

To:	Adherents to the ISDA Derivatives/FX PB Business Conduct Allocation Protocol
From:	Foreign Exchange Committee and Financial Markets Lawyers Group ¹
Date:	September 30, 2013
Re:	Best Practices for Designation of Covered PB Counterparties

In the interest of facilitating the provision and updating of information by Prime Brokers (“PBs”) to Executing Dealers (“EDs”) pursuant to paragraphs (b)(3) and (b)(8) of the Annex to the ISDA Derivatives/FX Prime Brokerage Business Conduct Allocation Protocol (the “PB Protocol”) under consistent operational practices, the Foreign Exchange Committee (the “FXC”) and the Financial Markets Lawyers Group (the “FMLG”) recommend that PBs and EDs take into consideration the attached Best Practices for Designation of Covered PB Counterparties as a market practice (the “Market Practice”).

¹ This Market Practice is being issued by the FXC and FMLG to facilitate implementation of the PB Protocol. While the FXC and FMLG are sponsored by the Federal Reserve Bank of New York, this Market Practice is not endorsed by and does not necessarily reflect the views of the Federal Reserve Bank of New York or the Federal Reserve System. This Market Practice, including the Annexes, does not purport to be legal advice with respect to a particular transaction or situation, nor does it prevent PB Protocol adhering parties from adopting other practices or using other forms of agreement. If legal advice or other expert assistance is required, the services of a qualified professional should be obtained.

Best Practices for Designation of Covered PB Counterparties²

The ISDA Derivatives/FX Prime Brokerage Business Conduct Allocation Protocol (“**ISDA PB Protocol**”) allows Adhering Parties that are CFTC-registered swap dealers to agree upon an allocation of responsibilities for compliance with certain CFTC External Business Conduct Standards, as contemplated in CFTC Letter No. 13-11 and as set forth in the Annex to the ISDA PB Protocol. This contractual allocation applies to “Covered PB counterparties”. Paragraph (b)(3) of the Annex governs additional or changed designations of Covered PB counterparties:

“... The prime broker may designate additional PB counterparties as Covered PB counterparties, or change the designation of any Covered PB counterparty, in subsequent notices to the executing dealer, with such designation or change to take effect following a notice period to be negotiated in good faith by the prime broker and the executing dealer. [emphasis added]”

This best practice note discusses possible methods a prime broker (“PB”) and an executing dealer (“ED”) may choose to adopt to manage the ongoing process of additions, removals and changed information with respect to Covered PB counterparties. This note discusses the forms of notices that may be used to effect such changes, the time period for effectiveness of notices, and considerations that the PB and ED should bear in mind in order to facilitate performance of allocated external business conduct obligations. This note includes as Annex B a form of agreement that a PB and ED may choose to enter into in order to agree that notices shall be deemed effective after a period of 48 Weekday Hours. Terms used in this best practice note that are defined in the Annex have the same meanings.

Form of Notices

Option 1: Consolidated Designation Notice – “**EBCS Information**” (i.e., status as a Covered PB counterparty, consents regarding oral and standard disclosure and pre-trade mid waiver) is integrated into the Designation Notice (“**DN**”), together with conventional DN information (i.e., product scope and limits) (“**DN Information**”). The PB notifies the ED of amendments to the EBCS Information by delivery of an amended & restated DN. Existing practices for amendments that change only DN Information are not affected by this best practice note. Designation of a PB counterparty as a Covered PB counterparty is made by including in the DN a section in the form of the “**USP Rider**” attached hereto as Annex A.

Option 2: Separate Notices – EBCS Information relating to a PB counterparty is set out in a notice (“**EBCS Notice**”) in the form of the USP Rider, a separate document from the DN. This EBCS Notice may be delivered concurrently with a DN or separately. An EBCS Notice should generally relate to a single PB counterparty or class of related PB counterparties (such as those to whom an investment advisor may allocate transactions).

Under either option, the PB may choose to adopt the practice of delivering amended & restated versions of the appropriate notice in order to allow the ED to have a consolidated view of the DN and EBCS terms applicable to the particular named entity without the need to search, and check the consistency of, multiple notices.

² This best practice note was developed by the Foreign Exchange Committee (FXC) and the Financial Markets Lawyers Group (FMLG). While the FXC and FMLG are sponsored by the Federal Reserve Bank of New York, this note is not endorsed by and does not necessarily reflect the views of the Federal Reserve Bank of New York or the Federal Reserve System. Furthermore, this note does not purport to be legal advice with respect to a particular transaction or situation, nor does it prevent ISDA PB Protocol adhering parties from adopting other practices. If legal advice or other expert assistance is required, the services of a qualified professional should be obtained.

Timing of Notice Effectiveness as to EBCS Information

Existing terms of the Master Give-up Agreement (“MGUA”) will continue to govern the effectiveness of changes to DN Information (e.g., a change to an NOP limit). For changes to EBCS Information, parties may consider the following alternatives.

- The PB and ED may choose to agree in writing (which agreement may be in the form attached as Annex B hereto) that notices, whether delivered in accordance with Option 1 or Option 2, that designate a new in-scope Covered PB counterparty or a previously out-of-scope PB counterparty as a Covered PB counterparty or that modify the information regarding consents (e.g., pre-trade mid waivers) or other matters set out in paragraph (b)(8) of the Annex with respect to a Covered PB counterparty take effect 48 Weekday Hours³ after receipt by the ED.⁴ However, as provided in Annex B, if the ED believes in good faith that the EBCS Information in a notice is erroneous, it may notify the PB of its belief, and the changed EBCS Information in the notice from the PB will not take effect until the PB and ED have resolved the discrepancy in their EBCS Information regarding the PB counterparty. A PB and ED that have entered into an agreement in the form of Annex B are not precluded by these best practices from mutually agreeing to a shorter period for notice effectiveness in particular cases.
- The PB may choose to adopt a practice permitting a longer period for implementation or requiring ED countersignature of notices prior to effectiveness. If ED countersignature is required, the parties should make clear their understanding regarding whether the EBCS duties of the ED commence on delivery by the ED of the countersigned notice or at some other time.
- The PB should consider the appropriate periods for effectiveness of changes in its arrangements with PB counterparties and, to the extent those changes make necessary or affect EBCS duties of the ED, synchronize them with the time period for effectiveness of notices to the ED that change related EBCS information.⁵ Some illustrations are provided in the examples below.
- If the ED determines that it will not be prepared to comply with the obligations allocated to it under the ISDA PB Protocol with respect to a Covered PB counterparty identified in any USP Rider or EBCS Notice by the end of the 48 Weekday Hour period (or other agreed period), the ED must discontinue trading with such Covered PB counterparty (or, in the event that the PB has notified the ED that the USP Rider or EBCS Notice is triggered by the type of product being traded (e.g., non-spot), the ED must discontinue trading such product) until it is able to comply.
- After receipt of a notice that removes a Covered PB counterparty from EBCS scope, the ED may implement an operational “turn off” of EBCS on a timeline of its choosing

Examples

The discussion of effectiveness periods in the examples below assumes that the PB and ED have entered into an agreement in the form of Annex B.

³ For this purpose, “Weekday Hour” means an hour during a Business Day in the specified location. References to a period comprising a stated number of Weekday Hours are to that number of consecutive Weekday Hours. “Business Day” means the twenty-four hour calendar day on any day on which commercial banks in New York are open for general business (including dealings in foreign exchange and foreign currency deposits).

⁴ If this option is used, the PB should consider adding a sentence to the appropriate notice to the following effect: “As we have previously agreed, this notice [(as it relates to “EBCS Information”)] is deemed effective 48 Weekday Hours after receipt by you (the “*EBCS Effective Time*”), unless you notify us within that time period of your good faith belief that information in this notice is erroneous in accordance with the terms of our agreement.”

⁵ Note that the relief under CFTC Letter No. 13-11 applies once the ED has accepted the allocated duties. See also condition (c) of the no-action letter regarding notice to counterparties of the duties that have been allocated.

(1) New DN: ED receives DN for a person that was not previously a PB counterparty

EBCS obligations do not take effect unless the ED has received a USP Rider in accordance with option 1 or option 2. If the DN is countersigned by the ED, parties should be alert to the possibility of inconsistencies with other agreements if the DN contains statements regarding its effectiveness with respect to EBCS Information.

(2) Changes to EBCS Information for an existing PB counterparty

(a) Product expansion results in EBCS being required. For example, a U.S. person (“USP”) PB client that was trading spot only requests expansion of the product offering to include forwards, options and NDFs. The ED may not have been performing any EBCS obligations because spot FX is out of scope.

- If a USP Rider has been sent by the PB under Option 1 or Option 2, EBCS obligations take effect upon lapse of notice period or, if a discrepancy in EBCS Information is identified by the ED before the notice period expires, upon resolution of the discrepancy. PB’s arrangements with the PB counterparty regarding commencement of trading for the product additions should take into account this notice period.

(b) No product expansion, but addition of a U.S. person as an underlying account, resulting in EBCS being required. For example, a non-US PB has an existing Advisor as customer and named in a DN. Under the existing DN on day 1, Advisor does not have any USP accounts. On day 10, Advisor requests that PB onboard an account that is a USP (in other words, a USP account is a potential recipient of an allocation).

- If a USP Rider has been sent by the PB under Option 1 or Option 2, EBCS obligations take effect upon lapse of notice period or, if a discrepancy in EBCS Information is identified by the ED before the notice period expires, upon resolution of the discrepancy. PB’s arrangements with Advisor regarding the commencement date for allocation to the USP account should take into account this notice period.

(c) Change in EBCS Information for reasons that do not require mutual agreement of PB and PB counterparty. For example, a Covered PB counterparty informs PB that it is revoking consent to non-disclosure of the pre-trade mid market mark for BIS 31 currencies. In this case, the ED would have already accepted EBCS obligations. Another example is a non-USP PB counterparty becoming a USP due to a change of circumstances (e.g., an investment fund becomes majority-owned by USPs). In this case, unless the PB has been informed of the change prospectively with enough time for it to deliver notice to the ED and for the notice to take effect, and the PB has done so, the allocation of EBCS duties to the ED will not have taken effect.

(d) Amendments unrelated to EBCS. An example is a change to an NOP limit, currencies or tenors. This amendment to DN information takes effect according to existing MGUA terms.

(e) Product reduction or account removal results in EBCS no longer being required. A PB client that was previously identified as in scope for EBCS may become out-of-scope if the underlying products are changed to spot only or Advisor no longer has a potential allocation to a USP account.

- **if** the PB makes determination that EBCS are no longer required, **then** the PB sends the ED an amended & restated DN and (if Option 2 applies) EBCS Notice. If the previous DN included the USP Rider (Option 1), the PB, as a facilitating practice, may choose to include a blackline showing deletion of the USP rider. If no blackline was so included under Option 1, or a separate EBCS Notice was used to designate the Covered PB counterparty (Option 2), the amended & restated DN or the new EBCS Notice should state the reason for the removal of the Covered PB counterparty designation (e.g., reduction of product scope to spot only).

- Notice, as it relates to product changes, takes effect according to existing MGUA terms.
- The ED implements an operational “turn off” of EBCS on timeline of its choosing

USP Rider

Reference is made to the [(i) Master Give-Up Agreement between you and us (as such may be amended from time to time) in which [Prime Broker] (“**PB**”) acts as the prime broker and [Executing Dealer] (“**ED**”) acts as the executing dealer, and (ii)] ISDA Derivatives/FX Prime Brokerage Business Conduct Allocation Protocol (“**ISDA PB Protocol**”) to which both PB and ED are “Adhering Parties” (as defined in the ISDA PB Protocol). In accordance with paragraphs (b)(3) and (b)(8) of the Annex to the ISDA PB Protocol (the “**Annex**”), we hereby notify you that:

(Check applicable boxes)

we designate the PB counterparty or class of PB counterparties specified below as Covered PB counterparties and, with respect to each such counterparty or class, the relevant information for purposes of paragraph (b)(8) of the Annex is as follows:

with respect to the PB counterparty or class of PB counterparties specified below, the relevant information for purposes of paragraph (b)(8) of the Annex is hereby amended as follows:

Covered PB counterparty/ Class of Covered PB counterparties	Agreed in writing to (x) oral disclosure of pre-trade mid and basic METs and (y) disclosure for multiple swaps as described in CFTC Rule 23.402(f)? ⁷	Agreed in writing to non-disclosure of pre-trade mid in accordance with relief provided in the following CFTC Letters? ⁸		
		No. 12-42	No. 12-58	Additional relief
[E.g. - name of investment manager]	[Yes][No]	[Yes][No]	[Yes][No]	[Yes][No]

the designation of the following PB counterparty or class of PB counterparties as Covered PB counterparties is hereby withdrawn:

Covered PB counterparty/Class of Covered PB counterparties	Reason for removal of designation as a Covered PB counterparty or class of Covered PB counterparties.

⁶ This form was developed by the Foreign Exchange Committee (FXC) and the Financial Markets Lawyers Group (FMLG). While the FXC and FMLG are sponsored by the Federal Reserve Bank of New York, this form is not endorsed by and does not necessarily reflect the views of the Federal Reserve Bank of New York or the Federal Reserve System. Furthermore, this form does not purport to be legal advice with respect to a particular transaction or situation, nor does it prevent ISDA PB Protocol adhering parties from using other forms. If legal advice or other expert assistance is required, the services of a qualified professional should be obtained.

⁷ See paragraph (b)(8)(a) of the Annex. See Section 2.12 of ISDA August 2012 DF Supplement.

⁸ See paragraph (b)(8)(b) of the Annex and Section 2(a)-(c) of Addendum II to ISDA August 2012 DF Protocol Questionnaire. The column “Additional Relief” is intended to indicate an affirmative response to Section 2(c) of Addendum II.

[E.g. - name of investment manager]	
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Please feel free to contact [_____] if you have any questions or comments.⁹

Sincerely,

[Prime Broker]

⁹ As a facilitating practice, PBs may consider furnishing the following optional information to EDs (subject to any confidentiality restrictions that may apply), either in this notice or in a subsequent communication: CICI, LEI or fund identifiers for Covered PB counterparties; a contact email address for notifications to a Covered PB counterparty or class thereof.

Annex B
Form of Agreement as to EBCS Information
Changes¹⁰

Reference is made to (i) the ISDA Derivatives/FX Prime Brokerage Business Conduct Allocation Protocol (“**ISDA PB Protocol**”), to which each of us is an “Adhering Party” (as defined in the ISDA PB Protocol) and (ii) each “Covered Give-Up Agreement” (as defined in the ISDA PB Protocol) pursuant to which [Prime Broker] (“**PB**”) acts as the prime broker and [Executing Dealer] (“**ED**”) acts as the executing dealer.

We hereby agree that any notice pursuant to paragraph (b)(3) of the Annex to the ISDA PB Protocol (the “**Annex**”) that designates a PB counterparty as a Covered PB counterparty (as defined in the Annex) or any notice of changes to information that PB has previously provided pursuant to paragraph (b)(8) of the Annex with respect to a Covered PB counterparty shall be delivered to ED in the manner specified below and, unless otherwise agreed in writing by PB and ED, shall take effect 48 Weekday Hours after receipt by ED; provided, however, that if ED believes in good faith that EBCS Information contained in any such notice is erroneous, ED may notify PB by delivery of a notice in the form of the Attachment hereto prior to the expiry of such 48 Weekday Hour period, in which event such notice from PB shall not take effect until PB and ED have resolved the discrepancy in their EBCS Information regarding the relevant PB counterparty.

The effectiveness of any notice given pursuant to a Covered Give-Up Agreement, as to information contained therein other than EBCS Information, shall be governed by the terms of the Covered Give-Up Agreement, without regard to whether such notice also contains EBCS Information.

“**Business Day**” means the twenty-four hour calendar day on any day on which commercial banks in New York City are open for general business (including dealings in foreign exchange and foreign currency deposits).

“**EBCS Information**” means information described in paragraph (b)(3) or (b)(8) of the Annex.

“**Weekday Hour**” means an hour during a Business Day. References to a period comprising a stated number of Weekday Hours signify that number of consecutive Weekday Hours.

Contact details and manner of delivery for notices to ED:

[ED contact details]

Contact details and manner of delivery for notices to PB:

[PB contact details]

Accepted and agreed:

[PB signature block]

[ED signature block]

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Annex to Form of Agreement as to EBCS Information Changes

We refer to the agreement between us, dated [____], (“**Agreement**”) relating to the effectiveness of notices regarding information described in paragraphs (b)(3)(and (b)(8) of the Annex to the ISDA Derivatives/FX Prime Brokerage Business Conduct Allocation Protocol (“**ISDA PB Protocol**”), and the notice (attached hereto) we have received at [time of receipt] relating to the EBCS Information (as defined in the Agreement) with respect to [Name of Designated Party] (“EBCS Notice”). We hereby inform you that we believe in good faith that the following information contained in that notice is erroneous for the reason stated below.

Erroneous Information:

Reason for belief:

In accordance with the Agreement, the EBCS Notice shall not take effect until we have resolved the aforementioned discrepancy.

Yours sincerely,

[ED signature block]

Attachment