

Commodity Futures Trading Commission

§ 1.12

§ 1.11 [Reserved]

§ 1.12 Maintenance of minimum financial requirements by futures commission merchants and introducing brokers.

(a) Each person registered as a futures commission merchant or who files an application for registration as a futures commission merchant, and each person registered as an introducing broker or who files an application for registration as an introducing broker (except for an introducing broker or applicant for registration as an introducing broker operating pursuant to, or who has filed concurrently with its application for registration, a guarantee agreement and who is not also a securities broker or dealer), who knows or should have known that its adjusted net capital at any time is less than the minimum required by § 1.17 or by the capital rule of any self-regulatory organization to which such person is subject, if any, must:

(1) Give telephonic notice, to be confirmed in writing by facsimile notice, as set forth in paragraph (i) of this section that the applicant's or registrant's adjusted net capital is less than required by § 1.17 or by other capital rule, identifying the applicable capital rule. The notice must be given immediately after the applicant or registrant knows or should know that its adjusted net capital is less than required by any of the aforesaid rules to which the applicant or registrant is subject; and

(2) Provide together with such notice documentation in such form as necessary to adequately reflect the applicant's or registrant's capital condition as of any date such person's adjusted net capital is less than the minimum required. The applicant or registrant must provide similar documentation for other days as the Commission may request.

(b) Each person registered as a futures commission merchant, or who files an application for registration as a futures commission merchant, who knows or should have known that its adjusted net capital at any time is less than the greatest of:

(1) 150 percent of the minimum dollar amount required by § 1.17(a)(1)(i)(A);

(2) 110 percent of the amount required by § 1.17(a)(1)(i)(B);

(3) 150 percent of the amount of adjusted net capital required by a registered futures association of which it is a member, unless such amount has been determined by a margin-based capital computation set forth in the rules of the registered futures association, and such amount meets or exceeds the amount of adjusted net capital required under the margin-based capital computation set forth in § 1.17(a)(1)(i)(B), in which case the required percentage is 110 percent, or

(4) For securities brokers or dealers, the amount of net capital specified in Rule 17a-11(c) of the Securities and Exchange Commission (17 CFR 240.17a-11(c)), must file written notice to that effect as set forth in paragraph (i) of this section within twenty-four (24) hours of such event.

(c) If an applicant or registrant at any time fails to make or keep current the books and records required by these regulations, such applicant or registrant must, on the same day such event occurs, provide facsimile notice of such fact, specifying the books and records which have not been made or which are not current, and within forty-eight (48) hours after giving such notice file a written report stating what steps have been and are being taken to correct the situation.

(d) Whenever any applicant or registrant discovers or is notified by an independent public accountant, pursuant to § 1.16(e)(2) of this chapter, of the existence of any material inadequacy, as specified in § 1.16(d)(2) of this chapter, such applicant or registrant must give facsimile notice of such material inadequacy within twenty-four (24) hours, and within forty-eight (48) hours after giving such notice file a written report stating what steps have been and are being taken to correct the material inadequacy.

(e) Whenever any self-regulatory organization learns that a member registrant has failed to file a notice or written report as required by § 1.12, that self-regulatory organization must immediately report this failure by telephone, confirmed in writing immediately by facsimile notice, as provided in paragraph (i) of this section.

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(f)(1) Whenever a clearing organization determines that any position it carries for one of its clearing members which is registered as a futures commission merchant or as a leverage transaction merchant must be liquidated immediately, transferred immediately or that the trading of any account of such futures commission merchant or such leverage transaction merchant shall be only for the purposes of liquidation, because that clearing member has failed to meet a call for margin or to make other required deposits, the clearing organization must immediately give telephonic notice, confirmed in writing immediately by facsimile notice, of such a determination to the principal office of the Commission at Washington, DC.

(2) Whenever a registered futures commission merchant determines that any position it carries for another registered futures commission merchant or for a registered leverage transaction merchant must be liquidated immediately, transferred immediately or that the trading of any account of such futures commission merchant or leverage transaction merchant shall be only for purposes of liquidation, because the other futures commission merchant or the leverage transaction merchant has failed to meet a call for margin or to make other required deposits, the carrying futures commission merchant must immediately give telephonic notice, confirmed in writing immediately by facsimile notice, of such a determination to the principal office of the Commission at Washington, DC.

(3) Whenever a registered futures commission merchant determines that an account which it is carrying is undermargined by an amount which exceeds the futures commission merchant's adjusted net capital determined in accordance with § 1.17, the futures commission merchant must immediately give telephonic notice, confirmed in writing immediately by facsimile notice, of such a determination to the designated self-regulatory organization and the principal office of the Commission at Washington, DC. This paragraph (f)(3) shall apply to any account carried by the futures commission merchant, whether a customer, noncustomer, omnibus or proprietary

account. For purposes of this paragraph (f)(3), if any person has an interest of 10 percent or more in ownership or equity in, or guarantees, more than one account, or has guaranteed an account in addition to his own account, all such accounts shall be combined. A designated self-regulatory organization may grant an exemption from the provisions of this paragraph to a futures commission merchant with respect to any particular account on a continuous basis provided the designated self-regulatory organization documents the reasons for granting such an exemption and continues to monitor any such account.

(4) A futures commission merchant shall report immediately by telephone, confirmed immediately in writing by facsimile notice, whenever any commodity interest account it carries is subject to a margin call, or call for other deposits required by the futures commission merchant, that exceeds the futures commission merchant's excess adjusted net capital, determined in accordance with § 1.17, and such call has not been answered by the close of business on the day following the issuance of the call. This applies to all accounts carried by the futures commission merchant, whether customer, noncustomer, or omnibus, that are subject to margining, including commodity futures and options. In addition to actual margin deposits by an account owner, a futures commission merchant may also take account of favorable market moves in determining whether the margin call is required to be reported under this paragraph.

(5)(i) A futures commission merchant shall report immediately by telephone, confirmed immediately in writing by facsimile notice, whenever its excess adjusted net capital is less than six percent of the maintenance margin required by the futures commission merchant on all positions held in accounts of a noncustomer other than a noncustomer who is subject to the minimum financial requirements of:

(A) A futures commission merchant, or

(B) The Securities and Exchange Commission for a securities broker and dealer.

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(ii) For purposes of paragraph (f)(5)(i) of this section, maintenance margin shall include all deposits which the futures commission merchant requires the noncustomer to maintain in order to carry its positions at the futures commission merchant.

(g) A futures commission merchant shall provide written notice of a substantial reduction in capital as compared to that last reported in a financial report filed with the Commission pursuant to §1.10. This notice shall be provided as follows:

(1) If any event or series of events, including any withdrawal, advance, loan or loss cause, on a net basis, a reduction in net capital (or, if the futures commission merchant is qualified to use the filing option available under §1.10(h), tentative net capital as defined in the rules of the Securities and Exchange Commission) of 20 percent or more, notice must be provided within two business days of the event or series of events causing the reduction; and

(2) If equity capital of the futures commission merchant or a subsidiary or affiliate of the futures commission merchant consolidated pursuant to §1.17(f) (or 17 CFR 240.15c3-1e) would be withdrawn by action of a stockholder or a partner or a limited liability company member or by redemption or repurchase of shares of stock by any of the consolidated entities or through the payment of dividends or any similar distribution, or an unsecured advance or loan would be made to a stockholder, partner, sole proprietor, limited liability company member, employee or affiliate, such that the withdrawal, advance or loan would cause, on a net basis, a reduction in excess adjusted net capital (or, if the futures commission merchant is qualified to use the filing option available under §1.10(h), excess net capital as defined in the rules of the Securities and Exchange Commission) of 30 percent or more, notice must be provided at least two business days prior to the withdrawal, advance or loan that would cause the reduction: *Provided, however,* That the provisions of paragraphs (g)(1) and (g)(2) of this section do not apply to any futures or securities transaction in the ordinary course of business between a futures commission merchant

and any affiliate where the futures commission merchant makes payment to or on behalf of such affiliate for such transaction and then receives payment from such affiliate for such transaction within two business days from the date of the transaction.

(3) Upon receipt of such notice from a futures commission merchant, the Director of the Division of Clearing and Intermediary Oversight or the Director's designee may require that the futures commission merchant provide or cause a Material Affiliated Person (as that term is defined in §1.14(a)(2)) to provide, within three business days from the date of request or such shorter period as the Division Director or designee may specify, such other information as the Division Director or designee determines to be necessary based upon market conditions, reports provided by the futures commission merchant, or other available information.

(h) Whenever a person registered as a futures commission merchant knows or should know that the total amount of its funds on deposit in segregated accounts on behalf of customers, or that the total amount set aside on behalf of customers trading on non-United States markets, is less than the total amount of such funds required by the Act and the Commission's rules to be on deposit in segregated or secured amount accounts on behalf of such customers, the registrant must report such deficiency immediately by telephone notice, confirmed immediately in writing by facsimile notice, to the registrant's designated self-regulatory organization and the principal office of the Commission in Washington, DC, to the attention of the Director and the Chief Accountant of the Division of Clearing and Intermediary Oversight.

(i)(1) Every notice and written report required to be given or filed by this section (except for notices required by paragraph (f) of this section) by a futures commission merchant or a self-regulatory organization must be filed with the regional office of the Commission with jurisdiction over the state in which the registrant's principal place of business is located, with the principal office of the Commission in Washington, DC, with the designated self-regulatory organization, if any; and

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with the Securities and Exchange Commission, if such registrant is a securities broker or dealer. Every notice and written report required to be given or filed by this section by an applicant for registration as a futures commission merchant must be filed with the National Futures Association (on behalf of the Commission), with the designated self-regulatory organization, if any, and with the Securities and Exchange Commission, if such applicant is a securities broker or dealer. Any notice or report filed with the National Futures Association pursuant to this paragraph shall be deemed for all purposes to be filed with, and to be the official record of, the Commission.

(2) Every notice and written report which an introducing broker or applicant for registration as an introducing broker is required to give or file by paragraphs (a), (c) and (d) of this section must be filed with the National Futures Association (on behalf of the Commission), with the designated self-regulatory organization, if any, and with every futures commission merchant carrying or intending to carry customer accounts for the introducing broker or applicant for registration as an introducing broker. Any notice or report filed with the National Futures Association pursuant to this paragraph shall be deemed for all purposes to be filed with, and to be the official record of, the Commission.

(3) Every notice or report required to be provided in writing to the Commission under this section may, in lieu of facsimile, be filed via electronic transmission using a form of user authentication assigned in accordance with procedures established by or approved by the Commission, and otherwise in accordance with instructions issued by or approved by the Commission. Any such electronic submission must clearly indicate the registrant or applicant on whose behalf such filing is made and the use of such user authentication in submitting such filing will constitute and become a substitute for the manual signature of the authorized signer.

(Approved by the Office of Management and Budget under control number 3038-0024)

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EDITORIAL NOTE: For FEDERAL REGISTER citations affecting § 1.12, see the List of CFR Sections Affected, which appears in the Finding Aids sections of the printed volume and on GPO Access.

§ 1.13 [Reserved]

§ 1.14 Risk assessment recordkeeping requirements for futures commission merchants.

(a) *Requirement to maintain and preserve information.* (1) Each futures commission merchant registered with the Commission pursuant to Section 4d of the Act, unless exempt pursuant to paragraph (d) of this section, shall prepare, maintain and preserve the following information:

(i) An organizational chart which includes the futures commission merchant and each of its affiliated persons. Included in the organizational chart shall be a designation of which affiliated persons are "Material Affiliated Persons" as that term is used in paragraph (a)(2) of this section, which Material Affiliated Persons file routine financial or risk exposure reports with the Securities and Exchange Commission, a federal banking agency, an insurance commissioner or other similar official or agency of a state, or a foreign regulatory authority, and which Material Affiliated Persons are dealers in financial instruments with off-balance sheet risk and, if a Material Affiliated Person is such a dealer, whether it is also an end-user of such instruments;

(ii) Written policies, procedures, or systems concerning the futures commission merchant's:

(A) Method(s) for monitoring and controlling financial and operational risks to it resulting from the activities of any of its affiliated persons;

(B) Financing and capital adequacy, including information regarding sources of funding, together with a narrative discussion by management of the liquidity of the material assets of the futures commission merchant, the structure of debt capital, and sources of alternative funding;

(C) Establishing and maintaining internal controls with respect to market risk, credit risk, and other risks created by the futures commission merchant's proprietary and noncustomer