

# Cleared OTC Derivatives Customer Sequestered Regulatory Class

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# The Rules and The Regulations

**Lisa Dunsky**  
**Director and Associate General Counsel**

# CFTC Part 190 Bankruptcy Regulations: Revised Definition of “Account Class”

“... means each of the following types of customer accounts which must be recognized as a separate class of account by the trustee: futures accounts, foreign futures accounts, leverage accounts, commodity option accounts and delivery accounts..., and, only with respect to the bankruptcy of a commodity broker that is a [FCM], cleared OTC derivatives accounts....”

- *Proviso*: Cleared OTC derivatives in customer segregated account pursuant to a CFTC 4d Order “shall be treated, for purposes of [Part 190], as being held in an account of the futures account class.”

# Part 190 Definition of “Cleared OTC Derivatives”

*“... positions in commodity contracts that have not been entered into or traded on a contract market...or on a derivatives transaction execution facility..., but which nevertheless are submitted through a commodity broker that is a [FCM]...for clearing by a [DCO]..., along with the money, securities, and/or other property margining, guaranteeing, or securing such positions, which are required to be segregated or set aside, in accordance with a rule, regulation, or order issued by the [CFTC], or which are required to be held in a separate account for cleared OTC derivatives only, in accordance with the rules or bylaws of a [DCO]....”*

# DCO Role in Pre-Bankruptcy, Substantive Rules for OTC Account Class

As stated in the Adopting Release for CFTC's revised Part 190 Regulations, until CFTC adopts regulations for the OTC account class:

*“... a position in an OTC derivative (and relevant collateral) that a customer clears through an FCM with a DCO, which position (and relevant collateral) is not subject to a Section 4d Order, would be considered part of the cleared OTC derivative account class, as soon as, but only after, a DCO rule...that requires such positions (and relevant collateral) to be held in a separate account for cleared OTC derivatives becomes effective....”*

# CME Rules for the OTC Account Class ...

- To date, for cleared OTC derivatives not subject to a 4d Order, CME has utilized CFTC Regulation 30.7 (or “secured”) accounts.
- In early October, CME plans to implement new rules with substantive requirements for the treatment of customer “cleared OTC derivatives” that are cleared by CME.
- When CME’s rules become effective, customer cleared OTC derivative positions and related collateral currently held in CME’s 30.7 “secured” account will be transferred to the new customer OTC account.

## ... Will Mirror CFTC Regulations....

- CME rules for OTC account class essentially mirror CFTC Regulations for 4d/customer segregated accounts (17 C.F.R. §§ 1.20, *et seq*).
- CME rules will be in Chapter 8F (Over-the-Counter Derivative Clearing) of the CME rule book.
- CME rule numbers will track the related CFTC Regulations (*e.g.*, CME Rule 8F120 addresses the same issues as CFTC Reg 1.20).

## ... With A Few Differences

- Rather than using “segregated” or “secured”, CME rules will refer to new customer account origin as the Cleared OTC Derivatives *Sequestered* Account.
- CME rules won't include analog to CFTC Reg. 1.49, and CME Rule 8F132 won't require FCMs to compute “on a currency-by-currency basis” the amount of funds required to be in Cleared OTC Derivatives *Sequestered* Accounts.
- CME rules will require any clearing member carrying a customer omnibus account containing cleared OTC derivatives in the name of a non-clearing FCM to have a written agreement that requires non-clearing FCM to comply with CME rules relating to Cleared OTC Derivatives Customer *Sequestered* Accounts.

# Cleared OTC Derivatives Operational Impact

**Ed Gogol**  
**Managing Director Clearing IT Solutions**

# Cleared OTC Derivatives Operational Impact

## It's a new regulatory class

Today you have three regulatory classes:

- Customer Seg
- 30.7 Customer Secured
- Non-Seg (House)

Tomorrow you have **four** regulatory classes:

- Customer Seg
- Cleared OTC Customer Sequestered
- 30.7 Customer Secured (will be no longer used for CME)
- Non-Seg (House)

# Operational Impact Continued...

- (Almost) no change to how bookkeeping system interfaces with the clearing system
- On the trade, exactly as before, there are exactly two origin codes – customer or house.
- Slight change to the convention for assigning the clearing position account ID:
  - Use an appended “T” (for cleared oTc)
  - Instead of appended “S” (for secured)

For example, **123T CUST** instead of **123S CUST**  
You'll see this on the Trade Register file and report

- The Funds Segregation Type (used to characterize the Settlement Account) will change:
  - Will be COTC for Cleared OTC Derivatives Customer Sequestered
  - Instead of CNSEG used for 30.7 Secured

For example, settlement acct **123T COTC** instead of **123S CNSEG**  
You'll see this on Settlement and Banking reports

# What's Affected, and When

- Basically, applies to customer positions in anything CME-cleared that is today 30.7 Secured:
  - CME-cleared CDS contracts
  - NYMEX wet freight forwards
  - COMEX OTC London gold forwards
  - CME and CBOT Excess Return forwards and swaps
  - Eris interest-rate swap futures

And soon: CME-cleared interest-rate swap contracts

Goes live: Monday, October 4, 2010

- We'll change the clearing account ID's automatically over the weekend !!!  
(no impact to firms)

Start testing in New Release: Now

# Financial Reporting

Sequestration Requirement Statements/Computations

Sequestration Acknowledgement Letters

**Anne Bagan**

**Managing Director Audits**

# Banking Impact

**Mike Kobida**  
**Director Financial Management Clearing House**

# Cleared OTC Derivatives

For more information...

- Clearing Advisory Notice 10-256
- Audit Information Bulletin 10-07

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