

February 7, 1992

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

Re: National Futures Association: Proposed New Compliance Rule 2-7; Proposed Amendments to NFA Compliance Rule 3-12 and Registration Rule 501; Proposed Amendments to NFA Compliance Rule 2-26 and Financial Requirements Sections 9, 10 and 11; Proposed Amendments to NFA Financial Requirements Sections 1 and 6; Proposed Modifications to Interpretive Notice to Compliance Rule 2-9 Regarding a Member Self-Audit Requirement; and Proposed Modifications to Board Resolution to Grant a Temporary No-Action Position.

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 new Compliance Rule 2-7; proposed amendments to NFA Compliance Rule 3-12 and Registration Rule 501; proposed amendments to NFA Compliance Rule 2-26 and Financial Requirements Sections 9, 10 and 11; proposed amendments to NFA Financial Requirements Sections 1 and 6; proposed modifications to Interpretive Notice to Compliance Rule 2-9 regarding a Member self-audit requirement; and proposed modifications to Board Resolution to grant a temporary no-action position for the Comex's gold asset participation ("GAP") contract. The proposed rule and the proposed amendments were approved by NFA's Board of Directors (the "Board") at its meeting on November 21, 1991. NFA respectfully requests the Commission's review and approval of the proposed new rule and the proposed amendments to the rules, interpretive notice and temporary no-action position.

**I. PROPOSED NEW NFA COMPLIANCE RULE 2-7.**

- A. Proposed NFA Compliance Rule 2-7 to set a minimum experience requirement for branch office managers (additions are underscored):



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COMPLIANCE RULES

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Part 2 -- RULES GOVERNING THE BUSINESS CONDUCT OF MEMBERS  
REGISTERED WITH THE COMMISSION

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Rule 2-7. BRANCH OFFICE MANAGER MINIMUM EXPERIENCE REQUIRE-  
MENT

No Member shall allow an Associate to be a branch office manager, as that term is used in Registration Rule 101, unless that Associate has been continuously registered under the Act for a minimum of two years and has worked in such registered capacity for that period of time or that Associate is sponsored by a registered broker-dealer and is qualified to act as a branch office manager under the rules of either the New York Stock Exchange or National Association of Securities Dealers. This requirement may, in NFA's discretion, be waived upon a showing that the Associate has equivalent experience. Any Member seeking such a waiver may submit a written request to the Compliance Director and all such requests shall be ruled upon by a three-member panel consisting of one member from each Regional Business Conduct Committee, said members to be appointed by the Board from time to time. The decision of the panel shall be final and shall be based upon the written submissions and views of the Compliance Director. The panel shall communicate its decision to the Compliance Director or a person designated by the Compliance Director, who shall then inform the Member seeking the waiver.

- B. Explanation of Proposed NFA Compliance Rule 2-7 to set a minimum experience requirement for branch office managers.

Proposed Compliance Rule 2-7 requires branch office managers to have been continuously registered under the Act for a period of two years, be qualified to act as a branch office manager in the securities industry (if sponsored by a broker-dealer), or demonstrate that they have equivalent experience.<sup>1</sup>

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<sup>1</sup> The New York Stock Exchange and the National Association of Securities Dealers both require branch office managers to pass the Series 8 branch managers examination while the NYSE also requires branch office managers to have at least three years of experience as a registered representative or substantial experience in a related sales or managerial position.



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The Board believes that an experience requirement enhances customer protection by ensuring a minimum level of experience in and knowledge of the industry by those individuals responsible for the operation and supervision of branch offices.

In order to measure the impact of this requirement on Member firm operations and to help determine the appropriate minimum level of experience, NFA staff developed a computer program to analyze the existing pool of branch office managers. After review of the data and discussion, the Special Committee for the Review of NFA Enforcement Procedures ("Special Committee") determined that a two year requirement would have a relatively limited effect on the current pool of branch office managers while still providing the necessary customer protection. The Special Committee also noted that Associates cannot exercise discretion over customer accounts unless they have been registered for a period of two years and that it would be anomalous to allow individuals with less experience to supervise those Associates. The Board agreed with this analysis and adopted the experience requirement recommended by the Special Committee.

The rule proposal includes an experience waiver provision which is similar to that of the discretionary trading experience waiver provision in NFA Compliance Rule 2-8(c). Specifically, the waiver provision, as proposed, provides that the experience requirement may be waived, in NFA's discretion, if the Associate can demonstrate that he has equivalent experience. Requests for waivers will be decided by a three-member panel consisting of one member from each of NFA's three Regional Business Conduct Committees.

According to NFA's most current data, there are approximately 4,432 branch offices operated by a total of 611 Member firms. Only 153 of the managers of those 4,432 branch offices will have less than two years of continuous experience by October 1, 1992, the proposed effective date for the rule.

Approximately 80 of these 153 branch office managers work for firms which are also registered as broker-dealers. Therefore, assuming that these 80 individuals are branch office managers for the broker-dealer firms, approximately 70 branch office managers would be affected by the proposed minimum experience requirement.

The Board's ultimate goal is to implement a testing requirement for branch office managers. However, the Board recognizes that the development and subsequent CFTC approval of a



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test will take time.<sup>2</sup> The minimum experience requirement is meant to be an interim measure to protect investors while a branch office manager test is developed. In the Board's view, a test will more adequately gauge an individual's knowledge of supervisory responsibilities. The Board expects to rescind the minimum experience requirement once a branch office managers' examination has been developed and approved.<sup>3</sup>

Given the waiver provision and the relatively small number of current adversely affected branch office managers, the Board determined not to add a grandfather clause to the proposed minimum experience requirement. NFA will give advance notice to the membership to provide ample time for adversely affected individuals to file waiver requests.

NFA respectfully requests that proposed NFA Compliance Rule 2-7 be declared effective on October 1, 1992.

**II. PROPOSED AMENDMENTS TO NFA COMPLIANCE RULE 3-12 AND NFA REGISTRATION RULE 501.**

- A. Proposed Amendments to NFA Compliance Rule 3-12 and NFA Registration Rule 501 to codify current practice regarding conflicts of interest (additions are under-scored and deletions are [bracketed]):

**COMPLIANCE RULES**

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**PART 3 -- COMPLIANCE PROCEDURES**

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<sup>2</sup> However, the Board is confident that an initial version of the test will be available by next October and could be used on a voluntary basis in conjunction with the waiver process as evidence of qualification for a waiver.

<sup>3</sup> Because then current branch office managers will have been subject to the minimum experience requirement, the Board believes that they should be grandfathered and, therefore, would not be required to take the examination.



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**Rule 3-12 Member or Associate Responsibility Actions.**

**(a) Nature of Action.**

A Member or Associate may be summarily suspended from membership, or association with a Member, may be required to restrict its operations (e.g., restrictions on accepting new accounts), or may otherwise be directed to take remedial action, where the President, with the concurrence of the NFA Board of Directors or Executive Committee, has reason to believe that the summary action is necessary to protect the commodity futures markets, customers, or other Members or Associates. No member of either the Board of Directors or the Executive Committee shall participate in a summary action if the member, or any person with whom the member is connected, has a financial, personal or other direct interest in the matter under consideration. Notice of such summary action shall be given promptly to the Commission.

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**REGISTRATION RULES**

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**PART 500. PROCEDURES TO DENY, CONDITION, SUSPEND, RESTRICT, OR REVOKE REGISTRATION**

**Rule 501. Authority to Deny, Condition, Suspend, Restrict, and Revoke Registration.**

NFA may refuse to register, register conditionally, suspend or place restrictions on the registration, or revoke the registration of any person registered or applying for registration as a futures commission merchant, introducing broker, commodity pool operator, commodity trading advisor, leverage transaction merchant, or associated person of any of the foregoing, based upon the grounds for such action and the standards of fitness set forth in the Act applicable to registrations granted by the Commission. Final written orders denying registration, registering conditionally, suspending, restricting, or revoking registration shall be made by the President, the Membership Committee, or its designated Subcommittee in accordance with the procedures set forth in this Part 500: provided, however, that pending final determination, in cases submitted by the President to the Membership Committee or its designated Subcommittee, registration shall not be granted. Such designated Subcommittee shall consist of at least three members of the Membership Committee, all of whom shall be appointed by a majority of the Member-



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ship Committee. No member of the Membership Committee or its designated Subcommittee shall either review a registration matter or participate in a registration action if the member, or any person with whom the member is connected, has a financial, personal or other direct interest in the matter under consideration.

- B. Explanation of Proposed Amendments to NFA Compliance Rule 3-12 and NFA Registration Rule 501 to codify current practices regarding conflicts of interest.

From the time NFA first began operations, NFA has carefully guarded against any possible conflict of interest on the part of any Committee member concerning any NFA disciplinary proceeding, Member Responsibility Action ("MRA") or registration matter. Pursuant to NFA's longstanding practice, any Committee member or member of the Board will recuse himself from participating in any NFA decision or action if the member, or any person with whom the member is connected, has a financial, personal or other direct interest in the matter under consideration. NFA rules which relate to Business Conduct Committee actions (Compliance Rule 3-6) and appeals therefrom (Compliance Rule 3-10) contain specific language which codifies this conflict of interest prohibition for members of the Regional Business Conduct Committees and the Appeals Committee. However, Registration Rule 501 concerning the Membership Committee's registration actions and Compliance Rule 3-12 which establishes the procedures for the Board of Directors or the Executive Committee to issue MRAs do not contain similar language.

As a result, the Board has determined to amend Registration Rule 501 and Compliance Rule 3-12 to conform with the current practice governing conflicts of interest. The Board believes codification of the current practice could prevent the appearance of a conflict by giving notice to the public of such a prohibition. These amendments specifically apply to Membership Committee reviews and actions and the issuance of MRAs. The amendments to these rules are not intended to prohibit either Board or Committee members from participating in a discussion or decision which pertains to any rulemaking or similar matter in which such person may have an interest.

NFA respectfully requests that the proposed amendments to NFA Compliance Rule 3-12 and NFA Registration Rule 501 become effective upon Commission approval.



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**III. PROPOSED AMENDMENTS TO NFA COMPLIANCE RULE 2-26 AND TO NFA FINANCIAL REQUIREMENTS SECTIONS 9, 10 AND 11.**

- A. Proposed Amendments to NFA Compliance Rule 2-26 and to NFA Financial Requirements Sections 9, 10 and 11 to establish a sliding scale IB capital requirement (additions are underscored and deletions are [bracketed]):

**COMPLIANCE RULES**

**RULE 2-26. FCM and IB Restrictions**

Any Member or Associate who violates any of CFTC Regulations 1.33, 1.55 or 1.56 shall be deemed to have violated an NFA Requirement. Any Member IB who violates CFTC Regulation 1.57 shall be deemed to have violated an NFA Requirement.

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**FINANCIAL REQUIREMENTS**

**Section 9. Introducing Broker Financial [and Reporting] Requirements.**

Each Member IB, except an IB operating pursuant to a guarantee agreement which meets the requirements set forth in CFTC Regulation 1.10(j), must maintain "Adjusted Net Capital" (as defined in Schedule A hereto) equal to or in excess of the greatest of -

- (i) \$30,000; or,
- (ii) \$6,000 per office operated by the IB (including the main office); or,
- (iii) \$3,000 for each AP sponsored by the IB; or
- (iv) (for securities brokers and dealers), the amount of net capital required by Rule 15c3-1(a) of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

[Each Member IB must file with its DSRO the financial reports required under CFTC Regulation 1.10(b)(1) and (2) [Financial reports of futures commission merchants and introducing brokers - Filing of financial reports]. Any Member IB who violates any of CFTC Regulations 1.10, 1.12 [Maintenance of



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minimum financial requirements by futures commission merchants and introducing brokers], 1.17 [Minimum financial requirements for futures commission merchants and introducing brokers] or 1.57 [Operations and activities of introducing brokers], shall be deemed to have violated an NFA requirement.

[Note: CFTC Regulation 1.10(b)(1) generally requires IBs to file financial reports on a quarterly basis. In accordance with CFTC Regulation 1.10(b)(3), Section 9 requires that each Member IB for which NFA is DSRO which files financial reports must file such reports with NFA with a copy to the CFTC.]

A Member IB which is also a securities broker or dealer may in lieu of a form 1-FR file a copy of its Financial and Operational Combined Uniform Single Report under the Securities Exchange Act of 1934, Part II or Part IIA, in accordance with CFTC Regulation 1.10(h). A Member IB which is also a country elevator may file a copy of a financial report prepared by a grain commission firm in accordance with CFTC Regulation 1.10(i).

CFTC Regulation 1.12 requires, among other things, telegraphic notice to NFA in accordance with paragraph (g) when the adjusted net capital of such IBs described in that Section is less than the minimum required by Regulation 1.17 or by the capital rule of any self-regulatory organization to which it is subject. CFTC Regulation 1.17 sets forth the minimum financial requirements for IBs. CFTC Regulation 1.57 requires, among other things, that each IB must: (1) open and carry all accounts on a fully disclosed basis with a carrying FCM; (2) not carry proprietary accounts or accounts in foreign futures; and (3) not accept money, securities or property of a futures customer to margin, guarantee or secure any trades or contracts of such customers.

CFTC Regulations 1.10, 1.12, 1.17 and 1.57 impose other regulatory requirements on IBs. The full text of those Regulations should be consulted.]]

**Section 10. Introducing Broker Reporting Requirements.**

- (a) A Member IB which knows or should have known that its adjusted net capital is less than the amount required by Section 9 or by the capital rule of any self-regulatory organization to which it is subject, must give telegraphic notice to NFA within 24 hours.
- (b) A Member IB must file with NFA the financial reports required under CFTC Regulation 1.10(b)(1) and (2).





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- (c) A Member IB which is also a securities broker or dealer may in lieu of a form 1-FR file a copy of its Financial and Operational Combined Uniform Single Report under the Securities Exchange Act of 1934, Part II or Part IIA, in accordance with CFTC Regulation 1.10(h). A Member IB which is also a country elevator may file a copy of a financial report prepared by a grain commission firm in accordance with CFTC Regulation 1.10(i).

(Note: CFTC Regulation 1.10(b)(1) generally requires IBs to file financial reports on a quarterly basis. In accordance with CFTC Regulation 1.10(b)(3), Section 10 requires that each Member IB for which NFA is DSRO which files financial reports must file such reports with NFA with a copy to the CFTC.)

**Section [10] 11. Leverage Transaction Merchant Reporting Requirements.**

(The text of the rule remains unchanged.)

- B. Explanation of Proposed Amendments to NFA Compliance Rule 2-26 and to NFA Financial Requirements Section 9, 10 and 11 to establish a sliding scale IB capital requirement.

The proposed amendments to NFA Financial Requirements Section 9 establish a sliding scale capital requirement for independent introducing brokers ("IBs") which will require an independent IB to maintain capital equal to the greater of:

- a) \$30,000; or
- b) \$6,000 per office operated (including the main office); or
- c) \$3,000 per AP sponsored.

The amendments to NFA Financial Requirements Section 10 and Compliance Rule 2-26 merely incorporate provisions formerly included in NFA Financial Requirements Section 9.

1. Background

Early last year, the Special Committee and NFA's Advisory Committees (collectively "NFA Committees" or "Committees") began considering the adequacy of the current capital requirements of independent IBs. As part of this consideration,



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these Committees noted that when the current independent IB capital requirements were adopted in 1983, the Commission stated that the two primary purposes of the capital requirements were to ensure that independent IBs had a significant financial stake in the operation of their businesses and had sufficient financial resources to meet their financial obligations to customers and to others. NFA's Committees concluded that the current structure of independent IB capital requirements -- imposing a flat \$20,000 requirement on all IBs regardless of the size of their operations -- does not appear to satisfy these goals. These Committees further concluded that the current minimum of \$20,000, which has remained unchanged since 1983, does not appear adequate to cover the obligations and liabilities which may arise from the business operations of even a small IB.

On March 26, 1991, a Notice to Members was issued seeking comment on the concept of a sliding scale capital requirement which would correlate the amount of business an IB does with the amount of capital it is required to maintain. In addition, the Notice requested comment on whether the minimum requirement should be raised from the current \$20,000 level. The Advisory Committees and the Special Committee considered the comments received in response to the Notice in formulating the proposal recommended to the Board. Set forth below is a summary of the comments received from the Members.

## 2. Summary of Comments Received

NFA received a total of sixteen comments addressing the idea of restructuring IB capital requirements. Three comments were received from FCMs, three comments from independent IBs, one from a person intending to become an independent IB, six comments from guaranteed IBs and one comment from a CPO/CTA. In addition, the Managed Futures Association and the Chicago Board of Trade submitted comments. All but one of these comments expressed support for the restructuring of IB capital requirements and encouraged continued study of the idea.

The Managed Futures Association, although supporting the Special Committee's reconsideration of IB capital requirements, disagreed with the concept of calculating IB capital requirements based on percentages of customer equity, volume of business or number or types of customers. In the opinion of the Managed Futures Association, IB capital requirements should not be structured similarly to FCM capital requirements since IBs do not hold customer funds. Rather, the Managed Futures Association viewed enhanced compliance procedures as the most effective tool to accomplish the Special Committee's goals.



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### 3. Discussion

After considering the comments received, the Advisory Committees and the Special Committee recommended that the Board adopt a sliding scale capital requirement. The FCM Advisory Committee and the Special Committee specifically recommended that an IB be required to maintain capital equal to the greater of:

- a) \$30,000 or
- b) \$10,000 per office (including the main office) plus \$3,000 per AP

After some members of the Board expressed concern that imposing a capital charge for both branch offices and APs might unnecessarily increase the capital requirement of many IBs, the Advisory Committees and the Special Committee reconsidered the proposal and determined that the charge per office and the charge per AP should become separate alternative minimums. The Special Committee further refined the proposal by reducing the charge per office from \$10,000 to \$6,000 per office. The proposal recommended by the Special Committee to the Board was supported by both the FCM and IB Advisory Committees.

In determining the most appropriate factors in measuring an IB's business, the Advisory Committees and the Special Committee reviewed detailed information concerning the size and nature of 238 independent IBs. This information included the number of APs, branch offices, customer accounts, non-customer accounts, the percentage of the firm's business which represents hedge trading, the amount of equity in the IB's customer accounts, the firm's adjusted net capital and whether the firm is involved in the securities industry or any other business. After reviewing this information, NFA's Committees narrowed their focus to the number of branch offices operated by an IB, the number of APs sponsored by the firm, the amount of equity in an IB's customer accounts and the number of customer accounts serviced by an IB. After reviewing statistics related to each of these four factors, NFA's Committees concluded that the number of branch offices operated by an IB and the number of APs sponsored by an IB are clearly relevant factors in determining the appropriate level of capital that an IB should be required to maintain.

In terms of the number of branch offices sponsored by an independent IB, the Committees recognized that maintaining a network of branch offices substantially increases an IB's operating expenses due both to routine business expenses and increased compliance and supervisory costs. Despite these increased costs,



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however, the firms with the largest branch office operations are not necessarily the firms with the most adjusted net capital. For example, a review of the information provided to NFA's Committees indicated that a total of seven independent IBs operate ten or more branch offices. Three of those seven are broker-dealers which maintain between \$2 million and \$28 million in adjusted net capital. Of the remaining four firms, however, three have less than \$65,000 in adjusted net capital. Furthermore, a total of 28 independent IBs operate four or more branch offices. Ten of those firms are also broker-dealers and six of those have more than \$2 million in adjusted net capital. Of the remaining 18 firms with four or more branch offices, 15 have less than \$100,000 in adjusted net capital, nine have less than \$50,000 and five have less than \$26,000.

As illustrated above, although IBs with substantial branch office operations have increased business and compliance costs, many such firms have not devoted substantial amounts of capital to their businesses. Because the current capital requirements do not impose any additional charges for each branch office operated by an independent IB, there is no obligation for those firms to infuse the amount of capital which would be required to adequately staff and supervise their branch offices.

As a result, the Advisory Committees and the Special Committee concluded that the number of branch offices operated by an independent IB should be a component of a sliding scale capital formula. Besides addressing an apparent weakness in the current capital rules, this component of a capital formula would have the added benefit of being based on information which is easily measured by the IB, readily accessible to NFA and not subject to frequent fluctuation.

The Committees also concluded that the number of APs sponsored was a relevant factor to any capital formula. Although the majority of the independent IBs operate as either one-man shops or small operations employing five APs or less, there are a number of independent IBs which employ anywhere from 20 to over 100 APs. The cost of supervising the activities of 100 APs is substantially greater than supervising a relative handful of APs, even if they are all working at the same location. In addition, the greater the number of APs, the greater the potential liability to customers and the greater the need for adjusted net capital to ensure those obligations are met.

Although the usefulness of including the number of APs employed by an independent IB as a component of a capital formula may be somewhat diminished if branch offices are included in the



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formula, the Committees concluded that the number of APs sponsored by an IB is an essential component of a sliding scale requirement. A capital formula which does not consider the number of APs sponsored by an IB could result in an IB with a large sales force, but few offices, having the same capital requirement as a one-man operation. As noted earlier, however, in response to concerns raised by the Board, these Committees recognized that requiring capital for both branch offices and APs might unnecessarily increase the capital requirement of many IBs. As a result, the Committees concluded that the capital formula should be structured so that the amount of capital required based on branch offices and the amount of capital required based on APs should be alternative minimums. An IB would be required to maintain capital equal to the greater of the two amounts.

In terms of the amount of equity in an IB's customer's account, the Committees recognized that there was some basis for including the amount of customer equity in determining an IB's capital requirement. However, the Committees noted that the incidence of default on NFA arbitration awards by independent IBs which would rank among the top in terms of customer equity is virtually non-existent. Generally, the independent IBs which tend to close their doors when regulatory or customer problems surface have been those with many APs or branch offices. These firms, because of the customers they solicit and the manner in which accounts are handled, seldom rank among the top firms in terms of customer equity. Therefore, the Committees determined that this factor was not relevant to a sliding scale capital requirement.

The Committees also concluded that there was little utility in including the number of customer accounts handled by an IB in the capital formula. It would be difficult to quantify the additional expense and exposure attributable to a single customer account, in addition to the fact that the number of customer accounts handled by an IB at any given time would be continuously fluctuating. Furthermore, the Committees noted that there is overlap between the IBs with the most customer accounts and the IBs with the most branch offices.

While the Committees were confident that branch offices operated and APs sponsored were the most relevant factors in determining an IB's capital requirement, the Committees also concluded that all IBs should be subject to a flat minimum requirement which would be controlling if an IB's alternative minimum requirement based on branch offices and APs was less than the flat minimum. The Committees concluded, however, that the current minimum requirement of \$20,000 was not adequate to meet



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the Commission's objective of ensuring that an independent IB has a sufficient financial stake in its business.

The Committees noted that the \$20,000 minimum capital requirement has remained unchanged since it was adopted in 1983, while the value of the dollar has fallen as a result of inflation. As a result, an IB effectively has less capital available than it did in 1983 to cover obligations and liabilities which may arise.

In addition to the effects of inflation, the Committees also recognized that given the new dimensions in the marketplace and the changes in the industry since the adoption of the IB capital rules, an IB needs to make a greater financial commitment to its business than it did eight years ago. It must keep its personnel adequately trained on new regulations and products, and it must maintain the necessary technology to properly service customers.

Although the Committees concluded that an increase in the minimum was essential, the Committees also recognized that a significant increase was not warranted for small IB operations. As a result, the Committees concluded an increase of \$10,000 to \$30,000, along with the alternative sliding scale requirement, would ensure that IB capital is adequate to meet the Commission's objective, without imposing an unnecessary burden on small IB operations.

The Board agrees with the analysis done by the Advisory Committees and the Special Committee and has adopted the recommendation of the Special Committee. The Board has determined that a sliding scale capital requirement which considers the number of branch offices operated by an IB and the number of APs employed by an IB is a more appropriate method of determining the amount of capital needed by an IB to properly run its operation. The Board believes that such a sliding scale approach ensures that the IB capital requirement fulfills its stated purposes regardless of the size of an IB's operation. The Board also believes that the sliding scale approach has a limited effect on the capital requirements of most independent IBs. Under the proposal, 78% of all independent IBs would have a minimum capital requirement of \$30,000. Furthermore, only 59 of the 238 independent IBs would be undercapitalized and 39 of these firms would be within \$10,000 of compliance.

NFA respectfully requests that the proposed amendments to NFA Compliance Rule 2-26 and NFA Financial Requirements



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Sections 9, 10 and 11 become effective the later of July 1, 1992 or upon Commission approval.

**IV. PROPOSED AMENDMENTS TO NFA FINANCIAL REQUIREMENTS SECTIONS 1 AND 6.**

- A. Text of Proposed Amendments to NFA Financial Requirements Sections 1 and 6 to amend FCM capital requirements (additions are underscored and deletions are [bracketed]):

**FINANCIAL REQUIREMENTS**

**Section 1. Minimum Financial Requirement.**

Each NFA Member that is registered or required to be registered with the Commodity Futures Trading Commission (hereinafter "CFTC") as a Futures Commission Merchant (hereinafter "Member FCM") must maintain "Adjusted Net Capital" (as defined in Schedule A hereto) equal to or in excess of --

(a) The greater of --

- (i) \$250,000, or,
- (ii) 4 percent of the funds required to be segregated pursuant to the Commodity Exchange Act and CFTC Regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade, provided, however, the deduction for each customer shall be limited to the amount of customer funds in such customer's account and foreign futures and foreign options secured amounts; or,
- (iii) \$6,000 for each remote location operated (i.e., proprietary branch offices, main office of each guaranteed IB and branch offices of each guaranteed IB); or,
- (iv) \$3,000 for each AP sponsored (including APs sponsored by guaranteed IBs); or,
- (v) (for securities brokers and dealers) the amount of net capital specified in Rule 15c3-1(a) of the



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Regulations of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

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**Section 6. Reporting.**

- (a) A Member FCM that knows or should have known that its Adjusted Net Capital is less than the amount required by Section 1 must give telegraphic notice to its DSRO within 24 hours.
- (b) A Member FCM must file a written notice with its DSRO, within 5 business days, when the FCM knows or should have known that its Adjusted Net Capital is less than the greatest of (i) \$375,000, or (ii) 6 percent of the funds required to be segregated pursuant to the Commodity Exchange Act and CFTC Regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade, provided, however, the deduction for each customer shall be limited to the amount of customer funds in such customer's account and foreign futures and options secured amounts, or (iii) \$9,000 for each remote location operated (i.e., proprietary branch offices, main office of each guaranteed IB and branch offices of each guaranteed IB); or, (iv) \$4,500 for each AP sponsored (including APs sponsored by guaranteed IBs); or (v) for securities brokers or dealers, the amount of capital specified in Rule 17a-11(b) of the Regulations of the Securities and Exchange Commission (17 CFR 240.17a-11(b)).
- (c) Whenever a Member FCM is required to give notice to the CFTC pursuant to CFTC Regulation 1.12, the FCM also is required to give such notice to its DSRO.

**B. Explanation of the Proposed Amendments to NFA Financial Requirements Sections 1 and 6 to amend FCM Capital Requirements.**

The proposed amendments to NFA Financial Requirements Sections 1 and 6 establish two additional alternative minimum capital requirements for FCMs based on the size of an FCM's operations in terms of remote locations operated (guaranteed IBs, guaranteed IB branch offices and proprietary branch offices) and APs sponsored (including those sponsored by a guaranteed IB).





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The amendment is intended to parallel the changes made to independent IB capital requirement. Under the proposal, an FCM would be required to maintain capital equal to the greater of:

- a) \$250,000; or
- b) 4% of segregated funds; or
- c) \$6,000 for each remote location operated; or
- d) \$3,000 for each AP sponsored; or
- e) for securities broker dealers, the amount required under SEC regulations.

#### 1. Background

In formulating the new capital requirement for independent IBs, NFA's FCM Advisory Committee and the Special Committee concluded that the concept of linking the IB capital requirement to the size of the IB's business operations was equally applicable to the capital requirement of FCMs. These Committees proposed that the FCM capital requirement be amended to provide for a new alternative minimum which would be based on the number of branch offices operated by the FCM and the IBs it guarantees and the number of APs sponsored by the firm. The proposal set forth by these Committees was not intended to be a haircut to an FCM's capital. Rather, the proposal called for an alternative minimum requirement which would apply only if it was greater than the FCM's capital requirement under current rules.

Although the IB Advisory Committee did not believe that an FCM's capital should be tied to any factor other than customer equity, the IB Advisory Committee did not express an opinion on the specific proposal recommended to the Board. However, the IB representative Board member voted in favor of the amendments to FCM capital requirements.<sup>4</sup>

On July 31, 1991, a Notice to Members requesting comment on an alternative minimum requirement for FCMs was issued. For discussion purposes, the Notice included an alternative formula for FCMs which was similar to the originally proposed independent IB requirement and which would have required an

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<sup>4</sup> One of the IB representative Board members did not attend the Board meeting.



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FCM to maintain minimum capital of \$30,000 per guaranteed IB plus \$10,000 per branch office of each guaranteed IB plus \$3,000 per AP of the FCM. The comments received in response to this Notice were considered by the FCM Advisory Committee and the Special Committee when formulating the recommendation made to the Board. Set forth below is a summary of the comments received.

## 2. Summary of Comments Received

NFA received a total of fifty comments in response to the Notice to Members. The majority of those comments, thirty-eight, were received from guaranteed IBs. In addition, one comment was received directly from Howard Rothman on behalf of the Board of Directors of the National Introducing Brokers Association ("NIBA").

The Board of NIBA expressed its concern that an alternative minimum requirement for FCMs which imposed a charge of \$30,000 for each IB guaranteed by an FCM would have a chilling effect on the willingness of FCMs to guarantee IBs and a detrimental effect on the industry. According to NIBA, the number of guaranteed IBs would be reduced significantly because smaller guaranteed IBs would be unable to find a guarantor. Furthermore, the NIBA Board believed that FCMs which currently guarantee IBs are well capitalized firms and, therefore, there is no need for an alternative minimum related to the number of IBs the firms guarantee.

A number of the other comments received in response to the Notice also opposed the concept of an alternative minimum requirement for FCMs. Many commentators believed that such a requirement would result in the elimination of guaranteed IBs due to the increased costs of doing business which the commentators expected to follow from the proposal. Specifically, these commentators suggested that the FCM would pass the capital requirement directly on to the guaranteed IB or, in the alternative, require higher clearing fees from the guaranteed IB. It appears, however, that many of these commentators misunderstood the proposal and viewed it as one which would require additional capital from an FCM regardless of its current requirement rather than as an alternative minimum requirement.

A number of commentators expressed the view that the alternative FCM requirement would also reduce competition in the industry by causing most guaranteed IBs to become affiliated with a few large FCMs (because the smaller FCMs will be unable to afford guaranteed IBs) and by eliminating many guaranteed IBs. A few of these commentators went on to state that by reducing compe-



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tition, customers would end up paying higher fees and the net effect of the proposal would be to injure rather than protect customers.

Several commentors were bothered by the idea that an FCM's capital requirement would be tied to a factor unrelated to the amount of equity an FCM controlled. These commentors opined that if the current requirements do not offer adequate customer protection, then the capital requirements of all FCMs should be raised but that the amount of capital required should continue to be based on the amount of equity controlled.

### 3. Discussion

After considering the comments received from Members and the revised IB proposal to be recommended to the Board, the FCM Advisory Committee and the Special Committee determined that FCM capital requirements should be amended to include alternative minimums parallel to the requirements imposed upon independent IBs. The Committees also concluded that guaranteed IBs should be treated as the functional equivalent of branch offices for purposes of determining the amount of capital required.

The Board agrees that the FCM capital requirement should include an alternative which ensures that an FCM maintains capital commensurate with the size of its operation in terms of remote locations operated (guaranteed IB's, guaranteed IB branch offices and proprietary branch offices) and APs sponsored (including those sponsored by a guaranteed IB). Although the Board is sympathetic to many of the commentors' concerns, it believes the current proposal addresses those concerns.

The formula recommended by the Special Committee has a minimal effect on the capital requirement of FCMs. The Board noted at the time it adopted the proposal that only five FCMs would have minimum capital based on the proposal and that none of those five would become undercapitalized as a result of the increased requirements. In those few instances where an FCM is affected by the proposal, the Board believes the alternative minimum is necessary to ensure that all FCMs which maintain extensive sales forces (either through guaranteed IBs or proprietary operations) have adequate capital to support their responsibilities over their sales networks. Furthermore, the Board believes that the same factors should be considered in determining the minimum capital of independent IBs and FCMs since the costs and risks associated with maintaining a significant sales operation are similar for both independent IBs and FCMs. The Board concluded that it is illogical to require an IB to maintain



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certain capital based on the number of offices operated or APs sponsored while permitting an FCM to operate with capital that would be insufficient based on the same formula.

NFA respectfully requests that the proposed amendments to NFA Financial Requirements Sections 1 and 6 become effective the later of July 1, 1992 or upon Commission approval.

**V. MODIFICATION TO INTERPRETIVE NOTICE TO NFA COMPLIANCE RULE 2-9 REGARDING A MEMBER SELF-AUDIT REQUIREMENT.**

- A. Revised Interpretive Notice Regarding a Member Self-Audit Requirement (to read as follows):

**INTERPRETIVE NOTICE TO NFA  
COMPLIANCE RULE 2-9: SUPERVISION**

NFA Compliance Rule 2-9 places a continuing responsibility on every Member to diligently supervise its employees and agents in all aspects of their futures activities. NFA recognizes that, given the differences in the size and complexity of the operations of NFA Members, there must be some degree of flexibility in determining what constitutes "diligent supervision" for each firm. It is NFA's policy to leave the exact form of supervision to the Member thereby providing the Member with flexibility to design procedures that are tailored to the Member's own situation. The Board of Directors adheres to this principle, but feels that all Members should regularly review the adequacy of their supervisory procedures.

The Board of Directors has determined that in order to satisfy their continuing supervisory responsibilities, NFA Members must review on a yearly basis self-audit questionnaires to be distributed by NFA's Compliance Department. The questionnaires must be reviewed by the appropriate supervisory personnel in either the home or branch office. After reviewing the questionnaire, the appropriate supervisory person must sign the questionnaire stating that the Member's operations have been evaluated based on the questionnaire and attesting that the Member's procedure comply with all applicable NFA requirements. Members are required to retain the signed questionnaires in their files for a period of five years from the date of review, with the questionnaires being readily accessible during the first two years. In addition, guaranteed IBs must provide and guarantor FCMs must obtain copies of the signed questionnaires. Members must also provide the signed questionnaires for inspection upon request by NFA.



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Review of the questionnaires should aid Members in recognizing potential problem areas and alert them to procedures which need to be revised or strengthened. The questionnaires focus on a Member's regulatory responsibilities and require a review of the adequacy of the Member's internal procedures. For example, the FCM questionnaire requires review of a Member's procedures relating to customer order flow, customer account documentation, risk disclosure, margin policies, option accounts and transactions, customer complaints, advertising, cash flow and compliance with financial requirements. The questionnaire also contains a promotional material checklist which will assist a Member in reviewing its promotional material for compliance with NFA requirements. Similarly, the CPO/CTA questionnaires contain a checklist which will assist CPOs and CTAs in their review of their disclosure documents.

A Member firm that does not comply with this Interpretive Notice will violate NFA Compliance Rule 2-9.

Questions regarding this Interpretation or the questionnaires should be directed to the Compliance Department at 1-800-621-3570.

B. Explanation of Revised Interpretive Notice to NFA Compliance Rule 2-9 Regarding a Member Self-Audit Requirement.

In a letter dated June 11, 1991, NFA submitted an Interpretive Notice to Compliance Rule 2-9 which would require all Members to complete self-audit questionnaires on an annual basis, to retain the completed questionnaires in their files and to produce the completed questionnaires for inspection upon request by NFA. These self-audit questionnaires would have required Members to respond "yes" or "no" to numerous questions involving the Member's procedures over such areas as customer order flow, account documentation and sales procedures. The basic purpose was to ensure that Members were aware of their supervisory responsibilities and reviewed the adequacy of their own procedures at least annually.

Since that time, NFA has received a number of comments on the questionnaires. These comments supported the basic goal of the questionnaires but voiced concern that the completed questionnaires would be discoverable in any litigation, reparation or arbitration proceedings involving the Member and could unfairly impact the Member. Furthermore, comments regarding the absolute nature of the questions and the limited nature of the answers available to Members were also voiced. Specifically, because



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many questions are phrased in terms of all cash receipts, all voided checks, etc., there may be some unusual circumstance which would require the Member to answer "no" to a specific question, although under the firm's usual practice and procedures the answer to the question would be "yes."

As a result of these concerns, the Board has determined that it is appropriate to eliminate the "yes" and "no" response columns. Members will still be required to review the questionnaires, but will not have to document a response to each question on the form. Rather, an appropriate supervisory person will be required to sign the questionnaire stating that the Member's operations have been evaluated based on the questionnaire. The Board believes this format will achieve the initial goal of alerting Members to potential problem areas while addressing the concerns expressed to staff.

The revised Interpretive Notice requires Members to review and sign the questionnaire on a yearly basis. In accordance with CFTC requirements, the Notice continues to require Members to retain the signed questionnaire in their files for a period of five years from the date of review, with the questionnaire being readily accessible during the first two years. In addition, each self-audit questionnaire will be revised to include a statement which must be signed by an appropriate supervisory person of the Member indicating that the questionnaire has been reviewed, that all questions applicable to the Member's operations have been addressed, and that the Member's procedures comply with all applicable NFA Requirements.

The revised Interpretive Notice is intended to replace, in its entirety, the earlier submission dated June 11, 1991. The revised Self-Audit Questionnaires are attached for your information.

NFA respectfully requests that the Interpretive Notice become effective upon Commission approval.

**VI. PROPOSED MODIFICATION TO BOARD RESOLUTION TO ADOPT A TEMPORARY NO-ACTION POSITION.**

- A. Board Resolution to Adopt a Modified No-Action Position in response to a Commodity Exchange, Inc. ("Comex") petition for relief from NFA Registration Rules 203, 206 and 401 (to read as follows):

RESOLVED that, for a period of one year from the CFTC's approval of this action or for a period of one year after Comex's



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gold asset participation contract begins trading, whichever is later, NFA will take no action to enforce the filing requirements set forth in NFA Registration Rules 203 and 206 and the proficiency testing requirements set forth in NFA Registration Rule 401 providing that the applicant's sponsor provides NFA with the full name and CRD number of the applicant and a certification, signed by both the applicant and the applicant's sponsor, stating that:

- 1) the applicant is currently registered with the National Association of Securities Dealers, Inc. as a general securities representative; and
- 2) the applicant's sole activities subject to regulation by the Commission are and will continue to be limited to the solicitation and acceptance of customer orders initiating or offsetting long positions in the gold asset participation contract traded at the Comex or the supervision of such activities; and
- 3) the applicant's sponsor understands that the sponsor must supervise the applicant's compliance with the above limitations on the applicant's activities and that any failure of the applicant to adhere to such limitations may be cause for, among other things, disciplinary action by NFA against the sponsor for violation of NFA Compliance Rule 2-9; and
- 4) the applicant's sponsor's supervisory structure includes a sufficient number of APs who have passed the Series 3 examination to ensure that the applicant is properly trained for and supervised in the performance of his futures activities; and
- 5) the applicant and the applicant's sponsor understand that NFA may at some later date require the applicant to comply with the filing requirements set forth in NFA Registration Rules 203 and 206 or the proficiency testing requirements set forth in NFA Registration Rule 401 or both as a condition of remaining registered and that the applicant's failure to do so within the time period which may be specified by the Board will be deemed a request to withdraw the applicant's registration as an associated person; and
- 6) the applicant is not subject to any statutory disqualifications set forth in Sections 8a(2) and 8a(3) of the Commodity Exchange Act; and



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- 7) the applicant will promptly correct any certification which is no longer accurate or current; and
- 8) the applicant agrees that the sponsor's home office shall be applicant's official address for purposes of accepting delivery and service of communications issued by or on behalf of the Commission, NFA, any futures self-regulatory organization or any futures customer; and
- 9) the applicant and the applicant's sponsor understand that the certification required by this resolution acts as an application for registration as an associated person and that willfully making a materially false or misleading statement in the certification or willfully failing to correct any inaccuracy in the certification is cause for denial, suspension or revocation of registration and criminal prosecution.

B. Explanation of the Modified Board Resolution to Adopt a No-Action Position in response to a Comex petition for relief from NFA Registration Rules 203, 206 and 401.

At the request of Commission staff in the Division of Trading and Markets, NFA has revised its temporary no-action position relating to the Comex's GAP contract. Commission staff asked NFA to revise the no-action position slightly to ensure that APs who have taken the Series 3 examination are sufficiently involved in the firm's supervisory structure. In order to satisfy the Commission's concerns, the resolution adopted by the Board at its February 28, 1991 meeting has been revised by changing the language of paragraph 4 of the resolution. The new language simply states that the sponsor's supervisory structure includes a sufficient number of APs who have passed the Series 3 examination to ensure that affected applicants are properly trained and supervised.

NFA respectfully requests that the revised no-action position be declared effective upon the later of Commission approval or commencement of trading of the contract.

NFA respectfully requests that the proposed new Compliance Rule 2-7; proposed amendments to NFA Compliance Rule 3-12 and Registration Rule 501; proposed amendments to NFA Compliance Rule 2-26 and Financial Requirements Sections 9, 10 and 11; proposed amendments to NFA Financial Requirements Sections 1 and 6; proposed modifications to Interpretive Notice to Compliance Rule 2-9 regarding a Member Self-Audit Requirement; and proposed





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modifications to Board Resolution to grant a temporary no-action position for the GAP contract be approved by the Commission as authorized by Section 17(j) of the Act.

Respectfully submitted,

Daniel J. Roth  
General Counsel

DJR:pjf(Ltrs/Webb.CAW)

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.  
Dennis A. Klejna, Esq.  
Joanne T. Medero, Esq.  
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Susan C. Ervin, Esq.  
Lawrence B. Patent, Esq.  
David Van Wagner, Esq.

## FCM SELF EXAMINATION QUESTIONNAIRE

### Instructions

NFA Compliance Rule 2-9 requires Members to diligently supervise the futures related activities of their agents and employees. To help Members carry out their supervisory responsibilities, NFA has devised a questionnaire for each category of registrant, for branch office operations and for promotional material. The questionnaires focus on areas such as customer order flow, account documentation, and sales procedures. Completion of the questionnaire will provide a checklist for each Member to ensure that no major area of supervisory responsibility is being overlooked. NFA's Board of Directors has issued an interpretative notice requiring each Member to review and retain the "self-audit" questionnaires which will be provided periodically by NFA.

Questionnaires should be reviewed and signed by the appropriate supervisory personnel in either the home or branch office, who must then certify that they have reviewed the firm's operations in light of the matters covered by the questionnaire. Completed questionnaires should not be forwarded to NFA but should be retained in both the branch and home offices. Guaranteed IBs should provide and guarantor FCMs should obtain copies of the signed questionnaires. Signed questionnaires should be readily available for the last two years and retained for the last five.

If you have questions, please contact the NFA Compliance Department at 1-800-621-3570 (Out of State) and 1-800-572-9400 (Inside Illinois).

### General

1. Does your firm insure that all individuals which have the following authority or ownership are listed as principals on the firm's Form 7R?
  - a. Any person including, but not limited to, a sole proprietor, general partner, officer, director, or person occupying a similar status or performing similar functions, having the power, directly or indirectly, through agreement or otherwise, to exercise a controlling influence over the firm's activities which are subject to regulation by the CFTC.
  - b. Any holder or beneficial owner of ten percent or more of the outstanding shares of any class of stock?
  - c. Any person who has contributed ten percent or more of the capital?
2. Does your firm ensure that all individuals which are responsible for supervising APs are registered as APs?

3. Do your branches hold themselves out in the name of the firm?
4. If your firm is a one person office, do you inform customers when you will be unavailable to service your customer accounts (i.e., vacations) and who they should contact in your absence?
5. Does your firm have procedures to review all firms which you are doing business with to insure those which are required to be registered are registered?

**Customer Order Flow**

1. Are only registered Associated Persons allowed to handle customer accounts?
2. Are unregistered individuals accepting/receiving customer orders?  
  
If so, are they performing their duties in a purely clerical manner?
3. Does your firm utilize pre-numbered customer order tickets or assign an internally generated order number to each order ticket immediately upon receipt of the order from the customer?
4. Does your firm have controls in place to insure that all customer order tickets (filled, unfilled, open, cancelled) are properly retained and filed by date?
5. Are controls in place to insure that the following information is recorded on customer order tickets:
  - a. Date?
  - b. Commodity Options/Future?
  - c. Account Identification?
  - d. Quantity Long/Short?
  - e. Requested Price?
  - f. Fill Price?

For customer option orders only:

- g. Put or Call?
- h. Strike Price?
- i. Premium?

For discretionary futures/options customer orders only:

- j. Does your firm identify the customer order ticket as discretionary?

For discretionary options customer order only:

- k. Does an officer or supervisory individual from your firm approve, initial, and date each order ticket?
- 6a. Does your firm time-stamp futures order tickets immediately upon receipt of the order from the customer?
  - b. Does your firm time-stamp options order tickets immediately upon receipt of the order from the customer and upon transmission of the order for execution?
- 7. Upon receipt of a customer order during market hours, does your firm immediately call its carrying broker or the floor directly?
  - 8. Does your firm ensure that customer orders executable at or near the market are transmitted to the floor before any orders in the same commodity for proprietary accounts or other accounts affiliated with the firm?
  - 9. Does your firm record the fill price when it is received?
  - 10. Does your firm promptly call the customer with the fill information?
  - 11. Does your firm maintain any documents produced or obtained as a result of the order flow processes for a period of five years? (i.e., customer order tickets, equity run, customer statements, open position listing, day trade listing, P & S recap.)
  - 12. Does your firm mail confirmation statements to customers no later than the business day after the customer transaction?
  - 13. Does your firm mail monthly statements to active customers promptly after every month end?
  - 14. Does your firm mail monthly statements to inactive customers at least every three months?
  - 15. Does your firm offset positions on a FIFO basis unless the customer gives other instructions?
  - 16. When errors arise between requested customer order and the executed trade, does your firm absorb the losses and give the gains to the customer?

17. Does your firm prohibit the inclusion of discretionary and non-discretionary orders on a block order?
18. Does your firm prohibit trades for proprietary and non-customer accounts to be combined with its customer orders on block orders?
19. Does your firm utilize a system to allocate split fills in a fair and non-preferential manner?
20. Does your firm require individuals placing block orders to submit the customer account numbers at the time the order is received?
21. Does your firm have procedures to review the accounts of foreign omnibus accounts to look for unusual trading or money flow patterns which may indicate problems, such as bucketing of trades?
22. Does your firm have procedures to insure proper large trader reports are being filed with the appropriate agencies?

**Customer, Proprietary, Non-customer accounts**

1. Has your firm reviewed the customer account documentation to insure it complies with all applicable Rules and Regulations?
2. Does your firm require that all necessary information be on file before new accounts are allowed to commence trading?
3. Does your firm require a partner, officer, director, branch office manager or supervisory employee to approve customer accounts and document this review?
4. Does your firm have procedures to ensure adequate risk disclosure is provided to customers, other than partnerships, corporations, and floor traders, prior to opening an account?
5. Does your firm obtain the following information from its customers:
  - a. Customer's name?
  - b. Customer's occupation or business description?
  - c. Customer's estimated annual income?
  - d. Customer's estimated net worth?
  - e. Customer's approximate age?
  - f. Customer's prior investment and futures trading experience?

6. If your firm does not obtain the information in 5. above for any given customer, does your firm document that the customer declined to provide such information?
7. Does your firm provide training to the individuals which are responsible for assessing and providing risk disclosure to customers as required by NFA Compliance Rule 2-30?
8. Has your firm designated a supervisory individual to review the actions of the individuals providing risk disclosure to customers as required by NFA Compliance Rule 2-30?
9. If a predispute agreement is included in the customer account documentation, does your firm provide customers with a list of three forums, one of which is NFA arbitration, in the event the customer gives notice of its intent to file a claim?
10. If your firm carries accounts of employees of other commodity firms:
  - a. Do you receive written authorization from a person designated by such other Futures Commission Merchant (FCM) or Introducing Broker (IB) with responsibility for surveillance over the employees' account?
  - b. Do you transmit regularly to such FCM or IB, customer statements and order tickets for such account?
11. If your firm allows affiliated persons to maintain accounts at other FCMs and IBs:
  - a. Does your firm provide the affiliated person with a written authorization from a person designated by the firm which has responsibility for surveillance of the affiliated person's account?
  - b. Does your firm receive copies of statements and order tickets relating to the account of the affiliated person on a regular basis?
12. Does your firm have procedures to ensure that employees of exchanges and regulatory organizations are not allowed to trade at your firm?
13. Does your firm have procedures to ensure that corporate resolutions authorizing trading authority and account (strategy) limitations are signed by the appropriate level of authority at the corporation?
14. Does your firm review the financial standing of omnibus accounts and commodity pools before the account are accepted?

15. If your firm carries accounts of investment companies or pension funds, is your firm in compliance with CFTC Interpretation #10?
16. Does your firm maintain a record that clearly identifies which of the firm's accounts are discretionary?
17. Does your firm have procedures regarding supervision and review of discretionary trading activity?
18. Does your firm require power of attorney to be terminated in writing?
19. Does your firm ensure that APs have two years experience prior to handling discretionary accounts?
20. If your firm accepts customers which utilize a third party account controller:
  - a. Does your firm obtain a copy of the account controller's written trading authorization, or a written acknowledgement from the customer that such authorization has been given?
  - b. Does your firm obtain an acknowledgement from the customer that he received a disclosure document from the account controller, or a written statement from the account controller explaining why he is not required to give the customer a disclosure document?
21. If your firm assesses fees and charges which are not determined on a per trade or round-turn basis, does the firm provide customers with a written explanation of the charges and reasonable examples on a per trade or round-turn basis?
22. If your firm carries accounts of introducing brokers, do the customer's statements identify the name of the FCM and IB?
23. Does your firm inform NFA of the omnibus accounts it carries and its carrying brokers?
24. Does your firm review its customers to ensure it is not doing business with an entity/individual which is required to be registered but is not?

#### **Margins**

1. Does your firm make margin calls when an account is undermargined?
2. Does your firm prepare a written daily listing of outstanding calls?

3. Does the daily listing indicate the number of days the call is outstanding?
4. Are the margin calls cumulative?
5. Does your firm collect margin calls in a timely manner?
6. Has your firm set a pre-determined length of time allowed for the collection of outstanding margin calls?
7. Does your firm refuse to allow customers to make withdrawals from accounts when the margin therein is less than the initial requirements, or when the withdrawals would impair the initial requirements?
8. Are related accounts aggregated as if they were one account when determining if excess margin is available for withdrawal?
9. Are all payouts to customers made only after proper approval from the margin department or other appropriate level of authority?
10. Does your firm margin domestic omnibus accounts on a gross basis?
11. Does your firm utilize SPAN margin rates for Chicago Mercantile Exchange positions?
12. If not, how is your firm determining that your margin calls and undermargined capital charges are no less than those which would be calculated utilizing SPAN?
13. Does your firm obtain current margin rates and SPAN risk parameters on a regular or daily basis?

#### **Option Procedures**

1. Does your firm require that the customer be informed of all option transaction costs including commissions, mark-ups, costs to exercise an option, prior to the first option transaction?
2. Does your firm inform its customers of the premium and strike price for subsequent option transactions?
3. Does your firm document the fact that they provided the information in 1 and 2 above?

#### **NFA Fees**

1. Does your firm invoice NFA fees to all customers and non-customers in accordance with NFA Bylaw 1301?



2. Does your firm separately reflect NFA fees from commissions?

**Customer Complaints and Advertising**

1. Does your firm have a designated "compliance officer" who is responsible for handling customer complaints or inquiries of a compliance nature?
2. Does your firm have policies and procedures in effect to handle customer complaints and inquiries?
3. Does your firm maintain a compliance procedures manual or other written documentation which outlines the firm's policy with respect to handling compliance matters, such as customer complaints and/or inquiries?
4. Does your firm have a systematic method of recording, investigating and responding to customer complaints and/or inquiries?
5. Does your firm require your branches and GIBs to forward complaints to the home office?
6. Does your firm have an Internal Audit Department or other designated individual which monitors branches and GIBs ("Auditor")?
7. Does the Auditor report to a partner or officer?
8. Does the Auditor have responsibility for conducting on-site inspections of branch offices and guaranteed IBs?
9. Are the on-site inspections performed regularly?
10. Does the Auditor utilize an audit program when conducting on-site inspections?
11. Does your firm ensure that appropriate corrective action has been taken in the event the Auditor finds problems at a branch or GIB?
12. Is the Auditor familiar with NFA Notice I-90-14 regarding Branch Office and Guaranteed IB on-site visits?
13. Does your firm have policies and procedures regarding the hiring and supervision of APs who have been or whose past employers have been expelled or revoked by NFA or the CFTC for fraud?
14. Does your firm have procedures in effect to distribute changes in rules or regulatory agencies to appropriate personnel?

15. Does your firm utilize any of the following methods to supervise sales solicitation: direct listening, reviewing taped solicitations, silent phone monitoring or customer contact?
16. Does your firm provide its APs with training regarding the futures and options markets?
17. Does your firm provide sales solicitation training to APs?
18. Does your firm have procedures to monitor incoming and outgoing mail to ensure that customer complaints, etc. would be intercepted?
19. Does your firm provide adequate risk disclosure to customers wishing to purchase deep-out-of-the-money-options?
20. Does your firm review commission payout records to ensure only individuals or firms which are registered are being paid?
21. Does your firm have written procedures to supervise the preparation and use of promotional material?
22. Does your firm require an officer, general partner, sole proprietor, branch office manager or other supervisory employee other than the individual who prepared such material to approve promotional material before use?
23. Does your firm require the review and approval of promotional material to be in writing?
24. Does your firm maintain all promotional materials for a period of five years from the date last used?
25. Is the content of your firm's promotional material in compliance with NFA Compliance Rule 2-29? (See attached promotional material checklist.)

**Cash Flow**

1. Does your firm make all disbursements by check, except petty cash?
2. Does a responsible individual at your firm approve in writing invoices prior to payment?
3. If your firm allows branch offices to write checks or make other types of disbursements, does your firm have any controls in effect to review this activity?
4. Does your firm review this activity in a timely manner?

5. If your firm disburses money to a third party, does the firm have specific written authorization from the account owner on file?
6. Does your firm ensure all requests for monies have been initiated by the account owner?
7. If introducing brokers are allowed to deposit checks in a qualifying bank account or forward checks to the home office, does your firm maintain documents authorizing such procedures?
8. Does your firm have procedures to ensure cash received at branch offices and introducing brokers is communicated timely for accounting purposes and deposited timely?
9. Does your firm require introducing brokers and branch offices to prepare a listing of all cash receipts?
10. Does your firm require introducing brokers and branch offices to make and keep copies of customer checks prior to depositing them?
11. Does your firm review the records above on a regular basis and compare them to the bank records?
12. If physical cash is received by your firm, is it adequately controlled through the use of pre-numbered receipts or the like?
13. Does your firm restrictively endorse checks upon receipt?
14. Does your firm have procedures to carefully review third party checks received from customers and endorsed to your firm, to ensure the initial payee is not required to be registered?
15. Does your firm verify wire transfer receipts before they are booked?
16. Does your firm prepare bank reconciliations within a month of receipt of the bank statement?
17. Does your firm ensure that blank checks are only accessible to authorized personnel?
18. Does your firm ensure that all voided checks are mutilated to prevent reuse and kept on file?
19. If signature plates are used, does your firm have adequate controls and limited access over plates?

20. Does your firm review checks and wires received to ensure they are from account owners of the account to which they are to be credited?
21. Does your firm take action if money is found to be deposited by anyone other than the account owner?

#### Financial

1. Does your firm balance accounting records on a monthly basis?
2. Does your firm retain financial and compliance records for five years?
3. Does your firm maintain its general ledger on an accrual basis?
4. Does your firm prepare a trial balance on a monthly basis?
5. Does an individual at an appropriate level of authority approve journal entries?
6. Does your firm prepare detailed support to convert your firm's trial balance or general ledger to the financial statement format?
7. Does your firm prepare and maintain on file monthly capital computations within 30 days after the month end?
8. Does your firm prepare quarterly 1-FR or Focus statements including Supplementary Schedules and file them with NFA, the DSRO and the CFTC within 45 days after the end of the quarter?
9. Does your firm prepare daily segregation and secured amount computations by noon of the following day?
10. Does your firm ensure the preparer of the statements mentioned above is knowledgeable of all the requirements for financial statement preparation?
11. In the case of this individual's absence, does your firm have another knowledgeable individual available to prepare the above statements?
12. Does your firm monitor intra-month capital compliance?
13. Does your firm review positions in the firm's trading account to determine their effect on the firm's compliance with minimum capital requirements?

14. Does your firm have adequate physical safeguards in place to ensure that accounting and security records are accessible only to those individuals who have responsibility for maintaining such records?
15. Does your firm have procedures for reconciling positions and equities with your carrying brokers in a timely manner?
16. Does your firm maintain complete and detailed records of all securities held or owned by the firm?
17. Does your firm have adequate safeguards and controls over all negotiable instruments including proper segregation of duties?
18. Does your firm have procedures to reconcile securities held in safekeeping to the bank?
19. Does your firm properly segregate and account for customer securities and property?
20. Does your firm ensure that all customer property is clearly designated as customer segregated?
21. Does the firm regularly reconcile the customer statements to the equity system?
22. Does the firm have procedures to review the equity run to ensure accounts of officers, directors, partners and employees are reflected separately in the equity run as non-customer and proprietary accordingly?
23. Has your firm assigned an individual at an appropriate level of authority with responsibility for obtaining approval and/or renewal of subordination agreements and submitting them to the DSRO?

**ATTESTATION**

Appropriate supervisory personnel for \_\_\_\_\_  
(Member Firm)

have reviewed and evaluated \_\_\_\_\_ current  
(Member's)

procedures in light of the factors enumerated above. Based on

that review, \_\_\_\_\_  
(Member Firm)

believes that its current procedures are adequate to meet its  
supervisory responsibilities.

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Signature

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Date

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Title

fcm

## BRANCH SELF EXAMINATION QUESTIONNAIRE

### Instructions

NFA Compliance Rule 2-9 requires Members to diligently supervise the futures related activities of their agents and employees. To help Members carry out their supervisory responsibilities, NFA has devised a questionnaire for each category of registrant, for branch office operations and for promotional material. The questionnaires focus on areas such as customer order flow, account documentation, and sales procedures. Completion of the questionnaire will provide a checklist for each Member to ensure that no major area of supervisory responsibility is being overlooked. NFA's Board of Directors has issued an interpretative notice requiring each Member to review and retain the "self-audit" questionnaires which will be provided periodically by NFA.

Questionnaires should be reviewed and signed by the appropriate supervisory personnel in either the home or branch office, who must then certify that they have reviewed the firm's operations in light of the matters covered by the questionnaire. Completed questionnaires should not be forwarded to NFA but should be retained in both the branch and home offices. Guaranteed IBs should provide and guarantor FCMs should obtain copies of the signed questionnaires. Signed questionnaires should be readily available for the last two years and retained for the last five.

If you have questions, please contact the NFA Compliance Department at 1-800-621-3570 (Out of State) and 1-800-572-9400 (Inside Illinois).

### General

1. Does your branch insure that all individuals which have the following authority or ownership are listed as principals on the firm's Form 7R?
  - a. Any person including, but not limited to, a sole proprietor, general partner, officer, director, or person occupying a similar status or performing similar functions, having the power, directly or indirectly, through agreement or otherwise, to exercise a controlling influence over the branch's activities which are subject to regulation by the CFTC.
  - b. Any holder or beneficial owner of ten percent or more of the out-standing shares of any class of stock.
  - c. Any person who has contributed ten percent or more of the capital.

2. Does your firm ensure that all individuals which are responsible for supervising APs are registered as APs?
3. Does your branch office hold itself out in the name of the firm?
4. If your branch is a one person office, do you inform customers when you will be unavailable to service your customer accounts (i.e., vacations) and who they should contact in your absence?
5. Does your branch have procedures to review all firms which you are doing business with to insure those which are required to be registered are registered?

**Customer Order Flow**

1. Are only registered Associated Persons allowed to handle customer accounts?
2. Are unregistered individuals accepting/receiving customer orders?  

If so, are they performing their duties in a purely clerical manner?
3. Does your firm utilize pre-numbered customer order tickets or assign an internally generated order number to each order ticket immediately upon receipt of the order from the customer?
4. Does your firm have controls in place to insure that all customer order tickets (filled, unfilled, open, cancelled) are properly retained and filed by date or sent to the home office?
5. Are controls in place to insure that the following information is recorded on customer order tickets:
  - a. Date?
  - b. Commodity Options/Future?
  - c. Account Identification?
  - d. Quantity Long/Short?
  - e. Requested Price?
  - f. Fill Price?

For customer option orders only:

- g. Put or Call?
- h. Strike Price?
- i. Premium?



For discretionary futures/options customer orders only:

- j. Does your branch identify the customer order ticket as discretionary?

For discretionary options customer order only:

- k. Does an officer or supervisory individual from your branch approve, initial, and date each order ticket?
- 6a. Does your branch time-stamp futures order tickets immediately upon receipt of the order from the customer?
  - b. Does your branch time-stamp options order tickets immediately upon receipt of the order from the customer and upon transmission of the order for execution?
- 7. Upon receipt of a customer order during market hours, does your branch immediately call its carrying broker or the floor directly?
  - 8. Does your firm ensure that customer orders executable at or near the market are transmitted to the floor before any orders in the same commodity for proprietary accounts or other accounts affiliated with the firm?
  - 9. Does your branch record the fill price when it is received?
  - 10. Does your branch promptly call the customer with the fill information?
  - 11. Does your branch prohibit the inclusion of discretionary and non-discretionary orders on a block order?
  - 12. Does your branch prohibit trades for proprietary and non-customer accounts to be combined with its customer orders on block orders?
  - 13. Does your branch utilize a system to allocate split fills in a fair and non-preferential manner?
  - 14. Does your branch require individuals placing block orders to submit the customer account numbers prior to receiving the fill prices on those block orders?
  - 15. Does your branch have procedures to review the accounts of foreign omnibus accounts to look for unusual trading or money flow patterns which may indicate problems, such as bucketing of trades?

**Customer, Proprietary, Non-customer accounts**

1. Does your branch require that all necessary information be on file before new accounts are allowed to commence trading?
2. Does your branch have procedures to ensure adequate risk disclosure is provided to customers, other than partnerships, corporations, and floor traders, prior to opening an account?
3. Does your firm obtain the following information from its customers:
  - a. Customer's name?
  - b. Customer's occupation or business description?
  - c. Customer's estimated annual income?
  - d. Customer's estimated net worth?
  - e. Customer's approximate age?
  - f. Customer's prior investment and futures trading experience?
4. If your branch does not obtain the information in 3. above for any given customer, does your firm document that the customer declined to provide such information?
5. Does your branch provide training to the individuals which are responsible for assessing and providing risk disclosure to customers as required by NFA Compliance Rule 2-30?
6. Has your branch designated a supervisory individual to review the actions of the individuals providing risk disclosure to customers as required by NFA Compliance Rule 2-30?
7. If your branch allows affiliated persons to maintain accounts at other FCM's and IB's:
  - a. Does your branch provide the affiliate person with a written authorization from a person designated by the firm which has responsibility for surveillance of the affiliated person's account?
  - b. Does your branch receive copies of statements and order tickets relating to the account of the affiliated person on a regular basis?
8. Does your branch maintain a record that clearly identifies which of the branch's accounts are discretionary?
9. Does your branch have procedures regarding supervision and review of discretionary trading activity?

10. Does your branch require power of attorney to be terminated in writing?
11. Does your branch ensure that APs have two years experience prior to handling discretionary accounts?
12. If your branch assesses fees and charges which are not determined on a per trade or round-turn basis, does the branch provide customers with a written explanation of the charges and reasonable examples on a per trade or round-turn basis?
13. Does your branch review its customers to ensure it is not doing business with an entity/individual which is required to be registered, but is not?

#### **Option Procedures**

1. Does your branch require that the customer be informed of all option transaction costs including commissions, mark-ups, costs to exercise an option, prior to the first option transaction?
2. Does your branch inform its customers of the premium and strike price for subsequent option transactions?
3. Does your branch document the fact that they provided the information in 1 and 2 above?

#### **Customer Complaints and Advertising**

1. Does your branch have a designated "compliance officer" who is responsible for handling customer complaints or inquiries of a compliance nature?
2. Does your branch have policies and procedures in effect to handle customer complaints and inquiries?
3. Does your branch maintain a compliance procedures manual or other written documentation which outlines the firm's policy with respect to handling compliance matters, such as customer complaints and/or inquiries?
4. Does your branch have a systematic method of recording, investigating and responding to customer complaint and/or inquiries?
5. Do you forward complaints to the home office?
6. Does your branch have policies and procedures regarding the hiring and supervision of APs who have been or whose past employers have been expelled or revoked by NFA or CFTC for fraud?

7. Does your branch have procedures in effect to distribute changes in rules or regulatory agencies to appropriate personnel?
8. Does your branch utilize any of the following methods to supervise sales solicitation: direct listening, reviewing taped solicitations, silent phone monitoring or customer contact?
9. Does your branch provide its APs with training on the futures and options markets?
10. Does your branch provide sales solicitation training to APs?
11. Does your branch have procedures to monitor incoming and outgoing mail to ensure that customer complaints, etc. would be intercepted?
12. Does your branch provide adequate risk disclosure to customers wishing to purchase deep-out-of-the-money-options?
13. Does your branch have written procedures to supervise the preparation and use of promotional material?
14. Does your branch require an officer, general partner, sole proprietor, branch office manager or other supervisory employee other than the individual who prepared such material to approve promotional material before use?
15. Does your branch require the review and approval of promotional material to be in writing?
16. Does your branch maintain all promotional materials for a period of five years from the date last used?
17. Is the content of your branches' promotional material in compliance with NFA Compliance Rule 2-29? (See attached promotional material checklist.)

**Cash Flow**

For Omnibus FCM Branch Offices Only

1. If your branch utilizes a branch bank account, does your branch ensure that all customer deposits are made immediately, and that cash receipts are reported to the home office in a timely manner?
2. Does your branch restrictively endorse checks immediately upon receipt?
3. Does your branch prepare a listing of all customer deposits?

4. Does your branch make and keep copies of customer checks prior to depositing them?
5. Does your branch have procedures to carefully review third-party checks received from customers and endorsed to your branch, to ensure that initial payee is not required to be registered?

For IB and Fully Disclosed FCM Branch Offices

1. If your branch is allowed to deposit checks in a qualifying bank account or forward checks to the carrying broker FCM, does your branch maintain documents authorizing such procedures?
2. Does your branch ensure that all customer deposits are made immediately, and that cash receipts are reported to the carrying broker FCM in a timely manner?
3. Does your branch restrictively endorse checks immediately upon receipt?
4. Does your branch prepared a listing of all customer deposits?
5. Does your branch make and keep copies of customer checks prior to depositing them in a qualifying bank account?
6. Does your branch have procedures to carefully review third-party checks received from customers and endorsed to the carrying broker FCM, to ensure the initial payee is not required to be registered?
7. Does your branch prohibit the acceptance of checks in any name other than the carrying broker FCM, and physical cash from customers?
8. Does your branch return to the customer any check received which is not written to the carrying broker FCM?

ATTESTATION

Appropriate supervisory personnel for \_\_\_\_\_  
(Member Firm)  
have reviewed and evaluated \_\_\_\_\_ current  
(Member's)  
procedures in light of the factors enumerated above. Based on

that review, \_\_\_\_\_  
(Member Firm)

believes that its current procedures are adequate to meet its  
supervisory responsibilities.

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Date

\_\_\_\_\_  
Title

branch

## INDEPENDENT IB SELF EXAMINATION QUESTIONNAIRE

### Instructions

NFA Compliance Rule 2-9 requires Members to diligently supervise the futures related activities of their agents and employees. To help Members to carry out their supervisory responsibilities, NFA has devised a questionnaire for each category of registrant, for branch office operations and for promotional material. The questionnaires focus on areas such as customer order flow, account documentation, and sales procedures. Completion of the questionnaire will provide a checklist for each Member to ensure that no major area of supervisory responsibility is being overlooked. NFA's Board of Directors has issued an interpretative notice requiring each Member to review and retain the "self-audit" questionnaires which will be provided periodically by NFA.

Questionnaires should be reviewed and signed by the appropriate supervisory personnel in either the home or branch office, who must then certify that they have reviewed the firm's operations in light of the matters covered by the questionnaire. Completed questionnaires should not be forwarded to NFA but should be retained in both the branch and home offices. Guaranteed IBs should provide and guarantor FCMS should obtain copies of the signed questionnaires. Signed questionnaires should be readily available for the last two years and retained for the last five.

If you have questions, please contact the NFA Compliance Department at 1-800-621-3570 (Out of State) and 1-800-572-9400 (Inside Illinois).

### General

1. Does your firm insure that all individuals which have the following authority or ownership are listed as principals on the firm's Form 7R?
  - a. Any person including, but not limited to, a sole proprietor, general partner, officer, director, or person occupying a similar status or performing similar functions, having the power, directly or indirectly, through agreement or otherwise, to exercise a controlling influence over the firms' activities which are subject to regulation by the CFTC.
  - b. Any holder or beneficial owner of ten percent or more of the outstanding shares of any class of stock.
  - c. Any person who has contributed ten percent or more of the capital.

2. Does your firm ensure that all individuals which are responsible for supervising APs are registered as APs?
3. Do your branches hold themselves out in the name of the firm?
4. If your firm is a one person office, do you inform customers when you will be unavailable to service your customer accounts (i.e., vacations) and who they should contact in your absence?
5. Does your firm have procedures to review all firms which you are doing business with to insure those which are required to be registered are registered?

#### Customer Order Flow

1. Are only registered Associated Persons allowed to handle customer accounts?
2. Are unregistered individuals accepting/receiving customer orders?  
  
If so, are they performing their duties in a purely clerical manner?
3. Does your firm utilize pre-numbered customer order tickets or assign an internally generated order number to each order ticket immediately upon receipt of the order from the customer?
4. Does your firm have controls in place to ensure that all customer order tickets (filled, unfilled, open, cancelled) are properly retained and filed by date?
5. Are controls in place to insure that the following information recorded on customer order tickets:
  - a. Date?
  - b. Commodity Options/Future?
  - c. Account Identification?
  - d. Quantity Long/Short?
  - e. Requested Price?
  - f. Fill Price?

For customer option orders only:

- g. Put or Call?
- h. Strike Price?
- i. Premium?



For discretionary futures/options customer orders only:

- j. Does your firm identify the customer order ticket as discretionary?

For discretionary options customer order only:

- k. Does an officer or supervisory individual from your firm approve, initial, and date each order ticket?
- 6a. Does your firm time-stamp futures order tickets immediately upon receipt of the order from the customer?
  - b. Does your firm time-stamp options order tickets immediately upon receipt of the order from the customer, and upon transmission of the order for execution?
- 7. Upon receipt of a customer order during market hours does your firm immediately call its carrying broker or the floor directly?
  - 8. Does your firm ensure to the extent possible that customer orders executable at or near the market are transmitted to the floor before any orders in the same commodity for proprietary or other persons affiliated with the firm?
  - 9. Does your firm record the fill price when it is received?
  - 10. Does your firm promptly call the customer with the fill information?
  - 11. Does your firm maintain any documents produced or obtained as a result of the order flow processes for a period of five years (i.e., customer order tickets, equity run, customer statements, open position listing, day trade listing, P & S recap)?
  - 12. Does your firm prohibit the inclusion of discretionary and non-discretionary orders on a block order?
  - 13. Does your firm prohibit trades for proprietary and non-customer accounts to be combined with its customer orders on block orders?
  - 14. Does your firm utilize a system to allocate split fills in a fair and non-preferential manner?
  - 15. Does your firm require individuals placing block orders to submit the customer account numbers at the time the order is received?

16. Does your firm have procedures to review the accounts of foreign omnibus accounts to look for unusual trading or money flow patters which may indicate problems, such as bucketing of trades?
17. Does your firm have procedures to insure proper large trader reports are being filed with the appropriate agencies?

**Customer, Proprietary, Non-customer accounts**

1. Has your firm reviewed the customer account documentation to insure it complies with all applicable Rules and Regulations?
2. Does your firm require that all necessary information be on file before new accounts are allowed to commence trading?
3. Does your firm require a partner, officer, director, branch office manager or supervisory employee to approve customer accounts and document this review?
4. Does your firm have procedures to ensure adequate risk disclosure is provided to customers, other than partnerships, corporations, and floor traders, prior to opening an account?
5. Does your firm obtain the following information from its customers:
  - a. Customer's name?
  - b. Customer's occupation or business description?
  - c. Customer's estimated annual income?
  - d. Customer's estimated net worth?
  - e. Customer's approximate age?
  - f. Customer's prior investment and futures trading experience?
6. If your firm does not obtain the information in 5. above for any given customer, does your firm document that the customer declined to give such information?
7. Does your firm provide training to the individuals which are responsible for assessing and providing risk disclosure to customers as required by NFA Compliance Rule 2-30?
8. Has your firm designated a supervisory individual to review the actions of the individuals providing risk disclosure to customers as required by NFA Compliance Rule 2-30?

9. If a predispute agreement is included in the customer account documentation, does your firm provide customers with a list of three forums, one of which is NFA arbitration, in the event the customer gives notice of its intent to file a claim?
10. Does your firm have procedures to ensure that corporate resolutions authorizing trading authority and account (strategy) limitations are signed by the appropriate level of authority at the corporation?
11. If your firm allows affiliated persons to maintain accounts at other FCMs and IBs:
  - a. Does your firm provide the affiliated person with a written authorization from a person designated by the firm which has responsibility for surveillance of the affiliated person's account?
  - b. Does your firm receive copies of statements and order tickets relating to the account of the affiliated person on a regular basis?
12. Does your firm maintain a record that clearly identifies which of the firm's accounts are discretionary?
13. Does your firm have procedures regarding supervision and review of discretionary trading activity?
14. Does your firm require power of attorney to be terminated in writing?
15. Does your firm ensure that APs have two years experience prior to handling discretionary accounts?
16. If your firm accepts customers which utilize a third party account controller:
  - a. Does your firm obtain a copy of the account controller's written trading authorization, or a written acknowledgement from the customer that such authorization has been given?
  - b. Does your firm obtain an acknowledgement from the customer that he received a disclosure document from the account controller, or a written statement from the account controller explaining why he is not required to give the customer a disclosure document?
17. If your firm assesses fees and charges which are not determined on a per trade or round-turn basis, does not firm provide customers with a written explanation of the charges and reasonable examples on a per trade or round-turn basis?

18. If your firm carries accounts of introducing brokers do the customer statements identify the name of the FCM and IB?
19. Does your firm review its customers to ensure it is not doing business with an entity/individual which is required to be registered but is not?

#### **Option Procedures**

1. Does your firm require that the customer be informed of all option transaction costs including commissions, mark-ups, costs to exercise an option, prior to the first option transaction?
2. Does your firm inform its customers of the premium and strike price for subsequent option transactions?
3. Does your firm document the fact that they provided the information in 1 and 2 above?

#### **Customer Complaints and Advertising**

1. Does your firm have a designated "compliance officer" who is responsible for handling customer complaints or inquiries of a compliance nature?
2. Does your firm have policies and procedures in effect to handle customer complaints and inquiries?
3. Does your firm maintain a compliance procedures manual or other written documentation which outlines the firm's policy with respect to handling compliance matters, such as customer complaints and/or inquiries?
4. Does your firm have a systematic method of recording, investigating and responding to customer complaints and/or inquiries?
5. Does your firm require your branches and GIBs to forward complaints to the home office?
6. Does your firm have an Internal Audit Department or other designated individual which monitors branches and GIBs ("Auditor")?
7. Does the Auditor report to a partner or officer?
8. Does the Auditor have responsibility for conducting on-site inspections of branch offices and guaranteed IBs?
9. Are the on-site inspections performed regularly?

10. Does the Auditor utilize an audit program when conducting on-site inspections?
11. Does your firm ensure that appropriate corrective action has been taken in the event the Auditor finds problems at a branch?
12. Is the Auditor familiar with NFA Notice I-90-14 regarding Branch Office and Guaranteed IB On-site Visits?
13. Does your firm have policies and procedures regarding the hiring and supervision of APs who have been or whose past employers have been expelled or revoked by NFA or the CFTC for fraud?
14. Does your firm have procedures in effect to distribute changes in rules or regulatory agencies to appropriate personnel?
15. Does your firm utilize any of the following methods to supervise sales solicitation: direct listening, reviewing taped solicitations, silent phone monitoring and customer contact?
16. Does your firm provide its APs with training on the futures and options markets?
17. Does your firm provide sales solicitation training to APs?
18. Does your firm have procedures to monitor incoming and outgoing mail to ensure that customer complaints, etc. would be intercepted?
19. Does your firm provide adequate risk disclosure to customers wishing to purchase deep-out-of-the-money-options?
20. Does your firm review commission payout records to ensure only individuals or firms which are registered are being paid?
21. Does your firm have written procedures to supervise the preparation and use of promotional material?
22. Does your firm require an officer, general partner, sole proprietor, branch office manager or other supervisory employee other than the individual who prepared such material to approve promotional material before use?
23. Does your firm require the review and approval of promotional material to be in writing?
24. Does your firm maintain all promotional materials for a period of five years from the date last used?

25. Is the content of your firms' promotional material in compliance with NFA Compliance Rule 2-29? (See attached promotional material checklist.)

**Cash Flow**

1. Does your firm make all disbursements by check, except petty cash?
2. Does a responsible individual at your firm approve in writing invoices prior to payment?
3. If your firm allows branch offices to write checks or make other types of disbursements, does your firm have any controls in effect to review this activity?
4. Does your firm review this activity in a timely manner?
5. If your firm is allowed to deposit checks in a qualifying bank account or forward checks to the carrying broker, does your firm maintain document authorizing such procedures?
6. Does your firm have procedures to ensure cash received at branch offices and at your office is deposited immediately and communicated timely to the carrying broker for accounting purposes?
7. Does your firm prepare a listing of all cash receipts?
8. Does your firm make and keep copies of customer checks prior to depositing them in a qualifying bank account?
9. Does your firm prohibit the acceptance of checks made payable to anyone other than the carrying broker FCM and physical cash from customers?
10. Does your firm return to the customer any check received which is not written to the carrying broker FCM?
11. Does your firm restrictively endorse checks upon receipt?
12. Does your firm have procedures to carefully review third party checks received from customers and endorsed to your firm, to ensure the initial payee is not required to be registered?
13. Does your firm prepare bank reconciliations within a month of receipt of the bank statement?
14. Does your firm ensure that blank checks are only accessible to authorized personnel?

15. Does your firm ensure that all voided checks are mutilated to prevent reuse and kept on file?
16. If signature plates are used, does your firm have adequate controls and limited access over plates?

#### **Financial**

1. Does your firm balance accounting records on a monthly basis?
2. Does your firm retain financial and compliance records for five years?
3. Does your firm maintain its general ledger on an accrual basis?
4. Does your firm prepare a trial balance on a monthly basis?
5. Does an individual at an appropriate level of authority approve journal entries?
6. Does your firm prepare detailed support to convert your firm's trial balance or general ledger to the financial statement format?
7. Does your firm prepare and maintain on file monthly capital computations within 30 days after the month end?
8. Does your firm prepare quarterly 1-FR or Focus statements including Supplementary Schedules and file them with NFA, the DSRO and the CFTC within 45 days after the end of the quarter?
9. Does your firm ensure the preparer of the statements mentioned above is knowledgeable of all the requirements for financial statement preparation?
10. In the case of this individual's absence, does your firm have another knowledgeable individual available to prepare the above statements?
11. Does your firm monitor intra-month capital compliance?
12. Does your firm review positions in the firm's trading account to determine their effect on the firm's compliance with minimum capital requirements?
13. Does your firm have adequate physical safeguards in place to ensure that accounting and security records are accessible only to those individuals who have responsibility for maintaining such records?

- 14. Does your firm have procedures for reconciling positions and equities with your carrying brokers in a timely manner?
- 15. Does your firm maintain complete and detailed records of all securities held or owned by the firm?
- 16. Does your firm have adequate safeguards and controls over all negotiable instruments including proper segregation of duties?
- 17. Has your firm assigned an individual at an appropriate level of authority with responsibility for obtaining approval and/or renewal of subordination agreements and submitting them to NFA?

**ATTESTATION**

Appropriate supervisory personnel for \_\_\_\_\_  
(Member Firm)

have reviewed and evaluated \_\_\_\_\_ current  
(Member's)

procedures in light of the factors enumerated above. Based on

that review, \_\_\_\_\_  
(Member Firm)

believes that its current procedures are adequate to meet its  
supervisory responsibilities.

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Date

\_\_\_\_\_  
Title



## GUARANTEED IB SELF EXAMINATION QUESTIONNAIRE

### Instructions

NFA Compliance Rule 2-9 requires Members to diligently supervise the futures related activities of their agents and employees. To help Members to carry out their supervisory responsibilities, NFA has devised a questionnaire for each category of registrant, for branch office operations and for promotional material. The questionnaires focus on areas such as customer order flow, account documentation, and sales procedures. Completion of the questionnaire will provide a checklist for each Member to ensure that no major area of supervisory responsibility is being overlooked. NFA's Board of Directors has issued an interpretative notice requiring each Member to review and retain the "self-audit" questionnaires which will be provided periodically by NFA.

Questionnaires should be reviewed and signed by the appropriate supervisory personnel in either the home or branch office, who must then certify that they have reviewed the firm's operations in light of the matters covered by the questionnaire. Completed questionnaires should not be forwarded to NFA but should be retained in both the branch and home offices. Guaranteed IBs should provide and guarantor FCMs should obtain copies of the signed questionnaires. Signed questionnaires should be readily available for the last two years and retained for the last five.

If you have questions, please contact the NFA Compliance Department at 1-800-621-3570 (Out of State) and 1-800-572-9400 (Inside Illinois).

### General

1. Does your firm insure that all individuals which have the following authority or ownership are listed as principals on the firm's Form 7R?
  - a. Any person including, but not limited to, a sole proprietor, general partner, officer, director, or person occupying a similar status or performing similar functions, having the power, directly or indirectly, through agreement or otherwise, to exercise a controlling influence over the firms' activities which are subject to regulation by the CFTC.
  - b. Any holder or beneficial owner of ten percent or more of the outstanding shares of any class of stock.
  - c. Any person who has contributed ten percent or more of the capital.

2. Does your firm ensure that all individuals which are responsible for supervising APs are registered as APs?
3. Do your branches hold themselves out in the name of the firm?
4. If your firm is a one person office, do you inform customers when you will be unavailable to service your customer accounts (i.e., vacations) and who they should contact in your absence?
5. Does your firm have procedures to review all firms which you are doing business with to insure those which are required to be registered are registered?

**Customer Order Flow**

1. Are only registered Associated Persons allowed to handle customer accounts?
2. Are unregistered individuals accepting/receiving customer orders?  
  
If so, are they performing their duties in a purely clerical manner?
3. Does your firm utilize pre-numbered customer order tickets or assign an internally generated order number to each order ticket immediately upon receipt of the order from the customer?
4. Does your firm have controls in place to ensure that all customer order tickets (filled, unfilled, open, cancelled) are properly retained and filed by date?
5. Are controls in place to insure that the following information recorded on customer order tickets:
  - a. Date?
  - b. Commodity Options/Future?
  - c. Account Identification?
  - d. Quantity Long/Short?
  - e. Requested Price?
  - f. Fill Price?

For customer option orders only:

- g. Put or Call?
- h. Strike Price?
- i. Premium?

For discretionary futures/options customer orders only:

- j. Does your firm identify the customer order ticket as discretionary?

For discretionary options customer order only:

- k. Does an officer or supervisory individual from your firm approve, initial, and date each order ticket?
- 6a. Does your firm time-stamp futures order tickets immediately upon receipt of the order from the customer?
  - b. Does your firm time-stamp options order tickets immediately upon receipt of the order from the customer, and upon transmission of the order for execution?
- 7. Upon receipt of a customer order during market hours does your firm immediately call its carrying broker or the floor directly?
  - 8. Does your firm ensure to the extent possible that customer orders executable at or near the market are transmitted to the floor before any orders in the same commodity for proprietary or other persons affiliated with the firm?
  - 9. Does your firm record the fill price when it is received?
  - 10. Does your firm promptly call the customer with the fill information?
  - 11. Does your firm maintain any documents produced or obtained as a result of the order flow processes for a period of five years? (i.e., customer order tickets, equity run, customer statements, open position listing, day trade listing, P & S recap.)
  - 12. Does your firm prohibit the inclusion of discretionary and non-discretionary orders on a block order?
  - 13. Does your firm prohibit trades for proprietary and non-customer accounts to be combined with its customer orders on block orders?
  - 14. Does your firm utilize a system to allocate split fills in a fair and non-preferential manner?
  - 15. Does your firm require individuals placing block orders to submit the customer account numbers at the time the order is received?

16. Does your firm have procedures to review the accounts of foreign omnibus accounts to look for unusual trading or money flow patters which may indicate problems, such as bucketing of trades?
17. Does your firm have procedures to insure proper large trader reports are being filed with the appropriate agencies?

**Customer, Proprietary, Non-customer accounts**

1. Has your firm reviewed the customer account documentation to insure it complies with all applicable Rules and Regulations?
2. Does your firm require that all necessary information be on file before new accounts are allowed to commence trading?
3. Does your firm require a partner, officer, director, branch office manager or supervisory employee to approve customer accounts and document this review?
4. Does your firm have procedures to ensure adequate risk disclosure is provided to customers, other than partnerships, corporations, and floor traders, prior to opening an account?
5. Does your firm obtain the following information from its customers:
  - a. Customer's name?
  - b. Customer's occupation or business description?
  - c. Customer's estimated annual income?
  - d. Customer's estimated net worth?
  - e. Customer's approximate age?
  - f. Customer's prior investment and futures trading experience?
6. If your firm does not obtain the information in 5. above for any given customer, does your firm document that the customer declined to give such information?
7. Does your firm provide training to the individuals which are responsible for assessing and providing risk disclosure to customers as required by NFA Compliance Rule 2-30?
8. Has your firm designated a supervisory individual to review the actions of the individuals providing risk disclosure to customers as required by NFA Compliance Rule 2-30?

9. If a predispute agreement is included in the customer account documentation, does your firm provide customers with a list of three forums, one of which is NFA arbitration, in the event the customer gives notice of its intent to file a claim?
10. Does your firm have procedures to ensure that corporate resolutions authorizing trading authority and account (strategy) limitations are signed by the appropriate level of authority at the corporation?
11. If your firm allows affiliated persons to maintain accounts at other FCMs and IBs:
  - a. Does your firm provide the affiliated person with a written authorization from a person designated by the firm which has responsibility for surveillance of the affiliated person's account?
  - b. Does your firm receive copies of statements and order tickets relating to the account of the affiliated person on a regular basis?
12. Does your firm have procedures to ensure that employees of exchanges and regulatory organizations are not allowed to trade at your firm?
13. Does your firm maintain a record that clearly identifies which of the firm's accounts are discretionary?
14. Does your firm have procedures regarding supervision and review of discretionary trading activity?
15. Does your firm require power of attorney to be terminated in writing?
16. Does your firm ensure that APs have two years experience prior to handling discretionary accounts?
17. If your firm accepts customers which utilize a third party account controller:
  - a. Does your firm obtain a copy of the account controller's written trading authorization, or a written acknowledgement from the customer that such authorization has been given?
  - b. Does your firm obtain an acknowledgement from the customer that he received a disclosure document from the account controller, or a written statement from the account controller explaining why he is not required to give the customer a disclosure document?

18. If your firm assesses fees and charges which are not determined on a per trade or round-turn basis, does your firm provide customers with a written explanation of the charges and reasonable examples on a per trade or round-turn basis?
19. If your firm carries accounts of introducing brokers do the customer statements identify the name of the FCM and IB?
20. Does your firm review its customers to ensure it is not doing business with an entity/individual which is required to be registered but is not?

#### **Option Procedures**

1. Does your firm require that the customer be informed of all option transaction costs including commissions, mark-ups, costs to exercise an option, prior to the first option transaction?
2. Does your firm inform its customers of the premium and strike price for subsequent option transactions?
3. Does your firm document the fact that they provided the information in 1 and 2 above?

#### **Customer Complaints and Advertising**

1. Does your firm have a designated "compliance officer" who is responsible for handling customer complaints or inquiries of a compliance nature?
2. Does your firm have policies and procedures in effect to handle customer complaints and inquiries?
3. Does your firm maintain a compliance procedures manual or other written documentation which outlines the firm's policy with respect to handling compliance matters, such as customer complaints and/or inquiries?
4. Does your firm have a systematic method of recording, investigating and responding to customer complaints and/or inquiries?
5. Does your firm require your branches and GIBs to forward complaints to the home office?
6. Does your firm have an Internal Audit Department or other designated individual which monitors branches and GIBs ("Auditor")?
7. Does the Auditor report to a partner or officer?

8. Does the Auditor have responsibility for conducting on-site inspections of branch offices and guaranteed IBs?
9. Are the on-site inspections performed regularly?
10. Does the Auditor utilize an audit program when conducting on-site inspections?
11. Does your firm ensure that appropriate corrective action has been taken in the event the Auditor finds problems at a branch or GIB?
12. Is the Auditor familiar with NFA Notice I-90-14 regarding Branch Office and Guaranteed IB On-site Visits?
13. Does your firm have policies and procedures regarding the hiring and supervision of APs who have been or whose past employers have been expelled or revoked by NFA or the CFTC for fraud?
14. Does your firm have procedures in effect to distribute changes in rules or regulatory agencies to appropriate personnel?
15. Does your firm utilize any of the following methods to supervise sales solicitation: direct listening, reviewing taped solicitations, silent phone monitoring and customer contact?
16. Does your firm provide its APs with training on the futures and options markets?
17. Does your firm provide sales solicitation training to APs?
18. Does your firm have procedures to monitor incoming and outgoing mail to ensure that customer complaints, etc. would be intercepted?
19. Does your firm provide adequate risk disclosure to customers wishing to purchase deep-out-of-the-money-options?
20. Does your firm review commission payout records to ensure only individuals or firms which are registered are being paid?
21. Does your firm have written procedures to supervise the preparation and use of promotional material?
22. Does your firm require an officer, general partner, sole proprietor, branch office manager or other supervisory employee other than the individual who prepared such material to approve promotional material before use?

23. Does your firm require the review and approval of promotional material to be in writing?
24. Does your firm maintain all promotional materials for a period of five years from the date last used?
25. Is the content of your firms' promotional material in compliance with NFA Compliance Rule 2-29? (See attached promotional material checklist.)

**Cash Flow**

1. Does your firm make all disbursements by check, except petty cash?
2. Does a responsible individual at your firm approve in writing invoices prior to payment?
3. If your firm allows branch offices to write checks or make other types of disbursements, does your firm have any controls in effect to review this activity?
4. Does your firm review this activity in a timely manner?
5. If your firm is allowed to deposit checks in a qualifying bank account or forward checks to the carrying broker FCM, does your firm maintain documents authorizing such procedures?
6. Does your firm have procedures to ensure cash received at branch offices and at your office is deposited immediately and communicated timely to the carrying broker FCM for accounting purposes?
7. Does your firm prepare a listing of all cash receipts?
8. Does your firm make and keep copies of customer checks prior to depositing them in a qualifying bank account?
9. Does your firm prohibit the acceptance of checks made payable to anyone other than the carrying broker FCM and physical cash from customers?
10. Does your firm return to the customer any check received which is not written to the carrying broker FCM?
11. Does your firm restrictively endorse checks upon receipt?
12. Does your firm have procedures to carefully review third-party checks received from customers and endorsed to the carrying broker FCM, to insure the initial payee is not required to be registered?



13. Does your firm prepare bank reconciliations within a month of receipt of the bank statement?
14. Does your firm ensure that blank checks are only accessible to authorized personnel?
15. Does your firm ensure that all voided checks are mutilated to prevent reuse and kept on file?
16. If signature plates are used, does your firm have adequate controls and limited access over plates?

**Guarantee Agreements**

1. Does your firm file all guarantee agreements and termination notices with NFA?
2. Does your firm maintain a copy of a guarantee agreement which has been signed by principals of each party?

**ATTESTATION**

Appropriate supervisory personnel for \_\_\_\_\_  
(Member Firm)

have reviewed and evaluated \_\_\_\_\_ current  
(Member's)

procedures in light of the factors enumerated above. Based on

that review, \_\_\_\_\_  
(Member Firm)

believes that its current procedures are adequate to meet its

supervisory responsibilities.

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Date

\_\_\_\_\_  
Title

gib

**PROMOTIONAL MATERIAL  
REVIEW CHECKLIST**

Promotional Material Title: \_\_\_\_\_

Prepared By: \_\_\_\_\_ Date: \_\_\_\_\_

Reviewed By: \_\_\_\_\_ Date: \_\_\_\_\_

For FCMs and IBs Only:

Options Material submitted to DSRO Date: \_\_\_\_\_

- 1.\* Statistical data is mathematically accurate. [NFA Rule 2-29(b)]
- 2.\* Statistical data is accurate. [NFA Rule 2-29(b)]
- 3.\* Statements of fact are accurate. [NFA Rule 2-29(b)(2)]
- 4.\* Statements of opinion are readily identifiable as such. [NFA Rule 2-29(c)]
- 5.\* Statements of opinion have a reasonable basis in fact. (Note: any statement of opinion which does not have a reasonable basis in fact, may be deemed to be a statement which is likely to deceive the public.) [NFA Rule 2-29(c)]
6. The promotional material does not contain any potentially fraudulent claims, omissions of fact, or misleading statements. [NFA Rule 2-29(b)(2)]
7. The material mentions the risk of loss in an equally prominent manner with respect to the possibility of profit. [NFA rule 2-29(b)(3)]
8. If the promotional material includes hypothetical trading results:
  - a. The material includes the statement prescribed by CFTC Regulation 4.41(b)(1). [NFA Rule 2-29(b)(4)]
  - b.\* The actual and hypothetical returns for the same time periods are similar or reasonable explanations for any differences are disclosed. [NFA Rule 2-29(b)(2)]
9. The material states that past results are not necessarily indicative of future results, when actual past results are mentioned. [NFA Rule 2-29(b)(5)]

10. If the material contains actual past performance: [NFA Rule 2-29(b)(6)]
  - a.\* The actual past performance data is based on the performance of reasonably comparable accounts.
  - b.\* If the material contains the actual past performance of the CTA's personal account and not that of the customer's: [NFA Rule 2-29(b)(2)]
    1. This fact is clearly identified.
    2. Differences in the performance results, commission and fee charges, strategies and other material information is fully disclosed.
11. If the data is based on the performance of a "model" account: [NFA Rule 2-29(b)(2) and (6)]
  - a.\* There were no accounts traded comparably and this fact is disclosed.
  - b.\* The fact that the account is hypothetical and that all trades were never made for a single account is disclosed.
  - c. The firm's overall actual trading results are disclosed.
  - d. Explanation for any differences between model and actual results are disclosed.
  - e. Differences in the performance results, commission and fee charges, strategies and other material information are fully disclosed.
- 12.\* For actual and hypothetical results, the firm used an acceptable method of calculating rate of return and described how that rate of return was calculated. [NFA Rule 2-29(b)(2) and (6)]
13. The material does not guarantee a customer against loss. [NFA Rule 2-29(b)(1)]
14. The term "control" is not utilized to imply that the customer will own, or hold the underlying commodity. [NFA Rule 2-29(b)(2)]
15. If the material states that options have limited risk and no margin calls, it states that this applies to long options only. [NFA Rule 2-29(b)(2)]

16. If the material states that long options have a pre-determined limited risk, it also states that the risk is the full amount of the option's premium. [NFA Rule 2-29(b)(2)]
17. If the promotional material is a paid promotional appearance, this fact has been prominently identified immediately prior, subsequent to, and during the broadcast if necessary. [NFA Rule 2-29(b)(2)]
18. If material contains results and ratings by outside sources:
  - a. Material has adequately disclosed all information about the results and ratings to ensure material is not misleading. [NFA Rule 2-29(b)(2)]
  - b.\* Firm must insure it has adequate support documentation for all information included in the material. [NFA Rule 2-29(d)]
- 19.\* If trading championship results are advertised, material contains adequate disclosure of information about strategies employed which might differ from those utilized to trade customer accounts, smaller commission rates, incentive fee rate differences, etc., so as to not make the material misleading. [NFA Rule 2-29(b)(2)]
- 20.\* If the promotional material is in the form of a reprinted article, material has been supplemented if necessary with proper disclosures and disclaimers, to insure material is not misleading. [NFA Rule 2-29(b)]

\* Adequate support documentation must be on file at the firm.

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**PROMOTIONAL MATERIAL  
REVIEW CHECKLIST**

**Promotional Material Title:** \_\_\_\_\_

**Prepared By:** \_\_\_\_\_ **Date:** \_\_\_\_\_

**Reviewed By:** \_\_\_\_\_ **Date:** \_\_\_\_\_

For FCMS and IBs Only:

**Options Material submitted to DSRO** **Date:** \_\_\_\_\_

- 1.\* Statistical data is mathematically accurate. [NFA Rule 2-29(b)]
- 2.\* Statistical data is accurate. [NFA Rule 2-29(b)]
- 3.\* Statements of fact are accurate. [NFA Rule 2-29(b)(2)]
- 4.\* Statements of opinion are readily identifiable as such. [NFA Rule 2-29(c)]
- 5.\* Statements of opinion have a reasonable basis in fact. (Note: any statement of opinion which does not have a reasonable basis in fact, may be deemed to be a statement which is likely to deceive the public.) [NFA Rule 2-29(c)]
6. The promotional material does not contain any potentially fraudulent claims, omissions of fact, or misleading statements. [NFA Rule 2-29(b)(2)]
7. The material mentions the risk of loss in an equally prominent manner with respect to the possibility of profit. [NFA rule 2-29(b)(3)]
8. If the promotional material includes hypothetical trading results:
  - a. The material includes the statement prescribed by CFTC Regulation 4.41(b)(1). [NFA Rule 2-29(b)(4)]
  - b.\* The actual and hypothetical returns for the same time periods are similar or reasonable explanations for any differences are disclosed. [NFA Rule 2-29(b)(2)]
9. The material states that past results are not necessarily indicative of future results, when actual past results are mentioned. [NFA Rule 2-29(b)(5)]

10. If the material contains actual past performance: [NFA Rule 2-29(b)(6)]
  - a.\* The actual past performance data is based on the performance of reasonably comparable accounts.
  - b.\* If the material contains the actual past performance of the CTA's personal account and not that of the customer's: [NFA Rule 2-29(b)(2)]
    1. This fact is clearly identified.
    2. Differences in the performance results, commission and fee charges, strategies and other material information is fully disclosed.
11. If the data is based on the performance of a "model" account: [NFA Rule 2-29(b)(2) and (6)]
  - a.\* There were no accounts traded comparably and this fact is disclosed.
  - b.\* The fact that the account is hypothetical and that all trades were never made for a single account is disclosed.
  - c. The firm's overall actual trading results are disclosed.
  - d. Explanation for any differences between model and actual results are disclosed.
  - e. Differences in the performance results, commission and fee charges, strategies and other material information are fully disclosed.
- 12.\* For actual and hypothetical results, the firm used an acceptable method of calculating rate of return and described how that rate of return was calculated. [NFA Rule 2-29(b)(2) and (6)]
13. The material does not guarantee a customer against loss. [NFA Rule 2-29(b)(1)]
14. The term "control" is not utilized to imply that the customer will own, or hold the underlying commodity. [NFA Rule 2-29(b)(2)]
15. If the material states that options have limited risk and no margin calls, it states that this applies to long options only. [NFA Rule 2-29(b)(2)]

16. If the material states that long options have a pre-determined limited risk, it also states that the risk is the full amount of the option's premium. [NFA Rule 2-29(b)(2)]
17. If the promotional material is a paid promotional appearance, this fact has been prominently identified immediately prior, subsequent to, and during the broadcast if necessary. [NFA Rule 2-29(b)(2)]
18. If material contains results and ratings by outside sources:
  - a. Material has adequately disclosed all information about the results and ratings to ensure material is not misleading. [NFA Rule 2-29(b)(2)]
  - b.\* Firm must insure it has adequate support documentation for all information included in the material. [NFA Rule 2-29(d)]
- 19.\* If trading championship results are advertised, material contains adequate disclosure of information about strategies employed which might differ from those utilized to trade customer accounts, smaller commission rates, incentive fee rate differences, etc., so as to not make the material misleading. [NFA Rule 2-29(b)(2)]
- 20.\* If the promotional material is in the form of a reprinted article, material has been supplemented if necessary with proper disclosures and disclaimers, to insure material is not misleading. [NFA Rule 2-29(b)]

\* Adequate support documentation must be on file at the firm.

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## CPO SELF EXAMINATION QUESTIONNAIRE

### Instructions

NFA Compliance Rule 2-9 requires Members to diligently supervise the futures related activities of their agents and employees. To help Members to carry out their supervisory responsibilities, NFA has devised a questionnaire for each category of registrant, for branch office operations and for promotional material. The questionnaires focus on areas such as customer order flow, account documentation, and sales procedures. Completion of the questionnaire will provide a checklist for each Member to ensure that no major area of supervisory responsibility is being overlooked. NFA's Board of Directors has issued an interpretative notice requiring each Member to review and retain the "self-audit" questionnaires which will be provided periodically by NFA.

Questionnaires should be reviewed and signed by the appropriate supervisory personnel in either the home or branch office, who must then certify that they have reviewed the firm's operations in light of the matters covered by the questionnaire. Completed questionnaires should not be forwarded to NFA but should be retained in both the branch and home offices. Guaranteed IBs should provide and guarantor FCMS should obtain copies of the signed questionnaires. Signed questionnaires should be readily available for the last two years and retained for the last five.

If you have questions, please contact the NFA Compliance Department at 1-800-621-3570 (Out of State) and 1-800-572-9400 (Inside Illinois).

### General

1. Does your firm insure that all individuals which have the following authority or ownership are listed as principals on the firm's Form 7R?
  - a. Any person including, but not limited to, a sole proprietor, general partner, officer, director, or person occupying a similar status or performing similar functions, having the power, directly or indirectly, through agreement or otherwise, to exercise a controlling influence over the firms' activities which are subject to regulation by the CFTC.
  - b. Any holder or beneficial owner of ten percent or more of the outstanding shares of any class of stock.
  - c. Any person who has contributed ten percent or more of the capital.



2. Does your firm ensure that all individuals which are responsible for supervising APs are registered as APs?
3. Do your branches hold themselves out in the name of the firm?
4. If your firm is a one person office, do you inform customers when you will be unavailable to service your customer accounts (i.e., vacations) and who they should contact in your absence?
5. Does your firm have procedures to insure that checks are received in the name of the applicable pool or carrying broker (for deposit in the pool's trading account) and not in the name of your firm?
6. Does your firm have procedures to review all firms which you are doing business with to insure those which are required to be registered are registered?
7. Is your firm a separate legal entity from each of the pools it operates?

#### **Records**

1. If a predispute agreement is included in the customer account documentation, does your firm provide customers with a list of three forums, one of which is NFA arbitration, in the event the customer gives notice of its intent to file a claim?
2. Does your firm maintain the following documents for each pool operated for five years?
  - a. Cash receipts and disbursements journal
  - b. Security purchases and sales journal
  - c. Adjusting journal entries
  - d. Subsidiary Ledger for each Participant, including:
    1. Name
    2. Address
    3. Dates of deposits, withdrawals, etc.
    4. Amount of deposits and withdrawals, etc.
    5. Gains/Losses accruing to participant
    6. Participant equity calculated on a quarterly/monthly basis
    7. Number of units owned
  - e. General Ledger
  - f. Copies of statements received from carrying broker
  - g. Bank statements and cancelled checks
  - h. Dated copies of all reports and letters

- i. Balance sheets
    1. Prepared quarterly if pool's net asset value is less than \$500,000 at the beginning of the pool's fiscal year.
    2. Prepared monthly if pool's net asset value is greater than \$500,000 at the beginning of the pool's fiscal year.
  - j. Income statement
    1. Prepared either quarterly or monthly as described in i. 1 and 2 above.
    2. Prepared on a year-to-date basis.
  - k. Account statement prepared either quarterly or monthly as described in i. 1 and 2 above.
    1. Signed and dated acknowledgement of receipt of the disclosure document which was prior to the initial deposit and no more than 6 months after the date of the disclosure document.
  - m. Acknowledgement of receipt of the foreign futures and options disclosure statement.
3. If your firm or principals have trading accounts, does your firm maintain copies of the statements received from the carrying broker?
  4. Does your firm have procedures to file with the CFTC a Statement of Reporting Trader in the event your firm holds or controls reportable positions (CFTC Form 40)?

**Customer Complaints, Sales Practices & Promotional Material**

1. Does your firm have a designated "compliance officer" who is responsible for handling customer complaints or inquiries of a compliance nature?
2. Does your firm have policies and procedures in effect to handle customer complaints and inquiries?
3. Does your firm maintain a compliance procedures manual or other written documentation which outlines the firm's policy with respect to handling compliance matters, such as customer complaints and/or inquiries?
4. Does your firm have a systematic method of recording, investigating and responding to customer complaints and/or inquiries?
5. Does your firm require your branches to forward complaints to the home office?
6. Does your firm have an Internal Audit Department or other designated individual which monitors branches ("Auditor")?
7. Does the Auditor report to a partner or officer?

8. Does the Auditor have responsibility for conducting on-site inspections of branch offices?
9. Are the on-site inspections performed regularly?
10. Does the Auditor utilize an audit program when conducting on-site inspections?
11. Does your firm ensure that appropriate corrective action has been taken in the event the Auditor finds problems at a branch?
12. Is the Auditor familiar with NFA Notice 1-90-14 regarding Branch Office On-site Visits?
13. Does your firm have policies and procedures regarding the hiring and supervision of APs who have been or whose past employers have been expelled or revoked by NFA or the CFTC for fraud?
14. Does your firm have procedures in effect to distribute changes in rules or regulatory agencies to appropriate personnel?
15. Does your firm utilize any of the following methods to supervise sales solicitation: direct listening, reviewing taped solicitations, silent phone monitoring and customer contact?
16. Does your firm provide its APs with training on the futures and options markets?
17. Does your firm provide sales solicitation training to APs?
18. Does your firm have procedures to monitor incoming and outgoing mail to insure that customer complaints, etc. would be intercepted?
19. Does your firm have written procedures to supervise the preparation and use of promotional material?
20. Does your firm require an officer, general partner, sole proprietor, branch office manager or other supervisory employee other than the individual who prepared such material to approve promotional material before use?
21. Does your firm require the review and approval of promotional material to be in writing?
22. Does your firm maintain all promotional materials for a period of five years from the date last used?

23. Is the content of your firms' promotional material in compliance with NFA Compliance Rule 2-29? (See attached promotional material checklist.)

#### **Fees**

1. Does your firm calculate fees in accordance with the disclosure document?
2. If your firm collects fees from clients directly instead of from the carrying broker, does your firm reflect the amount in the performance record as an addition and as a debit to net performance?

#### **Block Orders**

1. If your firm is also the CTA and operates more than one pool, does your firm utilize a system to allocate split fills in a systematic and non-preferential manner?
2. If your CTA or carrying broker allocates split fills, are you aware of the method utilized and is it systematic and non-preferential?
3. Are your block order procedures in writing?
4. Does your firm provide the carrying broker with the account numbers to receive the fill at the time a trade is placed?

#### **Financial**

1. Does your firm's monthly/quarterly account statement include:
  - a. Statement of Income and Loss itemizing:
    1. Realized commodity trading gain or loss?
    2. Change in OTE?
    3. Other gains and losses?
    4. Management fees?
    5. Advisory fees?
    6. Brokerage commissions?
    7. Other fees?
    8. Other expenses?
  - b. Statement of Changes in NAV itemizing:
    1. Beginning NAV?
    2. Additions?
    3. Withdrawals?
    4. Net Income/Loss?
    5. Ending NAV?
    6. NAV per unit or individual's interest in the pool?

- c. Signed oath or affirmation:
    - 1. Manually signed?
    - 2. Signed by proper individual?
  - d. Beneath the oath does the following appear:
    - 1. The name of the individual signing the document?
    - 2. The capacity in which the individual is signing?
    - 3. The name of the commodity pool operator for which the individual is signing?
    - 4. The name of the commodity pool for which the document is being distributed?
  - e. Does the account statement disclose any changes or material business dealings between the pool and its operator, trading advisor, FCM or principals not previously disclosed in the disclosure document?
- 2. Has your firm examined each investment made with pool funds and the disclosure document to insure the investment is allowed?
  - 3. Has your firm engaged an independent certified public accountant to perform a certified audit of each pool operated during the past fiscal year?
  - 4. If trading in any of your pools has permanently ceased have you engaged an independently certified public accountant to do a certified audit?
  - 5. Has your firm distributed copies of the certified audit reports to the CFTC, NFA and to each of the participants within 90 days of the fiscal year end or within 90 days of when the pool funds were returned to participants?
  - 6. Do the certified audit reports include the following information for the preceding two year ends?
    - a. Net asset value of the pool?
    - b. Net asset value per outstanding participation unit in the pool?
    - c. Total value of the participant's interest or share in the pool?
    - d. Statement of financial condition?
    - e. Statement of Income and Loss?
    - f. Changes in Financial Position?
    - g. Changes in Ownership Equity?
    - h. Appropriate footnote disclosure and such further material information as may be necessary to ensure that the required statements are not misleading?

**Disclosure Document**

1. Does your firm file two copies to the CFTC and one copy to NFA of your disclosure documents and any amendments at least 21 calendar days prior to the date you first intend to solicit customers with the document?
2. Does your firm file amendments or a new disclosure document when the existing document becomes materially incomplete or inaccurate?
3. Does your firm provide prospective clients with a disclosure document, including any existing amendments, which is six months old or less prior to soliciting, directing or guiding a clients account?
4. Does your firm provide existing participants with all amendments to the disclosure document?
5. If disclosure document deficiency letters are received by the CFTC or NFA, does your firm promptly correct your document and submit your corrections to both organizations?

**ATTESTATION**

Appropriate supervisory personnel for \_\_\_\_\_  
(Member Firm)

have reviewed and evaluated \_\_\_\_\_ current  
(Member's)

procedures in light of the factors enumerated above. Based on

that review, \_\_\_\_\_  
(Member Firm)

believes that its current procedures are adequate to meet its  
supervisory responsibilities.

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Date

\_\_\_\_\_  
Title

**COMMODITY POOL  
DISCLOSURE DOCUMENT CHECKLIST**

Date \_\_\_\_\_

Pool Name \_\_\_\_\_

D.D. Date \_\_\_\_\_

**A. SPECIFIC RISK STATEMENTS**

1. Does the cover page of the Disclosure Document contain the cautionary statement using the language in Section 4.21(a)(18) and is the disclosure displayed in capital letters and in boldface type?
2. Does the cover page of the Disclosure Document highlight in tabular form the following, as described in the Guideline for Disclosure of Up Front Fees:
  - a. initial investment?
  - b. all up front fees and charges, including all organizational and operating expenses?
  - c. net proceeds available for trading?
  - d. Is the table complete and accurate? (If CPO does not require a standard initial investment, the table must highlight the up front fees and expenses proportionately as \$1,000 units.)
3. Does the Risk Disclosure Statement contain the language in Section 4.21(a)(17)(i); is it the only language on the page immediately following any disclosures required to appear pursuant to registered futures associations, the commission and applicable securities law; and is the disclosure displayed in capital letters and in boldface type?
4. If the potential liability to the participant is greater than the contributions and profits, is the LAST paragraph of the Risk Disclosure Statement as stated in Section 4.21(a)(17)(ii) and is the disclosure displayed in capital letters and in boldface type?
5. If the pool intends to trade foreign futures and options is the disclosure statement required by 30.6 included and in boldface type? If not, ensure that the disclosure is provided to pool participants?

B. DOCUMENT SPECIFICS

1. Is the Disclosure Document dated?
2. Is the date of the Disclosure Document less than six months from today?  
  
If not, is the document currently being used?
3. Does the CPO include the pool's most current account statement and annual report with each Disclosure Document sent to participants?
4. Is the document paginated and fastened in a secure manner?

C. POOL OPERATOR AND PRINCIPALS

Does the Disclosure Document contain the following information about the CPO and its principals:

1. Name of CPO and principals?
2. Address and telephone of main business office?
3. If address is P.O. Box, location of records?
4. Form of organization?
5. Business background for past 5 years of CPO and principals, including:
  - a. Name of employers?
  - b. Nature of business/venture?
  - c. Duties?
6. Extent of ownership/interest in pool. If none, must state?
7. Material, administrative, civil or criminal action against CPO/principals in past 5 years. If none, must state?
8. If commodity interest will be/are traded for own account(s)? If not, must state.
9. If trading own account(s), statement as to whether participants may inspect records?



D. CTA OF SUBJECT POOL AND/OR PRINCIPALS

Does the Disclosure Document contain the following information about the trading advisor and its principals:

1. Name of CTA and principals?
2. Business background of CTA and its principals for past 5 years, including:
  - a. Name of employers?
  - b. Nature of business/venture?
  - c. Duties?
3. Extent of ownership/interest in pool. If none, must state?
4. Material, administrative, civil or criminal action against CTA/principals in past 5 years. If none, must state?
5. If commodity interest will be/are traded for own account(s)? If not, must state.
6. If trading own account(s), statement as to whether participants may inspect records?

E. FCM/IB AND PRINCIPALS

Does the Disclosure Document contain the following information about the FCM/IB and its principals:

1. If known, does Disclosure Document state which FCM will be clearing trades?
2. Material, administrative, civil or criminal action against FCM and principals in past five years. If none, must state?
3. If applicable, the IB through which the pool will introduce its trades to the FCM?
4. Material, administrative, civil, or criminal actions against IB and principals in past five years. If none, must state?

F. SUBJECT POOL

Does the Disclosure contain the following information about the pool:

1. Name?
2. Form of organization?

3. Types of commodity interests the pool will trade?
4. Any restrictions or limitations on trading?
5. Name of person who will make trading decisions?

G. CONFLICTS OF INTEREST

1. Are actual or potential conflicts of interest disclosed relating to:
  - a. CPO?
  - b. Principals of the CPO?
  - c. CTA?
  - d. Principals of the CTA?
  - e. FCM?
  - f. Principals of the FCM?
  - g. IB?
  - h. Principals of the IB?
2. If the CPO, CTA, or any of their principals may benefit from the maintenance of the pool's account with an FCM or IB, is the arrangement described?
3. If the firm includes trades for its principals, APs, and/or proprietary account in block orders, is this potential conflict of interest disclosed?

H. REQUIREMENTS/RESTRICTIONS ON POOL

Does the Disclosure Document contain the following information:

1. Minimum amount of funds necessary before pool commences trading? If none, must state.
2. Disposition of funds if minimum isn't reached, including time period of disposition?
3. Maximum amount of funds accepted by pool? If none, must state.
4. Maximum time period funds can be held before pool commences trading? If none, must state.
5. Where funds will be deposited prior to the commencement of trading and who will receive interest earned on these funds?

I. PAST PERFORMANCE OF POOL/POOL OPERATOR

1. If the subject pool has not begun trading,
  - a. Has the CPO disclosed this fact prominently in the same manner as outlined in Section 4.21(a)(4)(i)(C)?
  - b. Has the actual performance of each pool operated by the CPO and its principals for the past three years been disclosed?
  - c. If CPO and principals have not operated any other pools, is the statement required by Section 4.21(a)(4)(i)(C) included?
2. If the subject pool has traded for less than one year,
  - a. Has the actual performance for this pool been disclosed?
  - b. Has the actual performance of each pool operated by the CPO and its principals for the past three years been disclosed?
  - c. If CPO and principals have not operated any other pools, is the statement required by Section 4.21(a)(4)(i)(B) included?
3. If the subject pool has traded for one year or more, has the actual performance, for at least the past three years, of this pool been disclosed?
4. Is actual performance displayed at least quarterly in a table containing the following information current as of a date not more than three months preceding the date of the Disclosure Document:
  - a. Beginning Net Asset Value?
  - b. Additions?
  - c. Withdrawals?
  - d. Net performance?
  - e. Ending Net Asset Value?
  - f. Rate of return (net performance/beginning NAV)?
  - g. # of outstanding units?
5. If actual performance of all pools is shown on a composite basis, is individual performance also detailed for the subject pool?
6. If composite is presented, are material differences of the pools described?

7. Does the document describe how the composite was developed?
8. Is the past performance of all other pools operated by the pool operator and directed by the pool's advisor presented in a composite separate and apart from any other composite?
9. If past trading profits are presented, is statement prescribed by NFA Rule 2-29(b)(5) also included?
10. If hypothetical performance results are presented, is the statement prescribed by CFTC Regulation Section 4.41(b)(1) also included?

J. PAST PERFORMANCE OF CTA

1. If subject pool has not commenced trading and the CTA has not previously advised any accounts, does Disclosure Document contain a statement relating these facts as described in Section 4.21(a)(5)(i)?
2. Are actual performance results of the CTA and principals for the past three years disclosed for all accounts other than subject pool?
3. Are actual performance results of the CTA displayed in table format at least quarterly and current as of date not more than three months preceding the date of the document?
4. If actual performance is displayed on a composite basis, does document describe how composite was developed?
5. If composite is presented, are material differences in the accounts described?
6. If past trading profits are presented, is statement prescribed by NFA Rule 2-29(b)(5) also included?
7. If hypothetical performance results are presented, is the statement prescribed by CFTC Regulation Section 4.41(b)(1) also included?

K. MARGINS

Does the Disclosure state the following pertaining to margins:

1. How margins will be met?

2. If margin is met with non-cash items,
  - a. Nature of items?
  - b. Who will receive interest?
3. The form in which funds not deposited as margin or paid as premiums will be held after the commencement of trading. If funds will be held in assets other than cash, the CPO must disclose:
  - a. Nature of items?
  - b. Who will receive interest?
4. If margin is held outside U.S., does Disclosure Document specify where?

L. EXPENSES OF POOL

1. Does the Disclosure Document or audited annual report promoted with the Disclosure Document contain the actual amount of each expense of the pool for the preceding year, including:
  - a. Organizational costs?
  - b. Management fees?
  - c. Trading advisory fees?
  - d. Brokerage commissions?
  - e. Legal fees?
  - f. Accounting fees?
2. Does the Disclosure Document outline estimated dollar amounts for each expense for the current fiscal year, including:
  - a. Organizational costs?
  - b. Management fees?
  - c. Trading advisory fees?
  - d. Brokerage commissions?
  - e. Legal fees?
  - f. Accounting fees?
3. If base amounts are used in determining expenses, are these amounts defined?
4. If a fee is based on an increase in value of the pool, is the following disclosed:
  - a. How increase is calculated?
  - b. Time period used for the calculations?
  - c. Fee to be charged at the end of the time period?
  - d. Value of pool when payment of fees begins?

5. If any expense of the pool is paid by a person other than pool, is the following disclosed:
  - a. Nature of expense?
  - b. Amount?
  - c. Who paid or will pay expense?
6. If any commission or other fee will be or is paid directly or indirectly by the pool, CPO, CTA, or principals thereof, to any person in connection with solicitation of assets, is this disclosed?

M. POLICIES AND REPORTING

1. In relation to distribution of profits and capital, does the Disclosure Document outline the following:
    - a. Policies/procedures?
    - b. Frequency?
    - c. Income tax effects of such distributions and tax objectives of the pool?
  2. Does the Disclosure Document state the CPO will provide participants with monthly or quarterly statements and annual audited report?
  3. Are restrictions or transferability of participants' interest disclosed? If none, must state.
  4. Does the Disclosure Document describe procedures for redemption of participants' interests:
    - a. Calculation of redemption value?
    - b. Costs involved in redemption?
    - c. Restrictions on redemption? If none, must state.
- N. Does your Disclosure Document include all other material information not specifically mentioned in the regulations?
- O. Does your firm have a method to review the Federal Register for Commodity Futures Trading Commission advisories and rule changes which may affect your operations?
- P. If uncertain about background and/or disciplinary history of any FCM, IB, CPO or CTA which should be disclosed in this document has your firm contacted NFA to verify and/or obtain information?

## CTA SELF EXAMINATION QUESTIONNAIRE

### Instructions

NFA Compliance Rule 2-9 requires Members to diligently supervise the futures related activities of their agents and employees. To help Members to carry out their supervisory responsibilities, NFA has devised a questionnaire for each category of registrant, for branch office operations and for promotional material. The questionnaires focus on areas such as customer order flow, account documentation, and sales procedures. Completion of the questionnaire will provide a checklist for each Member to ensure that no major area of supervisory responsibility is being overlooked. NFA's Board of Directors has issued an interpretative notice requiring each Member to review and retain the "self-audit" questionnaires which will be provided periodically by NFA.

Questionnaires should be reviewed and signed by the appropriate supervisory personnel in either the home or branch office, who must then certify that they have reviewed the firm's operations in light of the matters covered by the questionnaire. Completed questionnaires should not be forwarded to NFA but should be retained in both the branch and home offices. Guaranteed IBs should provide and guarantor FCMs should obtain copies of the signed questionnaires. Signed questionnaires should be readily available for the last two years and retained for the last five.

If you have questions, please contact the NFA Compliance Department at 1-800-621-3570 (Out of State) and 1-800-572-9400 (Inside Illinois).

### General

1. Does your firm insure that all individuals which have the following authority or ownership are listed as principals on the firm's Form 7R?
  - a. Any person including, but not limited to, a sole proprietor, general partner, officer, director, or person occupying a similar status or performing similar functions, having the power, directly or indirectly, through agreement or otherwise, to exercise a controlling influence over the firms' activities which are subject to regulation by the CFTC.
  - b. Any holder or beneficial owner of ten percent or more of the outstanding shares of any class of stock.

- c. Any person who has contributed ten percent or more of the capital.
2. Does your firm ensure that all individuals which are responsible for supervising APs are registered as APs?
3. Do your branches hold themselves out in the name of the firm?
4. If your firm is a one person office, do you inform customers when you will be unavailable to service your customer accounts (i.e., vacations) and who they should contact in your absence?
5. Does your firm have procedures to insure that checks are received in the name to margin, guarantee or secure commodity trading?
6. Does your firm have procedures to review all firms which you are doing business with to insure those which are required to be registered are registered?

**Disclosure Document**

1. Does your firm file two copies to the CFTC and one copy to NFA of your disclosure documents and any amendments at least 21 calendar days prior to the date you first intend to solicit customers with the document?
2. Does your firm file amendments or a new disclosure document when the existing document becomes materially incomplete or inaccurate?
3. Does your firm provide prospective clients with a disclosure document, including any existing amendments, which is six months old or less prior to soliciting, directing or guiding a clients account?
4. Does your firm provide existing participants with all amendments to the disclosure document?
5. If disclosure document deficiency letters are received by the CFTC or NFA, does your firm promptly correct your document and submit your corrections to both organizations?
6. Has your firm reviewed its disclosure document to ensure its complies with CFTC Regulation 4.31 and NFA Compliance Rule 2-13? (See checklist guide attached.)



## Records

1. Does your firm require a partner, officer, director, branch office manager or supervisory employee to approve customer accounts and document this review?
2. Does your firm have procedures to ensure adequate risk disclosure is provided to customers, other than partnerships, corporations, and floor traders, prior to opening an account?
3. Does your firm provide training to the individuals which are responsible for assessing and providing risk disclosure to customers as required by NFA Compliance Rule 2-30?
4. Has your firm designated a supervisory individual to review the actions of the individuals providing risk disclosure to customers as required by NFA Compliance Rule 2-30?
5. If a predispute agreement is included in the customer account documentation, does your firm provide customers with a list of three forums, one of which is NFA arbitration, in the event the customer gives notice of its intent to file a claim?
6. Does your firm maintain the following documents or information for all clients for five years:
  - a. Client's name?
  - b. Client's address?
  - c. Client's occupation or business description?
  - d. Client's estimated annual income?
  - e. Client's estimated net worth?
  - f. Client's approximate age?
  - g. Client's prior investment and futures trading experience?
  - h. Signed and dated acknowledgement of receipt of the disclosure document which was prior to the initial deposit and no more than 6 months after the date of the disclosure document?
  - i. Signed and dated Power of Attorney or trading authorization?
  - j. Acknowledgement of receipt of the Foreign futures and options disclosure statement?
  - k. Daily and monthly activity statements from the carrying broker, or if not received, a listing of all transactions effecting each clients' account?
7. If one of your clients refuses to provide the information in 6. a-g, does your firm document that fact?

8. Does your firm have procedures to file with the CFTC a Statement of Reporting Trader in the event your firm holds or controls reportable positions (CFTC Form 40)?
9. If your firm or principals have trading accounts, does your firm maintain copies of the statements received from the carrying broker?

**Customer Complaints, Sales Practices & Promotional Material**

1. Does your firm have a designated "compliance officer" who is responsible for handling customer complaints or inquiries of a compliance nature?
2. Does your firm have policies and procedures in effect to handle customer complaints and inquiries?
3. Does your firm maintain a compliance procedures manual or other written documentation which outlines the firm's policy with respect to handling compliance matters, such as customer complaints and/or inquiries?
4. Does your firm have a systematic method of recording, investigating and responding to customer complaints and/or inquiries?
5. Does your firm require your branches to forward complaints to the home office?
6. Does your firm have an Internal Audit Department or other designated individual which monitors branches ("Auditor")?
7. Does the Auditor report to a partner or officer?
8. Does the Auditor have responsibility for conducting on-site inspections of branch offices?
9. Are the on-site inspections performed regularly?
10. Does the Auditor utilize an audit program when conducting on-site inspections?
11. Does your firm ensure that appropriate corrective action has been taken in the event the Auditor finds problems at a branch?
12. Is the Auditor familiar with NFA Notice 1-90-14 regarding Branch Office On-site Visits?
13. Does your firm have policies and procedures regarding the hiring and supervision of APs who have been or whose past employers have been expelled or revoked by NFA or the CFTC for fraud?

14. Does your firm have procedures in effect to distribute changes in rules or regulatory agencies to appropriate personnel?
15. Does your firm utilize any of the following methods to supervise sales solicitation, direct listening, reviewing taped solicitations, silent phone monitoring and customer contact?
16. Does your firm provide its APs with training on the futures and options markets?
17. Does your firm provide sales solicitation training to APs?
18. Does your firm have procedures to monitor incoming and outgoing mail to insure that customer complaints, etc. would be intercepted?
19. Does your firm have written procedures to supervise the preparation and use of promotional material?
20. Does your firm require an officer, general partner, sole proprietor, branch office manager or other supervisory employee other than the individual who prepared such material to approve promotional material before use?
21. Does your firm require the review and approval of promotional material to be in writing?
22. Does your firm maintain all promotional materials for a period of five years from the date last used?
23. Is the content of your firms' promotional material in compliance with NFA Compliance Rule 2-29? (See attached promotional material checklist.)

**Fees**

1. Does your firm calculate fees in accordance with the disclosure document?
2. If your firm collects fees from clients directly instead of from the carrying broker, does your firm reflect the amount in the performance record as an addition and as a debit to net performance?

**Block Orders**

1. Does your firm utilize a system to allocate split fills in a systematic and non-preferential manner?

2. If your carrying broker allocates split fills, are you aware of the method utilized and is it systematic and non-preferential?
3. Are your block order procedures in writing?
4. Does your firm provide the carrying broker with the account numbers to receive the fill at the time a trade is placed?

**ATTESTATION**

Appropriate supervisory personnel for \_\_\_\_\_  
(Member Firm)  
have reviewed and evaluated \_\_\_\_\_ current  
(Member's)  
procedures in light of the factors enumerated above. Based on  
that review, \_\_\_\_\_  
(Member Firm)  
believes that its current procedures are adequate to meet its  
supervisory responsibilities.

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Date

\_\_\_\_\_  
Title

cta

COMMODITY TRADING ADVISOR  
DISCLOSURE DOCUMENT CHECKLIST

Date \_\_\_\_\_

CTA \_\_\_\_\_

D.D. DATE \_\_\_\_\_

1. Does the Disclosure Document include the following:
  - A. A date.
  - B. The Cautionary Statement from 4.31(a)(9) on the cover in capital letters and boldface type.
  - C. If up front fees are charged:
    - (i) Is the table, described in the Guideline for Disclosure of Up Front Fees, on the cover? (effective July 1, 1986)
    - (ii) Is the table complete and accurate? (If CTA does not require a standard initial investment the table must highlight up front fees and expenses proportionately as \$1,000 units.)
  - D. The Risk Disclosure Statement from 4.31(a)(8)(i) on the first page, including as the last paragraph the statement from 4.31(a)(8)(ii) if the CTA is not an FCM in capital letters and boldface type.
  - E. If the CTA will trade foreign futures and options, is the disclosure statement required by 30.6 included and in boldface type? If not, ensure that the disclosure is given to clients.
  - F. Name, address, and telephone number of the CTA. (If address is a P.O. Box, location of records.)
  - G. Form of organization of the CTA.
  - H. The name of each principal of the CTA.
  - I. A description of the trading program.

- J. Types of commodity interests CTA intends to trade with a description of any restrictions or limitations on such trading established by the CTA.
- K. The name of the FCM with which the client will be required to maintain its account or, if the client is free to choose the FCM, the CTA must make such a statement.
- L. The name of the introducing broker or, if the client is free to choose the IB, the CTA must make a statement to that effect.
- M. The business background for five years, including name, main business, and nature of duties for:
  - a. CTA
  - b. Each principal of the CTA
- N. Actual performance for three years preceding the date of the Disclosure Document of all accounts directed by the CTA and each of its principals or the statement from CFTC Regulation 4.31(a)(3)(i) if accounts had not previously been directed.
  - (i) Presentation of actual performance must be displayed in a table showing at least quarterly information current as of a date not more than three months preceding the date of the Disclosure Document. The table should include:
    - a. Beginning Net Asset Value
    - b. All additions during the period
    - c. All withdrawals and redemptions during the period
    - d. The net performance for the period
    - e. The ending NAV for the period
    - f. The rate of return for the period, which shall be net performance/beginning Net Asset Value.
- O. A description of material differences among accounts and, if performance is presented on a composite basis, a description of how the composite was developed.
- P. The statement prescribed by NFA Rule 2-29(b)(5), if past trading profits are presented.
- Q. The statement prescribed by CFTC Regulation 4.41(b)(1), if hypothetical performance results are presented.

- R. A complete description of each fee, including the dollar amount, if possible. The description should include:
- (i) A definition of any term used to calculate the fee.
  - (ii) If the fee is based on an increase in the value of the account, how the increase is calculated, the period of time during which the increase is calculated, the fee charged at the end of the period, and the value of the account at which payment of the fee commences.
- S. A description of any actual or potential conflicts of interest or statement that there is no such conflict, for each of the following (any arrangement whereby the CTA or principal would benefit from the maintenance of clients' accounts with an FCM/IB should be disclosed):
- (i) CTA
  - (ii) Principals of the CTA
  - (iii) FCM
  - (iv) Principals of the FCM
  - (v) IB
  - (vi) Principals of the IB
- T. A statement whether or not the CTA or its principals will be trading for its own account and a statement whether clients will be able to inspect records of such trades.
- U. If firm includes trades for its principals, APs, and/or proprietary account in block orders, is this potential conflict of interest disclosed?
- V. Any material, administrative, civil, or criminal action within five years of the date of the Disclosure Document or a statement that there was no such action against each of the following:
- (i) CTA
  - (ii) Principals of the CTA
  - (iii) FCM
  - (iv) Principals of the FCM
  - (v) IB
  - (vi) Principals of the IB
2. Is the document paginated and fastened in a secure manner?
3. Does your Disclosure Document include all other material information not specifically mentioned in the regulations?

4. Does your firm have a method to review the Federal Register for Commodity Futures Trading Commission advisories and rule changes which may affect your operations?
5. If uncertain about background and/or disciplinary history of any FCM, IB, CPO or CTA which should be disclosed in this document, has your firm contacted NFA to verify and/or obtain information?

cta.lst



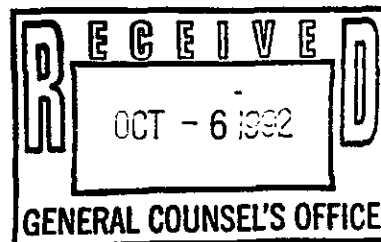
UNITED STATES OF AMERICA  
**COMMODITY FUTURES TRADING COMMISSION**

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



October 6, 1992

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



Re: Proposed amendments to Compliance  
Rule 2-26 and Financial  
Requirements Sections 1, 6, 9, 10  
and 11; and two proposed  
Interpretive Notices under  
Compliance Rule 2-9

Dear Mr. Roth:

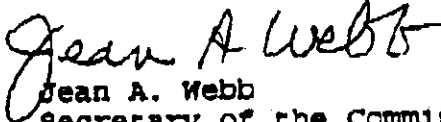
By letters dated June 11, 1991, February 7 and August 19, 1992, the National Futures Association ("NFA") submitted the captioned rule proposals pursuant to section 17(j) of the Commodity Exchange Act ("Act") for Commission approval. The proposed changes to Compliance Rule 2-26 and Financial Requirements Sections 1, 6, 9, 10, and 11 would increase the minimum net capital required of independent (i.e., non-guaranteed) introducing brokers ("IBs") and futures commission merchants. One of the new interpretive notices under Compliance Rule 2-9 would establish minimum standards for effective supervision by members of branch offices and guaranteed IBs. The other interpretive notice would require members to review and retain self-audit questionnaires to be distributed each year by NFA's Compliance Department. NFA consented to an extension of time until October 6, 1992, for the Commission to complete its review of these proposals.

The Commission notes that NFA cooperated with the Commission during the review process by responding to questions and concerns regarding the potential impact of the proposals on competition. In that regard, the Commission believes that the competitive implications of future NFA rule proposals should be taken into account prior to submission to the Commission under section 17(j).

Daniel J. Roth, Esq.  
Page 2

The Commission understands that the minimum capital changes would take effect at the end of calendar year 1992, and the self-audit and supervision matters would be implemented upon Commission approval. Please be advised that the Commission has approved these proposals.

Yours truly,



Jean A. Webb  
Secretary of the Commission



**COMMODITY FUTURES TRADING COMMISSION**

2033 K Street, NW, Washington, DC 20581

(202) 254 - 8955

(202) 254 - 8010 Facsimile

September 30, 1992

**DIVISION OF  
TRADING AND MARKETS**

Daniel J. Roth, Esq.  
General Counsel  
National Futures Association  
200 West Madison Street  
Chicago, Illinois 60606

Re: The National Futures Association's Proposed New  
Compliance Rule 2-7 and Proposed Amendments to  
Compliance Rule 3-12 and Registration Rule 501

Dear Mr. Roth:

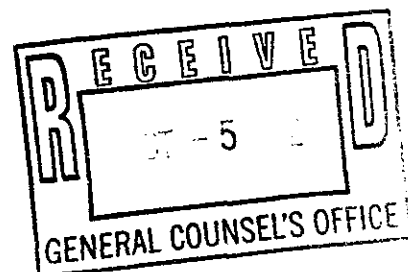
By letter dated February 7, 1992 and received on February 12, 1991, the National Futures Association ("NFA") submitted to the Commission, pursuant to Section 17(j) of the Commodity Exchange Act ("Act"), a proposed new Compliance Rule 2-7 and proposed amendments to Compliance Rule 3-12 and Registration Rule 501.

The Commission understands that NFA intends to implement the proposed amendment upon receipt of notice of Commission approval. Please be advised that on this date the Commission has approved the above-referenced proposed new rule and rule amendments under Section 17(j) of the Act.

Very truly yours,

*Jean A. Webb*

Jean A. Webb  
Secretary of the Commission



August 19, 1992

David Van Wagner, Esq.  
Commodity Futures Trading Commission  
Division of Trading and Markets  
2033 K Street, N.W.  
Washington, D.C. 20581

Re: Proposed Interpretive Notices to Compliance Rule 2-9  
Regarding a Member Self-Audit Requirement and the  
Supervision of Branch Offices and Guaranteed IBs

Dear Mr. Van Wagner:

By letters dated June 11, 1991 and February 7, 1992 (revisions to the Interpretive Notice Regarding Member Self-Audit Requirement), National Futures Association ("NFA") submitted the above-noted proposed Interpretive Notices to the Commodity Futures Trading Commission ("Commission") for review and approval pursuant to Section 17(j) of the Commodity Exchange Act. Copies of the proposed self-examination questionnaires were included for the Commission's information.

With respect to the self-audit questionnaire, it was never NFA's intention to require that all Members incorporate all of the points covered by the questionnaire into their own supervisory procedures. To the contrary, NFA has always maintained that Members may tailor their supervisory procedures to their own specific needs and the questionnaire was designed to help Members in that process. At the request of Commission staff, NFA has revised the instructions to each self-examination questionnaire to clarify that it is not intended to serve as "one size -- fits all" set of supervisory procedures. Copies of the cover memo and the instruction section of the self-examination questionnaires are enclosed for your review.

NFA also recognized the importance of providing Members with flexibility in designing their supervisory procedures in developing its "Interpretive Notice Regarding Supervision of Branch Office and Guaranteed IBs." In that Interpretive Notice NFA specifically stated:

NFA recognizes that, given the differences in the size of and complexity of the operation of NFA Members, there must be some degree of flexibility in determining what constitutes



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David Van Wagner, Esq.

August 19, 1992

diligent supervision for each firm. It is NFA's policy to leave the exact form of supervision to the Member thereby providing the Member with flexibility to design procedures that are tailored to the Member's own situation.

If I can be of further assistance, please do not hesitate to contact me.

Sincerely,

A handwritten signature in cursive script, appearing to read 'Daniel J. Roth'.

Daniel J. Roth  
General Counsel

DJR:cmc(1trs-inter.caw)  
Enclosure



August 19, 1992

Memo To: All Members  
From: Compliance Department  
Re: Self Audit Questionnaires

Enclosed please find a copy of NFA's self-examination questionnaire which should be reviewed by the appropriate supervisory personnel in your firm. An Interpretative Notice to NFA Compliance Rule 2-9 requires all Members to review the self-examination questionnaire and to evaluate their operations based on the questionnaire on an annual basis. A copy of the Interpretive Notice is attached.

NFA recognizes, of course, that there are significant differences in Members' operations and supervisory procedures. Given these differences, it is NFA's policy to give Members the flexibility to design supervisory procedures that are tailored to each Member's own situation. The questionnaire is designed to assist you in the process of developing adequate procedures.

If you have any questions regarding the questionnaire, please contact the Compliance Department at 1-800-621-3570.

CAW:cmc(memo-quest.caw)

## FCM SELF-EXAMINATION QUESTIONNAIRE

### Instructions

NFA Compliance Rule 2-9 requires Members to diligently supervise the futures related activities of their agents and employees. To help Members carry out their supervisory responsibilities, NFA has devised a questionnaire for each category of registrant, for branch office operations and for promotional material. The questionnaires focus on areas such as customer order flow, account documentation, and sales procedures. Completion of the questionnaire will provide a checklist for each Member to ensure that no major area of supervisory responsibility is being overlooked. NFA recognizes, of course, that given the differences in the size and complexity of the operations of NFA Members, the attached questionnaires will not be fully applicable to every Member. Furthermore, it has always been NFA's policy to give Members the flexibility to design supervisory procedures that are tailored to a Member's own situation. These questionnaires are being provided to Members to assist in the process of developing these procedures.

CAW:cmc(misc-audit.caw)