COMMODITY FUTURES TRADING COMMISSION

17 CFR Parts 1, 4, 41, and 190

RIN 3038–AE67

Bankruptcy Regulations

AGENCY: Commodity Futures Trading Commission.

ACTION: Final rule.

SUMMARY: The Commodity Futures Trading Commission (the ''Commission'') is amending its regulations governing bankruptcy proceedings of commodity brokers. The amendments are meant comprehensively to update those regulations to reflect current market practices and lessons learned from past commodity broker bankruptcies.

DATES:

Effective date: The effective date for this final rule is May 13, 2021.

Compliance date: The compliance date for § 1.43 is April 13, 2022, for all letters of credit accepted, and customer agreements entered into, by a futures commission merchant prior to May 13, 2021.

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I. Background

A. Background of the Notice of Proposed Rulemaking

The basic structure of the Commission's bankruptcy regulations, part 190 of title 17 of the Code of Federal Regulations, was proposed in 1981 and finalized in 1983. In April of this year, the Commission proposed a comprehensive revision of part 190 (the ''Proposal''),[1] and in September of this year, the Commission issued a supplemental proposal (the ''Supplemental Proposal'')[2] addressing a particular issue involving the interaction between bankruptcy and resolution of a clearing organization pursuant to Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act[3] (hereinafter, ''Title II'' and ''Dodd-Frank'').

The Commission is revising part 190 comprehensively in light of several major changes to the industry over the 37 years since part 190 was first finalized. These changes include exponential growth in the speed of transactions and trade processing, important lessons learned over prior bankruptcies, and the increased importance of derivatives clearing organizations (''DCOs'') to the financial system.

In promulgating these rules, the Commission is exercising its broad power under the Commodity Exchange Act (''CEA'' or ''Act'') to make regulations with respect to commodity broker debtors. Specifically, section 20(a) states that notwithstanding title 11, the Commission may provide, with respect to a commodity broker that is a debtor under chapter 7 of title 11, by rule or regulation (1) that certain cash, securities, other property, or commodity contracts are to be included in or excluded from customer property or member property; (2) that certain cash, securities, other property, or commodity contracts are to be specifically identifiable to a particular customer in a specific capacity; (3) the method by which the business of such commodity broker is to be conducted or liquidated after the date of the filing of the petition under such chapter, including the payment and allocation of margin with respect to commodity contracts not specifically identifiable to a particular customer pending their orderly liquidation; (4) any persons to which customer property and commodity contracts may be transferred under section 766 of title 11; and (5) how the net equity of a customer is to be determined.[4]

In developing this rulemaking, the Commission benefited from outside contributions. In particular, the Proposal benefited from a thoughtful and detailed model set of part 190 rules submitted by the Part 190 Subcommittee of the Business Law Section of the American Bar Association (''ABA Subcommittee'').[5] In addition, and as discussed further below, the Commission benefited from thoughtful, analytical, and detailed public comments submitted in response to the Proposal and Supplemental Proposal.

B. Major Themes in the Revisions to Part 190

The major themes in the revisions to part 190 include the following:

(1) The Commission is adding § 190.00, which sets out the statutory authority, organization, core concepts, scope, and rules of construction for part 190. More generally, this section sets out, after notice and comment rulemaking, the Commission's thinking and intent regarding part 190 in order to benefit and to enhance the understanding of DCOs, FCMs, their customers, trustees,[6] and the public at large.

(2) Some of the provisions support the implementation of the requirements, established consistent with section 4d of the CEA, that shortfalls in segregated property should be made up from the FCM's general assets, while others further the preferences, arising from both title 11 of the United States Code (*i.e.,* the ''Bankruptcy Code''), section 766(h), and Commission policy, that with respect to customer property, public customers are favored over non-public customers, and that public customers are entitled *inter se* to a *pro rata* distribution based on their respective claims.

(3) Other provisions foster the longstanding and continuing policy preference for transferring (as opposed to liquidating) positions of public customers and those customers' proportionate share of associated collateral.[7]

(4) The Commission is promulgating a new subpart C to part 190, governing the bankruptcy of a clearing organization. In doing so, the Commission is establishing *ex ante* the approach to be taken in addressing such a bankruptcy, in order to foster prompt action in the event such a bankruptcy occurs, and in order to establish a more clear counterfactual (*i.e.,* ''what would creditors receive in a liquidation in bankruptcy?'') in the event of a resolution of a clearing organization pursuant to Title II of Dodd-Frank.[8] The Commission's approach toward a DCO bankruptcy is characterized by three overarching concepts:

a. First, the trustee should follow, to the extent practicable and appropriate, the DCO's pre-existing default management rules and procedures and recovery and wind-down plans that have been submitted to the Commission. These rules, procedures, and plans will, in most cases,[9] have been developed pursuant to the Commission's regulations in part 39, and subject to staff oversight. This approach relieves the trustee of the burden of developing, in the moment, models to address an extraordinarily complex situation. It would also enhance the clarity of the counterfactual for purposes of resolution under Title II. However, as discussed further below, such plans are not rigid formulae. Moreover, the Commission's approach gives the trustee discretion in following those plans. Accordingly, the approach seeks to balance advance planning with flexibility to tailor the implementation to the specific circumstances.

b. Second, resources that are intended to flow through to members as part of daily settlement (including both daily variation payments and default resources) are devoted to that purpose, rather than to the general estate.[10]

c. Third, other provisions draw, with appropriate adaptations, from provisions applicable to FCMs.[11]

(5) The Commission is noting the applicability of part 190 in the context

[1] 85 FR 36000 (June 12, 2020).

[2] 85 FR 60110 (Sept. 24, 2020).

[3] Public Law 111–203 (July 21, 2010).

[4] *See* CEA section 20(a), 7 U.S.C. 24(a).

[5] The submission by the ABA Subcommittee cautioned that ''[t]he views expressed in this letter, and the proposed Model Part 190 Rules, are presented on behalf of the [ABA Subcommittee]. They have not been approved by the House of Delegates or Board of Governors of the ABA and, accordingly, should not be construed as representing the policy of the ABA. In addition, they do not represent the position of the ABA Business Law Section, nor do they necessarily reflect the views of all members of the Committee.''

[6] Including bankruptcy and SIPA trustees, as well as the FDIC in its role as a receiver.

[7] This policy preference is manifest in section 764(b) of the Bankruptcy Code, 11 U.S.C. 764(b) (protecting from avoidance transfers approved by the Commission up to seven days *after* the order for relief), and in current § 190.02(e).

[8] Section 210(d)(2), 12 U.S.C. 5390(d)(2), provides that the maximum liability of the FDIC, acting as a receiver for a covered financial company in a resolution under Title II, is the amount the claimant would have received if the FDIC had not been appointed receiver and the covered financial company had instead been liquidated under chapter 7 of the Bankruptcy Code. Thus, in developing resolution strategies for a DCO while mitigating claims against the FDIC as receiver, it is important to understand what would happen if the DCO was instead liquidated pursuant to chapter 7 of the Bankruptcy Code (and this part 190), and such a liquidation is the counterfactual to resolution of that DCO under Title II.

[9] Only those DCOs that are subject to subpart C of part 39 (*i.e.,* those that have been designated as systemically important by the Financial Stability Oversight Council (FSOC) or that have elected to be subject to subpart C of part 39) are subject to § 39.35 (default rules and procedures) and § 39.39 (recovery and wind-down plans).

[10] *See generally* § 190.19.

[11] *See, e.g.,* §§ 190.16, 190.17(c).

of proceedings under the Securities Investors Protection Act (''SIPA'') in the case of FCMs subject to a SIPA proceeding,[12] and Title II of Dodd-Frank in the case of a commodity broker where the Federal Deposit Insurance Corporation (''FDIC'') is acting as a receiver.

(6) The Commission is enacting changes to the treatment of letters of credit as collateral, both during business as usual and during bankruptcy, in order to ensure that, consistent with the *pro rata* distribution principle, customers who post letters of credit as collateral suffer the same proportional loss as customers who post other types of collateral.

(7) The Commission is granting trustees enhanced discretion, based on both practical necessity and positive experience.

a. Recent commodity broker bankruptcies have involved many thousands of customers, with as many as hundreds of thousands of commodity contracts. Trustees must make decisions as to how to handle such customers and contracts in the days—in some cases, the hours—after being appointed. Moreover, each commodity broker bankruptcy has unique characteristics, and bankruptcy trustees need to adapt correspondingly quickly to those unique characteristics.

i. In order to foster the ability of the trustee to operate effectively, some of the changes would permit the trustee enhanced discretion generally.

ii. Others, recognizing the difficulty in treating large numbers of public customers on a bespoke basis, would permit the trustee to treat public customers on an aggregate basis. These changes represent a move from a model where the trustee receives and complies with instructions from individual public customers, to a model—reflecting actual practice in commodity broker bankruptcies in recent decades—where the trustee transfers as many open commodity contracts as possible on an omnibus basis.

b. These grants of discretion are also supported by the Commission's positive experience working in cooperation and consultation with bankruptcy and SIPA trustees.

c. On a related note, and as discussed further as the third overarching concept in the section below on cost-benefit considerations,[13] part 190 favors cost effectiveness and promptness over precision in certain respects, particularly with respect to the concept of *pro rata* treatment. Following the policy choice made by Congress in section 766(h) of the Bankruptcy Code, the Commission's policy is that it is more important to be cost effective and prompt in the distribution of customer property (*i.e.,* in terms of being able to treat customers as part of a class) than it is to value each customer's entitlements on an individual basis. The Commission believes that this approach would lead to (1) in general, a faster administration of the proceeding, (2) customers receiving their share of the debtor's customer property more quickly, and (3) a decrease in administrative costs (and thus, in case of a shortfall in customer property, a greater return to customers).

(8) Many of the changes are intended to update part 190 in light of changes to the regulatory framework over the past three decades, including cross-references to other Commission regulations. Some of these codify actual practice in prior bankruptcies, such as a requirement that an FCM notify the Commission of its imminent intention to file for voluntary bankruptcy. In another case, the Commission is addressing for the first time the interaction between part 190 and recent revisions to the Commission's customer protection rules.[14]

(9) Other changes follow from changes to the technological ecosystem, in particular changes from paper-based to electronic-based means of communication and recording, (for example, the use of communication to customers' electronic addresses rather than by paper mail, as well as the use of websites as a means for the trustee to communicate with customers on a regular basis). The proposal would also recognize the change from paper-based to electronic recording of ''documents of title.'' Many of these changes also recognize the actual practice in prior bankruptcies.

(10) Finally, many of the changes are intended to clarify language in existing regulations, without any intent to change substantive results. While some of these changes will, as discussed below, address ambiguities that have complicated past bankruptcies, this comprehensive revision of part 190 has also provided opportunities to clarify language in order to avoid future ambiguities, and to add provisions to address circumstances that have not yet arisen, in order to accomplish better and more reliably the goals of promptly and cost-effectively resolving commodity broker bankruptcies while mitigating systemic risk and protecting the commodity broker's customers.

The Commission invited comments on all aspects of the proposed rulemaking and received a total of 16 substantive comment letters in response.[15] The comments generally supported the adoption of revisions to part 190, though several provided suggestions as to particular elements of the proposal that should be modified, clarified, deleted, or otherwise improved. The Commission has adopted many, though not all, of these suggestions, and in some cases has sought to address the concerns raised through alternative drafting.[16]

II. Finalized Regulations

In the discussion below, the Commission highlights topics of interest to commenters and discusses comment letters that are representative of the views expressed on those topics. The discussion does not explicitly respond to every comment submitted; rather, it addresses important issues raised by the proposed rulemaking and analyzes those issues in the context of specific comments.

A. Subpart A—General Provisions [17]

The Commission is adopting as subpart A (§§ 190.00–190.02) general provisions to address both debtors that are both FCMs and debtors that are DCOs.

[12] Those would be FCMs that are also registered as broker-dealers with the Securities and Exchange Commission. *See generally* SIPA, 15 U.S.C. 78aaa *et seq.*

[13] *See* the overarching concept discussed in section III.A.2.c below.

[14] 78 FR 68506 (Nov. 14, 2013). This refers to § 190.05(f) in section II.B.3 below.

[15] The Commission received comment letters submitted by the following: American Council of Life Insurers (ACLI); Better Markets, Inc. (Better Markets); Cboe Global Markets, Inc. (CBOE); CME Group Inc. (CME); Commodity Markets Council (CMC); Futures Industry Association (FIA); Investment Company Institute (ICI); Intercontinental Exchange Inc. (ICE); International Swaps and Derivatives, Inc. (ISDA); LCH Group (LCH); National Grain and Feed Association (NGFA); Options Clearing Corporation (OCC); Part 190 Subcommittee of the Business Law Section of the American Bar Association (ABA Subcommittee); Securities Industry and Financial Markets Asset Management Group and Managed Funds Association (SIFMA AMG/MFA);); Kathryn Trkla; Geoffrey Goodman; and Vincent Lazar, as individuals (Subcommittee Members), and Vanguard Group, Inc. (Vanguard).

[16] The Commission also issued the Supplemental Proposal, which withdrew proposed § 190.14(b)(2) and (3), and proposed an alternative. The Commission received 5 substantive comment letters in response, each of which was from an entity that had also submitted a comment letter on the Proposal. For the reasons discussed in section II.H below, the Commission is not adopting the Supplemental Proposal.

[17] The Commission is adopting the proposed technical corrections and updates to parts 1, 4, and 41, which are discussed in section II.F. below. Moreover, as discussed in section II.B.8, parts of proposed § 190.10 are being adopted, but codified in part 1.

1. Regulation § 190.00: Statutory Authority, Organization, Core Concepts, Scope, and Construction

The Commission is adopting § 190.00 as proposed with the addition of § 190.00(c)(3)(i)(C) and the modification to § 190.00(d)(3)(v), as set forth below. The Commission is adopting § 190.00 to set forth general provisions that state facts and concepts that exist in the Commission's bankruptcy regulations. It is applicable to all of part 190. The Commission's intent is to assist trustees, bankruptcy courts, customers, clearing members, clearing organizations, and other interested parties in understanding the Commission's rationale for, and intent in promulgating, the specific provisions of part 190. The Commission also believes that the regulation may be particularly useful in a time of crisis for those individuals who may not have extensive experience with the CEA or Commission regulations.

The Commission requested comment with respect to all aspects of proposed § 190.00. The Commission also raised specific questions as to whether a regulation setting forth core concepts would be useful; whether the core concepts were under or over inclusive; and whether the definitions and discussions for each core concept would be helpful. The Commission received several comments expressing support for various aspects of proposed § 190.00, including comments from SIFMA AMG/MFA, CME, and the ABA Subcommittee. CME noted in particular that it believed that the regulation ''may prove particularly useful to a trustee who has little experience with the CEA or the Commission's customer funds segregation rules, as they try to get 'up to speed' in the critical early hours and days following the trustee's appointment when the trustee is expected to act quickly on various matters.''

The Commission is adopting § 190.00(a) to set forth the Commission's statutory authority to adopt the proposed part 190 regulations under section 8a(5) of the CEA, which empowers the Commission to make and promulgate such rules and regulations as are necessary to effectuate any of the provisions or to accomplish any of the purposes of the CEA, and section 20 of the CEA, which provides that the Commission may, notwithstanding the Bankruptcy Code, adopt certain rules or regulations governing a proceeding involving a commodity broker that is a debtor under subchapter IV of chapter 7 of the Bankruptcy Code. The Commission received comments from CME and the ABA Subcommittee specifically supporting the inclusion of an explanation of the Commission's authority to adopt the part 190 regulations in § 190.00.

The Commission is adopting § 190.00(b) to explain that the part 190 regulations are organized into three subparts. Subpart A contains general provisions applicable in all cases. Subpart B contains provisions that apply when the debtor is an FCM, the definition of which includes acting as a foreign FCM.[18] Subpart C contains provisions that apply when the debtor is a DCO, as defined by the CEA. The Commission received comments from the ABA Subcommittee, CME, and ICI in support of the reorganization of part 190.

The Commission is adopting § 190.00(c) to set forth the core concepts [19] of part 190 that are central to understanding how a commodity broker bankruptcy works. These include concepts related to commodity brokers and commodity contracts, account classes, public customers and non-public customers, Commission segregation requirements, member property,[20] porting of public customer commodity contract positions, *pro rata* distribution, and deliveries.

The Commission is adopting § 190.00(c)(1) to explain that subchapter IV of chapter 7 of the Bankruptcy Code applies to a debtor that is a ''commodity broker,'' the definition of which requires a ''customer.'' [21] Section 190.00(c)(1) states that the regulations in part 190 apply to commodity brokers that are FCMs as defined by the Act, or DCOs as defined by the Act.

The Commission is adopting § 190.00(c)(2) to explain that the CEA and Commission regulations provide separate treatment and protections for different types of cleared commodity contracts or account classes. The four account classes include the (domestic) futures account class (including options on futures),[22] the foreign futures account class (including options on foreign futures),[23] the cleared swaps account class for swaps cleared by a registered DCO (including cleared options other than options on futures or foreign futures),[24] and the delivery account class for property held in an account designated as a delivery account. Delivery accounts are used for effecting delivery under commodity contracts that provide for settlement via delivery of the underlying when a commodity contract is held to expiration or, in the case of an option on a commodity, is exercised.[25]

The Commission is adopting § 190.00(c)(3)(i) to prescribe the separate treatment of ''public customers'' and ''non-public customers,'' as defined in § 190.01, within each account class in the event of a proceeding in which the debtor is an FCM. It explains that, in a bankruptcy, public customers are generally entitled to a priority distribution of cash, securities, or other customer property over ''non-public customers,'' and both are given a priority over all other claimants (except for claims relating to the administration of customer property) pursuant to section 766(h) of the Bankruptcy Code.[26] The Commission is adopting § 190.00(c)(3)(ii) to address the division of customer property and member property in proceedings in which the debtor is a clearing organization. In such a proceeding, customer property consists of member property, which is distributed to pay member claims based on members' house accounts, and

[18] *See* CEA section 1a(28), 7 U.S.C. 1a(28). The definition of foreign FCM involves soliciting or accepting orders for the purchase or sale of a commodity for future delivery executed on a foreign board of trade, or by accepting property or extending credit to margin, guarantee or secure any trade or contract that results from such a solicitation or acceptance. *See* section 761(12) of the Bankruptcy Code, 11 U.S.C. 761(12).

[19] The Commission is using to use the term ''core concepts'' to avoid confusion with the core principles applicable to registered entities. *Cf.* CEA section 5b(c)(2), 7 U.S.C. 7a–1(c)(2).

[20] ''Member property'' is defined in § 190.01 and will be used to identify cash, securities, or property available to pay the net equity claims of clearing members based on their house account at the clearing organization. *Cf.* 11 U.S.C. 761(16).

[21] *See* 11 U.S.C. 101(6) (definition of ''commodity broker''), 761(9) (definition of ''customer'' referred to in 101(6)).

[22] This corresponds to segregation pursuant to section 4d(a) of the CEA, 7 U.S.C. 6d(a).

[23] This corresponds to segregation pursuant to § 30.7 (enacted pursuant to section 4(b)(2)(A) of the CEA, 7 U.S.C. 6(b)(2)(A).

[24] This corresponds to segregation pursuant to section 4d(f) of the CEA, 7 U.S.C. 6d(f).

[25] Delivery accounts are discussed further below in, *e.g.,* §§ 190.00(c)(6), 190.01 (definition of delivery account, cash delivery property, physical delivery property) and 190.06.

[26] Section 766(h) of the Bankruptcy Code explicitly states that the trustee shall distribute property ratably to customers in priority to all other claims, except claims that are attributable to the administration of customer property. Notwithstanding any other provision of this subsection, a customer net equity claim based on a proprietary account may not be paid either in whole or in part, directly or indirectly, out of customer property unless all other customer net equity claims have been paid in full. Thus, all customer property will be allocated to public customers so long as the funded balance in any account class for public customers is less than one hundred percent of public customer net equity claims. Once all account classes for public customers are fully funded (*i.e.,* at one hundred percent of net equity claims), any excess will be allocated to non-public customers' net equity claims until all of those are fully funded.

customer property other than member property, which is reserved for payment of claims for the benefit of members' public customers. The Commission is adopting § 190.00(c)(3)(iii) to address the preferential assignment of property among customer classes and account classes in clearing organization bankruptcies. Certain customer property, as specified in § 190.18(c), will be preferentially assigned to ''customer property other than member property'' (*i.e.,* property for the public customers of members) instead of ''member property'' to the extent that there is a shortfall in funded balances for members' public customer claims. To the extent that there are excess funded balances for members' claims in any customer class/account class combination, that excess will also be assigned preferentially to ''customer property other than member property'' for other account classes to the extent of any shortfall in funded balances for members' public customer claims in such account classes. Where property will be assigned to a particular customer class with more than one account class, it will be assigned on a least funded to most funded basis among the account classes.

The Commission is adopting § 190.00(c)(4) to explain that, in a proceeding in which the debtor is an FCM, part 190 details the policy preference for transferring to another FCM (commonly known as ''porting''), the open commodity contract positions of the debtor's customers along with all or a portion of such customers' account equity.[27]

The Commission is adopting § 190.00(c)(5) to address *pro rata* distribution. It explains that, if the aggregate value of customer property in a particular account class is less than the amount needed to satisfy the net equity claims of public customers in that account class (*i.e.,* there is a ''shortfall''), customer property in that account class will be distributed *pro rata* to those public customers. The *pro rata* distribution principle carries forth the statutory direction in section 766(h) of the Bankruptcy Code. It ensures that all public customers within an account class will suffer the same proportional loss, including those public customers that post as collateral letters of credit or specifically identifiable property.[28] Any customer property that is not attributable to any particular account class or which is in excess of public customer net equity claims for the account class to which it is attributed, will be distributed to public customers in respect of net equity claims in other account classes where there is a shortfall. Thus, as noted in § 190.00(c)(3), all public customer net equity claims would receive priority over non-public customer claims.

The Commission is adopting § 190.00(c)(6) to address deliveries. It explains that the delivery provisions of part 190 apply to any commodity that is subject to delivery under a commodity contract, including agricultural commodities, other non-financial commodities (such as metals or energy), and commodities that are financial in nature (including virtual currencies). In the ordinary course of business, commodity contracts with delivery obligations are offset before reaching the delivery stage (*i.e.,* prior to triggering bilateral delivery obligations). Nonetheless, when delivery obligations do arise, a delivery default could have a disruptive effect on the cash market for the commodity and could adversely impact the parties to the transaction. In a proceeding in which the debtor is an FCM, the delivery provisions in part 190 reflect the policy preferences (A) to liquidate commodity contracts that settle via delivery before they move into a delivery position and (B) when contracts do move into a delivery position, to allow the delivery to occur, where practicable, outside the administration of the debtor's estate (*i.e.,* directly between the debtor's customer and the delivery counterparty assigned by the clearing organization).

The Commission received several comments expressing support for certain provisions in § 190.00(c) and two comments expressing concerns. CME expressed support for ''limiting the scope of part 190 to the bankruptcy of a commodity broker that is an FCM or a DCO and to commodity contracts that are cleared'' as set forth § 190.00(c)(1). CME, OCC, Vanguard, and NGFA supported the concept of preferring the claims of public customers over non-public customers in a bankruptcy proceeding. CME agreed with the inclusion of the core concept set forth § 190.00(c)(3)(ii), noting that ''it aids understanding to explain how the distinction between the public customer class and the non-public customer class is reflected at the DCO-level in the distinctions made between customer accounts and house accounts and between the two categories of customer property—customer property and member property—that are available to satisfy the net equity claims of each.'' Better Markets supported the clarification in § 190.00(c)(5)(ii) that customers relying on letters of credit must carry the same proportional losses as customers posting other forms of acceptable collateral.

NGFA supported the core concept of prioritizing the prompt transfer of customer accounts and positions to another FCM as opposed to liquidating customer accounts. OCC, however, disagreed with this policy preference. OCC supported ''the Commission's objective to mitigate risk to an FCM's customers and limit market volatility,'' noting that ''[p]orting positions and associated collateral in an FCM bankruptcy proceeding can be an effective way to achieve these objectives in some instances.'' OCC believed, however, that the trustee should retain broad discretion to decide, on a case-by-case basis and in consideration of certain factors (*e.g.,* the defaulting FCM's total book of positions and market conditions) whether porting or liquidating positions will achieve the best result for customers involved in an FCM's bankruptcy. OCC further commented that the market risk associated with closing out and reopening positions for certain customers that may be introduced with liquidation should be weighed against potential drawbacks of porting, including that ''(i) a trustee (or DCO) must first identify a transferee to accept the open position[s] and collateral, which depending on market conditions could be a difficult and time consuming process; (ii) until the transfer is complete, the customer may face uncertainty as to how its position and associated collateral will be resolved and may not be able to exit the position in a timely and efficient manner; and (iii) a customer may be required to post additional collateral at a new FCM prior to or immediately after a transfer.''

In response to the concerns raised by OCC, the Commission notes first that, as OCC forthrightly acknowledges,

[27] Transfer or porting of customer positions mitigates risks to both the customers of the debtor FCM and to the markets. Specifically, porting (rather than the alternative, liquidation) of customer positions protects customers' hedges from changes in value between the time they are liquidated and the time, if any, that the customer may be able to re-establish them (and thus mitigates the market risk that some customers use the futures markets to counteract), and similarly protects customers' directional positions. Moreover, not all customers may be able to re-establish positions with the same speed—in particular, smaller customers may be subject to longer delays in re-establishing their positions. In addition, liquidation of an FCM's book of positions can increase volatility in the markets, to the detriment of all market participants (and also contribute to making it more expensive for customers to re-establish their hedges and other positions).

[28] In prior bankruptcies, some customers posting letters of credit or specifically identifiable property as collateral sought to escape *pro rata* treatment for these categories of collateral, contrary to the Commission's intent. *See* discussion of § 190.04(d)(3) in section II.B.2 below.

liquidating customer positions may introduce market risk associated with closing out and reopening positions for certain customers. Additionally, liquidating a mass of customer positions may roil the markets, if any, where those positions are concentrated. For these reasons, the policy preference in favor of transfer is both supported by statute and quite longstanding. It is supported by § 764(b) of the Bankruptcy Code, which explicitly permits transfers of commodity contracts that are authorized by the Commission up to seven calendar days *after* the order for relief. It is also embodied in current § 190.02(e), which requires the trustee to immediately use its best efforts to effect a transfer, and is continued in proposed (and adopted) § 190.04(a)(1).

Furthermore, § 190.00(c)(4) establishes, consistent with § 764(b), a policy *preference* for porting, rather than a *mandate* for porting. This recognizes that finding willing and able transferees for all customer positions may or may not be practicable. Moreover, § 190.04(a)(1) requires the trustee to use its best efforts to effect a transfer no later than the seventh calendar day after the order for relief,[29] and § 190.04(d) requires the trustee promptly to liquidate most remaining contracts after than time. Indeed, as a practical matter, there is cause for doubt that a DCO will permit the trustee of a debtor that is a clearing member to hold open contracts quite that long.[30] Thus, despite the preference for porting, there are practical limits to how long contracts will be held open before being liquidated. This also imposes temporal limits on the uncertainty customers will face as to how their positions will be resolved.

Finally, while a customer may indeed be called for additional collateral at a transferee FCM (particularly if less than 100% of the collateral is transferred along with the positions), a customer that is unwilling to meet such a call will at the least be permitted to have their positions liquidated. That would entitle the customer to prompt return by the transferee FCM of the remaining collateral that was transferred—which may well be more prompt than a distribution in the bankruptcy proceeding of the debtor.

ICI expressed concerns with respect to the discretion granted to the trustee under the part 190 regulations. ICI agreed with the Commission ''that trustees need flexibility given the myriad of decisions they must make in a short period of time and the unique circumstances that each commodity broker insolvency may present,'' and that ''trustees to date have exercised their discretion in a manner that has generally promoted customer protection.'' ICI cautioned, however, that the Commission should take steps to help ensure that the trustee prioritizes the protection of public customers. ICI urged the Commission to make clear in § 190.00 ''that the trustee must exercise [its] discretion in a manner that it determines will result in the greatest recovery for, and the least disruption to, public customers.'' With respect to part 190 regulations that are ''specifically aimed at protecting customers,'' ICI asserted the trustee's discretion should be more limited. While ICI acknowledged that, at times, compliance with such provisions ''may be impractical or impossible or may cause harm to customers,'' ICI was concerned that a ''reasonable efforts'' standard ''could signal that the trustee has wider latitude to depart from the requirement at issue.'' ICI asked the Commission to impose a ''best efforts'' standard in certain cases.

The Commission agrees with ICI that the trustee should exercise its discretion in a manner that best achieves the overarching goal of protecting the interests of public customers as a class, and specifically should act in the manner that it determines will result in the greatest recovery for, and the least disruption to, public customers. The Commission notes that, at times, those two sub-goals may be in tension. Because the Commission does not believe that there is a universally optimal means to reconcile the two sub-goals in aid of best achieving the overarching goal of protecting the interests of public customers, the Commission concludes that it is best to leave the balancing of the two sub-goals to the discretion of the trustee. It is in that context that the Commission has decided to direct the trustee to exercise ''reasonable efforts'' rather than ''best efforts'' to achieve certain standards. In determining what efforts are ''reasonable,'' the trustee should act to achieve the overarching goal.

In light of the foregoing and to provide clarity with respect to the scope of the trustee's discretion, the Commission is adopting new § 190.00(c)(3)(i)(C) which provides that where a provision in part 190 affords the trustee discretion, that discretion should be exercised in a manner that the trustee determines will best achieve the overarching goal of protecting public customers as a class by enhancing recoveries for, and mitigating disruptions to, public customers as a class. In seeking to achieve that overarching goal, the trustee has discretion to balance those two subgoals when they are in tension. Where the trustee is directed to exercise ''reasonable efforts'' to meet a standard, those efforts should only be less than ''best efforts'' to the extent that the trustee determines that such an approach would support the foregoing goals.[31]

The Commission is adopting § 190.00(d)(1) to describe the scope of commodity broker proceedings under subchapter IV of chapter 7 of the Bankruptcy Code,[32] and the relationship between part 190 to SIPA proceedings (where the debtor is a commodity broker) and to resolution of commodity brokers under Title II of the Dodd-Frank Act.''

Section 190.00(d)(1)(i) acknowledges that, while section 101(6) of the Bankruptcy Code recognizes ''commodity options dealers'' and ''leverage transaction merchants'' (as defined in sections 761(6) and (13) of the Bankruptcy Code), as separate categories of commodity brokers, there are no commodity options dealers or leverage transaction merchants currently registered as such. As set forth in the Note to paragraph (d)(1)(i)(B), the Commission is declaring its intent to adopt regulations with respect to commodity options dealers and leverage transaction merchants, respectively, at such time as an entity registers as such.

Section 190.00(d)(1)(ii) explains that, pursuant to section 7(b) of SIPA,[33] the

[29] Indeed, the preference contained § 190.00(c)(4) does not represent a departure from the existing standards under current part 190. It merely highlights the requirement in § 190.04(a)(1) that the trustee use its best efforts to effect a transfer no later than the seventh calendar day after the order for relief; that requirement is substantially identical to the requirement in current § 190.02(e).

[30] For example, OCC Rule 1102(a) provides that OCC may summarily suspend any Clearing Member which is in such financial or operating difficulty that OCC determines and so notifies the Securities and Exchange Commission or the Commodity Futures Trading Commission that suspension is necessary for the protection of the Corporation, other Clearing Members, or the general public. OCC Rule 1106 permits OCC to close out the positions of a suspended clearing member.

[31] While '' '[b]est efforts' is a term which necessarily takes its meaning from the circumstances,'' the trustee in exerting best efforts to meet a standard must diligently exert efforts to meet that standard ''to the extent of its own total capabilities.'' *See generally Bloor* v. *Falstaff Brewing Corp,* 454 F.Supp. 258, 266–67 *aff'd* 601 F.2d 609 (2nd. Cir. 1979). By contrast, in exerting ''reasonable efforts'' to meet a standard, the Commission expects that the trustee will work in good faith to meet the standard, but will also take into account other considerations, including the impact of the effort necessary to meet the standard on the overarching goal of protecting public customers as a class.

[32] 12 U.S.C. 5381 *et seq.*

[33] 15 U.S.C. 78aaa *et seq.*

trustee in a SIPA proceeding where the debtor is also a commodity broker has the same duties as a trustee in a proceeding under subchapter IV of chapter 7 of the Bankruptcy Code, to the extent consistent with SIPA or as ordered by the court.[34] This part implements subchapter IV of chapter 7 by establishing the trustee's duties thereunder, consistent with the broad authority granted to the Commission pursuant to section 20 of the CEA. Therefore, this part also applies to a proceeding commenced under SIPA with respect to a debtor that is registered as a broker or dealer under section 15 of the Securities Exchange Act of 1934 [35] when the debtor also is an FCM.

Moreover, in the context of a resolution proceeding under Title II of Dodd-Frank, section 210(m)(1)(B) [36] provides that the FDIC (in its role as resolution authority) must apply the provisions of subchapter IV of chapter 7 of the Bankruptcy Code in respect of the distribution of customer property and member property of a resolution entity [37] that is a commodity broker as if the resolution entity were a debtor for purposes of subchapter IV. Accordingly, § 190.00(d)(1)(iii) explains that this part shall serve as guidance with respect to the distribution of property in a proceeding in which the FDIC acts as a receiver for an FCM or DCO pursuant to Title II of Dodd-Frank.[38]

The Commission is adopting § 190.00(d)(2)(i) to clarify that a trustee may not recognize any account classes not explicitly provided for in part 190. Section 190.00(d)(2)(ii) provides that no property that would otherwise be included in customer property, as defined in § 190.01, shall be excluded from customer property because it is considered to be held in a constructive trust, resulting trust, or other trust that is implied in equity.

Generally, in a commodity broker bankruptcy, the basis for distributing segregated customer property is *pro rata* treatment. To achieve this goal, the FCM's segregation records (including account statements) and reporting to the Commission and self-regulatory organizations (''SROs'') and DCOs must reflect what is actually available for customers. This is necessary to enable FCMs, SROs, DCOs, and the Commission to ensure, during business as usual, that (a) customer property is being properly protected pursuant to the segregation requirements of section 4d of the CEA and the regulations thereunder, and (b) customer property is not subject to hidden arrangements that cannot be accounted for transparently and reliably. Through § 190.00(d)(2)(ii), the Commission is making clear that customer property cannot be burdened by equitable trusts. Attempting to account for such equitable trusts in a bankruptcy proceeding under part 190 would undermine the Commission's implementation and enforcement of the statutory scheme under the CEA.

Section 190.00(d)(3) provides that certain transactions, contracts, or agreements are excluded from the term ''commodity contract.'' [39] The excluded agreements and transactions traditionally have not been considered to be commodity contracts for purposes of segregation and customer protection, while those that are excepted from these exclusions are so considered, and thus are covered by part 190.

The Commission received four comments supportive of specific provisions of proposed § 190.00(d) and one comment requesting a modification of the regulation. CME agreed that removing provisions relating to commodity option dealers and leverage transaction merchants would ''improve the rules' clarity.'' CME and Cboe expressed support for the clarification in § 190.00(d)(1)(ii) of the applicability of SIPA in the bankruptcy proceeding of a firm that is dually registered as an FCM and a broker-dealer where the bankruptcy must be handled pursuant to SIPA rather than by the FCM rules. Cboe noted that such clarity will be ''beneficial to the entire ecosystem, including customers of FCMs and broker-dealers'' and will ''further the ability of market participants to utilize portfolio margining and the associated efficiencies.'' CME expressed support for § 190.00(d)(1)(iii). CME specifically supported ''setting out that Part 190 'shall serve as guidance' to the FDIC as receiver for an FCM or DCO in a proceeding under Title II of Dodd Frank, with respect to the distribution of customer property and member property.'' Noting that ''Title II [of the Dodd-Frank Act] directs the FDIC to apply the provisions of subchapter IV of chapter 7 of the [Bankruptcy] Code with respect to such distributions,'' CME stated its belief that ''it is reasonable to read Title II's cross-reference to subchapter IV of chapter 7 ''as indirectly bringing [p]art 190 into the scope of that provision given the need for Commission regulations to give specificity and meaning to the general principles set out in subchapter IV.'' SIFMA AMG/MFA supported the principle of excluding property held in a constructive trust from customer property as set forth in § 190.00(d)(2)(ii), noting that this principle ''serves to preserve the integrity of customer property.'' ICI strongly supported setting forth the prohibition on excluding property from ''customer property'' because it is considered to be held in a trust implied in equity in § 190.00(d)(2)(ii), and the exclusion from the term ''commodity contract'' of off-exchange retail foreign currency transactions in § 190.00(d)(3)(iv).

The ABA Subcommittee recommended one modification to this regulation. It asked the Commission to amend proposed § 190.00(d)(3)(v) to clarify that mixed swaps could be commodity contracts subject to part 190. In support of its position, the ABA Subcommittee asserted that a DCO could theoretically provide clearing services to FCMs and their customers with respect to mixed swaps, where the mixed swap positions are carried in accounts subject to part 22 and customers are part of the cleared swap account class under part 190. The ABA Subcommittee analogized the inclusion of mixed swaps within the ''commodity contract'' definition to the Commission's proposal to not exclude security futures products from the commodity contract definition when the security futures product is carried in an account for which there is a corresponding account class under part 190. The Commission agrees with the

[34] *See* SIPA section 7(b), 15 U.S.C. 78fff–1(b) (To the extent consistent with the provisions of [SIPA] or as otherwise ordered by the court, a trustee shall be subject to the same duties as a trustee in a case under chapter 7 of title 11, including, if the debtor is a commodity broker, as defined under section 101 of such title, the duties specified in subchapter IV of such chapter 7).

[35] 15 U.S.C. 78*o*.

[36] 12 U.S.C. 5390(m)(1)(B).

[37] That is, the entity being resolved under Title II. Section 210(m)(1)(b) refers to ''any covered financial company or bridge financial company.''

[38] 12 U.S.C. 5390(m)(1)(B) provides that the FDIC must apply the provisions of subchapter IV of chapter 7 of the Code with respect to the distribution of customer property and member property in connection with the liquidation of a commodity broker that is a ''covered financial company'' or ''bridge financial company'' (terms defined in 12 U.S.C. 5381(a)).

[39] The contracts that would be excluded include: Options on commodities unless cleared by a DCO (or, in the context of a foreign futures clearing member, a foreign clearing organization); forwards (defined as such pursuant to the exclusions in sections 1a(27) or 1a(47)(B)(ii) of the CEA), unless they are cleared by a DCO (or, in the context of a foreign futures clearing member, a foreign clearing organization); security futures products when they are carried in a securities account; retail foreign currency transactions described in sections 2(c)(2)(B) or (C) of the CEA; security-based swaps or other securities carried in a securities account (other than security futures products carried in an enumerated account class); and retail commodity transactions described in section (2)(c)(2)(D) of the CEA (other than transactions executed on or subject to the rules of a designated contract market (''DCM'') or foreign board of trade (''FBOT'') as if they were futures).

ABA Subcommittee's reasoning with respect to proposed § 190.00(d)(3)(v) and is amending § 190.00(d)(3)(v) to read in pertinent part, that ''. . . a security futures product or mixed swap (as defined in 1a(47)(D) of the Act) that is, in either case, carried in an account for which there is a corresponding account class under part 190 is not excluded.''

The Commission is adopting § 190.00(e) to explain the context in which part 190 should be interpreted. It states that any references to other federal rules and regulations refer to the most current versions of these rules and regulations (*i.e.,* ''as the same may be amended, superseded or renumbered'') and that, where they differ, the definitions set forth in § 190.01 shall be used instead of the defined terms set forth in section 761 of the Bankruptcy Code. The Commission notes that other regulations in part 190 are designed to be consistent with subchapter IV of chapter 7 of the Bankruptcy Code.

Section 190.00(e) addresses account classes in the context of portfolio margining and cross margining programs. Where commodity contracts (and associated collateral) that would be attributable to one account class are, instead, commingled with the commodity contracts (and associated collateral) in a second account class (the ''home field''), then the trustee must treat all such commodity contracts and associated collateral as being held in, and consistent with the regulations applicable to, an account of the second account class. The approach of following the rules of the ''home field'' also pertains to securities positions held in a commodity account class (and thus treated in accord with the relevant commodity account class) and commodity contract positions (and associated collateral) held in the securities account, in which case the rules applicable to the securities account will apply, consistent with section 16(2)(b)(ii) of SIPA, 15 U.S.C. 78lll(2)(b)(ii).

The Commission received two comments on proposed § 190.00(e). ICI and Cboe expressed support for the clarity provided by § 190.00(e) with respect to portfolio margining and cross margining programs. ICI strongly supported the ''home field'' rule in proposed § 190.00(e), noting that providing ''clarity regarding how transactions and margin that are portfolio margined in the same account will be treated in the event that an FCM or broker-dealer becomes insolvent is a ''prerequisite for an effective portfolio margining regime.''

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.00 as proposed with the addition of § 190.00(c)(3)(i)(C) and the modification to § 190.00(d)(3)(v), as set forth above.

2. Regulation § 190.01: Definitions

The Commission is adopting § 190.01 as proposed with modifications set forth below, to update the definitions for revised part 190. Most of the changes in § 190.01 are conforming changes, such as correcting cross-references and deleting definitions of certain terms that are not used in part 190, as amended. Other changes tie the definitions in § 190.01 more closely to the definitions in § 1.3 and other Commission regulations, to reflect changes in Commission regulations. In some cases, the Commission is adopting more substantive changes to the definitions, such as amending or adding definitions to further clarify and provide additional details where the current definitions are silent or unclear, or to reflect concepts that are new to part 190. In particular, the Commission is separating the delivery account class into two subclasses, a physical delivery account class and a cash delivery account class; the relevant terms are defined below. The definitions of commodity contract and physical delivery property codify positions that the Commission has taken in recent commodity broker bankruptcies.[40]

The Commission is also amending § 190.01 to replace the paragraphs identified with an alphabetic designation for each defined term (*e.g.,* ''§ 190.01(ll)'') with a simple alphabetized list, as is recommended by the Office of the Federal Register, and as recently implemented by the Commission with respect to, *e.g.,* § 1.3.[41]

The Commission requested comment with respect to all aspects of proposed § 190.01, including the usefulness and any unintended consequences of the revised definitions. The Commission received a number of comments on the proposed definitions in § 190.01. As further detailed below, the Commission is modifying some of the definitions in response to comments. Unless stated otherwise below, the Commission did not receive any comments on a proposed definition in § 190.01 and is adopting each definition as proposed.[42]

The Commission is adopting the definition of ''account class'' as proposed with the modifications described below. The current definition of the term ''account class'' specifies that it includes certain types of customer accounts, each of which is to be recognized as a separate class of account. The types are ''futures account,'' ''foreign futures accounts,'' ''leverage accounts,'' ''delivery accounts,'' and ''cleared swap accounts.'' The Commission is adding detail to the definition of ''account class'' by including therein definitions of ''futures account,'' ''foreign futures accounts,'' ''cleared swaps accounts,'' and ''delivery accounts.'' However, as discussed above with respect to § 190.00(d)(1)(i), the Commission is removing, at least temporarily, the ''commodity options'' and ''leverage account'' account classes.[43]

[40] Respectively, *In Re Peregrine Financial Group, Inc.,* No. 12–B27488 (Bankr. N.D. Ill.), and *MF Global, Inc.*

[41] *See generally* 83 FR 7979, 7979 & n.6 (Feb. 23, 2018).

[42] The Commission did not receive comments with respect to the following part 190 definitions as proposed in § 190.00: Act, Bankruptcy code, Business day, Calendar day, Cash delivery account class, Cash equivalents, Clearing organization, Commodity broker, Commodity contract account, Court, Cover, Customer, Customer claim of record, Customer class, Dealer option, Debtor, Distribution, Equity, Exchange Act, FDIC, Filing Date, Final net equity determination date, Foreign board of trade, Foreign clearing organization, Foreign future, Foreign futures commission merchant, Foreign futures intermediary, Funded balance, Futures and futures contract, In-the-money amount, Joint account, Leverage contract, Leverage transaction merchant, Member property, Net equity, Open commodity contract, Order for relief, Person, Premium, Primary liquidation date, Principal contract, Securities Account, SIPA, Security, Short term obligation, Specifically identifiable property, Strike price, Substitute customer property, Swap, Trustee, and Undermargined. Accordingly, the Commission is adopting those definitions as proposed, as discussed later in section II.A.2.

[43] The Commission is adopting paragraph (2) of the definition of account class to address commingling orders and rules. Specifically, there are cases where commodity contracts (and associated collateral) that would be attributable to one account class are held separately from contracts and collateral associated with that first account class, and instead are allocated to a different account class and commingled with contracts and collateral in that latter account class. This would take place because the contracts in question are risk-offsetting to contracts in the latter account class. For example, this could involve portfolio margining within a DCO or cross-margining between a DCO and another central counterparty, which may or may not be a DCO. This commingling may be authorized pursuant to a Commission regulation or order, or pursuant to a clearing organization rule that is approved in accordance with § 39.15(b)(2). The Commission is adopting paragraph (2) to confirm that the trustee must treat the commodity contracts in question (and the associated collateral) as being held in an account of the latter account class. The Commission is also adopting paragraph (3) of the definition of account class to address cases where the commodity broker establishes internal books and records in which it records a customer's commodity contracts and

Continued

The Commission is adopting the definition of ''futures account'' to cross-reference the definition of the same term in § 1.3 of the Act, while the definition of ''cleared swaps account'' cross-references the definition of ''cleared swaps customer account'' in § 22.1. These definitions apply to both FCMs and DCOs. The definition of ''foreign futures account'' cross-references the definition of ''30.7 account'' in § 30.1(g). As that latter definition is limited to FCMs, the Commission is adopting a corresponding reference to such accounts at a clearing organization, in the event that a clearing organization clears foreign futures transactions for members that are FCMs, where those accounts are maintained on behalf of those FCM members' 30.7 customers (as that latter term is defined in § 30.1(f)). The Commission clarifies that this would not apply if a foreign clearing organization is clearing foreign futures for clearing members that are not subject to the requirements of § 30.7.

The ABA Subcommittee and CME recommended that the Commission expand the definitions of ''futures account,'' ''foreign futures account,'' and ''cleared swaps account'' within the § 190.01 definition of ''account class'' to cover the accounts of non-public customers. The ABA Subcommittee and CME stated that as proposed, the cross-references to § 1.3, the ''30.7 account'' in 30.1, and the ''cleared swaps customer account'' in § 22.1 within the account class definitions, limited the scope of those definitions to only segregated accounts of public customers despite the Commission's intention to use those same account class distinctions for non-public customers elsewhere in the part 190 rules. The ABA Subcommittee and CME suggested that those account class distinctions are also relevant for the non-public customer class (*i.e.,* the holders of proprietary accounts carried by FCMs and for clearing members' house accounts carried by DCOs).

The Commission is persuaded by the comments that there are, in at least some cases, account class distinctions within the customer class for non-public customers,[44] and thus agrees that the revised definitions of ''futures account,'' ''foreign futures account,'' and ''cleared swaps account'' within the § 190.01 definition of ''account class'' should address separately non-public customers, and has amended the definitions to do so.

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting the ''account class,'' ''futures account,'' foreign futures account,'' and ''cleared swaps account'' definitions in § 190.01 as proposed with the modifications referred to above.

The ''delivery account'' class is the fourth type of account class. It is the relevant account through which an FCM or DCO accounts for the making or taking of physical delivery under commodity contracts whose terms require settlement by delivery of a commodity. The FCM or DCO designates such account as a delivery account on its books and records. The Commission is adopting the definition of ''delivery account'' as proposed within paragraph (1)(iv) of the definition of account class, with a modification to conform to the issue addressed in the preceding paragraph: The delivery account applies to ''both public and non-public customers, considered separately.''[45]

The current definition of ''delivery account'' in § 190.05(a)(2) refers to an account that contains only property described in three of the nine categories of property in the current definition of ''specifically identifiable property.'' The Commission has determined to adopt a more functional definition of ''delivery account'' in § 190.01. This revised definition will focus on an account maintained on the books and records of an FCM or DCO for the purpose of accounting for the making or taking of delivery under commodity contracts whose terms require settlement by delivery of a commodity.[46]

The Commission is thus adopting paragraph (1)(iv)(A)(*1*) to define delivery accounts for FCMs. The Commission is adopting paragraph (1)(iv)(A)(*2*) to incorporate the same concepts for clearing organizations, and also permit a clearing organization to act as a central depository for physical delivery property represented by electronic title documents, or otherwise in electronic (dematerialized) form.

As set forth in paragraph (1)(iv)(B), the delivery account class is being subdivided into separate physical and cash delivery account classes, as provided in § 190.06(b), for purposes of *pro rata* distributions to customers for their delivery claims. The definitions of the terms ''physical delivery property'' and ''cash delivery property'' are addressed in detail later in this section.

As customer property held in a delivery account is not subject to the Commission's segregation requirements, the Commission believes it may be more challenging and time-consuming to identify customer property for the cash delivery account class,[47] (and such cash would thus be commingled with the FCM's own cash intended for operations). Consequently, the Commission believes separating (1) most cash delivery property and customer claims from (2) most physical delivery property and customer claims should promote more efficient and prompter distribution of the latter to customers. For these reasons, the Commission is adopting the delivery account definition to be further divided into physical delivery and cash delivery account classes, for purposes of *pro rata* distributions to customers for their delivery claims.

The claims with respect to the physical delivery and cash delivery subclasses are fixed on the ''filing date.''[48] Thus, the physical delivery account class includes, in addition to certain physical delivery property, cash delivery property received post-filing date in exchange for physical delivery property held on the filing date that has been delivered under a commodity contract. Conversely, the cash delivery account class includes, in addition to certain cash delivery property, physical delivery property that has been received post-filing date in exchange for cash delivery property held on the filing date.

CME and ICE supported separate subaccounts of the delivery account for physical property (the property being delivered) and cash property (cash used

collateral, and related activity. It confirms that the commodity broker is considered to maintain such an account for the customer regardless of whether it has kept such books and records current or accurate.

[44] *See, e.g.,* § 190.09(c)(2)(iv) (allocating residual property to the non-public customer estate for each account class in the same order as is prescribed in paragraphs (c)(2)(i) through (iii) of this section for the allocation of the customer estate among account classes.)

[45] This separate consideration is a consequence of the fact that, pursuant to Bankruptcy Code section 766(h), public customer claims must be paid in full before non-public customer claims.

[46] *See* § 190.01.

[47] The Commission agrees with a point previously made by the ABA Committee: ''Based on lessons learned from the MF Global Bankruptcy, those challenges are likely greater for tracing cash. Physical delivery property, in particular when held in the form of electronic documents of title as is prevalent today, is more readily identifiable and less vulnerable to loss, compared to cash delivery property that an FCM may hold in an operating bank account.'' *See* Transmittal Letter from The Part 190 Subcommittee of the Business Law Section of the American Bar Association accompanying Model Part 190 Rules (''ABA Cover Note''), *available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=61330&SearchText* at 14. *See also In re MF Global Inc.,* 2012 WL 1424670 (noting how physical delivery property was traceable).

[48] ''Filing date'' means the date that a petition under the Bankruptcy Code or application under SIPA commencing a proceeding is filed or on which the FDIC is appointed as a receiver pursuant to 12 U.S.C. 5382(a).

to pay for delivery). CME agreed with the proposed definition of the delivery account class and supported the proposed separation of the delivery account class into the cash delivery account and physical delivery account classes, as they delineate the customer property that is available to distribute to customers in each account class on a *pro rata* basis. CME agreed that cash delivery property should include cash or cash equivalents recorded in a customer's delivery account as of the filing date, along with any physical delivery property subsequently received in accepting a delivery, and likewise that physical delivery property should include any cash delivery property received subsequent to the filing date in exchange for making a delivery. CME also had specific comments on each of the two subaccount definitions as discussed below.

CME noted that the Commission does not impose segregation requirements on FCMs with respect to the cash or physical delivery property that an FCM holds on behalf of its customers and records in a delivery account. As learned from the *In re MF Global,* Inc. bankruptcy (hereinafter ''MF Global''),[49] CME agreed that it can be more challenging for a trustee to trace the cash recorded in delivery accounts than to trace physical delivery property. For example, the *MF Global* trustee could more readily identify physical delivery property in the form of electronic title documents, compared to identifying non-segregated cash belonging to the delivery account class given the fungible nature of cash.

CME recommended that the Commission address through a separate rulemaking the broader issues around whether customer property carried in delivery accounts should be subject to any special customer protections, such as requirements that FCMs should hold such property in custody accounts or limitations on how long cash or cash equivalents should be held in delivery accounts that are not subject to custody requirements.[50]

At this time, after consideration of the comments and for the reasons stated above the Commission is adopting the definition of ''delivery account'' as proposed, with the modification to note that it applies to each of public and non-public customers, considered separately.

The Commission is adopting the definition of ''cash delivery property'' as proposed with the modifications described below. The Commission proposed to define cash delivery property to carry through the concepts from current § 190.01(ll)(4) and (5) that the cash or cash equivalents, or the commodity must be identified on the books and records of the debtor as having been received, from or for the account of a particular customer, on or after three calendar days before the relevant (i) first delivery notice date in the case of a futures contract or (ii) exercise date in the case of an option.

The Commission is adopting the cash delivery property definition to mean any cash or cash equivalents recorded in a delivery account that is, as of the filing date: (1) Credited to such account to pay for receipt of delivery of a commodity under a commodity contract; (2) credited to such account to collateralize or guarantee an obligation to make or take delivery of a commodity under a commodity contract, or (3) has been credited to such account as payment received in exchange for making delivery of a commodity under a commodity contract. It includes property in the form of commodities that have been delivered after the filing date in exchange for cash or cash equivalents held in a delivery account as of the filing date. The definition also requires that the cash or cash equivalents, or the commodity, must be identified on the books and the records of the debtor as having been received, from or for the account of a particular customer, on or after seven calendar days before the relevant (i) first delivery notice date in the case of a futures contract or (ii) exercise date in the case of a cleared option.[51] In response to comments discussed below, the Commission is adopting the definition of cash delivery property to also include any cash transferred by a customer to the trustee on or after the filing date for the purpose of paying for delivery, consistent with § 190.06(a)(3)(ii)(B)(*1*). The Commission is also adopting the definition in response to comments that requested that the Commission provide that in the case of a contract where one fiat currency is to be exchanged for another fiat currency, each currency will be considered cash delivery property to the extent that it is recorded in a delivery account.

Commenters generally supported separate subaccounts of the delivery account, and that cash delivery property should include cash or cash equivalents recorded in a customer's delivery accounts as of the filing date, along with any delivery property subsequently received in accepting a delivery. However, the Commission also received several comments on three aspects of the proposed definition of cash delivery property.

First, the ABA Subcommittee, CME, ICE, FIA, and CMC recommended that the Commission remove the three-calendar day restriction proposed in the definition of cash delivery property in § 190.01. While several of these commenters recognized the Commission's intention to encourage customers and their FCMs to hold cash in a segregated account where it is better protected until needed to pay for a delivery that is effected in the delivery account, the commenters were concerned that cash or cash equivalents might be posted to delivery accounts sooner than three days before the first notice date or exercise date, and therefore this property might be denied the cash delivery property protection.

FIA stated that the **Federal Register** release did not explain why the Commission proposed to restrict cash delivery property to cash and cash equivalents received no earlier than three calendar days before the relevant first notice day or exercise date. FIA and ICE could not identify any justification as to why cash or cash equivalents that may be received by a debtor FCM and properly deposited in a cash delivery account prior to this period should receive different protections under part 190 than cash and cash equivalents received within the three-calendar day time frame. The ABA Subcommittee noted that their Committee eliminated this provision in the Model Part 190 Rules to avoid unintended consequences.

CME recognized that the three-day limitation is based on the limitation in current part 190, but stated that it does not make sense and if not eliminated from the definition, it could be detrimental to customers, which is contrary to the goal of enhancing customer protections. CME further explained that if a customer posts cash or cash equivalents to its delivery account in anticipation of paying for an upcoming delivery or to guarantee its obligation to take delivery, the timing of the payment should not matter. If the parties intend to make and take delivery, CME believed the trustee should be able to follow the customers' intention. CME explained that a customer is unlikely to leave cash in an unsegregated delivery account with an FCM for any extended time, without reason, when it would be better

[49] *In re MF Global,* No. 11–2790 (MG) (SIPA) (Bankr. S.D.N.Y.).

[50] This recommendation is addressed in section II.G below.

[51] As discussed below, the proposal had specified a period of three calendar days; after consideration of the comments, that period has been changed to seven calendar days.

protected by holding the cash in a segregated account or withdrawing the cash if not needed to meet upcoming delivery obligations. CME noted that there can be times, though, when a customer will legitimately post cash to its delivery account sooner than the definition would allow, for example, out of caution to assure that the necessary funds are available to pay for a delivery when the first notice date or exercise date immediately follows a weekend or holiday, or to meet payment deadlines imposed by the FCM, or based on market convention. CME noted that some FCMs may require customers to post cash sooner than three days prior to the relevant notice or exercise date, as applicable, to satisfy a delivery-related obligation. CME believed it could be potentially disruptive to the delivery process to deny the customer the protection of having its funds classified as cash delivery property because it posted the cash or cash equivalents needed to complete an upcoming delivery too soon.

CME also believed the three-day timing element does not make sense with respect to cash recorded in a customer's delivery account as of the filing date, which the customer had previously received as payment for delivering a commodity under an expired or exercised contract. CME believed the Commission intended for the timing limitation to apply to this situation, but the proposed definition does not exclude such cash from the requirement.

CME understood that the Commission proposed to keep the timing limitation to encourage FCMs and their delivery customers to hold cash intended to pay for a delivery in a segregated account until bilateral delivery obligations are near at hand. However, CME questioned whether the limitation was effective in encouraging the desired behavior, in particular when it is contained in bankruptcy regulations and parties with delivery obligations may not necessarily be aware of it. As a result, CME recommended that the Commission address the protection of customer property held in delivery accounts in a more direct and transparent matter, through a separate rulemaking. Specifically, CME recommended that the Commission revise the ''cash delivery property'' definition to remove the limitation that cash delivery property must be recorded in the delivery account no sooner than three calendar days before the first notice date or exercise date.

The Commission notes that part 190 currently contains the three-day limitation, which serves to limit delivery property to property that is transferred into a delivery account shortly before the notice or exercise date.[52] Thus, the Commission considered whether a change in the current standard is warranted. As discussed further below, the Commission concludes that while the case has been made to extend the limitation from three calendar days to seven calendar days, the case has not been made to remove the limitation in its entirety at this time.

While delivery accounts provide some customer protection, in that they benefit from favorable treatment in bankruptcy, they lack the protection of segregation requirements, in contrast to futures account, foreign futures account, and cleared swaps accounts. In the case of the latter types of accounts, the FCM must maintain in accounts, protected from the claims of creditors of the FCM other than the customers for whom they are segregated, sufficient funds to repay the claims of such customers in full, at all times. Such segregation protections are a very important means of ensuring that sufficient funds are in fact available to pay customers in full in the (highly unlikely) event of the insolvency of an FCM.

Accordingly, the Commission is of the view that changing current part 190 to completely remove any time limitation for protecting property transferred into a delivery account would, in light of this lack of segregation protection, carry the risk of significant unintended consequences, *e.g.,* customers being encouraged to transfer funds prematurely into an account without such protection, and thus a bankruptcy where a greater number of customers receive less than the full amount of their claims, and greater total shortfalls in repayment of such claims.

CME, while noting their preference for simply deleting the three-day limitation, observed that protection of customer property held in delivery accounts should be addressed in a direct and transparent manner through a separate rulemaking. The Commission concludes that deleting entirely the time limitation on posting cash delivery property should only be undertaken, if at all, in the context of a separate, dedicated, and explicit rulemaking, in which moving property more quickly to a delivery account is considered in conjunction with segregation protection for property in such an account.

However, the Commission believes CME's concerns about long weekends raise important issues. For example, in the context of an FCM's global business, there could be a bank holiday on a Friday in the jurisdiction where a customer is based, a Federal holiday on the following Monday in the U.S., and the exercise or notice date might be on a Tuesday; in which event three calendar days may be too short. Similarly, in the vein of CME's comment, there may be legitimate reasons to transfer the funds a day or two in advance of when they are needed, to account for the possibility of a failure in the transfer process.

Weighing the concerns of having funds for an extended time in an account that is not protected by segregation against the need to provide a modest amount of flexibility in the process, the Commission has determined that a reasonable balance can be achieved by changing the three-day (before notice or exercise date) period to a seven-day period. The Commission believes this extended time period will address completely the concern that a delivery date may come after a holiday weekend, and should mitigate concerns about FCM funding requirements that extend beyond three days. If and when a separate rulemaking results in additional protection for delivery accounts, it will be appropriate to revisit this aspect of part 190 as part of such a rulemaking.

Second, the ABA Subcommittee, CME, and CMC recommended that the Committee revise the definition of cash delivery property to allow for the possibility that cash or cash equivalents could be posted after the filing date for the purpose of paying for a delivery, and to provide protection for such deposits. The commenters requested that the Commission expand the definition to allow for the rare possibility that a customer may be unable to post funds needed to pay for a delivery in advance of the filing date so that the definition should also cover cash delivery property received after the filing date in anticipation of taking delivery of a commodity. CME noted that as has been seen with other FCM bankruptcies, the days prior to actual filing can be chaotic and customers may not have had the opportunity to meet such a deadline. To allow the delivery to be completed reduces a potential disruptive situation to commodities markets during an otherwise tumultuous time.

This issue is illuminated by considering the interplay of other

[52] *See* current § 190.05(a)(2) (tying delivery account to portions of the definition of specifically identifiable property in § 190.01); § 190.01(ll)(4) and (5) (limiting recognition of cash as specifically identifiable property to cases where it is identified on the books and records of the FCM as being received from or for the account of a particular customer on or after three calendar days before the first notice date or exercise date specifically for the purpose of a delivery or exercise).

regulations that affect delivery. The Commission notes that while § 190.04(c) continues the preference for the trustee to liquidate contracts moving into delivery position before they do so, and § 190.06(a)(2) continues the preference, in cases where the trustee is unable to do so, for the trustee to arrange for delivery to occur outside the estate, § 190.06(a)(3) acknowledges that there may be cases where the trustee will need to facilitate the making or taking of delivery. Regulation § 190.06(a)(3)(ii)(B)(*1*) refers to cases where the trustee pays for delivery (in whole or in part) with cash transferred by the customer to the trustee on or after the filing date for the purpose of paying for delivery.

Thus, the Commission agrees with the arguments made by the commenters who suggested that the Commission expand the definition of ''cash delivery property'' in this context, and consequently is adding an explicit reference to the cash transferred from a customer to the trustee after the filing date, consistent with § 190.06(a)(3)(ii)(B)(*1*). Moreover, for consistency, the Commission will amend § 190.08(c)(1)(ii) as proposed to explicitly give such post-petition transfers treatment as 100% funded.

Finally, the ABA Subcommittee suggested that the Commission clarify that the delivery of two different fiat currencies for foreign currency commodity contract constitutes cash delivery property. CME suggested a similar technical change to clarify in the definition that for a commodity contract that settles by delivery of a foreign currency as the underlying commodity or by an exchange of a pair of currencies, the USD or foreign currency recorded to a delivery account in connection with either side of the delivery constitutes cash delivery property.

In response to the ABA Subcommittee comment regarding the delivery of two fiat currencies, ''[g]iven the fungible nature of cash, regardless of currency denomination,'' the Commission has determined to amend further the definition of ''cash delivery property'' to clarify that for foreign exchange contracts, *i.e.,* contracts where one fiat currency is exchanged for another fiat currency, both fiat currencies will be treated as cash delivery property, and neither currency will be considered physical delivery property.

Accordingly, in consideration of the comments and the reasons discussed above, the Commission will adopt the definition of ''cash delivery property'' in § 190.01 as modified, with the additions referred to above.

The Commission is adopting the definition of ''physical delivery property'' in § 190.01 as proposed with modifications, as described below. The Commission is adopting the definition of ''physical delivery property'' to include, under the four specified sets of circumstances discussed below, a commodity, whether tangible or intangible, held in a form that can be delivered to meet and fulfill delivery obligations under a commodity contract that settles via delivery if held to a delivery position.[53] The Commission is adopting the definition to include warehouse receipts, other documents of title, or shipping certificates (including electronic versions of the forgoing), for the commodity, or the commodity itself.

The Commission is amending the physical deliver property definition to address changes in delivery practices since the 1980s. The reference to electronic versions of warehouse receipts, other documents of title, or shipping certificates explicitly recognizes that title documents for commodities are now commonly held in dematerialized, electronic form, in lieu of paper. Moreover, the types of commodities that might be physically delivered would extend beyond tangible commodities to those that are intangible, including Treasury securities, foreign currencies, or virtual currencies.[54]

For purposes of analytical clarity, the Commission is adopting the definition of physical delivery property as subdivided into four categories:

First, the commodities or warehouse receipts, other documents of title, or shipping certificates (including electronic versions of any of the foregoing) for the commodity that the debtor holds for the account of a customer for purposes of making delivery of such property and which, as of the filing date or thereafter, can be identified as held in a delivery account for the benefit of such customer on the books and records of the debtor.[55]

Second, the commodities or warehouse receipts, other documents of title, or shipping certificates (including electronic versions of any of the foregoing) for the commodity that the debtor holds for the account of the customer, where the customer received or acquired such property by taking delivery under an expired or exercised commodity contract, and which, as of the filing date or thereafter, can be identified as held in a delivery account for the benefit of such customer on the books and records of the debtor.[56]

The third category addresses property that (a) is in fact being used, or has in fact been used, for the purpose of making or taking delivery, but (b) is held in a futures, foreign futures, cleared swaps, or (if the commodity is a security) securities account.[57] This property would be considered physical delivery property *solely* for the purpose of the obligations, pursuant to § 190.06, to make or take delivery of physical delivery property. The property in this category would be *distributed* as part of the account class in which it is held (futures, foreign futures, or cleared swaps, or, in the case of a securities account, as part of a SIPA proceeding).

Fourth, where such commodities or documents of title are not held by the debtor, but are delivered or received by a customer in accordance with § 190.06(a)(2) (either by itself in the case of an FCM bankruptcy or in conjunction with § 190.16(a) in the case of a clearing organization bankruptcy), they will be considered physical delivery property, but, again, *solely* for purposes of obligations to make or take delivery of physical delivery property pursuant to § 190.06. As this property is held outside of the debtor's estate (and there was no obligation to transmit it to the debtor's customer accounts), it is not subject to *pro rata* distribution.

The Commission is also adding a special case to correspond with the special case for cash delivery property, which states that where one fiat currency is exchanged for another, neither such currency, to the extent that it is recorded in the delivery account, will be considered physical delivery property. The Commission is also, as discussed further below, additionally amending the physical delivery property definition to address the possibility of a negative delivery price

[53] The current definition is found in § 190.01(ll)(3), and focuses on documents of title and physical commodities.

[54] *See* ABA Cover Note at 10, 12–13.

[55] These first two categories together correspond to current § 190.01(ll)(3), with the first category corresponding to physical delivery property held for the purpose of *making* delivery and the second category corresponding to physical delivery property held as a result of *taking* delivery. The property that is (or should be) within these two categories, as of the filing date, comprises the property that will be distributed as part of the physical delivery class.

[56] The current definition does not prescribe or imply a limit to how long such received property can be held in a delivery account, because there is no principled basis to draw a bright line delineating how long is too long. The definition the Commission is adopting explicitly codifies that position.

[57] As the ABA Cover Note explained at 13, ''[w]hen the FCM has a role in facilitating delivery, deliveries may occur via title transfer in a futures account, foreign futures account, cleared swaps account, delivery account, or, if the commodity is a security . . . in a securities account.''

where the party obliged to delivery physical delivery property under an expiring contract or an expired options contract is also obliged to make a cash payment to the buyer, as such cash or cash equivalents constitute physical delivery property.

CME and CMC agreed that physical delivery property should include any cash delivery property received subsequent to the filing date in exchange for making a delivery.

In light of the evolving nature of intangible assets, and of the manner in which they may be held, custodied or transferred, ICE suggested that the definition of physical delivery property include, as examples (and not by way of limitation), other electronic representations of commodities (whether or not technically ''an electronic title document'') or any property entitlement to a commodity (such as for a commodity held as a financial asset in a securities account under Article 8 of the Uniform Commercial Code (whether or not a security) or similar structure).

ICE strongly agreed with the Commission's proposal to clarify that intangible property received or held for purposes of delivery is appropriately regarded as subject to the delivery account, without regard to whether it is ''physical'' as under the current rule. ICE argued that any asset, tangible or intangible, that can be delivered in settlement of a contract should be eligible to be treated as delivery property, as set out in the proposed definition of ''physical delivery property.'' ICE believed this proposed definition would avoid questions that may otherwise arise in connection with the delivery of digital currencies or other novel digital assets. CME also supported the decision to expand the delivery account class to cover intangible commodities.

Additionally, CME supported modernizing the definition of physical delivery property to recognize the use of electronic delivery documents in effecting deliveries under physical delivery commodity contracts. CME recommended that the Commission further expand the physical delivery property definition to cover within its scope any cash or cash equivalents that a seller may deposit in its delivery account when its obligation to deliver physical delivery property under an expiring futures or exercised options contract also includes an obligation to make a cash payment to the buyer, as could arise if the contract's final settlement price is negative. CME acknowledged that this scenario would be unprecedented and may never occur, but believed it prudent to contemplate the possibility in light of events in April 2020 where certain physical-delivery oil futures contracts traded below zero in the days prior to establishment of the final settlement prices.

CME also recommended a technical correction to the definition relating to the fact that shipping certificates are not electronic title documents, and instead represent the contractual obligation of a facility to deliver the underlying commodity to the buyer. Thus, for clarity CME recommended that the Commission revise the phrase ''including warehouse receipts, shipping certificates or other documents of title (including electronic title documents) for the commodity'' to read ''including warehouse receipts, shipping certificates or *other* similar documents (including electronic *versions thereof*).'' The Commission is not amending the examples to explicitly address additional ''electronic representations of commodities'' within the definition of physical delivery property because the definition already broadly covers ''a commodity, whether tangible or intangible, held in a form that can be delivered to meet and fulfill delivery obligations under a commodity contract. . . .''

The Commission is amending the definition of physical delivery property to address the technical correction recommended by CME by acknowledging that shipping certificates are not documents of title while avoiding the phrase ''similar documents'' by instead amending the last phrase to read ''including warehouse receipts, other documents of title, or shipping certificates (including electronic versions of any of the foregoing) for the commodity, or the commodity itself.''

The Commission is also adding a special case, corresponding to the special case for cash delivery property, stating that where one fiat currency is exchanged for another, neither such currency would be considered physical delivery property.

The Commission is further amending the physical delivery property definition with a second special case in response to CME's suggestion to address the possibility of a negative delivery price. While negative prices for deliverable commodities are rare, they are not unprecedented (*e.g.,* the price of crude oil briefly went negative in April 2020). While a negative price for actual delivery may be even rarer, it is theoretically possible. Thus, the Commission is amending the definition of ''physical delivery property'' to address this special case by adding the following: In a case where the final settlement price is negative, *i.e.,* where the party obliged to deliver physical delivery property under an expiring futures contract or an expired options contract is also obliged to make a cash payment to the buyer, such cash or cash equivalents constitute physical delivery property.

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting the definition of ''physical delivery property'' as proposed with the appropriate modifications to the structure, as set forth above, to correspond to ''(1) *In general.*'' and to address two special cases in ''(2) *Special cases.*'' The Commission is adopting the definition of ''allowed net equity'' as proposed in § 190.01 and as modified to become ''funded net equity'' as described below. The Commission proposed ''allowed net equity'' to update cross-references and allow for two definitions of the term (as used in subparts B and C of part 190).

The ABA Subcommittee expressed concern in their comment letter that the definition and the use of the term ''allowed net equity'' as proposed in §§ 190.01 and 190.08(a) could create inconsistencies and confusion between part 190 and the settled bankruptcy law terminology in which ''allowed'' typically refers to the fixed amount of a creditor's claim rather than the amount distributable on such claim. The ABA Subcommittee recommended three modifications to address this potential confusion, including the deletion of the definition of ''allowed net equity'' in proposed §§ 190.01 and 190.08(a), as the ABA Subcommittee believes the remainder of proposed § 190.08 would address how to calculate a customer's net equity claims and the funded balances for each such claims.[58]

The Commission agrees with the ABA Subcommittee that the inclusion of ''allowed'' in the defined term ''allowed net equity'' could cause confusion in the broader context of established bankruptcy law, where ''allowed'' refers to the trustee's measure of the proper amount of a claim, rather than to the

[58] The ABA Subcommittee also recommended that the Commission further amend § 190.02 by adding new paragraph (g) to proposed § 190.02 to state that the term 'allowed' in this part shall have the meaning ascribed to it in the Bankruptcy Code. The ABA Subcommittee believed that this would confirm that ''allowed'' under part 190 equates with the use of ''allowed'' under the Bankruptcy Code. The ABA Subcommittee also recommended that the Commission add ''funded balance of'' before ''such customer's allowed net equity claim'' in proposed § 190.09(d)(3). The Commission agrees that these recommended amendments would avoid confusion with the meaning of ''allowed'' in § 190.02(g) and is therefore making these suggested changes.

portion of a claim that is funded (in *pro rata* distribution).

Accordingly, after consideration of the comments, including the ABA Subcommittee's suggestion regarding the funded portion of a customer's allowed claim throughout part 190, and for the reasons stated above, the Commission is changing the defined term ''allowed net equity'' to ''funded net equity,'' and adopting the definition as so modified. The Commission is also adding § 190.02(g) (as discussed below) and adding ''funded balance of'' before ''such customer's allowed net equity claim'' in § 190.09(d)(3) as suggested.

The Commission is adopting the definition of ''commodity contract'' in § 190.01 as proposed, in order to amend the definition to incorporate and extend in context (through references to current Commission regulations) the definition in section 761(4) of the Bankruptcy Code.[59]

ICI strongly supported the proposed amendments to the definition of ''commodity contract'' to include any ''futures contract'' and any ''swap'' thereby permitting transactions carried in a futures or cleared swaps account in accordance with the Commission's regulations to be eligible for the protections that part 190 affords.

Accordingly, after consideration of the comment and for the reasons stated above, the Commission is adopting the definition of ''commodity contract'' as proposed.

The Commission is adopting the definition of ''customer property and customer estate'' as proposed to update the definition to clarify cross-references within part 190 and to note that customer property distribution is addressed in section 766(i) of the Bankruptcy Code in addition to section 766(h).

ICE supported the Commission's decision to include forward contracts that are traded on a DCM and cleared by a DCO as customer property.

Accordingly, after consideration of the comment, and for the reasons stated above, the Commission is adopting the definition of ''Customer property, customer estate'' in § 190.01 as proposed.

The Commission is adopting the definition of ''house account'' with modifications, as set forth below to modify the existing definition to (a) clarify the connection between the concept of a ''house account'' in part 190 and the concept of a proprietary account in § 1.3, and (b) separately define the term in relation to an FCM, a foreign futures commission merchant, and a DCO.

The ABA Subcommittee and CME agreed with expanding the current definition to cover the house accounts that DCOs maintain for clearing members. However, the commenters noted that ''house account'' is used in only three places for an FCM proceeding: (i) Proposed § 190.06(a)(5), which addresses deliveries made or taken with respect to the debtor FCM's house account under open commodity contracts; (ii) proposed § 190.07(c), which prohibits transfer of the debtor FCM's house account after the filing date; and (iii) proposed § 190.08(b)(2)(ix), which provides that when a non-debtor FCM maintains an omnibus account and a house account with a debtor FCM, it holds the accounts in a separate capacity for purposes of calculating its net equity claims against the debtor FCM. Assuming the Commission intended to expand the scope of these provisions in each case, the ABA Subcommittee and CME suggested that the Commission modify the three provisions to clarify that they apply to proprietary accounts of FCMs, and to limit the defined term to house accounts maintained by a DCO for clearing members. The ABA Subcommittee believed it was unnecessary, potentially confusing, and could preclude porting of proprietary accounts.

The Commission agrees with the commenters' recommendation to streamline the ''house account'' definition and amend the respective subpart B provisions to limit the use of ''house account'' to the context of clearing organization bankruptcies to avoid any potential confusion regarding the ability to port proprietary accounts. Accordingly, after considering the comments, and for the reasons stated above, the Commission is adopting the definition of ''house account'' in § 190.01, as modified.

The Commission is adopting the definitions of ''non-public customer'' and ''public customer'' as proposed to define who is considered a public versus a non-public customer separately for FCMs and for clearing organizations. These definitions are complements (*i.e.,* every customer is either a ''public customer'' or a ''non-public customer,'' but never both).

In the case of a customer of an FCM, the Commission is adopting the definition of ''public customer,''[60] which would be analyzed separately for each of the relevant account classes (futures, foreign futures, cleared swaps, and delivery) with the relevant cross-references to other Commission regulations. For the ''futures account class,'' this would be a futures customer as defined in § 1.3, whose futures account is subject to the segregation requirements of section 4d(a) of the Act and the Commission regulations thereunder; for the foreign futures account class, a 30.7 customer as defined in § 30.1, whose foreign futures account is subject to the segregation requirements of § 30.7; for the cleared swaps account class, a cleared swaps customer as defined in § 22.1, whose cleared swaps account is subject to the segregation requirements of part 22; and for the delivery account class, a customer that would be classified as a ''public customer'' if the property held in the customer's delivery account had been held in an account described in one of the prior three categories. The Commission is tying the definition of public customer for bankruptcy purposes to the definitions of ''customer'' (and segregation requirements) that apply during business as usual. An FCM's non-public customers are customers that are not public customers.

As part of the process for introducing a bespoke regime for the bankruptcy of a clearing organization, the Commission is differentiating between public and non-public customers such that customers of clearing members (whether such clearing members are FCMs or foreign brokers) acting on behalf of their proprietary (*i.e.,* house) accounts, would be non-public customers, while all other customers of clearing members would be public customers.

In the case of members of a DCO that are foreign brokers, the determination as to whether a customer of such a member is a proprietary member would be based on either the rules of the clearing organization or the jurisdiction of incorporation of such member: If either designates the customer as a proprietary member, then the customer would be treated as a non-public customer.

Vanguard agreed that the proposed definition of public customer in § 190.01 included any customer of an FCM whose commodity contract is subject to the Commission's segregation

[59] It should be noted that, consistent with § 190.00(d)(3)(iv) and the decision *In re Peregrine Financial Group, Inc.,* 866 F.3d 775, 776 (7th Cir. 2017), *adopting by reference Secure Leverage Group, Inc.* v. *Bodenstein,* 558 B.R. 226 (N.D. Ill. 2016), retail foreign exchange contracts do not fit within the definition of commodity contracts.

[60] This is in contrast to the current definition in § 190.01(cc) and (ii), which explicitly define non-public customer, and define public customer as a customer that is not a non-public customer. This change is not substantive, but rather fosters closely tying the account classes to business-as-usual segregation requirements.

requirements, and for a DCO, a person whose account with the FCM is not classified as a proprietary account. CME also supported the proposed definitions of public customer and non-public customer as it believed they are more understandable than the prior part 190 definitions.

CME, however, asked the Commission to reconsider the recommendation of the ABA Subcommittee to include non-U.S. customers of foreign broker clearing members of a DCO within the public customer definition. CME noted that it previously considered admitting foreign brokers as clearing members to clear trades of their non-U.S. customers in futures or options on futures listed on the CME or the other designated contract markets (''DCMs'') owned by CME Group, which would be analogous to a foreign clearing organization admitting FCMs as members to clear trades of their public customers in futures or options on futures listed by a foreign board of trade. While that model does not currently exist for U.S. DCOs and the DCMs for which they provide clearing services, CME believed it is appropriate to include that flexibility in part 190 to accommodate that possibility. OCC also requested clarification as to whether customers of foreign brokers that access a DCO through an FCM clearing member affiliated with the foreign broker would be treated as public customers.

The Commission is of the view that including non-U.S. customers of foreign-broker clearing members as public customers should be considered as part of a comprehensive review of the issues at such time as the model of admitting foreign brokers as clearing members for U.S. DCOs becomes empirical. Such a review of the issues, including issues related to both bankruptcy and risk management, can be more reliably, and more efficiently, be conducted in the context of empirical rather than hypothetical circumstances.

In response to OCC's request for clarification, the Commission notes that where a foreign broker clears the trades of its (foreign) customers through an affiliated FCM that is a clearing member, those trades would be cleared on an omnibus basis through the FCM's customer account, and would be required to be kept separate from the proprietary trades of the affiliated foreign broker. Thus, those customers would be treated as public customers. If a foreign broker clears its own proprietary trades through an unaffiliated FCM (*i.e.,* there is no proprietary relationship between the foreign broker and the FCM as set forth in § 1.3), those trades would be considered as public customer trades at the FCM, but would not be part of the customer omnibus account of the foreign broker at the FCM.

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting the definitions of ''non-public customer'' and ''public customer'' as proposed in § 190.01.

The Commission is adopting the definitions of ''variation settlement'' as proposed to define the payments that a trustee may make with respect to open commodity contracts. The definition of variation settlement includes ''variation margin'' as defined in § 1.3, and also includes ''all other daily settlement amounts (such as price alignment payments) that may be owed or owing on the commodity contract'' to cover all of the potential obligations associated with an open commodity contract.

CME supported defining variation settlement and generally agreed with the substance of the definition, but recommended that the Commission adopt one self-contained definition that does not rely on cross-reference to another Commission definition. CME suggested that the Commission adopt the ABA Subcommittee's variation settlement definition which would cover ''any amount paid or collected (or to be paid or collected) on an open commodity contract relating to changes in the market value of the commodity contract since the trade was executed or the previous time the commodity contract was marked to market along with all other daily settlement amounts (such as price alignment payments) that may be owed or owing on the commodity contract.''

The ABA Subcommittee believed that the definition of variation settlement was not used consistently in the Proposal and identified two places in proposed § 190.14(b) where the term ''variation'' is used instead of ''variation settlement.'' The ABA Committee recommended using ''variation settlement'' in both places, to avoid any confusion as to whether ''variation'' refers to the Commission's variation margin definition or variation settlement definition.

The Commission notes that the cross-references in § 190.01 to definitions in other parts of the Commission's rules is intentional to clarify the relationships with those other definitions, and thus the Commission declines to make the change proposed by the commenters.[61]

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting the definition of ''variation settlement'' in § 190.01 as proposed.

The Commission did not receive comments on the remaining definitions in § 190.01 and is therefore adopting them as proposed.

The Commission is adopting the definition of ''Act'' in § 190.01 to refer to the Commodity Exchange Act.

The Commission is amending the definition of ''Bankruptcy Code'' in § 190.01 to update cross-references.

The Commission is amending the definition of ''Business day'' to define what constitutes a Federal holiday and clarify that the end of a business day is one second before the beginning of the next business day.

The Commission is amending the definition of ''Calendar day'' to include a reference to Washington, DC as the reference location for the Calendar day.

The Commission is adopting the definition of ''Cash delivery account class'' to cross-reference it to the new definition in ''Account class.''

The Commission is adopting the definition of ''Cash equivalents'' to define assets that might be accepted as a substitute for United States dollar cash.

The Commission is amending the definition of ''Cleared swaps account'' in § 190.01 to cross-reference it to the new definition in ''Account class.''

The Commission is adopting the amended definition of ''Clearing organization'' to update cross-references.

The Commission is amending the definition of ''Commodity broker'' to reflect the current definition of commodity broker in the Bankruptcy Code and the relevant cross-references.

The Commission is adding the definition of ''Commodity contract account'' to refer to accounts of a customer based on commodity contracts in one of the four account classes, as well as, for purposes of identifying customer property for the foreign futures account class (subject to § 190.09(a)(1)), accounts maintained by foreign clearing organizations or foreign futures intermediaries reflecting foreign futures or options on futures executed on or subject to the rules of a foreign board of trade, including any account maintained on behalf of the debtor's public customers.

The Commission is amending the definition of ''Court'' to clarify that the court having jurisdiction over the

[61] The technical correction suggested by the ABA subcommittee to § 190.14(b) (change ''variation'' to ''variation settlement'') will be adopted in one case; the subsection where the second case was found has been removed entirely by the supplemental notice of proposed rulemaking.

debtor's estate may not be a bankruptcy court (*e.g.,* in the event of a withdrawal of the reference).[62]

The Commission is amending the definition of ''Cover'' to improve clarity without any substantive change to the current definition.

The Commission is amending the definition of ''Customer'' to reflect the revisions to part 190 through this rulemaking, specifically, noting the different meanings of ''customer'' with respect to an FCM in contrast to with respect to a DCO.

The Commission is amending the definition of ''Customer claim of record'' to improve clarity without any substantive changes to the current definition.

The Commission is amending the definition of ''Customer class'' to reflect the revisions to part 190 through this rulemaking, specifically emphasizing the difference between public customers and non-public customers.

The Commission is deleting the definition of ''Dealer option'' as this term is no longer used.

The Commission is amending the definition of ''Debtor'' to explicitly refer to commodity brokers involved in a bankruptcy proceeding, a proceeding under SIPA, or a proceeding under which the FDIC is appointed as a receiver.

The Commission is newly adopting a definition of ''Distribution'' to include the transfer of property on a customer's behalf, return of property to a customer, as well as distributions to a customer of valuable property that is different than the property posted by that customer.

The Commission is amending the definition of ''Equity'' to update a cross-reference.

The Commission is adding definitions for ''Exchange Act'' and ''FDIC'' to incorporate the statute and regulator, respectively, in part 190.

The Commission is revising the definition of ''Filing date'' to include the commencement date for proceedings under SIPA or Title II of the Dodd-Frank Act.[63]

The Commission is revising the definition of ''Final net equity determination date'' stylistically, to provide updated cross-references, and to further clarify who the parties involved are intended to be.

The Commission is adding the definition of ''Foreign board of trade'' and adopting by reference the definition in § 1.3 (which is consistent with § 48.2(a)).

The Commission is adding the definition of ''Foreign clearing organization'' to refer to a clearing house, clearing association, clearing corporation or similar entity, facility or organization that clears and settles transactions in futures or options on futures executed on or subject to the rules of a foreign board of trade.

The Commission is retaining the definitions of ''Foreign future'' and ''Foreign futures commission merchant'' as proposed to be unchanged.

The Commission is adopting the definition of ''Foreign futures intermediary'' to refer to a foreign futures or options broker, as defined in § 30.1, acting as an intermediary for foreign futures contracts between a foreign futures commission merchant and a foreign clearing organization.

The Commission is revising the definition of ''Funded balance'' to the definition in § 190.08(c). That definition is discussed further below in section II.B.6.

The Commission is adding a definition for ''Futures'' and ''Futures contract,'' used interchangeably, to clarify what these terms mean for purposes of part 190.

The Commission is deleting the definition of ''In-the-money amount'' as the term will no longer be used and replacing it with ''in-the-money,'' a term that is Boolean, and is used in § 190.04(c).

The Commission is amending the definition of ''Joint account'' to reflect that a commodity pool must be a legal entity.[64] Thus, the Commission is removing the reference to a commodity pool that is not a legal entity.

The Commission is deleting the definitions of ''Leverage contract'' and ''Leverage transaction merchant'' consistent with the discussion above with respect to § 190.00(d)(1)(i)(B).

The Commission is removing the definition of ''Member property'' from current § 190.09(a) and addressing it in § 190.01, and clarifying that member property is the property that may be used to pay net equity claims based on both the members' house account as well as claims on behalf of non-public customers of the member.

The Commission is revising the definition of ''Net equity'' to update cross-references, including the difference between bankruptcy of an FCM and of a clearing organization.

The Commission is revising the definition of ''Open commodity contract'' to improve clarity without any substantive changes to the definition.

The Commission is revising the definition of ''Order for relief'' to update cross-references and incorporate stylistic, non-substantive changes.

The Commission is adding the definition of ''Person'' to clarify what this term means in the context of part 190.

The Commission is adding the definition of ''Physical delivery account class'' to be cross-referenced to the new definition in ''Account class.''

The Commission is deleting the definition of ''Premium'' as that term is no longer used.

The Commission is revising the definition of ''Primary liquidation date'' to reflect the removal of the concept of accounts being held open for later transfer. As a result of such removal, the Commission is also deleting current § 190.03(a), which set forth provisions regarding the operation of accounts held open for later transfer, since there will no longer be any such accounts.

The Commission is deleting the definition of ''Principal contract'' as that term is no longer used. This term was previously used to refer to contracts that are not traded on designated contract markets, but the definition excluded cleared swaps.

The Commission is adding the definition of the ''Securities account'' and ''SIPA'' to address the bankruptcy of an FCM that is also subject to the Securities Investor Protection Act. These are based on appropriate cross-references to the Exchange Act and SIPA.

The Commission is amending the definition of ''Security'' to update the cross-reference to the Bankruptcy Code without any substantive changes to the definition.

The Commission is removing the definition of ''Short term obligation'' from § 190.01 as the term is no longer used within the definition of ''specifically identifiable property.'' The Commission is instead amending the ''specifically identifiable property''

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[62] *Cf.* 28 U.S.C. 157(d).

[63] In SIPA, the term ''filing date'' is defined to occur earlier than the filing of an application for a protective decree if the debtor is the subject of a proceeding in which a receiver, trustee, or liquidator for the debtor has been appointed and such proceeding is commenced before the date on which the application for a protective decree under SIPA is filed. In such case, the term ''filing date'' is defined to mean the date on which such proceeding is commenced. By contrast, this rulemaking does not define the term ''filing date'' to occur earlier in such a case, although it would (in § 190.02(f) as discussed below) authorize such a to receiver themselves file a voluntary petition for bankruptcy of the FCM.

This difference is due to the different uses of the ''filing date'' in these rules and in SIPA. For purposes of part 190, ''filing date'' refers to the date on and after which a commodity broker is treated as a debtor in bankruptcy. *See, e.g.,* §§ 190.00(c)(4), 190.06(a)(1) and (b)(1), 190.08(b)(4), and 190.09(a)(1)(ii)(A). For purposes of SIPA, by contrast, the ''filing date'' is the date on which securities are valued. *See, e.g.,* SIPA sections 8(b), 8(c)(1), 8(d), 9 ff–2(b), (c)(1), (d), and 78fff–3(a)(3).

[64] *See* § 4.20(a)(1).

definition with respect to securities, as discussed immediately below.

The Commission is amending the definition of ''Specifically identifiable property'' to update and streamline the definition in current § 190.01(ll). Paragraph (1)(i) focuses on ''futures accounts,'' ''foreign futures accounts,'' and ''cleared swaps accounts.'' Paragraph (1)(i)(A) corresponds in major part to paragraphs (ll)(1) and (6) of the current definition. For securities, paragraph (1)(i)(A)(*1*) substantially copies current paragraph (ll)(1)(i), but clarifies that a security, to be included as specifically identifiable property, must have ''a duration or maturity date of more than 180 days.'' Paragraph (1)(i)(A)(*2*) reformats current paragraph (ll)(6). For warehouse receipts, bills of lading, or other documents of title (paragraph (i)(B), corresponding to current paragraph (ll)(1)(ii)), the definition restates the corresponding portion of the current definition.

Paragraph (1)(ii) of the definition furthers the approach of providing discretion to the trustee. It includes as specifically identifiable property commodity contracts that are treated as such in accordance with § 190.03(c)(2). As discussed further below,[65] the latter provision permits (but does not require) the trustee, following consultation with the Commission, to treat open commodity contracts of public customers as specifically identifiable property if they are held in a futures account, foreign futures account, or cleared swaps account that is designated as a hedging account in the debtor's books and records, and if the trustee determines that treating the commodity contracts as specifically identifiable property is reasonably practicable under the circumstances of the case. In contrast, paragraph (ll)(2) of the current definition is more prescriptive.

The Commission is amending the definition of ''Strike price'' for brevity without any substantive change.

The Commission is adding the definition of ''Substitute customer property'' to refer to the property (in the form of cash or cash equivalents) delivered to the trustee by or on behalf of a customer in order to redeem either specifically identifiable property or a letter of credit.

The Commission is adopting the definition of ''Swap'' to replace the current definition of ''Cleared swap''[66] in part 190. The definition of reflects the current definition and meaning of the term ''swap'' in section 1a(47) of the CEA and Commission regulation § 1.3.

The Commission is also adopting the definition to add as a swap, for purposes of this part, ''any other contract, agreement or transaction that is carried in a cleared swaps account pursuant to a rule, regulation or order of the Commission, provided, in each case, that it is cleared by a clearing organization [*i.e.,* a DCO] as, or the same as if it were, a swap.''[67]

The Commission is amending the definition of ''Trustee'' to include the trustee in a SIPA proceeding.

The Commission is adopting a definition of ''Undermargined'' for purposes of part 190 to mean when the funded balance of a debtor's futures account, foreign futures account, or cleared swaps account is below the minimum amount that the debtor is required to collect and maintain for the open commodity contracts in such account under the rules of the relevant clearing organization, foreign clearing organization, DCM, Swap Execution Facility (''SEF''), or FBOT. If any such rules establish both an initial margin requirement and a lower maintenance margin[68] requirement applicable to any commodity contracts (or to the entire portfolio of commodity contracts or any subset thereof) in a particular commodity contract account of the customer, the trustee will use the lower maintenance margin level to determine the customer's minimum margin requirement for such account. An undermargined account may or may not be in deficit.[69]

Accordingly, after consideration of the comments, and for the reasons discussed above, the Commission will adopt § 190.01 as proposed, with the amendments discussed above.

3. Regulation § 190.02: General

Regulation § 190.02 is being adopted as proposed, with the addition of paragraph (g) as described below. The Commission is adopting § 190.02(a)(1) based on current § 190.10(b)(1) with one substantive change to permit a trustee to request an exemption from the Commission from any procedural provision (rather than limiting such requests to exemptions from, or extension of, a time limit). Such an exemption may be subject to conditions, and must be consistent with the purposes of this part and of subchapter IV of the Bankruptcy Code. The Commission is adopting § 190.02(a)(1) consistent with major theme 7, discussed in section I.B. above regarding enhanced trustee discretion. Section 190.02(a)(1) allows the trustee to request to be permitted to extend a deadline or to amend a form.

The Commission is also adopting § 190.02(a)(2)(i) and (ii), (a)(3), and (b), as derived from current §§ 190.10(b)(2), (3), and (4) and 190.10(d), respectively, with minor editorial and conforming changes.

The Commission is adopting § 190.02(b) to delegate the functions of the Commission set forth in part 190, other than the authority to disapprove pre-relief transfers pursuant to § 190.07(e)(1), to the Director of the Division of Clearing and Risk, after consultation with the Director of the Market Participants Division[70] (with the possibility of further delegations to members of the respective Directors' staffs).

The Commission is adopting § 190.02(c) to exclude from the definition of ''customer'' entities who hold claims against a debtor solely on account of uncleared forward contracts. The Commission is adopting § 190.02(d) to provide that the Bankruptcy Code will not be construed to prohibit a commodity broker from doing certain combinations of business, or to permit any otherwise prohibited operation, trade or business. The Commission is adopting § 190.02(e) to provide that security futures products held in a securities account shall not be considered to be part of commodity futures or options accounts as those terms are used in section 761(9) of the Bankruptcy Code. The Commission is adopting § 190.02(c) (forward contracts), (d) (other), and (e) (rule of construction) as transposed from current § 190.10(e), (g), and (h), respectively.

The Commission continues to believe, as stated in the proposal, that § 190.02(f) should enhance customer protection in cases where a receiver has been

[65] *See* section II.B.1.c.

[66] *See* current § 190.01(pp).

[67] *Cf.* 11 U.S.C. 761(4)(F)(ii) (including as a commodity contract ''with respect to a futures commission merchant or clearing organization, any other contract, option, agreement, or transaction, in each case, that is cleared by a clearing organization'').

[68] For further discussion of maintenance margin and its relationship to initial margin, *see, e.g., https://www.cmegroup.com/education/courses/introduction-to-futures/margin-know-what-isneeded.html.*

[69] An account is in deficit if the balance is negative (*i.e.,* the customer owes the debtor instead of the reverse). An account can be undermargined but not in deficit (if the balance is positive, but less than the required margin). *See* discussion of § 190.04(b)(f). For example, if the margin requirement is $100 and the account balance is $20, the account is undermargined by $80, but is not in deficit. If the account loses a further $35, the balance would be ($15). The account would be in deficit by $15, and would be undermargined by $115.

[70] The Market Participants Division is the successor to the Division of Swap Dealer and Intermediary Oversight, the title of that division at the time of the Proposal.

appointed (pursuant to *e.g.,* section 6c of the CEA) for an FCM due to a violation or imminent violation [71] of the customer property protection requirements of section 4d of the CEA or of the regulations thereunder, or of the Commission's capital rule (§ 1.17). Section 190.02(f) explicitly permits such a receiver to file a voluntary petition for bankruptcy of such FCM in appropriate cases. For example, the receiver may determine that, due to a deficiency in property in segregation, bankruptcy is necessary to protect customers' interests in customer property.

The Commission requested comment with respect to all aspects of proposed § 190.02. In particular, the Commission requested comment as to whether it would be appropriate to permit trustees to request relief from procedural provisions such as requirements as to forms, in addition to requesting relief from deadlines; whether it would be appropriate to permit receivers for FCMs to file voluntary petitions in bankruptcy; and whether any portion of proposed § 190.02 would likely to lead to unintended consequences, and, if so, how may these be mitigated.

The Commission received two comments on proposed § 190.02. CME generally supported proposed § 190.02, including adding a provision that would allow the trustee to request an exemption from the procedural requirements of the rules. CME also favored adding the proposed provision to clarify that a receiver appointed for an FCM due to segregation or net capital violations may, in an appropriate case, file a petition for bankruptcy of the FCM pursuant to section 301 of the Bankruptcy Code. In contrast, FIA recommended that the Commission require a receiver to obtain the Commission's consent before the receiver may file a voluntary petition in bankruptcy on behalf of an FCM. FIA believed that any receiver that may be appointed by a court would be in response to a proceeding initiated by the Commission pursuant to section 6c of the Act, which authorizes the Commission to file an action in the appropriate U.S. District Court when it appears that a person has engaged, is engaging, or is about to engage in any act or practice constituting a violation of any provision of this Act or any rule, regulation, or order thereunder. FIA noted that there may be circumstances in which a receiver may determine that a voluntary petition under the Bankruptcy Code is warranted. However, in light of the fact that such a petition would effectively close the FCM, FIA believed that § 190.02(f) should provide that the receiver may file a voluntary petition only with the prior consent of the Commission.

The Commission notes that § 190.02(f) is limited to cases where the receiver was appointed due to concerns about either protection of customer property, or of capital inadequacy, and the appointment would be in response to a proceeding initiated by the Commission. In such a case, the Commission believes that it would be appropriate and most effective to defer to the judgment of the appointed receiver as to the necessity of the filing of a petition in bankruptcy.

As a technical point, the ABA Subcommittee recommended (consistent with their recommendation in the definitions section, § 190.01, to more precisely use the term ''allowed net equity'') [72] that the Commission further amend § 190.02 by adding new paragraph (g) to proposed § 190.02 to state that the term ''allowed'' in this part shall have the meaning ascribed to it in the Bankruptcy Code. The ABA Subcommittee believed that this would confirm that ''allowed'' under part 190 equates with the use of ''allowed'' under the Bankruptcy Code. The Commission agrees, and is making the change.

Accordingly, after consideration of the comments, and for the reasons stated above, the Commission is adopting § 190.02 as proposed, with the addition of paragraph (g).

B. Subpart B—Futures Commission Merchant (FCM) as Debtor

The Commission is adopting subpart B (§§ 190.03–190.10) to address debtors that are FCMs.

1. Regulation § 190.03: Notices and Proofs of Claims

The Commission is adopting § 190.03 as proposed with modifications to § 190.03(c)(2), as set forth below.

The Commission is adopting § 190.03 to set forth requirements for the notices and proofs of claim that are applicable to subpart B of part 190. It reorganizes and revises much of current § 190.02, and incorporates some portions of current § 190.10.

a. Regulation § 190.03(a): Notices—Means of Providing

The Commission is adopting § 190.03(a) to set forth the means by which notices required under subpart B of part 190 are to be provided. Section 190.03(a)(1) is substantially similar to current § 190.10(a), but, in an effort to modernize part 190, the Commission is deleting the requirement that notices be given to it via overnight mail (*i.e.,* in hard copy). The Commission is retaining the requirement that all such notices be sent via electronic mail. The Commission believes that overnight hard copy delivery is unnecessary and that removing the requirement to send notices to the Commission via overnight mail will result in cost savings.

The Commission is adopting § 190.03(a)(2) to provide a generalized approach for giving notice to customers under part 190. In light of evolving technology, § 190.03(a)(2) replaces the specific procedures for providing notice to customers that appear in current § 190.02(b) with the requirement that the trustee must establish and follow procedures ''reasonably designed'' for giving notice to customers under subpart B of part 190. Such notice procedures should generally include the use of a website and customers' electronic addresses. In the Commission's view, this new approach provides trustees with the necessary flexibility to determine the best way to provide notice and is consistent with the manner in which bankruptcy trustees in recent FCM bankruptcy cases have provided notice to customers. The Commission also believes that adopting a generalized notice requirement in lieu of retaining more specific notice obligations (*e.g.,* newspaper publication) will result in both cost savings for the debtor's estate, and more efficient and effective notification of customers.

The Commission requested comment on the approach to the notice requirements set forth in proposed § 190.03(a). The Commission specifically asked whether the proposed changes would be helpful; would be likely to lead to unintended consequences; and how any unintended consequences could be mitigated. CME supported providing trustees with the flexibility, in consultation with the Commission, to establish appropriate procedures for giving notice to customers and moving away from outdated and impractical notice requirements. CME also agreed that the changes align with how trustees in recent FCM cases have communicated with the FCM's customers and are more customer-friendly.

[71] Section 6c of the CEA provides in relevant part that whenever it shall appear to the Commission that any person has engaged, is engaging, or *is about to engage* in any act or practice constituting a violation of any provision of this Act or any rule, regulation, or order thereunder the Commission may bring an action in the proper district court to enjoin such act or practice, or to enforce compliance with this Act (emphasis supplied). Section 6c also refers to an order appointing a temporary receiver to administer such restraining order and to perform such other duties as the court may consider appropriate. 7 U.S.C. 13a–1.

[72] *See* section II.A.2. (recommending that the Commission instead use ''funded net equity'' as the defined term in the § 190.01 definitions.)

b. Regulation § 190.03(b): Notices to the Commission and Designated Self-Regulatory Organizations

Section 190.03(b)(1) is derived from current § 190.02(a)(1), but includes revised notice requirements that are designed to ensure that the Commission and the relevant designated self-regulatory organization (''DSRO'') [73] will be aware of a voluntary or involuntary bankruptcy filing or SIPA application as soon as is practicable and to codify the practices observed in recent bankruptcy and SIPA cases.[74] First, § 190.03(b)(1) provides that, in the event of a voluntary bankruptcy filing, the commodity broker must notify the Commission and the appropriate DSRO as soon as practicable before, and in any event no later than, the time of filing. Second, § 190.03(b)(1) provides that, in the event of an involuntary bankruptcy filing or an application for a protective decree under SIPA,[75] the commodity broker must notify the Commission and the appropriate DSRO immediately upon the filing of such petition or application. The Commission notes that, as a practical matter, a decision to file for bankruptcy takes measurable time, as does the preparation of the necessary papers. In previous FCM voluntary bankruptcy filings, the commodity broker has provided the Commission and its DSRO with notice ahead of the bankruptcy filing. Section 190.03(b)(1) merely codifies the expectation that such advance notice should, in fact, occur to the extent practicable. Section 190.03(b)(1) allows the commodity broker to provide the relevant docket number of the bankruptcy or SIPA proceeding to the Commission and the DSRO ''as soon as known,'' in order to account for the fact that there may be a time lag between the filing of a proceeding and the assignment of a docket number.

Section 190.03(b)(2) sets forth the requirements for the provision of notice to the Commission of an intent to transfer or to apply to transfer open commodity contracts in accordance with section 764(b) of the Bankruptcy Code and relevant provisions of part 190. It is derived from current § 190.02(a)(2). While § 190.03(b)(2) retains the requirement that such notice be provided ''[a]s soon as possible,'' it removes the requirement that such notice be provided no later than three days after the order for relief. The Commission believes that the three-day deadline set forth in current § 190.02(a)(2) is likely in many cases to be too long, but may, in some cases, be too short.

The Commission expects that the bankruptcy trustee would begin working on transferring any open commodity contracts as soon as the trustee is appointed and that, by the end of three days following entry of the order for relief, any such transfers likely will be either completed, actively in process, or determined not to be possible. Indeed, the Commission expects that a DCO would, in most cases, be reluctant to hold a position open for more than three days following the entry of the order for relief unless a transfer is actively in process and imminent. Thus, while the Commission recognizes that the ''[a]s soon as possible'' language is somewhat vague, given past experience, the Commission views the current timeframe of three days after the entry of the order for relief as generally too long, and it is not clear what precise shorter period of time would be generally appropriate, given the uniqueness of each case. Under different circumstances, that is, where transfer arrangements cannot be made within three days after the order for relief, a specified deadline for notification may in fact be harmful, in that it could be interpreted to prohibit notification after the expiration of such deadline (and thus, impliedly prohibit the trustee from forming the intent to transfer after that time).

In the event of an FCM bankruptcy, the Commission anticipates that there will be frequent contact between the trustee, the relevant DSRO, any relevant clearing organization(s), and Commission staff. Thus, a specified deadline for such notification would not appear to be helpful. Section 190.03(b)(2) also clarifies that notification should be made with respect to a transfer of customer property.

The Commission requested comment on proposed § 190.03(b). Specifically, the Commission asked whether proposed § 190.03 would meet the objective of ensuring that the Commission and the relevant DSRO will be aware of a bankruptcy filing or SIPA proceeding as soon as is practicable. LCH expressed support for the requirement that FCMs notify DSROs, in addition to the CFTC, of involuntary bankruptcy filings. LCH also requested that the Commission consider ways in which this information could be quickly transmitted to the DCOs that may be impacted, given the interconnectedness of the derivatives market. While, as noted above, staff would be in contact with DCOs that might be impacted by a bankruptcy proceeding involving an FCM as a matter of supervisory practice, this practice does not need to be incorporated into regulation. Moreover, the Commission notes that many DCOs, including LCH, require as part of their own rules and procedures that their clearing members provide prompt notice of a bankruptcy filing affecting the clearing member.[76]

c. Regulation § 190.03(c): Notices to Customers; Treatment of Hedging Accounts and Treatment of Specifically Identifiable Property

The Commission is adopting § 190.03(c) to address notices to customers and the treatment of hedging accounts and specifically identifiable property.

Section 190.03(c)(1) requires the trustee to use all reasonable efforts to notify promptly any customer whose futures account, foreign futures account, or cleared swaps account includes specifically identifiable property, other than open commodity contracts, which has not been liquidated, that such property may be liquidated on and after the seventh day after the order for relief if the customer has not instructed the trustee in writing before the deadline specified in the notice to return such property pursuant to the terms for distribution of customer property contained in part 190. It also requires that the trustee's notice to customers with specifically identifiable property include, where applicable, a reference to substitute property.

Section 190.03(c)(1) is derived from current § 190.02(b)(1), but replaces the requirement that the trustee publish such notice to customers in a newspaper for two consecutive days prior to liquidating the specifically identifiable property with the requirement that the trustee notify customers in accordance with § 190.03(a)(2). This change is intended to provide the trustee with flexibility in notifying customers regarding specifically identifiable

[73] For further detail regarding SROs and DSROs *see generally* § 1.52.

[74] A voluntary case under a chapter of the Bankruptcy Code is commenced by the debtor by filing a petition under that chapter. Section 301(a) of the Bankruptcy Code, 11 U.S.C. 301(a). Under certain circumstances, creditors of a person may file an involuntary case against that person pursuant to section 303 of the Bankruptcy Code, 11 U.S.C. 303. In such cases, the order for relief will be granted only if the petition is not timely controverted or if the court makes specific findings. *Id.* There is no historical precedent for an involuntary petition in bankruptcy being filed against a commodity broker.

[75] A SIPA proceeding is commenced when the Securities Investors Protection Corporation (''SIPC'') files a petition for a protective order. *See generally* SIPA section 5, 15 U.S.C. 78eee.

[76] *See, e.g.,* LCH Ltd.: FCM Procedures of the Clearing House 1.6(b)(G) (''All FCM Clearing Members must provide the Clearing House in a prompt and timely manner with: . . . notice if the FCM Clearing Member becomes the subject of a bankruptcy petition.'').

property and to modernize part 190 to allow the trustee to provide notice to customers in a way that will maximize the number of customers reached. The timeframe in which the Commission would allow the trustee to commence liquidation of specifically identifiable property has been modified to reflect the revised notice requirements. Because § 190.03(c)(1) does not require newspaper publication of customer notice, the Commission is allowing the trustee to commence liquidation of specifically identifiable property on the seventh day after the order for relief (or such other date as specified by the trustee with the approval of the Commission or the court), so long as the trustee has used all reasonable efforts promptly to notify the customer under § 190.03(a)(2) and the customer has not instructed the trustee in writing to return such specifically identifiable property.

The Commission is adopting § 190.03(c)(2) to address how a bankruptcy trustee may treat open commodity contracts carried in hedging accounts. This regulation moves from the bespoke approach of current § 190.02(b)(2) to a categorical approach, in light of the practical difficulties of treating large numbers of customers with similar open contracts on a bespoke basis.[77] The Commission notes that recent commodity broker bankruptcies have involved thousands of customers, with as many as hundreds of thousands of commodity contracts. Trustees must make decisions as to how to handle such customers and contracts within days—in some cases, hours—after being appointed. Therefore, the Commission is giving the trustee the authority (*i.e.,* an option, but not an obligation) to treat open commodity contracts of public customers held in hedging accounts designated as such in the debtor's records as specifically identifiable property, after consulting with the Commission and when practical under the circumstances. To the extent the trustee exercises such authority, the trustee is required to notify each relevant public customer in accordance with § 190.03(a)(2). As proposed, § 190.03(c)(2) would have required the trustee, in all cases, to request that the customer provide instructions as to whether to transfer or liquidate the relevant open commodity contracts.[78] As discussed further below, in response to a comment, the Commission is modifying this proposal to address cases where, in the judgment of the trustee, the books and records of the debtor reveal a clear preference by the public customer with respect to transfer or liquidation of open commodity contracts.

Section 190.03(c)(2) also delineates certain information that the trustee must include in the notice. As proposed, the notice must inform the customer that (1) if the customer does not provide instructions in the prescribed manner and by the prescribed deadline, the customer's open commodity contracts will not be treated as specifically identifiable property; (2) any transfer of the open commodity contracts is subject to the terms for distribution contained in § 190.09(d)(2); (3) absent compliance with any terms imposed by the trustee or the court, the trustee may liquidate the open commodity contracts; and (4) providing instructions may not prevent the open commodity contracts from being liquidated. The Commission is making conforming changes to this portion of proposed § 190.03(c)(2) to reflect the modification referenced above. To the extent the trustee does not exercise its authority to treat public customer positions carried in a hedging account as specifically identifiable property, the trustee must endeavor to, as the baseline expectation, treat open commodity contracts of public customers carried in hedging accounts the same as other customer property and effect a transfer of such contracts to the extent possible.[79] The Commission is making these changes to reflect the policy preference to port *all* positions of public customers. Requiring a trustee to identify hedging accounts and provide hedging account holders the opportunity to keep their positions open may be a resource and time intensive process, which the Commission believes could interfere with the trustee's ability to take prudent and timely action to manage the debtor FCM's estate to protect all of the FCM's customers. The Commission believes that allowing the FCM to rely on representations made by customers during business-as-usual will alleviate this concern. In cases where it may be practical, the trustee may elect to provide special hedging account treatment.

The Commission is adopting § 190.03(c)(3) to make minor modifications to the notice of the commencement of an involuntary proceeding that the trustee may provide to customers prior to entry of an order for relief, and upon leave of the court. Such modifications include clarifying that such notice must be in accordance with the notice provisions set forth § 190.03(a)(2), amending certain terminology, and removing unnecessary references.

Section 190.03(c)(4) requires the bankruptcy trustee to notify customers that an order for relief has been entered and instruct customers to file a proof of customer claim. The regulation is derived from current § 190.02(b)(4), but adds that the notice must be provided in accordance with § 190.03(a)(2). Section 190.03(c)(4) replaces the term ''customer of record'' with the term ''customer,'' as ''customer of record'' is not a defined term in part 190 and all customers should receive notice that an order of relief has been entered. Section 190.03(c)(4) also provides that the trustee shall cause the proof of customer claim form to set forth the bar date for its filing consistent with the current § 190.03(a)(2).

The Commission requested comment on proposed § 190.03(c). It specifically asked whether the proposed changes to the notice requirements would be helpful; whether the discretion granted to the trustee concerning the treatment of hedging accounts as specifically identifiable property is appropriately tailored; whether the proposed revisions appeared likely to lead to unintended consequences; and how such consequences; if any, could be mitigated.

The Commission received three comments on proposed § 190.03. CME fully endorsed the policy preference that the trustee should use their best efforts to transfer all public customer positions and related customer property from the debtor FCM to one or more other FCMs. Accordingly, CME supported the provisions in § 190.03(c) that grant the trustee the discretion to not treat customer positions carried in hedge accounts as specifically identifiable property, unless the trustee determines that doing so would be practicable under the circumstances, following consultation with the Commission. CME asserted that this discretion will allow the trustee to devote their attention to transferring open positions of all public customers, along with their proportionate share of the customer property, in the aggregate.

[77] *See* major theme 7 in section I.B. above.

[78] The Commission is also making other changes that are intended to make it simpler for the trustee to identify hedging positions and allow an FCM to designate an account as a hedging account by relying on explicit customer representations that the account contains a hedging position. *See* § 1.41. This would simplify the existing requirement that FCMs provide a hedging instructions form when a customer first opens up a hedging account. For commodity contract accounts opened prior to the effective date of the part 190 revisions, the Commission is proposing that FCMs may rely on written hedging instructions received from the customer in accordance with current § 190.06(d). *See* § 1.41(c).

[79] *See* § 190.00(c)(4).

SIFMA AMG/MFA also generally agreed with § 190.03(c)(2) in that it grants to the trustee the authority (that is, the option but not the obligation) to treat open commodity contracts of public customers held in hedging accounts designated as such in the debtor's record as specifically identifiable property. SIFMA AMG/MFA stated that permitting the trustee this flexibility would serve the interest of customers as a whole by facilitating a more rapid transfer of customer positions and property. SIFMA AMG/MFA recommended, however, that the Commission explicitly clarify that § 190.03(c)(2) is not intended to affect the treatment of hedging accounts under part 39 of the Commission's regulations and that, to the extent reasonably practicable, the trustee's goal will be to maximize value to the public customer.[80] Additionally, in the context of the treatment of hedging accounts, SIFMA AMG/MFA recommended that, if the trustee exercises the authority as granted in this provision, the trustee should be first required to consult the instructions (regarding preferences with respect to transfer or liquidation of open commodity contracts) provided by a public customer to the debtor at the time of opening the relevant hedging account, and only if such instructions are missing or unclear should the trustee require such customer to provide it with written instructions as contemplated by proposed § 190.03(c)(2). SIFMA AMG/MFA noted that the notice sent by the trustee to the customer can still provide that existing or previously provided instructions may not prevent the open commodity contracts from being liquidated. SIFMA AMG/MFA asserted that adding this first step would further the goal of expediency.

The Commission agrees with the suggestion by SIFMA AMG/MFA that it is more efficient to endeavor to follow clear instructions previously provided rather than to request new instructions. Moreover, this approach mitigates the risk that a customer who has already made their preference patent will fail to reply to the request and thus be treated in a manner contrary to that previously expressed preference.

Accordingly, the Commission is amending and reorganizing § 190.03(c)(2) to implement that suggestion. Specifically, § 190.03(c)(2)(ii)(B) is being amended to provide, in pertinent part that: (1) Where, in the judgment of the trustee, the books and records of the debtor reveal a clear preference by a relevant public customer with respect to transfer or liquidation of open commodity contracts, the trustee shall endeavor, to the extent reasonably practicable, to comply with that preference; and (2) Where, in the judgment of the trustee, the books and records of the debtor do not reveal a clear preference by a relevant public customer with respect to transfer or liquidation of open commodity contracts, the trustee will request the customer to provide written instructions whether to transfer or liquidate such open commodity contracts. Such notice must specify the manner for providing such instructions and the deadline by which the customer must provide instructions.

Other conforming changes are being made to § 190.03(c)(2). With respect to SIFMA AMG/MFA's request that the Commission explicitly clarify that proposed § 190.03(c)(2) is not intended to affect the treatment of hedging accounts under part 39, the Commission notes that § 190.03(c)(2) governs the trustee's actions, and does not govern the actions a DCO may take under its default rules or otherwise.

ACLI recommended that the Commission amend proposed § 190.03(c)(2) to require a trustee to transfer a public customer's hedge positions where the customer has requested the transfer and met the required terms unless, in consultation with the Commission, it is determined that it would be unreasonable to transfer such positions. ACLI further recommended that the Commission add a threshold such as ''impossibility'' or ''exigent circumstances'' to limit a trustee's ability to liquidate a customer's hedge position in lieu of a requested transfer. ACLI asserted that the Commission's oversight should be specifically mandated. In response to ACLI's comment, the Commission notes that § 190.00(c)(4) sets forth a preference for the porting of *all* open commodity contract positions of public customers, along with all or a portion of such customers' account equity, and § 190.04(a)(1) instructs the trustee promptly to use its best efforts to effect a transfer of such positions and property in accordance with § 190.07(c) and (d) not later than seven calendar days after the order for relief. The discretion granted to the trustee in § 190.03(c)(2) is based on the reality that, in light of limited time and administrative resources, achieving porting to the maximum extent is fostered by treating customers on an omnibus, rather than an individualized, basis. For these reasons, the Commission declines to adopt ACLI's specific suggestions.

d. Regulation § 190.03(d): Notice of Court Filings

Section 190.03(d) addresses notices of court filings. It is derived from current § 190.10(f), but makes modernizing changes to the terminology and method of providing notice to the Commission. The Commission requested comment on proposed § 190.03(d). The Commission specifically asked whether the proposed revisions appeared likely to lead to unintended consequences, and, if so, how such consequences could be mitigated. The Commission did not receive any comments on proposed § 190.03(d).

e. Regulation § 190.03(e): Proof of Customer Claim

The Commission is adopting § 190.03(e) to require a trustee to request that customers provide information sufficient to determine a customer's claim in accordance with the regulations contained in part 190. Section 190.03(e) lists certain information that customers shall be requested to provide, to the extent reasonably practicable, but grants the trustee discretion to adapt the request to the facts of the particular case. Such discretion is being granted to the trustee in order to enable the trustee to tailor the proof of claim form to the information that is most appropriate in light of the specifics of the types of business that the debtor did (and did not do), the way in which such types of business were organized, and the available records of the debtor (as well as the reliability of those records). Section 190.03(e) is generally derived from current § 190.02(d), although certain items on the list of information to be requested of customers have been revised and reorganized to: *Inter alia,* improve clarity; tie the questions to definitions of terms in part 190; give the claimant an opportunity to provide a more complete picture of its claims; and provide its own view as to the value of such open positions, unliquidated securities or other unliquidated property in order to support its claim against the debtor.

The Commission requested comment on proposed § 190.03(e). Specifically, the Commission asked whether the proposed changes would be helpful; whether the discretion granted to the trustee was appropriately tailored; whether the proposed revisions appeared likely to lead to unintended consequences; and how such consequences, if any, could be mitigated. The Commission received one comment on proposed § 190.03(e). CME noted that the proposed regulation

[80] This last point is addressed with the addition of § 190.00(c)(3)(i)(C).

is a major improvement over the current regulation.

f. Regulation § 190.03(f): Proof of Claim Form

Regulation § 190.03(f) provides that a template proof of claim form is included as appendix A to part 190.[81] The Commission substantially revised the customer proof of claim form in order to streamline it and better map it to the information listed in § 190.03(e). The revised customer proof of claim form now includes, in each section, citations to the location in the text of § 190.03(e) where such information is listed.

Section 190.03(f)(1) provides that, to the extent there are no open commodity contracts that are being treated as specifically identifiable property, the bankruptcy trustee should modify the proof of claim form to delete any references to open commodity contracts as specifically identifiable property. For example, this would be the case if all open commodity contracts had been transferred or liquidated before the proof of claim form is sent. Section 190.03(f)(2) makes clear that the trustee has discretion as to whether to use the template proof of claim form, and that the proof of claim form should be modified to reflect the specific facts and circumstances of the case. The provisions of § 190.03(f), taken together, are meant to provide bankruptcy trustees with appropriate flexibility to determine the best and most efficient way to compose the customer proof of claim.

The Commission requested comment on proposed § 190.03(f). Specifically, the Commission asked whether the proposed changes to the treatment of the proof of customer claim form would be helpful; whether they would lead to unintended consequences; and how such consequences, if any, could be mitigated. The Commission also asked whether the discretion granted to the trustee was appropriately tailored and, if not, what changes should be made. CME commented that the proof of claim form had been improved and supported the flexibility provided to the trustee.

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.03 as proposed, with modifications to § 190.03(c)(2), as set forth above.

2. Regulation § 190.04: Operation of the Debtor's Estate—Customer Property

The Commission is adopting § 190.04 as proposed with modifications, as set forth below to address the collection of margin and variation settlement, as well as the liquidation and valuation of positions. The Commission is adopting § 190.04 to clarify and update portions of §§ 190.02, 190.03, and 190.04.

The Commission requested comment with respect to all aspects of proposed § 190.04 including: Whether the revisions create any unintended conflicts with customer protection regulations set forth in parts 1, 22, and 30; how any such conflicts may be resolved; whether there are any proposed clarification changes that are likely to create unintended consequences; and, if so, how might those be avoided or mitigated.

a. Regulation § 190.04(a): Transfers

The Commission is adopting § 190.04(a) as proposed. Section 190.04(a) largely retains the current provisions in current § 190.02(e) regarding transfers for customers in a bankruptcy proceeding. It also retains the policy preference[82] that the trustee should use its best efforts to transfer open commodity contracts and property held by the failed FCM for or on behalf of its public customers to one or more solvent FCMs.[83] Regulation § 190.04(a)(1) provides that the trustee ''shall promptly'' use its best efforts to effect such transfers, while current § 190.02(e)(1) states that the trustee must ''must immediately'' do so. This revision signals that the trustee must take action to transfer open commodity contracts as soon as practicable, while avoiding potential pressure of the term ''immediately'' in light of the challenges presented in an FCM bankruptcy. Regulation § 190.04(a)(2) replaces the term ''equity'' with ''property'' to clarify that the trustee should endeavor to transfer all types of property that the commodity broker is holding on behalf of customers; the transfer is not limited to equity. The Commission is also adding the word ''public'' before ''customers'' to clarify that the transfers discussed in § 190.04(a)(1) relate to the open commodity contracts and property of the debtor's public customers.[84]

The Commission is adopting § 190.04(a)(2), as derived from § 190.02(e)(2), to remove the liquidation-only trading limitations on an FCM that is subject to an involuntary bankruptcy petition unless otherwise directed by the Commission, by any applicable self-regulatory organization, or by court. The Commission is instead adopting limitations on the business of an FCM in bankruptcy in § 190.04(g) to more generally address involuntary proceedings.[85]

The Commission is adopting § 190.04(a)(2), as derived from current § 190.02(e)(2), to provide that if such commodity broker demonstrates to the Commission within a specified period of time that it is in compliance with the Commission's segregation and financial requirements on the filing date, the Commission may determine to allow the commodity broker to continue in business. The Commission is retaining this provision because any requirement to transfer customers is properly addressed pursuant to § 1.17(a)(4), which deals with FCMs that do not meet minimum financial requirements. The Commission is of the view that an FCM that does meet such requirements should not be compelled to cease business and transfer its customers absent an appropriate finding by a court or the Commission.

In addition, similar to § 190.04(a)(1), as discussed above, the Commission is replacing the term ''equity'' with ''property'' to clarify that the transfers discussed in § 190.04(a)(2) are for all types of property that the commodity broker is holding on behalf of customers, rather than limited to only equity. Also, the Commission is adding the word ''public'' before ''customers'' to clarify in § 190.04(a)(2) that the transfers discussed in § 190.04(a)(1) relate to the open commodity contracts and property of the debtor's public customers.

The Commission did not receive any comments on this aspect of the Proposal. Accordingly, for the reasons stated above, the Commission is adopting § 190.04(a) as proposed.

b. Regulation § 190.04(b): Treatment of Open Commodity Contracts

The Commission is adopting § 190.04(b) as proposed to clarify and update the provisions in current § 190.02(g)(1), which allow a trustee to make ''variation and maintenance margin payments'' on behalf of the

[81] Appendix A is discussed in section II.D below.

[82] The Commission discussed the rationale for this policy preference in the discussion of § 190.00(c)(4). *See* section II.A.1. *See also* ABA Cover Note at 14 (recommending explicitly identifying in § 190.04(a) a clear policy that the trustee should use best efforts to transfer open commodity contracts and property held by the failed FCM for or on behalf of its public customers to one or more solvent FCMs).

[83] The Commission is also adopting cross-references in § 190.04(a) to other provisions within proposed part 190 that discuss transfers of customer property.

[84] The Commission is adopting the same change—addition of the word ''public'' before ''customers''—to § 190.04(a)(2), as discussed below.

[85] The Commission is deleting the reference to ''liquidation'' in § 190.02(e)(4) accordingly since the limitation to trading for liquidation only is being deleted from § 190.04(a)(2).

debtor FCM's customers. The Commission is adopting § 190.04(b) to be generally consistent with the current regulation but with a number of substantive changes.

First, the Commission is adopting § 190.04(b) to permit the trustee to make margin payments pending *transfer or* liquidation; not just pending liquidation as required by current § 190.02(g)(1). The amendment is consistent with the Commission's longstanding policy for the trustee to endeavor to *transfer* open commodity contracts. The trustee has *two* paths for the treatment of such contracts: Transfer and, if transfer is not possible, liquidation.

Second, the Commission is adopting § 190.04(b)(1) to delete the phrase ''required to be liquidated under paragraph (f)(1) of this section'' in current § 190.02(g)(1) to eliminate a complete prohibition against paying margin on open contracts. While holding contracts open may or may not be practicable given the particular circumstances of the bankruptcy, a complete prohibition against paying margin on such open contracts would undermine the point of having the possibility to hold those contracts open. Accordingly, the Commission is deleting the phrase ''required to be liquidated under paragraph (f)(1) of this section'' and thus will instead apply more broadly to any open commodity contracts.

The Commission is also adopting several technical amendments. Third, the Commission is replacing the phrase ''variation and maintenance margin payments'' with ''payments of initial margin and variation settlement'' which, in the Commission's view, more accurately describes the types of payments being reflected in this provision. Fourth, the Commission is replacing the phrase ''to a commodity broker'' with ''to a clearing organization, commodity broker, foreign clearing organization or foreign futures intermediary'' to account for the various types of entities to which a margin payment described in this provision may be made. Lastly, the Commission is replacing the phrase ''specifically identifiable to a particular customer'' with ''specifically identifiable property of a particular customer'' in order to be consistent with the definitions in part 190, which includes as a defined term ''specifically identifiable property.''

The Commission is adopting § 190.04(b)(1)(i), as derived from current § 190.02(g)(1)(i), to prevent the trustee from making any payments on behalf of any commodity contract account that is in deficit, to the extent within the trustee's control. The Commission is including the phrase ''to the extent within the trustee's control'' to recognize that certain commodity contract accounts may be held on an omnibus basis (*i.e.,* on behalf of several customers), so to the extent the trustee is making a margin payment on behalf of the omnibus account, it may be out of the trustee's control to identify and only pay on behalf of those underlying customer accounts (within the omnibus account) that are not in deficit. The Commission is including a proviso to note that § 190.04(b)(1)(i) shall not be construed to prevent a clearing organization, foreign clearing organization, FCM, or foreign futures intermediary from exercising its rights to the extent permitted under applicable law. This proviso is intended to remove any doubt that the right of these ''upstream'' entities to use collateral posted by the FCM on an omnibus basis is not affected by the prohibition on making margin payments on behalf of accounts that are in deficit.

The Commission is adopting § 190.04(b)(1)(ii) as a new provision to prohibit the trustee from making an upstream margin payment with respect to a specific customer account that would exceed the funded balance of that account. This restriction is consistent with the *pro rata* distribution principle discussed in § 190.00(c)(5), in that any payment in excess of a customer's funded balance would be to the detriment of other customers.

The Commission is adopting some non-substantive clarifications in § 190.04(b)(1)(iii), as derived from current § 190.02(g)(1)(ii), to retain the limitation that the trustee may not make payments on behalf of non-public customers of the debtor from funds that are segregated for the benefit of public customers.

The Commission is adopting § 190.04(b)(1)(iv)–(v) to clarify and expand upon current § 190.02(g)(1)(iii),[86] to require that margin is used consistent with the requirements of section 4d of the CEA.[87] First, the Commission is adopting § 190.04(b)(1)(iv) to provide that, if the trustee receives payments from a customer in response to a margin call, then to the extent within the trustee's control,[88] the trustee must use such payments to make margin payments for the open commodity contract positions of such customer. Second, the Commission is adopting § 190.04(b)(1)(v) to provide that the trustee may not use payments received from one public customer to meet the margin (or any other) obligations of any other customer. Given the restriction in paragraph (b)(1)(v), the Commission believes it may in some cases be impracticable for a trustee to follow paragraph (b)(1)(iv). In such a situation, therefore the trustee would hold onto the funds received in response to a margin payment and such funds would be credited to the account of the customer that made the payment.[89]

Regulation § 190.04(b)(1)(vi) builds upon current § 190.02(g)(1)(iv), which provides that no payments need to be made to restore initial margin, thus noting that such payments are not required but implicitly allowed to be made. Revised § 190.04(b)(1)(vi) explains in this in more detail and provides more comprehensive guidance to the trustee about when such payments may be made. Specifically, § 190.04(b)(1)(vi) provides that, in the event that the funds segregated for the benefit of public customers in a particular account class exceed the aggregate net equity claims for all customers in that account class, the trustee is permitted to use such funds to meet the margin obligations for any public customer in such account class whose account is undermargined, but not in deficit, and sets conditions around such use.

Regulation § 190.04(b)(2) updates current § 190.02(g)(2), which concerns margin calls made by trustee with respect to undermargined accounts of public customers. The Commission is removing the current requirement in § 190.02(g)(2) that the trustee issue margin calls, by replacing the term ''must issue margin calls'' with ''may issue a margin call,'' in light of the possibility that the trustee will determine it impracticable or inefficient to do so. Current § 190.02(g)(2), which sets up a retail-level analysis on issuing mandatory margin calls based on the funded balance of the account, is based on a model of the FCM continuing in business. Revised § 190.04(b)(d) recognizes that an FCM in bankruptcy will be operated in crisis mode, and may be pending wholesale transfer or liquidation of open positions.[90] Therefore, the Commission is allowing for the possibility that the trustee may issue margin calls. The specification of

[86] Current § 190.02(g)(1)(iii) provides that the trustee must make margin payments if payments of margin are received from customers after bankruptcy in response to margin calls.

[87] *See* 7 U.S.C. 6d.

[88] The phrase ''to the extent within the trustee's control'' recognizes the reality that certain accounts are held on an omnibus basis. *See* discussion of § 190.04(b)(1)(i) above.

[89] *See* § 190.08(c)(1)(ii).

[90] *See generally* major theme 7 discussed in section I.B. above.

highly prescriptive conditions for issuing such calls is no longer appropriate, given the Commission whether or not to make a margin call is now based on the trustee's discretion.

Regulation § 190.04(b)(3), as derived from current § 190.02(g)(3) with updated cross-references, retains the important concept that margin payments made by a customer in response to a trustee's margin call are fully credited to the customer's funded balance. As these post-petition payments made by the customer are fully counted toward the customer's funded net equity claims under § 190.04(b)(3), they are not subject to *pro rata* distribution (in contrast to the treatment of the debtor commodity broker's pre-petition obligations to customers).

Regulation § 190.04(b)(4) is derived from a combination of current §§ 190.03(b)(1) and (2) and 190.04(e)(4), and addresses the trustee's obligation to liquidate certain open commodity contracts; in particular, those in deficit and those where the customer has failed to promptly meet a margin call. During business-as-usual, an FCM is required to cover, at all times, any customer accounts in deficit (*i.e.,* those with debit balances) with its own capital.[91] The FCM is also required to cover with its own capital any undermargined amounts in customer accounts each day by no later than the Residual Interest Deadline.[92] These ongoing requirements are intended to protect other customers with positive account balances.

An FCM in bankruptcy will generally not have capital available to protect other customers by covering these obligations; rather, any loss suffered by customers whose accounts are in deficit will be at the risk of those other customers.[93] The Commission intends for § 190.04(b)(4) to mitigate the risk to those other customers by directing the trustee to liquidate such accounts.

In light of the importance of mitigating this fellow-customer risk, § 190.04(b)(4), in contrast to many of the other proposed changes to part 190, curtails the trustee's discretion. Specifically, § 190.04(b)(4), as derived from current § 190.03(b)(1) and (2), provides that the trustee shall, as soon as practicable, liquidate all open commodity contract accounts in any commodity contract account (i) that is in deficit; (ii) for which any mark-to-market calculation would result in a deficit; or (iii) for which the customer fails to meet a margin call made by the trustee within a reasonable time. Pursuant to current § 190.03(b)(1), a trustee must liquidate open commodity contracts if any payment of margin would result in a deficit in the account in which they are held.[94] Revised § 190.04(b)(4) adds a requirement to liquidate all open commodity contracts in any commodity contract account that is in deficit. The existing language applies to an account that is on the threshold of deficit; the Commission is revising the language to clarify that the provision also applies to an account that is already in deficit. Moreover, the change from ''payment of margin'' to ''mark-to-market'' calculations addresses the case where the trustee is aware, based on mark-to-market calculations, that the account is in deficit. In order to protect other customers more effectively, the trustee should begin the liquidation process immediately upon gaining that awareness, rather than delaying until the time when a margin payment is due.

Regulation § 190.04(b)(4) also provides that, absent exigent circumstances or unless otherwise provided, a reasonable time for meeting margin calls made by a trustee shall be one hour or such greater period not to exceed one business day, as determined by the trustee.[95] This language is largely reflective of current § 190.04(e)(4), but adds the concept of ''exigent circumstances'' as a new exception to the general and long-established rule that a minimum of one hour is sufficient notice for a trustee to liquidate an undermargined account. The Commission intends this revision to provide the trustee with the discretion to deem a period of less than one hour as sufficient notice to liquidate an undermargined account if the ''exigent circumstances'' so require.

The Commission is deleting current § 190.03(b)(3) to permit the trustee to liquidate open commodity contracts where the trustee has received no customer instructions with respect to such contracts by the sixth calendar day following the entry of the order for relief. The Commission is adopting this change as part of a model where the trustee receives and complies with instructions from individual customers to a model—that reflects actual practice in commodity broker bankruptcies in recent decades—where the trustee transfers as many open commodity contracts as possible.[96]

The Commission is adopting new § 190.04(b)(5) to provide guidance to the trustee in assigning liquidating positions[97] to the debtor FCM's customers when only a portion of the open commodity contracts in an omnibus account are liquidated. The new guidance is designed to protect the customer account as a whole, in light of the fact that any losses which cause a customer account to go into deficit are, as discussed in connection with § 190.04(b)(4), at the risk of other customers. To mitigate the risk of such losses, § 190.04(b)(5) establishes a preference, subject to the trustee's exercise of reasonable business judgment, for assigning liquidating transactions to individual customer accounts in a risk-reducing manner. Specifically, the trustee should endeavor to assign such liquidating transactions first, in a risk-reducing manner, to commodity contract accounts that *are* in deficit; second, in a risk-reducing manner, to commodity contract accounts that are undermargined;[98] and finally to liquidate any remaining open commodity contracts. Where there are multiple accounts in any of these groups, the trustee is instructed to, as practicable, to allocate such liquidating transactions *pro rata.* The term ''risk-reducing manner'' is measured by the margin methodology and parameters

[91] *See, e.g.,* §§ 1.22(i)(4), 1.23(a)(2).

[92] *See, e.g.,* § 1.22(c)(3).

[93] While the trustee may seek to recover any debit balance from a customer, *see* § 190.09(a)(1)(ii)(E), § 190.04(b)(4) proceeds from the conservative assumption that such efforts will be unsuccessful.

[94] An account is in deficit if the balance is negative (*i.e.,* the customer owes the debtor instead of the reverse). An account can be undermargined but not in deficit (if the balance is positive, but less than the amount of required margin). For example, a customer may have a margin requirement of $100 and an equity balance of $80. Such customer is undermargined by $20, but is not in deficit, because the liquidation value of the commodity contracts is positive.

[95] *See Morgan Stanley & Co. Inc.* v. *Peak Ridge Master SPC Ltd.,* 930 F.Supp.2d 532, 539–540 (S.D.N.Y. 2013)(Morgan Stanley, in its business discretion, determined Peak Ridge's account had assumed overly risky positions, necessitating an increase in the margin requirement and giving Peak Ridge a limited amount of time to bring the account into compliance. ''Courts have held that as little as one hour is sufficient notice under similar circumstances.''). *See also Capital Options Invs., Inc.* v. *Goldberg Bros. Commodities, Inc.,* 958 F.2d 186, 190 (7th Cir. 1992) (''One-hour notice to post additional margin . . . is reasonable where a contract specifically provides for margin calls on options at any time and without notice.''); *Prudential–Bache Sec., Inc.* v. *Stricklin,* 890 F.2d 704, 706–07 (4th Cir. 1989) (rejecting a claim that 24-hour notice, which the broker normally gave to customers, was necessary before broker could liquidate an under-margined account and upholding notice of one hour as in accordance with the customer agreement); *Modern Settings, Inc.* v. *Prudential–Bache Sec. Inc.,* 936 F.2d 640, 645 (2d Cir. 1991) (upholding a provision of a customer agreement allowing Defendant-broker to liquidate an under-margined account without notice).

[96] *Cf.* major theme 7 in section I.B above.

[97] A liquidating position or transaction is one that offsets a position held by the debtor, in whole or in part. Thus, if the debtor has three long March '21 corn contracts, then three (or two, or one) short March '21 corn contracts would be a liquidating transaction.

[98] And thus are next at risk of going into deficit.

followed by the DCO at which such contracts are cleared. Specifically, where allocating a transaction to a particular customer account reduces the margin requirement for that account, such an allocation is ''risk-reducing.''

The Commission requested comment on whether the revised approach in proposed § 190.04(b)(4) regarding the required liquidation of certain open commodity contract accounts would provide the trustee with an appropriate amount of discretion and is practicable; whether customers, who believe they did not benefit from those decisions, would likely challenge the trustee's choices given the level of discretion provided; whether such challenges could materially slow down the distribution of customer property relative to a context where the trustee was granted less discretion; and whether the proposed approach in § 190.04(b)(5) for the assignment of liquidating positions to debtor FCM customers in a ''risk-reducing manner'' is practicable when only a portion of the open commodity contracts in an omnibus account are liquidated.

SIFMA AMG/MFA supported most of the substantive amendments in subpart B of part 190 and believed such changes are generally helpful for purposes of reducing risk for market participants and allowing the trustee to act as efficiently as possible. SIFMA AMG/MFA approved of the inclusion of transfers in addition to liquidation, and the clarification to apply the proposed regulation to any open commodity contracts in proposed § 190.04(b).

CME agreed with the general concept of providing the trustee for a debtor FCM with significant flexibility to operate the FCM and favored any provision that encourages the transfer of customer positions and property and continuation of margin payments on behalf of the debtor FCM pending transfer or liquidation of positions. ICE suggested that the Commission should clarify that any trustee discretion proposed in § 190.04 for managing a failed FCM should be subject to the obligations of the defaulting clearing member and the rights of the DCO as provided by the DCO's rules.

ICE supported the Commission's proposal in § 190.04(b)(1) to clarify that a trustee may make variation margin payments on open contracts, pending their liquidation or transfer. ICI agreed with proposed § 190.04(b)(1)(ii), which prohibits a trustee from making any margin payments with respect to a customer account that would exceed the funded balance for that account.

ICI and Vanguard agreed with the preservation of the existing requirement within proposed § 190.04(b)(3) that the trustee fully credit the customer's funded balance for any margin payment made by a customer in response to trustee's margin call. Vanguard noted that any customer concerns as to the ability to fully recover margin would surely de-incentivize customers to post additional margin in critical times.

SIFMA AMG/MFA generally supported proposed § 190.04(b), but had concerns regarding the calculation of whether a customer is undermargined, and the timing of margin calls. SIFMA AMG/MFA questioned whether the trustee would be able to calculate accurately whether a customer is undermargined, particularly if the FCM's books and records do not accurately reflect margin amounts transferred by such customer to the FCM. SIFMA AMG/MFA requested that the Commission clarify how the trustee will try to protect customers from being called upon to provide duplicate margin amounts. SIFMA AMG/MFA recommended that the Commission amend proposed § 190.04(b) to provide customers with the opportunity to demonstrate that a margin payment was made even if the FCM's books and records do not yet reflect its receipt.

SIFMA AMG/MFA disagreed that absent exigent circumstances, a reasonable time for meeting margin calls made by the trustee shall be deemed to be one hour, or such greater period not to exceed one business day, as the trustee may determine in its sole discretion. SIFMA AMG/MFA stated that the necessary assets may not be readily available to customers and urged the Commission to require the trustee to defer to the margin call timings present in the applicable underlying agreements entered into by the customer pursuant to § 39.13 when determining a reasonable time for meeting margin calls. SIFMA AMG/MFA opined that this is a reasonable level of deference, since the trustee will have access to these agreements, which are already in place with the Commission regulations, and will allow for customers to satisfy margin calls without causing needless market panic.

ICI and Vanguard agreed with proposed § 190.04(b)(4), which would require the trustee to liquidate any customer account in deficit. ICI supported maintaining the existing requirement that the trustee promptly liquidate any customer account when a customer fails to meet a margin call in a reasonable time or where any payment of margin from the account would result in an account deficit. ICI agreed with the proposal that a debtor FCM will generally not have capital available to protect other customers by covering account deficits, so any loss suffered by customers whose accounts are in deficit will be at risk of those other non-defaulting customers. As a result, ICI noted that it is vital that the trustee be required to swiftly crystallize, and therefore cap the losses resulting from, such deficits by promptly liquidating accounts in deficit or for which a customer has failed to meet a margin call. ICI cautioned that if the accounts were allowed to remain open, additional losses on the delinquent customers' transactions would be borne by the FCM's non-defaulting customers, which could dissuade non-defaulting customers from continuing to meet their margin obligations post-petition.

OCC was concerned that the proposed definition of ''undermargined'' in §§ 190.01 and 190.04(b)(2) and (4) could create a situation in which a trustee offers one public customer an opportunity to deposit additional margin that ultimately prevents an account deficit and resulting liquidation of the public customer's account, but exercises discretion not to offer another public customer the same opportunity to deposit margin and subsequently must liquidate the account because it is in deficit, notwithstanding the customer's willingness to post additional margin to keep its positions open. OCC was concerned that the use of such trustee discretion would expose a trustee to challenge by a public customer that asserts, though it was similarly situated to a public customer that was given this opportunity, it was not given this opportunity and received inequitable treatment.

In response to SIFMA AMG/MFA's comment, the Commission notes that, in the case of an FCM in bankruptcy, any deficit in the account of one customer may come at the expense of distributions to other customers. As ICI noted, the normal buffer of the capital of an FCM in continuing operation cannot be relied upon. Accordingly, where a trustee believes, based on the records and limited time available to them, that a customer is undermargined, it is important that they act on that belief in order to protect other customers. Similarly, in a case where a customer fails to meet a margin call within what the trustee determines, in their sole discretion, is a reasonable time, the trustee should liquidate the contracts of that customer to protect other customers. Forcing the trustee to defer to margin call timings in pre-bankruptcy agreements, or to give the customer an opportunity to demonstrate that a margin payment was made, as requested by the comment, may increase: (1) The risk that such customer would default; (2) the risk that delaying liquidation of such a customer's positions increases the potential for and likelihood that they would do so with a debit balance; and (3) the risk that the size of that debit balance would increase as a result of that delay, thereby reducing the funded balances of other customers. The Commission is of the view that timeframes that may have been acceptable during business-as-usual cannot bind the trustee in addressing the context of an FCM in bankruptcy, because any post-petition losses incurred by a customer will be at the cost of other customers (without the normal buffer of the capital of a going-concern FCM). Moreover, the Commission agrees with the view championed by ICI and Vanguard that the trustee should be required to swiftly crystallize and therefore cap the losses resulting from deficit balances by promptly liquidating accounts in deficit and those for which a customer has failed to meet a margin call. OCC's concerns about treating customers equitably *inter se* are understandable, but, in the Commission's view, ensuring complete equity may not be practicable. A trustee must make decisions within a severely limited timeframe in a situation that is likely to be chaotic and with information that is limited and may be imperfect. In these circumstances, the Commission is of the view that it is appropriate to defer to the trustee's discretion to make the best decisions they can under the circumstances. Accordingly, the Commission believes that, where a trustee makes in good faith decisions with regard to margin and liquidation of accounts, that are, in retrospect, inequitable, the Commission's regulations should discourage challenges to such a decision (and, if such a challenge is made, should reduce the likelihood that it is successful).

While the trustee retains discretion, as specified in, *inter alia,* proposed § 190.04, to manage the affairs of the debtor FCM, the Commission can confirm, as requested by ICE, that a DCO of which that FCM is a member retains its rights to act under its rules.[99]

SIFMA AMG/MFA recommended that the Commission amend proposed § 190.04(b) to clearly state that, to the extent gains-based haircutting has been utilized by a DCO in respect of customer positions, the trustee should give customers of an FCM credit for any gains that were haircut during such gains-based haircutting. With respect to this suggestion, the Commission notes that, where a DCO at which a debtor FCM is a member applies gains-based haircutting under that DCO's rules, the measure of the claim of a customer whose account at the debtor FCM contains contracts cleared on that DCO will be based on the customer agreement between that customer and the debtor FCM. If, outside of the FCM's bankruptcy and pursuant to that customer agreement, the customer's gains would have been reduced by *X*% or $*Y,* then the amount of the customer's claim in bankruptcy would be adjusted accordingly.[100] Accordingly, the Commission does not accept that suggestion.

ICI and Vanguard agreed with proposed § 190.04(b)(5) which prohibits a trustee from making margin payments that would exceed the customer's funded account balance or transfer a customer's transactions or property and thereby increase the exposure of other customers. Vanguard supported addressing situations where the trustee could allow certain customers to avoid the core customer protection of *pro rata* treatment at the expense of other customers.

Accordingly, after consideration of the comments, and for the reasons stated above, § 190.04(b) will be adopted as proposed.

c. Regulation § 190.04(c): Contracts Moving Into Delivery

The Commission is adopting § 190.04(c), as proposed, to direct the trustee to use its best efforts to avoid delivery obligations concerning contracts held through the debtor FCM by transferring or liquidating such contracts before they move into delivery position. The Commission is adopting § 190.04(c) based on its analog in current § 190.03(b)(5) and is incorporating a portion of current § 190.02(f)(1)(ii). Current § 190.03(b)(5) instructs the trustee to liquidate promptly, and in an orderly manner, commodity contracts that are not settled in cash (implicitly, those that settle via physical delivery of a commodity) where the contract would remain open beyond the earlier of (i) the last day of trading or (ii) the first day on which notice of delivery may be tendered—that is, where the contract would move into delivery position. The Commission intends § 190.04(c) to have the same purpose as its predecessors, but uses more explicit language regarding physical delivery to refer to ''any open commodity contract that settles upon expiration or exercise via the making or taking of delivery of a commodity,'' and that is moving into the delivery position. The Commission also intends § 190.04(c) to expand current § 190.03(b)(5), with the incorporation of some aspects of current § 190.02(f)(1)(ii), to include an explicit reference to how options on commodities move into delivery position.

CME supported proposed § 190.04(c), which directs the trustee to use their best efforts to liquidate open physical delivery commodity contracts that have not been transferred before the contracts move into a delivery position as CME believed this would avoid unnecessary disruptions to the delivery process by customers that did not intend to participate in making or taking delivery. ICI supported adding provisions that clarify the standards applicable to an FCM's liquidation of a debtor FCM's transactions and the way a trustee must assign liquidating transactions in the context of a partial liquidation.

According, after consideration of the comments, and for the reasons stated above, the Commission is adopting § 190.04(c) as proposed.

d. Regulation § 190.04(d): Liquidation or Offset

The Commission is adopting § 190.04(d) as proposed with modifications, as set forth below. Regulation § 190.04(d), as derived from current §§ 190.02(f) and 190.04(d), sets forth the categories of commodity contracts and other property held by or for the account of a debtor that must be liquidated by the trustee in the market or by book entry offset, promptly, and in an orderly manner.[101]

Importantly, the Commission is retaining the requirement, present in the header language to current § 190.02(f), that the trustee must effect such

[99] *See, e.g.,* § 190.04(b)(1) (while trustee shall, to the extent within its control, not make payments on behalf of an account in deficit, this shall not be construed to prevent a clearing organization from exercising its rights to the extent permitted under applicable law).

[100] Moreover, there are other reasons to forego an approach that would reverse the effects of gains-based haircutting. As discussed in more detail in section II.C.7 below, there is a limited amount of customer property available. Any increase in some customers claims (and thus their distributions) due to the reversal of gains-based haircutting would thus come at the expense of a reduced share of that limited customer property, and thus reduced distributions, to other customers.

[101] The Commission is also adopting three non-substantive changes in the header language to proposed § 190.04(d) from that in current § 190.02(f): (1) The addition of the phrase ''except as otherwise set forth in this paragraph (d)'' to account for any exceptions that are included in the paragraphs under the header language; (2) the addition of cross-references to proposed § 190.04(e) when discussing liquidation, as that provision contains instructions on how to effect liquidation; and (3) the deletion of the phrase ''subject to limit moves and to applicable procedures under the Bankruptcy Code.''

liquidation ''in an orderly manner.'' Regulation § 190.04(d) recognizes that any factor which, in the trustee's discretion, makes it imprudent to liquidate a position at a particular point in time would contribute to the trustee's judgment as to what constitutes liquidation ''in an orderly manner.''

Section 190.04(d)(1), as derived from § 190.02(f)(1), requires that all open commodity contracts must be liquidated, subject to two exceptions: (1) Commodity contracts that are specifically identifiable property and are subject to customer instructions to transfer as provided in proposed § 190.03(c)(2); and (2) open commodity contract positions that are in a delivery position.[102] In the former case (specifically identifiable property), the Commission is adopting § 190.04(d)(1) to revise the language of current § 190.02(f)(1)(ii) to add references to the provisions of § 190.03(c)(2) (concerning the trustee's option to treat hedging accounts as specifically identifiable property) and § 190.09(d)(2) (concerning the payments that customers on whose behalf specifically identifiable commodity contracts will be transferred must make to ensure that they do not receive property in excess of their *pro rata* share).[103] The latter exception, for open commodity contract positions that are in a delivery position is new, and provides that such positions should be treated in accordance with § 190.06, which concerns delivery.[104]

Regulation § 190.04(d)(2) describes when specifically identifiable property, other than open commodity contracts or physical delivery property, must be liquidated. The Commission derived § 190.04(d)(2) from current § 190.02(f)(2), with a number of revisions.

First, the provision applies to specifically identifiable property, other than open commodity contracts *or physical delivery property,* while the current regulation applies only to specifically identifiable property other than open commodity contracts. The Commission intends for this change to provide the trustee with discretion to avoid interfering with the physical delivery process.

Second, while the current regulation would require liquidation of such property if the fair market value of the property drops below 90% of its value on the date of the entry of the order for relief,[105] § 190.04(d)(2)(i) changes that standard to 75% of the fair market value, in order to provide greater discretion to the trustee to forego or postpone liquidation in appropriate cases.

Third, revised § 190.04(d)(2)(ii) adds an additional condition that will require liquidation where failure to liquidate the specifically identifiable property may result in a deficit balance in the applicable customer account, which corresponds to the general policy of liquidating any accounts that are in deficit.

Lastly, § 190.04(d)(2)(iii), which is similar to current § 190.02(f)(2)(ii), includes updated cross-references to the provisions in proposed part 190 that discuss the return of specifically identifiable property.

Regulation § 190.04(d)(3) is a new provision that codifies the Commission's longstanding policies of *pro rata* distribution and equitable treatment of customers in bankruptcy, as described in § 190.00(c)(5) above, as applied to letters of credit posted as margin.[106] Accordingly, customers who post letters of credit as margin will be treated no differently than other customers and thus would suffer the same *pro rata* loss.

The implementation of this policy in current § 190.08(a)(1)(i)(E) was challenged in an adversary proceeding in the *MF Global* bankruptcy; [107] the codification of this policy in §§ 190.00(c)(5) (clarifying policy), 190.04(d)(3) (treatment in bankruptcy), and 1.43 (treatment during business-as-usual) are intended to implement the policy effectively and to forestall any future challenge.

Regulation § 190.04(d)(3) provides that the trustee may request that such a customer deliver substitute customer property with respect to any letter of credit received, acquired or held to margin, guarantee, secure, purchase, or sell a commodity contract. This applies whether the letter of credit is held by the trustee on behalf of the debtor's estate, a DCO, a foreign broker, or foreign clearing organization, and whether it is held on a pass-through or other basis. The amount of the substitute customer property to be posted may be less than the full-face amount of the letter of credit, in the trustee's discretion, if such lesser amount is sufficient to ensure *pro rata* treatment consistent with proposed §§ 190.08 and 190.09. If required, the trustee may require the customer to post property equal to the full-face amount of the letter of credit to ensure *pro rata* treatment. Regulation § 190.04(d)(3)(i) provides that, if such a customer fails to provide substitute customer property within a reasonable time specified by the trustee, the trustee may draw upon the full amount of the letter of credit or any portion thereof.

Regulation § 190.04(d)(3)(ii) addresses cases where a letter of credit received, acquired or held to margin, guarantee, secure, purchase, or sell a commodity contract is not fully drawn upon. The trustee is instructed to treat any portion of the letter of credit that is not fully drawn upon as having been distributed to the customer. However, the amount treated as having been distributed will be reduced by the value of any substitute customer property delivered by the customer to the trustee. For example, if the face amount of the letter of credit is $1,000,000, the customer delivers $250,000 in substitute customer property, and no portion of the letter of credit is drawn upon, then the trustee will treat the customer as having received a distribution of $750,000. In order to avoid an effective transfer of value, due to an expiration of the letter of credit on or after the date of the order for relief, to the customer who posted the letter of credit, this calculation will not be changed due to such an expiration.

Regulation § 190.04(d)(3)(iii) confirms that any proceeds of a letter of credit drawn by the trustee, or substitute customer property posted by a customer, shall be considered customer property in the account class applicable to the original letter of credit.

Regulation § 190.04(d)(4), as derived from current § 190.02(f)(3), provides for the liquidation of all other property not required to be transferred or returned pursuant to customer instructions and which has not been liquidated. Regulation § 190.04(d)(4) excepts from the liquidation requirement any ''physical delivery property held for delivery in accordance with the provision of'' § 190.06, in order to avoid interfering with the physical delivery process.

[102] Regulation § 190.04(d)(1) deletes the reference in current § 190.02(f)(1)(i) to dealer option contracts since such term is no longer used.

[103] The Commission is incorporating part of current § 190.02(f)(1)(ii) into § 190.04(c), and therefore that will not appear in § 190.04(d)(1).

[104] As noted in section II.A.1 above in the discussion of § 190.00(c)(6), a delivery default could have a disruptive effect on the cash market for the commodity and could adversely impact the parties to the transaction.

[105] *See* current § 190.02(f)(2)(i).

[106] *See, e.g.,* 48 FR 8716, 8718–19 (March 1, 1983) (Commission intends to assure that customers using a letter of credit to meet original margin obligations would be treated no differently than customers depositing other forms of non-cash margin or customers with excess cash margin deposits. If letters of credit are treated differently than Treasury bills or other non-cash deposits, there would be a substantial incentive to use and accept such letters of credit as margin as they would be a means of avoiding the *pro rata* distribution of margin funds, contrary to the intent of the Bankruptcy Code (11 U.S.C. 766).)

[107] *See ConocoPhillips* v. *Giddens,* No. 12 Civ. 6014, 2012 WL 4757866 (S.D.N.Y. 2012).

Several commenters supported proposed § 190.04(d)(3). SIFMA AMG/MFA, ICI, and Vanguard strongly supported proposed § 190.04(d)(3) because it permits a trustee to demand substitute margin so that other customers' margin need not be accessed to meet any shortfall occasioned by the inability to draw on the letters of credit. SIFMA AMG/MFA noted that the addition of proposed § 190.04(d)(3) would ensure that customers using letters of credit to meet original margin obligations will be treated no differently from customers depositing other forms of non-cash margin or excess cash margin deposits. SIFMA AMG/MFA ''agree[d] that most letters of credit currently in use by the industry follow the Joint Audit Committee forms [and believed] that the impact of these additional requirements concerning letters of credit will result in clearer guidance for more equitable treatment of customers within each account class.'' However, SIFMA AMG/MFA ''questione[d] the one-year transition period and urge[d] the Commission to shorten it in the interest of investor protection. For example, if an FCM were to enter bankruptcy proceedings during the one-year transition period,'' SIFMA AMG/MFA inquired as to how the letters of credit would be treated in such proceeding.

OCC also supported proposed § 190.04(d)(3) and the *pro rata* loss policy objective. OCC stated that it ''expects that it would generally, to the extent permitted by OCC's rules and default management arrangements, draw on a defaulted member's letter of credit collateral as soon as practicable after a declaration of default. OCC would attempt to do so, whether or not it has immediately identified a need to draw on a letter of credit to meet the defaulted member's settlement obligations, as a protective action in anticipation of any potential increase in the credit risk associated with the letter of credit. In such cases, a trustee would obtain any remaining proceeds from the drawn-down letter to distribute *pro rata* among the FCM's customers as appropriate.''

However, several commenters including CME, FIA, and CMC believed the policy reasons for the trustee's general right to demand substitute collateral do not exist with respect in the narrow context of a delivery letter of credit.

CME agreed ''that a letter of credit posted to secure obligations under open commodity contracts (whether drawn upon or not) must be deemed as part of the customer's property, in addition to any additional collateral posted by the customer, for purposes of distribution calculations. [CME agreed] that it is prudent to make clear that the trustee in either an FCM or DCO bankruptcy can draw upon posted letters of credit.'' CME supported ''granting the trustee the power to require a customer to deliver substitute customer property to the estate and allowing the trustee to draw on the letter of credit if the customer does not post additional collateral, provided that those conditions apply only to letters of credit letter that are received, acquired, or held to guarantee or secure a customer's obligations under open commodity contracts, and do not apply to delivery letters of credit.''

With respect to a delivery letter of credit posted as collateral to secure the customer's obligation to pay for delivery of a commodity it will receive, CME and CMC believed it was ''critically important that the letter of credit be available to draw upon if the customer defaults or is expected to default on its obligation to pay the seller.'' However, CME, CMC, and FIA recommended that the Commission revise proposed § 190.04(d)(3) to confirm that the authority of the trustee to require a customer that posts a letter of credit to deliver substitute customer property does not extend to letters of credit posted to a delivery account.

CME argued that ''[c]ustomers routinely post letters of credit in connection with delivery obligations under certain physical delivery futures contracts held to maturity.'' CME noted that this is the case for deliveries under certain oil futures listed on the New York Mercantile Exchange. ''The buyers are required to post collateral for the full payment amount owed because actual delivery is effected via physical transfer of oil and thus is typically completed 30 days or so after buyers and sellers are matched for bilateral delivery obligations. Given the substantial dollar amounts involved, often hundreds of millions, letters of credit are often posted as collateral.'' CMC emphasized that ''unlike other situations, a delivery [letter of credit] simply serves as collateral for delivery of a futures contract after expiry but before delivery is taken and while the seller still has possession of the commodity for delivery.'' CME stated that ''[t]he value available to CME under such a letter of credit is wholly independent from the solvency of an FCM, unlike a letter of credit posted as performance bond, which decays when utilized to meet margin or variation calls post-FCM bankruptcy.'' CME posited that the delivery letter of credit does not pose the same issues that the Commission encountered in the *MF Global* bankruptcy. FIA argued that ''[a] purchaser that takes delivery under a commodity contract frequently is not required to take delivery for a significant period of time after the purchaser and seller have been matched. In these circumstances, the purchaser may be required to post a letter of credit as security for full payment when delivery is made.''

CME, CMC, and FIA warned that a trustee's decision to request substitute collateral of cash or cash equivalents for a delivery letter of credit or risk having the letter of credit drawn down prior to the time that delivery is made would create a sudden and unexpected liquidity need for the delivery participant and introduce unnecessary strain into physical and derivatives markets. The commenters were concerned that because the parties' obligations under the delivery account arise from a commodity account, a trustee's authority under proposed § 190.04(d)(3) could be interpreted to apply to letters of credit held in a delivery account. Accordingly, CME and CMC recommended ''that the Commission limit or eliminate the trustee's powers to request that a market participant substitute other forms of collateral for a delivery letter of credit upon which the DCO is a beneficiary.'' Specifically, CME and FIA recommended that the Commission revise proposed § 190.04(d)(3) to exclude delivery letters of credit, *i.e.,* letters of credit posted by buyers to guarantee their payment for commodities that they are contractually obligated to purchase under an expired futures or exercised commodity option contract.

CME also requested clarity in the context of § 190.06 ''that when a customer posts a delivery letter of credit directly with the DCO or with its delivery counterparty, and not with or through the FCM, the letter of credit is outside the delivery account class, *i.e.,* it does not constitute cash delivery property (or property of the debtor's estate), and the provisions in other parts of the proposed revisions regarding treatment of letters of credit posted with or through the debtor FCM do not apply.''

The Commission notes that, despite the comments of CME, CMC, and FIA, there are reasons to forego excluding delivery letters of credit as a class from the application of § 190.04(d)(3), and to adopt § 190.04(d)(3) as proposed, as supported by ICI, SIFMA AMG/MFA, and Vanguard: If, at the end of the bankruptcy proceeding, there are shortfalls in customer property in the cash delivery account class, those shortfalls will necessarily be borne by public customers. If public customers posting letters of credit (including in the delivery account) are shielded from such losses, they will be borne in greater proportion by other public customers. That result would be inconsistent with the Commission's longstanding policy, embodied in section 766(h) of the Bankruptcy Code, to treat all customers on a *pro rata* basis.[108]

However, the concerns raised by commenters regarding sudden and unexpected liquidity needs are important ones. They are important both in the context of delivery letters of credit, as discussed by some commenters, and more broadly as well.[109] The Commission agrees that these concerns can and should be mitigated. Specifically, the trustee has discretion in managing this process with respect to letters of credit, and should exercise that discretion with the goal of achieving *pro rata* treatment among customers in a manner that mitigates, to the extent practicable, the adverse effects upon customers that have posted letters of credit.

First, with regard to timing, the commenters expressed concern that requests for substitute property would cause ''sudden'' liquidity needs. Regulation § 190.04(d)(3)(i) states that the trustee may draw upon the letter of credit if the customer fails to provide substitute customer property within a reasonable time specified by the trustee. If the expiry date of the letter of credit is not imminent, the Commission expects that a ''reasonable time'' would be sufficiently long to enable the customer to mitigate liquidity concerns (consistent with the trustee's plans to make distributions). If the expiry date of the letter of credit *is* imminent, and the customer can and does arrange to have that expiry date extended, the parties could work in the context of that extended expiry date. However, if the expiry date is imminent, and cannot be extended, then the trustee will need to take promptly whatever steps are, in their discretion, necessary to ensure *pro rata* treatment among customers.

Second, with regard to the amount requested, § 190.04(d)(3) provides that the trustee may request that a customer deliver substitute customer property with respect to a letter of credit, and that the amount of the request may equal the full face amount of the letter of credit *or any portion thereof, to the extent required or may be required, in the trustee's discretion to ensure pro rata treatment among customer claims within each account class,* consistent with §§ 190.08 and 190.09. Thus, the amount of the substitute customer property requested (or, if substitute customer property is not provided, the amount of the letter of credit drawn upon (if partial draws are permitted)) should be proportionate to the amount required or may be required, in the trustee's discretion, to ensure *pro rata* treatment among customer claims. If the amount of the shortfall in the relevant account class (whether cash delivery property or otherwise) is estimated to be a small percentage, the amount of substitute customer property requested would also be a small percentage (subject to the trustee adding an appropriate buffer for later corrections in estimates, and taking into account any need to use the letter of credit as ongoing performance bond for the customer's obligations).

To re-enforce these concepts, the Commission is adding a new § 190.04(d)(3)(iv), which provides that the trustee shall, in exercising their discretion with regard to addressing letters of credit, including as to the timing and amount of a request for substitute customer property, endeavor to mitigate, to the extent practicable, the adverse effects upon customers that have posted letters of credit in a manner that achieves *pro rata* treatment among customer claims. The Commission intends that this new paragraph will confirm to trustees that they should steer their discretion in the specified manner, and will provide assurance to customers that have posted letters of credit that the trustees will exercise their discretion in that manner. The Commission believes that this provision will appropriately address concerns regarding the manner in which the trustee ensures that customers that have posted letters of credit are treated economically in the same manner as customers who have posted other forms of collateral

Moreover, in the context of § 190.06, CME requested that the Commission confirm that ''when a customer posts a delivery letter of credit directly with the DCO or with its delivery counterparty, and not with or through the FCM, the letter of credit is outside the delivery account class, *i.e.,* it does not constitute cash delivery property (or property of the debtor's estate), and the provisions in other parts of the proposed revisions regarding treatment of letters of credit posted with or through the debtor FCM do not apply.''

For example, the Commission understands that upon expiry of certain deliverable contracts and assignment of delivery obligation, the long/buyer of the contract must post collateral to the DCO against its final payment obligation on the delivery. In certain cases, collateral in the form of a delivery letter of credit collateral is posted by the customer directly to the DCO. The delivery letters of credit in these cases are subject to uniform terms that name the DCO as the sole beneficiary on the instrument. These delivery letters of credit do not create an obligation of or to a customer's FCM as they are posted directly to the DCO and the FCM is not a named beneficiary on the instrument.[110]

In the context of a delivery letter of credit that is posted directly with the DCO or with the delivery counterparty, rather than with or through the FCM, and for which the FCM is not a named beneficiary, the Commission confirms that the letter of credit is outside the delivery account class, *i.e.,* it does not constitute cash delivery property (or property of the debtor's estate), and the provisions in other parts of the proposed revisions regarding treatment of letters of credit posted with or through the debtor FCM do not apply.[111]

The Commission believes that this clarification, in combination with the new provision directing the trustee's discretion in the context of letters of credit, will ameliorate the commenters concerns regarding delivery letters of credit.

The foregoing applies to the trustee. DCOs remain free to exercise any of the rights and powers in their rules vis-à-vis their clearing members, in particular with respect to risk management, limited only by requirements within the Commission's regulations.[112] However, in this context, the Commission would encourage DCOs holding letters of credit posted by customers of FCMs in bankruptcy to exercise their rights under such letters of credit in a

[108] Pursuant to § 190.08(c)(1)(ii), the customer's funded balance includes 100% of margin posted after the order for relief. Accordingly, this principle would not apply to a delivery letter of credit posted after the order for relief (unless the letter of credit was delivered in substitution for a pre-bankruptcy letter of credit).

[109] Moreover, and for the avoidance of doubt, as delivery is simply a stage in the life of a commodity contract, § 190.04(d)(3) applies to letters of credit in connection with delivery obligations under a commodity contract.

[110] Similarly, CMC's concerns focus on ''a delivery LOC upon which the DCO is beneficiary.''

[111] The Commission was not requested to opine on whether this approach vis-à-vis letters of credit is permissible outside of the context of the delivery account class, and expresses no view on that question.

[112] *See, e.g.,* § 190.04(e) (Rules providing for liquidation other than on the open market shall be designed to achieve, to the extent feasible under market conditions at the time of liquidation, a process for liquidating open commodity contracts that results in competitive pricing.)

measured fashion, in order to achieve risk management goals fully but in a manner that mitigates, to the extent practicable, adverse effects upon customers that have posted letters of credit.[113]

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.04(d) as proposed, with the addition of new § 190.04(d)(3)(iv) as set forth above.

e. Regulation § 190.04(e): Liquidation of Open Commodity Contracts

The Commission is adopting § 190.04(e) as proposed to provide details regarding the liquidation and valuation of open positions.[114] Paragraph (e) is derived from current § 190.04(d), subject to a number of changes.

The Commission is adopting § 190.04(e)(1)(i), as derived from current § 190.04(d)(1)(ii), to describe the process of liquidating open commodity contracts when the debtor is a member of a clearing organization. Regulation § 190.04(e)(1)(i), like its predecessor, emphasizes the goal of competitive pricing to the extent feasible under market conditions at the time of liquidation. Treatment under the CEA of clearing organization rules has evolved from a pre-approval regime to a primarily self-certification regime. The Commission is of the view that the various processes set forth in part 40 of the Commission's regulations (including self-certifications under § 40.6, voluntary submission for rule approval under § 40.5, and Commission review of certain rules of systemically important DCOs under § 40.10) are sufficient, and that a separate rule approval process for rules regarding settlement price in the context of a bankruptcy is no longer necessary. The Commission is accordingly adopting § 190.04(e)(1)(i) to delete the requirement contained in current § 190.04(d)(1)(i) that a clearing organization must obtain approval pursuant to section 5c(c) of the CEA for its rules regarding liquidation of open commodity contracts.

Section 190.04(e)(1)(i) also adds a provision regarding open commodity contracts that are futures or options on futures that were established on or subject to the rules of a foreign board of trade and cleared by the debtor as a member of a foreign clearing organization, providing that such contracts shall by liquidated pursuant to the rules of the foreign clearing organization or foreign board of trade or, in the absence of such rules, in the manner the trustee deems appropriate. This the new provision is analogous to the existing provision but would extend to cases where the debtor FCM is a member of a foreign clearing organization.

Section 190.04(e)(1)(ii) provides instructions to the trustee regarding the liquidation of open commodity contracts where the debtor is not a member of a DCO or foreign clearing organization, but instead clears through one or more accounts established with an FCM or a foreign futures intermediary. In such a case, § 190.04(e)(1)(ii) provides that the trustee shall use commercially reasonable efforts to liquidate the open commodity contracts to achieve competitive pricing, to the extent feasible under market conditions at the time of liquidation. The Commission is adding this provision to account for those circumstances where the trustee must liquidate open commodity contracts for a debtor that is not a clearing member.

As with § 190.04(e)(1)(i), the Commission is adopting § 190.04(e)(2) to delete the rule approval requirement, for the same reasons stated above. Regulation § 190.04(e)(2) is derived from current § 190.04(d)(1)(ii) which requires a trustee or clearing organization to apply to the Commission for permission to liquidate open commodity contracts by book entry. In such a case, the settlement price for such commodity contracts shall be determined by the clearing organization in accordance with its rules, which shall be designed to establish, to the extent feasible under market conditions at the time of liquidation, such settlement prices in a competitive manner.

The Commission is adopting § 190.04(e)(3) to recognize that an FCM or foreign futures intermediary through which a debtor FCM carries open commodity contracts will generally have enforceable contractual rights to liquidate such commodity contracts. New § 190.04(e)(3) confirms that the upstream intermediary may exercise such rights. However, the liquidating FCM or foreign futures intermediary shall use commercially reasonable efforts to liquidate the open commodity contracts to achieve competitive pricing, to the extent feasible under market conditions at the time of liquidation and subject to any rules or orders of the relevant clearing organization, foreign clearing organization, DCM, SEF or foreign board of trade governing its liquidation of such open commodity contracts.

If the liquidating FCM or foreign futures intermediary fails to do so, the trustee may seek damages reflecting the difference in price(s) resulting from such failure. However, such damages would be the trustee's sole available remedy as the regulation makes clear that ''[i]n no event shall any such liquidation be voided.''

The Commission is adopting § 190.04(e)(4)(i) and (ii) based on current § 190.04(d)(2) and (3), respectively, with some minor non-substantive language changes and updated cross-references.

The Commission requested comment in particular on the treatment of letters of credit in bankruptcy, as set forth in proposed § 190.04(e). The Commission did not receive any comments on this aspect of the Proposal. Accordingly, for the reasons stated above, the Commission is adopting § 190.04(e) as proposed.

f. Regulation § 190.04(f): Long Option Contracts

The Commission is adopting § 190.04(f) as proposed to contain only minor non-substantive changes from the current § 190.04(e)(5), including (1) a cross-reference to the liquidation provisions in proposed § 190.04(d) and (e), and (2) a clarification that the provision is referring to commodity contracts that are long option contracts, rather than to long option contracts more generally.

The Commission did not receive any comments on this aspect of the Proposal. Accordingly, for the reasons stated above, the Commission is adopting § 190.04(f) as proposed.

3. Regulation § 190.05: Operation of the Debtor's Estate—General

The Commission is adopting § 190.05 to revise parts of current § 190.04 and add new provisions to (1) require a trustee to use all reasonable efforts to continue to issue account statements for customer accounts holding open commodity contracts or other property and (2) clarify the trustee's obligation with respect to residual interest. The Commission requested comment with respect to all aspects of proposed § 190.05.

The Commission is adopting § 190.05(a) to amend the requirement in current § 190.04(a) that the trustee ''shall'' comply with all provisions of

[113] In this connection, the Commission notes that OCC Rule 1104(a)(ii) permits OCC, if the issuer of a letter of credit agrees to extend the irrevocability of its commitment thereunder in a manner satisfactory to OCC, to ''demand only such amounts as it may from time to time deem necessary to meet anticipated disbursements.''

[114] The Commission is amending § 190.08(d) to also clarify the process by which customer positions and other customer property are valued for purposes of determining the amount of a customer's claim.

the CEA and of the regulations thereunder as if it were the debtor, to state that the trustee ''shall use reasonable efforts to comply'' with all provisions of the CEA and of the regulations thereunder as if it were the debtor. This change is intended to provide the trustee with some flexibility in making decisions in an emergency bankruptcy situation, subject to the requirements of the Bankruptcy Code. Given that an FCM bankruptcy will likely be a fast-paced situation requiring the trustee to make decisions with little time for consideration, the Commission recognizes that there may be circumstances under which strict compliance with the CEA and the regulations thereunder may not be practicable. The Commission did not receive any comments on proposed § 190.05(a).[115]

The Commission is adopting § 190.05(b) to address the computation of funded balances. It is derived from, and makes several revisions to, § 190.04(b). The Commission's objective in making such revisions is to provide the bankruptcy trustee with the latitude to act reasonably given the circumstances with which the trustee is confronted, recognizing that information may be more reliable and/or accurate in some insolvency situations than in others and permitting an approach that, to an appropriate extent, favors cost effectiveness and promptness over precision.[116] First, whereas current § 190.04(b) provides that a trustee ''must'' compute a daily funded balance for the relevant customer accounts, § 190.05(b) requires the trustee to use ''reasonable efforts'' to make such computations. Such computations are required to be ''as accurate as reasonably practicable under the circumstances, including the reliability and availability of information.'' Second, § 190.05(b) increases the scope of customer accounts for which the bankruptcy trustee is obligated to compute a funded balance from accounts that contain open commodity contracts to accounts that contain open commodity contracts or other property. In the Commission's view, there is no reason to exclude customer accounts that contain only property (the value of which may change) from the scope of those for which bankruptcy trustees must compute a daily funded balance. Third, § 190.05(b) revises the length of time that the trustee is obligated to compute the funded balance of customer accounts from ''until the final liquidation date'' to until the open commodity contracts and other property in the account have been transferred or liquidated. This change ties the computation requirement to each specific account, such that a bankruptcy trustee is not required to continue to compute the funded balance of customer accounts that do not contain any open commodity contracts or other property. Lastly, the specific deadline by which the computation must be completed is being removed. The Commission does not believe that the deadline in current § 190.04(b) (by noon the next business day) is crucial in a bankruptcy context (as it is with respect to an FCM conducting ongoing daily business).[117] Such computation would, however, inherently need to be accomplished prior to performing any action where knowledge of funded balances is essential, such as transfers of accounts or property.

The Commission received one comment regarding proposed § 190.05(b). CME agreed that allowing the trustee to compute the funded balance for customers' accounts before transferring or liquidating customer positions or property using ''reasonable efforts'' to be ''as accurate as reasonably practicable under the circumstances, including the reliability and availability of information'' ''should allow the trustee to act more promptly to transfer the positions of public customers and their *pro rata* share of the customer property than if the trustee were held to a strict standard of precision in calculating funded balances before it could undertake such transfers.'' This is consistent with the Commission's view. The Commission is adopting § 190.05(c)(1) to amend the record retention requirements in current § 190.04(c) to be more comprehensive. Section 190.05(c)(1) expands the referenced records from ''computations required by this [p]art'' to ''records required under this chapter to be maintained by the debtor, including records of the computations required by this part.'' To enable the trustee to mitigate the expenses of record retention, however, it reduces the time that records are required to be retained from ''the greater of the period required by § 1.31 of this chapter or for a period of one year after the close of the bankruptcy proceeding for which they were compiled'' to ''until such time as the debtor's case is closed.'' Section 190.05(c)(2) simplifies the corresponding portion of current § 190.04(c)(2) by omitting the requirement that the records required in § 190.05(c)(1) be available to the Court and parties in interest. The requirement that such records be available to the Commission and the United States Department of Justice is being retained. A court generally will not itself look at records, and any parties in interest should have access to records under the discovery provisions of the Federal Rules of Bankruptcy Procedure and the Federal Rules of Civil Procedure, as applicable. The Commission did not receive any comments on proposed § 190.05(c).

The Commission is adopting new § 190.05(d) to facilitate the ability of customers of the bankrupt FCM with open commodity contracts or property to keep track of such open commodity contracts or property even during insolvency, and promptly to make them aware of the specifics of the liquidation or transfer of such contracts or property. Section 190.05(d) requires the trustee to use all reasonable efforts to continue to issue account statements with respect to any customer for whose account open commodity contracts or other property is held that has not been liquidated or transferred. Section 190.05(d) also requires the trustee to issue an account statement reflecting any liquidation or transfer that has taken place with respect to a customer account promptly after such liquidation or transfer has occurred.

The Commission sought comment on the practicability of the proposed requirements regarding the issuance of account statements. ICI commented in support of the account statement requirements.

The Commission is adopting § 190.05(e)(1) to amend the requirement in current § 190.04(e)(2) that a trustee must obtain court approval to make disbursements to customers, to specifically carve out transfers of customer property made in accordance with § 190.07. The Commission is making this change to reflect the policy preference to transfer as many public customer positions as practicable in the event of an FCM insolvency.[118] The Commission notes, however, that this

[115] To the extent that ICI's comment raising concerns about trustee discretion applies here, the Commission notes that the addition of § 190.00(c)(3)(i)(C), which directs the trustee to use their discretion with the overarching goal of protecting public customers, should mitigate that concern.

[116] *See* major theme 7 discussed in section I.B above.

[117] *See, e.g.,* § 1.32(d).

[118] The Commission notes that current § 190.08(d) provides for the return of specifically identifiable property other than commodity contracts under certain circumstances (namely, where the customer makes good any *pro rata* loss related to that property) without court approval; however, the Commission is deleting this provision in favor of allowing transfers without court approval for the reasons stated above.

carve out does not detract from the trustee's ability to, in their discretion, nonetheless seek and obtain court approval for certain transfers of property. The Commission recognizes that there is an inherent tension between distributing to public customers as much customer property as possible from the debtor's estate, as quickly as possible, and ensuring accuracy in distribution, and believes that § 190.05(e)(1) strikes the right balance between these competing objectives.[119]

Section 190.05(e)(2) addresses how a bankruptcy trustee may invest the proceeds [120] from the liquidation of open commodity contracts and specifically identifiable property, and other customer property. It is derived from, and retains much of, current § 190.04(e)(3), but it expands the provision permitting the bankruptcy trustee to ''invest any customer equity in accounts which remain open in accordance with § 190.03'' to permit the investment of ''any other customer property.'' It continues to limit the permissible investments to obligations of, or fully guaranteed by, the United States, and to limit the location of permissible depositories to those located in the United States or its territories or possessions. The Commission did not receive any comments on proposed § 190.05(e).

The Commission is adopting new § 190.05(f) to require a bankruptcy trustee to apply the residual interest provisions contained in § 1.11 ''in a manner appropriate to the context of their responsibilities as a bankruptcy trustee'' and ''in light of the existence of a surplus or deficit in customer property available to pay customer claims.'' The purpose of the residual interest provisions is to have the FCM maintain a sufficient buffer in segregated funds ''to reasonably ensure that the [FCM] . . . remains in compliance with the segregated funds requirements at all times.'' [121] The Commission requested comment with respect to all aspects of proposed § 190.05. Specifically, the Commission sought comment on the practicability and appropriateness of proposed § 190.05(f).

The Commission received supportive comments from CME, SIFMA AMG/MFA, ICI, and Vanguard. CME supported adding clarity that the trustee should use reasonable efforts to operate the debtor FCM's estate in compliance with the CEA and CFTC regulations governing FCMs, including to apply the residual interest provisions in § 1.11, in a manner appropriate to the context of their responsibilities and in light of the existence of a surplus or deficit in customer property available to pay customer claims. ICI and Vanguard supported the clarification in proposed § 190.05(f) that an FCM's residual interest is to be applied to public customer claims. Vanguard noted its belief that ''FCM residual interest is a valuable buffer to insulate FCM customers from the risk of delayed or failed margin transfers from other customers.'' Vanguard was ''pleased that the Commission has confirmed that, while residual interest is fronted by FCMs, it must be used to support customers through an FCM insolvency,'' noting that its ''purpose is to enhance core customer protections.'' SIFMA AMG/MFA also believed that ''the proposed use of residual interest as contemplated by proposed §§ 190.05(f) and 190.09 is appropriate,'' and agreed with the Commission that ''the residual interest provisions contained in § 1.11 remain important.''

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.05 as proposed.

4. Regulation § 190.06: Making and Taking Delivery Under Commodity Contracts

The Commission is adopting § 190.06 as proposed. The Commission is adopting § 190.06 to provide more specificity regarding making and taking deliveries on commodity contracts in the context of an FCM bankruptcy and to reflect current delivery practices. Section 190.06 is derived from current § 190.05, but implements new concepts (with respect to delivery practices, intangible commodities, and separation of physical and cash delivery property), as discussed further below.

Generally, open positions may enter a delivery position where the parties incur bilateral contractual delivery obligations.[122] It is important to address deliveries to avoid disruption to the cash market for the commodity and to avoid adverse consequences to parties that may be relying on delivery taking place in connection with their business operations.

The delivery provisions in the current regulations largely reflect the delivery practices at the time current part 190 was adopted in 1983. At that time, delivery was effected largely by tendering paper warehouse receipts or certificates. In contrast, most deliverable title documents today are held and transferred in electronic form, typically with the clearing organization serving as the central depository for such instruments. Under the terms of some contracts (such as oil or gas futures) the party with the contractual obligation to make delivery will physically transfer a tangible commodity to meet its obligations. In other cases, intangible commodities may be delivered, including virtual currencies. As noted previously, in the definitions section (§ 190.01), the Commission is dividing the delivery account class into physical delivery and cash delivery account subclasses to recognize the differing issues that apply to physical delivery property versus cash delivery property. The Commission is also recognizing that, consistent with current practice, physical deliveries [123] may be effected in different types of accounts.[124] For example, when an FCM has a role in facilitating delivery, deliveries may occur via title transfer in a futures account, foreign futures account, cleared swaps account, delivery account, or, if the commodity is a security, in a securities account. [125]

Section 190.06(a) applies to commodity contracts that settle upon expiration or exercise by making or taking delivery of physical delivery property, if such commodity contracts are in a delivery position on the filing date or the trustee is unable to liquidate such commodity contracts in accordance with § 190.04(c) to prevent them from moving into a delivery position.[126] The Commission is

[119] The concept of prioritizing cost effectiveness and promptness over precision is discussed in detail in major theme 7 in section I.B above and in overarching concept three in the cost-benefit considerations, section III.A.2.iii below.

[120] Section 190.05(e)(2) uses the term ''proceeds'' rather than the term ''equity,'' which is used in current § 190.04(e)(3). This change in wording is not meant to be a substantive.

[121] Section 1.11(e)(3)(i)(D).

[122] The timing of the entry of the order for relief in a subchapter IV proceeding relative to when physical delivery contracts move into a delivery positions will generally influence whether a delivery issue may arise. Additionally, during business as usual, market participants typically offset contracts before incurring delivery obligations.

[123] Current § 190.05 applies to the delivery of a physical commodity, or of documents of title to physical commodities. Section 190.06 applies to any type of commodity that is subject to delivery, whether tangible or intangible. This is captured in the definition of physical property. Given the different ways in which delivery may take place, physical delivery property is not limited to property that an FCM holds for or on behalf of a customer in a delivery account. For a discussion of those different ways, *see* the third and fourth categories under the definition of physical delivery property in § 190.01 in section II.A.2 above.

[124] *See also* § 1.42.

[125] *See also* § 1.42.

[126] As discussed above, § 190.04(c) directs the trustee to use its best efforts to avoid delivery obligations concerning contracts held through the

Continued

adopting § 190.06(a)(2) to address delivery made or taken on behalf of a customer outside of the administration of the debtor's estate, (*i.e.,* directly between the debtor's customer and the delivery counterparty assigned by the clearing organization). It replaces current § 190.05(b). Current § 190.05(b) requires a DCO, DCM, or SEF to enact rules that permit parties to make or take delivery under a commodity contract outside the debtor's estate, through substitution of the customer for the commodity broker. The Commission believes that deliveries should occur in this manner only where feasible. Deliveries may not always happen in this manner, as customers largely rely on their FCMs to hold physical delivery property on their behalf in electronic form.[127]

Section 190.06(a)(2)(i) [128] directs the trustee to use ''reasonable efforts'' to allow a customer to deliver physical delivery property that is held directly by the customer in settlement of a commodity contract, and to allow payment in exchange for such delivery, to occur outside the debtor's estate, where the rules of the exchange or clearing organization prescribe a process for delivery that allows delivery to be fulfilled either (A) in the ordinary course by the customer, (B) by substitution of the customer for the commodity broker, or (C) through agreement of the buyer and seller to alternative delivery procedures. In adopting a ''reasonable efforts'' standard rather than (as in current § 190.05(a)(1)) ''best efforts,'' the Commission is recognizing that, in the event that the trustee is unable to transfer or earlier liquidate the positions, delivery involves a significant degree of bespoke administration. Moreover, requiring the trustee's ''best efforts'' for delivery might require the trustee to spend an inordinate amount of time focusing on the needs of a few customers and detract from the trustee's ability to manage the short term challenges of the administration of the estate in the days immediately following the filing date.

Section 190.06(a)(2)(ii) addresses the circumstance where, while the customer makes physical delivery in satisfaction of a commodity contract using property that is outside the administration of the estate of the debtor, the customer nonetheless has property held in connection with that contract at the debtor (*i.e.,* collateral posted in connection with that contract pre-petition). Consistent with current § 190.05(b)(2), § 190.06(a)(2)(ii) provides that the property held at the debtor becomes part of the customer's claim and can only be distributed *pro rata,* despite the customer fulfilling the delivery obligation outside the administration of the debtor's estate.

Section 190.06(a)(3) applies when it is not practicable to effect delivery outside the estate. Section 190.06(a)(3) clarifies that which was implied, but was not addressed, in current § 190.05(c)(1)–(2), by providing additional details for when delivery is made or taken within the debtor's estate. It contains provisions for the trustee to deliver physical or cash delivery property on a customer's behalf, or return such property to the customer so that the customer may fulfill its delivery obligation. The regulation also includes restrictions designed to assure that a customer does not receive (or otherwise benefit from) a distribution of customer property (or other use of such property that benefits the customer) that exceeds the customer's *pro rata* share of the relevant customer property pool.

The Commission is adopting new § 190.06(a)(4) to recognize that delivery may need to be made in a securities account if an open commodity contract held in a futures account, foreign futures account, or cleared swaps account requires the delivery of securities, and property from any of these accounts is transferred to the securities account for the purpose of effecting delivery. The value of the property transferred to the securities account must be limited to the customer's funded balance for a commodity contract account, and only to the extent that funded balance exceeds (*i.e.,* the surplus over) the customer's minimum margin requirements for that account. Such a transfer may not be made if the customer is undermargined or has a deficit balance in any other commodity contract accounts.

Section 190.06(a)(5), as proposed, addressed deliveries made or taken on behalf of ''a house account of the debtor.'' It was derived from current § 190.05(c)(3), with some clarifying wording. Consistent with the suggestion from the ABA Subcommittee, as discussed in section II.A.2 above, the Commission is deleting in this final rule the definition of house account as it applies to FCMs. The reference in the provision as proposed to ''a house account of the debtor'' is being replaced in the final rule with a reference to ''the debtor's own account or the account of any non-public customer of the debtor.'' No substantive change vis-à-vis either the current regulation or the regulation as proposed is intended.

The Commission is adopting new § 190.06(b) to divide the delivery account class into separate physical delivery and cash delivery account subclasses, for purposes of *pro rata* distributions to customers in the delivery account class on their net equity claims. Because claims in each subclass are fixed as of the filing date, § 190.06(b)(1)(i) provides that the physical delivery account class includes physical delivery property held in delivery accounts as of the filing date, and the proceeds of any such physical delivery property received subsequently (*i.e.,* cash received after the filing date, in exchange for physical delivery property on which delivery was made), and § 190.06(b)(ii) provides the cash delivery account class includes cash delivery property in delivery accounts as of the filing date, along with physical delivery property for which delivery is subsequently taken (*i.e.,* in exchange for cash delivery property paid after the filing date) on behalf of a customer in accordance with § 190.06(a)(3).

Section 190.06(b)(2) describes the customer property included in the cash delivery account class and in the physical delivery account class. Section 190.06(b)(2) provides that customer property in the cash delivery account class includes cash or cash equivalents that are held in an account under a name, or in a manner, that clearly indicates that the account holds property for the purpose of making payment for taking delivery of a commodity under commodity contracts. Customer property in the cash delivery account class also includes any other property that is (A) not segregated for the benefit of customers in the futures, foreign futures, or cleared swaps account classes) and (B) traceable (through, *e.g.,* account statements) as having been received after the filing date as part of taking delivery.

Section 190.06(b)(2) also provides, conversely, that customer property in the physical delivery account class includes cash or cash equivalents that are held in an account under a name, or in a manner, that clearly indicates that the account holds property received in payment for making delivery of a commodity under a commodity contract. Customer property in the

debtor FCM by transferring or liquidating such contracts before they move into delivery position.

[127] The requirement for registered entity rules to be submitted for approval in accordance with section 5c(c) of the Act has been deleted for reasons discussed in section II.B.2 above with respect to § 190.04(e)(1) and (2).

[128] The Commission notes that § 190.04(c) directs the trustee to use its best efforts to avoid delivery obligations concerning contracts held through the debtor FCM by transferring or liquidating such contracts before they move into delivery position. Section 190.06(a)(2) applies where the trustee is unable to do so.

physical delivery account class also includes any other property that is (A) not segregated for the benefit of customers in the futures, foreign futures, or cleared swaps account classes) and (B) traceable (through, *e.g.,* account statements) as having been held for the purpose of making delivery of a commodity under a commodity contract, or held as of the filing date as a result of taking delivery.

The Commission requested comment on all aspects of proposed § 190.06. In particular, the Commission sought comment on the implications of subdividing the delivery account class into separate physical delivery and cash delivery account subclasses, including any additional challenges or benefits that the Commission did not consider. CME expressed support for specific aspects of proposed § 190.06, such as: (1) The proposed enhancements to the delivery account class, including separating the account class into physical and cash delivery account classes; (2) the additional detail provided to the trustee on how to facilitate the completion of deliveries including, in particular, the requirement for the trustee to use reasonable efforts to allow delivery to occur outside administration of the debtor FCM's estate when the rules of the relevant exchange or DCO prescribe a process for allowing deliveries to be accomplished as set forth in the proposal; and (3) the clarification that cash or cash equivalents held by the debtor FCM in an account maintained at a bank, DCO, foreign clearing organization or elsewhere constitutes customer property when it is held under a name or in a manner clearly indicating the property in the account relates to deliveries. As to the latter, CME believes that this will facilitate identifying cash delivery property available to distribute to customers in the cash delivery account class.[129]

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.06 as proposed, with modifications to § 190.06(a)(5) as set forth above.

5. Regulation § 190.07: Transfers

Regulation § 190.07 was proposed to set forth detailed provisions governing transfers, consistent with the policy preference, explained in § 190.00(c)(4), for transferring (or ''porting'') public customer commodity contract positions, as well as all or a portion of such customers' account equity. It is being adopted as proposed with modifications to § 190.07(b), (d), and (e), as set forth below.

The Commission requested comment with respect to all aspects of proposed § 190.07, and raised particular questions with respect to the proposed six-month post-transfer period to complete customer diligence, partial transfers, and estimates of customer claims.

Section 190.07(a) addresses rules that clearing organizations and SROs may ''adopt, maintain in effect, or enforce'' that may affect transfers.

In § 190.07, paragraphs (a)(1) and (2) states that these organizations may not have such rules that, respectively, ''are inconsistent with the provisions of'' part 190 or that interfere with the acceptance by their members of commodity contracts and collateral from FCMs that are required to transfer accounts pursuant to § 1.17(a)(4). These provisions are derived from current § 190.06(a)(1) and (2), with technical changes. No comments were received with respect to these provisions.

Section 190.07(a)(3) is intended to promote transfers, to the extent consistent with good risk management. It provides that no clearing organization or other SRO may adopt, maintain in effect, or enforce rules that ''interfere with the acceptance by its members of transfers of commodity contracts, and the property margining or securing such contracts, from [an FCM that is a debtor] if such transfers have been approved by the Commission . . .'' Paragraph (a)(3) includes a proviso, however, that it shall not (i) ''[l]imit the exercise of any contractual right of a clearing organization or other registered entity to liquidate or transfer open commodity contracts''; or (ii) ''[b]e interpreted to limit a clearing organization's ability adequately to manage risk.''

FIA supported the proviso, and CME ''agree[ed] that transfers should be made consistent with sound risk management principles, and in that regard welcome[d] the proposed clarification that the requirements under the proposed rule do not limit the rights of a DCO (or a DCM or swap execution facility as ''registered entities'' as defined in the CEA) to liquidate or transfer open commodity contracts.'' ICE, by contrast, was concerned that the term ''interfere with'' is overly broad, and requested that the Commission ''clarify that a clearing organization is not precluded from managing the risks presented by any such transfer, including through bona fide changes in margin requirements and guarantee fund contributions for transferee clearing members.''

As discussed immediately above, the provision already states that ''this paragraph (a)(3) shall not . . . be interpreted to limit a clearing organization's ability adequately to manage risk.'' Moreover, recognizing the different or additional margin requirements or guarantee fund contribution requirements resulting from the additional positions carried by a transferee clearing member is not a rule that interferes with the acceptance of a transfer of commodity contracts.[130] Accordingly, the Commission concludes that § 190.07(a)(3) appropriately meets the goal of promoting transfers to the extent consistent with good risk management.

Regulation § 190.07(b) concerns requirements for transferees. Paragraph (b)(1) clarifies that it is the duty of the transferee—not of anyone else—to assure that the transfer will not cause the transferee to be in violation of the minimum financial requirements. Paragraph (b)(2) notes that the transferee accepts the transfer subject to any loss arising from deficit balances that cannot be recovered from the customer, and, in the case of customer accounts, must keep such counts open for at least one business day (unless the customer fails to respond to a margin call within a reasonable time) and may not collect commissions with respect to the transfer.

As stated in the proposal, the Commission understands that customer diligence processes would have already been required to have been completed by the debtor FCM with respect to each of its customers as part of opening their accounts. Regulation § 190.07(b)(3) thus provides that a transferee may accept open commodity contracts and property, and may open accounts on its records prior to completing customer diligence, provided that account opening diligence as required is performed as soon as practicable but no later than six months after transfer, unless the time is extended, by the Commission, for a particular account, transfer, or debtor. This provision is consistent with past practice in FCM bankruptcies.

CME supported this provision as a ''practical change'' that should assist in finding willing transferees, while ICI believed that it will help mitigate or

[129] CME noted that its support was ''subject to CME's comments which request changes to the cash delivery property and physical delivery property definitions.'' Specifically, CME requested that the Commission adopt more formal requirements with respect to delivery accounts through a separate rulemaking. That request is addressed in section II.G below.

[130] The Commission understands ICE's reference to ''bona fide changes in margin requirements and guarantee fund contributions'' to mean changes that are not based on the fact that positions were acquired by transfer.

eliminate ''speed bumps'' to porting. Vanguard supported the flexibility advanced by the Commission here, but urged the Commission to work to harmonize that flexibility across other regulatory regimes applicable at FCMs, particularly for those dually registered as broker-dealers.

FIA supported the policy underlying paragraph (b)(3), and noted that it is essential to realize the policy of favoring porting over liquidation of customer accounts. FIA also agreed that six months is a reasonable period of time for this process, subject to the Commission's authority to grant additional time in particular circumstances. FIA was, however, of the view that this regulation should ''provide transferee FCMs more specific relief from applicable law relating to 'customer diligence.' ''

FIA encouraged the Commission to specify the customer diligence rules from which transferee FCMs will have temporary relief. FIA stated that

> ''such rules may include, but not be limited to: (i) rules relating to anti-money laundering requirements (including rules requiring FCMs to implement customer identification programs and know your customer requirements and all corresponding self-regulatory organization (''SRO'') requirements); (ii) rules relating to risk and other disclosures (§§ 1.55, 30.6, 33.7 and similar SRO disclosure requirements); (iii) rules relating to capital and residual interest requirements (§§ 1.11, 1.17, 1.22, 1.23, 22.2, 22.17, 30.7 and 41.48 and related SRO requirements); (iv) rules relating to account statements required under § 1.33 in the event positions transfer with inadequate contact information (§ 1.33 and related SRO requirements); and [(v)] rules relating to margin in the event accounts transfer without adequate margin (§§ 1.17, 39.13, 41.42–41.49 and related SRO requirements).''

The Commission has considered each of the five types of requirements discussed by FIA:

With respect to anti-money laundering requirements, the Commission notes that, for purposes of the Customer Identification Program (''CIP'') requirements applicable to futures commission merchants pursuant to 31 CFR 1026.220, the term ''account'' is defined to *exclude* ''[a]n account that the futures commission merchant acquires through any acquisition, merger, purchase of assets, or assumption of liabilities.'' 31 CFR 1026.100(a)(2)(i). Thus, transferred accounts are not subject to the CIP requirements.

However, the Customer Due Diligence (''CDD'') requirements of 31 CFR 1026.210(b)(5) do appear to apply. These include a requirement for ''[a]ppropriate risk-based procedures for conducting ongoing customer due diligence, to include . . . [u]nderstanding the nature and purpose of customer relationships for the purpose of developing a customer risk profile . . . .'' 31 CFR 1026.210(b)(5)(i). The Commission is of the view that § 190.07(b)(3) would inform the determination of what constitutes *appropriate* risk-based procedures in the exigent context of an FCM accepting a transfer of accounts from an FCM that is a debtor in bankruptcy.

While FIA appears to request a reference to the account opening disclosure requirements in §§ 1.55, 30.6, and 33.7, these would appear to be addressed by the bulk transfer provisions of § 1.65. The Commission is amending § 190.07(b)(3) to include a parenthetical statement that explicitly refers to ''the risk disclosures referred to in § 1.65(a)(3).'' This will modify the sixty-day requirement of that paragraph.

The Commission declines to amend the regulation to extend the time to comply with capital and residual interest requirements. To do so would risk permitting a transfer of accounts to result in contagion of financial weakness. The Commission reiterates the importance of § 190.07(b)(1), which provides that ''it is the duty of each transferee to assure that it will not accept a transfer that would cause the transferee to be in violation of the minimum financial requirements set forth in this chapter.''

However, to the extent that shortfalls in compliance with these requirements are due to errors or shortfalls in the data received by the transferee from the transferor FCM, and the transferee acts with reasonable and appropriate diligence in seeking to detect such errors or shortfalls in data, and, where detected, in investigating and correcting them, such shortfalls in compliance would not be considered violations of such requirements.

Similarly, where account statements required by § 1.33 do not reach the customer due to errors or shortfalls in the contact information provided to the transferee, there would be no violation so long as the transferee takes reasonable steps to detect such errors or shortfalls (*e.g.,* by reacting promptly to rejected email or returned postal mail, or to complaints by a transferred customer that they are not receiving such statements) and to correct the situation once detected. The proposed regulation does not need to be amended to achieve this result.

Finally, with respect to FIA's request for relief with respect to regulations ''relating to margin in the event accounts transfer without adequate margin,'' the Commission believes that the determination of whether a transferee FCM is *promptly* collecting such margin should be informed by the exigencies of the situation. There is, however, no basis for a general exemption for transferee accounts from the requirements of § 39.13(g)(8)(iii), providing that a DCO shall require that its members do not permit customers to withdraw funds from their accounts unless the accounts would be fully margined after such withdrawal. If the transferee FCM is not confident of the information it has regarding the transferred account, it would seem appropriate to risk manage with caution. Once the transferee FCM is confident that it fully understands the situation, the transferee can act in accordance with its normal procedures.[131] Similarly, there is no basis to provide a general exemption from undermargined account capital charges in accordance with § 1.17.

In all of these cases, the Commission encourages DCOs and SROs to take similar approaches.

While the Commission has declined, in many of the above cases, to provide general relief by regulation, this is without prejudice to the possibility that more targeted relief may be appropriate in particular cases. Specifically, any further relief that might be appropriate in a particular situation could be requested by, *e.g.,* the transferee, in light of the relevant facts and circumstances.

The Commission observes that its staff have traditionally responded to requests for relief in emergency situations with great dispatch, and expects, and thus instructs staff, to continue to do so in this context in the future.[132]

OCC recommended that ''the Commission adopt a parallel regulation permitting a DCO to postpone any due diligence the DCO would typically have to perform on an FCM member accepting transferred positions from a bankrupt FCM.'' This would include the requirements of, *e.g.,* § 39.12, requiring a DCO to have ''continuing participation requirements for clearing members of the [DCO] that are objective, publicly available, and risk-based.''

The Commission does not agree that the situations are parallel: An FCM is required to perform individualized due

[131] Such normal procedures would include the ''ordinary course of business'' referred to in Letter 19–17, or any successor letter or regulation. *See* CFTC Letter 19–17, *https://www.cftc.gov/node/217076.*

[132] For the avoidance of doubt, the nature of the expectation and the instruction is that staff will provide *a* response to such requests with great dispatch. The nature of the response, whether affirmative, affirmative in part, or negative, will depend on the relevant facts and circumstances.

diligence on each of its customers, which in the case of a transfer such as was seen in historical situations such as *MF Global,* would amount to hundreds or even thousands of customers. By contrast, the focus of a DCO is on the financial and operational capability of each of its clearing members that is a transferee to manage, *in the aggregate,* the customer portfolios of which it accepts transfer. The number of transferee FCM clearing members is likely to be no more than a dozen.

In any event, the Commission expects that a DCO would, and would be permitted to, conduct its due diligence procedures in a manner consistent with balancing risk management requirements (*see, e.g.,* § 190.07(a)(3)(ii) (restrictions on a DCO interfering with the acceptance of transfers from a debtor FCM ''shall not be interpreted to limit a clearing organization's ability adequately to manage risk'') with the exigencies of the situation.

Section 190.07(b)(4) is designed to clarify what the account agreement between the transferred customer and the transferee is at and after the time the transfer becomes effective. This includes situations where an account is partially transferred. As proposed, it provides that any account agreements governing a transferred account shall be deemed assigned to the transferee and shall govern the customer's relationship unless and until a new agreement is reached. It also provides that a breach of the agreement prior to a transfer does not constitute a breach on the part of the transferee. CME, ICI, and Vanguard supported this provision.

FIA appreciated the need for legal certainty as to the terms of the relationship between a transferee FCM and each transferred customer, but was concerned that the transferee FCM might be disadvantaged by being subject to an account agreement between the transferred customer and the transferor (debtor) FCM. There are two possible situations with respect to each customer: Either the customer does, or does not, have a pre-existing account agreement with the transferee FCM.

FIA noted that many large customers, in particular, may maintain accounts at more than one FCM, and thus it may be the case that the customer already has an account agreement in place with the transferee FCM. FIA asked the Commission to confirm their view that, in this context, the transferee would not be required to manage the ported account(s) in accordance with the agreement with the transferor FCM. The Commission agrees with this view, and is modifying proposed § 190.07(b)(4) to state this explicitly: The proposed text will be renumbered as § 190.07(b)(4)(i), and paragraph (b)(4)(ii) will be added to provide that paragraph (b)(4)(i) shall not apply where the customer has a pre-existing account agreement with the transferee futures commission merchant. In such a case, the transferred account will be governed by that pre-existing account agreement.

However, where the transferred customer does not have a pre-existing account agreement with the transferee FCM, FIA conceded that ''the account agreement [between the transferor and the customer] should stay in place for a short defined interim period during which the parties may renegotiate. . . .'' FIA did not specify how long that ''short defined interim period'' should last, nor what should happen at the end of that period if the parties fail to reach agreement. The Commission notes that nothing prevents either the transferee FCM or customer from negotiating at any time to change the (in this case, assigned) account agreement between them, and that, aside from § 190.07(b)(2)(ii)(A) (requiring the transferee to keep the customer's commodity contracts open at least one business day after their receipt unless the customer fails to meet promptly a margin call), nothing in the Commission's regulations prevents either the transferee or customer from terminating their relationship if they cannot reach agreement as to the terms under which that relationship should continue, on what either party believes is a timely basis. Accordingly, the Commission declines to modify § 190.07(b)(4) in this context.

Lastly, FIA observed that a customer's account may not always be able to be physically transferred from the debtor FCM to the transferee FCM. The Commission notes that the reference in § 190.07(b)(4) to assignment of account agreements does not refer to the movement of physical documents.[133] As requested by FIA, the Commission can thus confirm that assignment of the agreement does not depend upon such movement.

Regulation § 190.07(b)(5) provides that customer instructions received by the debtor with respect to open commodity contracts or specifically identifiable property that has been, or will be, transferred in accordance with section 764(b) of the Bankruptcy Code, should be transmitted to any transferee, which shall comply therewith to the extent practicable (if the transferee subsequently enters insolvency).

[133] To be sure, a transfer agreement would likely include transfers of records or at least copies of records as a matter of good practice.

Regulation § 190.07(c) addresses eligibility of accounts for transfer under section 764(b) of the Bankruptcy Code. This provision states that ''[a]ll commodity contract accounts (including accounts with no open commodity contract positions) are eligible for transfer. . . .'' This language recognizes that accounts can be transferred even if they are intended for trading commodities but do not include any open commodity contracts at the time of the order for relief.[134]

Regulation § 190.07(d) addresses special rules for transfers under section 764(b) of the Bankruptcy Code. Paragraph (d)(1) instructs the trustee to ''use its best efforts to effect a transfer to one or more other commodity brokers of all eligible commodity contract accounts, open commodity contracts and property held by the debtor for or on behalf of its customers, based on customer claims of record, no later than the seventh calendar day after the order for relief.'' The Commission will correct a typographical error in the proposal, and refer to ''customer claims *of* record'' rather than ''customer claims *or* record.''

Regulation § 190.07(d)(2) addresses cases of partial transfers and multiple transferees. It includes a requirement that ''a partial transfer of contracts and property may be made *so long as such transfer would not result in an increase in the amount of any customer's net equity claim.*'' The added language is intended to caution against partial transfers that would break netting sets and make the customer worse off. The Commission has also decided to state that one way to accomplish a partial transfer is ''by liquidating a portion of the open commodity contracts held by a customer such that sufficient value is realized, or margin requirements are reduced to an extent sufficient, to permit the transfer of some or all of the remaining open commodity contracts and property.'' This language is intended to clarify that the liquidation may either crystalize gains or have the effect of reducing the required margin. Finally, with regards to the transfer of part of a spread or a straddle,

[134] *Cf.* 11 U.S.C. 761(9)(A)(ii)(II) (customer means, with respect to an FCM, an entity that holds a claim against the FCM arising out of ''a deposit or payment of cash, security, or other property with such [FCM] *for the purpose of* making or margining [a] commodity contract'') (emphasis added).

Thus, where a person opens a customer account and deposits collateral on day 1, intending to trade on day 3 (or some subsequent day when the customer determines that it is propitious to trade) and the FCM becomes a debtor on day 2 (or some other day when the customer has no positions open) such person nonetheless qualifies as a customer, and their claim would be a customer claim.

§ 190.07(d)(2)(ii) states that ''to the extent practicable under the circumstances,'' each side of the spread or straddle must be transferred or none of the open commodity contracts comprising the spread or straddle may be transferred. This language is intended to clarify that the trustee is required to protect customers holding spread or straddle positions from the breaking of netting sets, but only to the extent practicable given the circumstances.

Regulation § 190.07(d)(3) provides details regarding the treatment and transfer of letters of credit used as margin, consistent with other proposed provisions related to letters of credit. In particular, this provision states that a transfer of a letter of credit cannot be made if it would result in a recovery that exceeds the amount to which the customer is entitled in §§ 190.08 and 190.09. If the letter of credit cannot be transferred and the customer does not deliver substitute property, the trustee may draw upon a portion or upon all of the letter of credit, the proceeds of which will be treated as customer property in the applicable account class. The Commission believes a regulation detailing how letters of credit are to be treated in a transfer will provide more certainty, as there is currently no such regulation, and that the proposed treatment is both practical and consistent with the policy of *pro rata* distribution.[135]

Regulation § 190.07(d)(4) requires a trustee to use reasonable efforts to prevent physical delivery property from being separated from commodity contract positions under which the property is deliverable. The Commission is proposing this regulation to clarify its expectations in such situations, specifically, to promote the delivery process.

Regulation § 190.07(d)(5) is intended to prevent prejudice to customers generally by prohibiting the trustee from making a transfer that would result in insufficient customer property being available to make equivalent percentage distributions to all equity claim holders in the applicable account class. It clarifies that the trustee should make determinations in this context based on customer claims reflected in the FCM's records, and, for customer claims that are not consistent with those records, should make estimates using reasonable discretion based in each case on available information as of the calendar day immediately preceding transfer.

Regulation § 190.07(e) addresses the prohibition on avoidance of transfers under section 764(b) of the Bankruptcy Code. It explicitly approves specific types of transfers, unless such transfers are disapproved by the Commission.

Section 190.07(e)(1) approves (i) transfers that were made before the order for relief in compliance with § 1.17(a)(4) (FCM fails to meet capital requirements); (ii) pre-relief transfers, withdrawals or settlements at the request of public customers, unless the customer acted in collusion with the debtor to obtain a greater share than it would otherwise be entitled to; and (iii) pre-relief transfers of customer accounts or commodity contracts and other related property, either by a clearing organization or a receiver that has been appointed for the FCM that is now a debtor. In this context, ''public customers'' would include a lower-level (*i.e.,* downstream) FCM acting on behalf of its own public customers (*e.g.,* cleared at the debtor on an omnibus basis).

Regulation § 190.07(e)(2) pertains to post-relief transfers. Section 764(b) of the bankruptcy code permits the Commission to approve, and thus protect from avoidance, transfers that occur up to seven days after the order for relief. Section 190.07(e)(2)(i) approves transfers of eligible commodity contract accounts or customer property made by the trustee or any clearing organization. Section 190.07(e)(2)(ii) approves transfers made at the direction of the Commission upon such terms and conditions as the Commission may deem appropriate and in the public interest.

Regulation § 190.07(e)(3) was referred to in preamble to the proposal as derived from current § 190.06(g)(3). It was inadvertently omitted from the rule text in the proposal.

Section 190.07(e)(3) pertains to pre-relief withdrawals by customers (in contrast to the transfers dealt with previously in § 190.07(e)(1)(ii)). It states (in terms analogous to § 190.07(e)(1)(ii)) that notwithstanding the provisions of paragraphs (c) and (d) of this section, the following transfers are approved and may not be avoided under sections 544, 546, 547, 548, 549 or 724(a) of the Bankruptcy Code: The withdrawal or settlement of a commodity contract account by a public customer, including a public customer which is a commodity broker, prior to the filing date unless: (i) The customer making the withdrawal or settlement acted in collusion with the debtor or its principals to obtain a greater share of the bankruptcy estate than that to which such customer would be entitled in a bankruptcy distribution; or (ii) The withdrawal or settlement is disapproved by the Commission.

Regulation § 190.07(f) provides that, notwithstanding the other provisions of this section (with exceptions discussed below), the Commission may prohibit the transfer of a particular set or sets of the commodity contract accounts and customer property, or permit the transfer of a particular set or sets of commodity contract accounts and customer property that do not comply with the requirements of the section. The exceptions are the policy in favor of avoiding the breaking of netting sets in § 190.07(d)(2)(ii), and the avoidance of prejudice to other customers in § 190.07(d)(5).

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.07 as proposed with modifications to § 190.07(b), (d), and (e), as set forth above.

6. Regulation § 190.08: Calculation of Funded Net Equity

Section 190.08 is being adopted as proposed with a number of technical modifications, as set forth below.

The Commission requested comment with respect to all aspects of proposed § 190.08, and raised particular questions with respect to the revisions to the calculation of the equity balance of a commodity contract set forth in proposed § 190.08(b)(1), and the appropriateness of the proposal to determine the value of an open commodity contract at the end of the last settlement cycle on the day preceding the transfer rather than at the end of the day of the transfer, as set forth in § 190.08(d)(1)–(2).

As proposed, § 190.08(a) stated that the ''allowed net equity claim of a customer shall be equal to the aggregate of the funded balances of such customer's net equity claim for each account class.'' As discussed above, the ABA Subcommittee urged that there should be more precise use of the term ''allowed claim.''[136] The Commission agrees with this recommendation. Accordingly, the Commission is amending the language in the proposal to replace the term ''allowed net equity'' with the term ''funded net equity'' in the final rule in both § 190.08(a) and in the title of § 190.08.[137]

[135] *See also* discussion of treatment of letters of credit in bankruptcy under § 190.04(d)(3) in section II.B.2.

[136] *See* discussion of ''funded claim'' in section II.A.2 above.

[137] Proposed § 190.08(a) is derived from current § 190.07(a), but reflects the fact that, under the revised definition of the term ''primary liquidation date,'' all commodity contracts will be liquidated or transferred prior to the primary liquidation date. Since no (relevant) operations will occur

Section 190.08(b) sets forth the steps for a trustee to follow when calculating each customer's net equity.[138] Section 190.08(b)(1), equity determination, sets forth the steps for a trustee to follow when calculating the equity balance of each commodity contract account of a customer. When calculating the customer's claim against the debtor, the basis for calculating such claim is the data that appears in the debtor's records. Once the customer's claim based on the debtor's records is calculated, the customer will have the opportunity to dispute such claim based on their own records, and the trustee may adjust the debtor's records if it is persuaded by the customer. There were no comments directed specifically to this provision.

Section 190.08(b)(2), customer determination (aggregation), provides instructions to the trustee regarding how to aggregate the credit and debit equity balances of all accounts of the same class held by a customer. Specifically, the regulation sets forth how to determine whether accounts are held in the same capacity or in separate capacities. There were two comments applicable to this provision.

As proposed, § 190.08(b)(2)(ix) referred to the fact that an omnibus customer accounts is held in a separate capacity from the ''house account.'' As noted above,[139] the ABA Subcommittee has suggested the deletion of the term ''house account'' in the context of FCM bankruptcies, and the Commission has accepted this suggestion. Consistent with that approach, the Commission is accepting the ABA Subcommittee's revised drafting for this provision: An omnibus customer account *for public customers* of a futures commission merchant maintained with a debtor shall be deemed to be held in a separate capacity from any omnibus customer account for non-public customers of such futures commission merchant *and from any account maintained with the debtor on its own behalf or on behalf of any non-public customer* (emphasis added only for illustration).

As proposed, § 190.08(b)(2)(xii) provided that except as otherwise provided in this section, an account maintained with a debtor by an agent or nominee for a principal or a beneficial owner shall be deemed to be an account held in the individual capacity of such principal or beneficial owner.

SIFMA AMG/MFA urged the Commission to amend this provision to ''treat accounts of the same principal or beneficial owner maintained by different agents or nominees as separate accounts,'' noting that this approach would ''reduce the administrative difficulties the trustee would face in consolidating all accounts of the same principal or beneficial owner'' and would ''avoid[] any confusion as to the treatment of separate accounts that could arise with the overlay of the time-limited relief provided by Letter 19–17.''[140] SIFMA AMG/MFA asserted that this change would be similar to the approach taken by the Commission in proposed § 190.08(b)(2)(xiv), which provides that accounts held by a customer in separate capacities shall be deemed to be accounts of different customers.

The Commission notes that CFTC Letter 19–17 conditioned such relief on the FCM performing ''stress testing and credit limits . . . on a combined account basis'' and ''provid[ing] each beneficial owner using separate accounts with a disclosure that under CFTC [p]art 190 rules all separate accounts of the beneficial owner will be combined in the event of an FCM bankruptcy.''[141] Thus, treating separate accounts of the same beneficial owner on a combined basis is entirely consistent with the approach taken in Letter 19–17. Nor is the situation of separate accounts for the same beneficial owner analogous to a customer holding accounts in separate capacities, as referred to in § 190.08(b)(2)(xiv) (*e.g.,* in their personal capacity versus in their capacity as trustee for X, or in their capacity as trustee for Y versus their capacity as trustee for Z.). In those latter cases, the same legal owner is acting for separate beneficial owners. Accordingly, the Commission is declining to amend § 190.08(b)(2)(xii).

Section 190.08(b)(3), setoffs, sets forth instructions regarding how and when to set off positive and negative equity balances.

Section 190.08(b)(4), correction for distributions, provides that the value of property that has been transferred or distributed must be added to the net equity amount calculated for that customer after performing the steps contained in § 190.08(b)(1) through (3). Section 190.08(b)(4) also includes a proviso that clarifies that the calculation of net equity for any late-filed claims (in cases where all accounts for which there are customer claims of record as of the filing date are transferred with all of the equity pertaining thereto) will be based on the allowed amount of such claims.

Section 190.08(b)(5), correction for ongoing events, provides that the calculation of net equity will be adjusted to correct for misestimates or errors, including corrections for the liquidation of claims or specifically identifiable property at a value different from the estimate value previously used in computing net equity.

As proposed, § 190.08(c) set forth the method for calculation of a customer's funded balance, *i.e.,* ''a customer's *pro rata* share of the customer estate with respect to each account class available for distribution to customers of the same customer class.'' Section 190.08(c)(1) sets forth instructions for calculating the funded balance of any customer claim, while § 190.08(c)(2) requires the funded balance to be adjusted to correct for ongoing events.

One change is being made to paragraph (c)(1), as a result of addressing a comment that affected a prior section. As proposed, § 190.08(c)(1)(ii) addressed giving customers credit for 100% of margin payments made after the order for relief.

As discussed above,[142] a number of commenters (ABA Subcommittee, CME, CMC), suggested that the definition of cash delivery property be expanded to address the possibility of post-filing-date payments made by customers to the FCM to pay for delivery. Such payments should be credited in full to the customer's funded balance. Indeed, § 190.06(a)(3)(ii)(B)(*2*) provides that the trustee could issue payment calls in this context and that ''the full amount of any payment made by the customer in response to a payment call must be credited to the funded balance of the particular account for which such payment is made.''

In order to be consistent with the principle that 100% of post-filing-date payments are credited to a customer's funded balance, proposed § 190.08(c)(1)(ii) is being amended, with the proposed language addressing post-filing-date margin payments to be codified as § 190.08(c)(1)(ii)(A), and the addition of § 190.08(c)(1)(ii)(B) to address post-filing-date payments for deliveries, to read as follows: ''[then adding 100% of] . . . [f]or cash delivery property, any cash transferred to the trustee on or after the filing date for the purpose of paying for delivery.''

Section 190.08(d), valuation, sets forth instructions about how to value

subsequent to the liquidation date, provisions that address how to deal with commodity contracts after that time are moot.

[138] Pursuant to section 20(a)(5) of the CEA, 7 U.S.C. 24(a)(5), the Commission has the power to provide how the net equity of a customer is to be determined.

[139] *See* section II.A.2 above.

[140] *See* CFTC Letter 19–17, *https://www.cftc.gov/node/217076.*

[141] *Id.* at 5 (emphasis supplied).

[142] *See* discussion of cash delivery property in section II.A.2, above.

commodity contracts and other property for purposes of calculating net equity as set forth in the rest of § 190.08.

Section 190.08(d)(1) sets forth instructions regarding how to value commodity contracts, separately addressing: (i) Open commodity contracts, and (ii) liquidated commodity contracts.

As proposed, § 190.08(d)(1)(i), regarding the valuation of open commodity contracts, states that ''if an open commodity contract is transferred to another commodity broker, its value on the debtor's books and records shall be determined as of the end of the last settlement cycle on the day preceding such transfer.'' The Commission noted in the proposal that ''[t]his would allow the value of the open commodity contract to be known prior to the transfer,'' [143] and, as discussed above, specifically sought comments on this issue.

The Commission received contrasting comments on this provision. ICE ''d[id] not believe that valuation is the right one, particularly because the market may move significantly on the date of transfer.'' By contrast, CME ''agree[d]'' with valuation as of the end the last settlement cycle on the day preceding transfer, because it aligns with calculations of funded balances under proposed § 190.08(c), and noted that ''any mark-to-market gains or losses on the date of the transfer should be reflected by the receiving FCM(s) in the customer account statements as a result of that day's settlement cycle.'' The Commission is persuaded by the latter comment, and will adopt the provision as proposed, both for the reasons stated by the latter commenter, and because of concerns regarding practicability. Markets move on a continuous basis so long as they are open and, considering markets around the world, some markets on which futures, foreign futures, or cleared swaps are traded are moving at all times other than over a weekend.

Section 190.08(d)(1)(ii)(A) allows the trustee to use the weighted average of liquidation prices for identical commodity contracts that are liquidated within a 24-hour period or business day, but not at the same price.

Section 190.08(d)(1)(ii)(B) provides instructions on how to value commodity contracts that are liquidated as part of a bulk auction by a clearing organization or similarly outside of the open market. As proposed, this provision would value a commodity contract that is liquidated as part of a bulk auction at the settlement price calculated by the clearing organization as of the end of the settlement cycle during which the commodity contract was liquidated. ICE disagreed with this approach, stating that ''the price achieved in the auction should be used.'' However, as the Commission noted in the proposing release, the units being auctioned will often be a heterogenous (though risk-related) set of products, tenors (*e.g.,* contract months), and directions (*e.g.,* long or short). Different auctioned portfolios may contain the same or similar contracts. In this context, setting the price of a particular contract based on the auction price for a portfolio would require considerable interpretation. Accordingly, the Commission will implement the approach from the proposal.

Section 190.08(d)(2) sets forth the approach for valuing listed securities, and incorporates the same weighted average concept discussed above with respect to § 190.08(d)(1)(ii)(A).

Section 190.08(d)(3) sets forth the approach for valuing commodities held in inventory, directing the trustee to use fair market value. If such fair market value is not readily ascertainable from public sources of prices, the trustee is directed to use the approach in § 190.08(d)(5), discussed below.

Section 190.08(d)(4) addresses the valuation of letters of credit. The trustee is directed to use the face amount (less amounts, if any, drawn and outstanding). However, if the trustee makes a determination in good faith that a draw is unlikely to be honored on either a temporary or permanent basis, they are directed to use the approach in paragraph (d)(5).

Section 190.08(d)(5) provides the trustee with pragmatic flexibility in determining the value of customer property by allowing the trustee, in their sole discretion, to enlist the use of professional assistance to value all other customer property.[144] This provision further notes that, if such property is sold, its value for purposes of the calculations required by this part is equal to the actual value realized on sale of such property (the trustee, of course, retains discretion to engage professional assistance to allocate such value among a heterogenous set of items sold as a unit). Finally, the provision notes that any such sale shall be made in compliance with all applicable statutes, rules, and orders of any court or governmental entity with jurisdiction thereover.

Accordingly, after consideration of the comments and for the reasons stated above, § 190.08 is being adopted as proposed, with modifications to the title and to § 190.08(a), (b), and (c), as set forth above.

7. Regulation § 190.09: Allocation of Property and Allowance of Claims

Section 190.09 is being adopted to set forth rules governing the scope of customer property, the allocation of customer property between customer and account classes, and distribution of customer property. It was derived from current § 190.08. It is being adopted as proposed with modifications to § 190.09(d)(3), as set forth below.

The Commission requested comment with respect to all aspects of proposed § 190.09. The Commission also raised particular questions with respect to: Whether the proposed revisions to § 190.09(a)(1) would appropriately preserve customer property for the benefit of customers; whether proposed § 190.09(a)(1)(ii)(G), concerning property that other regulations require to be placed into segregation, and § 190.09(a)(1)(ii)(L), concerning remaining shortfalls, are appropriately crafted; whether it is advisable to permit customers to post ''substitute customer property'' rather than ''cash'' in proposed § 190.09(d); and whether it is appropriate to clarify the term ''like-kind securities'' by reference to the concept, derived from SIPA, of ''securities of the same class and series of an issuer?''

There are three substantive changes in new § 190.09, as compared to current regulations:

Section 190.09(a)(1)(ii)(G) and (L) are two categories of property that are defined to be included in customer property in order better to protect customers from shortfalls in customer property (*i.e.,* cases where customer property is insufficient to cover claims for customer property).

Section 190.09(a)(1)(ii)(G) is a new category of property that constitutes customer property. It includes any cash, securities, or other property which constitutes current assets of the debtor, including the debtor's trading or operating accounts and commodities of the debtor held in inventory, in the greater of (i) the amount of the debtor's targeted residual interest amount pursuant to § 1.11 with respect to each account class, or (ii) the debtor's obligations to cover debit balances or undermargined amounts as provided in §§ 1.20, 1.22, 22.2 and, 30.7. Each of the sets of regulations referred to in proposed § 190.09(a)(1)(ii)(G) requires an FCM to put certain funds into

[143] 85 FR 36028.

[144] The trustee's employment of professionals remains subject to the requirements of section 327 of the Bankruptcy Code.

segregation on behalf of customers. To the extent the FCM has failed to comply with those regulatory requirements prior to the filing of the bankruptcy, this provision requires the bankruptcy trustee to fulfill that requirement, and allows the trustee to use the current assets of the debtor to do that.

CME stated that this new provision is a ''substantial improvement over the current rule,'' and it was also supported by ICI and Vanguard.

Section 190.09(a)(1)(ii)(L) is the analog to current § 190.08(a)(1)(ii)(J) but with updated cross-references (and a new second sentence, discussed in the next paragraph). It states that customer property includes any cash, securities, or other property in the debtor's estate, but only to the extent that the customer property under the other definitional elements is insufficient to satisfy in full all claims of the FCM's public customers.[145]

A new second sentence of § 190.09(a)(1)(ii)(L) notes explicitly that customer property for purposes of these regulations includes any ''customer property,'' as that term is defined in SIPA, that remains after satisfaction of the provisions in SIPA regarding allocation of (securities) customer property. SIPA provides that such remaining customer property would be allocated to the general estate of the debtor.[146] Any securities customer property that remains after satisfaction in full of securities claims provided for in that section of SIPA proceeding and would accordingly become property of the general estate should, to the extent otherwise provided in proposed § 190.09(a)(1)(ii)(L), and for the same reasons, become customer property in the FCM bankruptcy proceeding.

Section 190.09(d) governs the distribution of customer property, and has its analog in current § 190.08(d). Section 190.09(d)(1)(i) and (ii) and (d)(2) require customers to deposit ''substitute customer property,'' to obtain the return or transfer of specifically identifiable property. ''Substitute customer property'' is defined in § 190.01 to mean (in relevant part) ''cash or cash equivalents.'' ''Cash equivalents,'' in turn, are defined as ''assets, other than United States dollar cash, that are highly liquid such that they may be converted into United States dollar cash within one business day without material discount in value.''

The purpose of requiring customers to, in essence, ''buy back'' specifically identifiable property is to implement the *pro rata* distribution principle set forth in section 766(h) of the Bankruptcy Code, and discussed in § 190.00(d)(5). Permitting customers to redeem specifically identifiable property with either cash or cash equivalents, rather than requiring cash, may mitigate the difficulty (and costs) such customers face in obtaining redemption, but will in any event fully implement the *pro rata* distribution principle.

As a technical point, the ABA Subcommittee recommended (consistent with their recommendation in the definitions section, § 190.01, to more precisely use the term ''allowed net equity'') that the reference in proposed § 190.09(d)(3) to the amount distributable on a customer's claim be amended to add ''[the] funded balance of'' before the phrase ''such customers allowed net equity claim.'' The Commission agrees, and is making the change.

The remaining provisions of revised § 190.09 include only technical changes to the current regulations.

Accordingly, after consideration of the comments, and for the reasons stated above, § 190.09 will be adopted as proposed, with the modification to § 190.09(d)(3) referred to above.

8. Regulation § 190.10: Provisions Applicable to Futures Commission Merchants During Business as Usual

The Commission proposed § 190.10 to contain new and relocated provisions that set forth an FCM's obligations during business as usual. The Commission requested comment with respect to all aspects of proposed § 190.10, and specifically with respect to (1) the impact of proposed § 190.10(b) regarding the designation of hedging accounts, (2) the impact of proposed § 190.10(c) regarding the establishment of delivery accounts during business as usual, (3) the changes in proposed § 190.10(d) to the business as usual requirements for acceptance of letters of credit, and in particular (a) whether its understanding is correct that most letters of credit currently in use by the industry follow the JAC forms, (b) the impact of additional requirements concerning letters of credit (as well as any alternative methods of achieving the goal of treating customers posting letters of credit consistent with the treatment of other customers), and (c) whether the proposed one year transition period is reasonable, and (4) the disclosure statement for non-cash margin set out in proposed § 190.10(e) (whether the statement is helpful, legally or practically, whether it should be changed, or whether it should be deleted).

Section 190.10 will be adopted as proposed with modifications. In particular, the ABA Subcommittee and CME suggested that the provisions in proposed § 190.10 be codified in part 1, along with other regulations that pertain to an FCM's business as usual. The ABA Subcommittee stated that, while they had originally suggested that these provisions belong in § 190.10, ''[u]pon further reflection, the Committee believes that such a rule more logically belongs in the Commission's Part 1 Regulations, along with other rules that apply to FCMs during business as usual. Compliance and legal personnel could inadvertently overlook obligations that are not located in the Commission rule set where they would expect to find them.''

The Commission agrees with the commenters that transparency would be fostered by putting the ''business as usual'' requirements proposed for § 190.10 into part 1 of the Commission's regulations. Accordingly, as discussed further below, most of the paragraphs of the regulation that was proposed as § 190.10 are being renumbered and will be codified in specified places in part 1. The provisions of proposed § 190.10 will otherwise be adopted as proposed.

The provision proposed as § 190.10(a) notes that an FCM is required to maintain current records relating to its customer accounts, pursuant to §§ 1.31, 1.35, 1.36, and 1.37, and in a manner that would permit them to be provided to another FCM in connection with the transfer of open customer contracts of other customer property. This provision recognizes that current and accurate records are imperative in arranging for the transfer of customer contracts and other property, both for the trustee of the estate of the defaulter and for an FCM that is accepting the transfer. Nonetheless, it does not add to an FCM's obligations under the specified regulations, but rather is useful as a reference for the trustee. Accordingly, this provision will not be moved to part 1.

No comments were received with respect to the substance of proposed § 190.10(a). As the remaining paragraphs of proposed § 190.10 will be moved to part 1, this provision will be codified as § 190.10.

The provision proposed as § 190.10(b) concerns the designation of hedging accounts. It incorporates concepts contained in current §§ 190.04(e) and 190.06(d) and the current Bankruptcy appendix form 3 instructions. As it sets

[145] ICE notes that the issues with respect to this provision may be complicated, and that it may warrant further consideration, but ultimately expresses no view on it.

[146] *See generally* SIPA section 8(c)(1), 15 U.S.C. 78fff–2(c)(1).

forth obligations for an FCM during business as usual, it will be moved to part 1. As it does not fit under any existing part 1 regulation, it will be moved under the miscellaneous heading of part 1, and codified as § 1.41.

For purposes of § 1.41, a customer will not need to provide, and an FCM will not be required to judge, evidence of hedging intent for purposes of bankruptcy treatment. Rather, § 1.41 will permit the FCM to treat the account as a hedging account for such purposes based solely upon the written record of the customer's representation. Hedging treatment for these bankruptcy purposes will not be determinative for any other purpose.

Section 1.41(a) will require an FCM to provide a customer an opportunity to designate an account as a hedging account when the customer first opens the account, rather than when the customer undertakes its first hedging contract, as specified in current § 190.06(d)(1). This provision will also require that the FCM indicate prominently in its accounting records for each customer account whether the account is designated as a hedging account.

Section 1.41(b) will set forth the requirements for an FCM to treat an account as a hedging account: If, but only if, the FCM obtains the customer's written representation that the customer's trading in the account will constitute hedging as defined under any relevant Commission regulation or rule of a DCO, DCM, SEF, or FBOT. CME supported this approach, and the clarity it adds.

In order to avoid the significant burden that would be associated with requiring FCMs to re-obtain hedging instructions for existing accounts, § 1.41(c) will provide that the requirements of § 1.41(a) and (b) do not apply to commodity contract accounts opened prior to the effective date of these revisions. Rather, the provision will recognize expressly that an FCM may continue to designate existing accounts as hedging accounts based on written hedging instructions obtained under former § 190.06(d).

Finally, § 1.41(d) will permit an FCM to designate an existing futures, foreign futures or cleared swaps account of a particular customer as a hedging account, provided that the FCM obtains the representation required under § 1.41(b).

The provision proposed as § 190.10(c) addresses the establishment of delivery accounts during business as usual.[147] As it sets forth obligations for an FCM during business as usual, it will be moved to part 1. As it does not fit under any existing part 1 regulation, it will be moved under the miscellaneous heading, and codified as § 1.42.

When a commodity contract is in the delivery phase, or when a customer has taken delivery of commodities that are physically delivered, associated property may be held in a ''delivery account'' rather than in the segregated accounts pursuant to, *e.g.,* § 1.20 or § 22.2. Section 1.42 recognizes that when an FCM facilitates delivery under a customer's physical delivery contract, and such delivery is effected outside of a futures account, foreign futures account, or cleared swaps account, it must be effected through (and the associated property held in) a delivery account. If, however, the commodity that is subject to delivery is a security, the FCM may effect delivery through (and the property may be held in) a securities account. The regulation clarifies that the property must be held in one of these types of accounts. ICE and CME generally support this provision.[148]

The provision proposed as § 190.10(d) addresses letters of credit that an FCM accepts as collateral. As it sets forth obligations for an FCM during business as usual, it will be moved to part 1. As it does not fit under any existing part 1 regulation, it will be moved under the miscellaneous heading, and codified as § 1.43.

Section 1.43 will prohibit an FCM from accepting a letter of credit as collateral unless certain conditions (1) are met at the time of acceptance and (2) remain true through its date of expiration.

First, pursuant to § 1.43(a), the trustee must be able to draw upon the letter of credit, in full or in part, in the event of a bankruptcy proceeding, the entry of a protective decree under SIPA, or the appointment of FDIC as receiver pursuant to Title II of the Dodd-Frank Act. Second, pursuant to § 1.43(b), if the letter of credit is permitted to be and is passed through to a clearing organization, the bankruptcy trustee for such clearing organization or (if applicable) FDIC must be able to draw upon the letter of credit, in full or in part, in the event of a bankruptcy proceeding, or where the FDIC is appointed as receiver pursuant to Title II.

The Commission has considered the impact that implementation of this regulation would have on FCMs and their customers, since letters of credit are currently in use by the industry.[149] The Commission proposed that, upon the effective date of the regulation, what is now codified as § 1.43 would apply only to *new* letters of credit and customer agreements. In order to mitigate the impact of implementing this regulation with respect to *existing* letters of credit and customer agreements, the Commission proposed a transition period of one year from the effective date until § 1.43 will apply to existing letters of credit and customer agreements.

CME supported this one-year transition period. By contrast, SIFMA AMG/MFA urged the Commission to shorten it in the interest of investor protection. They asked how letters of credit would be treated if an FCM were to go into bankruptcy during the transition period?

The provisions in this rulemaking regarding letters of credit are intended to codify the Commission's longstanding policy that ''customers using a letter of credit to meet original margin obligations [sh]ould be treated no differently than customers depositing other forms of non-cash margin or customers with excess cash margin deposits.'' [150] This is the policy that has been advanced by the Commission, including in litigation,[151] under the current rules. Moreover, this policy is supported by the provision in revised § 190.04(d)(3)(ii) that, for a letter of credit posted as collateral, ''the trustee shall treat any portion that is not drawn upon (less the value of any substitute customer property delivered by the customer) as having been distributed to the customer for purposes of calculating entitlements to distribution or transfer.'' That provision is not subject to the one-year transition period.

While the Commission will decline to shorten the one-year transition period for existing letters of credit, trustees will be expected to treat such letters of credit in accordance with the Commission's policy.

The provision proposed as § 190.10(e) concerns the disclosure statement for non-cash margin. No comments were received specific to this provision.

[147] *See* § 190.06 regarding the making and taking of deliveries during bankruptcy.

[148] CME again recommended that the Commission consider adopting customer protection requirements with respect to delivery accounts via a separate rulemaking.

[149] The Joint Audit Committee (''JAC'') forms for an Irrevocable Standby Letter of Credit (both Pass-Through and Non Pass-Through) appear to be consistent with the requirements of § 1.43.

[150] *See, e.g.,* 48 FR 8716, 8718 (March 1, 1983) (Adopting release for part 190); Proposal, 86 FR at 36019 & n. 103.

[151] *See, e.g.* Brief of the Commodity Futures Trading Commission In Support Of The Trustee's Motion To Confirm in *ConocoPhillips* v. *Giddens,* Case No. 1:12–cv–06014–KBF, Document 33.

As it sets forth obligations for an FCM during business as usual, it will be moved to part 1. This provision does fit under existing § 1.55 (Public disclosures by futures commission merchants), and will be added at the end, codified as § 1.55(p).

Accordingly, after consideration of the comments, and for the reasons stated above, § 190.10 will be adopted as proposed, with modifications: Proposed § 190.10(a) will be codified as § 190.10, proposed § 190.10(b) will be codified as § 1.41, proposed § 190.10(c) will be codified as § 1.42, proposed § 190.10(d) will be codified as § 1.43, and proposed § 190.10(e) will be codified as § 1.55(p).

C. Subpart C—Clearing Organization as Debtor

The Commission is adopting a new subpart C of part 190 (proposed §§ 190.11–190.19), with certain modifications discussed below, to address the currently unprecedented scenario of a clearing organization as debtor.[152]

The customers of a clearing organization are its members, considered separately in two roles: (1) Each member may have a proprietary (also known as ''house'') account at the clearing organization, on behalf of itself and its non-public customers (*i.e.,* affiliates). The property that the clearing organization holds in respect of these accounts is referred to as ''member property.'' (2) Each member may have one or more accounts (*e.g.,* futures, cleared swaps) for that members' public customers. The property that the clearing organization holds in respect of these accounts is referred to as ''customer property other than member property.'' Many clearing members will have both such types of accounts, although some may have only one or the other.

1. Regulation § 190.11: Scope and Purpose of Subpart C

The Commission is adopting § 190.11 as proposed, but designated as new paragraph (a), and adding a new paragraph (b), as set forth below. The Commission is adopting § 190.11 to establish that subpart C of part 190 will apply to proceedings under subchapter IV to chapter 7 of the Bankruptcy Code where the debtor is a clearing organization.

When originally proposing part 190 in 1981, the Commission proposed to (and ultimately did) forego providing generally applicable rules for the bankruptcy of a clearing organization.[153] The Commission explained that it had proposed no other rules with respect to the operation of clearing organization debtors—other than proposing that all open commodity contracts, even those in a deliverable position, be liquidated in the event of a clearing organization bankruptcy—because the Commission viewed it as highly unlikely that an exchange could maintain a properly functioning futures market in the event of the collapse of its clearing organization. The Commission noted that, under section 764(b)(2) of the Bankruptcy Code, it had the power to permit a distribution of the proceeds of a clearing organization liquidation free from the avoidance powers of the trustee. The Commission further explained that it was not proposing a general rule, because the bankruptcy of a clearing organization would be unique. Instead, the Commission was inclined to take a case-by-case approach with respect to clearing organizations, given the potential for market disruption and disruption of the nation's economy as a whole, in the case of a clearing organization bankruptcy, as well as the desirability of the Commission's active participation in developing a means of meeting such an emergency.[154]

Much has changed in the intervening 39 years. Markets move much more quickly, and thus the importance of quick action in respect to the bankruptcy of a clearing organization has increased. The Commodity Futures Modernization Act established DCOs as a separate registration category.[155] The bankruptcy of a clearing organization would remain unique—it remains the case that no clearing organization registered with the Commission has ever entered bankruptcy—and thus the need for significant flexibility remains, but the balance has shifted towards establishing *ex ante* the approach that would be taken.

Two clearing organizations for which the Commission has been designated the agency with primary jurisdiction have been designated as systemically important to the United States financial system pursuant to Title VIII of Dodd-Frank.[156] If any clearing organization were to approach insolvency, it is possible, though not certain, that such an entity would be resolved pursuant to Title II of Dodd-Frank.[157]

Administration of a resolution under Title II of Dodd-Frank depends, in part, on clarity as to entitlements under chapter 7 of the Bankruptcy Code. Specifically, section 210(a)(7)(B) of Dodd-Frank [158] provides with respect to claims against the covered financial agency in resolution, that ''a creditor shall, in no event, receive less than the amount that the creditor is entitled to under paragraphs (2) and (3) of subsection (d), as applicable.'' Tracing to the cross-referenced subsection, section 210(d)(2) [159] provides that the maximum liability of the FDIC to a claimant is the amount that the claimant would have received if the FDIC had not been appointed receiver, and (instead), the covered financial company had been liquidated under chapter 7 of the Bankruptcy Code.[160] Thus, it is important to have a clear ''counterfactual'' that establishes what creditors would be entitled to in the case of the liquidation of a clearing

[152] After considering comments that were received on the original Proposal, the Commission subsequently issued a Supplemental Proposal that withdrew § 190.14(b)(2) and (3), and proposed other revisions to § 190.14. Bankruptcy Regulations, 85 FR 60110 (Sept. 24, 2020).

[153] At the time, the definition of clearing organization in section 761(2) of the Bankruptcy Code was an ''organization that clears commodity contracts on, or subject to the rules of, a contract market or board of trade.'' *See* Public Law 95–598 (1978), 92 Stat 2549.

[154] 46 FR 57535, 57545 (Nov. 24, 1981).

[155] Commodity Futures Modernization Act of 2000 Public Law 106–554 section 1(a)(5); Appendix E, section 112(f).

[156] *See* Dodd-Frank section 804 (designation of systemic importance), section 803(8) (definition of ''supervisory agency''), 12 U.S.C. 5463, 5462(8). These are CME and ICE Clear Credit. A third clearing organization (Options Clearing Corporation) has also been so designated, but the SEC is the supervisory agency in that case.

[157] Resolution under Title II would require a recommendation concerning factors specified in section 203(a)(2) of Dodd-Frank, 12 U.S.C. 5383(a)(2), by a ⅔ majority of the members then serving of each of the Board of Governors of the Federal Reserve System and of the FDIC, followed by a determination concerning a related set of factors specified in section 203(b), 12 U.S.C. 5383(b), by the Secretary of the Treasury in consultation with the President. Thus, the choice of resolution versus bankruptcy for a DCO that is, in the terminology of Dodd-Frank, ''in default or in danger of default,'' *see* Dodd-Frank section 203(c)(4), 12 U.S.C. 5383(c)(4), cannot be considered certain.

It is, however, clear that Title II applies to clearing organizations. *See, e.g.,* Dodd-Frank section 210(m), 12 U.S.C. 5390(m) (applying ''the provisions of subchapter IV of chapter 7 of the bankruptcy code'' to ''member property'' of ''commodity brokers''). Pursuant to section 761(16) of the Bankruptcy Code, ''member property'' applies only to a debtor that is a ''clearing organization.'' 11 U.S.C. 761(16).

[158] 12 U.S.C. 5390(a)(7)(B).

[159] 12 U.S.C. 5390(d)(2).

[160] For the sake of completeness, it should be noted that section 210(d)(2), 12 U.S.C. 5390(d)(2), provides, as an additional comparator, ''any similar provision of State insolvency law applicable to the covered financial company.'' Given Federal regulation of DCOs, it would appear that this phrase is inapplicable. Similarly, section 210(d)(3), 12 U.S.C. 5390(d)(3), which refers to covered financial companies that are brokers or dealers resolved by SIPC, is also inapplicable here, given the inconsistency in being both a DCO and a broker-dealer.

organization under chapter 7 (subchapter IV) of the Bankruptcy Code.

Although the Commission believes that the potential—albeit unprecedented—scenario of a clearing organization as debtor would require significant flexibility, the Commission also believes it necessary and appropriate to establish an *ex ante* set of regulations for such a scenario.

The Commission requested comment regarding the proposed scope of subpart C, as set forth in proposed § 190.11. The Commission also specifically asked commenters whether they supported or opposed the establishment of an explicit, bespoke set of regulations for the bankruptcy of a clearing organization.

The Commission received two comments that raised concerns about how the proposed subpart C regulations would apply in the case of a debtor clearing organization that is organized and/or domiciled in a foreign country. SIFMA AMG/MFA commented that ''Part 190 should include a clear statement of public policy . . . that if an insolvency proceeding is commenced in respect of a DCO located outside the United States, such home country proceeding should take precedence over any case under the [U.S.] Bankruptcy Code.''

ICE commented that such a clearing organization, if insolvent, ''is likely to be subject to an insolvency proceeding in its home jurisdiction.'' ICE also commented that many such DCOs ''have significant assets (including for this purpose, the assets of clearing members and their customers.'' In particular, ICE stated that ''a foreign DCO may have, in addition to the customer account classes contemplated by the CEA and CFTC regulations (and the Part 190 regulations), one or more classes of customer accounts that are required to be segregated or separately accounted for under applicable foreign law, generally for the protection of foreign clearing members and their customers.'' ICE further commented that, ''[t]o the extent the Part 190 rules mandate a distribution scheme for property of the [DCO in bankruptcy] that would be inconsistent with foreign law applicable to the DCO, and that could disadvantage foreign members or their customers, significant conflicts may arise . . . .'' ICE suggested two alternative approaches for the Commission to consider: (1) The ''Commission could provide that the new Part 190 regulations would not apply to a foreign DCO;'' or (2) ''[a]lternatively, the Commission could provide that the new Part 190 regulations, including the distributional regime, would apply only to the separate customer account class structure provided for under U.S. law (futures, cleared swaps and foreign futures), to the extent carried through FCM clearing members.''

After considering the comments, the Commission is adopting § 190.11 with modifications. With respect to the protection of customer property in connection with foreign DCOs, the Commission has traditionally focused its efforts on the protection of the public customers of FCM members of such foreign DCOs. While protecting public customers of FCM members of foreign DCOs would not be well served by disapplying part 190 in the case of foreign DCOs, as suggested in ICE's first approach, as well as in the comment by SIFMA AMG/MFA, balancing the goal of protecting public customers of FCM members with the goal of mitigating conflict with foreign proceedings would appear to be supported by following ICE's second approach, and limiting the applicability of part 190, in the case of a foreign DCO subject to a proceeding in its home jurisdiction, to focus on the contracts and property of public customers of FCM members.

In order to balance the goal of protecting public customers of FCM members with the goal of mitigating conflict with foreign proceedings, the Commission believes it to be appropriate that, in a situation where a debtor clearing organization is organized outside the United States and is subject to a foreign bankruptcy proceeding, part 190 should apply as follows. First, the Commission believes it to be appropriate that subpart A should apply to such proceedings, given that those provisions set forth core concepts, definitions and general provisions. Second, the Commission believes it to be appropriate that § 190.12 should apply to such proceedings, given that the regulation sets forth requirements for records and reporting, which are critical in such proceedings. And third, the Commission believes it to be appropriate that three regulations should be applicable in a limited fashion, to focus on the contracts and property of public customers of FCM members:[161] (1) § 190.13, setting forth the prohibition on avoidance of transfers, but only with respect to futures and cleared swaps contracts cleared by FCM clearing members on behalf of their public customers; (2) § 190.17, setting forth the calculation of net equity; and (3) § 190.18, setting forth the treatment of property. In such a scenario, §§ 190.13, 190.17, and 190.18 would only apply with respect to: (1) Claims of FCM clearing members on behalf of their public customers; and (2) property that is or should have been segregated for the benefit of FCM clearing members' public customers, or that has been recovered for the benefit of FCM clearing members' public customers.

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is: (1) Adopting the language of § 190.11 as proposed, but designated as new paragraph (a); and (2) modifying proposed § 190.11 by adding the following as new paragraph (b): If the debtor clearing organization is organized outside the United States, and is subject to a foreign proceeding, as defined in 11 U.S.C. 101(23), in the jurisdiction in which it is organized, then only the following provisions of part 190 shall apply: (1) Subpart A; (2) § 190.12; (3) § 190.13, but only with respect to futures contracts and cleared swaps contracts cleared by FCM clearing members on behalf of their public customers and the property margining or securing such contracts; and (4) §§ 190.17 and 190.18, but only with respect to claims of FCM clearing members on behalf of their public customers, as well as property that is or should have been segregated for the benefit of FCM clearing members' public customers, or that has been recovered for the benefit of FCM clearing members' public customers.''

2. Regulation § 190.12: Required Reports and Records

The Commission is adopting § 190.12 to establish the recordkeeping and reporting obligations of a debtor clearing organization and/or trustee in a bankruptcy proceeding under subpart C.

The operations of a clearing organization are extremely time-sensitive. For example, § 39.14 requires that a clearing organization complete settlement with each clearing member at least once every business day. It is thus critical that the Commission receive notice of a DCO bankruptcy in an extraordinarily rapid manner. Similarly, the trustee that is appointed (as well as the Commission) must receive critical documents rapidly, and proper notice should be provided to the DCO's members.

Regulation § 190.12 sets forth the timing and content of notices that must be provided to the Commission and the DCO's members, as well as the timing and content of reports and records that

[161] As noted above, the Commission has traditionally focused its efforts on the protection of the public customers of FCM members of such foreign DCOs. In a DCO bankruptcy, the Commission believes that the application of these three regulations would be critical to fulfilling the agency's mission to protect customers.

must be provided to the Commission and trustee.

Section 190.12(a)(1) is analogous to § 190.03(a), as amended herein, in that it would provide instructions regarding how to give notice to the Commission and to a clearing organization's members, where such notice would be required under subpart C of part 190.[162] Section 190.12(a)(2) would require the clearing organization to notify the Commission either in advance of, or at the time of, filing a petition in bankruptcy (or within three hours of receiving notice of a filing of an involuntary petition against it).[163] Notice would need to include the filing date and the court in which the proceeding has been or will be filed. While the clearing organization would also need to provide notice of the docket number, if the docket number is not immediately assigned, that information would be provided separately as soon as available.

It is also important to permit the trustee to begin to understand the business of the clearing organization as soon as practicable, and within hours. Accordingly, § 190.12(b)(1) requires the clearing organization to provide to the trustee copies of each of the most recent reports filed with the Commission under § 39.19(c), which includes § 39.19(c)(1) (daily reports, including initial margin required and on deposit by clearing member, daily variation and end-of-day positions (by member, by house and customer origin), and other daily cash flows), § 39.19(c)(2) (quarterly reports, including of financial resources), § 39.19(c)(3) (annual reporting, including audited financial statements and a report of the chief compliance officer), § 39.14(c)(4) (event-specific reporting, which would include the most up-to-date version of any recovery and wind-down plans the debtor maintained pursuant to § 39.39(b),[164] and which may well include events that contributed to the clearing organization's bankruptcy), and § 39.19(c)(5) (reporting specially requested by the Commission or, by delegated authority, staff). In order to provide the trustee with an initial overview of the business and status of the clearing organization, with respect to quarterly, annual, or event-specific reports, the clearing organization would be required to provide any such reports filed during the preceding 12 months. These reports would need to be provided to the trustee as soon as practicable, but in any event no later than three hours following the later of the commencement of the proceeding or the appointment of the trustee. It is the Commission's expectation that in the event of an impending bankruptcy event, staff at the DCO would, as soon as practicable, be preparing these materials for transmission to the trustee.

Similarly, § 190.12(b)(2) requires the debtor clearing organization, in the same time-frame, to provide the trustee and the Commission with copies of the default management plan and default rules and procedures maintained by the debtor pursuant to § 39.16 and, as applicable, § 39.35. While some of this information may have previously been filed with the Commission pursuant to § 39.19, it is important that the Commission have readily available what the clearing organization believes are the most up-to-date versions of these documents. Moreover, given that these documents must be provided to the trustee, providing copies to the Commission should impose minimal additional burden (particularly if the documents are provided in electronic form).

Regulation § 39.20(a) requires a DCO to maintain records of all activities related to its business as such, and sets forth a non-exclusive list of the records that are included in that term. To enable the trustee and the Commission further to understand the business of the clearing organization, § 190.12(c) requires the debtor clearing organization to make copies of such records available to the trustee and to the Commission no later than the business day after the commencement of the proceeding. In order to inform the trustee and the Commission better concerning the enforceability in bankruptcy of the clearing organization's rules and procedures, the clearing organization is similarly required to make available any opinions of counsel or other legal memoranda provided to the debtor, by inside or outside counsel, in the five years preceding the commencement of the proceeding, relating to the enforceability of those arrangements in the event of an insolvency proceeding involving the debtor.[165]

The Commission requested comment with respect to all aspects of proposed § 190.12. The Commission raised specific questions as to whether the reports and records identified in proposed § 190.12 to be provided to the Commission are useful and appropriate, and whether additional reports and records should be included. The Commission also asked if the proposed time deadlines are appropriate.

The Commission received two comments on proposed § 190.12.

CME expressed support for proposed § 190.12, and agreed with the Commission that ''the reports and records identified in [the proposed regulation] would be useful for the trustee and the Commission.'' CME also agreed with the Commission that certain items, such as the DCO's default rules and recovery and wind-down plans, should be furnished as soon as possible.

OCC ''generally support[ed] a requirement for a DCO to provide a trustee and the Commission with information they need for efficient resolution of the DCO,'' recognizing that ''time would be of the essence in such a proceeding.'' OCC also noted that, because the ''information is periodically reported to, or filed with, the Commission,'' OCC did not ''foresee any challenge in identifying and providing this information without delay.'' However, OCC requested that proposed § 190.12(b) be amended to require a DCO to provide the information delineated therein ''as soon as practicable.'' OCC ''believe[d] that a specific deadline of three hours is overly prescriptive.''

After considering the comments, the Commission is adopting § 190.12 as proposed. As the commenters observed, the information specified in § 190.12 is

[162] While § 190.03(a)(2), as amended herein, applies to notice to an FCM's customers, and § 190.12(a)(1)(ii) applies to notice to a clearing organization's members, the means of giving notice are identical. For a discussion of how these notice provisions differ from the prior iteration of part 190, please refer to the discussion of § 190.03(a) above.

[163] Commodity broker bankruptcies are rare, and outside the experience of most chapter 7 trustees, who are chosen from a panel of private trustees eligible to serve as such for all chapter 7 cases. *See generally* 11 U.S.C. 701(a)(1), 28 U.S.C. 586(a)(1). Historically, Commission staff, on being notified of an impending commodity broker bankruptcy, have worked with the office of the relevant regional United States Trustee, *see generally* 28 U.S.C. 581 *et seq.,* to identify, and have then briefed, the chapter 7 trustee that would then be appointed. This would be even more important in the context of a clearing organization bankruptcy.

[164] *See* § 39.19(c)(4)(xxiv).

[165] The trustee of a corporation in bankruptcy controls the corporation's attorney-client privilege for pre-bankruptcy communications. *Commodity Futures Trading Comm'n* v. *Weintraub,* 471 U.S. 343 (1985). Production to the Commission pursuant to the proposed regulation would not waive that privilege (although voluntary production would). *See, e.g., U.S.* v. *de la Jara,* 973 F.2d 746, 749 (9th Cir. 1992) (''a party does not waive the attorney-client privilege for documents which he is *compelled* to produce'') (emphasis in original); Office of Comptroller of the Currency Interpretative Letter, 1991 WL 338409 (with respect to ''internal Bank documents'' that are ''subject to the attorney-client privilege'' and are ''requested by OCC examiners for their use during examinations of the Bank,'' OCC ''has the power to request and receive materials from national banks in carrying out its supervisory duties. It follows that national banks must comply with such requests. That being the case, it is our position that when national banks furnish documents to us at our request they are not acting voluntarily and do not waive any attorney-client privilege that may attach to such documents.'').

important for the trustee and the Commission, and time would be of the essence in a DCO bankruptcy. Moreover, the prescribed task in § 190.12 is to gather and transmit documents that already exist, rather than to generate new information. The documents to be sent to the trustee are documents that were recently sent to the Commission, and the documents to be sent to the trustee and to the Commission are documents that one would expect, as the commenter noted, to be readily accessible. In this context, the Commission believes that a deadline of ''as soon as practicable and in any event no later than three hours following the commencement of the proceeding'' (or, where appropriate, the appointment of the trustee) is reasonable and will set clear expectations for relevant parties that will facilitate DCOs' contingency planning.

Accordingly, after consideration of the comments, and for the reasons stated above, the Commission is adopting § 190.12 as proposed.

3. Regulation § 190.13: Prohibition on Avoidance of Transfers

The Commission is adopting § 190.13 as proposed, to implement section 764(b) of the U.S. Bankruptcy Code, protecting certain transfers from avoidance (sometimes referred to as ''claw-back'') with respect to a debtor clearing organization. Regulation § 190.13 is analogous to new § 190.07(e) (and current § 190.06(g)), with certain changes. Specifically, while § 190.07(e) allows FCM transfers unless they are explicitly disapproved by the Commission, § 190.13 requires explicit Commission approval for DCO transfers. The difference in approach is rooted in the inherent difference between FCM transfers and DCO transfers: Whereas an FCM is capable of transferring only a portion of its customer positions, a DCO would be expected to transfer all of its customer positions (or at least all positions in a given product set) simultaneously in order to maintain a balanced book. Given the importance of transferring all open commodity contracts—and the property margining such contracts—in the event of a DCO bankruptcy, the Commission believes that any such transfer should require explicit Commission approval, either before or after such transfer.

Thus, whereas § 190.07(e)(1) provides that a pre-relief transfer by a clearing organization cannot be avoided as long as it is *not disapproved* by the Commission, § 190.13(a) instead provides that a pre-relief transfer of open commodity contracts and the property margining or securing such contracts cannot be avoided as long as it was *approved* by the Commission, either before or after such transfer. Similarly, whereas § 190.07(e)(2)(i) provides (for all commodity brokers, including clearing organizations) that a post-relief transfer of a customer account cannot be avoided as long as it is *not disapproved* by the Commission, § 190.13(b) instead provides that a post-relief transfer of open commodity contracts and the property margining or securing such contracts made to another clearing organization cannot be avoided as long as it was *approved* by the Commission, either before or after such transfer.

The Commission requested comment with respect to all aspects of proposed § 190.13, and in particular, the Commission asked whether commenters agreed with the proposed approach of requiring explicit Commission approval of transfers by debtor DCOs.

The Commission received one comment on proposed § 190.13. CME expressed support for proposed § 190.13, particularly the allowance for Commission approval of transfers after such transfers have occurred. CME noted that porting customer positions to a DCO would be the preferred course of action in a bankruptcy, and a DCO may need to act quickly.

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.13 as proposed.

4. Regulation § 190.14: Operation of the Estate of the Debtor Subsequent to the Filing Date

The Commission is adopting § 190.14 as proposed, with certain modifications discussed below.

Section 190.14(a) provides discretion to the trustee to design the proof of claim form and to specify the information that is required. The Commission believes that broad discretion is appropriate in this context, given the bespoke nature of a clearing organization bankruptcy.

Section 190.14(b) addresses the operation of a debtor clearing organization in bankruptcy and provides that, after the order for relief, the DCO shall cease making calls for either variation or initial margin.

As originally proposed, § 190.14(b) included additional provisions that were intended to provide a brief opportunity, after the order for relief, to enable paths alternative to liquidation—that is, resolution under Title II of the Dodd-Frank Act, or transfer of clearing operations to another DCO—in cases where a short delay (*i.e.,* less than or equal to six days) might facilitate such an alternative path. Subsequent to the issuance of the Proposal, the Commission received several comments on proposed § 190.14(b), and based on its consideration of those comments, the Commission determined it to be appropriate to issue the Supplemental Proposal. The Supplemental Proposal modified proposed § 190.14(b) in several respects, including the withdrawal of proposed § 190.14(b)(2) and (3) and the new proposal of an alternative approach.[166] Further discussion of the Supplemental Proposal, including the Commission's consideration of comments received in response to the Supplemental Proposal, is set forth in section II.H below.

Section 190.14(c)(1) requires the trustee to liquidate, no later than seven calendar days after the order for relief, all open commodity contracts that had not earlier been terminated, liquidated or transferred. However, in the Proposal, paragraph (c)(1) also provided that such liquidation would not be required if the Commission (whether at the request of the trustee or *sua sponte*) determined that such liquidation would be inconsistent with the avoidance of systemic risk[167] or, in the expert judgment of the Commission, would not be in the best interests of the debtor clearing organization's estate.[168] In such a situation, the trustee would be directed to carry out such liquidation in accordance with the rules and procedures of the debtor clearing

[166] In withdrawing proposed § 190.14(b)(2) and (3), the Commission determined, after considering the comments, that those provisions would not be a practicable and effective way to foster the transfer of clearing operations—to the extent that such an opportunity presents itself—at an acceptable cost. The Commission also endeavored to propose (in the Supplemental Proposal) a more cost-effective alternative to foster the resolution of a DCO—in particular, a systemically important DCO—under Title II of the Dodd-Frank Act. Specifically, as set forth in the Supplemental Proposal, the Commission proposed ''a limited revision to the Proposal that would (1) stay the termination of SIDCO contracts for a brief time after bankruptcy in order to foster the success of a Title II Resolution, if the FDIC is appointed receiver in such a Resolution within that time, but (2) do so in a manner that does not undermine the QMNA status of SIDCO rules.''

The Commission sought comment on the Supplemental Proposal, and in particular, whether the new approach could reasonably be expected to achieve the Commission's stated goals, would be feasible, would be the best design for such a solution, and appropriately reflected consideration of benefits and costs.

[167] *See* section 3(b) of the CEA, 7 U.S.C. 5(b) (''It is the purpose of [the CEA] . . . to ensure . . . the avoidance of systemic risk . . . .'').

[168] *See* section 20(a)(3) of the CEA, 7 U.S.C. 24(a)(3) (''Notwithstanding title 11 . . . , the Commission may provide, with respect to a commodity broker that is a debtor . . . [,] the method by which the business of such commodity broker is to be conducted or liquidated after the date of the filing of the petition . . . .'').

organization, to the extent applicable and practicable.[169]

Section 190.14(c)(2) permits the trustee to make distributions to members in the form of securities that are equivalent (*i.e.,* securities of the same class and series of an issuer) to those that were originally delivered to the debtor by the clearing member or such member's customer, rather than liquidating securities and making distributions in the form of cash. Section 190.14(c)(2) is analogous to § 190.09(d)(3), discussed above in section II.B.7.

Section 190.14(d) requires the trustee to use reasonable efforts to compute the funded balance of each customer account immediately prior to the distribution of any property in the account, ''which shall be as accurate as reasonably practicable under the circumstances, including the reliability and availability of information.'' Section 190.14(d) is analogous to § 190.05(b), discussed above in section II.B.3, but is modified for the context of a DCO bankruptcy. Similar to § 190.05(b), the Commission's objective in § 190.14(d) is to provide the bankruptcy trustee with the latitude to act reasonably, given the circumstances they are confronted with, recognizing that information may be more reliable and/or accurate in some insolvency situations than in others. However, at a minimum, the trustee is required to calculate each customer's funded balance prior to distributing property, to achieve an appropriate allocation of property between customers.

The Commission requested comment with respect to all aspects of proposed § 190.14. The Commission also raised specific questions regarding § 190.14(b)(2).[170] The comments received in response to those specific questions on § 190.14(b)(2) have already been considered by the Commission in the Supplemental Proposal, wherein the Commission ultimately withdrew § 190.14(b)(2) and (3). Although such comments on the Proposal relate to proposed paragraphs that were withdrawn in the Supplemental Proposal, the comments relating to proposed § 190.14(b)(2) and (3) nonetheless are noted below.[171]

The Commission received some comments that related to § 190.14 generally. ICI commented in favor of the requirement proposed in § 190.14 that ''any decision to continue operating a DCO in liquidation must be made with [the Commission's] input and consent.'' ICI asserted, however, that the Commission should only approve an application from a trustee to continue operating a DCO in liquidation if the Commission determines that the trustee ''has the knowledge and experience to manage such operations.'' Noting that the continued operation of a DCO has the potential to result in significant continued losses for customers and exacerbate stress, ICI further asserted that, ''[i]n considering whether to grant a request to allow a failed DCO to continue operating, the Commission should consider the potential harm to customers and should request input from both DCO members and customers.'' OCC commented that additional considerations should be considered in determining ''whether continued operation of a DCO in bankruptcy would be practical.'' Specifically, OCC stated that ''a DCO may . . . maintain contractual arrangements with various counterparties . . . that are necessary for the DCO's continued operation,'' such as contract markets and other trade sources, other DCOs, banking and liquidity providers, and information technology vendors). OCC asserted that ''a trustee would need to review the DCO's recovery and wind-down plan[s] and/or consult with a DCO to determine whether such arrangements necessary for the DCO's continued operation would—or could—be terminated [by the counterparties] upon the DCO's entry into bankruptcy and, if so, determine whether the counterparties . . . would continue to provide those necessary services for a period of time.''

The Commission also received comments on § 190.14(a). CME commented in support of paragraph (a). ICE commented that § 190.14(a) did not clearly account for ''non-CFTC-regulated clearing or other activity occurring at a DCO, including security-based swaps and other securities, cleared forward contracts or spot contracts to the extent such instruments are not carried in a CFTC regulated futures or swap account.'' ICE recommended that while ''such activity may be outside the scope of the Part 190 regulations, claims of members with respect to such activity, whether for their proprietary or customer accounts, need to be properly accounted for in a DCO's bankruptcy and should not be disadvantaged.''

Several commenters expressed concern that proposed § 190.14(b) would inadvertently create legal uncertainty with respect to the enforceability of a DCO's close-out netting rules and related issues, and requested that the Commission address these concerns in varying ways.

ICE did not object to proposed § 190.14(b), but believed that the Commission ''should clarify that the rule does not interfere with either the automatic termination of contracts upon insolvency or clearing member rights to terminate contracts upon insolvency.'' Noting ''that clearing member capital and accounting often take into account the ability of a clearing member to terminate, or the automatic termination of, its cleared positions in the event of a clearinghouse insolvency,'' ICE asserted that it would be important that the final rules ''not upset settled expectations of clearing members'' in this regard. ICE further noted that ''automatic termination is common,'' and thus, continuing the operations of a clearinghouse after insolvency would likely be infeasible, in practice.

CME requested that the Commission add a provision to § 190.14 stating that: ''if the Commission permits the trustee to continue to operate the DCO, that the action is not in derogation of, and clearing members fully retain and may exercise, their right under the DCO's rules and procedures with respect to close-out netting.'' CME stated that ''[s]ome have expressed concern that proposed Regulation 190.14 creates uncertainty around the enforceability of close-out netting rules if the trustee is allowed to continue the DCO's operations under the conditions as drafted.'' CME asserted that it would be ''critical that any decision to continue to operate the DCO not be contrary to the DCO's rules or be construed in any way to abrogate clearing members' close-out netting rights under the rules.'' CME noted that the enforceability of close-out rights is of ''paramount importance'' to clearing members as part of their contract with the DCO, and that CME and other DCOs have obtained detailed legal analyses on the enforceability of their close-out netting rules and other features of their default rules to assure clearing members of their rights. CME commented that it did not believe that

[169] As discussed below, § 190.14(c)(1) is being modified to remove language that commenters stated would raise uncertainties concerning the enforceability of close-out netting provisions in a DCO bankruptcy.

[170] In particular, the Commission asked about the framing of the concepts of usefulness and practicability in the context of permitting the trustee to continue to operate a DCO in insolvency, in accordance with proposed § 190.14(b)(2), in order to facilitate the transfer of clearing operations to another DCO or placing the debtor DCO into resolution pursuant to Title II of the Dodd-Frank Act. The Commission also asked whether there is a better way to frame either of those terms, and whether it is appropriate to provide for the possibility that the trustee may be permitted to delay liquidating contracts.

[171] For further discussion of the Supplemental Proposal and the Commission's consideration of comments received thereto, see section II.H below.

proposed § 190.14 would create an issue with respect to its own close-out netting rules or netting opinions, because its own rules ''would compel termination of open contracts upon a CME bankruptcy event and, thus the conditions of Regulation 190.14(b) would not be satisfied and the trustee could not continue CME's DCO operations.'' Nonetheless, CME speculated that other DCOs ''could potentially have rules that permit a clearing member to terminate open positions at their discretion without compelling termination.''

ISDA supported the provision in proposed § 190.14(b) that would ''prevent the trustee from continuing operation of the DCO subsequent to the order for relief if the DCO's rules contain closeout netting provisions.'' However, ISDA also recommended that the Commission modify proposed § 190.14(c)(1) to delete the second sentence and amend the first sentence to affirmatively provide that: ''notwithstanding anything else to the contrary in Subpart C, the trustee shall liquidate all open contracts in accordance with the close-out needing provisions in the DCO's rules (or bylaws) and, in any event, no later than seven calendar days after the entry of the order for relief.'' ISDA commented that it is ''critical'' that ''all aspects of [the] Part 190 regulations . . . support, and in no event be inconsistent with, . . . exposure netting.'' ISDA noted that ''[e]nforceable close-out netting rights provide the legal basis for netting of exposures between derivative counterparties, which reduces costs, increases market liquidity and reduces credit and systemic risks.'' ISDA stated that a ''firm's right to terminate outstanding transactions with a counterparty following an event of default and calculate the net amount due to one party by another is the primary means of mitigating credit risks associated with financial contracts.'' ISDA further argued that, [w]ithout enforceable close-out netting rights, firms would need to manage their credit risk on a gross basis, dramatically reducing liquidity and credit capacity.''

OCC commented that ''the Commission should continue to consult with DCOs and market participants who rely on closeout netting opinions to ensure that the proposed rules[, including proposed § 190.14(b)(2),] do not raise uncertainty related to the enforceability of DCOs' closeout netting rules or have other unintended consequences.''

FIA commented that proposed § 190.14(b)(2) and proposed § 190.14(c) are ''fundamentally flawed and should not be adopted.'' FIA raised concerns that those provisions may inadvertently create ''an unacceptable level of legal uncertainty related to the enforcement of closeout netting provisions'' set out in DCO rulebooks, which all but four DCOs maintain. FIA asserted that, if proposed § 190.14(b)(2)(ii)(A) ''could be read to provide the trustee some level of discretion to determine whether or when DCO rules may 'compel' the termination of contracts, such discretion, in turn, may call into question whether the DCO's rules constitute a 'qualifying master netting agreement' as described in the rules of the several bank regulatory authorities.'' FIA also commented that the ''continued operation of a DCO after an order for relief would be ill-advised'' and impracticable. FIA stated that a trustee with no familiarity or understanding of central clearing would be highly unlikely to be able to manage effectively the operation of a bankrupt DCO. In the case of SIDCOs, FIA noted that ''the prospect of a bankruptcy trustee operating the DCO for even a brief interim period prior to commencement of Title II [resolution] proceedings could result in a loss of market confidence and a destabilizing rush to exit by clearing members and their clients, [thereby] potentially frustrat[ing] the successful resolution of the DCO.'' In the case of other DCOs, FIA commented that ''the post-filing transfer of . . . clearing operations to another DCO would be difficult at best,'' and ''clearing members and their clients should not be expected to take the execution risk of being forced to continue clearing through a bankrupt DCO when successful completion of a transfer to a new DCO in bankruptcy is not certain.'' FIA also stated its belief that ''non-defaulting clearing members or their clients would be [unwilling] to continue to pay margin to the estate of a bankrupt DCO.''

The ABA Subcommittee requested that the Commission revise proposed § 190.14(b) ''to clarify that the DCO's close-out netting rules remain in effect and are enforceable as written, notwithstanding any decision under [proposed §] 190.14(b) by the Commission to allow the trustee to continue making calls for variation settlement and margin.'' The ABA Subcommittee raised a concern that proposed § 190.14(b) ''may create unintended ambiguity'' regarding the enforceability of such rules.

After considering the comments, the Commission is adopting § 190.14(a) as proposed. The Commission notes that § 190.14(a) provides that the trustee shall ''instruct each customer [a term that, in the context of a debtor DCO, includes members] to file a proof of claim containing such information as is deemed appropriate by the trustee.'' To the extent that the DCO is conducting non-CFTC-regulated activity that is outside the scope of the part 190 regulations, the proof of claim form should include an opportunity to claim for debts of the DCO related to activity that is not regulated by the CFTC. These would be payable from the general estate (outside of customer property) or, if secured, from the property securing the debts. Thus, such activity will be properly accounted for in the DCO bankruptcy, and members will not be disadvantaged. For those reasons, the Commission does not believe that § 190.14(a) should be modified in the manner recommended by ICE.

The Commission is adopting § 190.14(b)(1) as proposed, with two modifications that reflect the Commission's previous withdrawal of paragraphs (b)(2) and (3) in the Supplemental Proposal: (1) Proposed paragraph (b)(1) is re-designated as paragraph (b); and (2) new paragraph (b) is modified to remove the phrase: ''except as otherwise explicitly provided in this paragraph (b).'' [172]

Several commenters expressed concern that proposed § 190.14(b) inadvertently creates legal uncertainty with respect to the enforceability of a DCO's close-out netting rules and requested that the Commission address this concern in varying ways.[173] The Commission considered those comments in advance of issuing the Supplemental Proposal, and determined that § 190.14(b)(2) and (3) would not be a practicable and effective way to foster the transfer of clearing operations—to the extent that such an opportunity presents itself—at an acceptable cost. Consequently, the Commission withdrew § 190.14(b)(2) and (3) in the Supplemental Proposal and instead proposed an alternative approach. The Supplemental Proposal, including the Commission's consideration of comments thereto, is discussed below in section II.H of this adopting release.

Commenters' concerns regarding the legal uncertainty of close-out netting rules in the context of § 190.14(b) also apply to § 190.14(c), as proposed, specifically the language that states that the trustee shall liquidate all open positions no later than seven calendar days after the order for relief ''unless the

[172] *See* 85 FR at 60112 n.12 (''The Commission will make appropriate edits to the language in proposed § 190.14(b)(1) as part of the process of finalizing the [p]art 190 rule proposal.'').

[173] *See* comment letters from ICE, CME.

Commission determines that liquidation would be inconsistent with the avoidance of systemic risk or would not be in the best interests of the debtor's estate'' (the ''Unless Clause''). Some commenters—including FIA and ISDA—explicitly raised this issue in the context of § 190.14(c), to the extent that the proposed language would afford the trustee with some level of discretion to determine whether or when a DCO rule may ''compel'' the termination of contracts. Although the Commission believes that commenters' concerns were largely addressed in the Supplemental Proposal through the withdrawal of § 190.14(b)(2) and (3), the Commission agrees that the Unless Clause raises similar concerns, in that it suggests that the Commission may decide that a DCO's contracts should not be terminated in bankruptcy, and accordingly that paragraph (c)(1) should be modified by removing the Unless Clause. Thus, after considering the comments, the Commission is adopting § 190.14(c) as proposed, with a modification to paragraph (c)(1) by deleting the phrase: ''unless the Commission determines that liquidation would be inconsistent with the avoidance of systemic risk or would not be in the best interests of the debtor's estate.'' This modification—when taken in conjunction with the Commission's prior withdrawal of § 190.14(b)(2) and (3)—should remove any lingering uncertainties in § 190.14 concerning the enforceability of close-out netting provisions in a DCO bankruptcy.

The Commission received no specific comments on the proposed language of § 190.14(d) and, thus, is adopting that paragraph as proposed.

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.14 as proposed, with the deletion of paragraphs (b)(2) and (3) and modifications to paragraphs (b)(1) and (c)(1), as set forth above.[174]

5. Regulation § 190.15: Recovery and Wind-Down Plans; Default Rules and Procedures

The Commission is adopting § 190.15 substantially as proposed (with a modification, as discussed below), to favor the implementation of a debtor clearing organization's default rules and procedures maintained pursuant to § 39.16 and, as applicable, § 39.35, and any recovery and wind-down plans maintained by the debtor and filed with the Commission, pursuant to §§ 39.39 and 39.19, respectively. Section 39.16 requires each DCO to, among other things, ''adopt rules and procedures designed to allow for the efficient, fair, and safe management of events during which clearing members become insolvent or default on the obligations of such clearing members to the'' DCO. In adopting § 39.35, the Commission explained that it ''was designed to protect SIDCOs, [s]ubpart C DCOs, their clearing members, customers of clearing members, and the financial system more broadly by requiring SIDCOs and [s]ubpart C DCOs to have plans and procedures to address credit losses and liquidity shortfalls beyond their prefunded resources.''[175] Similarly, in adopting § 39.39, the Commission explained that it was ''designed to protect the members of such DCOs and their customers, as well as the financial system more broadly, from the consequences of a disorderly failure of such a DCO.''[176]

Section 190.15(a) states that the trustee shall not avoid or prohibit any action taken by the debtor DCO that was reasonably within the scope of, and was provided for, in any recovery and wind-down plans maintained by the debtor and filed with the Commission, subject to section 766 of the Bankruptcy Code. The Commission's intent is to provide finality and legal certainty to actions taken by a DCO to implement its recovery and wind-down plans, which are developed subject to Commission regulations.

Section 190.15(b) instructs the trustee to implement, in consultation with the Commission, the debtor DCO's default rules and procedures maintained pursuant to § 39.16, and, as applicable, § 39.35, as well as any termination, close-out and liquidation provisions included in the rules of the debtor, subject to the trustee's reasonable discretion and to the extent that implementation of such default rules and procedures is practicable.

Similarly, § 190.15(c), as proposed, instructs the trustee, in consultation with the Commission, to take actions in accordance with any recovery and wind-down plans maintained by the debtor and filed with the Commission, to the extent reasonable and practicable. The Commission's intent is to provide the trustee, who will need to take prompt action to manage the DCO (and any member default), with a roadmap to manage such action. The Commission further intends that the roadmap be based on the rules, procedures, and plans that the DCO has developed in advance, and that are subject to the requirements of the Commission's regulations.

The Commission requested comment with respect to all aspects of proposed § 190.15. The Commission also raised specific questions as to whether it is appropriate to steer the trustee towards implementation of the debtor DCO's default rules and procedures and recovery and wind-down plans, and whether the proposed language concerning discretion, reasonability, and practicability is appropriate and sufficient.

The Commission received several comments on proposed § 190.15. CME and ICE generally supported the proposal, although ICE raised concerns about the discretion afforded to the trustee. In contrast, Vanguard, FIA, ACLI, SIFMA AMG/MFA, and ICI expressed concerns with the proposed rule, in whole or in part.

ICE, while generally supporting the proposal, objected to the language in § 190.15 that a ''trustee's obligation to [follow a DCO's default rules and recovery and wind-down plans] is 'subject to the reasonable discretion' of the trustee or is limited 'to the extent reasonable and practicable.' '' While ICE acknowledged ''the need for some degree of flexibility in the conduct of a bankruptcy proceeding,'' it contended that ''the Commission should make clear that the trustee cannot override the DCO rules . . . [or] deviate from an approved recovery or wind-down plan.''

Vanguard requested that proposed § 190.15(a) be removed, arguing that it would be ''imprudent to give deference'' to a DCO's rules because such rules ''do not set forth a comprehensive roadmap to dealing with DCO insolvency.'' Vanguard noted that ''DCO rulebooks set forth a variety of powers the DCO may employ'' (*e.g.,* ''assessments, variation margin gains haircutting, and tear-ups''), and that such rules ''lack [the] necessary specificity and detail to provide certainty to FCMs and customers, or to the trustee,'' with respect to what would follow in DCO insolvency. Vanguard was concerned that such uncertainty may ''contribute to further market stresses during a critical time,'' and that expressly instructing the trustee to implement a DCO's default rules and procedures ''where practicable,'' permits a DCO to ''override the fundamental customer protections intended by Part 190.''

[174] The modifications to paragraph (b)(1) include both the addition of the language described above and the re-designation of proposed paragraph (b)(1) as new paragraph (b), in light of the withdrawal of proposed paragraphs (b)(2) and (3) in the Supplemental Proposal.

For further discussion of the Supplemental Proposal and the Commission's consideration of comments thereto, see section II.H below.

[175] 78 FR 72476, 72492 (Dec. 2, 2013).

[176] *Id.* at 72494.

FIA did not support the adoption of proposed § 190.15(b) and (c), commenting that the proposal's post-bankruptcy implementation of all DCO default rules and procedures and recovery and wind-down plans is ''inappropriate.'' FIA was concerned that the proposal's ''concept of 'default rules and procedures' could encompass a number of different tools or actions, some of which would be inappropriate and risky for a bankruptcy trustee to attempt to execute.'' In addition, ''to the extent that the Commission would select some but not other default rules and procedures for a trustee to implement,'' uncertainty with respect to possible bankruptcy scenarios would increase. FIA stated that a DCO's default rules and procedures should not be used ''for any purpose other than to ensure enforcement of a DCO's closeout netting provisions,'' and that, ''[b]y their terms, the default rules and procedures . . . represent contractual arrangements between a DCO and its members whose purpose is to provide resources and tools to the DCO to *prevent* its bankruptcy.'' FIA argued that ''a fundamental term'' of these arrangements is that ''such resources and tools are only available *prior* to bankruptcy,'' and that instructing a trustee in bankruptcy to implement, with discretion, the DCO's default rules and procedures would ''undermine the long-standing and settled expectations of DCOs and their members.'' In the alternative, FIA recommended that the Commission revise proposed § 190.15(b) ''to confirm that, in administering a proceeding under Subpart C, the trustee must implement any termination, close-out and liquidation provisions included in the rules (or bylaws) of the debtor'' (including loss allocation provisions). FIA raised further concerns about the treatment of a DCO's recovery plans in proposed § 190.15. FIA asserted that such plans are intended to address ''actions to be taken prior to the DCO's bankruptcy and [are] not relevant post-filing.'' FIA also stated that such plans ''would provide no meaningful guidance to a trustee'' because they ''do not prescribe a particular course of action.'' Rather, they ''present a menu of options that a DCO might consider.'' FIA asserted that reliance on a DCO's recovery and wind-down plans is ''particularly inappropriate'' because some of them ''have been developed with no input or opportunity for comment by clearing members and other market participants.''

ACLI also expressed concern with the deference that a trustee in bankruptcy would be required to afford a DCO's rules and procedures and recovery and wind-down plans under proposed § 190.15(a) and (c). ACLI claimed that ''DCO recovery and wind-down plans include such drastic measures as Variation Margin Gains Haircutting . . . and Partial Tear-Up . . . [that] are not subject to routine public input at the DCO level or at the Commission.'' ACLI identified several circumstances in which deference to the DCO's rules or recovery and wind-down plans should be reduced. ACLI asserted that: (a) A trustee should not be expected to defer to recovery and wind-down measures unless they were originally adopted with public input at the DCO level and made public for a reasonable period before the bankruptcy proceeding; (b) the trustee should ''have discretion to override a DCO's recovery or wind-down actions if they violate proposed [p]art 190's goal of protecting customer property on no worse than a *pro rata* basis''; and (c) consistent with proposed § 190.15(b), the trustee should be able to avoid or prohibit any DCO action that it determines, in consultation with the Commission, is not ''reasonable and practicable.''

SIFMA AMG/MFA commented that requiring a trustee to defer to a DCO's recovery and wind-down plans as set forth in proposed § 190.15(a) and (c) is ''inadvisable'' and, in some cases, ''unworkable,'' and recommended that the provisions be deleted. SIFMA AMG/MFA recommend that, if the Commission retains proposed § 190.15(a), the provision be amended to remove the words ''was reasonably in the scope of'' and replace references to the DCO's recovery and wind-down plans with references to the DCO's default rules and procedures. In support of their position, SIFMA AMG/MFA asserted that recovery and wind-down plans are insufficiently prescriptive, and that because they tend to be drafted as a menu of options, such plans are not likely to provide the trustee with clear direction, effectively causing the trustee to defer to the judgment of the debtor itself. SIFMA AMG/MFA also asserted that recovery and wind-down plans do not require Commission approval or reflect significant input from customers, and because DCOs are not required to make such plans public, the plans are not a fair reflection of the *ex ante* expectations of a DCO's stakeholders. SIFMA AMG/MFA further asserted that ''requiring the trustee . . . to defer to the debtor's resolution plans would be inconsistent with other regimes for the resolution of systemically important financial institutions.'' SIFMA AMG/MFA requested that the Commission add a new clause to proposed § 190.15 requiring the trustee and Commission, in implementing § 190.15, to ''consider whether implementation of the debtor's default rules and procedures [and recovery and wind-down plans] may undermine the core principles set forth in § 190.00 or may pose additional systemic risk.'' [177] If the trustee and Commission determine that such implementation would have that effect, SIFMA AMG/MFA suggested that the provision permit the trustee to override the rules, procedures, and plans. SIFMA AMG/MFA further commented that, in the event that deference to a DCO's default management rules and procedures and recovery and wind-down plans is mandated in subpart C of the proposal, the Commission should amend parts 39 and 40 of the Commission's regulations ''to ensure that customers have the opportunity to provide meaningful input during the development and application of such rules, procedures, and plans.''

ICI did not support the proposal's deference to a DCO's loss allocation, recovery, and wind-down rules in a DCO liquidation. ICI asserted that such rules are neither ''clear'' nor ''well-vetted.'' ICI stated that DCO rules ''do not provide the level of specificity and detail that is required to give certainty to market participants,'' but rather, they ''enumerate a wide variety of tools that a DCO may deploy to recover losses,'' some of which ''have the capacity to alter the entitlements of customers'' under part 190 (*e.g.,* ''a customer would only be entitled to such a *pro rata* share of customer property to the extent the DCO rules did not modify the distribution of the DCO's assets'' through variation margin gains haircutting or partial tear-up). ICI recommended that, ''[b]efore the Commission gives effect to any DCO loss allocation, recovery, and wind-down rules in a [p]art 190 proceeding, . . . the Commission should develop and codify minimum principles that must be reflected in [those rules,] . . . review both existing DCO rules and proposed rule changes to ensure that they are consistent with the Commission's minimum principles . . . [, and] require DCOs to change their governance process for rule changes to give stakeholders greater opportunity for input.''

As an initial matter, the Commission notes that some commenters, including ACLI, FIA, ICI, and SIFMA AMG/MFA, objected to the application of DCO recovery and wind-down plans and rules, in particular the application of

[177] Alteration in original.

variation margin gains haircutting, because they believed that changes should be made to the process by which parts 39 and 40 permit DCOs to adopt such plans and rules.

Amendments to parts 39 and 40 are beyond the scope of this rulemaking, and the Commission does not believe that these concerns with the content and operation of parts 39 and 40 should inhibit the use of such plans and rules in the context of part 190. However, the Commission continues actively to review these issues, in particular with respect to governance, as they relate to parts 39 and 40.

The Commission also notes that other commenters, including FIA, believed that default rules and procedures and recovery plans are designed to avoid bankruptcy, and should not be applied if they fail in achieving that goal. However, the DCO's rules, procedures, and plans set forth *ex ante* the manner in which losses are allocated—that is, who is exposed to them, and to what extent. In the event that losses must be borne in bankruptcy, the Commission believes, as was noted in the preamble to the proposal, that ''allocation of losses should not depend on the happenstance of when default management or recovery tools were used—*e.g.,* when assessments were called for, or when such assessments were met.'' The Commission does not believe that the comments offer a persuasive reason why the allocation of losses—who wins, who loses, and how much—should change on the basis of when a bankruptcy is filed.

The Commission further notes that a number of commenters, including ACLI and Vanguard, were concerned with the application in bankruptcy of recovery tools such as variation margin gains haircutting and partial tear-up. Variation margin gains haircutting, to the extent set forth in DCO rules, will be applied in bankruptcy, in that it represents the *ex ante* manner in which losses are allocated.[178] By contrast, partial tear-up of contracts will not be applied; rather, pursuant to § 190.14(c)(1), ''the trustee shall liquidate *all* open commodity contracts that have not been terminated, liquidated or transferred no later than seven calendar days after entry of the order for relief'' (emphasis added).

Turning to SIFMA AMG/MFA's suggestion that ''the trustee and the Commission should explicitly be required to consider the core concepts set forth in proposed § 190.00 and systemic risk in implementing a debtor DCO's rules procedures and plans'': With respect to the core concepts, § 190.00(c) states that ''the specific requirements in [part 190] should be interpreted and applied consistently with these core concepts.'' In short, that requirement is already present. Moreover, the Commission has added § 190.00(c)(3)(i)(C) to provide that where a provision in part 190 affords the trustee discretion, that discretion should be exercised in a manner that the trustee determines will best achieve the overarching goal of protecting public customers by enhancing recoveries for, and mitigating disruptions to, public customers as a class. Thus, in exercising their discretion to determine what is ''reasonable'' for purposes of § 190.15, the trustee is already directed to focus on the ''core concepts'' in § 190.00(c), and, in particular, the ''overarching goal of protecting public customers.''

However, while a DCO's default rules and procedures are required to be made public, posted on the DCO's website,[179] the same is not true for the DCO's recovery and wind-down plans. Thus, in implementing the DCO's default rules and procedures, the trustee would be implementing rules and procedures that, prior to the bankruptcy, were both subject to the supervision of the Commission and transparently available to both clearing members and their customers. By contrast, in implementing the DCO's recovery and wind-down plans, the trustee would be implementing plans that, prior to the bankruptcy, were subject to the supervision of the Commission,[180] but may not have been transparently available to clearing members or their customers. In light of this distinction, a more customer-protective approach seems appropriate in the latter context.

Accordingly, the Commission is modifying proposed § 190.15(c), which reads that in administering a proceeding under this subpart, the trustee shall, in consultation with the Commission, take actions in accordance with any recovery and wind-down plans maintained by the debtor and filed with the Commission pursuant to § 39.39, to the extent reasonable and practicable—to add at the end the qualifier that these actions should also only be taken to the extent consistent with the protection of customers.[181]

With respect to systemic risk, while the Commission, as a governmental agency, is attentive to considerations of mitigating systemic risk in all that it does,[182] it may be difficult for a trustee to make meaningful determinations as to how to do so. Moreover, the trustee is the representative of the bankruptcy estate, *see* 11 U.S.C. 323(a), with fiduciary duties to estate beneficiaries,[183] rather than to the financial system as a whole. Accordingly, the Commission does not believe it appropriate to add an explicit requirement concerning considerations of systemic risk, as suggested by SIFMA AMG/MFA.

The Commission does not agree that FIA's observation that DCO recovery and wind-down plans may ''not prescribe a particular course of action but, rather, present a menu of options that a DCO may consider'' supports FIA's conclusion that ''these plans would appear to provide no meaningful guidance to a trustee.'' To the contrary, the Commission believes that providing a ''menu of options'' among which the trustee may select (and adapt) in a manner that is ''reasonable and practicable'' would provide the trustee—who would be stepping into a complex and difficult situation with little preparation—with a helpful roadmap to determine strategy and tactics, in order to act in a prompt and cost-effective manner.

The Commission also declines to provide that the trustee cannot override the DCO's rules or deviate from an approved recovery or wind-down plan. Even if part 39 were to require that such plans be ''approved''—and it does not—they are designed in the context of operation of the DCO outside of bankruptcy. Thus, the Commission believes it to be appropriate for the trustee to apply them with flexibility to the extent reasonable and practicable.

Accordingly, after consideration of the comments and for the reasons stated above, the Commission is adopting § 190.15 as proposed, with the modification to § 190.15(c) discussed above.

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[178] Moreover, as discussed in more detail in section II.C.7 below, there is a limited amount of customer property available. Any increase in some customers claims (and thus, their distributions) due to the disapplication of gains-based haircutting would come at the expense of a reduced share of that limited customer property (*i.e.,* reduced distributions) to other customers, which could total less than the amount of their claim arising from initial margin.

[179] *See* § 39.21(c)(6).

[180] Note that § 190.15(c) only applies to recovery and wind-down plans that were ''filed with the Commission pursuant to § 39.39 of this chapter.''

[181] The ''customers'' of a DCO are, as noted at the top of this section II.C, the clearing members with respect to their public customers, as well as the clearing members with respect to their proprietary or ''house'' accounts.

[182] *See* CEA section 3(b), 7 U.S.C. 5(b) (purposes of the CEA include ''the avoidance of systemic risk'').

[183] *See* U.S. Department of Justice, Executive Office for United States Trustees, Handbook for Chapter 7 Trustees Section 4.B, at 4–2.

6. Regulation § 190.16: Delivery

The Commission is adopting § 190.16 as proposed with a modification to paragraph (a), as set forth below.

Regulation § 190.16(a) instructs the trustee to use reasonable efforts to facilitate and cooperate with completion of delivery in a manner consistent with § 190.06(a) (which instructs trustees of FCMs in bankruptcy to foster delivery where a contract has entered delivery phase before the filing date or where it is not practicable for the trustee to liquidate a contract moving into delivery position after the filing date) and the *pro rata* distribution principle in § 190.00(c)(5). The Commission believes that it is important to address deliveries to avoid disruption to the cash market for the commodity and to avoid adverse consequences to parties that may be relying on delivery taking place in connection with their business operations. However, given the potential for competing demands on the trustee's resources, including time, this instruction is limited to requiring ''reasonable efforts.''

Regulation § 190.16(b) carries forward, to the context of a DCO in bankruptcy, the delineation between the physical delivery property account class and the cash delivery property account class in § 190.06(b), as discussed above. Specifically, physical delivery property that is held in delivery accounts for the purpose of making delivery shall be treated as physical delivery property, as will the proceeds from any sale of such property. By contrast, cash delivery property that is held in delivery accounts for the purpose of paying for delivery shall be treated as cash delivery property, as would any physical delivery property for which delivery is subsequently taken.

The Commission requested comment with respect to all aspects of proposed § 190.16. The Commission raised specific questions as to whether it is appropriate, in the context of a clearing organization bankruptcy, to separate the physical delivery account class from the cash delivery account class, and if so, whether the physical delivery account class should be further sub-divided. The Commission also asked whether the delivery account class should be treated as a single, undivided account class.

CME supported the requirement in proposed § 190.16 that the trustee use reasonable efforts to facilitate deliveries of commodity contracts that have moved into delivery prior to the date and time of relief on behalf of a clearing member or customer, but asked that the Commission ''expand the rule to require the trustee to facilitate deliveries'' under contracts that move into delivery position after the filing and that the trustee is unable to liquidate. CME stated that ''[i]t is equally important to protect deliveries under [such] contracts . . . to protect against disruption to commercial markets and operations,'' and that the trustee may not be able to terminate them.

The ABA Subcommittee similarly expressed concern that proposed § 190.16(a) ''does not address contracts that are unable to be liquidated and that then move into delivery position,'' noting that ''it may be impossible or impracticable for a trustee to liquidate every'' physical-delivery commodity contract that is open at the date and time of the order for relief before the contract moves into delivery position. The ABA Subcommittee recommended that the Commission ''remove the timing limitation in Proposed Rule 190.16(a),'' and add language stating that ''the trustee should use reasonable efforts to liquidate open physical delivery commodity contracts before they move into a delivery position.''

The Commission agrees with comments raised by CME and the ABA Subcommittee that deliveries should be facilitated after the order for relief for contracts that are not otherwise terminated, liquidated, or transferred. The Commission believes that modifying the proposal to address that scenario is appropriate to avoid disruption to the cash market and to avoid adverse consequences to parties that may be relying on delivery taking place in connection with their business operations.

Accordingly, after consideration of the comments, and for the reasons stated above, the Commission is adopting § 190.16 with a modification to apply paragraph (a) to any contract that ''moves into delivery after [the date and time of the order for relief], but before being terminated, liquidated, or transferred.''

7. Regulation § 190.17: Calculation of Net Equity

The Commission is adopting § 190.17 as proposed, with a modification to § 190.17(b)(2), as discussed below. Section 190.17 establishes net equity calculations to be used in determining the claims against the debtor DCO (and the allocation of losses) among members and their accounts.

Section 190.17(a) with respect to net equity is parallel to § 190.18(a) with respect to the treatment of customer property. Section 190.17(a)(1) confirms that a member of a clearing organization may have claims in separate capacities. Specifically, a member may have claims on behalf of its public customers (customer account) and claims on behalf of itself and its non-public customers (*i.e.,* affiliates) (house account), and, within those separate customer classes, the claims may be further separated by account class. The member shall be treated as part of the public customer class with respect to claims based on commodity customer accounts carried as ''customer accounts'' by the clearing organization for the benefit of the member's public customers, and as part of the non-public customer class with respect to claims based on its house account. Section 190.17(a)(2) directs that net equity shall be calculated separately with respect to each customer capacity and, within such customer capacity, by account class.

Section 190.17(b) sets forth how a debtor DCO's pre-existing rules and procedures governing the allocation of losses—including the default rules and procedures—should be applied in a DCO bankruptcy.

Section 190.17(b)(1) confirms that the calculation of members' net equity claims—and, thus, the allocation of losses among members and their accounts—shall be based on the full application of the debtors' loss allocation rules and procedures, including the default rules and procedures referred to in §§ 39.16 and 39.35. These pre-existing loss allocation rules and procedures are the contract between and among the members and the DCO, and the Commission believes that it is appropriate to give them effect regardless of the bankruptcy of the DCO or the timing of any such bankruptcy. In other words, the pre-existing loss allocation rules and procedures (such as member assessments) should be given the same effect in a bankruptcy, regardless of whether default management or recovery tools were fully applied prior to the order for relief. While certain DCOs may have discretion, consistent with governance procedures, as to precisely when they call for members to meet assessment obligations, the Commission believes that allocation of losses should not depend on the happenstance of when default management or recovery tools were used—*e.g.,* when assessments were called for, or when such assessments were met.

Section 190.17(b) also addresses DCO rules that govern how recoveries on claims against defaulting members are allocated to non-defaulting members' accounts,[184] which effectively ''reverse

[184] These recoveries might be based on prosecution of such claims in an insolvency or receivership proceeding, or, in the reasonable

the waterfall'' by allocating recovered assets to member accounts in reverse order of the allocation of the losses to those member accounts.[185] Section 190.17(b)(2) implements such DCO rules in bankruptcy, thereby adjusting members' net equity claims (and the basis for distributing any such recoveries) in light of such recoveries. The provision similarly implements DCO loss allocation rules in other contexts, for example, (i) rights to portions of mutualized default resources that are either prefunded or assessed and collected, and, in either event, not used, as well as (ii) rules that would allocate to members recoveries against third parties for non-default losses that are, under the DCO's rules, originally borne by members.

Section 190.17(c) adopts by reference the equity calculations set forth in proposed § 190.08, to the extent applicable.

Finally, § 190.17(d) implements section 766(i) of the Bankruptcy Code, which: (1) Allocates a debtor DCO's customer property (other than member property) to the DCO's customers (*i.e.,* clearing members) ratably based on the clearing members' net equity claims based on their (public) customer accounts; and (2) allocates a debtor DCO's member property to the DCO's clearing members ratably based on the clearing members' net equity claims based on their proprietary (*i.e.,* house) accounts. To implement section 766(i), § 190.17(d) defines ''funded balance'' as a clearing member's *pro rata* share of member property (for a clearing member's house accounts) or customer property other than member property (for accounts for a clearing member's public customers). The *pro rata* amount shall be calculated with respect to each account class available for distribution to customers of the same customer class. Moreover, given that the calculation of funded balance for FCMs is an analogous exercise, the Commission intends that such calculations under § 190.17(d) will be made in the manner provided in § 190.08(c), to the extent applicable.

The Commission requested comment with respect to all aspects of proposed § 190.17. The Commission raised a specific question as to whether it is appropriate to base the calculations proposed § 190.17 on the full application of the debtors' loss allocation rules and procedures, including the DCO's default rules and procedures.

Commenters addressed the proposed language of paragraph (b), or of § 190.17 generally, but did not offer specific comments on the proposed language of paragraph (a), (c), or (d).

CME commented in support of § 190.17(b)(1)'s application of ''the DCO's loss allocation rules and procedures, including the DCO's default rules and procedures, to the calculation of clearing members' net equity claims,'' but suggested a clarification to the proposed rule. Specifically, CME suggested that the Commission ''clarify that 'full application' of the DCO's loss allocation rules and procedures to the calculation of clearing members' house net equity claims means that assessments or similar loss allocation arrangements thereunder are part of the calculation only if and to the extent that the DCO's rules and procedures provide for post-filing assessments and payments.'' CME noted that a ''DCO's rules are the contract between and among the members and the DCO,'' and that, ''[i]f the calculation of net equity claims deviates from the DCO's loss allocation under its rules, including determination of amounts owned under close-out netting rules, that could adversely affect CME's netting opinion as to the enforceability of its netting rules.'' CME also commented in support of ''giving effect to provisions in the debtor DCO's loss allocation rules that entitle clearing members to return of guaranty fund deposits or other mutualized default resources that are not used, or to payments out of amounts that the DCO recovers on claims against a defaulting clearing member, through adjustments to clearing member's net equity claims against member property to reflect their entitlement to such payments.'' CME also commented in support of § 190.17(b)(2).

The ABA Subcommittee expressed concern with respect to perceived ambiguity in § 190.17(b)(1) regarding ''how assessments that were not called for, or that were called for but not paid before the filing date, would impact the calculation of a clearing member's net equity claim with respect to its house account.'' The ABA Subcommittee requested that the Commission modify the proposed regulation to clarify that ''house account net equity claims would be adjusted to reflect post-filing obligations only if and to the extent that the DCO's rules and procedures impose obligations on clearing members to continue making such payments following the DCO's bankruptcy.'' Specifically, the ABA Subcommittee suggested that the following phrase be added to the end of § 190.17(b)(1): If and to the extent that the debtor's loss allocation rules and procedures impose obligations on clearing members to make such payments on or after the filing date.

FIA did not support the adoption of § 190.17(b)(1). FIA stated that it would be ''inappropriate to require a clearing member to reduce the value of its net equity claim by the amount of an assessment that, under the rules of the relevant DCO, either may no longer be made or are not required to be paid.'' FIA asserted that a DCO's default fund is ''a multilateral indemnification arrangement between the DCO and its members pursuant to which members' contributions are used to cover the DCO's losses resulting from member default(s) and thereby prevent the DCO's bankruptcy.'' FIA stated that a ''DCO has no authority under its rules to request or to apply these funds for any other purpose, nor do we believe that a trustee would have any authority under the [Bankruptcy] Code to do so.'' FIA noted further that, ''by requiring that a clearing member's net equity claim must include the full application of the DCO's loss allocation rules and procedures, proposed Rule 190.17(b)(1) appears to have the effect of reducing a clearing member's potential recovery, even when the full application of the DCO's loss allocation rules is not necessary to meet the DCO's obligations to non-defaulting clearing members,'' thereby impermissibly benefitting the DCO's general creditors and shareholders to the detriment of clearing members.

ICE commented that the Commission should refrain from adopting § 190.17(b) or providing ''specific guidance as to what assumptions the CFTC would make and how the net equity claim is to be calculated hypothetically.'' ICE stated that, in determining a clearing member's net equity claim, it is neither appropriate nor feasible to consider a potential assessment that could have been called for before a bankruptcy filing but was not. ICE asserted that a DCO's determination of whether ''to call

commercial judgment of the DCO, the settlement or sale of such claims.

[185] For example, if the DCO rules allocate losses in excess of the defaulters' available resources first to the DCO's own contributions, second to the mutualized default fund contributions of members other than the defaulter, third to assessments, and fourth to gains-based haircutting (*pro rata*), all of which tools were in fact used in a particular case, then recoveries on claims against the defaulting members would be allocated (to the extent available) first to those member accounts for which gains were haircut, *pro rata* based on the aggregate amount of such haircuts per member account, until all such haircuts have been reversed, second to those members who paid assessments, *pro rata* based on the amount of such assessments paid, until all such assessments have been repaid, third to members whose mutualized default-fund contributions were consumed, *pro rata* based on such default-fund contributions, until all such contributions have been repaid, and fourth to the DCO to the extent of its own contribution.

for an assessment and/or implement other loss allocation arrangements'' accounts for many considerations that would not be appropriate to revisit in an insolvency. ICE also asserted that calculating the full application of loss allocation rules, or determining what would have happened in any full allocation, may not be possible. ICE noted, for example: (a) Because a DCO is not obligated to impose assessments against its clearing members, it is unclear how the CFTC or the trustee would determine how many assessments the DCO should have made; (b) in the event that ''clearing members have the right to cap their liability by terminating their membership in a DCO,'' it is unclear how the CFTC or the trustee would determine whether a clearing member should have terminated its membership; [186] and (c) it ''may not be possible to determine definitively what the [DCO's] losses . . . would have been if additional loss allocation steps, such as variation margin gains haircutting or tear-up, had been taken.''

SIFMA AMG/MFA commented that §§ 190.17 and 190.18(b)(1) should be modified to explicitly state that any gains that were haircut during gains-based haircutting will be treated as customer property and included in the net equity claims of the clearing members and customers whose gains were haircut. SIFMA AMG/MFA further commented in support of § 190.17(b) but suggested that the proposal be modified to provide that, if a debtor DCO either (i) does not have ''reverse the waterfall'' rules or (ii) has ''reverse the waterfall'' rules that do not address each level of the debtor DCO's waterfall, the net equity clams of the debtor DCO's clearing members and customers will be calculated as though the debtor DCO, in fact, ''has 'reverse the waterfall' rules that address each level of the DCO's waterfall.

Vanguard commented on § 190.17(b)(1)'s requirement that a trustee's calculation of DCO members' net equity claims include the full application of DCO loss allocation rules and procedures. Vanguard expressed concern that the requirement would result in a customer being entitled to only ''a *pro rata* share to the extent the DCO rules did not modify the distribution of the DCO's asset, whether pre- or post-petition, through measures such as variation margin gains haircutting or partial tear-up of transactions.'' Vanguard noted the possibility that, ''as the DCO begins to fail,'' the DCO's rules ''could be changed without the appropriate vetting by FCMs and customers who presently bear an inordinate share of the risk.'' Vanguard believed that ''any application of non-defaulting customer gains haircutting, or any other margin haircutting, should be prohibited as being fundamentally at odds with normal insolvency practice and highly counterproductive to incentivizing customers not to abandon a failing DCO.'' Vanguard asserted that, if haircutting is to be allowed, customers should ''receive full compensation in the form of a credit or equity claim against the DCO [that is] superior to that of other creditors.'' Vanguard also suggested that § 190.17(b)(2) be modified in the same manner as suggested by SIFMA AMG/MFA, with respect to situations in which a debtor DCO does not have ''reverse the waterfall'' rules, or has ''reverse the waterfall'' rules that do not address each level of the debtor DCO's waterfall.

ICI expressed concern that § 190.17(b)(1) would permit a DCO's loss allocation, recovery, and wind-down rules ''to override the fundamental customer protections that Part 190 and Subchapter IV [of the Bankruptcy Code] are meant to safeguard,'' because they would ''no longer guarantee to a customer a *pro rata* share of customer property based on its transactions and margin in accordance with Subchapter IV.'' In that scenario, ICI commented that ''a customer would only be entitled to such a *pro rata* share to the extent the DCO rules did not modify the distribution of the DCO's assets, whether pre- or post-petition, through measures such as variation gains haircutting or partial tear-up of transactions.''

Having received no specific comments on the proposed language of paragraphs (a), (c), and (d) of § 190.17, the Commission is adopting those paragraphs as proposed.

As described above, the Commission received several comments on paragraph (b). After considering the comments, the Commission notes that DCO default rules and procedures (also referred to as ''default waterfalls''), as a general matter, first use the resources of the defaulter (*i.e.,* the defaulter's initial margin and contribution to the default fund) to cover a shortfall. Should those resources be insufficient to cover the shortfall, such default waterfalls generally proceed to use the DCO's own capital contribution, and only after those resources are extinguished is the remaining shortfall mutualized among the clearing members: (1) First, through the prefunded default fund contributions of non-defaulting clearing members; (2) then, through limited assessment powers against those non-defaulting clearing members, which are generally set as a multiple of each clearing member's prior contributions to the default fund; and (3) finally, through gains-based haircuts that affect both clearing members and (through customer agreements) the customers of clearing members (*i.e.,* public customers).

The Commission notes two important takeaways from the general structure of default waterfalls. First, each clearing member knows, in advance of a default, the maximum amount of its exposure to contribute to mutualized loss through the guarantee fund and the DCO's assessment powers. Second, should there be any reduction in the amount of funds collected through such assessments, then any losses in excess of the waterfall (*i.e.,* up through the assessments) would instead be allocated to both clearing members and their public customers. In other words, if the losses are large enough, a reduced allocation of losses to clearing members would necessarily mean that their public customers would bear an increased allocation of losses.

The Commission remains of the view that, as discussed in the proposal, ''[w]hile certain DCOs may have discretion, consistent with governance procedures, as to precisely when they call for members to meet assessment obligations, . . . allocation of losses should not depend on the happenstance of when default management or recovery tools were used—*e.g.,* when assessments were called for, or when such assessments were met.'' [187] As discussed above, the losses in a DCO bankruptcy ultimately would be allocated between clearing members and customers, and clearing members' exposure to this allocation of losses is already capped by the *ex ante* limits on assessment powers. If the Commission were to modify the language of paragraph (b) in the manner suggested by multiple commenters, the modification would effectively decrease the allocation of losses that would be borne by clearing members—below the *ex ante* limits of which they are on

[186] *But see* ICE Clear Credit Rules 806, 807. To mitigate the risk that their members will ''rush to the exits'' after a default, DCOs generally hold departing members liable for assessments due to the defaults that occurred before they withdrew from membership, as well as during a ''cooling-off'' period that extends past the date the member gives notice of intent to withdraw. The ICE Clear Credit rules cited, which include a ''cooling-off period'' of at least 30 days, are examples of this phenomenon. Thus, the possibility that clearing members would withdraw is not likely to affect their liability for assessments in this context.

[187] 85 FR at 36038.

notice—and correspondingly increase the allocation of losses that would be borne by customers. In other words, in such a scenario, the Commission believes that the suggested language could harm customers and run counter to the Commission's policy that, with respect to customer property, public customers be favored over non-public customers. For those reasons, the Commission declines to adopt commenters' suggestions to modify the net equity calculations in § 190.17(b) by limiting (or eliminating) the allocation of assessments that were not exercised prior to a bankruptcy filing.

By contrast, gains-based haircuts are also part of the pre-bankruptcy arrangements for allocating losses. If that part of the ''waterfall'' is reached, then that *ex ante* arrangement should be followed. Moreover, there is a limited amount of customer property available. Thus, to the extent the application of gains-based haircuts was to be reversed, and some customers would realize increases in the allowed amounts of their claims (and thus a greater share of customer property), other customers would suffer a decreased share of customer property; indeed, the latter customers may, as a result, receive less than the amount of their claims for initial margin. This could have the effect of reducing those customers' recoveries below the initial margin they have posted. The Commission stands firmly against initial margin haircutting as inimical to the principles of segregation. Thus, the Commission declines to adopt the suggestion by SIFMA AMG/MFA and Vanguard to reverse the application of gains-based haircutting in a DCO bankruptcy.

FIA's comment letter raised two points that should be further addressed. First, FIA stated that a DCO, under its rules, lacks the authority to apply the DCO's default fund for any purpose other than preventing the DCO's bankruptcy, and a trustee would similarly lack the authority to do so under the Bankruptcy Code.[188] FIA further argued that, as a result of that limitation, the DCO's authority to make new assessments or otherwise require that members contribute additional funds to a DCO's default fund would not continue into bankruptcy. Consequently, FIA argued that a clearing member's net equity claim should not be reduced in bankruptcy by the amount of an assessment that would no longer be required to be paid under the DCO's rules. However, the Commission notes that § 190.17(b)(1) does not instruct the trustee to call any clearing member to pay in additional funds; rather, paragraph (b)(1) reduces the clearing member's net equity claim against the estate of the DCO, to account for uncalled or uncollected assessments. Pursuant to section 20(a)(5) of the CEA, the Commission has the power to provide, with respect to a commodity broker in bankruptcy, ''how the net equity of a customer is to be determined,'' [189] and the Commission believes that by setting the net equity calculation as proposed, the rule would appropriately set such calculations in a manner that does ''not depend on the happenstance of when default management or recovery tools were used,'' as discussed more fully above.

Second, FIA noted that, ''by requiring that a clearing member's net equity claim must include the full application of the DCO's loss allocation rules and procedures, proposed [§] 190.17(b)(1) appears to have the effect of reducing a clearing member's potential recovery, even when the full application of the DCO's loss allocation rules is not necessary to meet the DCO's obligations to non-defaulting clearing members'' and that ''[s]uch a result would impermissibly benefit the DCO's general creditors and shareholders to the detriment of clearing members.'' The Commission did not intend for the potential outcome suggested by FIA; rather, in proposed § 190.17(b)(2)(i), the Commission intended to provide that, where the full amount of assessment powers is not needed to cover a default, an appropriate adjustment shall be made to the net equity claims of clearing members. The Commission believes that the rule text should be modified in order to communicate its intent more clearly, and avoid the possibility of the unintended outcome raised by FIA. Accordingly, the Commission is modifying § 190.17(b)(1) to clarify that the DCO's ''loss allocation arrangements shall be applied to the extent necessary to address losses arising from default by clearing members.''

This modification separates paragraph (b)(1) into two separate parts. First, paragraph (b)(1)(i) will provide that the calculation of a clearing member's net equity claim shall include the full application of the debtor's loss allocation rules and procedures, including the default rules and procedures referred to in § 39.16 and, if applicable, § 39.35. Second, paragraph (b)(1)(ii) will provide that the calculation in paragraph (b)(1)(i) will include, with respect to the clearing member's house account, any assessments or similar loss allocation arrangements provided for under those rules and procedures that were not called for before the filing date, or, if called for, have not been paid. Such loss allocation arrangements shall be applied to the extent necessary to address losses arising from default by clearing members.

The ABA Subcommittee, in its comment letter, was concerned that the proposed rule is ambiguous on whether assessments or similar loss allocation arrangements would be included in the calculation where the clearing organization's rules do not impose obligations on clearing members to make such payments on or after the filing date. The modified structure of paragraph (b)(1), as described above, should remove that ambiguity, albeit not in the direction that the ABA Subcommittee would prefer: The calculation ''*will include,* with respect to the clearing member's house account, *any* assessments or similar loss allocation arrangements that were not called for before the filing date . . . to the extent necessary to address losses arising from default . . .'' (emphasis added).

CME's comment letter also raises a concern that should be addressed. In particular, CME is concerned that deviating from the DCO's rules with respect to loss allocation in this context could adversely affect the DCO's netting opinion as to the enforceability of its netting rules. The Commission notes that this argument conflates bank capital charge calculations for cleared transactions with capital charge calculations for default fund contributions. Pursuant to, *e.g.,* 12 CFR 217.133(a)(2), a clearing member that is (or is part of) a bank holding company regulated by the Federal Reserve Board and that uses the internal ratings and advanced measurement approaches to bank capital requirements is required to use the methodologies described in the applicable paragraph of 12 CFR 217.133 to calculate its risk-weighted assets *for a cleared transaction* (that is, paragraph (c) of that section) and the methodologies described in a different paragraph to calculate its risk-weighted assets *for its default fund contribution to a CCP* (that is, paragraph (d) of that section).[190] Netting opinions are necessary to treat cleared transactions

[188] FIA at 9.

[189] In the bankruptcy of a clearing organization, clearing members are a species of customer.

[190] There are analogous provisions for bank holding companies regulated by the Federal Reserve Board that use the standardized approach for calculating bank capital requirements (12 CFR 217.35) as well as banks regulated by the FDIC and the Office of the Comptroller of the Currency.

on a net basis,[191] while assessments are related to default fund contributions. Thus, the treatment of *assessment obligations* is irrelevant to netting opinions for *cleared transactions.*

The Commission also received comments on proposed § 190.17(b)(2) concerning the treatment of ''reverse the waterfall'' rules in the context of a DCO bankruptcy. After considering the comments, the Commission continues to believe that it is useful and appropriate to use ''reverse the waterfall'' rules for recoveries made by a clearing organization (including a debtor clearing organization). Some commenters suggested that proposed § 190.17(b)(2) be modified to address situations where the debtor DCO lacks ''reverse the waterfall'' rules, or where such rules do not address each level of the debtor clearing organization's waterfall. Although the commenters did not provide specific language that could be used to apply to such situations, the Commission believes that such a complicated modification is beyond the bounds of what was proposed, and thus, the Commission declines to make the modification here. Nonetheless, the commenters' suggestion is well taken, and the Commission may consider further work on that issue in the future.

Accordingly, after consideration of the comments, and for the reasons stated above, the Commission is: (1) Adopting § 190.17(a), (b)(1), (c), and (d) as proposed; and (2) adopting § 190.17(b)(2) with the modification discussed above.

8. Regulation § 190.18: Treatment of Property

The Commission is adopting § 190.18 to establish the allocation of the debtor DCO's estate in order to satisfy claims of clearing members, as customers of the debtor. The Commission is adopting § 190.18 as proposed, with the following modifications: (1) Adding new paragraph (b)(1)(iv), as described below; and (2) removing paragraph (c)(1) and renumbering the remaining paragraphs of paragraph (c).

Section 190.18(a) with respect to customer property is parallel to § 190.17(a) with respect to net equity. Paragraph (a) provides that property of the debtor clearing organization's estate is allocated between member property, and customer property other than member property, in order to satisfy claims of clearing members as customers of the debtor. Such property would constitute a separate estate of the customer class (*i.e.,* member property, and customer property other than member property) and the account class to which it is allocated, and would be designated by reference to such customer class and account class.

Section 190.18(b) sets out the scope of customer property for a clearing organization,[192] and is based in large part on § 190.09(a). Specifically, in § 190.18, paragraphs (b)(1)(i)(A) through (G) are based on § 190.09(a)(1)(i)(A) through (G). Section 190.18(b)(1)(i) does not include a provision that is parallel to § 190.09(a)(1)(i)(H), because loans of margin are not applicable to DCOs. In § 190.18, paragraphs (b)(1)(ii)(A) through (D) are based on § 190.09(a)(1)(ii)(A), (D), (E), and (F), while § 190.18(b)(1)(ii)(E) adopts by reference § 190.09(a)(1)(ii)(H) through (K) as if the term debtor used therein refers to a clearing organization as debtor. Section 190.18(b)(1)(ii) does not include provisions that are parallel to § 190.09(a)(1)(ii)(B), (C), (G), and (L), because they would not be applicable due to the differences in business models, structures, and activities of DCOs and FCMs, respectively. Section 190.18(b)(1)(iii) is unique to clearing organizations, and includes as customer property any guarantee fund deposit, assessment, or similar payment or deposit made by a member, to the extent any remains following administration of the debtor's default rules and procedures. Section 190.18(b)(1)(iii) also includes any other property of a member that, pursuant to the debtor's rules and procedures, is available to satisfy claims made by or on behalf of public customers of a member. Finally, § 190.18(b)(2), which identifies property that is not included in customer property, adopts by reference § 190.09(a)(2) as if the term debtor used therein refers to a clearing organization as debtor and to the extent relevant to a clearing organization.

Section 190.18(c) allocates customer property between customer classes, favoring allocation to customer property other than member property over allocation to member property, so long as the funded balance in any account class for members' public customers is less than one hundred percent of net equity claims. Once all account classes for customer property other than member property are fully funded (*i.e.,* at one hundred percent of net equity claims), any excess could be allocated to member property. Section 190.18(c)(1), as proposed (but not adopted herein, as discussed below), would allocate any property referred to in § 190.18(b)(1)(iii) (guarantee deposits, assessments, etc.) first to customer property other than member property, to the extent that any account class therein is not fully funded, and then to member property. In proposing this provision, the Commission intended such treatment of property to favor public customers over non-public customers. Section 190.18(c)(2) allocates any excess funds in any account class for members' house accounts first to customer property other than member property to the extent that any account class therein is not fully funded, and then any remaining excess to house accounts to the extent that any account class therein is not fully funded. Finally, § 190.18(c)(3) allocates any excess funds in any account for members' customer accounts first to customer property other than member property to the extent that any account class therein is not fully funded, and then any remaining excess to house accounts, to the extent that any account class therein is not fully funded.

Section 190.18(d) allocates customer property among account classes within customer classes. Section 190.18(d)(1) confirms that, where customer property is tied to a specific account class—that is, where it is segregated on behalf of, readily traceable on the filing date to, or recovered by the trustee on behalf of or for the benefit of an account class within a customer class—the property must be allocated to the customer estate of that account class (that is, the account class for which it is segregated, to which it is readily traceable, or for which it is recovered). Section 190.18(d)(2) provides that customer property that cannot be allocated in accordance with paragraph (d)(1) shall be allocated in a manner that promotes equality of percentage distribution among account classes within a customer class. Thus, in such a scenario, such property would be allocated first to the account class for which funded balance—that is, the percentage that each member's net equity claim is funded—is the lowest. This would continue until the funded balance percentage of that account class equals the funded balance percentage of the account class with the next lowest percentage of funded claims. The remaining customer property would be allocated to those two account classes so that the funded balance for each such account class remains equal. This would continue until the funded balance percentage of those two account classes is equal to the funded balance of the account class with the next lowest percentage of funded claims, and so

[191] *See* 12 CFR 217.3(d).

[192] This is another provision prescribed pursuant to the Commission's authority under section 20(a)(1) of the CEA, 7 U.S.C. 24(a)(1).

forth, until all account classes within the customer class are fully funded.

Section 190.18(e) confirms, however, that where the debtor DCO has, prior to the order for relief, kept initial margin for house accounts in accounts without separation by account class, then member property will be considered to be in a single account class.

Section 190.18(f) reserves the right of the trustee to assert claims against any person to recover the shortfall of property enumerated in § 190.18(b)(1)(i)(E) and (b)(1)(ii) and (iii). Paragraph (f) is analogous in the DCO context to § 190.09(a)(3) in the context of FCMs. The purpose of paragraph (f), as with § 190.09(a)(3), is to clarify that any claims that the trustee may have against a person to recover customer property will not be undermined or reduced by the fact that the trustee may have been able to satisfy customer claims by other means.

The Commission requested comment with respect to all aspects of proposed § 190.18. The Commission raised a specific question about the comprehensiveness of the scope of customer property for a clearing organization in proposed § 190.18(b). The Commission also asked specifically about the appropriateness of the proposed allocation of customer property between customer classes in proposed § 190.18(c) and within customer classes in proposed § 190.18(d).

The Commission received several comments on the proposal. Whereas some commenters supported the proposal, in whole or in part, others raised concerns particularly with respect to the scope of customer property in proposed § 190.18(b) and the treatment of guarantee fund deposits and other payments in proposed § 190.18(c)(1), among other issues.

ICI commented in support of the proposal and agreed with the Commission that the proposal is necessary to further the policy in section 766(h) of the Bankruptcy Code of prioritizing the claims of public customers over the claims of non-public customers. ICI stated that public customers need the proposed protections because they ''typically have no direct participation in the DCO's risk management and no insight into the transactions other customers have with the DCO.'' ICI also stated that public customers may have less access to information concerning the DCO's financial health, and may have fewer tools available to protect themselves against losses, when compared to DCO members.

The ABA Subcommittee commented that the treatment of clearing members' guaranty fund deposits and similar payments in proposed § 190.18(c)(1) represents a ''significant policy change'' with ''significant competing policy considerations and complex issues'' that warrant consideration outside of the Proposal. The ABA Subcommittee contended, for example, that such payments ''may be exposed to risk in asset classes in which [the clearing member] does not trade, and which the clearing member does not expect to assume based on the DCO's rules.'' Without taking a formal position on the proposal, the ABA Subcommittee identified issues that it believed warrant further attention by the Commission and market participants, including whether the language in paragraph (c)(1): (a) Should be implemented ''through a Part 190 rule that would have the effect of overruling inconsistent DCO rules,'' or through an amendment to part 39 to require DCOs ''to have loss allocation rules that align with [the] policy change''; (b) would place U.S. DCOs ''at a competitive disadvantage to non-U.S. DCOs''; (c) would ''discourage firms from becoming or remaining direct clearing members of a DCO for the purpose of clearing trades solely for their own account or for non-public customers''; and/or (d) would ''create a risk that U.S. banking regulators will want to revisit the methodology for determining the amount of regulatory capital that bank and bank-affiliated clearing members must hold with respect to cleared derivatives.'' The ABA Subcommittee therefore recommended that the Commission maintain the status quo by revising proposed § 190.18(c)(1) ''to confirm that customer property described in Rule 190.09(b)(1) will be allocated to member property after such property is applied to cover losses in accordance with the DCO's rules . . . [until] the Commission separately considers the merits of the [proposed] policy change.''

SIFMA AMG/MFA requested that the Commission amend proposed § 190.18(b)(1) to provide explicitly ''that customer property includes property a debtor DCO contributes to its default waterfall,'' as seemingly was intended by proposed § 190.18(b)(1)(ii)(E).

Consistent with its comments on proposed § 190.17(b), FIA commented that customer property should not include guaranty fund deposits as set forth in proposed § 190.18(b)(1)(iii) and recommended that the Commission remove that provision. FIA stated that a ''default fund represents a multilateral indemnification arrangement between the DCO and its members pursuant to which members' contributions are used to cover the DCO's losses resulting from member default(s) and thereby prevent the DCO's bankruptcy.'' FIA contended that a DCO has no authority under its rules, and a trustee has no authority under the Bankruptcy Code, ''to request or to apply these funds for any other purpose.''

CME commented in support of the decision to set forth the elements that comprise customer property in proposed § 190.18(b)(1). CME specifically agreed that the scope of customer property should include any guaranty fund deposit, assessment or similar deposit made by a clearing member or recovered by the trustee, to the extent any remains following administration of the debtor's default rules and procedures, and any other property of a member available under the debtor's default rules and procedures to satisfy claims made by or on behalf of pubic customers of a member. For clarity and transparency, CME encouraged the Commission to expand the scope of customer property to explicitly include the amounts that the DCO commits to the financial resources in the waterfall under its rules, to the extent that those resources have not already been applied under the DCO's default rules. CME stated, however, that the Commission should eliminate the requirement set forth in proposed § 190.18(c)(1) that the payments described in proposed § 190.18(b)(1) be allocated to customer property other than member property for use ''to cover a shortfall in the funded balances for clearing members' customer accounts in *any* account class'' and, instead, ''reaffirm that guaranty fund deposits are to be applied to cover losses in accordance with the DCO's rules, with any remaining funds allocated to member property.'' In support of its view, CME stated that such requirement set forth in proposed § 190.18(c)(1): (1) Would materially change ''the definition of member property in current Regulation 190.10, under which any guaranty funds remaining after payments *in accordance with the DCO's rules* would be returned to clearing members as member property''; (2) ''may significantly alter how clearing members assess the risks they have assumed in joining CME,'' by undermining CME's ''rules limiting use of clearing members' guaranty fund deposits to cover losses in the relevant product class to which they have contributed to the guaranty fund and in which they participate''; and (3) would ''compromise CME's ability under Regulation 39.27 to 'operate pursuant to a well-founded, transparent, and *enforceable* legal framework that addresses each aspect' of CME's obligations as a DCO, including netting arrangements and 'other significant aspects' of CME's 'operations, risk management procedures, and related requirements' as a DCO.'' [193] CME also asserted that: (a) Proposed § 190.18(c)(1) ''is vulnerable to legal challenge as exceeding the Commission's authority'' in section 20 of the CEA, because such authority is not being exercised consistent with the Bankruptcy Code and other provisions of the CEA; [194] (b) the Commission does not have the authority under the CEA ''to adopt rules that have the effect of directly rewriting a DCO's rules,'' and that doing so would be contrary to the reasonable discretion afforded to DCOs under section 5b of the CEA to comply with DCO core principles and Commission regulations; (c) the Commission may not alter or supplement the rules of a registered entity until it satisfies the requirement under section 8a(7) of the CEA to request that the registered entity amend its rules and provide the registered entity with notice and an opportunity for a hearing if it does not do so; (d) amending the contract between and among clearing members and the DCO through a Commission regulation ''would call into question . . . the enforceability of the DCO's rules''; and (e) ''a proposed rule impacting the manner in which bank or bank-affiliated clearing members' guaranty fund deposits and assessment obligations can be utilized may drive subsequent changes to the methodology and resulting amount of capital such members must hold for those exposures under the Cleared Transactions Framework in the Regulatory Capital Rules.''

ICE agreed with the Commission's approach not to propose ''that property in an insolvent DCO's general estate can be treated as customer property where customer property is otherwise insufficient to pay customer claims.'' ICE suggested that the Commission clarify ''that any ability to use residual assets should be only to the extent such assets are not required to be used for any other purpose under other applicable law (*e.g.*[,] for other classes of customers or for other products).'' ICE suggested that ''[t]he definition of customer property should also respect any express limitations on recourse that have been implemented under DCO rules.'' ICE did not believe that the distributional preference for public customers over clearing members and any non-public customers of clearing members, as established by proposed § 190.18, is appropriate in the context of a DCO failure, because it could ''impose losses, or greater losses, on non-defaulting clearing members in a manner that overrides the negotiated and approved frameworks in the DCO's rules.'' ICE asserted that this ''change could require fundamental restructuring of DCO operations,'' and should be ''part of a separate rulemaking that addresses the interaction [of the proposal] with the Part 39 requirements.'' ICE also noted that the liability caps that limit the overall amount of a clearing member's contributions and assessments—and the manner in which they may be used for a particular default—are important for the clearing members' risk management and are often necessary under such clearing members' capital requirements. ICE stated that requiring the use of contributions or assessments for purposes other than what is set forth in the DCO's rules ''would render such caps and limitations ineffective.'' ICE further posited that proposed § 190.18 is ''unworkable for clearing houses that have separate guaranty funds for separate products, or other limited recourse provisions in their rulebooks [that are used] to designate particular default resources for particular products, and to ring-fence the liability of clearing members from particular products that they may choose not to clear.'' ICE also raised a concern that proposed § 190.18's potential subordination of the claims of the self-clearing members of a defaulting DCO to customers of other clearing members could serve as a ''significant disincentive'' to self-clearing, sponsored clearing, or direct clearing. ICE commented that proposed § 190.18 ''should not be applied to require the use of clearing member guarantee fund, margin, or other resources in the context of a non-default loss where the rules of the DCO specifically do not contemplate (or expressly forbid) the use of such assets for such purposes.'' On that issue, ICE noted that many DCOs have sought to address separately the allocation of non-default losses through rules that ''may allocate certain losses, and not others, to clearing members and/or to the clearing organization itself, and/or provide for the sharing of certain losses in certain amounts.''

After considering the comments, the Commission is adopting § 190.18 with modifications, specifically with respect to paragraphs (b)(1) and (c)(1).

Multiple commenters suggested that the Commission modify § 190.18(b)(1) to make explicit that customer property includes the amounts of its own funds that a debtor DCO had committed as part of its loss allocation rules. Given that the DCO's commitment, in DCO rules, of a specified amount of its own funds to loss allocation sets a market-wide understanding and expectation that such an amount will be used for such a purpose, the Commission agrees that this clarification is warranted. Therefore, the Commission is modifying § 190.18(b)(1) by adding a new paragraph (b)(1)(iv), which will explicitly include in customer property: ''Amounts of its own funds that the debtor had committed as part of its loss allocation rules, to the extent that such amounts have not already been applied under such rules.''

Multiple commenters addressed proposed § 190.18(c)(1)(i), which assigned guarantee funds to customer property other than member property (*i.e.,* to the benefit of members' public customers) if and to the extent that a shortfall existed in the funded balance for such customers. The proposal was supported by ICI, but opposed by CME, FIA, and ICE, while the ABA Subcommittee also noted potential issues.

The Commission separately considered each of the arguments raised by the commenters in opposition to proposed § 190.18(c)(1). In the discussion below, the Commission reviews the arguments raised by the commenters and explains why it is modifying the proposal by not adopting proposed § 190.18(c)(1), and renumbering the remaining paragraphs of proposed § 190.18(c).

In response to concerns that the Commission lacks the authority to implement this provision, the Commission notes that it has the authority under section 20(a)(1) of the CEA to determine, ''[n]otwithstanding title 11 of the United States Code'' (*i.e.,* the Bankruptcy Code) both ''(1) that certain . . . property [including, *e.g.,* guarantee fund deposits] [is] to be included in or excluded from . . . member property'' and ''(5) how the net equity of a customer is to be determined.'' Thus, § 190.18(c)(1) is legally sound because of the ''notwithstanding title 11'' clause in section 20 of the CEA.

Moreover, proposed § 190.18(c)(1) would allocate guarantee fund deposits to customer property other than member

[193] Emphasis in original.

[194] CME commented that the proposal would be contrary to the Bankruptcy Code's definition of ''member property'' as ''customer property received, acquired, or held by or for the account of a debtor that is a clearing organization, from or for the proprietary account of a customer that is a clearing member of the debtor.''

property only where the funded balance is less than one hundred percent of net equity claims for members' public customers in an account class, *i.e.,* where the DCO had failed to maintain in segregation sufficient funds to pay members' public customer account balances in full. In other words, in that scenario, the debtor DCO would be non-compliant with Commission regulations. This is not a re-writing of the DCO's rules,[195] nor a re-writing of the contract between the DCO and its members, nor an undermining of the DCO's ''well-founded, transparent, and enforceable legal framework,'' but an allocation of shortfall in a bankruptcy case where the DCO is non-compliant with Commission regulations.

The use of guarantee funds in the manner specified in proposed § 190.18(c)(1) would not be an ''unexpected loss'' to non-defaulting clearing members, given that the *regulation* would be transparently available to all. To the extent that the consequences of the application of the regulation (re-allocation of their default fund contributions to cover a shortfall in customer property for members' public customers) would be unexpected by clearing members, and unpredicted by their risk management systems, it is equally the case that the public customers of clearing members would be surprised by a shortfall in customer property, which their risk management systems would also see as unexpected.[196] Thus, the choice is not simply whether to impose an unexpected loss to clearing members or not, but rather a choice of who should bear that unexpected loss, clearing members (as a group) or their customers (as a group). To that point, in addition to the statutory authority that is provided in the CEA, the Commission agrees with the comment from ICI that § 190.18(c)(1) would further the policy goal—stated in section 766(h) of the Bankruptcy Code, but also running throughout the Commission's approach to part 190—of prioritizing the claims of public customers over the claims of non-public customers.

However, despite the foregoing analysis supporting adoption of § 190.18(c)(1), the Commission is concerned about bank regulators' potential analysis of § 190.08(c)(1). In particular, the Commission has considered that bank regulators may conclude that, because § 190.08(c)(1) directs the use of DCO default funds for reasons other than addressing mutualized member defaults, member contributions to DCO default funds do not fit within the definition (in bank capital regulations) of ''default fund contribution,'' *see, e.g.,* 12 CFR 217.2. Specifically, such member contributions may not constitute ''funds contributed or commitments made by a clearing member to a CCP's mutualized loss sharing arrangement,'' *see, e.g., id.* If this were the case, members' default fund contributions would be subject to more onerous capital treatment than they would receive if such contributions did fit within the definition of ''default fund contributions.'' [197] That more onerous capital treatment would have a direct, negative impact on normal day-to-day activities for bank-affiliated clearing members, and not merely in the uncertain future event of a DCO bankruptcy. In other words, as discussed further below in section III.D.8, while the benefits to public customers of § 190.18(c)(1) in case of bankruptcy would be balanced by the costs to clearing members, the present-day costs to (bank-affiliated) clearing members of more onerous capital treatment would not be offset by significant benefits to public customers.

The Commission acknowledges that the decision not to adopt proposed § 190.18(c)(1) differs from the Commission's approach to § 190.17(b)(1). In § 190.17(b)(1), uncalled or unmet assessments would be applied to address default losses, with the only difference being the timing of the bankruptcy relative to the timing of the calls for, or payment of, the assessments. In short, the Commission concludes in that context that the default fund contributions would be treated as such for bank capital purposes, and thus would not be subject to more onerous capital treatment. In contrast, proposed § 190.18(c)(1) would apply guarantee funds to cases that are distinct from a member default. As discussed above, it seems entirely plausible that doing so would take such contributions outside of the definition (in bank capital regulations) of ''default fund contribution,'' and thus subject them to more onerous capital treatment. The Commission believes that this distinction is significant and forms the basis for the difference in the Commission's respective approaches to § 190.17(b)(1) and proposed § 190.18(c)(1).

Accordingly, after consideration of the comments, and for the reasons stated above, the Commission is adopting § 190.18 as proposed, with the following modifications, as set forth above: (1) Adding new paragraph (b)(1)(iv), as described above; and (2) by removing paragraph (c)(1) and renumbering the remaining paragraphs of paragraph (c).

9. Regulation § 190.19: Support of Daily Settlement

The Commission is adopting § 190.19 as proposed, with a modification to paragraph (b)(1), as discussed below.

As the Commission noted in proposing § 39.14(b), ''[t]he daily settlement of financial obligations arising from the addition of new positions and price changes with respect to all open positions is an essential element of the clearing process at a DCO.'' [198] Indeed, Congress confirmed this by requiring that each DCO complete money settlements not less frequently than once each business day.[199]

In the ordinary course of business, variation settlement payments are, at a set time or times each day,[200] sent to the DCO from the customer and proprietary accounts of each clearing member with net losses in such accounts (since the last point of computation of settlement obligations for that member), and then sent from the DCO to the customer and proprietary accounts of each clearing member with net gains in such accounts over that time period.

There is no necessary relationship between the aggregate amount of payments to the DCO from all clearing

[195] And, thus, does not require the Commission to invoke or follow the procedures of CEA section 8(a)(7).

[196] Indeed, the risk would be even more unexpected by public customers: Clearing members are entirely aware that their default fund contributions are at risk of use to cover a mutualized default. Their customers, on the other hand, expect that their customer funds are fully protected by the CEA's and the Commission's segregation requirements.

[197] That treatment could be significantly more onerous: For example, under the FDIC's regulations, the capital requirement for a clearing member's prefunded default fund contribution to a qualifying CCP can be as low as 0.16% of that default fund contribution. *See* 12 CFR 324.133(d)(4). By contrast, the capital requirement for a clearing member's prefunded default fund contribution to a non-qualifying CCP is 100% of that default fund contribution. *See* 12 CFR 324.10(a)(1)(iii), (b)(3) (requiring capital of 8% of risk-weighted asset amount, 324.133(d)(2) (setting risk-weighted asset amount for default fund contributions to non-qualifying CCP at 1,250% of the contribution). (1,250% * 8% = 100%). The Federal Reserve and Office of the Comptroller of the Currency have similar regulations.

Default fund contributions to DCOs total many billions of dollars. While not all default fund contributions to DCOs come from bank-affiliated clearing members, the majority of them do.

[198] 76 FR 3608, 3708 (Jan. 11, 2011).

[199] *See* Core Principle E(i), 7 U.S.C. 7a–1(c)(2)(E)(i).

[200] DCOs are required to effect settlement with each clearing member at least once each business day. They are additionally required to have the capability to effect a settlement with each clearing member on an intraday basis. *See* § 39.14(b).

member customer accounts with net losses and the aggregate amount of payments from the DCO to clearing members' customer accounts with net gains. On the other hand, it is the case that, for each business day, the sum of variation settlement payments to the clearinghouse from clearing members' customer and house accounts with net losses will equal the sum of variation settlement payments from the clearinghouse to clearing members' customer and house accounts with net gains.[201] Those variation settlement payments will be received into the DCO's accounts at one or more settlement banks from the accounts of the clearing members with net losses and subsequently be disbursed from the DCO's accounts at settlement banks to the accounts of the clearing members with net gains.[202] Depending on the settlement bank and operational arrangements of the particular DCO, the variation settlement funds will remain in the DCO's accounts between receipt and disbursement for a time period of between several minutes and several hours.

The Commission believes that it is crucial to the settlement process that the variation settlement payments that flow into the DCO from accounts with net losses are available promptly to flow out of the DCO as variation settlement to accounts with net gains.

The Commission is adopting § 190.19(a), pursuant to section 20(a)(1) of the CEA,[203] to provide that, upon and after an order for relief, variation settlement funds shall be included in the customer property of the DCO, and that they shall be considered traceable to—and shall promptly be distributed to—member and customer accounts entitled to payment with respect to the same daily settlement.[204] This customer property would be allocated to (i) member property and (ii) customer property other than member property, in proportion to the ratio of total gains in member accounts with net gains, and total gains in customer accounts with net gains, respectively.

The Commission is adopting § 190.19(b) to address cases where there is a shortfall in funds received pursuant to paragraph (a) (*i.e.,* settlement payments received by the DCO), such as in the case of a member default. Paragraph (b)(1) sets forth how such a shortfall shall be supplemented, to the extent necessary, and further states that such funds shall be allocated in the same proportion as referred to in paragraph (a). Paragraph (b)(1) provides that four types of property shall be included as customer property: (i) Initial margin held for the account of a member that has defaulted on a daily settlement, including initial margin segregated for the customers of such member;[205] (ii) Assets of the debtor to the extent dedicated to such use as part of the debtor's default rules and procedures, or as part of any recovery and wind-down plans described in the paragraph (a) (*i.e.,* the debtor DCO's ''skin in the game''); (iii) Prefunded guarantee or default funds maintained pursuant to the DCO debtor's default rules and procedures; and (iv) Payments made by members pursuant to assessment powers maintained pursuant to the debtor DCO's default rules and procedures. Paragraph (b)(2) provides that, to the extent that the funds that are included as customer property pursuant to paragraph (a), supplemented as described in paragraph (b)(1), such funds would be allocated between (i) member property; and (ii) customer property other than member property, in proportion to the ratio of total gains in member accounts with net gains, and total gains in customer accounts with net gains, respectively.

The Commission requested comment with respect to all aspects of proposed § 190.19.

CME expressed support for proposed § 190.19, commenting that the provisions in the proposal ''are appropriate to support the daily settlement cycle when the trustee obtains the Commission's approval to continue operating the DCO.'' FIA commented that it did not support proposed § 190.19(b), stating that the provision's reliance on a debtor DCO's recovery and wind-down plans post-bankruptcy would be inappropriate.[206] SIFMA AMG/MFA requested that the Commission modify proposed § 190.19(b)(1) to clarify the Commission's presumed intent that ''the debtor's recovery and wind-down plans shall only apply with respect to proposed § 190.19(b)(1)(ii)—the debtor's ''skin in the game'' [(*i.e.,* its own capital contributions)]—and not with respect to the other'' categories of customer property that are enumerated in § 190.19(b)(1). The Commission agrees that its intent should be clarified to reflect the comment from SIFMA AMG/MFA,[207] and is modifying the language of § 190.19 to reflect that clarification.

Accordingly, after consideration of the comments, and for the reasons stated above, the Commission is adopting § 190.19 as proposed, with a modification to clarify that the reference to the debtor's recovery and wind-down plans in paragraph (b)(1) applies only to paragraph (b)(1)(ii), as set forth above.

D. Appendix A Forms

The Commission is deleting forms 1 through 3 contained in appendix A and is replacing form 4 with a streamlined proof of claim form. Current forms 1 through 3 contain outdated provisions that require unnecessary information to be collected. The Commission believes these changes will provide a trustee with flexibility to act based on the specific circumstances of the case, while still acting consistently with the rules.

As noted in § 190.03(f), the trustee will be permitted, but not required, to use the revised template proof of claim form included as new appendix A. That

[201] Thus, while (for each settlement cycle), customer account losses (x) plus house account losses (y) will equal customer account gains (p) plus house account gains (q) (that is, $x + y = p + q$), x would only equal p by random chance.

[202] In some cases, the DCO will use one settlement bank, and all settlement funds will flow into and out of that bank. In other cases, the DCO may use a system of settlement banks, and the DCO may, after receiving payments from members with payment obligations, move funds between and among the settlement banks (possibly through a ''concentration bank'') to match the settlement funds at each bank to the DCO's settlement obligations to members who are entitled to settlement payments.

[203] 7 U.S.C. 24(a)(1) (''Notwithstanding title 11 of the United States Code, the Commission may provide, with respect to a commodity broker that is a debtor under chapter 7 of title 11 of the United States Code, by rule or regulation . . . that certain cash, securities, other property, or commodity contracts are to be included in or excluded from customer property or member property.'').

[204] Because deposits of initial margin described in § 39.14(a)(1)(iii) are separate from the variation settlement process, they are treated separately in § 190.19(a). Such funds would be member property to the extent that they are deposited on behalf of members' house accounts, and customer property other than member property to the extent that they are deposited on behalf of members' customer accounts.

[205] This is restricted to the extent that such margin may only be used to the extent that such use is permitted pursuant to parts 1, 22, and 30 of the Commission's regulations, which include provisions restricting the use of customer margin.

[206] FIA's concerns with the language in § 190.19(b) are the same as its concerns with § 190.15(b) and (c), discussed in greater detail above. *See supra* section II.C.5. However, for the reasons noted in section II.C.5, the Commission believes that providing a ''menu of options'' among which a trustee may select (and adapt) in a manner that is ''reasonable and practicable'' would provide the trustee with a helpful roadmap to determine strategy and tactics, given that the trustee will likely face a complex and difficult situation with little preparation.

[207] As SIFMA AMG/MFA correctly suggested, the Commission intends for the debtor DCO's recovery and wind-down plans to apply to the property described in § 190.19(b)(1)(ii), and not to the property described in paragraph (b)(1)(i), (iii) or (iv), in the manner and to the extent described in paragraph (b)(1). As noted in the preamble to the proposal, and as found in the regulation itself, § 190.19(b)(1)(ii) contains an explicit reference to ''recovery and wind-down plans,'' whereas § 190.19(b)(1)(i), (iii) and (iv) do not contain such references.

template is intended to implement § 190.03(e), and includes cross-references to the detailed paragraphs of that section. Similarly, the instructions for this template form that are included in appendix A are also designed to aid customers in providing information and documentation to the trustee that will enable the trustee to decide whether, and in what amount, to allow each customer's claim consistent with part 190.

The Commission received one comment with respect to appendix A, from CME, which opined that ''the proposed template proof of claim form included as Appendix A [is a] major improvement[ ] over the current . . . proof of claim template. CME also support[ed] giving the trustee the flexibility to tailor the proof of claim form to request information of customers as appropriate under the circumstances.''

Accordingly, after consideration of this comment, and for the reasons stated above, appendix A to part 190 will be adopted as proposed.

E. Appendix B Forms

Appendix B to part 190 contains special bankruptcy distribution rules. These rules are broken into two frameworks. Framework 1 provides special rules for distributing customer funds when the debtor FCM participated in a futures-securities cross-margining program that refers to that framework. Framework 2 provides special rules for allocating as shortfall in customer funds to customers when the shortfall is incurred with respect to funds held in a depository outside the U.S. or in a foreign currency.

The Commission proposed clarifying changes to framework 1. No comments were received with respect to framework 1. Accordingly, and for the reasons stated above, the Commission is adopting appendix B, framework 1 as proposed.

The Commission proposed to retain framework 2 with some clarifying changes to the opening paragraph, but without proposing any substantive change. It proposed to retain the current instructions and examples following the first paragraph in appendix B, framework 2 entirely unchanged. It requested comment with respect to framework 2. The Commission received two comments on framework 2: From the ABA Subcommittee, and from a number of individual members of that subcommittee writing on their own behalf.

The ABA Subcommittee expressed the concern that ''[f]ramework 2 creates some ambiguity on when and how the special distribution framework it prescribes should apply.'' First, the ABA Subcommittee stated that ''framework 2 could be read to apply whenever there is a loss resulting from a sovereign action, even if there is sufficient customer property to otherwise pay all customer net equity claims in full.'' The ABA Subcommittee suggested that an additional sentence be added to the opening paragraph of framework 2 clarifying that it applies only when there is a loss due to sovereign action *and* there is insufficient customer property to pay all customer net equity claims in full. Second, the ABA Subcommittee (in conjunction with a clarifying comment from the Subcommittee Members) noted that framework 2 uses the term ''reduction in claims'' in a potentially confusing manner—framework 2 is intended to reduce distributions allocated to those customers who are allocated losses due to sovereign risk; those customers claims are not reduced. If the sovereign action is later reversed or modified, those customers whose distributions were reduced will receive increased distributions on their claims.

Third, the existing instructions to framework 2 ''establish the 'Final Net Equity Determination Date' as the date for both converting customer claims to U.S. dollars and determining the amount of the Sovereign Loss.'' However, in prior bankruptcies of FCM/commodity brokers, ''claims stated in foreign currencies were either valued on the date of transfer (where porting was available), or converted to U.S. dollars as of either as of the petition date or the date on which the foreign currency reflected in the customer's account was liquidated (and thus the customer bore the risk of interim currency fluctuations).'' Furthermore, ''a sovereign action could take place at any time after the petition date, and the trustee is required to make funded balance calculations throughout the course of the bankruptcy case for purposes of porting and/or making interim distributions.''

The Commission finds the comments on framework 2 of the ABA Subcommittee, as clarified by the comment of the Subcommittee Members, persuasive. First, framework 2 is indeed only intended to address cases where there is insufficient customer property to pay all customer net equity claims in the relevant account class in full (if there is no shortfall, then there is no need to allocate losses), and that point should be made clear. Second, it is correct that framework 2 is intended to reduce distributions, it is not intended to reduce claims, and it is indeed appropriate to change the language used in framework 2 to clarify this fact.[208] Third, the relevant date is the date of the calculation, not the ''Final Net Equity Determination Date,'' and this should be clarified as well.

Accordingly, the Commission is:

(1) Modifying the first paragraph of framework 2 to include the statement that: ''If a futures commission merchant enters into bankruptcy and maintains futures customer funds or Cleared Swaps Customer Collateral in a depository outside the U.S. or in a depository located in the U.S. in a currency other than U.S. dollars, *and a sovereign action of a foreign government or court has occurred that contributes to shortfalls in the amounts of futures customer funds or Cleared Swaps Customer Collateral,* the trustee shall use the following allocation procedures'' (emphasis added solely for illustration).

(2) Amending the instructions and examples within the whole of framework 2 to replace references to ''reduction in claims'' with references to ''reduction in distributions,'' and with conforming changes to other text.

(3) Deleting the phrase ''Final Net Equity Determination Date'' from current section II.B.2.b of framework 2, and replacing it with the phrase ''date of the calculation.''

Accordingly, after consideration of the comments, and for the reasons stated above, the Commission is adopting appendix B, framework 2 as proposed, with the modifications described above.

F. Technical Corrections to Other Parts

1. Part 1

The Commission is making as proposed several technical corrections and updates to part 1 in order to update cross-references. These are as follows:

- In § 1.25(a)(2)(ii)(B) the Commission will revise the cross-reference to specifically identifiable property, since the definition will be updated in § 190.01.
- In § 1.55(d) introductory text and (d)(1) and (2), references to current § 190.06 will be removed consistent

[208] The fact that sovereign action reduces *distributions* rather than *claims* means that, if the sovereign action is later reversed or modified (*e.g.,* by appeal in the foreign courts, or due to recovery of assets in the foreign insolvency proceeding) resulting in reduced losses due to sovereign action in a particular jurisdiction, those customers whose distributions have been reduced due to sovereign action in that jurisdiction will receive increased distributions on their claims (with those distributions adjusted to reflect the revised amount of losses due to sovereign action). Thus, in this case, the claims remain constant, while the distributions increase.

with the revisions to new § 1.41 (which was proposed as § 190.10(b) and renumbered).

• In §§ 1.55(f) and 1.65(a)(3) introductory text and (a)(3)(iii) the Commission will update references to the customer acknowledgment in § 1.55(p) (which was proposed as § 190.10(e) and renumbered).

2. Part 4

In part 4, the Commission is making as proposed minor technical corrections: In §§ 4.5(c)(2)(iii)(A), 4.12(b)(1)(i)(C), and 4.13(a)(3)(ii)(A), the Commission will change the cross-references to the defined term for ''in-the-money-amount.''

3. Part 41

In part 41, the Commission is making as proposed one technical correction. In § 41.41(d), the Commission will delete the cross-reference to the recordkeeping obligations in current § 190.06, pursuant to the revisions to § 1.41 (which was proposed as § 190.10(b) and renumbered).

No comments were received with any of these technical corrections and accordingly, for the reasons stated above, they are being adopted as proposed.

G. Additional Comments

In addition to the comments discussed above, the Commission received several general comments that addressed matters outside the scope of the Proposal. The Commission appreciates the additional feedback. Because these comments do not address proposed changes and are therefore outside the scope of this rulemaking, the Commission may take the comments under advisement for future rulemakings.

ISDA encouraged the Commission to continue working on DCO recovery and resolution issues alongside the Federal Deposit Insurance Corporation (FDIC) in the United States, and with global standard setters such as CPMI–IOSCO and the Financial Stability Board and other CCP supervisors and resolution authorities internationally. The Commission notes that staff are actively doing each of those things.

ISDA also noted that it would be advisable to engage in workshops with both market participants (including DCOs, FCMs and other clearing members and customers) and the FDIC prior to finalizing the Proposal to develop examples that illustrate both how net equity claims would be calculated in a hypothetical DCO insolvency under various loss scenarios and how the claims of creditors and equity would be treated in a resolution of the DCO under Title II of the Dodd-Frank Act. ISDA observed that the Proposal's treatment of a DCO's insolvency contains significant subtleties and nuances that could have implications for the counterfactual in a DCO resolution. ISDA suggested that further engagement could help ensure that these subtleties and nuances would not result in any unintended consequences, and that they are broadly understood by all entities that could be impacted by a DCO's insolvency or resolution.

While the Commission is finalizing the Proposal, it agrees that workshops and similar interactions between staff and other agencies, as well as with industry participants, are an excellent way to expose subtleties and nuances, build common understanding, and enhance planning.

CME and CMC commented on various issues relating to delivery, and requested that ''the Commission consider, in a separate rulemaking, the merits of imposing custody requirements or other customer protection requirements with respect to delivery accounts, along with the possibility of further subdividing delivery accounts and delivery account classes by underlying asset class or delivery mechanism, *e.g.,* electronic transfer versus physical load-out.'' [209] CME recommended that the separate rulemaking consider requirements such as whether FCMs should hold such property in custody accounts or limitations on how long cash or cash equivalents should be held in delivery accounts that are not subject to custody requirements.[210] CME believed that any such rules would fit best in the Commission's part 1 regulations and not in part 190 as parties with delivery obligations may not necessarily be aware of requirements in the bankruptcy regulations. CME recommended that the part 190 provisions relating to the delivery account class should be consistent with any such rules the Commission may ultimately adopt. Thus, CME believed that the Commission may have to revisit the delivery account class definition, and any appropriate subdivisions within the account class, along with the definitions of cash delivery property and physical delivery property definitions, based on the outcome of such a rulemaking.

As noted above, the Commission recognizes the importance of addressing deliveries and delivery accounts, in order to protect customer funds in delivery accounts, to avoid disruptions to cash markets for delivered commodities, and to avoid adverse consequences to parties that may be relying on delivery taking place in connection with their business operations. The Commission notes that there potentially would be benefits to requiring segregation for delivery accounts, but there would be corresponding costs as well. The Commission expects to continue its consideration of such delivery and delivery account issues in the future.

SIMFA AMG/MFA understood the Commission's decision, due to limited resources, not to amend certain key definitions and concepts outside part 190, as proposed by the ABA Subcommittee in its model set of part 190 rules, within this rulemaking. These amendments include, *e.g.,* the definitions of foreign option and variation margin, as well as regulations concerning non-swap and non-futures over-the-counter transactions cleared by a DCO and concerning leverage transaction merchants. However, SIFMA AMG/MFA recommended that the Commission make these amendments as soon as possible, given the beneficial impact such changes will have on the administration of an FCM or DCO insolvency. The Commission may consider these proposed changes in the future.

ICI and Vanguard encouraged the Commission to work with other regulators to minimize existing barriers to porting, particularly for FCMs dually registered as broker-dealers, FCMs within consolidated groups that are subject to certain due diligence requirements, and FCMs that are subject to the FDIC's Orderly Liquidation Authority proceedings. The commenters encouraged the Commission to work with regulators to permit similar six-month grace periods and remove the requirement to port ''all or none'' of the positions instead of allowing partial transfers of customer positions, including those of separately managed accounts.

ICI also recommended that the Commission engage with SIPC or the relevant bankruptcy court to ensure that any selected trustee has the experience and knowledge to act in accordance with the duties contained in part 190 and Subchapter IV of the Bankruptcy Code.

Commission staff have and will continue to work with staff of other regulators to minimize barriers to

[209] See CMC, CME.

[210] *See* CME. CME believed that the Commission has authority to adopt such a rule pursuant to its anti-fraud authority under CEA section 4b and its plenary authority to regulate commodity options under CEA section 4c(b).

porting, and have worked and will, if and when necessary in future, work with SIPC and the office of the U.S. Trustee, to promote the appointment of the most knowledgeable trustees available in the context of SIPA or Chapter 7 proceedings, respectively, involving a commodity broker.

ICI recommended that the Commission continue its portfolio margining harmonization efforts with the SEC to further facilitate portfolio margining, including with respect to security-based swaps and swaps. The Commission notes that the two Commissions are actively engaging in such efforts, and, on October 22, 2020, held a joint meeting during which they jointly approved a ''Request for Comment: Portfolio Margining of Uncleared Swaps and Non-Cleared Security-Based Swaps.'' [211]

ICI and Vanguard recommended that the Commission extend the ''legally segregated operationally commingled'' (''LSOC'') model applied to cleared swaps contracts (and associated collateral) within part 22 to also apply to futures, foreign futures, and options thereon (and associated collateral) to limit non-defaulting customer exposure to defaulting customers.

ICI also requested that the Commission or Commission staff provide guidance, such as an interpretive letter, that interprets part 22 to require that OTC transactions cleared by DCOs and carried in a cleared swaps account be treated as cleared swaps subject to part 22.[212]

ICI and Vanguard recommended that the Commission prohibit non-defaulting customer gains haircutting, or any other margin haircutting, and if such gains haircutting is allowed at all, it should be limited in scope and duration, overseen by the DCO's resolution authority and/or the systemic risk authority, and the customer must receive full compensation in the form of a credit or equity claim against the DCO, superior to that of other creditors.

ICI and Vanguard also requested that the Commission require DCOs to increase their ''skin-in-the-game'' as a foundational incentive for the DCO to set appropriate margin levels and avoid clearing illiquid or highly volatile products. Vanguard also recommended that a DCO's capital should be required to backstop clearing risk, should the assets available for DCO recovery prove inadequate.

FIA requested that the Commission confirm that amendments to part 190, including to appendix B, framework 2, would not prohibit the Commission from amending § 1.49 at a later date to expand the definition of ''money center currency.''

The Commission confirms that the amendments to part 190 that are being made herein will not prohibit the Commission from amending any other regulation, including § 1.49, in the future. If future amendments to other parts of the Commission's regulations lead to a situation where it would be advisable to make conforming changes to part 190, the Commission will consider such conforming changes along with those amendments.

H. Supplemental Proposal

In the Supplemental Proposal, the Commission noted a problem to be solved: There is a possibility that a SIDCO could file for bankruptcy before the process for placing that SIDCO into Title II resolution is complete. Due to closeout netting rules adopted by many DCOs, including the SIDCOs, that filing could have the consequence of terminating all of the SIDCO's cleared contracts. Terminating those contracts could undermine the success of any subsequent Title II resolution.

The Supplemental Proposal suggested one approach to solve the problem, and requested comment, *inter alia,* on better ways to do so. In light of concerns raised in the comments received in response to the Supplemental Proposal, and for reasons discussed below, the Commission has determined not to finalize the alternative that was proposed in the Supplemental Proposal.

The process for placing a financial company into Title II Resolution is deliberate and intricate.[213] By contrast, a voluntary petition in bankruptcy commences the case, which in turn constitutes an order for relief. Accordingly, there exists a possibility that, in the highly unlikely event that a SIDCO would consider bankruptcy, the SIDCO could file for bankruptcy before a process to place that SIDCO into a Title II Resolution would have completed. While the appointment of the FDIC as receiver under Title II would automatically result in the dismissal of the prior bankruptcy, if the bankruptcy filing were to necessarily result in the termination of the SIDCO's derivatives contracts with its members, that would undermine the potential success of any subsequent Title II Resolution.

To address the problem, the Commission proposed, in the Supplemental Proposal, to adopt a provision that would stay the termination of SIDCO contracts for a brief time after bankruptcy in order to provide advance notice to the Commission (and, thus, to enable the Commission to notify the key turners) of the point at which the SIDCO's contracts could be terminated, in order to foster the success of a Title II resolution by avoiding that termination, if the FDIC is appointed receiver in such a Resolution within that time. During this stay, variation margin would neither be collected nor paid. Due to concerns raised by commenters to the original Proposal regarding the effect of any restriction on termination of DCO contracts on treatment, under the capital regulations of Prudential Regulators of the banks that many clearing members are affiliated with, of SIDCO rules, the proposal provided that this provision would become effective only if the Commission were to find that the Prudential Regulators (*i.e.,* the Federal Reserve, the FDIC, and the Office of the Comptroller of the Currency) have taken steps to make such a stay consistent with SIDCO rules retaining status as QMNAs.[214]

[211] 85 FR 70536 (November 5, 2020).

[212] Such an interpretation may be superfluous. Previously, the Commission issued an ''Interpretative Statement Regarding Funds Related to Cleared-Only Contracts Determined To Be Included in a Customer's Net Equity.'' 73 FR 57235 (October 2, 2008). At the time, prior to Dodd-Frank, there were questions as to whether cleared-only transactions were commodity contracts. The Commission noted that, in cases where such contracts are held in a futures account at an FCM and margined as a portfolio with exchange-traded futures, assets margining that portfolio are likely to be includable within ''net equity'' even if such contracts were found not to be commodity contracts: Where the assets in an entity's account collateralize a portfolio containing both commodity contracts and other contracts, the entirety of those serves as performance bond for each type of contracts. *See id.* at 57236. *See also* 17 CFR 22.1 (defining ''Cleared Swaps Customer Collateral,'' in relevant part, as all property that ''[i]s intended to or does margin, guarantee, or secure a Cleared Swap . . . .'').

[213] In the case of a SIDCO, this would include a written recommendation by each of the FDIC and the Federal Reserve covering eight statutory factors. Following that recommendation, the Secretary of the Treasury would then need to make a determination, in consultation with the President, that each of seven statutory factors is met. (The FDIC, Federal Reserve, and Secretary of the Treasury are often referred to as the ''key turners'' for Title II resolution). Following such a determination, the board of directors of the financial company may acquiesce or consent to the appointment of the FDIC as receiver, or there may be a period of judicial review which may extend to 24 hours.

[214] Any stay (in bankruptcy) on the termination of the SIDCO's derivatives contracts would—under the regulations of the Prudential Regulators of the banks and bank holding companies that SIDCO clearing members may be affiliated with or part of—be inconsistent with the status of a DCO's rules as a qualifying master netting agreement (''QMNA''). Qualification of DCO rules as a QMNA is necessary in order for the banks and bank holding companies that clearing members are affiliated with or part of

Continued

The Commission requested comment on all aspects of the Supplemental Proposal, including as to whether the approach proposed ''is the best design for such a solution.''

The Commission received five comments on the Supplemental Proposal, each of which was from an entity that commented on the Proposal.[215]

Many of the commenters argued that the proposed stay is unnecessary, because the Commission would inevitably have received notice of the impending bankruptcy. For instance, ICI (2) commented that:

> Although it may indeed take some time for the relevant agencies to ''turn the three keys,'' a DCO's recovery tools should give the agencies more than enough time. DCOs have clearing fund provisions, operational default provisions, and a variety of other risk management tools at their disposal. In practice, these tools may not be completely effective to preclude an insolvency. However, it seems extraordinarily unlikely that they would be so ineffective as to fail to give the FDIC, Federal Reserve Board, and Secretary of the Treasury enough time to decide whether to trigger OLA proceedings.

Similarly, SIFMA AMG/MFA (2) stated that ''the possibility of a surprise bankruptcy filing [is] implausible given the regulatory oversight framework.''

FIA (2) agreed, stating that:

> A determination with regard to invoking Title II will almost certainly be made before a SIDCO is subject to an order for relief. . . . [W]e fully anticipate that the Commission, the FRB, the FDIC, and the Department of the Treasury will be making an assessment regarding the necessity and feasibility of recommending that the President invoke Title II and taking appropriate action before the SIDCO concludes that it must file a petition for bankruptcy.

CME (2) argued that:

> under the CEA oversight framework, including a SIDCO's reporting obligations, surely it is reasonable to expect that the Commission, FDIC, FRB and Treasury will be well aware of any circumstances that could portend a SIDCO's failure, whatever the cause, and will be closely monitoring the situation. If the relevant parties are contemplating placing the SIDCO into a Title II resolution proceeding, and doing so is feasible, it is hard to imagine that a SIDCO could file a voluntary petition for relief under subchapter IV of Chapter 7 of the Bankruptcy Code without their prior knowledge.
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> * * *
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> In the highly unlike event a SIDCO were to face a decision whether to file for bankruptcy, it would be one of last resort, taken only after careful deliberation. The decision to file a voluntary petition for relief is certainly not one that CME, or any DCO, would take lightly.

The Commission agrees that, pursuant to the DCO oversight framework, including a SIDCO's reporting obligations under § 39.19, the Commission would promptly be notified of a DCO's financial distress. Upon learning of such distress—whether through notification by the DCO or by risk surveillance by Commission staff—the Commission and staff would monitor the situation closely, and, in appropriate cases, promptly contact and act in coordination with fellow regulators, including the Federal Reserve and FDIC (and, as appropriate, the Department of the Treasury). Moreover, DCOs have strong and effective ''clearing fund provisions, operational default provisions, and other risk management tools at their disposal,'' as noted in the comment letter from ICI (2). The Commission believes it to be ''extraordinarily unlikely'' that these tools would fail, let alone fail before the ''key turners'' have time to act.

It is also true that, given prior experience with discussions with DCOs concerning defaults of clearing members (none of which resulted in financial distress to the DCOs), the Commission fully expects that any DCO that *is* in financial distress would be in close contact with Commission staff. The Commission also appreciates the sentiment expressed by CME and quoted above, implying that ''it is hard to imagine'' that a SIDCO would not provide the Commission with prior knowledge of a voluntary bankruptcy filing. Finally, the Commission is confident that the decision to file a voluntary petition for relief in bankruptcy is ''not one that . . . any DCO would take lightly.''

Nevertheless, given the destructive impact that termination of the derivatives contracts of a SIDCO would cause, the Commission remains concerned about the effects that a bankruptcy filing would have on the ability to resolve the SIDCO pursuant to Title II successfully. In this context, it is not enough that such an event is ''implausible,'' ''hard to imagine,'' or ''extraordinarily unlikely.'' Knowledge of the SIDCO's financial distress is distinct from knowledge of the timing of a potential bankruptcy filing. While the Commission would most likely be aware of the SIDCO's distress, it is at this point not certain that there would be clear communication of the SIDCO's intention to file for bankruptcy sufficiently in advance that the key turners would have time to act.

As noted in the Supplemental Proposal, the destructive impact of a full tear-up of a SIDCO's contracts would be significant. The FSOC has found that a significant disruption or failure of either SIDCO could have a major adverse impact on the U.S. financial markets, the impact of which would be exacerbated by the limited number of clearing alternatives currently available for the products cleared by each SIDCO. A failure or disruption of either SIDCO would likely have a significant detrimental effect on the liquidity of the futures and options markets (for CME) or swaps markets (for ICC), and on clearing members, which include large financial institutions, and other market participants. These significant effects would, in turn, likely threaten the stability of the broader U.S. financial system.[216] For those reasons, *inter alia,* the Commission continues to be concerned about avoiding a circumstance where the derivatives contracts of a SIDCO are irrevocably terminated because the SIDCO files for bankruptcy before a process to place that SIDCO into a Title II Resolution.

However, the comments expressed strong concerns about achieving those goals through the use of a bankruptcy stay, especially in light of the fact that variation margin would neither be collected nor paid during that period.

The Supplemental Proposal acknowledged that risk levels would increase during the stay period. Commenters argued that such increase in risk exposures during the stay period would pose unacceptable risks. For example, CME (2) stated that ''permitting the accumulation of uncovered risk for 48 hours during an extremely volatile time would pose a risk to financial stability.'' Similarly, SIFMA AMG/MFA (2) warned that the proposed part 190 stay, in conjunction with the Title II stay, ''would result in extraordinary market exposures to market participants during highly volatile market conditions. The non-payment of margin could also result in a multiple day liquidity problem for

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to net the exposures of their contracts cleared with the DCO in calculating bank capital requirements. If they cannot net such exposures, there would be significantly increased bank capital requirements associated with such contracts. Such an increase in bank capital requirements would disrupt both proprietary and customer clearing. *See generally* Supplemental Proposal, 85 FR 60110, 60112 (Sept. 24, 2020).

[215] Comments on the Supplemental Proposal were submitted by: CME Group Inc. (''CME (2)''); Futures Industry Association (''FIA (2)''); Intercontinental Exchange Inc. (''ICE (2)''); Investment Company Institute (''ICI (2)''), and Securities Industry and Financial Markets Asset Management Group and Managed Funds Association (''SIFMA AMG/MFA (2)'').

[216] *See* 2012 FSOC Annual Report, Appendix A, at 163, 178.

market participants clearing at the SIDCO.''

The Supplemental Proposal also acknowledged that there is a significant cost to the proposed stay, in that ''[f]or the duration of the stay period, clearing members and clients will be uncertain whether their contracts will continue (as part of a Resolution) or be terminated (and thus would need to be replaced). That uncertainty would mean that clearing members and clients would be disadvantaged in determining how best to protect their positions.'' Again, commenters agreed that this cost would ensue, and argued that it would be unacceptable. For example, ICI (2) observed that during the stay:

> the price of the relevant underlying assets could (and if a SIDCO is insolvent, likely would) move dramatically. However, customers would be precluded from entering into risk-reducing or replacement transactions to stem potential losses, since they will not know whether their contracts will be terminated or reinstated. Such a freeze not only threatens to cause public customers significant losses that they cannot mitigate; it would also create a liquidity event because customers will need to preserve as much liquidity as possible during the pendency of the stay in order to meet potential margin calls.

Commenters also raised issues relating to legal uncertainty. For instance, FIA (2) acknowledged that section 20 ''authorizes the Commission to adopt rules '[n]otwithstanding title 11 of the United States Code' '' (*i.e.,* the Bankruptcy Code). However, FIA observed that ''[w]hether a stay contemplated under the Supplemental Proposal would conflict with section 404(a) of FDICIA . . . is unclear.''

In light of the persuasive arguments of the commenters, the Commission concludes that a bankruptcy stay is not an appropriate means of achieving the goal of fostering the success of a Title II Resolution by avoiding the possibility that the SIDCO could file for bankruptcy before a process to place that SIDCO into a Title II Resolution would have completed with the result that all of the SIDCO's contracts were terminated. This would be true even if action was taken by the Prudential Regulators to avoid having such a stay undermine the QMNA status of SIDCO rules. Thus, while the goal remains important, the Commission will not adopt such a stay.

A number of the comments answered the Commission's call for a better way of achieving that goal. SIFMA AMG/MFA(II) stated that ''[a]s an alternative to the proposed stay, the Commission could require, as part of its Part 39 or Part 190 rules, that a SIDCO provide a 1 or 2 day notice to the Commission of any bankruptcy petition by a SIDCO. We believe this notice requirement would achieve the same goal in a materially less detrimental manner.''

CME (2) suggested the same alternative approach to achieve the same regulatory goal, in somewhat more detail. CME (2) urged that the Commission should address the problem:

> in a more direct manner, consistent with its rulemaking authority. For example, the Commission could require a DCO to notify the CFTC in advance of its plan to file a voluntary petition for relief under subchapter IV of Chapter 7 of the Code, to allow Treasury time to determine whether to appoint the FDIC as receiver before the SIDCO files its petition. We note that before a commodity broker may file a voluntary petition for relief under subchapter IV, its board of directors must approve a resolution authorizing the debtor to take that step.

The Commission agrees that the alternative suggested by the commenters in response to the Commission's request—providing the advance notice sought by the Commission, but before a bankruptcy filing rather than thereafter—is one that, as FIA (2) observed, ''deserves the Commission's strong consideration.'' It appears that it may achieve the regulatory goals specified in the Supplemental Proposal while avoiding the concerns raised by the commenters: By providing advance notice to the Commission, it appears that it may allow the Commission, which will be coordinating with the ''key-turners,'' to advise those agencies of the imminence of a bankruptcy filing, and to provide them with warning at a time that may be sufficient to enable them to act with dispatch to complete the process.

Because the alternative approach would not involve a post-bankruptcy stay, it would appear to avoid affecting the QMNA status of SIDCO rules (and, thus, would appear not to require any action by the Prudential Regulators).[217] Moreover, because this notice would occur in advance of a bankruptcy filing, the suspension of payments and collections of variation margin would not occur, and there would appear to be no ambiguity concerning the status of the cleared contracts of market participants. By avoiding the mechanism of a bankruptcy stay, the Commission would also appear to avoid the legal uncertainty issues raised by the commenters with respect to that mechanism. Instead, this notice approach would appear to be, as noted by CME, well within the Commission's rulemaking authority.[218]

However, in light of the concerns raised with the previous approaches to addressing this problem, both the one advanced in the Supplemental Proposal as well as one advanced in the Proposal, the Commission concludes that, at this point, it should engage in further analysis and development before proposing this, or any other, alternative approach. Such further analysis and development might better enable the Commission to propose, in detail, a solution that is effective, and that mitigates any attendant costs. Thus, the Commission will, at present, keep this issue under advisement.

III. Cost-Benefit Considerations

A. Introduction

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders.[219] Section 15(a) further specifies that the costs and benefits shall be evaluated in light of the following five broad areas of market and public concern: (1) Protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission considers the costs and benefits resulting from its discretionary determinations with respect to the section 15(a) factors (collectively referred to herein as ''Section 15(a) Factors'') below.

In the Proposal, the Commission endeavored to assess the expected costs and benefits of the proposed rulemaking in quantitative terms, including costs related to matters addressed in the Paperwork Reduction Act[220] (''PRA-related costs''), where possible. In situations where the Commission was unable to quantify the costs and benefits, the Commission identified and considered the costs and benefits of the applicable proposed rules in qualitative terms. The lack of data and information to estimate those costs was attributable in part to the nature of the proposed

[217] This also avoids the issue, raised by ICE (2), that action by the Prudential Regulators with respect to QMNA status may not be sufficient to address netting issues for non-U.S. clearing members.

[218] *See, e.g.,* CEA section 5b(c)(2)(J), 7 U.S.C. 7a–1(c)(2)(J) (reporting core principle); CEA section 3(b), 7 U.S.C. 5(b) (purpose of the CEA is to ensure the financial integrity of transactions subject to the CEA and the avoidance of systemic risk); CEA section 8a(5), 7 U.S.C. 12a(5) (general rule-making authority).

[219] CEA section 15(a), 7 U.S.C. 19(a).

[220] 44 U.S.C. 3501 *et seq.*

rules. None of the comments identified quantifiable costs or benefits.

In a number of cases, commenters suggested alternative approaches or modifications to the proposed provisions. The Commission has carefully considered these alternatives and modifications and in a number of instances, for reasons discussed in detail above, has adopted such alternative approaches or modifications where, in the Commission's judgment, the alternative or modified approach is more appropriate to accomplish the regulatory objectives. The rationale in these cases was discussed in detail above.

1. Baseline

The baselines for the Commission's consideration of the costs and benefits of this rulemaking are: (1) The Commission's current regulations in part 190, which establish bankruptcy rules in the event of an FCM bankruptcy; (2) current appendix A to part 190, which contains four bankruptcy forms (form 1—Operation of the Debtor's Estate—Schedule of Trustee's Duties; form 2—Request for Instructions Concerning Non-Cash property Deposited with (Commodity Broker); form 3—Request for Instructions Concerning Transfer of Your Hedging Contracts Held by (Commodity Broker); and form 4—Proof of Claim); and (3) current appendix B to part 190, which contains two frameworks setting forth rules concerning distribution of customer funds or allocation of shortfall to customer claims in specific circumstances.

2. Overarching Concepts

a. Changes to Structure of Industry

The Commission is making several revisions to part 190 in order to reflect the changes to the structure of the industry since part 190 was originally published in 1983. In particular, FCMs and DCOs now operate in a different world, where matters such as market moves, transactions, and movements of funds tend to happen much more quickly, in part due to the advances in technology and the global nature of underlying markets.

These changes include major structural changes in the financial markets, including regulatory reforms following the 2008 financial crisis and consequent changes to the structure of the derivatives markets, changes in the governance of the market utilities, such as DCOs, from non-profit organizations to public companies, and major reforms in the banking sector, followed by the creation of large, publicly held financial holding companies with different attitudes towards risk.

As a result, several of the changes to part 190 will address these changed circumstances. The Commission believes that the revisions in proposed part 190 that address the computerized and fast-paced nature of the industry will benefit all parties involved in a bankruptcy proceeding, since the rules would reflect how the industry actually works today and will avoid unnecessary delay to the administration of a bankruptcy proceeding.

b. Trustee Discretion

In several places in revised part 190, the Commission provides additional flexibility and discretion to the bankruptcy trustee in taking certain actions.[221] This principles-based approach is in contrast to the customer notice procedures in current part 190, which are more prescribed and depend on the type of notice being given.

The Commission has concluded that, in general, affording more discretion to the bankruptcy trustee in appropriate circumstances is beneficial, and indeed necessary, where matters are unique and fast-paced, as they often are in commodity broker bankruptcy proceedings. In many areas, it is unlikely that a prescriptive approach can be designed that will reliably be ''fit for purpose'' in all plausible future circumstances.

Granting the trustee discretion is expected to decrease, though it certainly does not eliminate, the number and extent of cases in which the trustee will petition the bankruptcy court for formal approval of an action. Each formal approval the trustee is required to obtain—*i.e.,* each time the trustee moves for an order from the bankruptcy court authorizing the trustee to take a particular action in a particular way—takes significant time and involves significant administrative costs—in particular, the time of professionals such as attorneys and financial experts to draft legal pleadings and analyses. These professionals charge significant hourly fees, and thus their time leads to significant administrative costs. As discussed further below, administrative costs can be charged against customer property, leading to reduced recoveries by public customers.

Therefore, increased discretion of the trustee will benefit the estate by allowing the trustee to make principles-based decisions that are uniquely tailored to the facts and circumstances of the particular case, rather than compelling the trustee to follow a procrustean framework, or *requiring* the trustee to request formal approval from the bankruptcy court or the Commission before implementing those decisions. This approach leads to approaches that are better tailored to the specifics of the circumstances, reductions in administrative costs (leaving more funds available for distribution to public customers and/or other creditors) and faster distributions of customer property (to the benefit of public customers). It is also intended to mitigate the negative externalities arising from the distressed circumstances that tend to result in further reduction in the value of customer assets.[222]

The Commission recognizes, however, that with increased discretion comes a risk of trustee mistake or misfeasance; in other words, a trustee making decisions that turn out not to be in the best interests of public customers as a class, or other creditors.[223] While this is certainly a potential cost in situations where the trustee is given increased discretion or flexibility, the Commission believes that this potential cost will be mitigated by (1) the high degree of informal (and, where necessary, formal) involvement of Commission staff in FCM and DCO bankruptcy matters,[224] and (2) the fact that such discretion would not be unbounded and would apply only in particular circumstances, as discussed below.

Moreover, in response to a comment by ICI, and as discussed further below, the Commission is adding a clarification in § 190.00 that where a provision in part 190 affords the trustee discretion, that discretion should be exercised in a manner that the trustee determines will best achieve the overarching goal of protecting public customers as a class by enhancing recoveries for, and mitigating disruptions to, public customers as a class. The Commission is of the view that adding this principles-based provision will further clarify the duty of trustees in commodity broker bankruptcy proceedings to act in a

[221] The alternative, to forego providing such flexibility or discretion, would invert the benefits and costs discussed below.

[222] As discussed above, *see* section II.B.2, while the trustee has discretion as to how they administer the affairs of the bankruptcy estate, a DCO of which that FCM is a member retains its rights to act under its rules.

[223] Certain discretionary decisions a trustee may take, for example, the frequency with which the trustee provides information.

[224] As a formal matter, the Commission has the right to appear and be heard on any issue in any such case. *See* 11 U.S.C. 762(b). As a practical matter, trustees and their counsel have, in previous commodity broker bankruptcies, consulted with Commission staff frequently and on an ongoing basis, particularly in making and implementing important decisions.

manner that adds benefits, and reduces costs, to public customers as a class by, respectively, enhancing their recoveries and mitigating disruptions to them.

However, channeling the trustee's discretion towards protecting public customers as a class may well work to the detriment of (and thus impose costs upon) individual public customers, or classes of public customers, whose interests differ from that of the class in general. For example, certain customers may have a particular need for current and precise information about their account balances and positions.[225] It is possible (though unlikely) that the trustee might determine that it is inordinately costly to do so for a particular time, looking at the interests of public customers as a class. Such a decision would not be a mistake or malfeasance, though one would expect the trustee to endeavor to avoid the necessity for doing so.

An additional risk related to increased discretion is the possibility that parties that are dissatisfied with the trustee's exercise of discretion may challenge it in court, potentially leading to increased litigation costs. The Commission believes that this risk is mitigated by (1) the fact that certain of these decisions would be made in contexts where the trustee would be seeking an order of the bankruptcy court approving the trustee's approach (and thus the trustee's discretion would be subject to judicial review within a proceeding in which interested parties already have an opportunity to object) and (2) the likelihood that bankruptcy courts would respect the Commission's rules granting the trustee discretion, rendering such litigation less likely to succeed, and quicker to resolve. Litigation that is less likely to succeed is less likely to be brought, and litigation that is quicker to resolve is likely to cost less. Thus, by granting the trustee discretion, the Commission mitigates the cost of such litigation.

Instances where the revisions to proposed part 190 will afford more flexibility or discretion to the bankruptcy trustee are discussed in further detail where they appear in each provision below.

c. Cost Effectiveness and Promptness Versus Precision

In revising part 190, the Commission has endeavored to effect a proper balance between cost effectiveness and promptness, on the one hand, and precision, on the other hand. Current part 190 favors cost effectiveness and promptness over precision in certain respects, particularly with respect to the concept of *pro rata* treatment. As a result of the policy choice made by Congress in section 766(h) of the Bankruptcy Code, part 190 proceeds from the principle that it is more important to be cost effective and prompt in the distribution of customer property (*i.e.,* in terms of being able to treat public customers as part of a class) than it is to value each customer's entitlements on an individual basis. The revisions to part 190 take this concept further, recognizing that there are additional circumstances where cost effectiveness and promptness in the administration of a bankruptcy proceeding should have higher priority than precision. However, in response to ICI's comment, the Commission has clarified that where the trustee is directed to exercise ''reasonable efforts'' to meet a standard, those efforts should only be less than ''best efforts'' to the extent that the trustee determines that such an approach would support the goal of protecting public customers by enhancing recoveries for, and mitigating disruptions to, public customers as a class.[226] Thus, the Commission recognizes that there are limits to the extent to which cost effectiveness and promptness will be favored over precision as discretion must be exercised in furtherance of the overarching goal of protecting the interests of public customers as a class.

The Commission believes that these revisions favoring cost effectiveness and promptness over precision further the policy embodied in section 766(h) of the Bankruptcy Code and benefit parties involved in a bankruptcy proceeding overall, in that they will in general lead to: (1) A faster administration of the proceeding; (2) public customers receiving their share of the debtor's customer property more quickly; and (3) a decrease in administrative costs.

There could, however, be corresponding costs to this approach for some public customers in that they may lose out on being treated precisely in terms of their individual circumstances (and, for example, may receive a smaller distribution of customer property than otherwise).

d. Unique Nature of Bankruptcy Events

The Commission recognizes in revised part 190 that there is no one-size-fits-all approach to the administration of the bankruptcy of an FCM or a DCO, and that it is important that the rules allow the trustee, in conducting that administration, to take into account the unique nature of each of these events. The revisions to proposed part 190, therefore, address the uniqueness of these bankruptcy events and allow for the bankruptcy trustee to tailor their approach in the way that most makes sense given the individual circumstances of the case at hand.[227] History has shown that FCM bankruptcies play out in very different ways, and several of the Commission's revisions to part 190 address that reality. These new provisions reflect the fact that each FCM and DCO bankruptcy presents individual circumstances, and that the proof of claim form will likely have to be modified to fit the unique facts and circumstances of each case. The Commission believes that the revisions of this type will benefit all parties involved in a bankruptcy proceeding by better tailoring such a proceeding to the unique needs of the particular case.

However, by providing for a bespoke tailoring of the approach to commodity broker bankruptcy, the Commission inherently provides less transparency, and thus less certainty, of the particulars of the approach that will be followed.

e. Administrative Costs are Costs to the Estate, and Often to the Customers

In many instances in this adopting release, the Commission is noting that a certain provision will impose or reduce administrative costs, that is, the actual and necessary costs of preserving the bankruptcy estate and administering the case. In each of these cases, administrative costs will be a cost to the estate of the debtor, since administrative expenses that the bankruptcy trustee incurs in administering the estate (including for the time of the trustee, accountants, counsel, consultants, etc.) [228] will be passed onto the estate

[225] *See* ICI at 22 (failure of trustee to provide account statements or information about funded balances could ''hinder the ability of a regulated fund to confirm the existence and value of its transactions and associated margin.'')

[226] *See* comparison of best efforts to reasonable efforts in section II.A.1 above.

[227] Circumstances that may vary include: The accuracy of the commodity broker's records at the time of bankruptcy; whether the bulk of an FCM's customer accounts were transferred in the days after the filing date (or otherwise migrated in the days before); the number of customer accounts; the existence and extent of a shortfall in customer funds; and the complexity of the positions carried by the commodity broker.

[228] Pursuant to section 503(b)(1) of the Code, administrative costs include the actual, necessary costs and expenses of preserving the estate; and pursuant to section 330(a)(1)(A) of the Code, the Court may award ''reasonable compensation for actual, necessary services rendered by the trustee . . . professional person, or attorney . . . .'' Factors that are considered in determining ''reasonable compensation'' include the time spent on the services, the rates charged, the customary compensation charged by comparably skilled

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itself. This means that, in the event of a shortfall, such costs will ultimately be borne by the public customers of the debtor, who will receive smaller dividends on their claims as the value of the debtor's estate decreases.[229] By a parity of reasoning, reducing such administrative costs will reduce the shortfall, and increase recoveries by public customers.

To be sure, the actions taken to achieve these cost efficiencies that enhance the value of the estate for public customers as a whole may impose costs on individual public customers.

f. Preference for Public Customers Over Non-Public Customers and for Both Over General Creditors

As noted repeatedly above, and consistent with the requirements of section 766(h) of the Bankruptcy Code and longstanding Commission policy, many provisions in part 190 favor public customers over non-public customers, and both over general creditors, whenever there is a shortfall in customer property in any account class for public customers (or, with reference to general creditors, for non-public customers).

The preference for public customers benefits them, and provides them with incentives to participate in transactions protected by part 190, and to post collateral willingly. However, this preference correspondingly disfavors non-public customers. Accordingly, it arguably provides them with incentives to participate less in transactions protected by part 190—or, perhaps, to clear through unaffiliated FCMs (and thus, to do so as public customers of those FCMs).

Similarly, the preference for both public and non-public customers over general creditors may incentivize general creditors to be less willing to extend credit to commodity brokers. However, in light of the fact that commodity brokers are highly regulated entities subject to stringent capital or resource requirements, this incentive effect with respect to general creditors is not likely to be strong.

practitioners, and whether the services were necessary to the administration of the case. *See generally* 11 U.S.C. 330(a)(3).

[229] While such costs may in certain cases be borne instead by general creditors, section 766(h) permits customer property to be used to meet ''claims of a kind specified in section 507(a)(2)'' of the Bankruptcy Code (which in turn include claims for the expenses of administering the estate) ''that are attributable to the administration of customer property.''

B. Subpart A—General Provisions

1. Regulation § 190.00: Statutory Authority, Organization, Core Concepts, Scope, and Construction: Consideration of Costs and Benefits

Section 190.00 contains general provisions applicable to all of part 190. These provisions set forth the concepts that guide the Commission's bankruptcy regulations. All of § 190.00 is new, in that current part 190 does not contain an analogous regulation. However, only certain provisions within § 190.00 have cost-benefit implications, since the bulk of § 190.00 is designed to explain concepts that are either (1) not different from those contained in current part 190, but are simply stated more explicitly in the revised rules, or (2) new, in that they are not contained in current part 190, but are concepts that are meant to clarify how revised substantive provisions operate. In the latter case, cost and benefit considerations are addressed with respect to the substantive provisions.

The Commission requested comment on all aspects of its cost and benefit considerations with respect to proposed § 190.00.

There are potential costs associated with § 190.00(c)(4) which promotes the transfer or porting of the open commodity contract positions of a bankrupt FCM's public customers rather than the liquidation of these positions. For example, OCC commented that while liquidating customer positions may introduce market risk associated with closing out and reopening positions for certain customers, those risks should be weighed against the potential drawbacks of porting, especially if an FCM to accept the transfer is not immediately identified. Specifically, OCC identified three potential drawbacks with the proposed § 190.00(c)(4). First, that it could be difficult for a trustee (or DCO) to identify a transferee to accept the open positions and collateral, which depending on the market conditions could be a difficult and time-consuming process. Second, a customer could face uncertainty as to how its position and associated collateral will be resolved until a transfer is complete and also may be unable to exit a position in a timely and efficient manner. Third, a customer might need to post additional collateral at a new FCM prior to or immediately after a transfer.

In considering the costs and benefits of the preference for transfer versus liquidation, the Commission notes first that, as OCC forthrightly acknowledged, liquidating customer positions may introduce market risk associated with closing out and reopening positions for certain customers. Additionally, liquidating a mass of customer positions may roil the markets, if any, where those positions are concentrated.

Furthermore, § 190.00(c)(4) establishes a *preference* for transfer rather than a *mandate.* Thus, if after exerting their best efforts, the trustee finds that the process of transfer is indeed too ''difficult and time-consuming,'' the trustee is not obligated to implement a transfer. Moreover, as a practical matter, there are narrow limits to how long a trustee will have to endeavor to transfer before being compelled to liquidate positions by the DCO at which they are held, or, if applicable, an FCM through which they are held. (Either the DCO or the FCM, whichever is applicable, will have the discretion to liquidate positions that are being cleared/carried for an FCM that is in bankruptcy).[230] Pursuant to § 190.04(d), if the trustee is not successful in transferring an open contract by the seventh calendar day after the order for relief consistent with § 190.04(a), the trustee is directed to liquidate such contract promptly and in an orderly manner. Thus, while a customer could face uncertainty as to how its position and associated collateral will be resolved until a transfer is complete (or until the customer's positions are otherwise liquidated), the time of that uncertainty is both practically and legally limited. Finally, a customer who does not wish to post additional collateral at a new FCM would be entitled to have the new FCM liquidate their positions, and promptly receive any remaining transferred collateral. In this light, the Commission believes that the benefits of continuing the preference for transfer remain significant, while the costs of this preference are mitigated.

There are potential benefits arising from reduced uncertainty as a result of clarifications provided in several provisions. For example, § 190.00(d)(1)(ii), clearly expresses that part 190 applies to a proceeding commenced under SIPA with respect to a debtor that is registered as a broker or dealer under the CEA when the debtor also is an FCM. Similarly, § 190.00(e) clarifies how transactions and collateral that are portfolio margined are treated as an important prerequisite to an effective portfolio margining program. Cboe's comment letter expressed the view that the clarity provided in § 190.00(d)(1)(ii) will be beneficial to the entire

[230] For example, as noted above in section II.A.1, OCC's own rules would appear to permit it to liquidate such positions.

ecosystem, including customers of FCMs and broker-dealers, as it furthers the ability of market participants to utilize portfolio margining and the associated efficiencies. CME also saw benefits to ''remov[ing] any doubt'' that part 190 applies to a SIPA proceeding involving an FCM that is also registered with the SEC as a broker-dealer.

Similarly, ICI's comment letter considered that the ''home field'' rule in § 190.00(e) is highly beneficial.

With respect to the remaining provisions within proposed § 190.00, the Commission has not received comment letters that identify costs or benefits explicitly attributed to these provisions, and does not believe that there are material cost-benefit implications with respect to them:

- Proposed § 190.00(a), which sets forth the statutory authority pursuant to which the Commission is proposing to adopt proposed part 190.
- Proposed § 190.00(b), which describes how the proposed rules are organized into three subparts. While the addition of DCO-specific rules in this proposal is new, the cost-benefit implications of the DCO-specific provisions (§§ 190.11 through 190.18) are discussed separately below.
- Section 190.00(c)(2), which provides that part 190 establishes four separate account classes, each of which is treated differently under the regulations. In the Commission's view, this provision is a mere clarification, as current part 190 also establishes different account classes for different types of cleared commodity contracts, and treats each account class differently.
- Section 190.00(c)(5), which explains that part 190 applies the concept of *pro rata* distribution when it comes to shortfalls of property in a particular account class. This provision is merely explanatory.
- Section 190.00(d)(1)(i)(A), which provides that the definition of ''commodity broker'' in proposed part 190 covers both ''futures commission merchants'' and ''foreign futures commission merchants'' because both are required to register as FCMs under the CEA and Commission regulations.
- Section 190.00(d)(2)(i), which states that the bankruptcy trustee may not recognize any account class that is not one of the account classes enumerated in proposed § 190.01.
- Section 190.00(d)(3), which sets forth the transactions that are excluded from the definition of ''commodity contract.'' This provision explains and carries over concepts that are already embedded in current part 190.

While the Commission has not received comment letters that identify costs or benefits explicitly attributed to the following provisions in § 190.00, it believes that there will be cost-benefit implications to these provisions:

- Section 190.00(c)(1) states that part 190 is limited to a commodity broker that is (1) an FCM as defined by the CEA and Commission regulations, or (2) a DCO under the CEA and Commission regulations. Current part 190 applies to a broader set of ''commodity brokers,'' including FCMs, clearing organizations, commodity options dealers, and leverage transaction merchants. This narrowing of the application of part 190 (by excluding the empty categories of commodity options dealers and leverage transaction merchants) benefits the bankruptcy estate, and the customers, by allowing the Commission to promulgate regulations that are less complex and better tailored to the narrower, set of commodity brokers that are covered by the revised regulations.[231]
- Section 190.00(c)(3) explains the distinction between ''public customers'' and ''non-public customers,'' and the priority that public customers (and, after them, non-public customers) enjoy over all other claimants with respect to distributions of customer property. Both of these concepts exist in current part 190 and are clarified and explained further in § 190.00(c)(3). In its comment, ICI urged the Commission to take steps ''to help ensure that the trustee prioritizes the protection of [public] customers.'' In response, Commission has added a provision, § 190.00(c)(3)(i)(C), directing the trustee to exercise its discretion (where it has such discretion) in a manner that will best achieve the overarching goal of protecting public customers by enhancing recoveries for, and mitigating disruptions to, public customers as a class.[232] This approach has the benefit of guiding the trustee's discretion in a manner consistent with the Commission's regulatory and statutory goals. However, it has the limitation of still leaving the trustee with discretion. As noted above in section III.A.2 above, with discretion comes a risk of trustee mistake or misfeasance.
- Section 190.00(c)(6) addresses the treatment of commodity contracts that require delivery performance. The revised regulations, in allowing the trustee more flexibility in how a customer could effect delivery outside of the debtor's estate, will benefit customers by allowing for a more bespoke approach to effecting delivery when customers incur delivery obligations under their open commodity contracts. There will, however, be costs in acting in such a bespoke fashion in contrast to following standards established during business as usual.
- Section 190.00(d)(1)(i)(B) notes that while there are currently no registered leverage transaction merchants or commodity options dealers, the Commission intends to adopt rules with respect to leverage transaction merchants or commodity options dealers at such time as an entity registers as one of those categories of commodity brokers. This forward-looking flexibility will generate benefits by fostering bankruptcy rules specifically tailored to leverage transaction merchants or commodity options dealers when and if an entity registers as such.
- Section 190.00(d)(1)(iii), provides that part 190 shall serve as guidance as to the distribution of customer property and member property in a proceeding in which the FDIC is acting as receiver pursuant to Title II of Dodd-Frank.[233] This provision has the benefits associated with transparently providing to FDIC during business-as-usual the expertise and guidance of the agency with regulatory and supervisory responsibility for commodity brokers (*i.e.,* FCMs and DCOs).[234]
- Section 190.00(d)(2)(ii) provides that no property that would otherwise be included in customer property shall be excluded from customer property because it is considered to be held in a constructive, resulting, or other trust that is implied in equity. It prevents public customers from evading *pro rata* exposure to shortfalls in customer property by keeping their collateral in a trust structure. This provision has the

[231] Moreover, prescribing regulations that are intended to be applicable to entities that, at some unknown point in the future, enter these empty categories risks poor tailoring due to lack of data concerning the characteristics of those unknown future entrants.

[232] As noted above in section III.A.2.vi, the preference for public customers over non-public customers creates incentives for both groups.

[233] Section 210(m)(1)(B) of title II,12 U.S.C. 5390(m)(1)(B), requires the FDIC, where the covered financial company or bridge financial company is a commodity broker, to apply the provisions of subchapter IV as if the financial company were a debtor for purposes of such subchapter.

[234] DCOs operate nearly 24-hours a day, between Sunday afternoon and Friday evening. Moreover, the risks that a DCO is required to manage are based on market movements and events (including in OTC markets) that may occur whether or not the DCO is able to operate. Accordingly, Commission staff (in cooperation with FDIC staff) have engaged, and will continue to engage, in significant efforts to plan for the unlikely event that resolution under Title II would be necessary for a DCO.

Thus, there is a public benefit to facilitating FDIC's efforts in resolution planning for DCOs by setting forth clear guidance as to the distribution of customer property and member property in a DCO resolution proceeding.

benefit of supporting the statutory policy of *pro rata* distribution for the pool of customers, by ensuring that all property that properly belongs in the category of ''customer property'' would be considered such customer property. It should mitigate costs in cases where particular customers might structure their relationships with their FCMs in order to establish such a trust for the purpose of thwarting their exposure to *pro rata* distribution, rather than structuring those relationships in ways that otherwise make sense for their business. It would also reduce those customers' incentives to do so, and would mitigate the costs of litigation within the bankruptcy proceeding over the effectiveness of such structures in achieving that goal. It also benefits the remaining customers, since if such litigation were successful, it would spread the *pro rata* shortfall over a smaller volume of customer claims.

- However, this approach will impose costs on those customers, if any there be, who would otherwise endeavor to rely on the trust concept to shield certain of their property from entering the pool of customer property. Such customers might (despite opposition from the Commission and the trustee) otherwise be successful in litigation over the effectiveness of such arrangements, or may obtain settlements that would benefit their individual claims (albeit to the detriment of other customers, and to the policy of *pro rata* distribution). Such customers may view the inability to protect their collateral under a trust concept as an incentive to reduce their use of transactions subject to part 190.

2. Regulation § 190.01: Definitions: Consideration of Costs and Benefits

Section 190.01 sets forth definitions as they are used for purposes of part 190. In the Commission's view, only certain of the definitions in proposed § 190.01 will have cost-benefit implications, and these are discussed in more detail below, as are any definitions concerning which there were comments. The remainder of the definitions set forth in revised § 190.01 do not, in the Commission's view, impose any costs or benefits, as the changes to the definitions are minor (in the vein of, for example, updating cross-references or updating language to reflect the changes in the rest of revised part 190) or merely clarify the current definition.

Where, in the Commission's view, a definition in revised § 190.01 has cost-benefit implications, and/or where comments have identified costs or benefits concerning such a definition, those implications are discussed in more detail below:

- ''Account class,'' ''cash delivery property,'' and ''physical delivery property'': The definition of the term ''account class'' is expanded to include definitions of each type of account class set forth in proposed part 190: Futures account, foreign futures account, cleared swaps account, and delivery account. The ABA Subcommittee recommended that the Commission clarify that these types of account classes apply to non-public customers in addition to public customers. The Commission agrees that it is appropriate to clarify this point, and to include a specific definition for each type of account class. Doing so will benefit all parties involved in a bankruptcy proceeding by ensuring that all have a common understanding of how these various types of accounts are defined for purposes of part 190. Accordingly, the Commission is adopting the ABA Subcommittee's recommendation.
- The definition of ''account class'' also removes the category in current part 190 of ''leverage account'' because, as noted above, there are currently no registered leverage transaction merchants. Rather, the Commission intends to adopt rules with respect to leverage transaction merchants (and, accordingly, with respect to leverage accounts) at such time as an entity registers as such. Removal of the category of ''leverage account'' from the ''account class'' definition benefits market participants by allowing the Commission to promulgate bankruptcy rules specifically tailored to leverage transaction merchants (and, accordingly, to leverage accounts) in the event an entity registers as such.
- The definition of ''account class'' also splits ''delivery accounts'' into separate physical and cash delivery account classes. Because cash delivery property is, in some cases, more difficult to trace to specific customers and more vulnerable to loss,[235] this separate treatment of physical delivery property and cash delivery property should benefit customers with physical delivery property by allowing for more prompt distribution of such physical delivery property. This separation should also benefit the estate, because the trustee will not have to wait to distribute physical delivery property to customers while attempting to trace cash delivery property, which could result in a more prompt resolution of the bankruptcy as a whole. However, there may be costs as a result of complications, since the trustee will have to deal with two delivery account subclasses rather than one delivery account class. Moreover, in the event of a shortfall, some customers could ultimately obtain larger recoveries than they would have if the delivery account had not been split into two subclasses, while others could obtain smaller recoveries.

The ABA Subcommittee and CME suggested changes to the definition of ''cash delivery property.'' Under the current definition, cash falls within the delivery class if, *inter alia,* it is received on or after three calendar days before the first notice date or exercise date. The definition of cash delivery property in the Proposal continued that limitation. CME suggested that the three-day limitation should be removed to address cases where

> ''a customer will legitimately post cash to its delivery account sooner than the definition would allow, for example, out of caution to assure that the necessary funds are available to pay for a delivery when the first notice date or exercise date immediately follows a weekend or holiday, or to meet payment deadlines imposed by the FCM, or based on market convention.''

The comments acknowledged that the Commission's policy objective is to ''encourage FCMs and their delivery customers to hold cash intended to pay for delivery in a segregated account until bilateral delivery obligations are near at hand'' (the segregation obligations that apply to futures, foreign futures, and cleared swaps accounts do *not* apply to delivery accounts), but express some doubt that the limitation is effective in encouraging the desired behavior, because parties with delivery obligations may not be aware of it.

Thus, the benefit of retaining the three-calendar day limitation is mitigating the time during which cash delivery property is held in an account that is not subject to the protection of segregation requirements, and in encouraging business models that take that approach. The cost of doing so is the risk that funds may nonetheless be transferred earlier into a delivery account, and would then be denied protection as delivery property in an FCM bankruptcy.[236]

As discussed above,[237] the Commission has determined to take a middle-ground approach by expanding the three-calendar day limitation to a

[235] These reasons for this difficulty and vulnerability are discussed above in section II.B.4 in the explanation of the changes to proposed § 190.06(b).

[236] The Commission also notes CME's suggestion that it ''consider adopting more formal requirements with respect to delivery accounts through separate rulemaking.''

[237] *See* section II.A.2 above.

seven-calendar day limitation. This approach has the benefit of addressing fully the possibility that delivery property is transferred slightly early because of, *e.g.,* a holiday weekend (and especially cases where FCMs and their customers or contracts span across jurisdictions with different holidays). By expanding the period by four days, it should address most of the cases where there are legitimate reasons to transfer the funds in advance of when they are needed, to account for the possibility of a failure in the transfer process.[238] Significantly, it avoids the cost of encouraging the use of the delivery account (that is not subject to segregation requirements) as a long-term place to hold cash.

Commenters also suggested technical additions to the definitions of cash delivery property (to address cash provided post-petition to facilitate taking deliveries in cases where necessary) to physical delivery property (to address the possibility of a negative final settlement price), and (in the case of both cash delivery property and physical delivery property) to provide that, for contracts exchanging one fiat currency for another, both ends of the transaction would be considered cash delivery property. The Commission incorporated these suggestions in the definitions as adopted. The benefit of these approaches is to deal properly with these scenarios; there are no discernable material costs.

• Pursuant to section 4d of the CEA, certain contracts and associated collateral that would be associated with one account class may instead (pursuant to Commission regulation[239] or order) be commingled with a different account class.[240] The purpose of these arrangements, referred to as portfolio-margining, is to associate such contracts with an account class in which they are risk-reducing related to other contracts in that latter account class.

Paragraph (2) of the definition of account class confirms that these portfolio-margining arrangements will be respected in bankruptcy, that is, such contracts and associated collateral will be treated as being part of the account class into which they are commingled. The benefit of this treatment in bankruptcy is to foster and incentivize such risk-reducing (and capital-efficient) arrangements during business as usual; there should be no associated costs in bankruptcy.

Finally, paragraph (3) of the definition of account class addresses cases where a commodity broker's account for a customer is non-current, or otherwise inaccurate. These are situations over which public customers have, at best, limited control, and thus it is ineffective to endeavor to create incentives for public customers to police the behavior of their FCM. Paragraph (3) confirms that a commodity broker is considered to maintain an account for a customer where it establishes internal books and records for the customer's contracts and collateral and related activity, regardless of whether the commodity broker has kept those internal books or records current or accurate. The benefit of this treatment will be to treat customers in accordance with their entitlements, regardless of whether the commodity broker has maintained its books and records current or accurate.

• ''Customer,'' ''Customer class,'' ''public customer,'' and ''non-public customer:'' The definitions of the terms ''public customer'' and ''non-public customer'' are being revised to include separate definitions of those terms for FCMs and DCOs. This change reflects the new organization of part 190, which includes separate provisions for when the debtor is (1) an FCM (subpart B) and (2) a DCO (subpart C). The ''public customer'' definition for FCMs is also being revised to define that term with respect to each of the relevant account classes.[241]

These changes will generate benefits as they bring clarity to the question of who qualifies as a ''public'' versus a ''non-public'' customer, and transparency to the distribution of property to which each customer is entitled. Furthermore, this clarity and transparency is likely to reduce the administrative costs to the estate, and the costs to claimants, associated with the claims allowance process, as well as the likelihood of litigation by dissatisfied claimants (and associated costs). These changes could, however, impose costs on customers for whom, under current part 190, it will not be clear which category they fall into. The pool of customer property would be different for public and non-public customers under the new policy regime. Thus, a hypothetical customer who could have been considered ''public'' under current part 190 but will be categorized as ''non-public'' under revised part 190 could receive less in the distribution of customer property (with other customers receiving more).

• ''Futures, futures contract:'' The Commission is adding a definition for the terms ''futures'' and ''futures contract'' to clarify what those terms mean for purposes of part 190. This clarification will lower administrative costs by providing clarity and transparency to the types of transactions that are considered ''futures'' for purposes of proposed part 190 and therefore form part of the futures account or foreign futures account.

• ''House account:'' The definition of the term ''house account'' will be revised to include a definition of that term solely for DCOs. This change will reflect the new organization of part 190, which is revised to include separate provisions for when the debtor is (1) an FCM (subpart B) or (2) a DCO (subpart C). CME and the ABA Subcommittee urged that the term ''house account'' be deleted in the few cases where it was proposed to be used in subpart B in order to avoid the implication that the accounts of non-public customers could not be ported. This change would enhance clarity and transparency (and, thus, would reduce administrative costs) by (1) avoiding that incorrect implication, while (2) clarifying what precisely constitutes a house account for a DCO bankruptcy proceeding.

• ''Primary liquidation date:'' The definition of the term ''primary liquidation date'' is being revised to delete references to holding accounts open for later transfer. This is consistent with the policy of transferring as many open commodity contracts as possible within seven calendar days after entry of an order for relief or, if that is not possible, liquidating such commodity contracts. [242] This change in policy should benefit some customers, who will more quickly have clarity as to how their positions and associated collaterals will be resolved.[243] There may, however, be costs to customers who might have preferred having their open commodity contracts held open for transfer after the primary liquidation

[238] The commenters have not identified any legitimate reason for an FCM to impose a payment deadline of more than seven days before first notice or exercise date, or any relevant market convention that would require earlier payment, which in either case would require that the funds be held in a delivery account.

[239] *See* § 39.15(b)(2), which provides a mechanism for these arrangements to be implemented pursuant to clearing organization rules.

[240] Securities positions may also be commingled in an account class subject to section 4d of the CEA. 7 U.S.C. 6d.

[241] CME suggested that the Commission should include non-U.S. customers of foreign broker clearing members of a DCO within the public customer definition. As discussed above, the Commission has determined to consider this suggestion as part of a comprehensive review of the issues, to be conducted at such time as the model of admitting foreign brokers as clearing members for U.S. DCOs becomes empirical.

[242] *See* § 190.04(a)(1).

[243] *See* discussion of § 190.00(c)(4) in section II.B.1 above for concerns about customers lacking such clarity for an extended time.

date. [244] In the event that a larger number of contracts is liquidated rather than transferred, there will be costs resulting from additional downward pressure on prices.

- ''Specifically identifiable property:'' The Commission is revising the definition of the term ''specifically identifiable property'' to clarify and streamline the current definition of that term. The use of definitions that are clearer should reduce administrative costs. Of course, increasing clarity may be to the detriment of those customers for whom such clarity results in assignment to a category that they view as less favorable.
- ''Substitute customer property:'' The definition of the term ''substitute customer property'' is being added to refer to cash or cash equivalents delivered to the trustee by or on behalf of a customer in order to redeem specifically identifiable property or a letter of credit. This provision will benefit customers who, in a bankruptcy event, seek to redeem their specifically identifiable property or letters of credit.[245] Introducing the concept of substitute customer property may impose administrative costs, however, because the trustee may have to expend time and resources on tracking the substitute customer property and ensuring that such property ends up in the proper pool of customer property once received.
- ''Swap:'' The Commission is amending the definition of ''cleared swap'' that appears in the current rules in order to clarify what this term means for purposes of proposed part 190. This clarification should serve the goals of clarity and transparency (and, consequently, reducing administrative costs).

3. Regulation § 190.02: General: Consideration of Costs and Benefits

Section 190.02(a)(1) is revised to provide that the bankruptcy trustee may, for good cause shown, request from the Commission an exemption from the requirements of any procedural provision in proposed part 190. This is in contrast to current § 190.10(b)(1), which provides only that a bankruptcy trustee may request an exemption from, or extension of, any time limit prescribed in current part 190. This expanded mechanism for a trustee to request exemptions should benefit the estate and customers by allowing the trustee to request an exemption that lowers administrative costs and increases timeliness. This change, however, may impose administrative costs if the trustee's request is ill-founded and the Commission were nonetheless to grant the request.

The Commission does not believe that there will be any cost-benefit implications to § 190.02(a)(2) and (3), (b), (c), (d), and (e), as those provisions largely align with the provisions in current part 190 from which they are derived.

Regulation § 190.02(f) is a new provision which addresses the context of a receiver for an FCM appointed due to a violation or imminent violation of the customer property protection requirements of section 4d of the CEA or of the regulations thereunder, or of the FCM's minimum capital requirements in § 1.17. In this context, the FCM has been found to be in precarious financial condition. This provision will permit the receiver to file a petition for bankruptcy of such an FCM in appropriate cases. This provision may benefit public customers, in that a bankruptcy proceeding may be necessary to protect those customers' interests in customer property from losses in value. However, this provision may have distributional effects as there may be some customers who do not receive as much in bankruptcy as they otherwise would have under the receivership. In addition, there could be additional administrative costs that result from this provision, as the bankruptcy trustee would have to spend time and resources overseeing a bankruptcy proceeding that might not be entered into absent the power granted to the receiver under this regulation. These costs could possibly be greater than the costs of continuing to administer the FCM under receivership.

Indeed, FIA suggested that the Commission should require that the receiver must receive permission from the Commission before filing a voluntary petition, given that this action ''would effectively close the FCM.'' Closing the FCM would impose significant costs on the FCM and, in a case where the Commission would have denied permission, those costs could be unnecessary.

In considering the costs (discussed above) of what could be an unnecessary voluntary filing for bankruptcy in contrast to the benefits of avoiding delay in filing a necessary filing for bankruptcy, the Commission determines that the context where this rule would be applicable—only cases where a receiver has been appointed due to violation or imminent violation of customer property protection requirements, or of the FCM's minimum capital requirements—minimizes the likelihood that a filing would turn out to be unnecessary, and counsels in favor of avoiding delay.

4. Section 15(a) Factors—Subpart A

No comments were received on the application of the section 15(a) factors to subpart A.

i. Protection of Market Participants and the Public

Subpart A of the proposed rules should increase the protection of market participants and the public by clearly setting forth how customers of FCMs and DCOs will be classified and treated, and how their accounts will be categorized and treated, in the event of an FCM or DCO insolvency. The goal of subpart A of the proposed rules is to promote an orderly and cost-effective resolution of the insolvency of an FCM or DCO, and to increase transparency to the customers of FCMs and DCOs as to how their property would be treated in the event of such an insolvency. However, as noted above, some of the provisions of subpart A provide discretion to the trustee. While enhanced discretion for the trustee has the benefit of permitting a more tailored approach, it also has the cost of increasing the possibility of trustee mistake or misfeasance.

ii. Efficiency, Competitiveness, and Financial Integrity

Subpart A of the proposed rules should promote efficiency (in the sense of both cost effectiveness and timeliness) in the administration of insolvency proceedings of FCMs and DCOs and the financial integrity of derivatives transactions carried by FCMs and/or cleared by DCOs by clearly communicating the goals and core concepts involved in such insolvencies, and by setting forth clear definitions that have been updated to account for current market practices. These effects should, in turn, enhance the competitiveness and financial integrity of U.S. FCMs and DCOs, by enhancing market confidence in the protection of public customer funds and positions entrusted to U.S. FCMs and DCOs, even if such an entity were to become insolvent.

iii. Price Discovery

Price discovery is the process of determining the price level for an asset

[244] Given that the clearing organization for such contracts may not be willing to permit such contracts to be held open for an extended period of time, the existence of such customers is quite hypothetical.

[245] Benefits and costs associated with the use of substitute customer property are addressed further below in connection with § 190.04(d)(3) in section III.C.2.

through the interaction of buyers and sellers and based on supply and demand conditions. To the extent that the revised regulations should mitigate the need for liquidations in conditions of distress, they will help avoid negative impacts on price discovery.

iv. Sound Risk Management Practices

Subpart A of the proposed rules should generally promote sound risk management practices by setting forth the core concepts to which the bankruptcy trustee must adhere in administering an FCM or DCO bankruptcy.

v. Other Public Interest Considerations

Some of the FCMs or DCOs that might enter bankruptcy are very large financial institutions, and some are (or are part of larger groups that are) considered to be systematically important. A bankruptcy process that effectively facilitates the proceedings is likely to help to attenuate the detrimental effects of the bankruptcy on the financial marketplace and thus benefit the financial system and thus the public interest.

C. Subpart B—Futures Commission Merchant as Debtor

1. Regulation § 190.03: Notices and Proofs of Claims: Consideration of Costs and Benefits

Section 190.03(a)(1) replaces the requirement in current § 190.10(a) that all mandatory or discretionary notices be sent to the Commission via overnight mail with the requirement of sending the notices by electronic mail.[246] This change is expected to result in a benefit to all parties required to provide notices to the Commission because they will be able to avoid the costs of sending such notice in hardcopy form via overnight mail. These revisions will also allow the Commission to receive such notices—and thus, to act—much more expeditiously.

Section 190.03(a)(2) is a new, principles-based provision that replaces the more specific procedures for providing notice to customers that appear in current § 190.02(b) by allowing the trustee to establish and follow procedures ''reasonably designed'' for giving adequate notice to customers. Paragraph (a)(2) also provides that the trustee's procedures for providing notice to customers should include ''the use of a prominent website as well as communication to customers' electronic addresses that are available in the debtor's books and records.'' A generalized and more modernized approach to notifying customers will benefit the debtor's estate, as the process allows the trustee to choose cost effective means of providing notice to customers within the more flexible bounds of the proposed regulation, resulting in savings of administrative costs. Similarly, it will benefit parties interested in the proceedings, by permitting the trustee flexibly to choose methods of notification that are more prompt and effective. On the other hand, affording the trustee increased discretion in how to provide notice to customers will carry the potential cost of trustee misfeasance and abuse of such discretion, as discussed above in section III.A.2.ii.

Section 190.03(b)(1) will revise the time in which a commodity broker must notify the Commission of a bankruptcy filing. These revisions codify procedures whereby (1) in a voluntary bankruptcy proceeding, the commodity broker will provide advance notice to the Commission ahead of the filing to the extent practicable, and (2) in an involuntary bankruptcy proceeding, the commodity broker will notify the Commission immediately upon the filing. These revisions will foster the ability of the Commission and its staff to perform their duties to protect customers by providing the Commission with notice of any bankruptcy proceeding as soon as possible.

Section 190.03(b)(2) removes the current deadline of three days after the order for relief by which the trustee, the relevant DSRO or a clearing organization must notify the Commission of an intent to transfer or to apply to transfer open commodity contracts in accordance with section 764(b) of the Bankruptcy Code. It instead instructs such parties to give such notice of an intent to transfer ''[a]s soon as possible.'' To the extent that the three-day deadline was limiting transfer arrangements, this revision will benefit the estate and some customers by removing time constraints that could be construed to prohibit notification after expiration of the deadline (and thus, allow the trustee to form the intent to transfer after such time).

The revision will also enhance the orderly functioning of the marketplace at a time of severe market disruption by facilitating prompt notice of intent to transfer. On the other hand, by giving the trustee, DSRO, or clearing organization more latitude for providing notice of an intent to transfer, there will be the potential cost of misfeasance in waiting an unreasonable amount of time to provide such notice (or to form such intent), which could ultimately impose additional costs on customers who would have benefited from an earlier transfer.[247]

Section 190.03(c)(1) removes the requirement that the trustee must publish notice to customers with specifically identifiable property in a newspaper of general circulation serving the location of each branch office of the debtor prior to liquidating such property and instead establishes a requirement to notify the customers with specifically identifiable property in accordance with § 190.03(a)(2). The Commission believes that this change will result in lower administrative costs, as the trustee will be relieved of the cost of identifying, and publishing notice in, such newspapers. Moreover, the trustee will no longer be required to wait seven days after the second publication date to commence liquidation of specifically identifiable property. Rather, the trustee will be free to commence liquidation of specifically identifiable property starting on the seventh day after entry of the order for relief. This will benefit the estate, and potentially the affected customers, by allowing the trustee more freedom (from the time constraints set forth in the current regulations) in liquidating the specifically identifiable property, which, in turn, is expected ultimately to result in a better price. Moreover, the provisions in § 190.03(a)(2) that describe the notification of customers with specifically identifiable property will benefit public customers by allowing them to receive notice on a ''prominent website'' and, more specifically, at their electronic addresses (to the extent such addresses are in the debtor's books and records), thereby enhancing their ability to request the return of their specifically identifiable property within the specified timeframe.

Section 190.03(c)(2) provides the bankruptcy trustee with authority to treat open commodity contracts of public customers held in hedging accounts designated as such in the debtor's records as specifically identifiable property.[248] This is a change from the current framework, under which the trustee treats customers with specifically identifiable property on a bespoke basis. Specifically, to the extent the trustee does not receive transfer instructions regarding a customer's specifically identifiable open commodity contracts, the trustee will be required to liquidate

[246] *See also* § 190.03(d), which is adopting this new method of providing notice to the Commission for any court filings filed in a bankruptcy.

[247] *See* discussion of § 190.00(c)(4) in section III.b.1 above.

[248] *See* proposed § 190.10(b)(2) for the process of designating an account as a ''hedging account.''

such contracts within a certain time period. To the extent the trustee exercises the authority derived from revised § 190.03(c)(2), they will (subject to the revision discussed in the next paragraph) be required to notify each relevant customer and request instructions whether to transfer or liquidate the open commodity contracts. To the extent the trustee would not exercise such authority, the trustee will treat these open commodity contracts the same as other customer property and effect a transfer of such contracts. This new framework should reduce administrative costs and benefit the bankruptcy estate by allowing the trustee to rely on hedging designations made during business as usual, thereby allowing the trustee to make swift and cost effective decisions regarding the treatment of open commodity contracts during a bankruptcy situation.

ACLI suggested that § 190.03(c)(2) should express a preference for transfer over liquidation with respect to specifically identifiable property in the form of positions that are identified as hedging positions, and consult (on an individual basis) each customer's expressed preferences. However, § 190.00(c)(4) sets forth a preference for porting (transfer) of *all* open commodity contract positions of public customers. Thus, while treating customers with hedging positions on a bespoke basis may benefit some of them, it may be at the cost of effectively transferring a larger group of customer positions. Some of those may be customers with hedging positions whose positions are not transferred due to limited time and resources available to be devoted to bespoke treatment. Indeed, SIFMA AMG/MFA noted that ''permitting the trustee this flexibility (subject to the additional customer protections [of consulting existing instructions, as described immediately below]) serves the interest of customers as a whole by facilitating a more rapid transfer of customer positions and property.''

SIFMA AMG/MFA suggested that it would ''further the goal of expediency'' if the regulation would require the trustee to ''first consult the instructions (regarding preferences with respect to transfer or liquidation of open commodity contracts) provided by a public customer to the debtor at the time of opening the relevant hedging account, and only if such instructions are missing or unclear, to then require such customer to provide the trustee with written instructions as contemplated by proposed § 190.03(c)(2).'' The Commission agrees, and has made corresponding changes to the regulation. While there is a cost involved in scanning to determine if there are instructions, there is a significant benefit in avoiding duplication, and in avoiding cases where the customer, having already provided instructions, does not reply to a duplicative request in time for that reply to be acted upon.

The Commission does not believe that there are any cost-benefit implications to § 190.03(c)(3) or (4) (other than those discussed above with respect to the new notice provision referenced in each) or to § 190.03(d).

Section 190.03(e), sets forth the information required from customers regarding their claims against the debtor. As revised, § 190.03(e), reorganizes and adds certain information items to those listed in the current regulation. The Commission anticipates that, while customers are likely to have this information at their disposal, there could be costs associated with gathering it all in one place. However, this additional and more detailed information should benefit the estate, the bankruptcy court and customers alike by allowing all parties to have a fuller, more detailed and more transparent picture of the customer claims against the debtor. It should foster the reduction of administrative costs and the prompt administration of the estate. Moreover, the Commission is of the view that clarifying several of the information items listed in proposed § 190.03(e) and revising the proof of claim form to match more closely the text of the regulation should result in benefits to all parties involved in an FCM bankruptcy—the estate, the bankruptcy court, and the customers—by making the bankruptcy claims process more prompt and cost effective. CME sees § 190.03(e) and (f), and the revised proof of claim form, as ''major improvements over the current rules and proof of claim template.''

This regulation also provides that the specific items referred to are to be included ''in the discretion of the trustee.'' This discretion will permit the trustee to tailor the information requested to the specifics of the debtor's prior business, as well as the already-available records. This will permit the trustee to limit or to increase the information requested, in appropriate cases, with a corresponding increase in cost effectiveness. To be sure, there may be corresponding costs (both in administrative expense and time) if the set of information requested by the trustee in the exercise of their discretion turns out, in retrospect, to be overly narrow (or broad).

Proposed § 190.03(f) is new and provides the trustee with flexibility to modify the customer proof of claim form set forth in appendix A to part 190. Specifically, § 190.03(f) allows the trustee to modify the proof of claim form to take into account the particular facts and circumstances of the case. This provision should benefit the estate because the trustee will be able to modify the proof of claim form in a way that gathers the information necessary in a manner that is both effective and cost effective based on the specific facts of the case, and the trustee no longer will be required to get an order from the bankruptcy court to make such modifications, thereby saving time and resources. This new provision should also benefit customers, who will be able to take advantage of the more streamlined and tailored proof of claim forms developed by the trustee, and should, therefore, spend less time filling out such forms. It should also benefit the estate, which should bear less administrative cost in evaluating such forms. Again, there may be corresponding administrative costs if the set of information in a modified proof of claim form turns out, in retrospect, to be overly narrow (or broad).

2. Regulation § 190.04: Operation of the Debtor's Estate—Customer Property: Consideration of Costs and Benefits

Regulation § 190.04(a) explicitly provides a policy and a direction by which the trustee should use best efforts to transfer open commodity contracts and property held by the failed FCM for or on behalf of its public customers. This policy and direction is substantially similar to the policy and direction under current regulations.[249] The changes set forth a clear policy for trustees to follow, which should benefit customers of the failed FCM in a streamlined description of the transfer process that is consistent with the core concepts set forth in this part. The costs and benefits of the preference for transfer are discussed in section III.B.1 above, in the context of § 190.00(c)(4).

In § 190.04(a)(1), the Commission is clarifying language; these clarifications should benefit customers of the failed FCM by minimizing the likelihood of future disputes concerning qualification of property for transfer. The Commission is also changing the direction in current § 190.02(e) that the trustee ''*must immediately* use its best efforts to effect a transfer'' to a direction that the trustee ''*shall promptly* use its best efforts to effect a transfer.'' This modest change in focus will benefit public customers by recognizing that,

[249] *See* current § 190.02(e).

while effecting transfer is an extraordinarily high priority, it is possible that there may be higher priorities at the inception of the bankruptcy proceeding, *e.g.,* it may be necessary to preserve some portion of customer property from an immediate threat.[250] Once again, by enhancing the trustee's discretion as to how to manage the liquidation, there is the cost that the trustee will make a mistake.

Section 190.04(a)(2) directs the FCM (or a trustee, if one has been appointed) in a case where an involuntary petition for bankruptcy is filed against the FCM to use best efforts to effect a transfer within seven calendar days. The current regulation limits the commodity broker to trading for liquidation unless otherwise directed by the Commission, by any applicable self-regulatory organization or by the court. Revised § 190.04(a)(2) removes this limitation. Rather, revised § 190.04(e)(4) more generally covers limitations on the business of an FCM in bankruptcy. Similarly, any requirement to transfer customer positions would more properly be addressed by § 1.17(a)(4). The Commission believes that these changes will benefit the estate and the public customers by mitigating the administrative costs by removing a redundant regulation. The Commission does not anticipate any resulting increase in cost.

In § 190.04(b)(1), the Commission is clarifying and updating conditions under which the trustee may make payments of variation settlement and initial margin. In sum, the revisions clarify that payments can be made prior to pending transfers or liquidation, not just pending liquidation. The revision should benefit the customers of the FCM debtor in clarifying that the trustee has two paths in treating open commodity contracts—transfer, and if transfer is not possible, liquidation. The changes describe more accurately the types of payments that the trustee will be permitted to make and account specifically for the types of entities to which the trustee is permitted to make the types of payments referred to in this section. The revisions clarify the current regulatory text, which should benefit stakeholders. The Commission does not anticipate any increased cost from these changes.

Section 190.04(b)(1)(i) prevents the trustee from making any payments of behalf of any commodity contract account that is in deficit, to the extent within the trustee's control. The revised provision recognizes that certain accounts may be held on an omnibus basis on behalf of many customers. To the extent the trustee is making a margin payment with respect to such an omnibus account, it may be out of the trustee's control to only make payment with respect to those customer accounts that are not in deficit. The proviso similarly will clarify that this prohibition on making margin payments on behalf of accounts in deficit is not intended to prohibit ''upstream'' entities (*e.g.,* a CCP or an intermediary through which the debtor clears) from exercising legal rights to margin under applicable law. Due to the structure of omnibus accounts and the explicit requirement of lack of trustee control, any payments that are made under the revised provision would have been made pursuant to Commission authorization under the current regulation. Thus, neither provision should add any new regulatory burden and the Commission does not estimate that there will be any additional cost associated with the proposed changes.

Section 190.04(b)(1)(ii) is a new regulation that adds an explicit restriction, that the trustee cannot make a margin payment with respect to a specific customer account that would exceed the funded balance of that account. ICI agrees that this restriction supports the *pro rata* distribution principle, and should benefit the other customers of the FCM debtor—any payment of customer property in excess of a particular customer's funded balance is to the detriment of other customers.[251]

Section 190.04(b)(1)(iii) is a minor, non-substantive clarification of current § 190.02(g)(1)(ii), that should not create any changes from the status quo with regards to costs and benefits.

In § 190.04(b)(1)(iv)–(v), the Commission is clarifying that margin must only be used (*i.e.,* paid to a clearing organization or upstream intermediary) consistent with section 4d of the CEA. Section 190.04(b)(1)(vi) states explicitly the conditions under which the trustee may make payments to meet margin obligations.

Together, these changes protect customers who make payments after the order for relief by ensuring that they fully benefit from those payments (and thus incentivize customers to make such payments in appropriate circumstances). Moreover, more clearly permitting the trustee, for the purpose of curing customer margin deficiencies, to use funds in an account class that exceed the sum of all of the net equity claims for that account class, should facilitate the orderly transfer of positions and contracts following the default, lessening the potential for further roiling markets. Finally, these changes taken together also benefit the broader group of customers of the FCM debtor by clarifying the treatment of funds in segregated accounts, and thus mitigating administrative costs.

These changes are designed to clarify the statutory requirements applicable to funds in the customer account. While there may be accounting requirements associated with funds in segregated accounts, substantially all of the costs of such accounting are already incurred pursuant to the segregation rules. Thus, the Commission does not anticipate that there should be any material additional costs associated with this change.

Section 190.04(b)(2) allows the trustee discretion as to whether to issue margin calls to customers who are undermargined, deleting highly prescriptive conditions from the current rule. The revision should benefit public customers of the FCM debtor by giving the trustee the flexibility to recognize that there may be situations in which issuing a margin call is impracticable because the trustee is operating the FCM in ''crisis mode'' and may be pending wholesale transfer of liquidation of open positions.

It is, however, possible that the trustee would exercise their discretion poorly, or in a manner that, in retrospect, would be seen to be to the detriment of the estate, and that the trustee would have failed to issue a margin call in a situation in which a public customer would have paid the call (and in which the balance of administrative cost and amount recovered would mean that, in retrospect, it would have profited the estate if the call was made). Such failure could result in a cost to the estate of the FCM debtor to the extent that such funds are not available.

The balance of the revisions to § 190.04(b) should cause no change to the related costs and benefits.

Section 190.04(b)(3) retains the concept in current § 190.02(g)(3), with updated cross-references. The Commission does not anticipate that there will be any costs or benefits to the proposed minor revisions.

[250] The Commission is implementing the same change—the addition of the word ''public'' before ''customers''—to § 190.04(a)(2). The anticipated cost and benefit analysis of the change is the same as in § 190.04(a)(1).

[251] While there will be a corresponding detriment to the customers who may have benefited from such excess payments, those customers would only be losing something that runs counter to the statutory goal of *pro rata* distribution. Moreover, there are no likely incentive effects because, on this issue, customers stand behind the ''veil of ignorance''—it is difficult to identify, *ex ante,* which customers would be in the group of gaining customers (or in the group of losing customers).

Section 190.04(b)(4) addresses the trustee's obligation to liquidate accounts in deficit, or where a mark-to-market calculation would result in a deficit, or where the customer fails to meet a margin call within a reasonable time. The revision will clarify the applicability of current authority to a situation that is already implicit in the current rule. The regulation does not require the trustee to make additional calculations but, if a calculation made by the trustee reveals that the mark-to-market value of the account is a deficit, the trustee is instructed to liquidate the account as soon as practicable rather than to wait for the time that payment would be due. The benefit of this change should be to liquidate accounts in deficit more promptly (thus mitigating potential further losses); the cost will be the cost of engaging in such liquidation, as well as the possibility that, absent prompt liquidation, the deficit would have been mitigated due to favorable intervening changes in market value (or, potentially, an intervening deposit of additional collateral by the customer).[252]

Second, the Commission is adding the concept of ''exigent circumstances'' as a new exception to the general and long-established rule that a minimum of one hour is sufficient notice for a trustee to liquidate an undermargined account.

SIFMA AMG/MFA urged the Commission to curtail the trustee's discretion in § 190.04(b)(4) in a number of ways: By requiring the trustee to defer to the margin call timings present in applicable underlying agreements between the customer and the (pre-bankruptcy) debtor, and by providing customers with the opportunity to demonstrate that a margin payment was made even if the FCM's books and records do not yet reflect its receipt. By contrast, ICI noted that it is vital that the trustee be required to swiftly crystallize, and therefore cap the losses resulting from, such deficits by promptly liquidating accounts in deficit or for which a customer has failed to meet a margin call. ICI further stated that if the accounts were allowed to remain open, additional losses on the delinquent customers' transactions would be borne by the FCM's non-defaulting customers.

The Commission has determined not to make the requested changes. While making those changes would benefit those customers who are treated on a more bespoke it would be to the detriment of the FCM's other customers. Enhancing the trustee's discretion to determine how long a customer has to meet a margin call, and to rely on the FCM's books and records in doing—and refusing to curtail that discretion (by forcing the trustee to defer to margin call timings in pre-bankruptcy agreements, or to give the customer an opportunity to demonstrate that the a margin payment was made) as requested by the comment—will benefit other customers of the debtor FCM by giving the trustee flexibility to respond to market conditions following an FCM default. It is important to recognize that in stressed markets or in situations where communication protocols cannot practicably be followed, permitting a customer time to post margin in accordance with a pre-bankruptcy agreement—or, in some cases, even notice of one hour—may be insufficiently prompt to mitigate appropriately (1) the risk that such customers would default, (2) the risk that delaying liquidation of such a customer's positions increases the potential for and likelihood that they would do so with a debit balance, and (3) the risk that the size of that debit balance would increase as a result of that delay, thereby reducing the funded balances of those other customers. However, customers who are required to make payments more promptly would bear associated costs, from making such payments in a reduced time frame, from having to make duplicate payments (while these would ultimately be returned in full, this would be without interest) or from having contracts liquidated that would otherwise not have been liquidated if the customer had more time to make payment.[253]

The Commission is adding § 190.04(b)(5) to guide the trustee in assigning liquidating positions to the FCM debtor's customers when only a portion of the open contracts are liquidated. The benefit of this new provision is that it presents a clear and transparent mechanism by which the trustee is to allocate the positions. This mechanism will protect the customer account as a whole, by establishing a preference for assigning liquidating transactions to individual customer accounts in a risk-reducing manner. The allocation mechanism will, however, be subject to the trustee's exercise of reasonable business judgement. It is possible that such judgment could be exercised in a poor manner (or in a manner that, in retrospect, turns out to be regrettable), with resultant cost to the FCM debtor estate.

Section 190.04(c) requires the trustee to use its best efforts to liquidate open commodity contracts that are not settled in cash (*i.e.,* those that settle via physical delivery of a commodity) where the contract would move into delivery position. These clarifications are likely to reduce administrative costs, to the benefit of the estate (and, ultimately, customers). CME believed that this provision would have the benefit of avoiding unnecessary disruptions to the delivery process by customers that did not intend to participate in making or taking delivery. There should be no cost associated with the revision because, while there may be some customers who would prefer to hold their contracts through delivery, the current regulations, just as the revised regulations, direct the trustee to liquidate contracts coming into delivery position.[254]

Section 190.04(d) will clarify requirements concerning the liquidation and valuation of open positions. Section 190.04(d)(1) and (2) clarify requirements for liquidating open commodity contracts and specifically identifiable property other than commodity contracts.

Section 190.04(d)(3) codifies the Commission's longstanding policies of *pro rata* distribution and equitable treatment of customers in bankruptcy, as described in § 190.00(c)(5) above, as applied to letters of credit posted as margin. Under the new provision, the trustee may request that a customer deliver substitute customer property with respect to any letter of credit received, acquired or held to margin, guarantee, secure, purchase, or sell a commodity contract. The amount of the substitute customer property to be posted may, in the trustee's discretion, be less than the full-face amount of the letter of the credit, if such lesser amount is sufficient to ensure *pro rata* treatment consistent with §§ 190.08 and 190.09. If necessary, the trustee may require the customer to post property equal to the full-face amount of the letter of credit to ensure *pro rata* treatment. Pursuant to paragraph (d)(3)(i), if such a customer fails to provide substitute customer property within a reasonable time specified by the trustee, the trustee may draw upon the full amount of the letter of credit or any portion thereof (if the

[252] This change may also provide incentives for a customer whose account is in, or is approaching, deficit to make such payments promptly to avoid liquidation of their positions.

[253] SIFMA AMG and MFA also suggested that the regulation should be amended to give customers credit for any gains that were haircut due to gains-based haircutting by a DCO. Any such haircutting of a customer's gains is due to application of the customer's agreement with the FCM. Moreover, giving some customers credit despite such agreements would increase their recovery, but at the expense of other customers, as discussed in detail in section II.C.7 above.

[254] *See, e.g.,* current § 190.03(b)(5).

letter of credit has not expired). Under paragraph (d)(3)(ii), the trustee is instructed to treat any portion of the letter of credit that is not fully drawn upon as having been distributed to the customer. However, the amount treated as having been distributed will be reduced by the value of any substitute customer property delivered by the customer to the trustee. Any expiration of the letter of credit after the date of the order for relief would not affect this calculation. Pursuant to paragraph (d)(3)(iii), letters of credit drawn by the trustee, or substitute customer property posted by a customer, are to be considered customer property in the account class applicable to the original letter of credit.

ICI, SIFMA AMG/MFA, and Vanguard supported § 190.04(d)(3) on the grounds that it has the benefit of treating customers equitably by avoiding a more favorable treatment of customers who post letters of credit than those who post cash and securities.

These proposed new provisions could impose costs on customers who use letters of credit as collateral for their positions. Such customers could be considered to have received distributions up to the full amount of the letter of credit, or the trustee may draw upon a portion or possibly the full amount of the letter of credit.

Moreover, a number of commenters,[255] expressed the concern that requests for substitute customer property in the special context of delivery letters of credit could cause sudden liquidity needs, and substantial hardship to customers. For example, CME noted that, while they support § 190.04(d)(3) outside the context of delivery letters of credit, they see difficulties in that context, specifically in the case of deliveries for certain energy contracts, often which take place over 30 days. The delivery letters of credit for these contracts can involve hundreds of millions of dollars in face amounts, and CME is of the view that it would cause substantial liquidity hardship for buyers to have to substitute cash in such amounts.

While the discussion above represents potentially important costs, the Commission is noting factors that can alleviate these costs, and is implementing provisions that it believes substantially mitigate these costs: First, the Commission is adding a new § 190.04(d)(3)(iv), which provides that the trustee shall, in exercising their discretion with regard to addressing letters of credit, including as to the timing and amount of a request for substitute customer property, endeavor to mitigate, to the extent practicable, the adverse effects upon customers that have posted letters of credit, in a manner that achieves *pro rata* treatment among customer claims. Second, the Commission notes the likelihood that requests for substitute customer property may not apply to the particular delivery letters of credit the commenters have expressed concerns about: As requested by CME, the Commission confirms that (1) a delivery letter of credit that is posted directly with the DCO or with the delivery counterparty, rather than with or through the FCM, and for which the FCM is not a named beneficiary, is outside the delivery account class, *i.e.,* it does not constitute cash delivery property (or property of the debtor's estate), and (2) the provisions in other parts of the part 190 regulations regarding treatment of letters of credit posted with or through the debtor FCM do not apply such a letter of credit.

The Commission's priority in this context is to ensure the customers using letters of credit to meet margin obligations are treated in an economically equivalent manner to those who have posted other types of collateral, so that there is no incentive to use such letters of credit to circumvent the *pro rata* distribution of margin funds as set forth in section 766(h) of the Bankruptcy Code.[256] Moreover, if there are shortfalls in customer property in a particular account class, and public customers posting letters of credit are protected from sharing in those shortfalls, those public customers would benefit. However, the shortfalls would, inevitably, instead be allocated to other public customers, who would suffer corresponding losses. Regulation § 190.04(d)(3) supports the policy of *pro rata* treatment of public customers embodied in section 766(h) of the Bankruptcy Code by clarifying that letters of credit cannot be used to avoid *pro rata* distribution of margin funds. It therefore avoids concentrating losses on those public customers (who are likely to be smaller customers) that cannot qualify for, or cannot afford the cost of, letters of credit, or otherwise do not use letters of credit as collateral. Moreover, by directing the trustee to exercise their discretion, including with respect to amounts and timing of requests for customer property, in a manner that mitigates adverse effects on those customers that have posted letters of credit, it will mitigate the liquidity costs to such customers.

Section 190.04(e)(1) concerns liquidation of open commodity contracts in the market, while paragraph (e)(2) addresses liquidation by book entry offset. Both of these revised regulations delete the requirement in the current regulations that a clearing organization must obtain approval for its rules regarding liquidation of open commodity contracts, a requirement that is superfluous in light of the regulatory framework set forth in part 40 of the Commission's regulations, and in light of the notice-filing regime established by Congress in section 5c(c) of the CEA.[257] This has the benefit of enabling clearing organizations to avoid the cost of filing a request for rule approval, pursuant to CEA section 5c(c)(4) and Regulation § 40.5. There are potential costs, in that an ill-conceived rule could be more readily identified, and addressed, in a rule approval process. However, Commission staff, as a matter of practice, closely reviews all notice-filed clearing organization rules.

Section 190.04(e)(3) is new, and confirms that an FCM or foreign futures intermediary through which a debtor FCM carries open commodity contracts may exercise any enforceable contractual rights that the FCM or foreign futures intermediary has to liquidate such commodity contracts. It provides that the liquidating FCM or foreign futures intermediary must use ''commercially reasonable efforts'' in the liquidation and provides the trustee a damages remedy if the FCM or foreign futures intermediary fails to do so. Damages are the only remedy; under no circumstance can the liquidation be voided.

This new provision will benefit carrying FCMs by confirming explicitly that carrying FCMs are allowed to exercise enforceable contractual rights to liquidate contracts, which reduces ambiguity and thus will reduce administrative costs. At the same time, clarification of the availability of the damages remedy will help to protect creditors of the debtor FCM's estate in the event that the carrying FCM does not use commercially reasonable efforts in liquidating the open contracts (and thus will incentivize carrying FCMs to act in a commercially reasonable manner). Thus, the regulation itself provides the estate with a potential mitigant for the costs in the form of a damages remedy.

The remainder of the revisions to § 190.04(e)(4) and (f) are non-substantive language changes and

[255] CMC, CME, FIA.

[256] *See, e.g.,* 48 FR at 8718–19.

[257] 7 U.S.C. 7a–2(c).

clarifications and updated cross-references and should not have associated costs or benefits.

3. Regulation § 190.05: Operation of the Debtor's Estate—General: Consideration of Costs and Benefits

In § 190.05, the Commission is addressing general issues regarding the operation of the debtor's estate. In both § 190.05(a) and (b), the Commission is making revisions providing the trustee with more flexibility to act in a bankruptcy situation. Section 190.05(a), for example, provides that the trustee ''shall use reasonable efforts'' to comply with the CEA and the Commission's regulations. Section 190.05(b) requires the trustee to ''use reasonable efforts'' to compute a funded balance for each customer account that contains open commodity contracts or other property as of the close of business each business day until such open commodity contracts and other property in such account have been transferred or liquidated, ''which shall be as accurate as reasonably practicable under the circumstances, including the reliability and availability of information.'' These two revisions will benefit the estate by recognizing that a bankruptcy could be an emergency event, that perfectly reliable information could be unavailable or inordinately expensive to obtain, and that therefore the trustee should be allowed some measure of flexibility to act reasonably given the particular circumstances of the case. CME noted that § 190.05(b) will have the benefit of allowing the trustee to transfer more promptly public customers' positions and property than if the trustee were held to a strict standard of precision. On the other hand, affording the trustee increased discretion in complying with the CEA and the Commission's regulations, and in computing a funded balance for each customer account, may carry the potential cost of trustee mistake, misfeasance, or abuse of such discretion, as discussed above.

Whereas current § 190.04(b) requires a trustee to compute a funded balance only for those customer accounts with open commodity contracts, revised § 190.05(b) expands the scope of customer accounts for which a trustee is required to compute a funded balance to those accounts with open commodity contracts or other property (including, but not limited to, specifically identifiable property). This expansion of the trustee's duties represents an administrative cost, as the trustee will have to expend time and resources at the close of business each business day to compute the funded balance of all customer accounts. However, this revision should also result in a benefit to those customers whose accounts hold property but no open commodity contracts, in the form of enhanced information about their financial position (including with regard to collateral, the value of which may change on a daily basis, and with regard to the percentage distribution currently available). These customers will, under the revised provision, receive daily computations of the funded balance of their accounts with the debtor.

However, revised § 190.05(b) also narrows the trustee's duty compared to current § 190.04(b): While the current provision states that the trustee ''must compute a funded balance for each customer account . . . each day,'' the revised provision only requires the trustee to ''use reasonable efforts'' to do so. Regulation § 190.00(c)(3)(i)(C) provides that ''reasonable efforts'' should only be less than ''best efforts'' to the extent that this would benefit public customers *as a class.* Exercises of discretion by a trustee that, on a net basis, benefit public customers as a class may, on a net basis, impose costs on individuals or groups within that class. For example, there theoretically may be cases where, because the administrative cost of computing a funded balance would outweigh the benefit of doing so to public customers *as a class,* the trustee, in exerting ''reasonable efforts,'' determines not to do so on a particular day or for a particular time. As ICI points out in their comment letter, that decision would harm certain customers, *i.e.,* regulated funds, who have a particular need to confirm the existence and value of their transactions and associated margin.

Section 190.05(c) requires the debtor to maintain ''records required under this chapter to be maintained by the debtor, including records of the computations required by this part'' ''until such time as the debtor's case is closed.'' This revision expands the scope of records that must be maintained, thereby imposing certain administrative costs, but should benefit the estate, because it will limit the amount of time the trustee will have to maintain the relevant records.

Section 190.05(d) requires the bankruptcy trustee to use all reasonable efforts to continue to issue account statements for customer accounts that contain open commodity contracts or other property, and to issue account statements reflecting any liquidation or transfer of open commodity contracts or other property promptly after such liquidation or transfer. This provision will likely result in administrative costs, as the trustee will have to expend time and resources issuing account statements to customers. It will benefit customers because it should help them to keep track of their commodity contracts (and the continued availability of hedges) and the property in their accounts, including in particular when such contracts and property are liquidated or transferred, even during a bankruptcy. ICI noted that this is of particular benefit to regulated funds, providing them with a basis to confirm the existence and value of their transactions and associated margin.

Section 190.05(e)(1) allows a bankruptcy trustee to effect transfers of customer property in accordance with § 190.07, but requires the trustee to obtain court approval prior to making any other disbursements to customers. This provision should benefit the estate and customers by allowing the trustee, without court approval, to port customers' positions and associated property to a solvent FCM as quickly as possible in a bankruptcy situation. In the event that too much customer property (that is, an amount in excess of the ultimate *pro rata* share) is transferred for those customers whose positions are being ported, and cannot be offset or clawed back, it could result in costs to other customers, for whom less than their *pro rata* share would be available.

Section 190.05(e)(2) allows the bankruptcy trustee to invest the proceeds from the liquidation of commodity contracts or specifically identifiable property, and any other customer property, in obligations of or guaranteed by the United States, so long as the obligations are maintained in depositories located in the United States or its territories or possessions. The revised regulation expands the scope of customer property that the trustee is permitted to invest in such a manner to include ''any other customer property.'' This change should benefit customers, in that additional customer property could be invested (in this limited manner).

Section 190.05(f) requires the trustee to apply the residual interest provisions contained in § 1.11 ''in a manner appropriate to the context of their responsibilities as a bankruptcy trustee pursuant to'' the Bankruptcy Code and ''in light of the existence of a surplus or deficit in customer property available to pay customer claims.'' This explicit requirement to continue to apply the residual interest requirements set forth in § 1.11 may result in administrative costs, since the trustee would require resources to do so. However, this provision should benefit customers by making it more likely that they would receive what they are entitled to receive from the debtor's estate. Indeed, Vanguard noted that the residual interest requirement is a valuable buffer to protect customers.

4. Regulation § 190.06: Making and Taking Delivery Under Commodity Contracts: Consideration of Costs and Benefits

Section 190.06 addresses the making and taking of deliveries under commodity contracts.

Specifically, § 190.06(a)(2) requires the trustee to use ''reasonable efforts'' (in contrast to the current ''best efforts'') to allow a customer to deliver physical delivery property that is held directly by the customer in settlement of a commodity contract, and to allow payment in exchange for such delivery, and for both of these to occur outside the debtor's estate, where the rules of the exchange or clearing organization prescribe a process for delivery that allows this.

Management of contracts in the delivery positions involves a significant degree of tailored administration. Under the best efforts standard, the trustee may spend more time (and thus incur higher costs) focusing on the needs of a few customers, which could detract from the trustee's ability to manage the estate more broadly. Accordingly, the change from ''best efforts'' to ''reasonable efforts'' should benefit creditors of the estate (as a whole) as the trustee should not need to provide a disproportionate amount of individualized treatment to such contracts.[258] However, particular customers that would otherwise have received the trustee's focused treatment under the ''best efforts'' standard could suffer a cost from the change.

Section 190.06(a)(3) provides guidance to address situations when the trustee determines that it is not practicable to effect delivery outside the estate and therefore, delivery is made or taken within the debtor's estate. The revisions provide the trustee with the flexibility to act ''as it deems reasonable under the circumstances of the case,'' but set an outer bound to the trustee's discretion in requiring them to act ''consistent with the *pro rata* distribution of customer property by account class.'' This provision again will have the benefits and costs of enhanced discretion discussed above, but includes an outer bound to that discretion.

In § 190.06(a)(4), the Commission adds a new provision to reflect that delivery may need to be made in a securities account.[259] The new provision should benefit customers who require the delivery of securities, and the trustee, by permitting those securities to be delivered to the proper type of account. By setting limits, the provision should mitigate the risk of transferring too much value out of the commodity contract account (and creating a risk of an undermargin or deficit balance).

Section 190.06(b) is also new. It creates an account class for physical delivery property held in delivery accounts and the proceeds of such physical delivery property. This account class is further be sub-divided into separate physical delivery and cash delivery account subclasses. In general, creating the delivery account class should help protect customers with property in delivery accounts following a default, because delivery accounts are not subject to the Commission's segregation requirements. The further sub-division into sub-classes recognizes that cash is more vulnerable to loss, and more difficult to trace, as compared to physical delivery property. This will likely benefit those with physical delivery claims; customers in the cash delivery sub-class would be likely get a *pro rata* distribution that is less. The benefits and costs of creating these sub-classes were discussed more fully above in reference to the definition of account class in proposed § 190.01.

5. Regulation § 190.07: Transfers: Consideration of Costs and Benefits

Section 190.07(a) works to promote transfers of commodity contracts from a debtor FCM. It does so by prohibiting any clearing organization or self-regulatory organization from adopting, maintaining in effect, or enforcing rules that interfere with the acceptance by its members of transfers of open commodity contracts and the equity margining or securing of such contracts from FCMs with respect to which a petition in bankruptcy has been filed, if the transfers have been approved by the Commission.

The revised regulation includes the provisos that it (1) does not limit the exercise of any contractual right of a clearing organization or other registered entity to liquidate or transfer open commodity contracts, and (2) should not be interpreted to limit a DCO's ability adequately to manage risk. The revision modifies, in a balanced fashion, the standard for clearing organization and SRO rules that are adopted, maintained, in effect, and enforced and where transfers are approved by the Commission. While clearing organizations and SROs will need to comply with the revised standard, the compliance cost should not be different than under the prior standard. The clarification that the regulations do not limit contractual risk management rights should provide a benefit to clearing organizations and their members in clarifying that the regulation will not nullify the contracts in this regard, and will not have an associated cost.

In § 190.07(b)(1), the Commission clarifies that it is the transferee FCM itself who has the responsibility to determine whether it would be in violation of regulatory minimum financial requirements upon accepting a transfer. It is not the trustee's duty. The Commission does not anticipate any material cost from this revision.

Section 190.07(b)(3) permits a transferee to accept open commodity contracts and associated property prior to completing customer diligence requirements, provided that such diligence is completed as soon as practicable thereafter, and no later than six months after transfer. It is intended to incentivize potential transferees to accept transfers by making it more practicable to do so. It recognizes that customer diligence processes would have already been required to have been completed by the debtor FCM with respect to each of its customers as part of opening their accounts. CME, ICI and Vanguard agree that the proposal would provide a benefit to customers and transferee clearing members and trustees, by facilitating the transfer process.[260] If such flexibility were not provided, under the current regulations, transfer might not be accomplished, or may not be accomplished promptly. The provision recognizes the importance of the account opening diligence

[258] As discussed above in section II.A.1, the trustee in exerting best efforts to meet a standard must diligently exert efforts to meet that standard ''to the extent of its own total capabilities.'' By contrast, in exerting ''reasonable efforts'' to meet a standard, the Commission expects that the trustee will work in good faith to meet the standard, but will also take into account other considerations, including the impact of the effort necessary to meet the standard on the overarching goal of protecting public customers as a class.

[259] This is only relevant for debtor FCMs that are also broker-dealers.

[260] The customer diligence requirements in question focus on anti-money-laundering requirements and ensuring that risk disclosures have been provided to customers and acknowledgements of such disclosures have been received. The corresponding costs would arise from the possibility that the transferee's diligence would have revealed problems that had been missed by the debtor FCM's customer diligence process, or arose subsequent to the time that the original process was conducted, and that conducting the revised diligence more promptly would sooner reveal the concerns, thus permitting them to be addressed more expeditiously.

requirements and would mitigate the risk from delay by requiring the diligence to be performed as soon as practicable and setting an outer limit at six months, unless that time is extended by the Commission.

FIA has requested that the Commission provide transferee FCMs with more specific relief from applicable law relating to ''customer diligence'' and to add specific references to certain rules, in order to provide certainty, and to mitigate regulatory risk, to a transferee. FIA requested various points of specific relief under five headings: (i) Rules relating to anti-money laundering requirements; (ii) rules relating to risk and other disclosures; (iii) rules relating to capital and residual interest requirements; (iv) rules relating to account statements; and (v) rules relating to margin.

As discussed in more detail in Section II.B.5 above, the Commission has decided that, with respect to certain points of the requested relief, providing the relief is warranted, and there are no material associated costs from doing so. Thus, for example, § 190.07(b)(3) is being amended to refer explicitly to the risk disclosure requirements in § 1.65(a)(3).

With respect to the other points of requested relief, the comment requests relief that the Commission has decided carries unacceptable costs. Thus, the Commission is not providing a general exemption from undermargined account capital charges in accordance with § 1.17, nor is the Commission extending the time to comply with capital or residual interest requirements. While such relief might have the advantage of further incentivizing FCMs to accept transferred accounts, it would do so at the cost of potentially causing or accepting financial weakness at transferee FCMs.

In a third group of points of requested relief, the Commission notes that interpretations of existing regulations should adequately address the concerns. Thus, transferred accounts are (based on the terms of the regulations) excluded from the Customer Identification Program requirements of 31 CFR 1026.220, while the provisions of § 190.07(b)(3) adequately inform what constitutes ''*appropriate* risk-based procedures for conducting ongoing customer due diligence'' (emphasis supplied) in the context of 31 CFR 1026.210(b)(5)(i). While providing more specific regulatory provisions might enhance regulatory certainty (and thus redound to the benefit of transferee FCMs, and potentially incentivize FCMs to accept transferred accounts), it carries the risk of being under-inclusive or over-inclusive, and thus failing to achieve the regulatory goals.

Moreover, as to both the second and third categories, there may be a more tailored approach to achieving the goal: As the Commission explicitly notes above, any further relief that might be appropriate in a particular situation can be requested by the transferee in light of the relevant facts and circumstances. The Commission observed that its staff have traditionally responded to requests for relief in emergency situations with great dispatch, and expects, and has instructed staff, to continue to do so in this context in the future.[261] While this approach provides less certainty in advance, it has the benefit of making tailored relief available (and mitigating the possibility that relief leads to unintended consequences).

Section 190.07(b)(4) clarifies that account agreements governing a transferred account are deemed assigned to the transferee until and unless a new agreement is reached. At the request of FIA, the Commission is confirming that if there is a pre-existing account agreement between a transferred customer and the transferee FCM, that pre-existing agreement will govern the relationship rather than the agreement between the customer and the transferor (debtor) FCM. The provision also confirms that consequences for breaches pre-transfer are borne by the transferor rather than the transferee. Section 190.07(b)(4) provides important transparency regarding the agreement between a transferred customer and a transferee FCM pending the negotiation of a new agreement between them, or, if such negotiation is unsuccessful, until either party decides to terminate the relationship.

Section 190.07(b)(5) provides that in the event of transfer, customer instructions that are received by the debtor with respect to any open commodity contracts or specifically identifiable property should be transmitted to the transferee, who should comply with such instructions to the extent practicable. The slight revisions to current § 190.02(c) are merely clarifications, and there should be no costs or benefits associated with such revisions.

Section 190.07(c) provides that ''all commodity contract accounts (including accounts with no open commodity contract positions) are eligible for transfer. . . .'' This recognizes explicitly that accounts can be transferred if the accounts are intended for trading commodities, but do not include any open commodity contracts at the time of the order for relief. The revision clarifies the current language and will not change the types of accounts that can be transferred. Accordingly, the Commission does not anticipate that there will be material added cost associated with the revision.

Section 190.07(d) revises special rules for transfers under section 764(b) of the Bankruptcy Code. The revision is being made to promote transfer. Cost and benefit considerations related to transfer are as discussed above.[262] The revised regulation permits partial transfers, but (to the extent practicable) not in cases where netting sets for spreads or straddles would be broken or where customers' net equity claims would increase. The revised regulation should provide a benefit to customers by codifying this limitation. This recognizes that there may be circumstances where partial transfer is not practicable and implies that the trustee makes that decision. It is therefore possible that certain customers holding spread or straddle positions could have positions liquidated or not transferred under the revised provision, or could have spreads or straddles broken because of the trustee's exercise of discretion.

The Commission has declined to adopt ICI's suggestion to provide guidance to the effect that the trustee should not effectuate a transfer that will result in a separately managed account having a significant deficit following the porting, in order to avoid a circumstance where ''the manager of that account would likely need to liquidate the bulk of the account's portfolio and other positions in order to eliminate or reduce the deficit.'' While adopting such a suggestion might benefit the beneficial owner by enabling the account manager to manage the separate account in accord with the account manager's investment program, it may instead have the opposite effect, in that it may prevent any transfer of the customer's positions before the seventh calendar day after the order for relief, in which event the trustee will be required to liquidate the entirety of the customer's account, promptly and in an orderly manner, causing the very disruptions that the transfer provisions (and ICI's suggestion) are designed to avoid. Moreover, many FCMs carry hundreds or even thousands of separately managed accounts. It may well not be practical for a trustee, in addition to their numerous other responsibilities (and in a context where they need to learn those responsibilities

[261] *See* discussion in Section II.B.5 above.

[262] *See* section III.B.1 above.

in a compressed timeframe) to take ''due account'' of the particular circumstances of each of these separately managed accounts in the hours, or perhaps a small number of days, that the trustee may be allowed by the clearing organizations carrying the FCMs accounts to negotiate and effectuate a transfer. Endeavoring to do so might well have the cost of diverting the trustee and their assistants from carrying out more pressing tasks.

Section 190.07(d)(3) permits a letter of credit associated with a commodity contract to be transferred with an eligible commodity contract account. If the letter of credit cannot be transferred and the customer does not deliver substitute property, the provision will permit the trustee to draw upon all or a portion of the letter of credit and treat the proceeds as customer property in the applicable account class. The revised regulation ensures that letters of credit are treated in an economically similar fashion to other types of collateral and that customers using letters of credit will not receive any differential economic advantages, thus serving the goal of *pro rata* distribution. If the trustee does draw upon the letter of credit, there may be administrative costs incurred by the estate, as well as costs to the customer that posted the letter of credit as collateral. These costs may be mitigated if the customer delivers substitute property, as set forth in the proposed regulation. Moreover, consistent with § 190.04(d)(3)(iv), the trustee is directed to ''endeavor to achieve *pro rata* treatment among customer claims in a manner that mitigates, to the extent practicable, the adverse effects upon customers that have posted letters of credit.'' [263]

Section 190.07(d)(4) will require a trustee to use reasonable efforts to prevent physical delivery property from being separated from commodity contract positions under which the property is deliverable. While this provision will impose an administrative cost on the estate, it is already a best practice for trustees; keeping delivery property with the underlying contract positions is necessary for (and thus should benefit) the delivery process. Therefore, the additional administrative cost from the revised regulation should be minimal.

In § 190.07(d)(5), the Commission prohibits the trustee from making a transfer that would result in insufficient remaining customer property to make an equivalent percentage distribution to all customers in the applicable account class (taking into account all previous transfers and distributions). The Commission is further clarifying that the trustee should make determinations in this context based on customer claims reflected in the FCM's records, and, for customer claims that are not consistent with those records, should make estimates using reasonable discretion based in each case on available information as of the calendar day immediately preceding transfer. This will support achieving the statutory policy of *pro rata* distribution and give the trustee discretion to make decisions based on the overarching principle set forth above, valuing cost effectiveness over precise values of entitlement. However, this is designed to work to the detriment of any customer who, absent the provision, would otherwise benefit from a larger distribution. Moreover, in giving the trustee discretion, it carries the risk of mistake or misfeasance.

Section 190.07(e) will add language to clarify that certain transfers are approved by the Commission pursuant to the procedure set forth in the Bankruptcy Code (and thus protected from avoidance) and will prohibit the trustee from avoiding such transfers, unless the transfer is *disapproved* by the Commission. These include a transfer made by ''a receiver that has been appointed for the FCM that is now a debtor.'' The new provision is being added in order to respect the actions of a receiver that is acting to protect the property of the FCM that has become the debtor in bankruptcy. It will provide certainty to the actions of such a receiver, whose duties, among others, include protecting the customer property of the FCM. However, to the extent that the receiver takes actions that are, considered in retrospect, mistaken or ill-advised, the revised provision will prevent the correction of such actions unless the Commission acts affirmatively to disapprove them.[264]

Section 190.07(f) will clarify that the Commission may prohibit the transfer of a particular set or sets of the commodity contract accounts, or permit the transfer of a particular set or sets of commodity contract accounts that do not comply with the requirements of the section. In addition, the Commission is clarifying that the transfers of the commodity contract accounts include the associated customer property. These revisions are clarifications and should not have any associated costs.

6. Regulation § 190.08: Calculation of Funded Net Equity: Consideration of Costs and Benefits

In § 190.08, the Commission addresses calculation of funded net equity. Section 190.08(a) simply states that a customer's funded net equity claim is equal to the aggregate of such customers funded net equity claims for each account class.

Section 190.08(b) sets forth the steps for a trustee to follow when calculating each customer's net equity. SIFMA AMG/MFA requested that the Commission amend proposed § 190.08(b)(2)(xii) to treat accounts of the same principal or beneficial owner maintained by different agents or nominees as separate accounts and not all held in the individual capacity of such principal or beneficial owner, suggesting that this would have the benefit of reducing the administrative difficulties the trustee would face in consolidating all accounts of the same principal or beneficial owner, and it would have the further benefit of avoiding any confusion as to treatment of separate accounts that could arise with the overlay of the time-limited relief provided by Letter 19–17.

The Commission declined to make this change. The change would not achieve those benefits and would have associated costs: First, the FCM, to the extent it does treat such accounts separately pursuant to the relief set forth in Letter 19–17, will already be consolidating (for purposes of certain calculations) all accounts of the same principal or beneficial owner, in that the Letter conditions its relief on the FCM applying credit limits and stress testing on a combined account basis.[265] Second, given that Letter 19–17 also conditions relief on the FCM disclosing that ''under CFTC [p]art 190 rules all separate accounts of the beneficial owner will be combined in the event of an FCM bankruptcy,'' amending § 190.08(b)(2)(xii) to treat them separately would be inconsistent with that disclosure, and would cause, rather than relieve, inconsistency with the approach taken under the Letter.

While the Commission is making certain revisions in § 190.08(b)(3), (4), and (5), the Commission views such revisions as non-substantive and merely clarifying the text in the current analogous provisions. Thus, the Commission does not expect these

[263] The costs and benefits of allowing the trustee to draw upon the letter of credit have been discussed above in section III.C.2 with respect to § 190.04(d)(3).

[264] Regulation § 190.02(b)(1) explicitly excepts from the delegation to the Director of the Division of Clearing and Risk the authority to disapprove a pre-relief transfer pursuant to § 190.07(e)(1).

[265] See CFTC Letter 19–17, *https://www.cftc.gov/node/217076* at 4.

changes to result in any costs or benefits.

Section 190.08(c) sets forth instructions for calculating each customer's funded balance, while in § 190.08(d), the Commission is in general implementing changes to provide more flexibility to the trustee in valuing commodity contracts and other property held by or for a commodity broker. For instance, in § 190.08(d)(5), the Commission is deleting the requirement that the trustee seek approval of the court prior to enlisting professional assistance to value customer property. These changes should benefit the estate by providing the trustee with more flexibility to determine how to value certain customer property, including whether or not to enlist professional assistance in doing so. Likewise, these revisions should serve the goal of a *pro rata* distribution to customers, as the accurate valuation of customer property can benefit from the input of a professional. On the other hand, affording the trustee increased discretion in how to value commodity contracts and other property held by a debtor carries the potential cost of mistake, misfeasance, or abuse of discretion by the trustee, as discussed above, or possibly by the professional whose service is retained.

With respect to commodity contracts that have been transferred, § 190.08(d)(1)(i) provides that such contracts be valued at the end of the last settlement cycle on the day preceding such transfer, rather than at the end of the settlement cycle in which it is transferred. Again, this revision should benefit both the estate and customers by making it practical to calculate the value of the transferred commodity contracts prior to the transfer.

The Commission has declined to accept ICE's suggestion that it adopt a ''more flexible approach'' because ''the market may move significantly on the date of the transfer.'' While prices may move intra-day during the period between opening and the time of auction, they may also move between the time of auction and closing. Therefore, there is no *ex ante* reason to expect that the previous day's price is less reflective of the price at the time of the auction than the closing price on the auction day. Moreover, an alternative approach, using the price set in the auction as the price for individual contracts, is unlikely to be practicable. Units auctioned will frequently contain a heterogenous (though risk-related) set of products, tenors (*e.g.,* contract months), and directions (*e.g.,* long or short). Thus, it will often be impracticable to translate an auction price for a portfolio to prices for individual contracts within that portfolio.

7. Regulation § 190.09: Allocation of Property and Allowance of Claims: Consideration of Costs and Benefits

In § 190.09, the Commission is addressing allocation of property and allowance of claims. Section 190.09(a)(1) defines the scope of ''customer property'' that is available to pay the claims of a debtor FCM's customers, and § 190.09(a)(1)(i) sets forth the categories of ''cash, securities, or other property or the proceeds of such cash, securities, or other property received, acquired, or held by or for the account of the debtor, from or for the account of a customer'' that are included in customer property. In § 190.09(a)(1)(i), the Commission is making certain substantive changes to the categories listed in current § 190.08(a)(1)(i), as discussed below:

- First, § 190.09(a)(1)(i)(D) is new and provides that customer property includes any property ''received by the debtor as payment for a commodity to be delivered to fulfill a commodity contract from or for the commodity customer account of a customer.'' Clarifying this point explicitly should benefit both the estate and customers by avoiding confusion or potential litigation.
- Second, § 190.09(a)(1)(i)(F) provides that letters of credit, including proceeds of letters of credit drawn by the trustee, or substitute customer property, constitute ''customer property.'' This section is being revised to be consistent with the other letters of credit provisions that are being added throughout part 190. The Commission does not anticipate that this provision will result in any material costs or benefits, as current § 190.08(a)(1)(i) already includes a provision regarding letters of credit.[266]

Section 190.09(a)(1)(ii) sets forth the categories of ''[a]ll cash, securities, or other property'' that would be included in customer property. In § 190.09(a)(1)(ii), the Commission is making certain substantive changes to the categories listed in current § 190.08(a)(1)(ii), as discussed below:

- First, § 190.09(a)(1)(ii)(D) provides that any cash, securities, or other property that was property received, acquired or held to margin, guarantee, secure, purchase, or sell a commodity contract and that is subsequently recovered by the avoidance powers of the trustee or is otherwise recovered by the trustee on any other claim or basis constitutes customer property. The current version of this provision refers only to the trustee's avoidance powers (leaving out the possibility for recovery other than through avoidance powers). The Commission's revisions to this section will benefit the estate, by assuring that any property they recover will be included in the pool of customer property, rather than going to some other creditor (to be sure, those other creditors will receive correspondingly less).
- Second, § 190.09(a)(1)(ii)(G) is new, and provides that any current assets of the debtor in the greater of (i) the amount that the debtor is obligated to be set aside as its targeted residual interest amount, pursuant to § 1.11, or (ii) the debtor's obligations to cover debit balances or undermargined amounts, pursuant to § 1.20, § 1.22, § 22.2, or § 30.7, constitute customer property. This new provision will result in administrative costs, because the trustee will need to take the extra step of determining whether any current assets of the debtor need to be set aside as customer property and, if so, how much. This provision should benefit public customers (and serve the policy of protecting customer collateral), however, because it will mitigate the risk of a shortfall in customer funds by ensuring that the trustee fulfills the Commission's regulations that require an FCM to put certain funds into segregation on behalf of customers. ICI and Vanguard agreed that this provision will benefit customers, while CME considered it a ''substantial improvement over the current rule.'' This approach will result in such funds being included in the pool of customer property, rather than going to some other creditor. It will, to the same extent, operate to the detriment of general creditors.
- Third, § 190.09(a)(1)(ii)(K) is also new, and provides that any cash, securities, or other property that is payment from an insurer to the trustee arising from or related to a claim related to the conversion or misuse of customer property constitutes customer property. This provision should benefit customers (and, again, the policy of protecting customer collateral), since any insurance payment as described in this proposed section will enlarge the pool of customer property, rather than going

[266] The costs and benefits of the underlying policy decision to take steps to ensure that customers posting letters of credit are treated (with respect to *pro rata* allocation of losses) in a manner consistent with the manner in which customers posting other forms of collateral are treated are discussed in connection with § 190.04(d)(3) in section III.C.2 above.

to general creditors.[267] It could result in administrative costs, however, as the trustee will need to spend time and resources in order to determine whether any such insurance payments exist, and in prosecuting such insurance claims.

• Fourth, the second sentence of § 190.09(a)(1)(ii)(L) is new, and will provide that customer property for purposes of these regulations includes any ''customer property,'' as that term is defined in SIPA, that remains after satisfaction of the provisions in SIPA regarding allocation of customer property constitutes customer property. This provision should benefit commodity customers (and act to the detriment of general creditors) because any securities customer property remaining after full allocation to securities customers will enlarge the pool of commodity customer property. It could result in administrative costs, however, since the trustee could need to spend time and resources determining the extent to which such property is left over after allocation to customers in a SIPA proceeding.[268]

Section 190.09(a)(2) sets forth the categories of property that are not included in customer property. In § 190.09(a)(2), the Commission has made certain substantive changes to the categories listed in current § 190.08(a)(2), as discussed below:

• First, in § 190.09(a)(2)(iii), the Commission is adding explicit language to state that only those forward contracts that are not cleared by a clearing organization are excluded from the pool of customer property. This revision will benefit customers (and act to the detriment of general creditors), since the pool of customer property would increase by explicitly including any cleared forward contracts.

• Second, § 190.09(a)(2)(v) provides that any property deposited by a customer with a commodity broker after the entry of an order for relief that is not necessary to meet the margin requirements of such customer is not customer property. The deletion of the word ''maintenance'' before ''margin'' will eliminate any distinction between initial and variation margin; this deletion will benefit customers by ensuring that any amount deposited by a customer after the entry of an order for relief that is necessary to meet that customer's margin requirements will be included in the pool of customer property. This provision would correspondingly act to the detriment of general creditors.

• Third, § 190.09(a)(2)(viii), which is new, provides that any money, securities, or other property held in a securities account to fulfill delivery, under a commodity contract that is a security futures product, from or for the account of a customer, is excluded from customer property. This provision avoids conflict with the resolution, under SIPA, of claims for securities and related collateral.

Section 190.09(a)(3), which is new, gives the trustee the authority to assert claims against any person to recover the shortfall of customer property enumerated in certain paragraphs elsewhere in § 190.09(a). This provision could impose administrative costs, since the trustee could have to expend time and resources to assert and prosecute such claims to make up for any shortfall in customer property. The provision will, however, benefit customers, since it will ensure that the trustee is in a position to recover any such shortfalls and gives the trustee authority to act to do so. Moreover, since this provision makes explicit what is implicit in current part 190, an additional benefit of this provision may be reduced litigation costs over a trustee's authority to engage in attempts to recover shortfalls in customer property.[269]

Section 190.09(b) adds the phrase ''or attributable to'' to the language that is in current § 190.08(b), when describing how to treat property segregated on behalf of or attributable to non-public customers, namely, as part of the public customer estate; the addition of this phrase, as described above, will clarify that § 190.09(b)(1) applies both to property that is in the debtor's estate at the time of the bankruptcy filing, as well as property that is later recovered by the trustee and becomes part of the debtor's estate at the time of recovery. This additional phrase would benefit public customers and the statutory policy in favor of them (and correspondingly act to the detriment of non-public customers and general creditors), since it could increase the amount of property that is treated as part of the public customer estate. It could impose administrative costs because it could take time and resources to properly allocate any property that is recovered after the time the bankruptcy is filed.[270]

Section 190.09(c)(1)(ii) is a new provision that instructs the trustee, in the event there is property remaining allocated to a particular account class after payment in full of all allowed customer claims in that account class, to allocate the excess in accordance with proposed § 190.09(c)(2), which in turn sets forth the order of allocation for any customer property that cannot be traced to a specific customer account class. These provisions will benefit public customers who would otherwise face shortfalls (and then, non-public customers who would otherwise face shortfalls). Since these provisions make explicit what is implicit in current part 190, an additional benefit of these provisions will result from the increased clarity over what to do with any excess customer property. However, the provisions will act to the detriment of non-public customers (relative to public customers) and general creditors (relative to both) who, under the current regime, could have been more likely to receive any excess customer property in the absence of an explicit provision providing what to do with any such excess customer property.[271]

Section 190.09(d) governs the distribution of customer property. The only substantive change in § 190.09(d) from its analog in current § 190.08(d) is in § 190.09(d)(1)(i) and (ii), which import the concept of ''substitute customer property.'' Whereas current § 190.08(d)(1)(i) and (ii) require customers to deposit cash in order to obtain the return of specifically identifiable property, § 190.09(d)(1)(i) and (ii) allow the posting of ''substitute customer property.'' This term, which is defined in § 190.01, means cash or cash equivalents. This revision will benefit customers because it makes it easier for customers to redeem their specifically identifiable property by no longer limiting customers to only using cash to do so. It could, however, impose administrative costs in the form of time and resources of the trustee, who, in the event a customer chooses to post cash equivalents to redeem their specifically identifiable property, will be required to

[267] It will, again, to the same extent, act to the detriment of general creditors.

[268] The Commission further notes that the first sentence of § 190.09(a)(1)(ii)(L), which provides that customer property includes any cash, securities, or other property in the debtor's estate, but only to the extent that the customer property under the other definitional elements is insufficient to satisfy in full all claims of the debtor's public customers, will impose no new costs or benefits because such provision already appears in current § 190.08, and the only changes to the provision would be non-substantive updates to cross-references.

[269] Of course, these recoveries are derived from persons against whom such claims are successfully asserted. The transfer to customers from these individuals advances the goal of pro-rata distribution.

[270] Section 190.09(c)(1) will have a similar change in the addition of the phrase ''or recovered by the trustee on behalf of or for the benefit of an account class,'' which is meant to clarify that any property recovered by the trustee on behalf of or for the benefit of a particular account class after the bankruptcy filing must be allocated to the customer estate of that account class. This revision will present similar costs and benefits to those discussed above.

[271] The incentive effects of such preferences are discussed in section III.A.2.vi, above.

value (and potentially to liquidate) such cash equivalents. Moreover, while ''cash equivalents'' are required to be assets ''that are highly liquid such that they may be converted into United States dollar cash within one business day without material discount in value,'' it is possible that such assets could nonetheless decrease in value, potentially to the detriment of other customers.

8. Regulation § 190.10: Provisions Applicable to Futures Commission Merchants During Business as Usual: Consideration of Costs and Benefits

As proposed, § 190.10 addresses provisions applicable to FCMs during business as usual. The ABA Subcommittee and CME recommended that these ordinary course provisions should be codified in part 1 of the Commission's regulations, to be more transparent to FCM compliance personnel. As discussed further below, the Commission has accepted that suggestion and is adopting in part 1 of its regulations the provisions that were proposed as § 190.10 (b), (c), (d), and (e).

In the regulation proposed as § 190.10(a), the Commission notes that an FCM is required to maintain current records related to its customer accounts, consistent with current Commission regulations, and in a manner that will permit them to be provided to another FCM in connection with the transfer of open customer contracts and other customer property. This regulation does not impose new obligations, but rather informs the trustee regarding their duties by incorporating references to the Commission's existing regulations. Thus, this provision is remaining in part 190, and, as the sole remaining paragraph, will be codified as § 190.10.

The regulation proposed as § 190.10(b) addresses designation of accounts as intended for the purpose of hedging. It is being codified as § 1.41. An FCM will be permitted to rely upon a customer's written representation of hedging intent regarding the designation of a hedging account, without being required to look behind that representation, thus mitigating administrative costs.

Section 1.41(a) requires an FCM to provide a customer an opportunity to designate an account as a hedging account when the customer first opens the account, allowing for clear instruction to FCMs at the outset of the relationship. Clear instruction at the outset will facilitate the ability properly to account for customer property. There will be some disclosure and accounting costs associated with this provision. For those customers that do engage in hedging, it will be more cost effective to designate the account at opening than to monitor the transactions for the first qualifying transaction to provide the opportunity to make the designation, as applicable under the current regulation. Thus, the regulation should reduce the probability that the opportunity to designate the account as a hedging account will be missed.

Section 1.41(b) sets forth the conditions for treating an account as a hedging account, permitting such treatment upon the customer's written representation that their trading would constitute hedging as defined under any relevant Commission rule or the rule of a DCO, DCM, SEF, or FBOT. There will be record-keeping costs for FCMs and customers associated with the provision.

Section 1.41(c) provides that the foregoing requirements do not apply to commodity contract accounts opened prior to the effective date of this final rulemaking, and that an FCM can continue to designate such existing accounts as hedging accounts based on written hedging instructions obtained under current regulations. This provision should mitigate the impact of the changes to current requirements in § 1.41(a) and (b) by not applying those provisions to already opened hedging accounts, instead relying upon the information collected and maintained during the current regulatory framework.

Section 1.41(d) will permit an FCM to designate an existing customer account as a hedging account for purposes of bankruptcy treatment, provided that the FCM obtains the necessary customer representation. This provision will give FCMs and customers flexibility to apply the proposed regulations to existing accounts where the impact would not be overly burdensome.

The regulation proposed as § 190.10(c) addresses the establishment of delivery accounts during business as usual. It is being codified as § 1.42, and recognizes that when an FCM facilitates delivery under a customer's physical delivery contract and such delivery is effected outside of a futures account, foreign futures account, or cleared swaps account, it must be effected through (and the associated property held in) a delivery account. While there are costs associated with the opening and maintenance of delivery accounts, the Commission views that the use of such accounts is cost effective in facilitating delivery.[272] The benefit of using such accounts is twofold: To protect customer assets during the delivery process, and to foster the well-functioning of the delivery process.

The regulation proposed as § 190.10(d) addresses letters of credit, and will prohibit an FCM from accepting a letter of credit as collateral during business as usual unless certain conditions are met at the time of acceptance and remain true through the date of expiration. It is being codified as § 1.43.

The first condition is that the trustee must be able to draw upon the letter of credit in full or in part in the event of a bankruptcy proceeding, the entry of a protective decree under SIPA, or the appointment of FDIC as receiver pursuant to Title II of the Dodd-Frank Act. Second, if the letter of credit is permitted to be and in fact is passed through to a clearing organization, the trustee for such clearing organization (or the FDIC) must be able to draw upon the letter of credit in full or in part in the event of a bankruptcy proceeding for such clearing organization (or where the FDIC is appointed as receiver).

Section 1.43 will ensure that an FCM's treatment and acceptance of letters of credit during business as usual is consistent with and does not preclude the trustee's treatment of letters of credit in accordance with §§ 190.00(c)(5) and 190.04(d)(3). The Commission understands that under industry practice, most existing letter of credit arrangements are consistent with the Joint Audit Committee Forms of Irrevocable Standby Letter of Credit, both Pass-Through and Non Pass-Through,[273] and that these forms are consistent with these new requirements. Nevertheless, FCMs will need to review the existing letters of credit for consistency with the regulation, and it is plausible that some could need to be re-negotiated to be consistent therewith.

To mitigate the costs of this change, the Commission has considered the extent of the use of letters of credit in the industry and has determined that upon the effective date of the regulation, § 1.43 will apply only to *new* letters of credit and customer agreements. The Commission further is including a transition period of one year from the effective date until § 1.43 will apply to existing letters of credit and customer agreements. The transition period is intended to give FCMs an adequate opportunity to conduct the necessary review of existing letters of credit and customer agreements, and to make any

[272] The Commission further understands that it is already industry practice to use such accounts, therefore, as a practical matter, the cost associated with mandating the use of such accounts should be mitigated.

[273] *See* section II.B.8 above.

necessary changes. SIFMA AMG/MFA have urged the Commission to shorten that one-year transition period, questioning how a (non-conforming) letter of credit would be treated if an FCM that is holding such a letter of credit went into bankruptcy during that period. Nonetheless, the Commission has concluded that the one-year time period appropriately balances the goals of mitigating burden on FCMs who are required to conduct such reviews, and make such changes, with the goal of mitigating the risk that an FCM that has accepted one or more letters of credit that do not conform to the new requirements becomes a debtor during that transition period. Even if such a situation occurs, the risk that the customer who posted that letter of credit would obtain treatment that is not consistent with (*i.e.,* better than) *pro rata* treatment (at the expense of other public customers) is mitigated by the provision in § 190.04(d)(3)(ii)—which is not subject to the one-year transition period—that, for a letter of credit posted as collateral, ''the trustee shall treat any portion that is not drawn upon (less the value of any substitute customer property delivered by the customer) as having been distributed to the customer for purposes of calculating entitlements to distribution or transfer.''

It is possible that some letters of credit could become more expensive for customers to obtain, as there will be an increased likelihood that the letter of credit will be drawn upon. (As discussed above, this appears to not apply to the majority of existing arrangements). As noted in the discussion of § 190.04(d)(3), the benefit of the regulation is ensuring that letters of credit are treated in an economically consistent manner with other types of collateral, thus promoting the goal of *pro rata* distribution. However, it could create incentives for customers who had, or who would prefer to, post letters of credit that could not be drawn upon unless the customer defaulted, to reduce their participation in transactions cleared through FCMs.

The provision proposed as § 190.10(e) concerns the disclosure statement for non-cash margin, and is being codified as § 1.55(p). It largely aligns with the provisions in current part 190 from which it was derived; there will be no additional cost or benefit implications.

9. Section 15(a) Factors—Subpart B

a. Protection of Market Participants and the Public

Subpart B of the revised regulations will increase the protection of market participants and the public by clarifying certain provisions (thereby promoting transparency for customers, other claimholders, and the general public), by providing, in certain other provisions, discretion to the trustee in determining how best to achieve the goal of protecting public customers as a class, by fostering transfer (and therefore mitigating the market risk associated with closing out and reopening positions for certain customers), by enhancing the likelihood that customer net equity claims will be fully funded, and by promoting fairness to customers as a class by achieving *pro rata* distribution.

b. Efficiency, Competitiveness, and Financial Integrity

Subpart B of the revised regulations will promote efficiency (in the sense of both cost effectiveness and timeliness) in the administration of insolvency proceedings of FCMs and the financial integrity of derivatives transactions carried by FCMs by setting forth clear and well-thought-out instructions for a bankruptcy trustee to follow in the event of an FCM insolvency, and by ensuring that these instructions are and remain consistent with current market practices. Moreover, subpart B will provide the bankruptcy trustee with discretion, in certain circumstances, to react flexibly to the particulars of the insolvency proceeding, guided by the goal of protecting public customers as a class, thereby promoting cost-effective administration of the proceeding. These effects will, in turn, enhance the competitiveness of U.S. FCMs, by enhancing market confidence in the protection of customer funds and positions entrusted to U.S. FCMs, even in the case of insolvency.

c. Price Discovery

Price discovery is the process of determining the price level for an asset through the interaction of buyers and sellers and based on supply and demand conditions. The revised regulations work to promote the transfer, rather than liquidation, of customer positions. To the extent that they therefore mitigate the likelihood of the need for liquidations of customer positions, particularly in conditions of market distress, they will mitigate the negative impacts of bankruptcy proceedings on price discovery.

d. Sound Risk Management Practices

Subpart B of the revised regulations will promote sound risk management practices by facilitating the bankruptcy trustee' effective management of the risk of the debtor FCM. Subpart B will accomplish this by revising the bankruptcy regulations for an FCM insolvency to reflect current market practices and thereby make it easier for the trustee to act effectively to protect customer property in the event of such an insolvency.

e. Other Public Interest Considerations

Subpart B of the revised regulations supports the implementation of statutory policy such as promoting protection of public customers and ensuring *pro rata* distribution of customer funds. Moreover, some of the FCMs that might enter bankruptcy are very large financial institutions, and some are (or are part of larger groups that are) considered to be systematically important. A well-structured and effective bankruptcy process that efficiently facilitates the proceedings is likely to benefit the financial system (and thus the public interest), as that process will help to attenuate the detrimental effects of the bankruptcy on the financial system and reduce the likelihood that uncertainty as to the outcome of the insolvency could cause disruption to financial markets.

D. Subpart C—Clearing Organization as Debtor

Subpart C to part 190 is intended to create a tailored set of regulations to govern a proceeding under subchapter IV of chapter 7 of the Bankruptcy Code in which the debtor is a clearing organization. As discussed further below, while these regulations are fitted to the context of a commodity broker that is a clearing organization, they are principles-based rather than prescriptive, and flexible rather than rigid.

The overarching benefits of this approach include the following. First, uncertainty will be reduced during business-as-usual (thus enhancing the ability of both clearing members and their customers better to understand their exposures to the possible insolvency of a clearing organization, and to tailor their risk management practices (and use of clearing services) in light of this enhanced understanding). This better understanding may well foster greater trust in the cleared derivatives marketplace, and thus greater participation therein. To be sure, it is also possible that some market participants, upon achieving a greater understanding, may decide not to participate. There are other limitations to these benefits, noted below. Second, by developing a more detailed, yet flexible, framework and procedures for the bankruptcy of a DCO, the costs (to the estate, to clearing members, and to public customers) of the case should be reduced.

Third, the resolution regime established under Title II of Dodd-Frank provides that the maximum liability of FDIC as receiver of a covered financial company to a claimant is the amount the claimant would have received if the FDIC had not been appointed receiver and the covered financial company had been liquidated under chapter 7 of the Bankruptcy Code. By establishing a clearer counterfactual, subpart C will: (a) Enhance the ability of FDIC to plan for and to execute its responsibilities as receiver; (b) enhance the ability of market participants to predict in advance their exposures in the unlikely event of the resolution as a DCO; and (c) mitigate the cost of litigation over the value of such claims. The Commission notes that there can, to a certain extent, be costs imposed by proposed subpart C, in that there may be a corresponding reduction in flexibility with the addition of rules specifically tailored to address a DCO bankruptcy, but the Commission has drafted these proposed rules with the intent of maintaining significant flexibility, where warranted.

It is apposite to note an important issue that affects incentives: A significant group of commenters have expressed strong concerns, both in comments to this rulemaking [274] and elsewhere,[275] that clearing members and their customers have no meaningful role in DCO risk governance, and, most relevant here, that DCOs' default rules and procedures and recovery and wind-down plans are developed without sufficient input from members and their customers. As discussed in detail in section II.C above and in this section II.D, subpart C is based, in large part, on a debtor DCO's *ex ante* default rules and procedures and recovery and wind-down plans, though applied flexibly by the trustee—that is, only to the extent they determine is ''reasonable'' and ''practicable.''

Most of those concerns transcend the topic of this rulemaking: As a general matter, risk governance is intended to mitigate the possibility of default and, where default does occur, to foster the result that it is the defaulter that pays for all of the losses; skin-in-the-game provides an additional layer of loss-absorbency that (i) comes before mutualizing costs to non-defaulters and (ii) creates incentives for DCOs to engage in successful risk management. Default rules and procedures are intended to, *inter alia,* ensure that the DCO can take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a clearing member default. Recovery plans address credit losses that exceed the DCO's available resources, as well as the manifestation of other risks, as necessary to maintain the derivatives clearing organization's viability as a going concern, while wind-down involves the actions of the DCO to effect the permanent cessation or sale or transfer of one or more services.

Commission regulations require DCOs to: Take steps to ensure their resilience, have effective rules and procedures to manage defaults, address fully any individual or combined default loss, and maintain viable plans for recovery in the event that they suffer a default loss or any other (non-default) loss.[276]

DCOs' rules and arrangements for default management and their recovery plans work to allocate losses that are not covered by the resources of the defaulter between the DCOs themselves, their clearing members, and (in some cases such as gains-based haircutting), will have the effect (along with clearing agreements between FCMs and their public customers) of allocating certain losses to public customers. These include default losses that are not covered by margin posted by the defaulter (or the defaulter's own contribution to mutualized loss arrangements) or by the DCO's ''skin-in-the-game,'' as well as certain investment or custody losses. All of this would occur outside of bankruptcy.[277]

Those rules, plans, and arrangements—and the extent to which they are considered helpful or noxious—thus influence the incentives of DCOs, their clearing members, and the customers of those clearing members. Accordingly, the concerns that these clearing members and money managers have raised with respect to their limited ability to influence these rules, plans, and arrangements that have effects outside of bankruptcy are likely to have important incentive effects on how, and the extent to which, clearing members and their public customers (including money managers) are willing to and do participate in cleared markets.

To the extent that subpart C of part 190 applies those rules, plans and arrangements, even if flexibly, then the incentive effects described above may be felt more strongly by clearing members and their public customers, albeit only marginally so.[278] The level of that enhanced incentive is difficult to measure, since it depends, in significant part, on the perception of those entities as to the effect of referring to those rules, plans, and procedures in bankruptcy under part 190, subpart C: Those rules, plans, and procedures, which they dislike, are and will be applicable in cases where the DCO engages in either default management or recovery *outside of* bankruptcy. The references to these rules, plans, and procedures in part 190 increases the likelihood that they will be used (because bankruptcy represents an additional circumstance in which they would be applicable). The incentive effects also depend on the perception of clearing members and their public customers on the effect of such use in bankruptcy.

A note on terminology: As discussed above in section II.C, the customers of a clearing organization are its members, considered separately in two roles: (1) Each member may have a proprietary (also known as ''house'') account at the clearing organization, on behalf of itself and its non-public customers (*i.e.,* affiliates). The property that the clearing organization holds in respect of these accounts is referred to as ''member property.'' (2) Each member may have an account for that members' public customers. The property that the clearing organization holds in respect of these accounts is referred to as ''customer property other than member property.'' Many clearing members will have both such accounts, although some may have only one or the other.

1. Regulation § 190.11: Scope and Purpose of Subpart C: Consideration of Costs and Benefits

Section 190.11(a) will simply state that the new subpart C of part 190 will apply to a proceeding commenced under subchapter IV of chapter 7 of the Bankruptcy Code in which the debtor is a clearing organization. Therefore, the costs and benefits of § 190.11(a) are the overarching costs and benefits stated above.

[274] *See* ACLI, FIA, ICI, SIFMA AMG/MFA, and Vanguard.

[275] *See, e.g.,* A Path Forward for CCP Resilience, Recovery, and Resolution (published by a group of prominent clearing members and money managers).

[276] *See generally* part 39 of the Commission's regulations. Only SIDCOs, or other DCOs that have elected to become subject to the provisions of subpart C of part 39, are required to address fully any default loss, or to maintain recovery and wind-down plans. However, among DCOs based in the United States, the vast majority of activity is conducted on DCOs that fall within one of those two categories.

[277] Moreover, among U.S. DCOs (and among all DCOs registered with the Commission), no loss has ever been so large that it was mutualized.

[278] The effects of those rules on incentives for DCOs is even more difficult to measure, since a chapter 7 liquidation (the only bankruptcy available to a commodity broker, *see* 11 U.S.C. 109(d)) is highly likely to reduce severely, if it does not eliminate, the DCO's value to its shareholders.

ICE and SIFMA AMG/MFA noted that, in the case of the bankruptcy of a DCO organized outside the United States, there may be conflicts with a bankruptcy proceeding in the home jurisdiction unless the applicability of part 190 is limited. For example, there may be differing—and irreconcilable—rules for distributing property. Such differing rules could incentivize, *e.g.* a customer of a non-FCM clearing member to bring litigation seeking to apply part 190's customer protection rules to what they might describe as the customer claims of their non-FCM clearing member.[279]

The Commission has determined to adopt a suggestion by ICE and, in a newly created § 190.11(b), to limit the applicability of part 190, in the case of a foreign DCO subject to a proceeding in its home jurisdiction, to provisions that (a) focus on the contracts and property of public customers of FCM members[280] or (b) general provisions, and those that provide notice and reports to the Commission and a U.S. bankruptcy trustee.[281] By limiting the applicability of part 190 in this manner, the Commission will foster the goal of mitigating such conflicts,[282] while by including those provisions (rather than disapplying part 190 entirely to the bankruptcy of a foreign-based clearing organization), the Commission will foster the goal of protecting customers of U.S. FCM members of such a foreign-based DCO.

[279] As noted immediately below, public customers of FCM clearing members will benefit from protection under part 190.

[280] *I.e.,* §§ 190.13, 190.17, and 190.18, but only with respect to: (1) Claims of FCM clearing members on behalf of their public customers; and (2) property that is or should have been segregated for the benefit of FCM clearing members' public customers, or that has been recovered for the benefit of FCM clearing members' public customers.

[281] *I.e.,* subpart A, and § 190.12.

[282] The Commission notes that conflicts involving a DCO based outside the United States with the insolvency law in that DCO's home jurisdiction as applied to claims of FCM clearing members on behalf of their public customers should be mitigated by the fact that, pursuant to § 39.27(c)(3) and Exhibit R to appendix A to part 39, the DCO is required to submit and to keep current a memorandum demonstrating, *inter alia,* the basis for the conclusion that the DCO's arrangements to ring-fence the customer funds of FCM clearing member are effective under the relevant non-U.S. law in the event of the insolvency of the DCO, and the basis for the conclusion that a local court or insolvency official in the DCO's jurisdiction of domicile would respect the choice of U.S. law in that context, and the basis for the conclusion that the DCO would be able to comply with relevant provisions of the Bankruptcy Code and Commission regulations with respect to *pro rata* distribution and relevant orders of a U.S. court regarding the distribution of customer funds.

2. Regulation § 190.12: Required Reports and Records: Consideration of Costs and Benefits

Section 190.12(a)(1) is analogous to § 190.03(a), in that it provides instructions regarding how to give notice to the Commission and to a clearing organization's members, where such notice is required under subpart C. For a discussion of the costs and benefits of this section, please refer to the discussion of the cost and benefit implications of § 190.03(a).

Section 190.12(a)(2) will revise the time in which a debtor clearing organization must notify the Commission of a bankruptcy filing. In particular: (1) In the event of a voluntary bankruptcy filing, the debtor will be required to notify the Commission at or before the time of filing, and (2) in the event of an involuntary bankruptcy filing, the debtor must notify the Commission as soon as possible, but in any event no later than three hours after the receipt of the notice of such filing. These revisions codify expectations that (1) in a voluntary bankruptcy proceeding, the debtor clearing organization will provide advance notice to the Commission ahead of the filing to the extent practicable, and (2) in an involuntary bankruptcy proceeding, the debtor clearing organization will notify the Commission immediately upon receiving notice of the filing, or within at the most three hours thereafter.

With respect to a voluntary bankruptcy filing, the Commission expects that the DCO will have reported its financial distress in the lead-up to a bankruptcy filing in accordance with the mandatory reporting requirements in § 39.19(c)(4); the revision in proposed § 190.12(a) merely codifies the expectation that the clearing organization will notify the Commission of an intent to file for bankruptcy protection as soon as practicable before, and in no event later than, the time of the filing. In addition, § 190.12(a) also will allow a debtor clearing organization to provide the relevant docket number of the bankruptcy proceeding to the Commission ''as soon as available,'' while not delaying notifying the Commission of the filing itself, to account for the potential for a time lag between the filing of a proceeding and the assignment by the relevant court of a docket number. These revisions will enhance the ability of the Commission to perform its responsibilities to support the interests of clearing members, customers of clearing members, markets, and the broader financial system, by providing the Commission with prompt notice of any DCO bankruptcy proceeding.

Section 190.12(b) and (c) involve the provision of certain reports and records to the trustee and/or the Commission by the debtor clearing organization. In particular: § 190.12(b) sets forth the reports and records that the clearing organization will be required to provide to the Commission and to the trustee within three hours following the later of the commencement of the proceeding or the appointment of the trustee, and § 190.12(c) sets forth the records to be provided to the Commission and to the trustee no later than the next business day following commencement of a bankruptcy proceeding. These provisions will impose administrative costs on the debtor clearing organization and/or the trustee, which will be obligated to spend time and resources transmitting copies of the required reports and records to the trustee and/or Commission. However, these provisions should both benefit the estate, and enhance the Commission's ability to fulfil its responsibilities, by providing them with the most current information about the clearing organization, and by allowing the trustee to begin to understand the business of the clearing organization as soon as possible following a bankruptcy filing, which is critically necessary to the administration of the debtor clearing organization's estate. This would in turn promote confidence in the clearing system in particular, and financial markets more broadly.

OCC indicated that, while they ''maintain[ ] this information in a readily accessible place and do[ ] not foresee any challenge in identifying and providing this information without delay,'' they believe that the three hour time period is ''overly prescriptive'' because of the possibility of ''unforeseen delays that could occur on the day in which a DCO enters bankruptcy.'' The Commission has declined to modify the proposal, because the Commission believes that setting this specific deadline will result in significant benefits: Providing this information to the trustee and the Commission with much-needed expediency, and facilitating DCOs' contingency planning. By comparison, the burden of providing the reports, which as the commenter notes, are already in existence and are readily accessible, appears modest.

3. Regulation § 190.13: Prohibitions on Avoidance of Transfers: Consideration of Costs and Benefits

Section 190.13 implements section 764(b) of the Bankruptcy Code with respect to DCOs, and prohibits the avoidance of certain transfers made either before or shortly after entry of the order for relief. While the prohibition of avoidance of pre- and post-relief transfers in the context of FCM debtors in § 190.07(e) applies so long as the transfer is not *disapproved* by Commission, the same prohibition on avoidance of pre- and post-relief transfers in § 190.13(a) and (b) will require the affirmative *approval* of the Commission (though such approval can be given either before or after the transfer is made). This distinction will impose administrative costs on the clearing organization or the trustee, who will have to expend time and resources to seek affirmative approval from the Commission for such a transfer in the context of administering a DCO, respectively, either before or after bankruptcy. As noted above,[283] a clearing organization is mandated to maintain a ''balanced book.'' Thus, a transferee clearing organization may only accept transfer of all of the transferor's customer positions (or at least all positions in a given product set).[284] Any such transfer will have significant effects on the markets cleared, and on the broader financial system. There are important benefits from requiring the Commission's approval of such a significant transaction, and thus permitting the administrative agency responsible for oversight of the derivatives markets to maintain a level of discretion which will help accomplish the goal of an orderly functioning of the marketplace.

4. Regulation § 190.14: Operation of the Estate of the Debtor Subsequent to the Filing Date: Consideration of Costs and Benefits

Section 190.14(a) provides that the trustee may, in their discretion based upon the facts and circumstances of the case, instruct each customer to file a proof of claim containing such information as is deemed appropriate by the trustee. Allowing the bankruptcy trustee to use their discretion in tailoring the proof of claim form to the specific facts and circumstances of the case should benefit both the trustee and customers by limiting the information requested to only that which is necessary for purposes of administering the debtor's estate and thereby increasing cost effectiveness, particularly given the bespoke nature of a clearing organization bankruptcy.

[283] *See* section II.C.3 above.

[284] If the transferor clearing organization does not have a balanced book, *e.g.,* because of a member default, it could nonetheless only transfer a balanced book.

Thus, the Commission has not proposed a prescribed proof of claim form. There could, however, be corresponding administrative costs to both the estate and the customers if the set of information requested by the trustee in the exercise of their discretion turns out in retrospect to be overly narrow or broad.

ICE believed that the proposal did not clearly take into account non-CFTC-regulated clearing, and that claims of members with respect to such activity should be properly accounted for in bankruptcy and should not be disadvantaged. As the Commission noted above,[285] to the extent that the DCO is conducting non-CFTC-regulated activity, the Commission expects that the proof of claim form will include the opportunity to claim for debts of the DCO related to activity that is not regulated by the CFTC. Thus, no change is necessary to address this concern.

Section 190.14(b) provides that a debtor clearing organization will cease making calls for variation settlement or initial margin.[286] Under current regulations, it would not be possible to continue the operations of a debtor clearing organization for any amount of time after entry of the order for relief, as there is no clear and coherent mechanism to do so. Thus, § 190.14(b) affirms current legal requirements and maintains the status quo. Section 190.14(c)(1) provides that the trustee shall liquidate all open commodity contracts that have not been terminated, liquidated or transferred no later than seven calendar days after the entry of the order for relief. This provision will impose administrative costs in that the trustee will have a hard deadline for terminating, liquidating or transferring any open commodity contracts within a certain timeframe, whereas under current part 190 there was no specified timeframe for such termination, liquidation or transfer. It could, however, benefit clearing members and customers, who will have certainty that their open commodity contracts would be liquidated within a particular timeframe rather than being held open for an undetermined amount of time. A deadline for liquidation or transfer of open contracts may benefit the broader financial markets by mitigating uncertainty.

[285] *See* section II.C.4.

[286] As originally proposed, § 190.14(b) also contained provisions that were intended to provide a brief opportunity, after the order for relief, to enable paths alternative to liquidation—that is, resolution under Title II of the Dodd-Frank Act, or transfer of clearing operations to another DCO—in cases where a short delay (*i.e.,* less than or equal to six days) might facilitate such an alternative path. The Commission subsequently issued the Supplemental Proposal, which withdrew those proposed provisions—§ 190.14(b)(2) and (3)—and proposed a new alternative to facilitate the potential resolution of a SIDCO pursuant to Title II of the Dodd-Frank Act. As discussed in section II.C.4 above, the Commission is not adopting the Supplemental Proposal.

Section 190.14(c)(2), which is derived from current § 190.08(d)(3), will provide that the trustee may, at their discretion, make distributions in the form of securities that are equivalent to the securities originally delivered to the debtor by a clearing member or such clearing member's customer, rather than liquidating the securities and making distributions in cash. Unlike current § 190.08(d)(3), § 190.14(c)(2) will not allow the customer to request that the trustee purchase like-kind securities and distribute those instead of cash, but instead will leave it to the discretion of the trustee whether to do so. This change could impose costs on customers who would prefer to have a distribution of equivalent securities rather than cash, since it will remove their option to request such a distribution. However, it could benefit the estate by allowing the trustee to use their discretion as to whether to purchase and distribute equivalent securities, rather than being obligated to do so at the request of a customer.

Section 190.14(d) will require the trustee to use reasonable efforts to compute the funded balance of each customer account immediately prior to the distribution of any property in the account, ''which shall be as accurate as reasonably practicable under the circumstances, including the reliability and availability of information.'' This requirement applies with respect to accounts of the customers of the clearing organization: That is, its members, separately in respect of each such member's (1) house account (on behalf of the member and its non-public customers and (2) customer account or accounts (on behalf of the member's public customers, one such account for each account class, to the extent relevant).

This requirement will impose administrative costs due to the time and effort involved in making such calculations. However, the regulation gives the trustee a certain amount of discretion, and this calculation will be necessary to achieve the goal of making distributions that are consistent with each customer's proportionate share.

5. Regulation § 190.15: Recovery and Wind-Down Plans; Default Rules and Procedures: Consideration of Costs and Benefits

Section 190.15 provides that (1) the trustee shall not avoid or prohibit any action taken by a debtor that was within the scope of and was provided for in the debtor's recovery and wind-down plans; (2) in administering a DCO bankruptcy, the trustee shall, subject to the reasonable discretion of the trustee and to the extent practicable, implement the default rules and procedures maintained by the debtor; and (3) in administering a DCO bankruptcy, the trustee shall, to the extent reasonable and practicable, and consistent with the protection of customers, take actions in accordance with the debtor's recovery and wind-down plans.

The Commission considered two alternatives to directing the trustee to implement the debtor's own default rules and procedures and recovery and wind-down plans: First, continuing to allow a bankruptcy trustee to develop, in the moment, a plan for liquidating the debtor clearing organization, and second, prescribing an across-the-board method for liquidating a debtor clearing organization.

A number of commenters appeared to support the first alternative approach. Some (*e.g.,* ACLI, FIA, ICI, SIFMA AMG/MFA, Vanguard) expressed concern that they lack transparency with regard to the DCO risk management decisions and DCOs' default rules and procedures and recovery and wind-down plans are developed without sufficient input from clearing members and their customers. For example, Vanguard argued that the existing DCO governance regime provides them with no meaningful voice in critical DCO risk management practices and new cleared product introductions; and since public customers have only a very limited ability to mitigate clearing risks contractually, they ''rely heavily on the Commission to protect the interests of [their] investors in the mandated cleared market.'' Commenters also expressed the concern that there is a risk that, as a DCO begins to fail, otherwise prudent DCO rules could be changed without the appropriate vetting by clearing members and public customers who, given mutualized allocation of losses, bear the risk of poor risk management choices undertaken by the DCO.[287]

The Commission has considered the potential interplay of the amendments to part 190 with other Commission regulations and applicable statutes. As noted above, these commenters' concerns predominantly relate to the economic interests of clearing members and their customers in contexts outside of bankruptcy.

A DCO's operations and rules outside of bankruptcy are governed by parts 39 and 40 of the Commission's regulations. The Commission, in particular through its Division of Clearing and Risk, applies these regulations and conducts a rigorous program of oversight of DCOs designed to protect the interests of market participants and of the financial system, including through careful reviews of their rules (including default rules) and their recovery and wind-down plans, through detailed daily and periodic risk surveillance, and through in-depth remote and on-site examinations addressing a wide spectrum of risk management issues.

As noted by a commenter above, they ''rely heavily on the Commission to protect the interests of our investors in the mandated cleared market.'' Over the years, the Commission has taken seriously its responsibilities in this regard, through its regulatory, surveillance, and examinations programs.

As discussed above, there are important costs to addressing, in the context of part 190, market participants' concerns regarding DCOs' rules, procedures, and plans for allocating losses that apply outside of a DCO bankruptcy: Establishing a bankruptcy regime where some market participants would be allocated a smaller amount of losses in bankruptcy than outside of bankruptcy would risk creating incentives for those participants to act in a manner that promotes the likelihood that the DCO will enter bankruptcy.

In view of these considerations, the Commission believes the commenters' concerns are effectively mitigated by the existing provisions of parts 39 and 40 of its regulations and by the Commission's supervision of DCOs.[288] Therefore, the adoption of part 190, subpart C, which is applicable to a DCO's potential bankruptcy, appropriately complements parts 39 and 40 and the Commission's ongoing supervision, which apply to a DCO's operations and rules outside of bankruptcy.

Other commenters are concerned with the inclusion in those DCO rules and plans of ''drastic measures as Variation Margin Gains Haircutting (VMGH) and Partial Tear-Up (PTU) of open positions.'' Gains haircutting, however, is part of the *ex ante* allocation of losses, and thus is an inherent part of the way in which losses will be allocated in bankruptcy. Moreover, there is a limited amount of customer property available. Thus, to the extent the application of VMGH were to be disallowed, and some customers would realize corresponding benefits through increases in the allowed amounts of their claims (and thus a greater share of customer property), other customers would suffer corresponding costs, through a decreased share of customer property—indeed, the latter customers may receive less than the amount of their claims for initial margin.[289] Accordingly, the Commission concludes that it is inadvisable to prohibit VMGH, or to mandate that its effects be reversed, in cases of DCO bankruptcy.

Partial tear-up, on the other hand, is inapplicable in a clearing organization bankruptcy: § 190.14(b) prohibits further collection of variation margin, while § 190.14(c) requires the trustee to liquidate all open commodity contracts. Together, they effectively mandate *full* tear-up of open positions. Thus, the question of whether partial tear-up should be prohibited is moot.

Other commenters were concerned that these plans do not prescribe a specific course of action, but rather ''present a menu of options.'' *See, e.g.,* FIA, Vanguard. The Commission is of the view that, given the complexity of the operations of a DCO, and the need for extremely prompt action, having the trustee develop an entire plan in the moment would be likely to turn out to be impracticable. By contrast, being presented with a ''menu of options'' among which the trustee may select (and adapt) in a manner that is ''reasonable and practicable'' provides the benefit of a helpful roadmap to determine strategy and tactics.

The commenters, and potentially other clearing members and public customers who share the concerns of the commenters, appeared to view DCO default rules and procedures and recovery and wind-down plans that they believe have been adopted with

[287] With respect to DCO rules adopted as the DCO is on the threshold of failure: DCO rules are subject to review by the Commission. In all cases, they are subject to review for consistency with the CEA and Commission regulations (*see* § 40.6). In the case of SIDCOs, they are additionally subject to review for consistency with the purposes of the Dodd-Frank Act or any applicable rules, orders, or standards prescribed under section 805(a) thereof. Moreover, to the extent commenters are concerned that such late-enacted rules will be unfair to clearing members or their customers, the Commission expects that such unfairness would affect the trustee's judgment of the extent to which it is ''reasonable'' to apply those rules.

[288] Nonetheless, the Commission is sensitive to the concerns raised by commenters with respect to the development and maintenance of DCO recovery and wind-down plans and default rules and procedures, and is actively reviewing these issues, in particular with respect to governance, as they relate to parts 39 and 40.

[289] *Cf.* ISDA: Safeguarding Clearing: The Need for a Comprehensive CCP Recovery and Resolution Framework (2017) at 2 (''Initial margin haircutting should never be permitted.'')

inadequate input from them as noxious, and thus they may already be incentivized to reduce their exposure to such DCOs. Those incentives may be (marginally) increased by the fact that the Commission is establishing in § 190.15 a model for the trustee that is based on those rules, procedures, and plans.

Other commenters (CME and ICE) supported the second alternative, specifically, a requirement that the trustee cannot override the DCO's default rules or deviate from the DCO's recovery or wind-down plans. However, given that these rules and plans are designed to operate outside of bankruptcy, a requirement to follow them in procrustean fashion would have the cost of compelling the trustee to adopt an approach that may be poorly tailored to the situation, and the Commission will accordingly not adopt such a requirement.

Finally, given the differences between DCOs (and potential bankruptcy situations), a one-size-fits-all approach prescribed by the Commission is likely to prove too rigid, and thus will not be adopted.

The Commission is accordingly of the view that, relative to these alternatives, directing a trustee to implement the DCO's own default rules and procedures, and recovery and wind-down plans, would benefit the estate by providing the trustee with a menu of purpose-built rules, procedures and plans to liquidate a DCO, which rules, procedures and plans the DCO has developed subject to the requirements of the Commission's regulations and supervision of the Commission. Adding concepts of reasonability and practicability will give the trustee the discretion to modify those rules, procedures, and plans where and to the extent appropriate. Hence, the Commission believes that an approach whereby the trustee would follow the DCO's own purpose-built default rules and procedures and recovery and wind-down plans, but have the discretion to vary them as appropriate, would be the most cost effective.

6. Regulation § 190.16: Delivery: Consideration of Costs and Benefits

Regulation § 190.16 addresses delivery in the context of a clearing organization bankruptcy. Current part 190 does not contain any regulations specific to delivery in that context.

Section 190.16(a) provides that a bankruptcy trustee is required to use ''reasonable efforts'' to facilitate and cooperate with the completion of the delivery on behalf of the clearing organization's clearing member or the clearing member's customer. This has the benefit of mitigating disruption to the cash market for the commodity and mitigating adverse consequences to parties that may be relying on delivery taking place in connection with their business operations. While the exertion of such reasonable efforts will necessarily involve administrative costs (predominantly, time of the trustee or their agents), the Commission is of the view that this approach has important benefits relative to the two alternatives. Given the importance of reliable delivery to physical markets, it would be inappropriate to relieve the trustee of the obligation to endeavor to facilitate and cooperate with the members' or members' customers' efforts to accomplish delivery. On the other hand, mandating that the trustee go beyond reasonable efforts would risk compelling the trustee to expend unwarranted amounts of resources in this endeavor.

While proposed § 190.16(a) applied this approach only to contracts that had moved into delivery position prior to the date and time of the order for relief, the ABA Subcommittee and CME suggested that this approach should be extended to contracts that move into delivery position after that date and time, with CME noting that ''it is equally important to protect deliveries under [such contracts] to avoid disruption to commercial markets and operations.'' The Commission has accepted this suggestion and notes that, if any contracts move into delivery position after the order for relief, but before being terminated, liquidated, or transferred, the benefits and costs of this approach are analogous to those of contracts that move into delivery position prior to the order for relief.

Section 190.16(b) clarifies which property will be part of the physical delivery account class and which will be part of the cash delivery account class. It is analogous to § 190.06(b) in the FCM context, and carries forward the concepts in that section, but has been modified for the context of a DCO bankruptcy. Clearly delineating between the physical delivery account class and the cash delivery account class will benefit customers because it will increase transparency in terms of which account class their property belongs in. Section 190.16(b) will likely impose administrative costs, since accounting separately for physical delivery property and cash delivery property will take the trustee's time and resources. As noted above,[290] the sub-division of the delivery account class into the physical and cash delivery account classes will recognize that cash is more vulnerable to loss, and more difficult to trace, as compared to physical delivery property. Therefore, this sub-division will likely benefit those with physical delivery claims. Since cash is more vulnerable to loss and more difficult to trace, then under this approach, clearing members and customers with claims in the cash delivery sub-class will be more likely to get a *pro rata* distribution that would be less than those with claims in the physical delivery property sub-class.[291]

7. Regulation § 190.17: Calculation of Net Equity: Consideration of Costs and Benefits

Section 190.17(a) clarifies that a member of a debtor clearing organization may have claims against the clearing organization in separate capacities: On behalf of its public customers (customer accounts) and on behalf of its non-public customers (house accounts). It further states that net equity shall be calculated separately for each customer capacity in which the clearing member has a claim against the debtor. In the Commission's view, the provisions in § 190.17(a) are clarifications that reflect customer classifications set forth in section 766(i) of the Bankruptcy Code, and account classifications that have long been used in other contexts, and will not impose any costs or benefits on any parties.

Section 190.17(b)(1) provides that the calculation of a clearing member's net equity claim in the bankruptcy of a clearing organization shall include the full application of the debtor's loss allocation rules and procedures. It also provides that, with respect to a clearing member's house account, this will include any assessments or similar loss allocation arrangements provided for under those rules and procedures that were not called for before the filing date, or, if called for, have not been paid.

A number of commenters, including the ABA Subcommittee, CME, FIA, and ICE, objected to including assessments that had not been called for before the order for relief in the calculation of net equity claims where the debtor clearing organization's rules provide that assessments cannot be called for after bankruptcy. Taking these commenters' preferred approach would benefit the clearing members in circumstances where there are both uncalled

[290] *See* discussion of § 190.06(b) in section II.B.4 above.

[291] Costs and benefits of the separation of the delivery account class into physical delivery and cash delivery subclasses were also addressed in respect to the costs and benefits section addressing the definition of ''account class'' in § 190.01, section II.A.2 above.

assessments, and remaining default losses. As FIA noted in its comment letter, the inclusion of uncalled assessments ''appears to have the effect of reducing a clearing member's potential recovery.'' However, all losses will ultimately be allocated, and if uncalled assessments are not taken into account, any remaining losses that haven't been covered by other default resources will be allocated through gains-based haircutting. Thus, the commenters' preferred approach would be at the cost of the customers of clearing members, who would bear additional losses even as the clearing members would benefit.

Relative to the alternative suggested by these commenters, the direct effect of § 190.17(b)(1) is to ensure that the uncalled assessment will make up more of the default losses, and conversely that haircutting of the gains (of both clearing members and customers) will make up less of that loss. Hence, the rule could harm clearing members, and correspondingly benefit their customers. In addition, there can be indirect effects. While the maximum amount of assessments that clearing members are exposed to will not increase, there is a marginally [292] increased likelihood that those assessments will be used.[293] Because clearing members' potential assessments are more likely to be used, they will have a marginally increased incentive to reduce their level of exposure to assessments—for example, by reducing their clearing activity for themselves or on behalf of their customers. While it is conceivable that clearing members could work to influence DCOs to reduce their own assessment powers as a result of these incentives, there are mitigants in the Commission's regulations.[294]

Section 190.17(b)(2) provides that where the debtor's loss allocation rules and procedures provide that clearing members are entitled to payments due to portions of mutualized default resources that are either prefunded, or assessed and collected, but in either case not used, or to the clearing organization's recoveries on claims against others (including recoveries on claims against defaulting clearing members), then ''appropriate adjustments shall be made to the net equity claims of clearing members that are so entitled.'' These provisions will benefit the estate by providing the trustee with tools to act promptly and efficiently, with lower administration costs. The trustee will have a clear roadmap to calculate net equity in the bankruptcy of a clearing organization and will not be obligated to come up with an ad hoc methodology for doing so. The provisions would also benefit clearing members (and, therefore, their customers) by providing transparency as to how their net equity will be calculated, as well as facilitating the efficient administration of the estate.[295]

In those cases where the debtor has excess mutualized default funds, or recovers on claims against defaulters, application of the debtor's ''reverse waterfall'' rules will benefit clearing members (and, in certain cases, their customers) by increasing the net equity claims of the entitled clearing members.

In addition to the potential for these transfers between general creditors and clearing members and their customers, this rule can create incentives for clearing members and their customers. In particular, it makes clearing members' contributions to mutualized resources (and the possibility that gains-based haircutting will affect clearing members and their customers) less onerous, because they enhance the possibility that if the clearing member's contribution to mutualized default resources (or gains-based haircutting affecting clearing members or their customers) is used to meet a default, it ultimately will come back to the clearing member or their customers as it is recovered by the DCO (or the DCO's trustee) from the (bankruptcy) estate of the defaulter.

Section 190.17(c) adopts by reference the net equity calculations set forth in proposed § 190.08, to the extent applicable.[296]

Section 190.17(d) sets forth a definition of the term ''funded balance'' that is taken directly from the relevant Bankruptcy Code provisions. Clarifying the meaning of the term ''funded balance'' in the context of a clearing organization bankruptcy will benefit clearing members, in that they will know *ex ante* what is and is not included in their funded balance and how that amount is calculated. In addition, § 190.17(d) adopts by reference the methodology for calculating funded balance that is set forth in § 190.08(c).[297]

8. Regulation § 190.18: Treatment of Property: Consideration of Costs and Benefits

Section 190.18(a) is analogous to § 190.17(a), in that it will provide that property of the debtor clearing organization's estate will be allocated between member property and customer property other than member property in order to satisfy the proprietary and customer claims, respectively, of clearing members. In the Commission's view, the provisions in § 190.18(a) are mere clarifications and do not impose any costs or benefits on any parties.

Section 190.18(b)(1)(i) and (ii) set out the scope of customer property for a clearing organization, and are largely based on § 190.09(a).[298]

Section 190.18(b)(1)(iii) provides that customer property for a clearing organization includes any guaranty fund deposit, assessment or similar payment or deposit made by a clearing member or recovered by a trustee, to the extent any remains following administration of the debtor's default rules and procedures, and any other property of a member available under the debtor's rules and procedures to satisfy claims made by or on behalf of public customers of a member. This provision supports the goal of making customers of the clearing organization whole, since it clarifies that any property described in this section will be included in the scope of customer property, rather than ultimately going to some other creditor of the debtor. It would result in corresponding costs to non-customer creditors, and could result in administrative costs, however, since the trustee could need to spend time and resources in order to determine whether any such property exists in order to properly allocate such property to customers.

[292] ''Marginal'' because this happens only if (a) there is a DCO bankruptcy, (b) there is a default loss suffered by the DCO in connection with the bankruptcy, and (c) not all of the assessments necessary to address that default loss were called before that bankruptcy.

[293] While § 190.17(b)(1) will not result in uncalled assessments being ''called''—the clearing members will not have to pay them to the estate—uncalled assessments will be ''used'' to reduce the clearing member's net equity claim.

[294] For example, § 39.39(b)(1) requires SIDCOs and Subpart C DCOs to have *viable* plans for recovery necessitated by uncovered credit losses, and the extent of a DCO's assessment power contributes to the viability of its recovery plan. Moreover, the two SIDCOs, CME and ICE Clear Credit, already have significant assessment powers, and any proposed rule change to reduce those powers would need to withstand review under § 40.10 for consistency with *inter alia,* the purposes of the CEA and the Dodd-Frank Act, which include the mitigation of systemic risk and the promotion of financial stability.

[295] *See also* 17 CFR 39.16 (requiring each DCO to, among other things, ''adopt rules and procedures designed to allow for the efficient, fair, and safe management of events during which clearing members become insolvent or default on the obligations of such clearing members to the'' DCO).

[296] For a discussion of the cost and benefit considerations for § 190.08, please see section IV.C.6 above.

[297] For a discussion of the cost and benefit considerations for § 190.08(c), please see section III.C.6 above.

[298] For a discussion of the cost and benefit considerations for § 190.09(a), please see section III.C.7 above.

A number of commenters (CME, SIFMA AMG/MFA) have suggested that the Commission make it explicit that customer property should include the amounts of its own funds a debtor DCO had committed as part of its loss allocation rules. The Commission has accepted this suggestion in the final rule, incorporating this provision in § 190.18(b)(1)(iv). This will benefit customers, who will have additional funds allocated to their claims, thereby increasing the payment that they receive on their claims and/or increasing the likelihood of full payment of their claims (due to an increase in customer property). However, this benefit would accrue at the possible expense of general creditors, as there will be an equivalent reduction in assets in the general estate. An indirect consequence of this change might be to marginally incentivize customers to retain open positions in contracts that are cleared by a potentially-failing DCO, which might marginally contribute to preserving liquidity in those markets.

Regulation § 190.18(b)(2) adopts by reference, in the context of a DCO as a debtor, the exclusions from customer property applied in the context of debtor FCMs in § 190.09(a)(2), as if the term debtor used therein would refer to a clearing organization as debtor and to the extent relevant to a clearing organization.[299]

Regulation § 190.18(c) sets forth the allocation of customer property among customer classes (*i.e.,* allocation between (1) customer property other than member property, and (2) member property). This provision, in general, applies the principle, consistent with the Commission's policy to favor public customers over non-public customers, that allocation to customer property other than member property is favored over allocation to member property, so long as the funded balance in any account class for members' public customers is less than one hundred percent of net equity claims. This provision would, in the event and at the time it applied, benefit the public customers of the debtor's clearing members, since it makes clear that allocation to such customers is preferred over allocation to the clearing members' house accounts. It imposes corresponding costs on the debtor's clearing members and affiliates to the extent that, under the current regime, there is a possibility that more customer property would be allocated to their house accounts. Overall, this provision provides the benefit of *ex ante* transparency to the estate, the debtor's clearing members, and their customers, who would know during business-as-usual how customer property would be allocated in the event of a bankruptcy.

However, the ABA Subcommittee, CME, FIA, and ICE objected to proposed § 190.18(c)(1), which would apply the debtor's mutualized (and, in general, member-funded) default fund to customer property other than member property, that is, to the customer class for members' public customers, to the extent the funded balance is less than one hundred percent for members' public customers in any account class. CME raised a particularly trenchant point: Devoting member-funded guarantee funds to purposes other than mutualizing member defaults may result in more onerous capital treatment for the contributions of bank- or bank-affiliated-members to such funds, increasing the capital charges for such exposures manifold.[300]

As noted, the costs and benefits discussed above will only accrue if there is both a clearing organization bankruptcy and a shortfall in customer funds in one or more of the account classes for members' public customers for that clearing organization in that bankruptcy. The costs and benefits at that potential future time would be balanced, in that the costs to clearing members (whose guarantee funds were devoted to claims of the clearing members' customers) would be benefits to those customers. By contrast, less favorable capital treatment would have a present-day effect, in the form of higher capital costs for clearing members. Moreover, those higher costs would not create any direct benefit (present day or otherwise) for, *e.g.,* customers. In light of these factors, the Commission has decided not to adopt proposed § 190.18(c)(1) and to renumber the remaining paragraphs of § 190.18(c).

Section 190.18(d) sets forth the allocation of customer property among account classes. This provision is similar in concept to § 190.09(c). This provision will benefit clearing members and their customers, who will have increased transparency, *ex ante,* into how customer property will be allocated. Prescribing this allocation will, however, impose administrative costs, because the trustee will lose some amount of flexibility in terms of how to allocate customer property between account classes.

Section 190.18(e) provides that, where the debtor has, prior to the order for relief, kept initial margin for house accounts in accounts without separation by account class, then member property will be considered to be in a single account class.[301] This provision will benefit the estate in those cases, because the trustee will not be put to the considerable task of separating in bankruptcy that which was treated as a single account during business-as-usual. Paragraph (e) will also benefit the debtor's clearing members, who will have increased transparency as to how their member property will be treated.

Section 190.18(f) gives the trustee the authority to assert claims against any person to recover the shortfall of customer property enumerated in certain paragraphs elsewhere in § 190.18, analogous to § 190.09(a)(3). This provision could impose administrative costs, since the trustee will need to expend time and resources to assert claims to make up for any shortfall in customer property. The provision will, however, benefit customers, since it will support the trustee's efforts to recover any such shortfalls by giving the trustee authority to act to do so. Moreover, since this provision will make explicit what is implicit in current part 190, an additional benefit of this provision is a reduction in potential litigation costs over a trustee's attempts to recover shortfalls in customer property.[302]

9. Regulation § 190.19: Support of Daily Settlement: Consideration of Costs and Benefits

Section 190.19 deals with the treatment of variation settlement in a clearing organization bankruptcy, and sets forth the approach for the trustee to follow when there is a shortfall in variation settlement owed to a debtor clearing organization's clearing members and customers. Specifically, § 190.19(a) provides that any variation settlement payments received by the clearing organization after entry of an order for relief shall be included in customer property, and shall promptly be distributed to the member and customer accounts entitled to such payments. Section 190.19(b) deals with a situation where there is a shortfall in

[299] For a discussion of the cost and benefit considerations for proposed § 190.09(a)(2), please see section III.C.7 above.

[300] As discussed in detail in a footnote in section II.C.8, those capital charges could increase by literally hundreds of times, for a total impact of billions of dollars in increased capital charges.

[301] ''Account class'' is defined in § 190.01 as meaning one or more of each of the following types of accounts, as described in greater detail in that provision: (1) Futures account; (2) foreign futures account; (3) cleared swaps account; and (4) delivery account.

[302] As discussed above in section III.C.7, while the persons against whom claims are successfully asserted may perceive a subjective cost, the Commission does not find these costs relevant to the analysis.

variation settlement received by the clearing organization, and provides that such funds shall be supplemented with four specified categories of funds (margin, to the extent permissible under parts 1, 22, and 30, assets of the debtor, to the extent dedicated to such purpose, prefunded guarantee funds, and assessments) in accordance with the clearing organization's default rules and procedures and (with respect to assets of the debtor) any recovery and wind-down plans maintained by the clearing organization.

Section 190.19 will benefit clearing members and their customers because it will ensure that any variation settlement received by the clearing organization will be sent to those member and customer accounts that would be entitled to payment of variation settlement, and that the trustee would be able to supplement any shortfall in variation settlement amounts with the property listed in proposed § 190.19(b). This approach will also benefit the financial system more broadly, by mitigating the effect of the bankruptcy of the debtor on settlement payments. There will be corresponding costs to general creditors of the clearing organization since, under current part 190, it is conceivable that, contrary to the Commission's interpretation of the current rules, variation settlement received by the clearing organization could be diverted to the pool of general creditors rather than becoming customer property (even though such diversion would be contrary to the expectations of both the Commission and the industry). In clarifying how variation settlement received by the clearing organization is to be treated by the bankruptcy trustee, § 190.19 will also benefit clearing members and their customers by providing enhanced transparency.

10. Section 15(a) Factors—Subpart C

i. Protection of Market Participants and the Public

Subpart C of the part 190 regulations will increase the protection of market participants and the public by setting forth a bespoke framework for how the bankruptcy trustee is expected to treat the property of DCO clearing members and their customers in the event of a DCO insolvency, thereby promoting *ex ante* transparency for such clearing members and customers, and by providing, in certain provisions, discretion to the trustee in determining how best to address the bankruptcy of the DCO, and to achieve the goal of protecting public customers as a class. Moreover, the addition in part 190 of bespoke bankruptcy rules for a DCO bankruptcy will provide better protections to market participants by accounting for the unique position of clearing members (and the customers of such clearing member) of a DCO that is going through an insolvency proceeding. Finally, provisions such as § 190.18(c), which preferentially allocate excess property in any account class to the customer class that benefits public customers, to the extent there is a shortfall in any account class in that customer class, will further protect public customers.

ii. Efficiency, Competitiveness, and Financial Integrity

Subpart C of the part 190 regulations will promote efficiency (in the sense of both cost effectiveness and timeliness) in the administration of insolvency proceedings of DCOs, and the financial integrity of transactions cleared by DCOs by setting forth clear instructions for a bankruptcy trustee to follow in the event of a DCO insolvency. Moreover, subpart C will provide the bankruptcy trustee with discretion, in certain circumstances, to react flexibly to the particulars of the insolvency proceeding, guided by the goal of protecting public customers as a class, thereby promoting efficiency of the administration of the proceeding. These effects will, in turn, enhance the competitiveness of U.S. DCOs and their FCM clearing members, by enhancing market confidence in the protection of customer funds and positions entrusted to U.S. DCOs through their clearing members, even in the case of insolvency.

iii. Price Discovery

Price discovery is the process of determining the price level for an asset through the interaction of buyers and sellers and based on supply and demand conditions. Because a DCO bankruptcy inevitably leads to full close-out of the positions carried at the DCO, the part 190 regulations will not contribute to avoiding the resultant negative impacts on price discovery.

iv. Sound Risk Management Practices

Subpart C of the part 190 regulations will promote sound risk management practices by facilitating the bankruptcy trustee's efforts to manage effectively the risk of the debtor DCO. Subpart C will accomplish this by adding bankruptcy regulations to part 190 for a DCO insolvency that reflect current market practices and thereby make it easier for the trustee to act effectively to protect customer property in the event of such an insolvency. Moreover, subpart C will promote sound risk management practices by instructing a bankruptcy trustee to implement the debtor DCO's default rules and procedures and to take actions in accordance with the debtor DCO's recovery and wind-down plans, which rules, procedures and plans are developed and overseen by the Commission, though subject to the trustee's discretion. Some portions of subpart C may make additional resources available to the trustee. On the other hand, some commenters expressed concern about changes (such as § 190.15) that they believe might lead to inappropriate risk management choices by DCOs.

v. Other Public Interest Considerations

By favoring the implementation of the clearing organization's default rules, recovery plans, and procedures established *ex ante* under the supervision of the Commission, and by supporting daily settlement, the part 190 regulations will support financial stability. Moreover, some of the DCOs that might enter bankruptcy are very large financial institutions, and some are considered to be systematically important. An effective bankruptcy process that efficiently facilitates the proceedings is likely to benefit the financial system (and thus the public interest), as that process will help to attenuate the detrimental effects of the bankruptcy on the financial network.

E. Changes to Appendices A and B

The Commission is deleting forms 1 through 3 contained in appendix A, which contain outdated provisions that require the collection of unnecessary information, and is replacing form 4 with a streamlined template proof of claim form, which the trustee can use in a flexible manner. CME considered the template proof of claim ''a major improvement'' over the current version. These changes have the benefit of reducing administrative costs, and there are no obvious increased costs.

Similarly, the Commission is making clarifying changes to framework 1 of appendix B, and making, consistent with the suggestions of the ABA Subcommittee and the Subcommittee Members, a significant set of clarifying changes to framework 2. These changes have the benefit of having framework 2 work in a more accurate, and less confusing manner, thus reducing administrative costs, and there are no obvious increased costs.

F. Technical Corrections to Parts 1, 4, and 41

The Commission is making technical corrections to parts 1, 4, and 41 to update cross-references. These corrections are clarifying and do not have any impact on the substantive obligations related to these sections. Thus, there are no increased costs associated with these minor technical updates.

IV. Related Matters

A. Antitrust Considerations

Section 15(b) of the CEA requires the Commission to take into consideration the public interest to be protected by the antitrust laws and endeavor to take the least anticompetitive means of achieving the purposes of the CEA in issuing any order or adopting any Commission rule or regulation.[303]

The Commission believes that the public interest to be protected by the antitrust laws is the promotion of competition. The Commission has considered this rulemaking to determine whether it might have anticompetitive effects, and has not identified any effect this rulemaking, which would apply only in the rare instance of an FCM or DCO bankruptcy, would have on competition. Accordingly, the Commission has not identified any less anticompetitive means of achieving the purposes of the CEA.

B. Regulatory Flexibility Act

The Regulatory Flexibility Act (''RFA'') requires that agencies consider whether the regulations they propose will have a significant economic impact on a substantial number of small entities and, if so, provide a regulatory flexibility analysis on the impact.[304] The regulations being adopted by the Commission affect clearing organizations, FCMs, bankruptcy trustees, and customers. The Commission has previously established certain definitions of ''small entities'' to be used in evaluating the impact of its regulations in accordance with the RFA.[305]

The Commission has previously determined that clearing organizations and FCMs are not small entities for purposes of the RFA.[306] In the event of a bankruptcy, a trustee is appointed as receiver to manage the estate of the insolvent FCM or clearing organization. Accordingly, since the trustee is representing the estate of either an FCM or clearing organization, the trustee is not a small entity for purposes of the RFA. The Commission recognizes that many customers of an FCM or DCO in bankruptcy could be considered to be small entities for purposes of the RFA. The Commission believes, however, that the amendments to part 190 are designed so that they can be implemented without imposing a significant economic burden on a substantial number of small entities. These regulations take into account existing trading practices and the logistical considerations of implementing the regulations.

Accordingly, the Commission Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b), that the rule adopted herein will not have a significant economic impact on a substantial number of small entities.

C. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (PRA) [307] imposes certain requirements on Federal agencies (including the Commission) in connection with their conducting or sponsoring a collection of information as defined by the PRA. The regulations adopted herein would result in such a collection, as discussed below. A person is not required to respond to a collection of information unless it displays a currently valid control number issued by the Office of Management and Budget (OMB). The regulations include a collection of information for which the Commission has previously received control numbers from OMB. The title of this collection of information is: OMB Control Number 3038–0021, ''Regulations Governing Bankruptcies of Commodity Brokers.''

Information Collection 3038–0021 [308] contains the reporting, recordkeeping and third-party disclosure requirements in the Commission's bankruptcy regulations for commodity broker liquidations (17 CFR part 190). These regulations apply to liquidations under chapter 7, subchapter IV of the Bankruptcy Code.[309] The Commission promulgated part 190 pursuant to the authority of 7 U.S.C. 24. The Commission is amending Information Collection 3038–0021 as a result of these final regulations to (1) accommodate new information collection requirements for FCMs and DCOs, and (2) revise the existing information collection requirements for FCMs and DCOs. The Commission did not receive any comments regarding its PRA burden analysis in the preamble to the proposal.

1. Reporting Requirements in an FCM Bankruptcy

Regulation § 190.03(b)(1) requires FCMs that file a petition in bankruptcy to notify the Commission and the relevant DSRO, as soon as practicable before and in any event no later than the time of such filing, of the anticipated or actual filing date, the court in which the proceeding will be or has been filed and, as soon as known, the docket number assigned to that proceeding. It further requires an FCM against which an involuntary bankruptcy petition or application for a protective decree under SIPA is filed to notify the Commission and the relevant DSRO immediately upon the filing of such petition or application.

Regulation § 190.03(b)(2) requires the trustee, the relevant DSRO, or an applicable clearing organization to notify the Commission if such person intends to transfer or apply to transfer open commodity contracts or customer property on behalf of the public customers of the debtor.

Based on its experience, the Commission anticipates that an FCM bankruptcy would occur once every three years.[310] The Commission has estimated the burden hours for the reporting requirements in an FCM bankruptcy as follows:

Estimated number of respondents: 1.

Estimated annual number of responses per respondent: 1.[311]

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[303] Section 15(b) of the CEA, 7 U.S.C. 19(b).

[304] 5 U.S.C. 601 *et seq.*

[305] 47 FR 18618 (Apr. 30, 1982).

[306] *See* 66 FR 45604, 45609 (Aug. 29, 2001); 67 FR 53146, 53171 (Aug. 14, 2002).

[307] 44 U.S.C. 3501 *et seq.*

[308] There are two information collections associated with OMB Control No. 3038–0021. The first includes the reporting, recordkeeping, and third-party disclosure requirements applicable to a single respondent in a commodity broker liquidation (*e.g.,* a single FCM, DCO, or trustee) within the relevant time period. This includes both (1) requirements on a single FCM or a single trustee in an FCM bankruptcy which correspond to current requirements on a single FCM or a single trustee in an FCM bankruptcy, as provided for in §§ 190.03(b)(1) and (2) and (c)(1), (2), and (4), 190.05(b) and (d), and 190.07(b)(5); and (2) new requirements on a single DCO or a single trustee in a DCO bankruptcy as provided for in §§ 190.12(a)(2), (b)(1) and (2), and (c)(1) and (2) and 190.14(a) and (d). The second information collection includes the third-party disclosure requirements that are applicable during business as usual to multiple respondents (*e.g.,* multiple FCMs). These requirements were proposed as § 190.10(b) and (e) (which are analogs to current §§ 190.06(d) and 190.10(c)), as well as a new third-party disclosure requirement provided for in § 190.10(d) (regarding letters of credit); however, the third-party disclosure requirements are being adopted as §§ 1.41, 1.43, and 1.55(p).

[309] 11 U.S.C. 761 *et seq.*

[310] These estimates express the burdens in terms of those that would be imposed on *one* respondent during the three-year period.

[311] The Commission estimates that (1) under § 190.03(b)(1), an FCM would make two notifications per bankruptcy (one to the Commission and one to its DSRO), and (2) under § 190.03(b)(2), an FCM would make one notification per bankruptcy. Dividing those numbers by three (since the Commission anticipates an FCM bankruptcy occurring once every three years) results in 0.67 notifications annually pursuant to

Estimated total annual number of responses for all respondents: 1.

Estimated annual number of burden hours per respondent: 1.[312]

Estimated total annual burden hours for all respondents: 1.

2. Recordkeeping Requirements in an FCM Bankruptcy

Regulation § 190.05(b) requires the trustee to use reasonable efforts to compute a funded balance for each customer account that contains open commodity contracts or other property as of the close of business each business day subsequent to the order for relief until the date all open commodity contracts and other property in such account has been transferred or liquidated.

Regulation § 190.05(d) requires the trustee to use reasonable efforts to continue to issue account statements with respect to any customer for whose account open commodity contracts or other property is held that has not been liquidated or transferred.

Based on its experience, the Commission anticipates that an FCM bankruptcy would occur once every three years.[313] The Commission has estimated the burden hours for the recordkeeping requirements in an FCM bankruptcy as follows:

Estimated number of respondents: 1.

Estimated annual number of responses per respondent: 26,666.67.[314]

Estimated total annual number of responses for all respondents: 26,666.67.

Estimated annual number of burden hours per respondent: 266.67.[315]

Estimated total annual burden hours for all respondents: 266.67.

3. Third-Party Disclosure Requirements Applicable to a Single Respondent in an FCM Bankruptcy

Regulation § 190.03(c)(1) requires the trustee to use all reasonable efforts to promptly notify any customer whose futures account, foreign futures account, or cleared swaps account includes specifically identifiable property, and that such specifically identifiable property may be liquidated on and after the seventh day after the order for relief if the customer has not instructed the trustee in writing before the deadline specified in the notice to return such property pursuant to the terms for distribution of customer property contained in part 190.

Regulation § 190.03(c)(2) allows the trustee to treat open commodity contracts of public customers identified on the books and records of the debtor has held in an account designated as a hedging account as specifically identifiable property of such customer.[316]

Regulation § 190.03(c)(4) requires the trustee to promptly notify each customer that an order for relief has been entered and instruct each customer to file a proof of customer claim containing the information specified in § 190.03(e).

Regulation § 190.07(b)(5) requires the trustee, in the event that specifically identifiable property has been or will be transferred, to transmit any customer instructions previously received by the trustee with respect to such specifically identifiable property to the transferee of such property.

Based on its experience, the Commission anticipates that an FCM bankruptcy would occur once every three years.[317] The Commission has estimated the burden hours for the third-party disclosure requirements applicable to a single respondent in an FCM bankruptcy as follows:

Estimated number of respondents: 1.

Estimated annual number of responses per respondent: 10,003.32.[318]

Estimated total annual number of responses for all respondents: 10,003.32.

Estimated annual number of burden hours per respondent: 1,336.67.[319]

Estimated total annual burden hours for all respondents: 1,336.67.

4. Reporting Requirements in a Derivatives Clearing Organization (DCO) Bankruptcy

Regulation § 190.12(a)(2) requires a clearing organization that files a petition in bankruptcy to notify the Commission, at or before the time of such filing, of the filing date, the court in which the proceeding will be or has been filed and, as soon as known, the docket number assigned to that proceeding. It further requires a clearing organization against which an involuntary bankruptcy petition is filed to similarly notify the Commission within three hours after the receipt of notice of such filing.

Regulation § 190.12(b)(1) requires the debtor clearing organization to provide to the trustee, no later than three hours following the later of the commencement of a bankruptcy proceeding or the appointment of the trustee, copies of each of the most recent reports that the debtor was required to file with the Commission under § 39.19(c).

Regulation § 190.12(b)(2) requires the debtor clearing organization to provide to the trustee and the Commission, no later than three hours following the commencement of a bankruptcy proceeding, copies of (1) the most recent recovery or wind-down plans of the debtor maintained pursuant to § 39.39(b), and (2) the most recent version of the debtor's default management plan and default rules and procedures maintained pursuant to § 39.16 and, as applicable, § 39.35.

Regulations § 190.12(c)(1) and (2) require the debtor clearing organization

§ 190.03(b)(1), and 0.33 notifications annually pursuant to § 190.03(b)(2), for a total of one notification annually per respondent.

[312] The Commission estimates that (1) the notifications required under § 190.03(b)(1) would take 0.5 hours to make, and (2) the notification required under § 190.03(b)(2) would take 2 hours to make. In terms of burden hours, this amounts to (0.5*0.67 under § 190.03(b)(1)) plus (2*0.33 under § 190.03(b)(2)), or a total of one burden hour annually per respondent.

[313] These estimates express the burdens in terms of those that would be imposed on *one* respondent during the three-year period.

[314] The Commission estimates that (1) under § 190.05(b), a trustee would compute a funded balance for customer accounts 40,000 times; and (2) under § 190.05(d), a trustee would issue 40,000 account statements for customer accounts. Dividing those numbers by three (since the Commission anticipates an FCM bankruptcy occurring once every three years) results in 13,333.33 records annually pursuant to § 190.05(b), and 13,333.33 records annually pursuant to § 190.05(d), for a total of 26,666.67 records annually per respondent.

[315] The Commission estimates that each record required under § 190.05(b) and 190.05(d) would take 0.01 hours to prepare. In terms of burden hours, this amounts to (0.01*13,333.33 under § 190.05(b)) plus (0.01*13,333.33 under § 190.05(d)), or a total of 266.67 burden hours annually per respondent.

[316] The Commission no longer assigns burden hours to the discretionary notice that a trustee may provide to customers in an involuntary FCM bankruptcy proceeding pursuant to § 190.03(c)(3). There have been no involuntary FCM liquidations and none are anticipated. Accordingly, continuing to assign burden hours to this voluntary requirement would inappropriately inflate the burden hours of this information collection.

[317] These estimates express the burdens in terms of those that would be imposed on *one* respondent during the three-year period.

[318] The Commission estimates that a trustee would make the required disclosures under each of § 190.03(c)(1), (2), and (4) 10,000 times per bankruptcy. Dividing those numbers by three (since the Commission anticipates an FCM bankruptcy occurring once every three years) results in 3,333.33 disclosures annually pursuant to each of § 190.03(c)(1), (2), and (4). The Commission further estimates that a trustee would make the required disclosure under § 190.07(b)(5) 10 times per bankruptcy. Dividing this number by three results in 3.33 disclosures annually pursuant to § 190.07(b)(5). This amounts to a total of 10,003.32 disclosures annually per respondent.

[319] The Commission estimates that (1) each disclosure required under § 190.03(c)(1) and (2) and (b) would take 0.1 hours to prepare; (2) each disclosure required under § 190.03(c)(4) would take 0.2 hours to prepare; and (3) each disclosure required under § 190.07(b)(5) would take 1 hour to prepare. In terms of burden hours, this amounts to (0.1*3,333.33 under § 190.03(c)(1)) plus (0.1*3,333.33 under § 190.03(c)(2)) plus (0.2*3,333.33 under § 190.03(c)(4)) plus (1*3.33 under § 190.07(b)(5)), or a total of 1336.66 burden hours annually per respondent.

to make available to the trustee and the Commission, no later than the next business day following commencement of a bankruptcy proceeding, copies of (1) all records maintained by the debtor pursuant to § 39.20(a), and (2) any opinions of counsel or other legal memoranda provided to the debtor in the five years preceding the bankruptcy proceeding relating to the enforceability of the rules and procedures of the debtor in the event of an insolvency proceeding involving the debtor.

Based on its experience, the Commission anticipates that a clearing organization bankruptcy would occur once every fifty years.[320] The Commission has estimated the burden hours for the reporting requirements in a DCO bankruptcy as follows:

Estimated number of respondents: 1.

Estimated annual number of responses per respondent: 2.98.[321]

Estimated total annual number of responses for all respondents: 2.98.

Estimated annual number of burden hours per respondent: 0.61.[322]

Estimated total annual burden hours for all respondents: 0.61.

5. Recordkeeping Requirements in a DCO Bankruptcy

Regulation § 190.14(d) requires the trustee to use reasonable efforts to compute a funded balance for each customer account that contains open commodity contracts or other property as of the close of business each business day subsequent to the order for relief on which liquidation of property within the account has been completed or immediately prior to any distribution of property within the account.

Based on its experience, the Commission anticipates that a clearing organization bankruptcy would occur once every fifty years.[323] The Commission has estimated the burden hours for the recordkeeping requirements in a DCO bankruptcy as follows:

Estimated number of respondents: 1.

Estimated annual number of responses per respondent: 9.[324]

Estimated total annual number of responses for all respondents: 9.

Estimated annual number of burden hours per respondent: 0.9.[325]

Estimated total annual burden hours for all respondents: 0.9.

6. Third-Party Disclosure Requirements Applicable to a Single Respondent in a DCO Bankruptcy

Regulation § 190.14(a) allows the trustee, in their discretion based upon the facts and circumstances of the case, to instruct each customer to file a proof of claim containing such information as is deemed appropriate by the trustee, and seek a court order establishing a bar date for the filing of such proofs of claim.

Based on its experience, the Commission anticipates that a clearing organization bankruptcy would occur once every fifty years.[326] The Commission has estimated the burden hours for the third-party disclosure requirements applicable to a single respondent in a DCO bankruptcy as follows:

Estimated number of respondents: 1.

Estimated annual number of responses per respondent: 0.9.[327]

Estimated total annual number of responses for all respondents: 0.9.

Estimated annual number of burden hours per respondent: 0.18.[328]

Estimated total annual burden hours for all respondents: 0.18.

7. Third-Party Disclosure Requirements Applicable to Multiple Respondents During Business as Usual

As discussed in Section II.B.8 above, the Commission is codifying the provisions proposed as § 190.10(b), (d), and (e) in part 1, along with other regulations that pertain to an FCM's business as usual. Regulation § 1.41, which was proposed as § 190.10(b), requires an FCM to provide an opportunity to each of its customers, upon first opening a futures account or cleared swaps account with such FCM, to designate such account as a hedging account.

Regulation § 1.43, which was proposed as § 190.10(d), prohibits an FCM from accepting a letter of credit as collateral unless such letter of credit may be exercised under certain conditions specified in the regulation.

Regulation § 1.55(p), which was proposed as § 190.10(e), requires an FCM to provide any customer with the disclosure statement set forth in § 1.55(p) prior to accepting property other than cash from or for the account of a customer to margin, guarantee, or secure a commodity contract.

The requirements described above are applicable on a regular basis (*i.e.,* during business as usual) to multiple respondents. The Commission has estimated the burden hours for the third-party disclosure requirements applicable to multiple respondents during business as usual as follows:

Estimated number of respondents: 125.

Estimated annual number of responses per respondent: 3,000.[329]

[320] No U.S. clearing organization has ever been the subject of a bankruptcy proceeding, and none has come anywhere near insolvency. While there have been less than a handful of central counterparties worldwide that became functionally insolvent during the twentieth century, none of those were subject to modern resiliency requirements. Accordingly, the Commission believes that an estimate of one DCO bankruptcy every fifty years is an appropriate estimate. These burden estimates express the burdens in terms of those that would be imposed on *one* respondent during the fifty-year period.

[321] The Commission estimates that (1) under § 190.12(a)(2), a clearing organization would make two notifications per bankruptcy; (2) under § 190.12(b)(1), a clearing organization would provide 40 reports to the trustee; (3) under § 190.12(b)(2), a clearing organization would provide 5 reports to the trustee and the Commission; (4) under § 190.12(c)(1), a clearing organization would provide 100 records to the trustee and the Commission; and (5) under § 190.12(c)(2), a clearing organization would provide 2 records to the trustee and the Commission. Dividing those numbers by 50 (since the Commission anticipates a clearing organization bankruptcy occurring once every 50 years) results in (1) 0.04 reports annually pursuant to § 190.12(a)(2); (2) 0.8 reports annually pursuant to § 190.12(b)(1); (3) 0.1 reports annually pursuant to § 190.12(b)(2); (4) 2 reports annually pursuant to § 190.12(c)(1); and (5) 0.04 reports annually pursuant to § 190.12(c)(2), for a total of 2.98 reports annually per respondent.

[322] The Commission estimates that (1) each notification required under § 190.12(a)(2) and (d)(2) would take 0.5 hours to make; (2) gathering the reports required under § 190.12(b)(1) would take 0.2 hours; (3) gathering the reports required under § 190.12(b)(2) would take 0.2 hours; (4) gathering the reports required under § 190.12(c)(1) would take 0.2 hours; and (5) gathering the reports required under § 190.12(c)(2) would take 0.2 hours. In terms of burden hours, this amounts to (0.5*0.04 under § 190.12(a)(2)) plus (0.2*0.8 under § 190.12(b)(1)) plus (0.2*0.1 under § 190.12(b)(2)) plus (0.2*2 under § 190.12(c)(1)) plus (0.2*0.04 under § 190.12(c)(2)), or a total of 0.61 burden hours annually per respondent.

[323] These estimates express the burdens in terms of those that would be imposed on *one* respondent during the fifty-year period.

[324] The Commission estimates that, under § 190.14(d), a clearing organization would compute a funded balance for customer accounts 450 times during a bankruptcy. This number is based on an average of 45 clearing members, each with two accounts (house and customer). Dividing that number by 50 (since the Commission anticipates a clearing organization bankruptcy occurring once every 50 years) results in 9 records annually per respondent.

[325] The Commission estimates that computing the funded balance of customer accounts pursuant to § 190.14(d) would take 0.1 hours per computation. In terms of burden hours, this amounts to (0.1*9), or 0.9 burden hours annually per respondent.

[326] These estimates express the burdens in terms of those that would be imposed on *one* respondent during the fifty-year period.

[327] The Commission estimates that, under § 190.14(a), a trustee would make the disclosure 45 times during a bankruptcy. This number is based on an average of 45 clearing members. Dividing that number by 50 (since the Commission anticipates a clearing organization bankruptcy occurring once every 50 years) results in 0.9 records annually per respondent.

[328] The Commission estimates that instructing customers to file a proof of claim pursuant to § 190.14(a) would take 0.2 hours. In terms of burden hours, this amounts to (0.2*0.9), or 0.18 burden hours annually per respondent.

[329] The Commission estimates that under §§ 1.41, 1.43, and 1.55(p), an FCM would make the required

Estimated total annual number of responses for all respondents: 375,000.

Estimated annual number of burden hours per respondent: 60.[330]

Estimated total annual burden hours for all respondents: 7,500.

List of Subjects

17 CFR Part 1

Brokers, Commodity futures, Consumer protection, Reporting and recordkeeping requirements.

17 CFR Part 4

Brokers, Commodity futures, Consumer protection, Reporting and recordkeeping requirements.

17 CFR Part 41

Brokers, Reporting and recordkeeping requirements, Securities.

17 CFR Part 190

Bankruptcy, Brokers, Reporting and recordkeeping requirements.

For the reasons stated in the preamble, the Commodity Futures Trading Commission amends 17 CFR chapter I as follows:

PART 1—GENERAL REGULATIONS UNDER THE COMMODITY EXCHANGE ACT

■ 1. The authority citation for part 1 continues to read as follows:

Authority: 7 U.S.C. 1a, 2, 5, 6, 6a, 6b, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6k, 6l, 6m, 6n, 6o, 6p, 6r, 6s, 7, 7a–1, 7a–2, 7b, 7b–3, 8, 9, 10a, 12, 12a, 12c, 13a, 13a–1, 16, 16a, 19, 21, 23, and 24 (2012).

■ 2. In § 1.25, revise paragraph (a)(2)(ii)(B) to read as follows:

§ 1.25 Investment of customer funds.

(a) * * *

(2) * * *

(ii) * * *

(B) Securities subject to such repurchase agreements must not be ''specifically identifiable property'' as defined in § 190.01 of this chapter.

* * * * *

■ 3. Add § 1.41 to read as follows:

§ 1.41 Designation of hedging accounts.

(a) A futures commission merchant must provide an opportunity to each customer, when it first opens a futures account, foreign futures account or cleared swaps account with such futures commission merchant, to designate such account as a hedging account. The futures commission merchant must indicate prominently in the accounting records in which it maintains open trade balances whether, for each customer account, the account is designated as a hedging account.

(b) A futures commission merchant may permit the customer to open an account as a hedging account only if it obtains the customer's written representation that the customer's trading of futures or options on futures, foreign futures or options on foreign futures, or cleared swaps (as applicable) in the account constitutes hedging as such term may be defined under any relevant Commission regulation or rule of any clearing organization, designated contract market, swap execution facility or foreign board of trade.

(c) The requirements set forth in paragraphs (a) and (b) of this section do not apply to a futures commission merchant with respect to any commodity contract account that the futures commission merchant opened prior to May 13, 2021. The futures commission merchant may continue to designate as a hedging account any account with respect to which the futures commission merchant received written hedging instructions from the customer in accordance with former § 190.06(d) of this chapter.

(d) A futures commission merchant may designate an existing futures account, foreign futures account or cleared swaps account of a particular customer as a hedging account, provided that it has obtained the representation set out in paragraph (b) of this section from such customer.

■ 4. Add § 1.42 to read as follows:

§ 1.42 Delivery accounts.

In connection with the making or taking of delivery of a commodity under a commodity contract whose terms require settlement via physical delivery, if a futures commission merchant facilitates or effects the transfer of the physical delivery property and payment therefor on behalf of the customer, and does so outside the futures account, foreign futures account or cleared swaps account in which the commodity contract was held, the futures commission merchant must do so in a delivery account, *provided, however,* that when the commodity subject to delivery is a security, a futures commission merchant may, consistent with any applicable regulatory requirements, do so in a securities account.

■ 5. Add § 1.43 to read as follows:

§ 1.43 Letters of credit as collateral.

A futures commission merchant shall not accept a letter of credit as collateral unless such letter of credit may be exercised, through its stated date of expiry, under the following conditions, regardless of whether the customer posting that letter of credit is in default in any obligation:

(a) In the event that an order for relief under chapter 7 of the Bankruptcy Code or a protective decree pursuant to section 5(b)(1) of SIPA is entered with respect to the futures commission merchant, or if the FDIC is appointed as receiver for the futures commission merchant pursuant to 12 U.S.C. 5382(a), the trustee for that futures commission merchant (or, as applicable, FDIC) may draw upon such letter of credit, in full or in part, in accordance with § 190.04(d)(3) of this chapter.

(b) If the letter of credit is passed through to a clearing organization, then in the event that an order for relief under chapter 7 of the Bankruptcy Code is entered with respect to the clearing organization, or if the FDIC is appointed as receiver for the clearing organization pursuant to 12 U.S.C. 5382(a), the trustee for that clearing organization (or, as applicable, FDIC) may draw upon such letter of credit, in full or in part, in accordance with § 190.04(d)(3) of this chapter.

(c) A futures commission merchant shall not accept a letter of credit from a customer as collateral if it has any agreement with the customer that is inconsistent with this section.

■ 6. In § 1.55:

■ a. Revise paragraphs (d) and (f);

■ b. Remove the parenthetical control number sentence and parenthetical authority citation following paragraph (h);

■ c. Remove the paragraph (k) heading; and

■ d. Add paragraph (p).

The revision and addition read as follows:

§ 1.55 Public disclosures by futures commission merchants.

* * * * *

(d) Any futures commission merchant, or (in the case of an introduced account) any introducing broker, may open a commodity futures account for a customer without obtaining the separate acknowledgments of disclosure and elections required by this section and by §§ 1.33(g) and 33.7 of this chapter, provided that:

(1) Prior to the opening of such account, the futures commission merchant or introducing broker obtains an acknowledgement from the customer, which may consist of a single signature

disclosures 1,000 times per year. This amounts to a total of 3,000 responses annually per respondent.

[330] The Commission estimates that each disclosure required under §§ 1.41, 1.43, and 1.55(p) would take 0.02 hours to make. In terms of burden hours, this amounts to (0.02*1,000 under § 1.41) plus (0.02*1,000 under § 1.43 plus (0.02*1,000 under § 1.55(p)), or 60 burden hours annually per respondent.

at the end of the futures commission merchant's or introducing broker's customer account agreement, or on a separate page, of the disclosure statements, consents, and elections specified in this section and § 1.33(g), and in §§ 33.7, 155.3(b)(2), and 155.4(b)(2) of this chapter, and which may include authorization for the transfer of funds from a segregated customer account to another account of such customer, as listed directly above the signature line, provided the customer has acknowledged by check or other indication next to a description of each specified disclosure statement, consent, or election that the customer has received and understood such disclosure statement or made such consent or election; and

(2) The acknowledgment referred to in paragraph (d)(1) of this section is accompanied by and executed contemporaneously with delivery of the disclosures and elective provisions required by this section and § 1.33(g), and by § 33.7 of this chapter.

* * * * *

(f) A futures commission merchant or, in the case of an introduced account, an introducing broker, may open a commodity futures account for an ''institutional customer'' as defined in § 1.3 without furnishing such institutional customer the disclosure statements or obtaining the acknowledgments required under paragraph (a) of this section, or §§ 1.33(g), 1.55(p), and 1.65(a)(3), and §§ 30.6(a), 33.7(a), 155.3(b)(2), and 155.4(b)(2) of this chapter.

* * * * *

(p)(1) Except as provided in § 1.65, no commodity broker (other than a clearing organization) may accept property other than cash from or for the account of a customer, other than a customer specified in paragraph (f) of this section, to margin, guarantee, or secure a commodity contract unless the commodity broker first furnishes the customer with the disclosure statement set forth in paragraph (p)(2) of this section in boldface print in at least 10 point type which may be provided as either a separate, written document or incorporated into the customer agreement, or with another statement approved under paragraph (c) of this section and set forth in appendix A to this section which the Commission finds satisfies the requirement of this paragraph (p)(1).

(2) The disclosure statement required by paragraph (p)(1) of this section is as follows:

THIS STATEMENT IS FURNISHED TO YOU BECAUSE REGULATION 1.55(p) OF THE COMMODITY FUTURES TRADING COMMISSION REQUIRES IT FOR REASONS OF FAIR NOTICE UNRELATED TO THIS COMPANY'S CURRENT FINANCIAL CONDITION.

1. YOU SHOULD KNOW THAT IN THE UNLIKELY EVENT OF THIS COMPANY'S BANKRUPTCY, PROPERTY, INCLUDING PROPERTY SPECIFICALLY TRACEABLE TO YOU, WILL BE RETURNED, TRANSFERRED OR DISTRIBUTED TO YOU, OR ON YOUR BEHALF, ONLY TO THE EXTENT OF YOUR PRO RATA SHARE OF ALL PROPERTY AVAILABLE FOR DISTRIBUTION TO CUSTOMERS.

2. THE COMMISSION'S REGULATIONS CONCERNING BANKRUPTCIES OF COMMODITY BROKERS CAN BE FOUND AT 17 CODE OF FEDERAL REGULATIONS PART 190.

(3) The statement contained in paragraph (p)(2) of this section need be furnished only once to each customer to whom it is required to be furnished by this section.

■ 7. In § 1.65, revise paragraphs (a)(3) introductory text and (a)(3)(iii) to read as follows:

§ 1.65 Notice of bulk transfers and disclosure obligations to customers.

(a) * * *

(3) Where customer accounts are transferred to a futures commission merchant or introducing broker, other than at the customer's request, the transferee introducing broker or futures commission merchant must provide each customer whose account is transferred with the risk disclosure statements and acknowledgments required by § 1.55 (domestic futures and foreign futures and options trading) and § 33.7 of this chapter (domestic exchange-traded commodity options) and receive the required acknowledgments within sixty days of the transfer of accounts. This paragraph (a)(3) shall not apply:

* * * * *

(iii) If the transfer of accounts is made from one introducing broker to another introducing broker guaranteed by the same futures commission merchant pursuant to a guarantee agreement in accordance with the requirements of § 1.10(j) and such futures commission merchant maintains the relevant acknowledgments required by §§ 1.55(a)(1)(ii) and 33.7(a)(1)(ii) of this chapter and can establish compliance with § 1.55(p).

* * * * *

PART 4—COMMODITY POOL OPERATORS AND COMMODITY TRADING ADVISORS

■ 8. The authority citation for part 4 continues to read as follows:

Authority: 7 U.S.C. 1a, 2, 6(c), 6b, 6c, 6l, 6m, 6n, 6o, 12a, and 23.

■ 9. In § 4.5, revise paragraph (c)(2)(iii)(A) to read as follows:

§ 4.5 Exclusion for certain otherwise regulated persons from the definition of the term ''commodity pool operator.''

* * * * *

(c) * * *

(2) * * *

(iii) * * *

(A) Will use commodity futures or commodity options contracts, or swaps solely for bona fide hedging purposes within the meaning and intent of the definition of bona fide hedging transactions and positions for excluded commodities in §§ 1.3 and 151.5 of this chapter; Provided however, That, in addition, with respect to positions in commodity futures or commodity options contracts, or swaps which do not come within the meaning and intent of the definition of bona fide hedging transactions and positions for excluded commodities in §§ 1.3 and 151.5 of this chapter, a qualifying entity may represent that the aggregate initial margin and premiums required to establish such positions will not exceed five percent of the liquidation value of the qualifying entity's portfolio, after taking into account unrealized profits and unrealized losses on any such contracts it has entered into; and, Provided further, That in the case of an option that is in-the-money at the time of the purchase, the in-the-money amount as defined in § 190.01of this chapter may be excluded in computing such five percent; or

* * * * *

■ 10. In § 4.12, revise the section heading and paragraph (b)(1)(i)(C) to read as follows:

§ 4.12 Exemption from provisions of this part.

* * * * *

(b) * * *

(1) * * *

(i) * * *

(C) Will not enter into commodity interest transactions for which the aggregate initial margin and premiums, and required minimum security deposit for retail forex transactions (as defined in § 5.1(m) of this chapter) exceed 10 percent of the fair market value of the pool's assets, after taking into account unrealized profits and unrealized losses on any such contracts it has entered into; *Provided, however,* That in the case of an option that is in-the-money at the time of purchase, the in-the-money amount as defined in § 190.01 of this chapter may be excluded in computing such 10 percent; and

* * * * *

■ 11. In § 4.13, revise paragraph (a)(3)(ii)(A) to read as follows:

§ 4.13 Exemption from registration as a commodity pool operator.

* * * * *

(a) * * *

(3) * * *

(ii) * * *

(A) The aggregate initial margin, premiums, and required minimum security deposit for retail forex transactions (as defined in § 5.1(m) of this chapter) required to establish such positions, determined at the time the most recent position was established, will not exceed 5 percent of the liquidation value of the pool's portfolio, after taking into account unrealized profits and unrealized losses on any such positions it has entered into; *Provided,* That in the case of an option that is in-the-money at the time of purchase, the in-the-money amount as defined in § 190.01 of this chapter may be excluded in computing such 5 percent; or

* * * * *

PART 41—SECURITY FUTURES PRODUCTS

■ 12. The authority citation for part 41 continues to read as follows:

Authority: Sections 206, 251 and 252, Pub. L. 106–554, 114 Stat. 2763, 7 U.S.C. 1a, 2, 6f, 6j, 7a–2, 12a; 15 U.S.C. 78g(c)(2).

■ 13. In § 41.41, revise paragraph (d) to read as follows:

§ 41.41 Security futures products accounts.

* * * * *

(d) *Recordkeeping requirements.* The Commission's recordkeeping rules set forth in §§ 1.31, 1.32, 1.35, 1.36, 1.37, 4.23, 4.33, and 18.05 of this chapter shall apply to security futures product transactions and positions in a futures account (as that term is defined in § 1.3 of this chapter). The rules in the preceding sentence shall not apply to security futures product transactions and positions in a securities account (as that term is defined in § 1.3 of this chapter); provided, that the SEC's recordkeeping rules apply to those transactions and positions.

* * * * *

■ 14. Revise part 190 to read as follows:

PART 190—BANKRUPTCY RULES

Subpart A—General Provisions

Sec.

Subpart B—Futures Commission Merchant as Debtor

Subpart C—Clearing Organization as Debtor

Authority: 7 U.S.C. 1a, 2, 6c, 6d, 6g, 7a–1, 12, 12a, 19, and 24; 11 U.S.C. 362, 546, 548, 556, and 761–767, unless otherwise noted.

Subpart A—General Provisions

§ 190.00 Statutory authority, organization, core concepts, scope, and construction.

(a) *Statutory authority.* The Commission has adopted the regulations in this part pursuant to its authority under sections 8a(5) and 20 of the Act. Section 8a(5) provides general rulemaking authority to effectuate the provisions and accomplish the purposes of the Act. Section 20 provides that the Commission may, notwithstanding title 11 of the United States Code, adopt certain rules or regulations governing a proceeding involving a commodity broker that is a debtor under subchapter IV of chapter 7 of the Bankruptcy Code. Specifically, the Commission is authorized to adopt rules or regulations specifying:

(1) That certain cash, securities, or other property, or commodity contracts, are to be included in or excluded from customer property or member property;

(2) That certain cash, securities, or other property, or commodity contracts, are to be specifically identifiable to a particular customer in a particular capacity;

(3) The method by which the business of the commodity broker is to be conducted or liquidated after the date of the filing of the petition under chapter 7 of the Bankruptcy Code, including the payment and allocation of margin with respect to commodity contracts not specifically identifiable to a particular customer pending their orderly liquidation;

(4) Any persons to which customer property and commodity contracts may be transferred under section 766 of the Bankruptcy Code; and

(5) How a customer's net equity is to be determined.

(b) *Organization.* This part is organized into three subparts. This subpart contains general provisions applicable in all cases. Subpart B of this part contains provisions that apply when the debtor is a futures commission merchant (as that term is defined in the Act or Commission regulations). This includes acting as a foreign futures commission merchant, as defined in section 761(12) of the Bankruptcy Code, but excludes a person that is ''notice-registered'' as a futures commission merchant pursuant to section 4f(a)(2) of the Act. Subpart C contains provisions that apply when the debtor is registered as a derivatives clearing organization under the Act.

(c) *Core concepts.* The regulations in this part reflect several core concepts. The descriptions of core concepts in paragraphs (c)(1) through (6) of this section are subject to the further specific requirements set forth in this part, and the specific requirements in this part should be interpreted and applied consistently with these core concepts.

(1) *Commodity brokers.* Subchapter IV of chapter 7 of the Bankruptcy Code applies to a debtor that is a commodity broker, against which a customer holds a ''net equity'' claim relating to a commodity contract. This part is limited to a commodity broker that is:

(i) A futures commission merchant; or

(ii) A derivatives clearing organization registered under the Act and § 39.3 of this chapter.

(2) *Account classes.* The Act and Commission regulations in parts 1, 22, and 30 of this chapter provide differing treatment and protections for different types of cleared commodity contracts. This part establishes three account classes that correspond to the different types of accounts that futures

commission merchants and clearing organizations are required to maintain under the regulations in the preceding sentence, specifically, the futures account class (including options on futures), the foreign futures account class (including options on foreign futures), and the cleared swaps account class (including cleared options other than options on futures or foreign futures). This part also establishes a fourth account class, the delivery account class (which may be further subdivided as provided in this part), for property held in an account designated within the books and records of the debtor as a delivery account, for effecting delivery under commodity contracts whose terms require settlement via delivery when the commodity contract is held to expiration or, in the case of a cleared option, is exercised.

(3) *Public customers and non-public customers; Commission segregation requirements; member property*—(i) *Public customers and non-public customers.* This part prescribes separate treatment of ''public customers'' and ''non-public customers'' (as these terms are defined in § 190.01) within each account class in the event of a proceeding under this part in which the debtor is a futures commission merchant. Public customers of a debtor futures commission merchant are entitled to a priority in the distribution of cash, securities, or other customer property over non-public customers, and both have priority over all other claimants (except for claims relating to the administration of customer property) pursuant to section 766(h) of the Bankruptcy Code.

(A) The cash, securities, or other property held on behalf of the public customers of a futures commission merchant in the futures, foreign futures, or cleared swaps account classes are subject to special segregation requirements imposed under parts 1, 22, and 30 of this chapter for each account class. Although such segregation requirements generally are not applicable to cash, securities, or other property received from or reflected in the futures, foreign futures, or cleared swaps accounts of non-public customers of a futures commission merchant, such transactions and property are customer property within the scope of this part.

(B) While parts 1, 22, and 30 of this chapter do not impose special segregation requirements with respect to treatment of cash, securities, or other property of public customers carried in a delivery account, such property does constitute customer property. Thus, the distinction between public and non-public customers is, given the priority for public customers in section 766(h) of the Bankruptcy Code, relevant for the purpose of making distributions to delivery account class customers pursuant to this part.

(C) Where a provision in this part affords the trustee discretion, that discretion should be exercised in a manner that the trustee determines will best achieve the overarching goal of protecting public customers as a class by enhancing recoveries for, and mitigating disruptions to, public customers as a class. In seeking to achieve that overarching goal, the trustee has discretion to balance those two sub-goals when they are in tension. Where the trustee is directed to exercise ''reasonable efforts'' to meet a standard, those efforts should only be less than ''best efforts'' to the extent that the trustee determines that such an approach would support the foregoing goals.

(ii) *Clearing organization bankruptcies: Member property and customer property other than member property.* For a clearing organization, ''customer property'' is divided into ''member property'' and ''customer property other than member property.'' The term member property is used to identify the cash, securities, or property available to pay the net equity claims of clearing members based on their house account at the clearing organization. Thus, in the event of a proceeding under this part in which the debtor is a clearing organization, the classification of customers as public customers or non-public customers also is relevant, in that each member of the clearing organization will have separate claims against the clearing organization (by account class) with respect to:

(A) Commodity contract transactions cleared for its own account or on behalf of any of its non-public customers (which are cleared in a ''house account'' at the clearing organization); and

(B) Commodity contract transactions cleared on behalf of any public customers of the clearing member (which are cleared in accounts at the clearing organization that is separate and distinct from house accounts).

(iii) *Preferential assignment among customer classes and account classes for clearing organization bankruptcies.* Section 190.18 is designed to support the interests of public customers of members of a debtor that is a clearing organization.

(A) Certain customer property is preferentially assigned to ''customer property other than member property'' instead of ''member property'' to the extent that there is a shortfall in funded balances for members' public customer claims. Moreover, to the extent that there are excess funded balances for members' claims in any customer class/account class combination, that excess is also preferentially assigned to ''customer property other than member property'' to the extent of any shortfall in funded balances for members' public customer claims.

(B) Where property is assigned to a particular customer class with more than one account class, it is assigned to the account class for which the funded balance percentage is the lowest until there are two account classes with equal funded balance percentages, then to both such account classes, keeping the funded balance percentage the same, and so forth following the analogous approach if the debtor has more than two account classes within the relevant customer class.

(4) *Porting of public customer commodity contract positions.* In a proceeding in which the debtor is a futures commission merchant, this part sets out a policy preference for transferring to another futures commission merchant, or ''porting,'' open commodity contract positions of the debtor's public customers along with all or a portion of such customers' account equity. Porting mitigates risks to both the customers of the debtor futures commission merchant and to the markets. To facilitate porting, this part addresses the manner in which the debtor's business is to be conducted on and after the filing date, with specific provisions addressing the collection and payment of margin for open commodity contract positions prior to porting.

(5) *Pro rata distribution.* (i) The commodity broker provisions of the Bankruptcy Code, subchapter IV of chapter 7, in particular section 766(h), have long revolved around the principle of pro rata distribution. If there is a shortfall in the cash, securities or other property in a particular account class needed to satisfy the net equity claims of public customers in that account class, the customer property in that account class will be distributed pro rata to those public customers (subject to appendix B of this part). Any customer property not attributable to a specific account class, or that exceeds the amount needed to pay allowed customer net equity claims in a particular account class, will be distributed to public customers in other account classes so long as there is a shortfall in those other classes. Non-public customers will not receive any distribution of customer property so long as there is any shortfall, in any account class, of customer property

needed to satisfy public customer net equity claims.

(ii) The pro rata distribution principle means that, if there is a shortfall of customer property in an account class, all customers within that account class will suffer the same proportional loss relative to their allowed net equity claims. The principle in this paragraph (c)(5)(ii) applies to all customers, including those who post as collateral specifically identifiable property or letters of credit. The pro rata distribution principle is subject to the special distribution provisions set forth in framework 1 in appendix B of this part for cross-margin accounts and framework 2 in appendix B of this part for funds held outside of the U.S. or held in non-U.S. currency.

(6) *Deliveries.* (i) Commodity contracts may have terms that require a customer owning the contract:

(A) To make or take delivery of the underlying commodity if the customer holds the contract to a delivery position; or

(B) In the case of an option on a commodity:

(*1*) To make delivery upon exercise (as the buyer of a put option or seller of a call option); or

(*2*) To take delivery upon exercise (as seller of a put option or buyer of a call option).

(ii) Depending upon the circumstances and relevant market, delivery may be effected via a delivery account, a futures account, a foreign futures account or a cleared swaps account, or, when the commodity subject to delivery is a security, in a securities account (in which case property associated with the delivery held in a securities account is not part of any customer account class for purposes of this part).

(iii) Although commodity contracts with delivery obligations are typically offset before reaching the delivery stage (*i.e.,* prior to triggering bilateral delivery obligations), when delivery obligations do arise, a delivery default could have a disruptive effect on the cash market for the commodity and adversely impact the parties to the transaction. This part therefore sets out special provisions to address open commodity contracts that are settled by delivery, when those positions are nearing or have entered into a delivery position at the time of or after the filing date. The delivery provisions in this part are intended to allow deliveries to be completed in accordance with the rules and established practices for the relevant commodity contract market or clearing organization, as applicable and to the extent permitted under this part.

(iv) In a proceeding in which the debtor is a futures commission merchant, the delivery provisions in this part reflect policy preferences to:

(A) Liquidate commodity contracts that settle via delivery before they move into a delivery position; and

(B) When such contracts are in a delivery position, to allow delivery to occur, where practicable, outside administration of the debtor's estate.

(v) The delivery provisions in this part apply to any commodity that is subject to delivery under a commodity contract, as the term commodity is defined in section of 1a(9) of the Act, whether the commodity itself is tangible or intangible, including agricultural commodities as defined in § 1.3 of this chapter, other non-financial commodities (such as metals or energy commodities) covered by the definition of exempt commodity in section 1a(20) of the Act, and commodities that are financial in nature (such as foreign currencies) covered by the definition of excluded commodity in section 1a(19) of the Act. The delivery provisions also apply to virtual currencies that are subject to delivery under a commodity contract.

(d) *Scope*—(1) *Proceedings*—(i) *Certain commodity broker proceedings under subchapter IV of chapter 7 of the Bankruptcy Code.* (A) Section 101(6) of the Bankruptcy Code recognizes ''futures commission merchants'' and ''foreign futures commission merchants,'' as those terms are defined in section 761(12) of the Bankruptcy Code, as separate categories of commodity broker. The definition of commodity broker in § 190.01, as it applies to a commodity broker that is a futures commission merchant under the Act, also covers foreign futures commission merchants because a foreign futures commission merchant is required to register as a futures commission merchant under the Act.

(B) Section 101(6) of the Bankruptcy Code recognizes ''commodity options dealers,'' and ''leverage transaction merchants'' as defined in sections 761(6) and (13) of the Bankruptcy Code, as separate categories of commodity brokers. There are no commodity options dealers or leverage transaction merchants as of December 8, 2020.

Note 1 to paragraph (b)(1)(i)(B). The Commission intends to adopt rules with respect to commodity options dealers or leverage transaction merchants, respectively, at such time as an entity registers as such.

(ii) *Futures commission merchants subject to a SIPA proceeding.* Pursuant to section 7(b) of SIPA, 15 U.S.C. 78fff–1(b), the trustee in a SIPA proceeding, where the debtor also is a commodity broker, has the same duties as a trustee in a proceeding under subchapter IV of chapter 7 of the Bankruptcy Code, to the extent consistent with the provisions of SIPA or as otherwise ordered by the court. This part therefore also applies to a proceeding commenced under SIPA with respect to a debtor that is registered as a broker or dealer under section 15 of the Securities Exchange Act of 1934 when the debtor also is a futures commission merchant.

(iii) *Commodity brokers subject to an FDIC proceeding.* Section 5390(m)(1)(B) of title 12 of the United States Code provides that the FDIC must apply the provisions of subchapter IV of chapter 7 of the Bankruptcy Code in respect of the distribution of customer property and member property in connection with the liquidation of a covered financial company or a bridge financial company (as those terms are defined in section 5381(a) of title 12) that is a commodity broker as if such person were a debtor for purposes of subchapter IV, except as specifically provided in section 5390 of title 12. This part therefore shall serve as guidance as to such distribution of property in a proceeding in which the FDIC is acting as a receiver pursuant to title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act with respect to a covered financial company or bridge financial company that is a commodity broker whose liquidation otherwise would be administered by a trustee under subchapter IV of chapter 7 of the Bankruptcy Code.

(2) *Account class and implied trust limitations.* (i) The trustee may not recognize any account class that is not one of the account classes enumerated in § 190.01.

(ii) No property that would otherwise be included in customer property, as defined in § 190.01, shall be excluded from customer property because such property is considered to be held in a constructive, resulting, or other trust that is implied in equity.

(3) *Commodity contract exclusions.* For purposes of this part, the following are excluded from the term ''commodity contract'':

(i) Options on commodities (including swaps subject to regulation under part 32 of this chapter) that are not centrally cleared by a clearing organization or foreign clearing organization.

(ii) Transactions, contracts or agreements that are classified as ''forward contracts'' under the Act pursuant to the exclusion from the term ''future delivery'' set out in section 1a(27) of the Act or the exclusion from the definition of a ''swap'' under section

1a(47)(B)(ii) of the Act, in each case that are not centrally cleared by a clearing organization or foreign clearing organization.

(iii) Security futures products as defined in section 1a(45) of the Act when such products are held in a securities account.

(iv) Any off-exchange retail foreign currency transaction, contract or agreement described in sections 2(c)(2)(B) or (C) of the Act.

(v) Any security-based swap or other security (as defined in section 3 of the Exchange Act), but a security futures product or a mixed swap (as defined in 1a(47)(D) of the Act) that is, in either case, carried in an account for which there is a corresponding account class under this part is not so excluded.

(vi) Any off-exchange retail commodity transaction, contract or agreement described in section 2(c)(2)(D) of the Act, unless such transaction, contract or agreement is traded on or subject to the rules of a designated contract market or foreign board of trade as, or as if, such transaction, contract, or agreement is a futures contract.

(e) *Construction.* (1) A reference in this part to a specific section of a Federal statute or specific regulation refers to such section or regulation as the same may be amended or superseded.

(2) Where they differ, the definitions set forth in § 190.01 shall be used instead of defined terms set forth in section 761 of the Bankruptcy Code. In many cases, these definitions are based on definitions in parts 1, 22, and 30 of this chapter. Notwithstanding the use of different defined terms, the regulations in this part are intended to be consistent with the provisions and objectives of subchapter IV of chapter 7 of the Bankruptcy Code.

(3) In the context of portfolio margining and cross margining programs, commodity contracts and associated collateral will be treated as part of the account class in which, consistent with part 1, 22, 30, or 39 of this chapter, or Commission Order, they are held.

(i) Thus, as noted in paragraph (2) of the definition of *account class* in § 190.01, where open commodity contracts (and associated collateral) that would be attributable to one account class are, instead, commingled with the commodity contracts (and associated collateral) in a second account class (the ''home field''), then the trustee must treat all such commodity contracts and collateral as part of, and consistent with the regulations applicable to, the second account class.

(ii) The concept in paragraph (e)(3)(i) of this section, that the rules of the ''home field'' will apply, also pertains to securities positions that are, pursuant to an approved cross margining program, held in a commodities account class (in which case the rules of that commodities account class will apply) and to commodities positions that are, pursuant to an approved cross-margining program, held in a securities account (in which case, the rules of the securities account will apply, consistent with section 16(2)(b)(ii) of SIPA, 15 U.S.C. 78lll(2)(b)(ii)).

§ 190.01 Definitions.

For purposes of this part:

Account class:

(1) Means one or more of each of the following types of accounts maintained by a futures commission merchant or clearing organization (as applicable), each type of which must be recognized as a separate account class by the trustee:

(i) *Futures account* means:

(A) With respect to public customers, the same definition as set forth in § 1.3 of this chapter.

(B) With respect to non-public customers:

(*1*) With respect to a futures commission merchant, an account maintained on the books and records of the futures commission merchant for the purpose of accounting for a person's transactions in futures or options on futures contracts executed on or subject to the rules of a designated contract market registered under the Act (and related cash, securities, or other property); and

(*2*) With respect to a clearing organization, an account maintained on the books and records of the clearing organization for the purpose of accounting for transactions in futures or options on futures contracts cleared or settled by the clearing organization for a member or a member's non-public customers (and related cash, securities, or other property).

(ii) *Foreign futures account* means:

(A) With respect to public customers:

(*1*) With respect to a futures commission merchant, a 30.7 account, as such term is defined in § 30.1(g) of this chapter; and

(*2*) With respect to a clearing organization, an account maintained on the books and records of the clearing organization for the purpose of accounting for transactions in futures or options on futures contracts executed on or subject to the rules of a foreign board of trade, cleared or settled by the clearing organization for a member that is a futures commission merchant (and related cash, securities or other property), on behalf of that member's 30.7 customers (as that latter term is defined in § 30.1(f) of this chapter).

(B) With respect to non-public customers:

(*1*) With respect to a futures commission merchant, an account maintained on the books and records of the futures commission merchant for the purpose of accounting for a person's transactions in futures or options on futures contracts executed on or subject to the rules of a foreign board of trade (and related cash, securities, or other property); and

(*2*) With respect to a clearing organization, an account maintained on the books and records of the clearing organization for the purpose of accounting for transactions in futures or options on futures contracts executed on or subject to the rules of a foreign board of trade, cleared or settled by the clearing organization for a member or a member's non-public customers (and related cash, securities, or other property).

(iii) *Cleared swaps account* means:

(A) With respect to public customers, a cleared swaps customer account, as such term is defined in § 22.1 of this chapter.

(B) With respect to non-public customers:

(*1*) With respect to a futures commission merchant, an account maintained on the books and records of the futures commission merchant for the purpose of accounting for a person's transactions in cleared swaps (as defined in § 22.1 of this chapter) (and related cash, securities, or other property); and

(*2*) With respect to a clearing organization, an account maintained on the books and records of the clearing organization for the purpose of accounting for transactions in cleared swaps (as defined in § 22.1 of this chapter) (or in other contracts permitted to be cleared in the account) cleared or settled by the clearing organization for a member or a member's non-public customers (including any property related thereto).

(iv)(A) *Delivery account* means (for both public and non-public customers, considered separately):

(*1*) An account maintained on the books and records of a futures commission merchant for the purpose of accounting for the making or taking of delivery under commodity contracts whose terms require settlement by delivery of a commodity, and which is designated as a delivery account on the books and records of the futures commission merchant; and

(*2*) An account maintained on the books and records of a clearing organization for a clearing member (or a customer of a clearing member) for the purpose of accounting for the making or taking of delivery under commodity contracts whose terms require settlement by delivery of a commodity, as well as any account in which the clearing organization holds physical delivery property represented by electronic title documents or otherwise existing in an electronic (dematerialized) form in its capacity as a central depository, in each case where the account is designated as a delivery account on the books and the records of the clearing organization.

(B) The delivery account class is further divided into a ''physical delivery account class'' and a ''cash delivery account class,'' as provided in § 190.06(b), each of which shall be recognized as a separate class of account by the trustee.

(2)(i) If open commodity contracts that would otherwise be attributable to one account class (and any property margining, guaranteeing, securing or accruing in respect of such commodity contracts) are, pursuant to a Commission rule, regulation, or order, or a clearing organization rule approved in accordance with § 39.15(b)(2) of this chapter, held separately from other commodity contracts and property in that account class and are commingled with the commodity contracts and property of another account class, then the trustee must treat the former commodity contracts (and any property margining, guaranteeing, securing, or accruing in respect of such commodity contracts), for purposes of this part, as being held in an account of the latter account class.

(ii) The principle in paragraph (2)(i) of this definition will be applied to securities positions and associated collateral held in a commodity account class pursuant to a cross margining program approved by the Commission (and thus treated as part of that commodity account class) and to commodity positions and associated collateral held in a securities account pursuant to a cross margining program approved by the Commission (and thus treated as part of the securities account).

(3) For the purpose of this definition, a commodity broker is considered to maintain an account for another person by establishing internal books and records in which it records the person's commodity contracts and cash, securities or other property received from or on behalf of such person or accruing to the credit of such person's account, and related activity (such as liquidation of commodity contract positions or adjustments to reflect mark-to-market gains or losses on commodity contract positions), regardless whether the commodity broker has kept such books and records current or accurate.

Act means the Commodity Exchange Act.

Bankruptcy Code means, except as the context of the regulations in this part otherwise requires, those provisions of title 11 of the United States Code relating to ordinary bankruptcies (chapters 1 through 5) and liquidations (chapter 7 with the exception of subchapters III and V), together with the Federal Rules of Bankruptcy Procedure relating thereto.

Business day means weekdays, not including Federal holidays as established annually by 5 U.S.C. 6103. A business day begins at 8:00 a.m. in Washington, DC, and ends at 7:59:59 a.m. on the next day that is a business day.

Calendar day means the time from midnight to midnight in Washington, DC.

Cash delivery account class has the meaning set forth under *account class* in this section.

Cash delivery property means any cash or cash equivalents recorded in a delivery account that is, as of the filing date:

(1) Credited to such account to pay for receipt of delivery of a commodity under a commodity contract;

(2) Credited to such account to collateralize or guarantee an obligation to make or take delivery of a commodity under a commodity contract; or

(3) Has been credited to such account as payment received in exchange for making delivery of a commodity under a commodity contract. It also includes property in the form of commodities that have been delivered after the filing date in exchange for cash or cash equivalents held in a delivery account as of the filing date. The cash or cash equivalents must be identified on the books and the records of the debtor as having been received, from or for the account of a particular customer, on or after seven calendar days before the relevant:

(i) First notice date in the case of a futures contract; or

(ii) Exercise date in the case of a (cleared) option.

(4) Cash delivery property also includes any cash transferred by a customer to the trustee on or after the filing date for the purpose of paying for delivery, consistent with § 190.06(a)(3)(ii)(B)(*1*).

(5) In the case of a contract where one fiat currency is exchanged for another fiat currency, each such currency, to the extent that it is recorded in a delivery account, will be considered cash delivery property.

Cash equivalents means assets, other than United States dollar cash, that are highly liquid such that they may be converted into United States dollar cash within one business day without material discount in value.

Cleared swaps account has the meaning set forth under *account class* in this section.

Clearing organization means a derivatives clearing organization that is registered with the Commission as such under the Act.

Commodity broker means any person that is:

(1) A futures commission merchant under the Act, but excludes a person that is ''notice-registered'' as a futures commission merchant under section 4f(a)(2) of the Act; or

(2) A clearing organization, in each case with respect to which there is a ''customer'' as that term is defined in this section.

Commodity contract means:

(1) A futures or options on futures contract executed on or subject to the rules of a designated contract market;

(2) A futures or option on futures contract executed on or subject to the rules of a foreign board of trade;

(3) A swap as defined in section 1a(47) of the Act and § 1.3 of this chapter, that is directly or indirectly submitted to and cleared by a clearing organization and which is thus a cleared swap as that term is defined in section 1a(7) of the Act and § 22.1 of this chapter; or

(4) Any other contract that is a swap for purposes of this part under the definition in this section and is submitted to and cleared by a clearing organization.

(5) Notwithstanding paragraphs (1) through (4) of this definition, a security futures product as defined in section 1a(45) of the Act is not a commodity contract for purposes of this part when such contract is held in a securities account. Moreover, a contract, agreement, or transaction described in § 190.00(d)(3) as excluded from the term ''commodity contract'' is excluded from this definition.

Commodity contract account means:

(1) A futures account, foreign futures account, cleared swaps account, or delivery account; or

(2) If the debtor is a futures commission merchant, for purposes of identifying customer property for the foreign futures account class (subject to § 190.09(a)(1)), an account maintained for the debtor by a foreign clearing

organization or a foreign futures intermediary reflecting futures or options on futures executed on or subject to the rules of a foreign board of trade, including any account maintained on behalf of the debtor's public customers.

Court means the court having jurisdiction over the debtor's estate.

Cover has the meaning set forth in § 1.17(j) of this chapter.

Customer means:

(1)(i) With respect to a futures commission merchant as debtor (including a foreign futures commission merchant as that term is defined in section 761(12) of the Bankruptcy Code), the meaning set forth in sections 761(9)(A) and (B) of the Bankruptcy Code.

(ii) With respect to a clearing organization as debtor, the meaning set forth in section 761(9)(D) of the Bankruptcy Code.

(2) The term customer includes the owner of a portfolio cross-margining account covering commodity contracts and related positions in securities (as defined in section 3 of the Exchange Act) that is carried as a futures account or cleared swaps customer account pursuant to an appropriate rule, regulation, or order of the Commission.

Customer claim of record means a customer claim that is determinable solely by reference to the records of the debtor.

Customer class means each of the following two classes of customers, which must be recognized as separate classes by the trustee: Public customers and non-public customers; *provided, however,* that when the debtor is a clearing organization the references to public customers and non-public customers are based on the classification of customers of, and in relation to, the members of the clearing organization.

Customer property and *customer estate* are used interchangeably to mean the property subject to pro rata distribution in a commodity broker bankruptcy in the priority set forth in sections 766(h) or (i), as applicable, of the Bankruptcy Code, and includes cash, securities, and other property as set forth in § 190.09(a).

Debtor means a person with respect to which a proceeding is commenced under subchapter IV of chapter 7 of the Bankruptcy Code or under SIPA, or for which the Federal Deposit Insurance Corporation is appointed as a receiver pursuant to 12 U.S.C. 5382, *provided, however,* that this part applies only to such a proceeding if the debtor is a commodity broker as defined in this section.

Delivery account has the meaning set forth under *account class* in this section.

Distribution of property to a customer includes transfer of property on the customer's behalf, return of property to a customer, as well as distributions to a customer of valuable property that is different than the property posted by that customer.

Equity means the amount calculated as equity in accordance with § 190.08(b)(1).

Exchange Act means the Securities Exchange Act of 1934, as amended, 15 U.S.C. 78a *et seq.*

FDIC means the Federal Deposit Insurance Corporation.

Filing date means the date a petition under the Bankruptcy Code or application under SIPA commencing a proceeding is filed or on which the FDIC is appointed as a receiver pursuant to 12 U.S.C. 5382(a).

Final net equity determination date means the latest of:

(1) The day immediately following the day on which all commodity contracts held by or for the account of customers of the debtor have been transferred, liquidated, or satisfied by exercise or delivery;

(2) The day immediately following the day on which all property other than commodity contracts held for the account of customers has been transferred, returned or liquidated;

(3) The bar date for filing customer proofs of claim as determined by rule 3002(c) of the Federal Rules of Bankruptcy Procedure, the expiration of the six-month period imposed pursuant to section 8(a)(3) of SIPA, or such other date (whether earlier or later) set by the court (or, in the case of the FDIC acting as a receiver pursuant to 12 U.S.C. 5382(a), the deadline set by the FDIC pursuant to 12 U.S.C. 5390(a)(2)(B); or

(4) The day following the allowance (by the trustee or by the bankruptcy court) or disallowance (by the bankruptcy court) of all disputed customer net equity claims.

Foreign board of trade has the same meaning as set forth in § 1.3 of this chapter.

Foreign clearing organization means a clearing house, clearing association, clearing corporation or similar entity, facility, or organization clears and settles transactions in futures or options on futures executed on or subject to the rules of a foreign board of trade.

Foreign future shall have the same meaning as that set forth in section 761(11) of the Bankruptcy Code.

Foreign futures account has the meaning set forth under *account class* in this section.

Foreign futures commission merchant shall have the same meaning as that set forth in section 761(12) of the Bankruptcy Code.

Foreign futures intermediary refers to a foreign futures and options broker, as such term is defined in § 30.1(e) of this chapter, acting as an intermediary for foreign futures contracts between a foreign futures commission merchant and a foreign clearing organization.

Funded balance means the amount calculated as funded balance in accordance with § 190.08(c) and, as applicable, § 190.17(d).

Funded net equity means, for purposes of subpart B of this part, the amount calculated as funded net equity in accordance with § 190.08(a), and for purposes of subpart C of this part, the amount calculated as funded net equity in accordance with § 190.17(c).

Futures and *futures contract* are used interchangeably to mean any contract for the purchase or sale of a commodity (as defined in section 1a(9) of the Act) for future delivery that is executed on or subject to the rules of a designated contract market or on or subject to the rules of a foreign board of trade. The term also covers, for purposes of this part:

(1) Any transaction, contract or agreement described in section 2(c)(2)(D) of the Act and traded on or subject to the rules of a designated contract market or foreign board of trade, to the extent not covered by the foregoing definition; and

(2) Any transaction, contract, or agreement that is classified as a "forward contract" under the Act pursuant to the exclusion from the term "future delivery" set out in section 1a(27) of the Act or the exclusion from the definition of a "swap" under section 1a(47)(B)(ii) of the Act, provided that such transaction, contract, or agreement is traded on or subject to the rules of a designated contract market or foreign board of trade and is cleared by, respectively, a clearing organization or foreign clearing organization the same as if it were a futures contract.

Futures account has the meaning set forth under *account class* in this section.

House account means, in the case of a clearing organization, any commodity contract account of a member at such clearing organization maintained to reflect trades for the member's own account or for any non-public customer of such member.

In-the-money means:

(1) With respect to a call option, when the value of the underlying interest (such as a commodity or futures contract) which is the subject of the

option exceeds the strike price of the option; and

(2) With respect to a put option, when the value of the underlying interest (such as a commodity or futures contract) which is the subject of the option is exceeded by the strike price of the option.

Joint account means any commodity contract account held by more than one person.

Member property means, in connection with a clearing organization bankruptcy, the property which may be used to pay that portion of the net equity claim of a member which is based on the member's house account at the clearing organization, including any claims on behalf of non-public customers of the member.

Net equity means, for purposes of subpart B of this part, the amount calculated as net equity in accordance with § 190.08(b), and for purposes of subpart C of this part, the amount calculated as net equity in accordance with § 190.17(b).

Non-public customer means:

(1) With respect to a futures commission merchant, any customer that is not a public customer; and

(2) With respect to a clearing organization, any person whose account carried on the books and records of:

(i) A member of the clearing organization that is a futures commission merchant, is classified as a proprietary account under § 1.3 of this chapter (in the case of the futures or foreign futures account class) or as a cleared swaps proprietary account under § 22.1 of this chapter (in the case of the cleared swaps account class); or

(ii) A member of the clearing organization that is a foreign broker, is classified or treated as proprietary under and for purposes of:

(A) The rules of the clearing organization; or

(B) The jurisdiction of incorporation of such member.

Open commodity contract means a commodity contract which has been established in fact and which has not expired, been redeemed, been fulfilled by delivery or exercise, or been offset (*i.e.,* liquidated) by another commodity contract.

Order for relief has the same meaning set forth in section 301 of the Bankruptcy Code, in the case of the filing of a voluntary bankruptcy petition, and means the entry of an order granting relief under section 303 of the Bankruptcy Code in an involuntary case. It also means, where applicable, the issuance of a protective decree under section 5(b)(1) of SIPA or the appointment of the FDIC as receiver pursuant to 12 U.S.C. 5382(a)(1)(A).

Person means any individual, association, partnership, corporation, trust, or other form of legal entity.

Physical delivery account class has the meaning set forth under *account class* in this section.

Physical delivery property means:

(1) *In general.* A commodity, whether tangible or intangible, held in a form that can be delivered to meet and fulfill delivery obligations under a commodity contract that settles via delivery if held to a delivery position (as described in § 190.06(a)(1)), including warehouse receipts, other documents of title, or shipping certificates (including electronic versions of any of the foregoing) for the commodity, or the commodity itself:

(i) That the debtor holds for the account of a customer for the purpose of making delivery of such commodity on the customer's behalf, which as of the filing date or thereafter, can be identified on the books and records of the debtor as held in a delivery account for the benefit of such customer. Cash or cash equivalents received after the filing date in exchange for delivery of such physical delivery property shall also constitute physical delivery property;

(ii) That the debtor holds for the account of a customer and that the customer received or acquired by taking delivery under an expired or exercised commodity contract and which, as of the filing date or thereafter, can be identified on the books and records of the debtor as held in a delivery account for the benefit of such customer, regardless how long such property has been held in such account; or

(iii) Where property that the debtor holds in a futures account, foreign futures account, or cleared swaps account, or, if the commodity is a security, in a securities account, would meet the criteria listed in paragraph (1) or (2) of this definition, but for the fact of being held in such account rather than a delivery account, such property will be considered physical delivery property solely for purposes of the obligations to make or take delivery of physical delivery property pursuant to § 190.06.

(iv) Commodities or documents of title that are not held by the debtor and are delivered or received by a customer in accordance with § 190.06(a)(2) (or in accordance with § 190.06(a)(2) in conjunction with § 190.16(a) if the debtor is a clearing organization) to fulfill a customer's delivery obligation under a commodity contract will be considered physical delivery property solely for purposes of the obligations to make or take delivery of physical delivery property pursuant to § 190.06. As this property is held outside of the debtor's estate, it is not subject to pro rata distribution.

(2) *Special cases.* (i) In the case of a contract where one fiat currency is exchanged for another fiat currency, neither such currency, to the extent that it is recorded in a delivery account, will be considered physical delivery property.

(ii) In a case where the final settlement price is negative, *i.e.,* where the party obliged to deliver physical delivery property under an expiring futures contract or an expired options contract is also obliged to make a cash payment to the buyer, such cash or cash equivalents constitute physical delivery property.

Primary liquidation date means the first business day immediately following the day on which all commodity contracts (including any commodity contracts that are specifically identifiable property) have been liquidated or transferred.

Public customer means:

(1) With respect to a futures commission merchant and in relation to:

(i) The futures account class, a futures customer as defined in § 1.3 of this chapter whose futures account is subject to the segregation requirements of section 4d(a) of the Act and the regulations in this chapter that implement section 4d(a), including as applicable §§ 1.20 through 1.30 of this chapter;

(ii) The foreign futures account class, a 30.7 customer as defined in § 30.1 of this chapter whose foreign futures accounts is subject to the segregation requirements of § 30.7 of this chapter;

(iii) The cleared swaps account class, a Cleared Swaps Customer as defined in § 22.1 of this chapter whose cleared swaps account is subject to the segregation requirements of part 22 of this chapter; and

(iv) The delivery account class, a customer that is or would be classified as a public customer if the property reflected in the customer's delivery account had been held in an account described in paragraph (1)(i), (ii), or (iii) of this definition.

(2) With respect to a clearing organization, any customer of that clearing organization that is not a non-public customer.

Securities account means, in relation to a futures commission merchant that is registered as a broker or dealer under the Exchange Act, an account maintained by such futures commission merchant in accordance with the requirements of section 15(c)(3) of the

Exchange Act and § 240.15c3–3 of this title.

Security has the meaning set forth in section 101(49) of the Bankruptcy Code.

SIPA means the Securities Investor Protection Act of 1970, 15 U.S.C 78aaa *et seq.*

Specifically identifiable property means:

(1)(i) The following property received, acquired, or held by or for the account of the debtor from or for the futures account, foreign futures account, or cleared swaps account of a customer:

(A) Any security which as of the filing date is:

(*1*)(*i*) Held for the account of a customer;

(*ii*) Registered in such customer's name;

(*iii*) Not transferable by delivery; and

(*iv*) Has a duration or maturity date of more than 180 days; or

(*2*)(*i*) Fully paid;

(*ii*) Non-exempt; and

(*iii*) Identified on the books and records of the debtor as held by the debtor for or on behalf of the commodity contract account of a particular customer for which, according to such books and records as of the filing date, no open commodity contracts were held in the same capacity.

(B) Any warehouse receipt, bill of lading, or other document of title which as of the filing date:

(*1*) Can be identified on the books and records of the debtor as held for the account of a particular customer; and

(*2*) Is not in bearer form and is not otherwise transferable by delivery;

(ii) Any open commodity contracts treated as specifically identifiable property in accordance with § 190.03(c)(2); and

(iii) Any physical delivery property described in paragraphs (1) through (3) of the definition of physical delivery property in this section.

(2) Notwithstanding paragraphs (1) and (3) of this definition, security futures products, and any money, securities, or property held to margin, guarantee, or secure such products, or accruing as a result of such products, shall not be considered specifically identifiable property for the purposes of subchapter IV of the Bankruptcy Code or this part, if held in a securities account.

(3) No property that is not explicitly included in this definition may be treated as specifically identifiable property.

Strike price means the price per unit multiplied by the total number of units at which a person may purchase or sell a futures contract or a commodity or other interest underlying an option that is a commodity contract.

Substitute customer property means cash or cash equivalents delivered to the trustee by or on behalf of a customer in connection with:

(1) The return of specifically identifiable property by the trustee; or

(2) The return of, or an agreement not to draw upon, a letter of credit received, acquired or held to margin, guarantee, secure, purchase, or sell a commodity contract.

Swap has the meaning set forth in section 1a(47) of the Act and § 1.3 of this chapter, and, in addition, also means any other contract, agreement, or transaction that is carried in a cleared swaps account pursuant to a rule, regulation, or order of the Commission, provided, in each case, that it is cleared by a clearing organization as, or the same as if it were, a swap.

Trustee means, as appropriate, the trustee in bankruptcy or in a SIPA proceeding, appointed to administer the debtor's estate and any interim or successor trustee, or the FDIC, where it has been appointed as a receiver pursuant to 12 U.S.C. 5382.

Undermargined means, with respect to a futures account, foreign futures account, or cleared swaps account carried by the debtor, the funded balance for such account is below the minimum amount that the debtor is required to collect and maintain for the open commodity contracts in such account under the rules of the relevant clearing organization, foreign clearing organization, designated contract market, swap execution facility or foreign board of trade. If any such rules establish both an initial margin requirement and a lower maintenance margin requirement applicable to any commodity contracts (or to the entire portfolio of commodity contracts or any subset thereof) in a particular commodity contract account of the customer, the trustee will use the lower maintenance margin level to determine the customer's minimum margin requirement for such account.

Variation settlement means variation margin as defined in § 1.3 of this chapter plus all other daily settlement amounts (such as price alignment payments) that may be owed or owing on the commodity contract.

§ 190.02 General.

(a) *Request for exemption.* (1) The trustee (or, in the case of an involuntary petition pursuant to section 303 of the Bankruptcy Code, any other person charged with the management of a commodity broker) may, for good cause shown, request from the Commission an exemption from the requirements of any procedural provision in this part, including an extension of any time limit prescribed by this part or an exemption subject to conditions, provided that the Commission shall not grant an extension for any time period established by the Bankruptcy Code.

(2) A request pursuant to paragraph (a)(1) of this section—

(i) May be made *ex parte* and by any means of communication, written or oral, provided that the trustee must confirm an oral request in writing within one business day and such confirmation must contain all the information required by paragraph (b)(3) of this section. The request or confirmation of an oral request must be given to the Commission as provided in paragraph (a) of this section.

(ii) Must state the particular provision of this part with respect to which the exemption or extension is sought, the reason for the requested exemption or extension, the amount of time sought if the request is for an extension, and the reason why such exemption or extension would not be contrary to the purposes of the Bankruptcy Code and this part.

(3) The Director of the Division of Clearing and Risk, or members of the Commission staff designated by the Director, shall grant, deny, or otherwise respond to a request, on the basis of the information provided in any such request and after consultation with the Director of the Market Participants Division or members of the Commission staff designated by the Director, unless exigent circumstances require immediate action precluding such prior consultation, and shall communicate that determination by the most appropriate means to the person making the request.

(b) *Delegation of authority to the Director of the Division of Clearing and Risk.* (1) Until such time as the Commission orders otherwise, the Commission hereby delegates to the Director of the Division of Clearing and Risk, and to such members of the Commission's staff acting under the Director's direction as they may designate, after consultation with the Director of the Market Participants Division, or such members of the Commission's staff under the Director's direction as they may designate, unless exigent circumstances require immediate action, all the functions of the Commission set forth in this part, except the authority to disapprove a pre-relief transfer of a public customer commodity contract account or customer property pursuant to § 190.07(e)(1).

(2) The Director of the Division of Clearing and Risk may submit to the

Commission for its consideration any matter which has been delegated to the Director pursuant to paragraph (b)(1) of this section.

(3) Nothing in this section shall prohibit the Commission, at its election, from exercising its authority delegated to the Director of the Division of Clearing and Risk under paragraph (b)(1) of this section.

(c) *Forward contracts.* For purposes of this part, an entity for or with whom the debtor deals who holds a claim against the debtor solely on account of a forward contract, that is not cleared by a clearing organization, will not be deemed to be a customer.

(d) *Other.* The Bankruptcy Code will not be construed by the Commission to prohibit a commodity broker from doing business as any combination of the following: Futures commission merchant, commodity options dealer, foreign futures commission merchant, or leverage transaction merchant, nor will the Commission construe the Bankruptcy Code to permit any operation, trade, or business, or any combination of the foregoing, otherwise prohibited by the Act or by any of the Commission's regulations in this chapter, or by any order of the Commission.

(e) *Rule of construction.* Contracts in security futures products held in a securities account shall not be considered to be ''from or for the commodity futures account'' or ''from or for the commodity options account'' of such customers, as such terms are used in section 761(9) of the Bankruptcy Code.

(f) *Receivers.* In the event that a receiver for a futures commission merchant is appointed due to the violation or imminent violation of the customer property protection requirements of section 4d of the Act, or of the regulations in part 1, 22, or 30 of this chapter that implement section 4d or 4(b)(2) of the Act, or of the futures commission merchant's minimum capital requirements in § 1.17 of this chapter, such receiver may, in an appropriate case, file a petition for bankruptcy of such futures commission merchant pursuant to section 301 of the Bankruptcy Code.

(g) *Definition of* ''*allowed.*'' The term ''allowed'' in this part shall have the meaning ascribed to it in the Bankruptcy Code.

Subpart B—Futures Commission Merchant as Debtor

§ 190.03 Notices and proofs of claims.

(a) *Notices-means of providing*—(1) *To the Commission.* Unless instructed otherwise by the Commission, all mandatory or discretionary notices to be given to the Commission under this subpart shall be directed by electronic mail to *bankruptcyfilings@cftc.gov.* For purposes of this subpart, notice to the Commission shall be deemed to be given only upon actual receipt.

(2) *To Customers.* The trustee, after consultation with the Commission, and unless otherwise instructed by the Commission, will establish and follow procedures reasonably designed for giving adequate notice to customers under this subpart and for receiving claims or other notices from customers. Such procedures should include, absent good cause otherwise, the use of a prominent website as well as communication to customers' electronic addresses that are available in the debtor's books and records.

(b) *Notices to the Commission and designated self-regulatory organizations*—(1) *Of commencement of a proceeding.* Each commodity broker that is a futures commission merchant and files a petition in bankruptcy shall as soon as practicable before, and in any event no later than, the time of such filing, notify the Commission and such commodity broker's designated self-regulatory organization of the anticipated or actual filing date, the court in which the proceeding will be or has been filed and, as soon as known, the docket number assigned to that proceeding. Each commodity broker that is a futures commission merchant and against which a bankruptcy petition is filed or with respect to which an application for a protective decree under SIPA is filed shall immediately upon the filing of such petition or application notify the Commission and such commodity broker's designated self-regulatory organization of the filing date, the court in which the proceeding has been filed, and, as soon as known, the docket number assigned to that proceeding.

(2) *Of transfers under section 764(b) of the Bankruptcy Code.* As soon as possible, the trustee of a commodity broker that is a futures commissions merchant, the relevant designated self-regulatory organization, or the applicable clearing organization must notify the Commission, and in the case of a futures commission merchant, the trustee shall also notify its designated self-regulatory organization and clearing organization(s), if such person intends to transfer or to apply to transfer open commodity contracts or customer property on behalf of the public customers of the debtor in accordance with section 764(b) of the Bankruptcy Code and § 190.07(c) or (d).

(c) *Notices to customers*—(1) *Specifically identifiable property other than open commodity contracts.* In any case in which an order for relief has been entered, the trustee must use all reasonable efforts to promptly notify, in accordance with paragraph (a)(2) of this section, any customer whose futures account, foreign futures account, or cleared swaps account includes specifically identifiable property, other than open commodity contracts, which has not been liquidated, that such specifically identifiable property may be liquidated commencing on and after the seventh day after the order for relief (or such other date as is specified by the trustee in the notice with the approval of the Commission or court) if the customer has not instructed the trustee in writing before the deadline specified in the notice to return such property pursuant to the terms for distribution of specifically identifiable property contained in § 190.09(d)(1). Such notice must describe the specifically identifiable property and specify the terms upon which that property may be returned, including if applicable and to the extent practicable any substitute customer property that must be provided by the customer.

(2) *Open commodity contracts carried in hedging accounts.* To the extent reasonably practicable under the circumstances of the case, and following consultation with the Commission, the trustee may treat open commodity contracts of public customers identified on the books and records of the debtor as held in a futures account, foreign futures account, or cleared swaps account designated as a hedging account in the debtor's records, as specifically identifiable property of such customer.

(i) If the trustee does not exercise such authority, such open commodity contracts do not constitute specifically identifiable property.

(ii) If the trustee exercises such authority:

(A) The trustee shall use reasonable efforts to promptly notify, in accordance with paragraph (a)(2) of this section, each relevant public customer of such determination.

(B)(*1*) Where, in the judgment of the trustee, the books and records of the debtor reveal a clear preference by a relevant public customer with respect to transfer or liquidation of open commodity contracts, the trustee shall endeavor, to the extent reasonably practicable, to comply with that preference.

(*2*) Where, in the judgment of the trustee, the books and records of the debtor do not reveal a clear preference by a relevant public customer with respect to transfer or liquidation of open commodity contracts, the trustee will request the customer to provide written instructions whether to transfer or liquidate such open commodity contracts. Such notice must specify the manner for providing such instructions and the deadline by which the customer must provide instructions.

(C) Such notice must also inform the customer that:

(*1*) (Where instructions have been requested pursuant to paragraph (c)(2)(ii)(B)(*2*) of this section), if the customer does not provide instructions in the prescribed manner and by the prescribed deadline, the customer's open commodity contracts will not be treated as specifically identifiable property under this part;

(*2*) Any transfer of the open commodity contracts is subject to the terms for distribution contained in § 190.09(d)(2);

(*3*) Absent compliance with any terms imposed by the trustee or the court, the trustee may liquidate the open commodity contracts; and

(*4*) Providing (or having provided) instructions may not prevent the open commodity contracts from being liquidated.

(3) *Involuntary cases.* Prior to entry of an order for relief, and upon leave of the court, a trustee appointed in an involuntary proceeding pursuant to section 303 of the Bankruptcy Code may notify customers, in accordance with paragraph (a)(2) of this section, of the commencement of such proceeding and may request customer instructions with respect to the return, liquidation, or transfer of specifically identifiable property.

(4) *Notice of bankruptcy and request for proof of customer claim.* The trustee shall promptly notify, in accordance with paragraph (a)(2) of this section, each customer that an order for relief has been entered and instruct each customer to file a proof of customer claim containing the information specified in paragraph (e) of this section. Such notice may be given separately from any notice provided in accordance with paragraph (c) of this section. The trustee shall cause the proof of customer claim form referred to in paragraph (e) of this section to set forth the bar date for its filing.

(d) *Notice of court filings.* The trustee shall promptly provide the Commission with copies of any complaint, motion, or petition filed in a commodity broker bankruptcy which concerns the disposition of customer property. Court filings shall be directed to the Commission addressed as provided in paragraph (a)(1) of this section.

(e) *Proof of customer claim.* The trustee shall request that customers provide, to the extent reasonably practicable, information sufficient to determine a customer's claim in accordance with the regulations contained in this part, including in the discretion of the trustee:

(1) The class of commodity contract account upon which each claim is based (*i.e.,* futures account, foreign futures account, cleared swaps account, or delivery account (and, in the case of a delivery account, how much is based on cash delivery property and how much is based on the value of physical delivery property);

(2) Whether the claimant is a public customer or a non-public customer;

(3) The number of commodity contract accounts held by each claimant, and, for each such account:

(i) The account number;

(ii) The name in which the account is held;

(iii) The balance as of the last account statement for the account, and information regarding any activity in the account from the date of the last account statement up to and including the filing date that affected the balance of the account;

(iv) The capacity in which the account is held;

(v) Whether the account is a joint account and, if so, the amount of the claimant's percentage interest in that account and whether participants in the joint account are claiming jointly or separately;

(vi) Whether the account is a discretionary account;

(vii) Whether the account is an individual retirement account for which there is a custodian; and

(viii) Whether the account is a cross-margining account for futures and securities;

(4) A description of any accounts held by the claimant with the debtor that are not commodity contract accounts;

(5) A description of all claims against the debtor not based upon a commodity contract account of the claimant or an account listed in response to paragraph (e)(4) of this section;

(6) A description of all claims of the debtor against the claimant not included in the balance of a commodity contract account of the claimant;

(7) A description of and the value of any open positions, unliquidated securities, or other unliquidated property held by the debtor on behalf of the claimant, indicating the portion of such property, if any, which was included in the information provided in paragraph (e)(3) of this section, and identifying any such property which would be specifically identifiable property as defined in § 190.01;

(8) Whether the claimant holds positions in security futures products, and, if so, whether those positions are held in a futures account, a foreign futures account, or a securities account;

(9) Whether the claimant wishes to receive payment in kind, to the extent practicable, for any claim for unliquidated securities or other unliquidated property; and

(10) Copies of any documents which support the information contained in the proof of customer claim, including without limitation, customer confirmations, account statements, and statements of purchase or sale.

(f) *Proof of claim form.* A template customer proof of claim form which may (but is not required to) be used by the trustee is set forth in appendix A to this part.

(1) If there are no open commodity contracts that are being treated as specifically identifiable property (*e.g.,* if the customer proof of claim form was distributed after the primary liquidation date), the trustee should modify the customer proof of claim form to delete references to open commodity contracts as specifically identifiable property.

(2) In the event the trustee determines that the debtor's books and records reflecting customer transactions are not reasonably reliable, or account statements are not available from which account balances as of the date of transfer or liquidation of customer property may be determined, the proof of claim form used by the trustee should be modified to take into account the particular facts and circumstances of the case.

§ 190.04 Operation of the debtor's estate—customer property.

(a) *Transfers*—(1) *All cases.* The trustee for a commodity broker shall promptly use its best efforts to effect a transfer in accordance with § 190.07(c) and (d) no later than the seventh calendar day after the order for relief of the open commodity contracts and property held by the commodity broker for or on behalf of its public customers.

(2) *Involuntary cases.* A commodity broker against which an involuntary petition in bankruptcy is filed, or the trustee if a trustee has been appointed in such case, shall use its best efforts to effect a transfer in accordance with § 190.07(c) and (d) of all open commodity contracts and property held by the commodity broker for or on behalf of its public customers and such other property as the Commission in its discretion may authorize, on or before the seventh calendar day after the filing

date, and immediately cease doing business; *provided, however,* that if the commodity broker demonstrates to the Commission within such period that it was in compliance with the segregation and financial requirements of this chapter on the filing date, and the Commission determines, in its sole discretion, that such transfer is neither appropriate nor in the public interest, the commodity broker may continue in business subject to applicable provisions of the Bankruptcy Code and of this chapter.

(b) *Treatment of open commodity contracts*—(1) *Payments by the trustee.* Prior to the primary liquidation date, the trustee may make payments of initial margin and variation settlement to a clearing organization, commodity broker, foreign clearing organization, or foreign futures intermediary, carrying the account of the debtor, pending the transfer, or liquidation of any open commodity contracts, whether or not such contracts are specifically identifiable property of a particular customer, provided, that:

(i) To the extent within the trustee's control, the trustee shall not make any payments on behalf of any commodity contract account on the books and records of the debtor that is in deficit; *provided, however,* that the provision in this paragraph (b)(1) shall not be construed to prevent a clearing organization, foreign clearing organization, futures commission merchant, or foreign futures intermediary carrying an account of the debtor from exercising its rights to the extent permitted under applicable law;

(ii) Any margin payments made by the trustee with respect to a specific customer account shall not exceed the funded balance for that account;

(iii) The trustee shall not make any payments on behalf of non-public customers of the debtor from funds that are segregated for the benefit of public customers;

(iv) If the trustee receives payments from a customer in response to a margin call, then to the extent within the trustee's control, the trustee must use such payments to make margin payments for the open commodity contract positions of such customer;

(v) The trustee may not use payments received from one public customer to meet the margin (or any other) obligations of any other customer; and

(vi) If funds segregated for the benefit of public customers in a particular account class exceed the aggregate net equity claims for all public customers in such account class, the trustee may use such excess funds to meet the margin obligations for any public customer in such account class whose account is under-margined (as described in paragraph (b)(4) of this section) but not in deficit, provided that the trustee issues a margin call to such customer and provided further that the trustee shall liquidate such customer's open commodity contracts if the customer fails to make the margin payment within a reasonable time as provided in paragraph (b)(4) of this section.

(2) *Margin calls.* The trustee (or, prior to appointment of the trustee, the debtor against which an involuntary petition was filed) may issue a margin call to any public customer whose commodity contract account contains open commodity contracts if such account is under-margined.

(3) *Margin payments by the customer.* The full amount of any margin payment by a customer in response to a margin call under paragraph (b)(2) of this section must be credited to the funded balance of the particular account for which it was made.

(4) *Trustee obligation to liquidate certain open commodity contracts.* The trustee shall, as soon as practicable under the circumstances, liquidate all open commodity contracts in any commodity contract account that is in deficit, or for which any mark-to-market calculation would result in a deficit, or for which the customer fails to meet a margin call made by the trustee within a reasonable time. Except as otherwise provided in this part, absent exigent circumstances, a reasonable time for meeting margin calls made by the trustee shall be deemed to be one hour, or such greater period not to exceed one business day, as the trustee may determine in its sole discretion.

(5) *Partial liquidation of open commodity contracts by others.* In the event that a clearing organization, foreign clearing organization, futures commission merchant, foreign futures intermediary, or other person carrying a commodity customer account for the debtor in the nature of an omnibus account has liquidated only a portion of open commodity contracts in such account, the trustee will exercise reasonable business judgment in assigning the liquidating transactions to the underlying commodity customer accounts carried by the debtor. Specifically, the trustee should endeavor to assign the contracts as follows: First, to liquidate open commodity contracts in a risk-reducing manner in any accounts that are in deficit; second, to liquidate open commodity contracts in a risk-reducing manner in any accounts that are undermargined; third, to liquidate open commodity contracts in a risk-reducing manner in any other accounts, and finally to liquidate any remaining open commodity contracts in any accounts. If more than one commodity contract account reflects open commodity contracts in a particular account class for which liquidating transactions have been executed, the trustee shall to the extent practicable allocate the liquidating transactions to such commodity contract accounts pro rata based on the number of open commodity contracts of such commodity contract accounts. For purposes of this section, the term ''a risk-reducing manner'' is measured by margin requirements set using the margin methodology and parameters followed by the derivatives clearing organization at which such contracts are cleared.

(c) *Contracts moving into delivery position.* After entry of the order for relief and subject to paragraph (a) of this section, which requires the trustee to attempt to make transfers to other commodity brokers permitted by § 190.07 and section 764(b) of the Bankruptcy Code, the trustee shall use its best efforts to liquidate any open commodity contract that settles upon expiration or exercise via the making or taking of delivery of a commodity:

(1) If such contract is a futures contract or a cleared swaps contract, before the earlier of the last trading day or the first day on which notice of intent to deliver may be tendered with respect thereto, or otherwise before the debtor or its customer incurs an obligation to make or take delivery of the commodity under such contract;

(2) If such contract is a long option on a commodity and has value, before the first date on which the contract could be automatically exercised or the last date on which the contract could be exercised if not subject to automatic exercise; or

(3) If such contract is a short option on a commodity that is in-the-money in favor of the long position holder, before the first date on which the long option position could be exercised.

(d) *Liquidation or offset.* After entry of the order for relief and subject to paragraph (a) of this section, which requires the trustee to attempt to make transfers to other commodity brokers permitted by § 190.07 and section 764(b) of the Bankruptcy Code, and except as otherwise set forth in this paragraph (d), the following commodity contracts and other property held by or for the account of a debtor must be liquidated in the market in accordance with paragraph (e)(1) of this section or liquidated via book entry in accordance with paragraph (e)(2) of this section by the trustee promptly and in an orderly manner:

(1) *Open commodity contracts.* All open commodity contracts, except for:

(i) Commodity contracts that are specifically identifiable property (if applicable) and are subject to customer instructions to transfer (in lieu of liquidating) as provided in § 190.03(c)(2), provided that the customer is in compliance with the terms of § 190.09(d)(2); and

(ii) Open commodity contract positions that are in a delivery position, which shall be treated in accordance with the provisions of § 190.06.

(2) *Specifically identifiable property, other than open commodity contracts or physical delivery property.* Specifically identifiable property, other than open commodity contracts or physical delivery property, to the extent that:

(i) The fair market value of such property is less than 75% of its fair market value on the date of entry of the order for relief;

(ii) Failure to liquidate the specifically identifiable property may result in a deficit balance in the applicable customer account; or

(iii) The trustee has not received instructions to return pursuant to § 190.03(c)(1), or has not returned such property upon the terms contained in § 190.09(d)(1).

(3) *Letters of credit.* The trustee may request that a customer deliver substitute customer property with respect to any letter of credit received, acquired, or held to margin, guarantee, secure, purchase, or sell a commodity contract, whether the letter of credit is held by the trustee on behalf of the debtor's estate or a derivatives clearing organization or a foreign intermediary or foreign clearing organization on a pass-through or other basis, including in cases where the letter of credit has expired since the date of the order for relief. The amount of the request may equal the full face amount of the letter of the credit or any portion thereof, to the extent required or may be required in the trustee's discretion to ensure pro rata treatment among customer claims within each account class, consistent with §§ 190.08 and 190.09.

(i) If a customer fails to provide substitute customer property within a reasonable time specified by the trustee, the trustee may, if the letter of credit has not expired, draw upon the full amount of the letter of credit or any portion thereof.

(ii) For any letter of credit referred to in this paragraph (d)(3), the trustee shall treat any portion that is not drawn upon (less the value of any substitute customer property delivered by the customer) as having been distributed to the customer for purposes of calculating entitlements to distribution or transfer. The expiration of the letter of credit on or at any time after the date of the order for relief shall not affect such calculation.

(iii) Any proceeds of a letter of credit drawn by the trustee, or substitute customer property posted by a customer, shall be considered customer property in the account class applicable to the original letter of credit.

(iv) The trustee shall, in exercising their discretion with regard to addressing letters of credit, including as to the timing and amount of a request for substitute customer property, endeavor to mitigate, to the extent practicable, the adverse effects upon customers that have posted letters of credit, in a manner that achieves *pro rata* treatment among customer claims.

(4) *All other property.* All other property, other than physical delivery property held for delivery in accordance with the provisions of § 190.06, which is not required to be transferred or returned pursuant to customer instructions and which has not been liquidated in accordance with paragraphs (d)(1) through (3) of this section.

(e) *Liquidation of open commodity contracts*—(1) *By the trustee or a clearing organization in the market*—(i) *Debtor as a clearing member.* For open commodity contracts cleared by the debtor as a member of a clearing organization, the trustee or clearing organization, as applicable, shall liquidate such open commodity contracts pursuant to the rules of the clearing organization, a designated contract market, or a swap execution facility, if and as applicable. Any such rules providing for liquidation other than on the open market shall be designed to achieve, to the extent feasible under market conditions at the time of liquidation, a process for liquidating open commodity contracts that results in competitive pricing. For open commodity contracts that are futures or options on futures that were established on or subject to the rules of a foreign board of trade and cleared by the debtor as a member of a foreign clearing organization, the trustee shall liquidate such open commodity contracts pursuant to the rules of the foreign clearing organization or foreign board of trade or, in the absence of such rules, in the manner the trustee determines appropriate.

(ii) *Debtor not a clearing member.* For open commodity contracts submitted by the debtor for clearing through one or more accounts established with a futures commission merchant (as defined in § 1.3 of this chapter) or foreign futures intermediary, the trustee shall use commercially reasonable efforts to liquidate the open commodity contracts to achieve competitive pricing, to the extent feasible under market conditions at the time of liquidation and subject to any rules or orders of the relevant clearing organization, foreign clearing organization, designated contract market, swap execution facility, or foreign board of trade governing the liquidation of open commodity contracts.

(2) *By the trustee or a clearing organization via book entry offset.* Upon application by the trustee or clearing organization, the Commission may permit open commodity contracts to be liquidated, or settlement on such contracts to be made, by book entry. Such book entry shall offset open commodity contracts, whether matched or not matched on the books of the commodity broker, using the settlement price for such commodity contracts as determined by the clearing organization in accordance with its rules. Such rules shall be designed to establish, to the extent feasible under market conditions at the time of liquidation, such settlement prices in a competitive manner.

(3) *By a futures commission merchant or foreign futures intermediary.* For open commodity contracts cleared by the debtor through one or more accounts established with a futures commission merchant or a foreign futures intermediary, such futures commission merchant or foreign futures intermediary may exercise any enforceable contractual rights it has to liquidate such commodity contracts, provided, that it shall use commercially reasonable efforts to liquidate the open commodity contracts to achieve competitive pricing, to the extent feasible under market conditions at the time of liquidation and subject to any rules or orders of the relevant clearing organization, foreign clearing organization, designated contract market, swap execution facility, or foreign board of trade governing its liquidation of such open commodity contracts. If a futures commission merchant or foreign futures intermediary fails to use commercially reasonable efforts to liquidate open commodity contracts to achieve competitive pricing in accordance with this paragraph (e)(3), the trustee may seek damages reflecting the difference between the price (or prices) at which the relevant commodity contracts would have been liquidated using commercially reasonable efforts to

achieve competitive pricing and the price (or prices) at which the commodity contracts were liquidated, which shall be the sole remedy available to the trustee. In no event shall any such liquidation be voided.

(4) *Liquidation only.* (i) Nothing in this part shall be interpreted to permit the trustee to purchase or sell new commodity contracts for the debtor or its customers except to offset open commodity contracts or to transfer any transferable notice received by the debtor or the trustee under any commodity contract; *provided, however,* that the trustee may, in its discretion and with approval of the Commission, cover uncovered inventory or commodity contracts of the debtor which cannot be liquidated immediately because of price limits or other market conditions, or may take an offsetting position in a new month or at a strike price for which limits have not been reached.

(ii) Notwithstanding paragraph (e)(4)(i) of this section, the trustee may, with the written permission of the Commission, operate the business of the debtor in the ordinary course, including the purchase or sale of new commodity contracts on behalf of the customers of the debtor under appropriate circumstances, as determined by the Commission.

(f) *Long option contracts.* Subject to paragraphs (d) and (e) of this section, the trustee shall use its best efforts to assure that a commodity contract that is a long option contract with value does not expire worthless.

§ 190.05 Operation of the debtor's estate—general.

(a) *Compliance with the Act and regulations in this chapter.* Except as specifically provided otherwise in this part, the trustee shall use reasonable efforts to comply with all of the provisions of the Act and of the regulations in this chapter as if it were the debtor.

(b) *Computation of funded balance.* The trustee shall use reasonable efforts to compute a funded balance for each customer account that contains open commodity contracts or other property as of the close of business each business day subsequent to the order for relief until the date all open commodity contracts and other property in such account have been transferred or liquidated, which shall be as accurate as reasonably practicable under the circumstances, including the reliability and availability of information.

(c) *Records*—(1) *Maintenance.* Except as otherwise ordered by the court or as permitted by the Commission, records required under this chapter to be maintained by the debtor, including records of the computations required by this part, shall be maintained by the trustee until such time as the debtor's case is closed.

(2) *Accessibility.* The records required to be maintained by paragraph (c)(1) of this section shall be available during business hours to the Commission and the U.S. Department of Justice. The trustee shall give the Commission and the U.S. Department of Justice access to all records of the debtor, including records required to be retained in accordance with § 1.31 of this chapter and all other records of the commodity broker, whether or not the Act or this chapter would require such records to be maintained by the commodity broker.

(d) *Customer statements.* The trustee shall use all reasonable efforts to continue to issue account statements with respect to any customer for whose account open commodity contracts or other property is held that has not been liquidated or transferred. With respect to such accounts, the trustee must also issue an account statement reflecting any liquidation or transfer of open commodity contracts or other property promptly after such liquidation or transfer.

(e) *Other matters*—(1) *Disbursements.* With the exception of transfers of customer property made in accordance with § 190.07, the trustee shall make no disbursements to customers except with approval of the court.

(2) *Investment.* The trustee shall promptly invest the proceeds from the liquidation of commodity contracts or specifically identifiable property, and may invest any other customer property, in obligations of the United States and obligations fully guaranteed as to principal and interest by the United States, provided that such obligations are maintained in a depository located in the United States, its territories or possessions.

(f) *Residual interest.* The trustee shall apply the residual interest provisions of § 1.11 of this chapter in a manner appropriate to the context of their responsibilities as a bankruptcy trustee pursuant subchapter IV of chapter 7 of the Bankruptcy Code and this part, and in light of the existence of a surplus or deficit in customer property available to pay customer claims.

§ 190.06 Making and taking delivery under commodity contracts.

(a) *Deliveries*—(1) *General.* The provisions of this paragraph (a) apply to commodity contracts that settle upon expiration or exercise by making or taking delivery of physical delivery property, if such commodity contracts are in a delivery position on the filing date, or the trustee is unable to liquidate such commodity contracts in accordance with § 190.04(c) to prevent them from moving into a delivery position, *i.e.,* before the debtor or its customer incurs bilateral contractual obligations to make or take delivery under such commodity contracts.

(2) *Delivery made or taken on behalf of a customer outside of the administration of the debtor's estate.* (i) The trustee shall use reasonable efforts to allow a customer to deliver physical delivery property that is held directly by the customer and not by the debtor (and thus not recorded in any commodity contract account of the customer) in settlement of a commodity contract, and to allow payment in exchange for such delivery, to occur outside the administration of the debtor's estate, when the rules of the exchange or other market listing the commodity contract, or the clearing organization or the foreign clearing organization clearing the commodity contract, as applicable, prescribe a process for delivery that allows the delivery to be fulfilled:

(A) In the normal course directly by the customer;

(B) By substitution of the customer for the commodity broker; or

(C) Through agreement of the buyer and seller to alternative delivery procedures.

(ii) Where a customer delivers physical delivery property in settlement of a commodity contract outside of the administration of the debtors' estate in accordance with paragraph (a)(2)(i) of this section, any property of such customer held at the debtor in connection with such contract must nonetheless be included in the net equity claim of that customer, and, as such, can only be distributed pro rata at the time of, and as part of, any distributions to customers made by the trustee.

(3) *Delivery as part of administration of the debtor's estate.* When the trustee determines that it is not practicable to effect delivery as provided in paragraph (a)(2) of this section:

(i) To facilitate the making or taking of delivery directly by a customer, the trustee may, as it determines reasonable under the circumstances of the case and consistent with the pro rata distribution of customer property by account class:

(A) When a customer is obligated to make delivery, return any physical delivery property to the customer that is held by the debtor for or on behalf of the customer under the terms set forth in § 190.09(d)(1)(ii), to allow the customer to deliver such property to fulfill its delivery obligation under the commodity contract; or

(B) When a customer is obligated to take delivery:

(*1*) Return any cash delivery property to the customer that is reflected in the customer's delivery account, provided that cash delivery property returned under this paragraph (a)(3)(i)(B)(*1*) shall not exceed the lesser of:

(*i*) The amount the customer is required to pay for delivery of the commodity; or

(*ii*) The customer's net funded balance for all of the customer's commodity contract accounts;

(*2*) Return cash, securities, or other property held in the customer's non-delivery commodity contract accounts, provided that property returned under this section shall not exceed the lesser of:

(*i*) The amount the customer is required to pay for delivery of the commodity; or

(*ii*) The net funded balance for all of the customer's commodity contract accounts reduced by any amount returned to the customer pursuant to paragraph (a)(3)(i)(B)(*1*) of this section, and provided further, however, that the trustee may distribute such property only to the extent that the customer's funded balance for each such account exceeds the minimum margin obligations for such account (as described in § 190.04(b)(2)); and

(C) Impose such conditions on the customer as it considers appropriate to assure that property returned to the customer is used to fulfill the customer's delivery obligations.

(ii) If the trustee does not return physical delivery property, cash delivery property, or other property in the form of cash or cash equivalents to the customer as provided in paragraph (a)(3)(i) of this section, subject to paragraph (a)(4) of this section:

(A) To the extent practical, the trustee shall make or take delivery of physical delivery property in the same manner as if no bankruptcy had occurred, and when making delivery, the party to which delivery is made must pay the full price required for taking such delivery; or

(B) When taking delivery of physical delivery property:

(*1*) The trustee shall pay for the delivery first using the customer's cash delivery property or other property, limited to the amounts set forth in paragraph (a)(3)(i)(B) of this section, along with any cash transferred by the customer to the trustee on or after the filing date for the purpose of paying for delivery.

(*2*) If the value of the cash or cash equivalents that may be used to pay for deliveries as described in paragraph (a)(3)(i)(B) of this section is less than the amount required to be paid for taking delivery, the trustee shall issue a payment call to the customer. The full amount of any payment made by the customer in response to a payment call must be credited to the funded balance of the particular account for which such payment is made.

(*3*) If the customer fails to meet a call for payment under paragraph (a)(3)(ii)(B)(*2*) of this section before payment is made for delivery, the trustee must convert any physical delivery property received on behalf of the customer to cash as promptly as possible.

(4) *Deliveries in a securities account.* If an open commodity contract held in a futures account, foreign futures account, or cleared swaps account requires delivery of a security upon expiration or exercise of such commodity contract, and delivery is not completed pursuant to paragraph (a)(2) or (a)(3)(i) of this section, the trustee may make or take delivery in a securities account in a manner consistent with paragraph (a)(3)(ii) of this section, *provided, however,* that the trustee may transfer property from the customer's commodity contract accounts to the securities account to fulfill the delivery obligation only to the extent that the customer's funded balance for such commodity contract account exceeds the customer's minimum margin obligations for such accounts (as described in § 190.04(b)(2)) and provided further that the customer is not under-margined or does not have a deficit balance in any other commodity contract accounts.

(5) *Delivery made or taken on behalf of proprietary account.* If delivery of physical delivery property is to be made or taken on behalf of the debtor's own account or the account of any non-public customer of the debtor, the trustee shall make or take delivery, as the case may be, on behalf of the debtor's estate, provided that if the trustee takes delivery of physical delivery property it must convert such property to cash as promptly as possible.

(b) *Special account class provisions for delivery accounts.* (1) Within the delivery account class, the trustee shall treat—

(i) Physical delivery property held in delivery accounts as of the filing date, and the proceeds of any such physical delivery property subsequently received, as part of the physical delivery account class; and

(ii) Cash delivery property in delivery accounts as of the filing date, along with any physical delivery property for which delivery is subsequently taken on behalf of a customer in accordance with paragraph (a)(3) of this section, as part of a separate cash delivery account class.

(2)(i) If the debtor holds any cash or cash equivalents in an account maintained at a bank, clearing organization, foreign clearing organization, or other person, under a name or in a manner that clearly indicates that the account holds property for the purpose of making payment for taking delivery, or receiving payment for making delivery, of a commodity under commodity contracts, such property shall (subject to § 190.09) be considered customer property—

(A) In the cash delivery account class if held for making payment for taking delivery; and

(B) In the physical delivery account class, if held as a result of receiving such payment for a making delivery after the filing date.

(ii) Any other property (excluding property segregated for the benefit of customer in the futures, foreign futures or cleared swaps account class) that is traceable as having been held or received for the purpose of making delivery, or as having been held or received as a result of taking delivery, of a commodity under commodity contracts, shall (subject to § 190.09) be considered customer property—

(A) In the cash delivery account class if received after the filing date in exchange for taking delivery; and

(B) Otherwise shall be considered customer property in the physical delivery account class.

§ 190.07 Transfers.

(a) *Transfer rules.* No clearing organization or self-regulatory organization may adopt, maintain in effect, or enforce rules that:

(1) Are inconsistent with the provisions of this part;

(2) Interfere with the acceptance by its members of transfers of commodity contracts, and the property margining or securing such contracts, from futures commission merchants that are required to transfer accounts pursuant to § 1.17(a)(4) of this chapter; or

(3) Interfere with the acceptance by its members of transfers of commodity contracts, and the property margining or securing such contracts, from a futures commission merchant that is a debtor as defined in § 190.01, if such transfers have been approved by the Commission,

provided, however, that this paragraph (a)(3) shall not—

(i) Limit the exercise of any contractual right of a clearing organization or other registered entity to liquidate or transfer open commodity contracts; or

(ii) Be interpreted to limit a clearing organization's ability adequately to manage risk.

(b) *Requirements for transferees.* (1) It is the duty of each transferee to assure that it will not accept a transfer that would cause the transferee to be in violation of the minimum financial requirements set forth in this chapter.

(2) Any transferee that accepts a transfer of open commodity contracts from the estate of the debtor—

(i) Accepts the transfer subject to any loss that may arise in the event the transferee cannot recover from the customer any deficit balance that may arise related to the transferred open commodity contracts.

(ii) If the commodity contracts were held for the account of a customer:

(A) Must keep such commodity contracts open at least one business day after their receipt, unless the customer for whom the transfer is made fails to respond within a reasonable time to a margin call for the difference between the margin transferred with such commodity contracts and the margin which such transferee would require with respect to a similar set of commodity contracts held for the account of a customer in the ordinary course of business; and

(B) May not collect commissions with respect to the transfer of such commodity contracts.

(3) A transferee may accept open commodity contracts and property, and open accounts on its records, for customers whose commodity contracts and property are transferred pursuant to this part prior to completing customer diligence, provided that account opening diligence as required by law (including the risk disclosures referred to in § 1.65(a)(3) of this chapter) is performed, and records and information required by law are obtained, as soon as practicable, but in any event within six months of the transfer, unless this time is extended for a particular account, transferee, or debtor by the Commission.

(4)(i) Any account agreements governing a transferred account (including an account that has been partially transferred) shall be deemed assigned to the transferee by operation of law and shall govern the transferee and customer's relationship until such time as the transferee and customer enter into a new agreement; *provided, however,* that any breach of such agreement by the debtor existing at or before the time of the transfer (including, but not limited to, any failure to segregate sufficient customer property) shall not constitute a default or breach of the agreement on the part of the transferee, or constitute a defense to the enforcement of the agreement by the transferee.

(ii) Paragraph (b)(4)(i) of this section shall not apply where the customer has a pre-existing account agreement with the transferee futures commission merchant. In such a case, the transferred account will be governed by that pre-existing account agreement.

(5) If open commodity contracts or any specifically identifiable property has been, or is to be, transferred in accordance with section 764(b) of the Bankruptcy Code and this section, customer instructions previously received by the trustee with respect to open commodity contracts or with respect to specifically identifiable property, shall be transmitted to the transferee of property, which shall comply therewith to the extent practicable.

(c) *Eligibility for transfer under section 764(b) of the Bankruptcy Code—accounts eligible for transfer.* All commodity contract accounts (including accounts with no open commodity contract positions) are eligible for transfer after the order for relief pursuant to section 764(b) of the Bankruptcy Code, except:

(1) The debtor's own account or the accounts of general partners of the debtor if the debtor is a partnership; and

(2) Accounts that are in deficit.

(d) *Special rules for transfers under section 764(b) of the Bankruptcy Code—* (1) *Effecting transfer.* The trustee for a commodity broker shall use its best efforts to effect a transfer to one or more other commodity brokers of all eligible commodity contract accounts, open commodity contracts and property held by the debtor for or on behalf of its customers, based on customer claims or record, no later than the seventh calendar day after the order for relief.

(2) *Partial transfers; multiple transferees*—(i) *Of the customer estate.* If all eligible commodity contract accounts held by a debtor cannot be transferred under this section, a partial transfer may nonetheless be made. The Commission will not disapprove such a transfer for the sole reason that it was a partial transfer. Commodity contract accounts may be transferred to one or more transferees, and, subject to paragraph (d)(4) of this section, may be transferred to different transferees by account class.

(ii) *Of a customer's commodity contract account.* If all of a customer's open commodity contracts and property cannot be transferred under this section, a partial transfer of contracts and property may be made so long as such transfer would not result in an increase in the amount of any customer's net equity claim. One, but not the only, means to effectuate a partial transfer is by liquidating a portion of the open commodity contracts held by a customer such that sufficient value is realized, or margin requirements are reduced to an extent sufficient, to permit the transfer of some or all of the remaining open commodity contracts and property. If any open commodity contract to be transferred in a partial transfer is part of a spread or straddle, to the extent practicable under the circumstances, each side of such spread or straddle must be transferred or none of the open commodity contracts comprising the spread or straddle may be transferred.

(3) *Letters of credit.* A letter of credit received, acquired, or held to margin, guarantee, secure, purchase, or sell a commodity contract may be transferred with an eligible commodity contract account if it is held by a derivatives clearing organization on a pass-through or other basis or is transferable by its terms, so long as the transfer will not result in a recovery which exceeds the amount to which the customer would be entitled under §§ 190.08 and 190.09. If the letter of credit cannot be transferred as provided for in the foregoing sentence, and the customer does not deliver substitute customer property to the trustee in accordance with § 190.04(d)(3), the trustee may draw upon a portion or all of the letter of credit, the proceeds of which shall be treated as customer property in the applicable account class.

(4) *Physical delivery property.* The trustee shall use reasonable efforts to prevent physical delivery property held for the purpose of making delivery on a commodity contract from being transferred separate and apart from the related commodity contract, or to a different transferee.

(5) *No prejudice to other customers.* No transfer shall be made under this part by the trustee if, after taking into account all customer property available for distribution to customers in the applicable account class at the time of the transfer, such transfer would result in insufficient remaining customer property to make an equivalent percentage distribution (including all previous transfers and distributions) to all customers in the applicable account class, based on—

(i) Customer claims of record; and

(ii) Estimates of other customer claims made in the trustee's reasonable discretion based on available information, in each case as of the calendar day immediately preceding transfer.

(e) *Prohibition on avoidance of transfers under section 764(b) of the Bankruptcy Code*—(1) *Pre-relief transfers.* Notwithstanding the provisions of paragraphs (c) and (d) of this section, the following transfers are approved and may not be avoided under sections 544, 546, 547, 548, 549, or 724(a) of the Bankruptcy Code:

(i) The transfer of commodity contract accounts or customer property prior to the entry of the order for relief in compliance with § 1.17(a)(4) of this chapter unless such transfer is disapproved by the Commission;

(ii) The transfer, withdrawal, or settlement, prior to the order for relief at the request of a public customer, including a transfer, withdrawal, or settlement at the request of a public customer that is a commodity broker, of commodity contract accounts or customer property held from or for the account of such customer by or on behalf of the debtor unless:

(A) The customer acted in collusion with the debtor or its principals to obtain a greater share of customer property or the bankruptcy estate than that to which it would be entitled under this part; or

(B) The transfer is disapproved by the Commission;

(iii) The transfer prior to the order for relief by a clearing organization, or by a receiver that has been appointed for the futures commission merchant (FCM) that is now a debtor, of one or more accounts held for or on behalf of customers of the debtor, or of commodity contracts and other customer property held for or on behalf of customers of the debtor, provided that the transfer is not disapproved by the Commission.

(2) *Post-relief transfers.* Notwithstanding the provisions of paragraphs (c) and (d) of this section, the following transfers are approved and may not be avoided under sections 544, 546, 547, 548, 549, or 724(a) of the Bankruptcy Code:

(i) The transfer of a commodity contract account or customer property eligible to be transferred under paragraphs (c) and (d) of this section made by the trustee or by any clearing organization on or before the seventh calendar day after the entry of the order for relief, as to which the Commission has not disapproved the transfer; or

(ii) The transfer of a commodity contract account or customer property at the direction of the Commission on or before the seventh calendar day after the order for relief, upon such terms and conditions as the Commission may deem appropriate and in the public interest.

(f) *Commission action.* Notwithstanding any other provision of this section (other than paragraphs (d)(2)(ii) and (d)(5) of this section), in appropriate cases and to protect the public interest, the Commission may:

(1) Prohibit the transfer of a particular set or sets of commodity contract accounts and customer property; or

(2) Permit transfers of a particular set or sets of commodity contract accounts and customer property that do not comply with the requirements of this section.

§ 190.08 Calculation of funded net equity.

For purposes of this subpart, funded net equity shall be computed as follows:

(a) *Funded claim.* The funded net equity claim of a customer shall be equal to the aggregate of the funded balances of such customer's net equity claim for each account class.

(b) *Net equity.* Net equity means a customer's total customer claim of record against the estate of the debtor based on the customer property, including any commodity contracts, held by the debtor for or on behalf of such customer less any indebtedness of the customer to the debtor. Net equity shall be calculated as follows:

(1) *Step 1-equity determination.* (i) Determine the equity balance of each commodity contract account of a customer by computing, with respect to such account, the sum of:

(A) The ledger balance;

(B) The open trade balance; and

(C) The realizable market value, determined as of the close of the market on the last preceding market day, of any securities or other property held by or for the debtor from or for such account, plus accrued interest, if any.

(ii) For the purposes of this paragraph (b)(1), the ledger balance of a customer account shall be calculated by:

(A) Adding:

(*1*) Cash deposited to purchase, margin, guarantee, secure, or settle a commodity contract;

(*2*) Cash proceeds of liquidations of any securities or other property referred to in paragraph (b)(1)(i)(C) of this section;

(*3*) Gains realized on trades; and

(*4*) The face amount of any letter of credit received, acquired or held to margin, guarantee, secure, purchase or sell a commodity contract; and

(B) Subtracting from the result:

(*1*) Losses realized on trades;

(*2*) Disbursements to or on behalf of the customer (including, for these purposes, transfers made pursuant to §§ 190.04(a) and 190.07); and

(*3*) The normal costs attributable to the payment of commissions, brokerage, interest, taxes, storage, transaction fees, insurance, and other costs and charges lawfully incurred in connection with the purchase, sale, exercise, or liquidation of any commodity contract in such account.

(iii) For purposes of this paragraph (b)(1), the open trade balance of a customer's account shall be computed by subtracting the unrealized loss in value of the open commodity contracts held by or for such account from the unrealized gain in value of the open commodity contracts held by or for such account.

(iv) For purposes of this paragraph (b)(1), in calculating the ledger balance or open trade balance of any customer, exclude any security futures products, any gains or losses realized on trades in such products, any property received to margin, guarantee, or secure such products (including interest thereon or the proceeds thereof), to the extent any of the foregoing are held in a securities account, and any disbursements to or on behalf of such customer in connection with such products or such property held in a securities account.

(2) *Step 2-customer determination (aggregation).* Aggregate the credit and debit equity balances of all accounts of the same class held by a customer in the same capacity. Paragraphs (b)(2)(i) through (xii) of this section prescribe which accounts must be treated as being held in the same capacity and which accounts must be treated as being held in a separate capacity.

(i) Except as otherwise provided in this paragraph (b)(2), all accounts that are maintained with a debtor in a person's name and that, under this paragraph (b)(2), are deemed to be held by that person in its individual capacity shall be deemed to be held in the same capacity.

(ii) An account maintained with a debtor by a guardian, custodian, or conservator for the benefit of a ward, or for the benefit of a minor under the Uniform Gift to Minors Act, shall be deemed to be held in a separate capacity from accounts held by such guardian, custodian or conservator in its individual capacity.

(iii) An account maintained with a debtor in the name of an executor or administrator of an estate in its capacity as such shall be deemed to be held in a separate capacity from accounts held by such executor or administrator in its individual capacity.

(iv) An account maintained with a debtor in the name of a decedent, in the name of the decedent's estate, or in the name of the executor or administrator of such estate in its capacity as such shall be deemed to be accounts held in the same capacity.

(v) An account maintained with a debtor by a trustee shall be deemed to be held in the individual capacity of the grantor of the trust unless the trust is created by a valid written instrument for a purpose other than avoidance of an offset under the regulations contained in this part. A trust account which is not deemed to be held in the individual capacity of its grantor under this paragraph (b)(2)(v) shall be deemed to be held in a separate capacity from accounts held in an individual capacity by the trustee, by the grantor or any successor in interest of the grantor, or by any trust beneficiary, and from accounts held by any other trust.

(vi) An account maintained with a debtor by a corporation, partnership, or unincorporated association shall be deemed to be held in a separate capacity from accounts held by the shareholders, partners or members of such corporation, partnership, or unincorporated association, if such entity was created for purposes other than avoidance of an offset under the regulations contained in this part.

(vii) A hedging account of a person shall be deemed to be held in the same capacity as a speculative account of such person.

(viii) Subject to paragraphs (b)(2)(ix) and (xiv) of this section, the futures accounts, foreign futures accounts, delivery accounts, and cleared swaps accounts of the same person shall not be deemed to be held in separate capacities: *Provided, however,* that such accounts may be aggregated only in accordance with paragraph (b)(3) of this section.

(ix) An omnibus customer account for public customers of a futures commission merchant maintained with a debtor shall be deemed to be held in a separate capacity from any omnibus customer account for non-public customers of such futures commission merchant and from any account maintained with the debtor on its own behalf or on behalf of any non-public customer.

(x) A joint account maintained with the debtor shall be deemed to be held in a separate capacity from any account held in an individual capacity by the participants in such account, from any account held in an individual capacity by a commodity pool operator or commodity trading advisor for such account, and from any other joint account; *provided, however,* that if such account is not transferred in accordance with §§ 190.04(a) and 190.07, it shall be deemed to be held in the same capacity as any other joint account held by identical participants and a participant's percentage interest therein shall be deemed to be held in the same capacity as any account held in an individual capacity by such participant.

(xi) An account maintained with a debtor in the name of a plan that is subject to the terms of the Employee Retirement Income Security Act of 1974 and the regulations in 29 CFR chapter XXV, or similar state, Federal, or foreign laws or regulations applicable to retirement or pension plans, shall be deemed to be held in a separate capacity from an account held in an individual capacity by the plan administrator, any employer, employee, participant, or beneficiary with respect to such plan.

(xii) Except as otherwise provided in this section, an account maintained with a debtor by an agent or nominee for a principal or a beneficial owner shall be deemed to be an account held in the individual capacity of such principal or beneficial owner.

(xiii) With respect to the cleared swaps account class, each individual cleared swaps customer account within each cleared swap omnibus customer account referred to in paragraph (b)(2)(viii) of this section shall be deemed to be held in a separate capacity from each other such individual cleared swaps customer account, subject to the provisions of paragraphs (b)(2)(i) through (xi) of this section.

(xiv) Accounts held by a customer in separate capacities shall be deemed to be accounts of different customers. The burden of proving that an account is held in a separate capacity shall be upon the customer.

(3) *Step 3-setoffs.* (i) The net equity of one customer account may not be offset against the net equity of any other customer account.

(ii) Any obligation to the debtor owed by a customer which is not required to be included in computing the equity of that customer under paragraph (b)(1) of this section (defined as x), must be deducted from any obligation to the customer owed by the debtor which is not required to be included in computing the equity of that customer (defined as y). If the former amount (x) exceeds the latter (y), the excess (x-y) must be deducted from the equity balance of the customer obtained after performing the preceding calculations required by paragraph (b) of this section, provided, that if the customer owns more than one class of accounts with a positive equity balance, the excess (again, x-y) must be allocated and offset against each positive equity balance in the same proportion as that positive equity balance bears to the total of all positive equity balances of accounts of different classes held by such customer.

(iii) A negative equity balance obtained with respect to one customer account class must be set off against a positive equity balance in any other account class of such customer held in the same capacity, provided, that if a customer owns more than one class of accounts with a positive equity balance, such negative equity balance must be offset against each positive equity balance in the same proportion as that positive equity balance bears to the total of all positive equity balances in accounts of different classes held by such customer.

(iv) To the extent any indebtedness of the debtor to the customer which is not required to be included in computing the equity of such customer under paragraph (b)(1) of this section exceeds such indebtedness of the customer to the debtor, the customer claim therefor will constitute a general creditor claim rather than a customer property claim, and the net equity therefor shall be separately calculated.

(v) The rules pertaining to separate capacities and permitted setoffs contained in this section shall only be applied subsequent to the entry of an order for relief; prior to that date, the provisions of § 1.22 of this chapter and of sections 4d(a)(2) and 4d(f) of the Act (and, in each case, the regulations in part 1, 22, or 30 of this chapter that implement sections 4d(a)(2) and 4d(f)) shall govern what setoffs are permitted.

(4) *Step 4-correction for distributions.* The value on the date of transfer or distribution of any property transferred or distributed subsequent to the filing date and prior to the primary liquidation date with respect to each class of account held by a customer must be added to the equity obtained for that customer for accounts of that class after performing the steps contained in paragraphs (b)(1) through (3) of this section: *Provided, however,* that if all accounts for which there are customer claims of record and 100% of the equity pertaining thereto is transferred in accordance with § 190.07 and section 764(b) of the Bankruptcy Code, net equity shall be computed based solely upon those allowed customer claims, if any, filed subsequent to the order for relief which are not claims of record on the filing date.

(5) *Step 5-correction for ongoing events.* Compute any adjustments to the steps in paragraphs (b)(1) through (4) of this section required to correct

misestimates or errors including, without limitation, corrections for ongoing events such as the liquidation of unliquidated claims or specifically identifiable property at a value different from the estimated value previously used in computing net equity.

(c) *Calculation of funded balance. Funded balance* means a customer's pro rata share of the customer estate with respect to each account class available for distribution to customers of the same customer class.

(1) *Funded balance computation.* The funded balance of any customer claim shall be computed (separately by account class and customer class) by:

(i) Multiplying the ratio of the amount of the net equity claim of such customer (defined as x) less the amounts referred to in paragraph (c)(1)(ii) of this section of such customer for any account class (defined as y) divided by the sum of the net equity claims of all customers for accounts of that class (defined as p) less the amounts referred to in paragraph (c)(1)(ii) of this section of all customers for accounts of that class (defined as q) (thus, ((x-y)/(p-q)) by the sum of:

(A) The value of letters of credit received, acquired, or held to margin, guarantee, secure, purchase, or sell a commodity contract relating to all customer accounts of the same class;

(B) The value of the money, securities, or other property segregated on behalf of all customer accounts of the same class less the amounts referred to in paragraph (c)(1)(ii) of this section;

(C) The value of any money, securities, or other property which must be allocated under § 190.09 to all customer accounts of the same class; and

(D) The amount of any add-back required under paragraph (b)(4) of this section; and

(ii) Then adding 100% of—

(A) Any margin payment made between the entry of the order for relief (or, in an involuntary case, the date on which the petition for bankruptcy is filed) and the primary liquidation date; *provided, however,* that if margin is posted to substitute for a letter of credit, such margin does not increase the funded balance; and

(B) For cash delivery property, any cash transferred to the trustee on or after the filing date for the purpose of paying for delivery.

(2) *Corrections to funded balance.* The funded balance must be adjusted to correct for ongoing events including, without limitation:

(i) Added claimants;

(ii) Disallowed claims;

(iii) Liquidation of unliquidated claims at a value other than their estimated value; and

(iv) Recovery of property.

(d) *Valuation.* In computing net equity, commodity contracts and other property held by or for a commodity broker must be valued as provided in this paragraph (d).

(1) *Commodity contracts*—(i) *Open contracts.* Unless otherwise specified in this paragraph (d), the value of an open commodity contract shall be equal to the settlement price as calculated by the clearing organization pursuant to its rules; *provided, however,* that if an open commodity contract is transferred to another commodity broker, its value on the debtor's books and records shall be determined as of the end of the last settlement cycle on the day preceding such transfer.

(ii) *Liquidated contracts.* Except as specified in paragraphs (d)(1)(ii)(A) and (B) of this section, the value of a commodity contract liquidated on the open market shall equal the actual value realized on liquidation of the commodity contract.

(A) *Weighted average.* If identical commodity contracts are liquidated within a 24-hour period or business day (or such other period as the bankruptcy court may determine is appropriate) as part of a general liquidation of commodity contracts, but cannot be liquidated at the same price, the trustee may use the weighted average of the liquidation prices in computing the net equity of each customer for which the debtor held such commodity contracts.

(B) *Bulk liquidation.* The value of a commodity contract liquidated as part of a bulk auction, taken into inventory or under management by a clearing organization, or similarly liquidated outside of the open market shall be equal to the settlement price calculated by the clearing organization as of the end of the settlement cycle during which the commodity contract was liquidated.

(2) *Securities.* The value of a listed security shall be equal to the closing price for such security on the exchange upon which it is traded. The value of all securities not traded on an exchange shall be equal in the case of a long position, to the average of the bid prices for long positions, and in the case of a short position, to the average of the asking prices for the short positions. If liquidated, the value of such security shall be equal to the actual value realized on liquidation of the security; *provided, however,* that if identical securities are liquidated within a 24-hour period or business day (or such other period as the bankruptcy court may determine is appropriate) as part of a general liquidation of securities, but cannot be liquidated at the same price, the trustee may use the weighted average of the liquidation prices in computing the net equity of each customer for which the debtor held such securities. Securities which are not publicly traded shall be valued by the trustee pursuant to paragraph (d)(5) of this section.

(3) *Commodities held in inventory.* Commodities held in inventory, as collateral or otherwise, shall be valued at their fair market value. If such fair market value is not readily ascertainable based upon public sources of prices, the trustee shall value such commodities pursuant to paragraph (d)(5) of this section.

(4) *Letters of credit.* The value of any letter of credit received, acquired or held to margin, guarantee, secure, purchase, or sell a commodity contract shall be its face amount, less the amount, if any, drawn and outstanding, provided that, if the trustee makes a determination in good faith that a draw on a letter of credit is unlikely to be honored on either a temporary or a permanent basis, the trustee shall value the letter of credit pursuant to paragraph (d)(5) of this section.

(5) *All other property.* Subject to the other provisions of this paragraph (d), all other property shall be valued by the trustee using such professional assistance as the trustee deems necessary in its sole discretion under the circumstances; *provided, however,* that if such property is sold, its value for purposes of the calculations required by this part shall be equal to the actual value realized on the sale of such property; and, provided further, that the sale shall be made in compliance with all applicable statutes, rules, and orders of any court or governmental entity with jurisdiction there over.

§ 190.09 Allocation of property and allowance of claims.

The property of the debtor's estate must be allocated among account classes and between customer classes as provided in this section. (Property connected with certain cross-margining arrangements is subject to the provisions of framework 1 in appendix B to this part.) The property so allocated will constitute a separate estate of the customer class and the account class to which it is allocated, and will be designated by reference to such customer class and account class.

(a) *Scope of customer property.* (1) Customer property includes the following:

(i) All cash, securities, or other property or the proceeds of such cash, securities, or other property received, acquired, or held by or for the account of the debtor, from or for the account of a customer, including a non-public customer, which is:

(A) Property received, acquired, or held to margin, guarantee, secure, purchase or sell a commodity contract;

(B) Open commodity contracts;

(C) Physical delivery property as that term is defined in paragraphs (1) through (3) in the definition of that term in § 190.01;

(D) Cash delivery property, or other cash, securities, or other property received by the debtor as payment for a commodity to be delivered to fulfill a commodity contract from or for the commodity customer account of a customer;

(E) Profits or contractual rights accruing to a customer as the result of a commodity contract;

(F) Letters of credit, including any proceeds of a letter of credit drawn by the trustee, or substitute customer property posted by the customer, pursuant to § 190.04(d)(3);

(G) Securities held in a portfolio margining account carried as a futures account or a cleared swaps customer account; or

(H) Property hypothecated under § 1.30 of this chapter to the extent that the value of such property exceeds the proceeds of any loan of margin made with respect thereto; and

(ii) All cash, securities, or other property which:

(A) Is segregated for customers on the filing date;

(B) Is a security owned by the debtor to the extent there are customer claims for securities of the same class and series of an issuer;

(C) Is specifically identifiable to a customer;

(D) Was property of a type described in paragraph (a)(1)(i)(A) of this section that is subsequently recovered by the avoidance powers of the trustee or is otherwise recovered by the trustee on any other claim or basis;

(E) Represents recovery of any debit balance, margin deficit, or other claim of the debtor against a customer;

(F) Was unlawfully converted but is part of the debtor's estate;

(G) Constitutes current assets of the debtor (as of the date of the order for relief) within the meaning of § 1.17(c)(2) of this chapter, including the debtor's trading or operating accounts and commodities of the debtor held in inventory, in the greater of—

(*1*) The amount that the debtor is obligated to set aside as its targeted residual interest amount pursuant to § 1.11 of this chapter and the debtor's residual interest policies adopted thereunder, with respect to each of the futures account class, the foreign futures account class, and the cleared swaps account class; or

(*2*) The debtor's obligations to cover debit balances or under-margined amounts as provided in §§ 1.20, 1.22, 22.2, and 30.7 of this chapter;

(H) Is other property of the debtor that any applicable law, rule, regulation, or order requires to be set aside for the benefit of customers;

(I) Is property of the debtor's estate recovered by the Commission in any proceeding brought against the principals, agents, or employees of the debtor;

(J) Is proceeds from the investment of customer property by the trustee pending final distribution;

(K) Is a payment from an insurer to the trustee arising from or related to a claim related to the conversion or misuse of customer property; or

(L) Is cash, securities, or other property of the debtor's estate, including the debtor's trading or operating accounts and commodities of the debtor held in inventory, but only to the extent that the property enumerated in paragraphs (a)(1)(i)(F) and (a)(1)(ii)(A) through (K) of this section is insufficient to satisfy in full all claims of public customers. Such property includes ''customer property,'' as defined in section 16(4) of SIPA, 15 U.S.C. 78lll(4), that remains after allocation in accordance with section 8(c)(1)(A)–(D) of SIPA, 15 U.S.C. 78fff–2(c)(1)(A)–(D) and that is allocated to the debtor's general estate in accordance with section 8(c)(1) of SIPA, 15 U.S.C. 78fff–2(c)(1).

(2) Customer property will not include:

(i) Claims against the debtor for damages for any wrongdoing of the debtor, including claims for misrepresentation or fraud, or for any violation of the Act or of the regulations in this chapter;

(ii) Other claims for property which are not based upon property received, acquired, or held by or for the account of the debtor, from or for the account of the customer;

(iii) Forward contracts (unless such contracts are cleared by a clearing organization or, in the case of forward contracts treated as foreign futures, a foreign clearing organization);

(iv) Physical delivery property that is not held by the debtor, and is delivered or received by a customer in accordance with § 190.06(a)(2) or § 190.16(a) to fulfill the customer's delivery obligation under a commodity contract;

(v) Property deposited by a customer with a commodity broker after the entry of an order for relief which is not necessary to meet the margin requirements applicable to the accounts of such customer;

(vi) Property hypothecated pursuant to § 1.30 of this chapter to the extent of the loan of margin with respect thereto;

(vii) Money, securities, or property held to margin, guarantee or secure security futures products, or accruing as a result of such products, if held in a securities account; and

(viii) Money, securities, or property held in a securities account to fulfill delivery, under a commodity contract from or for the account of a customer, as described in § 190.06(b)(2).

(3) Nothing contained in this section, including, but not limited to, the satisfaction of customer claims by operation of this section, shall prevent a trustee from asserting claims against any person to recover the shortfall of property enumerated in paragraphs (a)(1)(i)(F) and (a)(1)(ii)(A) through (L) of this section.

(b) *Allocation of customer property between customer classes.* No customer property may be allocated to pay non-public customer claims until all public customer claims have been satisfied in full. Any property segregated on behalf of or attributable to non-public customers must be treated initially as part of the public customer estate and allocated in accordance with paragraph (c)(2) of this section.

(c) *Allocation of customer property among account classes*—(1) *Property identified to an account class*—(i) *Segregated property.* Subject to paragraph (b) of this section, property held by or for the account of a customer, which is segregated on behalf of a specific account class, or readily traceable on the filing date to customers of such account class, or recovered by the trustee on behalf of or for the benefit of an account class, must be allocated to the customer estate of the account class for which it is segregated, to which it is readily traceable, or for which it is recovered.

(ii) *Excess property.* If, after payment in full of all allowed customer claims in a particular account class, any property remains allocated to that account class, such excess shall be allocated in accordance with paragraph (c)(2) of this section.

(2) *All other property.* Money, securities, and property received from or for the account of customers which cannot be allocated in accordance with

paragraph (c)(1)(i) of this section, must be allocated in the following order:

(i) To the estate of the account class for which, after the allocation required in paragraph (c)(1) of this section, the percentage of each public customer net equity claim which is funded is the lowest, until the funded percentage of net equity claims of such class equals the percentage of each public customer's net equity claim which is funded for the account class with the next lowest percentage of the funded claims; and then

(ii) To the estate of the two account classes referred to in paragraph (c)(2)(i) of this section so that the percentage of the net equity claims which are funded for each class remains equal until the percentage of each public customer net equity claim which is funded equals the percentage of each public customer net equity claim which is funded for the account class with the next lowest percentage of funded claims, and so forth, until the percentage of each public customer net equity claim which is funded is equal for all classes of accounts; and then,

(iii) Among account classes in the same proportion as the public customer net equity claims for each such account class bears to the total of public customer net equity claims of all account classes until the public customer claims of each account class are paid in full; and, thereafter,

(iv) To the non-public customer estate for each account class in the same order as is prescribed in paragraphs (c)(2)(i) through (iii) of this section for the allocation of the customer estate among account classes.

(d) *Distribution of customer property*—(1) *Return or transfer of specifically identifiable property.* Specifically identifiable property not required to be liquidated under § 190.04(d)(2) may be returned or transferred on behalf of the customer to which it is identified:

(i) If it is margining an open commodity contract, only if substitute customer property is first deposited with the trustee with a value equal to the greater of the full fair market value of such property on the return date or the balance due on the return date on any loan by the debtor to the customer for which such property constitutes security; or

(ii) If it is not margining an open commodity contract, at the option of the customer, either pursuant to the terms of paragraph (d)(1)(i) of this section, or pursuant to the following terms: Such customer first deposits substitute customer property with the trustee with a value equal to the amount by which the greater of the value of the specifically identifiable property to be transferred or returned on the date of such transfer or return or the balance due on the return date on any loan by the debtor to the customer for which such property constitutes security, together with any other disbursements made, or to be made, to such customer, plus a reasonable reserve in the trustee's sole discretion, exceeds the estimated aggregate of the funded balances for each class of account of such customer less the value on the date of its transfer or return of any property transferred or returned prior to the primary liquidation date with respect to the customer's net equity claim for such account; *provided, however,* that adequate security to assure the recovery of any overpayments by the trustee is provided to the debtor's estate by the customer.

(2) *Transfers of specifically identifiable commodity contracts under section 766 of the Bankruptcy Code.* Any open commodity contract that is specifically identifiable property and which is not required to be liquidated under § 190.04(d), and which is not otherwise liquidated, may be transferred on behalf of a public customer, *provided, however,* that such customer must first deposit substitute customer property with the trustee with a value equal to the amount by which the equity to be transferred to margin such contract together with any other transfers or returns of specifically identifiable property or disbursements made, or to be made, to such customer, plus a reasonable reserve in the trustee's sole discretion, exceeds the estimated aggregate of the funded balances for each class of account of such customer less the value on the date of its transfer or return of any property transferred or returned prior to the primary liquidation date with respect to the customer's net equity claim for such account; and, provided further, that adequate security to assure the recovery of any overpayments by the trustee is provided to the debtor's estate by the customer.

(3) *Distribution in kind of specifically identifiable securities.* If any securities of a customer are specifically identifiable property as defined in paragraph (1)(i)(A) of the definition of that term in § 190.01 of this chapter, but the customer has no open commodity contracts, the customer may request that the trustee purchase or otherwise obtain the largest whole number of like-kind securities (*i.e.,* securities of the same class and series of an issuer), with a fair market value (inclusive of transaction costs) which does not exceed that portion of the funded balance of such customer's allowed net equity claim that constitutes a claim for securities, if like-kind securities can be purchased in a fair and orderly manner.

(4) *Proof of customer claim.* No distribution shall be made pursuant to paragraphs (d)(1) and (3) of this section prior to receipt of a completed proof of customer claim as described in § 190.03(e) or (f).

(5) *No differential distributions.* No further disbursements may be made to customers with respect to a particular account class for whom transfers have been made pursuant to § 190.07 and paragraph (d)(2) of this section, until a percentage of each net equity claim equivalent to the percentage distributed to such customers is distributed to all public customers in such account class. Partial distributions, other than the transfers referred to in § 190.07 and paragraph (d)(2) of this section, with respect to a particular account class made prior to the final net equity determination date must be made pursuant to a preliminary plan of distribution approved by the court, upon notice to the parties and to all customers, which plan requires adequate security to the debtor's estate to assure the recovery of any overpayments by the trustee and distributes an equal percentage of net equity to all public customers in such account class.

§ 190.10 Current records during business as usual.

A person that is a futures commission merchant is required to maintain current records relating to its customers' accounts, including copies of all account agreements and related account documentation, and ''know your customer'' materials, pursuant to §§ 1.31, 1.35, 1.36, and 1.37 of this chapter, which may be provided to another futures commission merchant to facilitate the transfer of open commodity contracts or other customer property held by such person for or on behalf of its customers to the other futures commission merchant, in the event an order for relief is entered with respect to such person.

Subpart C—Clearing Organization as Debtor

§ 190.11 Scope and purpose of this subpart.

(a) This subpart applies to a proceeding commenced under subchapter IV of chapter 7 of the Bankruptcy Code in which the debtor is a clearing organization.

(b) If the debtor clearing organization is organized outside the United States, and is subject to a foreign proceeding, as defined in 11 U.S.C. 101(23), in the jurisdiction in which it is organized, then only the following provisions of this part shall apply:

(1) Subpart A.

(2) Section 190.12.

(3) Section 190.13, but only with respect to futures contracts and cleared swaps contracts cleared by FCM clearing members on behalf of their public customers and the property margining or securing such contracts.

(4) Sections 190.17 and 190.18, but only with respect to claims of FCM clearing members on behalf of their public customers, as well as to property that is or should have been segregated for the benefit of FCM clearing members' public customers, or that has been recovered for the benefit of FCM clearing members' public customers.

§ 190.12 Required reports and records.

(a) *Notices*—(1) *Means of providing*—(i) *To the Commission.* Unless instructed otherwise by the Commission, all mandatory or discretionary notices to be given to the Commission under this subpart shall be directed by electronic mail to *bankruptcyfilings@cftc.gov.* For purposes of this subpart, notice to the Commission shall be deemed to be given only upon actual receipt.

(ii) *To members.* The trustee, after consultation with the Commission, and unless otherwise instructed by the Commission, will establish and follow procedures reasonably designed for giving adequate notice to members under this subpart and for receiving claims or other notices from members. Such procedures should include, absent good cause otherwise, the use of a prominent website as well as communication to members' electronic addresses that are available in the debtor's books and records.

(2) *Of commencement of a proceeding.* A debtor that files a petition in bankruptcy that is subject to this subpart shall, at or before the time of such filing, and a debtor against which such a petition is filed shall, as soon as possible, but in any event no later than three hours after the receipt of notice of such filing, notify the Commission of the filing date, the court in which the proceeding has been or will be filed, and, as soon as available, the docket number assigned to that proceeding by the court.

(b) *Reports and records to be provided to the trustee and the Commission within three hours.* (1) As soon as practicable following the commencement of a proceeding that is subject to this subpart and in any event no later than three hours following the later of the commencement of such proceeding or the appointment of the trustee, the debtor shall provide to the trustee copies of each of the most recent reports that the debtor was required to file with the Commission under § 39.19(c) of this chapter, including copies of any reports required under § 39.19(c)(2), (3), and (4) of this chapter (including the most up-to-date version of any recovery and wind-down plans of the debtor maintained pursuant to § 39.39(b) of this chapter) that the debtor filed with the Commission during the preceding 12 months.

(2) As soon as practicable following the commencement of a proceeding that is subject to this subpart and in any event no later than three hours following the commencement of such proceeding (or, with respect to the trustee, the appointment of the trustee), the debtor shall provide to the trustee and the Commission copies of the most up-to-date versions of the default management plan and default rules and procedures maintained by the debtor pursuant to § 39.16 and, as applicable, § 39.35 of this chapter.

(c) *Records to be provided to the trustee and the Commission by the next business day.* As soon as practicable following commencement of a proceeding that is subject to this subpart and in any event no later than the next business day, the debtor shall make available to the trustee and the Commission copies of the following records:

(1) All records maintained by the debtor described in § 39.20(a) of this chapter; and

(2) Any opinions of counsel or other legal memoranda provided to the debtor (whether by external or internal counsel) in the five years preceding the commencement of such proceeding relating to the enforceability of the rules and procedures of the debtor in the event of an insolvency proceeding involving the debtor.

§ 190.13 Prohibition on avoidance of transfers.

The following transfers are approved and may not be avoided under sections 544, 546, 547, 548, 549, or 724(a) of the Bankruptcy Code:

(a) *Pre-relief transfers.* Any transfer of open commodity contracts and the property margining or securing such contracts made to another clearing organization that was approved by the Commission, either before or after such transfer, and was made prior to entry of the order for relief; and

(b) *Post-relief transfers.* Any transfers of open commodity contracts and the property margining or securing such contracts made to another clearing organization on or before the seventh calendar day after the entry of the order for relief, that was made with the approval of the Commission, either before or after such transfer.

§ 190.14 Operation of the estate of the debtor subsequent to the filing date.

(a) *Proofs of claim.* The trustee may, in its discretion based upon the facts and circumstances of the case, instruct each customer to file a proof of claim containing such information as is deemed appropriate by the trustee, and seek a court order establishing a bar date for the filing of such proofs of claim.

(b) *Operation of the derivatives clearing organization.* Subsequent to the order for relief, the derivatives clearing organization shall cease making calls for variation settlement or initial margin.

(c) *Liquidation.* (1) The trustee shall liquidate all open commodity contracts that have not been terminated, liquidated, or transferred no later than seven calendar days after entry of the order for relief. Such liquidation of open commodity contracts shall be conducted in accordance with the rules and procedures of the debtor, to the extent applicable and practicable.

(2) In lieu of liquidating securities held by the debtor and making distributions in the form of cash, the trustee may, in its reasonable discretion, make distributions in the form of securities that are equivalent (*i.e.,* securities of the same class and series of an issuer) to the securities originally delivered to the debtor by a clearing member or such clearing member's customer.

(d) *Computation of funded balance.* The trustee shall use reasonable efforts to compute a funded balance for each customer account immediately prior to any distribution of property within the account, which shall be as accurate as reasonably practicable under the circumstances, including the reliability and availability of information.

§ 190.15 Recovery and wind-down plans; default rules and procedures.

(a) *Prohibition on avoidance of actions taken pursuant to recovery and wind-down plans.* Subject to the provisions of section 766 of the Bankruptcy Code and §§ 190.13 and 190.18, the trustee shall not avoid or prohibit any action taken by a debtor subject to this subpart that was reasonably within the scope of and was provided for in any recovery and wind-down plans maintained by the debtor and filed with the Commission pursuant to § 39.39 of this chapter.

(b) *Implementation of debtor's default rules and procedures.* In administering a proceeding under this subpart, the trustee shall implement, in consultation with the Commission, the default rules and procedures maintained by the debtor under § 39.16 and, as applicable, § 39.35 of this chapter and any termination, close-out and liquidation provisions included in the rules of the debtor, subject to the reasonable discretion of the trustee and to the extent that implementation of such default rules and procedures is practicable.

(c) *Implementation of recovery and wind-down plans.* In administering a proceeding under this subpart, the trustee shall, in consultation with the Commission, take actions in accordance with any recovery and wind-down plans maintained by the debtor and filed with the Commission pursuant to § 39.39 of this chapter, to the extent reasonable and practicable, and consistent with the protection of customers.

§ 190.16 Delivery.

(a) *General.* In the event that a commodity contract, cleared by the derivatives clearing organization, that settles upon expiration or exercise by making or taking delivery of physical delivery property, has moved into delivery position prior to the date and time of the order for relief, or moves into delivery position after that date and time, but before being terminated, liquidated, or transferred, then, in either such event, the trustee must use reasonable efforts to facilitate and cooperate with the completion of delivery on behalf of the clearing member or the clearing member's customer in a manner consistent with § 190.06(a) and the pro rata distribution principle addressed in § 190.00(c)(5).

(b) *Special provisions for delivery accounts.* (1) Consistent with the separation of the physical delivery property account class and the cash delivery account class set forth in § 190.06(b), the trustee shall treat—

(i) Physical delivery property held in delivery accounts as of the filing date, along with the proceeds from any subsequent sale of such physical delivery property in accordance with § 190.06(a)(3) to fulfill a clearing member's or its customer's delivery obligation or any other subsequent sale of such property, as part of the physical delivery account class; and

(ii) Cash delivery property in delivery accounts as of the filing date, along with any physical delivery property for which delivery is subsequently taken on behalf of a clearing member or its customer in accordance with § 190.06(a)(3), as part of the separate cash delivery account class.

(2) If the debtor holds any cash or property in the form of cash equivalents in an account with a bank or other person under a name or in a manner that clearly indicates that the account holds property for the purpose of making payment for taking physical delivery, or receiving payment for making physical delivery, of a commodity under any commodity contracts, such property shall (subject to § 190.19) be considered customer property in the cash delivery account class if held for making payment for taking delivery, or in the physical delivery account class, if held for the purpose of receiving such payment.

§ 190.17 Calculation of net equity.

(a) *Net equity–separate capacities and calculations.* (1) If a member of the clearing organization clears trades in commodity contracts through a commodity contract account carried by the debtor as a customer account for the benefit of the clearing member's public customers and separately through a house account, the clearing member shall be treated as having customer claims against the debtor in separate capacities with respect to the customer account and house account at the clearing organization, and by account class. A member shall be treated as part of the public customer class with respect to claims based on any commodity customer accounts carried as ''customer accounts'' by the clearing organization for the benefit of the member's public customers, and as part of the non-public customer class with respect to claims based on its house account.

(2) Net equity shall be calculated separately for each separate customer capacity in which the clearing member has a claim against the debtor, *i.e.,* separately by the member's customer account and house account and by account class.

(b) *Net equity—application of debtor's loss allocation rules and procedures.* (1)(i) The calculation of a clearing member's net equity claim shall include the full application of the debtor's loss allocation rules and procedures, including the default rules and procedures referred to in § 39.16 and, if applicable, § 39.35 of this chapter.

(ii) The calculation in paragraph (b)(1)(i) of this section will include, with respect to the clearing member's house account, any assessments or similar loss allocation arrangements provided for under those rules and procedures that were not called for before the filing date, or, if called for, have not been paid. Such loss allocation arrangements shall be applied to the extent necessary to address losses arising from default by clearing members.

(2) Appropriate adjustments shall be made to the net equity claims of the clearing members that are so entitled under the following circumstances: Where the debtor's loss allocation rules and procedures would entitle clearing members to additional payments of cash or other property due to—

(i) Portions of mutualized default resources that are prefunded, or assessed and collected, but in either event not used; or

(ii) The debtor's recoveries on claims against others (including, but not limited to, recoveries on claims against clearing members who have defaulted on their obligations to the debtor).

(c) *Net equity—general.* Subject to paragraph (b) of this section, net equity shall be calculated in the manner provided in § 190.08, to the extent applicable.

(d) *Calculation of funded balance. Funded balance* means a clearing member's pro rata share of customer property other than member property (for accounts for a clearing member's customer accounts) or member property (for a clearing member's house accounts) with respect to each account class available for distribution to customers of the same customer class, calculated in the manner provided in § 190.08(c) to the extent applicable.

§ 190.18 Treatment of property.

(a) *General.* The property of the debtor's estate must be allocated between member property and customer property other than member property as provided in this section to satisfy claims of clearing members, as customers of the debtor. The property so allocated will constitute a separate estate of the customer class (*i.e.,* member property, and customer property other than member property) and the account class to which it is allocated, and will be designated by reference to such customer class and account class.

(b) *Scope of customer property.* Customer property is the property available for distribution within the relevant account class in respect of claims by clearing members, as customers of the clearing organization, based on customer accounts carried by the debtor for the benefit of such members' public customers or, considered separately, such members' house accounts.

(1) Customer property includes the following:

(i) All cash, securities, or other property, or the proceeds of such cash, securities, or other property, that is received, acquired, or held by or for the account of the debtor, from or for any commodity contract account of a clearing member carried by the debtor, which is:

(A) Property received, acquired, or held, in order to margin, guarantee, secure, purchase, or sell a commodity contract;

(B) Open commodity contracts;

(C) Physical delivery property as that term is defined in paragraphs (1) through (3) of the definition of that term in § 190.01;

(D) Cash, securities or other property received by the debtor as payment for a commodity to be delivered to fulfill a commodity contract from or for the commodity customer account of a clearing member or a customer of a clearing member;

(E) Profits or contractual rights accruing as a result of a commodity contract;

(F) Letters of credit, including any proceeds of a letter of credit drawn upon by the trustee, or substitute customer property posted by a clearing member or a customer of a clearing member, pursuant to § 190.04(d)(3); or

(G) Securities held in a portfolio margining account carried as a futures account or a cleared swaps customer account;

(ii) All cash, securities, or other property which:

(A) Is segregated by the debtor on the filing date for the benefit of clearing members' house accounts or clearing members' public customer accounts;

(B) Was of a type described in paragraph (b)(1)(i)(A) of this section that is subsequently recovered by the avoidance powers of the trustee or is otherwise recovered by the trustee on any other claim or basis;

(C) Represents a recovery of any debit balance, margin deficit or other claim of the debtor against any commodity contract account carried for the benefit of a member's house accounts or a member's public customer accounts;

(D) Was unlawfully converted but is part of the debtor's estate; or

(E) Was of a type described in paragraphs (a)(1)(ii)(H) through (K) of § 190.09 (as if the term debtor used therein refers to a clearing organization as debtor);

(iii) Any guaranty fund deposit, assessment, or similar payment or deposit made by a clearing member, or recovered by the trustee, to the extent any remains following administration of the debtor's default rules and procedures, and any other property of a member available under the debtor's rules and procedures to satisfy claims made by or on behalf of public customers of a member; and

(iv) Amounts of its own funds that the debtor had committed as part of its loss allocation rules, to the extent that such amounts have not already been applied under such rules.

(2) Customer property will not include property of the type described in § 190.09(a)(2), as if the term debtor used therein refers to a clearing organization and to the extent relevant to a clearing organization.

(c) *Allocation of customer property between customer classes.* (1) Where the funded balance for members' house accounts is greater than one hundred percent with respect to any account class:

(i) Any excess should be allocated to customer property other than member property to the extent that the funded balance is less than one hundred percent of net equity claims for members' public customers in any account class; and

(ii) Any remaining excess after the application of paragraph (c)(1)(i) of this section should be allocated to member property to the extent that the funded balance is less than one hundred percent of net equity claims for members' house accounts in any other account class.

(2) Where the funded balance for members' public customers in any account class is greater than one hundred percent:

(i) Any excess should be allocated to customer property other than member property to the extent that the funded balance is less than one hundred percent of net equity claims for members' public customers in any other account class; and

(ii) Any remaining excess after the application of paragraph (c)(2)(i) of this section should be allocated to member property to the extent that the funded balance is less than one hundred percent of net equity claims for members' house accounts in any account class.

(d) *Allocation of customer property among account classes*—(1) *Segregated property.* Subject to paragraph (b) of this section, property held by or for the account of a customer, which is segregated on behalf of a specific account class within a customer class, or readily traceable on the filing date to customers of such account class within a customer class, or recovered by the trustee on behalf of or for the benefit of an account class within a customer class, must be allocated to the customer estate of the account class for which it is segregated, to which it is readily traceable, or for which it is recovered.

(2) *All other property.* Customer property which cannot be allocated in accordance with paragraph (d)(1) of this section, shall be allocated within customer classes, but between account classes, in the following order:

(i) To the estate of the account class for which the percentage of each members' net equity claim which is funded is the lowest, until the funded percentage of net equity claims of such account class equals the percentage of each members' net equity claim which is funded for the account class with the next lowest percentage of the funded claims; and then

(ii) To the estate of the two account classes so that the percentage of the net equity claims which are funded for each such account class remains equal until the percentage of each net equity claim which is funded equals the percentage of each net equity claim which is funded for the account class with the next lowest percentage of funded claims, and so forth, until all account classes within the customer class are fully funded.

(e) *Accounts without separation by account class.* Where the debtor has, prior to the order for relief, kept initial margin for house accounts in accounts without separation by account class, then member property will be considered to be in a single account class.

(f) *Assertion of claims by trustee.* Nothing in this section, including, but not limited to, the satisfaction of customer claims by operation of this section, shall prevent a trustee from asserting claims against any person to recover the shortfall of property enumerated in paragraphs (b)(1)(i)(E) and (b)(1)(ii) and (iii) of this section.

§ 190.19 Support of daily settlement.

(a) Notwithstanding any other provision of this part, funds received (whether from clearing members' house or customer accounts) by a debtor clearing organization as part of the daily settlement required pursuant to § 39.14 of this chapter shall, upon and after an order for relief, be included as customer property that is reserved for and traceable to, and promptly shall be distributed to, members entitled to payments of such funds with respect to such members' house and customer accounts as part of that same daily settlement. Such funds when received, other than deposits of initial margin described in § 39.14(a)(1)(iii) of this chapter, shall be considered member property and, separately, customer property other than member property, in proportion to the ratio of total gains in member accounts with net gains, and total gains in clearing members' customer accounts with net gains, respectively. Deposits of initial margin described in § 39.14(a)(1)(iii) of this chapter shall be considered member property and, separately, customer property other than member property, to the extent deposited on behalf of, respectively, clearing members' house accounts and customer accounts.

(b) To the extent there is a shortfall in funds received pursuant to paragraph (a) of this section:

(1) Such funds shall be supplemented with the property described in paragraphs (b)(1)(i) through (iv) of this section, as applicable, to the extent necessary to meet the shortfall, in accordance with the derivatives clearing organization's default rules and procedures adopted pursuant to § 39.16 and, as applicable, § 39.35 of this chapter, and (with respect to paragraph (b)(1)(ii) of this section) any recovery and wind-down plans maintained pursuant to § 39.39 of this chapter and submitted pursuant to § 39.19 of this chapter. Such funds shall be included as member property and customer property other than member property in the proportion described in paragraph (a) of this section, and shall be distributed promptly to members' house accounts and members' customer accounts which accounts are entitled to payment of such funds as part of that daily settlement.

(i) Initial margin held for the account of a member, including initial margin segregated for the customers of such member, that has defaulted on payments required pursuant to a daily settlement, but only to the extent that such margin is permitted to be used pursuant to parts 1, 22, and 30 of this chapter.

(ii) Assets of the debtor, to the extent dedicated to such use as part of the debtor's default rules and procedures, and any recovery and wind-down plans, described in this paragraph (b)(1).

(iii) Prefunded guarantee or default funds maintained pursuant to the debtor's default rules and procedures.

(iv) Payments made by members pursuant to assessment powers maintained pursuant to the debtor's default rules and procedures.

(2) If the funds that are included as customer property pursuant to paragraph (a) of this section, supplemented as described in paragraph (b)(1) of this section, are insufficient to pay in full members entitled to payment of such funds as part of daily settlement, then such funds shall be distributed pro rata to such members' house accounts and customer accounts in proportion to the ratio of total gains in member accounts with net gains, and total gains in customer accounts with net gains, respectively.

Appendix A to Part 190—Customer Proof of Claim Form

[CASE CAPTION]

CLAIM FORM FOR COMMODITY BROKER CUSTOMERS OF [DEBTOR]

<table>
<tr><td>Debtor: [INSERT]</td><td></td></tr>
<tr><td>Customer Name:</td><td>COURT USE ONLY</td></tr>
<tr><td>Account Number(s):

Daytime Telephone number:

Email:</td><td>❒ Check this box if this claim amends a previously filed claim.

Court Claim Number:____________________
(If known)

Filed on:______________________</td></tr>
<tr><td>Name and address where payment should be sent (if different from above):

Telephone number:

Email:</td><td>❒ Check this box if you are aware that anyone else has filed a proof of claim relating to this claim. Attach copy of statement giving particulars.</td></tr>
</table>

THIS CLAIM FORM SHOULD BE USED ONLY IF YOU ARE A CUSTOMER HOLDING A CLAIM BASED ON A COMMODITY CONTRACT ACCOUNT (A FUTURES, FOREIGN FUTURES, CLEARED SWAPS OR DELIVERY ACCOUNT) AT THE DEBTOR. A DIFFERENT CLAIM FORM MUST BE USED TO ASSERT OTHER TYPES OF CLAIMS AGAINST THE DEBTOR.

THE DEADLINE FOR FILING ALL CUSTOMER CLAIMS BASED ON COMMODITY CONTRACT ACCOUNTS IS [BAR DATE]. NO CUSTOMER CLAIM WILL BE ALLOWED IF IT IS RECEIVED AFTER THIS DATE. CLAIMS MUST BE RECEIVED BY 11:59 P.M. ([TIME ZONE]) ON _________________ TO BE CONSIDERED TIMELY.

[Include case-specific instructions for how to file a claim]

If you require additional space to answer any question, please attach separate pieces of paper and label the answers to the corresponding questions.

I. CLAIM AMOUNT

For each type of commodity contract account that is applicable, state the amount of your claim against the Debtor.

(1) Futures account claim: $__________[§ 190.03(e)(1)][331]

(2) Foreign futures account claim: $__________[§ 190.03(e)(1)]

(3) Cleared swaps account claim: $__________[§ 190.03(e)(1)]

(4) Delivery account claim: $__________[§ 190.03(e)(1)]

Of the amount in (4), please note how much is in the form of cash or cash equivalents ($) and how much is the value of commodities that have been or were/are to be delivered ($_________)

(5) Total claim: $__________________________

(6) Date on which your claim is valued (*see instructions*): _____________________

II. ACCOUNT INFORMATION

For each commodity contract account with the Debtor, please provide the following information. To the extent you have multiple commodity contract accounts with the Debtor, please provide the following information for each account separately in an attachment.

(1) Account number: ___________________[§ 190.03(e)(3)(i)]

(2) Name in which the account is held: ______________________[§ 190.03(e)(3)(ii)]

(3) Please specify all capacities in which you hold the account (check all that are applicable) [§ 190.03(e)(3)(iv)]:

☐ a. Individual capacity

☐ b. Guardian, custodian, or conservator for the benefit of a ward or a minor under the Uniform Gift to Minors Act

☐ c. Executor or administrator of an estate

☐ d. Trustee for a trust beneficiary

☐ e. Corporation, partnership, or unincorporated association

☐ f. Omnibus customer account of a futures commission merchant

☐ g. Part owner of a joint account

☐ h. Individual retirement account

[331] Bracketed references are to the corresponding provision in § 190.03(e) where the relevant information item is listed.

☐ i. Agent or nominee for a principal or beneficial owner (and not described in Items (a)-(h))

☐ j. In any other capacity not described above in Items (a)-(i) (please specify the capacity): ___________________________________

If you selected more than one box, please attach an explanation.

(4) Please specify whether the account is a joint account [§ 190.03(e)(3)(v)]:

Check one: ☐ YES ☐ NO

If you selected "YES," please specify your percentage interest in the account, and whether all participants in the joint account are claiming jointly. In addition, please see the instructions for additional information required for joint accounts.

a. My percentage interest in the joint account is: _______%

b. Participants in the joint account are claiming:

Check one: ☐ SEPARATELY ☐ JOINTLY

(5) Please specify whether the account is a discretionary account (*i.e.*, does another person have trading authority over the account) [§ 190.03(e)(3)(vi)]:

Check one: ☐ YES ☐ NO

If you selected "YES," please see the instructions for additional information required for discretionary accounts.

(6) Please specify whether the account is an individual retirement account for which there is a custodian [§ 190.03(e)(3)(vii)]:

Check one: ☐ YES ☐ NO

1. If you selected "YES," please see the instructions for additional information required for individual retirement accounts for which there is a custodian.

(7) Please specify whether the account is a cross-margining account for futures and securities [§ 190.03(e)(3)(viii)]:

Check one: ☐ YES ☐ NO

If you selected "YES," please see the instructions for additional information required for cross-margining accounts for futures and securities.

III. ACCOUNT STATEMENT: OPEN POSITIONS, UNLIQUIDATED SECURITIES AND OTHER UNLIQUIDATED PROPERTY

(1) Account balance per most recent account statement: $_______ [§ 190.03(e)(3)(iii)]

a. Date of the most recent account statement: ___________________________

PLEASE ATTACH A* COPY *OF THIS STATEMENT (NOT THE ORIGINAL)

b. Do you agree with the account balance(s) on your most recent account statement(s), as set forth above?

Check one: ☐ YES ☐ NO

If you selected "NO," please explain in an attachment the reasons why you disagree with the account balance reflected on your most recent statement.

c. Has there been activity in the account since the date of the last account statement up to and including the filing date that has affected the balance of the account ("subsequent activity")?

Check one: ☐ YES ☐ NO

If you selected "YES," please provide full information regarding any such subsequent activity in an attachment.

(2) On the date on which your claim is valued, did you have any open positions, unliquidated securities and/or other unliquidated property in or associated with any of your commodity contract accounts? [§ 190.03(e)(7)]

2. **Check one:** ☐ YES ☐ NO

If you selected "YES," please state below the value of your open positions, unliquidated securities and/or other unliquidated property. In addition, please see the instructions for additional information required regarding open positions, unliquidated securities and other unliquidated property.

Value of all open positions, unliquidated securities and/or other unliquidated property: $__________________________

(3) To the extent you are claiming unliquidated securities or other unliquidated property held in your account, do you wish to receive payment in kind, if possible? [§ 190.03(e)(9)]

Check one: ☐ YES ☐ NO

If you selected "YES," please see the instructions for additional required information.

IV. CONNECTIONS WITH THE DEBTOR [§ 190.03(e)(2)]

(1) Is the customer making this claim one of the following persons (check all that are applicable):

☐ a. Officer, director, general partner or owner of ten percent or more of the capital stock of the Debtor.

☐ b. An employee, limited partner or special partner of the Debtor whose duties include (1) the management of the business of the Debtor or any part thereof; (2) the handling of the trades or customer funds; (3) the keeping of records pertaining to the trades or funds of customers; or (4) the signing or cosigning of checks or drafts on behalf of Debtor.

☐ c. A spouse or minor dependent living in the same household as any person listed in this section.

☐ d. A business affiliate that directly or indirectly controls the Debtor, or is directly or indirectly controlled by or is under common control with the Debtor.

(2) Is the customer making the claim on behalf of any account that is owned 10% or more by the Debtor or by any of the persons, alone or jointly, identified in IV.(1)?

Check one: ☐ YES ☐ NO

If you selected "YES," please identify such person(s) and the category identified in IV.(1) under which they fit.

V. SECURITY FUTURES PRODUCTS [§ 190.03(e)(8)][332]

Is any portion of your claim based on security futures products (i.e. futures whose underlying instrument is either a single security or a narrow-based security index) held in a securities account with the Debtor?

Check one: ☐ **YES** ☐ **NO**

If you selected "YES," you will need to file a separate claim in accordance with the procedures established for claims based on securities accounts at the Debtor.

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[332] This section is for use only in cases where the debtor is jointly registered as a futures commission merchant and securities broker-dealer.

VI. **OTHER ACCOUNTS WITH DEBTOR** [§ 190.03(e)(4)]

Do you have any accounts with the Debtor that are not commodity contract accounts listed in response to Section III above?

Check one: ☐ YES ☐ NO

If you selected "YES," specify the other account number(s) and the type of each such account.

Account Number	Type of Account
1. ______________________	______________________
2. ______________________	______________________

(Attach additional page(s) if necessary)

VII. **OTHER CLAIMS AGAINST DEBTOR** [§ 190.03(e)(5)]

Do you have any other claims against the Debtor not already taken into account in the claim and account information provided in response to Sections I, II, III and VI above?

Check one: ☐ YES ☐ NO

If you selected "YES," please provide a detailed description in an attachment of any such claim or claims, and attach any supporting documentation you have.

VIII. **AMOUNTS OWED TO DEBTOR** [§ 190.03(e)(6)]

Do you owe any amounts to the Debtor not already taken into account in the claim and account balance information provided in response to the questions in sections I and II above?

Check one: YES ☐ NO ☐

If you selected "YES," please provide a detailed description in an attachment of any such claim or claims, and attach any supporting documentation you have.

IX. VERIFICATION

CHECK THE APPROPRIATE BOX:

❒ I am the customer ❒ I am the customer's authorized agent.

❒ I am a guarantor, surety, indorser
or other (See Bankruptcy Rule 3005.)

I declare under penalty of perjury that the information provided in this claim is true and correct to the best of my knowledge, information, and reasonable belief.

Print Name: ____

Title: ____

Company: ____

Address and telephone number (if different from notice address above):

____

____

____

Telephone number:__________________________________

Email:____

____
Signature (Date)

Penalty for presenting fraudulent claim: Fine of up to $500,000 or imprisonment for up to 5 years, or both. 18 U.S.C. §§ 152 and 3571.

INSTRUCTIONS FOR CUSTOMER PROOF OF CLAIM FORM	
Customer's Name and Address: Fill in the name of the person or entity asserting the claim, and the name and address of the person who should receive notices issued during the bankruptcy case. A separate space is provided for the payment address if it differs from the notice address. The customer has a continuing obligation to keep the court informed of its current address. See Federal Rule of Bankruptcy Procedure (FRBP) 2002(g).	**Date on Which Claim is Valued:** Your claim should be valued as of [the last date on which any contracts or property not liquidated to cash balances remained in your account. Do not include the value of any contracts, funds or other property transferred to another commodity broker] [^, the date established by the Court as the date on which customer accounts should be valued].
• **Types of Customer Accounts**: • A "futures account" is an account opened for the purpose of trading futures or options on futures on a U.S. futures exchange. Your account statement for a "futures account" would typically include the term "SEG" in the title or description of the account. • A "foreign futures account" is an account opened for the purpose of trading futures or options on futures on an exchange located outside the U.S. Your account statement for a "foreign futures account" would typically include the term "30.7" in the title or description of the account. • A "cleared swaps account" is an account opened for the purpose of holding swaps traded bilaterally or in off-exchange markets that are submitted to a CFTC-registered derivatives clearing organization for settlement and clearing. A "cleared swaps account" also is an account opened for the purpose of trading swaps or options on swaps on a designated contract market or swap execution facility and cleared by a CFTC-registered derivatives clearing organization. Your account statement for a "cleared swaps account" would typically include the term "swap" in the title or description of the account. • A "delivery account" is an account denominated as such and through which deliveries of commodities, whether tangible or intangible, occur or have occurred under expiring futures contracts. A delivery account also may hold cash balances, title documents for commodities such as metals warehouse receipts, or other commodities, whether tangible or intangible, that are deliverable under an exchange's futures contract. • Your account statement may include multiple types of customer accounts in a single account statement.	**Estimated Claim Amount**: If you cannot compute the amount of your claim, you **must** file an estimated claim. In that case, please be sure to indicate that your claim is an estimated claim. **Joint Accounts:** If any commodity contract account for which you are making a claim is a joint account, please include an attachment listing the account number and the name, address and contact information for each joint account holder other than yourself. If you are making a claim with respect to multiple joint accounts, and those joint accounts are not owned by the same holders in the same legal capacities and in identical ownership percentages, please complete a separate claim form for each joint account. **Discretionary Accounts:** If any commodity contract account for which you are making a claim is a discretionary account, please include an attachment listing the account number and the name, address, and contact information for all persons with trading authority over any of those accounts. If different persons have trading authority over different accounts, please provide this information for each such account, listing applicable account numbers. **Individual Retirement Accounts for which there is a Custodian:** If any commodity contract account for which you are making a claim is an individual retirement account for which there is a custodian, please include an attachment listing the account number and the name, address, and contact information for both the custodian and the account owner. **Cross-Margining Accounts for Futures and Securities:** If any commodity contract account for which you are making a claim is a cross-margining account for futures and securities, please include an attachment listing the account number and whether the securities positions are held in an account with the debtor or in an account with an affiliate of the debtor. If such positions are held in an account with an affiliate of the debtor, please identify and include contact information for such affiliate.

Other types of derivatives trading accounts that you may have with the debtor, such as accounts holding off-exchange retail forex positions subject to part 5 of the regulations of the CFTC and funds to margin such positions, are not customer accounts entitled to special protection under the Bankruptcy Code. **Claim in foreign currencies**: If some or all of your claim is based on a currency other than U.S. dollars, please file you claim in U.S. dollars based on the exchange rate in effect as of the petition date ([INSERT]), and identify the exchange rate used in calculating your claim in a separate attachment.	
Open positions, Unliquidated Securities and Other Unliquidated Property: To the extent you have any open positions, unliquidated securities and/or other unliquidated property in a commodity contract account, please include an attachment (i) describing each such open position, unliquidated security and/or other item of unliquidated property (*e.g.*, for positions, by contract, delivery date, long/short, quantity, and strike price for options; for securities, by CUSIP and quantity); (ii) identifying whether such open position, unliquidated security and/or other unliquidated property is specifically identifiable property; and (iii) identifying whether you would prefer, if practicable, payment in kind for each unliquidated security or other item of unliquidated property or to have it liquidated. If the position, unliquidated security or other item of unliquidated property is already reflected in the account statement that you attached in response to Section III of this form, and you agree with the quantity and any value set forth therein, please say so. Otherwise, please (i) state the quantity and value you claim with respect to such open position, unliquidated security and/or other unliquidated property, and explain the basis for that quantity and value; and (ii) attach any documentary evidence supporting such value.	• **Documentation**: • Please attach a copy (not the original) of the most recent account statement for each account on which this claim is based. • Please enclose copies (not originals) of any documentation or correspondence you believe will be of assistance in processing your claim, including, but not limited to, customer confirmations, account statements, and statements of purchase or sale. If, at any time, you complained in writing about the handling of your account to any person or entity or regulatory authority, and the complaint relates to the claim that you are asserting in this claim form, please provide copies of the complaint and all related correspondence, as well as any replies that you received.

Verification: The individual completing this proof of claim must sign and date it. If the claim is filed electronically, the Bankruptcy Code authorizes courts to establish local rules specifying what constitutes a signature. If you sign this form, you declare under penalty of perjury that the information provided is true and correct to the best of your knowledge, information, and reasonable belief. Your signature is also a certification that the claim meets the requirements of FRBP 9011(b). Whether the claim is filed electronically or in person, if your name is on the signature line, you are responsible for the declaration. • Print the name and title, if any, of the customer or other person authorized to file this claim. State the filer's address and telephone number if it differs from the address given on the top of the form for purposes of receiving notices. If the claim is filed by an authorized agent, provide both the name of the individual filing the claim and the name of the agent. Criminal penalties apply for making a false statement on a proof of claim.	**Credits:** An authorized signature on this proof of claim serves as an acknowledgment that when calculating the amount of the claim, the customer gave the Debtor credit for any obligations of the customer to the Debtor.
ADDITIONAL INFORMATION	
Acknowledgment of Receipt of Claim [Instructions for acknowledgment of filing]	**Offers to Purchase a Claim** Certain entities are in the business of purchasing claims for an amount less than the face value of the claims. One or more of these entities may contact you and offer to purchase the claim. Some of the written communications from these entities may easily be confused with official court documentation or communications from the Debtor. These entities do not represent the Bankruptcy Court or the Debtor. A customer has no obligation to sell its claim. However, if a customer decides to sell its claim, any transfer of such claim is subject to FRBP 3001(e), any applicable provisions of the Bankruptcy Code (11 U.S.C. § 101 *et seq*.), and any applicable orders of the Bankruptcy Court.

Appendix B to Part 190—Special Bankruptcy Distributions

Framework 1—Special Distribution of Customer Funds When the Cross-Margining Account Is a Futures Account

(a) This framework 1 applies when a debtor futures commission merchant has participated in a cross-margining (''XM'') program for futures and securities under which the cross-margined positions of its futures customers (as defined in § 1.3 of this chapter) and the property received to margin, secure or guarantee such positions are held in one or more accounts pursuant to a Commission order that requires such positions and property to be segregated, pursuant to section 4d(a) of the Act, from the positions and property of:

(1) The futures commission merchant;

(2) If applicable, any affiliate carrying the securities positions as a participant in the XM program (''Affiliate''); and

(3) Other futures customers of the futures commission merchant (such segregated accounts, the ''XM accounts'').

(b) The futures commission merchant may, and any Affiliate that holds the securities positions in an XM account that it directly carries will, be registered as a broker-dealer under the Exchange Act. The Commission order approving the XM program may limit participating customers to market professionals and will require a participating customer to sign an agreement, in a form approved by the Commission, that refers to this distributional rule.

(c) A futures commission merchant is deemed to receive securities held in an XM account, including securities and other property held by an Affiliate in an XM account, as ''futures customer funds'' (as defined in § 1.3 of this chapter) that margin, guarantee or secure commodity contracts in the XM account (or paired XM accounts at the futures commission merchant and an Affiliate). Under the agreement signed by the customer, in the event that the futures commission merchant (or Affiliate) is the subject of a SIPA proceeding, the customer agrees that securities in an XM account are excluded from the securities estate for purposes of SIPA, and that its claim for return of the securities will not be treated as a customer claim under SIPA. These restrictions apply to the customer only, and should not be read to limit any action that the trustee may take to seek recovery of property in an XM account carried by an Affiliate as part of the customer estate of the futures commission merchant.

(d) XM accounts, and other futures accounts that are subject to segregation under section 4d(a) of the Act (pursuant to the Commission's regulations in part 1 of this chapter) (''non-XM accounts''), are treated as two subclasses of futures account with two separate pools of segregated futures customer property, an XM pool and a non-XM pool, each of which constitutes a segregated pool under section 4d(a) of the Act. If the futures commission merchant has participated in multiple XM programs, the XM accounts in the different programs are combined and treated as part of the same XM subclass of futures accounts. A futures customer could hold both non-XM and XM accounts.

(e) Customer claims under this part arising out of the XM subclass of accounts are subordinated to customer claims arising out of the non-XM subclass of accounts in certain circumstances in which the futures commission merchant does not meet its segregation requirements. The segregation requirement is the amount of futures customer funds that the futures commission merchant is required by the Act and Commission regulations in part 1 of this chapter or Commission orders to hold on deposit in segregated accounts on behalf of its futures customers (exclusive of its targeted residual amount obligations pursuant to § 1.3 of this chapter).

(f)(1) If there is a shortfall in the non-XM pool and no shortfall in the XM pool, all customer net equity claims, whether or not they arise out of the XM subclass of accounts, will be combined and paid pro rata out of the combined XM and non-XM pools of futures customer property.

(2) If there is a shortfall in the XM pool and no shortfall in the non-XM pool, customer net equity claims arising from the XM subclass of accounts must be satisfied first from the XM pool, and customer net equity claims arising from the non-XM subclass of accounts must be satisfied first from the non-XM pool.

(3) If there is a shortfall in both the non-XM and XM pools:

(i) If the non-XM shortfall as a percentage of the segregation requirement for the non-XM pool is greater than or equal to the XM shortfall as a percentage of the segregation requirement for the XM pool, all customer net equity claims will be paid pro rata out of the combined XM and non-XM pools of futures customer property; and

(ii) If the XM shortfall as a percentage of the segregation requirement for the XM pool is greater than the non-XM shortfall as a percentage of the segregation requirement for the non-XM pool, non-XM customer net equity claims will be paid pro rata out of the available non-XM pool, and XM customer net equity claims will be paid pro rata out of the available XM pool.

(4) In this way, non-XM customers will never be adversely affected by an XM shortfall.

(g) The following examples illustrate the operation of this framework 1. The examples assume that the FCM has two futures customers, one with exclusively XM accounts and one with exclusively non-XM accounts.

1. Sufficient Funds to Meet Non-XM and XM Customer Claims:

	Non-XM	XM	Total
Funds in 4d(a) segregation	150	150	300
4d(a) Segregation requirement	150	150	300
Shortfall (dollars)	0	0	
Shortfall (percent)	0	0	
Distribution	150	150	300

There are adequate funds available and both the non-XM and the XM customer claims will be paid in full.

2. Shortfall in Non-XM Only:

	Non-XM	XM	Total
Funds in 4d(a) segregation	100	150	250
4d(a) Segregation requirement	150	150	300
Shortfall (dollars)	50	0	
Shortfall (percent)	50/150=33.3	0	
Pro rata (percent)	150/300=50	150/300=50	
Pro rata (dollars)	125	125	
Distribution	125	125	250

Due to the non-XM account, there are insufficient funds available to meet both the non-XM and the XM customer claims in full. Each customer will receive his pro rata share of the funds available, or 50% of the $250 available, or $125.

3. Shortfall in XM Only:

	Non-XM	XM	Total
Funds in 4d(a) segregation	150	100	250
4d(a) Segregation requirement	150	150	300
Shortfall (dollars)	0	50	
Shortfall (percent)	0	50/150=33.3	
Pro rata (percent)	150/300=50	150/300=50	
Pro rata (dollars)	125	125	
Distribution	150	100	250

Due to the XM account, there are insufficient funds available to meet both the non-XM and the XM customer claims in full. Accordingly, the XM funds and non-XM funds are treated as separate pools, and the non-XM customer will be paid in full, receiving $150 while the XM customer will receive the remaining $100.

4. Shortfall in Both, With XM Shortfall Exceeding Non-XM Shortfall:

	Non-XM	XM	Total
Funds in 4d(a) segregation	125	100	225
4d(a) Segregation requirement	150	150	300
Shortfall (dollars)	25	50	
Shortfall (percent)	25/150=16.7	50/150=33.3	
Pro rata (percent)	150/300=50	150/300=50	
Pro rata (dollars)	112.50	112.50	
Distribution	125	100	225

There are insufficient funds available to meet both the non-XM and the XM customer claims in full, and the XM shortfall exceeds the non-XM shortfall. The non-XM customer will receive the $125 available with respect to non-XM claims while the XM customer will receive the $100 available with respect to XM claims.

5. Shortfall in Both, With Non-XM Shortfall Exceeding XM Shortfall:

	Non-XM	XM	Total
Funds in 4d(a) segregation	100	125	225
4d(a) Segregation requirement	150	150	300
Shortfall (dollars)	50	25	
Shortfall (percent)	50/150=33.3	25/150=16.7	
Pro rata (percent)	150/300=50	150/300=50	
Pro rata (dollars)	112.50	112.50	
Distribution	112.50	112.50	225

There are insufficient funds available to meet both the non-XM and the XM customer claims in full, and the non-XM shortfall exceeds the XM shortfall. Each customer will receive 50% of the $225 available, or $112.50.

6. Shortfall in Both, Non-XM Shortfall = XM Shortfall:

	Non-XM	XM	Total
Funds in 4d(a) segregation	100	100	200
4d(a) Segregation requirement	150	150	300
Shortfall (dollars)	50	50	
Shortfall (percent)	50/150=33.3	50/150=33.3	
Pro rata (percent)	150/300=50	150/300=50	
Pro rata (dollars)	100	100	
Distribution	100	100	200

There are insufficient funds available to meet both the non-XM and the XM customer claims in full, and the non-XM shortfall equals the XM shortfall. Each customer will receive 50% of the $200 available, or $100.

These examples illustrate the principle that pro rata distribution across both accounts is the preferable approach except when a shortfall in the XM account could harm non-XM customers. Thus, pro rata distribution occurs in Examples 1, 2, 5 and 6. Separate treatment of the XM and non-XM accounts occurs in Examples 3 and 4.

Framework 2—Special Allocation of Shortfall to Customer Claims When Customer Funds for Futures Contracts and Cleared Swaps Customer Collateral are Held in a Depository Outside of the United States or in a Foreign Currency

The Commission has established the following allocation convention with respect to futures customer funds (as § 1.3 of this chapter defines such term) and Cleared Swaps Customer Collateral (as § 22.1 of this chapter defines such term) (both of which are customer funds (as § 1.3 of this chapter defines such term) that are segregated pursuant to the Act and Commission rules thereunder), which applies in certain circumstances when futures customer funds or Cleared Swaps Customer Collateral are held by a futures commission merchant in a depository outside the United States (''U.S.'') or in a foreign currency. If a futures commission merchant enters into bankruptcy and maintains futures customer funds or Cleared Swaps Customer Collateral in a depository outside the U.S. or in a depository located in the U.S. in a currency other than U.S. dollars, the trustee shall use the following allocation procedures to calculate the claim of each public customer in the futures account class or each public customer in the cleared swaps account class, as applicable, when a sovereign action of a foreign government or court has occurred that contributes to shortfalls in the amounts of futures customer funds or Cleared Swaps Customer Collateral. In the event a sovereign action creates or contributes to a shortfall in customer property, applying the allocation convention will result in a reallocation of distributions of futures customer funds or Cleared Swaps Collateral to take into account the impact of the sovereign action. For purposes of this bankruptcy convention, sovereign action of a foreign government or court would include, but not be limited to, the application or enforcement of statutes, rules, regulations, interpretations, advisories, decisions, or orders, formal or informal, by a Federal, state, or provincial executive, legislature, judiciary, or government agency. The trustee should perform the allocation procedures separately with respect to each public customer in the futures account class or cleared swaps account class.

I. Reduction In Distributions For General Shortfall

A. ***Determination of losses not attributable to sovereign action***

1. Convert the claim of each futures customer or Cleared Swaps Customer in each currency to U.S. Dollars at the exchange rate in effect on the Final Net Equity Determination Date, as defined in §190.01(s) (the "Exchange Rate").

2. Determine the amount of assets available for distribution to futures customers or Cleared Swaps Customers. In making this calculation, include customer funds for futures contracts and Cleared Swaps Customer Collateral that would be available for distribution but for the sovereign action.

3. Convert the amount of customer funds for futures contracts and Cleared Swaps Customer Collateral available for distribution to U.S. Dollars at the Exchange Rate.

4. Determine the Shortfall Percentage that is not attributable to sovereign action, as follows:

$$\text{Shortfall Percentage} = \left(1- \left[\frac{\text{Total Customer Assets}}{\text{Total Customer Claims}} \right] \right)$$

B. ***Allocation of Losses Not Attributable to Sovereign Action***

1. Reduce the claim of each futures customer or Cleared Swaps Customer by the Short fall Percentage.

II. Reduction in Distributions for Sovereign Loss

A. ***Determination of Losses Attributable to Sovereign Action ("Sovereign Loss")***

1. If any portion of the claim of a futures customer or Cleared Swaps Customer is required to be kept in U.S. dollars in the U.S., that portion of the claim is not exposed to Sovereign Loss.

2. If any portion of the claim of a futures customer or Cleared Swaps Customer is authorized to be kept in only one location and that location is:

a. The U.S. or a location in which there is no Sovereign Loss, then that portion of the claim is not exposed to Sovereign Loss.

b. A location in which there is Sovereign Loss, then that entire portion of the claim is exposed to Sovereign Loss.

3. If any portion of the claim of a futures customer or Cleared Swaps Customer is authorized to be kept in only one currency and that currency is:

a. U.S. dollars or a currency in which there is no Sovereign Loss, then that portion of the claim is not exposed to Sovereign Loss.

b. A currency in which there is Sovereign Loss, then that entire portion of the claim is exposed to Sovereign Loss.

4. If any portion of the claim of a futures customer or Cleared Swaps Customer is authorized to he kept in more than one location and:

a. There is no Sovereign Loss in any of those locations, then that portion of the claim is not exposed to Sovereign Loss.

b. There is Sovereign Loss in one of those locations, then that entire portion of the claim is exposed to Sovereign Loss.

c. There is Sovereign Loss in more than one of those locations, then an equal share of that portion of the claim will be exposed to Sovereign Loss in each such location.

5. If any portion of the claim of a futures customer or Cleared Swaps Customer is authorized to be kept in more than one currency and:

a. There is no Sovereign Loss in any of those currencies, then that portion of the claim is not exposed to Sovereign Loss.

b. There is Sovereign Loss in one of those currencies, then that entire portion of the claim is exposed to Sovereign Loss.

c. There is Sovereign Loss in more than one of those currencies, then an equal share of that portion of the claim will be exposed to Sovereign Loss.

B. ***Calculation of Sovereign Loss***

1. The total Sovereign Loss for each location is the difference between:

a. The total customer funds for futures contracts or Cleared Swaps Customer Collateral deposited in depositories in that location and

b. The amount of customer funds for futures contracts or Cleared Swaps Customer Collateral in that location that is available to be distributed to futures customers or Cleared Swaps Customers, after taking into account any sovereign action.

2. The total Sovereign Loss for each currency is the difference between:

a. The value, in U.S. dollars, of the customer funds for futures contracts or Cleared Swaps Customer Collateral held in that currency on the day before the sovereign action took place and

b. The value, in U.S. dollars, of the customer funds for futures contracts or Cleared Swaps Customer Collateral held in that currency on the date of the calculation.

C. *Allocation of Sovereign Loss*

1. Each distribution on account of the claim of a futures customer or Cleared Swaps Customer exposed to Sovereign Loss in a location will be reduced by:

$$\text{Total Sovereign Loss } x \left| \frac{\text{Portion of the customer's claim exposed to loss in that location}}{\text{All portions of customer claims exposed to loss in that location}} \right|$$

2. Each distribution on account of the claim of a futures customer or Cleared Swaps Customer exposed to Sovereign Loss in a currency will be reduced by:

$$\text{Total Sovereign Loss } x \left| \frac{\text{Portion of the customer's claim exposed to loss in that currency}}{\text{All portions of customer claims exposed to loss in that currency}} \right|$$

3. A distribution to a futures customer or Cleared Swaps Customer exposed to Sovereign Loss in a location or currency will not be reduced below zero. (The above calculations might yield a result below zero where the FCM kept more customer funds for futures contracts or Cleared Swaps Customer Funds in a location or currency than it was authorized to keep.)

4. Any amount of Sovereign Loss from a location or currency in excess of the total amount of customer funds for futures contracts or Cleared Swaps Customer Funds authorized to be kept in that location or currency (calculated in accord with section II.1 above) ("Total Excess Sovereign Loss") will be allocated among all futures customers or Cleared Swaps Customer that have authorized funds to be kept outside the U.S., or in currencies other than U.S. dollars, with each such futures customer or Cleared Swaps Customer distribution reduced by the following amount:

$$\text{Total Excess Sovereign Loss } x \left[\frac{\text{This customer's total claim} - \text{The portion of this Customer's claim required to be kept in U.S. dollars, in the U.S.}}{\text{Total customer claims} - \text{Total of all customer claims required to be kept in U.S. dollar, in the U.S.}} \right]$$

The following examples illustrate the operation of this convention.

Example 1. No shortfall in any location.

Customer	Claim	Location(s) customer has consented to having funds held
A	$50	U.S.
B	€50	U.K.
C	€50	Germany
D	£300	U.K.
Location		**Actual asset balance**
U.S.		$50
U.K.		£300
U.K.		€50
Germany		€50

Note: Conversion Rates: €1 = $1; £1=$1.5.

Convert the claim of each futures customer or Cleared Swaps Customer in each currency to U.S. Dollars:

Customer	Claim	Conversion rate	Claim in U.S. dollars
A	$50	1.0	$50
B	€50	1.0	50
C	€50	1.0	50
D	£300	1.5	450
Total			$600

Determine assets available for distribution to futures customers or Cleared Swaps Customers, converting to U.S. dollars:

Location	Assets	Conversion rate	Assets in U.S. dollars	Shortfall due to sovereign action percentage	Actual shortfall due to sovereign action	Amount actually available
U.S.	$50	1.0	$50			$50
U.K.	£300	1.5	450			450
U.K.	€50	1.0	50			50
Germany	€50	1.0	50			50
Total			$600		0	$600

There are no shortfalls in funds held in any location. Accordingly, there will be no reduction in distributions to holders of futures or Cleared Swaps Customer claims.

Claims:

Customer	Claim in U.S. dollars after allocated non-sovereign shortfall	Allocation of shortfall due to sovereign action	Distributions after all reductions
A	$50	$0	$50
B	50	0	50
C	50	0	50
D	450	0	450
Total	$600	$0	$600

Example 2. Shortfall in funds held in the U.S.

Customer	Claim	Location(s) customer has consented to having funds held
A	$100	U.S.
B	€50	U.K.
C	€100	U.S., Germany, or Japan
Location		**Actual asset balance**
U.S.		$50
U.K.		€100
Germany		€50

Note: Conversion Rates: €1=$1.

REDUCTION IN DISTRIBUTIONS FOR GENERAL SHORTFALL

There is a shortfall in the funds held in the U.S. such that only 1/2 of the finds are available. Convert the claim of each futures customer or Cleared Swaps Customer in each currency to U.S. Dollars:

Convert each customer's claim in each currency to U.S. Dollars:

Customer	Claim	Conversion rate	Claim in US$
A	$100	1.0	$100
B	€50	1.0	50
C	€100	1.0	100
Total			$250

Determine assets available for distribution to futures customers or Cleared Swaps Customers, converting to U.S. dollars:

Location	Assets	Conversion rate	Assets in U.S. dollars	Shortfall due to sovereign action percentage	Actual shortfall due to sovereign action	Amount actually available
U.S.	$50	1.0	$50			$50
U.K.	€100	1.0	100			100
Germany	€50	1.0	50			50
Total			$200			$200

Determine the percentage of shortfall that is not attributable to sovereign action:
Shortfall Percentage = (1–(200/250)) = (1–80%) = 20%.

Reduce each distribution to the holder of a futures or Cleared Swaps Customer claim by the Shortfall Percentage:

Customer	Claim in US$	Allocation shortfall (non-sovereign)	Distribution in U.S. dollars after allocated shortfall
A	$100	$20	$80
B	50	10	40
C	100	20	80
Total	$250	$50	$200

REDUCTION IN DISTRIBUTIONS DUE TO SOVEREIGN ACTION

There is no shortfall due to sovereign action. Accordingly, distributions to holders of futures or Cleared Swaps Customer claims will not be further reduced.

DISTRIBUTIONS AFTER REDUCTIONS

Customer	Distribution in US$ before allocation of sovereign shortfall	Allocation of shortfall due to sovereign action	Distribution after all reductions
A	$80		$80
B	40		40
C	80		80
Total	$200	$0	$200

Example 3. Shortfall in funds held outside the U.S., or in a currency other than U.S. dollars, not due to sovereign action.

Customer	Claim	Location(s) customer has consented to having funds held
A	$150	U.S.
B	€100	U.K.
C	€50	Germany
D	$100	U.S.
D	€100	U.K. or Germany
Location		**Actual asset balance**
U.S.		$250
U.K.		€50
Germany		€100

Note: Conversion Rates: €1=$1.

REDUCTION IN DISTRIBUTIONS FOR GENERAL SHORTFALL

Convert the claim of each futures customer or Cleared Swaps Customer in each currency to U.S. Dollars:

Customer	Claim	Conversion rate	Claim in US$
A	$150	1.0	$150
B	€100	1.0	100
C	€50	1.0	50
D	$100	1.0	100
D	€100	1.0	100
Total			$500

Determine assets available for distribution to futures customers or Cleared Swaps Customers, converting to U.S. dollars:

Location	Assets	Conversion rate	Assets in U.S. dollars	Shortfall due to sovereign action percentage	Actual shortfall due to sovereign action	Amount actually available
U.S.	$250	1.0	$250			$250
U.K.	€50	1.0	50			50
Germany	€100	1.0	100			100
Total			$400		$0	$400

Determine the percentage of shortfall that is not attributable to sovereign action:
Shortfall Percentage = (1–400/500) = (1–80%) = 20%.

Reduce each distribution to the holder of a futures customer or Cleared Swaps Customer by the Shortfall Percentage:

Customer	Claim in US$	Allocation shortfall (non-sovereign)	Distribution in U.S. dollars after allocated shortfall
A	$150	$30	$120
B	100	20	80
C	50	10	40
D	200	40	160
Total	$500	$100	$400

REDUCTION IN DISTRIBUTIONS DUE TO SOVEREIGN ACTION

There is no shortfall due to sovereign action. Accordingly, the distributions will not be further reduced.

DISTRIBUTIONS AFTER REDUCTIONS

Customer	Distribution in US$ before allocation of sovereign shortfall	Allocation of shortfall due to sovereign action	Distribution after all reductions
A	$120		$120
B	80		80
C	40		40
D	160	0	160
Total	$400	$0	$400

Example 4. Shortfall in funds held outside the U.S., or in a currency other than U.S. dollars, due to sovereign action.

Customer	Claim	Location(s) customer has consented to having funds held
A	$50	U.S.
B	€50	U.K.
C	€50	Germany
D	$100	U.S.
D	€100	U.K. or Germany
Location		**Actual asset balance**
U.S.		$150
U.K.		100
Germany		100

Notice: Conversion Rates: €1 = $1; £1 = $1.5.

REDUCTION IN DISTRIBUTIONS FOR GENERAL SHORTFALL

Convert each futures customer or Cleared Swaps Customer claim in each currency to U.S. Dollars:

Customer	Claim	Conversion rate	Claim in US$
A	$50	1.0	$50
B	€50	1.0	50
C	€50	1.0	50
D	$100	1.0	100
D	€100	1.0	100
Total			$350

Determine assets available for distribution to futures customers or Cleared Swaps Customers, converting to U.S. dollars:

Location	Assets	Conversion rate	Assets in U.S. dollars	Shortfall due to sovereign action percentage	Actual shortfall due to sovereign action	Amount actually available
U.S.	$150	1.0	$150			$150
U.K.	€100	1.0	100			100
Germany	€100	1.0	100	50%	50	50
Total			$350		$50	$300

Determine the percentage of shortfall that is not attributable to sovereign action:
Shortfall Percentage = (1–350/350) = (1–100%) = 0%.

Reduce each distribution to the holder of a futures customer or Cleared Swaps Customer claim by the Shortfall Percentage:

Customer	Claim in US$	Allocation shortfall (non-sovereign)	Distribution in U.S. dollars after allocated shortfall
A	$50	$0	$50
B	50	0	50
C	50	0	50
D	200	0	200
Total	$350	$0	$350

REDUCTION IN DISTRIBUTIONS FOR DUE TO SOVEREIGN ACTION

Due to sovereign action, only 1/2 of the funds in Germany are available.

Customer	Presumed location of funds		
	U.S.	U.K.	Germany
A	$50		
B		$50	
C			$50
D	100		100
Total	$150	$50	$150

Calculation of the allocation of the shortfall due to sovereign action—Germany ($50 shortfall to be allocated):

Customer	Allocation share	Allocation share of actual shortfall	Actual shortfall allocated
C	$50/$150	33.3% of $50	$16.67
D	$100/$150	66.7% of $50	33.33
Total			$50.00

DISTRIBUTIONS AFTER REDUCTIONS

Customer	Distribution in US$ before allocation of sovereign shortfall	Allocation of shortfall due to sovereign action from Germany	Distribution after all reductions
A	$50		$50
B	50		50
C	50	$16.67	33.33
D	200	33.33	166.67
Total	$350.00	$50.00	$300.00

__Example 5__. Shortfall in funds held outside the U.S., or in a currency other than U.S. dollars, due to sovereign action and a shortfall in funds held in the U.S.

Customer	Claim	Location(s) customer has consented to having funds held
A	$100	U.S.
B	€50	U.K.
C	€150	Germany
D	$100	U.S.
D	£300	U.K.
D	€150	U.K. or Germany

Location	Actual asset balance
U.S.	$100
U.K.	£300
U.K.	€200
Germany	€150

Conversion Rates: €1 = $1; £1 = $1.5.

REDUCTION IN DISTRIBUTIONS FOR GENERAL SHORTFALL

Convert each futures customer or Cleared Swaps Customer claim in each currency to U.S. Dollars:

Customer	Claim	Conversion rate	Claim in US$
A	$100	1.0	$100
B	€50	1.0	50
C	€150	1.0	150
D	$100	1.0	100
D	£300	1.5	450
D	€150	1.0	150
Total			$1000

Determine assets available for distribution to futures customers or Cleared Swaps Customers, converting to U.S. dollars:

Location	Assets	Conversion rate	Assets in U.S. dollars	Shortfall due to sovereign action percentage	Actual shortfall due to sovereign action	Amount actually available
U.S.	$100	1.0	$100			$100
U.K.	£300	1.5	450			450
U.K.	€200	1.0	200			200
Germany	€150	1.0	150	100%	$150	0
Total			$900		$150	$750

Determine the percentage of shortfall that is not attributable to sovereign action:
Shortfall Percentage = (1 – 900 / 1000) = (1 – 90%) = 10%.

Reduce each distribution to the holder of a futures customer or Cleared Swaps Customer claim by the Shortfall Percentage:

Customer	Claim in US$	Allocation shortfall (non-sovereign)	Distribution in U.S. dollars after allocated shortfall
A	$100	$10	$90
B	50	5	45
C	150	15	135
D	700	70	630
Total	$1000	$100	$900

REDUCTION IN DISTRIBUTIONS FOR SHORTFALL DUE TO SOVEREIGN ACTION

Due to sovereign action, none of the money in Germany is available.

Customer	Presumed location of funds		
	U.S.	U.K.	Germany
A	$100		
B		$50	
C			$150
D	100	450	150
Total	$200	$500	$300

Calculation of the allocation of the shortfall due to sovereign action Germany ($150 shortfall to be allocated):

Customer	Allocation share	Allocation Share of actual shortfall	Actual shortfall allocated
C	$150/$300	50% of $150	$75
D	$150/$300	50% of $150	75
Total			$150

DISTRIBUTIONS AFTER REDUCTIONS

Customer	Distribution in US$ before allocation of sovereign shortfall	Allocation of shortfall due to sovereign action from Germany	Distributions after all reductions
A	$90		$90
B	45		45
C	135	$75	60
D	630	75	555
Total	$900	$150	$750

Example 6. Shortfall in funds held outside the U.S., or in a currency other than U.S. dollars, due to sovereign action, shortfall in funds held outside the U.S., or in a currency other than U.S. dollars, not due to sovereign action, and a shortfall in funds held in the U.S.

Customer	Claim	Location(s) customer has consented to having funds held
A	$50	U.S.
B	€50	U.K.
C	$20	U.S.
C	€50	Germany
D	$100	U.S.
D	£300	U.K.
D	€100	U.K., Germany, or Japan
E	$80	U.S.
E	¥10,000	Japan
Location		**Actual asset balance**
U.S.		$200
U.K.		£200
U.K.		€100
Germany		€50
Japan		¥10,000

Conversion Rates: €1 = $1; ¥1 = $0.01, £1 = $1.5.

REDUCTION IN DISTRIBUTIONS FOR GENERAL SHORTFALL

Convert each futures customer or Cleared Swaps Customer claim in each currency to U.S. Dollars:

Customer	Claim	Conversion rate	Claim In US$
A	$50	1.0	$50
B	€50	1.0	50
C	$20	1.0	20
C	€50	1,0	50
D	$100	1.0	100
D	£300	1.5	450
D	€100	1.0	100
E	$80	1.0	80
E	¥10,000	0.01	100
Total			$1000

Determine assets available for distribution to futures customers or Cleared Swaps Customers, converting to U.S. dollars:

Location	Assets	Conversion rate	Assets in U.S. dollars	Shortfall due to sovereign action percentage	Actual shortfall due to sovereign action	Amount actually available
U.S.	$200	1.0	$200			$200
U.K.	£200	1.5	300			300
U.K.	€100	1.0	100			100
Germany	€50	1.0	50	100%	$50	0
Japan	¥10,000	0.01	100	50%	50	50
Total			$750		$100	$650

Determine the percentage of shortfall that is not attributable to sovereign action:
Shortfall Percentage = (1=750/1000) = (1=75%) = 25%.

Reduce each distribution to the holder of a futures or Cleared Swaps Customer claim by the Shortfall Percentage:

Customer	Claim in US$	Allocation shortfall (non-sovereign)	Distributions in U.S. dollars after allocated shortfall
A	$50	$12.50	$37.50
B	50	12.50	37.50
C	70	17.50	52.50
D	650	162.50	487.50
E	180	45.00	135.00
Total	$1000.00	$250.00	$750.00

REDUCTION IN DISTRIBUTIONS DUE TO SOVEREIGN ACTION

Due to sovereign action, none of the money in Germany and only 1/2 of the funds in Japan are available.

Customer	Presumed location of funds			
	U.S.	U.K.	Germany	Japan
A	$50			
B		$50		
C	20		$50	
D	100	450	50	$50
E	80			100
Total	$250	$500	$100	$150

Calculation of the allocation of the shortfall due to sovereign action—Germany ($50 shortfall to be allocated):

Customer Allocation	Allocation share	Allocation Share of actual shortfall	Actual shortfall allocated
C	$50/$100	50% of $50	$25
D	50/100	50% of 50	25
Total			50

Japan ($50 shortfall to be allocated):

Customer Allocation	Allocation share	Allocation Share of actual shortfall	Actual shortfall allocated
D	$50/$150	33.3% of $50	$16.67
E	100/150	66.6% of 50	33.33
Total			$50.00

DISTRIBUTIONS AFTER REDUCTIONS

Customer	Distribution in US$ before allocation of sovereign shortfall	Allocation of shortfall due to sovereign action from Germany	Allocation of shortfall due to sovereign action from Japan	Distribution after all reductions
A	$37.50			37.50
B	37.50			37.50
C	52.50	$25		27.50
D	487.50	$25	16.67	445.83
E	135.00		33.33	101.67
Total	$750.00	$50.00	$50.00	$650.00

Example 7. Shortfall in funds held outside the U.S., or in a currency other than U.S. dollar, due to sovereign action, where the FCM kept more funds than permitted in such location or currency.

Customer	Claim	Location(s) customer has consented to having funds held
A	$50	U.S.
B	50	U.S.
B	€50	U.K.
C	€50	Germany
D	100	U.S.
C	€100	U.K. or Germany
E	50	U.S.
E	€50	U.K.

Location	Actual asset balance
U.S.	$250
U.K.	€50
Germany	€200

Conversion Rates: 1 = $1.

REDUCTION IN DISTRIBUTIONS FOR GENERAL SHORTFALL

Convert each futures customer or Cleared Swaps Customer claim in each currency to U.S. Dollars:

Customer	Claim	Conversion rate	Claim in US$
A	$50	1.0	$50
B	50	1.0	50
B	€50	1.0	50
C	€50	1.0	50
D	€100	1.0	100
D	€100	1.0	100
E	50	1.0	50
E	€50	1.0	50
Total			500.00

Determine assets available for distribution to futures customers or Cleared Swaps Customers, converting to U.S. dollars:

Location	Assets	Conversion rate	Assets in U.S. dollars	Shortfall due to sovereign action percentage	Actual shortfall due to sovereign action	Amount actually available
U.S.	$250	1.0	$250			$250
U.K.	€50	1.0	50			50
Germany	€200	1.0	200	100%	200	0
Total			$500		$200	$300

Determine the percentage of shortfall that is not attributable to sovereign
Shortfall Percentage = (1–500/500) = (1–100%) = 0%.

Reduce each distribution to the holder of a futures or Cleared Swaps Customer claim by the Shortfall Percentage:

Customer	Claim in US$	Allocation shortfall (non-sovereign)	Distribution in U.S. dollars after allocated shortfall
A	$50	$0	$50
B	100	0	100
C	50	0	50
D	200	0	200
E	100	0	100
Total	$500	$0	$500

REDUCTION IN DISTRIBUTIONS DUE TO SOVEREIGN ACTION

Due to sovereign action, none of the money in Germany is available.

Customer	Presumed location of funds		
	U.S.	U.K.	Germany
A	$50		
B	50	50	
C			50
D	100		100
E	50	50	
Total	$250	$100	$150

Calculation of the allocation of the shortfall due to sovereign action—Germany ($200 shortfall to be allocated):

Customer	Allocation share	Allocation Share of actual shortfall	Actual shortfall allocated
C	$50/$150	33.3% of $200	$66.67
D	$100/$150	66.7% of $200	$133.33
Total			$200.00

This would result in the distributions to customers C and D being reduced below zero.

Accordingly, the distributions to customer C and D will only be reduced to zero, or $50 allocated to C and $100 allocated to D. This results in a Total Excess Shortfall of $50.

Actual shortfall	Allocation of shortfall for customer C	Allocation of shortfall for customer D	Total excess shortfall
$200	$50	$100	$50

This shortfall will be allocated among the remaining futures customers or Cleared Swaps Customers who have authorized funds to be held outside the U.S. or in a currency other than U.S. dollars.

Customer	Total claims of customers permitting funds to be held outside the U.S.	Portion of claim required to be in the U.S.	Allocation share (column B-C/column B Total—all customer claims in U.S.)	Allocation share of actual total excess shortfall	Actual total excess shortfall allocated
B	$100	$50	$50/$200	25% of $50	$12.50
C	50	0	(1)		0
D	200	100	$100/200	50% of $50	25
E	100	50	50/100	25% of $50	12.50
Total	$450.00				$50.00

[1] Claim already reduced to $0.

DISTRIBUTIONS AFTER REDUCTIONS

Customer	Distribution in US$ before allocation of sovereign shortfall	Allocation of shortfall due to sovereign action Germany	Allocation of total excess shortfall	Distribution after all reductions
A	$50			$50.00
B	100		12.50	87.50
C	50	50		0
D	200	100	25	75.00
E	100		12.50	87.50
Total	$500.00	$150.00	$50.00	$300.00

Issued in Washington, DC, on December 17, 2020, by the Commission.

Christopher Kirkpatrick,
Secretary of the Commission.

Note: The following appendices will not appear in the Code of Federal Regulations.

Appendices to Bankruptcy Regulations—Commission Voting Summary, Chairman's Statement, and Commissioners' Statements

Appendix 1—Commission Voting Summary

On this matter, Chairman Tarbert and Commissioners Quintenz, Behnam, Stump, and Berkovitz voted in the affirmative. No Commissioner voted in the negative.

Appendix 2—Statement of Support of Chairman Heath P. Tarbert

When our Commission considered the proposal to amend the CFTC's bankruptcy rules in Part 190,[1] I noted that, in his 1926 novel *The Sun Also Rises,* Ernest Hemingway offered what is perhaps the best chronicle of the anatomy of a typical bankruptcy. In the novel, the character Mike Campbell is asked how he went bankrupt. He answers: ''two ways . . . gradually and then suddenly.'' [2]

As Hemingway's dialogue succinctly describes, bankruptcies often come on unexpectedly. A business's relatively minor financial or operational troubles may be exacerbated by a sudden crisis—whether a firm-level issue, or a national or even global event. Many catalysts for insolvency are entirely unpredictable. We must therefore be prepared with a bankruptcy regime that fosters a swift and equitable resolution to protect customer funds and promote financial stability.

Background on the CFTC's Bankruptcy Regime

Part 190 of the CFTC's rules, addressing commodity broker [3] bankruptcies, was finalized in 1983. Since that time, the commodity broker bankruptcy process and the state of the industry have gradually changed. Yet in the nearly four decades since, Part 190 has never been comprehensively updated. This regime is intended to protect customer funds, but having antiquated rules does not help achieve that goal.

CFTC staff has accordingly embarked on a process of updating Part 190 over the last several years, when a then-healthy economy made bankruptcies relatively unlikely. Now that we find ourselves in the midst of the COVID–19 pandemic and its economic ramifications, the fruits of our investment arguably could have not been better timed. The good news is that during 2020, U.S. derivatives markets and their participants have weathered the volatility associated with the coronavirus pandemic admirably. But as I just noted, we cannot know for certain what the future holds—for bankruptcy often comes ''gradually and then

[1] Bankruptcy Regulations, 85 FR 36000 (June 12, 2020).

[2] *See* Statement of Chairman Heath P. Tarbert in Support of Long-Awaited Updates to the CFTC's Bankruptcy Regime (Apr. 14, 2020), available at *https://www.cftc.gov/PressRoom/SpeechesTestimony/tarbertstatement041420.*

[3] The term ''commodity broker'' may refer either to a futures commission merchant (''FCM'') or a derivatives clearing organization (''DCO''). 11 U.S.C. 101(6).

suddenly.'' We must therefore be prepared for all contingencies.

Accordingly, I am pleased to support today's final rule to update Part 190 for the 21st century.[4] The final rule is a product of both hard work by CFTC staff and Commissioners as well as contributions from external stakeholders and subject matter experts, including a subcommittee of the American Bar Association. The final rule promotes the CFTC's core values in a number of ways, particularly the values of *clarity* and *forward thinking.* It also furthers the agency's strategic goal of regulating our derivatives markets to promote the interests of all Americans.[5]

Clarity for Customers and Creditors

The final rule serves our core value of clarity by incorporating key principles and actual practice as they have evolved in commodity broker bankruptcies and related judicial decisions in the years since 1983.

A new introductory section of the rule enumerates certain ''core concepts'' of commodity broker bankruptcies. This section is intended to offer a readily understandable primer on relevant law, policy, and practical considerations in this area, thereby providing a common mental framework for brokers, customers, bankruptcy trustees, courts, and the public. Among other things, this section provides an overview of the various classes of customer segregated accounts held by a commodity broker; the priority of public customers over insiders; the requirement of *pro rata* distribution; and the preference to transfer rather than liquidate open positions.

The final rule codifies a number of approaches and practices that have proven necessary or desirable in commodity broker bankruptcies in the intervening years since 1983. For example, the final rule authorizes a bankruptcy trustee to treat a broker's customers in the aggregate for certain purposes, rather than handling each customer's account on a bespoke basis. This aggregate treatment has in practice proven unavoidable in more recent commodity broker bankruptcies, which have required disposition of hundreds of thousands of derivatives contracts—on behalf of thousands or tens of thousands of customers—within days or even hours. By making clear that such aggregate disposition of accounts is permissible and may even be more likely to occur than the alternative, the final rule provides greater clarity on potential outcomes for trustees, brokers, and customers.

For example, the final rule expressly permits the trustee—following consultation with CFTC staff—to determine whether to treat open positions of public customers in a designated hedging account as specifically identifiable property (requiring the trustee to solicit and comply with individual customer instructions), or instead transfer or ''port'' all such positions to a solvent commodity broker where possible. This provision recognizes that requiring the trustee to identify hedging accounts and provide account holders the opportunity to give individual instructions is often a resource-intensive endeavor, which could interfere with the trustee's ability to act in a timely and effective manner to protect all the broker's customers.[6]

The final rule also includes explicit rules governing the bankruptcy of a clearinghouse, otherwise known as a derivatives clearing organization or DCO. Since its inception, Part 190 has contemplated only a ''case-by-case'' approach with no corresponding rules to spell out what would happen in the event of a DCO bankruptcy. While such a bankruptcy is extremely unlikely, it is important to provide *ex ante* clarity to DCO members and customers as to how it would be handled. The final rule favors following the DCO's existing default management and recovery and wind-down rules and procedures, but gives the trustee discretion to apply them reasonably and practicably. This allows the bankruptcy trustee to take advantage of and adapt an established ''playbook,'' rather than being forced either to follow a rigid, ''one-size-fits-all'' framework or to form a resolution plan in a matter of hours during the onset of a crisis. The final rule also gives legal certainty to DCO actions taken in accordance with a recovery and wind-down plan filed with the CFTC by precluding the trustee from voiding any such action.

I support codifying these and other practices within our rules in order to provide greater transparency and predictability to brokers, customers, and other key stakeholders regarding permissible and expected procedures in a bankruptcy scenario.

Forward Thinking on Future Insolvencies

The final rule updates a number of provisions to reflect changes in financial technology since Part 190 was enacted 37 years ago. The enhanced discretion discussed above would in many cases help the trustee to account for the increase in transaction execution and processing speed, as well as the potential for large and unpredictable market moves given the rise of global trading and the 24-hour trading cycle. In addition, the final rule acknowledges digital assets as a physically deliverable asset class, in light of the listing of a number of physically delivered ''virtual currency'' derivatives contracts.

The final rule also reflects advances in communications technology. For example, under the final rule, notice of a bankruptcy filing and related filed documents will be provided to the CFTC by electronic rather than paper means. Furthermore, required customer notice procedures no longer include publication in a ''newspaper of general circulation'' in light of the downward trend in newspaper readership. The final rule similarly recognizes changes from paper-based to electronic recording of documents of title.

Promoting the Interests of All Americans

Protection of customer funds is the lynchpin of the commodity broker bankruptcy regime of Part 190. The final rule includes a number of measures to enhance those protections, including by buttressing provisions already in place under existing law and regulation. In doing so, the final rule seeks to ensure that the CFTC's bankruptcy regime works for the derivatives market participants it was meant to serve—particularly public brokerage customers, with a special emphasis on customers using derivatives to hedge their commercial risks.

For example, the final rule reinforces the bankruptcy priority of public broker customers over ''non-public'' customers (*e.g.,* the broker's proprietary and affiliate accounts). It also strengthens the CFTC's longstanding position that shortfalls in segregated customer assets should be made up from the broker's general estate. As a result, our final rule

[4] After considering comments that were received on the original proposal, our Commission subsequently issued a Supplemental Proposal that withdrew § 190.14(b)(2) and (3), and proposed other revisions to § 190.14. *See* Bankruptcy Regulations, 85 FR 60110 (Sept. 24, 2020) (''Supplemental Proposal''). However, in light of comments raised on the Supplemental Proposal, as well as the original proposal, our Commission concluded that, at this point, it should engage in further analysis and development before proposing this, or any other, alternative approach. Such further analysis and development will better enable the CFTC to propose, in detail, a solution that is effective, and that mitigates any attendant concerns.

[5] *See* Remarks of CFTC Chairman Heath P. Tarbert to the 35th Annual FIA Expo 2019 (Oct. 30, 2019), available at *https://www.cftc.gov/PressRoom/SpeechesTestimony/opatarbert2* (outlining the CFTC's strategic goals).

[6] The final rule also grants the trustee appropriate discretion in other respects—for example, by allowing the trustee to modify the customer proof of claim form as needed for a particular bankruptcy.

makes clear that the CFTC's bankruptcy regime is complementary to relatively recently-enacted customer protection rules for day-to-day broker operations.[7]

The final rule also furthers the preference—consistent with Subchapter IV of the Bankruptcy Code[8]—for transferring or ''porting'' customer positions to a solvent broker, rather than liquidating those positions. Porting of positions protects the utility of customer hedges by avoiding the risk of market moves between liquidation and re-establishment of the customer's hedging position. It also mitigates the risk that liquidation itself will cause such market moves. Among other measures, the grant of trustee discretion as to whether to treat hedging positions as specifically identifiable property will serve these objectives by facilitating porting of such positions *en masse,* promptly and efficiently, along with other customer property.

Conclusion

While updates to the CFTC's bankruptcy rules have been years in the making, I believe today's final rule was well worth the wait. The commodity broker resolution regime of Part 190 is respected throughout the world for its effectiveness and efficiency. In addition, Part 190 is important to the continued global competitiveness of American exchanges, clearinghouses, and market intermediaries. The final rule further enhances these features of our regime. Through its focus on promoting customer protection, clarity, and forward thinking, I believe the final rule will position us well for this decade and beyond.

Appendix 3—Statement of Support of Commissioner Brian D. Quintenz

I am pleased to support today's final rule amending the Commission's regulations governing the bankruptcy proceedings of commodity brokers.[1] This rulemaking makes the first comprehensive change to these regulations since they were first issued in 1983. I commend both Chairman Tarbert for his leadership in continuing the Commission's rulemaking agenda and former Chairman Giancarlo for laying the groundwork for this important rulemaking when he launched the CFTC's Project KISS initiative.[2]

I am pleased that today's final rule carefully took into consideration comments from FCMs, DCOs, asset managers and other market participants. I would like to highlight a few aspects of today's final rule. The rulemaking reaffirms the special treatment the U.S. Bankruptcy Code affords to the customer account of an insolvent commodity broker, so that customers' positions can promptly be transferred.[3] The Commission is, for the first time, issuing rules specific to an insolvent DCO, which are similar to the rules applicable to an insolvent FCM. Next, taking advantage of the Commission's experience with a few insolvent FCMs over the past decades, the final rule provides deference to the trustee that a U.S. Bankruptcy Court appoints to oversee the proceedings of an insolvent commodity broker. This increased deference is intended to expedite the transfer of customer funds. In response to comments from the asset management community, the final provisions provide additional guidance on how a trustee should balance various interests in seeking to protect public customers.[4] In light of the Commission's experience from the bankruptcy of MF Global in 2011, the new bankruptcy rules generally treat letters of credit equivalently to other collateral posted by customers, so that the *pro rata* distribution of customer property in the event of a shortfall in the customer account will apply equally to all collateral. The final rule also reflects experience from MF Global by dividing the delivery account into ''physical delivery'' and ''cash delivery'' account classes. Property other than cash is generally easier to trace, so it should have the benefit of a separate account class. Finally, the final rule's revised treatment of the ''delivery account,'' applicable in the context of physically-settled futures and cleared swaps, will apply not only to tangible commodities, as is currently the case, but also to digital assets. This amendment will provide important legal certainty to the growing exchange-traded market for cleared, physically-settled, digital asset derivatives.

I acknowledge that the asset management community has raised concerns with certain existing DCO rules that would be recognized in the bankruptcy of an FCM or DCO. I would support an on-going dialogue between the DCOs and their members and customers on resolution and resiliency concerns.

Appendix 4—Statement of Commissioner Rostin Behnam

I respectfully support the Commodity Futures Trading Commission's (the ''Commission'' or ''CFTC'') final rule amending Part 190 of its regulations, which governs bankruptcy proceedings of commodity brokers. First and foremost, I want to thank Commission staff for all of their hard work on the final rule. This is the first major update of the CFTC's existing Part 190 since 1983, when it was originally implemented by the Commission.[1]

The final rule is the product of years of staff analysis and engagement with market participants, including the Part 190 Subcommittee of the Business Law Section of the American Bar Association, which provided a detailed submission of suggested model Part 190 rules in response to a prior Commission request for information.[2] Several agency Chairs going back many years deserve recognition and thanks for pushing to update Part 190 and starting this process. Customer protections are at the heart of the Commodity Exchange Act, and it is imperative that the Commission have clear rules that direct how proceedings occur during a commodity broker bankruptcy.

The revision is designed to recognize the many changes in our industry over the past 37 years. Most importantly, it is informed by the Commission's experience with past bankruptcies. More recently, the MF Global bankruptcy in 2011 was the eighth largest corporate bankruptcy in American history.[3] It gave the Commission first hand experience with what worked, what did not, and what could be improved.

I was a lead advisor during the U.S. Senate's investigation of the MF Global bankruptcy, and during the Senate investigation, I learned the intricate contours of Part 190, its relationship to the Bankruptcy Code, and how the larger puzzle of creditors, customers, and equity holders, among others, fits

[7] 17 CFR 1.23 (enacted in 2013 and revised in 2014) (requiring an FCM to contribute its own funds as ''residual interest'' to top up shortfalls in customer segregated accounts in the ordinary course of business).

[8] Statutory authority for Part 190 includes Subchapter IV of Chapter 7 of the Bankruptcy Code.

[1] Part 190 of the Commission's regulations (17 CFR part 190).

[2] CFTC Requests Public Input on Simplifying Rules, *https://www.cftc.gov/PressRoom/PressReleases/pr7555-17.*

[3] 11 U.S.C. 761 *et seq.*

[4] § 190.00(c)(3)(i)(C).

[1] *Bankruptcy,* 48 FR 8716 (March 1, 1983).

[2] 82 FR 23765 (May 3, 2017). The ABA Submission can be found at: *https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=61331&SearchText;* the accompanying cover note (''ABA Cover Note'') can be found at: *https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=61330&SearchText.*

[3] John Gapper and Isabella Kaminska, *Downfall of MF Global,* Financial Times, Nov. 4, 2011, *available at https://www.ft.com/content/2882d766-06fb-11e1-90de-00144feabdc0.*

together. It was during those frenzied days that I truly appreciated the regulatory principle that *customer margin is sacrosanct property.* Because of my experience during those few months, I have made customer protections an absolute priority in my time as a Commissioner. Having spoken with many market participants throughout the MF Global bankruptcy proceedings, including those whose money disappeared in the days immediately following, customer protection is my most pressing responsibility.

Just a few months later in early 2012, the bankruptcy of Peregrine Financial Group (''PFG''), the catastrophic culmination of a fraudulent scheme by a futures commission merchant (''FCM'') involving over $220M in customer funds,[4] further laid bare the strengths and weaknesses of the Commission's bankruptcy regime. Important lessons have been learned, both in terms of what works and what does not, and I believe today's final rule implements the lessons learned in both of those events, and those that preceded them.

Many of the changes to Part 190 in today's final rule further support provisions that have worked in prior bankruptcies. One of the themes of this refresh is clarity. The goal is to be as clear as possible about the Commission's intentions regarding Part 190 in order to enhance the understanding of Designated Clearing Organizations (''DCOs''), FCMs, their customers, trustees, and the public at large. Changes in this final rule will foster the longstanding and continuing policy preference for transferring (as opposed to liquidating) the positions of public customers—an important customer protection aimed at preserving the status quo/asset value. Other changes further support existing requirements including that shortfalls in segregated property should be shored up from the FCM's general assets, and that *public customers are favored over non-public customers.* The new provisions provide trustees with enhanced discretion based upon prior positive experience, and codify practice adopted in past bankruptcies by requiring FCMs to notify the Commission of their intent to file for voluntary bankruptcy.

Other changes address what has not worked or become outdated. In light of lessons learned from MF Global, the Commission is enacting changes to the treatment of letters of credit as collateral, both during business as usual and during bankruptcy, in order to ensure that customers who post letters of credit as collateral have the same proportional loss as customers who post other types of collateral.

The final rule also addresses a number of changes that have naturally occurred in our markets since the original Part 190 finalization in 1983. The Commission is promulgating a new subpart C to part 190, specifically governing the bankruptcy of a clearing organization. As DCOs have grown in importance over time, including being deemed systemically important by the Financial Stability Oversight Council following the financial crisis,[5] the Commission believes that it is imperative to have a clear plan in place for exactly how a DCO bankruptcy would be resolved. The final rule also addresses changes in technology over the past 37 years, and the movement from paper-based to electronic-based means of communication—a lesson learned from the PFG bankruptcy.

In many ways, this final rule is exactly how the rulemaking process should work. It looks retrospectively at major relevant events, and applies important lessons learned regarding what works in the existing Part 190 rules, what does not, and what can be improved. But it also looks forward in a sense, recognizing changes in market structure and thinking ahead to the possibility of the bankruptcy of a clearing organization. This is a stark contrast to the risk principles final rule that we consider today. While the bankruptcy final rule looks back at the Commission's past experiences with MF Global and PFG, the risk principles final rule seems to ignore past events. While the bankruptcy final rule looks ahead and plans for the possibility of addressing a DCO bankruptcy, the risk principles final rule ignores future events such as climate change.

My only concern regarding the bankruptcy rule, and it is a relatively small one, is one of timing. The proposal for this rule was issued this past April.[6] The comment period just closed on July 13. The Commission then issued a supplemental notice of proposed rulemaking in September.[7] That comment period ended October 26. Particularly for a rule of this size and intricacy, the time that staff had to review and analyze the comment letters and draft the final rule and preamble has been incredibly short. Staff has worked tirelessly on this rule to get to the finish line. However, I think both the Commission and the public might well have benefited from more time for review and reflection before issuing such an important rule.

On that note, I would like to close by again thanking staff for all of their hard work in producing this refresh of the Commission's part 190 rules to provide important customer protections.

Appendix 5—Statement of Commissioner Dan M. Berkovitz

I support the final rule amending the Commission's part 190 bankruptcy regulations. The amendments comprehensively update these regulations to address the increased size and speed of our markets and incorporate ''lessons learned'' from futures commission merchant (FCM) bankruptcies that occurred since the regulations were first adopted in 1983. The new derivatives clearing organization (DCO) bankruptcy regulations provide a framework to help market participants be prepared for such an event. While FCM bankruptcies are infrequent, and a registered DCO has never gone bankrupt, any such event could have significant financial impacts on many market participants, which, in turn, could have systemic implications. Improving the overall effectiveness and efficiency of the bankruptcy process fosters systemic stability and helps to better protect, preserve, and quickly return customer assets.

The Bankruptcy Code provides express preferences for positions and property of customers of an FCM or DCO debtor so that the customers and their counterparties can be assured that those positions and property will not be included in the debtor's general assets or clawed back post-filing. As a result, those positions and property (*e.g.,* customer margin) can be transferred to another FCM or liquidated for value quickly and returned to customers following the filing of the bankruptcy. In this way, an FCM bankruptcy can be resolved expeditiously, greatly reducing any uncertainty as to the treatment of positions and property held in the name of the debtor.[1] The protection of

[4] *See* Press Release Number 6300–12, CFTC, CFTC Files Complaint Against Peregrine Financial Group, Inc. and Russell R. Wasendorf, Sr., Alleging Fraud, Misappropriation of Customer Funds, Violation of Customer Fund Segregation Laws, and Making False Statements (July 10, 2012), *https://www.cftc.gov/PressRoom/PressReleases/6300-12.*

[5] *https://www.federalreserve.gov/paymentsystems/designated_fmu_about.htm.*

[6] Bankruptcy Regulations, 85 FR 36000 (June 12, 2020). *https://www.cftc.gov/LawRegulation/FederalRegister/proposedrules/2020-08482.html.*

[7] Bankruptcy Regulations, 85 FR 60110 (September 24, 2020). *https://www.cftc.gov/LawRegulation/FederalRegister/proposedrules/2020-21005.html.*

[1] The bankruptcy trustee is directed to ''return promptly to a customer any specifically identifiable security, property, or commodity contract to which such customer is entitled, or shall transfer, on such

customer assets and positions furthers market stability by reducing the need for customers to rush to liquidate or transfer the positions themselves prior to the bankruptcy to avoid such assets being entangled in the debtor's general assets. I am voting for the final rule because it significantly improves the likelihood of achieving these objectives.

As a general matter, commenters agreed that, overall, the final rule is a significant improvement. As described in the final rule release and my statement on the proposed rule, the revised regulations further solidify and implement important principles such as the preference for public customers, pro rata distributions within account classes, and prompt return of assets. The final rule does this not only through general statements, but also in specific procedures established in the rule.

Commenters raised a number of specific concerns regarding the final rule. As would be expected, these concerns were often (though not always) grouped by the specific interests of different types of market participants in the event of a bankruptcy of an FCM or DCO.

Bankruptcy occurs because there are not enough assets to cover a debtor's liabilities. In resolving the claims on the debtor's assets during a bankruptcy proceeding, the allocation of the shortfall must entail a balancing of equities that, unfortunately, most often leaves one or more creditors and other interested parties (*e.g.,* shareholders) with less than they expected to have if a bankruptcy had not occurred. As such, different creditor groups may have competing interests in the preferences and processes established in the Commission's bankruptcy regulations.

This reality is reflected in the thoughtful comments we received in response to the proposed rule. The final rule release addresses these comments in turn, discussing the pros and cons of the changes requested. In a number of instances, the final rule has been modified to address concerns raised where such modifications better achieve the stated principles of the regulations. For other concerns raised, as explained in the release, the balancing of the equities meant that the overall outcome of the bankruptcy proceeding would be better served by maintaining the rule as proposed. Particularly with respect to the bankruptcy rules, the fact that *nobody* gets *everything* they want likely means that the rule, for the most part, is well-balanced.

I would like to take this opportunity to address two particular areas of comments. Entities that represent certain ''public customers'' expressed concern regarding the greater ''reasonable'' discretion provided to bankruptcy trustees, which is intended to facilitate a speedier resolution and return of value to customers generally. These commenters are concerned that some customers could receive less than they could otherwise if the trustee makes poor choices when exercising its discretion or does not implement specific customer instructions. This concern is partially addressed with the addition of § 190.00(c)(3)(i)(C) to clarify how a trustee shall exercise its discretion to ''best achieve the overarching goal of protecting public customers as a class by enhancing recoveries for, and mitigating disruptions to, public customers as a class.'' Otherwise, as explained in the preamble, the discretion granted to the trustee is appropriate when weighing the benefits of prompt resolution of the bankruptcy with the other goals of the regulations.

The Commission also received numerous comments on the proposed DCO bankruptcy regulations. This is not surprising given that these regulations create, for the first time, a regulatory scheme for DCO bankruptcies. Many commenters expressed concerns regarding the direction in § 190.15 to the trustee to, within reasonable discretion, follow the debtor DCO's recovery and wind-down plans. The final rule, while largely leaving the proposed provision in place, did modify the rule text to emphasize that the trustee must act in a manner ''consistent with the protection of customers.'' In addition, the preamble notes that some of the concerns raised in this context are part of a broader discussion in the derivatives industry regarding the involvement of DCO members and customers in the governance, rulemaking, and structuring of the DCOs, and that the Commission continues to review these matters. I look forward to engaging in further discussions on these issues.

I commend the Commission staff, particularly Bob Wasserman, for the thoughtful effort that has clearly been put into the final rule release. The Commission staff has done an exemplary job of reviewing the comments received, addressing those concerns, and drafting the preamble in very understandable language. I also appreciate Commission staff's engagement with my office on a number of areas in the final rule.

The final rule modernizes the Commission's bankruptcy regulations and furthers the general principles these regulations serve. Public customers and markets will be better protected in the event of an FCM or DCO bankruptcy. For these reasons, I support the final rule.

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customer's behalf, such security, property, or commodity contract to a commodity broker that is not a debtor'' subject to CFTC regulations. 11 U.S.C. 766(c). Section 764(a) of the Bankruptcy Code provides that ''any transfer by the debtor of property that, but for such transfer, would have been customer property, may be avoided by the [bankruptcy] trustee . . . .'' 11 U.S.C. 764(a).