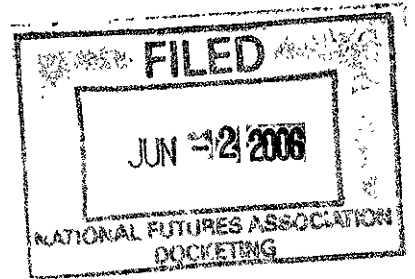


**NATIONAL FUTURES ASSOCIATION  
BEFORE THE  
BUSINESS CONDUCT COMMITTEE**



In the Matter of:

INTERACTIVE BROKERS LLC  
(NFA ID #258600),

Respondent.

NFA Case No. 06-BCC-010

**COMPLAINT**

Having reviewed the investigative report submitted by the Compliance Department of National Futures Association ("NFA"), and having found reason to believe that NFA Requirements are being, have been or are about to be violated and that the matter should be adjudicated, NFA's Business Conduct Committee ("Committee") issues this Complaint against Interactive Brokers LLC ("Interactive").

**ALLEGATIONS**

**JURISDICTION**

1. At all times relevant to this Complaint, Interactive was a futures commission merchant ("FCM") Member of National Futures Association located in Greenwich, Connecticut. Interactive has been registered as an FCM and NFA Member since December 2, 1994. Interactive is also a registered securities broker dealer.

**BACKGROUND**

2. Interactive's business is primarily that of providing electronic, online, discount futures brokerage to retail customers. Interactive also conducts some off-

exchange foreign currency (FOREX) business as well as proprietary and non-customer trading.

3. Interactive's customers direct their own trading and place their own orders with Interactive via the Internet from their personal computers. The firm does not provide investment or trading advice to customers. Interactive's account documents – customer account agreement, account opening forms, monthly account statements, etc. – are available online instead of in paper form.
4. At the time of NFA's most recent examination, in March 2005, Interactive had approximately 2,500 to 3,000 active futures and options customer accounts. The firm had over \$73 million in domestic segregated funds and \$29 million in foreign secured amount funds on deposit.

#### **APPLICABLE RULES**

5. NFA Compliance Rule 2-10 provides that each Member shall maintain adequate books and records necessary and appropriate to conduct its business including, without limitation, the records required to be kept under Commodity Futures Trading Commission ("CFTC") Regulations 1.18 and 1.32 through 1.37 for the period required under CFTC Regulation 1.31.
6. NFA Compliance Rule 2-5, in pertinent part, requires Members to cooperate promptly and fully with NFA in any NFA investigation, inquiry, audit, and examination regarding compliance with NFA requirements.
7. NFA Bylaw 1101, in pertinent part, prohibits an NFA Member from doing business with a non-Member of NFA that is required to be registered with the CFTC.

## COUNT I

### **VIOLATION OF NFA COMPLIANCE RULE 2-10: FAILURE TO MAINTAIN REQUIRED BOOKS AND RECORDS.**

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8. The allegations contained in paragraphs 1 through 5 are realleged as paragraph 8.
9. Interactive's online monthly customer account statements, which were in use in 2004, failed to include the following information, as required by NFA Compliance Rule 2-10 and CFTC Regulation 1.33(a): net unrealized profits or losses for all open contracts; the price at which open positions were acquired; the transaction date of all open option positions; and NFA assessment fees and exchange fees.
10. Interactive's online monthly customer account statements also failed to separate the customer's open trade equity ("OTE") balance from the customer's cash balance, but, instead, combined these amounts, which is inconsistent with CFTC Regulations requiring that these balances be separated on account statements. In February 2004, NFA advised Interactive that if it wanted relief from this requirement, it should seek a no-action letter from the CFTC, but, to date, the firm has not yet requested a no-action letter.
11. In 2004, Interactive failed to maintain any records supporting the OTE balances on the daily and month-end segregation calculations, as required by NFA Compliance Rule 2-10. As a result, during NFA's 2004 audit of Interactive, NFA was unable to determine the accuracy of the OTE balances. Also in 2004, Interactive failed to maintain records for each business day that separately showed all commodity futures and options transactions executed on that day, designated by customer; total open trade equity of the customer accounts; and

total net liquidating value of the customer accounts – all of which records were required to be kept by NFA Compliance Rule 2-10.

12. In June 2004, NFA issued an audit report to Interactive requesting a response to the deficiencies described in paragraphs 9 through 11, above. In August 2004, Interactive filed a response in which it indicated that it would make modifications to its computer system so that its online monthly customer account statements would include all required information and it would be able to generate internal records to support its segregation calculations and OTE balances. Interactive told NFA that the modifications to its computer system would be completed during the 4th quarter of 2004. However, as of March 2005, Interactive still had not made these modifications to its computer system.
13. Also, in the course of NFA's 2004 audit of Interactive, NFA noted that Interactive's online monthly customer account statements failed to reflect NFA assessment fees. To address this situation, Interactive asked NFA to allow it to provide a link from the online monthly account statements to a web page disclosing information about NFA and exchange fees. NFA indicated to Interactive that this procedure was acceptable to NFA. Yet, as of NFA's March 2005 audit of Interactive, the firm was still not reflecting assessment fees on its online monthly account statements. When NFA reminded the firm about the assessment fee link the firm had suggested during the 2004 audit, the firm's representatives claimed not to remember anything about this proposed link.
14. As alleged above, NFA performed another audit of Interactive in March 2005. During the March 2005 audit, NFA sought to determine if Interactive had made

the necessary modifications to its computer system – or taken alternative measures – to correct the recordkeeping deficiencies noted during the 2004 audit. For the most part, NFA found little improvement in Interactive's records. For example, Interactive's online monthly account statements still omitted certain required information. Moreover, the firm was still unable to produce to NFA a report separately showing for each business day all commodity futures and options transactions executed on that day, designated by customer; the total open trade equity of the customer accounts; and the total net liquidating value of the customer accounts. Not only was the firm unable to generate a report or reports showing such information, it could not show that it even maintained this information. Thus, the firm was unable to produce underlying data to support its domestic and foreign segregation calculations.

15. By reason of the foregoing acts and omissions, Interactive is charged with violations of NFA Compliance Rule 2-10.

## **COUNT II**

### **VIOLATION OF NFA COMPLIANCE RULE 2-5: FAILURE TO COOPERATE PROMPTLY AND FULLY WITH NFA IN AN NFA AUDIT.**

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16. The allegations contained in paragraphs 1 through 4 and 6 are realleged as paragraph 16.
17. Interactive has repeatedly failed to respond in a timely fashion to NFA's numerous requests for information relative to NFA's 2004 and 2005 audits. Interactive was informed of deficiencies in the firm's online customer account statements, as well as its internal daily trading records, during NFA's 2004 audit of the firm and again during the 2005 audit. As far back as 2001, Interactive's

prior DSRO raised concerns with the firm about its segregation calculations. Yet, despite these warnings and the firm's assurances that these problems would be fixed, Interactive made no real progress in this area until after NFA's 2005 audit. In fact, Interactive still has not resolved all of the deficiencies noted in NFA's 2004 and 2005 audits.

18. Interactive has also failed to provide information requested by NFA in connection with a rebate claim it asserted concerning a purported overpayment of its assessment fees.
19. The assessment issue arose in early 2004, when NFA's treasurer's office noted that Interactive had failed to make its assessment fee payments. NFA contacted the firm to inquire about its non-payment of assessment fees. According to Interactive, it had determined that it had overpaid its assessment fees from July 2001 through December 2003, in an amount of approximately \$205,000, as a result of mistakenly paying assessment fees on trades placed by non-U.S. customers on foreign exchanges. Interactive informed NFA that, beginning in January 2004, it unilaterally decided to stop making assessment fee payments until it recouped the amount of its claimed overpayment, which occurred in June 2004. Since then Interactive has paid its monthly assessment fees to NFA.
20. NFA asked Interactive to provide support for its overpayment claim by identifying the trades and the customer accounts which it maintains were incorrectly assessed the assessment fee. The firm said it would provide this information but, despite repeated requests from NFA, it has failed to do so. Although the firm has produced some information to NFA, it has not been able to identify the trades

or the accounts that it claims were wrongly assessed the assessment fee. After going back and forth, the firm finally advised NFA that due to modifications to its computer system, it is no longer able to access information that would identify the specific trades involved.

21. By reason of the foregoing acts and omissions, Interactive is charged with violations of NFA Compliance Rule 2-5.

### **COUNT III**

#### **VIOLATION OF NFA BYLAW 1101: DOING BUSINESS WITH A NON-MEMBER OF NFA THAT WAS REQUIRED TO BE REGISTERED WITH THE CFTC.**

22. The allegations contained in paragraphs 1 through 4 and 7 are realleged as paragraph 22.
23. In May 2005, the CFTC took an enforcement action against Kevin Steele ("Steele"), a Canadian resident, alleging that he operated an illegal commodity pool, through which he defrauded hundreds of investors. The CFTC's complaint alleged that Steele traded for the pool using personal trading accounts that were in his name at Interactive, which Steele funded with money he received from investors. Steele allegedly issued false statements to investors showing profits when, in reality, the pool suffered substantial trading losses in addition to monies Steele misappropriated for his personal use. In November 2005, an Illinois Federal District Court entered an order of default judgment against Steele requiring him to pay over \$7 million in restitution to the defrauded pool investors and a contingent civil monetary penalty of \$6.2 million for his violations of federal commodities laws.

24. When NFA learned of the CFTC's complaint against Steele, NFA commenced an inquiry into Interactive's role in the matter and whether it exercised due diligence in handling Steele's account. Based on NFA's inquiry, it is alleged as follows:

- Steele opened a trading account at Interactive in February 2003, identified as account number U82666, which he labeled as a personal account. In his account opening documents, Steele indicated that his liquid net worth was \$175,000.
- The account was active between February 2003 and May 2005, during which time the account received 134 deposits, most of which were via wire transfer, totaling more than \$7 million. These deposits ranged in size from \$3,500 to \$411,000, although at least half of these deposits were for \$30,000 or less.
- Of the 134 deposits to the account, 79 came from an entity called "Abriel Asset Management"; 12 came from an entity called "Custom House Currency Exchange"; and 43 came from 16 individuals (other than Steele) in Canada, the United States (California and Idaho), and Germany.
- Between August 2003 and May 2005, the account had 191 withdrawals, totaling over \$3.2 million. Withdrawals ranged in size from \$2,000 to \$100,000. Most of the early withdrawals were for less than \$10,000. Later withdrawals were usually for \$20,000 to \$25,000.
- There were instances where there were both deposits and withdrawals made on the same day. For example, on February 13, 2004, there was a deposit for \$5,997 and a withdrawal for \$5,000. There were also instances where there were multiple withdrawals on the same day.
- During the first year that the account was open (February 2003 to March 2004), the account received deposits totaling over \$580,000, had withdrawals of nearly \$100,000, and sustained trading losses of approximately \$240,000 – which figures seem out of synch with the liquid net worth of \$175,000, as stated in Steele's account opening documents.
- In May 2005, an individual contacted Interactive concerning an account statement he had received from Steele, which appeared to be an Interactive account statement. Interactive determined that the account statement was fictitious since no account was ever opened in the individual's name at Interactive.



25. NFA asked Interactive about the due diligence it performed with respect to Steele's account. Interactive told NFA that Steele had always maintained that the funds in his account belonged to him and that all the trading in his account was solely for his personal benefit. As support, Interactive furnished NFA with a summary of its communications with Steele. According to this summary, Interactive contacted Steele in April 2004, September 2004, and May 2005 to inquire about the large number of withdrawals and deposits in his account.
26. When Interactive contacted Steele in April and September 2004, he told Interactive that he was a "full-time trader," who was trying to make a living off "day trading," and that the numerous withdrawals were to pay his living expenses. During their September 2004 exchange, Interactive advised Steele to make fewer deposits and withdrawals. Interactive also received a September 2004 e-mail from Steele in which he claimed that most of his income was derived from "revenue property and real estate in various countries." This e-mail makes no mention of "day trading."
27. When Interactive contacted Steele in April 2005, the firm requested that he "consolidate [his] activity as to deposits and withdrawals because ... the regular activity is what is drawing flags ... especially when the withdrawals are coupled with deposits the same day ... it raises the question." Interactive told Steele that it would "prefer to see a withdrawal once a month for \$250,000."
28. In addition to the above communications, Interactive also represented that it spoke to Steele when its internal surveillance program identified Steele's account as an account with substantial losses compared to the account holder's net

worth. According to Interactive, Steele claimed that he had understated his net worth on his account application.

29. Under NFA Bylaw 1101, a Member is liable for doing business with a non-Member where the evidence indicates that the Member knew or should have known that the non-Member was acting in a capacity that required CFTC registration and NFA membership.
30. In light of the totality of the suspicious circumstances surrounding Steele's account – i.e., the large number of deposits from different entities and numerous individuals from all parts of the United States and Canada; frequent and numerous withdrawals in small amounts; and the wide disparity between Steele's reported net worth, on the one hand, and the amount of the deposits and losses, on the other hand – Interactive knew or should have known that Steele was acting as a commodity pool operator, without being registered as such, and using his trading account to trade on behalf of third parties.
31. By reason of the foregoing acts and omissions, Interactive is charged with violations of NFA Bylaw 1101.

### **PROCEDURAL REQUIREMENTS**

#### **ANSWER**

You must file a written Answer to the Complaint with NFA within thirty days of the date of the Complaint. The Answer shall respond to each allegation in the Complaint by admitting, denying or averring that you lack sufficient knowledge or information to admit or deny the allegation. An averment of insufficient knowledge or

information may only be made after a diligent effort has been made to ascertain the relevant facts and shall be deemed to be a denial of the pertinent allegation.

The place for filing an Answer shall be:

National Futures Association  
200 West Madison Street  
Suite 1600  
Chicago, Illinois 60606-3447  
Attn: Legal Department-Docketing

Failure to file an Answer as provided above shall be deemed an admission of the facts and legal conclusions contained in the Complaint. Failure to respond to any allegation shall be deemed an admission of that allegation. Failure to file an Answer as provided above shall be deemed a waiver of hearing.

#### **POTENTIAL PENALTIES, DISQUALIFICATION AND INELIGIBILITY**

At the conclusion of the proceedings conducted as a result of or in connection with the issuance of this Complaint, the Committee may impose one or more of the following penalties:

- (a) expulsion or suspension for a specified period from NFA membership;
- (b) bar or suspension for a specified period from association with an NFA Member;
- (c) censure or reprimand;
- (d) a monetary fine not to exceed \$250,000 for each violation found; and
- (e) order to cease and desist or any other fitting penalty or remedial action not inconsistent with these penalties.

The allegations in this Complaint may constitute a statutory disqualification from registration under Section 8a(3)(M) of the Commodity Exchange Act. Respondents in this matter who apply for registration in any new capacity, including as an

associated person with a new sponsor, may be denied registration based on the pendency of this proceeding.

Pursuant to the provisions of CFTC Regulation 1.63, penalties imposed in connection with this Complaint may temporarily or permanently render Respondents who are individuals ineligible to serve on disciplinary committees, arbitration panels and governing boards of a self-regulatory organization, as that term is defined in CFTC Regulation 1.63.

**NATIONAL FUTURES ASSOCIATION  
BUSINESS CONDUCT COMMITTEE**

Dated: 6/2/06

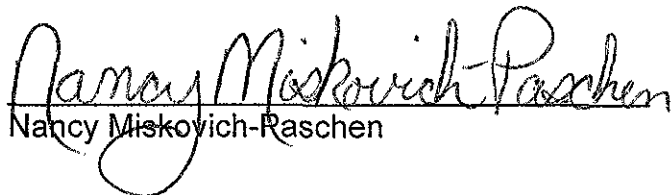
By: [Signature]  
Chairperson

m/rvh/Interactive Complaint

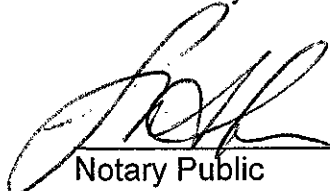
## AFFIDAVIT OF SERVICE

I, Nancy Miskovich-Paschen, on oath state that on June 2, 2006, I served a copy of the attached Complaint, by sending such copy by regular mail, first-class delivery, and by overnight mail, in envelopes addressed as follows:

David Battan, Esq.  
Interactive Brokers LLC  
1725 Eye Street, NW  
Suite 300  
Washington, DC 20006

  
Nancy Miskovich-Paschen

Subscribed and sworn to before me on  
this 2nd day of June 2006.

  
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Notary Public

