

March 5, 1992

Ms. Jean A. Webb
Secretariat
Commodity Futures Trading
Commission
2033 K Street, N.W.
Washington, D.C. 20581

Re: National Futures Association: Proposed Amendments to
NFA Bylaw 1301 and Registration Rules 203, 204, 301 and
302; and Proposed Amendments to NFA Code of Arbitration
Section 2.

Dear Ms. Webb:

Pursuant to Section 17(j) of the Commodity Exchange Act as amended (the "Act"), National Futures Association ("NFA") hereby submits to the Commodity Futures Trading Commission ("Commission") proposed amendments to NFA Bylaw 1301 and Registration Rules 203, 204, 301 and 302; and proposed amendments to NFA Code of Arbitration Section 2. The proposed amendments were approved by NFA's Board of Directors ("the Board") at its meeting on February 27, 1992. NFA respectfully requests the Commission's review and approval of the proposed amendments to the Bylaws, Registration Rules and Code of Arbitration.

The proposed rule changes regarding membership dues and registration fees are particularly vital to NFA since they directly impact NFA's financial ability to perform its mandated functions. These rule changes are the result of a lengthy process which included a thorough review of all relevant issues not only by NFA's Board and Executive Committee, but also by a Special Committee for the Review of NFA's Revenue Structure, the FCM Advisory Committee, the CPO/CTA Advisory Committee and the IB Advisory Committee. In addition, all NFA Members were provided with an opportunity to comment on these proposals and their views were carefully considered at every level of discussion. We have also attempted to keep the Commission fully informed during NFA's consideration of these issues. It is important that NFA be able to implement these changes at the start of its new fiscal year, July 1, 1992. We will, of course, cooperate fully with the Commission to expedite the Commission's review of these proposals.



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I. PROPOSED AMENDMENTS TO NFA BYLAW 1301 AND REGISTRATION RULES 203, 204, 301 AND 302.

- A. Proposed Amendments to NFA Bylaw 1301 and Registration Rules 203, 204, 301 and 302 to raise NFA membership dues and registration fees and implement procedures which enhance the collection of registration fees (additions are underscored and deletions are [bracketed]):

Bylaws of the National Futures Association.

* * *

Bylaw 1301. Schedule of Dues and Assessments.

Subject to the provisions of Article XII, dues and assessments of Members shall be as follows:

* * *

(b) FCM Members.

* * *

- [(ii) Each FCM Member shall pay to NFA annual dues of \$1,000 if such FCM Member does not carry dealer option contracts for customers, or \$1,500 if such FCM Member does carry dealer option contracts for customers.]

- (ii) Each FCM for which NFA serves as the DSRO, as defined in NFA Financial Requirements Section 2, shall pay to NFA annual dues of \$5,000 and each FCM for which NFA does not serve as the DSRO, as defined in NFA Financial Requirements Section 2, shall pay to NFA annual dues of \$1,000.

* * *

(d) Other Members.

Annual dues for the other membership categories shall be as follows:

- (i) Commodity Trading Advisor -- [\$250] \$500;
(ii) Commodity Pool Operator -- [\$250] \$500;



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- (iii) Introducing Broker -- [\$250, except that for an introducing broker not required to maintain minimum adjusted net capital the dues shall be \$150] \$500;
- (iv) Commercial Firm -- \$100; and
- (v) Commercial Bank -- \$100.

* * *

Registration Rules

* * *

Rule 203. Registration Fees

(a) Amount.

- (1) **Associated Person.** Each Form 8-R submitted in connection with the registration of an associated person must be accompanied by a fee of [\$40] \$70.
- (2) **Futures Commission Merchant.** Each application for registration as a futures commission merchant must be accompanied by a fee of \$250.
- (3) **Introducing Broker.** Each application for registration as an introducing broker must be accompanied by a fee of [\$75] \$100.
- (4) **Commodity Pool Operator and Commodity Trading Advisor.** Each application for registration as a commodity pool operator or commodity trading advisor must be accompanied by a fee of [\$50] \$100.
- (5) **Leverage Transaction Merchant.** Each application for registration as a leverage transaction merchant must be accompanied by a fee of \$250.
- (6) **Floor Broker.** Each application for registration as a floor broker must be accompanied by a fee of [\$35] \$70.
- (7) **Principal.** Each Form 8-R submitted by a principal of an applicant or registrant must be accompanied by a fee of \$70 unless the principal is also



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applying for registration as an associated person of the applicant or registrant.

- (8) Annual Update. Each Form 7-R submitted on an annual basis by a futures commission merchant, introducing broker, commodity pool operator, commodity trading advisor or leverage transaction merchant in compliance with Registration Rule 204(c) shall be accompanied by a fee of \$100 for each registration category.
- (9) Late Termination Notice. Each notice required by Registration Rule 210(c) which is filed more than 20 days after the occurrence of the event requiring the notice shall be accompanied by a fee of \$100.
- (10) Disqualification Fee. A written submission to the President filed under Registration Rule 505 shall be accompanied by a fee of \$1,000 for the first submission only.
- (b) Form of Remittance. Registration fees must be remitted by check, bank draft or money order payable to NFA. All registration fees are non-refundable.

* * *

Rule 204. Registration of Futures Commission Merchants, Introducing Brokers, Commodity Pool Operators, Commodity Trading Advisors, and Leverage Transaction Merchants.

* * *

- (c) Periodic Filings. Any person who becomes registered as a futures commission merchant, introducing broker, commodity pool operator, commodity trading advisor, or leverage transaction merchant in accordance with paragraph (a) of this Rule shall be required to file a properly completed Form 7-R with NFA annually on a date specified by NFA. Failure to file the Form 7-R and pay the required annual update fee pursuant to Registration Rule 203(a)(8) within 30 days following such date will be deemed a request for withdrawal from registration. On at least 30 days written notice, and following such action, if any, deemed neces-



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sary by the CFTC or NFA, NFA may grant the request for withdrawal from registration.

* * *

Rule 301. Temporary Licensing of Applicants for Associated Person Registration.

* * *

(b) Withdrawal of application.

Failure of an applicant's sponsor or an applicant to respond to a written request by NFA for clarification of application information, to pay the required registration fee pursuant to Registration Rule 203(a)(1) or [resubmission of] to resubmit fingerprints in accordance with such request will be deemed to constitute a withdrawal of the applicant's registration application and shall result in the immediate termination of the applicant's temporary license.

* * *

(d) Termination.

(1) A temporary license shall terminate:

- (A) five days after service upon the applicant of a notice by NFA pursuant to Rule 504 that the applicant for registration may be found subject to a statutory disqualification under Sections 8(a)(2) through 8(a)(4) of the Act; or
- (B) immediately upon termination of the association of the applicant with the registrant which filed the sponsorship certification described in paragraph (a)(3) of this Rule; or
- [(C) upon withdrawal of the registration application pursuant to paragraph (b) of this Rule.]
- (C) upon failure of an applicant's sponsor or an applicant to respond to NFA's request for clarification of application information, to pay the required registration fee pursuant to Registration Rule 203(a)(1) or to resubmit



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fingerprints in accordance with such request pursuant to paragraph (b) of this Rule.

- (2) Upon termination, the applicant may not engage in any activity which requires registration with the Commission as an associated person.

* * *

Rule 302. Temporary Licensing for Guaranteed Introducing Brokers.

* * *

(b) Withdrawal of Application.

Failure of an applicant to respond to a written request by NFA for clarification of application information, to pay the required registration fee pursuant to Registration Rule 203(a)(3) or [resubmission of] to resubmit fingerprints in accordance with such request will be deemed to constitute a withdrawal of the registration application and shall result in the immediate termination of the applicant's temporary license.

* * *

(d) Termination.

- (1) A temporary license shall terminate:

- (A) five days after service upon the applicant of a notice by NFA that the applicant for registration may be found subject to a statutory disqualification under Sections 8(a)(2) through 8(a)(4) of the Act; or
- (B) immediately upon termination or suspension of the applicant's or guarantor futures commission merchant's NFA membership or upon termination of the applicant's guarantee agreement in accordance with NFA Financial Requirements Section 9 and CFTC Regulations 1.10(j)(4)(ii) or (j)(5) unless a new guarantee agreement is filed in accordance with paragraph (c)(2) of this Rule; or
- (C) upon failure of an applicant to respond to NFA's request for clarification of applica-



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tion information, to pay the required registration fee pursuant to Registration Rule 203(a)(3) or [resubmission of] to resubmit fingerprints in accordance with such request pursuant to paragraph (b) of this Rule.

- (2) Upon termination, the applicant may not engage in any activity which requires registration as an introducing broker.

* * *

B. Explanation of Proposed Amendments to NFA Bylaw 1301 and Registration Rules 203, 204, 301 and 302 to raise NFA membership dues and registration fees and implement procedures which enhance the collection of registration fees.

1. Background

The amendments to Bylaw 1301 increase membership dues for FCMs for which NFA is the DSRO to \$5,000¹ and increase CTA, CPO, and IB dues to \$500. However, the Board directed, for reasons set forth below, that the increased dues, except as applied to FCMs holding customer funds, be implemented over two years. As such, the Board approved the following schedule for membership dues:

Membership Dues

	Current	FY 1993	FY 1994
FCMs (exchange)	1,000	1,000	1,000
FCM (non-exchange)			
-Omnibus	1,000	5,000	5,000
-fully disclosed	1,000	3,000	5,000
CPO	250	375	500
CTA	250	375	500
IBI	250	375	500
IBG	150	325	500

¹ In general, NFA acts as the DSRO for FCMs which are not members of any exchange. NFA also acts as DSRO for a limited number of FCMs which are members of the Minneapolis Grain Exchange ("MGE"). NFA is compensated for the additional expenses it incurs in performing its DSRO responsibilities for those firms by the MGE. Where NFA receives compensation from an exchange it will avoid, in effect, "double charging" those exchange member FCMs for which NFA is the DSRO by retaining the \$1,000 membership dues.



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The amendments to Registration Rule 203 increase current and impose additional registration fees according the following schedule:

Registration Fees

	Current Fee	Revised Fee
AP Applications	40	70
Floor Broker Applications	35	70
FCM Applications	250	250
IB Applications	75	100
CPO Applications	50	100
CTA Applications	50	100

Additional Fees

Late Termination Notice	\$ 100.00
Registration Annual Update - FCM, CTA, CPO, IB	\$ 100.00
Disqualification Fee	\$1,000.00
Principal Applications	\$ 70.00

The Board believes that these increases to membership dues and registration fees are necessary for NFA to maintain sufficient working capital to effectively perform those functions mandated by Congress and those functions delegated to NFA by the Commission.

When the Board approved an increase in the NFA assessment fee in May 1991 it recognized that even with the increase NFA was projected to operate at a deficit of \$1.7 million in fiscal year 1992. That deficit would reduce NFA's working capital to approximately \$5.1 million, the lowest level deemed prudent by the Board. The Board also recognized that to avoid further erosion of NFA's working capital it would have to either further increase the assessment fee, reduce costs or increase revenue from other sources as part of the budgeting process for fiscal year 1993. At the suggestion of the Finance Committee, the Board appointed the Special Committee for the Review of NFA's Revenue Structure ("Special Committee") to consider each of these options in detail.

The Special Committee began this process with a thorough examination of NFA's current cost containment policies. The Special Committee noted the savings which have resulted from the 12% reduction in staff over the last several years and the hiring freeze imposed in April 1991. In addition, the Special Committee reviewed the savings achieved in the renegotiation of NFA's New York and Chicago office leases, NFA's continuing

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efforts to trim travel costs and economies which have been achieved in NFA's computer operations. The Special Committee concluded that any further significant cost cutting could seriously impair NFA's overall effectiveness and therefore focused its attention on reviewing NFA's current membership dues and registration fees.

a. Membership Dues

With respect to membership dues, the Special Committee noted that NFA's Articles of Incorporation provide that NFA's membership dues should "reflect differences in the financial burden borne or expected to be borne by NFA in carrying out its duties" for each of the categories or sub-categories of Members that it regulates. The Special Committee therefore directed staff to compile information concerning the amount of resources expended by NFA in regulating the various categories of Members. In reviewing this information, the Special Committee noted that NFA's mandated compliance responsibilities fall into three broad categories: audits, financial surveillance and investigations.

The compliance department's audit function constitutes the most time consuming and financially burdensome compliance responsibility. During 1990, NFA performed 1,130 audits which accounted for 67% of all the man-hours spent by NFA's compliance department. The compliance department audits non-exchange member FCMs, exchange member FCMs pursuant to a compensation agreement with the Minneapolis Grain Exchange, IBIs, IBGs, CPOs and CTAs. Among the firms that NFA audits, non-exchange member FCMs are the fewest in number but by far the most time consuming to audit due to comprehensive regulatory requirements. Additionally, NFA is required to audit non-exchange member FCMs which hold customer funds each year, alternating between full-scope and limited-scope examinations. Due to the complexity and frequency of non-exchange member FCM audits, NFA spends on average 246 man-hours to audit these Members, almost twice as many hours than for any other type of Member. As shown in the chart below, audits of IBIs and CPOs averaged approximately 119 man-hours while audits of IBGs and CTAs averaged approximately 81 man-hours per audit.

<u>Category</u>	<u># Firms</u>	<u># Audits</u>	<u>Total Audit Hours</u>	<u>Average Audit Hours/Member</u>
FCM (exchange)	206	0	0	0
FCM (non-exchange)	117	128	28,735	246
IBI	470	257	29,750	63
IBG	1,208	278	22,442	19
CPO	1,145	245	32,191	28
CTA	1,815	222	17,880	10



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Financial surveillance constitutes the second largest of the compliance department's three principal functions. This broadly defined area includes: NFA's review of FCM and IBI financial statements, daily monitoring of FCMs for which NFA is the DSRO, review of FCM and IBI subordinated loan agreements, processing and tracking of IBG agreements, review of Member CTA and CPO disclosure documents, analysis of annual certified financial statements for each Member commodity pool, and data entry and analysis of annual questionnaires completed by each Member. During 1990, staff spent almost 45,000 man-hours performing these varied responsibilities, which accounted for 23% of all the man-hours spent by NFA's compliance department. Again, with respect to NFA's financial surveillance function, staff spends considerably more hours regulating non-exchange member FCMs. NFA staff's analysis illustrates that the compliance department devotes on average 133 man-hours to perform NFA's financial surveillance function for non-exchange member FCMs, almost four times as many hours than for any other type of Member. As indicated in the chart below, financial surveillance of IBIs averaged 34 hours per Member, IBGs and CTAs averaged 2 hours per Member and CPOs averaged 6 hours per Member.

<u>Category</u>	<u># Members</u>	<u># Items Reviewed</u>	<u>Total Hours</u>	<u>Average Hours/Member</u>
FCM (exchange)	206	0	0	0
FCM (non-exchange)	117	803	15,592	133
IBI	470	2,451	15,864	34
IBG	1,208	1,800	2,987	2
CPO	1,145	2,113	6,838	6
CTA	1,815	2,322	3,757	2

NFA's compliance department's investigatory function constitutes NFA's third regulatory responsibility. In contrast to the audit and financial surveillance functions, staff hours devoted to investigations of particular Member categories are difficult to quantify. Since exchange member FCMs, non-exchange member FCMs, IBIs, IBGs, CPOs and CTAs are all subject to NFA's customer protection rules, each Member category is subject to NFA investigations for possible rule violations. In any given year, the investigative resources devoted to any given Member category may greatly vary depending on the type of compliance matters which arise.

In addition to reviewing the above information relating to the amount of resources expended by NFA in regulating the various categories of Members, the Special Committee also reviewed historical information concerning previous adjustments to NFA's membership dues and noted that these dues have been reduced



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four times since NFA's inception in 1982. Dues for CPOs, CTAs and IBs were reduced from \$500 to their current levels in 1985. This is the first time in its ten year history that NFA has acted to raise membership dues.

b. Registration Fees

The Special Committee also directed staff to compile information concerning NFA's financial burden in performing its various registration responsibilities. NFA's registration functions fall into two broad categories -- processing routine registration forms and conducting fitness examinations where circumstances warrant. The Special Committee noted that the registration department's administrative expenses in NFA's 1992 budget are approximately \$2.2 million, accounting for roughly 8% of NFA's total administrative expenses. However, NFA's true cost in performing its registration function is much higher. Resources from virtually all other NFA departments, including compliance, general counsel, information systems and others contribute in varying degrees to the registration function. In addition, a certain portion of NFA's overhead expenses, including space and utilities, are attributable to registration. When all these associated resources are computed along with the department's administrative expenses, NFA's actual financial burden of performing its registration function is approximately \$7 million.

After reviewing this information, the Special Committee concluded that NFA's financial burden should in fairness be borne by both the trading public and the industry, since both benefit from an efficient and thorough registration operation. The Special Committee therefore felt that NFA registration fees should be set to recoup approximately half of NFA's registration related expenses and directed staff to seek Member comment on a proposal which would accomplish that goal. The Special Committee also proposed certain new registration fees for processing annual updates for Member firms, applications for principals of firms, late AP termination notices, and disqualifications.

On November 6, 1991, NFA issued a Notice to Members which outlined the proposed adjustments to membership dues and registration fees and requested Member comment on the proposed adjustments as previously set forth on pages 4-5 (without any phase-in). The FCM, IB and CPO/CTA Advisory Committees considered the comments received in response to the Notice and provided their own comments to the Special Committee. Set forth below is a summary of the comments received from the Members and Advisory Committees.

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2. Summary of Comments Received

NFA received a total of 71 Member comments regarding the proposed increases to membership dues and registration fees.² Three FCMs, four IBIs, thirty-nine IBGs, twenty-four CTAs and one CPO submitted comments. NFA also received comments from the Managed Futures Association and Fishman & Merrick, P.C., attorneys for the National Introducing Broker Association.

Generally, Members opposed the proposed increases to membership dues and registration fees. Most commentators believed that the proposed dues and fees are unduly burdensome, particularly to smaller firms and industry entrants. However, several Member commentators recognized that some increase in membership dues and registration fees may be appropriate and expressed that any increased membership dues should be gradually phased-in. The majority of Members who opposed the proposed increases favored an increase in the per trade assessment fee as a means to obtain additional NFA revenue.

The Managed Futures Association ("MFA") objected to the proposed adjustments to CPO/CTA membership dues and stated that the proposed dues are unduly burdensome to industry entrants, IBs and smaller CPO/CTA firms. However, after noting opposition to the proposed dues, MFA agreed that membership dues should be adjusted for inflation but should not be adjusted to reflect the costs associated with regulating Members or the industry. Additionally, MFA favored an increase in the per trade assessment fee as a means to obtain additional NFA revenue.

All of the Advisory Committees supported the proposed adjustments and recognized the need to increase membership dues and registration fees. Additionally, the FCM Advisory Committee felt that NFA should recoup all of its registration expenses through its fees and the CPO/CTA Advisory Committee felt that in light of the Member comments NFA should phase-in the membership dues increases over two years.

3. Discussion

On January 8, 1992, the Special Committee met to review Member comments on the proposed adjustments to registration fees and membership dues. After a full discussion, the Special Committee recommended the adjustments to membership dues and

² With respect to these Member comments, a significant number only addressed the proposed increases to membership dues without addressing the registration fee increases.



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registration fees previously summarized on pages 4-5. The Special Committee concluded that while the proposed increases in membership dues would not be unduly burdensome, phasing in those increases over two years would provide a more equitable allocation of dues, ease pressure to further increase the assessment fee and demonstrate a responsiveness to Member concerns. Since the regulation of FCMs holding customer funds for which NFA is the DSRO imposes by far the greatest regulatory burden upon NFA, the Special Committee concluded that the membership dues for those FCMs should not be phased-in. Additionally, the Special Committee felt that NFA should retain the current policy of charging Members with multiple registration dues in only the highest category. The Special Committee also concluded that the proposed increased registration fees should be immediately implemented.

On February 27, 1992, the Board, after a full discussion, agreed with the analysis performed by the Special Committee and approved the increases in membership dues and registration fees. Based on current membership totals and last year's registration filings, these proposals could generate as much as an additional \$800,000 in membership dues and an additional \$1.3 million in registration fees for NFA fiscal year 1993. More realistically, however, NFA expects that Members may alter their current operations in light of these changes. More conservative projections would be for an additional \$400,000 in membership dues and an additional \$600,000 in registration fees.

The Board also adopted amendments to implement procedures to enhance the collection of registration fees. NFA Bylaw 1303 provides a procedure whereby NFA's President may suspend a Member's membership if the Member is in default in the payment of dues or assessments for a period of three months after such dues or assessments became payable. However, NFA does not have any procedures to enhance the collection of registration fees.

Currently, NFA does not incur a problem collecting the majority of registration fees. With respect to most initial registrations, NFA will not grant the applicant's registration until NFA receives full payment of the appropriate registration fee. However, NFA foresees a potential problem relating to the collection of the proposed annual update fee. In addition, there have been occasional collection difficulties with APs and guaranteed IBs who are granted temporary licenses but whose checks subsequently bounce.

Due to these collection problems, the Board amended NFA Registration Rule 204 to provide NFA with a remedy for the non-payment of the proposed annual update fee, whereby the failure to



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pay the annual update fee shall be deemed a withdrawal from registration. Additionally, the Board amended NFA Registration Rules 301 and 302 to provide for the termination of a temporary license granted to either an AP or guaranteed IB after the AP or guaranteed IB subsequently defaults on payment of the required NFA registration fee.

NFA respectfully requests that the proposed amendments to Bylaw 1301 and Registration Rules 203, 204, 301 and 302 become effective the later of July 1, 1992 or upon commission approval with the membership dues being phased-in and becoming fully effective on July 1, 1993.

II. PROPOSED AMENDMENTS TO NFA CODE OF ARBITRATION SECTION 2.

- A. Proposed Amendments to NFA Code of Arbitration Section 2 to expand NFA's arbitration jurisdiction to allow for the adjudication of unrelated futures and securities claims (additions are underscored and deletions are [bracketed]):

CODE OF ARBITRATION

* * *

Section 2. Arbitrable Disputes.

* * *

(b) [Discretionary Arbitration] Disputes Which May be Arbitrated in the President's Discretion

(1) At the option of any party, the securities portion of a dispute involving unrelated futures and securities claims may, in the President's discretion, be arbitrated under this Code if the timeliness requirements of Sections 5 and 6 of this Code are met.

(2) Except as required by the Member Arbitration Rules, other disputes involving commodity futures contracts between or among customers, Members, or Associates may, in the President's discretion, be arbitrated under this Code if the parties agree or have agreed to such arbitration and the timeliness requirements of Section 5 and 6 of this Code are met.

- B. Explanation of Proposed Amendments to NFA Code of Arbitration Section 2 to expand NFA's arbitration jurisdiction to allow for the adjudication of unrelated futures and securities claims.



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1. Background

As you know, the Commission recently concluded a study of arbitration programs administered by certain organizations outside the futures industry, which included the American Arbitration Association ("AAA"), the National Association of Securities Dealers ("NASD") and the New York Stock Exchange ("NYSE"). One purpose of the study was to determine the degree of futures-related customer arbitrations occurring at these forums. The Commission found that, although the number of futures claims filed at these forums over the past few years has been relatively small, a notable portion of the cases has involved a combination of futures and securities claims.

In a letter to NFA President Robert K. Wilmouth dated September 9, 1991, Commission Chairman Wendy L. Gramm asked NFA to explore expanding NFA's arbitration jurisdiction to include securities claims filed in connection with futures claims because resolving such claims in a single proceeding at a single arbitration forum could provide significant administrative efficiencies and other benefits to futures customers and their brokers, particularly in light of the growing integration of commodities and securities products and activities. NFA agrees that there are certain advantages to having securities and futures claims resolved in a single proceeding at one forum as long as unrelated securities claims do not place an undue drain on NFA's resources, thereby interfering with NFA's ability to efficiently resolve futures claims. Therefore, NFA's staff studied the overall effect of accepting unrelated securities claims filed with futures claims and reported this study's findings to NFA's FCM, IB and CPO/CTA Advisory Committees and subsequently to the Executive Committee and the Board of Directors.

2. The Study

NFA's arbitration forum already adjudicates claims involving securities transactions that are part of or directly connected with futures transactions.³ However, NFA rejects claims for securities losses that are unrelated to futures transactions. There are only two situations where this occurs. First, NFA rejects claims which relate solely to securities. Second, NFA rejects the securities portions of claims which allege separate losses in futures accounts and securities

³ Whenever NFA staff arbitrates a case involving both futures and securities claims, staff carefully screens potential arbitrators to find individuals who are knowledgeable about both industries.



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accounts where the only connection between the accounts is that they involve the same customer and the same brokerage firm.

To see what impact expanding NFA's jurisdiction to hear unrelated securities cases could have on NFA's resources, staff has reviewed the filings historically. For purposes of the study, staff looked at the cases filed at NFA from January 1, 1988 through November 30, 1991 by reviewing data from NFA's computer system and by drawing on staff's experience with the cases. Therefore, staff is fairly confident that all of the cases filed at NFA involving both futures and securities transactions have been identified.

An analysis of the information indicates that a total of 15 cases involving securities have been filed at NFA during the period studied. Twelve of the identified cases involved claims where the securities losses were part of or directly connected with the futures losses. The other three cases involved claims for separate securities losses that were unrelated to futures so that only the futures portion was accepted by NFA. Therefore, cases involving both futures and securities have made up less than 2% of NFA's caseload over the past four years and less than .3% of NFA's caseload has involved cases where NFA rejected the securities portion of the claim.⁴

As part of the study, staff also asked the Commission for copies of awards which were available from its recent study of the arbitration programs administered by the NASD and the NYSE. In reviewing the public awards, staff looked at a summary of the issues to try to identify the products involved and determine whether the claims involved related or unrelated securities and futures transactions.

By looking at the public award data from the NASD and the NYSE, staff estimated that from 1988 to 1991 NFA's caseload could have increased by a maximum of 40 claims, or four percent, if NFA had accepted all of the cases filed at the NASD and the NYSE involving futures transactions, which is a minimal increase in filings. The actual impact of expanding NFA's current policy would probably have been less. Under its current policy, NFA would have accepted 23 of the 40 claims filed at the NASD and the

⁴ The total number of arbitration cases filed at NFA during the period under study equals 1252. During the same time period, NFA also rejected an additional five cases which solely involved securities transactions.

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NYSE.⁵ Therefore, it appears that only 17 cases might have been added to NFA's caseload, which is roughly a two percent increase overall.⁶

3. Discussion

Neither the Commodity Exchange Act nor the Commission's regulations appear to preclude NFA from accepting cases involving unrelated futures and securities claims. After reviewing staff's study with NFA's Advisory Committees, the Advisory Committees noted that expanding NFA's jurisdiction to include securities claims filed with unrelated futures claims should not create a significant drain on NFA's resources. Therefore, the Committees recommended that NFA expand its arbitration jurisdiction to accept unrelated futures and securities claims. The Advisory Committees further recommended that any Code of Arbitration amendment give NFA's President discretion over accepting these claims so as not to place NFA in a position of jeopardizing NFA's successful futures-related arbitration program in case the impact to filings is greater than anticipated.

On February 27, 1992, the Board agreed with the Advisory Committee's recommendation that NFA should expand its arbitration jurisdiction to allow for the adjudication of

⁵ There are perhaps several reasons why some of these cases are filed elsewhere. First, some parties may choose to go to a forum other than NFA because they are more familiar with the other forum. Second, some people are prevented from filing a case at NFA where the claim is barred by NFA's two-year time limitation period. In such a case, the claim would likely be accepted at the NASD or the NYSE since each forum has a six-year time limitation period for claims to be filed. To illustrate, one of the public awards available from the Commission's study involved a futures claim which may have been filed at the NASD because it was outside NFA's limitation period. Third, for tactical reasons some attorneys in certain cases prefer to have arbitrators who lack knowledge and experience in the futures industry, a point recently raised by several attorneys at a 1991 Kent Conference panel on litigation issues.

⁶ This analysis, however, does not take into consideration the futures-related cases heard at the AAA. An undetermined number of futures-related disputes were apparently heard at the AAA between 1988 and 1991, some of which were categorized as securities cases. The AAA did inform the Commission that in 1990 eight "commodity broker-client" cases were decided under its commercial rules and 172 securities cases were heard.

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unrelated futures and securities claims where the only connection between the claims is a common customer and the same brokerage firm. Therefore, the Board amended NFA's Code of Arbitration Section 2 to allow for the arbitration of disputes involving unrelated futures and securities claims.

NFA respectfully requests that the Commission review and approve the proposed amendments to NFA's Code of Arbitration Section 2. NFA further requests that the amendments be declared effective upon Commission approval.

Respectfully submitted,



Daniel J. Roth
General Counsel

DJR:cmc(ltrs-webb4)

cc: Chairman Wendy L. Gramm
Commissioner Fowler C. West
Commissioner William P. Albrecht
Commissioner Sheila C. Bair
Commissioner Joseph B. Dial
Andrea M. Corcoran, Esq.
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UNITED STATES OF AMERICA
COMMODITY FUTURES TRADING COMMISSION

2033 K Street, N.W.
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September 8, 1992



Daniel J. Roth, Esq.
General Counsel
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200 West Madison Street -- Suite 1600
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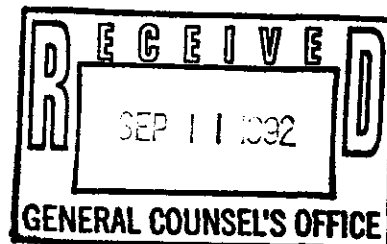
Re: Proposed amendment to NFA Code of
Arbitration §2(b)

Dear Mr. Roth:

By letter dated March 5, 1992, the National Futures Association ("NFA") submitted the captioned rule proposal pursuant to section 17(j) of the Commodity Exchange Act ("Act") for Commission approval. Proposed Code §2(b)(1) extends NFA's arbitration jurisdiction, in the discretion of NFA's President, to cover the securities portion of a dispute involving unrelated futures and securities claims. Please be advised that the Commission has approved the proposal effective immediately.

Yours truly,

Jean A. Webb
Secretary of the Commission

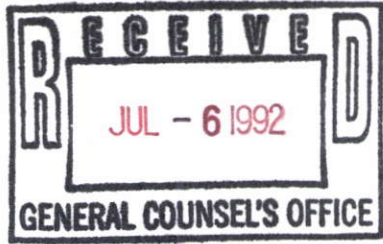


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UNITED STATES OF AMERICA
COMMODITY FUTURES TRADING COMMISSION

2033 K Street, N.W.
Washington, D.C. 20581

June 30, 1992



Daniel J. Roth, Esq.
General Counsel
National Futures Association
200 West Madison Street -- Suite 1600
Chicago, IL 60606

Re: Proposed amendments to NFA Registration
Rules 203, 204, 301 and 302 and Bylaw
1301

Dear Mr. Roth:

By letters dated March 5 and May 27, 1992, the National Futures Association ("NFA") submitted the captioned rule proposals pursuant to section 17(j) of the Commodity Exchange Act ("Act") for Commission approval. NFA requested that the Commission approve the proposals in a timely fashion to enable NFA to implement them on July 1, 1992, the first day of NFA fiscal year 1993.

Please be advised that the Commission has approved NFA's rule proposals. Nevertheless, the Commission again reminds NFA that the Commission expects NFA to continue to evaluate and, as necessary, modify the revised dues schedule to ensure that particular dues do not become barriers to entry or reflect inequitable allocations among members as prohibited by Section 17(b)(6) of the Act and Regulation 170.4. The Commission also expects NFA to continue to evaluate the revised registration fee schedule to ensure that the fees do not exceed NFA's actual costs of performing the registration functions.

Yours truly,

Jean A Webb
Jean A. Webb
Secretary of the Commission

COMMODITY FUTURES
TRADING COMMISSION
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SECRETARY
June 23 1992

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M E M O R A N D U M

TO: The Commission
FROM: Division of Trading and Markets *Amc*
RE: Proposed Rule Changes by the National Futures
Association -- Registration Fees and Membership Dues

RECOMMENDATION: That the Commission approve NFA's proposed
amendments to Bylaw 1301 and Registration
Rules 203, 204, 301 and 302 pursuant to
Section 17(j) of the Commodity Exchange Act.

OFFICES CONSULTED: Division of Economic Analysis *MDA*
Division of Enforcement *PK*
Office of the Executive Director *EMW*
Office of the General Counsel *STM*

I. INTRODUCTION

Pursuant to Section 17(j) of the Commodity Exchange Act
("Act"), the National Futures Association ("NFA") submitted
proposed amendments to the captioned rules governing registration
fees^{1/} and membership dues^{2/} by the attached letter dated

^{1/} With certain exceptions, all persons and firms that intend
to do business as futures professionals must register under
the Act within the appropriate category: futures commission
merchant ("FCM"); introducing broker ("IB"); commodity pool
operator ("CPO"); commodity trading advisor ("CTA"); lever-
age transaction merchant ("LTM"); associated person ("AP")
of any of the foregoing; or floor broker ("FB"). NFA, by
Commission delegation, has the responsibility for admini-
stering the registration functions under the Act in accor-
dance with Commission regulations and NFA rules approved by
the Commission. Commission Regulation 3.2(a) and Part 3
generally; NFA Registration Rules. NFA's authority includes
setting fees.

^{2/} NFA is a self-regulatory membership organization, the
primary purpose of which is to assure high standards of
professional conduct and financial responsibility by its
members. Every FCM, IB, CTA or CPO that conducts a futures-
related business with the public is required to be a member

March 5, 1992, as amended by the attached letter dated May 27, 1992.^{3/} NFA is proposing to increase registration fees for certain registration categories, add certain new registration fees, and increase the current annual dues for certain NFA membership categories. On April 9, 1992, the Commission published a Federal Register notice requesting public comment on NFA's proposals. Having reviewed NFA's submission and the public comments, the Division recommends that the Commission approve the captioned rule changes pursuant to Section 17(j) of the Act. NFA intends to put the revised fee and dues schedules into effect on July 1, 1992, the start of NFA fiscal year 1993.^{4/}

II. BACKGROUND

NFA is an entirely self-financed organization, with income for its operations derived primarily from assessments paid by public participants in the futures markets.^{5/} During the first 10 months of fiscal year 1992, for instance, such transactional

of NFA. NFA Bylaw 1101; Commission Regulation 170.15. Membership in NFA also is available to futures exchanges and other persons engaged in the futures business. Members must pay dues annually to maintain their membership. NFA Bylaw 1301(b)(ii), (c)(ii), and (d).

^{3/} The March submission also contains a proposed rule amendment pertaining to NFA's arbitration program. The Division will address that proposal in a separate memorandum.

^{4/} NFA's fiscal year runs from July 1 to June 30.

^{5/} NFA requires FCM members and LTM members to collect a specified per-trade fee from their customers for remittance to NFA. NFA Bylaw 1301(b)(i) and (c)(i). In addition, each contract market member must pay a transaction assessment for contracts executed on the contract market, subject to a ceiling of \$100,000 for a small contract market member or \$150,000 for a large contract market member. Bylaw 1301(a).

assessments accounted for 91.3% of NFA's revenues.^{6/} Membership dues and registration fees are the next largest sources of income, respectively accounting for 4.3% and 2.3% of the total revenues in the current fiscal year.^{7/} The remaining revenue comes from fines,^{8/} fees for particular services (such as arbitration),^{9/} and interest on its cash balances and U.S. Treasury bill holdings.

NFA maintains that the proposed increases in membership dues and registration fees are needed to enable it to retain working capital at approximately its current level.^{10/} Between the end of fiscal year 1989, when it had \$15.1 million in working capital, and the end of fiscal year 1991 (with \$6.8 million in working capital), NFA intentionally reduced its working capital by \$8.3 million, principally by operating at a deficit.^{11/} In the first 10 months of fiscal year 1992, NFA has had an additional net loss of \$1.1 million despite various cost-containment efforts (including a hiring freeze and reduction in staff) and an increase in transactional fees coupled with recent

^{6/} See NFA Statement of Revenue and Expense by Account Category as of April 30, 1992, NFA Status Report (May 1992) ("April 1992 revenue statement").

^{7/} See April 1992 revenue statement.

^{8/} NFA Compliance Rule 3-11.

^{9/} E.g., NFA Code of Arbitration §11.

^{10/} "Working capital," in this context, is the difference between total current assets (primarily cash, U.S. Treasury bills, and assessments receivable) and total current liabilities.

^{11/} See NFA 1990 and 1991 Annual Reports.

higher-than-expected trading volume.^{12/} NFA currently is operating with the smallest amount of working capital since fiscal year 1983, when it began operations. Assuming the Commission approves the proposed increases in registration fees and membership dues, NFA projects a further deficit of \$300,000 for fiscal year 1993.

Last year, the Board of Directors appointed a Special Committee for the Review of NFA's Revenue Structure to study ways for NFA to avoid further erosion in the working capital. The Special Committee concluded that additional significant operational cost cutting could impair NFA's overall effectiveness in performing its mandated and delegated functions. While affirming that transactional assessments should continue to be the primary source of NFA revenue, the Special Committee determined that the trading public should not shoulder most of the financial burden alone. It recommended raising the registration fees and membership dues so that the industry would pay a fairer share of NFA's operations. Previously in its nearly 10-year history, NFA raised registration fees only for APs and FBs to cover a portion of increases imposed by the Federal Bureau

^{12/} See April 1992 revenue statement. To augment the 12% staff reduction it has experienced over the last few years, NFA has had a freeze on routine hiring since April 1991. See NFA's March 5, 1992 submission, at 8. NFA raised the transaction assessment fee for the first time in its history at the start of fiscal year 1992. See memorandum to the Commission from the Division dated June 27, 1991. In the budget for fiscal year 1992 (which incorporated the hiring freeze and the increased assessment fee schedule), NFA had projected a year-end loss of \$1.7 million, reducing working capital to \$5.1 million, the lowest level deemed prudent by NFA's Board of Directors. NFA now expects the actual results to be somewhat better than the budget.

of Investigation ("FBI")^{13/} and reduced but never raised membership dues.

After soliciting comments on the Special Committee's recommendations from the various advisory committees and the membership,^{14/} NFA proposed and submitted rule changes to the Commission to increase the annual membership dues and to raise or add new registration fees. NFA requested Commission approval to enable NFA to implement the changes on July 1, 1992, the beginning of NFA's next fiscal year. NFA subsequently submitted an amendment to one of the registration fee proposals to authorize refunds in certain circumstances.

The Commission published notice of the proposals in the Federal Register and requested public comment on all aspects of the amendments, including any competitive implications.^{15/} In the latter regard, the Commission solicited specific comment on whether any of the proposals would impose any undue burdens on particular market participants or on potential industry entrants. The Commission received 14 comment letters. The comment letters came from NFA,^{16/} several members of NFA's Board of Directors

^{13/} See discussion in III.B.1. infra.

^{14/} NFA received 71 comments from members, a significant number of which addressed only the proposed dues increases without addressing the registration fee changes. The FCM, IB, and CPO/CTA Advisory Committees provided their own comments in support of the recommended adjustments after considering the member comments. The Special Committee modified its original proposal to address certain membership concerns.

^{15/} 57 FR 12295 (April 9, 1992).

^{16/} Letter dated May 11, 1992.

and committees,^{17/} two small CTAs,^{18/} the National Introducing Broker Association ("NIBA"), which is a trade association representing IBs,^{19/} one guaranteed IB,^{20/} and Arthur Andersen & Co.^{21/} Most of the commenters, including NFA and its leadership, supported the proposals. The individual guaranteed IB and the CTA-commenters, on the other hand, objected to the dues increase applicable to themselves. In addition, the

^{17/} [1] Anthony V. Czapla (Dellsher Investment Company, FCM), chairman of NFA's CPO/CTA Advisory Committee (letter dated May 4, 1992); [2] J. Dewey Daane (Vanderbilt University), NFA Public Director and member of the Finance and Special Committees (letter dated May 4, 1992); [3] Dennis D. Dunn (Dunn & Hargitt Investment, CTA), NFA Director and member of the Finance and Special Committees (letter dated April 30, 1992); [4] Hal T. Hansen (Cargill Investor Services, Inc., FCM), Vice Chairman of NFA's Board of Directors and member of the Finance and Special Committees (letter dated May 4, 1992); [5] Harold J. Heinhold (B.E.B., Inc., guaranteed IB), member of NFA's IB Advisory Committee (letter dated April 28, 1992); [6] Warren W. Lebeck, NFA Public Director (letter dated April 22, 1992); [7] Leo Melamed (Chicago Mercantile Exchange), NFA Director and Permanent Special Advisor (letter dated April 22, 1992); and [8] Mark J. Powers (Classic Futures, Inc., CTA and independent IB), member of NFA's CPO/CTA Advisory Committee (letter dated April 22, 1992).

^{18/} Craig R. Niemann, who is registered as a CPO also (letter dated May 10, 1992); Peter C.L. Timmons, T/R Financial Management Group, Inc. (letter to Chairman Gramm, dated March 31, 1992).

^{19/} Letter from Fishman & Merrick, P.C., representing the NIBA (dated May 11, 1992).

^{20/} A. James Gulotta, Gulotta Trading Service (letter to Ray McKenna, dated May 27, 1992).

^{21/} Letter dated May 8, 1992. The certified public accounting firm stated that it was familiar with NFA's budgeting process and financial policies as a result of performing a review in 1984 of NFA's then-forecasted expenses and evaluating alternative revenue methods for NFA. The comments affirmed the reasonableness of NFA's strategy of more equitable diversification of revenue sources aimed at achieving, over time, a more stable revenue flow.

NIBA, while supporting the increases in registration application fees, objected to certain other new registration fees and to the dues increase for IBs.

III. REGISTRATION FEES

A. Proposed Changes

NFA has proposed to amend its Registration Rules 203, 204, 301 and 302 with the following revised fee schedule and related provisions:

<u>Application Fees (Category)</u>	<u>Current</u>	<u>Proposed</u>	<u>Change</u>
FCM or LTM	\$ 250	\$ 250	\$ 0
IB	75	100	+25
CPO or CTA	50	100	+50
FB	35	70	+35
Principal	--	70	+70
AP	40	70	+30

Nonpayment of the fee for an AP or guaranteed IB would be deemed the withdrawal of the registration application, resulting in immediate termination of the applicant's temporary license.

<u>Additional Fees</u>	<u>Current</u>	<u>Proposed</u>	<u>Change</u>
Disqualification Challenge	\$ 0	\$ 1,000	\$ +1,000

The fee for challenging a disqualification would be refunded if, as a result of the challenge, the applicant were found not to be subject to a statutory disqualification.^{22/}

^{22/} NFA's rules governing denial or revocation of registration permit an applicant or registrant to submit written evidence challenging an NFA intention to act adversely on a registration based on one or more alleged statutory disqualifications as enumerated in Sections 8a(2)-(4) of the Act. Registration Rule 505. The refund provision was submitted to the Commission by letter dated May 27, 1992, as

Late Filing by Sponsor of Termination Notice (Form 8-T) ^{23/} 0	100	+100
Annual Registration Update (FCM; CTA; CPO; IB) 0	100	+100

Payment of the registration update fee would be required for each category in which a registrant is registered. Failure to pay the new fee for the annual registration update would be deemed a request for withdrawal from registration.

B. Discussion

NFA has the authority, subject to Commission review and approval, to establish fees related to its delegated responsibility for performing registration functions under the Act on behalf of the Commission with respect to various categories of registrants.^{24/} As the Commission has stated, NFA is in the best position to determine the costs associated with performing those functions and to set or adjust the registration fees, so long as the fees do not exceed NFA's actual costs of performing registration activities.^{25/}

NFA collects less than \$650,000 a year in registration fees, although the direct and indirect expenses for performing the

an amendment to the original submission.

^{23/} Under Registration Rule 210(c)-(d), a sponsoring firm is required to file a termination notice (Form 8-T) within 20 days after termination of an AP's or principal's association with the sponsor. The proposed fee would be imposed only when the notice is not timely filed.

^{24/} 48 FR 34732, 34733 (August 1, 1983) (IBs and their APs); 49 FR 39518, 39522 (October 9, 1984) (FCMs, CPOs, CTAs, and APs of those categories); 54 FR 19556, 19557 (May 8, 1989) (LTMs and their APs); 55 FR 32241, 32242 (August 8, 1990) (FBs).

^{25/} 55 FR 32241, 32242 (August 8, 1990).

delegated registration functions -- processing routine registration forms and, where warranted, conducting fitness examinations -- currently total approximately \$7 million.^{26/} As previously noted, transactional assessments are the primary source of funding for NFA's operations, including these registration activities. Believing that the financial burden should be borne more equitably by both the trading public and the industry, NFA proposed to revise the registration fees with the intention of recouping approximately half of NFA's registration-related expenses. NFA projects that the proposed application fee increases alone would generate additional revenues between \$600,000 and \$1.3 million, depending on whether the volume of registration filings falls or remains steady.

1. Application Fees

Each of NFA's application fees for individuals covers the amount paid to the FBI for processing an applicant's fingerprint card.^{27/} In 1990, NFA raised the application fees for APs and

^{26/} The total expenses include the direct expenses of NFA's registration department (approximately \$2.2 million currently), as well as resources of other NFA departments that are attributable to registration functions (e.g., compliance, general counsel, information systems) plus a portion of NFA's overhead. When the Commission established its own registration fees, it included similar categories of costs. See, e.g., 48 FR 34732, 34733 (August 1, 1983).

The Division notes that NFA currently is operating a direct entry pilot program which allows participating firms to send registration data electronically to NFA with respect to applicants for registration as associated persons with such firms. This program may allow the NFA to attain certain time and cost efficiencies which could lessen the amount of resources NFA may have to expend for its registration responsibilities.

^{27/} The FBI currently charges \$23 per request.

FBS \$10 to their current levels after the FBI increased the fee \$11 in four years.^{28/} The application fees for the other categories have never been increased by NFA.

2. Update Fee

The new registration update fee is analogous to the processing fee that NFA, and the Commission before it, charged in connection with the annual registration renewal formerly required of registrants. The Commission replaced the renewal procedure in 1988 with permanent registration subject to an annual filing requirement,^{29/} but NFA did not retain the requirement of a filing fee at that time. The currently proposed fee is intended to defray half of NFA's costs to process the updates. The NIBA has objected to a flat fee, arguing that such a fee would place a disproportionate burden on small registrants, in particular, guaranteed IBs. NFA staff has indicated, however, that the cost to process an update is not dependent upon the size of the registrant.

3. Late Termination Notice Fee

In addition to covering part of NFA's costs, the new fee for late filing of termination notices is intended to encourage timely filings. NFA staff notes (and the Division's Registration Unit concurs) that NFA has experienced some problem in receiving Form 8-T notices within 20 days of the AP's or principal's

^{28/} When NFA began processing registration applications for the Commission in the mid-1980's, the FBI fee was \$12. The FBI raised the fee three times between 1987 and 1990.

^{29/} See Commission Regulation 3.10(d); 53 FR 8428 (March 15, 1988); 52 FR 45350, 45351 (November 27, 1987).

termination, as required by NFA's registration rules. As a practical consequence, an ex-sponsor's delinquency in filing the notice can delay NFA's processing of the terminated AP's registration with a new firm.

4. Disqualification Challenge Fee

With respect to the \$1,000 fee for challenging a disqualification, the NIBA argued that (1) a flat fee would burden smaller firms unduly and (2) the proposal is unfair in that it would penalize the sponsor for having to pay the fee for an applicant who lied or made a mistake.

NFA staff has indicated to the Division that disqualification proceedings are expensive to administer. NFA believes it is fairer to have the allegedly disqualified applicants who want to pursue these matters bear part of the associated costs through a separate flat fee than to have the general population of applicants, most of which are not subject to apparent disqualifications, absorb those expenses through even higher application fees. Moreover, requiring a flat fee for disqualification challenges is not unprecedented. The National Association of Securities Dealers ("NASD") imposes a \$1,000 fee upon member firms applying for relief in order to employ an individual who is subject to a disqualification under the Securities Exchange Act and the NASD's rules.^{30/} Unlike the NASD's rule, however, NFA's proposal does not impose the fee directly on the sponsoring firm as the NIBA's comments imply,

^{30/} NASD Bylaws, Schedule A, §12.

although the sponsor is not prohibited from covering the fee for the applicant if it chooses.

NFA staff recognizes that setting the disqualification-challenge fee at \$1,000 may discourage frivolous challenges from being filed. The proposal, however, would provide for the refund of the fee if the applicant is found not to be subject to a statutory disqualification.^{31/} In contrast, the NASD fee is nonrefundable.

5. Nonpayment Consequences

NFA also has proposed amendments that are intended to address existing or potential collection difficulties regarding certain fees. While collection of most registration fees generally has not been a problem, NFA indicated that occasionally the application-fee checks of APs and guaranteed IBs bounce after NFA grants the temporary licenses. NFA also foresees a potential problem in collecting the new annual update fee. Accordingly, it proposes to deem nonpayment of such fees as an application withdrawal or a request for withdrawal from registration, as applicable. The proposal appears to be consistent with Commission Regulations 3.42, 3.46, 3.10(d), and 3.33 governing the termination of temporary licenses and requests for withdrawal from registration.

^{31/} There would be no refund if the proceeding results in the applicant's registration despite a statutory disqualification.

IV. MEMBERSHIP DUES

A. Proposed Changes

NFA has proposed to amend Bylaw 1301 to revise its membership dues schedule as follows:

<u>Membership Category</u>	<u>Current</u>	<u>Proposed</u>	<u>Change</u>
FCM (exchange member)	\$ 1,000/1,500 ^{32/}	\$ 1,000	\$ 0
FCM (non-exchange)	1,000/1,500	5,000	+4K/3,500
CTA or CPO	250	500	+250
IB	150/250 ^{33/}	500	+350/250

The dues increases would be phased in over two years for all members except non-exchange FCMs carrying customer funds (i.e., omnibus basis), since oversight of the latter members imposes the greatest regulatory burden on NFA as DSRO. Members with multiple registrations would continue to be charged dues in only the highest dues category.^{34/}

B. Discussion

Section 17(b)(6) of the Act requires NFA to provide for equitable allocation of dues among its members to defray reasonable expenses of administering NFA. Commission Regulation 170.4 further prohibits NFA from structuring such dues in a

^{32/} Under the existing rule, any FCM member (exchange and non-exchange) carrying dealer option contracts for customers would pay \$1,500 dues instead of \$1,000. NFA has no members that carry dealer option contracts and is proposing to eliminate the dues distinction.

^{33/} Currently, independent IBs pay \$250 dues, while guaranteed IBs pay \$150 dues.

^{34/} As previously mentioned, every member also would have to pay, separate from NFA dues, the registration update fee (\$100) for each category in which the member is registered.

manner constituting a barrier to entry of any person seeking to engage in commodity-related business activities. Moreover, Article XV, Section 3 of NFA's Articles of Incorporation authorizes NFA to prescribe different dues amounts for different categories or subcategories of members in an endeavor to reflect differences in the financial burden borne or expected to be borne by NFA in carrying out its duties and programs for each such category or subcategory.

NFA collects less than \$1.1 million a year in membership dues. In contrast, the total cost of NFA's compliance program currently is approximately \$17 million. As described in detail in NFA's March submission, the revised dues schedule is intended to reflect differences in NFA's financial burden in carrying out its compliance responsibilities with respect to different membership categories.

The compliance functions are primarily: auditing, which in 1990, for example, accounted for 67% of the compliance department's time; financial surveillance, which accounted for 23% of the department's time; and investigations. NFA spends four or more times the number of staff-hours per member on audits and surveillance of non-exchange FCMs than on any other membership category. For example, in 1990 NFA spent an average of 379 audit and surveillance hours on each non-exchange FCM. By comparison, NFA spent an average of 12 hours per CTA, 34 hours per CPO, 21 hours per guaranteed IB and 97 hours per independent IB during the same period. NFA does not conduct audits or surveillance of exchange FCMs, as they are overseen by the

appropriate designated-self-regulatory-organization exchanges. Accordingly, under NFA's proposed revisions in its dues schedule, non-exchange FCMs would pay substantially higher dues than any other category. NFA anticipates that, depending on whether membership numbers fall or remain steady, the proposals could generate between \$400,000 and \$800,000 in additional revenue in fiscal year 1993.

The Commission received no public comments against the proposed increase in dues for non-exchange FCMs. The NIBA objected to the amount of the IB dues increase and especially to the elimination of a differential between guaranteed IBs and independent IBs. The guaranteed IB-commenter objected to the proposed IB dues of \$500 as anti-business, stating that the additional revenues should come from public customers rather than NFA's members.^{35/} The two CTA-commenters opposed the increase in CTA dues, noting the current economic recession. One stated that having to pay an additional \$125 in dues in fiscal year 1993 and another \$125 increase the next year under the two-step phase-in might make it prohibitive to stay in business in light of the very low revenues earned by the commenter.^{36/} The other CTA-commenter suggested using a sliding scale based on amounts under management or, in the alternative, raising the transactional assessment further.^{37/}

^{35/} Letter from Gulotta Trading Service (A. James Gulotta).

^{36/} Letter from T/R Financial Management Group, Inc. (Peter C.L. Timmons).

^{37/} Letter from Craig R. Niemann.

When NFA was registered as a futures association in 1981, it set the annual dues at \$1,000 for each membership category.^{38/} Between 1982 and 1985, however, it reduced the dues for CPOs, CTAs and IBs in stages to their present levels. The proposed dues increase to \$500 for these categories would remain significantly lower than the amount required in the early 1980's. Even with the increase, dues would account for less than 10% of NFA's revenues, as one commenter from NFA's Board pointed out.^{39/} NFA believes that any differences in compliance costs for different types of IBs or different sizes of CTAs or CPOs tend to fluctuate from year to year and currently are not significant enough to justify further subcategorization of the modest amount of dues proposed. NFA also has determined that additional increases in the transactional assessment fees are inappropriate at this time.

The NFA believes that the proposed increases are relatively modest and should not impose an unreasonable burden. As one commenter, a guaranteed IB, noted, "any business that would be deterred from continuing or from being established by this negligible dues increase is already playing it too close to that point [beyond which a business is not cost effective] for the safety of the public."^{40/}

^{38/} Dues for new CPOs and CTAs were set at \$500, but only for their first year of registration. IBs were added as a membership category in mid-1983 with dues comparable to CPOs and CTAs.

^{39/} Letter from Leo Melamed.

^{40/} Letter from B.E.B., Inc. (Harold J. Heinhold).

The Division also notes that NFA has proposed to phase in the increases over a two-year period (except for non-exchange FCMs that carry customer accounts) in order to minimize the impact. In addition, NFA's Board of Directors has authority to reduce or waive the annual dues for particular members.^{41/} If a member believes that the dues increase creates an undue financial hardship on its operations, the member may submit its justification for a reduction or waiver to the Board.

V. CONCLUSION AND RECOMMENDATION

As indicated above, NFA collects less than \$1.75 million a year in registration fees and membership dues toward the approximately \$24 million a year in total expenses for the two programs. NFA anticipates that the proposals would generate between \$1 million and \$2.1 million of additional revenue in the upcoming fiscal year. Even with such revenue, however, NFA projects operating at a \$300,000 deficit for fiscal year 1993.

The Division believes that the proposed amendments to NFA's bylaws and registration rules do not violate, and are not otherwise inconsistent with, the Act or the Commission's regulations. Accordingly, the Division recommends that the Commission, pursuant to Section 17(j) of the Act, approve the proposed amendments to NFA Registration Rules 203, 204, 301, and 302 and to NFA Bylaw 1301. The attached approval letter contains a reminder that NFA is expected to continue to evaluate and, as necessary, modify the revised registration fee and membership dues schedules to ensure that the above criteria, especially

^{41/} NFA Bylaw 1301.

regarding barriers to entry and inequities, continue to be met.

L.Kurjan