Chapter 7

Client money rules

7.16 The standard methods of internal client money reconciliation

7.16.1 | G | (1) *Firms* are required to carry out an *internal client money reconciliation* each *business day* (■ CASS 7.15.12 R and ■ CASS 7.15.15R(1)) or as required by ■ CASS 7.15.15R(4) after a *primary pooling event*. This section sets out methods of reconciliation that are appropriate for these purposes (the *standard methods of internal client money reconciliation*).

(2) Where a *firm* establishes one or more *sub-pools*, the provisions of ■ CASS 7.16 (The standard methods of internal client money reconciliation) shall be read as applying to the *firm's general pool* and each *sub-pool* individually, in line with ■ CASS 7.19.3 R and ■ CASS 7.19.4 R.

7.16.2 | G | (1) A *non-standard method of internal client money reconciliation* is a method of *internal client money reconciliation* which does not meet the requirements of this section.

(2) Where a *firm* uses a *non-standard method of internal client money reconciliation* it is reminded that it must comply with the requirements in ■ CASS 7.15.18 R.

7.16.3 | G | Regardless of whether a *firm* is following one of the *standard methods of internal client money reconciliation* or a *non-standard method of internal client money reconciliation*, it is reminded that it must maintain its records so that it is able to promptly calculate the total amount of *client money* it should be holding for each *client* (see ■ CASS 7.15.15 R (1)).

7.16.4 | G | *Firms* are reminded that the *internal client money reconciliation* should achieve the purposes set out in ■ CASS 7.15.14 G.

7.16.5 | G | (1) A *firm* that adopts the normal approach to segregating *client money* (■ CASS 7.13.6 R) will be using the methods in this section to check whether it has correctly segregated *client money* in its *client bank accounts*.

(2) A *firm* that adopts the alternative approach to segregating *client money* (■ CASS 7.13.54 G) will be using the methods in this section to calculate how much *money* it needs to withdraw from, or place in, *client bank accounts* as a result of any discrepancy arising between its

client money requirement and its *client money resource* at the close
of business on the previous *business day*.

7.16.6 | G | Unless otherwise stated, *firms* are reminded that they are required to receive
all *client money* receipts directly into a *client bank account* (see
■ CASS 7.13.6 R).

7.16.7 | G | A *firm* that receives *client money* in the form of cash, a cheque or other
payable order is reminded that it must pay that *money* (eg, into a *client
bank account*) no later than on the *business day* after it receives the *money*
(see ■ CASS 7.13.32 R). Once deposited into a *client bank account*, that receipt
of *client money* should form part of the *firm's client money resource* (see
■ CASS 7.16.8 R). In calculating its *client money requirement*, a *firm* will need
to take into account any *client money* received as cash, cheques or payment
orders but not yet deposited into a *client bank account* (see
■ CASS 7.16.25 R (3) and ■ CASS 7.16.26 G).

Client money resource

7.16.8 | R | The *client money resource* is the aggregate balance on the *firm's client bank
accounts*.

7.16.9 | G | (1) A *firm* should ensure that the amount it reflects in its *internal client
money reconciliation* as its *client money resource* is equal to the
aggregate balance on its *client bank accounts*. For example, if:

(a) a *firm* holds *client money* received as cash, cheques or payment
orders but not yet deposited in a *client bank account* (in
accordance with ■ CASS 7.13.32 R); and

(b) that *firm* records all receipts from *clients*, whether or not yet
deposited with a bank, in its cashbook (see ■ CASS 7.16.26 G (1)(a));

its *client money resource* should not include the cash, cheques or
payment orders received but not yet deposited in a *client bank
account*.

(2) The *guidance* in (1) is consistent with a *firm's* obligations to maintain
its internal records in an accurate way, particularly their
correspondence to the *client money* held for *clients*.

Client money requirement

7.16.10 | R | Subject to ■ CASS 7.16.12 R, the *client money requirement* must be calculated
by one, but not both, of the following of two methods:

(1) the *individual client balance method* (■ CASS 7.16.16 R); or

(2) the *net negative add-back method* (■ CASS 7.16.17 R).

7.16.11 | R | The *net negative add-back method* may only be used, under this section, by
a *CASS 7 asset management firm* or a *CASS 7 loan-based crowdfunding firm*
and only if such *firms* do not undertake any *margined transactions* for, or on
behalf of, their *clients*.

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7.16.12 R A *CASS 7 loan-based crowdfunding firm* must not use the *individual client balance method* under this section.

7.16.13 G
(1) The *client money requirement* should represent the total amount of *client money* a *firm* is required to have segregated in *client bank accounts* under the *client money rules*.

(2) ■ CASS 7.16.11 R does not prevent a *firm* from adopting a *net negative add-back method* as part of a *non-standard method of internal client money reconciliation*.

(3) ■ CASS 7.16.12 R does not prevent a CASS loan-based crowdfunding firm from adopting the *individual client balance method* as part of a *non-standard method of internal client money reconciliation*.

(4) If a *firm* uses the *individual client balance method* in respect of some of its business lines and the *net negative add-back method* in respect of others it will be conducting a *non-standard method of internal client money reconciliation*.

7.16.14 G
(1) The *individual client balance method* (■ CASS 7.16.16 R) may be applied by any *firm* except a *CASS 7 loan-based crowdfunding firm*. This method requires a *firm* to calculate the total amount of *client money* it should be segregating in *client bank accounts* by reference to how much the *firm* should be holding in total (ie, across all its *client bank accounts* and businesses) for each of its individual *clients* for:

(a) *non-margined transactions* (■ CASS 7.16.16 R (1) and ■ CASS 7.16.21 R);

(b) *margined transactions* (■ CASS 7.16.16 R (2) and ■ CASS 7.16.32 R); and

(c) certain other matters (■ CASS 7.16.16 R (3) and ■ CASS 7.16.25 R).

(2) (a) ■ CASS 7.16.22 E is an *evidential provision* which sets out a method *firms* should use for calculating how much they should be holding in total for each individual *client* for *non-margined transactions*.

(b) The calculation in ■ CASS 7.16.22 E permits a *firm* to calculate either one *individual client balance* across all its products and business lines for each *client* or a number of *individual client balances* for each *client* equal to the number of products or business lines operated by the *firm* in connection with that *client* (see ■ CASS 7.16.22 E (1)).

(c) The calculation referred to in (2)(b) may also be applied by different types of *firms* and, as a result, each *firm* will need to apply the calculation in way which recognises the business model under which that *firm* operates.

7.16.15 G The *net negative add-back method* (■ CASS 7.16.17 R) is available to *CASS 7 asset management firms* and *CASS 7 loan-based crowdfunding firms*, many of whom may operate internal ledger systems on a bank account by bank account, not *client*-by-*client*, basis. This method allows a *firm* to calculate the

total amount of *client money* it is required to have segregated in *client bank accounts* by reference to:

(1) the balances in each *client bank account* (see ■ CASS 7.16.17 R (1) and ■ CASS 7.16.18 G (2));

(2) whether any individual *client's* net position in a specific *client bank account* is negative (see ■ CASS 7.16.17 R (2) and ■ CASS 7.16.18 G (2)); and

(3) certain other matters (see ■ CASS 7.16.17 R (2) and ■ CASS 7.16.25 R).

Client money requirement calculation: individual client balance method

7.16.16   R   Subject to ■ CASS 7.16.25 R and ■ CASS 7.16.37 R, under this method the *client money requirement* must be calculated by taking the sum of, for all *clients* and across all products and accounts:

(1) the *individual client balances* calculated under ■ CASS 7.16.21 R, excluding:

  (a) *individual client balances* which are negative (ie, debtors); and

  (b) *clients'* equity balances;

(2) the total *margined transaction requirement* (calculated under ■ CASS 7.16.32 R); and

(3) any amounts that have been segregated as *client money* according to the *firm's* records under any of the following: ■ CASS 7.13.51 R (1) (*prudent segregation record*), ■ CASS 7.13.66 R (*alternative approach mandatory prudent segregation record*) and/or ■ CASS 7.13.74 R (*clearing arrangement mandatory prudent segregation record*).

Client money requirement calculation: net negative add-back method

7.16.17   R   Subject to ■ CASS 7.16.25 R, under this method the *client money requirement* must be calculated by taking the sum of, for each *client bank account*:

(1) the amount which the *firm's* internal records show as held on that account; and

(2) an amount that offsets each negative net amount which the *firm's* internal records show attributed to that account for an individual *client*.

7.16.18   G   (1) A *firm* which utilises the *net negative add-back method* is reminded that it must do so in a way which allows it to maintain its records so that, at any time, the *firm* is able to promptly determine the total amount of *client money* it should be holding for each *client* (see ■ CASS 7.15.5 R (1)).

(2) For the purposes of ■ CASS 7.16.17 R, a *firm* should be able to readily use the figures previously recorded in its internal records and ledgers (for example, its cashbook or other internal accounting records) as at

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the close of business on the previous *business day* without undertaking any additional steps to determine the balances in the *firm's client bank accounts*.

7.16.19 ☐G (1) A *firm* which utilises the *net negative add-back method* may calculate its *client money requirement* and *client money resource* on a bank account by bank account basis;

(2) For the purposes of ■ CASS 7.16.17 R, a *firm* should take into account any amounts that have been segregated as *client money* according to the *firm's* records under either or both ■ CASS 7.13.50 R (*prudent segregation record*) and ■ CASS 7.13.66 R (*alternative approach mandatory prudent segregation record*).

Non-margined transactions (eg, securities): individual client balance

7.16.20 ☐G The sum of positive *individual client balances* for each *client* should represent the total amount of all *money* the *firm* holds, has received or is obligated to have received or be holding as *client money* in a *client bank account* for that *client* for *non-margined transactions*.

7.16.21 ☐R A *firm* must calculate a *client's individual client balances* in a way which captures the total amount of all *money* the *firm* should be holding as *client money* in a *client bank account* for that *client* for *non-margined transactions* under the *client money rules*.

7.16.22 ☐E (1) A *firm* may calculate either:

(a) one *individual client balance* for each *client*, based on the total of the *firm's* holdings for that *client*; or

(b) a number of *individual client balances* for each *client*, equal to the number of products or business lines the *firm* operates for that *client* and each balance based on the total of the *firm's* holdings for that *client* in respect of the particular product or business line.

(2) Each *individual client balance* for a *client* should be calculated in accordance with this table:

Individual client balance calculation	
Free *money* (sums held for a *client* free of sale or purchase (eg, see (3)(a)) and	A
sale proceeds due to the *client*:	
(a) for principal deals when the *client* has delivered the *designated investments*; and	B
(b) for agency *deals*, when:	
(i) the sale proceeds have been received by the *firm* and the *client* has delivered the *designated investments*; or	C1
(ii) the *firm* holds the *designated investments* for the *client*; and	C2
the cost of purchases:	

(c)   for principal deals, paid for by the *client* when   D
the *firm* has not delivered the *designated in-
vestments* to the client; and

(d)   for agency *deals*, paid for by the *client* when:

    (i)   the *firm* has not remitted the *money* to,   E1
    or to the order of, the counterparty; or

    (ii)   the *designated investments* have been   E2
    received by the firm but have not been
    delivered to the *client*;

Less

money owed by the *client* for unpaid purchases by,   F
or for, the *client* if delivery of those *designated invest-
ments* has been made to the *client*; and

proceeds remitted to the *client* for sales transactions   G
by, or for, the *client* if the *client* has not delivered
the *designated investments*.

Individual client balance 'X' = (A+B+C1+C2+D+E1+E2)-F-G   X

(3) When calculating an *individual client balance* for each *client*, a *firm*
should also:

(a) ensure it includes:

    (i) *client money* consisting of dividends received and interest
earned and allocated (see ■ CASS 7.11.32 R);

    (ii) *client money* consisting of dividends (actual or payments in
lieu), stock lending fees and other payments received and
allocated (see ■ CASS 6.1.2 G);

    (iii) *money* the *firm* appropriates and segregates as *client money*
to cover an unresolved *shortfall* in *safe custody assets* it
identifies in its internal records which is attributable to an
individual *client* (see ■ CASS 6.6.54R (2)); and

    (iv) *money* the *firm* segregates as *client money* instead of an
individual *client's safe custody asset* until such time as the
relevant delivery versus payment transaction settles under
■ CASS 6.1.12R (2); and

(b) deduct any amounts due and payable by the *client* to the *firm*
(see ■ CASS 7.11.25 R).

(4) Compliance with (1), (2) and (3) may be relied on as tending to establish
compliance with ■ CASS 7.16.21 R.

7.16.23   R   A *firm* must calculate an *individual client balance* using the contract value of
any *client* purchases or sales, being the value to which the *client* would be
contractual entitled to receive or contractually obligated to pay.

7.16.24   G   If a *firm* calculates each *individual client balance* on a product-by-product or
business line-by-business line basis under ■ CASS 7.16.22 E (1)(b), the result
should be that the *firm* does not net *client* positions across all products and
accounts.

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Other requirements for calculating the client money requirement

7.16.25 **R** When calculating the *client money requirement* under either of the methods in ■ CASS 7.16.10 R, a *firm* must:

(1) include any unallocated *client money* (see ■ CASS 7.13.36 R) and unidentified receipts of *money* it considers prudent to segregate as *client money* (see ■ CASS 7.13.37 R);

(2) include any money the *firm* appropriates and holds as *client money* to cover an unresolved *shortfall* in *safe custody assets* identified in its internal records which is not attributable, or cannot be attributed to, an individual *client* (see ■ CASS 6.6.49 R, ■ CASS 6.6.50 R and ■ CASS 6.6.54 R);

(3) take into account any *client money* received as cash, cheques or payment orders but not yet deposited into a *client bank account* under ■ CASS 7.13.32 R (see also ■ CASS 7.15.9 R);

(4) if it has drawn any cheques or other payable orders, to discharge its fiduciary duty to its *clients* and continue to treat the sum concerned as forming part of its *client money requirement* until the cheque or order is presented and paid by the bank (see ■ CASS 7.11.40 R); and

(5) ensure it has taken into account all *client money* the *firm* should be holding in connection with *clients' non-margined transactions*.

7.16.26 **G** (1) Under ■ CASS 7.16.25 R (3), where a *firm* holds *client money* received as cash, cheques or payment orders but not yet deposited in a *client bank account* under ■ CASS 7.13.32 R, it may:

(a) include these balances when calculating its *client money requirement* (eg, where the *firm* records all receipts from clients, whether or not yet deposited with a bank, in its cashbook); or

(b) exclude these balances when calculating its *client money requirement* (eg, where the *firm* only records client receipts to its cashbook once deposited with a bank).

(2) In line with (1)(a), the *firm* will need to ensure that, before finalising the calculation of its *client money requirement* within this section, it deducts these balances, to ensure that they do not give rise to a discrepancy between the *firm's client money requirement* and *client money resource* (see ■ CASS 7.15.29 R).

(3) In line with (1)(b), although the balances concerned do not form part of the *firm's client money requirement*, the *firm* must continue to account for all receipts of *client money* as cash, cheques or payment orders but not yet deposited in a *client bank account* in its records and accounts (see ■ CASS 7.13.32 R and ■ CASS 7.15.9 R).

7.16.27 **G** (1) In accordance with ■ CASS 7.16.25 R (5), where a *firm* has allowed another *person* to hold *client money* in connection with a *client's non-margined transaction* (eg, in a *client transaction account* under ■ CASS 7.14 (Client money held by a third party)), the *firm* should include these balances when calculating its *client money requirement*.

(2) If a *firm* is utilising the *individual client balance method*
(■ CASS 7.16.16 R) to calculate its *client money requirement*,
■ CASS 7.16.21 R requires the *firm* to include the sums its holds for each
client that are placed with another *person* in connection with a
client's non-margined transaction when calculating a *client's
individual client balance* (eg, see ■ CASS 7.16.22 E and items C1 and E2).

(3) Under (1) and (2), the *firm* will need to ensure that, before finalising
the calculation of its *client money requirement* within this section, it
deducts positive balances held for *clients* adding back negative
balances attributable to *clients' non-margined transactions* in *client
transaction accounts*, to ensure that they do not give rise to a
discrepancy between the *firm's client money requirement* and *client
money resource* (see ■ CASS 7.15.29 R).

(4) Under (1), (2) and (3), in determining the balances of *client money* a
firm has allowed another person to hold in connection with a *client's
non-margined transaction* or the balances held for *clients' non-
margined transactions* in *client transaction accounts*, a *firm* should use
the values contained in its internal records and ledgers (see
■ CASS 7.15.13 R).

Margined transactions (eg, derivatives): equity balances

7.16.28 | R | Subject to ■ CASS 7.16.30 R, a *client's equity balance* is the amount which the
firm would be liable to pay to the *client* (or the *client* to the *firm*) under the
client money rules for *margined transactions* if each of the open positions
were liquidated at the closing or settlement prices published by the relevant
exchange or other appropriate pricing source and the account with the *firm*
were closed. This notional balance should include any unrealised losses or
profits associated with that *client's* open positions, and any margin the *firm*
has received from the *client* in connection with those positions.

7.16.29 | R | Subject to ■ CASS 7.16.30 R, a *firm's equity balance* is the amount which the
firm would be liable to pay to the exchange, *clearing house*, *intermediate
broker* or *OTC* counterparty (or vice-versa) for the *firm's margined
transactions* if each of the open positions of those of the *firm's clients* that
are entitled to protection under the *client money rules* were liquidated at
the closing or settlement prices published by the relevant exchange or other
appropriate pricing source and the *firm's client transaction accounts* with
that exchange, *clearing house*, *intermediate broker* or *OTC* counterparty
were closed. This notional balance should include any unrealised losses or
profits associated with the open positions the *firm* holds for *clients* and any
margin the *firm* holds for *clients* in the relevant *client transaction accounts*.

7.16.30 | R | The terms '*client's equity balance*' and '*firm's equity balance*' refer to cash
values and do not include non-cash *collateral* or other *designated
investments* (including *approved collateral*) the *firm* holds for a *margined
transaction*.

**Margined transactions (eg, derivatives): margined transaction
requirement**

7.16.31 | G | The *margined transaction requirement* should represent the total amount of
client money a *firm* is required under the *client money rules* to segregate in

client bank accounts for *margined transactions*. The calculation in
■ CASS 7.16.33 R is designed to ensure that an amount of *client money* is held
in *client bank accounts* which equals at least the difference between the
equity the *firm* holds at exchanges, *clearing houses*, *intermediate brokers*
and *OTC* counterparties for *margined transactions* for *clients* entitled to
protection under the *client money rules*, and the amount due to *clients*
under the *client money rules* for those same *margined transactions*. With this
calculation, a *firm's margined transaction requirement* should represent, if
positions were unwound, the *firm's* gross liabilities to *clients* entitled to
protection under the *client money rules* for *margined transactions*.

7.16.32 | R | The total *margined transaction requirement* is:

(1) the sum of each of the *client's equity balances* which are positive; less

(2) the proportion of any individual negative *client equity balance* which
is secured by *client approved collateral*; and

(3) the net aggregate of the *firm's equity balance* (negative balances
being deducted from positive balances) on *client transaction accounts*
for *customers* with exchanges, *clearing houses*, *intermediate brokers*
and *OTC* counterparties.

7.16.33 | R | (1) To meet the total *margin transaction requirement*, a *firm* may
appropriate and use its own *approved collateral*, provided it meets
the requirements in (2).

(2) The *firm* must hold the *approved collateral* in a way which ensures
that, in accordance with ■ CASS 7A.2.3A R, the *approved collateral* will
be liquidated on the occurrence of a *primary pooling event* and the
proceeds paid into a *client bank account*, and in so doing:

(a) ensure the *approved collateral* is clearly identifiable as separate
from the *firm's* own property and is recorded by the *firm* in its
records as being held for its *clients*;

(b) keep a record of the actions the *firm* has taken under this *rule*
which includes a description of the terms on which the *firm* holds
the *approved collateral*, identifies that the *approved collateral* is
held for the benefit of its *clients* and specifies the *approved
collateral* that the *firm* has appropriated for the purposes of this
rule; and

(c) update the record made under (b) whenever the *firm* ceases to
appropriate and use *approved collateral* under this *rule*.

7.16.34 | G | Where ■ CASS 7.16.33 R applies, the *firm* will be reducing the requirement
arising from ■ CASS 7.16.16 R (2) and, as such, simultaneously reducing its
overall *client money requirement* (ie, the amount of money the *firm* is
required to segregate in *client bank accounts*).

7.16.35 | R | If a *firm's* total *margined transaction requirement* is negative, the *firm* must
treat it as zero for the purposes of calculating its *client money requirement*.

LME bond arrangements

7.16.36 [R] A *firm* with a *Part 30 exemption order* which also operates an *LME bond arrangement* for the benefit of US-resident investors must exclude the *client equity balances* for transactions undertaken on the *LME* on behalf of those US-resident investors from the calculation of the *margined transaction requirement*, to the extent those transactions are provided for by an *LME bond arrangement* (see ■ CASS 12.2.3 G).

Reduced client money requirement option

7.16.37 [R] Where appropriate, a *firm* may:

(1) when, in respect of a *client*, there is a positive *individual client balance* and a negative *client equity balance*, offset the credit against the debit and, therefore, have a reduced *individual client balance* in ■ CASS 7.16.21 R for that *client*; and

(2) when, in respect of a *client*, there is a negative *individual client balance* and a positive *client equity balance*, offset the credit against the debit and, therefore, have a reduced *client equity balance* (■ CASS 7.16.28 R) for that *client*.

7.16.38 [G] The effect of ■ CASS 7.16.37 R is to allow a *firm* to offset, on a *client*-by-*client* basis, a negative amount with a positive amount arising out of the calculations in ■ CASS 7.16.21 R and ■ CASS 7.16.28 R and, therefore, reduce its overall *client money requirement*.

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