

CFTC Letter No. 97-47**June 16, 1997****Division of Trading & Markets**

Re: Segregated Bank Account in Germany

Dear :

This is in response to your letter dated May 28, 1997 submitted on behalf of X , a registered futures commission merchant (FCM), as supplemented by telephone conversations with myself and Division staff. In your letter, you stated that X would like to open a segregated bank account in Germany that would be used to facilitate the process of receiving and paying funds from and to X s foreign customers. You requested that the requirement that X obtain a subordination agreement from foreign customers in accordance with Division Financial and Segregation Interpretation No. 12 (Interp. 12)¹ in these circumstances be waived since X has no U.S. customers.

Based upon the representations in your letter, as supplemented, we understand the relevant facts to be as follows. X s customers are predominantly German, generally high income persons, and X has no U.S. customers.² Typically, a German customer would pay X Deutsche marks in connection with trading on U.S. contract markets, although certain non-U.S. customers deal with X exclusively in dollars. These Deutsche marks would be deposited into X s customer segregated account in Germany and then converted into dollars for transfer to X s segregated account in New York under the normal two business day currency conversion process.³ When a German customer is owed funds, Deutsche marks will usually be sent by wire transfer or by check from X s New York segregated account to X s segregated account in Frankfurt, Germany. These funds will generally be available to the customer the following business day due to the time differences between New York and Frankfurt. The customer could direct that the funds be transferred to the customer s account at another German bank or, if dollars rather than Deutsche marks are requested by the customer, the bank holding X s segregated account in New York will transfer dollars to its own correspondent bank in Germany for distribution to the German customer. You stated in your letter that X does not intend to use the German segregated account to hold balances and expects daily activity in the account to pay and to receive funds from customers.

Interp. 12 provided, among other things, that beginning six months after its issuance, an FCM will not be permitted to hold in a customer segregated account foreign currency deposited by a foreign-domiciled customer in connection with trading on or subject to the rules of a United States

contract market, unless the customer has signed a subordination agreement as set forth in Interp. 12.⁴

The Division's purpose in requiring a subordination agreement under Interp. 12 was to shield customers who deposit funds with an FCM in a particular currency to be held in a particular country from bearing the exchange rate and location risks attendant to other currencies and other countries, in the unlikely circumstances where the FCM is placed in receivership or bankruptcy and there are insufficient funds available for distribution denominated in such other currencies to satisfy customer claims against those funds. The principal impetus for the requirement was to protect the funds and claims of U.S. customers depositing dollars with an FCM to be held in the U.S., where the FCM also has foreign customers or U.S. customers trading in contracts traded on or subject to the rules of a U.S. contract market but denominated in a foreign currency, in which case the FCM will also hold customer funds in currencies other than U.S. dollars outside of the U.S. Since X has no U.S. customers, the Division is prepared to grant relief from the subordination agreement requirement subject to the condition that X continue to have no U.S. customers.

We further note that Interp. 12 states that one of the principles a subordination agreement requirement is designed to effectuate is that [n]o customer whose funds are held in a particular foreign currency may receive less than his pro-rata share of the funds held in that foreign currency as a result of the shortfall or unavailability of funds held in an account denominated in another foreign currency. Thus, even if X has no U.S. customers, to the extent that X has customers who use dollars exclusively and others who have deposited Deutsche marks with X, there could be an adverse impact on non-U.S. customers depositing dollars exclusively if X were to be placed in receivership or bankruptcy and there are insufficient Deutsche marks to satisfy the claims of customers who have deposited that currency with X, even if there were sufficient dollars available to satisfy the claims of the former group of customers. See Example 5 of Interp. 12. Therefore, we will further condition relief from the subordination agreement requirement under Interp. 12 upon X providing notice to all customers as required under Commission Rule 190.10(c)⁵ with respect to the deposit of non-cash margin to the effect that all property available for distribution to customers in the event of X's bankruptcy is subject to pro rata distribution.⁶

In light of the foregoing, the Division will not recommend that the Commission commence enforcement action against X pursuant to Section 4d(2) of the Act and rules promulgated thereunder⁷ based solely upon X's failure to obtain a subordination agreement from X's foreign customers in accordance with Interp. 12. This relief is subject to the conditions that: (1) X continue to have no U.S. customers; and (2) X provide each new customer at the time of account opening, and each existing customer with the next monthly or quarterly account statement pursuant to Commission Rule 1.33(a),⁸ with the statement required by Commission Rule 190.10(c), unless such statement has already been provided to the customer.⁹

This letter is based upon the representations made to us and is subject to compliance with the conditions set forth above. Any different, changed or omitted facts or circumstances might require us to reach a different conclusion. In this connection, we request that you notify us immediately in the event that the facts and circumstances pertaining to this issue differ in any respect from those as represented to us. This letter represents the views of this Division only and does not necessarily represent the views of the Commission or any other office or division of the Commission. If you have any questions concerning this correspondence, please contact me, Deputy Director Paul H. Bjarnason, Jr., or Associate Chief Counsel Lawrence B. Patent at (202) 418-5430.

Very truly yours,

Andrea M. Corcoran

Director

¹ 1 Comm. Fut. L. Rep. (CCH) ¶ 7122 (Nov. 16, 1988).

² In a telephone conversation with Division staff, you indicated that none of X's customers are U.S. residents but that one or two customers might be U.S. citizens living abroad. For purposes of this letter, we will consider the phrase "X has no U.S. customers" to mean no customers residing in the U.S.

³ On those occasions when German customers pay X in dollars, those funds are sent directly to X's segregated account in New York without passing through X's German segregated account.

⁴ Interp. 12 at 7141.

⁵ 17 C.F.R. §190.10(c) (1996).

⁶ You have indicated that X routinely provides this notice with its account opening documents.

⁷ 17 C.F.R. §1.33(a) (1996).

⁸ See 17 C.F.R. §§1.20-1.30, 1.32 and 1.36 (1996).

⁹ This statement may be presented to a non-English speaking customer in the foreign language that such customer understands rather than in English, provided that the statement provided is an accurate translation of the English version and that the English text is provided upon request. Further, the Division will not require a separate acknowledgment of this statement. See 58 Fed. Reg. 17495, 17497, 17498 (Apr. 5, 1993).