



U.S. COMMODITY FUTURES TRADING COMMISSION

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Gary Barnett
Director

Division of Swap Dealer and Intermediary Oversight

CFTC Letter No. 14-08
No-Action
January 10, 2014
Division of Swap Dealer and Intermediary Oversight

Re: Commission Regulation 30.7(c) – Staff No-Action position regarding holding of foreign futures secured amount outside the United States

Dear _____:

This is in response to your letter dated January 10, 2014, as supplemented by email correspondence submitted to the Division of Swap Dealer and Intermediary Oversight (“Division” or “DSIO”) of the Commodity Futures Trading Commission (“Commission”) on behalf of your client, “X”, a registered futures commission merchant (“FCM”). By your correspondence, you request that DSIO confirm it will not recommend that the Commission take enforcement action against “X” if, subject to certain terms and conditions noted below, “X” maintains 30.7 accounts with “Y” (in London) and “Z” (in Hong Kong) (collectively, “YZ”) in a manner described below.¹

¹ The Commission’s regulations are found at 17 CFR Part 1 et seq. (2013). Amendments to Regulation 30.7(c), among others, were recently adopted by the Commission as part of a package of comprehensive enhancements to the Commission’s customer protection regulations and may be found at 78 Fed. Reg. 68506 (Nov. 14, 2013). The term “30.7 account” is defined in new Regulation 30.1(g) to mean “any account maintained by [an FCM] for or on behalf of 30.7 customers to hold money, securities, or other property to margin, guarantee, or secure foreign futures or options positions.” 78 Fed Reg. at 68648.

Background

As represented in your correspondence, we understand that “X”, on behalf of its 30.7 customers,² currently maintains customer omnibus accounts in London and Hong Kong with “Y” and “Z”, respectively.³ “X” currently holds, and intends to hold in the future, only cash in these accounts.

Y takes advantage of the so-called “bank exemption” available under UK regulations with respect to the account held in London. The “bank exemption” permits banks to hold cash as a deposit rather than treating such funds as “client money” under the UK Financial Conduct Authority’s (“FCA”) Client Assets sourcebook (“CASS”). Under this “exemption,” banks are required to provide disclosure to clients advising them that their funds will be held as a deposit (*i.e.*, that the firm will hold the funds as a bank and not as a trustee) and that the funds will not be held in accordance with the FCA’s client money rules.⁴ Similarly, the Supervisory Policy Manual issued by the Hong Kong Monetary Authority provides, in relevant part, that in order to avoid regulatory overlap, a Registered Institution, *i.e.*, a bank that is a registered institution under the Securities and Futures Ordinance, is not subject to the Securities and Futures (Client Money) Rules.⁵

“YZ” has advised “X” that it is not in a position to offer client money protection under the Client Money Rules. Nonetheless, “X” desires to continue to clear its foreign futures and foreign options customers’ transactions through “YZ”.

Discussion

As noted above, the Commission recently adopted various new regulations, and amendments to existing regulations, designed to enhance the protections afforded to customers and customer funds. In this regard, the Commission amended Regulation 30.7(c) to provide in relevant part that:

“A [FCM] must deposit 30.7 customer funds under the laws and regulations of the foreign jurisdiction that provide the greatest degree of protection to such funds. A

² The term “30.7 customer” is defined in amended Regulation 30.1(f) to include any foreign futures or foreign options customer, as defined in Regulation 30.1(c), as well as any foreign-domiciled person who trades in foreign futures or foreign options through an FCM.

³ “X” maintains 30.7 accounts in other jurisdictions. However, this request is limited to 30.7 accounts maintained in London and Hong Kong.

⁴ See CASS 7.1.8R and 7.1.9G.

⁵ Supervisory Policy Manual, Supervision of Regulated Activities of SFC-Registered Authorized Institutions, par. 3.2.1. The UK and Hong Kong rules will be referred collectively herein as the “Client Money Rules.”

[FCM] may not by contract or otherwise waive any of the protections afforded customer funds under the laws of the foreign jurisdiction.”

In light of the amendment to this regulation, “X” has requested no-action relief from the Division to ensure that “X” may continue to hold its 30.7 customer accounts through “YZ” on and after January 13, 2014, the effective date of the Commission’s amendments to Regulation 30.7.⁶ Specifically, “X” requests that the Division confirm that it will not recommend enforcement action against “X” if “X” continues to hold its customer omnibus account(s) with “YZ”, provided that “X”, at all times, holds in properly-designated 30.7 accounts, in depositories located in the US, money and securities equal to or greater than the 30.7 customer funds that “X” maintains with “YZ” on behalf of 30.7 customers that are not subject to the Client Money Rules in the UK and Hong Kong, but rather are treated in accordance with the relevant jurisdiction’s “bank exemption.” You represent that this amount would also include money and securities that would constitute “X”’s targeted residual financial interest in the 30.7 accounts, as calculated and required in accordance with Commission Regulation 1.11 and NFA Financial Requirements, Section 16. In other words, you have represented that, with respect to those 30.7 accounts maintained with “YZ”, “X” would use its own funds to margin 30.7 customers’ foreign futures and foreign options positions and would effectively “double segregate” such accounts.

Based on the foregoing, the Division believes that it is appropriate to provide the no-action relief requested. Accordingly, the Division confirms that it will not recommend that the Commission take enforcement action against “X” if “X” continues to hold customer omnibus accounts with “YZ”, provided that, as represented, “X” holds, at all times, in properly-designated 30.7 accounts, in depositories located in the US: (1) money and securities equal to or greater than the 30.7 customer funds that “X” maintains with “YZ” on behalf of 30.7 customers that are not subject to the Client Money Rules in the UK and Hong Kong, but rather are treated subject to the relevant jurisdiction’s “bank exemption,” and (2) such additional money and securities required to constitute “X”’s targeted residual financial interest in the 30.7 accounts, as calculated in accordance with Commission Regulation 1.11 and NFA Financial Requirements, Section 16. This no-action position is intended to provide “X” with sufficient time to complete an assessment of whether the Client Money Rules provide a higher degree of protection relative to the “bank exemption” provisions under UK and Hong Kong laws. “X” must report to DSIO the result of its assessment by May 12, 2014. This no-action position will expire on September 10, 2014.

⁶ “X” has advised that it is currently considering, and has made no determination, whether 30.7 customer funds may be held pursuant to the “bank exemption,” discussed herein, consistent with the provisions of Commission Regulation 30.7(c). Due to the nature of this no-action request and the Division’s disposition thereof, it has not been necessary, and the Division is not taking a position with respect to, whether the “bank exemption” under UK regulations and/or the similar exemption under Hong Kong laws provide “the greatest degree of protection” under those regulatory regimes with respect to deposited 30.7 customer funds.

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This letter, and the position taken herein, are based upon the representations made to us and are subject to compliance with the conditions stated above. Any different, changed or omitted material facts or circumstances might require DSIO to reach a different conclusion and render this letter void. You must notify DSIO immediately in the event there is any change to the facts presented to the Division. This letter does not provide no-action relief to "X" from any provision of Regulation 30.7 except as specifically noted above, or from any other applicable requirements in the Commodity Exchange Act or in the Regulations issued thereunder. Further, this letter represents the position of DSIO only and does not necessarily represent the views of the Commission or of any other division or office of the Commission. Finally, this letter does not create or confer any rights for or obligations on any person or persons subject to compliance with the Commodity Exchange Act that bind the Commission or any of its other offices or divisions.

If you have any questions concerning this correspondence, please feel free to contact Lawrence Eckert, Special Counsel, at 646-746-9704.

Sincerely,

Gary Barnett
Director