

CFTC Letter No. 00-48

April 3, 2000

Interpretation

Division of Trading and Markets

Re: Part 30: London Metal Exchange - - Request for Clarification
Regarding Customer Fund
Segregation Rules

Dear :

This is in response to your recent correspondence with Andrea Corcoran, Director, Office of International Affairs, as supplemented by telephone conversations with Commodity Futures Trading Commission ("Commission") staff. By your correspondence, as supplemented, you request confirmation that The London Metal Exchange Limited ("LME") member firms ("LME Firms") may segregate United States customers' funds used for trading the LMEX contract on the LME in the manner described in the May 15, 1989 Rule 30.10¹ Order ("UK 30.10 Order") issued to the Association of Futures Brokers and Dealers ("AFBD").²

A firm operating under the UK 30.10 Order currently must agree to a segregation provision which provides that the firm:

consents to refuse customers resident in the United States the option of not segregating funds notwithstanding relevant provisions of the United Kingdom regulatory system and to provide all customers resident in the United States no less stringent regulatory protection than that provided to United Kingdom customers under all relevant provisions of United Kingdom law, *or, in the case of business done on the London Metal Exchange only, agrees to maintain a binding letter of credit(s) or bank guarantee(s) to cover forward profits and clearing exposures on the London Metal Exchange, drawn in favor of "X", pursuant to the terms set forth in the letter dated October 10, 1989 from the Division of Trading and Markets, Commodity Futures Trading Commission.* (emphasis added)

The non-italicized portion of the above representation is the segregation provision prescribed by the UK

30.10 Order ("Standard Segregation Provision").³ The italicized portion of the representation ("Alternative Segregation Provision") was added as a result of the October 10, 1989 letter from the Commission's Division of Trading and Markets ("Division") to the AFBD ("October 10 No-Action Letter") wherein the Division stated that it would not recommend enforcement action against LME Firms doing business on the LME if those firms complied with the Alternative Segregation Provision in lieu of complying with the Standard Segregation Provision.⁴

In issuing the October 10 No-Action Letter, the Division stated that:

in view of the fact that the LME is not a cash cleared market, and of the use of letters of credit or bank guarantees to cover forward profits and clearing exposure at the LME, the Division believes that such a form of security for customer obligations marked to market is not unacceptable.

The LMEX contract, however, will be cash cleared, and we concur with your view that it would be prudent to require use of the Standard Segregation Provision with respect to LMEX transactions rather than the Alternative Segregation Provision. Accordingly, the Division confirms that, for United States customers trading the LMEX contract, LME Firms may comply with the Standard Segregation Provision rather than with the Alternative Segregation Provision. Further, because LME Firms are allowed generally to comply with the Alternative Segregation Provision as a result of the October 10 No-Action Letter, those firms may choose to proceed under that letter with respect to all LME contracts other than the LMEX contract and to comply with the Standard Segregation Provision for the LMEX contract, even if the same customer is involved. We understand that firm records would clearly identify the amounts to which each segregation provision applied, and that, as the Standard Segregation Provision would be applied pursuant to LME and Securities and Futures Authority rules to LMEX contracts, customers would understand how United Kingdom segregation would be achieved.

This letter, and the position outlined herein, are based upon the representations that you have made to us. Any different, changed, or omitted material facts or circumstances might render this position void. You must notify us immediately in the event that the operations or activities of the LME change in any material way from those represented to us. Further, this letter represents the position of the Division only. It does not necessarily reflect the views of the Commission or any other division or office of the Commission.

If you have any questions concerning this correspondence, please contact Lawrence B. Patent, Associate Chief Counsel, at (202) 418-5439.

Very truly yours,

John C. Lawton
Acting Director

1 Commission Rules referred to herein are found at 17 C.F.R. Ch. I (1999).

2 *See* 54 Fed. Reg. 21604 (May 19, 1989).

3 *Id.* at 21606.

4 CFTC Staff Letter from Andrea M. Corcoran, Director, Division of Trading and Markets, to The Honorable Christopher J. Sharples, Chairman, Association of Futures Brokers and Dealers, dated October 10, 1989 [unpublished].