

§ 30.11

17 CFR Ch. I (4-1-06 Edition)

forth with particularity the reasons why that person believes that he should be exempt from such requirement. The Commission may, in its discretion, grant such an exemption if that person demonstrates to the Commission's satisfaction that the exemption is not otherwise contrary to the public interest or to the purposes of the provision from which exemption is sought. The petition will be granted or denied on the basis of the papers filed. The petition may be granted subject to such terms and conditions as the Commission may find appropriate.

(b) Any foreign person that files a petition for an exemption under this section shall be eligible for such an exemption notwithstanding its presence in the United States through U.S. bank branches or divisions if, in conjunction with a petition for confirmation of relief granted under an existing Commission order issued pursuant to this section, it complies with the following conditions:

(1) No U.S. bank branch, office or division will engage in the trading of futures or options on futures within or from the United States, except for its own proprietary account;

(2) No U.S. bank branch, office or division will refer any foreign futures or foreign options customer to the foreign person or otherwise be involved in the foreign person's business in foreign futures or foreign option transactions;

(3) No U.S. bank branch, office or division will solicit any foreign futures or foreign option business or purchase or sell foreign futures or foreign option contracts on behalf of any foreign futures or foreign option customers or otherwise engage in any activity subject to regulation under this part or engage in any clerical duties related thereto. If any U.S. division, office or branch desires to engage in such activities, it will only do so through an appropriate Commission registrant;

(4) The foreign person will maintain outside the United States all contract documents, books and records regarding foreign futures and foreign option transactions;

(5) The foreign person and each of its U.S. bank branches, offices or divisions agree upon request of the Commission, the National Futures As-

sociation or the U.S. Department of Justice, access to their books and records for the purpose of ensuring compliance with the foregoing undertakings and consent to make such records available for inspection at a location in the United States within 72 hours after service of the request; and

(6) Although it will continue to engage in normal commercial activities, no U.S. bank branch, office or division of the foreign person will establish relationships in the United States with the applicant's foreign futures or foreign option customers for the purpose of facilitating or effecting transactions in foreign futures or foreign option contracts.

[52 FR 28998, Aug. 5, 1987, as amended at 69 FR 49803, Aug. 12, 2004]

§ 30.11 Applicability of state law.

Pursuant to section 12(e)(2) of the Act, the provisions of any state law, including any rule or regulation thereunder, may be applicable to any person required to be registered under this part who solicits foreign futures and foreign options customers and who shall fail or refuse to obtain such registration, unless such person is exempt from such registration in accordance with the provisions of § 30.4, § 30.5 or § 30.10 of this part.

§ 30.12 Direct foreign order transmittal.

(a) *Authorized customers defined.* For the purposes of this section, an "authorized customer" of a futures commission merchant shall mean any foreign futures or foreign options customer, as defined in § 30.1(c), or its designated representative, that:

(1) The futures commission merchant has authorized to place orders for the account of the futures commission merchant's foreign futures and options customer omnibus account; and

(2)(i) Is an eligible swap participant, as defined in § 35.1(b)(2) of this chapter, or

(ii) Whose investment decisions with respect to foreign futures and foreign option transactions are made by a commodity trading advisor subject to regulation under the Act, including any investment adviser registered as such

with the Securities and Exchange Commission that is exempt from regulation as a commodity trading advisor under the Act or Commission regulations, or a foreign person performing a similar role or function subject as such to foreign regulation, *provided* that the commodity trading advisor has total assets under management exceeding \$50,000,000 and that the commodity trading advisor places the foreign futures or foreign options order.

(b) *Procedures for futures commission merchants.* It shall be unlawful for any futures commission merchant to permit an authorized customer to place orders for execution in the futures commission merchant's foreign futures and options customer omnibus account directly with a person exempt from registration under paragraphs (c) and (d) of this section, unless, such futures commission merchant:

(1) Meets one of the following capital requirements, as determined by the futures commission merchant's most recent required filing of a Form 1-FR-FCM with the Commission:

(i) Possesses \$20,000,000 in adjusted net capital, as defined by §1.17(c)(5) of this chapter; or

(ii) Possesses the greater of three times the amount of adjusted net capital required by §1.17(a)(1)(i)(A) of this chapter or three times the amount of adjusted net capital required by §1.17(a)(1)(i)(B) of this chapter; and

(2) Has established control procedures that will serve as guidelines for permitting direct contacts between any authorized customer of the futures commission merchant and any person exempt from registration under paragraphs (c) or (d) of this section, and has in place appropriate risk management procedures to monitor its own risk relative to its authorized customers' risk aggregated across all markets, including, but not limited to, procedures to ensure that each authorized customer satisfies the participation criteria set forth in paragraph (a) of this section and to specify the manner in which trades may be executed through its customer omnibus account pursuant to this section;

(3) Furnishes a written disclosure statement to each such authorized customer advising the customer of the ad-

ditional risks the customer may be assuming in placing orders directly with the foreign broker. The disclosure statement must read as follows:

Direct Order Transmittal Client Disclosure Statement

This statement applies to the ability of authorized customers¹ of [FCM] to place orders for foreign futures and options transactions directly with non-US entities (each, an "Executing Firm") that execute transactions on behalf of [FCM's] foreign futures and options customer omnibus accounts.

Please be aware of the following should you be permitted to place the type of orders specified above.

- The orders you place with an Executing Firm are for [FCM's] foreign futures and options customer omnibus account maintained with a foreign clearing firm. Consequently, [FCM] may limit or otherwise condition the orders you place with the Executing Firm.

- You should be aware of the relationship of the Executing Firm and [FCM]. [FCM] may not be responsible for the acts, omissions, or errors of the Executing Firm, or its representatives, with which you place your orders. In addition, the Executing Firm may not be affiliated with [FCM]. If you choose to place orders directly with an Executing Firm, you may be doing so at your own risk.

- It is your responsibility to inquire about the applicable laws and regulations that govern the foreign exchanges on which transactions will be executed on your behalf. Any orders placed by you for execution on that exchange will be subject to such rules and regulations, its customs and usages, as well as any local laws that may govern transactions on that exchange. These laws, rules, regulations, customs and usages may offer different or diminished protection from those that govern transactions on US exchanges. In particular, funds received from customers to margin foreign futures transactions may not be provided the same protections as funds received to margin futures transactions on domestic exchanges. Before you trade, you should familiarize yourself with the foreign rules which will apply to your particular transaction. United States regulatory authorities may be unable to compel the enforcement of the rules of regulatory authorities or markets in non-US jurisdictions where transactions may be effected.

- It is your responsibility to determine whether the Executing Firm has consented to the jurisdiction of the courts in the United States. In general, neither the Executing Firm nor any individuals associated

¹You should contact your account executive regarding your eligibility to participate in the direct order transmittal process.

with the Executing Firm will be registered in any capacity with the Commodity Futures Trading Commission. Similarly, your contacts with the Executing Firm may not be sufficient to subject the Executing Firm to the jurisdiction of courts in the United States in the absence of the Executing Firm's consent. Accordingly, neither the courts of the United States nor the Commission's reparations program may be available as a forum for resolution of any disagreements you may have with the Executing Firm, and your recourse may be limited to actions outside the United States.

- Unless you object within five (5) days, by giving notice as provided in your customer agreement after receipt of this disclosure, [FCM] will assume your consent to the aforementioned conditions.

(c) *Exemption for foreign futures and options brokers.* Any person not located in the United States, its territories or possessions, who is otherwise required in accordance with this part to be registered with the Commission as a futures commission merchant or as an introducing broker will be exempt from such registration, notwithstanding that such person accepts orders for foreign futures and foreign options transactions from authorized customers of a registered futures commission merchant that meets the requirements of paragraph (b)(1) of this section, provided, that:

(1) The orders are executed for or on behalf of the foreign futures and options customer omnibus account of a registered futures commission merchant;

(2) The person does not solicit or accept any money, securities or property (or extend credit in lieu thereof) directly from any U.S. foreign futures and options customer to margin, guarantee or secure any trades or contracts that result or may result therefrom; and

(3) The person is a foreign futures and options broker, as defined by §30.1(e).

(d) *Exemption for foreign futures and options brokers carrying a foreign futures and options customer omnibus account.* Any person not located in the United States, its territories or possessions, who is otherwise required in accordance with this part to be registered with the Commission as a futures commission merchant will be exempt from

such registration, notwithstanding that such person:

(1) Carries the foreign futures and options customer omnibus account of a futures commission merchant that meets the requirements of paragraph (b)(1) of this section;

(2) Accepts orders for foreign futures and foreign options transactions from authorized customers for the execution of the trades for or on behalf of the foreign futures and options customer omnibus account of a registered futures commission merchant either directly or pursuant to a give-up arrangement; and

(3) The person is a foreign futures and options broker, as defined by §30.1(e).

[65 FR 47280, Aug. 2, 2000]

APPENDIX A TO PART 30—INTERPRETATIVE STATEMENT WITH RESPECT TO THE COMMISSION'S EXEMPTIVE AUTHORITY UNDER §30.10 OF ITS RULES

Part 30 of the Commission's regulations establishes the regulatory structure governing the offer and sale in the United States of futures and options contracts made or to be made on or subject to the rules of a foreign board of trade. Section 30.10 of these regulations provides that, upon petition, the Commission may exempt any person from any requirement of this part. Specifically, section 30.10 states:

Any person adversely affected by any requirement of this part may file a petition with the Secretary of the Commission, which petition must set forth with particularity the reasons why that person believes that he should be exempt from such requirement. The Commission may, in its discretion, grant such an exemption if that person demonstrates to the Commission's satisfaction that the exemption is not otherwise contrary to the public interest or to the purposes of the provision from which exemption is sought. The petition will be granted or denied on the basis of the papers filed. The petition may be granted subject to such terms and conditions as the Commission may find appropriate.

As the provisions of this section make clear, any person subject to regulation under part 30 may petition the Commission for an exemption. In adopting these regulations, however, the Commission noted in particular that persons located outside the United States that solicit or accept orders directly from United States customers for foreign futures or options transactions and that are

subject to a comparable regulatory scheme in the country in which they are located may apply under section 30.10 for exemption from some or all of the requirements that would otherwise be applicable to such persons. This interpretative statement sets forth the elements that the Commission intends to evaluate in determining whether a particular regulatory program may be found to be comparable to the Commission's program.

The Commission wishes to emphasize, however, that this interpretative statement is not all inclusive, and that information with respect to other aspects of a particular regulatory program may be submitted by a petitioner or requested by the Commission. In this connection, the Commission would have broad discretion to determine that the policies of any program element generally are met, notwithstanding the fact that the offshore program does not contain an element identical to that of the Commission's regulatory program and conversely may assess how particular elements are in fact applied by offshore authorities. Thus, for example, in order to find that a particular program is comparable, the regulations thereunder would have to be applicable to all United States customers, notwithstanding any exemptions that might otherwise be available to particular classes of customer located offshore. A petitioner, therefore, must set forth with particularity the factual basis for a finding of comparability and the reasons why such policies and purposes are met, notwithstanding differences of degree and kind in its regulatory program.

No exemptions of a general nature will be granted unless the persons to which the exemption is to be applied consent to submit to jurisdiction in the United States by designating an agent for service of process pursuant to the provisions of rule 30.5 with respect to any activities of such persons otherwise subject to regulation under this part and to notify the National Futures Association of the commencement or termination of business in the United States. In this connection, to be exempted, such person must further agree to respond to a request to confirm that it continues to do business in the United States.

Persons located outside the United States may seek an exemption on their own behalf or an exemption may be sought on a general basis through the governmental agency responsible for the implementation and enforcement of the regulatory program in question, or the self-regulatory organizations of which such persons are members. The appropriate petitioner is a matter of judgment and may be determined by the parties seeking the exemption. The Commission, however, notes that it will be able to address petitions more efficiently if they are filed by the governmental agency or self-regulatory organi-

zation responsible for the regulatory program.

In this connection, as will be discussed in more detail below, any exemption of a general nature based on comparability will be conditioned upon appropriate information sharing arrangements between the Commission and the relevant governmental agency and/or self-regulatory organization. Representations from the appropriate governmental agency with respect to the applicability of any blocking statutes that may prevent the sharing of information requested under private arrangements would also be considered. Finally, in considering an exemption request, the Commission will take into account the extent to which United States persons or contracts regulated by the Commission are permitted to engage in futures-related activities or be offered in the country from which an exemption is sought.

In the Commission's review, the minimum elements of a comparable regulatory program would include: (1) Registration, authorization or other form of licensing, fitness review or qualification of persons through which customer orders are solicited and accepted; (2) minimum financial requirements for those persons that accept customer funds; (3) protection of customer funds from misapplication; (4) recordkeeping and reporting requirements; (5) minimum sales practice standards, including disclosure of the risks of futures and options transactions and, in particular, the risk of transactions undertaken outside the jurisdiction of domestic law; and (6) compliance.

Qualification. Under domestic law, registration identifies to the Commission, the public and other governmental agencies the individuals and entities that are properly authorized to solicit and accept customer orders and are in good standing. Equally important, the procedure provides the Commission, through the National Futures Association, the opportunity to determine whether applicants are unfit to deal with the public. In this connection, the standards for determining whether a person through its principals is fit for registration with the Commission are set forth in section 8a(2)-8a(4) of the Act. Timely access to information as to a firm's good standing and the application by relevant authorities of membership and licensing criteria, as well as the criteria themselves, will be considered by the Commission in assessing comparability.

Minimum Financial Requirements. Minimum financial requirements for persons that handle customer funds serve at least three critical functions. First, they provide a cushion together with margin such that in the event of a default of a customer, the losses of that customer need not adversely affect the funds held on behalf of other customers. Second, they help ensure that the person has sufficient funds to operate its business and,

therefore, is less likely to be tempted to misapply customer funds for its own purposes. Third, they ensure that the person holding customer funds has some financial stake in its business and, therefore, is serious in its intent. In assessing comparability, capital rules or their equivalent will be considered together with any provisions made for insuring customer losses, the scope of clearing guarantees and segregation or customer trust calculation and accounting requirements which, to the extent they cover undermargined accounts, can provide significant protection of one customer from another customer's losses.

Customer Funds. The Act requires the strict segregation of customer funds from those of the person holding such funds. One of the primary purposes of this requirement is to prevent the misapplication of those funds for purposes other than those intended by the customer, which may affect not only the customer but the market as a whole. The purpose of segregation is also to identify customer deposits as assets of the customer, rather than the firm, in order that in bankruptcy such funds are payable only to satisfy the carrying firm's obligations to such customers and not other obligations of the firm. In assessing comparability of protection of customer funds, the Commission will consider protections accorded customer funds in a bankruptcy under applicable law, as well as protection from fraud.

Recordkeeping and Reporting. Recordkeeping requirements have long been recognized as the linchpin of the Commission's regulatory scheme. Reporting and recordkeeping requirements assist in determining that a registrant is acting in accordance with the provisions of the Act and the rules, regulations and orders of the Commission thereunder. Similarly, reporting requirements ensure that customers are timely advised of the transactions that have been executed on their behalf, thus ensuring that they are aware of their positions in the markets and may object to any transactions that they believe are in error. The Commission will consider the types of records maintained, the ability through those records to trace funds and transactions, and the period of retention and accessibility of records under the information sharing arrangements discussed below in considering comparability.

Sales Practice Standards. In 1982, Congress reaffirmed the importance of minimum sales practice standards to protect customers from fraud or misrepresentation by requiring any futures association registered by the Commission to adopt and enforce rules governing the sales practices of its members. The Commission has consistently provided that written disclosure of the risks of futures and options trading is essential to ensure that potential customers are aware of these risks

and are not otherwise misled and that other appropriate disclosure is made. The Commission will review the type and manner of disclosure given and the mechanisms for assuring the disclosure requirements are met and, in particular, the treatment of discretionary accounts for which, for example, Commission rule 166.2 requires particularized documentation of intent to confer discretion in the case of foreign futures and options transactions.

Compliance. Finally, in assessing comparability of a program, the Commission will examine the procedures employed by the governmental authority or the appropriate self-regulatory organization to audit for compliance with, and to take action as appropriate against those persons that violate, the requirements of that program.

Information Sharing. As noted above, any exemption of a general nature would also require an information sharing arrangement between the Commission and the appropriate governmental or self-regulatory organization to ensure Commission access to information on an as needed basis as may be necessary to fulfill its regulatory responsibilities. The information subject to these arrangements generally would be of a type necessary in the first instance to monitor domestic markets and to protect domestic customers trading on foreign markets.

Firm-specific information that is potentially relevant to protection of domestic customers engaged in foreign transactions could include the following: (1) Registration qualification status; (2) names of principals; (3) current capital; (4) location of customer funds; (5) address of main office and branches; (6) exchange and self-regulatory organization memberships; (7) the existence of any derogatory information such as that required to be disclosed on the Commission's Form 7-R; (8) notice of limitations imposed on activities; (9) notice of undersegregation or undercapitalization; (10) notice of misuse of customer funds; and (11) notice of sanctions or of expulsion from exchange or self-regulatory organization membership. The Commission believes that much of the above information would be public in the ordinary course in most jurisdictions. From time to time, the Commission also may need immediate access to financial information concerning risks posed to domestic firms by the carrying of foreign positions.

In addition to information that relates to the financial stability and creditworthiness of the firm, the Commission should have access to transaction-specific information that confirms the execution of orders and prices and facilitates tracing of customer funds. Such data could include records reflecting: (1) That an order has been received by a firm on behalf of one or more United States customers; (2) that an order has been executed on an exchange on behalf of one or more United States customers; (3) that funds to

margin, guarantee or secure United States customer transactions have been received by a firm and deposited in an appropriate depository; and (4) the price at which a transaction was executed and general access to pricing information.

Again, such information is likely to be maintained in the ordinary course of business. Tracing of customer funds would be most essential in cases of insolvency where repatriation of funds is at issue.

The Commission may also seek relevant position data information, including the identity of the position holder and related positions, in connection with surveillance of a potential "market disruption." This is particularly true in the case of integrated markets.

The Commission wishes to emphasize that the information sharing arrangements discussed herein are not necessarily a substitute for, nor would they preclude, a more formal agreement or arrangement with respect to the sharing of information.

Marketing Activities by Firms Granted Rule 30.10 Relief

FR date and citation: November 3, 1992, 57 FR 49644; August 17, 1994, 59 FR 42158.

[52 FR 28998, Aug. 5, 1987, as amended at 59 FR 42158, Aug. 17, 1994]

APPENDIX B TO PART 30—INTERPRETATIVE STATEMENT WITH RESPECT TO THE SECURED AMOUNT REQUIREMENT SET FORTH IN § 30.7

1. Rule 30.7 requires FCMs who accept money, securities or property from foreign futures and foreign options customers to maintain in a separate account or accounts such money, securities and property in an amount at least sufficient to cover or satisfy all of its current obligations to those customers.¹ This amount is denominated as the

¹"Foreign futures or foreign options customer" means "any person located in the United States, its territories or possessions who trades in foreign futures or foreign options: Provided, That an owner or holder of a proprietary account as defined in paragraph (y) of [Rule 1.3] shall not be deemed to be a foreign futures or foreign options customer within the meaning of [Rules 30.6 and 30.7]." Rule 30.1(c). "Foreign futures" means "any contract for the purchase or sale of any commodity for future delivery made, or to be made, on or subject to the rules of any foreign board of trade." Rule 30.1(a). "Foreign option" means "any transaction or agreement which is or is held out to be of the character of, or is commonly known to the trade as, an 'option,' 'privilege,' 'indemnity,' 'bid,' 'offer,' 'put,' 'call,' 'advance guaranty,' or 'decline guaranty,' made or to be made on

"foreign futures or foreign options secured amount" and that term is defined in Rule 1.3(rr). The separate accounts must be maintained under an account name that clearly identifies the funds as belonging to foreign futures and foreign options customers at a depository that meets the requirements of Rule 30.7(c). Further, each FCM must obtain and retain in its files for the period provided in Rule 1.31 an acknowledgment from the depository that the depository was informed that such money, securities or property are held for or on behalf of foreign futures and foreign options customers and are being held in accordance with the provisions of these regulations.

2. In a series of orders issued pursuant to Rule 30.10, the Commission required that certain foreign firms exempt from registration as FCMs essentially comply with the standards of Rule 30.7.² Specifically, the Commission stated that "[the secured amount] requirement is intended to ensure that funds

or subject to the rules of any foreign board of trade." Rule 30.1(b).

²Under Rule 30.10, the Commission may exempt a foreign firm acting in the capacity of an FCM from registration under the Commodity Exchange Act ("Act") and compliance with certain Commission rules based upon the firm's compliance with comparable regulatory requirements imposed by the firm's home-country regulator or self-regulatory organization ("SRO"). Once the Commission determines that the foreign jurisdiction's regulatory structure offers comparable regulatory oversight, the Commission may issue an Order granting general relief subject to certain conditions. Firms seeking confirmation of relief (referred to herein as "Rule 30.10 firms") must make certain representations set forth in the Rule 30.10 order issued to the regulator or SRO from the firm's home country. For a list of those foreign regulators and SROs that have been issued a Rule 30.10 order, see Appendix C to Part 30. In certain cases, where a foreign regulator or SRO has requested that firms subject to its jurisdiction be granted broader relief to engage in transactions on exchanges other than in its home jurisdiction (referred to herein as "expanded relief"), the relief has been granted where the relevant authority has represented that it will monitor its firms for compliance with the terms of the order in connection with such offshore transactions. Although Rule 30.10 orders generally exempt foreign intermediaries from compliance with the secured amount requirement under Rule 30.7, firms seeking confirmation of the expanded relief must represent that, with respect to transactions entered into on behalf of U.S. customers on any non-U.S. exchange located outside their home country, they

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provided by U.S. customers for foreign futures and options transactions, whether held at a U.S. FCM under Rule 30.7(c) or a firm exempted from registration as an FCM under CFTC Rule 30.10, will receive equivalent protection at all intermediaries and exchange clearing organizations.”³ The Commission further interpreted Rule 30.7 to require each FCM and Rule 30.10 firm to take appropriate action (i.e., set aside funds in a “mirror” account) in the event that it becomes aware of facts leading it to conclude that foreign futures and foreign options customer funds are not being handled consistent with the requirements of Commission rules or relevant order for relief by any subsequent intermediary or exchange clearing organization.

3. Upon further analysis and reconsideration of this matter, the Commission has determined to revise its prior interpretation of the Rule 30.7 secured amount requirement. The Commission notes that the initial depository’s ability to identify customer funds affords foreign futures and foreign options customers a measure of protection in the event that the intermediating FCM or foreign firm becomes insolvent. Moreover, Rule 30.6(a) requires that foreign futures and foreign options customers receive a Rule 1.55 written disclosure explaining that the treatment of customer funds outside the U.S. may not afford the same level of protection offered in the U.S. These protections exist whether the intermediating firm is a U.S. FCM or a firm exempt from such registration under Rule 30.10.⁴

4. The Commission further notes, however, that, in February 1998, Rule 30.6 was amended to permit an FCM to open a commodity account for a foreign futures or foreign options customer without providing the Rule 1.55 risk disclosure statement or obtaining an acknowledgment of receipt of such statement, provided that the customer is, at the time at which the account is opened, one of several types of sophisticated customers enumerated in Rule 1.55(f) (“Rule 1.55(f) cus-

tomers”).⁵ While the amendment to Rule 30.6(a) extinguished the obligation to provide a standardized risk disclosure statement to Rule 1.55(f) customers at the time of the account opening, the Commission stated that FCMs have obligations to these customers independent of such a duty that would be material in the circumstances of a given transactions.⁶

5. After careful consideration of the issue, the Commission has determined that intermediaries should advise all customers (regardless of their level of sophistication) to consider making appropriate inquiries relating to the treatment of customer funds by depositories located outside the jurisdiction of the intermediating firm. Accordingly, the Commission has determined that an FCM, at a minimum, must provide each foreign futures or foreign option customer with a written disclosure tracking the language in either: (1) Rule 1.55(b)(7),⁷ or (2) Paragraphs 6 and 8 of Appendix A to Rule 1.55(c).⁸ Rule

will treat U.S. customer funds in a manner consistent with the provisions of Rule 30.7. For the most recent order granting expanded relief, see 64 FR 50248 (September 16, 1999) (Singapore Exchange Derivatives Trading Limited).

³64 FR 50248, 50251, n.19 (emphasis added).

⁴Although orders for expanded relief exempt foreign firms from compliance with Rule 1.55, sales practice standards and the treatment of customer funds constitute two of the specific elements examined in evaluating whether the particular foreign regulatory program provides a basis for permitting substituted compliance for purposes of exemptive relief pursuant to Rule 30.10. Appendix A to Part 30.

⁵63 FR 8566 (February 20, 1998). The list of sophisticated customers referenced in Rule 1.55(f) closely tracks, with one exception, the list of “eligible swap participants” in Rule 35.1.

⁶*Id.* at 8569.

⁷Rule 1.55(b)(7) reads as follows: Foreign futures transactions involve executing and clearing trades on a foreign exchange. This is the case even if the foreign exchange is formally “linked” to a domestic exchange whereby a trade executed on one exchange liquidates or establishes a position on the other exchange. No domestic organization regulates the activities of a foreign exchange, including the execution, delivery and clearing of transactions on such exchange, and no domestic regulator has the power to compel enforcement of the rules of the foreign exchange or the laws of the foreign country. Moreover, such laws or regulations will vary depending on the foreign country in which the transaction occurs. For these reasons, customers who trade on foreign exchanges may not be afforded certain of the protections which apply to domestic transactions, including the right to use alternative dispute resolution. In particular, funds received from customers to margin foreign futures transactions may not be provided the same protections as funds received to margin futures transactions on domestic exchanges. Before you trade, you should familiarize yourself with the foreign rules which will apply to your particular transaction.

⁸Appendix A to Rule 1.55(c) is the Generic Risk Disclosure Statement, which FCMs may use as an alternative to the Risk Disclosure Statement prescribed in Rule 1.55(b). The Commission understands that most

30.10 firms must provide each foreign futures or foreign options customer with a written disclosure tracking the language in either Rule 1.55(b)(7) or paragraphs 6 and 8 of Appendix A to Rule 1.55(c), or a comparable disclosure statement prescribed by the firm's home country regulator. The Commission further encourages all firms, whether domestic or foreign, to provide a Rule 1.55 written risk disclosure to all customers, regardless of each customer's respective level of experience. The Commission notes that, in any instance where a firm provides a Rule 1.55(f) customer with a written disclosure, it is not necessary for the firm to obtain an acknowledgment of receipt. In addition, those FCMs that already have provided customers with a disclosure tracking either Rule 1.55(b)(7) or paragraphs 6 and 8 of Appendix A to Rule 1.55(c) (or in the case of Rule 30.10 firm, a comparable disclosure statement prescribed by its home country regulatory) need not provide those same customers with an additional written disclosure.

6. For the reasons set forth above, the Commission is revising its interpretation of the secured amount requirement set forth in Rule 30.7. The Commission believes that the Rule 30.7 acknowledgment required of FCMs,

FCMs, in particular those that are most active in international markets, use the Generic Risk Disclosure Statement.

Paragraphs 6 and 8 of Appendix A to Rule 1.55(c) read as follows:

6. Deposited cash and property.

You should familiarize yourself with the protections accorded money or property you deposit for domestic and foreign transactions, particularly in the event of a firm insolvency or bankruptcy. The extent to which you may recover your money or property may be governed by specified legislation or local rules. In some jurisdictions, property which has been specifically identifiable as your own will be pro-rated in the same manner as cash for purposes of distribution in the event of a shortfall.

8. Transactions in other jurisdictions.

Transactions on markets in other jurisdictions, including markets formally linked to a domestic market, may expose you to additional risk. Such markets may be subject to regulation which may offer different or diminished investor protection. Before you trade you should enquire about any rules relevant to your particular transactions. Your local regulatory authority will be unable to compel the enforcement of the rules of the regulatory authorities or markets in other jurisdictions where your transactions have been effected. You should ask the firm with which you deal for details about the types of redress available in both your home jurisdiction and other relevant jurisdictions before you start to trade.

or other appropriate acknowledgment required by Rule 30.10 firms, only applies to the maintenance of the account or accounts containing foreign futures and foreign options customer funds by the initial depository, and not to the manner in which any subsequent depository holds or subsequently transmits those funds. If an FCM receives from the initial depository the acknowledgment described in Rule 30.7, furnishes to each foreign futures or foreign options customer a written disclosure statement tracking the language set forth in Rule 1.55(b)(7) or paragraphs 6 and 8 of Appendix A of Rule 1.55(c) and otherwise complies with the provisions of Rule 30.7, then it may include all funds maintained in the separate account or accounts in calculating its secured amount requirement. A Rule 30.10 firm must satisfy the same requirements, except that it may provide each foreign futures or foreign options customer with a comparable disclosure statement prescribed by its home regulator.

7. IF an FCM or Rule 30.10 firm fails to receive the required acknowledgment from the initial depository or provide the above written disclosure statement (and in certain circumstances, receive from customers and acknowledgment of receipt), then it must set aside funds with an acceptable depository and receive from such depository the required acknowledgment.

8. The Commission's interpretation of the Rule 30.7 secured amount requirement will apply to all regulated activities with all new and existing foreign futures and foreign options customers as of October 11, 2000. The Commission's interpretation does not alter any other requirement set forth in Rule 30.7 or any other section of Part 30.

[65 FR 60553, Oct. 11, 2000]

APPENDIX C TO PART 30—FOREIGN PETITIONERS GRANTED RELIEF FROM THE APPLICATION OF CERTAIN OF THE PART 30 RULES PURSUANT TO § 30.10

Firms designated by the Sydney Futures Exchange Limited.

FR date and citation: November 7, 1988, 53 FR 44856.

FR date and citation: April 13, 1993, 58 FR 19210.

FR date and citation: March 7, 1997, 62 FR 10447.

Firms designated by the Singapore International Monetary Exchange Limited.

FR date and citation: January 10, 1989, 54 FR 809.

FR date and citation: September 16, 1999, 64 FR 50251.

Firms designated by the Montreal Exchange.

FR date and citation: March 17, 1989, 54 FR 11182.

FR date and citation: February 27, 1997, 62 FR 8877.

Firms designated by the Toronto Futures Exchange.

FR date and citation: March 22, 1990, 55 FR 10614.

Authorized Persons as designated in Annex E to the Mutual Recognition Memorandum of Understanding

FR date and citation: June 13, 1990, 55 FR 2390; December 23, 1991, 56 FR 66345.

Firms designated by the Tokyo Grain Exchange.

FR date and citation: February 23, 1993, 58 FR 10957; May 2, 1994, 59 FR 22506.

Firms designated by the MEF S Sociedad Rectora de Productos Financieros Derivados de Renta Fija (“MEFF Renta Fija”).

FR date and citation: June 9, 1995, 60 FR 30466.

Firms designated by the New Zealand Futures and Options Exchange (“NZFOE”).

FR date and citation: December 10, 1996, 61 FR 64989.

Firms designated by the MEF S Sociedad Rectora de Productos Financieros Derivados de Renta Variable (“MEFF Renta Variable”).

FR date and citation: April 8, 1997, 62 FR 16690.

Firms designated by the Financial Services Authority (“FSA”).

FR date and citation: October 10, 2003, 68 FR 58587.

Firms designated by the Australian Stock Exchange Limited (“ASXL”).

FR date and citation: 68 FR 39006, July 1, 2003.

FR date and citation: 70 FR 75937, December 22, 2005.

[54 FR 809, Jan. 10, 1989, as amended at 54 FR 11182, Mar. 17, 1989; 54 FR 21604, 21609, 21614, and 21618, May 19, 1989; 55 FR 10614, Mar. 22, 1990; 55 FR 23909, June 13, 1990; 56 FR 14019, Apr. 5, 1991; 56 FR 66345, Dec. 23, 1991; 58 FR 10957, Feb. 23, 1993; 58 FR 19210, Apr. 13, 1993; 59 FR 22506, May 2, 1994; 60 FR 30466, June 9, 1995; 61 FR 64989, Dec. 10, 1996; 62 FR 8877, Feb. 27, 1997; 62 FR 10447-10450, Mar. 7, 1997; 62 FR 16690, Apr. 8, 1997; 64 FR 50251, Sept. 16, 1999; 68 FR 58587, Oct. 10, 2003; 70 FR 75937, Dec. 22, 2005]

APPENDIX D TO PART 30—INFORMATION THAT A FOREIGN BOARD OF TRADE SHOULD SUBMIT WHEN SEEKING NO-ACTION RELIEF TO OFFER AND SELL, TO PERSONS LOCATED IN THE UNITED STATES, A FUTURES CONTRACT ON A FOREIGN NON-NARROW-BASED SECURITY INDEX TRADED ON THAT FOREIGN BOARD OF TRADE

A. Section 2(a)(1)(C)(iv) of the Commodity Exchange Act (“Act”) generally prohibits

any person from offering or selling a futures contract based on a security index in the U.S., except as otherwise permitted under the Act, including Section 2(a)(1)(C)(ii) of the Act. By its terms, Section 2(a)(1)(C)(iv) of the Act applies to futures contracts on security indices traded on both domestic and foreign boards of trade. Section 2(a)(1)(C)(ii) of the Act sets forth three criteria to govern the trading of futures contracts on a group or index of securities on contract markets and derivatives transaction execution facilities:

- (1) The contract must provide for cash settlement;
- (2) The contract must not be readily susceptible to manipulation or to being used to manipulate any underlying security; and
- (3) The group or index of securities must not constitute a narrow-based security index.

B. While Section 2(a)(1)(C)(ii) of the Act provides that no board of trade or derivatives transaction execution facility may trade a security index futures contract unless it meets the three criteria noted above, it does not explicitly address the standards to be applied to a foreign security index futures contract traded on a foreign board of trade. The Office of General Counsel has applied those same three criteria in evaluating requests by foreign boards of trade to allow the offer and sale within the United States of their foreign security index futures contracts when those foreign boards of trade do not seek designation as a contract market or registration as a derivatives transaction execution facility to trade those products.¹

C. In the analysis of a no-action request for a foreign security index futures contract traded on a foreign board of trade, the Office of the General Counsel asks the Division of Market Oversight (Division) to evaluate the foreign security index futures contract to ensure that it complies with the three criteria of Section 2(a)(1)(C)(ii) of the Act.

D. Because security index futures contracts are cash settled, the Division also

¹With regard to the third criterion, and CFTC and SEC jointly promulgated Rule 41.13 under the Act and Rule 3a55-3 under the Securities Exchange Act of 1934 (“Exchange Act”), governing security index futures contracts traded on foreign boards of trade. These rules provide that “[w]hen a contract of sale for future delivery on a security index is traded on or subject to the rules of a foreign board of trade, such index shall not be a narrow-based security index if it would not be a narrow-based security index if a futures contract on such index were traded on a designated contract market or registered derivatives transaction execution facility.” CFTC Rule 41.13, 17 C.F.R. § 41.13; Exchange Act Rule 3a55-3, 17 C.F.R. § 240.3a55-3.

evaluates the contract to ensure that the contract terms and conditions relating to cash settlement are consistent with the Commission's Guideline No. 1 requirements for cash settled contracts. In that regard, Guideline No. 1 requires that the cash price series be reliable, acceptable, publicly available and timely; that the cash settlement price be reflective of the underlying cash market; and that the cash settlement price not be readily susceptible to manipulation. In making its determination, the Division considers the design and maintenance of the index, the method of index calculation, the nature of the component security prices used to calculate the index, the breadth and frequency of index dissemination, and any other relevant factors.

E. In considering the susceptibility of an index to manipulation, the Division examines several factors, including the structure of the primary and secondary markets for the component equities, the liquidity of the component stocks, the method of index calculation, the total capitalization of stocks underlying the index, the number, weighting and capitalization of individual stocks in the index, and the existence of surveillance sharing agreements between the board of trade and the securities exchange(s) on which the underlying securities are traded.

F. To verify that the index is not narrow based, the Division considers the number and weighting of the component securities and the value of average daily trading volume of the lowest weighted quartile of securities. Under the Act, a security index is narrow-based if it meets any one of the following criteria:

- (1) The index is composed of fewer than 10 securities;
- (2) Any single security comprises more than 30% of the total index weight
- (3) The five largest securities comprise more than 60% of the total index weight; or
- (4) The lowest-weighted securities that together account for 25% of the total weight of the index have an aggregate dollar value of average daily trading volume of less than US\$30 million (or US\$50 million if the index includes fewer than 15 securities).

G. Accordingly, a foreign board of trade seeking no-action relief to offer and to sell, to persons located in the U.S., a futures contract on a non-narrow based foreign security index traded on that foreign board of trade should submit to the Office of General Counsel the following in English:

(1) The terms and conditions of the contract and all other relevant rules of the exchange and, if applicable, of the exchange on which the underlying securities are traded, which have an effect on the over-all trading of the contract, including circuit breakers, price limits, position limits or other controls on trading;

(2) Surveillance agreements between the foreign board of trade and the exchange(s) on which the underlying securities are traded;

(3) Assurances from the foreign board of trade of its ability and willingness to share information with the Commission, either directly or indirectly;

(4) When applicable, information regarding foreign blocking statutes and their impact on the ability of United States government agencies to obtain information concerning the trading of such contracts;

(5) Information and data denoted in U.S. dollars (and the conversion date and rate used) relating to:

(i) The method of computation, availability, and timeliness of the index;

(ii) The total capitalization, number of stocks (including the number of unaffiliated issuers if different from the number of stocks), and weighting of the stocks by capitalization and, if applicable, by price in the index as well as the combined weighting of the five highest-weighted stocks in the index;

(iii) Procedures and criteria for selection of individual securities for inclusion in, or removal from, the index, how often the index is regularly reviewed, and any procedures for changes in the index between regularly scheduled reviews;

(iv) Method of calculation of the case-settlement price and the timing of its public release;

(v) Average daily volume of trading, measured by share turnover and dollar value, in each of the underlying securities for a six-month period of time and, separately, the dollar value of the average daily trading volume of the securities comprising the lowest weighted 25% of the index for the past six calendar months, calculated pursuant to Commission Rule 41.11; and

(vi) If applicable, average daily futures trading volume;

(6) A statement that the index is not a narrow-based security index as defined in Section 1a(25) of the Act and the analysis supporting that statement; and

(7) When applicable, a request to make the futures contract available for trading in accordance with the terms and conditions of, and through the electronic trading devices identified in, the Foreign Trading System No-Action letter that the foreign board of trade received from Commission staff and a certification from the foreign board of trade that it is in compliance with the terms and conditions of that no-action letter.

[68 FR 33624, June 5, 2003]