(2) of the Act and the provision in §1.20(c), which prohibit the commingling of customer funds with the funds of a futures commission merchant, shall not be construed to prevent a futures commission merchant from having a residual financial interest in the customer funds, segregated as required by the Act and the rules in this part and set apart for the benefit of commodity or option customers; nor shall such provisions be construed to prevent a futures commission merchant from adding to such segregated customer funds such amount or amounts of money, from its own funds or unencumbered securities from its own inventory, of the type set forth in §1.25, as it may deem necessary to ensure any and all commodity or option customers' accounts from becoming undersegregated at any time. The books and records of a futures commission merchant shall at all times accurately reflect its interest in the segregated funds. A futures commission merchant may draw upon such segregated funds to its own order, to the extent of its actual interest therein, including the withdrawal of securities held in segregated safekeeping accounts held by a bank, trust company, contract market clearing organization or other futures commission merchant. Such withdrawal shall not result in the funds of one commodity and/or option customer being used to purchase, margin or carry the trades, contracts or commodity options, or extend the credit of any other commodity customer, option customer or other person.]

(a)(1) The provision in sections 4d(a)(2) and 4d(b) of the Act and the provision in §1.20 that prohibit the commingling of futures customer funds with the funds of a futures commission merchant, shall not be construed to prevent a futures commission merchant from having a residual financial interest in the futures customer funds segregated as required by the Act and the regulations in this part and set apart for the benefit of futures customers; nor shall such provisions be construed to prevent a futures commission merchant from adding to such segregated futures customer funds such amount or amounts of money, from its own funds or unencumbered securities from its own inventory, of the type set forth in §1.25 of this part, as it may deem necessary to ensure any and all futures customers' accounts from becoming undersegregated at any time.

(2) If a futures commission merchant discovers at any time that it is holding insufficient funds in segregated accounts to meet its obligations under §§1.20 and 1.22, the futures commission merchant shall immediately deposit sufficient funds into segregation to bring the account into compliance.

(b) A futures commission merchant may not withdraw funds, except withdrawals that are made to or for the benefit of futures customers, from an account or accounts holding futures customer funds unless the futures commission merchant has prepared the daily segregation calculation required by §1.32 as of the close of business on the previous business day. A futures commission merchant that has completed its daily segregation calculation may make withdrawals, in addition to withdrawals that are made to or for the benefit of futures customers, to the extent of its actual residual financial interest in funds held in segregated futures accounts, adjusted to reflect market activity and other events that may have decreased the amount of the firm's residual financial interest since the close of business on the previous business day, including the withdrawal of

securities held in segregated safekeeping accounts held by a bank, trust company, derivatives clearing organization or other futures commission merchant. Such withdrawal(s), however, shall not result in the funds of one futures customer being used to purchase, margin or carry the trades, contracts or commodity options, or extend the credit of any other futures customer or other person.

(c) Notwithstanding paragraphs (a) and (b) of this section, each futures commission merchant shall establish a targeted residual interest (i.e., excess funds) that is in an amount that, when maintained as its residual interest in the segregated funds accounts, reasonably ensures that the futures commission merchant shall remain in compliance with the segregated funds requirements at all times. Each futures commission merchant shall establish policies and procedures designed to reasonably ensure that the futures commission merchant maintains the targeted residual amounts in segregated funds at all times. The futures commission merchant shall maintain sufficient capital and liquidity, and take such other appropriate steps as are necessary, to reasonably ensure that such amount of targeted residual interest is maintained as the futures commission merchant's residual interest in the segregated funds accounts at all times. In determining the amount of the targeted residual interest, the futures commission merchant shall analyze all relevant factors affecting the amounts in segregated funds from time to time, including without limitation various factors, as applicable, relating to the nature of the futures commission merchant's business including, but not limited to, the composition of the futures commission merchant's customer base, the general creditworthiness of the customer base, the general trading activity of the customers, the types of markets and products traded by the customers, the proprietary trading of the futures commission merchant, the general volatility and liquidity of the markets and products traded by customers, the futures commission merchant's own liquidity and capital needs, and the historical trends in customer segregated fund balances and debit balances in customers' and undermargined accounts. The analysis and calculation of the targeted amount of the future commission merchant's residual interest must be described in writing with the specificity necessary to allow the Commission and the futures commission merchant's designated self-regulatory organization to duplicate the analysis and calculation and test the assumptions made by the futures commission merchant. The adequacy of the targeted residual interest and the process for establishing the targeted residual interest must be reassessed periodically by the futures commission merchant and revised as necessary.

(d) Notwithstanding any other paragraph of this section, a futures commission merchant may not withdraw funds, in a single transaction or a series of transactions, that are not made to or for the benefit of futures customers from futures accounts if such withdrawal(s) would exceed 25 percent of the futures commission merchant's residual interest in such accounts as reported on the daily segregation calculation required by §1.32 and computed as of the close of business on the previous business day, unless:

(1) The futures commission merchant's chief executive officer, chief finance officer or other senior official that is listed as a principal of the futures commission merchant on its Form 7-R and is knowledgeable about the futures commission merchant's financial requirements and financial position pre-approves in writing the withdrawal, or series of withdrawals;

(2) The futures commission merchant files written notice of the withdrawal or series of withdrawals, with the Commission and with its designated self-regulatory organization immediately after the chief executive officer, chief finance officer or other senior official as described in paragraph (c)(1) of this section pre-approves the withdrawal or series of withdrawals. The written notice must:

(i) Be signed by the chief executive officer, chief finance officer or other senior official as described in paragraph (c)(1) of this section that pre-approved the withdrawal, and give notice that the futures commission merchant has withdrawn or intends to withdraw more than 25 percent of its residual interest in segregated accounts holding futures customer funds;

(ii) Include a description of the reasons for the withdrawal or series of withdrawals;

(iii) List the amount of funds provided to each recipient and each recipient's name;

(iv) Include the current estimate of the amount of the futures commission merchant's residual interest in the futures accounts after the withdrawal;

(v) Contain a representation by the chief executive officer, chief finance officer or other senior official as described in paragraph (c)(1) of this section that pre-approved the withdrawal, or series of withdrawals, that, after due diligence, to such person's knowledge and reasonable belief, the futures commission merchant remains in compliance with the segregation requirements after the withdrawal. The chief executive officer, chief finance officer or other senior official as described in paragraph (c)(1) of this section must consider the daily segregation calculation as of the close of business on the previous business day and any other factors that may cause a material change in the futures commission merchant's residual interest since the close of business the previous business day, including known unsecured futures customer debits or deficits, current day market activity and any other withdrawals made from the futures accounts; and

(vi) Any such written notice filed with the Commission must be filed via electronic transmission using a form of user authentication assigned in accordance with procedures established by or approved by the Commission, and otherwise in accordance with instruction issued by or approved by the Commission. Any such electronic submission must clearly indicate the registrant on whose behalf such filing is made and the use of such user authentication in submitting such filing will constitute and become a substitute for the manual signature of the authorized signer. Any written notice filed must be followed up with direct communication to the Regional office of the Commission that has supervisory authority over the futures commission merchant whereby the Commission acknowledges receipt of the notice; and

(3) After making a withdrawal requiring the approval and notice required in paragraphs (c)(1) and (2) of this section, and before the completion of its next daily segregated funds calculation, no futures commission merchant may make any further withdrawals from accounts holding futures customer funds, except to or for the benefit of futures customers, without, for each withdrawal, obtaining the approval required under paragraph (c)(1) of this section and filing a written notice in the manner specified under paragraph (c)(2) of this section with the Commission and its designated self-regulatory organization signed by the chief executive officer, chief finance officer, or other senior official. The written notice must:

(i) List the amount of funds provided to each recipient and each recipient's name;

(ii) Disclose the reason for each withdrawal;

(iii) Confirm that the chief executive officer, chief finance officer, or other senior official (and identify of the person if different from the person who signed the notice) pre-approved the withdrawal in writing;

(iv) Disclose the current estimate of the futures commission merchant's remaining total residual interest in the segregated accounts holding futures customer funds after the withdrawal; and

(v) Include a representation that, after due diligence, to the best of the notice signatory's knowledge and reasonable belief the futures commission merchant remains in compliance with the segregation requirements after the withdrawal.

(e) If a futures commission merchant withdraws funds from futures accounts that are not made to or for the benefit of futures customers, and the withdrawal causes the futures commission merchant to not hold sufficient funds in the futures accounts to meet its targeted residual interest, as required to be computed under §1.11, the futures commission merchant should deposit its own

funds into the futures accounts to restore the account balance to the targeted residual interest amount by the close of business on the next business day, or, if appropriate, revise the futures commission merchant's targeted amount of residual interest pursuant to the policies and procedures required by §1.11. Notwithstanding the foregoing, if a the futures commission merchant's residual interest in customer accounts is less than the amount required by §1.22 at any particular point in time, the futures commission merchant must immediately restore the residual interest to exceed the sum of such amounts. Any proprietary funds deposited in the futures accounts must be unencumbered and otherwise compliant with §1.25, as applicable.

**[527] 528. Compliance with Commission Regulation 1.24 - Segregated Funds; Exclusions Therefrom**

Any Trading Privilege Holder subject to Commission Regulation 1.24 that violates Commission Regulation 1.24 shall be deemed to have violated this Rule [527] 528. Commission Regulation 1.24 is set forth below and incorporated into this Rule [527] 528.

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**[528] 529. Compliance with Commission Regulation 1.25 - Investment of Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.25 that violates Commission Regulation 1.25 shall be deemed to have violated this Rule [528] 529. Commission Regulation 1.25 is set forth below and incorporated into this Rule [528] 529.

Commission Regulation 1.25 - Investment of customer funds.

(a) *Permitted investments.* (1) Subject to the terms and conditions set forth in this section, a futures commission merchant or a derivatives clearing organization may invest customer money in the following instruments (permitted investments):

(i) Obligations of the United States and obligations fully guaranteed as to principal and interest by the United States (U.S. government securities);

(ii) General obligations of any State or of any political subdivision thereof (municipal securities);

(iii) Obligations of any United States government corporation or enterprise sponsored by the United States government (U.S. agency obligations);

(iv) Certificates of deposit issued by a bank (certificates of deposit) as defined in section 3(a)(6) of the Securities Exchange Act of 1934, or a domestic branch of a foreign bank that carries deposits insured by the Federal Deposit Insurance Corporation;

(v) Commercial paper fully guaranteed as to principal and interest by the United States under the Temporary Liquidity Guarantee Program as administered by the Federal Deposit Insurance Corporation (commercial paper);

(vi) Corporate notes or bonds fully guaranteed as to principal and interest by the United States under the Temporary Liquidity Guarantee Program as administered by the Federal Deposit Insurance Corporation (corporate notes or bonds); and

(vii) Interests in money market mutual funds.

(2)(i) In addition, a futures commission merchant or derivatives clearing organization may buy and sell the permitted investments listed in paragraphs (a)(1)(i) through (vii) of this section pursuant to agreements for resale or repurchase of the instruments, in accordance with the provisions of paragraph (d) of this section.

(ii) A futures commission merchant or a derivatives clearing organization may sell securities deposited by customers as margin pursuant to agreements to repurchase subject to the following:

(A) Securities subject to such repurchase agreements must be "highly liquid" as defined in paragraph (b)(1) of this section.

(B) Securities subject to such repurchase agreements must not be "specifically identifiable property" as defined in §190.01(kk) of this chapter.

(C) The terms and conditions of such an agreement to repurchase must be in accordance with the provisions of paragraph (d) of this section.

(D) Upon the default by a counterparty to a repurchase agreement, the futures commission merchant or derivatives clearing organization shall act promptly to ensure that the default does not result in any direct or indirect cost or expense to the customer.

(3) Obligations issued by the Federal National Mortgage Association or the Federal Home Loan Mortgage Association are permitted while these entities operate under the conservatorship or receivership of the Federal Housing Finance Authority with capital support from the United States.

(b) *General terms and conditions.* A futures commission merchant or a derivatives clearing organization is required to manage the permitted investments consistent with the objectives of preserving principal and maintaining liquidity and according to the following specific requirements:

(1) *Liquidity.* Investments must be "highly liquid" such that they have the ability to be converted into cash within one business day without material discount in value.

(2) *Restrictions on instrument features.* (i) With the exception of money market mutual funds, no permitted investment may contain an embedded derivative of any kind, except as follows:

(A) The issuer of an instrument otherwise permitted by this section may have an option to call, in whole or in part, at par, the principal amount of the instrument before its stated maturity date; or

(B) An instrument that meets the requirements of paragraph (b)(2)(iv) of this section may provide for a cap, floor, or collar on the interest paid; *provided, however,* that the terms of such instrument obligate the issuer to repay the principal amount of the instrument at not less than par value upon maturity.

(ii) No instrument may contain interest-only payment features.

(iii) No instrument may provide payments linked to a commodity, currency, reference instrument, index, or benchmark except as provided in paragraph (b)(2)(iv) of this section, and it may not otherwise constitute a derivative instrument.

(iv)(A) Adjustable rate securities are permitted, subject to the following requirements:

( 1 ) The interest payments on variable rate securities must correlate closely and on an unleveraged basis to a benchmark of either the Federal Funds target or effective rate, the prime rate, the three-month Treasury Bill rate, the one-month or three-month LIBOR rate, or the interest rate of any fixed rate instrument that is a permitted investment listed in paragraph (a)(1) of this section;

( 2 ) The interest payment, in any period, on floating rate securities must be determined solely by reference, on an unleveraged basis, to a benchmark of either the Federal Funds target or effective rate, the prime rate, the three-month Treasury Bill rate, the one-month or three-month LIBOR rate, or the interest rate of any fixed rate instrument that is a permitted investment listed in paragraph (a)(1) of this section;

( 3 ) Benchmark rates must be expressed in the same currency as the adjustable rate securities that reference them; and

( 4 ) No interest payment on an adjustable rate security, in any period, can be a negative amount.

(B) For purposes of this paragraph, the following definitions shall apply:

( 1 ) The term *adjustable rate security* means, a floating rate security, a variable rate security, or both.

( 2 ) The term *floating rate security* means a security, the terms of which provide for the adjustment of its interest rate whenever a specified interest rate changes and that, at any time until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have market value that approximates its amortized cost.

( 3 ) The term *variable rate security* means a security, the terms of which provide for the adjustment of its interest rate on set dates (such as the last day of a month or calendar quarter) and that, upon each adjustment until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have a market value that approximates its amortized cost.

(v) Certificates of deposit must be redeemable at the issuing bank within one business day, with any penalty for early withdrawal limited to any accrued interest earned according to its written terms.

(vi) Commercial paper and corporate notes or bonds must meet the following criteria:

(A) The size of the issuance must be greater than \$1 billion;

(B) The instrument must be denominated in U.S. dollars; and

(C) The instrument must be fully guaranteed as to principal and interest by the United States for its entire term.

(3) *Concentration* —(i) *Asset-based concentration limits for direct investments.* (A) Investments in U.S. government securities shall not be subject to a concentration limit.

(B) Investments in U.S. agency obligations may not exceed 50 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(C) Investments in each of commercial paper, corporate notes or bonds and certificates of deposit may not exceed 25 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(D) Investments in municipal securities may not exceed 10 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(E) Subject to paragraph (b)(3)(i)(G) of this section, investments in money market mutual funds comprising only U.S. government securities shall not be subject to a concentration limit.

(F) Subject to paragraph (b)(3)(i)(G) of this section, investments in money market mutual funds, other than those described in paragraph (b)(3)(i)(E) of this section, may not exceed 50 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(G) Investments in money market mutual funds comprising less than \$1 billion in assets and/or which have a management company comprising less than \$25 billion in assets, may not exceed 10 percent of the total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(ii) *Issuer-based concentration limits for direct investments.* (A) Securities of any single issuer of U.S. agency obligations held by a futures commission merchant or derivatives clearing organization may not exceed 25 percent of total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(B) Securities of any single issuer of municipal securities, certificates of deposit, commercial paper, or corporate notes or bonds held by a futures commission merchant or derivatives clearing organization may not exceed 5 percent of total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(C) Interests in any single family of money market mutual funds described in paragraph (b)(3)(i)(F) of this section may not exceed 25 percent of total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(D) Interests in any individual money market mutual fund described in paragraph (b)(3)(i)(F) of this section may not exceed 10 percent of total assets held in segregation by the futures commission merchant or derivatives clearing organization.

(E) For purposes of determining compliance with the issuer-based concentration limits set forth in this section, securities issued by entities that are affiliated, as defined in paragraph (b)(5) of this section, shall be aggregated and deemed the securities of a single issuer. An interest in a permitted money market mutual fund is not deemed to be a security issued by its sponsoring entity.

(iii) *Concentration limits for agreements to repurchase* —(A) *Repurchase agreements.* For purposes of determining compliance with the asset-based and issuer-based concentration limits set forth in this section, securities sold by a futures commission merchant or derivatives clearing

organization subject to agreements to repurchase shall be combined with securities held by the futures commission merchant or derivatives clearing organization as direct investments.

(B) *Reverse repurchase agreements.* For purposes of determining compliance with the asset-based and issuer-based concentration limits set forth in this section, securities purchased by a futures commission merchant or derivatives clearing organization subject to agreements to resell shall be combined with securities held by the futures commission merchant or derivatives clearing organization as direct investments.

(iv) *Treatment of customer-owned securities.* For purposes of determining compliance with the asset-based and issuer-based concentration limits set forth in this section, securities owned by the customers of a futures commission merchant and posted as margin collateral are not included in total assets held in segregation by the futures commission merchant, and securities posted by a futures commission merchant with a derivatives clearing organization are not included in total assets held in segregation by the derivatives clearing organization.

(v) *Counterparty concentration limits.* Securities purchased by a futures commission merchant or derivatives clearing organization from a single counterparty, or from one or more counterparties under common ownership or control, subject to an agreement to resell the securities to [that] the counterparty or counterparties, shall not exceed 25 percent of total assets held in segregation or under §30.7 of this chapter by the futures commission merchant or derivatives clearing organization.

(4) *Time-to-maturity.* (i) Except for investments in money market mutual funds, the dollar-weighted average of the time-to-maturity of the portfolio, as that average is computed pursuant to §270.2a-7 of this title, may not exceed 24 months.

(ii) For purposes of determining the time-to-maturity of the portfolio, an instrument that is set forth in paragraphs (a)(1)(i) through (vii) of this section may be treated as having a one-day time-to-maturity if the following terms and conditions are satisfied:

(A) The instrument is deposited solely on an overnight basis with a derivatives clearing organization pursuant to the terms and conditions of a collateral management program that has become effective in accordance with §39.4 of this chapter;

(B) The instrument is one that the futures commission merchant owns or has an unqualified right to pledge, is not subject to any lien, and is deposited by the futures commission merchant into a segregated account at a derivatives clearing organization;

(C) The derivatives clearing organization prices the instrument each day based on the current mark-to-market value; and

(D) The derivatives clearing organization reduces the assigned value of the instrument each day by a haircut of at least 2 percent.

(5) *Investments in instruments issued by affiliates.* (i) A futures commission merchant shall not invest customer funds in obligations of an entity affiliated with the futures commission merchant, and a derivatives clearing organization shall not invest customer funds in obligations of an entity affiliated with the derivatives clearing organization. An affiliate includes parent companies, including all entities through the ultimate holding company, subsidiaries to the lowest level, and companies under common ownership of such parent company or affiliates.

(ii) A futures commission merchant or derivatives clearing organization may invest customer funds in a fund affiliated with that futures commission merchant or derivatives clearing organization.

[(6) *Recordkeeping*. A futures commission merchant and a derivatives clearing organization shall prepare and maintain a record that will show for each business day with respect to each type of investment made pursuant to this section, the following information:

(i) The type of instruments in which customer funds have been invested;

(ii) The original cost of the instruments; and

(iii) The current market value of the instruments.]

(c) *Money market mutual funds*. The following provisions will apply to the investment of customer funds in money market mutual funds (the fund).

(1) The fund must be an investment company that is registered under the Investment Company Act of 1940 with the Securities and Exchange Commission and that holds itself out to investors as a money market fund, in accordance with §270.2a-7 of this title.

(2) The fund must be sponsored by a federally-regulated financial institution, a bank as defined in section 3(a)(6) of the Securities Exchange Act of 1934, an investment adviser registered under the Investment Advisers Act of 1940, or a domestic branch of a foreign bank insured by the Federal Deposit Insurance Corporation.

(3) A futures commission merchant or derivatives clearing organization shall maintain the confirmation relating to the purchase in its records in accordance with §1.31 and note the ownership of fund shares (by book-entry or otherwise) in a custody account of the futures commission merchant or derivatives clearing organization in accordance with §1.26. The futures commission merchant or the derivatives clearing organization shall obtain the acknowledgment letter required by §1.26 from an entity that has substantial control over the fund shares purchased with customer [segregated] funds and has the knowledge and authority to facilitate redemption and payment or transfer of the customer [segregated] funds. Such entity may include the fund sponsor or depository acting as custodian for fund shares.

(4) The net asset value of the fund must be computed by 9 a.m. of the business day following each business day and made available to the futures commission merchant or derivatives clearing organization by that time.

(5)(i) General requirement for redemption of interests. A fund shall be legally obligated to redeem an interest and to make payment in satisfaction thereof by the business day following a redemption request, and the futures commission merchant or derivatives clearing organization shall retain documentation demonstrating compliance with this requirement.

(ii) Exception. A fund may provide for the postponement of redemption and payment due to any of the following circumstances:

(A) For any period during which there is a non-routine closure of the Fedwire or applicable Federal Reserve Banks;

(B) For any period:

( 1 ) During which the New York Stock Exchange is closed other than customary week-end and holiday closings; or

( 2 ) During which trading on the New York Stock Exchange is restricted;

(C) For any period during which an emergency exists as a result of which:

( 1 ) Disposal by the company of securities owned by it is not reasonably practicable; or

( 2 ) It is not reasonably practicable for such company fairly to determine the value of its net assets;

(D) For any period as the Securities and Exchange Commission may by order permit for the protection of security holders of the company;

(E) For any period during which the Securities and Exchange Commission has, by rule or regulation, deemed that:

( 1 ) Trading shall be restricted; or

( 2 ) An emergency exists; or

(F) For any period during which each of the conditions of §270.22e-3(a)(1) through (3) of this title are met.

(6) The agreement pursuant to which the futures commission merchant or derivatives clearing organization has acquired and is holding its interest in a fund must contain no provision that would prevent the pledging or transferring of shares.

(7) The appendix to this section sets forth language that will satisfy the requirements of paragraph (c)(5) of this section.

(d) *Repurchase and reverse repurchase agreements.* A futures commission merchant or derivatives clearing organization may buy and sell the permitted investments listed in paragraphs (a)(1)(i) through (vii) of this section pursuant to agreements for resale or repurchase of the securities (agreements to repurchase or resell), provided the agreements to repurchase or resell conform to the following requirements:

(1) The securities are specifically identified by coupon rate, par amount, market value, maturity date, and CUSIP or ISIN number.

(2) Permitted counterparties are limited to a bank as defined in section 3(a)(6) of the Securities Exchange Act of 1934, a domestic branch of a foreign bank insured by the Federal Deposit Insurance Corporation, a securities broker or dealer, or a government securities broker or government securities dealer registered with the Securities and Exchange Commission or which has filed notice pursuant to section 15C(a) of the Government Securities Act of 1986.

(3) A futures commission merchant or derivatives clearing organization shall not enter into an agreement to repurchase or resell with a counterparty that is an affiliate of the futures commission merchant or derivatives clearing organization, respectively. An affiliate includes parent companies, including all entities through the ultimate holding company, subsidiaries to the lowest level, and companies under common ownership of such parent company or affiliates.

(4) The transaction is executed in compliance with the concentration limit requirements applicable to the securities transferred to the customer segregated custodial account in connection with the agreements to repurchase referred to in paragraphs (b)(3)(iii)(A) and (B) of this section.

(5) The transaction is made pursuant to a written agreement signed by the parties to the agreement, which is consistent with the conditions set forth in paragraphs (d)(1) through (13) of this section and which states that the parties thereto intend the transaction to be treated as a purchase and sale of securities.

(6) The term of the agreement is no more than one business day, or reversal of the transaction is possible on demand.

(7) Securities transferred to the futures commission merchant or derivatives clearing organization under the agreement are held in a safekeeping account with a bank as referred to in paragraph (d)(2) of this section, a Federal Reserve Bank, a derivatives clearing organization, or the Depository Trust Company in an account that complies with the requirements of §1.26.

(8) The futures commission merchant or the derivatives clearing organization may not use securities received under the agreement in another similar transaction and may not otherwise hypothecate or pledge such securities, except securities may be pledged on behalf of customers at another futures commission merchant or derivatives clearing organization. Substitution of securities is allowed, *provided, however, that:*

(i) The qualifying securities being substituted and original securities are specifically identified by date of substitution, market values substituted, coupon rates, par amounts, maturity dates and CUSIP or ISIN numbers;

(ii) Substitution is made on a "delivery versus delivery" basis; and

(iii) The market value of the substituted securities is at least equal to that of the original securities.

(9) The transfer of securities to the customer segregated custodial account is made on a delivery versus payment basis in immediately available funds. The transfer of funds to the customer segregated cash account is made on a payment versus delivery basis. The transfer is not recognized as accomplished until the funds and/or securities are actually received by the custodian of the futures commission merchant's or derivatives clearing organization's customer funds or securities purchased on behalf of customers. The transfer or credit of securities covered by the agreement to the futures commission merchant's or derivatives clearing organization's customer segregated custodial account is made simultaneously with the disbursement of funds from the futures commission merchant's or derivatives clearing organization's customer segregated cash account at the custodian bank. On the sale or resale of securities, the futures commission merchant's or derivatives clearing organization's customer segregated cash account at the custodian bank must receive same-day funds credited to such segregated account simultaneously with the delivery or transfer of securities from the customer segregated custodial account.

(10) A written confirmation to the futures commission merchant or derivatives clearing organization specifying the terms of the agreement and a safekeeping receipt are issued immediately upon entering into the transaction and a confirmation to the futures commission merchant or derivatives clearing organization is issued once the transaction is reversed.

(11) The transactions effecting the agreement are recorded in the record required to be maintained under §1.27 of investments of customer funds, and the securities subject to such transactions are specifically identified in such record as described in paragraph (d)(1) of this section and further identified in such record as being subject to repurchase and reverse repurchase agreements.

(12) An actual transfer of securities to the customer segregated custodial account by book entry is made consistent with Federal or State commercial law, as applicable. At all times, securities received subject to an agreement are reflected as "customer property."

(13) The agreement makes clear that, in the event of the bankruptcy of the futures commission merchant or derivatives clearing organization, any securities purchased with customer funds that are subject to an agreement may be immediately transferred. The agreement also makes clear that, in the event of a futures commission merchant or derivatives clearing organization bankruptcy, the counterparty has no right to compel liquidation of securities subject to an agreement or to make a priority claim for the difference between current market value of the securities and the price agreed upon for resale of the securities to the counterparty, if the former exceeds the latter.

(e) *Deposit of firm-owned securities into segregation.* A futures commission merchant [shall not be prohibited from directly depositing] may deposit unencumbered securities of the type specified in this section, which it owns for its own account, into a [segregated safekeeping account or from transferring any such securities from a segregated account to its own account, up to the extent of its residual financial interest in customers' segregated funds; provided, however, that such investments] customer account. A futures commission merchant must include such securities, transfers of securities, and disposition of proceeds from the sale or maturity of such securities [are recorded] in the record of investments required to be maintained by §1.27. All such securities may be segregated in safekeeping only with a bank, trust company, derivatives clearing organization, or other registered futures commission merchant[. Furthermore, for] in accordance with the provisions of §1.20 part. For purposes of this section and §§[1.25, 1.26,] 1.27, 1.28, [and 1.29, investments permitted by §1.25] 1.29, and 1.32, securities of the type specified by this section that are owned by the futures commission merchant and deposited into [such a segregated] a customer account shall be considered customer funds until such investments are withdrawn from segregation in accordance with the provisions of §1.23. Investments permitted by §1.25 that are owned by the futures commission merchant and deposited into a futures customer account pursuant to §1.26 shall be considered futures customer funds until such investments are withdrawn from segregation in accordance with §1.23. Investments permitted by §1.25 that are owned by the futures commission merchant and deposited into a Cleared Swaps Customer Account, as defined in §22.1 of this chapter, shall be considered Cleared Swaps Customer Collateral, as defined in §22.1 of this chapter, until such investments are withdrawn from segregation in accordance with §22.17 of this chapter.

Appendix to §1.25 - Money Market Mutual Fund Prospectus Provisions Acceptable for Compliance With Section 1.25(c)(5)

Upon receipt of a proper redemption request submitted in a timely manner and otherwise in accordance with the redemption procedures set forth in this prospectus, the [Name of Fund] will redeem the requested shares and make a payment to you in satisfaction thereof no later than the business day following the redemption request. The [Name of Fund] may postpone and/or suspend redemption and payment beyond one business day only as follows:

- a. For any period during which there is a non-routine closure of the Fedwire or applicable Federal Reserve Banks;
- b. For any period (1) during which the New York Stock Exchange is closed other than customary week-end and holiday closings or (2) during which trading on the New York Stock Exchange is restricted;
- c. For any period during which an emergency exists as a result of which (1) disposal of securities owned by the [Name of Fund] is not reasonably practicable or (2) it is not reasonably practicable for the [Name of Fund] to fairly determine the net asset value of shares of the [Name of Fund];

- d. For any period during which the Securities and Exchange Commission has, by rule or regulation, deemed that (1) trading shall be restricted or (2) an emergency exists;
- e. For any period that the Securities and Exchange Commission, may by order permit for your protection; or
- f. For any period during which the [Name of Fund,] as part of a necessary liquidation of the fund, has properly postponed and/or suspended redemption of shares and payment in accordance with federal securities laws.

**[529] 530. Compliance with Commission Regulation 1.26 - Deposit of Instruments Purchased with Futures Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.26 that violates Commission Regulation 1.26 shall be deemed to have violated this Rule [529] 530. Commission Regulation 1.26 is set forth below and incorporated into this Rule [529] 530.

Commission Regulation 1.26 - Deposit of instruments purchased with futures customer funds.

[(a) Each futures commission merchant who invests customer funds in instruments described in §1.25 shall separately account for such instruments and segregate such instruments as belonging to such commodity or option customers. Such instruments, when deposited with a bank, trust company, clearing organization or another futures commission merchant, shall be deposited under an account name which clearly shows that they belong to commodity or option customers and are segregated as required by the Act and this part. Each futures commission merchant upon opening such an account shall obtain and retain in its files an acknowledgment from such bank, trust company, clearing organization or other futures commission merchant that it was informed that the instruments belong to commodity or option customers and are being held in accordance with the provisions of the Act and this part. *Provided, however,* that an acknowledgment need not be obtained from a clearing organization that has adopted and submitted to the Commission rules that provide for the segregation as customer funds, in accordance with all relevant provisions of the Act and the rules and orders promulgated thereunder, of all funds held on behalf of customers and all instruments purchased with customer funds. Such acknowledgment shall be retained in accordance with §1.31. Such bank, trust company, clearing organization or other futures commission merchant shall allow inspection of such obligations at any reasonable time by representatives of the Commission.]

(b) Each clearing organization which invests money belonging or accruing to commodity or option customers of its clearing members in instruments described in §1.25 shall separately account for such instruments and segregate such instruments as belonging to such commodity or option customers. Such instruments, when deposited with a bank or trust company, shall be deposited under an account name which will clearly show that they belong to commodity or option customers and are segregated as required by the Act and this part. Each clearing organization upon opening such an account shall obtain and retain in its files a written acknowledgment from such bank or trust company that it was informed that the instruments belong to commodity or option customers of clearing members and are being held in accordance with the provisions of the Act and this part. Such acknowledgment shall be retained in accordance with §1.31. Such bank or trust company shall allow inspection of such instruments at any reasonable time by representatives of the Commission.]

(a) Each futures commission merchant who invests futures customer funds in instruments described in §1.25, except for investments in money market mutual funds, shall separately account for such instruments as futures customer funds and segregate such instruments as funds belonging to such futures customers in accordance with the requirements of §1.20. Each derivatives clearing organization which invests money belonging or accruing to futures customers of its clearing members in instruments described in §1.25, except for investments in money market mutual funds, shall separately account for such instruments as customer funds and segregate such instruments as customer funds belonging to such futures customers in accordance with §1.20.

(b) Each futures commission merchant or derivatives clearing organization which invests futures customer funds in money market mutual funds, as permitted by §1.25, shall separately account for such funds and segregate such funds as belonging to such futures customers. Such funds shall be deposited under an account name that clearly shows that they belong to futures customers and are segregated as required by sections 4d(a) and 4d(b) of the Act and by this part. Each futures commission merchant or derivatives clearing organization, upon opening such an account, shall obtain and maintain readily accessible in its files in accordance with §1.31, for as long as the account remains open, and thereafter for the period provided in §1.31, a written acknowledgment and shall file such acknowledgment in accordance with the requirements of §1.20. In the event such funds are held directly with the money market mutual fund or its affiliate, the written acknowledgment shall be in the form as set out in Appendix A or B to this section. In the event such funds are held with a depository, the written acknowledgment shall be in the form as set out in Appendix A or B to §1.20. In either case, the written acknowledgment shall be obtained, provided to the Commission and designated self-regulatory organizations, and retained as required under §1.20.

APPENDIX A TO §1.26—FUTURES COMMISSION MERCHANT ACKNOWLEDGMENT LETTER FOR CFTC REGULATION 1.26 CUSTOMER SEGREGATED MONEY MARKET MUTUAL FUND ACCOUNT

[Date]

[Name and Address of Money Market Mutual Fund]

We propose to invest funds held by [Name of Futures Commission Merchant] ("we" or "our") on behalf of our customers in shares of [Name of Money Market Mutual Fund] ("you" or "your") under account(s) entitled (or shares issued to):

[Name of Futures Commission Merchant] [if applicable, add "FCM Customer Omnibus Account"] CFTC Regulation 1.26 Customer Segregated Money Market Mutual Fund Account under Sections 4d(a) and 4d(b) of the Commodity Exchange Act [and, if applicable, ", Abbreviated as [short title reflected in the depository's electronic system]" ]

Account Number(s): []

(collectively, the "Account(s)").

You acknowledge that we are holding these funds, including any shares issued and amounts accruing in connection therewith (collectively, the "Shares"), for the benefit of customers who trade commodities, options, swaps and other products ("Commodity Customers"), as required by Commodity Futures Trading Commission ("CFTC") Regulation 1.26, as amended; that the Shares held by you, hereafter deposited in the Account(s) or accruing to the credit of the Account(s), will be separately accounted for and segregated on your books from our own funds and from any other funds or accounts held by us in accordance with the provisions of the Commodity Exchange Act, as amended (the "Act"), and part 1 of the CFTC's regulations, as amended; and that the Shares must otherwise be treated in accordance with the provisions of Section 4d of the Act and CFTC regulations thereunder.

Furthermore, you acknowledge and agree that such Shares may not be used by you or by us to secure or guarantee any obligations that we might owe to you, and they may not be used by us to secure or obtain credit from you. You further acknowledge and agree that the Shares in the Account(s) shall not be subject to any right of offset or lien for or on account of any indebtedness, obligations or liabilities we may now or in the future have owing to you.

In addition, you agree that the Account(s) may be examined at any reasonable time by the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent or employee of our designated self-regulatory organization ("DSRO"), [Name of DSRO], and this letter constitutes the authorization and direction of the undersigned on our behalf to permit any such examination to take place without further notice to or consent from us.

You agree to reply promptly and directly to any request for confirmation of account balances or provision of any other account information regarding or related to the Account(s) from the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent, or employee of [Name of DSRO], acting in its capacity as our DSRO, and this letter constitutes the authorization and direction of the undersigned on our behalf to release the requested information without further notice to or consent from us.

You further acknowledge and agree that, pursuant to the authorization granted by us to you previously or herein, you have provided, or will provide following the opening of the Account(s), the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor division, or such director's designees, with technological connectivity, which may include provision of hardware, software, and related technology and protocol support, to facilitate direct, read-only electronic access to transaction and account balance information for the Account(s). This letter constitutes the authorization and direction of the undersigned on our behalf for you to establish this connectivity and access if not previously established, without further notice to or consent from us.

The parties agree that all actions on your part to respond to the above information and access requests will be made in accordance with, and subject to, such usual and customary authorization verification and authentication policies and procedures as may be employed by you to verify the authority of, and authenticate the identity of, the individual making any such information or access request, in order to provide for the secure transmission and delivery of the requested information or access to the appropriate recipient(s).

We will not hold you responsible for acting pursuant to any information or access request from the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC or the director of the Division of Clearing and Risk of the CFTC, or any successor divisions, or such directors' designees, or an appropriate officer, agent, or employee of [Name of DSRO], acting in its capacity as our DSRO, upon which you have relied after having taken measures in accordance with your applicable policies and procedures to assure that such request was provided to you by an individual authorized to make such a request.

In the event we become subject to either a voluntary or involuntary petition for relief under the U.S. Bankruptcy Code, we acknowledge that you will have no obligation to release the Shares held in the Account(s), except upon instruction of the Trustee in Bankruptcy or pursuant to the Order of the respective U.S. Bankruptcy Court.

Notwithstanding anything in the foregoing to the contrary, nothing contained herein shall be construed as limiting your right to assert any right of offset or lien on assets that are not Shares maintained in the Account(s), or to impose such charges against us or any proprietary account maintained by us with you. Further, it is understood that amounts represented by checks, drafts or other items shall not be considered to be part of the Account(s) until finally collected. Accordingly, checks, drafts and other items credited to the Account(s) and subsequently dishonored or otherwise returned to you or reversed, for any reason and any claims relating thereto, including but not limited to claims of alteration or forgery, may be charged back to the Account(s), and we shall be responsible to you as a general endorser of all such items whether or not actually so endorsed.

You may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry, provided that, in the ordinary course of your business as a depository, you have no notice of or actual knowledge of a potential violation by us of any provision of the Act or the CFTC regulations that relates to the segregation of customer funds; and you shall not in any manner not expressly agreed to herein be responsible to us for ensuring compliance by us with such provisions of the Act and CFTC regulations; however, the aforementioned presumption does not affect any obligation you may otherwise have under the Act or CFTC regulations.

You may, and are hereby authorized to, obey the order, judgment, decree or levy of any court of competent jurisdiction or any governmental agency with jurisdiction, which order, judgment, decree or levy relates in whole or in part to the Account(s). In any event, you shall not be liable by reason of any action or omission to act pursuant to such order, judgment, decree or levy, to us or to any other person, firm, association or corporation even if thereafter any such order, decree, judgment or levy shall be reversed, modified, set aside or vacated.

We are permitted to invest customers' funds in money market mutual funds pursuant to CFTC Regulation 1.25. That rule sets forth the following conditions, among others, with respect to any investment in a money market mutual fund:

- (1) The net asset value of the fund must be computed by 9:00 a.m. of the business day following each business day and be made available to us by that time;
- (2) The fund must be legally obligated to redeem an interest in the fund and make payment in satisfaction thereof by the close of the business day following the day on which we make a redemption request except as otherwise specified in CFTC Regulation 1.25(c)(5)(ii); and,
- (3) The agreement under which we invest customers' funds must not contain any provision that would prevent us from pledging or transferring fund shares.

The terms of this letter agreement shall remain binding upon the parties, their successors and assigns, and for the avoidance of doubt, regardless of a change in the name of either party. This letter agreement supersedes and replaces any prior agreement between the parties in connection with the Account(s), including but not limited to any prior acknowledgment letter agreement, to the extent that such prior agreement is inconsistent with the terms hereof. In the event of any conflict between this letter agreement and any other agreement between the parties in connection with the Account(s), this letter agreement shall govern with respect to matters specific to Section 4d of the Act and the CFTC's regulations thereunder, as amended.

This letter agreement shall be governed by and construed in accordance with the laws of [Insert governing law] without regard to the principles of choice of law.

Please acknowledge that you agree to abide by the requirements and conditions set forth above by signing and returning to us the enclosed copy of this letter agreement, and that you further agree to provide a copy of this fully executed letter agreement directly to the CFTC (via electronic means in a format and manner determined by the CFTC) and to [Name of DSRO], acting in its capacity as our DSRO, in accordance with CFTC Regulation 1.20. We hereby authorize and direct you to provide such copies without further notice to or consent from us, no later than three business days after opening the Account(s) or revising this letter agreement, as applicable.

[Name of Futures Commission Merchant]

By:

Print Name:

Title:

ACKNOWLEDGED AND AGREED:

[Name of Money Market Mutual Fund]

By:

Print Name:

Title:

Contact Information: [Insert phone number and email address]

Date:

APPENDIX B TO §1.26—DERIVATIVES CLEARING ORGANIZATION ACKNOWLEDGMENT  
LETTER FOR CFTC REGULATION 1.26 CUSTOMER SEGREGATED MONEY MARKET  
MUTUAL FUND ACCOUNT

[Date]

[Name and Address of Money Market Mutual Fund]

We propose to invest funds held by [Name of Derivatives Clearing Organization] ("we" or "our") on behalf of customers in shares of [Name of Money Market Mutual Fund] ("you" or "your") under account(s) entitled (or shares issued to):

[Name of Derivatives Clearing Organization] Futures Customer Omnibus Account, CFTC Regulation 1.26 Customer Segregated Money Market Mutual Fund Account under Sections 4d(a) and 4d(b) of the Commodity Exchange Act [and, if applicable, " Abbreviated as [short title reflected in the depository's electronic system]" ]

Account Number(s): []

(collectively, the "Account(s)").

You acknowledge that we are holding these funds, including any shares issued and amounts accruing in connection therewith (collectively, the "Shares"), for the benefit of customers who trade commodities, options, swaps and other products, as required by Commodity Futures Trading Commission ("CFTC") Regulation 1.26, as amended; that the Shares held by you, hereafter deposited in the Account(s) or accruing to the credit of the Account(s), will be separately accounted for and segregated on your books from our own funds and from any other funds or accounts held by us in accordance with the provisions of the Commodity Exchange Act, as amended (the "Act"), and part 1 of the CFTC's regulations, as amended; and that the Shares must otherwise be treated in accordance with the provisions of Section 4d of the Act and CFTC regulations thereunder.

Furthermore, you acknowledge and agree that such Shares may not be used by you or by us to secure or guarantee any obligations that we might owe to you, and they may not be used by us to secure or obtain credit from you. You further acknowledge and agree that the Shares in the Account(s) shall not be subject to any right of offset or lien for or on account of any indebtedness, obligations or liabilities we may now or in the future have owing to you.

You agree to reply promptly and directly to any request for confirmation of account balances or provision of any other account information regarding or related to the Account(s) from the director of the Division of Clearing and Risk of the CFTC or the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor divisions, or such directors' designees, and this letter constitutes the authorization and direction of the undersigned on our behalf to release the requested information without further notice to or consent from us.

The parties agree that all actions on your part to respond to the above information requests will be made in accordance with, and subject to, such usual and customary authorization verification and authentication policies and procedures as may be employed by you to verify the authority of, and authenticate the identity of, the individual making any such information request, in order to provide for the secure transmission and delivery of the requested information to the appropriate recipient(s).

We will not hold you responsible for acting pursuant to any information request from the director of the Division of Clearing and Risk of the CFTC or the director of the Division of Swap Dealer and Intermediary Oversight of the CFTC, or any successor divisions, or such directors' designees, upon which you have relied after having taken measures in accordance with your applicable policies and procedures to assure that such request was provided to you by an individual authorized to make such a request.

In the event that we or any of our futures commission merchant clearing members become(s) subject to either a voluntary or involuntary petition for relief under the U.S. Bankruptcy Code, we acknowledge that you will have no obligation to release the Shares held in the Account(s), except upon instruction of the Trustee in Bankruptcy or pursuant to the Order of the respective U.S. Bankruptcy Court.

Notwithstanding anything in the foregoing to the contrary, nothing contained herein shall be construed as limiting your right to assert any right of offset or lien on assets that are not Shares maintained in the Account(s), or to impose such charges against us or any proprietary account maintained by us with you. Further, it is understood that amounts represented by checks, drafts or other items shall not be considered to be part of the Account(s) until finally collected. Accordingly, checks, drafts and other items credited to the Account(s) and subsequently dishonored or otherwise returned to you, or reversed, for any reason and any claims relating thereto, including but not limited to claims of alteration or forgery, may be charged back to the Account(s), and we shall be responsible to you as a general endorser of all such items whether or not actually so endorsed.

You may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry, provided that, in the ordinary course of your business as a depository, you have no notice of or actual knowledge of a potential violation by us of any provision of the Act or the CFTC regulations that relates to the segregation of customer funds; and you shall not in any manner not expressly agreed to herein be responsible to us for ensuring compliance by us with such provisions of the Act and CFTC regulations; however, the aforementioned presumption does not affect any obligation you may otherwise have under the Act or CFTC regulations.

You may, and are hereby authorized to, obey the order, judgment, decree or levy of any court of competent jurisdiction or any governmental agency with jurisdiction, which order, judgment, decree or levy relates in whole or in part to the Account(s). In any event, you shall not be liable by reason of any action or omission to act pursuant to any such order, judgment, decree or levy, to us or to any other person, firm, association or corporation even if thereafter any such order, decree, judgment or levy shall be reversed, modified, set aside or vacated.

We are permitted to invest customers' funds in money market mutual funds pursuant to CFTC Regulation 1.25. That rule sets forth the following conditions, among others, with respect to any investment in a money market mutual fund:

(1) The net asset value of the fund must be computed by 9:00 a.m. of the business day following each business day and be made available to us by that time;

(2) The fund must be legally obligated to redeem an interest in the fund and make payment in satisfaction thereof by the close of the business day following the day on which we make a redemption request except as otherwise specified in CFTC Regulation 1.25(c)(5)(ii); and,

(3) The agreement under which we invest customers' funds must not contain any provision that would prevent us from pledging or transferring fund shares.

The terms of this letter agreement shall remain binding upon the parties, their successors and assigns, and for the avoidance of doubt, regardless of a change in the name of either party. This letter agreement supersedes and replaces any prior agreement between the parties in connection with the Account(s), including but not limited to any prior acknowledgment letter agreement, to the extent that such prior agreement is inconsistent with the terms hereof. In the event of any conflict between this letter agreement and any other agreement between the parties in connection with the Account(s), this letter agreement shall govern with respect to matters specific to Section 4d of the Act and the CFTC's regulations thereunder, as amended.

This letter agreement shall be governed by and construed in accordance with the laws of [Insert governing law] without regard to the principles of choice of law.

Please acknowledge that you agree to abide by the requirements and conditions set forth above by signing and returning to us the enclosed copy of this letter agreement, and you further agree to provide a copy of this fully executed letter agreement directly to the CFTC (via electronic means in a format and manner determined by the CFTC) in accordance with CFTC Regulation 1.20. We hereby authorize and direct you to provide such copies without further notice to or consent from us, no later than three business days after opening the Account(s) or revising this letter agreement, as applicable.

[Name of Derivatives Clearing Organization]

By:

Print Name:

Title:

ACKNOWLEDGED AND AGREED:

[Name of Money Market Mutual Fund]

By:

Print Name:

Title:

Contact Information: [Insert phone number and email address]

Date:

### **[530] 531. Compliance with Commission Regulation 1.27 - Record of Investments**

Any Trading Privilege Holder subject to Commission Regulation 1.27 that violates Commission Regulation 1.27 shall be deemed to have violated this Rule [530] 531. Commission Regulation 1.27 is set forth below and incorporated into this Rule [530] 531.

\* \* \* \* \*

### **[531] 532. Compliance with Commission Regulation 1.28 - Appraisal of Instruments Purchased with Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.28 that violates Commission Regulation 1.28 shall be deemed to have violated this Rule [531] 532. Commission Regulation 1.28 is set forth below and incorporated into this Rule [531] 532.

\* \* \* \* \*

**[532] 533. Compliance with Commission Regulation 1.29 – [Increment of Interest] Gains and Losses Resulting from Investment of Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.29 that violates Commission Regulation 1.29 shall be deemed to have violated this Rule [532] 533. Commission Regulation 1.29 is set forth below and incorporated into this Rule [532] 533.

Commission Regulation 1.29 – [Increment of interest] Gains and losses resulting from investment of customer funds.

(a) The investment of customer funds in instruments described in §1.25 shall not prevent the futures commission merchant or derivatives clearing organization so investing such funds from receiving and retaining as its own any [increment] incremental income or interest income resulting therefrom.

(b) The futures commission merchant or derivatives clearing organization, as applicable, shall bear sole responsibility for any losses resulting from the investment of customer funds in instruments described in §1.25. No investment losses shall be borne or otherwise allocated to the customers of the futures commission merchant and, if customer funds are invested by a derivatives clearing organization in its discretion, to the futures commission merchant.

**[533] 534. Compliance with Commission Regulation 1.30 - Loans by Futures Commission Merchants; Treatment of Proceeds**

Any Trading Privilege Holder subject to Commission Regulation 1.30 that violates Commission Regulation 1.30 shall be deemed to have violated this Rule [533] 534. Commission Regulation 1.30 is set forth below and incorporated into this Rule [533] 534.

Commission Regulation 1.30 - Loans by futures commission merchants; treatment of proceeds.

Nothing in [these] the regulations in this chapter shall prevent a futures commission merchant from lending its own funds to [commodity or option] customers on securities and property pledged by such [commodity or option] customers, or from repledging or selling such securities and property pursuant to specific written agreement with such [commodity or option] customers. The proceeds of such loans used to purchase, margin, guarantee, or secure the trades, contracts, or commodity options of [commodity or option] customers shall be treated and dealt with by a futures commission merchant as belonging to such [commodity or option] customers, in accordance with and subject to the provisions of [section 4d(a)(2) of] the Act and these regulations. A futures commission merchant may not loan funds on an unsecured basis to finance customers' trading, nor may a futures commission merchant loan funds to customers secured by the customer accounts of such customers.

**[534] 535. Compliance with Commission Regulation 1.31 - Books and Records; Keeping and Inspection**

Any Trading Privilege Holder subject to Commission Regulation 1.31 that violates Commission Regulation 1.31 shall be deemed to have violated this Rule [534] 535. Commission Regulation 1.31 is set forth below and incorporated into this Rule [534] 535.

\* \* \* \* \*

**[535] 536. Compliance with Commission Regulation 1.32 – [Segregated Account; Daily Computation and Record]**  
**Reporting of Segregated Account Computation and Details Regarding the Holding of Futures Customer Funds**

Any Trading Privilege Holder subject to Commission Regulation 1.32 that violates Commission Regulation 1.32 shall be deemed to have violated this Rule [535] 536. Commission Regulation 1.32 is set forth below and incorporated into this Rule [535] 536.

[Commission Regulation 1.32 - Segregated account; daily computation and record.

(a) Each futures commission merchant must compute as of the close of each business day, on a currency-by-currency basis:

(1) The total amount of customer funds on deposit in segregated accounts on behalf of commodity and option customers;

(2) the amount of such customer funds required by the Act and these regulations to be on deposit in segregated accounts on behalf of such commodity and option customers; and

(3) the amount of the futures commission merchant's residual interest in such customer funds.

(b) In computing the amount of funds required to be in segregated accounts, a futures commission merchant may offset any net deficit in a particular customer's account against the current market value of readily marketable securities, less applicable percentage deductions (*i.e.*, "securities haircuts") as set forth in Rule 15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 241.15c3-1(c)(2)(vi)), held for the same customer's account. The futures commission merchant must maintain a security interest in the securities, including a written authorization to liquidate the securities at the futures commission merchant's discretion, and must segregate the securities in a safekeeping account with a bank, trust company, clearing organization of a contract market, or another futures commission merchant. For purposes of this section, a security will be considered readily marketable if it is traded on a "ready market" as defined in Rule 15c3-1(c)(11)(i) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(11)(i)).

(c) The daily computations required by this section must be completed by the futures commission merchant prior to noon on the next business day and must be kept, together with all supporting data, in accordance with the requirements of §1.31.]

Commission Regulation 1.32 – Reporting of segregated account computation and details regarding the holding of futures customer funds

(a) Each futures commission merchant must compute as of the close of each business day, on a currency-by-currency basis:

(1) The total amount of futures customer funds on deposit in segregated accounts on behalf of futures customers;

(2) The amount of such futures customer funds required by the Act and these regulations to be on deposit in segregated accounts on behalf of such futures customers; and

(3) The amount of the futures commission merchant's residual interest in such futures customer funds.

(b) In computing the amount of futures customer funds required to be in segregated accounts, a futures commission merchant may offset any net deficit in a particular futures customer's account against the current market value of readily marketable securities, less applicable deductions (i.e., "securities haircuts") as set forth in Rule 15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 241.15c3-1(c)(2)(vi)), held for the same futures customer's account. Futures commission merchants that establish and enforce written policies and procedures to assess the credit risk of commercial paper, convertible debt instruments, or nonconvertible debt instruments in accordance with Rule 240.15c3-1(c)(2)(vi) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(2)(vi)) may apply the lower haircut percentages specified in Rule 240.15c3-1(c)(2)(vi) for such commercial paper, convertible debt instruments and nonconvertible debt instruments. The futures commission merchant must maintain a security interest in the securities, including a written authorization to liquidate the securities at the futures commission merchant's discretion, and must segregate the securities in a safekeeping account with a bank, trust company, derivatives clearing organization, or another futures commission merchant. For purposes of this section, a security will be considered readily marketable if it is traded on a "ready market" as defined in Rule 15c3-1(c)(11)(i) of the Securities and Exchange Commission (17 CFR 240.15c3-1(c)(11)(i)).

(c) Each futures commission merchant is required to document its segregation computation required by paragraph (a) of this section by preparing a Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges contained in the Form 1-FR-FCM as of the close of each business day. Nothing in this paragraph shall affect the requirement that a futures commission merchant at all times maintain sufficient money, securities and property to cover its total obligations to all futures customers, in accordance with §1.20.

(d) Each futures commission merchant is required to submit to the Commission and to the firm's designated self-regulatory organization the daily Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges required by paragraph (c) of this section by noon the following business day.

(e) Each futures commission merchant shall file the Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges required by paragraph (c) of this section in an electronic format using a form of user authentication assigned in accordance with procedures established or approved by the Commission.

(f) Each futures commission merchant is required to submit to the Commission and to the firm's designated self-regulatory organization a report listing the names of all banks, trust companies, futures commission merchants, derivatives clearing organizations, or any other depository or custodian holding futures customer funds as of the fifteenth day of the month, or the first business day thereafter, and the last business day of each month. This report must include:

(1) The name and location of each entity holding futures customer funds;

(2) The total amount of futures customer funds held by each entity listed in paragraph (f)(1) of this section; and

(3) The total amount of cash and investments that each entity listed in paragraph (f)(1) of this section holds for the futures commission merchant. The futures commission merchant must report the following investments:

(i) Obligations of the United States and obligations fully guaranteed as to principal and interest by the United States (U.S. government securities);

(ii) General obligations of any State or of any political subdivision of a State (municipal securities);

(iii) General obligation issued by any enterprise sponsored by the United States (government sponsored enterprise securities);

(iv) Certificates of deposit issued by a bank;

(v) Commercial paper fully guaranteed as to principal and interest by the United States under the Temporary Liquidity Guarantee Program as administered by the Federal Deposit Insurance Corporation;

(vi) Corporate notes or bonds fully guaranteed as to principal and interest by the United States under the Temporary Liquidity Guarantee Program as administered by the Federal Deposit Insurance Corporation; and

(vii) Interests in money market mutual funds.

(g) Each futures commission merchant must report the total amount of futures customer-owned securities held by the futures commission merchant as margin collateral and must list the names and locations of the depositories holding such margin collateral.

(h) Each futures commission merchant must report the total amount of futures customer funds that have been used to purchase securities under agreements to resell the securities (reverse repurchase transactions).

(i) Each futures commission merchant must report which, if any, of the depositories holding futures customer funds under paragraph (f)(1) of this section are affiliated with the futures commission merchant.

(j) Each futures commission merchant shall file the detailed list of depositories required by paragraph (f) of this section by 11:59 p.m. the next business day in an electronic format using a form of user authentication assigned in accordance with procedures established or approved by the Commission.

(k) Each futures commission merchant shall retain its daily segregation computation and the Statement of Segregation Requirements and Funds in Segregation for Customers Trading on U.S. Commodity Exchanges required by paragraph (c) of this section, and its detailed list of depositories required by paragraph (f) of this section, together with all supporting documentation, in accordance with the requirements of §1.31.

**[536] 537. Compliance with Commission Regulation 1.36 -  
Record of Securities and Property Received from  
Customers and Options Customers**

Any Trading Privilege Holder subject to Commission Regulation 1.36 that violates Commission Regulation 1.36 shall be deemed to have violated this Rule [536] 537. Commission Regulation 1.36 is set forth below and incorporated into this Rule [536] 537.

\* \* \* \* \*

Questions regarding this submission may be directed to Arthur Reinstein at (312) 786-7570 or Eric Seinsheimer at (312) 786-8740. Please reference our submission number CFE-2014-07 in any related correspondence.

CBOE Futures Exchange, LLC



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cc: Nancy Markowitz (CFTC)