

Joint Audit Committee

REGULATORY ALERT

TO: Chief Executive Officers #20-03
Chief Financial Officers
Chief Compliance Officers

CC: Division of Clearing and Risk, CFTC
Division of Swap Dealer and Intermediary Oversight, CFTC

DATE: September 23, 2020

SUBJECT: CFTC Letter No. 20-28 – Supplemental Advisory to CFTC Letter No. 19-17

The Commodity Futures Trading Commission (“CFTC”) issued CFTC Letter No. 19-17, dated July 10, 2019, containing, in part, guidance with respect to CFTC Regulation 1.56(b). CFTC Letter No. 19-17 may be found on the CFTC’s website at <https://www.cftc.gov/csl/19-17/download>.

On September 15, 2020, the CFTC issued CFTC Letter No. 20-28 Supplemental Advisory and Time-Limited No-Action Relief with Respect to the Treatment of Separate Accounts by FCMs (the “CFTC Letter 20-28”), containing, in part, further guidance and a March 31, 2021 timeframe for compliance with CFTC Regulations 1.56(b) and 1.56(c). CFTC Letter 20-28 may be found on the CFTC’s website at <https://www.cftc.gov/csl/20-28/download>.

As such, in accordance with CFTC Letter 20-28, JAC Regulatory Alert #19-03 (attached) is amended to allow FCMs until March 31, 2021 to take corrective action to identify and rectify any customer and noncustomer agreements which are not in compliance with CFTC Regulation 1.56(b). All other requirements of JAC Regulatory Alert #19-03 remain in effect.

Finally, FCMs should review and where necessary enhance their internal controls and procedures pertaining to the customer and noncustomer on-boarding process to ensure all account agreements/documentation are in compliance with all industry rules and regulations.

If you have any questions, please contact your DSRO.

Joint Audit Committee

REGULATORY ALERT

TO: Chief Executive Officers #19-03
Chief Financial Officers
Chief Compliance Officers

CC: Division of Swap Dealer and Intermediary Oversight, CFTC

DATE: May 14, 2019

SUBJECT: CFTC Regulation 1.56(b) – Prohibition of Guarantee Against Loss

Recently clarification has been sought as to the acceptability of certain clauses in FCM account agreements with their customers and noncustomers as it pertains to the prohibition of guarantees against loss. This JAC Regulatory Alert serves as a reminder of an FCM's responsibility to comply with CFTC Regulations concerning the prohibition of guarantees against loss as stated in CFTC Regulation 1.56(b). To assist FCMs in this regard, the JAC is providing the following guidance as to its reading, interpretation and application of CFTC Regulation 1.56(b).

CFTC Regulation §1.56 – Prohibition of Guarantees Against Loss

https://www.ecfr.gov/cgi-bin/text-idx?SID=9a8a903ae806435d004067de3b4442de&mc=true&node=se17.1.1_156&rgn=div8

(b) No futures commission merchant or introducing broker may in any way represent that it will, with respect to any commodity interest in any account carried by the futures commission merchant for or on behalf of any person:

- (1) Guarantee such person against loss;
- (2) Limit the loss of such person; or
- (3) Not call for or attempt to collect initial and maintenance margin as established by the rules of the applicable board of trade.

FCM Account Agreements and CFTC Regulation 1.56(b)

In accordance with CFTC Regulation 1.56(b) an FCM may not in any way represent that it will: (i) guarantee a customer or noncustomer against loss; (ii) limit the loss of such customer or noncustomer; or (iii) not call for or attempt to collect required margin. Therefore, for example, JAC deems limited recourse and nonrecourse clauses are not in compliance with industry regulations and are not permitted

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in any agreements between an FCM and its customers and noncustomers. CFTC regulations require an FCM to have at all times the absolute right to look to funds in all accounts of the beneficial owner, including accounts that are under different control, as well as the right to call the beneficial owner for funds. For clarity, in the case of a separate account of a beneficial owner managed by an asset manager, the FCM must have at all times the absolute right to look to funds in all accounts of the beneficial owner even accounts that are under different control, as well as the right to call the underlying beneficial owner for funds even if beyond the amount the beneficial owner has allocated to the asset manager(s).

FCMs should perform a comprehensive and thorough review of all their customer and noncustomer account agreements for language which does not comply with CFTC Regulation 1.56(b). For the avoidance of doubt, limited recourse and nonrecourse clauses are not in compliance with industry regulations and are not allowed in any agreements with customers and noncustomers. Further, any terms or clauses which in any way prevent an FCM from accessing funds in other accounts of an underlying beneficial owner or calling on the underlying beneficial owner for additional funds are prohibited.

Thus, FCMs must take immediate corrective action to identify and rectify any customer and noncustomer agreements which are not in compliance with CFTC Regulation 1.56(b).

Finally, FCMs should review and where necessary enhance their internal controls and procedures pertaining to the customer and noncustomer on-boarding process to ensure all account agreements/documentation are in compliance with all industry rules and regulations.

If you have any questions, please contact your DSRO.