

September 1, 1983

Ms. Jane K. Stuckey
Office of the Secretariat
Commodity Futures Trading Commission
2033 K Street, N.W.
Washington, D.C. 20581

Re: National Futures Association; Proposed Amendments
to Bylaws

Dear Ms. Stuckey:

Pursuant to Section 17(j) of the Commodity Exchange Act, as amended, ("Act") National Futures Association ("NFA") hereby submits to the Commodity Futures Trading Commission ("Commission") the following amendments to Section I(e) of Schedule A to NFA's Bylaws and NFA Bylaw 301(i) which NFA intends to make effective ten days after receipt of this submission by the Commission. These amendments were approved by the NFA Board of Directors at its meeting on August 18, 1983. In the text below, where appropriate, additions are underscored.

I. Schedule A

Schedule A is amended to read as follows:

SCHEDULE A

* * *

I. REGISTRATION

* * *



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(e) Registration Fees

Associated Persons - Each Form 8-R submitted in connection with the registration of an associated person must be accompanied by a fee of \$30 for each registration capacity for which application is made.

Introducing Brokers - Each application for registration as an introducing broker must be accompanied by a fee of \$75 plus \$6 for each domestic branch office and each application for renewal of an existing registration as an introducing broker must be accompanied by a fee of \$25 plus \$6 for each domestic branch office.

* * *

II. Bylaw 301

Bylaw 301(i) is amended to read as follows:

CHAPTER 3

MEMBERSHIP AND ASSOCIATION WITH A MEMBER

Bylaw 301. Requirements and Restrictions.

* * *

(i) Name and Address.

Each Member shall at all times register and maintain with the Secretary its correct name and principal address, and the correct name and address of each registered Associate employed by the Member. The principal address of each Member and the address of each registered Associate currently on file with NFA shall be deemed by NFA the correct address for delivery to the Member or Associate of any communication, document or notice from NFA.

* * *

EXPLANATION OF AMENDMENTS

Schedule A

The amendment to Section I(e) of Schedule A, which is incorporated by reference into NFA's Bylaws through Bylaw 305, sets forth registration fees for introducing brokers in order to



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recover costs for processing registration applications for those categories of persons for whom NFA has registration responsibilities.

Bylaw 301

Bylaw 301(i) currently requires that each Member at all times maintain with NFA its correct name and principal address. It is essential that NFA know how to get in touch with each of its Members. However, if a Member fails to keep NFA informed of address changes NFA may have difficulty in delivering actual notice to the Member in connection with disciplinary proceedings or other matters. The purpose of this amendment is to parallel Commission Regulation 3.30 and specifically authorize NFA to deem the last principal address submitted by a Member to be its correct address for delivery to the Member of any communication, document or notice from NFA.

Pursuant to Section 17(j) of the Act, NFA also hereby files and requests review and approval of proposed Section II(a) of Schedule A to NFA's Bylaws and amendments to NFA Bylaws 1301(c) and 1302 adopted by NFA's Board of Directors at its meeting on August 18, 1983 and set forth below. In the following text, where appropriate, additions are underscored.

III. Schedule A

* * *

II. PROFICIENCY REQUIREMENTS

(a) Associated Person Qualification Testing Requirement

Any person applying to NFA for registration as an associated person of an introducing broker under the Act pursuant to Section I(a) of this Schedule A (except for persons who were registered as an associated person or who had applied for such registration as of August 1, 1983 and whose registration is not lapsed when application to NFA is made) shall not be so registered unless NFA receives satisfactory evidence that such person has taken and passed the National Commodity Futures Examination.

* * *



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IV . Bylaw 1301(c)

Bylaw 1301(c) is amended to read as follows:

CHAPTER 13

DUES AND ASSESSMENTS

Bylaw 1301. Schedule of Dues and Assessments.

* * *

(c) Other Members.

Annual dues for a Commodity Pool Operator or Introducing Broker shall be \$500 for the year of such entity's initial registration under the Act and thereafter shall be \$1,000 except that annual dues for an introducing broker not required to maintain minimum adjusted net capital shall be \$150. Annual dues for a Commodity Trading Advisor shall be \$500. All Members of NFA, other than those previously set forth in this Bylaw, shall pay to NFA annual dues of \$1,000. The Board may in its discretion waive or establish lower annual dues for such other Members, excluding Introducing Brokers, Commodity Pool Operators and Commodity Trading Advisors.

* * *

V. Bylaw 1302

Bylaw 1302 is amended to read as follows:

CHAPTER 13

DUES AND ASSESSMENTS

* * *

Bylaw 1302. Payment of Dues and Assessment.

Annual dues shall be payable in advance on the first day of January of each year, or at such other time or times as the Board shall determine. Members paying dues after the date such dues are payable shall be subject to a late payment charge of \$25 per month or portion thereof. Assessments based upon futures transactions shall be payable to NFA



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within thirty (30) days after the end of each NFA fiscal quarter for transactions effected during that quarter. In addition to such assessments each FCM shall pay to NFA an amount equal to one month's interest at an annual rate of 10% (or such other rate of interest as the President, with the concurrence of the Executive Committee, may determine from time to time) on the amount of any such assessment payable by the FCM for every month or fraction thereof such assessment payment is late. Except as the Board may otherwise provide by resolution, each Member shall pay dues and assessments, as applicable, for each category in which the Member --or an affiliate thereof, unless such affiliate is a Member in its own right-- is registered with the Commission and conducts business.

* * *

EXPLANATION OF AMENDMENTS

Schedule A

Section II(a) of Schedule A requires that all new APs of IBs have taken and passed the National Commodity Futures Examination. The amendment would "grandfather" all persons who were registered or who had applied for registration as an associated person of an FCM or IB as of August 1, 1983 and who are currently so registered.

Bylaw 1301(c)

The CFTC has adopted rules relating to IBs which will permit an IB which obtains a guarantee of its liabilities from an FCM to be registered without maintaining any minimum net capital. NFA understands this provision to be intended for the benefit of smaller entities which are closely tied to an FCM willing to accept responsibility for the IB and which cannot afford to meet a minimum capital requirement. Because the type of IBs which would do business under an FCM guarantee may be quite distinct from the type which would maintain their own capital, the Board determined to establish different dues requirements for the two types of IBs.

Bylaw 1302

The Board previously has adopted an amendment to Bylaw 1302 to establish a penalty for late payment by FCMs of NFA Assessment Fees. The pattern of payment of Assessment Fees for



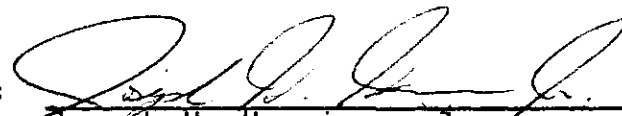
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the last quarter of fiscal 1983 indicates that the late payment penalty is working well to assure timely payment. As a result of the success of the rule, NFA has further amended Bylaw 1302 to establish a late annual dues payment charge of \$25 per month.

NFA respectfully requests that Section II(a) of Schedule A and the amendments to Bylaw 1301(c) and Bylaw 1302 be declared effective upon approval by the Commission and that Section I(e) of Schedule A and the amendment Bylaw 301(i) become effective ten days after receipt by the Commission.

Very truly yours,

NATIONAL FUTURES ASSOCIATION

By: 
Joseph H. Harrison, Jr.
General Counsel and Secretary

JHH:ep
cc: Acting Chairman Susan M. Phillips
Commissioner Kalo A. Hineman
Commissioner Fowler C. West
Andrea A. Corcoran, Esq.
Theodore W. Urban, Esq.
Linda Kurjan, Esq.



COMMODITY FUTURES TRADING COMMISSION
2033 K STREET, N.W., WASHINGTON, D.C. 20581

SEP 19 1983

September 15, 1983

Mr. Joseph H. Harrison, Jr.
General Counsel and Secretary
National Futures Association
200 West Madison Street, Suite 1600
Chicago, Illinois 60606

Dear Mr. Harrison:

On September 6, 1983, the Commission received your September 1 letter which submitted, among other rule proposals, NFA's proposed amendment to Bylaw 310(i) regarding current addresses of members and associates on file with NFA. This proposal was submitted under the provision in section 17(j) of the Act that would permit the amendment to take effect ten days after Commission receipt (i.e., September 16) unless the Commission notified NFA in writing that the Commission determined to review the rule proposal for approval. This is to inform you that this Division examined the proposed amendment to Bylaw 301(i) and does not intend to recommend that the Commission review it for approval.

Very truly yours,

Theodore W. Urban
Commission Liaison to NFA

UNITED STATES OF AMERICA
COMMODITY FUTURES TRADING COMMISSION

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



September 15, 1983

SEP 19 1983

Joseph H. Harrison, Jr.
General Counsel and Secretary
National Futures Association
200 West Madison Street, Suite 1600
Chicago, Illinois 60606

Dear Mr. Harrison:

On September 6, the Commission received your submission of various NFA rule proposals, including an amendment to Part I(e) of Schedule A to Bylaw 305. That amendment sets forth the fees NFA proposes to assess applicants for initial and renewed registration as introducing brokers. NFA submitted these fee proposals under the provision of section 17(j) of the Commodity Exchange Act that permits a rule proposal to take effect 10 days after Commission receipt unless the Commission notifies NFA of a determination to review the rule proposal for approval.

This is to notify you that the Commission has determined to review this amendment for approval in accordance with the provisions of section 17(j). In order to proceed with its review, however, the Commission will need additional information to support NFA's statement in its submission that NFA is proposing these fees in order to recover costs for processing the applications for introducing brokers. Specifically, the Commission requests that NFA describe the costs involved in performing these registration functions and the degree to which the proposed fees will offset those costs. In addition, the Commission requests that NFA explain how it will implement the fees. In this regard, will the proposed fees be imposed only on applications submitted after a particular date or does NFA also intend to collect fees from those who will have already applied by the time the rule takes effect? If the latter, please describe what measures NFA has taken to notify applicants that they may be subject to such a fee.

Very truly yours,

Jane K. Stuckey
Jane K. Stuckey
Secretary of the Commission

UNITED STATES OF AMERICA
COMMODITY FUTURES TRADING COMMISSION

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



November 30, 1983

DEC - 2 1983

Mr. Joseph H. Harrison, Jr.
General Counsel
National Futures Association
200 West Madison Street
Chicago, Illinois 60606

Re: Section I(e) of Schedule A under Bylaw 305,
and Bylaws 1301(c) and 1302

Dear Mr. Harrison:

By your letter of September 1, 1983, NFA submitted amendments to the captioned rules pursuant to section 17(j) of the Commodity Exchange Act. With the exception of Section II(a) of Schedule A under Bylaw 305, the Commission approved those amendments on November 29, 1983. The Commission understands that the approved amendments will be implemented immediately.

In approving the fee proposals, the Commission finds that they appear to reflect an equitable allocation of projected costs. Nevertheless, the Commission reminds NFA that, as it gains experience with the services and programs which these fees are intended to support, the Commission expects NFA to continue to evaluate its fees to assure that they reflect an equitable allocation among its members of the actual costs of performing its regulatory functions.

As you are aware, the Commission has not yet completed its review of proposed Section II(a) of Schedule A under Bylaw 305, which was also submitted in your September 1, letter. That provision would require certain new applicants for registration as an associated person of an introducing broker to pass a proficiency test as a condition of such registration under the Act. The Commission understands that you intend to submit additional information and analysis on the issue of whether section 17(p) of the Act requires NFA to establish a testing requirement for all categories of registrants and whether other alternative criteria may be adopted to exempt certain persons from any such proficiency testing requirement. The Commission expects that its review will be concluded as soon thereafter as possible.

Very truly yours,

Jane K. Stuckey

Jane K. Stuckey
Secretary of the Commission

January 3, 1983

Ms. Jane K. Stuckey
Secretary
Commodity Futures Trading Commission
2033 K Street, N.W.
Washington, D.C. 20581

Dear Ms. Stuckey:

On September 1, 1983 National Futures Association ("NFA") submitted to the Commodity Futures Trading Commission ("Commission") for its review pursuant to Section 17(j) of the Commodity Exchange Act ("Act") a number of proposed amendments to NFA Bylaws, including proposed Section II(a) of Schedule A to NFA Bylaws ("Section II(a)"). Section II(a) would establish a proficiency testing requirement for associated persons ("APs") of introducing brokers ("IBs"). Section II(a) also provides that, for the time being, those persons who were registered as or who had applied for registration as APs of either an FCM or an IB by August 1, 1983 and who are currently so registered would be exempted from the testing requirement. NFA intends Section II(a) to be its first step toward its program to establish proficiency standards (through training, experience or testing) for all persons for whom NFA has registration responsibility. This letter is intended to supply the additional information and analysis referred to in your letter of November 30, 1983 concerning whether an exemption from the testing requirement is an acceptable method under Section 17(p)(1) of the Act to phase in NFA's comprehensive proficiency standards. It is our understanding that the Act clearly permits such flexibility and that practical considerations require it.

An analysis of the validity of Section II(a) must begin with Section 8a(10) of the Act. Section 8a(10) allows the Commission:

"to authorize any person to perform any portion of the registration functions under this Act, in accordance with rules, notwithstanding any other provision of law, adopted by such person and submitted to the Commission . . . for review pursuant to Section 17(j) of this Act. . . ." (emphasis supplied)

On July 28, 1983 the Commission exercised its authority under Section 8a(10) and issued its Notice and Order "to authorize NFA to grant applications for registration of IBs and APs of IBs under sections 4(d) and 4k(1) of the Act. . . ." 48 Fed. Reg. 35,158 (1983). This Order, the product of careful and thorough consideration by both the Commission and NFA,



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clearly authorizes NFA to do more than issue a registration. The authority to register applicants necessarily includes the authority to determine their fitness for registration by applying the same standards of fitness which the Commission itself would apply under the Act. In fact, Section 8a(10) of the Act makes clear that an authorization to perform registration functions is "subject to the provisions of [the] Act applicable to registrations granted by the Commission."

Section 4p of the Act forms an integral part of the Commission's authority to determine an applicant's fitness for registration. Logic dictates, and NFA assumes, that the Commission's registration function outlined in Section 4p of the Act is within the penumbra of registration functions which NFA has been authorized to perform pursuant to Section 8a(10). Since Section 8a(10) provides that NFA perform its authorized registration functions in accordance with NFA rules, it is clear that the Commission has already authorized NFA to adopt rules, subject to Commission approval, under which NFA will perform the following registration functions defined in Section 4p:

- 1) "[to] specify . . . appropriate standards with respect to training, experience and such other qualifications . . . as are necessary or desirable to insure the fitness of persons required to be registered with the Commission;"
- 2) "[to] adopt written proficiency examinations to be given to applicants for registration and charge reasonable fees to such applicants to cover the administration of such examinations;"
and
- 3) "[to] specify . . . such terms and conditions as it deems appropriate to protect the public interest wherein exception to any proficiency examination shall be made with respect to individuals who have demonstrated, through training and experience, the degree of proficiency and skill necessary to protect the interests of customers, clients, pool participants, or other members of the public with whom such individuals deal."

Section II(a) is, therefore, a valid, albeit partial, exercise of a Commission function under Section 4p which the Commission has authorized NFA to perform pursuant to Section 8a(10). Section II(a) is the first step by NFA to establish the network of safeguards authorized by Section 4p to insure that all applicants for whom NFA has registration responsibility possess a required degree of expertise. NFA assures



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the Commission that, as NFA develops and adopts its proficiency standards, it will reevaluate and adjust its requirements so that no applicant or registrant shall become or remain registered absent some assurance that such person possesses the required degree of expertise.

Fundamental rules of statutory construction, the legislative history of the Act, the language of Section 17(p)(1) and plain common sense all indicate that Section 17(p)(1) in no way curtails the Commission's authority, pursuant to Section 8a(10), to authorize NFA to perform any aspect of the Commission's Section 4p registration functions, including the granting of exemptions to a proficiency testing requirement.

Section 4p and Section 17(p)(1) are in pari materia in that both Sections deal with the same subject matter--the performance by a registered futures association of certain proficiency screening functions. It is a fundamental rule of construction that statutes in pari materia must be construed together and that, whenever possible, their provisions be harmonized. When read in this light it is clear that there is no conflict between these two Sections. Section 4p simply authorizes the Commission to perform certain enumerated registration functions and, by that Section's own terms and by operation of Section 8a(10), to authorize NFA to perform those functions. Although Section 17(p)(1) also addresses the subject of proficiency, the Congress which carefully preserved the flexibility of futures associations in amending 4p, could not have intended to remove that flexibility through Section 17(p)(1). Clearly the purpose of Section 17(p)(1) was merely to make mandatory implementation of NFA proficiency screening by September 30, 1985 and to remove any doubt that such screening could be applied to non NFA members.

This conclusion is confirmed by the legislative history of Section 4p. In discussing the 1982 amendments to Section 4p, the Senate Committee on Agriculture, Nutrition and Forestry stated in its Report that:

"The Committee envisions that any fitness standards for registrants will be developed in cooperation with the National Futures Association. Administration of proficiency examinations is an area the Committee believes is appropriate for delegation to the National Futures Association, with oversight by the Commission." (S. Rep. No. 384, 97th Cong., 2nd Sess., 40 (1982)).

It is, thus, apparent, that the Congress felt that the "administration of proficiency examinations" under Section 4p, which includes granting appropriate exemptions to such examinations, is "appropriate for delegation" to NFA.



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The Congressional intent that Section 17(p)(1) not deprive NFA of the flexibility provided by Section 4p was also apparent in the legislative record of the House of Representatives. The Report of the House Committee on Agriculture on the 1982 amendments to the Act discussing Section 4p stated:

"Mr. Richmond suggested that it might be worthwhile to indicate in the language of the bill that the National Futures Association should test salesmen. Mr. Glickman indicated that he would offer a later amendment to mandate testing by the National Futures Association. He also pointed out that the proposed amendment was necessary because some people required to register with CFTC would not be covered by the National Futures Association." (H.R. Rep. No. 565, 97th Cong., 2nd Sess., 133-134 (1982)).

Section 17(p)(1), the "later amendment" referred to above, is clearly described as a mandate that NFA perform the proficiency screening functions described in Section 4p with respect to certain persons. There is no indication, explicit or implicit, that NFA should be barred from performing the full range of functions described in Section 4p.

Even without the benefit of legislative history, the language of Section 17(p)(1) does not preclude exemptions to proficiency testing requirements. Section 17(p)(1) does not require NFA to administer proficiency tests for all persons for whom it has registration responsibility. Rather, Section 17(p)(1) requires, in relevant part, that NFA adopt rules which require NFA to establish "training standards and proficiency testing for . . . all persons for which it has registration responsibilities."* (emphasis supplied). The

*NFA complied with the requirements of Section 17(p)(1) by amending Bylaw 301(b)(ii) (currently NFA Bylaw 301(d)) to read as follows:

(A) no person may become or remain an FCM, CTA, CPO or Introducing Broker Member or associated with such a Member unless qualified to do so in conformity with such standards of training and experience and proficiency testing requirements as NFA shall establish and such other qualification standards as NFA finds necessary or desirable;"

NFA submitted this amendment for the Commission's review pursuant to Section 17(j) of the Act by letter dated March 9, 1983, and the Commission approved it on April 11, 1983. It should be noted that Section II(a) is consistent with the amended Bylaw 301 as cited above.



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January 3, 1984
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obvious intent of Congress was that NFA establish, by its own rules, training standards and testing requirements which together operate to filter out unqualified applicants in the registration process. Section II(a) is a concrete step toward establishing such a filtering system. As NFA adopts its training standards it will reevaluate its testing program to insure that its training standards and testing program mesh to form the comprehensive safeguard to the public envisioned by both Section 17(p)(1) and Section 4(p).

The potentially overwhelming practical problems* which would be created by immediate universal proficiency testing by NFA demonstrate that Congress was wise to create and the Commission was wise to implement the opportunity for NFA to take the flexible approach set forth in Section 4p. If an immediate universal testing requirement were imposed, NFA would be required to make a separate determination for each of the approximately 5,000 APs of IBs that each such AP had passed the examination. Further, NFA would be required to design and administer an appropriate revocation procedure for those registrants who, for whatever reason, were unable to produce evidence that they had passed the examination. Even without this added burden, NFA has been required to more than double its registration staff to administer the manual registration system currently in place.

The problems outlined above would, of course, be literally multiplied when NFA assumes registration responsibility for the approximately 65,000 APs of FCMs. Universal application of the proficiency testing requirement from its very outset would unnecessarily clog the registration process and would create the sort of administrative delays

*The Commission was apparently well aware of these practical problems when it granted NFA registration. In its September 22, 1981 Order Granting Registration and Approving Rules the Commission stated:

"The NFA initially will screen applicants for membership and registration as associates to determine whether they meet the qualifications prescribed in Bylaw 301 and, if they are qualified, grant them membership or registration. The NFA has indicated, however, that it intends to develop fitness standards and administer proficiency examinations for associates. Thus, while the NFA initially may grandfather APs registered with the Commission, unrestricted continuing registration by the NFA may be conditioned upon subsequent passage of such an examination." (Registration Order at page 8; footnotes omitted) (emphasis supplied)



Ms. Jane K. Stuckey
January 3, 1984
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which all parties would hope to avoid. Doubtless, it was practical concerns such as these which led the New York Stock Exchange and the National Association of Securities Dealers to adopt "grandfathering" provisions of their own similar to that provided in Section II(a).

In sum, the Commission, by its Order of July 28, 1983, has acted, pursuant to Section 8a(10) of the Act, to authorize NFA to perform a portion of the Commission's registration functions, including the Commission's registration functions as set forth in Section 4p. Section II(a) is NFA's first step in implementing its derivative authority under Sections 8a(10) and 4p. Nothing in Section 17(p)(1) invalidates either the Commission's delegation of or NFA's implementation of that authority.

Sincerely,

Joseph H. Harrison, Jr.
General Counsel

JHH:dmc

cc: Chairman Susan M. Phillips
Commissioner Kalo A. Hineman
Commissioner Fowler C. West
Commissioner William E. Seale
Andrea M. Corcoran, Esq.
Kenneth Raisler
Theodore W. Urban, Esq.

UNITED STATES OF AMERICA
COMMODITY FUTURES TRADING COMMISSION

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



MAY 7 1984

May 4, 1984

Mr. Joseph H. Harrison, Jr.
General Counsel and Secretary
National Futures Association
200 West Madison Street
Chicago, Illinois 60606

Re: Section II(a) of Schedule A (Bylaw 305) and
Compliance Rule 2-24

Dear Mr. Harrison:

By your letter of September 1, 1983, NFA submitted, among other things, Section II(a) of Schedule A for Commission approval pursuant to section 17(j) of the Commodity Exchange Act. This proposal establishes a testing requirement for certain applicants for registration as associated persons of introducing brokers ("AP/IB"). The requirement will operate as a condition of registration for APs/IBs. NFA supplemented the original submission by letter dated January 3, 1984. Subsequently, NFA submitted Compliance Rule 2-24 for Commission approval (your letter dated February 29, 1984). This second proposal establishes a testing requirement for certain associated persons of NFA-member futures commission merchants ("AP/FCM"). Unlike the AP/IB proposal, AP/FCM testing will operate as a compliance requirement affecting the employing FCM. This is to inform you that the Commission approved the proposed rule on May 4, 1984. Both Section II(a) and Compliance Rule 2-24 may be made effective immediately.

In approving the testing requirements, the Commission relies upon section 17 of the Act and NFA's commitment to establish appropriate standards of training and experience to serve as an effective alternative measure of the proficiency of those APs/IB and APs/FCM who are not required by these rules to take and pass the National Commodity Futures Examination. Although NFA has until September 30, 1985, to implement such alternative proficiency criteria, the Commission urges NFA to develop those standards as soon as possible. Similarly, the Commission urges NFA not to delay proposing appropriate testing and other proficiency requirements for IB applicants who are individuals, since the Commission has also granted NFA registration responsibilities over the introducing broker category of registrants, as well as all other individuals within NFA's regulatory jurisdiction who are involved in the solicitation of transactions subject to the provisions of the Act and their supervisors.


Mr. Joseph H. Harrison, Jr.
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In this regard, the Commission requests NFA to provide within 60 days a detailed description of NFA's plans to develop and implement the remaining elements of the comprehensive program mandated by sections 17(p)(1) and (q) of the Act. This information should cover (but not be limited to) the particular types of standards being developed, the minimum qualifications preliminarily being considered to demonstrate sufficient proficiency and skill under each standard, and a timetable for implementing these standards for each category of NFA members and associates and for each category of registrant for which NFA acquires responsibilities.

The Commission expects NFA to justify any substitution of other standards in place of testing requirements by demonstrating how these standards will assure equivalent expertise by an individual. In this regard, any use of work experience in establishing such other standards should include an analysis explaining how such experience would demonstrate at least a comparable level of expertise. Moreover, the Commission expects NFA, in developing these plans, to reevaluate the two testing rules approved herein and provide an assessment as to what adjustments may be needed to assure that all APs of IBs and APs of FCMs will demonstrate a satisfactory level of expertise.

Although the Commission's approval will be necessary to institute the additional standards which must be adopted in fulfillment of section 17(p)(1), the information that NFA is being asked to provide now is being requested to apprise the Commission of NFA's plans and to assist it in monitoring NFA's progress and will, of course, not be viewed as a submission under section 17(j) of the Act. If you have any questions concerning this Commission request, please contact Linda Kurjan, Special Counsel in the Division of Trading and Markets, at (202) 254-8955.

Very truly yours,


Jane K. Stuckey
Secretary of the Commission

July 2, 1984

Ms. Jane K. Stuckey
Office of the Secretariat
Commodity Futures Trading Commission
2033 K Street, N.W.
Washington, D.C. 20581

Re: NFA Plans for Fulfillment of Responsibility under
Section 17(p)(1) of the Commodity Exchange Act

Dear Ms. Stuckey:

Your letter of May 4, 1984, approving NFA Compliance Rule 2-24 and Section II(a) of Schedule A to NFA Bylaw 305 ("Section II(a)"), requested that NFA provide the Commodity Futures Trading Commission ("Commission") with "a detailed description of NFA's plans to develop and implement the remaining elements of the comprehensive program mandated by Section 17(p)(1) and (q) of the Act." More specifically, your letter requested information concerning the alternative proficiency standards being considered by NFA, the qualifications which may be deemed to satisfy those standards and a timetable for their implementation.*

As the Commission knows, Section 17(p)(1) requires NFA to adopt rules which "establish training standards and proficiency testing for persons involved in the solicitation of transactions subject to the provisions of this Act, supervisors of such persons and all persons for which it has registration responsibilities, and a program to audit and enforce compliance with such standards." Furthermore, Section 301(d) of NFA's Bylaws, as approved by the Commission, requires NFA to establish standards of training and experience and proficiency testing requirements and Bylaw 305 makes clear that those standards of proficiency are to be used both for determining fitness to be registered and qualification for NFA membership. NFA intends to comply with the congressional mandate and the mandate of its own rules by developing a thorough screening process to insure that all

* This information was requested for each category of NFA Member and Associate and for each category of registrant for which NFA acquires registration responsibility. Since NFA expects its qualifications for Associate membership to parallel its rules governing registration, no distinction between registration and membership criteria will be noted for the purposes of this response.



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Page Two

persons subject to NFA regulatory jurisdiction or for whom NFA has registration responsibility possess a required degree of knowledge. This screening process will be based on proficiency testing requirements which will filter applicants for registration or membership on the basis of minimum entry level knowledge needed to perform their duties. NFA believes that testing requirements, which necessarily determine whether the tested individual has been adequately trained, obviate the need to establish separate training standards for persons for which NFA has registration responsibility. Although, as discussed below, NFA must rely on the training and experience of a closed group of "grandfathered" individuals as a substitute for testing, NFA does not intend in the future to accept on-the-job experience or training programs, alone or together, as an alternative to the testing requirements.

The adoption of NFA Compliance Rule 2-24 and Section II(a) represents the first step in implementing a comprehensive associated person ("AP") testing program. NFA is currently developing an appropriate proficiency test for APs of Commodity Pool Operators ("CPOs") and Commodity Trading Advisors ("CTAs") which should be operational by December 31, 1984. At that time there will be in place a testing requirement for all APs of Futures Commission Merchants ("FCMs"), Introducing Brokers ("IBs"), CPOs and CTAs.

Once the AP testing requirement is fully established it will necessarily satisfy NFA's responsibility to apply proficiency testing to the FCMs, IBs, CPOs and CTAs themselves.* Under the Commission's Interpretive Statement Regarding the Scope of the Term "Supervision" in the Associated Person Registration Requirement, [1980-82 Transfer Binder] Comm. Fut. L. Rep. (CCH) §21,069 (1980), to which NFA has strictly adhered in performing registration respon-

* Your letter also urged NFA "not to delay proposing appropriate testing and other proficiency requirements for IB applicants who are individuals..." NFA has consistently treated individual applicants for IB registration as both principals and APs and has required such individuals to comply with Section II(a)'s testing requirements. NFA staff will, however, seek the approval of NFA's Board of Directors of an amendment to Section II(a) which clarifies the requirement that sole proprietor IBs must pass the NCPE.



Ms. Jane K. Stuckey
July 2, 1984
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sibilities with respect to IBs and their APs, every individual in the supervisory "chain of command" will be required to become an AP and, therefore, be tested. Although NFA's appropriate Member committees and Board of Directors may in the future consider adoption of additional testing requirements which focus on the expertise necessary to perform particular management or supervisory functions within a firm (e.g., tests similar to those required of various types of principals by the National Association of Securities Dealers, Inc. ("NASD")), NFA believes that the basic AP testing requirement will be adequate to satisfy NFA's statutory testing responsibilities with respect to FCMs, IBs, CPOs, CTAs as well as their respective APs.

NFA has, and will maintain, an adequate program to audit and enforce compliance with its proficiency testing requirements. Currently the testing requirement for APs of IBs is established through Section II(a), which makes testing a condition of registration, and the testing requirement for APs of FCMs is established through Compliance Rule 2-24 as a compliance requirement of the sponsoring FCM Member. NFA contemplates that, for categories of APs for which NFA does not yet have registration responsibilities, testing requirements will be imposed by amendment of Compliance Rule 2-24. As NFA assumes registration responsibility for those categories of APs, NFA will also adopt rules similar to Section II(a) which will apply the testing requirement as a direct condition of registration. After this set of rules is in place (no later than December 31, 1984) NFA will be able to avail itself of two approaches to enforcement. First, NFA will require APs to prove that they have passed the appropriate test prior to registration. Second, NFA's audit programs will include steps designed to determine if Member firms have complied with the appropriate testing requirement with respect to their APs.

Once the testing requirement for APs of CPOs and CTAs is made effective, NFA could continue to require one test (the National Commodity Futures Examination ("NCFE" or "Series 3 Examination")) to be passed by all new APs of FCMs and IBs and require a separate test to be passed by APs of CPOs or CTAs. Alternatively NFA is considering providing for and requiring passage of only specialized examinations for APs whose futures-related activities will be limited



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appropriately.* NFA believes that adoption of requirements prescribing such specialized tests would be consistent with NFA's statutory responsibility provided that NFA takes appropriate steps to enforce adherence by the relevant APs to the necessary limitations on their activities. NFA is also aware of the possibility that entry level knowledge necessary to perform certain specialized activities may already be adequately tested by an existing examination administered by another agency or organization such as NASD. Although NFA generally intends to develop and administer its own examinations, NFA believes that it would also be consistent with its statutory responsibility to establish a requirement that certain APs who will engage in specifically limited futures-related activities demonstrate the necessary minimum entry level knowledge by passing an examination administered by NASD or another regulatory organization.

NFA does not believe that the grandfathering provisions necessarily incorporated in Compliance Rule 2-24 and in Section II(a) defeat or are inconsistent with the purposes of Section 17(p)(1) of the Act.** That section is aimed at ensuring that persons dealing with the public possess at least a minimum level of proficiency. As the Commission recognized in proposing its own testing requirements, profi-

* See NFA's Notice to IB Registrants and Applicants for IB Registration entitled "NFA Bylaw 305: Testing Requirements" dated May 25, 1984; and NFA's Notice to FCM Members of NFA entitled "NFA Compliance Rule 2-24: Testing Requirements" dated May 25, 1984; attached to this letter.

** NFA expects that its rules establishing a testing requirement for APs of CPOs and CTAs will also include a grandfathering provision. As the Commission has recognized in similar cases of actual or proposed application of new industry-wide requirements, the cost of compliance and the practical burden on NFA of reviewing the records of many thousands of existing APs to determine who must pass an examination in order to be able to work in a registered capacity or retain a registration requires implementation of grandfathering provisions. See [1980-82 Transfer Binder] Comm. Fut. L. Rep. (CCH) §21,114, 45 Fed. Reg. 80485 (December 5, 1980) ("grandfather" provision incorporated in fingerprinting requirements for APs); and [1980-82 Transfer Binder] Comm. Fut. L. Rep. (CCH) §21,172, 46 Fed. Reg. 20679 (April 7, 1981) ("grandfather" provision in proposed proficiency testing requirement).



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ciency testing does not determine skill or ability. Instead, the function of proficiency testing is to determine "entry level knowledge, that is, the minimum knowledge that an AP needs to function in a manner that protects the interests of customers...."* Although NFA has not collected empirical data on this point, common sense justifies the presumption that the actual experience of working as an AP for a significant period of time inevitably provides the type of entry level knowledge which Section 17(p)(1) seeks to establish throughout the industry. The experience of dealing with customers on a daily basis, subject to proper supervision, provides an individual with a unique perspective on customer concerns, the operation of the markets and the AP's duties to his customers.

The APs who have been grandfathered under the existing testing rules (or who will be grandfathered under the rules applicable to APs of CPOs and CTAs) constitute a closed universe of individuals whose experience as an AP must, as a practical matter, be continuous from at least the grandfathering date. Unlike the proposed CFTC proficiency testing rule which would have grandfathered all existing APs and continued the testing exemption for grandfathered APs who had a lapse in registration of less than two years, NFA's grandfathering provisions only relieve APs from the testing requirement for as long as they remain continuously registered as APs. The closed group of grandfathered APs will either continue to gain experience as APs, under the supervision required by NFA and CFTC rules, or they will be tested pursuant to NFA's testing rules. Therefore, the group of grandfathered APs will never increase in size but will only decrease and, with respect to those that remain grandfathered, NFA is permitted to make the reasonable assumption that they have achieved at least minimum entry level knowledge in the course of their continuous experience.

NFA, however, is not without the power to require testing of grandfathered APs in appropriate cases. Under NFA Compliance Rule 3-11(a)(v) NFA's Business Conduct Committees are empowered to take any fitting remedial action in response to a finding that NFA requirements have been violated. Therefore, if it were proved that grandfathered APs

* [1980-82 Transfer Binder] Comm. Fut. L. Rep. (CCH) §21,172 at 24,709, 46 Fed. Reg. 20679 (April 7, 1981).



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were not in a position to gain the necessary knowledge through experience due to a failure of the Member to adequately supervise its APs or due to some other violation by the Member, the Business Conduct Committee could, in response, order the Member to require its APs to be tested in addition to other sanctions. NFA staff will, of course, make the necessary recommendations to the Business Conduct Committees in appropriate cases.

NFA expects to have its AP testing requirements in place prior to December 31, 1984 by which time NFA expects to have assumed registration responsibilities for FCMS, CPOs, CTAs and their respective APs. NFA is aware that the Commission will need to assure itself of the validity and reliability of the tests which NFA relies upon as proficiency screening tools. NFA would be happy to discuss this with the Commission further and make appropriate arrangements.

If the Commission requires further information in this area, NFA will be pleased to respond.

Sincerely,

A handwritten signature in dark ink, appearing to read 'Joseph H. Harrison, Jr.', is written over a horizontal line.

Joseph H. Harrison, Jr.
General Counsel

JHH:cm

Enclosures

cc: Chairman Susan M. Phillips
Commissioner Kalo A. Hineman
Commissioner Fowler C. West
Commissioner William E. Seale
Andrea M. Corcoran, Esq.
Kenneth M. Raisler, Esq.
Kenneth M. Rosenzweig, Esq.

I-84-9

May 25, 1984

NOTICE TO IB REGISTRANTS AND APPLICANTS FOR IB REGISTRATION

NFA BYLAW 305: TESTING REQUIREMENTS

Section 17(p) of the Commodity Exchange Act requires NFA to adopt rules "which establish training standards and proficiency testing for persons involved in the solicitation of transactions subject to the provisions of this Act, supervisors of such persons, and all persons for which it has registration responsibilities and a program to audit and enforce compliance with such standards."

In order to comply with this statutory responsibility NFA is developing a comprehensive screening process to insure that all persons for which NFA has registration responsibility satisfy minimum proficiency standards. This screening process will include consideration of the training and experience of registrants as well as standardized testing programs. NFA is currently phasing in testing programs for APs of FCMS, IBs, CPOs and CTAs.

As an initial step, NFA's Board of Directors has adopted and the CFTC has approved the following amendment to Schedule A of NFA Bylaw 305:

II PROFICIENCY REQUIREMENTS

(a) Any person applying to NFA for registration as an associated person of an introducing broker under the Act pursuant to Section I (a) of this Schedule A (except for persons who were registered as an associated person or who had applied for such registration as of August 1, 1983 and whose registration is not lapsed when application to NFA is made) shall not be so registered unless NFA receives satisfactory evidence that such person has taken and passed the National Commodity Futures Examination.

Simply stated, the effect of this provision is that no person may become registered or temporarily licensed as a AP of an IB unless that person has either taken and passed the National Commodity Futures Examination ("NCFE" or "Series 3") or had been registered or had applied for registration as an AP by August 1, 1983.

This rule also applies to a person who applies for registration as an AP of an IB by filing Form 8-S. CFTC Regulations provide that in such cases the registration as

an AP of an IB is effective as of the mailing of the 8-S. While that remains true, anyone who becomes registered as an AP of an IB in that manner must, unless he qualifies for the "grandfathering" exemption, file with NFA within 60 days, along with a Form 8-R and a legible fingerprint card, proof that he has taken and passed the Series 3 examination. Failure to file any of these items within the 60 day period will cause the AP's registration to lapse.

One question which remains open is what type of testing program, if any, should be applied to persons registered with the NASD as General Securities Representatives whose only futures-related activity is the solicitation of prospective commodity pool participants. Until that question is resolved, such individuals may be registered as APs of IBs without passing the Series 3 examination, though they may be required to take and pass the Series 3 or another proficiency examination at a later date. Such an individual must supply to NFA proof of NASD registration and a certification (substantially equivalent to the form provided by NFA) signed by the individual applicant and his sponsoring IB stating that the individual's futures-related activity will be limited to solicitation of prospective pool participants.

In addition, NFA's Board of Directors has taken a "no action" position with respect to enforcement of the testing rule where the applicant for registration as an AP of an IB is registered with the NASD as a General Securities Representative, has passed the Series 20 examination offered by the New York Futures Exchange and limits his activities to the area of stock index products. This "no action" position will continue until December 31, 1984. Any person applying for registration as an AP of an IB before December 31, 1984, who wishes to take advantage of this "no action" position must submit with his application for registration proof of NASD registration, proof that he has passed the Series 20 examination and a certification (substantially equivalent to the form provided by NFA), signed both by the individual applicant and his sponsoring IB, stating that the person will limit his futures-related activity to soliciting or accepting orders for stock index products or supervising only persons whose futures-related activities are so limited.

Persons registered as an AP of an IB without having passed the Series 3 examination in reliance upon the limitations on activities described above will, upon registration, receive through their sponsors a notice of registration noting the applicable restriction. APs which are subject to the above restrictions and who transfer to a new sponsor and file a form 8-S will also receive notice of the applicable restriction through the sponsor shortly after filing the 8-S. IB sponsors are, pursuant to NFA Compliance Rule 2-9,

End

under a duty to determine applicable restrictions and to supervise all such APs to insure that the applicable restrictions are observed. Any AP who is subject to a restriction and who transfers to a new sponsor by filing a form 8-S must, within 60 days, also file the appropriate certification (described above) signed by the AP and by the new sponsor.

If you have any questions regarding this matter please do not hesitate to call NFA.

CERTIFICATION

STOCK INDEX PRODUCT TESTING "NO ACTION"

I, _____ ("Applicant"), and _____ ("Sponsor") as a part of Applicant's application for registration as an Associated Person ("AP") of Sponsor hereby certify as follows:

1. Applicant is currently registered with the National Association of Securities Dealers, Inc. ("NASD") as a General Securities Representative (documentation attached).
2. Applicant has taken and passed New York Futures Exchange Registered Commodity Representative (Series 20) Examination (documentation attached).
3. Applicant's sole activities, subject to regulation by the Commodity Futures Trading Commission ("CFTC"), are and will continue to be limited to the solicitation or acceptance of customer orders for stock index futures or options on such futures or to the supervision of persons whose activities are so limited unless and until Applicant submits to National Futures Association ("NFA") satisfactory evidence of having taken and passed the National Commodity Futures Examination as required by Section II(a) of Appendix A to NFA Bylaw 305.
4. Sponsor understands that Sponsor must supervise Applicant's compliance with the limitation on Applicant's activities set forth in paragraph 2 above and that any failure of Applicant to adhere to those limitations may be cause for, among other things, disciplinary action by NFA for violation of NFA Compliance Rule 2-9.
5. Applicant and Sponsor understand that willfully making a materially false or misleading statement in this Certification is cause for denial, suspension or revocation of registration and criminal prosecution.

(Signature of Applicant)

(Print Name of Sponsor)

(Print Name of Applicant)

(Signature & Title of Sponsor's Authorized Signatory*)

(Date)

(Print Name & Title of Sponsor's Authorized Signatory)

(Date)

* Must be signed by an officer if a corporation, a general partner if a partnership, or the sole proprietor if a sole proprietorship.

CERTIFICATION

TEMPORARY TESTING EXEMPTION FOR APs
SOLICITING ONLY POOL PARTICIPANTS

I, _____ ("Applicant"), and _____
("Sponsor") as a part of Applicant's application for registration as an
Associated Person ("AP") of Sponsor hereby certify as follows:

1. Applicant is currently registered with the National Association of Securities Dealers, Inc. ("NASD") as a General Securities Representative (documentation attached).
2. Applicant's sole activities, subject to regulation by the Commodity Futures Trading Commission ("CFTC"), are and will continue to be limited to the solicitation of funds, securities or property for a participation in a commodity pool or to the supervision of persons whose activities are so limited unless and until Applicant submits to National Futures Association ("NFA") satisfactory evidence of having taken and passed the National Commodity Futures Examination as required by Section II(a) of Appendix A to NFA Bylaw 305.
3. Sponsor understands that Sponsor must supervise Applicant's compliance with the limitation on Applicant's activities set forth in paragraph 2 above and that any failure of Applicant to adhere to those limitations may be cause for, among other things, disciplinary action by NFA for violation of NFA Compliance Rule 2-9.
4. Applicant understands that NFA may in the future prescribe a testing requirement applicable to Applicant as a condition of retaining Applicant's registration, if granted, and that Applicant's registration, if granted, may be suspended or revoked if Applicant does not comply with such testing requirement.
5. Applicant and Sponsor understand that willfully making a materially false or misleading statement in this Certification is cause for denial, suspension or revocation of registration and criminal prosecution.

(Signature of Applicant)

(Print Name of Sponsor)

(Print Name of Applicant)

(Signature & Title of Sponsor's
Authorized Signatory*)

(Date)

(Print Name & Title of Sponsor's
Authorized Signatory)

(Date)

* Must be signed by an officer if a corporation, a general partner if a partnership, or the sole proprietor if a sole proprietorship.

I-84-8

May 25, 1984

NOTICE TO FCM MEMBERS OF NFA

NFA COMPLIANCE RULE 2-24: TESTING REQUIREMENTS

Section 17(p) of the Commodity Exchange Act requires NFA to adopt rules "which establish training standards and proficiency testing for persons involved in the solicitation of transactions subject to the provisions of this Act, supervisors of such persons, and all persons for which it has registration responsibilities and a program to audit and enforce compliance with such standards."

In order to comply with this statutory responsibility NFA is developing a comprehensive screening process to insure that all persons for which NFA has registration responsibility satisfy minimum proficiency standards. This screening process will include consideration of the training and experience of registrants as well as a standardized testing program. NFA is currently phasing in testing programs for APs of FCMs, IBs, CPOs and CTAs.

As an initial step, NFA's Board of Directors has adopted and the CFTC has approved NFA Compliance Rule 2-24, which reads as follows:

Subject to the provisions of paragraphs (d) and (e) of Bylaw 301, no person (except any person who was registered as an associated person of an FCM or IB or who had applied for such registration as of March 1, 1984 and whose registration as an associated person of an FCM or IB has not lapsed since that date) may be associated with an FCM Member of NFA (See Bylaw 301 (b)) unless such person has taken and passed the National Commodity Futures Examination.

Simply stated, the effect of the Rule is that no Futures Commission Merchant ("FCM") may employ a person in the capacity of an Associated Person ("AP") who has not passed the National Commodity Futures Examination ("NCFE" or "Series 3") unless the AP was registered or had applied for registration before March 1, 1984. FCMs should note that the Rule also prohibits allowing a person to work as an AP under a temporary license if the person has not passed the Series 3 examination.

NFA recognizes that some FCMs will require time in which to arrange for current APs and AP applicants to take the Series 3 examination. In addition, NFA has received

certain requests to amend the Rule which, if acted on favorably by the Board, would exempt certain classes of APs from the requirement to pass the Series 3 examination. Therefore, NFA has determined to defer enforcement of the Rule with respect to the three situations described below.

First, in order to allow time in which to take the Series 3 examination, NFA will extend a 60-day "grace period" with respect to APs who have applied for registration between March 1, 1984, the cut-off date for the "grandfathering" provision, and the date of this notice. Thus, an FCM must insure that its APs who applied for registration between March 1, 1984 and May 25, 1984 have taken and passed the Series 3 examination by July 24, 1984.

Second, NFA will defer enforcement of NFA Compliance Rule 2-24 with respect to persons registered with the NASD as General Securities Representatives whose only futures-related activity is the solicitation of prospective commodity pool participants. Such individuals are exempted from registration as APs by CFTC regulation. The question of what type of testing program, if any, should be applied to those individuals who apply for registration in spite of the exemption is still under consideration. Therefore, enforcement of the Rule with respect to those individuals will be deferred pending resolution of the question by NFA's Board of Directors. Once the question is resolved, FCMs may be required to insure that such persons (who are not within the "grandfathering" provision) take and pass the Series 3 or another proficiency examination in order to continue to employ them in the capacity of AP.

Finally, NFA's Board has taken a "no action" position with respect to persons acting as APs of FCMs where such persons (1) are registered with the NASD as General Securities Representatives, (2) have passed the Series 20 examination offered by New York Futures Exchange and (3) limit their futures-related activities to the area of stock index products. This "no action" position will continue through December 31, 1984. The question of what type of examination such APs who apply for registration after December 31, 1984 will ultimately be required to pass remains under consideration.

Except during the "grace period" described above, an FCM may not employ in the capacity of an AP a person who has not been "grandfathered" or who has not passed the Series 3 examination unless that person's activities are appropriately restricted as described above. Of course, an FCM will be in violation of Compliance Rule 2-24 if any of its APs who have not passed the Series 3 examination (as a consequence of the restrictions on their activities described above) expand his or her activities beyond the scope of the relevant restrictions.

Successful application of a testing program as part of a comprehensive screening process for APs is an important part of NFA's congressional mandate. With the exception of the situations outlined above, NFA intends to begin vigorous enforcement of NFA Compliance Rule 2-24 immediately.

If you have any questions regarding this matter, feel free to contact NFA.

October 25, 1984

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

Dear Ms. Webb:

By letter dated May 4, 1984 the Commodity Futures Trading Commission ("CFTC") informed National Futures Association ("NFA") of the approval of Section II(a) of Schedule A to NFA Bylaw 305 ("Section II(a)") and Compliance Rule 2-24. These rules established testing requirements for all Associated Persons ("APs") of Introducing Brokers ("IBs") and Futures Commission Merchants ("FCMs") who were registered or who had applied for registration after a specified date. Under those rules persons who were registered or who had applied for registration prior to the relevant date were not required to take and pass the examination in order to maintain their existing registration although the rules require such persons to take and pass the examination in the event of a lapse in registration. While acknowledging that NFA has until September 30, 1985 to fully implement its program to assure that all APs have at least the required entry level knowledge, the CFTC's letter requested NFA to explain how its proficiency requirements will operate to provide such assurances with respect to APs who may not have previously been examined and who may not be required to be examined under NFA's rules. NFA provided such an explanation in its letter of July 2, 1984. However, in response to concerns of the CFTC and CFTC staff, this letter is intended to supersede the letter of July 2, 1984.

As NFA stated in its letter to the CFTC dated July 2, 1984, the purpose of the proficiency standards mandated under the Commodity Exchange Act ("Act") is to assure that all persons conducting a futures business with the public possess at least the minimum knowledge needed to function in a manner that protects the interests of customers. NFA is committed to serving the goal of the Act by having in place by September 30, 1985 comprehensive proficiency standards



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which supply such assurance. The standards will consist of two elements working in concert: (1) a testing requirement for all new APs as a condition of registration under the Act and as a condition of NFA Associate membership and (2) with respect to the relatively small group of APs who were not tested previously and who are not tested under NFA rules, the acquisition of minimum required knowledge through experience under the training which is an element of supervision required by NFA and CFTC rules.

Much of the first element was put in place with the adoption and CFTC approval of Section II(a) and Compliance Rule 2-24. NFA intends shortly to adopt a comprehensive set of testing rules which will establish, long before September 30, 1985, a mandatory testing requirement for all new applicants for AP registration in all categories. NFA does not intend to make exceptions to that requirement. All AP applicants under NFA Rules will be required to take and pass an appropriate examination as a condition of registration or temporary licensing and the CFTC will be provided with adequate evidence to confirm the validity and reliability of the examinations used for that purpose.

Once the AP testing requirement is fully established it will necessarily satisfy NFA's responsibility to apply proficiency testing to the FCMS, IBs, CPOs and CTAs themselves. Under the Commission's Interpretive Statement Regarding the Scope of the Term "Supervision" in the Associated Person Registration Requirement, [1980-82 Transfer Binder] Comm. Fut. L. Rep. (CCH) §21,069 (1980), to which NFA has strictly adhered in performing registration responsibilities with respect to IBs and their APs, every individual in the supervisory "chain of command" will be required to become an AP and, therefore, be tested. Although NFA's appropriate Member committees and Board of Directors may in the future consider adoption of additional testing requirements which focus on the expertise necessary to perform particular management or supervisory functions within a firm (e.g., tests similar to those required of various types of principals by the National Association of Securities Dealers, Inc. ("NASD")), NFA believes that the basic AP testing requirement will be adequate to satisfy NFA's statutory testing responsibilities with respect to FCMS, IBs, CPOs, CTAs as well as their respective APs.



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NFA has, and will maintain, an adequate program to audit and enforce compliance with its proficiency testing requirements. Currently the testing requirement for APs of IBs is established through Section II(a), which makes testing a condition of registration, and the testing requirement for APs of FCMs is established through Compliance Rule 2-24 as a compliance requirement of the sponsoring FCM Member. NFA contemplates that for all categories of APs NFA's rules will require passage of an appropriate examination as a condition of registration or temporary licensing and Associate membership and, through a Compliance rule applicable to the NFA Member sponsor, as a condition of employment. After this set of rules is in place NFA will be able to avail itself of two approaches to enforcement. First, NFA will require APs to prove that they have passed the appropriate test prior to registration or temporary licensing. Second, NFA's audit programs will include steps designed to determine if Member firms have complied with the appropriate testing requirement with respect to their APs.

The second element of NFA's proficiency standards is designed to assure that existing APs who were not previously tested and who are not required to be examined under NFA's rules possess the required minimum knowledge. This assurance will be gained through NFA's continuing surveillance to determine that such APs already have or will, by September 30, 1985, gain the required knowledge through experience under the training which is a necessary element of the supervision required under NFA and CFTC rules. In response to the CFTC's concerns regarding the level of knowledge possessed by such APs, NFA will promptly enhance its audit programs in the area of internal control to focus more directly on an assessment of the training provided for such APs. In addition, NFA staff will also recommend that its Advisory Committees undertake the task of prescribing guidelines concerning the minimum acceptable elements of training for such APs which would be consistent with the supervisory responsibilities of NFA Members.

NFA firmly believes that the experience which an AP gains under adequate sponsor supervision in a period of one year provides assurance that such an AP has the required level of knowledge necessary to protect customers which would otherwise be tested for through the examination. Because



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NFA intends to establish March 1, 1984 as the latest date after which all new APs will be required to be tested, all APs who were not previously tested or who are not tested under NFA's rules will have well more than one year's experience by September 30, 1985. Therefore, in order to assure full implementation of proficiency standards by the target date it remains only for NFA to adequately confirm on a case by case basis its assumption that the experience of those individuals has included adequate supervision. NFA will confirm that assumption through its ongoing program of routine and for cause compliance audits and examinations.

In this connection it is important to note that, due to long established contract market examination programs, the APs who were not previously tested and who are not required to be tested under NFA's rules are relatively few in number and concentrated in the FCMs, IBs, Commodity Pool Operators ("CPOs") and Commodity Trading Advisors ("CTAs") which are not contract market members and which, therefore, are the principal focus of NFA's compliance auditing activities. For this reason NFA will be able to confirm directly whether such sponsors provide the type of AP supervision which is calculated to instill the required minimum level of knowledge within the one-year period.

NFA's routine compliance auditing programs contain numerous steps designed to test the Member's system of internal controls. Supervision of APs is one of the specific areas of internal control which is the subject of such testing and training is one of the essential elements of adequate supervision. Because techniques of supervision in general and training in particular may appropriately vary depending on numerous factors such as the size and type of business of the Member firm, NFA does not measure the supervision and training programs of all Member firms against a single unbending standard. Instead through examination of any written supervision and training procedures and through interviews with principals and other supervisory personnel NFA auditors are able to gather the information needed for NFA's Compliance Department management in conjunction with NFA's legal staff, to determine whether a firm's supervision and training procedures are adequate under the circumstances and calculated to provide APs with the required minimum knowledge within the one-year period. Although current audit programs encom-

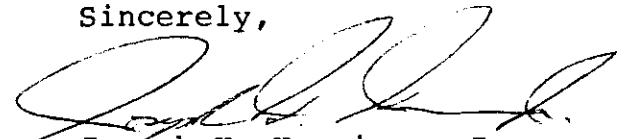


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pass a review of supervision and training, those programs will be enhanced as outlined above and may be further aided by general standards which may be promulgated by NFA's Advisory Committees. As part of the auditing program NFA will, where appropriate, on a test basis, require certain previously unexamined APs to sit for the appropriate examination to confirm the effectiveness of a Member's training program. In instances where internal control is inadequate in this area corrective and disciplinary action has been and will continue to be taken and, where appropriate, NFA staff will recommend to NFA's Business Conduct Committees that an order requiring testing of any untested APs be issued.

We hope that the foregoing adequately addresses any remaining concerns. If there are further questions, NFA would be happy to answer them.

Sincerely,



Joseph H. Harrison, Jr.
General Counsel

JHH:cm

cc: Chairman Susan M. Phillips
Commissioner Kalo A. Hineman
Commissioner Fowler C. West
Commissioner William E. Seale
Commissioner Robert Davis
Andrea M. Corcoran, Esq.
Kenneth M. Raisler, Esq.
Kenneth M. Rosenzweig, Esq.