

September 10, 1993

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

Re: National Futures Association: Proposed Amendments to NFA Bylaws 702, 704, 707 and 708; Part 3 of NFA Compliance Rules; NFA Code of Arbitration, Sections 1, 2, 4, 5, 6, 8, 9, 10, 11, 12, 16 and 18; NFA Member Arbitration Rules, Sections 1, 2, 3, 4, 5, 7, 8, 9, 10, 11, 12 and 16; and Proposed Deletion of NFA Compliance Rule 2-28

Dear Ms. Webb:

Pursuant to Section 17(j) of the Commodity Exchange Act, as amended, National Futures Association ("NFA") hereby submits to the Commodity Futures Trading Commission ("Commission") proposed amendments to the above-referenced NFA Bylaws, Compliance Rules, Code of Arbitration and Member Arbitration Rules. These amendments were approved by NFA's Board of Directors ("Board") at its meeting on August 19, 1993. NFA respectfully requests Commission review and approval of the amendments.

I. PROPOSED AMENDMENTS

- A. Proposed amendments to NFA Bylaws 702, 704, 707 and 708 and Part 3 of NFA Compliance Rules (additions are underscored and deletions are bracketed):

BYLAWS  
OF  
NATIONAL FUTURES ASSOCIATION

\* \* \*

CHAPTER 7

COMMITTEES

\* \* \*

**Bylaw 702. Appeals Committee.**

There shall be an Appeals Committee, consisting of nine (9) Directors, at least one of whom shall be a Public Director. A majority of the Committee members eligible to par-



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ticipate in a proceeding shall constitute a quorum. The Committee members shall be proposed by the President and appointed by the Board. The President and the Board shall [endeavor to] propose and appoint Directors who reflect the various categories of Members described in the Articles. The Committee shall hear and decide appeals from and reviews of decisions in disciplinary cases by any Regional Business Conduct Committee under the Compliance Rules. Each Committee member shall serve for three (3) years, except for the initial Committee members, whose terms shall be staggered, or until the member's successor is appointed and qualified, or until the member's death, resignation, ineligibility or removal. A Committee vacancy shall be filled in the manner prescribed in Bylaw 601 for officers. A Committee member may be removed by the Board whenever in its judgment the best interests of NFA will be served thereby.

\* \* \*

**Bylaw 704. [Regional] Business Conduct Committee[s].**

There shall be [three Regional] a Business Conduct Committee[s (hereinafter "Regional Committees"), one for each NFA Region (see Article V). Each Regional Committee shall consist], consisting of nine (9) individuals who shall be Members, persons connected therewith or members of the public [Members or persons connected therewith residing in that Region]. A majority of the [Regional] Business Conduct Committee members eligible to participate in a proceeding shall constitute a quorum, except that in cases in which a Panel has been appointed (see Compliance Rule [3-6] 3-11) a quorum shall consist of a majority of such Panel members but no fewer than three[, including at least one member of the Regional Committee]. The members of [each Regional] the Business Conduct Committee shall be proposed by the President and appointed by the Board. The President and the Board shall [endeavor to] propose and appoint individuals who reflect the various categories of NFA Members and NFA Regions (see Article V) and members of the public. At least one member of the Business Conduct Committee shall not be an NFA Member or Associate. Each member of [a Regional] the Business Conduct Committee shall serve for three (3) years, except for members of the initial [Regional] Business Conduct Committee[s], whose terms shall be staggered, or until the member's [successor is appointed and qualified, or until



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the member's] death, resignation, ineligibility or removal. A vacancy in [a Regional] the Business Conduct Committee shall be filled in the manner prescribed in Bylaw 601 for officers. A Business Conduct Committee member may be removed by the Board whenever in its judgment the best interests of NFA will be served thereby. [Each Regional Committee or its designated subcommittee shall have jurisdiction over those compliance matters arising in its Region, including the issuance of warning letters. A matter shall be deemed to arise where the NFA Member or Associate that is the subject of the inquiry resides (see Article XVIII). If a matter arises in two or more Regions, the President shall assign the matter to the Regional Committee the President deems most appropriate to consider the matter.] No Business Conduct Committee member shall use or disclose material, non-public information, obtained as a result of participation on the Business Conduct Committee, for any purpose other than the performance of official duties as a member of the Business Conduct Committee.

\* \* \*

**Bylaw 707. Hearing Committee.**

There shall be a Hearing Committee, consisting of at least fifteen (15) individuals who shall be Members, persons connected therewith or members of the public. A majority of the Hearing Committee members eligible to participate in a proceeding shall constitute a quorum, except that in cases in which a Panel has been appointed (see Compliance Rule 3-7) a quorum shall consist of a majority of such Panel members but no fewer than three. The members of the Hearing Committee shall be proposed by the President and appointed by the Board. The President and the Board shall propose and appoint individuals who reflect the various categories of NFA Members and NFA Regions (see Article V) and members of the public. At least one member of the Hearing Committee shall not be an NFA Member or Associate. Each member of the Hearing Committee shall serve for three (3) years, except for members of the initial Hearing Committee, whose terms shall be staggered, or until the member's death, resignation, ineligibility or removal. A vacancy in the Hearing Committee shall be filled in the manner prescribed in Bylaw 601 for officers. A Hearing Committee member may be removed by the Board whenever in its judgment the best interests of



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NFA will be served thereby. No Hearing Committee member shall use or disclose material, non-public information, obtained as a result of participation on the Hearing Committee, for any purpose other than the performance of official duties as a member of the Hearing Committee.

**Bylaw [707] 708. Qualifications of Members of [Regional] Business Conduct and Hearing Committees.**

[(a)] No individual shall be eligible to serve as a member of [a Regional] the Business Conduct Committee or the Hearing Committee if such person:

- [(i)] (a) is subject to any of the disqualifications set forth in CFTC Regulation 1.63(b);
- [(ii)] (b) has been convicted of a felony within the prior ten years; or
- [(iii)] (c) is subject to a Member Responsibility Action or Associate Responsibility Action which is currently in effect.

**COMPLIANCE RULES**

\* \* \*

**Part 3 - COMPLIANCE PROCEDURES.**

**Rule 3-2. INVESTIGATION.**

**(a) Initiation; Report.**

In each case in which the Compliance Director has reason to believe that any NFA requirement is being, has been or is about to be violated, the Compliance Director shall submit a written report of the matter to the [appropriate Regional] Business Conduct Committee. (See NFA Bylaw 704.) The report shall include -

- (i) the reason the investigation was begun;



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- (ii) a summary of the complaint, if the investigation was begun as the result of a complaint;
- (iii) the relevant facts; and
- (iv) the Compliance Director's conclusion whether the [Regional] Business Conduct Committee should proceed with the matter.

**(b) Termination.**

If upon completing the investigation the Compliance Director concludes that there is no reason to believe that an NFA requirement is being, has been or is about to be violated, the Compliance Director shall submit a report to the [Regional] Business Conduct Committee, containing the information specified in paragraph (a) above and, if applicable, recommending whether the [Regional] Business Conduct Committee should issue or authorize the Compliance Director to issue a warning letter. The report, and any warning letter issued, shall become part of the investigation file, which may thereafter be closed as the Compliance Director deems appropriate. Investigations shall be completed within four months of commencement except for good cause.

**(c) Review of Report.**

Each investigation report shall be reviewed by the [Regional] Business Conduct Committee. If, upon review of the report, the Business Conduct Committee finds that additional investigation or evidence is necessary, it shall so instruct the Compliance Director. Within thirty (30) days after receiving a completed report the [Regional] Business Conduct Committee shall either -

- (i) close the matter, if it finds (A) no reasonable basis that a violation has occurred, is occurring or is about to occur; or (B) that prosecution is otherwise unwarranted (in which case the [Regional] Business Conduct Committee may issue or cause to be issued a warning letter). The closure order shall be in writing and briefly state the reasons therefor, and a copy of the order shall be promptly furnished to the President. Such order shall become final ten (10) days after the Presi-



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dent's receipt thereof unless, within such time, the President refers the matter to the Appeals Committee (see NFA Bylaw 702) for its review. In such case, the closure order shall become final thirty (30) days after the date of referral by the President unless, within such time, the Appeals Committee directs the [Regional] Business Conduct Committee to issue a complaint; or

- (ii) serve a written and dated complaint, if it finds reason to believe that an NFA requirement is being, has been or is about to be violated and that the matter should be adjudicated.

No member of the Business Conduct Committee or its designated Panel shall participate in the matter if the member, or any person with which the member is connected, has a financial, personal or other direct interest in the matter under consideration.

**Rule 3-3. SERVICE.**

For purposes of any proceeding brought under Part 3 of these Rules -

- (a) service of a Complaint will be sufficient if mailed to the person charged ("the Respondent") by first class and overnight mail, to the last address provided by the Respondent on record with NFA, or the address of his duly authorized agent for service;
- (b) one copy of all pleadings, motions and briefs filed with NFA subsequent to the Complaint shall be served by the party upon all parties not in default (including the attorney of record in NFA's General Counsel's office), unless otherwise provided. Service on a party's representative shall be service on the party. Service shall be made either by personal service (effective upon delivery) or mail (effective upon deposit). Proof of service of a document shall be made by attaching thereto an affidavit or certificate of service. To mail means to deposit in the U.S. Mail.



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first-class postage prepaid, or with an overnight delivery service, delivery fee prepaid; and

- (c) documents filed with NFA under this Part must be delivered or mailed to:

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

Filing is effective upon receipt.

[Rule 3-3. COMPLAINT.] Rule 3-4. NOTICE OF CHARGES.

- (a) A Complaint issued by the [Regional] Business Conduct Committee under these Rules must -

[(a)] (i) state each NFA requirement alleged to be, to have been or about to be violated; and

[(b)] (ii) state each act or omission that constitutes, constituted or will constitute the alleged violation[;].

- (b) NFA shall advise the Respondent in writing regarding the --

(i) Answer --

(a) that the Respondent must file a written Answer to the Complaint with NFA, within ten (10) business days of the date of the Complaint, unless the Complaint states otherwise;

(b) that failure to file an Answer as provided in Part (i) (a) above shall be deemed an admission of the facts and legal conclusions contained in the Complaint;

(c) that failure to respond to any allegation shall be deemed an admission of that allegation; and



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(d) that failure to file an Answer as provided in Part (i) (a) above shall be deemed a waiver of hearing.

(ii) Hearing --

(a) that the Respondent must file a written Request for Hearing with NFA, within ten (10) business days of the date of the Complaint, unless the Complaint states otherwise;

(b) that the requirement that a hearing be requested in writing may be satisfied by the Respondent completing and filing with NFA the Request for Hearing form, which shall be provided to each Respondent with the Complaint;

(c) that failure to request a hearing as provided in Part (ii) (a) above, unless good cause is shown, shall be deemed a waiver of hearing;

(d) that if the Respondent waives his right to a hearing, the Compliance Department may proceed to submit testimonial or documentary evidence to the Hearing Committee (see Bylaw 707) or its designated Panel without further notice to the Respondent; and

(e) that if the Respondent waives his right to a hearing, he has waived his right to object to the Compliance Department's evidence, cross-examine witnesses and present evidence on his own behalf.

[(c) advise the person charged ("the Respondent") --

(i) that the Respondent is entitled to file an Answer, within 10 business days of the date of the Complaint unless the Complaint specifies otherwise, and to a hearing if the Respondent so requests in its Answer; and



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(ii) of the consequences of a failure to --

- (A) file an Answer,
- (B) respond in the Answer to each charge (See Rule 3-5), or
- (C) request a hearing in the Answer (See Rule 3-6).]

**Rule [3-4] 3-5. RIGHT TO COUNSEL.**

The Respondent may be represented by an attorney-at-law or other person at any stage of the investigation or disciplinary proceeding except as provided in Rule [3-12] 3-15(b)(iii), but the [Regional] Business Conduct Committee, the Hearing Committee or [its] a designated Panel may bar from the proceeding any representative for dilatory, disruptive or contumacious conduct.

**Rule [3-5] 3-6. ANSWER.**

The Respondent [shall submit an] must file a written Answer to the Complaint[. The Answer must be written and filed with the Regional Committee] with NFA within ten (10) business days from the date of the Complaint[, ] or such further time as the [Regional] Business Conduct Committee specifies in the Complaint. Failure to file a timely Answer shall be deemed an admission of the facts and legal conclusions contained in the Complaint, and a waiver of hearing. The Answer shall respond to each allegation in the Complaint by admitting, denying or averring that the Respondent lacks sufficient knowledge or information to admit or deny the allegation. An averment of insufficient knowledge or information may be made only after a diligent effort has been made to ascertain the relevant facts, and shall be deemed to be a denial of the pertinent allegation. The failure to [expressly] respond to any allegation shall be deemed an admission of that allegation. For good cause shown, the [Regional] Business Conduct Committee, the Hearing Committee or a designated Panel may waive the effects of failure to file a timely or complete Answer, or may grant an extension of time in which to comply with this Rule.



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**[Rule 3-6. HEARING.]**

The Respondent shall be afforded a hearing on the charges, if the Respondent so requests in the Answer, before the Regional Committee or its designated Panel consisting of no fewer than three individuals, at least one of whom shall be a member of the Regional Committee. Each individual on such Panel shall be appointed by a majority of the Regional Committee. The hearing shall be held at such location as the Regional Committee or its designated Panel shall determine. The hearing shall be held as soon as practicable after the request is received. The failure to request a hearing shall, unless good cause is shown, be deemed a waiver of the Respondent's right to a hearing.

If a hearing is held --

- (a) The Respondent shall be given reasonable advance notice of the hearing date and shall be entitled to reasonable pre-hearing examination of all evidence in NFA's possession or under its control that is to be relied upon by the Compliance Office or that is relevant to the Complaint;
- (b) The formal rules of evidence need not apply;
- (c) The Respondent may appear personally, examine any witness, call witnesses and present relevant testimony and other evidence; and
- (d) A substantially verbatim record of the hearing shall be made (i.e., one that can be accurately transcribed). The cost of transcription shall be borne by the Respondent only if it requests the transcript, appeals the decision under Rule 3-10 below, or applies for Commission review and review is granted (see paragraph (e)(iii) of Rule 3-10). Otherwise, any transcription costs shall be borne by NFA.

No member of the Regional Committee or its designated Panel shall participate in the matter if the member, or any person with which the member is connected, has a financial, per-



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sonal or other direct interest in the matter under consideration.]

**Rule 3-7. REQUEST FOR HEARING.**

- (a) The Respondent must file a written Request for Hearing within ten (10) business days of the date of the Complaint, unless the Complaint states otherwise. The requirement that a hearing be requested in writing may be satisfied by the Respondent completing and filing with NFA the Request for Hearing form, which shall be provided to each Respondent with the Complaint.
- (b) The Respondent shall be afforded a hearing on the charges and possible sanctions, if the Respondent requests a hearing as provided herein. The hearing shall be before the Hearing Committee as a whole or before a designated Panel ("Hearing Panel"). Should the hearing be conducted by the Committee as a whole, the Committee and its Chairman shall have the same powers as provided under these rules as the Hearing Panel and its Chairman. A Hearing Panel shall consist of no fewer than three members of the Hearing Committee, each whom shall be appointed by the Chairman of the Hearing Committee. The hearing shall be held at such location as the Hearing Panel shall determine. The hearing shall be held as soon as practicable after the request is received.
- (c) Failure to request a hearing as provided in (a) above, unless good cause is shown, shall be deemed a waiver of hearing. If the Respondent waives his right to a hearing, the Compliance Department may proceed to submit testimonial or documentary evidence to the Hearing Panel without further notice to the Respondent. If the Respondent waives his right to a hearing, he has waived his right to object to the Compliance Department's evidence, cross-examine witnesses and present evidence on his own behalf.



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Rule 3-8. PRE-HEARING PROCEDURES.

If the Respondent requests a hearing -

- (a) The Respondent shall be given reasonable advance notice of the hearing date; and
- (b) The Respondent shall be entitled to reasonable pre-hearing examination of all evidence in the Compliance Department's possession or under its control that is to be relied upon by the Compliance Department or that is relevant to the Complaint. Such pre-hearing examination -
  - (i) must be requested by the Respondent in writing;
  - (ii) can be conducted either by the Respondent examining all such evidence at the offices of NFA, or by the Respondent requesting that all such evidence be copied and sent to him with any transportation and copying costs to be borne by the Respondent making the request;
  - (iii) will be available up until thirty (30) days prior to the scheduled hearing date, except for good cause shown; and
  - (iv) is subject to the Compliance Department's right to withhold any privileged material (including, but not limited to, the investigation report), pursuant to all common law and statutory privileges it has available to it.
- (c) At least fifteen (15) days prior to the date assigned for oral hearing, each party who will participate in that hearing, including the Compliance Department, shall file with NFA and serve on every other party who will participate in the hearing:
  - (i) the name, address and phone number of each witness they intend to call as part of their direct case; and



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(ii) copies of all documents they intend to introduce into evidence as part of their direct case.

The Hearing Panel may preclude any party to the hearing from presenting witnesses or evidence that have not been previously disclosed, except for good cause shown.

(d) The Compliance Department or any Respondent who has requested a hearing may petition the Hearing Panel to schedule a pre-hearing conference, which request shall specify the issues which the party wishes to raise in the pre-hearing conference. The request may be granted at the discretion of the Hearing Panel. Either the Hearing Panel or the Chairman may also schedule a pre-hearing conference on its own motion. Any order scheduling a pre-hearing conference shall specify the issues which may be raised in the pre-hearing conference. Such conferences may be conducted by telephone. The Hearing Panel in its sole discretion shall decide which issues may be the subject of a pre-hearing conference conducted by the Chairman acting alone.

(e) All motions, including motions for continuance, shall be filed with NFA and served on all parties not in default no later than fifteen (15) days prior to the day of hearing, except for good cause shown. The Hearing Panel in its sole discretion shall decide which motions may be decided by the Chairman acting alone.

**Rule 3-9. HEARING.**

If a hearing is held -

(a) The formal rules of evidence need not apply;

(b) Telephonic testimony shall be permitted if ordered by the Hearing Panel;



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- (c) The Respondent may appear personally, examine any witnesses, call witnesses and present relevant testimony and other evidence;
- (d) Any party to a hearing may move for an order or the Hearing Panel, on its own motion, may issue an order requiring an NFA Member, Associate, or person connected therewith to testify or produce documents at a hearing at the moving party's expense. Such an order is discretionary with the Hearing Panel and shall be issued only for good cause shown; and
- (e) A substantially verbatim record of the hearing shall be made (i.e., one that can be accurately transcribed). The cost of transcription shall be borne by the Respondent only if it requests the transcript, appeals the decision under Rule 3-13 below, or applies for Commission review and review is granted (see paragraph (e) (iii) of Rule 3-13). Otherwise, any transcription costs shall be borne by NFA.

No member of the Hearing Panel shall participate in the matter if the member, or any person with which the member is connected, has a financial, personal or other direct interest in the matter under consideration.

**Rule [3-7] 3-10. DECISION.**

After the hearing or other consideration of the matter, the [Regional Committee or its designated] Hearing Panel shall render a written decision, based upon the weight of the evidence, containing -

- (a) the charges or a summary of the charges;
- (b) the Answer, if any, or a summary of the Answer;
- (c) a brief summary of the evidence produced at the hearing, or - where appropriate - incorporation by reference of the investigation report;



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- (d) a statement of findings and conclusions as to each allegation, including a statement setting forth: each act or practice the Respondent was found to have committed or omitted, is committing or omitting, or is about to commit or omit; each NFA requirement that such act or practice violated, is violating, or is about to violate; and whether the act or practice is deemed to constitute conduct inconsistent with just and equitable principles of trade;
- (e) a declaration of any penalty imposed (see Rule [3-11] 3-14) and the penalty's effective date; and
- (f) a statement that the Respondent may appeal an adverse decision to the Appeals Committee by filing a written notice of appeal with [the] NFA [Secretary] within fifteen (15) days after the date of the decision.

The decision shall be dated and promptly furnished to the Respondent and the Appeals Committee and shall be final [5 days after the] upon expiration of time for appeal or review of the decision[, unless appealed or reviewed]. (See Rule [3-10] 3-13.)

**Rule [3-8] 3-11. SETTLEMENT.**

**(a) Offer.**

- (i) A subject of an investigation in which the investigation report has been completed, or a Respondent in a disciplinary proceeding, [may] shall submit [a] any proposed settlement of the matter to the [Regional] Business Conduct Committee [or its designated Panel (or the Appeals Committee if the matter is before it on appeal or review)] or its designated Panel ("BCC Panel") at any time up until ten (10) business days before the date of a scheduled hearing. A BCC Panel shall consist of no fewer than three members of the Business Conduct Committee, each of whom shall be appointed by the Chairman of the Business Conduct Committee. After that date, any proposed settlement offer



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shall be submitted to the Hearing Panel. Settlement offers may also be submitted to the Appeals Committee if the matter is before it on appeal or review. The [Regional] Business Conduct Committee [or its designated], the BCC Panel, Hearing Panel, or [the] Appeals Committee[, as the case may be,] may accept or reject the settlement offer as it deems appropriate. The Compliance Director shall be afforded an opportunity to express [that office's] the Compliance Department's views with respect to the proposed settlement[.];

(ii) The [Regional] Business Conduct Committee [or its designated], BCC Panel, Hearing Panel or [the] Appeals Committee may in its discretion accept an offer in which the person neither admits nor denies violating NFA requirements[.]; and

(iii) Every settlement offer -

(a) shall contain the following language:

[Respondent] acknowledges that the Compliance Department will present the settlement offer and its views on the proposed settlement orally, in writing or both;

(b) presented to the Business Conduct Committee or BCC Panel shall also contain the following language:

[Respondent] acknowledges that any settlement offer rejected by the Business Conduct Committee or BCC Panel will be forwarded to the Hearing Panel for its information in the event that [Respondent] subsequently submits a settlement offer to the Hearing Panel;

(c) presented to the Hearing Panel shall also contain the following language:

[Respondent] waives any objection to the Hearing Panel's participation in the hearing in the event that [Respondent's] settlement offer is rejected; and



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(d) presented to the Appeals Committee shall also contain the following language:

[Respondent] acknowledges that any settlement offer rejected by the Appeals Committee will be forwarded to the Business Conduct Committee, BCC Panel or Hearing Panel for its information in the event that [Respondent] subsequently submits a settlement offer to the Business Conduct Committee, BCC Panel or Hearing Panel. [Respondent] waives any objection to the Appeals Committee's participation in the review in the event that [Respondent's] settlement offer is rejected.

**(b) Decision.**

If the [Regional] Business Conduct Committee [or its designated], BCC Panel, Hearing Panel or [the] Appeals Committee accepts the offer, it shall issue a written decision specifying each NFA requirement it has reason to believe is being, has been or is about to be violated, any penalty imposed and whether the settling party has admitted or denied any violation.

A decision on settlement by the [Regional] Business Conduct Committee, BCC Panel or [its designated] Hearing Panel shall be promptly furnished [by the Regional Committee or its designated Panel] to the President. A decision on settlement by the Business Conduct Committee, BCC Panel or Hearing Panel [and] shall become final and binding [within 10] fifteen (15) days after the [President's receipt thereof] date of the decision, unless the President, with notice to all parties, refers the matter to the Appeals Committee for its review. The Appeals Committee shall approve or disapprove the settlement within thirty (30) days after the date of such referral. Its decision to approve or disapprove the settlement shall become final and binding fifteen (15) days after the date of that decision.

A decision on settlement by the Appeals Committee shall become final and binding fifteen (15) days after the date of the decision. [In such case, the decision shall become final and binding unless disapproved by the Appeals Commit-



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tee within 30 days after the date of referral by the President.]

**(c) Withdrawal.**

A settlement offer may be withdrawn before final acceptance by the [Regional] Business Conduct Committee, [or its designated] BCC Panel, Hearing Panel or [by the] Appeals Committee [if the matter is before it on review]. An offer that is withdrawn or rejected shall not be deemed to have been an admission of any matter [nor shall it otherwise prejudice the offeror].

**Rule [3-9] 3-12. NOTICE AND PUBLICATION OF DECISION.**

Written notice of any action taken under Rule [3-7] 3-10 or Rule [3-8] 3-11 that is adverse to the Respondent, including reasons, findings, and conclusions, shall be furnished to the Commission within thirty (30) days after it becomes final. [The notice of action shall be made public but shall not disclose the evidence therefor.]

**Rule [3-10] 3-13. APPEAL; REVIEW.**

**(a) Appeal.**

The Respondent may appeal any adverse decision of [a Regional Committee or its designated] the Hearing Panel issued under Rule [3-7] 3-10 to the Appeals Committee by filing a written notice of appeal with [the Secretary] NFA within fifteen (15) days after the date of the decision. The notice must describe those aspects of the disciplinary action to which exception is taken, and must contain any request by the Respondent to present written or oral argument.

**(b) Review.**

The Appeals Committee may also order review of any decision of [a Regional Committee or its designated] the Hearing Panel issued under Rule [3-7] 3-10 [on its own motion by giving]. If such a review will be conducted, the Appeals Committee will give written notice to the Respon-



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dent[, ] within fifteen (15) days of the date of the decision[, that a review will be conducted]. Such review may be conducted by the Appeals Committee -

- (i) on its own motion, or
- (ii) pursuant to a petition filed by the Compliance Department, the granting of which shall be discretionary with the Appeals Committee. The petition will state why the Compliance Department is seeking review, and must contain any request by the Compliance Department to present written or oral argument.

**(c) Stay.**

The Respondent's filing of a notice of appeal under paragraph (a) above or the institution by the Appeals Committee of [its own] review under paragraph (b) above shall operate as a stay of the effective date of the disciplinary order, until the Appeals Committee renders its decision.

**(d) Conduct of Proceeding.**

No member of the Appeals Committee shall participate in the proceeding if the member participated in any prior stage of the disciplinary proceeding (other than the review of a settlement offer submitted under Rule [3-8] 3-11) or if the member, or any person with which the member is connected, has a financial, personal or other direct interest in the matter under consideration. Except for good cause shown, the appeal or review shall be conducted solely on the record before the [Regional Committee or its designated] Hearing Panel, the written exceptions filed under paragraph (a) above, and such written or oral arguments of the parties as the Appeals Committee may authorize.

**(e) Decision.**

Promptly after reviewing the matter, the Appeals Committee shall issue a written and dated decision, based on the weight of the evidence. The decision shall include -

- (i) the findings and conclusions of the Appeals Committee as to each charge and penalty reviewed,



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including the specific NFA requirement the Respondent was found by the [Regional Committee or its designated] Hearing Panel to have violated, to be violating, or to be about to violate;

- (ii) a declaration of any penalty imposed by the Appeals Committee, the basis for its imposition, and its effective date;
- (iii) a statement that any person aggrieved by the disciplinary action may appeal the action pursuant to Commission Regulations, Part 171, within thirty (30) days of service; and
- (iv) a statement that any person aggrieved by the disciplinary action may petition the Commission for a stay of the effective date pursuant to Commission Regulations, Part 171, within ten (10) days of service.

**(f) Finality.**

The decision of the Appeals Committee shall be final thirty (30) days after the date of service.

**Rule [3-11] 3-14. PENALTIES.**

**(a) Types of Penalties.**

The [Regional Committee or its designated] Business Conduct Committee, BCC Panel or Hearing Panel, or the Appeals Committee on appeal or review, may at the conclusion of the disciplinary proceeding impose one or more of the following penalties:

- (i) Expulsion, or suspension for a specified period, from NFA membership; a two-thirds vote of the members of the [Regional Committee or its designated] Hearing Panel or the Appeals Committee present and voting shall be required for expulsion. A suspended Member shall be liable for dues and assessments but shall have no membership rights during the suspension period nor shall a



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suspended Member hold itself out as an NFA Member during the suspension period[.]i

- (ii) Bar or suspension for a specified period from association with an NFA Member[.]i
- (iii) Censure or reprimand[.]i
- (iv) A monetary fine, not to exceed \$250,000 per violation[.]i
- (v) Order to cease and desist[, or]i and
- (vi) [a]Any other fitting penalty or remedial action not inconsistent with this rule.

**(b) Authority of Appeals Committee to Alter Penalty.**

The Appeals Committee may increase, decrease or set aside the penalties that were imposed by the [Regional Committee or its designated] Hearing Panel, or may impose other and different penalties, as it sees fit, subject to the requirements and limitations in paragraph (a) above.

**(c) Payment of Fines.**

All fines shall be paid to the NFA Treasurer within thirty (30) days of the date of the decision or within the time prescribed in the decision, and may be used for general NFA purposes. A person who fails to pay a fine on time may, after 7 days written notice, be summarily suspended from membership or association with a Member, by order of the President, until the fine is paid.

**Rule [3-12] 3-15. 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



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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.

**(b) Procedure.**

The following procedures shall be observed in actions under this Rule:

- (i) The subject of the action (the "Respondent") shall, whenever practicable, be served with a notice before the action is taken. If prior notice is not practicable, the Respondent shall be served with a notice at the earliest opportunity. This notice shall (A) state the action taken or to be taken; (B) briefly state the reasons for the action; (C) state the time and date when the action became or becomes effective and its duration; and (D) state that any person aggrieved by the action may petition the Commission for a stay of the effective date of the action pending a hearing pursuant to Commission Regulations, Part 171, within 10 days of service. Service may be made by personal delivery (effective upon receipt), by telefax (effective upon transmission), or by mail (effective upon deposit). When service is effected by mail, the time within which the person served may respond shall be increased by five days.
- (ii) The Respondent shall be given an opportunity for a hearing promptly after the summary action is taken. Any such hearing shall be conducted before [the appropriate Regional Committee (see Bylaw 704) or its designated] a Hearing Panel under the



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procedures of [paragraphs (b)-(d) of] Rule [3-6]  
3-9.

- (iii) The Respondent shall have the right to be represented by an attorney-at-law or other person in all proceedings after the summary action is taken, but the [Regional Committee or its designated] Hearing Panel may bar from the proceeding any representative for dilatory, disruptive, or contumacious conduct.
  
- (iv) Promptly after the hearing, the [Regional Committee or its designated] Hearing Panel shall issue a written and dated decision affirming, modifying or reversing the action taken, based upon the evidence contained in the record of the proceeding. A copy of the decision shall be furnished promptly to the Respondent and the Appeals Committee, and the Commission. The decision shall contain:
  - (A) A description of the action taken and the reasons for the action;
  - (B) A brief summary of the evidence received at the hearing;
  - (C) Findings and conclusions;
  - (D) A determination as to whether the summary action that was taken should be affirmed, modified or reversed; a declaration of any action to be taken against the Respondent as the result of that determination; the effective date and duration of that action; and a determination of the appropriate relief based on the findings and conclusions;
  - (E) A statement that any person aggrieved by the action may have a right to appeal the action pursuant to Commission Regulations, Part 171, within 30 days of service; and
  - (F) A statement that any person aggrieved by the action may petition to the Commission for a



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stay pursuant to Commission Regulations, Part 171, within 10 days of service.

**(c) Appeal.**

The Respondent shall have no right to appeal a final action taken under this Rule to the Appeals Committee.

**(d) Review.**

The Appeals Committee may on its own motion review a decision of the [Regional Committee or its designated] Hearing Panel issued under paragraph (b)(iv) above, by giving written notice to the Respondent of its decision to review within 15 days of the date of the decision. The review shall be conducted in accordance with paragraphs (d), (e)[(i), (e)(ii)] and (f) of Rule [3-10] 3-13.

**Rule [3-13] 3-16. RELATIONSHIP BETWEEN MEMBER OR ASSOCIATE RESPONSIBILITY ACTION AND DISCIPLINARY ACTION.**

The institution of a Member or Associate Responsibility Action (See Rule [3-12] 3-15) shall not preclude the institution, at the same or any other time, of a disciplinary action (see Rule 3-2) involving the same matters or persons, nor shall any pending or completed disciplinary action involving the same matters or persons preclude a proceeding under Rule [3-12] 3-15.

**Rule 3-17. COMPOSITION OF COMMITTEES.**

The Business Conduct Committee, Hearing Committee, Appeals Committee, Executive Committee, BCC Panel and Hearing Panel conducting a proceeding under these Part 3 rules shall include -

- (a)** at least one member who represents a membership category (see Article VI) other than the Respondent's membership category; and



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(b) at least one member who is not an NFA Member or Associate whenever the Respondent is a member of NFA's Board of Directors, the Business Conduct Committee, Hearing Committee or Appeals Committee.

- B. Proposed amendments to NFA Code of Arbitration, Sections 1, 2, 4, 5, 6, 8, 9, 10, 11, 12, 16 and 18 and NFA Member Arbitration Rules, Sections 1, 2, 3, 4, 5, 7, 8, 9, 10, 11, 12 and 16 (additions are underscored and deletions are bracketed):
- 

CODE OF ARBITRATION

\* \* \*

Section 1. Definitions

\* \* \*

(g) "Claim" -- means a Demand for Arbitration, counterclaim, cross-claim or third-party claim filed under this Code.

(h) "Cross-claim" -- means a claim filed by one Respondent against a co-Respondent.

(i) [(g)] **"Futures Commission Merchant"** -- means a futures commission merchant as that term is used in the Commodity Exchange Act, and that is required to be registered as such under the Commodity Exchange Act and Commission Rules.

(j) [(h)] **"Floor Broker"** -- means a floor broker as that term is used in the Commodity Exchange Act.

(k) [(i)] **"Futures"** -- includes:

- (1) options contracts traded on a CFTC-licensed exchange;
- (2) options contracts granted by a person that has registered with the Commission under Section 4(d) of the Act as a grantor of such option contracts or has notified the Commis-



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sion under the Commission's Rules that it is qualified to grant such option contracts;

- (3) foreign futures and foreign options transactions made or to be made on or subject to the rules of a foreign board of trade for or on behalf of foreign futures and foreign options customers as those terms are defined in the Commission's Rules; and
- (4) leverage transactions as that term is defined in the Commission's Rules.

(l) [(j)] **"Introducing Broker"** -- means an introducing broker as that term is used in the Commodity Exchange Act, and that is required to be registered as such under the Commodity Exchange Act and Commission Rules.

(m) [(k)] **"Leverage Transaction Merchant"** -- means a leverage transaction merchant as that term is used in Commission Rules, and that is required to be registered as such under the Commodity Exchange Act and Commission Rules.

(n) [(l)] **"Member"** -- means a Member of NFA or a person that was a Member at the time the acts or transactions that are the subject of the dispute occurred.

(o) [(m)] **"NFA"** -- means National Futures Association.

(p) [(n)] **"Panel"** -- means the arbitration panel appointed pursuant to Section 4(a) of the Code.

(q) [(o)] **"Person"** -- includes individuals, corporations, partnerships, trusts, associations and other entities.

(r) [(p)] **"Pleading[s]"** -- means a [includes the] Demand for Arbitration, counterclaim, cross-claim, third-party claim, [filed by a Claimant, the] Answer or [and any counterclaim filed by a Respondent, and any] Reply filed under this Code [to a counterclaim filed by a Claimant].



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- (s) [(q)] "President" -- means the President of NFA.
- (t) [(r)] "Respondent" -- means a person against whom a claim is asserted under this Code.
- (u) [(s)] "Secretary" -- means the Secretary of NFA.
- (v) "Third-party Claim" -- means a claim filed by a Respondent against a person not a party to the action.

## Section 2. Arbitrable Disputes.

\* \* \*

### (2) Counterclaims, Cross-claims and Third-party Claims.

Except as provided in Sections 5 and 6 of this Code with respect to timeliness requirements, a counterclaim, cross-claim or third-party claim may be asserted [against a customer] in an arbitration brought under this Code [paragraph (1) above] if the counterclaim, cross-claim or third-party claim [: (i)] arises out of an act or transaction that is the subject of the Demand for Arbitration [customer's claim: (ii) does not require for its adjudication the presence of witnesses or other third parties over whom NFA lacks jurisdiction and who are not otherwise available. A counterclaim that does not meet condition (i) above may be asserted against a customer only if the customer thereafter consents].

\* \* \*

## Section 4. Arbitration Panel.

### (a) Appointment of Panel.

All arbitration proceedings under this Code shall be conducted before an arbitration panel consisting of three NFA Members or individuals connected therewith (one such Member or individual designated as Panel Chairman) appointed by the President, except that where the aggregate amount of the [customer's] claims (exclusive of interest and costs) [plus the aggregate amount of any counterclaims (exclusive



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of interest and costs)] do not exceed \$10,000, the Panel shall consist of one such person unless the Secretary directs otherwise: Provided, however, if a [the] customer [in an arbitration under Section 2[(a)] of this Code] so requests in a timely filed pleading [the Demand for Arbitration (see Section 6(c) of this Code)], the Chairman and at least one other arbitrator [member of the Panel], and the sole arbitrator [Panel member] where there is a single-person [member] Panel, shall not be connected with an NFA Member or NFA (except as NFA arbitrators). For purposes of this section, any individual who performs a significant amount of work on behalf of NFA Members or Associates and any individual who was a Member or Associate or was an employee of a Member within the past three years shall be considered to be connected with an NFA Member.

\* \* \*

**(c) Appointment of Panel; Disclosure and Challenge.**

The President shall thereupon appoint, pursuant to Section 4(a), an arbitration Panel to resolve the dispute. No arbitrator shall have acted as the mediator in the same dispute. The Secretary shall promptly notify the parties of the names, business affiliations, and other information relevant to the classification of the arbitrator as a Member or non-Member panelist. Any objection of a party to such appointment shall be specific and for cause and submitted to the President in written form. Each party or their representative shall disclose to the President any circumstances likely to affect an arbitrator's impartiality, including any bias or financial interest in the result of the arbitration or any past or present relationship with the arbitrator. Any party who fails to disclose such information shall be deemed to have waived any objection to that arbitrator based on such information. Each arbitrator [member] appointed shall disclose to the President any circumstances likely to affect impartiality, including any bias or financial interest in the result of the arbitration or any past or present relationship with the parties or their representative. Upon receipt of such information from an arbitrator [such member] or other source, the President shall communicate such information to the parties, and if the President deems it appropriate to do so, to the Panel [members] and others. Thereafter, the President shall determine whether



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the arbitrator [member] should be disqualified and shall inform the parties of the decision, which shall be conclusive.

\* \* \*

**(e) Replacement.**

If an arbitrator becomes ineligible or otherwise unable to serve on the Panel, the President shall (unless the parties request otherwise) appoint a replacement to the Panel. In the event an arbitrator is excused or recuses himself after the commencement of the hearing because a party failed to disclose information which may be grounds for objecting to the arbitrator, the party withholding the information shall be deemed to have waived his right to object to proceeding with the remaining two arbitrators. If a replacement is appointed [such appointment is made] after the commencement of the hearing, the Panel shall determine whether all or any part of any prior hearing sessions shall be repeated [(unless the parties request otherwise) conduct a re-hearing].

\* \* \*

**Section 5. Time Period for Arbitration.**

No Demand for Arbitration [claim] may be arbitrated under this Code unless a notice of intent to arbitrate (see Section 6(a) below) is received by the Secretary within two years from the date when the party filing the Demand for Arbitration [asserting the claim] knew or should have known of the act or transaction that is the subject of the controversy. Except as provided under Sections 6(f) and (h) below, no counterclaim, cross-claim or third-party claim may be arbitrated under this Code unless it is asserted in a timely filed Answer in accordance with Section 6(e) below. The Secretary shall reject any claim [or counterclaim] that is not timely filed. If, in the course of any arbitration, the Panel determines that the requirements of this section have not been met as to a particular claim, [or counterclaim,] the Panel shall thereupon terminate the arbitration of the claim [or counterclaim] without decision or award.



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**Section 6. Initiation of Arbitration.**

\* \* \*

**(e) Answer to a Demand for Arbitration.**

The Respondent shall serve an Answer on the Secretary within 45 days from the date of service of the Demand for Arbitration on the Respondent by the Secretary. The Respondent shall concurrently serve a copy of the Answer on the Claimant. An allegation in the Demand for Arbitration that is not denied in the Answer shall be deemed by the Panel to be admitted.

**(f) [Section 2(a)(2)] Counterclaim and Cross-claim.**

Any counterclaim or cross-claim under Section 2(a)(2) must be asserted in the Answer, unless the person against whom the counterclaim or cross-claim is asserted [Claimant] consents to a later assertion of the counterclaim or cross-claim. If any counterclaim or cross-claim is asserted, the party asserting the counterclaim or cross-claim shall promptly remit the appropriate fee to the Secretary (see Sections 11 and 18 below). Any counterclaim or cross-claim which the Secretary deems to be incomplete, or which is not accompanied by the appropriate fee, shall be returned by certified mail. In that event, such person shall serve a completed counterclaim or cross-claim, together with any unpaid fee, within 20 days following service by the Secretary. The Secretary shall reject any counterclaim or cross-claim which has not been timely filed, or for which the appropriate fee has not been paid.

**(g) Reply to Counterclaim or Cross-claim.**

The person against whom the counterclaim or cross-claim is asserted shall reply to the counterclaim or cross-claim by serving a Reply on the Secretary within 35 days after the date of service of the Answer, [or] counterclaim or cross-claim by the Secretary, and shall concurrently serve a copy of the Reply on the counterclaiming or cross-claiming Respondent. Any allegation in the counterclaim or cross-claim that is not denied in the Reply shall be deemed by the Panel to be admitted.



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**(h) Third-party Claim.**

Any third-party claim under Section 2(a)(2) must be asserted in the Answer, unless the third-party consents to a later assertion of the claim. If the third-party is not a Member or Associate, such person must agree or have agreed to submit to arbitration. If any third-party claim is asserted, the Respondent asserting the third-party claim shall promptly remit the appropriate fee to the Secretary (see Sections 11 and 18 below). Any third-party claim which the Secretary deems to be incomplete, or which is not accompanied by the appropriate fee, shall be returned by certified mail. In that event, such person shall serve a completed third-party claim, together with any unpaid fee, within 20 days following service by the Secretary. The Secretary shall reject any third-party claim which has not been timely filed, or for which the appropriate fee has not been paid.

**(i) Notice to Third-party Respondent.**

The Secretary shall promptly serve a copy of the completed third-party claim on each person named therein as a Respondent, and a copy of any agreement to arbitrate.

**(j) Answer to Third-party Claim.**

The third-party Respondent shall serve an Answer on the Secretary within 45 days from the date of service of the third-party claim on the Respondent by the Secretary. The Respondent shall concurrently serve a copy of the Answer on the third-party Claimant. An allegation in the third-party claim that is not denied in the Answer shall be deemed by the Panel to be admitted.

**(k) [(h)] Amendments to Claims [or Counterclaim].**

After the appointment of a Panel, no new or different claim [or counterclaim] may be filed except with the Panel's consent.



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(l) [(i)] **Late Answer or Reply.**

The Secretary shall accept any Answer or Reply filed prior to the hearing. However, the Secretary or any party may present an objection to the Panel with regard to the timeliness of any filing.

(m) [(j)] **Consolidation.**

When Demands for Arbitration involving common questions of fact or arising from the same act or transaction are received by the Secretary, the Secretary may, whether or not at the request of any party, order any or all of the proceedings to be consolidated for hearing in the interest of providing a fair, equitable, and expeditious procedure and may take such action concerning the proceedings herein as may tend to avoid unnecessary or unreasonable delay.

(n) [(k)] **Dismissal Without Prejudice.**

The Panel may, at the written request of a party or on its own motion, dismiss without prejudice any claim [or counterclaim] which it determines is not a proper subject for NFA arbitration.

\* \* \*

**Section 8. Pre-Hearing.**

**(a) Exchange of Documents and Written Information.**

\* \* \*

(2) All requests for documents and written information shall be served on the responding party by the requesting party no later than 30 days after the last pleading [Answer] is due[, or no later than 30 days after a Reply is due if a counterclaim has been asserted]. The responding party shall serve the requesting party with the documents and written information, including written objections, no later than 30 days after the request is due. Written requests to compel production of documents and written information must be served on the Secretary and all parties no later than 10 days after the written objections are due, and written responses to the request to compel must be served on the



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Secretary and all parties no later than 10 days after the request to compel was served. Unless the Panel directs otherwise, requests to compel will be decided on the written submissions of the parties.

\* \* \*

**Section 9. Hearing.**

\* \* \*

**(f) Failure to Comply.**

The failure of any party to appear at any hearing or any session thereof, or to comply with any notice, order, or procedure in connection therewith, may subject the party to such adverse action as the Panel deems appropriate, including the entry of an award or the dismissal of a claim [or counterclaim].

\* \* \*

**(i) Summary Proceeding.**

The proceeding shall be conducted entirely through written submissions when:

(1) the aggregate amount of the claims (exclusive of interest and costs) [plus the aggregate amount of counterclaims (exclusive of interest and costs)] does not exceed \$5,000, unless the Secretary or the Panel directs otherwise; or

(2) the aggregate amount of the claims (exclusive of interest and costs) [plus the aggregate amount of counterclaims (exclusive of interest and costs)] is more than \$5,000 but not more than \$10,000, unless the Secretary or the Panel directs otherwise or one of the parties to the proceeding serves a written request for an oral hearing on the Secretary no later than 30 days after the last pleading [Answer] is due [, or no later than 30 days after the Reply is due if a counterclaim has been asserted]; or

\* \* \*



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**Section 10. Award, Settlement, and Withdrawal**

\* \* \*

**(h) Satisfaction of Demand.**

At any time during the course of an arbitration, a party [Respondent] may satisfy a claim [Demand for Arbitration and a Claimant may satisfy a counterclaim] by payment or settlement, including settlement through mediation. The arbitration proceeding will terminate upon receipt of written notice of satisfaction and withdrawal of the claim [Demand for Arbitration] duly executed by the parties and submitted to the Secretary. If the Secretary is notified that a claim [the Demand for Arbitration or a counterclaim] has been settled, but the notification is not in writing or is not duly executed by the parties, the Secretary shall send written notice to the parties that the arbitration proceeding will terminate within 20 days of service of such notice unless the Secretary receives written notice that the claim [Demand for Arbitration or counterclaim] has not been settled.

**(i) Consent Award.**

If parties agree to satisfy a claim [the Demand for Arbitration] at any time during the arbitration, the Panel may, at the request of such parties, set forth the terms of the satisfied claim [Demand for Arbitration] in a consent award.

**(j) Withdrawal of Claim [Demand].**

(1) At any time during the course of the arbitration, a party [Claimant] may withdraw a claim [the Demand for Arbitration] against any Respondent who has not filed an Answer. A written notice of withdrawal must be filed with the Secretary. The withdrawal will be without prejudice unless the notice states otherwise.

(2) After a party [Respondent] has filed a [n Answer] pleading, another party [Claimant] may not withdraw a [the] claim [Demand for Arbitration] against that party [Respondent] unless the party [Respondent] consents. The notice and the consent must be in writing and filed with the Secre-



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tary. The withdrawal will be without prejudice unless the notice or consent states otherwise.

[(3) A Respondent may not withdraw a counterclaim against a Claimant unless the Claimant consents. The notice and consent will be without prejudice unless the notice or consent states otherwise.]

**Section 11. Arbitration Fees.**

**(a) Filing and Hearing Fees.**

Except as provided in Section 18 of this Code, [E]each party filing a claim [claiming or counterclaiming] under this Code shall pay a filing and hearing fee based on the amount claimed [or counterclaimed], including punitive and treble damages but exclusive of interest and costs, as follows:

| <u>Amount of Claim [or Counterclaim]</u> | <u>Filing Fee</u>              | <u>Hearing Fee</u> |
|--|--------------------------------|--------------------|
| \$ 0.00 - \$ 2,500.00                    | \$ 50.00                       | \$ 50.00           |
| \$ 2,500.01 - \$ 5,000.00                | \$100.00                       | \$ 50.00           |
| \$ 5,000.01 - \$ 10,000.00               | \$150.00                       | \$ 150.00          |
| \$10,000.01 - \$ 15,000.00               | \$175.00                       | \$ 450.00          |
| \$15,000.01 - \$150,000.00               | \$200.00 plus<br>1% of excess  | \$ 675.00          |
| More than \$150,000.00                   | over \$15,000.00<br>\$1,550.00 | \$1,350.00         |

Where multiple hearing sessions are required in excess of those covered by the hearing fee, the arbitrators shall assess fees for the additional hearing sessions in an amount equal to the standard preset fees to be paid by the Secretary to the arbitrators for the additional hearing sessions. The arbitrators, in their discretion, may assess the entire fee against any party or may divide the fee among any or all parties. Hearing session fees shall be paid to the Secretary in advance of the hearing sessions to which they apply.



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**(b) Refunds.**

\* \* \*

(2) If all claims [and counterclaims] have been settled or withdrawn and the Secretary receives written notice of the settlement or withdrawal at least eight days in advance of the first scheduled hearing or preliminary hearing date, the hearing fee shall be refunded to the party paying the fee.

**(c) Postponement Fees.**

Each party causing a postponement of any scheduled oral hearing shall pay to the Secretary a postponement fee of \$250 for the first postponement request by that party, \$500 for the second request by that party, and \$1,000 for any subsequent request by that party. This fee may be waived at the discretion of the arbitrators. The arbitrators also may assess reasonable and necessary expenses incurred by the parties and their witnesses, including reasonable attorneys' fees, as a result of a postponement. No fee shall be assessed if an arbitrator becomes ineligible or otherwise unable to serve, or if a hearing extends over the expected time period.

**Section 12. Arbitration Costs.**

A Panel may assess against a party any one or more of the following costs, upon a finding that such party's claim[, counter-claim,] or defense was frivolous or was made in bad faith, or that the party engaged in willful acts of bad faith during the arbitration: Reasonable and necessary expenses incurred by (a) the arbitrators or (b) any other party or witness, including reasonable attorneys' fees. The Panel may also award attorneys' fees provided that a statutory or contractual basis exists for awarding such fees.

\* \* \*



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**Section 16. Miscellaneous**

\* \* \*

**(b) Service of Process.**

Unless otherwise indicated, service may be accomplished by hand delivery, or by first class or certified mail, or by use of a generally recognized overnight delivery service to the party's last known business or home address on record with NFA. All documents which are served on the Secretary shall be concurrently served on each party who has filed a pleading [Demand or Answer]. Service on a party's representative shall be service on the party.

\* \* \*

**Section 18. Applicability of Member Arbitration Rules.**

This Code shall govern any cross-claim or third-party claim filed by a Member or Associate against another Member or Associate under this Code, except that Section 2(a) and Section 11(a) of the Member Arbitration Rules shall apply to such cross-claim or third-party claim.

\* \* \*

**MEMBER ARBITRATION RULES**

\* \* \*

**Section 1. Definitions**

\* \* \*

**(b)** "Claim" -- means a Demand for Arbitration, counterclaim, cross-claim or third-party claim filed under these Rules.

**(c)** **[(b)]** "Claimant" -- means a person making a proper and timely claim [Demand for Arbitration] under these Rules.



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- (d) [(c)] "Commission" -- means the Commodity Futures Trading Commission.
- (e) [(d)] "Contract Market" -- means an exchange designated by the Commission as a contract market in one or more commodities.
- (f) "Cross-claim" -- means a claim filed by one Respondent against a co-Respondent.
- (g) [(e)] "Hearings" -- includes both oral hearings and summary proceedings, unless otherwise specified.
- (h) [(f)] "Member" -- means a Member of NFA or a person that was a Member at the time the acts or transactions that are the subject of the dispute occurred.
- (i) [(g)] "NFA" -- means National Futures Association.
- (j) [(h)] "Panel" -- means the arbitration panel appointed pursuant to Section 3 of these Rules.
- (k) [(i)] "Person" -- includes individuals, corporations, partnerships, trusts, associations and other entities.
- (l) [(j)] "Pleading[s]" -- means a [includes the] Demand for Arbitration, counterclaim, cross-claim, third-party claim, [filed by a Claimant, the] Answer or [and any counterclaim filed by a Respondent, and any] Reply filed under these Rules [to a counterclaim filed by a Claimant].
- (m) [(k)] "President" -- means the President of NFA.
- (n) [(l)] "Respondent" -- means a person against whom a claim is asserted under these Rules.
- (o) [(m)] "Secretary" -- means the Secretary of NFA.
- (p) [(n)] "Self-regulatory organization" -- means a contract market, a registered national secur-



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ities exchange, or a registered national securities association.

(g) "Third-party Claim" -- means a claim filed by a Respondent against a person not a party to the action.

### Section 2. Arbitrable Disputes.

\* \* \*

(a) **Claims.** Except as provided in Sections 4 and 5 of these Rules with respect to timeliness requirements, disputes between and among Members and Associates shall be arbitrated under these Rules upon the filing of a claim [Demand] by a Member or Associate unless:

- (1) the parties, by valid and binding agreement, have committed themselves to the resolution of such dispute in a forum other than NFA;
- (2) the parties to such dispute are required by the rules of another self-regulatory organization to submit the controversy to the settlement procedures of that self-regulatory organization; or
- (3) all parties to the dispute are members of a contract market which has jurisdiction over the dispute.

(b) **Counterclaims, Cross-claims and Third-party Claims.** Except as provided in Sections 4 and 5 of these Rules with respect to timeliness requirements, a counterclaim, cross-claim or third-party claim may be asserted in an arbitration brought under paragraph (a) above if the counterclaim, cross-claim or third-party claim arises out of an act or transaction that is the subject of the Demand for Arbitration [claim].

### Section 3. Arbitration Panel.

(a) **Appointment of Panel.**

All arbitration proceedings under these Rules shall be conducted before an arbitration panel consisting of three NFA Members or individuals connected therewith (one such

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Member or individual designated as Panel Chairman) appointed by the President, except that where the aggregate amount of the claims (exclusive of interest and costs) [plus the aggregate amount of any counterclaims (exclusive of interest and costs)] do not exceed \$10,000, the Panel shall consist of one such person unless the Secretary directs otherwise.

\* \* \*

**(c) Appointment of Panel; Disclosure and Challenge.**

The President shall thereupon appoint, pursuant to Section 3(a), an arbitration Panel to resolve the dispute. No arbitrator shall have acted as the mediator in the same dispute. The Secretary shall promptly notify the parties of the names, business affiliations, and other relevant information. Any objection of a party to such appointment shall be specific and for cause and submitted to the President in written form. Each party or their representative shall disclose to the President any circumstances likely to affect an arbitrator's impartiality, including any bias or financial interest in the result of the arbitration or any past or present relationship with the arbitrator. Any party who fails to disclose such information shall be deemed to have waived any objection to that arbitrator based on such information. Each arbitrator [member] appointed shall disclose to the President any circumstances likely to affect impartiality, including any bias or financial interest in the result of the arbitration or any past or present relationship with the parties or their representative. Upon receipt of such information from an arbitrator [such member] or other source, the President shall communicate such information to the parties, and if the President deems it appropriate to do so, to the Panel [members] and others. Thereafter, the President shall determine whether the arbitrator [member] should be disqualified and shall inform the parties of the decision, which shall be conclusive.

\* \* \*

**(e) Replacement.**

If an arbitrator becomes ineligible or otherwise unable to serve on the Panel, the President shall (unless the



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parties request otherwise) appoint a replacement to the Panel. In the event an arbitrator is excused or recuses himself after the commencement of the hearing because a party failed to disclose information which may be grounds for objecting to the arbitrator, the party withholding the information shall be deemed to have waived his right to object to proceeding with the remaining two arbitrators. If a replacement is appointed [such appointment is made] after the commencement of the hearing, the Panel shall determine whether all or any part of any prior hearing sessions shall be repeated [(unless the parties request otherwise) conduct a re-hearing].

\* \* \*

#### **Section 4. Time Period for Arbitration.**

No Demand for Arbitration [claim] may be arbitrated under these Rules unless a notice of intent to arbitrate (see Section 5(a) below) is received by the Secretary within two years from the date when the party filing the Demand for Arbitration [asserting the claim] knew or should have known of the act or transaction that is the subject of the controversy. No counterclaim, cross-claim or third-party claim may be arbitrated under these Rules unless it is received by the Secretary within two years from the date when the party asserting the counterclaim, cross-claim or third-party claim knew or should have known of the act or transaction that is the subject of the counterclaim, cross-claim or third-party claim or it is served on the Secretary within 45 days from the date of service of the Demand for Arbitration on the Respondent by the Secretary, whichever is later. The Secretary shall reject any claim [or counterclaim] that is not timely filed. If, in the course of any arbitration, the Panel determines that the requirements of this section have not been met as to a particular claim, [or counterclaim,] the Panel shall thereupon terminate the arbitration of the claim [or counterclaim] without decision or award.



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**Section 5. Initiation of Arbitration.**

\* \* \*

**(e) Answer to a Demand for Arbitration.**

The Respondent shall serve an Answer on the Secretary within 45 days from the date of service of the Demand for Arbitration on the Respondent by the Secretary. The Respondent shall concurrently serve a copy of the Answer on the Claimant. An allegation in the Demand for Arbitration that is not denied in the Answer shall be deemed by the Panel to be admitted.

**(f) Counterclaim and Cross-claim.**

If any counterclaim or cross-claim is asserted, the party asserting the counterclaim or cross-claim, shall promptly remit the appropriate fee to the Secretary (see Section 11 below). Any counterclaim or cross-claim which the Secretary deems to be incomplete, or which is not accompanied by the appropriate fee, shall be returned by certified mail. In that event, such person shall serve a completed counterclaim or cross-claim, together with any unpaid fee, within 20 days following service by the Secretary. The Secretary shall reject any counterclaim or cross-claim which has not been timely filed, or for which the appropriate fee has not been paid.

**(g) Reply to Counterclaim or Cross-claim.**

The person against whom the counterclaim or cross-claim is asserted shall reply to the counterclaim or cross-claim by serving a Reply on the Secretary within 35 days after the date of service of the counterclaim or cross-claim by the Secretary, and concurrently shall serve a copy of the Reply on the counterclaiming or cross-claiming Respondent. Any allegation in the counterclaim or cross-claim that is not denied in the Reply shall be deemed by the Panel to be admitted.

**(h) Third-party Claim.**

A Respondent may file a third-party claim against a Member or Associate under these Rules. If any third-party



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claim is asserted, the Respondent asserting the third-party claim shall promptly remit the appropriate fee to the Secretary (see Section 11 below). Any third-party claim which the Secretary deems to be incomplete, or which is not accompanied by the appropriate fee, shall be returned by certified mail. In that event, such person shall serve a completed third-party claim, together with any unpaid fee, within 20 days following service by the Secretary. The Secretary shall reject any third-party claim which has not been timely filed, or for which the appropriate fee has not been paid.

(i) Notice to Third-party Respondent.

The Secretary shall promptly serve a copy of the completed third-party claim on each person named therein as a Respondent, and a copy of any agreement to arbitrate.

(j) Answer to Third-party Claim.

The third-party Respondent shall serve an Answer on the Secretary within 45 days from the date of service of the third-party claim on the Respondent by the Secretary. The Respondent shall concurrently serve a copy of the Answer on the third-party Claimant. An allegation in the third-party claim that is not denied in the Answer shall be deemed by the Panel to be admitted.

(k) [(h)] Amendments to Claims [or Counterclaim].

After the appointment of the Panel, no new or different claim [or counterclaim] may be filed except with the Panel's consent.

(l) [(i)] Late Answer or Reply.

The Secretary shall accept any Answer or Reply filed prior to the hearing. However, the Secretary or any party may present an objection to the Panel with regard to the timeliness of any filing.

(m) [(j)] Consolidation.

When Demands for Arbitration involving common questions of fact or arising from the same act or transaction are



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received by the Secretary, the Secretary may, whether or not at the request of any party, order any or all of the proceedings to be consolidated for hearing in the interest of providing a fair, equitable, and expeditious procedure and may take such action concerning the proceedings herein as may tend to avoid unnecessary or unreasonable delay.

\* \* \*

**Section 7. Pre-Hearing.**

**(a) Exchange of Documents and Written Information.**

\* \* \*

(2) All requests for documents and written information shall be served on the responding party by the requesting party no later than 30 days after the last pleading [Answer] is due[, or no later than 30 days after a Reply is due if a counterclaim has been asserted]. The responding party shall serve the requesting party with the documents and written information, including written objections, no later than 30 days after the request is due. Written requests to compel production of documents and written information must be served on the Secretary and all parties no later than 10 days after the written objections are due, and written responses to the request to compel must be served on the Secretary and all parties no later than 10 days after the request to compel was served. Unless the Panel directs otherwise, requests to compel will be decided on the written submissions of the parties.

\* \* \*

**Section 8. Dismissal Without Prejudice.**

The Panel may, at the written request of a party or on its own motion, dismiss without prejudice any claim [or counterclaim] which it determines is not a proper subject for NFA arbitration.



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**Section 9. Hearing.**

\* \* \*

**(f) Failure to Comply.**

The failure of any party to appear at any hearing or any session thereof, or to comply with any notice, order, or procedure in connection therewith, may subject the party to such adverse action as the Panel deems appropriate, including the entry of an award or the dismissal of a claim [or counterclaim].

\* \* \*

**(i) Summary Proceeding.**

The proceeding shall be conducted entirely through written submissions when:

(1) the aggregate amount of the claims (exclusive of interest and costs) [plus the aggregate amount of counterclaims (exclusive of interest and costs)] does not exceed \$10,000, unless the Secretary or the Panel directs otherwise; or

(2) the aggregate amount of the claims (exclusive of interest and costs) [plus the aggregate amount of counterclaims (exclusive of interest and costs)] is more than \$10,000 but not more than \$20,000, unless the Secretary or the Panel directs otherwise or one of the parties to the proceeding serves a written request for an oral hearing on the Secretary no later than 30 days after the last pleading [Answer] is due[, or no later than 30 days after the Reply is due if a counterclaim has been asserted]; or

\* \* \*



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**Section 10. Award, Settlement, and Withdrawal**

\* \* \*

**(h) Satisfaction of Demand.**

At any time during the course of an arbitration, a party [Respondent] may satisfy a claim [Demand for Arbitration and a Claimant may satisfy a counterclaim] by payment or settlement, including settlement through mediation. The arbitration proceeding will terminate upon receipt of written notice of satisfaction and withdrawal of the claim [Demand for Arbitration] duly executed by the parties and submitted to the Secretary. If the Secretary is notified that a claim [the Demand for Arbitration or a counterclaim] has been settled, but the notification is not in writing or is not duly executed by the parties, the Secretary shall send written notice to the parties that the arbitration proceeding will terminate within 20 days of service of such notice unless the Secretary receives written notice that the claim [Demand for Arbitration or counterclaim] not been settled.

**(i) Consent Award.**

If parties agree to satisfy a claim [the Demand for Arbitration] at any time during the arbitration, the Panel may, at the request of such parties, set forth the terms of the satisfied claim [Demand for Arbitration] in a consent award.

**(j) Withdrawal of Claim [Demand].**

(1) At any time during the course of the arbitration, a party [Claimant] may withdraw a claim [the Demand for Arbitration] against any Respondent who has not filed an Answer. A written notice of withdrawal must be filed with the Secretary. The withdrawal will be without prejudice unless the notice states otherwise.

(2) After a party [Respondent] has filed a [n Answer] pleading, another party [Claimant] may not withdraw a [the] claim [Demand for Arbitration] against that party [Respondent] unless the party [Respondent] consents. The notice



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and the consent must be in writing and filed with the Secretary. The withdrawal will be without prejudice unless the notice or consent states otherwise.

[(3) A Respondent may not withdraw a counterclaim against a Claimant unless the Claimant consents. The notice and consent will be without prejudice unless the notice or consent states otherwise.]

**Section 11. Arbitration Fees.**

**(a) Filing and Hearing Fees.**

Each Member or Associate filing a claim [claiming or counterclaiming] under these Rules shall pay a filing and hearing fee based on the amount claimed [or counterclaimed], including punitive and treble damages but exclusive of interest and costs, as follows:

| <u>Amount of Claim [or Counterclaim]</u> | <u>Filing Fee</u> | <u>Hearing Fee</u> |
|--|-------------------|--------------------|
| \$ 0.00 - \$ 10,000.00                   | \$ 750.00         | \$ 50.00           |
| \$10,000.01 - \$ 20,000.00               | \$1,900.00        | \$ 150.00          |
| \$20,000.01 - \$150,000.00               | \$4,400.00        | \$ 675.00          |
| More than \$150,000.00                   | \$4,400.00        | \$1,350.00         |

Where multiple hearing sessions, including preliminary hearing sessions, are required in excess of those covered by the hearing fee, the arbitrators shall assess fees for the additional hearing sessions in an amount equal to the standard preset fees to be paid by the Secretary to the arbitrators for the additional hearing sessions. The arbitrators, in their discretion, may assess the entire fee against any party or may divide the fee among any or all parties. Hearing session fees shall be paid to the Secretary in advance of the hearing sessions to which they apply.

**(b) Refunds.**

\* \* \*

(2) If all claims [and counterclaims] have been settled or withdrawn and the Secretary receives written notice of the settlement or withdrawal at least eight days in advance of the first scheduled hearing or preliminary hear-



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ing date, the hearing fee shall be refunded to the party paying the fee.

**(c) Postponement Fees.**

Each party causing an adjournment or postponement of any scheduled oral hearing shall pay to the Secretary a postponement fee of \$300 for the first postponement request by that party, \$500 for the second request by that party, and \$1,000 for any subsequent request by that party. This fee may be waived at the discretion of the arbitrators. The arbitrators also may assess reasonable and necessary expenses incurred by the parties and their witnesses, including reasonable attorneys' fees, as a result of a postponement. No fee shall be assessed if an arbitrator becomes ineligible or otherwise unable to serve, or if a hearing extends over the expected time period.

**Section 12. Arbitration Costs.**

A Panel may assess against a party any one or more of the following costs, upon a finding that such party's claim[, counterclaim,] or defense was frivolous or was made in bad faith, or that the party engaged in wilful acts of bad faith during the arbitration: Reasonable and necessary expenses incurred by (a) the arbitrators or (b) any other party or witness, including reasonable attorneys' fees. The Panel may also award attorneys' fees provided that a statutory or contractual basis exists for awarding such fees.

**Section 16. Miscellaneous**

\* \* \*

**(b) Service of Process.**

Unless otherwise indicated, service may be accomplished by hand delivery, or by first class or certified mail, or by use of a generally recognized overnight delivery service to the party's last known business or home address on record with NFA. All documents which are served on the Secretary shall be concurrently served on each party who has filed a pleading [Demand or Answer]. Service on a party's representative shall be service on the party.



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- C. Proposed deletion of NFA Compliance Rule 2-28 (deletion is bracketed):

COMPLIANCE RULES

\* \* \*

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

\* \* \*

[Rule 2-28. LINKED MARKET TRANSACTION AUTHORIZATION AND  
DISCLOSURE REQUIREMENTS.

Each Member FCM or IB which engages in transactions on a foreign futures exchange pursuant to a linked market agreement between a domestic contract market and a foreign futures exchange on behalf of a customer's account carried or introduced by the Member must have on file an authorization executed by the customer to engage in such transactions. The authorization may either be in the customer agreement or on a separate form and must include either the language set forth in CFTC Regulation 30.6 or the following language in boldface type or print:

"[Name] may from time to time execute transactions as customer's agent on a foreign futures exchange pursuant to an agreement between the foreign futures exchange and a domestic futures exchange that a trade executed on one exchange liquidates or establishes a position on the other exchange. Participation in such a transaction may involve the execution and clearing of trades on a foreign futures exchange. Neither the Commodity Futures Trading Commission ("Commission"), the National Futures Association ("NFA") nor any domestic futures exchange regulates the activities of a foreign futures exchange, including the execution, delivery and clearing of transactions on such an exchange, or has the power to compel enforcement of the rules of the foreign futures



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exchange and the laws of the foreign country. For these reasons, customers who trade on a foreign futures exchange may not be afforded certain of the protective measures provided by the Commodity Exchange Act, the Commission's regulations, and the rules of NFA and any domestic futures exchange, including the right to use reparation proceedings before the Commission and arbitration proceedings provided by NFA or any domestic futures exchange."

In addition to the above requirements, each non-discretionary order executed on one exchange to liquidate or establish a position on another exchange pursuant to a linked market agreement must be authorized by the customer and designated as such when the order is taken. With respect to a discretionary customer account, if the authorization to engage in such transactions is in the customer agreement, the customer must separately acknowledge the section of the customer agreement that contains the risk disclosure language required under this rule. Provided, however, that if the language set forth in CFTC Regulation 30.6 is used, this requirement may be satisfied by incorporating into the text of the customer's written grant of discretion an express acknowledgment that the customer has received and understood the risk disclosure statement required by this rule. In the case of an introduced account carried by an FCM on a fully disclosed basis, the requirements of this rule apply only to the introducing IB or the introducing FCM unless the carrying FCM has agreed to be responsible for compliance.]



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## II. EXPLANATION OF AMENDMENTS

### A. Explanation of proposed amendments to NFA Bylaws 702, 704, 707 and 708 and Part 3 of NFA Compliance Rules:

#### 1) COMMITTEE STRUCTURE

##### a) **Creating a Business Conduct Committee and a Hearing Committee in Lieu of Regional Business Conduct Committees**

NFA's three regional Business Conduct Committees ("BCCs") perform the dual functions of deciding whether to bring charges against a Member based on staff's investigative report and then presiding over any hearing to resolve those charges. This dual function has led some to question the impartiality of the BCCs in presiding over hearings in which they already reviewed an investigative report and found probable cause to issue a complaint. NFA has no doubt that the BCCs have been scrupulously fair in conducting hearings but also realizes that the perception of fairness in disciplinary proceedings is as important as the fairness itself. For this reason, as well as practical and logistical concerns, the Board of Directors determined that the three regional BCCs should be replaced with two committees -- a Business Conduct Committee to review investigative reports and issue complaints and a Hearing Committee to preside over any hearings resulting from those complaints.

The practical advantage of a two-committee system is that the disproportionate time demands made on the BCC members resulting solely from geographical location of problem firms would be eliminated. Moreover, hearings involving telemarketing fraud tend to require even more time because of multiple respondents and numerous customer witnesses. Members of the hearing committee will be appointed based, in part, on their ability to contribute significant blocks of time to conduct lengthy hearings. The availability of such persons as hearing panel members should reduce the overall time needed to complete lengthy hearings.



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One of the purposes of the regional system was to avoid the possibility of regional bias. However, the regional BCCs have been very consistent both in deciding what conduct gives rise to charges and in imposing similar sanctions for similar conducts and have not demonstrated any significant regional differences in the way they administer NFA's disciplinary system. Consequently, there does not appear to be a need for a regional committee system.

Therefore, the Board amended the Bylaws and Part 3 of the Compliance Rules to provide for the adoption of a Business Conduct Committee which would review investigative reports, issue complaints when appropriate and review settlement offers, and a Hearing Committee which, through hearing panels comprised of a smaller number of its members, would conduct hearings, review settlement offers and issue decisions accordingly.

**b) Including Non-NFA Members on NFA Disciplinary Committees**

To conform NFA rules to the requirements of CFTC Regulation 1.64, NFA Bylaws 702, 704 and 707 were amended and Compliance Rule 3-17 was adopted to provide that the Business Conduct Committee, Hearing Committee and Appeals Committee include at least one non-NFA Member; to require that any disciplinary committee or panel include at least one person representing a membership category other than the respondent's membership category; and to require that any panel designated by a disciplinary committee to conduct proceedings in a case in which the respondent is a member of NFA's Board or an NFA disciplinary committee contain at least one non-NFA Member.

**2) PROCEDURAL RULES**

**a) Exchanging Names of Witnesses and Copies of Trial Exhibits**

NFA's current Part 3 rules do not require the parties in a disciplinary proceeding to give notice to each other or the panel of what they plan to present in their case-in-chief, either the witnesses they intend



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to call or the documentary evidence they plan to introduce. Pre-hearing disclosure of witnesses and exhibits is standard practice in almost every civil litigation forum. The reasons for this are obvious - such disclosure informs the trier of fact how long the litigation should last, allows the parties to be better prepared, expedites the hearing and facilitates settlement. NFA's review of other self-regulatory organizations' ("SRO") procedures, as well as NFA's Arbitration Rules and Part 10 of the Commission's regulations, revealed that all but one formally require an exchange of witness lists and exhibits.<sup>1</sup>

NFA proposes amending its Part 3 rules so that Compliance Rule 3-8 requires that at least fifteen days prior to the date assigned for oral hearing NFA and each party which has filed an answer shall serve on NFA and every other answering party the name, address and phone number of each witness the party intends to call and copies of all documents which the party intends to introduce into evidence at the hearing as part of its direct case. The rule also gives the panel the authority to preclude any party from presenting witnesses or evidence at the hearing that have not been previously disclosed, except for good cause shown.

**b) Pre-Hearing Conferences**

NFA's Part 3 rules currently have no provision for pre-hearing conferences. Such conferences are common in civil litigation, and the rules of several exchanges provide for them as well. This type of conference can be extremely useful in certain circumstances, i.e., where there are factual issues that lend themselves to stipulations or admissions, where the parties have reached an impasse on discovery or pre-hearing disclosure, or where a party needs to argue a particularly complex motion.

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<sup>1</sup> The Chicago Mercantile Exchange ("CME") does not have a formal requirement. However, CME Compliance staff informed NFA that such an exchange is routine as a matter of professional courtesy.



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The amendments to Compliance Rule 3-8 allow either side to petition the panel to schedule a pre-hearing conference, a request that the panel may grant at its discretion; allow the panel to schedule such a conference on its own motion; and authorize the panel to determine which issues may be the subject of a conference conducted by Chairman alone.

**c) Discovery Requirements**

NFA's current discovery rule -- which states that the respondent is entitled to reasonable pre-hearing examination of all evidence in NFA's possession or under its control that is to be relied upon by the Compliance Office or is relevant to the complaint -- is silent on three important issues that pertain to discovery: access, cost and timing. With respect to access and cost, there have at times been disputes as to what constitutes a "reasonable" pre-hearing examination, particularly when NFA's evidence is in Chicago and the respondent is not. Staff has generally taken the position that NFA's materials are available for inspection at NFA's offices and may be copied at the respondent's expense. Another recurring problem is respondents who wait until the last minute to request discovery, a practice that makes it difficult for NFA staff to prepare for trial.<sup>2</sup>

NFA proposes amending its Part 3 rules so that Compliance Rule 3-8 requires that the respondent must

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<sup>2</sup> NFA staff asked the various SROs about their discovery rules and practices. All of the exchanges interviewed have discovery rules virtually identical to ours, as the language is taken directly from Part 8 of the Commission's regulations. How to provide access to the documents is simply not an issue for the exchanges, because unlike NFA their members and their attorneys are almost always from the local area. Because access is not an issue, cost is much less of an issue, as respondents who actually come to the office to read through the materials are less likely to ask for a lot of useless copying of the material. Finally, the exchanges do not have cut-off dates for discovery and do not seem to need them, again because of the local nature of the litigation.



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affirmatively ask for access to NFA's materials, that the materials will be available for inspection at NFA's offices or will be copied at respondent's request, and that respondent's right to have access to the documents will terminate thirty days prior to the scheduled hearing date, except for good cause shown (e.g., substitution of counsel).

**d) Work-Product Privilege and Unavailability of Certain Material to Respondents in Discovery**

NFA's current rules are silent on which, if any, materials will be withheld from respondents in discovery. NFA's practice has been to provide all non-privileged materials to respondents. Compliance Rule 3-8 will now codify that access to discovery shall be granted subject to NFA's right to withhold any privileged material (including but not limited to its Investigative Report) under whatever common-law or statutory privileges it has available to it.

**e) Procedures for Filing Motions Before the Panel**

NFA's current Part 3 rules do not provide for any motion practice between the time a complaint is filed and a hearing is held, other than allowing a panel to grant an extension of time for respondent to answer the complaint. However, it has become increasingly common for respondents to request continuances on the eve of trial without being required to make any real showing that such last minute maneuvering was unavoidable, or even to notify their co-respondents of their requests. NFA's lack of formal notice and service requirements for such requests recently meant that an attorney for a party was enroute to Chicago with his client for a hearing when, unbeknownst to him, another party was requesting a continuance of that hearing from the panel. In the aforementioned situation, the problem was two-fold: the moving party waited until the last minute to request a continuance and also failed to provide notice to his co-respondent that he was making such a motion.

NFA feels that the absence of any rules regarding motions in NFA's procedures is no longer appropriate in



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light of the increasing length, complexity and frequency of NFA disciplinary hearings. Therefore, the Board amended NFA's Part 3 rules so that Compliance Rule 3-8 provides that all motions to be decided by a panel shall be filed with NFA and served upon all parties no later than fifteen days prior to the day of hearing, except for good cause shown.

**f) Requesting a Hearing**

NFA rules state that a respondent may request a hearing and that if he fails to do so, he has waived his right to a hearing. The rules do not describe a particular procedure that a respondent must follow in requesting a hearing or a timetable he must adhere to in doing so. NFA proposes that the procedure for requesting a hearing be formalized in Compliance Rules 3-4 and 3-7 by having the respondent request or waive a hearing in writing, a procedure followed by the NASD. This will provide NFA staff with a record of a respondent's waiver of his right to a hearing which, in combination with a second amendment (discussed below), will enable staff to conclude these cases more quickly. Compliance Rule 3-7 as proposed provides that each complaint will include a form labeled "Request for Hearing" which must be returned with the answer to the complaint, similar to a jury demand in a civil case.

**g) Giving Notice to Respondents of the Legal Consequences of Waiver of Right to a Hearing**

Under NFA's current rules, the complaint served on the respondent explains the legal ramifications of failure to answer (i.e., default) and the practical ramifications of failure to request a hearing (waiver of hearing). However, neither the rules nor the complaint specify the procedures that NFA will use to resolve factual and legal issues framed by the complaint and the answer. In practice, where a respondent answers the complaint but fails to request a hearing, staff conducts a "prove-up" before a BCC panel by calling witnesses and entering certain NFA business records into the record and having the panel make a determination on liability and sanctions based on that record. NFA proposes codifying this practice. As



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amended, Compliance Rules 3-4 and 3-7 state explicitly that if a respondent waives his right to a hearing, NFA may proceed to submit testimonial or documentary evidence to the BCC and the respondent will have waived his right to object to such evidence, to cross examine witnesses and to present evidence on his own behalf.

**h) Clarifying that Respondents are not Entitled to a Separate Hearing on the Issue of Sanctions**

NFA rules currently provide that the respondent shall be afforded a hearing "on the charges." NFA has always taken the position that the hearing shall be for the purpose of presenting evidence on the charges as well as possible sanctions, and that it is the only opportunity for either side to present evidence in mitigation or aggravation on the issue of appropriate penalties. NFA is not aware of any other SROs which provide for bifurcated hearings on the issues of rules violations and sanctions as a matter of right and proposes this change to codify that point. Therefore, NFA proposes to eliminate this problem by amending its Part 3 rules to add "and possible sanctions" to the language of Compliance Rule 3-7 notifying respondents of their right to a hearing "on the charges."

**i) Method of Service of Complaints**

The Part 3 rules are silent on what method must be utilized to serve a complaint on a respondent in a disciplinary action. However, NFA's practice has been to serve complaints, as well as all other pleadings, by certified mail. The CFTC has no rule regarding service in its Part 8 Rules governing exchange proceedings. Its Part 10 Rules governing enforcement actions do require the Division of Enforcement to serve its complaints by certified mail but allows it to serve all other documents by regular mail with a certificate of service. The NASD follows the same practice.

Pleadings sent by certified mail are often returned to NFA unclaimed, as it is the respondent's obligation to pick up the pleading at the post office if he is not at home when the mail is delivered. Consequently, NFA's current method gives the respondent control over whether he will accept service of process.

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Therefore, NFA has amended its Part 3 rules so that Compliance Rule 3-3 provides that every document filed in a disciplinary action, including the complaint, will be served upon the respondent by first-class regular mail at the last address provided, with an affidavit of service attached and that the complaint must also be served by overnight delivery.

**j) Telephone Testimony**

NFA proposes amending its Part 3 rules so that Compliance Rule 3-9 allows telephonic testimony at hearings if ordered by the panel. This would clarify the issue for respondents and aid those respondents who claim they are financially unable to bring witnesses to hearings.

**k) Allowing the Panel to Compel an NFA Member to Testify or Produce Documents**

Although NFA Compliance Rule 2-5 requires that each NFA Member and Associate cooperate fully in all NFA proceedings, the Part 3 rules do not have a specific provision allowing a party to compel a Member to appear or produce documents at a hearing. The interest in developing such a rule is more to prevent problems from arising in the future than to correct problems that have arisen in the past. Staff noted in its interviews that a number of SROs have such a rule to prevent a member from claiming that his inability to compel the attendance of a member witness rendered him incapable of defending the charges leveled against him. It could also be helpful to NFA staff to have such a rule so that Members and Associates understand that they can be called to testify or produce records in a proceeding even if they are not named as respondents.

NFA proposes amending its Part 3 rules so that Compliance Rule 3-9 allows the panel to compel an NFA Member or Associate to testify or produce documents at a hearing at the requesting party's expense. Such an order could be requested by any party to the proceeding, but would be at the discretion of the panel. Moreover, the party making the request would have to make a showing of the need for such an order.



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**1) Requiring Settlement Offers to Include Certain Waivers**

Although not all SROs feel the need to completely isolate the settlement process from the adjudicatory process (and, indeed, the Commission itself approves both complaints and settlements), there is concern that respondents not be allowed to use this as an issue on appeal. NFA proposes amending its Part 3 rules so that Compliance Rule 3-11 provides that any proposed settlement must include a waiver of any objection on the part of the respondent to the panel's participation in the settlement process, should the offer be rejected and the case proceed to hearing before that panel. The rule as proposed also requires that settlement offers be submitted to the BCC unless the settlement is proposed less than ten days before a scheduled hearing, in which case it will be presented to the hearing panel.

**m) Allowing the Compliance Department to Petition the Appeals Committee to Review a Decision of a Hearing Panel**

NFA's current rules provide that a decision may come before the Appeals Committee by a respondent filing a written notice of appeal or by the Appeals Committee taking review on its own motion. The Appeals Committee, in fact, recently took review of a BCC decision in response to a petition from the Compliance Department that it do so. NFA proposes formalizing this procedure by amending its Part 3 rules so that Compliance Rule 3-13 provides that the Compliance Department may petition the Appeals Committee to review a decision of the panel. NFA envisions that such a petition would be similar to a petition for writ of certiorari, in that it would be discretionary with the Appeals Committee whether they would grant such a petition from the Compliance Department. Moreover, NFA would not file such a petition except in extraordinary circumstances such as a decision issued by one panel which is at odds with a decision issued by another panel.



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**B. Explanation of proposed amendments to NFA Code of Arbitration, Sections 1, 2, 4, 5, 6, 8, 9, 10, 11, 12, 16 and 18 and NFA Member Arbitration Rules, Sections 1, 2, 3, 4, 5, 7, 8, 9, 10, 11, 12 and 16:**

**1) CROSS-CLAIMS AND THIRD-PARTY CLAIMS**

NFA proposes amendments to Sections 1, 2, 5, 6, 8, 9, 10, 11, 12, 16 and 18 of its Code of Arbitration and Sections 1, 2, 4, 5, 7, 8, 9, 10, 11, 12 and 16 of its Member Arbitration Rules to provide for the adoption of procedures for third-party and cross-claims.

The third-party claim procedure will allow a respondent, acting as a third-party claimant, to bring into the arbitration a person not a party to the action who is or may be liable for all or part of the original claim. To illustrate, if a customer brings an action against a futures commission merchant ("FCM") for churning and a commodity trading advisor ("CTA") was given discretionary authority to trade the customer's account, the FCM may wish to add the CTA as a third party. However, under the current procedures, the FCM respondent has to file a separate claim against the CTA, which then has to be either consolidated with the customer's claim or heard separately. This seems to be an inefficient use of resources for NFA and the parties. Therefore, NFA believes third-party procedures may be beneficial in situations where a claimant does not name all of the respondents necessary to fully dispose of the claim.

The cross-claim procedure will allow a respondent in NFA arbitration to assert a claim against any other respondent named in the proceeding. To illustrate, if an introducing broker ("IB") brings an action against a former associated person ("AP") and his new IB employer for stealing customer lists, the IB respondent may wish to assert a cross-claim against the AP, seeking to indemnify the IB respondent for any amount the arbitrators would award the IB claimant against it. NFA believes that this procedure may be more efficient than having the IB employer file a separate claim for indemnification against its AP.

The rules of other futures and securities arbitration forums, including the NASD, NYSE, CBOT and CME, permit third-party claims and cross-claims. In addition, a report



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recently issued by an American Arbitration Association task force recommended several significant changes to its arbitration rules governing securities disputes, including a suggestion that the AAA securities rules should provide for third-party claims.

**2) ARBITRATOR DISCLOSURES AND PANEL VACANCIES**

**a) Arbitrator Disclosures**

Perhaps the most important factor in arbitration is the quality of the panel. Therefore, NFA goes to great lengths to ensure that the procedures for selecting arbitrators are effective. Staff carefully screens potential panelists for possible conflicts of interest and discloses to each potential arbitrator the names of all the parties to the case, the parties' representatives, and any witnesses that have been disclosed to NFA. A potential arbitrator who feels he has a conflict of interest will be excused. Moreover, an arbitrator is required to disclose any facts and circumstances that might give even an appearance of partiality and, if the appearance of possible partiality is strong, he is excused.

Once the panel has been selected, NFA notifies the parties and provides them with the arbitrators' names, addresses, current business affiliations and recent employment history. If a party knows of any circumstances which might possibly create an appearance of bias or partiality, the party is required to disclose the relationship to NFA. NFA staff will decide whether or not to excuse the arbitrator after reviewing the circumstances.

NFA believes these procedures work well. Even so, incidents relating to the disclosure process do occur from time to time. Any problems which come up generally are a result of the parties' actions and beyond NFA's control. Furthermore, when they do happen, they result in a needless use of resources by NFA and some of the parties.

The following situation illustrates what can happen when a party fails to disclose relevant information to NFA about an arbitrator. After the hearing



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concluded but before the arbitrators began deliberations in an NFA arbitration proceeding, one of the arbitrators learned that the attorney representing the customer had become a client of the arbitrator's law firm after the arbitrator had done his conflicts check but before the hearing began. Upon learning of this relationship, the arbitrator promptly disclosed it to NFA which in turn disclosed the information to the parties. The Member's attorney chose not to challenge the arbitrator. On the other hand, the customer's attorney, who in all likelihood knew of the relationship and failed to make a timely disclosure, challenged the arbitrator's service in this case.

After reviewing the customer's objection, NFA determined that the objection was not sufficient to disqualify the arbitrator once the hearing had already begun. In light of the circumstances, though, the arbitrator decided to recuse himself, leaving only two arbitrators to decide the case. If an arbitrator becomes unavailable after the commencement of the hearing, NFA's rules require NFA to appoint a replacement arbitrator and conduct a re-hearing unless the parties agree to go forward with the remaining two arbitrators. In this case, the customer would not agree to a decision by two arbitrators so NFA was forced to disband the panel and appoint a new panel of arbitrators to re-hear the case.

This incident was particularly frustrating because the entire situation could have been avoided. The untimely disclosure was not the fault of the arbitrator since the customer's attorney was not even a client of his law firm at the time he was appointed to the case by NFA. On the other hand, the customer's attorney knew or should have known well in advance of the hearing of the arbitrator's affiliation with the law firm with which he was a client. When staff sent a letter to the parties informing them that a panel had been appointed, the customer's attorney was provided with information which clearly indicated the name of the law firm the arbitrator was affiliated with. As a result, this information was available to the customer's attorney when he later became a client of the firm. He knew or should have known of the arbitrator's affiliation with the firm with which he was a client, and he should



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have disclosed the relationship to NFA before NFA, the arbitrators and the other party expended time and resources attending the hearing.

NFA procedures worked in this case as far as the panelists were concerned. Unfortunately, the problem occurred in the portion of the disclosure process which is solely within the parties' control. Therefore, the Board determined to amend Section 4 of the Code of Arbitration and Section 3 of the Member Arbitration Rules to ensure that a party cannot, either intentionally or unintentionally, delay a proceeding by failing to timely disclose relevant information about an arbitrator. The amendments as proposed place an express, continuing obligation on the parties and their counsel to identify and raise any ground for objecting to an arbitrator in advance of the hearing. Obviously, NFA would excuse the arbitrator if there is a strong likelihood of bias or the arbitrator may choose to recuse himself. The proposed amendments also make it clear that any party who could have identified and raised an objection in advance of the hearing waives his right to object to an arbitrator based on that information and waives his right to object to the case proceeding with only two arbitrators if a vacancy occurs as a result of the untimely disclosure.

**b) Panel Vacancies**

As illustrated in the case above, a panel vacancy may occur after the commencement of the arbitration hearing. If that happens, NFA arbitration rules provide for NFA to appoint a replacement arbitrator and conduct a re-hearing unless the parties request otherwise. When a vacancy occurs, the parties in some cases agree to go forward with the remaining two arbitrators. However, it is more frequently the case that the parties do not agree to go forward without a full panel, so NFA appoints a replacement arbitrator.

Under the current arbitration rules, if the vacancy is filled, the panel is required to conduct a re-hearing. However, it may not be necessary in every situation for the new panel to re-hear the entire case. For example, it may be sufficient in some cases for the replacement panelist to review the documentary evidence



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and listen to the tapes or read the transcript of the hearing. Therefore, the current procedures may be an inefficient use of resources.

The AAA task force considered this same issue in its recent review of the AAA securities arbitration rules. The task force felt that providing for the cases to be automatically re-heard would often be wasteful and ill-advised. Accordingly, it recommended that the AAA amend its rules governing panel vacancies to give the new panel the discretion to determine whether all or part of any prior hearings should be repeated. NFA agrees that a re-hearing may not be suitable in every case and therefore proposes amending Section 4 of the Code of Arbitration and Section 3 of the Member Arbitration Rules governing panel vacancies and re-hearings to give the newly-reconstituted panel the authority to determine whether all or part of any prior hearings should be repeated.

### 3) MULTIPLE POSTPONEMENT REQUESTS

NFA's arbitration rules provide for a fee to be charged to a party causing an adjournment or postponement of any scheduled oral hearing, though the postponement fee may be waived at the discretion of the arbitrators. Currently, a \$250 fee is charged under the Code of Arbitration and a \$300 fee is charged under the Member Arbitration Rules.

NFA believed that adopting this rule would reduce requests for continuances and substantially aid the orderly resolution of disputes. Unfortunately, assessing the postponement fee has not proved to be a deterrence to parties in some cases. Certain parties involved in NFA arbitration end up requesting multiple continuances, which interferes with NFA's efforts to provide an expeditious forum for resolving disputes. This not only places a drain on NFA, but also on the arbitrators who may be tied up for months on cases where the hearings are repeatedly postponed.

This problem is not unique to NFA arbitration. Both the NASD and NYSE have similar difficulty with multiple continuance requests. However, they responded to the situation by adopting a graduated postponement fee schedule. NFA believes this is a good idea and recommends that we follow the NASD's and NYSE's lead. To reduce multiple requests for



Ms. Jean A. Webb

September 10, 1993

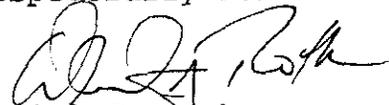
postponements, NFA proposes amendments to Section 11 of both the Code of Arbitration and the Member Arbitration Rules to provide for the adoption of a graduated fee schedule where the cost of each additional request goes up. A party would be charged \$250 for the first request (\$300 in a Member dispute), \$500 for the second request and \$1,000 for each subsequent request. NFA believes that such a rule change will limit the postponement requests in most cases to those that are absolutely essential.

**C. Explanation of proposed deletion of NFA Compliance Rule 2-28:**

On March 30, 1993, the CFTC amended CFTC Regulation 1.55 and adopted a consolidated futures risk disclosure statement which contains the same disclosures required by NFA Compliance Rule 2-28. Deleting Compliance Rule 2-28 will eliminate duplicative disclosure requirements but will not affect NFA's ability to enforce compliance with CFTC disclosure requirements since NFA Compliance Rule 2-30 requires all FCM and IB Members to comply with CFTC Regulation 1.55.

NFA respectfully requests that the Commission review and approve the proposed amendments to NFA Bylaws 702, 704, 707 and 708; Part 3 of NFA's Compliance Rules; NFA Code of Arbitration, Sections 1, 2, 4, 5, 6, 8, 9, 10, 11, 12, 16 and 18, and NFA Member Arbitration Rules, Sections 1, 2, 3, 4, 5, 7, 8, 9, 10, 11, 12 and 16; and the proposed deletion of NFA Compliance Rule 2-28. NFA intends to declare the proposed amendments effective upon Commission approval.

Respectfully submitted,

  
Daniel J. Roth  
General Counsel

DJR:cm(sub/081993)

cc: Acting Chairman Sheila C. Bair  
Commissioner Joseph B. Dial  
Andrea M. Corcoran, Esq.  
Dennis P. Klejna, Esq.  
Alan L. Seifert, Esq.

Susan C. Ervin, Esq.  
Lawrence B. Patent, Esq.  
David Van Wagner, Esq.  
Linda Kurjan, Esq.

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

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

March 24, 1994



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

Re: Proposed amendments to NFA Code of  
Arbitration (§§1, 2, 4, 5, 6, 8, 9, 10,  
11, 12, 16 and 18) and Member  
Arbitration Rules (§§1, 2, 3, 4, 5, 7,  
8, 9, 10, 11, 12 and 16)

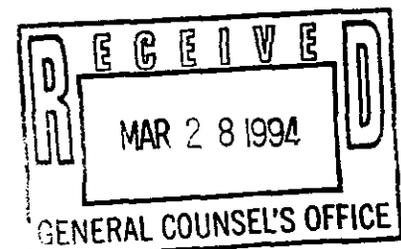
Dear Mr. Roth:

By letter dated September 10, 1993, 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 rule proposals relate to cross-claims and third-party claims, arbitrator disclosures and vacancies, and hearing postponements. Please be advised that the Commission has approved the proposal effective immediately.

Yours truly,

Jean A. Webb  
Secretary of the Commission

CHANGES WILL BE  
IMPLEMENTED ON  
5-1-94



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

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

March 15, 1994



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

Re: Proposed New Bylaw 707; Proposed Amendments  
 to Bylaws 702 and 704 and the Part 3  
 Compliance Rules; and Proposed Deletion of  
 Compliance Rule 2-28--Proposed Disciplinary  
 Procedures and Committee Structure

Dear Mr. Roth:

By letters dated September 10, 1993, and February 14, 1994,  
 the National Futures Association ("NFA") submitted to the  
 Commission the above-referenced proposed new rule, rule  
 amendments and rule deletion pursuant to Section 17(j) of the  
 Commodity Exchange Act.

Please be advised that on this date the Commission has  
 determined to approve the above-referenced proposed new rule,  
 rule amendments and rule deletion pursuant to Section 17(j) of  
 the Commodity Exchange Act.

Sincerely,

*Jean A. Webb*  
 Jean A. Webb  
 Secretary of the Commission

|  |                 |            |                  |
|--|-----------------|------------|------------------|
| Post-It™ brand fax transmittal memo 7671 |                 | # of pages | 1                |
| To                                       | Michael Crowley | From       | Daniel Van Wymer |
| Co.                                      | NFA             | Co.        | CFTC - T&W       |
| Dept.                                    | GEN COUNSEL     | Phone #    | 202-254-8955     |
| Fax #                                    | 312-781-1467    | Fax #      | 202-254-8010     |

March 3, 1994

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

Re: National Futures Association; Proposed Amendments to  
NFA Code of Arbitration, Sections 1, 2, 4, 5, 6, 8, 9,  
10, 11, 12, 16 and 18 and NFA Member Arbitration Rules,  
Sections 1, 2, 3, 4, 5, 7, 8, 9, 10, 11, 12 and 16

Dear Linda:

By letter dated September 10, 1993, National Futures Association ("NFA") submitted proposed amendments to the NFA Code of Arbitration and the NFA Member Arbitration Rules to the Commodity Futures Trading Commission for review and approval pursuant to Section 17(j) of the Commodity Exchange Act, as amended. As we discussed over the telephone today, NFA agrees to extend the time for Commission review and approval of the proposed amendments until March 31, 1994.

Very truly yours,



Kathryn Page Camp  
Associate General Counsel

KPC(letters\Kurjan.5)

February 14, 1994

Via Overnight Delivery

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

Dear Mr. Van Wagner:

I am writing to respond to your inquiries concerning certain portions of the amendments to NFA's rules governing disciplinary proceedings submitted to the Commission on September 10, 1993 for approval.

Hearing Committee and Subcommittee Size, Composition and Powers

You have asked a number of questions concerning the Hearing Committee and its Subcommittees related to size, composition and authority in the context of the obligation to comply with Commission regulations requiring diversity of representation on NFA's disciplinary committees. A number of proposed rules bear on these issues and result in complete compliance with the Commission's regulations.

Proposed Bylaw 708 (pages 3 and 4 of the submission letter dated September 10, 1993) provides that the Hearing Committee will consist of at least fifteen (15) members, at least one of whom shall not be an NFA Member or Associate. Proposed Compliance Rule 3-7 (page 11 of the submission letter) provides that the Chairman of the Hearing Committee may appoint a Hearing Panel consisting of no fewer than three (3) members of the Hearing Committee to conduct the proceedings. This rule also provides that the Hearing Committee as a whole may conduct proceedings, in which case it and its Chairman shall have the same powers as a Hearing Panel and its Chairman.

Proposed Compliance Rule 3-17 (pages 24 and 25 of the submission letter) requires that the Hearing Committee or Hearing Panel conducting a disciplinary proceeding must contain at least one person representing a membership category other than the respondent's membership category. This rule further requires that the Hearing Committee or Panel conducting a proceeding involving a respondent who is an NFA Director or member of the disciplinary committees must contain at least one person who is not an NFA Member or Associate.



David Van Wagner, Esq.

February 14, 1994

Proposed Compliance Rule 3-8(d) (page 13 of the submission letter) authorizes the Chairman of the Hearing Panel or the Panel to schedule a pre-hearing conference. It also authorizes the Hearing Panel to decide which issues may be the subject of a pre-hearing conference conducted by the Chairman acting alone. Similarly, proposed Compliance Rule 3-8(e) (page 13 of the submission letter) provides that the Hearing Panel may decide which motions may be decided by the Chairman acting alone.

The interaction of these rules will provide that no substantive decisions may be made by the Committee, Panels or Chairman in violation of the diversity requirements. The Chairman of the Hearing Committee must appoint Panels which comply with the diversity requirements embodied in proposed Compliance Rule 3-17. The flexibility incorporated in this rule will allow for the Chairman of the Panel to be the non-Member when appropriate. Additionally, the Chairman of the Panel or Committee may schedule a pre-hearing conference but may only conduct the pre-hearing conference with the prior approval of the Panel, the composition of which will meet the diversity requirements. Similarly, the Chairman may only decide those motions which the Panel authorizes.

#### Procedural Rules

Your other questions concern various procedural matters, including details of service requirements, compelling testimony in the form of telephone testimony and the nature of common law privileges which NFA may assert in response to discovery requests.

#### Service Requirements

You have inquired as to the definition of "mail" in connection with the service of pleadings. Proposed Compliance Rule 3-3(b) (pages 6 and 7 of the submission letter) provides that pleadings other than the Complaint must be served by mail or personal delivery with a certificate or an affidavit of service attached. This rule defines mail as depositing in the U.S. Mail, first-class postage prepaid, or with an overnight delivery service, delivery fee prepaid.

As explained in the explanation section of the submission letter (pages 57 and 58 of the submission letter), NFA has experienced some difficulty with service of pleadings by certified mail, return receipt requested, which gives the respondent



David Van Wagner, Esq.

February 14, 1994

complete control over whether to accept such service. The proposed rule, which is similar to the analogous Commission regulation governing service of pleadings in enforcement proceedings, Commission Regulation 10.12, permits the use of regular mail, thereby eliminating the respondent's control. Although NFA's rule does not provide for a defined expansion of time in the case of service by mail, NFA has always utilized a rule of reason in permitting technically late pleadings to be filed by respondents. No respondents have ever been denied the opportunity to file a pleading or have been otherwise prejudiced due to a late filing caused by service-related delays.

You have also inquired regarding whether the Hearing Panel may compel testimony in the form of telephone testimony. Proposed Compliance Rules 3-9(b) and (d) (pages 13 and 14 of the submission letter) address this question. These proposed rules permit the Panel to order telephonic testimony and to compel the testimony of an NFA Member, person connected with the Member or Associate at the expense of the party making the request. There is sufficient discretion contained in these proposed rules to permit the Panel to grant a request to compel testimony and to order that such testimony be given telephonically. The Panel, in exercising its discretion when considering such requests, would be bound to act in a reasonable fashion and consider all relevant circumstances. Such circumstances may include, among others, the costs involved, the convenience of the person compelled to testify and whether the witness's personal appearance is necessary for the Panel to assess the credibility of the testimony.

Your final inquiry related to NFA's assertion of common law and statutory privileges in response to respondents' discovery requests. Proposed Compliance Rule 3-8(b)(iv) (page 12 of the submission letter) provides that a respondent's right to pre-hearing examination of relevant materials does not extend to materials privileged pursuant to common law or statute. The two privileges which have been asserted by NFA in the past and which will undoubtedly form the basis of future assertions of privilege are the attorney-client and the work-product privileges. NFA will assert such privileges to protect confidential internal communications between its attorneys and other staff members and to avoid having to disclose what essentially amounts to its precise legal theories, strategy and analysis in a given case.

The proposed rule specifically states that the investigation report is a privileged document. The investigation report is an example of the type of material subject to the work-product



David Van Wagner, Esq.

February 14, 1994

privilege. It is a document which is created by NFA attorneys for the Compliance Department and contains substantial amounts of legal theories, opinion and analysis. Other types of documents which would be subject to these privileges may include attorney notes, communications between NFA attorneys and the Compliance Department staff working on an investigation and other similar internal memoranda.

NFA staff's assertion of such privileges is not without limit. For example, any document which staff intends to introduce in proving its case must be provided to the respondent prior to hearing pursuant to proposed Compliance Rule 3-8(c). Even with respect to the investigative report, the purely factual material contained in that report will be found in other documents which the respondent is entitled to review before hearing under proposed Compliance Rule 3-8(b).

I hope that this information sufficiently addresses your need for additional information. If you have any questions or require any other information, please do not hesitate to telephone me at (312)781-1388.

Sincerely,

A handwritten signature in black ink, appearing to read 'Michael J. Crowley'.

Michael J. Crowley  
Associate General Counsel

ckm(1tr\vanwag.mjc)



December 15, 1993

CFTC Dismisses Review of  
Proposed Amendments to  
NFA Bylaw 1301  
and New NFA Compliance Rule 3-17

By letter dated December 1, 1993, NFA submitted to the CFTC proposed amendments to NFA Bylaw 1301 to decrease the assessment fee to \$.20 per round-turn futures contract and \$.12 for options transactions. Please be advised that the Commission dismissed review of the proposed amendments. The amendments to Bylaw 1301 and the reduction in assessment fee will become effective on January 1, 1994.

By letter dated September 10, 1993, NFA submitted to the CFTC proposed new NFA Compliance Rule 3-17 entitled "Composition of Committees." Please be advised that the Commission dismissed review of this rule. New NFA Compliance Rule 3-17 became effective on December 10, 1993.

Chris Makino

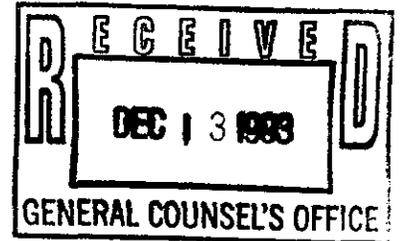


**COMMODITY FUTURES TRADING COMMISSION**

2033 K Street, NW, Washington, DC 20581

(202) 254 - 8955

(202) 254 - 8010 Facsimile



DIVISION OF  
TRADING AND MARKETS

December 8, 1993

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

Re: Proposed New Compliance Rule 3-17, Proposed  
Amendment to Bylaw 515 and Proposed Amendment  
and Renumbering of Bylaw 707 as Bylaw 708

Dear Mr. Roth:

By letters dated September 10, 1993 and November 29, 1993, the National Futures Association ("NFA") submitted the above-referenced proposal to the Commission. NFA's submissions invoked the "ten-day" provision of Section 17(j) of the Commodity Exchange Act ("Act") to permit the above-referenced proposal to become effective ten days after Commission receipt unless the Commission determined to review the proposal for approval and so notified NFA.

Please be advised that the Division of Trading and Markets has examined the above-referenced proposal and has decided to not review the proposal, as provided under Section 17(j) of the Act.

Very truly yours,

John C. Lawton  
Associate Director

November 29, 1993

Via Overnight Delivery

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

Re: National Futures Association: Proposed Amendments to  
NFA Bylaw 515, Proposed NFA Bylaw 708, and NFA Compli-  
ance Rules 2-8 and 2-9

Dear Ms. Webb:

Pursuant to Section 17(j) of the Commodity Exchange Act, as amended, National Futures Association ("NFA") hereby submits to the Commodity Futures Trading Commission ("Commission") proposed amendments to the above-referenced NFA Bylaws and Compliance Rules. The proposed amendments were approved by NFA's Board of Directors on November 18, 1993. By letter dated September 10, 1993, NFA submitted to the Commission for its review and approval proposed NFA Bylaw 708 (formerly NFA Bylaw 707). NFA hereby withdraws proposed NFA Bylaw 708 from that submission and herein resubmits it.

Unless the Commission notifies NFA within ten days after receipt of this letter by the Commission that the Commission has determined to review the amendments for approval, NFA intends to make the amendments to NFA Bylaws 515 and 708 effective ten days after receipt of this submission by the Commission and to make amendments to NFA Compliance Rules 2-8 and 2-9 effective upon the effective date of the revisions to the disciplinary rules submitted to the Commission by letter dated September 10, 1993.

- A. Proposed Amendments to NFA Bylaw 515, Proposed NFA Bylaw 708, and NFA Compliance Rules 2-8 and 2-9 (additions are underscored and deletions are bracketed):

BYLAWS  
OF  
NATIONAL FUTURES ASSOCIATION

\* \* \*

CHAPTER 5

BOARD OF DIRECTORS

\* \* \*



Ms. Jean A. Webb

November 29, 1993

Bylaw 515. Qualifications of Directors.

- (a) No individual shall be eligible to serve as a Director if such person:
  - (i) is subject to any of the disqualifications set forth in CFTC Regulation 1.63(b);
  - (ii) has been convicted of a felony within the prior ten years; or
  - (iii) is subject to a Member Responsibility Action or Associate Responsibility Action which is currently in effect.
- (b) In the event that a Director becomes disqualified after election to the Board, the vacancy shall be filled as prescribed by Article VII, Section 8. If the sanction is stayed or overturned on appeal before the vacancy is filled, the Director shall be entitled to resume his seat on the Board.
- (c) NFA shall publish a list of those Rules which, if violated, would [not] constitute a disciplinary offense as defined in CFTC Regulation 1.63(a) ([4]6) (i).

\* \* \*

CHAPTER 7

COMMITTEES

\* \* \*

Bylaw [707] 708. Qualifications of Members of [Regional Business Conduct] Committees.

- [(a)] No individual shall be eligible to serve as a member of [a Regional Business Conduct] any NFA Committee if such person:
  - [(i)] (a) is subject to any of the disqualifications set forth in CFTC Regulation 1.63(b);
  - [(ii)] (b) has been convicted of a felony within the prior ten years; or



Ms. Jean A. Webb

November 29, 1993

[(iii)] (c) is subject to a Member Responsibility Action or Associate Responsibility Action which is currently in effect.

\* \* \*

COMPLIANCE RULES

\* \* \*

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

\* \* \*

Rule 2-8. DISCRETIONARY ACCOUNTS

\* \* \*

(d) Minimum Experience Requirement.

No Member FCM or Introducing Broker shall allow an Associate to exercise discretion over a customer's commodity futures account 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. This requirement shall not apply to any individual registered as a Commodity Trading Advisor. 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] three members of the Business Conduct Committee and/or the Hearing 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 the 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. An Associate who has been determined to have equivalent experience pursuant to the rules of any contract market member of NFA having a similar minimum experience requirement shall be deemed to have satisfied the requirement of this Rule.

\* \* \*



Ms. Jean A. Webb

November 29, 1993

Rule 2-9. SUPERVISION.

(a) Each Member shall diligently supervise its employees and agents in the conduct of their commodity futures activities for or on behalf of the Member. Each Associate who has supervisory duties shall diligently exercise such duties in the conduct of that Associate's commodity futures business on behalf of the Member.

(b) NFA's Board of Directors may require Members which meet specific criteria established by the Board relating to the employment history of its associated persons to adopt supervisory procedures specified by the Board for the supervision of telemarketing. This requirement may, in NFA's discretion, be waived upon a showing by the Member that the Member's current supervisory procedures provide effective supervision over its employees and agents. Any Member seeking such a waiver may submit a written request to a three-member panel consisting of [one member from each Regional] three members of the Business Conduct Committee and/or the Hearing Committee, said Members to be appointed by the Board from time to time. Within 30 days after a Member submits a waiver request the Compliance Director will submit a written response to the panel. The decision of the panel shall be final and shall be based upon the written submissions of the Member and of the Compliance Director.

**B. Explanation of Proposed Amendments to NFA Bylaw 515, Proposed NFA Bylaw 708, and NFA Compliance Rules 2-8 and 2-9**

As the Commission is aware, CFTC Regulation 1.63 prohibits individuals with a history of recent disciplinary actions (other than those involving minor financial, recordkeeping or reporting violations) from serving on self-regulatory organizations' governing boards, disciplinary committees, and arbitration panels. The Commission recently amended CFTC Regulation 1.63 to broaden committees covered by the rule to include "oversight panels."

NFA Bylaw 515 and proposed NFA Bylaw 708 (formerly Bylaw 707) apply the qualification standards of CFTC Regulation 1.63 to members of the Board of Directors and the Business Conduct and Hearing Committees. Since many NFA committees are subsets of the Board, the only committees not covered by either of these Bylaws are the Advisory Committees. Although the Advisory Committees may not be "oversight panels" for the purposes of CFTC Regulation 1.63, NFA proposes amending NFA Bylaw



Ms. Jean A. Webb

November 29, 1993

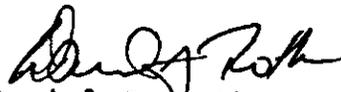
708 so that the qualification standards of CFTC Regulation 1.63 are applied to all NFA committees, thereby eliminating any ambiguity.

CFTC Regulation 1.63(d) required NFA to publish a list of the rules which can be violated without resulting in a disqualification, and this requirement was added to NFA Bylaw 515. The recent amendments revised CFTC Regulation 1.63(d) to require that NFA publish a list of those rules which do result in a disqualification if violated and changed a subsection number which was referenced in NFA Bylaw 515. Therefore, NFA proposes corresponding amendments to NFA Bylaw 515.

Finally, the discretionary review panel authorized by NFA Compliance Rule 2-8 (to grant waivers of the two-year experience requirement for exercising discretion over accounts) and the telemarketing review panel authorized by NFA Compliance Rule 2-9 (to grant waivers of the taping requirements imposed on certain telemarketing firms) are composed of one member of each of the three Regional Business Conduct Committees. Since NFA intends to eliminate the Regional Business Conduct Committees under the new disciplinary committee structure, NFA proposes that NFA Compliance Rules 2-8 and 2-9 be amended to provide that these committees will be composed of three members of the newly constituted Business Conduct or Hearing Committees.

As stated above, NFA intends to make the amendments to NFA Bylaws 515 and 708 effective ten days after receipt of this submission by the Commission unless NFA receives notification that the Commission has determined to review the amendments for approval. NFA intends to make the amendments to NFA Compliance Rules 2-8 and 2-9 effective simultaneously with the disciplinary rules submitted to the Commission for approval on September 10, 1993.

Respectfully submitted,

  
Daniel J. Roth  
General Counsel

DJR:ckm(sub\111993.515)

cc: Acting Chairman Sheila C. Bair  
Commissioner Joseph B. Dial  
Andrea M. Corcoran, Esq.  
Dennis P. Klejna, Esq.

Alan L. Seifert, Esq.  
Susan C. Ervin, Esq.  
Lawrence B. Patent, Esq.  
David Van Wagner, Esq.

October 25, 1993

Mr. John C. Lawton  
Associate Director  
Division of Trading and  
Markets  
Commodity Futures Trading  
Commission  
2033 K Street, NW  
Washington, D.C. 20581

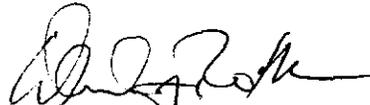
Re: Compliance with CFTC Regulation 1.64(c)

Dear Mr. Lawton:

I have received your October 19, 1993 letter regarding compliance with CFTC Regulation 1.64(c). NFA submitted complying rule amendments to the Commission on September 10, 1993. I direct your attention to Bylaws 702, 704, and 707 and Compliance Rule 3-17 in the enclosed copy of that submission.

If you have any questions, please contact either Kathryn Camp (312-781-1393) or me (312-781-1390).

Very truly yours,



Daniel J. Roth  
General Counsel

Enclosure

KPC(letters\lawton.2)

COMMODITY FUTURES TRADING COMMISSION

2033 K Street, NW, Washington, DC 20581

(202) 254 - 8955

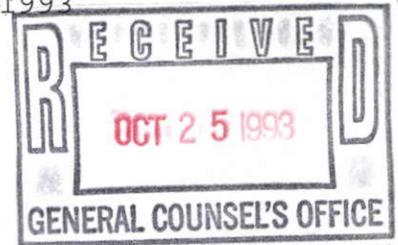
(202) 254 - 8010 Facsimile



DIVISION OF  
TRADING AND MARKETS

October 19, 1993

Mr. Daniel J. Roth  
Vice President, General Counsel  
and Secretary  
National Futures Association  
200 West Madison Street  
Chicago, Illinois 60606



Re: Compliance with Regulation 1.64(c)

Dear Mr. Roth:

As you know, on June 29, 1993, the Commission promulgated a new Regulation 1.64 implementing the statutory directives of Sections 5a, 8c and 17 of the Commodity Exchange Act as they were amended by Section 206 of the Futures Trading Practices Act of 1992 ("1992 Act"). See 58 Fed. Reg. 37644 (July 13, 1993). Among other things, Commission Regulation 1.64 established various composition standards for self-regulatory organization ("SRO") governing boards and major disciplinary committees and required that responsive SRO rule changes be submitted to the Commission and allowed to become effective by October 13, 1993.

As of this date, it appears that the National Futures Association ("NFA") has not met the requirements of Commission Regulation 1.64(c) regarding major disciplinary committee composition. The NFA should promptly submit to the Commission rules complying with the requirements of Regulation 1.64(c). If the NFA has existing rules which satisfy these requirements, it should so inform the Commission.

If you have any questions, please call David Van Wagner at (202) 254-8955.

Very truly yours,

John C. Lawton  
Associate Director