**Draft Sample Provisions for FCM Customer Agreements**

***JAC & CFTC Advisory Updates***

**WHEREAS**, on May 14, 2019, the Joint Audit Committee (“**JAC**”) issued Regulatory Alert #19-02 related to combining accounts for margin purposes and Regulatory Alert #19-03, related to Commodity Futures Trading Commission (the “**CFTC**”) Regulation 1.56(b) (together, the “**JAC Alerts**”);

**WHEREAS**, on July 10, 2019, the Division of Clearing and Risk (“**DCR**”) and the Division of Swap Dealer and Intermediary Oversight (“**DSIO**” and together with DCR, the “**Divisions**”) issued Letter No. 19-17 (the “**Advisory and No-Action Relief**”), which addressed margining practices and provided guidance with respect to the appropriate documentation required within customer agreements in accordance with CFTC Regulation 1.56.

**WHEREAS**, the Directors of DSIO and DCR issued a joint statement (the “**Joint Statement**”) on September 13, 2019 stating their expectation that market participants would comply with CFTC Regulation 1.56, as interpreted in Letter No. 19-17, no later than September 15, 2020;

**WHEREAS**, the Parties acknowledge that the Advisory and No-Action Relief, Joint Statement or JAC Alerts do not prescribe any specific language that must be included in any customer agreement.

**NOW, THEREFORE**, the Parties acknowledge and agree as follows:

1. **Definitions**. Capitalized terms used, but not defined herein, shall have the meaning ascribed to such terms in the Customer Agreement.

**Account** means [“Account” as defined in the Customer Agreement].

**Beneficial Owner** means the individual or entity that is the legal owner of the Account.

**Collateral** means [“Collateral” as defined in the Customer Agreement].

**Customer** means the Beneficial Owner of the Account.

**Customer Agreement** means [the Customer Agreement for the Account dated [DATE] between Customer and FCM].[[1]](#footnote-2)

**Event of Default** means [“Event of Default” as defined in the Customer Agreement].[[2]](#footnote-3)

**Defaulted Account** means a different cleared commodity interest account of the Customer other than the Account for which the FCM has declared an Event of Default and a shortfall remains for the account.

**FCM** means [the Customer’s futures commission merchant as defined in the Customer Agreement].

**Manager** means [“Manager” or “Adviser” as defined in the Customer Agreement].

**Other Excess Collateral** means excess collateral on deposit with FCM from other accounts of the same Customer (including accounts of Customer managed by a different manager).

1. Each Party hereby represents and warrants that it has the full power and authority (i) to enter into and deliver this Agreement; (ii) to perform its obligations under this Agreement (including, but not limited to, the transfer of required margin); and (iii) has taken all necessary action to authorize such execution, delivery and performance.
2. The Parties hereby agree that, notwithstanding anything to the contrary in the Customer Agreement, any provision of the Customer Agreement that purports to: (i) preclude FCM from calling Customer for required margin; (ii) in the event Customer fails to meet the margin call, preclude FCM from initiating a legal proceeding against Customer to recover any shortfall; or (iii) otherwise guarantee Customer against, or limit Customer’s loss, including, for the avoidance of doubt, any provision that purports to limit FCM’s recourse to less than all assets of Customer, is hereby removed and of no force and effect. The Parties further agree that nothing in CFTC Regulation 1.56 nor in this Section 3 prohibits the Customer Agreement from confirming that: (i) Manager shall not be personally responsible for any shortfall or other deficiency in the Account; (ii) any other customer of the Manager shall not be personally responsible for any shortfall in the Account; (iii) any third party (*e.g.*, a trustee) shall not be personally responsible for any shortfall in the Account, unless so provided in the Customer Agreement; and (iv) FCM may not apply assets held in accounts of customers of the Manager, other than the Customer, to meet any shortfall in the Account. Such latter provisions shall remain in full force and effect.
3. The Parties acknowledge and agree that, subject to the provisions herein and notwithstanding anything in the Customer Agreement (or any other agreement between FCM and Manager, acting by or on behalf of Customer that is incorporated with the Customer Agreement), in order to address any shortfall or in the Account, FCM is permitted to: (i) satisfy any amounts owed by Customer to FCM by looking to other amounts deposited by or on behalf of Customer with FCM relating to the Account or other accounts of the same Customer, in accordance with the agreements governing such accounts; and (ii) contact Customer directly for additional funds.
4. If FCM determines that the Account is operating outside the Ordinary Course of Business (as defined in the Advisory and No-Action Relief) and has not declared an Event of Default:
   1. FCM shall provide prompt notice to Manager, Customer (to the extent Customer maintains a self-directed account with FCM) and each of Customer’s other managers that have clearing accounts at FCM that Customer has an account that is operating outside the Ordinary Course of Business and, therefore, FCM is required to restrict withdrawals of excess funds from other accounts of Customer as required by CFTC Regulation 39.13(g)(8)(iii) and the Advisory and No-Action Relief.
   2. FCM shall, in its sole, reasonable discretion, and in accordance with its risk management policies, use any of the following non-exhaustive list of procedures to attempt to cure such shortfall:
      1. Obtain additional Collateral to satisfy all margin obligations in the Account on behalf of the Customer or from the Customer directly, provided, however, that the FCM has consulted with the Manager;
      2. Transfer Other Excess Collateral from other accounts of Customer managed by Manager at FCM, provided, however, that the FCM has consulted with the Manager;
      3. Agree to offset any long and short positions in the same contract and expiration month (or any other paired positions that can be offset and/or compressed under the rules of the relevant clearing house) that are carried in the Account;
      4. At the instruction of Manager and with the consent of the other FCM, transfer some or all of the Customer’s positions to another FCM that would result in a lower margin requirement in the Account (it being understood that FCM will not transfer any margin to the other FCM to support such transferred positions until all such obligations to FCM have been met or would be met as a result of such transfer); and/or
      5. At the instruction of Manager, liquidate some or all of the positions in the Account that would result in a lower margin requirement for the Account.
   3. For avoidance of doubt, FCM’s election to use any or all of the procedures described in subsection 5(b) above shall not constitute a waiver of, or condition upon, FCM’s ability to declare an Event of Default in accordance with the Customer Agreement or any other agreement between Customer and FCM.
5. Upon the declaration of an Event of Default that arises from Customer’s failure to make a payment or margin call when due (after giving effect to any applicable grace period):
   1. FCM may, without limitation and in each case in accordance with applicable provisions of the Customer Agreement: (i) close out, liquidate or value all positions in the Account; (ii) exercise all netting rights with respect to assets in the Account; and (iii) apply any Collateral remaining in the Account to cover any shortfall.
   2. If a shortfall remains in the Account after applying all Collateral in the Account, FCM shall provide prompt notice to Manager and Customer specifying the amount of the shortfall and requesting Manager and Customer to transfer promptly to FCM cash or other eligible collateral sufficient to cover such shortfall amount.
   3. FCM, in its sole, reasonable discretion, and subject at all times to its risk management policies, may apply Other Excess Collateral from other accounts of Customer to cure the shortfall in the following order:
      1. FCM may initially apply Other Excess Collateral from accounts maintained by the Customer directly with FCM (*i.e.*, to the extent Customer maintains a self-directed account with FCM and such account is not directed by an asset manager or other third party) to cure the shortfall, as directed by Customer or, if Customer does not provide direction, on a pro rata basis, as reasonably determined by FCM, across such accounts;
      2. In the event a shortfall continues to exist after applying all Other Excess Collateral from accounts maintained by Customer directly with FCM, FCM may apply Other Excess Collateral from accounts of Customer managed by Manager, as directed by Customer or, if Customer does not provide direction, on a pro rata basis, as reasonably determined by FCM, across such accounts; and
      3. In the event a shortfall continues to exist after applying all Other Excess Collateral from accounts of Customer managed by Manager, FCM may apply Other Excess Collateral from accounts of Customer managed by other managers, as directed by Customer or, if Customer does not provide direction, on a pro rata basis, as reasonably determined by FCM, across such accounts.
   4. FCM shall promptly provide to Customer a statement reasonably detailing the scope of its activities, including information sufficient to identify the purpose of a debit.
   5. FCM shall promptly provide to the Manager adequate information detailing the withdrawal from the Account managed by the Manager, including information sufficient to identify the purpose of a debit.
6. In the event FCM has declared an Event of Default with respect to a Defaulted Account and a shortfall remains for that account after applying all the collateral in such Defaulted Account and all excess collateral in Customer’s accounts held directly with FCM (*i.e.*, to the extent Customer maintains a self-directed account with FCM), FCM will provide written notice to Manager and Customer that such event of default has occurred and, to the extent required by CFTC Regulation 1.56(b), may, notwithstanding anything in the Customer Agreement to the contrary, apply excess collateral from this Account and any other account of Customer to cure the shortfall for the Defaulted Account as directed by Customer or, if Customer does not provide direction,[[3]](#footnote-4) as follows:
   1. If the Defaulted Account was managed by Manager, then excess Collateral from this Account may be applied to the remaining shortfall of the Defaulted Account on a pro rata basis, as reasonably determined by FCM, with excess collateral from other accounts of Customer managed by Manager.
   2. If the Defaulted Account was not managed by Manager and FCM has applied all Other Excess Collateral from accounts managed by the manager of the Defaulted Account, then excess Collateral from this Account may be applied to the remaining shortfall of the Defaulted Account on a pro rata basis, as reasonably determined by FCM, with excess collateral from other accounts of Customer.
7. Unless expressly stated herein, nothing in this Agreement shall supersede any provision or term agreed to by the Parties in their existing Customer Agreement or as otherwise bilaterally agreed to between the Parties.
8. Nothing in this Agreement, including Sections 6 and 7 herein, shall preclude FCM from initiating a legal proceeding against Customer to recover any shortfall in the Account in accordance with the Customer Agreement.

1. The term “Customer Agreement” is intended to coincide with the existing suite of documents that are tied to the Account. For example, the Customer Agreement may reference a prime brokerage agreement that is used to satisfy collateral requirements related to the Customer Agreement. [↑](#footnote-ref-2)
2. Market participants should review existing agreements to confirm “Event of Default” is the correct term. [↑](#footnote-ref-3)
3. The intent of this provision is to provide written notice so there are not undocumented movements of money between accounts. [↑](#footnote-ref-4)