

II. The New Rule and Amendments

A. New Rule 1.49

1. Definitions

In the proposed rule, the Commission had defined the terms “non-money center country” and “non-money center currency.” These terms, however, were not used elsewhere in Rule 1.49.

Accordingly, the Commission is not including these definitions in the final rule.

2. Permissible Currencies

The Commission is adopting Rule 1.49 to provide that FCM obligations owed to customers shall be held in: (1) U.S. dollars; (2) a currency in which funds were deposited by the customer, or converted to at the request of the customer, to the extent of such deposits and conversions; or (3) a currency in which funds have accrued to the customer as a result of trading on a designated contract market or registered derivatives transaction execution facility (“DTF”). Any customer may deposit foreign currency with an FCM if the FCM permits it, not just those customers trading contracts priced and settled in a foreign currency.

As noted above, the internationalization of the futures markets has resulted in customers who, for many different reasons, want funds denominated in currencies other than the U.S. dollar. If a customer or prospective customer of an FCM prefers to deposit funds with an FCM in a currency other than the U.S. dollar, or to convert funds from one currency to another, the FCM should not be prevented from accepting or holding funds in the preferred currency of the customer or prospective customer.

An FCM may not convert customer funds from one currency to another without customer authorization. An account agreement could provide, however, that by placing an order in a contract settled in a particular currency, a customer agrees to convert to the appropriate currency funds sufficient to meet the applicable margin requirement. Under Rule 1.49(b)(2), an FCM is required to prepare and maintain a written record each time customer funds are converted from one currency to another. The record must include the date the transaction was executed, the currencies converted, the amount converted, and the resulting amount. The FCM is also required to make the information contained in this record available to the customer upon the customer's request. Additionally, the Commission noted in the proposing release that, pursuant to Rule 1.33(a),

the FCM must include this information in the monthly statements provided to the customer.

FIA noted that FCMs frequently execute multiple transactions on behalf of a customer throughout a trading day. NFA noted that FCMs will often execute foreign currency transactions using bunched orders that combine orders involving multiple customers, multiple counterparties, and multiple transactions. To provide detailed information regarding each transaction on the customer's monthly statement would impose a significant burden on the FCM. FIA asked that the Commission confirm its view that providing the required information on the monthly statement in the aggregate rather than with respect to each transaction would be sufficient to meet the FCM's obligation under Rule 1.33. The Commission concurs that such a procedure would fulfill the FCM's obligation under Rule 1.33. As noted in the FIA comment letter, to be in compliance with Rule 1.49(b)(2), an FCM must be able to prepare a report that provides the details of individual transactions upon a customer's request.

Another aspect of the internationalization of the futures and options markets is the increasing number of contracts offered on foreign financial instruments and indices. These contracts are priced and settled in the currency of the underlying instrument or index. Accordingly, accruals resulting from trading in such instruments will be in currency other than U.S. dollars. Under the rule, such accruals may be held in the applicable currency. A customer, of course, may request that such accruals be converted to U.S. dollars.

Pursuant to Interp. 12, customers had to authorize the deposit of foreign currency funds into foreign depositories as part of a subordination agreement. The Commission is eliminating this written authorization requirement. If a customer deposits funds with an FCM in a currency other than U.S. dollars, or requests a conversion of funds to a non-U.S. dollar currency, the customer will be aware of the fact that the funds are being held in a currency other than U.S. dollars. With regard to funds other than U.S. dollars that are held for margin or have accrued to the customer as a result of trading in contracts priced and settled in a non-U.S. currency, the Commission notes that the specifications for contracts traded on designated contract markets are widely known and generally available.⁹ Accordingly, when a

customer trades in a futures or options contract that is priced and settled in a currency other than U.S. dollars, a customer should be aware that the margin for and accruals from such trading may be held in the applicable currency.

In the proposing release, the Commission noted “that if a customer has previously not traded in contracts that are priced and settled in a currency other than U.S. dollars, a firm *should* inform the customer if the accruals from the trades will be held in a currency other than U.S. dollars.”¹⁰ NFA and FIA both objected to this statement, as they believed it seemed to impose disclosure obligations beyond those under Commission Rule 1.55.¹¹ It was not the Commission's intention to impose a disclosure obligation with respect to such customers and such contracts. Rather, as suggested by FIA in its letter, the Commission “intended solely to caution FCMs to consider whether they should make such disclosure” by taking into consideration the facts and circumstances of the particular customer.

3. Location of Depositories

The rule permits an FCM or derivatives clearing organization (“DCO”) to hold customer funds of any denomination in the U.S. or in any money center country (Canada, France, Italy, Germany, Japan, and the United Kingdom). Hence, customer funds of any denomination could be held in any of the Group of Seven (“G7”) countries. The G7 countries represent the world's largest industrial democracies. Representatives from these countries meet several times a year to coordinate their cooperation on issues of economic policy. In this regard, the U.S. and its financial regulatory agencies have had successful cooperation with the respective financial regulatory agencies of these countries.

Both NFA and FIA indicated a desire to have the definition of a money center country expanded. NFA suggested that the definition include “other locations with stable currencies and other indicia that customer funds will be relatively secure.” The Commission has decided not to expand the definition in this manner. The Commission believes that the establishment of a broad and

transaction execution facilities, respectively, to make contract specifications publicly available. For example, the specifications for contracts traded on the Chicago Mercantile Exchange are available on its Web site at: <http://www.cme.com>.

¹⁰ 67 FR at 52643. (Emphasis added).

¹¹ Rule 1.55 permits FCMs to open an account for an “institutional customer” without first furnishing the customer with a disclosure statement.

⁹ Section 5(b)(7) of the Act and Section 5a(d)(4) of the Act require contract markets and derivatives