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COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 39

RIN 3038-AF21

Derivatives Clearing Organization Risk Management Regulations to Account for the Treatment of Separate Accounts by Futures Commission Merchants

AGENCY: Commodity Futures Trading Commission.

ACTION: Notice of proposed rulemaking.

SUMMARY: The Commodity Futures Trading Commission (Commission or CFTC) is proposing to amend its derivatives clearing organization (DCO) risk management regulations adopted under the Commodity Exchange Act (CEA) to permit futures commission merchants (FCMs) that are clearing members (clearing FCMs) to treat the separate accounts of a single customer as accounts of separate entities for purposes of certain Commission regulations. The proposed amendments would establish the conditions under which a DCO may permit such separate account treatment.

DATES: Comments must be received on or before [**INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER**].

ADDRESSES: You may submit comments, identified by RIN 3038–AF21, by any of the following methods:

- *CFTC Comments Portal: https://comments.cftc.gov*. Select the "Submit Comments" link for this rulemaking and follow the instructions on the Public Comment Form.

- *Mail:* Send to Christopher Kirkpatrick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street NW, Washington, DC 20581.
- *Hand Delivery/Courier:* Follow the same instructions as for Mail, above.

Please submit your comments using only one of these methods. Submissions through the CFTC Comments Portal are encouraged. All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to *https://comments.cftc.gov*. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that you believe is exempt from disclosure under the Freedom of Information Act, a petition for confidential treatment of the exempt information may be submitted according to the procedures established in § 145.9
of the Commission's regulations. The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse or remove any or all of your submission from *https://comments.cftc.gov* that it may deem to be inappropriate for publication, such as obscene language.

FOR FURTHER INFORMATION CONTACT: Robert B. Wasserman, Chief Counsel, Division of Clearing and Risk, at 202-418-5092 or *rwasserman@cftc.gov*, or Daniel O'Connell, Special Counsel, Division of Clearing and Risk, at 202-418-5583 or *doconnell@cftc.gov*, at the Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street NW, Washington, DC 20581.

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I. BACKGROUND

A. <u>The Commission's Customer Funds Protection Regulations</u>

Two of the fundamental purposes of the CEA are the avoidance of systemic risk and the protection of market participants from misuses of customer assets.[1] The Commission has promulgated a number of regulations in furtherance of those objectives, including regulations designed to ensure that clearing FCMs appropriately margin customer accounts, and are not induced to cover one customer's margin shortfall with

[1] Section 3(b) of the CEA, 7 U.S.C. 5(b).

another customer's funds. In addition to protecting customer assets, these regulations serve the purpose of avoidance of systemic risk by mitigating the risk that a customer default in its obligations to a clearing FCM results in the clearing FCM in turn defaulting on its obligations to a DCO, which could adversely affect the stability of the broader financial system.

Section 4d(a)(2) of the CEA and Commission regulation § 1.20(a) require an FCM to separately account for and segregate all money, securities, and property which it has received to margin, guarantee, or secure the trades or contracts of its commodity customers.[2] Additionally, section 4d(a)(2) of the CEA and Commission regulation § 1.22(a) prohibit an FCM from using the money, securities, or property of one customer to margin or settle the trades or contracts of another customer.[3] This requirement is designed to prevent disparate treatment of customers by an FCM and mitigate the risk that there will be insufficient funds in segregation to pay all customer claims if the FCM becomes insolvent.[4] Section 4d(a)(2) of the CEA and Commission regulations §§ 1.20 and 1.22 effectively require an FCM to add its own funds into segregation in an amount equal to the sum of all customer deficits to prevent the FCM from being induced to use one customer's funds to margin or carry another customer's trades or contracts.[5]

Section 5b of the CEA,[6] as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010,[7] sets forth eighteen core principles with which DCOs must comply to register and maintain registration as DCOs with the Commission. In

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[2] 7 U.S.C. 6d(a)(2); 17 CFR 1.20(a).
[3] 7 U.S.C. 6d(a)(2); 17 CFR 1.22(a).
[4] Prohibition of Guarantees Against Loss, 46 FR 11668, 11669 (Feb. 10, 1981).
[5] 7 U.S.C. 6d(a)(2); 17 CFR 1.20; 17 CFR 1.22; Prohibition of Guarantees Against Loss, 46 FR at 11669.
[6] 7 U.S.C. 7a-1(b).
[7] Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, 124 Stat. 1376 (2010).

2011, the Commission adopted regulations for DCOs to implement Core Principle D, which concerns risk management.[8] These regulations include a number of provisions that require a DCO to in turn require that its clearing members take certain steps to support their own risk management in order to mitigate the risk that such clearing members pose to the DCO. Specifically, regulation § 39.13(g)(8)(iii) provides that a DCO shall require its clearing members to ensure that their customers do not withdraw funds from their accounts with such clearing members unless the net liquidating value plus the margin deposits remaining in the customer's account after the withdrawal would be sufficient to meet the customer initial margin requirements with respect to the products or portfolios in the customer's account, which are cleared by the DCO.[9] Regulation § 39.13(g)(8)(iii) was designed to mitigate the risk that a clearing member fails to hold, from a customer, funds sufficient to cover the required initial margin for the customer's cleared positions, and, in light of the use of omnibus margin accounts, mitigate the likelihood that the clearing member will effectively cover one customer's margin shortfall using another customer's funds.

In adopting regulation § 39.13(g)(8)(iii), the Commission stated[10] that the regulation was consistent with the definition of "Margin Funds Available for Disbursement" in the Margins Handbook[11] prepared by the Joint Audit Committee (JAC), a representative committee of U.S. futures exchanges and the National Futures

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[8] Section 5b(c)(2)(D) of the CEA, 7 U.S.C. 7a-1(c)(2)(D); Derivatives Clearing Organization General Provisions and Core Principles, 76 FR 69334, 69335 (Nov. 8, 2011).
[9] 17 CFR 39.13(g)(8)(iii).
[10] Derivatives Clearing Organization General Provisions and Core Principles, 76 FR at 69379.
[11] JAC Margins Handbook, available at *https://www.jacfutures.com/jac/MarginHandBookWord.aspx*.

Association (NFA).[12] The Commission noted that while designated self-regulatory organizations (DSROs) reviewed FCMs to determine whether they appropriately prohibited their customers from withdrawing funds from their futures accounts, it was unclear to what extent that requirement applied to cleared swap accounts when such swaps were executed on a designated contract market that participated in the JAC.[13] The Commission also noted that clearing members that cleared only swaps that were executed on a swap execution facility were not subject to the requirements of the JAC Margins Handbook or review by a DSRO.[14] Thus, regulation § 39.13(g)(8)(iii) was also designed to provide certainty as to the scope of these risk mitigation and customer protection standards as they relate to futures and swap positions carried in customer accounts by clearing members and cleared by a DCO.

B. <u>The Divisions' No-Action Position</u>

On July 10, 2019, the Division of Swap Dealer and Intermediary Oversight (DSIO) (now Market Participants Division (MPD)) and the Division of Clearing and Risk (DCR) published CFTC Letter No. 19-17, which, among other things, provides guidance with respect to the processing of margin withdrawals under regulation § 39.13(g)(8)(iii) and announced a conditional and time-limited no-action position for certain such

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[12] Joint Audit Committee, JAC Members, available at *https://www.jacfutures.com/jac/Members.aspx*. Self-regulatory organizations, such as commodity exchanges and registered futures associations (*e.g.*, NFA), enforce minimum financial and reporting requirements, among other responsibilities, for their members. *See* Commission regulation § 1.3, 17 CFR 1.3. Pursuant to Commission regulation § 1.52(d), when an FCM is a member of more than one self-regulatory organization, the self-regulatory organizations may decide among themselves which of them will assume primary responsibility for these regulatory duties and, upon approval of such a plan by the Commission, the self-regulatory organization assuming such primary responsibility will be appointed the designated self-regulatory organization for the FCM. 17 CFR 1.52(d).
[13] Derivatives Clearing Organization General Provisions and Core Principles, 76 FR at 69379.
[14] *Id.*

withdrawals.[15] The advisory followed discussions with and written representations from the Asset Management Group of the Securities Industry and Financial Markets Association (SIFMA-AMG), the Chicago Mercantile Exchange (CME), the Futures Industry Association (FIA), the JAC, and several FCMs, regarding practices among FCMs and their customers related to the handling of separate accounts of the same customer.[16] CFTC Letter No. 19-17 used the term "beneficial owner" synonymously with the term "customer," as "beneficial owner" was, in this context, commonly used to refer to the customer that is financially responsible for an account. Additionally, as discussed further below, in the customer relationship context, FCMs often deal directly with a commodity trading advisor acting as an agent of the customer rather than the customer itself. For the avoidance of confusion (*e.g.*, with regard to the terms "owner" or "ownership," as those terms are used in Forms 40 and 102, or parts 17-20, or with regard to the term "beneficial owner," as that term may be used by other agencies), this proposed rulemaking uses only the term "customer."

The written representations preceding the issuance of CFTC Letter No. 19-17 included letters filed separately by SIFMA-AMG, CME, and FIA (collectively, the "Industry Letters").[17] Citing regulation § 39.13(g)(8)(iii)'s requirements related to the

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[15] CFTC Letter No. 19-17, July 10, 2019, available at *https://www.cftc.gov/csl/19-17/download* as extended by CFTC Letter No. 20-28, Sept. 15, 2020, available at *https://www.cftc.gov/csl/20-28/download*; CFTC Letter No. 21-29, Dec. 21, 2021, available at *https://www.cftc.gov/csl/21-29/download*; and CFTC Letter No. 22-11, Sept. 15, 2022, available at *https://www.cftc.gov/csl/22-11/download*.

[16] SIFMA-AMG letter dated June 7, 2019 to Brian A. Bussey and Matthew B. Kulkin (SIFMA-AMG Letter); CME letter dated June 14, 2019 to Brian A. Bussey and Matthew B. Kulkin (CME Letter); and FIA letter dated June 26, 2019 to Brian A. Bussey and Matthew B. Kulkin (First FIA Letter).

[17] The Commission notes that while CME disagreed with certain aspects of FIA's letter that fall beyond the scope of this rulemaking, CME's letter noted that CME was "amenable to the Commission amending Rule 39.13(g)(8)(iii) to allow a DCO to permit a[n] FCM to release excess funds from a customer's separate account notwithstanding an outstanding margin call in another account of the same customer provided that certain specified risk-mitigating conditions . . . are satisfied." CME Letter.

withdrawal of customer initial margin, and JAC Regulatory Alert #19-02 reminding FCMs of those requirements,[18] SIFMA-AMG and FIA explained that provisions in certain FCM customer agreements provide that certain accounts carried by the FCM that have the same customer are treated as accounts for different legal entities (*i.e.*, "separate accounts").[19]

As FIA explained, there are a variety of reasons why a customer may want separate treatment for its accounts under such an agreement.[20] For instance, an institutional customer, such as an investment or pension fund, may allocate assets to investment managers under investment management agreements that require each investment manager to invest a specified portion of the customer's assets under management in accordance with an agreed trading strategy, independent of the trading that may be undertaken for the customer by the same or other investment managers acting on behalf of other accounts of the customer.[21] In such a situation, an investment manager may, in order to implement their trading strategy effectively, want assurance that the portion of funds they have been given to manage is entirely available to them, and will not be affected by the activities of other investment managers who manage other portions of the customer's assets. Additionally, a commercial enterprise may establish separate agreements to leverage specific broker expertise on products or to diversify risk management strategies.[22] In such cases, each separate account is subject to a separate

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[18] JAC, Regulatory Alert #19-02, May 14, 2019, available at *https://www.jacfutures.com/jac/jacupdates/2019/jac1902.pdf*.
[19] SIFMA-AMG Letter; First FIA Letter.
[20] First FIA Letter.
[21] *See id.*
[22] *Id.*

customer agreement, which the FCM negotiates directly with, in many cases, the customer's agent, which often will be an investment manager.[23]

SIFMA-AMG and FIA asserted that, subject to appropriate FCM internal controls and procedures, separate accounts should be treated as separate legal entities for purposes of regulation § 39.13(g)(8)(iii); *i.e.*, separate accounts should not be combined when determining an account's margin funds available for disbursement.[24] SIFMA-AMG and FIA maintained that such separate account treatment should not be expected to expose an FCM to any greater regulatory or financial risk, and asserted that an FCM's internal controls and procedures could be designed to assure that the FCM does not undertake any additional risk as to the separate account.[25] The Industry Letters included a number of examples of such controls and procedures.[26]

In its letter, SIFMA-AMG suggested that it would be possible to allow for separate account treatment without undermining the risk mitigation and customer protection goals of regulation § 39.13(g)(8)(iii).[27] SIFMA-AMG recognized that there may be some instances, such as a customer default, in which separate account treatment would no longer be appropriate.[28] SIFMA-AMG stated that an FCM could agree to first satisfy any amounts owed from agreed assets related to a separate account, and continue to release funds until the FCM provided the separate account with a notice of an event of default under the applicable clearing account agreement, and determined that it is no longer prudent to continue to separately margin the separate accounts, provided that such

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[23] *Cf. id.*
[24] SIFMA-AMG Letter; First FIA Letter.
[25] SIFMA-AMG Letter; First FIA Letter.
[26] SIFMA-AMG Letter; First FIA Letter; CME Letter.
[27] SIFMA-AMG Letter.
[28] *Id.*

actions are consistent with the FCM's written internal controls and procedures.[29] SIFMA-AMG further stated that, in such instance, the FCM would retain the ability to ultimately look to funds in other accounts of the customer, including accounts under different control, and the right to call the customer for funds.[30] CME similarly asserted that disbursements on a separate account basis should not be permitted in certain circumstances, such as financial distress, that fall outside the "ordinary course of business."[31] While CME asserted that the plain language of regulation § 39.13(g)(8)(iii) unambiguously forbids disbursements on a separate account basis, CME noted that it would be amenable to the Commission amending the regulation to permit such disbursements, subject to certain such risk-mitigating conditions.[32]

SIFMA-AMG and FIA requested that DCR confirm that it would not recommend that the Commission initiate an enforcement action against a DCO that permits its clearing FCMs to treat certain separate accounts as accounts of separate entities for purposes of regulation § 39.13(g)(8)(iii),[33] and confirm that a clearing FCM may release excess funds from a separate customer account notwithstanding an outstanding margin call in another account of the same customer.[34]

In CFTC Letter No. 19-17, DCR stated that, in the context of separate accounts, the risk management goals of regulation § 39.13(g)(8)(iii) may effectively be addressed if a clearing FCM carrying a customer with separate accounts meets certain conditions,

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[29] *Id.*
[30] *Id.*
[31] CME Letter.
[32] *Id.*
[33] FIA specifically noted that such a no-action position could be conditioned on the FCM maintaining certain internal controls and procedures.
[34] SIFMA-AMG Letter; First FIA Letter; *see also* CME Letter.

which were derived from the Industry Letters and specified in CFTC Letter No. 19-17.[35] DCR stated that it would not recommend that the Commission take enforcement action against a DCO if the DCO permits its clearing FCMs to treat certain separate accounts as accounts of separate entities for purposes of regulation § 39.13(g)(8)(iii) subject to these conditions.[36] The no-action position extended until June 30, 2021, in order to provide DCR with time to recommend, and the Commission with time to determine whether to conduct and, if so, conduct, a rulemaking to implement a permanent solution.[37] CFTC Letter No. 20-28, published on September 15, 2020, extended the no-action position until December 31, 2021 due to challenges presented by the COVID-19 pandemic.[38] CFTC Letter No. 20-28 stated that if the process to consider codifying the no-action position provided for by CFTC Letter No. 19-17 was not completed by that date, DSIO and DCR would consider further extending the no-action position.[39] MPD and DCR published CFTC Letter No. 21-29, further extending the no-action position until September 30, 2022.[40] On September 15, 2022, MPD and DCR published CFTC Letter No. 22-11, which further extended the no-action position until the earlier of September 30, 2023 or the effective date of any final Commission action relating to regulation § 39.13(g).[41] As with CFTC Letter No. 21-29, this latest extension was issued in order to provide additional time for the Commission to consider a rulemaking.

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[35] CFTC Letter No. 19-17.
[36] *Id.*
[37] *Id.*
[38] CFTC Letter No. 20-28.
[39] *Id.*
[40] CFTC Letter No. 21-29.
[41] CFTC Letter No. 22-11.

II. PROPOSED AMENDMENTS TO REGULATION § 39.13

The Commission preliminarily believes that proposed regulation § 39.13(j) relating to separate account treatment in connection with the withdrawal of customer initial margin is consistent with the customer protection and risk management goals of regulation § 39.13(g)(8)(iii). As further described below, the Commission preliminarily believes that preventing the under-margining of customer accounts and mitigating the risk of a clearing member default (and the potential for systemic risk), is effectively addressed by the standards set forth in the proposed regulation where the clearing FCM treats the separate accounts of a customer as accounts of separate entities consistent with the conditions outlined in proposed regulation § 39.13(j).

A. Overview of Proposed Regulation § 39.13(j)

The Commission proposes to amend regulation § 39.13 to add new paragraph (j) allowing a DCO to permit a clearing FCM to treat the separate accounts of customers as accounts of separate entities for purposes of regulation § 39.13(g)(8)(iii), if such clearing member's written internal controls and procedures permit it to do so, and the DCO requires its clearing members to comply with conditions specified in proposed regulation § 39.13(j)(1) through (14), which are substantially similar to the conditions specified in CFTC Letter No. 19-17.[42] Those conditions are in turn designed to ensure that clearing FCMs (i) carry out such separate account treatment in a consistent and documented manner; (ii) monitor customer accounts on a separate and combined basis; (iii) identify

[42] CFTC Letter No. 19-17 conditioned the no-action position with regard to the treatment of separate accounts on 16 enumerated conditions. Proposed regulation § 39.13(j) incorporates conditions 15 and 16 in CFTC Letter No. 19-17, regarding, respectively, (i) the clearing member's notification to its DSRO and DCOs of which it is a clearing member of the application of separate account treatment; and (ii) the clearing member's maintenance of a list of all separate accounts, as proposed regulation § 39.13(j)(14)(ii) and (iii), respectively.

and act upon instances of financial or operational distress that necessitate a cessation of separate account treatment; (iv) provide appropriate disclosures to customers regarding separate account treatment; and (v) apprise their DSROs when they apply separate account treatment or an event has occurred that would necessitate cessation of separate account treatment. The Commission believes that separate account treatment, subject to these conditions, is consistent with Core Principle D. In addition, the Commission notes that nothing in this proposed rulemaking, or in proposed regulation § 39.13(j), would preclude a DCO from establishing or enforcing requirements for clearing FCMs that are additional to or more stringent than those set forth in the proposed regulation. Rather, proposed regulation § 39.13(j) is intended to establish a minimum set of risk-mitigating conditions that DCOs that wish to permit separate account treatment must require of their clearing FCMs that choose to engage in such treatment.

Proposed regulation § 39.13(j) is intended to provide an alternative means of achieving the risk management goals served by regulation § 39.13(g)(8)(iii). As a result, proposed regulation § 39.13(j) would not prohibit the application of portfolio margining or cross-margining treatment within a particular separate account. The Commission notes that because a number of clearing FCMs already comply with the conditions set forth in CFTC Letter No. 19-17, such clearing FCMs already comply in significant part with the requirements of proposed regulation § 39.13(j), which, if adopted, DCOs choosing to permit separate account treatment would be required to apply to such clearing FCMs.

Regulation § 39.13(g)(8)(iii) applies to margin in a customer's account with respect to all products and swap portfolios held in such customer's account *which are*

cleared by the derivatives clearing organization (emphasis added). Accordingly, the requirements of regulation § 39.13(g)(8)(iii) apply to a DCO[43] with respect to the clearing of (a) futures, (b) swaps, or (c) foreign futures or foreign options subject to Commission regulation § 30.7, to the extent the DCO clears those specific products in a customer's account. Additionally, because the requirements of proposed regulation § 39.13(j) are an alternative means to achieve the risk management goals of regulation § 39.13(g)(8)(iii), the requirements of proposed regulation § 39.13(j) would apply to a DCO with respect to the clearing of futures, swaps, or foreign futures or foreign options subject to regulation § 30.7, to the extent the DCO permits separate account treatment and clears those specific types of products in a customer account subject to separate account treatment.

For example, if a DCO that permits separate account treatment clears only futures contracts (or only futures and swaps), regulation § 39.13(g)(8)(iii) (and the alternative path in proposed regulation § 39.13(j)) would apply to the DCO only with respect to the clearing by its members of such futures contracts (or, respectively, such futures and swaps). Similarly, if a DCO clears foreign futures or foreign options subject to regulation § 30.7, regulation § 39.13(g)(8)(iii) (and the alternative path in proposed regulation § 39.13(j)) would apply to that DCO with respect to the clearing by its member of such 30.7 contracts.

As a practical matter, an FCM's futures account for a customer includes all futures products that the FCM clears for that customer, and the initial margin *requirement* for that account would be the sum of the initial margin the FCM charges the customer for each of those contracts (including, *e.g.*, effects of portfolio margining), regardless of the

[43] This discussion does not apply to a DCO regulated pursuant to subpart D of part 39.

DCO at which such contracts are cleared. The margin value available – "net liquidating value plus the margin deposits remaining" – is calculated across the account. Thus, by way of example, a customer whose account contains products cleared by an FCM as a clearing member at two DCOs could generally not be under-margined with respect to products cleared at only one of the two DCOs. Rather, since the margin value available collateralizes the products cleared at both DCOs, the customer would necessarily be under-margined with respect to products cleared at both DCOs, or at neither DCO.[44]

The same applies, *mutatis mutandis*, to a customer's swap portfolios cleared through the FCM at multiple DCOs. It would also apply, *mutatis mutandis*, to a customer's foreign futures or foreign options subject to regulation § 30.7 cleared through the FCM at multiple clearinghouses, with a slight modification: If all of those foreign futures or foreign options are cleared at a clearinghouse that is not registered with the Commission as a DCO (or is so registered, but only subject to subpart D of part 39), then there would be no DCO subject to § 39.13(g)(8)(iii) that would be required to apply that regulation to the FCM. However, if any of those foreign futures or foreign options are cleared by the FCM as a clearing member of a DCO registered with the Commission (other than one registered subject to subpart D), then that DCO would be required to apply § 39.13(g)(8)(iii), or, if adopted, the alternative in proposed § 39.13(j), and (because margin requirements apply across the customer's account, here, a § 30.7 account) the margin requirement that would need to be met would take into account all such foreign futures and foreign options, regardless of the clearinghouse at which they ultimately are cleared.

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[44] There may be slight complications if, *e.g.*, for certain of the collateral posted by the customer, one DCO requires the FCM to apply higher haircuts than the other DCO.

Clearing FCMs are additionally bound by the rules of DCOs and/or self-regulatory organizations (SROs), and such entities have taken the position that such rules apply to a broader set of circumstances than § 39.13(g)(8)(iii). For example, the JAC Margins Handbook, the provisions of which SROs may apply directly to FCMs, contains provisions that regulation § 39.13(g)(8)(iii) was based on.[45] The JAC Margins Handbook provides that "[a]ll identically owned accounts must be combined for purposes of determining the amount of funds available for disbursement within the account classifications of customer segregated, customer secured, or nonsegregated."[46] The JAC Margins Handbook further provides that an FCM may not make a disbursement to a customer if the value of such customer's combined accounts, less required margin on open positions in such accounts, is zero or negative.[47] Therefore the JAC Margins Handbook effectively calls for each FCM to ensure that its customers, including customers holding accounts subject to regulation § 30.7 (30.7 customers), do not withdraw funds from their accounts with such FCM unless the net liquidating value plus the margin deposits remaining in the applicable customer's account after the withdrawal is sufficient to meet the customer's margin requirements with respect to the products or portfolios in the customer's account.

The JAC issued Regulatory Alert 19-06 to effectively incorporate the no-action position provided by CFTC Letter 19-17 to the provisions of the JAC Margins Handbook as it relates to 30.7 customer accounts.[48] Specifically, Regulatory Alert 19-06 provides

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[45] *See supra* n. 11 and accompanying text.
[46] JAC Margins Handbook at 10-2, available at *https://www.jacfutures.com/jac/MarginHandBookWord.aspx*.
[47] *Id.*
[48] JAC, Regulatory Alert #19-06, Aug. 28, 2019, available at *https://www.jacfutures.com/jac/jacupdates/2019/jac1906.pdf.*

that, notwithstanding the restrictions contained in the JAC Margins Handbook, FCMs may apply CFTC Letter No. 19-17, including the appropriate conditions, to the separate accounts of 30.7 customers in determining margin funds available for disbursement.[49]

Similarly, CME, in Financial and Regulatory Bulletin 19-02,[50] noted that the foregoing provisions of the JAC Margins Handbook apply to CME, CBOT, NYMEX, and COMEX Rule 930.F. and CME Rule 8G930.F. (Release of Excess Performance Bond), and that "CME Clearing is permitting its FCM clearing members to treat separate accounts of the same beneficial owner as separate accounts under Rule 930.F. for purposes of determining performance bond funds available for disbursement under the conditions of the CFTC Letter."

Request for Comment

Question 1: The Commission requests comment regarding whether it should consider any conditions additional to those contained in proposed regulation § 39.13(j) below, or modify or remove any of the conditions proposed herein.

Question 2: The Commission requests comment regarding whether any further action is necessary and appropriate to apply the requirements DCOs are required to apply to their clearing members regarding customer withdrawal of initial margin under regulation § 39.13(g)(8)(iii) and proposed regulation § 39.13(j), directly to non-clearing FCMs or to FCMs that carry regulation § 30.7 customer accounts that are not cleared at a DCO that is registered with the Commission (or are so registered, but only subject to

[49] *Id.* at 2. The JAC subsequently issued Regulatory Alert 20-02 extending the relief for withdrawals from separate 30.7 customer accounts under the JAC Margins Handbook to the earlier of the termination of the no-action position provided by CFTC Staff Letters or to the adoption of a final regulation addressing the withdrawal of funds from separate 30.7 customer accounts. JAC, Regulatory Alert #20-02, Sept. 23, 2020, available at *https://www.jacfutures.com/jacupdates/2020/jac2002.pdf.*

[50] Available at *https://www.cmegroup.com/notices/clearing/2019/07/FRB-19-02.html*.

subpart D of part 39) . If so, who (*e.g.*, SROs or the Commission) should take such action, and what should that action be? Would such actions risk causing actual or potential conflicts with the rules or practices of foreign clearing organizations or foreign contract markets? If so, please provide references.

B. Proposed Regulation § 39.13(j)(1)

Proposed regulation § 39.13(j)(1)(i) defines "separate account" as referring to any one of multiple accounts of the same customer that are carried by the same FCM that is a clearing member of a DCO. Proposed regulation § 39.13(j)(1) also sets forth the first condition: the clearing member may only permit disbursements on a separate account basis during the "ordinary course of business," as that term is defined therein. Proposed regulation § 39.13(j)(1)(ii) provides that, for purposes of proposed regulation § 39.13(j), the term "ordinary course of business" refers to the standard day-to-day operation of the clearing member's business relationship with its customer, a condition where there are no unusual circumstances that might indicate either an increased level of risk that the customer may fail promptly to perform its financial obligations to the clearing FCM, or decreased financial resilience on the part of the clearing FCM.

Consistent with the conditions set forth in CFTC Letter No. 19-17, proposed regulation § 39.13(j)(1)(ii)(A) through (I) specifies events that are inconsistent with the ordinary course of business. The occurrence of such an event would require the clearing member to cease permitting disbursements on a separate account basis as to one or more specific customers (in the case of (A) through (F) below), or as to all customer accounts

receiving separate account treatment (in the case of (G) through (I) below).[51] Such events are as follows:

- (A) The customer, including any separate account of the customer, fails to deposit or maintain initial or maintenance margin or make payment of variation margin or option premium as specified in proposed regulation § 39.13(j)(4).
- (B) The occurrence and declaration by the clearing member of an event of default as defined in the account documentation executed between the clearing member and the customer.
- (C) A good faith determination by the clearing member's chief compliance officer, senior risk managers, or other senior management, following the clearing member's own internal escalation procedures, that the customer is in financial distress, or there is significant and bona fide risk that the customer will be unable promptly to perform its financial obligations to the clearing member, whether due to operational reasons or otherwise.
- (D) The insolvency or bankruptcy of the customer or a parent company of the customer.
- (E) The clearing member receives notification that a board of trade, a DCO, an SRO (as defined in Commission regulation § 1.3 or section 3(a)(26) of the Securities Exchange Act of 1934), the Commission, or another regulator with jurisdiction over the customer, has initiated an action with respect to the customer based on an allegation that the customer is in financial distress.

[51] Whether the clearing member would be required to cease permitting disbursements on a separate account basis as to one or more specific customers or as to all customer accounts receiving separate account treatment depends on whether the relevant non-ordinary course of business event occurs with respect to one or more specific customers or with respect to the clearing member itself.

- (F) The clearing member is directed to cease permitting disbursements on a separate account basis, with respect to one or more customers, by a board of trade, a DCO, an SRO, the Commission, or another regulator with jurisdiction over the clearing member, pursuant to, as applicable, board of trade or DCO rules, government regulations, or law.
- (G) The clearing member is notified by a board of trade, a DCO, an SRO, the Commission, or another regulator with jurisdiction over the clearing member,[52] that the board of trade, the DCO, the SRO, the Commission, or other regulator, as applicable, believes the clearing member is in financial or other distress.
- (H) The clearing member is under financial or other distress, as determined in good faith by its chief compliance officer, one of its senior risk managers, or other senior manager.
- (I) The bankruptcy of the clearing member or a parent company of the clearing member.

Proposed regulation § 39.13(j)(1)(iii) provides that the clearing member must communicate to its DSRO and any DCO of which it is a clearing member the occurrence of any one of the events enumerated in proposed regulation § 39.13(j)(1)(ii)(A) through (I). The clearing member would need to make such communication promptly in writing, and in any case no later than the next business day following the date on which the clearing member identifies or is informed that such event has occurred.

Additionally, proposed regulation § 39.13(j)(1)(iv) provides that a clearing member that has ceased permitting disbursements on a separate account basis as a result

[52] *E.g.*, the Securities and Exchange Commission, or a foreign regulator.

of the occurrence of a non-ordinary course of business event may resume permitting such disbursements if it reasonably believes, based on new information, that the circumstances leading it to cease separate account treatment have been cured.[53] The clearing member would be required to provide in writing to its DSRO and any DCO of which it is a clearing member a notification that it will resume separate account treatment, and the factual basis and rationale for its conclusion that the circumstances leading it to originally cease separate account treatment have been cured.

In requesting a no-action position, SIFMA-AMG stated that separate account treatment should not be expected to expose an FCM to any greater regulatory or financial risk, and that, subject to appropriate controls and procedures, an FCM could agree to release funds from separate accounts until the FCM provides the separate account with a notice of default and determines it is no longer prudent to continue separate account treatment.[54] That separate account treatment should be discontinued under certain circumstances is further reflected in CME's recommendation that separate account treatment be permitted only during the ordinary course of business. As CME explained, FCMs should maintain the flexibility to determine that either the customer or the FCM itself is in distress and pause disbursements until the customer's other account can demonstrably meet the call to deposit funds.[55] Similarly, as CME noted, an FCM should not be purposely releasing funds to a customer when the customer's overall account is in deficit, as doing so may create a shortfall in segregated, secured or cleared swaps

[53] If the circumstances in question were an action or direction by one of the entities described in paragraphs (E) through (G), then the cure of those circumstances would require the withdrawal or other appropriate termination of such action or direction.
[54] SIFMA-AMG Letter.
[55] CME Letter.

accounts in the event the FCM becomes insolvent.[56] However, the Commission acknowledges that in some instances, an FCM or customer may exit a state of financial, operational, or other distress, such that resumption of separate account treatment would be appropriate. By explicitly providing clearing members with an avenue to resume separate account treatment consistent with the resumption of the ordinary course of business, while requiring disclosure of the basis for doing so, the Commission seeks to incentivize transparency between clearing members and their DSROs and DCOs with respect to (a) conditions at clearing members or customers that could indicate operational or financial distress, and (b) more generally, the risk management program at the clearing member.

Proposed regulation § 39.13(j)(1) is designed to ensure that disbursements are permitted on a separate account basis only during the sound and routine operation of the clearing member's business relationship with its customer. Certain events signaling financial distress of the clearing member or customer are inconsistent with the normal operation of the business relationship between the clearing member and its customer. The Commission believes that, when such events occur—and during the duration of their occurrence—continuing to allow DCOs to permit separate account treatment would be contrary to the goals of protecting customer funds and mitigating systemic risk.

Request for Comment

Question 3: The Commission requests comment regarding whether it should (i) consider any events beyond those enumerated in proposed regulation § 39.13(j)(1)(ii)(A) through (I) as inconsistent with the ordinary course of business for purposes of the

[56] *Id.*

application of proposed regulation § 39.13(j); (ii) change the specification of any of the events in proposed regulation § 39.13(j)(1)(ii)(A) through (I); or (iii) delete any of those events (because the proposed event is not inconsistent with the ordinary course of business).

C. Proposed Regulation § 39.13(j)(2)

Proposed regulation § 39.13(j)(2) would require that the clearing member obtain from the customer or, as applicable, the manager of a separate account, information sufficient to (i) assess the value of the assets dedicated to the separate account and (ii) identify the direct or indirect parent company of the customer, as applicable, if the customer has a direct or indirect parent company.[57] Proposed regulation § 39.13(j)(2)(i) is intended to ensure that clearing members have visibility with respect to customers' financial resources appropriate to ensure that a customer's separate account is adequately margined, and to identify when a customer's financial circumstances would necessitate the cessation of separate account treatment. Proposed regulation § 39.13(j)(2)(i) contemplates that, in certain instances, an investment manager may manage one or more accounts under power of attorney on a customer's behalf; in such cases, a clearing member may obtain the requisite financial information from the investment manager. Proposed regulation § 39.13(j)(2)(ii) is intended to ensure that clearing members have sufficient information to identify the direct or indirect parent company of a customer so that they may identify when a parent company of a customer has become insolvent, for purposes of proposed regulation § 39.13(j)(1)(ii)(D).

[57] The Commission understands that, in certain cases, such as when a customer is a fund, the customer may not have a parent company. In such cases, the requirement to obtain information sufficient to identify the direct or indirect parent company would not apply.

Request for Comment

Question 4: The Commission requests comment on whether proposed regulation § 39.13(j)(2) should require a clearing member to obtain from a customer or, as applicable, the manager of a separate account, any specific information or documentation relevant to determining the value of assets dedicated to a separate account, or, more broadly, any information relevant to determining the value of assets available to meet the obligations of the customer's accounts on a combined basis. The Commission further requests comment on whether it should prescribe a minimum requirement of how often such information should be obtained and/or updated.

D. Proposed Regulation § 39.13(j)(3)

Proposed regulation § 39.13(j)(3) provides that the clearing member's internal risk management policies and procedures must provide for stress testing and credit limits for customers with separate accounts. Furthermore, proposed regulation § 39.13(j)(3) provides that stress testing must be performed, and credit limits must be applied, both on an individual separate account and on a combined account basis. By conducting stress testing on both an individual separate account and on a combined account basis, a clearing member can determine the potential for significant loss in the event of extreme market conditions, and the ability of traders and clearing members to absorb those losses, with respect to each individual account of a customer, as well as with respect to all of the customer's accounts.[58] Additionally, by applying credit limits on both an individual

[58] *See* 17 CFR 1.73(a)(4) (requiring each FCM that is a clearing member of a DCO to conduct stress tests under extreme but plausible conditions of all positions in the proprietary account and in each customer account that could pose material risk to the FCM at least once per week); *see also* Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management, 77 FR 217278, 21289 (Apr. 9, 2012).

separate account basis and on a combined account basis, a clearing member can be in a better position to manage the financial risks they incur as a result of clearing trades both for a customer's separate account and for all of the customer's accounts.[59] By better managing the financial risks posed by customers and understanding the extent of customers' risk exposures, clearing members can better mitigate the risk that customers do not maintain sufficient funds to meet initial margin requirements, and anticipate and mitigate the risk of the occurrence of certain of the events detailed in proposed regulation § 39.13(j)(1)(ii)(A)-(I), such as a customer's failure to make margin payments as specified by proposed regulation § 39.13(j)(4).

E. Proposed Regulation § 39.13(j)(4)

Proposed regulation § 39.13(j)(4) provides that each separate account must be on a one business day margin call, subject to certain requirements that apply solely for purposes of that proposed regulation. Providing for a "one business day margin call," as defined in this paragraph, ensures that margin shortfalls are timely corrected, and a customer's inability to meet a margin call is timely identified. However, in certain circumstances, it may be impracticable for payments to be received on a same-day basis due to the mechanics of international payment systems. In proposing requirements to define timely payment of margin for purposes of the standard set forth in proposed regulation § 39.13(j)(4), the Commission's goal is to establish requirements that reflect industry best practices among DCOs, clearing members, and customers.

[59] *See* 17 CFR 1.73(a)(1) (requiring clearing FCMs to establish risk-based limits in the proprietary account, and in each customer account, based on position size, order size, margin requirements, or similar factors); *see also* Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management, 77 FR at 21287.

Specifically, the Commission understands that, while margin calls made in the morning in the U.S. Eastern Time Zone are typically capable of being met on a same-day basis when margin is paid in United States dollars (USD) and Canadian dollars (CAD), the operation of time zones and banking conventions in other jurisdictions may necessitate additional time when margin is paid in other currencies. For example, the Commission understands that margin paid in Japanese yen (JPY) is typically received two business days after a margin call is issued, and margin paid in British pounds (GBP), euros (EUR), and other non-USD/CAD/JPY currencies is typically received one business day after a margin call is issued.

Proposed regulation § 39.13(j)(4)(i) provides that, subject to certain exceptions, discussed below, a "one business day margin call" (as that term used in proposed regulation § 39.13(j)(4)), issued by 11:00 a.m. Eastern Time (ET) on a United States business day,[60] must be met by the applicable customer by the close of the Fedwire Funds Service[61] on the day on which it is issued. A margin call issued after 11:00 a.m. ET on a United States business day, or on a Saturday, Sunday, or a Federal holiday, would be considered to have been issued before 11:00 a.m. ET on the next day that is a United States business day. The Commission proposes that a clearing member be prohibited from contractually agreeing to delay calling for margin until after 11:00 a.m. ET on any

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[60] The definition of "United States business day" is discussed below.

[61] The Fedwire Funds Service is an electronic funds transfer service commonly used for settlement and clearing arrangements. The service currently closes at 7:00 p.m. ET. For purposes of the Fedwire Funds Service, Federal Reserve Banks observe as holidays all Saturdays, all Sundays, and the holidays listed on the Federal Reserve Banks' Holiday Schedules. *See* The Federal Reserve, Fedwire® Funds Service and National Settlement Service Operating Hours and FedPayments® Manager Hours of Availability, available at *https://www.frbservices.org/resources/financial-services/wires/operating-hours.html*. Because the Fedwire Funds Service hours of operations may be subject to change, the Commission has determined to tie the timeframe to fulfill the one business day margin call requirements of proposed regulation § 39.13(j)(4) to the Fedwire Funds Service's closing rather than an absolute time.

given United States business day, and from engaging in practices that are designed to circumvent proposed regulation § 39.13(j)(4) by causing such delay.[62] Additionally, the Commission proposes, in proposed regulation § 39.13(j)(4)(vi), that a clearing member would not be in compliance with the requirements of proposed regulation § 39.13(j)(4) if it contractually agrees to provide for a period of time to meet margin calls that extends beyond the time periods specified in proposed regulation § 39.13(j)(4)(i)-(v)[63] or engages in practices designed to circumvent the requirements of proposed regulation § 39.13(j)(4).

The Commission proposes this provision in order to make clear that it is establishing a maximum period of time in which a margin call must be met for purposes of this regulation, rather than establishing a minimum time that must be allowed. Proposed regulation § 39.13(j)(4) would not preclude a clearing member from having customer agreements that provide for more stringent margining requirements, or applying more stringent margining requirements in appropriate circumstances.[64] Moreover, the statement that these requirements apply solely for purposes of this paragraph (j)(4) means that such requirements are not intended to apply to any other provision; *e.g.*, they are not

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[62] The clearing member would *not* be prohibited from making a margin call after 11:00 am ET if it deemed it appropriate to do so, it simply would be prohibited from contractually *agreeing to delay* making the margin call until after that time (which would have the effect of delaying the date on which payment is due).

[63] For example, if a clearing FCM and a customer contract for a grace or cure period that would operate to make margin due and payable later than the deadlines described herein, including a case where the FCM would not have the discretion to liquidate the customer's positions and/or collateral where margin is not paid by such time, such an agreement would be inconsistent with the conditions under which such clearing FCM may engage in separate account treatment.

[64] For example, a clearing member (or other contractual) requirement that a margin call issued by 12:00 p.m. ET be met by the applicable customer by 6:00 p.m. ET on the same day would not be inconsistent with proposed regulation § 39.13(j)(4).

intended to define when an account is under-margined for purposes of Commission regulation § 1.17.

Conversely, the Commission does not propose to prohibit contractual arrangements inconsistent with proposed regulation § 39.13(j)(4). However, the clearing member would not be permitted to engage in separate account treatment under such arrangements.

In light of challenges to same-day settlement posed by margining in certain currencies, as described above, and in recognition of the particular banking conventions around payments in JPY, proposed regulation § 39.13(j)(4)(ii) provides that payment of margin in JPY shall be considered in compliance with the requirements of proposed regulation § 39.13(j)(4) if received by the applicable clearing member by 12:00 p.m. ET on the second United States business day after the margin call is issued. Furthermore, proposed regulation § 39.13(j)(4)(iii) provides that payment of margin in fiat currencies other than USD, CAD, or JPY shall be considered in compliance with the requirements of proposed regulation § 39.13(j)(4) if received by the applicable clearing member by 12:00 p.m. ET on the United States business day after the day the margin call is issued.[65] The Commission proposes to define "United States business day" in proposed regulation § 39.13(j)(4)(vii) as meaning weekdays, not including Federal holidays as established by 5

[65] The Commission notes that while it proposes to require that a one business day margin call be *met by the applicable customer* by the close of the Fedwire Funds Service on the day it is issued (as long as it is issued by 11:00 a.m. ET on a United States business day) where margin is paid in USD or CAD, it proposes to require that a one business day margin call be *received by the applicable clearing member* by 12:00 p.m. ET on the next United States business day after the margin call is issued, where the payment of margin is in fiat currencies other than USD, CAD, or JPY, and *received by the applicable clearing member* by 12:00 p.m. ET on the second United States business day after the margin call is issued, where the payment of margin is in JPY. As discussed above, these distinct requirements are intended to account for the lead time required when fund transfers are made in non-USD and CAD currencies, and to ensure that clearing members are not unduly delayed in collecting margin.

U.S.C. 6103. The term "United States business day" is intended to encompass days on which banks and custodians are open in the United States to facilitate payment of margin for clearing members and their customers.[66]

The occurrence of a foreign holiday during which banks are closed may also create difficulties in payment of margin in a fiat currency other than USD. Therefore, the Commission proposes regulation § 39.13(j)(4)(iv), which provides that the relevant deadline for payments of margin in fiat currencies other than USD may be extended by up to one United States business day and still considered in compliance with the requirements of proposed regulation § 39.13(j)(4) if payment is delayed due to a banking holiday in the jurisdiction of issue of the currency in which margin is paid. Where margin is paid in EUR, the customer or investment manager managing the separate account may designate one country within the Eurozone with which the customer or investment manager, as applicable, has the most significant contacts for purposes of meeting margin calls, whose banking holidays will be referred to for purposes of compliance with the regulation.[67] Proposed regulation § 39.13(j)(4)(iv) is designed to provide clearing FCMs with a level of discretion in how they manage risk by allowing for limited delays in margin payments due to non-U.S. banking conventions. Proposed regulation § 39.13(j)(4)(iv) would not, however, require a clearing FCM to extend the deadline for payments of margin. Here, the Commission is seeking to allow DCOs to permit their members to exercise risk management judgment in balancing, within limits,

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[66] As used in proposed regulation § 39.13(j)(4), the term "United States business day" is specifically intended to be distinct from the intraday period encompassed by the definition of business day in regulation § 39.2.

[67] With respect to margin payments in EUR, proposed regulation § 39.13(j)(4)(iv) is intended to prevent customers or investment managers from leveraging banking holidays in jurisdictions with which they have no significant commercial nexus, or in a multiplicity of jurisdictions, to circumvent requirements to pay margin timely. The Commission requests comment on the practicability of this standard below.

the risk management challenges caused by extending the time before a margin call is met with the burdens involved in requiring the client or investment manager to prefund potential margin calls in advance of the holiday or to arrange to pay margin more promptly in USD or another currency not affected by the holiday.

The Commission expects that clearing FCM risk management decisions, including the use of any extension permitted under proposed regulation § 39.13(j)(4)(iv), will be made in consideration of a client's risk profile, market conditions, and other relevant factors, evaluated at the time the risk management decisions are made.[68]

Lastly, in CFTC Letter No. 19-17, staff stated that a failure to deposit, maintain, or pay margin or option premium due to administrative errors or operational constraints would not constitute a failure to timely deposit or maintain initial or variation margin that would place a customer out of the ordinary course of business. This provision was intended to prevent a clearing FCM from being excluded from relying on the no-action position as a result of one-off exceptions, such as mis-entered data, a flawed software update, or an unusual and unexpected information technology outage (*e.g.*, an unanticipated outage of the Fedwire Funds Service). Accordingly, the Commission proposes regulation § 39.13(j)(4)(v), which provides that a failure to deposit, maintain, or pay margin or option premium does not constitute a failure to comply with the

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[68] This expectation is consistent with the statement of the directors of DCR and DSIO in issuing CFTC Letter No. 19-17. CFTC, Statement by the Directors of the Division of Clearing and Risk and the Division of Swap Dealer and Intermediary Oversight Concerning the Treatment of Separate Accounts of the Same Beneficial Owner, Sept. 13, 2019, available at *https://www.cftc.gov/PressRoom/SpeechesTestimony/dcrdsiodirectorstatement091319* ("We fully expect that DCOs and FCMs and their customers will agree that FCMs must retain, at all times, the discretion to determine that the facts and circumstances of a particular shortfall are extraordinary and therefore necessitate accelerating the timeline and relying on the FCM's protocol for liquidation or for accessing funds in the other accounts of the beneficial owner held at the FCM."). *See also* CFTC Letter No. 20-28 (stating the same).

requirements of proposed regulation § 39.13(j)(4) if such failure is due to unusual administrative error or operational constraints that a customer or investment manager acting diligently and in good faith could not have reasonably foreseen.[69] Proposed regulation §39.13(j)(4)(v) provides that, for these purposes, a clearing member's determination that failure to deposit, maintain, or pay margin or option premium is due to such administrative error or operational constraint would be based on the clearing member's reasonable belief in light of information known to the clearing member, at the time the clearing member learns of the relevant administrative error or operational constraint.[70]

Request for Comment

Question 5: The Commission requests comment on whether the regulatory framework set forth in proposed regulation § 39.13(j)(4) appropriately balances practicability and burden with risk management. If not, what alternative approach should be taken? How would such an alternative approach better balance those considerations? In particular, the Commission requests comment on whether the proposed standard of timeliness for a one business day margin call set forth in proposed regulation § 39.13(j)(4)(i)-(iii) presents practicability challenges and, if so, what those challenges are, and how the proposed standard of timeliness could be improved.

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[69] One would expect that administrative errors at a well-run clearing FCM or money manager to be unusual and unforeseen. For the avoidance of doubt, "unforeseen" refers to the particular occurrence of a constraint or error; for example, the fact that some small percentage of errors may be foreseen does not mean that any particular error is foreseen (and "unusual" means that such percentage should indeed be small).

[70] For purposes of clarity and certainty, the Commission proposes to establish this reasonableness standard for a clearing member's determination that a failure to timely deposit, maintain, or pay margin or option premium on the basis of administrative error or operational constraints. The Commission believes the proposed standard confers significant discretion upon clearing FCMs to assess the disposition of their customers while requiring that clearing FCMs act reasonably and on the basis of current and relevant information, diligently gathered.

Question 6: With respect to the proposed standard of timeliness for a one business day margin call:

(a) Are there other currencies, besides JPY, where relevant banking conventions render payment before the second U.S. business day after a margin call is issued impracticable? If so, the Commission requests commenters to specifically identify any such currencies, and provide specifics about the operational issues involved for each.

(b) Should the Commission establish a mechanism (*e.g.*, through action by Commission order, potentially with authority delegated to the Director of the Division of Clearing and Risk, or through action by DCOs) to address cases where the taxonomy of which currencies can practicably be paid on the same day/first U.S. business day/second U.S. business day after a margin call is issued should be changed, due to changes in banking conventions or newly discovered information?

(c) The Commission requests comment on whether, and if so, how, proposed regulation § 39.13(j)(4) should explicitly address timing of payment of margin in the event of an unscheduled United States banking holiday (*e.g.*, due to a national day of mourning).

(d) The Commission requests comment on whether, and if so, how, proposed regulation § 39.13(j) should explicitly address timing of payment of margin in the event of scheduled or unscheduled closures of United States securities markets.

Question 7: With respect to the criteria for extending payment of margin in EUR due to a banking holiday in the Eurozone pursuant to proposed regulation § 39.13(j)(4)(iv), the Commission requests comment on whether, and if so, how, the banking laws of national authorities within the Eurozone, operational issues, or other factors present practicability challenges to compliance. If commenters believe such challenges exist, the Commission seeks comment on whether a different standard would be more practicable, while achieving the goal of preventing customers or investment managers from claiming an extension of time to pay margin due to banking holidays in a multiplicity of jurisdictions, or in (a) jurisdiction(s) with which such customer or investment manager has no significant commercial nexus.

Question 8: In anticipation of potential developments with respect to the use of central bank digital currencies or other digital assets, the Commission requests comment on whether and, if so, how, proposed regulation § 39.13(j)(4) should explicitly address the timing of payment of margin in digital assets.

Question 9: The Commission requests comment regarding whether there are any other international considerations, beyond the time required to process payment of margin in different currencies, that the Commission should take into account in establishing requirements for compliance with the "one business day" margin call standard for purposes of proposed regulation §39.13(j)(4). If so, the Commission requests comment regarding how proposed regulation §39.13(j) should be modified, if at all, to account for such considerations.

F. Proposed Regulation § 39.13(j)(5)-(10)

Where a clearing member permits disbursements on a separate account basis, it is important that the clearing member treat such accounts as separate in a consistent manner. As FIA noted in its June 26, 2019 letter, customer agreements that provide for separate account treatment generally require that a separate account be margined separately from any other account maintained for the customer with the FCM, and assets held in one separate account should not ordinarily be used to meet or offset any obligations of another separate account, including obligations that it or another investment manager may have incurred on behalf of a different account of the same customer.[71] FIA observed that these restrictions serve to assure the customer, or the asset manager responsible for a particular account, that the account will not be subject to unanticipated interference that may exacerbate stress on a customer's aggregate exposure to the FCM.[72] Additionally, FIA noted that where an FCM treats separate accounts as separate customers for risk management purposes, the FCM may manage risk more conservatively against the customer under the assumption that the customer has fewer assets than it may in fact have.[73]

Accordingly, the Commission in proposed regulation § 39.13(j)(5)-(10) proposes to adopt those conditions in CFTC Letter No. 19-17 designed to provide for consistent treatment of separate accounts. Proposed regulation § 39.13(j)(5)-(10) requires a separate account of a customer to be treated separately from other separate accounts of the same customer for purposes of certain existing computational and recordkeeping requirements,

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[71] First FIA Letter.
[72] *Id.*
[73] *Id.*

which would otherwise be met by treating accounts of the same customer on a combined basis. Because accounts subject to proposed regulation § 39.13(j) would be risk-managed on a separate basis, the Commission believes it is appropriate for the proposed regulation to provide that DCOs that permit separate account treatment require that the relevant clearing FCMs similarly apply these risk-mitigating computational and recordkeeping requirements on a separate account basis. The effect of the requirements in these paragraphs is to augment the FCM's existing obligations under various provisions of regulation § 1.17.

Proposed regulation § 39.13(j)(5) provides that the margin requirement for each separate account is calculated independently from all other separate accounts of the same customer, with no offsets or spreads recognized across the separate accounts. A clearing member would be required to treat each separate account of a customer independently from all other separate accounts of the same customer for purposes of computing capital charges for under-margined customer accounts in determining its adjusted net capital under regulation § 1.17. Additionally, proposed regulation § 39.13(j)(6) provides that the clearing member must record each separate account independently in its books and records. In other words, the clearing member must record the balance of each separate account either as a receivable or payable, with no offsets between other separate accounts of the same customer. A clearing member would be required to treat each separate account of a customer independently from all other separate accounts of the same customer for purposes of determining whether a receivable from a separate account that represents a debit or deficit ledger balance may be included in the clearing member's current assets in computing its adjusted net capital under regulation § 1.17(c)(2).

Proposed regulation § 39.13(j)(7) provides that the receivable for a debit or deficit from a separate account must only be considered a current or allowable asset for purposes of regulation §1.17(c)(2) based on the assets of that separate account, and not on the assets held in another separate account of the same customer. Proposed regulation § 39.13(j)(8) provides that in calculating the amount of its own funds it must use to cover debit or deficit balances, the clearing member must include any debit or deficit of any separate account, and reflect that calculation on the applicable report.

Proposed regulation § 39.13(j)(9) provides that the clearing member must include the margin deficiency of each separate account, and cover such deficiency with its own funds, as applicable, for purposes of its residual interest and legally segregated operationally commingled compliance calculations, as applicable under Commission regulations §§ 1.22, 22.2, and 30.7. Lastly, proposed regulation § 39.13(j)(10) provides that in determining its residual interest target for purposes of Commission regulation § 1.23(c), the clearing member must calculate customer receivables computed on a separate account basis. Currently, Commission regulations require an FCM to maintain its own capital, or residual interest, in customer segregated accounts in an amount equal to or greater than its customers' aggregate under-margined accounts.[74] Additionally, each day, an FCM is required to perform a segregated calculation to verify its compliance with segregation requirements. The FCM must file a daily electronic report showing its segregation calculation with its DSRO, and the DSRO must be provided with electronic access to the FCM's bank accounts to verify that the funds are maintained. The FCM must also assure its DSRO that when it meets a margin call for customer positions, it

[74] *See e.g.*, 17 CFR 1.22(c)(3); 17 CFR 22.2(f)(6)(iii)(A).

never uses value provided by one customer to meet another customer's obligation.[75] These requirements are intended to prevent FCMs from being induced to cover one customer's margin shortfall with another customer's excess margin, and allow DSROs to verify that FCMs are not in fact doing so. Proposed regulation § 39.13(j)(10) is designed to ensure that margin deficiencies are calculated accurately for accounts receiving separate treatment, and that such deficiencies are covered consistent with existing Commission regulations.

G. Proposed Regulation § 39.13(j)(11)

Proposed regulation § 39.13(j)(11) provides that where the customer of separate accounts subject to separate treatment has appointed a third party as the primary contact to the clearing member, the clearing member must obtain and maintain current contact information of an authorized representative at the customer and take reasonable steps to verify that such person is in fact an authorized representative of the customer. The clearing member would be required to review and, if necessary, update such information no less than annually. In many cases, an investment manager acts under a power of attorney on behalf of a customer, and the FCM has little direct contact with the customer. Proposed regulation § 39.13(j)(11) is designed to ensure that clearing FCMs have a reliable means of contacting customers directly if the investment manager fails to pay promptly.

Request for Comment:

Question 10: The Commission requests comment on whether it should prescribe specific steps that a DCO must require a clearing member to take to verify the identity of

[75] *See e.g.*, 17 CFR 22.2(g).

an authorized representative of a customer, and if so, what such steps should entail. The Commission further requests comment on the potential time and cost burden of such steps. Commenters are requested to provide quantitative data where available.

H. Proposed Regulation § 39.13(j)(12)

Proposed regulation § 39.13(j)(12) provides that the clearing member must provide each customer using separate accounts with a disclosure that, pursuant to part 190 of the Commission's regulations, all separate accounts of the customer in each account class will be combined in the event of the clearing member's bankruptcy. The disclosure statement must be delivered separately to the customer via electronic means in writing or in another manner in which the clearing member customarily delivers disclosures pursuant to applicable Commission regulations, and as permissible under its customer documentation. The clearing member must also maintain documentation demonstrating that the disclosure statement was delivered directly to the customer. The clearing member must also include the disclosure statement on its website or within its disclosure documentation, as required by Commission regulation § 1.55(i).

The Bankruptcy Reform Act of 1978[76] enacted subchapter IV of chapter 7 of the Bankruptcy Code, title 11 of the U.S. Code, to add certain provisions designed to afford enhanced protections to commodity customer property and protect markets from the reversal of certain transfers of money or other property, in recognition of the complexity of the commodity business.[77] The Commission enacted part 190 of its regulations, 17 CFR part 190, to implement subchapter IV. Under part 190, all separate accounts of a customer in an account class will be combined in the event of a clearing member's

[76] Public Law 95–598, 92 Stat. 2549.
[77] Bankruptcy, 46 FR 57535, 57535-36 (Nov. 24, 1981)

bankruptcy.[78] The Commission proposes to adopt proposed regulation § 39.13(j)(12) so that customers receive full and fair disclosure as to the treatment of their accounts in a clearing FCM bankruptcy.

I. Proposed Regulation § 39.13(j)(13)

Proposed regulation § 39.13(j)(13) provides that the clearing member must disclose in its Disclosure Document required under Commission regulation § 1.55(i) that it permits the separate treatment of accounts for the same customer. Regulation § 1.55 was adopted to "advise new customers of the substantial risk of loss inherent in trading commodity futures."[79] The Commission amended regulation § 1.55 in 2013 to, among other things, add new paragraph (i) requiring FCMs to disclose to customers all information about the FCM, including its business, operations, risk profile, and affiliates, that would be material to the customer's decision to entrust funds to and otherwise do business with the FCM and that is otherwise necessary for full and fair disclosure.[80] Such disclosures include material information regarding specific topics identified in regulation § 1.55(k), which include a basic overview of customer fund segregation, as well as current risk practices, controls, and procedures.[81] These disclosures are designed to enable customers to make informed judgments regarding the appropriateness of selecting

[78] 17 CFR 190.08(b)(2)(i) and (xii) (Aggregate the credit and debit equity balances of all accounts of the same class held by a customer in the same capacity – Except as otherwise provided in this paragraph (b)(2), all accounts that are deemed to be held by a person in its individual capacity shall be deemed to be held in the same capacity – 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.).
[79] Adoption of Customer Protection Rules, 43 FR 31886, 31888 (July 24, 1978).
[80] 17 CFR 1.55(i).
[81] 17 CFR 1.55(k)(8), (11).

an FCM and enhance the diligence that a customer can conduct prior to opening an account and on an ongoing basis.[82]

The Commission believes that the application of separate account treatment for some customers of a clearing FCM, as permitted by a DCO, is material to the decision to entrust funds to and otherwise do business with the FCM with respect to customers of such FCM generally because, in the event that separate account treatment for some customers were to contribute to a loss that exceeds the FCM's ability to cover, that loss might affect the segregated funds of all of the FCM's customers in one or more account classes. Accordingly, the Commission proposes regulation § 39.13(j)(13) to ensure that customers are apprised of a matter that is relevant to the clearing FCM's risk management policies.

J. Proposed Regulation § 39.13(j)(14)

Proposed regulation § 39.13(j)(14) provides that, to the extent the clearing member treats the separate accounts of a customer as accounts of separate entities, the clearing member must (i) apply such treatment in a consistent manner over time; (ii) provide a one-time notification to its DSRO and any DCO of which it is a clearing member that it will apply such treatment;[83] and (iii) maintain and keep current a list of all separate accounts receiving such treatment. With respect to proposed regulation § 39.13(j)(14)(iii), the clearing member would be required to conduct a review of its records of accounts receiving separate treatment no less than quarterly. Proposed

[82] Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations, 78 FR 68506, 68564 (Nov. 14, 2013).
[83] As stated in the proposed regulatory text below, once this notification is made, the clearing member would not be required to repeat it. In other words, once a clearing member notifies its DSRO that it will apply separate account treatment to one or more customers, such clearing member would not be required to provide the same notification to its DSRO each time it applies separate account treatment to a new or additional customer.

regulation § 39.13(j)(14) is intended to ensure that clearing FCMs employ separate account treatment in a way that is consistent with the customer protection and DCO risk management provisions of the CEA and Commission regulations, that DSROs are able to effectively monitor and regulate clearing FCMs that engage in separate account treatment, and that clearing FCMs have the records necessary to understand which accounts receive separate treatment for purposes of monitoring compliance with the proposed regulation.

The Commission recognizes that, while bona fide business or risk management purposes may at times warrant application or cessation of separate account treatment, clearing members should not apply or cease separate account treatment for reasons, or in a manner, that would contravene the customer protection and risk mitigation purposes of the CEA and Commission regulations. For instance, a clearing member should not switch between separate and combined treatment for customer accounts in order to achieve more preferable margining outcomes or offset margin shortfalls in particular accounts. The Commission recognizes that there are a wide variety of circumstances that may indicate inconsistent application of separate account treatment, and proposes to provide DCOs with a degree of discretion in ascertaining, consistent with their rules, whether a clearing member applies such treatment consistently over time.[84]

Request for Comment

Question 11: The Commission requests comment on the appropriateness of its proposed approach of providing DCOs with discretion in determining whether a clearing FCM has applied separate account treatment consistently over time.

[84] Core Principle A provides that a DCO shall have reasonable discretion in establishing the manner by which it complies with each core principle. Section 5b(c)(2)(A)(ii) of the CEA, 7 U.S.C. 7a-1(c)(2)(A)(ii).

III. COST BENEFIT CONSIDERATIONS

A. Statutory and Regulatory Background

Core Principle D, concerning risk management, imposes a number of duties upon DCOs related to their ability to manage the risks associated with discharging their responsibilities as DCOs, measuring credit exposures, limiting exposures to potential default-related losses, margin requirements, and risk management models and parameters.[85] Among other requirements, Core Principle D requires that the margin required from each member and participant of a DCO be sufficient to cover potential exposures in normal market conditions.[86] Commission regulation § 39.13 implements Core Principle D, including through regulation § 39.13(g)(8)(iii)'s restrictions on withdrawal of customer initial margin. Regulation § 39.13(g)(8)(iii) is designed to ensure that DCOs do not permit clearing FCMs to allow customers to withdraw funds from their accounts unless sufficient funds remain to meet customer initial margin requirements with respect to all products and swap portfolios held in the customer's account and cleared by the DCO. This requirement is intended to prevent the under-margining of customer accounts, and thus mitigate the risk of a clearing member default and the consequences that could accrue to the broader financial system.

Proposed regulation § 39.13(j) amends regulation § 39.13 by allowing a DCO to permit a clearing FCM to treat accounts separately for purposes of regulation § 39.13(g)(8)(iii), subject to specified conditions. Those conditions are in turn designed to ensure that clearing FCMs (i) carry out such separate account treatment in a consistent

[85] Section 5b(c)(2)(D) of the CEA, 7 U.S.C. 7a-1(c)(2)(D).
[86] Section 5b(c)(2)(D)(iv) of the CEA, 7 U.S.C. 7a-1(c)(2)(D)(iv).

and documented manner; (ii) monitor customer accounts on a separate and combined basis; (iii) identify and act upon instances of financial or operational distress that necessitate a cessation of separate account treatment; (iv) provide appropriate disclosures to customers regarding separate account treatment; and (v) apprise their DSROs when they apply separate account treatment or an event has occurred that would necessitate cessation of separate account treatment. The Commission believes that separate account treatment, subject to these conditions, is consistent with Core Principle D.

B. Consideration of the Costs and Benefits of the Commission's Action

1. CEA Section 15(a)

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.[87] Section 15(a) further specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) protection of market participants and the public, (2) efficiency, competitiveness and financial integrity of markets, (3) price discovery, (4) sound risk management practices, and (5) other public interest considerations (collectively referred to herein as the Section 15(a) Factors). Accordingly, the Commission considers the costs and benefits associated with the proposed regulation in light of the Section 15(a) Factors. In the sections that follow, the Commission considers: (1) the costs and benefits of the proposed regulation; (2) the alternatives contemplated by the Commission and their costs and benefits; and (3) the impact of the proposed regulation on the Section 15(a) Factors.

[87] 7 U.S.C. 19(a).

The Commission notes that this consideration of costs and benefits is based on, *inter alia*, the understanding that the futures and swaps markets function internationally, with many transactions involving U.S. firms taking place across international boundaries, with some Commission registrants and their clients being organized outside of the United States, with leading industry members typically conducting operations both within and outside the United States, and with industry members commonly following substantially similar business practices wherever located. Where the Commission does not specifically refer to matters of location, the discussion of costs and benefits below refers to the effects of the proposed regulation on all relevant futures and swaps activity, whether by virtue of the activity's physical location in the United States or by virtue of the activity's connection with activities in, or effect on, U.S. commerce under CEA section 2(i).

2. Costs and Benefits of the Proposed Regulation

The baseline for the Commission's consideration of the costs and benefits of the proposal is the Commission's current regulation § 39.13. The Commission recognizes, however, that to the extent that clearing FCMs have relied on CFTC Letter No. 19-17, the actual costs and benefits of the proposed regulation may not be as significant.

a. Benefits

Regulation § 39.13(g)(8)(iii) provides that a DCO shall require its clearing members to ensure that their customers do not withdraw funds from their accounts with such clearing members if such withdrawal would result in funds insufficient to meet the customer initial margin requirements with respect to all products and swap portfolios held

in the customer's account which are cleared by the DCO. This requirement serves important customer funds protection and risk mitigation purposes. However, combination of all accounts of the same customer within the same regulatory account classification for purposes of margining and determining funds available for disbursement may make it challenging for certain customers and their investment managers to achieve certain commercial purposes.[88] For example, where a customer has apportioned assets among multiple investment managers, neither the customer nor their investment managers may be able to obtain certainty that the individual portion of funds allocated to one investment manager will not be affected by the activities of other investment managers. Where clearing FCMs are able to treat the separate accounts of a single customer as accounts of separate entities, subject to certain regulatory safeguards, customers are better able to leverage the skills and expertise of investment managers, and realize the benefits of a balance of investment strategies in order to meet specific commercial goals in a manner that would not contravene the customer funds protection and risk mitigation purposes of the CEA and Commission regulations.

The Commission also notes that, to the extent that DCOs and their clearing FCMs currently rely on the no-action position in CFTC Letter No. 19-17, those FCMs would retain the benefit of costs and resources already expended in order to comply with the conditions of the no-action position. In a letter to the Commission staff dated April 1, 2022, FIA noted that, "For many FCMs and their customers, the terms and conditions of the no-action position . . . presented significant operational and systems challenges," as FCMs were required to "(i) adopt new practices for stress testing accounts; (ii) review

[88] *See* First FIA Letter.

and possibly change margin-timing expectations for non-US accounts; (iii) undertake legal analysis to clarify interpretive questions; and (iv) revise their segregation calculation and recordkeeping practices," as well as engage in "time-consuming documentation changes and customer outreach."[89]

FIA further described these challenges in a letter to the Commission staff dated May 11, 2022, noting that in order to meet the conditions of the no-action position, FCMs were required to review and in some cases amend customer agreements, and identify and implement information technology systems changes.[90] FIA also asserted that FCMs were likely required to revise internal controls and procedures.[91] FIA stated that while the costs incurred by each FCM varied depending on its customer base, among larger FCMs with a significant institutional customer base, personnel costs would have included identifying and reviewing up to 3,000 customer agreements to determine which agreements required modification, and then negotiating amendments with customers or their advisers.[92] FIA further stated that because the relevant provisions of these agreements were not uniform, they generally required individual attention.[93]

If the Commission were to decide to forego this rulemaking, and if the no-action position expired, these changes would need to be reversed. FIA noted that, if required to reverse these changes, the burdens on FCMs and their customers would be "significant."[94] Specifically, FIA asserted that FCMs would again be required to review

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[89] FIA letter dated Apr. 1, 2022 to Clark Hutchison and Amanda Olear (Second FIA Letter).
[90] FIA letter dated May 11, 2022 to Robert Wasserman (Third FIA Letter). FIA noted that these changes were particularly challenging for FCMs that are part of a bank holding company structure, as "[m]odifying integrated technology information systems across a bank holding company structure is complicated, expensive and time consuming." *Id.*
[91] *Id.*
[92] *Id.*
[93] *Id.*
[94] Second FIA Letter.

and amend customer agreements, noting that negotiations to amend such agreements would likely prove "extremely difficult" as "advisers would seek to assure that their ability to manage their clients' assets entrusted to them would not be adversely affected by the actions (or inactions) of another adviser."[95] FCMs would also again be required to revise their internal controls and procedures, and identify and implement information technology systems changes.[96] DCOs, FCMs, and customers of FCMs already relying on the no-action position would also obtain the benefit of continuing to leverage existing systems and procedures to provide for separate account treatment.

Request for Comment

Question 12: The Commission requests comment on the extent to which DCOs, clearing members, and customers currently rely on the no-action position in CFTC Letter No. 19-17 (including the extensions of time in CFTC Letters No. 20-28, 21-29, and 22-11) to permit and/or engage in separate account treatment. Commenters are requested to provide data where available (*e.g.*, number of DCOs and/or clearing members that allow for separate account treatment, or size of clearing members providing for separate account treatment by customer funds in segregation or number of customers, as well as the nature and the extent of the costs that they would incur if the relevant no-action position were to be permitted to expire).

[95] Third FIA Letter. FIA further noted that "an adviser may be less likely to use exchange-traded derivatives to hedge its customers' cash market positions if the adviser could not have confidence that it would be able to withdraw its customers' excess margin as necessary to meet its obligations in other markets." *Id.*
[96] *Id.*

b. Costs

The proposed regulation would not require DCOs to allow for separate account treatment, and DCOs that do not presently allow for separate account treatment, and do not desire to do so in the future, would not incur any costs as a result of the proposed regulation. Furthermore, the Commission believes that a DCO electing to allow for separate account treatment will do so because they believe that the benefits of doing so will exceed the costs of doing so.

DCOs that wish to allow for separate account treatment would likely incur certain costs related to the implementation of the proposed regulation, some of which would be incurred on a one-time basis, and some of which would be recurring. DCOs that wish to allow for separate account treatment would likely incur costs in connection with updating their rulebooks to allow for separate account treatment under the conditions codified in the proposed regulation. The Commission anticipates that this would generally be a one-time cost. Such DCOs would also likely incur legal, compliance, and other costs related to monitoring, examination, and enforcement with respect to clearing members and customers that engage in separate account treatment. The Commission expects that such costs may be reduced where a DCO already allows for separate account treatment under the terms of the no-action position and is able to leverage existing rules and compliance infrastructure to implement the proposed regulation. While the Commission anticipates that certain DCOs that do not now rely on the no-action position may in the future choose to allow for separate account treatment, the Commission also expects that the number of DCOs that would do so would be small.

The Commission notes however that because the provisions of the proposed regulation vary in some respects from the terms of the no-action position, and DCOs may implement the proposed regulation in their rules in a different manner than the conditions of the no-action position,[97] at least some additional costs are likely to be incurred by DCOs that already rely on the no-action position.

The costs of the proposed regulation will likely vary across DCOs depending on whether they already allow for separate account treatment and the nature of their existing rule and compliance infrastructures to support separate account treatment, and as such would be difficult to quantify with precision.

Similarly, the proposed regulation would not require clearing FCMs to engage in separate account treatment. Clearing FCMs that do not now engage in separate account treatment, and wish not to do so in the future, would not incur any costs as a result of the proposed regulation. However, for those clearing FCMs that choose to comply with the proposed regulation, the costs of compliance could be significant, and may vary based on factors such as the size and existing compliance resources of a particular FCM. While the Commission, in connection with its Paperwork Reduction Act assessment below, estimates that certain reporting, disclosure, and recordkeeping costs would not be significant on an entity level, as FIA noted, taken as a whole, compliance with the conditions that the proposed regulation would codify could result in significant operational and systems costs.

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[97] For instance, CME has provided for separate account treatment under the terms of the no-action position through member bulletins. *See, e.g.*, Financial and Regulatory Bulletin # 20-01, CFTC Letter No. 20-28 Extension of CFTC Letter No. 19-17 Time-Limited No-Action Relief with Respect to the Treatment of Separate Accounts by Futures Commission Merchants, Sept. 23, 2020, available at *https://www.cmegroup.com/notices/clearing/2020/09/frb--20-01.html*.

In other words, the Commission anticipates that clearing FCMs— specifically, existing clearing FCMs that do not already rely on the no-action position, but may choose in future to rely upon the proposed regulation—may incur relatively significant costs related to designing and implementing new systems, or enhancing existing systems, to comply with the proposed regulation, as well as negotiation costs, even where direct recordkeeping costs may not be significant on an entity-by-entity basis.[98] However, the Commission notes that many of the requirements of the proposed regulation would involve one-time costs in order to update systems, procedures, disclosure documents, and recordkeeping practices, and that ongoing costs of maintaining compliance may be less significant. To the extent clearing FCMs already rely on the no-action position, the tools (*e.g.*, software, as well as policies and procedures) necessary to comply with the proposed regulations on an ongoing basis will largely have already been built, and the costs associated with compliance will largely have already been incurred. Furthermore, while the Commission expects that certain FCMs that do not now rely on the no-action position may in the future choose to engage in separate account treatment, and would need to incur these costs to come into compliance with the proposed regulation, the Commission also anticipates that the number of FCMs that would do so would be small.

[98] This may be true to a lesser extent with respect to new entrants to the FCM business, in that those FCMs would incur the cost of implementing policies, procedures, and systems that comply with the conditions of the proposed regulation, but would not need to retrofit existing policies, procedures, and systems.

C. Costs and Benefits of the Commission's Action as Compared to Alternatives

The Commission considered several alternatives to the proposed regulation. On one hand, the Commission, for analytical completeness, considered allowing the no-action position announced in CFTC Letter No. 19-17 and its superseding letters to expire. When compared only to the existing regulation § 39.13(g)(8)(iii), which is the baseline for the cost and benefit considerations, this alternative imposes neither costs nor benefits, because this approach would effectively constitute a reversion to regulation § 39.13(g)(8)(iii) prior to the issuance of CFTC Letter No. 19-17 and its superseding letters. However, the Commission does not anticipate that there would be any significant benefit to this approach relative to the approach contemplated by the proposed regulation, and indeed, preliminarily believes that there would be significant costs to market participants when compared to the proposed regulation, particularly in consideration of market participants' reliance on the no-action letters, which the proposed regulation is designed to codify. Allowing the no-action position to expire without codifying its terms would, as noted above, preclude customers from achieving certain important financial objectives that could be achieved in a manner consistent with the customer funds protection and risk mitigation purposes of the CEA and Commission regulations. Additionally, while it would not result in costs for FCMs that do not now choose to comply with the conditions of the no-action position, it would appear to require clearing FCMs that currently rely on the no-action position to make significant expenditures of funds and resources in order to rework systems, procedures, and customer documentation to ensure compliance with regulation § 39.13(g)(8)(iii).

Because the no-action position has been applied successfully since July 2019, the Commission preliminarily believes codifying its provisions to be the most appropriate and beneficial approach for FCMs and their customers, and will preserve the customer funds protection and risk mitigation conditions of the no-action position.

Alternatively, the Commission, for analytical completeness, also considered extending the no-action position absent the conditions. This alternative would preserve the benefits of the no-action position for DCOs, FCMs, and customers. However, as discussed further below, the conditions of the no-action position—proposed to be codified herein—are designed to permit separate account treatment only to the extent that such treatment would not contravene the risk mitigation goals of regulation § 39.13. The Commission preliminarily believes that extending the no-action position without the conditions would exacerbate risks for DCOs, FCMs, and customers. For instance, without a requirement to cease separate account treatment in cases in which a customer is in financial distress, it is more likely that an under-margining scenario would be exacerbated, and a customer default to the clearing FCM —and potentially a default of the clearing FCM to the DCO—would be more likely.

D. Section 15(a) Factors

Section 15(a) of the CEA requires the Commission to consider the effects of its actions in light of the following five factors:

1. Protection of Market Participants and the Public

Section 15(a)(2)(A) of the CEA requires the Commission to evaluate the costs and benefits of a proposed regulation in light of considerations of protection of market participants and the public. The Commission preliminarily believes that the amendments proposed herein maintain the efficacy of protections for customers and the broader financial system contained in Core Principle D and regulation § 39.13.

Regulation § 39.13(g)(8)(iii) implements Core Principle D requirements for DCOs to limit exposure to potential losses from defaults and maintain margin sufficient to cover potential exposures in normal market conditions[99] by requiring DCOs to ensure that their members do not allow customers to withdraw funds from their accounts if such withdrawal would create or exacerbate an initial margin shortfall. This requirement protects not only market participants by requiring clearing FCMs to ensure that adequate margin exists to cover customer positions; it also protects the public from disruption to the wider financial system by mitigating the risk that a clearing FCM will default due to customer nonpayment of variation margin obligations combined with insufficient initial margin. While DCOs are required to, and do, maintain robust default management protections and procedures, any default of a clearing FCM nonetheless increases the risk of a DCO default. The conditions of the no-action position outlined in CFTC Letter No. 19-17, and proposed to be codified herein, are designed to effectuate these customer protection and risk mitigation goals notwithstanding a clearing FCM's application of separate account treatment. For example, separate account treatment is not permitted in certain circumstances outside the ordinary course of business (*e.g.*, where a clearing FCM learns a customer is in financial distress, and thus may be unable promptly to meet initial

[99] 7 U.S.C. 7a-1(c)(2)(D)(iii)-(iv).

margin requirements, whether in one or more separate accounts or on a combined account basis).

Proposed regulation § 39.13(j) would also codify conditions for clearing FCMs designed to ensure that they collect information sufficient to understand the value of assets dedicated to a separate account, apply separate account treatment consistently, and maintain reliable lines of contact for the ultimate customer of the account. DCOs have successfully relied on these conditions for over two years, and the Commission believes codification of these conditions, as proposed herein, supports protection of market participants and the public.

2. Efficiency, Competitiveness, and Financial Integrity of Futures Markets

Section 15(a)(2)(B) of the CEA requires the Commission to evaluate the costs and benefits of a proposed regulation in light of efficiency, competitiveness, and financial integrity of futures markets. The Commission preliminarily believes that the proposed regulation may carry potential implications for the financial integrity of markets, but not for the efficiency or competitiveness of markets, which the Commission preliminarily believes remain unchanged.

As stated above, the purposes of the Commission's customer funds protection and risk management regulations, including regulation § 39.13(g)(8)(iii) include not just protection of customer assets, but also mitigation of systemic risk: a customer in default to a clearing FCM may in turn trigger the clearing FCM to default to the DCO, with cascading consequences for the DCO and the wider financial system. The proposed amendments reflect the Commission’s preliminary determination that the conditions of

CFTC Letter No. 19-17, as proposed to be codified herein, are sufficient and appropriate to guard against such risk for purposes of regulation § 39.13(g)(8)(iii).

In CFTC Letter No. 19-17, the Commission staff highlighted market participants' concerns that the Commission should recognize "diverse practices among FCMs and their customers with respect to the handling of separate accounts of the same beneficial owner" as consistent with regulation § 39.13(g)(8)(iii). FIA, in particular, outlined several business cases in which a customer or a clearing FCM may want to apply separate account treatment, and each of SIFMA-AMG, FIA, and CME outlined controls that clearing FCMs could apply to ensure that, in instances in which separate account treatment is desired, such treatment can be applied in a manner that effectively prevents systemic risk.[100] By proposing to codify the no-action position provided for by CFTC Letter No. 19-17 and its superseding letters, the Commission is proposing to preserve the option for clearing FCMs to engage in separate account treatment, thereby providing clearing FCMs with further opportunity to compete on services offered to customers, and providing customers with a greater variety of options to address their financial needs.

3. Price Discovery

Section 15(a)(2)(C) of the CEA requires the Commission to evaluate the costs and benefits of a proposed regulation in light of price discovery considerations. The Commission preliminarily believes that the proposed amendments will not have a significant impact on price discovery.

[100] *See* First FIA Letter; SIFMA-AMG Letter; CME Letter.

4. Sound Risk Management Practices

Section 15(a)(2)(D) of the CEA requires the Commission to evaluate the costs and benefits of a proposed regulation in light of sound risk management practices. As discussed above, regulation § 39.13(g)(8)(iii) implements the risk management standards of Core Principle D by requiring DCOs to ensure that their members do not allow customers to increase under-margining in their accounts through withdrawals of funds. Thus, any amendment to regulation § 39.13 should not undermine these risk management goals. As discussed further above with regard to protection of customers and the public, the conditions of the no-action position proposed to be codified herein are designed, and have been successfully used, to allow clearing FCMs to engage in separate account treatment in a manner that is consistent with the protection of customer funds and the mitigation of systemic risk, including by requiring the application of separate account treatment in a consistent manner, and requiring regulatory notifications and the cessation of separate account treatment in certain instances of operational or financial distress. The Commission therefore preliminarily believes the proposed regulations promotes sound DCO risk management practices.[101]

5. Other Public Interest Considerations

Section 15(a)(2)(e) of the CEA requires the Commission to evaluate the costs and benefits of a proposed regulation in light of other public interest considerations. The Commission is identifying a public interest benefit in codifying the Divisions' no-action position, where the efficacy of that position has been demonstrated. In such a situation,

[101] *See, e.g.*, First FIA Letter (describing use of separate account treatment for hedging purposes).

the Commission believes it serves the public interest and, in particular, the interests of market participants, to engage in notice-and-comment rulemaking, where it seeks and considers the views of the public in amending its regulations, rather than for market participants to continue to rely on a time-limited no-action position that can be easily withdrawn, provides less long-term certainty for market participants, and offers a more limited opportunity for public input.

Request for Comment[102]

Question 13: The Commission requests comment, including any available quantifiable data and analysis, concerning the costs and benefits of the proposed regulation for DCOs, FCMs, and any other market participant(s), including regarding the extent to which market participants already enjoy any such benefits or incur any such costs.

Question 14: The Commission requests comment, including any available quantifiable data and analysis, concerning whether the tradeoff of costs and benefits of the proposed regulation for DCOs, FCMs, and any other market participant(s), could be improved by modifying the set of conditions set forth therein (*i.e.*, by deleting or modifying in a specified fashion any of the proposed conditions, or by adding specified additional conditions).

Question 15: The Commission requests comment regarding whether there are FCMs which chose not to rely on the no-action position provided by CFTC Letter No. 19-17 due to the conditions required to rely on that position. The Commission further

[102] In section II above, the Commission requested comment on the potential time and cost burden associated with specific steps to verify the identity of an authorized representative of a customer pursuant to proposed regulation §39.13(j)(11), to the extent that commenters believe the Commission should prescribe such steps.

requests comment on how those conditions could be modified to mitigate the burden of compliance while achieving the goals of mitigating systemic risk and protecting customer funds.

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.[103]

The Commission believes that the public interest to be protected by the antitrust laws is generally to protect competition. The Commission requests comment on whether the proposed regulation implicates any other specific public interest to be protected by the antitrust laws.

The Commission has considered the proposed regulation to determine whether it is anticompetitive and has preliminarily identified no anticompetitive effects. The Commission requests comment on whether the proposed regulation is anticompetitive and, if it is, what the anticompetitive effects are.

Because the Commission has preliminarily determined that the proposed regulation is not anticompetitive and has no anticompetitive effects, the Commission has not identified any less anticompetitive means of achieving the purposes of the CEA. The Commission requests comment on whether there are less anticompetitive means of

[103] 7 U.S.C. 19(b).

achieving the relevant purposes of the CEA that would otherwise be served by adopting the proposed regulation.

B. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) requires agencies to consider whether the rules they propose will have a significant economic impact on a substantial number of small entities and, if so, provide a regulatory flexibility analysis with respect to such impact.[104] The rules proposed herein would establish conditions under which DCOs may permit clearing FCMs to engage in separate account treatment, and therefore the rules would directly affect DCOs. However, the proposed regulation would also affect FCMs, insofar as FCMs permitted by DCOs to engage in separate account treatment, and which choose to do so, would be required to comply with the conditions proposed to be codified. The Commission has previously established certain definitions of "small entities" to be used by the Commission in evaluating the impact of its regulations on small entities in accordance with the RFA.[105] The Commission has previously determined that neither DCOs nor FCMs are small entities for the purpose of the RFA.[106] Accordingly, the Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that these proposed rules will not have a significant economic impact on a substantial number of small entities.

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[104] 5 U.S.C. 601 *et seq*.
[105] Bankruptcy Regulations, 86 FR 19324, 19416 (Apr. 13, 2021) (citing Policy Statement and Establishment of Definitions of "Small Entities" for Purposes of the Regulatory Flexibility Act, 47 FR 18618 (Apr. 30, 1982)).
[106] *See id.* (citing New Regulatory Framework for Clearing Organizations, 66 FR 45604, 45609 (Aug. 29, 2001); Customer Margin Rules Relating to Security Futures, 67 FR 53146, 53171 (Aug. 14, 2002)).

C. Paperwork Reduction Act

The Paperwork Reduction Act (PRA)[107] imposes certain requirements on Federal agencies in connection with their conducting or sponsoring any collection of information as defined by the PRA. Any agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number. The Office of Management and Budget (OMB) has not yet assigned a control number to the new collection.

This proposed rulemaking would result in a new collection of information within the meaning of the PRA, as discussed below. The Commission therefore is submitting this proposal to OMB for review, in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. If adopted, responses to this collection of information would be required to obtain a benefit. Specifically, clearing FCMs would be required to respond to the collection in order to obtain the benefit of engaging in separate account treatment for purposes of regulation § 39.13(g)(8)(iii), to the extent permitted by the DCOs of which they are clearing members.

The Commission will protect proprietary information it may receive according to the Freedom of Information Act and 17 CFR part 145, "Commission Records and Information." In addition, section 8(a)(1) of the CEA strictly prohibits the Commission, unless specifically authorized by the CEA, from making public "data and information that would separately disclose the business transactions or market positions of any person and trade secrets or names of customers."[108] The Commission also is required to protect

[107] 44 U.S.C. 3501 *et seq*.
[108] 7 U.S.C. 12(a)(1).

certain information contained in a government system of records according to the Privacy Act of 1974, 5 U.S.C. 552a.

1. Information Provided by Reporting Entities/Persons

The proposed regulation applies directly to DCOs and would not result in any new collections of information from DCOs. However, to the extent a DCO permits clearing FCMs to engage in separate account treatment pursuant to the proposed regulation, such clearing FCMs would be subject to certain reporting, disclosure, and recordkeeping requirements as a result of DCO requirements to comply with the conditions specified in proposed regulation §39.13(j)(1)-(14). The Commission estimates burden hours and costs using current regulation § 39.13 as a baseline. However, the Commission notes that many clearing FCMs already comply with the conditions of the no-action position, which are substantially similar to the proposed regulation. For these clearing FCMs, the Commission expects that any additional cost or administrative burden associated with complying with the proposed regulation would be negligible.[109]

a. Reporting Requirements

The proposed regulation contains three reporting requirements that could result in a collection of information from ten or more persons over a 12-month period.

First, proposed regulation § 39.13(j)(1)(iii) requires a clearing member to communicate promptly in writing to its DSRO and to any DCO of which it is a clearing member the occurrence of certain enumerated "non-ordinary course of business" events.

[109] However, the Commission expects that FCMs that do not currently rely on the no-action position, but choose to apply separate account treatment after the proposed regulation is finalized, would incur new costs.

There are currently approximately 62 registered FCMs.[110] The Commission staff estimates that slightly less than half of all FCMs would engage in separate account treatment under the proposed regulation, resulting in approximately 30 respondents. The Commission staff estimates that each such FCM may experience two non-ordinary course of business events per year, either with respect to themselves, or a customer. For purposes of determining the number of responses, the Commission staff anticipates that additional notifications of substantially the same information, and at substantially the same time, by means of electronic communication to additional DCOs of which the FCM is a clearing member (beyond the notification to the FCM's DSRO) would not materially increase the time and cost burden for such FCM. Therefore, for purposes of these estimates, the Commission staff treats a set of notifications sent to a DSRO and DCOs as a single response.[111] Accordingly, the Commission staff estimates a total of two responses per respondent on an annual basis. In addition, the Commission staff estimates that each response would take eight hours. This yields a total annual burden of 480 hours. In addition, the Commission staff estimates that respondents could expend up to $2,384 annually, based on an hourly rate of $149, to comply with this requirement.[112] This would result in an aggregated cost of $71,520 per annum (30 respondents ×$2,384).

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[110] *See* CFTC, Selected FCM Financial Data as of October 31, 2022 from Reports Filed by November 26, 2022, available at *https://www.cftc.gov/sites/default/files/2022-12/01%20-%20FCM%20Webpage%20Update%20-%20October%202022.pdf*.

[111] The Commission staff applies the same assumption to notifications to DSROs and DCOs with respect to proposed regulation § 39.13(j)(1)(iv) and proposed regulation §39.13(j)(14)(ii), discussed below.

[112] This figure is rounded to the nearest dollar and based on the annual mean wage for U.S. Bureau of Labor Statistics (BLS) category 13-2061, "Financial Examiners." BLS, Occupational Employment and Wages, May 2021 [hereinafter "BLS Data"], available at *https://www.bls.gov/oes/current/oes_nat.htm*. This category consists of professionals who "[e]nforce or ensure compliance with laws and regulations governing financial and securities institutions and financial and real estate transactions." BLS, Occupational Employment and Wages, May 2021: 13-2061 Financial Examiners, available at *https://www.bls.gov/oes/current/oes132061.htm*. According to BLS, the mean salary for this category is $96,180. This number is divided by 1,800 work hours in a year to account for sick leave and vacations and

Second, proposed regulation § 39.13(j)(1)(iv) provides an avenue for a clearing member to resume separate account treatment when it returns to the ordinary course of business, which would require a notification to its DSRO and any DCO of which it is a clearing member. The Commission staff estimates that, in many cases, there may be a reversion to the ordinary course of business, which a clearing FCM would need to report to its DSRO and any DCO of which it is a clearing member in order to resume separate account treatment, in accordance with the requirements of proposed regulation § 39.13(j)(1)(iv). The Commission staff estimates that for each non-ordinary course of business event, there would ultimately be a reversion to the ordinary course of business, resulting in two additional responses per respondent on an annual basis. In addition, the Commission staff estimates that each response would take eight hours. This yields a total annual burden of 480 hours. In addition, the Commission staff estimates that respondents could expend up to $2,384 annually, based on an hourly rate of $149, to comply with this requirement. This would result in an aggregated cost of $71,520 per annum (30 respondents × $2,384).

Third, proposed regulation § 39.13(j)(14)(ii) provides that, to the extent a clearing member treats the separate accounts of a customer as accounts of separate entities pursuant to the terms of proposed regulation § 39.13(j), the clearing member must provide a one-time notification to its designated self-regulatory organization and any

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multiplied by 2.5 to account for retirement, health, and other benefits, as well as for office space, computer equipment support, and human resources support. This number is further multiplied by 1.113625 to account for the 11.3625% change in the Consumer Price Index for Urban Wage-Earners and Clerical Workers between May 2021 and January 2023 (263.612 to 293.565). BLS, CPI for Urban Wage Earners and Clerical Workers (CPI-W), U.S. City Average, All Items – CWUR0000SA0, available at *https://www.bls.gov/data/#prices*. Together, these modifications yield an hourly rate of $149. The rounding and modifications applied with respect to the estimated average burden hour cost for this occupational category have been applied with respect to each occupational category discussed as part of this analysis.

DCO of which it is a clearing member that it will apply such treatment. The Commission staff estimates this would result in a total of one response per respondent on a one-time basis, and that respondents could expend up to $149, based on an hourly rate of $149, to comply with the proposed regulation. This would result in an annual burden of 30 hours and an aggregated cost of $4,470 (30 respondents × $149).

The aggregate information collection burden estimate associated with the proposed reporting requirements is as follows:[113]

Estimated number of respondents: 30.

Estimated number of reports: 150.

Estimated annual hours burden: 990.

Estimated annual cost: $147,510.

b. Disclosure Requirements

The proposed regulation contains three disclosure requirements that could affect ten or more persons in a 12-month period.

First, proposed regulation § 39.13(j)(12) requires a clearing member to provide each customer using separate accounts with a disclosure that, pursuant to part 190 of the Commission's regulations, all separate accounts of the customer will be combined in the event of the clearing member's bankruptcy. The Commission staff estimates that this would result in a total of one response per respondent on a one-time basis, and that respondents are likely to spend three hours to comply with this requirement for a total of

[113] This estimate reflects the aggregate information collection burden estimate associated with the proposed reporting requirements for the first annual period following implementation of the proposed regulation. Because proposed regulation § 39.13(j)(14)(ii) would result in a one-time reporting requirement, the Commission staff estimates that for each subsequent annual period, the number of reports, burden hours, and burden cost would be reduced accordingly.

90 annual burden hours and up to $447 annually, based on an hourly rate of $149. This would result in an aggregated cost of $13,410 (30 respondents × $447). This estimate reflects an initial disclosure distributed to existing customers subject to separate account treatment. The Commission staff expects that, on a going forward basis, this disclosure would be included in standard disclosures for new customers, and would therefore not result in any additional costs.

Second, proposed regulation § 39.13(j)(12)(iii) requires that a clearing member include the disclosure statement required by proposed regulation § 39.13(j)(12) on its website or within its Disclosure Document required by regulation § 1.55(i). If the clearing member opts to update its Disclosure Document, the Commission staff estimates that this proposed requirement would result in a total of one response on a one-time basis, and that respondents could expend up to $149 annually, based on an hourly rate of $149, to comply with the proposed regulation. This would result in an estimated 30 burden hours annually and an aggregated cost of $4,470 (30 respondents × $149). This estimate reflects one updated disclosure distributed to existing customers. If the clearing member opts to include the disclosure on its website, the Commission staff estimates that this proposed requirement would result in a total of one response on a one-time basis, and that respondents could expend up to $126 annually, based on an hourly rate of $126, to comply with the proposed regulation.[114] This would result in an estimated 30 burden hours annually and an aggregated cost of $3,780 (30 respondents × $126). The Commission staff expects that once the disclosure is included in the Disclosure

[114] This figure is based on the annual mean wage for U.S. Bureau of Labor Statistics (BLS) category 15-1254, "Web Developers." BLS Data.

Document required by regulation § 1.55(i) or posted on the clearing member's website, the clearing member would not incur any additional costs.

Third, proposed regulation § 39.13(j)(13) requires a clearing member to disclose in the Disclosure Document required under Commission regulation § 1.55(i) that it permits the separate treatment of accounts for the same customer under the terms and conditions of regulation § 39.13(j). The Commission staff estimates that this would result in a total of one response per respondent on a one-time basis, and that respondents could expend up to $149 annually, based on an hourly rate of $149, to comply with the proposed regulation. This would result in an estimated 30 burden hours annually and an aggregated cost of $4,470 (30 respondents × $149). This estimate reflects an initial updated disclosure distributed to existing customers. The Commission staff expects that once this disclosure is made, the disclosure would be included in the Disclosure Document required by regulation § 1.55(i) going forward, and would not result in any additional costs.

The aggregate information collection burden estimate associated with the proposed reporting requirements is as follows:[115]

Estimated number of respondents: 30.

Estimated number of reports: 120.

[115] For purposes of this analysis, the Commission staff calculates the aggregate information collection burden assuming that respondents choose to include the disclosure statement required by proposed regulation § 39.13(j)(12) on their websites *and* within their Disclosure Document required by proposed regulation §1.55(i), in order to comply with proposed regulation § 39.13(j)(12)(iii). Additionally, this estimate reflects the aggregate information collection burden estimate associated with the proposed disclosure requirements for the first annual period following implementation of the proposed regulation. Because each of proposed regulation § 39.13(j)(12), § 39.13(j)(12)(iii), and § 39.13(j)(13)(ii) would result in a one-time disclosure requirement for PRA purposes, the Commission staff estimates that for each subsequent annual period the number of respondents, reports, burden hours, and burden cost would be reduced accordingly.

Estimated annual hours burden: 180.

Estimated annual cost: $26,130.

c. Recordkeeping Requirements

The proposed regulation contains three recordkeeping requirements that could affect ten or more persons in a 12-month period.

First, proposed regulation § 39.13(j)(11) provides that where the customer of separate accounts subject to separate treatment pursuant to regulation § 39.13(j) has appointed a third-party as the primary contact to the clearing member, the clearing member must obtain and maintain current contact information of an authorized representative(s) at the customer and take reasonable steps to verify that such person is in fact an authorized representative of the customer. The clearing member would be required to review and, as necessary, update such information on at least an annual basis. The Commission staff estimates this would result in a total of 600 responses per respondent on an annual basis,[116] and that respondents could expend up to $42,000 annually, based on an hourly rate of $70.[117] This would result in an estimated 18,000 burden hours annually and an aggregated cost of $1,260,000 per annum (30 respondents × $42,000). This estimate contemplates annual validation of contact information for each customer.

[116] FIA stated that while the costs incurred by each FCM to comply with the conditions of CFTC Letter No. 19-17 varies depending on customer base, among larger FCMs with a significant institutional customer base, personnel costs would have included identifying and reviewing up to 3,000 customer agreements to determine which agreements required modification, and then negotiating amendments with customers or their advisors. The Commission staff estimates, based on the 30 largest FCMs by customer assets in segregation as of the Commission's FCM financial data report for May 31, 2022, that there are 18,000 customers of FCMs whose accounts could be in scope for the proposed regulation, with an average of 600 customers per FCM.

[117] This figure is based on the annual mean wage for BLS category 43-6010, "Secretaries & Administrative Assistants." BLS Data.

Second, proposed regulation § 39.13(j)(12)(ii) requires that a clearing member maintain documentation demonstrating that the part 190 disclosure statement required by proposed regulation § 39.13(j)(12) was delivered directly to the customer. The Commission staff estimates that this would result in a total of 600 responses on a one-time basis, and that respondents could expend up to $4,200 annually, based on an hourly rate of $70, to comply with the proposed regulation. This would result in an estimated 1,800 burden hours annually and an aggregated cost of $126,000 (30 respondents × $4,200). This estimate reflects initial recordkeeping of documentation that the disclosure was delivered to existing customers subject to separate account treatment. The Commission staff estimates that, once such recordkeeping is complete, the recordkeeping required by proposed regulation § 39.13(j)(12)(ii) would be required only with respect to new customers who receive disclosures pursuant to proposed regulation §39.13(j)(12), and the costs and burden hours associated with proposed regulation §39.13(j)(12)(ii) would be reduced accordingly.

Third, proposed regulation § 39.13(j)(14)(iii) provides that, to the extent the clearing member treats the separate accounts of a customer as accounts of separate entities, pursuant to the terms of proposed regulation § 39.13(j), the clearing member must maintain and keep current a list of all separate accounts receiving such treatment. The Commission staff believes the cost and time burden associated with, on an ongoing basis, maintaining and keeping current a list of all separate accounts receiving separate account treatment would vary among FCMs based on factors such as business conditions, customer needs, entry of new customers, and exit of other customers, and would be challenging to estimate with precision. The Commission staff anticipates that the

marginal time and cost burden of the recordkeeping required by the regulation, done in the routine course of business, would be negligible. However, proposed regulation § 39.13(j)(14)(iii) also requires a holistic review of such records no less than quarterly. The Commission staff estimates this would result in a total of four responses per respondent on an annual basis, and that respondents could expend up to $2,384 annually, based on an hourly rate of $149, to comply with the proposed regulation.[118] This would result in an estimated 480 burden hours annually and an aggregated cost of $71,520 per annum (30 respondents × $2,384).

The Commission notes that while certain other provisions of the proposed regulation may result in recordkeeping requirements, the Commission anticipates that any burden associated with these requirements is likely to be *de minimis* and therefore does not expect these provisions to increase the recordkeeping burden for FCMs.[119]

The aggregate information collection burden estimate associated with the proposed reporting requirements is as follows:[120]

Estimated number of respondents: 30.

Estimated number of reports: 36,120.

Estimated annual hours burden: 20,280.

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[118] For purposes of these estimates, the Commission staff treats each quarterly review by an FCM as a single response.

[119] *See, e.g.*, 17 CFR 1.32 (setting forth requirements for computation of customer segregated accounts); 17 CFR 1.73(a)(4) (requiring clearing FCMs to conduct stress tests in each customer account that could pose material risk to the FCM); 17 CFR 22.7(f)(6)(iii) (requirement to maintain residual interest); 17 CFR 1.22 & 22.7 (requirements to compute margin deficiencies).

[120] This estimate reflects the aggregate information collection burden estimates associated with the proposed disclosure requirements for the first annual period following implementation of the proposed regulation. Because, as noted above, proposed regulation § 39.13(j)(12)(ii) would result in a one-time recordkeeping requirement as to each customer (*i.e.*, once the disclosure is provided to existing customers, it would need to be provided only to new customers on a going forward basis), the Commission staff estimates that for each subsequent annual period the number of reports, burden hours, and burden cost would be reduced accordingly.

Estimated annual cost: $1,457,520.

2. Information Collection Comments

The Commission invites the public and other Federal agencies to comment on any aspect of the proposed information collection requirements discussed above. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission will consider public comments on this proposed collection of information regarding:

- Evaluating whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information will have a practical use;
- Evaluating the accuracy of the estimated burden of the proposed collection of information, including the degree to which the methodology and the assumptions that the Commission employed were valid;
- Enhancing the quality, utility, and clarity of the information proposed to be collected; and
- Reducing the burden of the proposed information collection requirements on registered entities, including through the use of appropriate automated, electronic, mechanical, or other technological information collection techniques; *e.g.*, permitting electronic submission of responses.

Organizations and individuals desiring to submit comments on the proposed information collection requirements should send those comments to:

- The Office of Information and Regulatory Affairs, Office of Management and Budget, Room 10235, New Executive Office Building, Washington, DC 20503, Attn: Desk Officer of the Commodity Futures Trading Commission;

- (202) 395-6566 (fax); or
- *OIRAsubmissions@omb.eop.gov* (email).

Please provide the Commission with a copy of submitted comments so that, if the Commission determines to promulgate a final rule, all such comments can be summarized and addressed in the final rule preamble. Refer to the **ADDRESSES** section of this notice of proposed rulemaking for comment submission instructions to the Commission. A copy of the supporting statements for the collections of information discussed above may be obtained by visiting RegInfo.gov. OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication of this document in the *Federal Register*. Therefore, a comment is best assured of receiving full consideration if OMB receives it within 30 days of publication of this notice of proposed rulemaking. Nothing in the foregoing affects the deadline enumerated above for public comment to the Commission on the proposed rules.

List of Subjects in 17 CFR Part 39

Clearing, Clearing Organizations, Commodity Futures, Consumer Protection.

For the reasons set forth in the preamble, the Commodity Futures Trading Commission proposes to amend 17 CFR part 39 as follows:

PART 39—DERIVATIVES CLEARING ORGANIZATIONS

1. The authority citation for part 39 continues to read as follows:

Authority: 7 U.S.C. 2, 6(c), 7a-1, and 12a(5); 12 U.S.C. 5464; 15 U.S.C. 8325; Section 752 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, title VII, sec. 752, July 21, 2010, 124 Stat. 1749.

2. In § 39.13, add paragraph (j) to read as follows:

§ 39.13 Risk management.

* * * * *

(j) *Separate account treatment with respect to withdrawal of customer initial margin.* For purposes of paragraph (g)(8)(iii) of this section, a derivatives clearing organization may permit a clearing member that is a futures commission merchant to treat the separate accounts of a customer as accounts of separate entities if such clearing member's written internal controls and procedures permit it to do so, and the derivatives clearing organization requires such clearing member to comply with the following conditions with respect to such separate accounts:

(1) The clearing member permits disbursements on a separate account basis only during the ordinary course of business.

(i) For purposes of this paragraph (j), "separate account" means any one of multiple accounts of the same customer that are carried by the same futures commission merchant that is a clearing member of a derivatives clearing organization.

(ii) For purposes of this paragraph (j), "ordinary course of business" means the standard day-to-day operation of the clearing member's business relationship with its customer. The following events are inconsistent with the ordinary course of business and would require the clearing member to cease permitting disbursements on a separate account basis with respect to all accounts of the relevant customer receiving separate account treatment, where such event occurs with respect to a customer as described in paragraphs (j)(1)(ii)(A) through (F) of this section, or with respect to all customer accounts receiving separate account treatment, where such event occurs with respect to the clearing member as described in paragraphs (j)(1)(ii)(G) through (I) of this section.

(A) Such customer, including any separate account of such customer, fails to deposit or maintain initial or maintenance margin or make payment of variation margin or option premium as specified in paragraph (j)(4) of this section.

(B) The occurrence and declaration by the clearing member of an event of default as defined in the account documentation executed between the clearing member and the customer.

(C) A good faith determination by the clearing member's chief compliance officer, one of its senior risk managers, or other senior manager, following such clearing member's own internal escalation procedures, that the customer is in financial distress, or there is significant and bona fide risk that the customer will be unable promptly to perform its financial obligations to the clearing member, whether due to operational reasons or otherwise.

(D) The insolvency or bankruptcy of the customer or a parent company of the customer.

(E) The clearing member receives notification that a board of trade, a derivatives clearing organization, a self-regulatory organization as defined in section 1.3 of this chapter or section 3(a)(26) of the Securities Exchange Act of 1934, the Commission, or another regulator with jurisdiction over the customer, has initiated an action with respect to the customer based on an allegation that the customer is in financial distress.

(F) The clearing member is directed to cease permitting disbursements on a separate account basis, with respect to one or more customers, by a board of trade, a derivatives clearing organization, a self-regulatory organization, the Commission, or another regulator with jurisdiction over the clearing member, pursuant to, as applicable,

board of trade, derivatives clearing organization or self-regulatory organization rules, government regulations, or law.

(G) The clearing member is notified by a board of trade, a derivatives clearing organization, a self-regulatory organization, the Commission, or another regulator with jurisdiction over the clearing member, that the board of trade, the derivatives clearing organization, the self-regulatory organization, the Commission, or other regulator, as applicable, believes the clearing member is in financial or other distress.

(H) The clearing member is under financial or other distress as determined in good faith by its chief compliance officer, senior risk managers, or other senior management.

(I) The bankruptcy of the clearing member or a parent company of the clearing member.

(iii) The clearing member must communicate to its designated self-regulatory organization and any derivatives clearing organization of which it is a clearing member the occurrence of any one of the events enumerated in paragraphs (j)(1)(ii)(A) through (I) of this section. Such communication must be made promptly in writing, and in any case no later than the next business day following the date on which the clearing member identifies or has been informed that such event has occurred.

(iv) A clearing member that has ceased permitting disbursements on a separate account basis pursuant to paragraph (j)(1)(ii) of this section may resume permitting disbursements on a separate account basis if such clearing member reasonably believes, based on new information, that the circumstances triggering cessation of separate account treatment pursuant to paragraphs (j)(1)(ii)(A) through (I) of this section have been cured,

and such clearing member provides in writing to its designated self-regulatory organization and any derivatives clearing organization of which it is a clearing member a notification that it will resume separate account treatment, and the factual basis and rationale for its conclusion that the circumstances triggering cessation of separate account treatment pursuant to paragraphs (j)(1)(ii)(A) through (I) of this section have been cured. If the circumstances triggering cessation of separate account treatment were an action or direction by one of the entities described in paragraphs (j)(1)(ii)(E) through (G) of this section, then the cure of those circumstances would require the withdrawal or other appropriate termination of such action or direction by that entity.

(2) The clearing member obtains from the customer or, as applicable, the manager of a separate account, information sufficient for the clearing member to:

(i) Assess the value of the assets dedicated to such separate account; and

(ii) Identify the direct or indirect parent company of the customer, as applicable, if such customer has a direct or indirect parent company.

(3) The clearing member's internal risk management policies and procedures must provide for stress testing and credit limits for customers with separate accounts. This stress testing must be performed, and the credit limits must be applied, both on an individual separate account and on a combined account basis.

(4) Each separate account must be on a "one business day margin call." The following requirements apply solely for purposes of this paragraph (j)(4):

(i) Except as explicitly provided in this paragraph (j)(4), if the margin call is issued by 11:00 a.m. Eastern Time on a United States business day, it must be met by the applicable customer no later than the close of the Fedwire Funds Service on the same

United States business day. In no case can a clearing member contractually agree to delay issuing such a margin call until after 11:00 a.m. Eastern Time on any given United States business day or to otherwise engage in practices that are intended to circumvent this paragraph (j)(4) by causing such delay.

(ii) Payment of margin in Japanese Yen shall be considered in compliance with the requirements of this paragraph (j)(4) if received by the applicable clearing member by 12:00 p.m., Eastern Time, on the second United States business day after the business day on which the margin call is issued.

(iii) Payment of margin in fiat currencies other than U.S. Dollars, Canadian Dollars, or Japanese Yen shall be considered in compliance with the requirements of this paragraph (j)(4) if received by the applicable clearing member by 12:00 p.m., Eastern Time, on the United States business day after the business day on which the margin call is issued.

(iv) The relevant deadline for payment of margin in fiat currencies other than U.S. Dollars may be extended by up to one additional United States business day and still be considered in compliance with the requirements of this paragraph (j)(4) if payment is delayed due to a banking holiday in the jurisdiction of issue of the currency. For payments in Euro, either the customer or the investment manager managing the separate account may designate one country within the Eurozone that they have the most significant contacts with for purposes of meeting margin calls, whose banking holidays shall be referred to for this purpose.

(v) A failure to deposit, maintain, or pay margin or option premium due to unusual administrative error or operational constraints that a customer or investment

manager acting diligently and in good faith could not have reasonably foreseen does not constitute a failure to comply with the requirements of this paragraph (j)(4). For these purposes, a clearing member's determination that the failure to deposit, maintain, or pay margin or option premium is due to such administrative error or operational constraints must be based on the clearing member's reasonable belief in light of information known to the clearing member at the time the clearing member learns of the relevant administrative error or operational constraint.

(vi) A clearing member would not be in compliance with the requirements of this paragraph (j)(4) if it contractually agrees to provide customers with periods of time to meet margin calls that extend beyond the time periods specified in paragraphs (j)(4)(i) through (v) of this section, or engages in practices that are designed to circumvent this paragraph (j)(4).

(vii) For purposes of this paragraph (j)(4), "United States business day" means weekdays not including Federal holidays as established by 5 U.S.C. 6103. A margin call issued after 11:00 a.m. Eastern Time on a United States business day, or on a Saturday, Sunday, or a Federal holiday, shall be considered to have been issued before 11:00 a.m. Eastern Time on the next day that is a United States business day.

(5) The margin requirement for each separate account is calculated independently from all other separate accounts of the same customer with no offsets or spreads recognized across the separate accounts. A clearing member is required to treat each separate account of a customer independently from all other separate accounts of the same customer for purposes of computing capital charges for under-margined customer accounts in determining its adjusted net capital under §1.17 of this chapter.

(6) The clearing member must record each separate account independently in its books and records (*i.e.*, the clearing member must record the balance of each separate account as a receivable (debit or deficit) or payable with no offsets between the other separate accounts of the same customer). A clearing member is required to treat each separate account of a customer independently from all other separate accounts of the same customer for purposes of determining whether a receivable from a separate account that represents a deficit or debit ledger balance may be included in the clearing member's current assets in computing its adjusted net capital under §1.17(c)(2) of this chapter.

(7) A customer receivable for a debit or deficit from a separate account must only be considered a current or allowable asset for purposes of §1.17(c)(2) of this chapter based on the assets of that separate account, and not on the assets held in another separate account of the same customer.

(8) In calculating the amount of its own funds the clearing member must use to cover debit or deficit balances pursuant to §1.20(i) or §22.2(f) of this chapter, the clearing member must include any debit or deficit of any separate account, and must reflect that calculation in each applicable report.

(9) The clearing member must include the margin deficiency of each separate account, and cover such deficiency with its own funds, as applicable, for purposes of its residual interest and legally segregated operationally commingled compliance calculations, as applicable under § 1.22, § 22.2, and 30.7 of this chapter.

(10) In determining its residual interest target for purposes of § 1.23(c) of this chapter, the clearing member must calculate customer receivables computed on a separate account basis.

(11) Where the customer of separate accounts subject to separate treatment pursuant to this paragraph (j) has appointed a third-party as the primary contact to the clearing member, the clearing member must obtain and maintain current contact information of an authorized representative(s) at the customer, and take reasonable steps to verify that such contact information is accurate and that person is in fact an authorized representative of the customer. The clearing member must review and, as applicable, update such contact information no less than annually.

(12) The clearing member must provide each customer using separate accounts with a disclosure that, pursuant to part 190 of this chapter, all separate accounts of the customer in each account class will be combined in the event of the clearing member's bankruptcy.

(i) The disclosure statement required by this paragraph (j)(12) must be delivered separately to the customer via electronic means in writing or in such other manner as the clearing member customarily delivers disclosures pursuant to applicable Commission regulations, and as permissible under the clearing member's customer documentation.

(ii) The clearing member must maintain documentation demonstrating that the disclosure statement required by this paragraph (j)(12) was delivered directly to the customer.

(iii) The clearing member must include the disclosure statement required by this paragraph (j)(12) on its website or within its Disclosure Document required by § 1.55(i) of this chapter.

(13) The clearing member must disclose in the Disclosure Document required under § 1.55(i) of this chapter that it permits the separate treatment of accounts for the same customer under the terms and conditions of this paragraph (j).

(14) To the extent the clearing member treats the separate accounts of a customer as accounts of separate entities, pursuant to the terms of this paragraph (j), the clearing member must:

(i) Apply such treatment in a consistent manner over time;

(ii) Provide a one-time notification (*i.e.*, once such a notification is made, the clearing member is not required to repeat it) to its designated self-regulatory organization and any derivatives clearing organization of which it is a clearing member that it will apply such treatment to one or more customers; and

(iii) Maintain and keep current a list of all separate accounts receiving such treatment. The clearing member must conduct a review of its records of accounts receiving separate treatment no less than quarterly.

* * * * *

Issued in Washington, DC, on March 22, 2023 by the Commission.

Robert Sidman,

Deputy Secretary of the Commission.

NOTE: The following appendices will not appear in the Code of Federal Regulations.

Appendices to Derivatives Clearing Organization Risk Management Regulations to Account for the Treatment of Separate Accounts by Futures Commission Merchants—Voting Summary and Commissioner's Statement

Appendix 1—Voting Summary

On this matter, Chairman Behnam and Commissioners Johnson, Goldsmith Romero, Mersinger, and Pham voted in the affirmative. No Commissioner voted in the negative.

Appendix 2—Statement of Commissioner Kristin N. Johnson

I support the issuance by the Commodity Futures Trading Commission (CFTC) of the Notice of Proposed Amendments to Derivatives Clearing Organization (DCO) Risk Management Regulations to Account for the Treatment of Separate Accounts by Futures Commission Merchants (FCMs) (the "NPRM").

The proposed amendments codify a no-action position issued by the CFTC's Division of Clearing and Risk (DCR) and Market Participants Division (MPD) that imposed certain conditions on FCM's ability to treat accounts owned by a single customer as separate accounts.[1] These conditions aim to protect customer assets and avoid systemic risk.[2] I write today to underscore the significance of these protections for customer assets.

Segregating or separating a firm's proprietary funds from customer funds is a critical element in protecting not only customers, but also the broader financial system. In the absence

[1] Advisory and Time-Limited No-Action Relief with Respect to the Treatment of Separate Accounts by Futures Commission Merchants, CFTC Letter No. 19-17, July 10, 2019, *https://www.cftc.gov/csl/19-17/download*.
[2] These conditions aim to ensure that FCMs "(i) carry out such separate account treatment in a consistent and documented manner; (ii) monitor customer accounts on a separate and combined basis; (iii) identify and act upon instances of financial or operational distress that necessitate a cessation of separate account treatment; (iv) provide appropriate disclosures to customers regarding separate account treatment; and (v) apprise their DSROs when they apply separate account treatment or an event has occurred that would necessitate cessation of separate account treatment." NPRM at Section II.A.

of the proposed risk management conditions and robust compliance with the same, conditions of financial distress could lead to preventable losses for customers or FCMs.[3]

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[3] *Id.* (discussing Proposed Regulation § 39.13(j)(1)).