

**Financial Crimes Enforcement Network
Commodity Futures Trading Commission**

Guidance

FIN-2007-G001

Issued: April 20, 2007

**Subject: Application of the Customer Identification Program Rule to Futures
Commission Merchants Operating as Executing and Clearing Brokers in
Give-Up Arrangements**

Q. It is an established practice in the futures industry that futures commission merchants engage in transactions through give-up arrangements, whereby a futures commission merchant, acting as an executing broker,¹ executes an order on an exchange for a commodity customer,² or an option customer,³ which in accordance with applicable exchange rules is then given-up to a clearing broker. Pursuant to a give-up arrangement, which may be formalized by a written agreement,⁴ an executing broker will execute a trade on order of the commodity customer or option customer and then direct it to the account that the customer has established with its clearing broker. The trade thereafter is subject to acceptance by the clearing broker.⁵ For the purposes of the rule requiring a futures commission merchant to implement a customer identification program,⁶ is an

¹ An executing broker in a give-up arrangement may be a futures commission merchant or a floor broker.

² See 17 C.F.R. § 1.3(k) and compare 31 C.F.R. §§ 103.123(a)(1)(i) and (a)(5)(i). The Commodity Futures Trading Commission's Regulation 1.3(k) defines the term "commodity customer" as "a customer trading in any commodity." This definition includes a wide array of persons that may trade commodity futures, including those that enter into a give-up arrangement with a futures commission merchant or floor broker who will execute trades, and a futures commission merchant who will submit trades for clearing, pursuant to the give-up arrangement. The term is not limited to circumstances in which the "commodity customer" establishes a "formal relationship with a futures commission merchant," and is therefore a "customer" for purposes of the customer identification program rule.

³ As used herein, the term "option customer" is defined in 17 C.F.R. § 1.3(jj), and it refers to a customer trading options. The term is not limited to circumstances in which the "option customer" establishes a "formal relationship with a futures commission merchant," and is therefore a "customer" for the purposes of the customer identification program rule.

⁴ The commodity or option customer, the executing broker and the clearing broker may enter into a written agreement specifying their rights and responsibilities with respect to the give-up arrangement, but there is no regulatory obligation to do so. See International Uniform Brokerage Execution Services ("Give-Up") Agreement, available at <http://www.futuresindustry.org/downloads/regulatory/intlgu1.pdf>. An advisor to the commodity or option customer also may be party to the agreement.

⁵ According to the provisions of the uniform give-up agreement, if a trade is not accepted by the clearing broker, the executing broker – if it is a futures commission merchant – then may enter into an agreement with the commodity or option customer for the purpose of clearing the executed trade. The trade also may be directed to an account at another clearing broker, or the trade may be liquidated.

⁶ See 31 C.F.R. § 103.123(b). The customer identification program rule applies to futures commission merchants registered, or required to be registered, with the Commodity Futures Trading Commission under the Commodity Exchange Act (except persons who register pursuant to Section 4f(a)(2) of the Act, 7 U.S.C. § 6f(a)(2)).

account established with a futures commission merchant when it operates solely as a commodity or option customer's executing broker pursuant to a give-up arrangement?

A. No. The customer identification program rule for futures commission merchants applies when a futures commission merchant opens a new account for a customer.⁷ The term "account" is defined for the purposes of the rule as a formal relationship with a futures commission merchant including, but not limited to, those established to effect transactions in commodity futures or options.⁸ Although an executing broker in a give-up arrangement will facilitate trades for a commodity or option customer, and the give-up arrangement may be governed by a written agreement, the clearing broker, but not the executing broker, will establish a formal relationship with the commodity or option customer for the purposes of the customer identification program rule.

In a give-up arrangement, the executing broker merely enters into an agreement with a commodity or option customer to execute certain orders given up for a fee. Unlike a clearing broker, the executing broker does not: (a) accept money, securities, or other property from the commodity or option customer for the purpose of margining, guaranteeing, or securing trades until they are offset or settled; (b) enter into an agreement with the commodity or option customer that establishes the parties' respective rights and obligations with respect to the acceptance of money, securities, or other property from the commodity or option customer for the purpose of margining, guaranteeing, or securing the customer's trades;⁹ (c) maintain records of, and have the ability to monitor on a daily basis, all of the commodity or option customer's transactions that are cleared by the clearing broker; and (d) issue confirmations and monthly statements.¹⁰ Moreover, according to the provisions of a give-up arrangement, a trade executed by a commodity or option customer through an executing broker is not effected until it is accepted by a clearing broker.¹¹ Thus, in a give-up arrangement, the executing broker, unlike the clearing broker, does not establish a formal relationship with the commodity or option customer.¹²

Although a futures commission merchant's customer identification program will not apply when it is operating solely as an executing broker in a give-up arrangement, the futures commission merchant's anti-money laundering program should contain risk-based

⁷ See 31 C.F.R. § 103.123(a)(5)(i) (defining "customer" for the purposes of the customer identification program rule as "a person that opens a new account with a futures commission merchant").

⁸ 31 C.F.R. § 103.123(a)(1)(i).

⁹ Pursuant to this agreement, the clearing broker will establish a "futures account" as that term is defined at 17 C.F.R. § 1.3(vv), for the commodity or option customer.

¹⁰ When executing trades for a commodity or option customer as an executing broker in a give-up arrangement, a futures commission merchant operates similarly to a floor broker, whose role is limited to providing order execution services for particular transactions.

¹¹ See *supra* note 5.

¹² In the event that an executing broker – if it is a futures commission merchant – establishes a futures account for a commodity or option customer whose trade was not accepted by its clearing broker, the executing broker then will become subject to the provisions of the customer identification program rule.

policies, procedures, and controls for assessing the money laundering risk posed by its operations, including its execution brokerage activities; for monitoring and mitigating that risk; and for detecting and reporting suspicious activity.