

***Futures and Options on Futures  
And Cleared Derivatives Transactions  
Risk Disclosures***

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## **RISK DISCLOSURE STATEMENT**

The risk of loss in trading commodity futures contracts can be substantial. You should, therefore, carefully consider whether such trading is suitable for you in light of your circumstances and financial resources. You should be aware of the following points:

1. You may sustain a total loss of the funds that you deposit with your broker to establish or maintain a position in the commodity futures market, and you may incur losses beyond these amounts. If the market moves against your position, you may be called upon by your broker to deposit a substantial amount of additional margin funds, on short notice, in order to maintain your position. If you do not provide the required funds within the time required by your broker, your position may be liquidated at a loss, and you will be liable for any resulting deficit in your account.
2. The funds you deposit with a futures commission merchant for trading futures positions are not protected by insurance in the event of the bankruptcy or insolvency of the futures commission merchant, or in the event your funds are misappropriated.
3. The funds you deposit with a futures commission merchant for trading futures positions are not protected by the Securities Investor Protection Corporation even if the futures commission merchant is registered with the Securities and Exchange Commission as a broker or dealer.
4. The funds you deposit with a futures commission merchant are generally not guaranteed or insured by a derivatives clearing organization in the event of the bankruptcy or insolvency of the futures commission merchant, or if the futures commission merchant is otherwise unable to refund your funds. Certain derivatives clearing organizations, however, may have programs that provide limited insurance to customers. You should inquire of your futures commission merchant whether your funds will be insured by a derivatives clearing organization and you should understand the benefits and limitations of such insurance programs.
5. The funds you deposit with a futures commission merchant are not held by the futures commission merchant in a separate account for your individual benefit. Futures commission merchants commingle the funds received from customers in one or more accounts and you may be exposed to losses incurred by other customers if the futures commission merchant does not have sufficient capital to cover such other customers' trading losses.
6. The funds you deposit with a futures commission merchant may be invested by the futures commission merchant in certain types of financial instruments that have been approved by the Commission for the purpose of such investments. Permitted investments are listed in Commission Regulation 1.25 and include: U.S. government securities; municipal securities; money market mutual funds; and certain corporate notes and bonds. The futures commission merchant may retain the interest and other earnings realized from its investment of customer funds. You should be familiar with the types of financial instruments that a futures commission merchant may invest customer funds in.
7. Futures commission merchants are permitted to deposit customer funds with affiliated entities, such as affiliated banks, securities brokers or dealers, or foreign brokers. You should inquire as to whether your futures commission merchant deposits funds with affiliates and assess whether such deposits by the futures commission merchant with its affiliates increases the risks to your funds.
8. You should consult your futures commission merchant concerning the nature of the protections available to safeguard funds or property deposited for your account.
9. Under certain market conditions, you may find it difficult or impossible to liquidate a position. This can occur, for example, when the market reaches a daily price fluctuation limit ("limit move").
10. All futures positions involve risk, and a "spread" position may not be less risky than an outright "long" or "short" position.
11. The high degree of leverage (gearing) that is often obtainable in futures trading because of the small margin requirements can work against you as well as for you. Leverage (gearing) can lead to large losses as well as gains.
12. In addition to the risks noted in the paragraphs enumerated above, you should be familiar with the futures commission merchant you select to entrust your funds for trading futures positions. The Commodity Futures Trading Commission requires each futures commission merchant to make publicly available on its

Web site firm specific disclosures and financial information to assist you with your assessment and selection of a futures commission merchant. Information regarding this futures commission merchant may be obtained by visiting our Web site, <http://www.morganstanley.com/institutional/sales/derivatives.html>

ALL OF THE POINTS NOTED ABOVE APPLY TO ALL FUTURES TRADING WHETHER FOREIGN OR DOMESTIC. IN ADDITION, IF YOU ARE CONTEMPLATING TRADING FOREIGN FUTURES OR OPTIONS CONTRACTS, YOU SHOULD BE AWARE OF THE FOLLOWING ADDITIONAL RISKS:

13. Foreign futures transactions involve executing and clearing trades on a foreign exchange. This is the case even if the foreign exchange is formally “linked” to a domestic exchange, whereby a trade executed on one exchange liquidates or establishes a position on the other exchange. No domestic organization regulates the activities of a foreign exchange, including the execution, delivery, and clearing of transactions on such an exchange, and no domestic regulator has the power to compel enforcement of the rules of the foreign exchange or the laws of the foreign country. Moreover, such laws or regulations will vary depending on the foreign country in which the transaction occurs. For these reasons, customers who trade on foreign exchanges may not be afforded certain of the protections which apply to domestic transactions, including the right to use domestic alternative dispute resolution procedures. In particular, funds received from customers to margin foreign futures transactions may not be provided the same protections as funds received to margin futures transactions on domestic exchanges. Before you trade, you should familiarize yourself with the foreign rules which will apply to your particular transaction.
14. Finally, you should be aware that the price of any foreign futures or option contract and, therefore, the potential profit and loss resulting therefrom, may be affected by any fluctuation in the foreign exchange rate between the time the order is placed and the foreign futures contract is liquidated or the foreign option contract is liquidated or exercised.

THIS BRIEF STATEMENT CANNOT, OF COURSE, DISCLOSE ALL THE RISKS AND OTHER ASPECTS OF THE COMMODITY MARKETS.

## **SUPPLEMENTAL RISK DISCLOSURE STATEMENT**

This brief statement does not disclose all of the risks and other significant aspects of trading in futures and options. In light of the risks, you should undertake such transactions only if you understand the nature of the contracts (and contractual relationships) into which you are entering and the extent of your exposure to risk. Trading in futures and options is not suitable for many members of the public. You should carefully consider whether trading is appropriate for you in light of your experience, objectives, financial resources and other relevant circumstances.

### **FUTURES**

#### **1. Effect of 'Leverage' or 'Gearing'**

Transactions in futures carry a high degree of risk. The amount of initial margin is small relative to the value of the futures contract so that transactions are 'leveraged' or 'geared.' A relatively small market movement will have a proportionately larger impact on the funds you have deposited or will have to deposit: this may work against you as well as for you. You may sustain a total loss of initial margin funds and any additional funds deposited with the firm to maintain your position. If the market moves against your position or margin levels are increased, you may be called upon to pay substantial additional funds on short notice to maintain your position. If you fail to comply with a request for additional funds within the time prescribed, your position may be liquidated at a loss and you will be liable for any resulting deficit.

#### **2. Risk-reducing orders or strategies**

The placing of certain orders (e.g., 'stop-loss' orders, where permitted under local law, or 'stop-limit' orders) which are intended to limit losses to certain amounts may not be effective because market conditions may make it impossible to execute such orders. Strategies using combinations of positions, such as 'spread' and 'straddle' positions, may be as risky as taking simple 'long' or 'short' positions.

### **OPTIONS**

#### **3. Variable degree of risk**

Transactions in options carry a high degree of risk. Purchasers and sellers of options should familiarize themselves with the type of option (i.e., put or call) which they contemplate trading and the associated risks. You should calculate the extent to which the value of the options must increase for your position to become profitable, taking into account the premium and all transaction costs.

The purchaser of options may offset or exercise the options or allow the options to expire. The exercise of an option results either in a cash settlement or in the purchaser acquiring or delivering the underlying interest. If the option is on a future, the purchaser will acquire a futures position with associated liabilities for margin (see the section on Futures above). If the purchased options expire worthless, you will suffer a total loss of your investment, which will consist of the option premium plus transaction costs. If you are contemplating purchasing deep-out-of-the-money options, you should be aware that the chance of such options becoming profitable ordinarily is remote.

Selling ('writing' or 'granting') an option generally entails considerably greater risk than purchasing options. Although the premium received by the seller is fixed, the seller may sustain a loss well in excess of that amount. The seller will be liable for additional margin to maintain the position if the market moves unfavorably. The seller will also be exposed to the risk of the purchaser exercising the option and the seller will be obligated to either settle the option in cash or to acquire or deliver the underlying interest. If the option is on a future, the seller will acquire a position in a future with associated liabilities for margin (see the section on Futures above). If the position is 'covered' by the seller holding a corresponding position in the underlying interest or a future or another option, the risk may be reduced. If the option is not covered, the risk of loss can be unlimited.

Certain exchanges in some jurisdictions permit deferred payment of the option premium, exposing the

purchaser to liability for margin payments not exceeding the amount of the premium. The purchaser is still subject to the risk of losing the premium and transaction costs. When the option is exercised or expires, the purchaser is responsible for any unpaid premium outstanding at that time.

#### **Additional risks common to futures and options**

##### **4. Terms and conditions of contracts**

You should ask the firm with which you deal about the terms and conditions of the specific futures or options which you are trading and associated obligations (e.g., the circumstances under which you may become obligated to make or take delivery of the underlying interest of a futures contract and, in respect of options, expiration dates and restrictions on the time for exercise). Under certain circumstances the specifications of outstanding contracts (including the exercise price of an option) may be modified by the exchange or clearing house to reflect changes in the underlying interest.

##### **5. Suspension or restriction of trading and pricing relationships**

Market conditions (e.g., illiquidity) and/or the operation of the rules of certain markets (e.g., the suspension of trading in any contract or contract month because of price limits or 'circuit breakers') may increase the risk of loss by making it difficult or impossible to effect transactions or liquidate/offset positions. If you have sold options, this may increase the risk of loss.

Further, normal pricing relationships between the underlying interest and the future, and the underlying interest and the option may not exist. This can occur when, for example, the futures contract underlying the option is subject to price limits while the option is not. The absence of an underlying reference price may make it difficult to judge 'fair' value.

##### **6. Deposited cash and property**

You should familiarize yourself with the protections accorded money or other property you deposit for domestic and foreign transactions, particularly in the event of a firm insolvency or bankruptcy. The extent to which you may recover your money or property may be governed by specified legislation or local rules. In some jurisdictions, property which had been specifically identifiable as your own will be pro-rated in the same manner as cash for purposes of distribution in the event of a shortfall.

##### **7. Commission and other charges**

Before you begin to trade, you should obtain a clear explanation of all commissions, fees and other charges for which you will be liable. These charges will affect your net profit (if any) or increase your loss.

##### **8. Transactions in other jurisdictions**

Transactions on markets in other jurisdictions, including markets formally linked to a domestic market, may expose you to additional risk. Such markets may be subject to regulation which may offer different or diminished investor protection. Before you trade, you should inquire about any rules relevant to your particular transactions. Your local regulatory authority will be unable to compel the enforcement of the rules of regulatory authorities or markets in other jurisdictions where your transactions have been effected. You should ask the firm with which you deal for details about the types of redress available in both your home jurisdiction and other relevant jurisdictions before you start to trade.

##### **9. Currency risks**

The profit or loss in transactions in foreign currency-denominated contracts (whether they are traded in your own or another jurisdiction) will be affected by fluctuations in currency rates where there is a need to convert from the currency denomination of the contract to another currency.

#### 10. Trading facilities

Most open-outcry and electronic trading facilities are supported by computer-based component systems for the order-routing, execution, matching, registration or clearing of trades. As with all facilities and systems, they are vulnerable to temporary disruption or failure. Your ability to recover certain losses may be subject to limits on liability imposed by the system provider, the market, the clearing house and/or member firms. Such limits may vary; you should ask the firm with which you deal for details in this respect.

#### 11. Electronic trading

Trading on an electronic trading system may differ not only from trading in an open-outcry market but also from trading on other electronic trading systems. If you undertake transactions on an electronic trading system, you will be exposed to risk associated with the system, including the failure of hardware and software. The result of any system failure may be that your order is either not executed according to your instructions or is not executed at all.

#### 12. Off-exchange transactions

In some jurisdictions, and only then in restricted circumstances, firms are permitted to effect off-exchange transactions. The firm with which you deal may be acting as your counterparty to the transaction. It may be difficult or impossible to liquidate an existing position, to assess the value, to determine a fair price or to assess the exposure to risk. For these reasons, these transactions may involve increased risks. Off-exchange transactions may be less regulated or subject to a separate regulatory regime. Before you undertake such transactions, you should familiarize yourself with applicable rules and attendant risks.

### **CROSS TRADE CONSENT**

Morgan Stanley & Co. LLC, its officers, directors employees or affiliates or other customers of Morgan Stanley & Co. LLC or of the servicing floor broker may be from time to time on the opposite side of orders for physicals or for purchase or sale of futures contracts and option contracts placed for your Account in conformity with regulations of the Commodity Futures Trading Commission and the by-laws, rules and regulations of the applicable market (and its clearing organization, if any) on which such order is executed.



## **ELECTRONIC TRADING AND ORDER ROUTING SYSTEMS DISCLOSURE STATEMENT**<sup>\*/</sup>

Electronic trading and order routing systems differ from traditional open outcry pit trading and manual order routing methods. Transactions using an electronic system are subject to the rules and regulations of the exchange(s) offering the system and/or listing the contract. Before you engage in transactions using an electronic system, you should carefully review the rules and regulations of the exchange(s) offering the system and/or listing contracts you intend to trade.

### **DIFFERENCES AMONG ELECTRONIC TRADING SYSTEMS**

Trading or routing orders through electronic systems vary widely among the different electronic systems. You should consult the rules and regulations of the exchange offering the electronic system and/or listing the contract traded or order routed to understand, among other things, in the case of trading systems, the system's order matching procedure, opening and closing procedures and prices, error trade policies, and trading limitations or requirements; and in the case of all systems, qualifications for access and grounds for termination and limitations on the types of orders that may be entered into the system. Each of these matters may present different risk factors with respect to trading on or using a particular system. Each system may also present risks related to system access, varying response times, and security. In the case of internet-based systems, there may be additional types of risks related to system access, varying response times and security, as well as risks related to service providers and the receipt and monitoring of electronic mail.

### **RISK ASSOCIATED WITH SYSTEM FAILURE**

Trading through an electronic trading or order routing system exposes you to risks associated with system or component failure. In the event of system or component failure, it is possible that, for a certain time period, you may not be able to enter new orders, execute existing orders, or modify or cancel orders that were previously entered. System or component failure may also result in loss of orders or order priority.

### **SIMULTANEOUS OPEN OUTCRY PIT AND ELECTRONIC TRADING**

Some contracts offered on an electronic trading system may be traded electronically and through open outcry during the same trading hours. You should review the rules and regulations of the exchange offering the system and/or listing the contract to determine how orders that do not designate a particular process will be executed.

### **LIMITATION OF LIABILITY**

Exchanges offering an electronic trading or order routing system and/or listing the contract may have adopted rules to limit their liability, the liability of Futures Commission Merchants, and software and communication system vendors and the amount of damages you may collect for system failure and delays. These limitations of liability provisions vary among the exchanges. You should consult the rules and regulations of the relevant exchanges(s) in order to understand these liability limitations.

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<sup>\*/</sup> Each exchange's relevant rules are available upon request from the industry professional with whom you have an account. Some exchanges' relevant rules also are available on the exchange's internet home page.

## **NOTICE REGARDING AVERAGE PRICE SYSTEM ("APS")**

You should be aware that certain US and non-US exchanges, including the CME and CBOT, may now or in the future allow a futures commission merchant ("FCM") such as Morgan Stanley & Co. LLC to confirm trades executed on such exchanges to some or all of their customers on an average price basis regardless of whether the exchanges have average price systems of their own. Average prices that are not calculated by an exchange system will be calculated by your FCM. In either case, trades that are confirmed to you at average prices will be designated as such on your daily and monthly statements.

APS enables a clearing firm to confirm to customers an average price when multiple execution prices are received on an order or series of orders for the same accounts. For example, if an order transmitted by an account manager on behalf of several customers is executed at more than one price, those prices may be averaged and the average may be confirmed to each customer. Customers may choose whether to use APS, and may request that APS be used for discretionary or non-discretionary accounts.

An order subject to APS must be for the same commodity. An APS order may be used for futures, options or combination transactions. An APS order for futures must be for the same commodity and month, and for options, it must be for the same commodity, month, put/call and strike.

An APS indicator will appear on the confirmation and monthly statement for a customer whose positions have been confirmed at an average price. This indicator will notify the customer that the confirmed price represents an average price or rounded average price.

The average price is not the actual execution price. APS will calculate the same price for all customers that participate in the order.

APS may be used when a series of orders are entered for a group of accounts. For example, a bunched APS order (an order that represents more than one customer account) executed at 10:00 a.m. could be averaged with a bunched APS order executed at 12:00 p.m. provided that each of the bunched orders is for the same accounts. In addition, market orders and limit orders may be averaged, as may limit orders at different prices, provided that each order is for the same accounts.

The following scenario exemplifies what occurs if an APS order is only partially executed. At 10:00 a.m. an APS order to buy 100 Dec S & P 500 futures contracts is transmitted at a limit price of 376.00; 50 are executed at 376.00, and the balance is not filled. At 12:00 p.m. an APS order to buy 100 Dec S & P 500 futures contracts is transmitted at a limit price of 375.00; 50 are executed at 375.00, and the balance is not filled. Both orders are part of a series for the same group of accounts. In this example, the two prices will be averaged. If the order was placed for more than one account, the account controller must rely on pre-existing allocation procedures to determine the proportions in which each account will share in the partial fill.

Upon receipt of an execution at multiple prices for an order with an APS indicator, an average will be computed by multiplying the execution prices by the quantities at those prices divided by the total quantities. An average price for a series of orders will be computed based on the average prices of each order in that series. The actual average price or the average price rounded to the next price increment may be confirmed to customers. If a clearing member confirms the rounded average price, the clearing member must round the average price up to the next price increment for a sell order. The rounding process will create a cash residual of the difference between the actual average price and the rounded average price that must be paid to the customer.

APS may produce prices that do not conform to whole cent increments. In such cases, any amounts less than one cent may be retained by the clearing member. For example, if the total residual to be paid to a customer on a rounded average price for 10 contracts is \$83.333333, the clearing member may pay \$83.33 to the customer.

If you would like more information on APS orders, please contact Morgan Stanley & Co. LLC Listed Derivatives Operations or your client service representative.

## **DIRECT ORDER TRANSMITTAL CLIENT DISCLOSURE STATEMENT**

This statement applies to the ability of authorized customers of Morgan Stanley & Co. LLC (“**MSCO**”) to place orders for foreign futures and options transactions directly with non-US entities (each, an “Executing Firm”) that execute transactions on behalf of MSCO’s customer omnibus accounts.

Please be aware of the following should you be permitted to place the type of orders specified above:

- The orders you place with an Executing Firm are for MSCO’s customer omnibus account maintained with a foreign clearing firm. Consequently, MSCO may limit or otherwise condition the orders you place with the Executing Firm.
- You should be aware of the relationship of the Executing Firm and MSCO. MSCO may not be responsible for the acts, omissions, or errors of the Executing Firm, or its representatives, with which you place your orders. In addition, the Executing Firm may not be affiliated with MSCO. If you choose to place orders directly with an Executing Firm, you may be doing so at your own risk.
- It is your responsibility to inquire about the applicable laws and regulations that govern the foreign exchanges on which transactions will be executed on your behalf. Any orders placed by you for execution on that exchange will be subject to such rules and regulations, its customs and usages, as well as any local laws that may govern transactions on that exchange. These laws, rules, regulations, customs and usages may offer different or diminished protection from those that govern transactions on US exchanges. In particular, funds received from customers to margin foreign futures transactions may not be provided the same protections as funds received to margin futures transactions on domestic exchanges. Before you trade, you should familiarize yourself with the foreign rules which will apply to your particular transaction. United States regulatory authorities may be unable to compel the enforcement of the rules of regulatory authorities or markets in non-US jurisdictions where transactions may be effected.
- It is your responsibility to determine whether the Executing Firm has consented to the jurisdiction of the courts in the United States. In general, neither the Executing Firm nor any individuals associated with the Executing Firm will be registered in any capacity with the Commodity Futures Trading Commission. Similarly, your contacts with the Executing Firm may not be sufficient to subject the Executing Firm to the jurisdiction of courts in the United States in the absence of the Executing Firm's consent. Accordingly, neither the courts of the United States nor the Commission's reparations program will be available as a forum for resolution of any disagreements you may have with the Executing Firm, and your recourse may be limited to actions outside the United States.

Unless you object within five (5) days by giving notice as provided in your customer agreement after receipt of this disclosure, MSCO will assume your consent to the aforementioned conditions.

## **FOREIGN TRADER DISCLOSURE STATEMENT**

Dear Customer:

In accordance with Rules 15.05 and 21.03 of the Commodity Futures Trading Commission ("CFTC"), 17 C.F.R. §§15.05 and 21.03, we are considered to be your agent for purposes of accepting delivery and service of communications from or on behalf of the CFTC regarding any commodity futures contracts or commodity option contracts which are or have been maintained in your account(s) with us. In the event that you are acting as agent or broker for any other person(s), we are also considered to be their agent, and the agent of any person(s) for whom they may be acting as agent or broker, for purposes of accepting delivery and service of such communications. Service or delivery to us of any communication issued by or on behalf of the CFTC (including any summons, complaint, order, subpoena, special call, request for information, notice, correspondence or other written document) will be considered valid and effective service or delivery upon you or any person for whom you may be acting, directly or indirectly, as agent or broker.

You should be aware that Rule 15.05 also provides that you may designate an agent other than Morgan Stanley & Co. LLC. Any such alternative designation of agency must be evidenced by a written agency agreement which you must furnish to us and which we, in turn, must forward to the CFTC. If you wish to designate an agent other than us, please contact us in writing. You should consult 17 C.F.R. § 15.05 for a more complete explanation of the foregoing.

Upon a determination by the CFTC that information concerning your account(s) with us may be relevant in enabling the CFTC to determine whether the threat of a market manipulation, corner, squeeze, or other market disorder exists, the CFTC may issue a call for specific information from us or from you. In the event that the CFTC directs a call for information to us, we must provide the information requested within the time specified by the CFTC. If the CFTC directs a call for information to you through us as your agent, we must promptly transmit the call to you, and you must provide the information requested within the time specified by the CFTC. If any call by the CFTC for information regarding your account(s) with us is not met, the CFTC has authority to restrict such account(s) to trading for liquidation only. You have the right to a hearing before the CFTC to contest any call for information concerning your account(s) with us, but your request for a hearing will not suspend the CFTC's call for information unless the CFTC modifies or withdraws the call. Please consult 17 C.F.R. §21.03 for a more complete description of the foregoing (including the type of information you may be required to provide).

Certain additional regulations may affect you. Part 17 of the CFTC Regulations, 17 C.F.R. Part 17, requires each futures commission merchant and foreign broker to submit a report to the CFTC with respect to each account carried by such futures commission merchant or foreign broker which contains a reportable futures position. (Specific reportable position levels for all futures contracts traded on U.S. exchanges are established in Rule 15.03.) In addition, Part 18 of the CFTC Regulations, 17 C.F.R. Part 18, requires all traders (including foreign traders) who own or control a reportable futures or options position and who have received a special call from the CFTC to file a Large Trader Reporting Form (Form 103) with the CFTC within one day after the special call upon such trader by the CFTC. Please consult 17 C.F.R. Parts 17 and 18 for more complete information with respect to the foregoing.

Very truly yours,

Morgan Stanley & Co. LLC

## **NOTICE TO CLIENTS**

### **POSITION LIMIT AND LARGE OPEN POSITION REPORTING REQUIREMENTS FOR OPTIONS AND FUTURES TRADED ON THE HONG KONG EXCHANGES**

The Hong Kong regulatory regime imposes position limit and reportable position requirements for stock options and futures contracts traded on the Stock Exchange of Hong Kong and on the Hong Kong Futures Exchange.

These requirements are set out in the Hong Kong Securities and Futures (Contracts Limits and Reportable Positions) Rules (as amended, the “**Rules**”) made by the Securities and Futures Commission (“**SFC**”) under the Securities and Futures Ordinance. The Rules impose monitoring and reporting obligations with regard to large open positions. Where you are holding a reportable position for your client, you must disclose the identity of the client. For the purposes of the Rules, a client is the person who is ultimately responsible for originating instructions you receive for transactions - i.e., the transaction originator.

Further guidance on the Rules and what they require is set out in the SFC’s Guidance Note on Position Limits and Large Open Position Reporting Requirements. Copies of the Rules and Guidance Note can be downloaded from the SFC’s website ([www.sfc.hk](http://www.sfc.hk)).

#### **Purpose of the Rules**

The purpose of the Rules is to avoid potentially destabilizing market conditions arising from an over-concentration of futures/options positions accumulated by a single person or group of persons acting in concert, and to increase market transparency.

Some of the major requirements of the Rules and Guidance Note are summarised below. However, you should review the Rules and Guidance Note in their entirety, and consult with your legal counsel in order to ensure that you have a full understanding of your obligations in connection with trading in Hong Kong.

Please note that the Rules make you responsible for ensuring that you comply with the Rules. Section 8 of the Rules makes it a criminal offence not to comply (subject to a maximum fine of HK\$100,000 and imprisonment for up to 2 years).

In 2004, the SFC investigated 6 breaches of the Rules, including a breach by a non-Hong Kong fund manager which was referred to the fund manager’s overseas regulator. It should be noted that the SFC has expressly stated that it is not sympathetic to claims by overseas persons that they are not aware of the Hong Kong restrictions, and that a failure to trade within the limits or make reports reflects badly on a firm’s internal control measures (which might itself lead to disciplinary action).

#### **Position Limits**

The Rules say that you may not hold or control futures contracts or stock options contracts in excess of the prescribed limit, unless you have obtained the prior authorisation of the Hong Kong regulators. For example, the prescribed limit for Hang Seng Index futures and options contracts and Mini-Hang Seng Index futures and options contracts is 10,000 long or short position delta limit for all contract months combined, provided the position delta for the Mini-Hang Seng Index futures contracts or Mini-Hang Seng Index options contracts shall not at any time exceed 2,000 long or short for all contract months combined. For many futures contracts and stock options contracts, the position limit is set at 5,000 contracts for any one contract/expiry month.

The prescribed limit for each contract traded on the Hong Kong exchanges is set out in the Rules.

## Reportable Positions

If you hold or control an open position in futures contracts or stock options contracts in excess of the specified level, the Rules require you to report that position in writing to the relevant Hong Kong exchange (i) within one day (ignoring Hong Kong public holidays and Saturdays) of first holding or controlling that position, and (ii) on each succeeding day on which you continue to hold or control that position.

The specified reporting level for each contract traded on the Hong Kong exchanges is set out in the Rules. The report must state:

- (a) the number of contracts held or controlled in respect of the position in each relevant contract month; and
- (b) if the position is held or controlled for a client, the identity of the client, and the number of contracts held or controlled for such person in respect of the reportable position in each relevant contract month.

## Scope of the Rules

You should note:

- The prescribed limits and reportable position requirements apply to all positions held or controlled by any person, including positions in any account(s) that such person controls, whether directly or indirectly. The SFC takes the view that a person is regarded as having control of positions if, for example, the person is allowed to exercise discretion to trade or dispose of the positions independently without the day-to-day direction of the owner of the positions. (Section 4 of the Rules and Para. 2.6 of the Guidance Note)
- If a person holds or controls positions in accounts at more than one intermediary, the Rules require him to aggregate the positions for the purposes of applying the prescribed limits and reportable position requirements. (Para. 6.1 of the Guidance Note)
- The person holding or controlling a reportable position in accounts at more than one intermediary has the sole responsibility to notify the relevant exchange of the reportable position. The person may request its intermediary to submit the notice of the reportable position. If a firm agrees to submit the notice on his behalf, the person should provide to the firm its total positions held at other intermediaries so that the firm can submit the notice of the reportable position. Alternatively, the person should ask all of his intermediaries to report the positions in each of the accounts separately to the exchange, even if the positions in the individual accounts do not reach the reportable level. (Paras. 4.6 and 6.2 of the Guidance Note)
- Where you are holding a reportable position for your client, the Rules say that you must disclose the identity of the client. The SFC's view is that, for the purposes of the Rules, a client is the person who is ultimately responsible for originating the transaction instructions - i.e., the transaction originator. (Para. 6.4 of the Guidance Note)
- The Rules apply separately to the positions held by each of the underlying clients of an omnibus account, except where the omnibus account operator has discretion over the positions in which case the account operator must also aggregate these positions with his own positions. Positions held by different underlying clients should not be netted off for purposes of calculating and reporting reportable positions or determining compliance with the prescribed limits. (Para. 6.8 of the Guidance Note)

## **UNIFORM NOTIFICATION REGARDING ACCESS TO MARKET DATA**

As a market user you may obtain access to Market Data available through an electronic trading system, software or device that is provided or made available to you by a broker or an affiliate of such. Market Data may include, with respect to products of an exchange ("Exchange") or the products of third party participating exchanges that are traded on or through the Exchange's electronic trading platform ("Participating Exchange"), but is not limited to, "real time" or delayed market prices, opening and closing prices and ranges, high-low prices, settlement prices, estimated and actual volume information, bids or offers and the applicable sizes and numbers of such bids or offers.

You are hereby notified that Market Data constitutes valuable confidential information that is the exclusive proprietary property of the applicable exchange, and is not within the public domain. Such Market Data may only be used for your firm's internal use. You may not, without the written authorization of the applicable exchange, redistribute, sell, license, retransmit or otherwise provide Market Data, internally or externally and in any format by electronic or other means, including, but not limited to the Internet. Further, you may not, without the written authorization of the applicable exchange, use Exchange Market Data for purposes of determining any price, including any settlement price, for any futures product, options on futures product, or other derivatives instrument traded on any exchange other than an Exchange or a Participating Exchange; or in constructing or calculating the value of any index or indexed product. Additionally, you agree you will not, and will not permit any other individual or entity to, (i) use Exchange Market Data in any way so as to compete with an Exchange or to assist or allow a third party to compete with an Exchange; or (ii) use that portion of Exchange Market Data which relates to any product of a Participating Exchange in any way so as to compete with that Participating Exchange or to assist or allow a third party to compete with such Participating Exchange.

You must provide upon request of the broker through which your firm has obtained access to Market Data, or the applicable exchange, information demonstrating your firm's use of the Market Data in accordance with this Notification. Each applicable exchange reserves the right to terminate a market user's access to Market Data for any reason. You also agree that you will cooperate with an exchange and permit an exchange reasonable access to your premises should an exchange wish to conduct an audit or review connected to the distribution of Market Data.

NEITHER AN EXCHANGE, NOR ANY PARTICIPATING EXCHANGE, NOR THE BROKER, NOR THEIR RESPECTIVE MEMBERS, SHAREHOLDERS, DIRECTORS, OFFICERS, EMPLOYEES OR AGENTS, GUARANTEE THE TIMELINESS, SEQUENCE, ACCURACY OR COMPLETENESS OF THE DESIGNATED MARKET DATA, MARKET INFORMATION OR OTHER INFORMATION FURNISHED NOR THAT THE MARKET DATA HAVE BEEN VERIFIED. YOU AGREE THAT THE MARKET DATA AND OTHER INFORMATION PROVIDED IS FOR INFORMATION PURPOSES ONLY AND IS NOT INTENDED AS AN OFFER OR SOLICITATION WITH RESPECT TO THE PURCHASE OR SALE OF ANY SECURITY OR COMMODITY.

NEITHER AN EXCHANGE, NOR ANY PARTICIPATING EXCHANGE, NOR THE BROKER NOR THEIR RESPECTIVE MEMBERS, SHAREHOLDERS, DIRECTORS, OFFICERS, EMPLOYEES OR AGENTS, SHALL BE LIABLE TO YOU OR TO ANY OTHER PERSON, FIRM OR CORPORATION WHATSOEVER FOR ANY LOSSES, DAMAGES, CLAIMS, PENALTIES, COSTS OR EXPENSES (INCLUDING LOST PROFITS) ARISING OUT OF OR RELATING TO THE MARKET DATA IN ANY WAY, INCLUDING BUT NOT LIMITED TO ANY DELAY, INACCURACIES, ERRORS OR OMISSIONS IN THE MARKET DATA OR IN THE TRANSMISSION THEREOF OR FOR NONPERFORMANCE, DISCONTINUANCE, TERMINATION OR INTERRUPTION OF SERVICE OR FOR ANY DAMAGES ARISING THEREFROM OR OCCASIONED THEREBY, DUE TO ANY CAUSE WHATSOEVER, WHETHER OR NOT RESULTING FROM NEGLIGENCE ON THEIR PART. IF THE FOREGOING DISCLAIMER AND WAIVER OF LIABILITY SHOULD BE DEEMED INVALID OR INEFFECTIVE, NEITHER AN EXCHANGE, NOR ANY PARTICIPATING EXCHANGE, NOR THE BROKER, NOR THEIR RESPECTIVE SHAREHOLDERS, MEMBERS, DIRECTORS, OFFICERS, EMPLOYEES OR AGENTS SHALL BE LIABLE IN ANY EVENT,

INCLUDING THEIR OWN NEGLIGENCE, BEYOND THE ACTUAL AMOUNT OF LOSS OR DAMAGE, OR THE AMOUNT OF THE MONTHLY FEE PAID BY YOU TO BROKER, WHICHEVER IS LESS. YOU AGREE THAT NEITHER AN EXCHANGE, NOR ANY PARTICIPATING EXCHANGE, NOR THE BROKER NOR THEIR RESPECTIVE SHAREHOLDERS, MEMBERS, DIRECTORS, OFFICERS, EMPLOYEES OR AGENTS, SHALL BE LIABLE TO YOU OR TO ANY OTHER PERSON, FIRM OR CORPORATION WHATSOEVER FOR ANY INDIRECT, SPECIAL OR CONSEQUENTIAL DAMAGES, INCLUDING WITHOUT LIMITATION, LOST PROFITS, COSTS OF DELAY, OR COSTS OF LOST OR DAMAGED DATA.



## **CME DISCLOSURE ON PAYMENT FOR ORDER FLOW**

When firms provide execution services to customers, either in conjunction with clearing services or in an execution only capacity, they may, in some circumstances, direct orders to unaffiliated market makers, other executing firms, individual floor brokers or floor brokerage groups for execution. When such unaffiliated parties are used, they may, where permitted, agree to price concessions, volume discounts or refunds, rebates or similar payments in return for receiving such business. Likewise, on occasion, in connection with exchanges that permit pre-execution discussions and “off-floor” transactions such as block trading, exchanges of physicals, swaps or options for futures or equivalent transactions, a counterparty solicited to trade opposite customers of an executing firm may make payments described above and/or pay a commission to the executing firm in connection with that transaction. This could be viewed as an apparent conflict of interest. In order to determine whether transactions executed for your account are subject to the above circumstances, please contact your executing firm account representative.

# A GUIDE TO THE STRUCTURE AND MARKET TERMINOLOGY OF THE LONDON METAL EXCHANGE

## INTRODUCTION AND PURPOSE

This document is designed to provide customers of the London Metal Exchange (LME) with an overview of the structure of the LME, market terminology, and order execution. It is not a comprehensive trading guide, nor a complete guide to market terminology. Customers should always ensure that their requirements are explained in detail to the member responsible for order execution.

## THE LME

### Principal Nature

There are two types of contracts traded on the LME - Exchange Contracts and Client Contracts. Exchange Contracts are contracts between clearing members of the LME. Client Contracts are contracts between customers and ring dealing members (RDMs), or associate broker clearing members (ABCMs), or associate broker members (ABMs). Only RDMs, ABCMs and ABMs may issue Client Contracts. Open Position Statements issued to clients must state clearly **“THIS IS AN LME REGISTERED CLIENT CONTRACT”**. Contract criteria relating to LME contracts, including metal/plastic specifications, acceptable currencies, prompt dates, option strike prices for metals etc. are detailed in the LME rulebook and appropriate notices.

Exchange Contracts are traded between members, **matched** in the LME matching and clearing system (LMEMS) and margined by LCH.Clearnet (LCH). Client Contracts are **registered** at the LCH but margining arrangements are left to members to agree with their customers (subject to LME rules).

All LME contracts are between parties acting as principals. This prevents any party entering into an LME Contract as agent for someone else but does not prevent an agent effecting a contract between two parties if the resulting LME contract is between disclosed parties, each acting as a principal. It is an essential requirement of an LME Client Contract that one party must be an RDM, ABCM or ABM. A list of members is available from the LME, and on the LME website: [www.lme.com](http://www.lme.com). A principal relationship does not mean that members do not take on quasi-fiduciary responsibilities when they effect trades for customers. In particular, if a member undertakes to deliver a particular service, for example deal a specific number of lots 'in the Ring' (see below), then it should take care to ensure that it complies with all the terms of such a transaction.

In respect of Exchange Contracts, an LME broker buying metal or plastic under an Exchange Contract from another LME broker cannot do so as agent for his customer. Where an LME broker buys metal or plastic under an Exchange Contract with a view to selling that metal or plastic to his customer, this is achieved by entering into a back-to-back Client Contract with the customer. Brokers and customers can agree the conditions that apply to their Client Contracts. For example, a customer may make it a condition of his Client Contract that the broker must enter into a back-to-back Exchange Contract for the metal or plastic being bought or sold. This does not make the customer a party to the Exchange Contract but does create additional duties and obligations owed by the broker under the Client Contract.

Customers should be clear about conditions that apply to their Client Contracts and about the obligations and duties that the broker owes as a result of those conditions.

Brokers should be clear about the duties and obligations they owe as a result of conditions attaching to their Client Contracts. They should also be clear about the duties they owe to their customers under the FSA's Conduct of Business Rules (COB).

## **Dual Capacity**

LME members may act both in the capacity of market maker and broker. They may act in a particular manner depending on a number of circumstances, including the size of the order, the liquidity of the market at the time the order was placed, and, not least, the customer's instructions. Customer orders may be filled directly from a member's 'book' or following the purchase/sale of metal or plastic in the LME market. Furthermore, customer orders may be offset, amalgamated, broken-up or netted for execution. These methodologies apply equally to orders whether any resulting Exchange Contract is effected in the ring, in the inter-office market, or on LME Select.

Customers with specific order requirements must make these known to the member at the time the order is placed. Customers wishing to know how their order was executed should request such information from the member.

## **Trading on the LME**

Trading takes place on the LME by open outcry in the rings and kerbs, between members in the inter-office, and over the Exchange's electronic trading system LME Select.

## **Open Outcry**

Historically, during ring and kerb sessions, the majority of customer business reflects prices traded in the open outcry sessions. Customers can follow the market activity by monitoring quoted and traded prices disseminated via the LME market data system (MDS), or by listening to the simultaneous floor commentary provided by member(s). The MDS publishes prices traded during ring and kerb times on price vendor information services such as Reuters. Members can continue to 'make a market' when requested by a customer during the ring and kerb sessions, although this is entirely at the member's discretion. Alternatively, the customer can decide whether to place an order using the 'order styles' mentioned below.

## **Inter-office**

Inter-office trading is conducted between members by telephone or by electronic means. On contacting an LME member for a quote, customers will usually be provided with the member's current bid and offer. The customer may trade on this quote, call another member in an attempt to improve the quote, leave a resting order with a member, or wait and monitor prices on the LME market data system. If an order cannot be filled from the member's book, it may be executed via a back-to-back Exchange Contract agreed via a telephone deal with another member or executed via an electronic trading system.

## **LME Select**

LME Select allows members to trade LME futures contracts in metals and plastics, traded options and TAPOs, and an Index future and option. Some brokers offer their customers an order-routing facility via an API where they can view Select prices, execute trades, and place resting orders. All trading on LME Select is in US dollars.

LME Select replaces neither inter-office trading nor trading in the ring. Depending on the time of day, it is possible for members to deal by telephone or electronically in the inter-office, by LME Select, or in the rings. Customers should specify which mechanism their broker should use to effect an order, where they have a preference.

Firm prices of the best bid and offer available on LME Select, the total volumes available at these prices, and the price and volume of each trade transacted are distributed to and displayed in real time by information vendors. Only LME Select prices are displayed, not those of other third party electronic trading systems providing LME prices. Only RDMs and ABCMs are eligible to become LME Select Participants and to have direct access to the system. Customers may effect back-to-back Client Contracts with RDMs and ABCMs based upon prices available on LME Select, whether on the telephone or via electronic order-routing systems.

## **ORDER STYLES**

### **Ring**

**Customer orders are not traded in the rings or kerbs**, so an order using the term 'in/on/during the ring/kerb' will be executed on the basis of the prices traded/quoted during the particular session. If a customer requires their order to be 'shown' or traded across the ring/kerb then they should make this requirement known to their executor, who may or may not accept this as a term of the order. The equivalent Exchange Contract for a customer order may not replicate its terms. As the customer is **not** a party to any Exchange Contracts i.e. those traded in open outcry between members in the ring/kerb sessions, in specifying ring/kerb, the customer is merely identifying a pricing mechanism. A member which undertakes to match a price traded in the ring/kerb is not necessarily undertaking that it will trade during that ring/kerb, only that it may do so. However, a customer may place an order with the specific request that the member trades an Exchange Contract replicating its order in the ring. In such circumstance the RDM can only trade this order by open outcry in the ring.

If a customer trades at the prevailing market quote proffered in the ring/kerb, their executor is not necessarily obliged to effect an Exchange Contract at the same price. This can lead to situations where the customer has traded at the prevailing market quote, without that same price trading in open outcry across the floor of the Exchange. However, if the instructions from the customer are to achieve a specific price i.e. close of ring 2, then this is the price that should be given, if that specific order is accepted.

### **Market**

In normal circumstances a market order is one executed on a timely basis at the prevailing market price. As mentioned above, at certain times of the business day, trading is taking place simultaneously in the ring or kerb, on LME Select, and in the inter-office market. Traditionally, when open outcry trading is in session, the market is defined by activity within the ring/kerb. At other times, the market is split between inter-office trading and trading on LME Select. During inter-office sessions, indicative quotes are available on the MDS; firm prices are available on LME Select and the LME Select page on information vendors' systems. The indicative prices might not be available to all parties.

### **Best**

Order styles on the LME using the word 'best' confer some discretion upon the members when executing the order, requiring them to use their 'best endeavours' on the customer's behalf. The extent of the discretion is fixed by the terms of the order. This type of order is distinct from 'best execution' as defined by the FSA.

Best orders may be executed both in rings/kerbs, inter-office and on LME Select. Inter-office trades rely upon the members' skill in determining the level of the market at any particular time. Best orders received during ring/kerb times may not result in the customer receiving the 'best' price achieved during the session if the price improves after the member has booked the metal or plastic intended to fill the order. At any given time, the best price on LME Select will be displayed on the system and by the information vendors. Customers should be aware that depending on market conditions, the best price may move during the period from when the order was placed and when it was executed.

### **Close**

Most orders placed 'on the close' are for either the close of the second ring (official LME prices) or the final kerb (closing prices). Both these prices are demonstrable because of the publication of official and closing prices. Closing prices for other sessions are harder to determine, although the LME does publish unofficial prices which are established at the close of the fourth ring. In all circumstances, customers and members need to agree the style of execution i.e. bid/offer, mean or traded price. Members may not always be able to guarantee execution (price or volume) due to prevailing market conditions. A closing price on LME Select is the last price traded before the system closes.

## **Open**

Customers placing orders to trade on the opening of a market session must provide clear instructions to the LME member which indicate how this order should be activated i.e. basis the opening bid/offer or basis the first trade in the session. Customers will also need to inform their executor of their requirements if the executor is unable to fill the order basis the 'opening' price in its entirety, due to market constraints such as insufficient liquidity. Customers may place orders with members for LME Select that can be placed into the system for activation when the market opens.

## **Resting Orders**

When placing resting orders such as 'good 'til cancelled' ('GTC', or any derivations thereof) or stop loss orders, customers should ensure that they are in agreement with their executor's definition of the 'trigger' point of the order. Usually, this is interpreted as being the point when the order price is seen to be trading in the market, but it is possible to request the order be activated when the order level is either bid or offered as appropriate, via the prevailing market quote. Stop loss orders become market orders when a trade, or a bid or an offer triggers the stop, with members then executing the order at the current market price.

It is possible for a customer not to receive a 'fill' on a resting order despite the 'trigger' point being 'touched'. This could be due to a number of circumstances such as order priority, illiquidity, prevailing market conditions etc. Whatever the reason, the executor should be able to provide the customer with a full explanation of why it was unable to fill the order.

Customers should be aware that resting orders might be activated during periods of illiquidity in the market. As previously mentioned, this could result in the trade not being filled, or for 'stop' orders, a worse fill than anticipated ('slippage'). Customers should ensure the executor is fully aware of their requirements regarding the execution of an order, and adheres to any limitations, especially if the customer is not in contact with the market/member when the trigger point is reached.

It is possible for customers to ask members to place resting orders in LME Select. Where the broker has an order routing system into Select, customers will be able to place orders more directly. The system accepts GTC and Good for Day (DAY) orders. DAY orders are automatically deleted from the system at close of trading.

## **Conclusion**

The above order styles do not represent all possible methods of order execution on the LME. Members and customers should ensure that orders are communicated in meaningful terms that deliver the required execution in accordance with LME rules.

For the purposes of this document these categories of members will be referred to as LME members, members or by the appropriate abbreviation

<sup>2</sup> TAPO traded average price option

<sup>3</sup> API Application Protocol Interface

## **DISCLOSURE STATEMENT ON FUTURES EXCHANGE OWNERSHIP INTERESTS AND INCENTIVE PROGRAMS**

You should be aware that your Futures Commission Merchant (“FCM”) or one or more of its affiliates may own stock of, or has some other form of ownership interest in, one or more U.S. or foreign exchanges and clearing houses that you may trade on or that may clear your trades. As a result, you should be aware that your FCM or its affiliate might receive financial benefits related to its ownership interest when trades are executed on such an exchange or cleared at such a clearing house.

In addition, futures exchanges from time to time have in place other arrangements that may provide members with volume or market making discounts or credits, may call for participating members to pre-pay fees based on volume thresholds or may provide other incentive or arrangements that are intended to encourage market participants to trade on or direct trades to that exchange. Your FCM, or one or more of its affiliates, may participate in and obtain financial benefits from such an incentive program.

You should contact your FCM directly if you would like to know whether it has an ownership interest in a particular exchange or clearing house, or whether it participates in any incentive program on a particular exchange or clearing house. You may also contact any particular futures exchange directly to ask if it has any such incentive program for member firms.

## **NOTICE REQUIRED PURSUANT TO CFTC RULE 190.10**

THIS STATEMENT IS FURNISHED TO YOU BECAUSE RULE 190.10(c) OF THE COMMODITY FUTURES TRADING COMMISSION REQUIRES IT FOR REASONS OF FAIR NOTICE UNRELATED TO MORGAN STANLEY'S CURRENT FINANCIAL CONDITION. YOU SHOULD KNOW THAT IN THE UNLIKELY EVENT OF MORGAN STANLEY'S BANKRUPTCY, PROPERTY, INCLUDING PROPERTY SPECIFICALLY TRACEABLE TO YOU, WILL BE RETURNED, TRANSFERRED OR DISTRIBUTED TO YOU, OR ON YOUR BEHALF, ONLY TO THE EXTENT OF YOUR PRO RATA SHARE OF ALL PROPERTY AVAILABLE FOR DISTRIBUTION TO CUSTOMERS. NOTICE CONCERNING THE TERMS FOR THE RETURN OF SPECIFICALLY IDENTIFIABLE PROPERTY WILL BE BY PUBLICATION IN A NEWSPAPER OF GENERAL CIRCULATION. THE CFTC'S REGULATIONS CONCERNING BANKRUPTCIES OF COMMODITY BROKERS CAN BE FOUND AT 17 CODE OF FEDERAL REGULATIONS PART 190.

## **DISCLOSURE TO AUSTRALIAN CLIENTS TRADING ICE FUTURES EUROPE PRODUCTS ON THE ICE PLATFORM**

All ICE Futures Europe members, including Morgan Stanley & Co. LLC, are required, prior to such members accepting the first order from a client domiciled or resident in Australia to deal on the ICE Platform, to disclose to the client the significant differences between trading derivatives on the ICE Platform and trading derivatives on an Australian-based market.

The ICE Platform is operated by ICE Futures Europe, a private company which is incorporated and has its principal place of business in the United Kingdom (“UK”). ICE Futures Europe is a holder of an Australian market licence (“AML”) granted by the Minister under the Corporations Act 2001 (Cwlth) (“Corporations Act”). It is registered as a foreign company with the Australian Securities and Investments Commission (ARBN 128 341 293).

ICE Futures Europe is a Recognised Investment Exchange in the United Kingdom. As such, the ICE Platform is regulated primarily under the regulatory regime of the United Kingdom. As a holder of an AML (as an overseas market operator) and a registered foreign company, ICE Futures Europe is also subject to certain requirements under the Corporations Act. ICE Futures Europe does not hold an Australian financial services licence.

The rights and remedies of, and compensation arrangements for, investors who acquire products offered on the ICE Platform may differ from the rights and remedies of, and compensation arrangements for, investors who acquire products offered on an Australian-based market. In addition, while the operating rules of ICE Platform generally deal with same kind of matters that the operating rules of an Australian-based market are required to deal with, ICE’s rules may not contain all the specific matters that rules of Australian-based markets are required to contain.

Australian investors who acquire products offered on the market may be subject to the effects of changes in currency exchange rates. All trades in ICE Futures Europe contracts are settled and cleared through ICE Clear Europe Limited (“ICE Clear”). ICE Clear is UK-based and recognised by the UK Financial Services Authority as a Recognised Clearing House. ICE Clear is regulated under the regulatory regime of the UK and is subject to UK laws. ICE Clear does not hold an Australian CS facility licence.



**DISCLOSURE OF  
FUTURES COMMISSION MERCHANT  
MATERIAL CONFLICTS OF INTEREST**

The purpose of this document is to provide you with information about some of the material conflicts of interest that may arise between you and Morgan Stanley & Co. LLC (“FCM” or “we”) in connection with FCM performing services for you with respect to futures, options on futures, swaps (as defined in the Commodity Exchange Act), forwards or other commodity derivatives (“Contracts”). Conflicts of interests can arise in particular when FCM has an economic or other incentive to act, or persuade you to act, in a way that favors FCM or its affiliates.

Under applicable law, including regulations of the Commodity Futures Trading Commission (“CFTC”), not all swaps are required to be executed on an exchange or swap execution facility (each, a “Trading Facility”), even if a Trading Facility lists the swap for trading. In such circumstances, it may be financially advantageous for FCM or its affiliate to execute a swap with you bilaterally in the over-the-counter market rather than on a Trading Facility and, to the extent permitted by applicable law, we may have an incentive to persuade you to execute your swap bilaterally.

Applicable law may permit you to choose the CFTC-registered derivatives clearing organization (“Clearing House”) to which you submit a swap for clearing. You should be aware that FCM may not be a member of, or may not otherwise be able to submit your swap to, the Clearing House of your choice. FCM consequently has an incentive to persuade you to use a Clearing House of which FCM or its affiliate is a member.

You also should be aware that FCM or its affiliate may own stock in, or have some other form of ownership interest in, one or more U.S. or foreign Trading Facilities or Clearing Houses where your transactions in Contracts may be executed and/or cleared. As a result, FCM or its affiliate may receive financial or other benefits related to its ownership interest when Contracts are executed on a given Trading Facility or cleared through a given Clearing House, and FCM would, in such circumstances, have an incentive to cause Contracts to be executed on that Trading Facility or cleared by that Clearing House. In addition, employees and officers of FCM or its affiliate may also serve on the board of directors or on one or more committees of a Trading Facility or Clearing House.

In addition, Trading Facilities and Clearing Houses may from time to time have in place other arrangements that provide their members or participants with volume, market-making or other discounts or credits, may call for members or participants to pre-pay fees based on volume thresholds, or may provide other incentives or arrangements that are intended to encourage market participants to trade on or direct trades to that Trading Facility or Clearing House. FCM or its affiliate may participate in and obtain financial benefits from such incentive programs.

When we provide execution services to you (either in conjunction with clearing services or in an execution-only capacity), we may direct orders to affiliated or unaffiliated market-makers, other executing firms, individual brokers or brokerage groups for execution. When such affiliated or unaffiliated parties are used, they may, where permitted, agree to price concessions, volume discounts or refunds, rebates or similar payments in return for receiving such business. Likewise, where permitted by law and the rules of the applicable Trading Facility, we may solicit a counterparty to trade opposite your order or enter into transactions for its own account or the account of other counterparties that may, at times, be adverse to your interests in a Contract. In such circumstances, that counterparty may make payments and/or pay a

commission to FCM in connection with that transaction. The results of your transactions may differ significantly from the results achieved by us for our own account, our affiliates, or for other customers. In addition, where permitted by applicable law (including, where applicable, the rules of the applicable Trading Facility), FCM, its directors, officers, employees and affiliates may act on the other side of your order or transaction by the purchase or sale for an account, or the execution of a transaction with a counterparty, in which FCM or a person affiliated with FCM has a direct or indirect interest, or may effect any such order with a counterparty that provides FCM or its affiliates with discounts related to fees for Contracts or other products. In cases where we have offered you a discounted commission or clearing fee for Contracts executed through FCM as agent or with FCM or its affiliate acting as counterparty, FCM or its affiliate may be doing so because of the enhanced profit potential resulting from acting as executing broker or counterparty.

FCM or its affiliate may act as, among other things, an investor, research provider, placement agent, underwriter, distributor, remarketing agent, structurer, securitizer, lender, investment manager, investment adviser, commodity trading advisor, municipal advisor, market maker, trader, prime broker or clearing broker. In those and other capacities, FCM, its directors, officers, employees and affiliates may take or hold positions in, or advise other customers and counterparties concerning, or publish research or express a view with respect to, a Contract or a related financial instrument that may be the subject of advice from us to you. Any such positions and other advice may not be consistent with, or may be contrary to, your interests or to positions which are the subject of advice previously provided by FCM or its affiliate to you, and unless otherwise disclosed in writing, we are not necessarily acting in your best interest and are not assessing the suitability for you of any Contract or related financial instrument. Acting in one or more of the capacities noted above may give FCM or its affiliate access to information relating to markets, investments and products. As a result, FCM or its affiliate may be in possession of information which, if known to you, might cause you to seek to dispose of, retain or increase your position in one or more Contracts or other financial instruments. FCM and its affiliate will be under no duty to make any such information available to you, except to the extent we have agreed in writing or as may be required under applicable law.

### **Derivatives Client Clearing Policy**

FCM's derivatives clearing business is highly competitive. The OTC Derivative Client Clearing department decides whether to accept a prospective client for derivatives clearing based on various factors which may include, among others: (1) the credit worthiness of the prospective client; (2) the prospective client's market activities, including without limitation the expected volume of trades for clearing and the risk to FCM associated with those trades; (3) the availability of resources to clear trades for clients; (4) the nature of the prospective client's current relationship with FCM; and (5) the completion of appropriate account documentation.

FCM sets price levels for derivatives clearing based on a variety of factors including without limitation the credit worthiness of the prospective client and the expected volume of the trades for clearing. FCM may also consider the prospective client's overall trading relationship with Morgan Stanley, including without limitation its existing or potential contribution to the firm's overall revenue.

## **DISCLOSURE FOR CLEARED SWAPS CUSTOMERS**

### **Default of a Non-Clearing Futures Commission Merchant**

Morgan Stanley & Co. LLC (“Morgan Stanley”) may not be a clearing member of the registered derivatives clearing organization (“DCO”) that you select to clear the Cleared Swaps (as defined under CFTC Rule 22.1) that you may enter into. In such circumstances, Morgan Stanley, in the capacity of a “Depositing Futures Commission Merchant” (as defined under CFTC Rule 22.1), will enter into an agreement with a clearing member (in the capacity of a “Collecting Futures Commission Merchant,” as defined under CFTC Rule 22.1) of such DCO that is registered with the CFTC as a futures commission merchant (the “Collecting FCM”), pursuant to which Morgan Stanley will maintain an omnibus account of behalf of all of its Cleared Swaps Customers (“Omnibus Account”).

In the event that Morgan Stanley ever enters into such an arrangement, you have the right under CFTC Rule 22.16 to require Morgan Stanley to disclose the provisions of the customer agreement between the Collecting FCM and Morgan Stanley, on the basis of which Morgan Stanley would intermediate Cleared Swaps for you through such an Omnibus Account. Specifically, you have the right to require that Morgan Stanley disclose the provisions of any such agreement relating to the use of Cleared Swaps Customer Collateral (as defined under CFTC Rule 22.1), transfer, neutralization of the risks, or liquidation of Cleared Swaps in the event of a default by either Morgan Stanley or the Collecting FCM. Please contact your Morgan Stanley representative for additional information relating to clearing arrangements in respect of your Cleared Swaps Customer Account at Morgan Stanley.

### **Default of a Clearing Futures Commission Merchant**

Each DCO is required to have rules that govern the use of Cleared Swaps Customer Collateral, and the transfer, neutralization of risks, and liquidation of Cleared Swaps in the event of a default by a clearing futures commission merchant relating to a Cleared Swaps Customer Account.

In further compliance with CFTC Rule 22.16, we are providing you with the URL links to the rules of the relevant derivatives clearing organizations. Please note that such rules and the URL links are susceptible to change. If you encounter difficulty accessing these rules, please contact your Morgan Stanley Representative for an updated URL link.

<http://www.cmegroup.com/rulebook/CME/index.html>

[https://www.theice.com/publicdocs/clear\\_credit/ICE\\_Clear\\_Credit\\_Rules.pdf](https://www.theice.com/publicdocs/clear_credit/ICE_Clear_Credit_Rules.pdf)

[http://www.lch.com/rules\\_and\\_regulations/ltd/default.asp](http://www.lch.com/rules_and_regulations/ltd/default.asp)

THE INCLUSION OF A DERIVATIVES CLEARING ORGANIZATION ON THIS LIST DOES NOT MEAN THAT YOUR ACCOUNT IS ELIGIBLE TO CLEAR ANY OR ALL PRODUCTS ON THAT DERIVATIVES CLEARING ORGANIZATION. SHOULD YOU REQUIRE ADDITIONAL INFORMATION OR HAVE ANY QUESTIONS CONCERNING THE ABOVE, PLEASE CONTACT YOUR MORGAN STANLEY REPRESENTATIVE.

**REQUIRED DISCLOSURE TO END-USERS OF LCH.CLEARNET  
SWAPCLEAR CLIENT CLEARING SERVICES**

Morgan Stanley hereby directs Customer to the Notice to End-users of FCM SwapClear Clearing Services published by LCH.Clearnet Limited (“LCH”) on LCH’s website:

[http://www.lchclearnet.com/swaps/swapclear\\_for\\_clients/swapclear\\_clearing\\_end\\_user\\_notice.asp](http://www.lchclearnet.com/swaps/swapclear_for_clients/swapclear_clearing_end_user_notice.asp)

## **REQUIRED DISCLOSURE TO CUSTOMERS CLEARING SWAPS AND SECURITY-BASED SWAPS UNDER AN APPROVED PORTFOLIO MARGIN PROGRAM**

The following disclosure is provided in accordance with certain requirements applicable to Morgan Stanley & Co. LLC (“Morgan Stanley”), in its capacity as a jointly registered broker-dealer and futures commission merchant, under the terms of an Order of the Securities and Exchange Commission, set forth in SEC Release No. 34-68433, dated December 14, 2012, entitled Order Granting Conditional Exemptions under the Securities Exchange Act of 1934 (“Exchange Act”) in Connection with Portfolio Margining of Swaps and Security-Based Swaps, granting conditional exemptive relief from compliance with certain provisions of the Exchange Act in connection with a program to commingle and portfolio margin customer positions in cleared credit default swaps (“CDS”), which include both swaps and security-based swaps (any such portfolio margined CDS, “PM CDS”), in a segregated account established and maintained in accordance with Section 4d(f) of the Commodity Exchange Act (“CEA”).

Customer acknowledges and understands that Customer’s money, securities, and property held by Morgan Stanley in connection with Customer’s transactions in CDS or PM CDS (i) will be held in an account maintained in accordance with the segregation requirements of Section 4d(f) of the CEA; (ii) will be subject to protections set forth under Subchapter IV of Chapter 7 of Title 11 of the United States Code and the rules and regulations promulgated thereunder as Part 190 of the rules of the Commodity Futures Trading Commission; and (iii) will not be subject to the broker-dealer segregation requirements of Section 15(c)(3) and Section 3E of the Exchange Act and the rules thereunder, or to any customer protections under the Securities Investor Protection Act of 1970 and the stockbroker liquidation provisions of the U.S. Bankruptcy Code.

# Morgan Stanley & Co. LLC Clearing Member Disclosure in relation to Futures and Cleared Swaps Customer Clearing Services under the European Market Infrastructure Regulation

Morgan Stanley

## Who should read this document and why?

This document should be reviewed by clients who are domiciled in a European Union (“EU”) jurisdiction whose futures or cleared swaps are cleared by Morgan Stanley & Co. LLC (“MS&Co.”) on an EU-domiciled central counterparty (an “EU CCP”) authorised under the European Market Infrastructure Regulation (“EMIR”). This document contains important information for clients entitled to choose between what EMIR refers to as omnibus and individual segregation for each such EU CCP, and should be reviewed by clients prior to making any election in that regard. Clients should also review information provided by such EU CCPs regarding their segregation offerings, which include further information on the legal and other implications of relevant segregation models and applicable insolvency laws – links to such information have been included below.

## What are the segregation requirements of EMIR?

As a registered futures commission merchant (“FCM”), MS&Co. is subject to the customer asset protection regime established under the Commodity Exchange Act, as amended (“CEA”), and the rules promulgated thereunder by the US Commodity Futures Trading Commission (“CFTC”) (collectively, “US Law”). As a clearing member of LCH.Clearnet Ltd. and ICE Clear Europe, both EU CCPs that are or in due course will be authorised under EMIR, MS&Co. is also subject to the customer asset protection regime established in the EU pursuant to EMIR.

In order to comply with its obligations as a clearing member under EMIR, MS&Co. is required to:

- offer you a choice of an individual customer account or an omnibus customer account; and
- publicly disclose the levels of protection, the costs, and the main legal implications associated with different levels of segregation.

As described in more detail below, MS&Co. intends to satisfy its obligations under EMIR by:

- offering you a choice between individual client segregation with its affiliate, Morgan Stanley & Co. International plc (“MSIP”), and omnibus client segregation, in accordance with the requirements of US Law, with MS&Co;
- disclosing the level of protection and the main legal implications associated with omnibus client segregation under US Law and referring you in turn to MSIP’s EMIR disclosure for (i) a description of the level of protection and the main legal implications associated with individual client segregation established with MSIP; and (ii) an overview of the main implications of the different levels of segregation available through MSIP; and
- disclosing the factors relating to costs associated with the different levels of segregation.

## Individual and Omnibus segregated accounts under EMIR and US Law

EMIR requires that a CCP offer to its clearing members, and that each clearing member offer to its EU-domiciled clients, the option of keeping records and accounts at the CCP that either distinguish the assets and positions of the clearing member from such clearing member’s clients (omnibus client segregation) or that distinguish the assets and positions held for the account of a client from those held for the account of other clients, as well as the accounts of the clearing member (individual client segregation). If a client

elects individual client segregation, EMIR also provides that such client's positions and assets (i) must be recorded in an account separate from other client accounts, (ii) may not be netted with any positions in any other house or client account, and (iii) may not be exposed to losses attributable to any other house or client account. **MS&Co. may not, consistent with its obligations as a registered FCM under US Law, offer to establish individual client segregation on its books and records; accordingly, the offer made herein to establish such an account is an introduction to its UK affiliate MSIP and to the offering made by MSIP of a choice between omnibus or individual segregated accounts for derivatives cleared by MSIP on the EU CCPs of which it is a clearing member.**

MS&Co.'s offer to introduce its EU-domiciled clients to MSIP, and MSIP's segregation offering constitute an ongoing offer in respect of any EU CCPs on which MS&Co. clears derivatives transactions for EU-domiciled clients, subject to EMIR. Currently the offer extends to MS&Co.'s clearing arrangements on LCH.Clearnet Ltd. and ICE Clear Europe, but may extend as well to any EU CCP of which MS&Co. becomes a clearing member in the future. By accessing the link below, clients will continue to have access to relevant information regarding this ongoing offer, and EU CCPs for which MS&Co. and MSIP provide derivatives clearing services.

If you wish to be introduced to a representative of MSIP in order further to discuss MSIP's segregation offerings under EMIR, please speak to your usual Morgan Stanley contact. MSIP's individual client segregation offering is further described at this link:

<http://www.morganstanley.com/institutional/sales/derivatives.html>

Please note the following important qualification relating to MSIP's ability to offer individual client segregation for certain energy contracts listed for trading on ICE Futures US (which clear on ICE Clear Europe) and Nodal Exchange (which clear on LCH.Clearnet Ltd.). Both ICE Futures US and Nodal Exchange are CFTC-registered designated contract markets ("DCM"). Currently under US Law a direct offering of clearing services for DCM-executed futures contracts must be made through a registered FCM, which, as noted, is not permitted to offer or maintain individual client segregation. Accordingly, under the current constraints of US Law (and subject to any regulatory developments that may change those constraints), MSIP's offering of individual client segregation to clients introduced by MS&Co. to MSIP hereunder would not extend to DCM-executed contracts listed on ICE Futures US or Nodal Exchange. To the extent those constraints change in the future, this offer will extend to those DCM's, as well.

#### **Omnibus Client Segregation under US Law**

As a registered FCM MS&Co. must keep customer cash, securities, and other property ("customer funds") provided to MS&Co. to margin or guarantee futures and cleared swap client transactions segregated from MS&Co.'s own funds. Depending on the purpose for which such funds are received, customer funds deposited with MS&Co. are allocated to (i) customer segregated accounts for U.S. futures and options on futures; (ii) customer cleared swaps accounts; or (iii) customer foreign futures and options on futures "secured amount" accounts (each, and collectively, "customer segregated accounts"). Customer funds required to be held in one type of customer segregated account may not be commingled with funds required to be held in another type of customer segregated account (except as specifically authorized under applicable law or by the CFTC). Customer segregated accounts under US Law are a form of omnibus client segregation that complies the requirements of EMIR. But under US Law, such omnibus client segregation is the only form of client segregation available from a registered FCM. **Accordingly, the only way permissible under the current constraints of US Law that a registered FCM can offer an alternative to such omnibus client segregation pursuant to EMIR is by way of an introduction to an EU-regulated dealer that is not a registered FCM.**

Following is a general description of omnibus client segregation under US Law, for futures traded on US futures exchanges, as well as cleared swaps cleared on derivatives clearing organizations registered with the CFTC.

## Omnibus Client Segregation for DCM-Executed Futures

- Customer funds provided to MS&Co. to margin or guarantee futures or options on futures traded on US futures exchanges must be deposited by MS&Co. in a customer segregated account held at a U.S bank or trust company, a clearing organization, or another FCM. Funds attributable to multiple customers may be commingled in a single account at a bank or trust company or other permitted custodian; however, customer funds attributable to one customer may not be used to meet the obligations of MS&Co. or of any other person, including another customer.
- Customer funds held to margin US futures must be held in an account with a name that clearly identifies the funds as customer funds and shows that the funds are segregated as required under US Law. An FCM is required to obtain written acknowledgements from each depository with which it custodies customer funds that the depository was informed that such customer funds belong to customers. The depository must acknowledge that it cannot use any portion of such customer funds to satisfy any obligations that the FCM may owe the depository. A copy of the letter must be filed with the CFTC and the FCM's designated self-regulatory organization ("DSRO"). The depository must agree that it will reply promptly and directly to any request for confirmation of account balances or any other information regarding or related to the customer segregated account from authorized members of the CFTC staff, or an appropriate representative of the FCM's DSRO. In addition, the depository will provide the CFTC with the technological capability to obtain direct, read-only access to account and transaction information. Separately, DSRO rules require each FCM to instruct each depository that holds customer funds, whether located in the US or outside the US, to confirm to the DSRO all account balances daily.
- MS&Co. is required, on each business day, to calculate its segregation requirement for each segregated customer account and to submit (on the next following business day) to the CFTC and to CME (as its DSRO) a report that sets out (i) the total amount of customer funds required to be held in each segregated customer account origin, (ii) the amount of such customer funds actually held in each segregated customer account origin, and (iii) its residual interest in each segregated customer account origin. In the event that the total amount of funds in a customer segregated account origin is less than the required amounts, MS&Co. would be required to give immediate notice of that fact to the CFTC, NFA, CME (as its DSRO) and other exchanges and clearing houses on which MS&Co. transacts as a member.
- To ensure that it is continuously in compliance with its segregation requirements, an FCM is required to deposit a portion of its own funds in each customer segregated account as a buffer. These excess funds represent MS&Co.'s "residual interest" in each segregated account. Residual interest funds are held for the exclusive benefit of MS&Co.'s customers while held in a segregated customer account. MS&Co. is required to have written policies and procedures regarding the establishment and maintenance of a targeted residual interest in each of the three segregated customer account origins. In establishing that targeted amount, the MS&Co. senior management have taken into consideration a number factors, including: (i) the nature of MS&Co.'s customers, their general creditworthiness, and their trading activity; (ii) the type of markets and products traded by those customers, as well as by MS&Co. for its own account; (iii) the general volatility and liquidity of those markets and products; (iv) MS&Co.'s own liquidity and capital needs; and (v) historical trends in balances and customer debits in each customer segregated account.
- An FCM is required to notify the CFTC and its DSRO immediately whenever the amount of residual interest in any segregated customer account falls below the FCM's targeted residual interest for such customer account. In addition, certain restrictions and conditions apply to an FCM's ability to withdraw funds comprising its residual interest from any segregated customer account. Specifically, an FCM must file a regulatory report of any withdrawal of funds from a customer segregated account that exceeds 25 percent of the FCM's residual interest in that account, and any such withdrawal must be pre-approved in writing by a senior financial officer of the FCM.



## Omnibus Segregation for Cleared Swaps

Under US Law, customer funds are subject to differing regimes depending on the type of product traded. The regulatory regime for the protection of cleared swaps collateral held for cleared swaps customers, commonly referred to as “LSOC” (an acronym for “legally segregated, operationally commingled”) is set out in Part 22 of the CFTC’s rules. For purposes of EMIR, the regime established under Part 22 is an omnibus segregated account regime.

Part 22 implements section 4d(f) of the CEA, which provides that an FCM treat and deal with the money, securities and property of any swaps customer received to margin a swap cleared by or through a DCO as belonging to such customer. Such cleared swaps customer collateral must be separately accounted for and not commingled with the funds of the FCM or be used to margin contracts of any person other than the person for whom the same are held.

Section 4d(f) further provides that an FCM’s cleared swaps customers collateral may be commingled and deposited in the same account or accounts, i.e., an omnibus account, with a bank or trust company or a DCO that clears cleared swaps customers positions on behalf of the FCM. It is unlawful for any person, including a bank or trust company or a DCO receiving cleared swaps customer collateral to hold such collateral as belonging to the depositing FCM or any person other than the swaps customer of the FCM.

Although cleared swap customer positions and collateral may be held in the same omnibus account, Part 22 requires each FCM and DCO to maintain books and records that identify the positions of, and the market value of the collateral posted by, each customer in order that, in the event of a customer default, the collateral of a non-defaulting customer is not exposed to losses attributable to the defaulting customer.

### **Risk Disclosure Relating to Omnibus Client Segregation Under US Law**

Under US Law a defaulting clearing member FCM is liquidated in accordance with the commodity broker liquidation provisions of the Bankruptcy Code and Part 190 of the CFTC’s rules. Among other requirements, the Part 190 rules instruct the trustee in bankruptcy to attempt to effect a transfer of customer accounts holding commodity contracts (futures and cleared swaps), together with the customer funds margining such commodity contracts. The Part 190 rules further provide that, if the FCM’s customer accounts cannot be transferred in their entirety, the trustee may effect a partial transfer of all customer accounts or of an individual customer account. The Code also sets forth special priority rules for distribution of property to futures customers and exceptions to the automatic stay and voidability provisions of the Code. The Code affords claims of public customers of the FCM (that is, customers of the FCM that are not affiliates of the FCM) the highest priority, subject only to the payment of claims relating to the administration of the FCM estate. However, where there is a shortfall in customer funds, customers participating in the relevant account class would be subject to a haircut based on a pro-rata distribution of customer property available in such account class, in accordance with the requirements of section 766 of the Code.

Under the LSOC model of segregation that applies under US Law to customer cleared swaps, FCMs and DCOs must segregate in its books and records the cleared swaps of each individual customer and relevant collateral. FCMs and DCOs must ensure that such entries are separate from entries indicating (i) FCM or DCO obligations, or (ii) the obligations of non-cleared swaps customers. Operationally, however, each FCM and DCO is permitted to commingle cleared swap customer collateral in a single account. FCMs and DCOs must further ensure that any such commingled account is separate from any account holding FCM or DCO property or holding property belonging to non-cleared swaps customers.

LSOC is intended to ensure that neither FCM nor DCO ever uses the collateral of one cleared swaps customer to support the obligations of another customer, by ensuring that the value of the cleared swaps customer collateral

that the DCO holds equals or exceeds the value of all cleared swaps customer collateral that it has received to secure the contracts of the FCM's customers. Following an FCM clearing member's default, the DCO would be permitted to access the collateral of any defaulting cleared swaps customers, but not the collateral of non-defaulting cleared swaps customers. Nevertheless, even under LSOC, Section 766(h) of the Code requires the pro rata distribution of customer property. Accordingly, in the event that losses among cleared swaps customers were so great that the FCM was unable to meet the shortfall with its own assets and defaulted, a cleared swaps customer could be exposed to losses of other customers.

It is important to note that the CFTC has emphasized its intent that any defaulting FCM carrying cleared swaps customer collateral must be liquidated in accordance with the US Bankruptcy Code and the CFTC's rules. This is the case even if the DCO is located outside of the US and also subject to the laws of another jurisdiction. Consequently, even if individual client segregated accounts were available, such accounts would not provide any additional protection in the event of the bankruptcy of a clearing FCM.

### **Disclosure relating to Costs**

Article 38(1) of EMIR requires that CCPs and their clearing members disclose the prices and fees associated with the services they offer. Information relating to the factors which affect fees and prices for clearing derivatives through MSIP, and the costs associated with an offering of omnibus client segregation and individual client segregation through MSIP, is available at this link:

<http://www.morganstanley.com/institutional/sales/derivatives.html>

### **Other information**

A summary setting forth the EU CCPs on which MSIP offers to its clients the clearing of swaps or listed derivatives, and the types of account which MSIP will offer from the date of the relevant CCP's EMIR authorization, is available at this link:

<http://www.morganstanley.com/institutional/sales/derivatives.html>

Set forth below are links to additional information relating to EU CCP segregation models, and the segregation choices offered by MSIP.

Please note that these links have been included for convenience only. If any of them do not work, you should contact the relevant EU CCP directly. Some EU CCPs have not yet published their disclosure documents but will be required to do so from the time of authorisation under EMIR. This document will be updated when those disclosures are published.

We are not responsible for, and do not accept any liability whatsoever for, any content or omissions or inaccuracies contained in the information produced by any EU CCP.

Nasdaq OMX:

<http://www.nasdaqomx.com/europeanclearing/accounts>

Eurex Clearing AG:

<http://www.eurexclearing.com/clearing-en/risk-management/client-assetprotection/143894/>

LCH Clearnet Limited:

[http://www.lchclearnet.com/about\\_us/corporate\\_governance/ltd\\_account\\_structures\\_and\\_er\\_emir.asp](http://www.lchclearnet.com/about_us/corporate_governance/ltd_account_structures_and_er_emir.asp)

LCH Clearnet SA:

[http://www.lchclearnet.com/about\\_us/corporate\\_governance/sa\\_account\\_structures\\_and\\_er\\_emir.asp](http://www.lchclearnet.com/about_us/corporate_governance/sa_account_structures_and_er_emir.asp)

ICE Clear Europe:

[https://www.theice.com/clear\\_europe.jhtml](https://www.theice.com/clear_europe.jhtml)

CME EU:

<http://www.cmegroup.com/europe/>

CC&G:

<http://www.ccg.it/jportal/pcontroller/NavigatorHandler?nodo=124594>

European Commodity Clearing AG:

<http://www.ecc.de/en/risk-management/emir>

May 1, 2013

To all account managers and trading advisors of our clients:

We are writing to inform you of a new regulation adopted by the CFTC which affects our futures clearing relationship and comes into effect on June 1, 2013.

**In April 2012, the CFTC adopted Regulation 1.73, prescribing certain risk management requirements applicable to both futures commission merchants that are clearing members of U.S. futures clearing houses and account managers who execute “bunched orders” on behalf of their clients.**

Morgan Stanley & Co. LLC, acting as a clearing futures commission merchant to your clients, is a clearing member of several U.S. futures clearing houses and, as such, is subject to Regulation 1.73. You, acting as an “account manager” with discretionary authority to control trading in the futures accounts of your clients, are thereby also subject to Regulation 1.73.

More specifically, paragraph (a)(2)(v)(B) of Regulation 1.73 requires a clearing member futures commission merchant – such as Morgan Stanley – to establish risk limits for each of its customers that trades through an account manager on a bunched order basis, and enter an agreement with the account manager under which the account manager is required to screen such bunched orders for compliance with those risk limits. (We’ve attached the text of the relevant excerpt of Regulation 1.73.)

Morgan Stanley has determined to rely for purposes of Regulation 1.73 compliance on the risk limits set forth in the attached schedule. You’ll see that the risk limits we propose are maximum quantity order limits that already apply per order as mandated by the rules and procedures of the designated contract markets on which you execute for your customers. We believe that reliance on these limits, as a systemic control already in place in the industry for risk management purposes, offers the simplest course available for achieving Regulation 1.73 compliance.

**We ask that you acknowledge this letter and return it to us. In doing so, you acknowledge, in your capacity as an “account manager” within the meaning of Regulation 1.73, that you have agreed with Morgan Stanley to screen orders for compliance with the limits set forth on the attached schedule.**

**Alternatively, you may do nothing, and if we do not hear from you by close of business on May 15, 2013, we will deem you to have made the same acknowledgment. Finally, if you prefer, we would be happy to enter with you into a form of Consent Agreement for Account Manager to Screen for Customer Limits, which may be available on the FIA’s EGUS system.**

Please note that this letter does not, and is not intended to, amend the terms and conditions of, or alter the rights and liabilities of any party to: (i) any Commodity Futures Customer Agreement entered into by your customer or you, as account manager on behalf of your customer, and Morgan Stanley (an “Agreement”); or (ii) any International Uniform Brokerage Execution Services (“Give-Up”) Agreement: Trader Version to which you, as account manager (“Trader”), and Morgan Stanley (“Clearing Broker”) are parties (an “FIA GUA”). In the event of a conflict between the provisions of this letter and either an Agreement or an FIA GUA, the provisions of such Agreement or FIA GUA, as applicable, shall govern solely and entirely, without regard to the terms of this letter.

If you have questions, or require further assistance, please contact your Client Service Representative.

Sincerely,

MORGAN STANLEY & CO. LLC

**Acknowledged:**

Account Manager Name: \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

Date: \_\_\_\_\_

**SCHEDULE OF RISK LIMITS**

The following Risk Limits apply under the terms of this letter:

The Risk Limits shall be the per product maximum order size limits as adopted by the applicable designated contract market (“DCM”), as may be in effect from time to time under applicable DCM rules and procedures.

By way of example, please see the schedule of limits for CME Globex products, in force as of the date hereof, which is set forth in Column U (“Maximum Quantity”) of the CME Globex Product Reference Sheet, available here:

<http://www.cmegroup.com/confluence/display/EPICSANDBOX/GCC+Product+Reference+Sheet>

**EXCERPT FROM CFTC REGULATION 1.73** (full text available at: <http://www.ecfr.gov/cgi-bin/text-idx?c=ecfr&SID=adfea334d6055506be2e6630cd990e6e&rgn=div8&view=text&node=17:1.0.1.1.1.0.6.65&idno=17>)

a) Each futures commission merchant that is a clearing member of a derivatives clearing organization shall:...

(2) Screen orders for compliance with the risk-based limits in accordance with the following:

(v) When an account manager bunches orders on behalf of multiple customers for execution as a block and post-trade allocation to individual accounts for clearing:

(A) The futures commission merchant that initially clears the block shall establish risk-based limits for the block account and screen the order in accordance with paragraph (a)(2)(i) or (ii) as applicable;

(B) The futures commission merchants that clear the allocated trades on behalf of customers shall establish risk-based limits for each customer and enter into an agreement in advance with the account manager that requires the account manager to screen orders for compliance with those limits . . . .