

To: All members, warehouse companies and their London agents, and other interested parties

Ref: 17/ 047

Classification: General updates

Date: 2 February 2017

Subject: **CLARIFICATION TO INTRODUCING BROKER ARRANGEMENTS FOR THE LME**

## Summary

1 This Notice (a) confirms how the LME's existing introducing broker ("IB") arrangements can be facilitated in the LME's inter-office market in respect of its Contracts, (b) clarifies the requirements for non-member brokers wishing to participate in LME Contracts, and (c) sets out explicitly the booking methodology for the matching and registration of such Contracts. This Notice supersedes LME Notice 16/202 : A196.

## Defined Terms

- 2 An IB is defined, for LME purposes<sup>1</sup>, as:
- (i) a person who introduces a prospective counterparty (i.e. a Client) to a Member (with a view to the counterparty and the Member transacting together on a principal to principal basis); or
  - (ii) a person who acts as agent for a counterparty and enters into transactions on behalf of the counterparty with LME Members; or
  - (iii) a person who acts as agent for an LME Member and enters into transactions on behalf of the Member with counterparties.
- 3 Terms not otherwise defined in this Notice shall have the meaning ascribed to them in the Rules and Regulations of the LME (the "Rulebook").

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<sup>1</sup> See LME Notice 00/385:A378:R012, Rules on Introducing Brokers dated 15 September 2000.



## Background

- 4 Notice 00/385 : A378 : R012, **RULES ON INTRODUCING BROKERS**, dated 15 September 2000 set out the definition of an IB and Members' obligations when dealing with IBs. Notice 16/202 : A196, **INTRODUCING BROKER ARRANGEMENTS FOR THE LME**, set out how the LME's existing IB arrangements could be facilitated in the LME's inter-office market in respect of its Ferrous Contracts. Following feedback from members since the issuance of LME Notice 16/202 : A196, the LME is clarifying the requirements for IBs wishing to participate in LME Contracts in respect of the agreements that need to be in place between the parties and the booking methodology for the resulting LME Contracts.
- 5 The LME understands that there are circumstances where counterparties may wish to agree trades in the LME's inter-office (i.e. telephone) market while retaining their anonymity. For example, Client A and Client B may each wish to execute a trade without showing their interest to the market. Such trades may be arranged utilising the services of an IB; the IB will know the identity of Client A and Client B, agree the price and trade with both parties, but will not reveal the identity of each to the other.
- 6 The LME is a principal to principal market. There are two types of Contract on the LME: Exchange Contracts and Client Contracts<sup>2</sup>. Broadly, Exchange Contracts are Contracts made between two Clearing Members. Client Contracts are Contracts made between a Category 1, 2 or 4 Member and any other person<sup>3</sup>. Only a Category 1, 2 or 4 Member or an agent of a Category 1, 2 or 4 Member can make an LME price to a Client or another Member, and agree an LME Contract.
- 7 Therefore, on the LME, a Client will never trade with another Client directly. The Client will enter into a Client Contract with a Category 1 or 2 Member, and the Category 1 or 2 Member will enter into an Exchange Contract with another

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<sup>2</sup> This will change with the proposed "open offer" amendments set out in the LME Consultation Notice 16 361 dated 24 November 2016 but this should not affect the analysis: there will still be Client Contracts and Cleared Contracts.

<sup>3</sup> Or a Contract made between a Category 1 or 2 Member and a Category 4 Member.



Category 1 or 2 Member. That other Category 1 or 2 Member may itself have a Client, in which case it may agree a Client Contract with such Client<sup>4</sup>.

8 Accordingly, the IB will effectively be facilitating this contractual flow. For example, in a scenario where an IB, acting as agent for LME Member A, arranges a trade between Client A and Client B in the inter-office market, where Client A holds a fully disclosed clearing account with Member A and Client B holds a fully disclosed clearing account with Member B, the resultant Contracts will be as follows:

- (i) Client A will enter into a Client Contract with Member A;
- (ii) Member A will enter into an Exchange Contract with Member B; and
- (iii) Member B will enter into a Client Contract with Client B.

9 In facilitating such an arrangement as set out in paragraph 8 above, the IB will never trade in a proprietary capacity, become the counterparty to an LME trade or a principal to the resultant LME Contracts but will receive a commission (either from Client A and/or Client B or from the relevant Member(s)) in respect of its services. Client A will never know the identity of Client B, and vice versa.

10 For the avoidance of doubt, the scenario noted in paragraph 8 above is for illustrative purposes only as there are a number of other scenarios in which the IB can arrange LME Contracts between counterparties.

### **Requirements for Introducing Broker Arrangements**

11 The LME confirms that its Category 1, 2 and 4 Members may enter into arrangements with IBs such that the IB can arrange LME Contracts in the inter-office market as long as the requirements set out in paragraphs 12–15 below are satisfied.

12 Under an arrangement where an IB is acting in the capacity of agent of an LME Member whereby the IB can make an LME price to Members and/or Clients in the name of the Member for whom he acts as agent and arrange LME Contracts, then the LME requires that there must be an agency agreement in

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<sup>4</sup> For simplicity, this description ignores Category 4 Member arrangements.



place between the Member and the IB setting out the terms of the arrangement. With such an agency agreement in place, LME Contracts arranged by the IB can be entered into the LME matching system under the matching mnemonic of the member with whom the IB has an agency agreement.

- 13 Where the IB is acting as agent of a Client for the purposes of arranging LME Contracts, the Client's Clearing Member must put in place arrangements with its Client and the IB such that the Clearing Member is willing to accept trades into the Client's account under instruction from the IB. Where the IB is acting as agent for a Clearing Member and a Client/group of Clients that hold clearing accounts with that same Clearing Member, then the agency agreement between the IB and the Clearing Member may be extended to additionally cover the acceptance of trades into the Clearing Members' Client accounts that have been arranged by the IB.
- 14 Where the IB acts as agent for one Member but arranges LME Contracts between Clients who hold clearing accounts with other Members, then the arrangement whereby Members can accept trades into their Client accounts arranged and instructed by an IB, with whom they have no agency agreement, should be set out in a Give-Up Agreement which must include (1) the IB, (2) the Member with whom the IB has an agency agreement, (3) the Clearing Member where the Client holds its LME clearing account, and (4) the Client<sup>5</sup>. Give-Up Agreements involving IBs can only be used to arrange LME Contracts in conjunction with an agency agreement between the IB and at least one LME Member. The Appendix to this Notice sets out specific trading scenarios, the arrangements that need to be put in place for compliance with LME Rules, the booking methodology for such trades and the resulting LME Contracts.
- 15 Category 1, 2 and 4 Members should undertake such due diligence as they deem appropriate in respect of the IBs and maintain a list of IBs with whom they have entered into such arrangements, and must produce such list upon request from the LME, together with any other documentation relating to such arrangements, including but not limited to give-up agreements and agency agreement(s) as the LME shall require from time to time.

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<sup>5</sup> See LME Notice 00/383:A376:R010, Rules for LME Give-Up Agreements dated 15 September 2000.



- 16 Any arrangements which a Category 1, 2 or 4 Member shall enter into with its Clients or with any IBs shall be the responsibility of the Category 1, 2 or 4 Member. The LME does not specify any form of agency agreement or have any liability in respect of any arrangements entered into. Members are reminded of the Rules for written agreements set out in LME Notice 00/383 : A376 : R010, **RULES FOR LME GIVE-UP AGREEMENTS**, and other administrative procedure from time to time.
- 17 The Category 1, 2 or 4 Member shall be responsible for the entry of all LME Contracts into the Matching System as currently and observe the matching deadlines as set out by administrative procedure from time to time.
- 18 The requirements of Notice 00/385:A378:R012, **RULES ON INTRODUCING BROKERS**, dated 15 September 2000 shall remain in effect.

#### **Questions**

- 19 Questions in relation to any issue raised by this Notice should be directed to the Client Advisory and Membership Services Department of the LME at [Client.Advisory@lme.com](mailto:Client.Advisory@lme.com).

**Gillian Hampson**  
**Head of Client Advisory & Membership Services**

cc: Board directors



## Appendix

1. **The IB as agent of Member 1 and Member 2, arranges a trade between Client A and Client B who hold a clearing account at Member 1 and Member 2 respectively.**

### Requirements:

- a) The IB has an agency agreement with Member 1 and Member 2;
- b) There is an agreement in place, which may form part of the respective agency agreements, whereby Member 1 will accept trades arranged by the IB into Client A's clearing account and Member 2 will accept trades arranged by the IB into Client B's clearing account.

### Trade Entry

- c) Member 1 registers a **NORMAL** client trade for Client A;
- d) Member 1 and Member 2 match a **NORMAL** Exchange trade;
- e) Member 2 registers a **NORMAL** client trade for Client B.

### LME Contracts

- f) Client A will enter into a Client Contract with Member 1;
- g) Member 1 will enter into an Exchange Contract with Member 2;
- h) Member 2 will enter into a Client Contract with Client B.

2. **The IB as agent of Member 1, arranges a trade between Client A and Client B who both hold clearing accounts at Member 1.**

### Requirements:

- a) The IB has an agency agreement with Member 1;
- b) There is an agreement in place, which may form part of the agency agreement, whereby Member 1 will accept trades arranged by the IB into Client A and Client B's clearing accounts.

### Trade Entry

- c) Member 1 registers a **NORMAL** client trade for Client A;
- d) Member 1 registers a **NORMAL** client trade for Client B.



### **LME Contracts**

- e) Client A will enter into a Client Contract with Member 1;
- f) Client B will enter into a Client Contract with Member 1.

### **3. The IB as agent of Member 1, arranges a trade between Client A and Client B who hold a clearing account at Member 1 and Member 2 respectively.**

#### **Requirements:**

- a) The IB has an agency agreement with Member 1;
- b) There is an agreement in place, which may form part of the agency agreement, whereby Member 1 will accept trades arranged by the IB into Client A's clearing account;
- c) There is a give-up agreement in place between the IB, Member 1, Member 2 and Client B whereby Member 2 will accept trades arranged by the IB into Client B's clearing account which may be set out as follows:

Executing Broker	Non-member IB
LME Executing Member	Member 1
LME Clearing Member	Member 2
Client	Client B

#### **Trade Entry**

- d) Member 1 registers a **NORMAL** client trade for Client A;
- e) Member 1 and Member 2 match a **GIVE-UP EXECUTOR / GIVE-UP CLEARER** Exchange trade;
- f) Member 2 registers a **GIVE-UP CLEARER** client trade for Client B.

### **LME Contracts**

- g) Client A will enter into a Client Contract with Member 1;
- h) Member 1 will enter into an Exchange Contract with Member 2;
- i) Member 2 will enter into a Client Contract with Client B.



**4. The IB as agent of Member 1, arranges a trade between Client A and Client B who hold a clearing account at Member 2 and Member 3 respectively.**

**Requirements:**

- a) The IB has an agency agreement with Member 1;
- b) There is a give-up agreement in place between the IB, Member 1, Member 2 and Client A whereby Member 2 will accept trades arranged by the IB into Client A's clearing account which may be set out as follows:

Executing Broker	Non-member IB
LME Executing Member	Member 1
LME Clearing Member	Member 2
Client	Client A

- c) There is a give-up agreement in place between the IB, Member 1, Member 3 and Client B whereby Member 3 will accept trades arranged by the IB into Client B's clearing account which may be set out as follows:

Executing Broker	Non-member IB
LME Executing Member	Member 1
LME Clearing Member	Member 3
Client	Client B

**Trade Entry**

- d) Member 1 and Member 2 match a **GIVE-UP EXECUTOR / GIVE-UP CLEARER** Exchange trade;
- e) Member 2 registers a **GIVE-UP CLEARER** client trade for Client A;
- f) Member 1 and Member 3 match a **GIVE UP EXECUTOR / GIVE-UP CLEARER** Exchange trade;
- g) Member 3 registers a **GIVE-UP CLEARER** client trade for Client B.

**LME Contracts**

- h) Member 1 will enter into an Exchange Contract with Member 2;
- i) Client A will enter into a Client Contract with Member 2;
- j) Member 1 will enter into an Exchange Contract with Member 3;
- k) Member 3 will enter into a Client Contract with Client B.





**5. The IB as agent of Member 1, arranges a trade between Member 1 and Member 2.**

**Requirements:**

- a) The IB has an agency agreement with Member 1.

**Trade Entry**

- b) Member 1 matches a **NORMAL** Exchange trade with Member 2.

**LME Contracts**

- c) Member 1 will enter into an Exchange Contract with Member 2.

**6. The IB as agent of Member 1, arranges a trade between Client A, who holds a clearing account at Member 1, and Member 2.**

**Requirements:**

- a) The IB has an agency agreement with Member 1;
- b) There is an agreement in place, which may form part of the agency agreement whereby Member 1 will accept trades arranged by the IB into Client A's clearing account.

**Trade Entry**

- c) Member 1 register a **NORMAL** client trade for Client A;
- d) Member 1 matches a **NORMAL** Exchange trade with Member 2.

**LME Contracts**

- e) Client A will enter into a Client Contract with Member 1;
- f) Member 1 will enter into an Exchange Contract with Clearing Member 2.

**7. The IB as agent of Member 1, arranges a trade between Member 1 and Client B who holds a clearing account at Member 2.**

**Requirements:**

- a) The IB has an agency agreement with Member 1



- b) There is a give-up agreement in place between the IB, Member 1, Member 2 and Client B whereby Member 2 will accept trades arranged by the IB into Client B's clearing account which may be set out as follows :

Executing Broker	Non-member IB
LME Executing Member	Member 1
LME Clearing Member	Member 2
Client	Client B

### **Trade Entry**

- c) Member 1 and Member 2 match a **GIVE-UP EXECUTOR / GIVE-UP CLEARER** trade;
- d) Member 2 registers a **GIVE-UP CLEARER** client trade for Client B

### **LME Contracts**

- e) Member 1 will enter into an Exchange Contract with Member 2;
- f) Member 2 will enter into a Client Contract with Client B.

This list is not exhaustive and Members are encouraged to contact [Client.Advisory@lme.com](mailto:Client.Advisory@lme.com) if there is any uncertainty as to what arrangements need to be in place or what booking methodology should be adopted for a particular trading scenario.