



NFA Regulatory Requirements

For FCMs, IBs, CPOs, and CTAs

January 2016 Revisions: Updated to reflect the amendments to NFA's Financial Requirements Section 1 and 16, and its related Interpretive Notice to conform NFA's requirements with the CFTC's rulemaking, *Enhancing Protections Afforded Customers and Customer Funds held by FCMs and DCOs*.

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Table of Contents

General Regulatory Requirements	1
Basic Records	1
Customer Statements	2
Customer Orders	2
Operations and Activities of IBs	3
Position Limits	3
Reportable Positions	3
Doing Business with Non-Members	3
Customer Information and Risk Disclosure	5
Anti-Money Laundering Program	6
Privacy Rules	14
Customer Protection	15
Risk Management Program	16
Public Disclosures by FCMs	16
Discretionary Accounts	17
Disclosure of Costs Associated with Futures Transactions	17
Ethics Training	18
Business Continuity and Disaster Recovery Planning	18
General Supervision	19
Chief Compliance Officer	22
Accounting for FCMs and IBs	23
Financial Requirements	23
Required Accounting Records	25
Financial Reporting	25
Subordinated Loan Agreements	27
Segregation Requirements	28
Margins	31
Requirements for a Guarantee Agreement	32
Termination of a Guarantee Agreement	32
Accounting for Commodity Pools	34
Required Accounting Records	35
Financial Statements	37
Reports to Pool Participants	40
Quarterly Reporting Requirements	42
NFA Examinations	43

How to Prepare for an Examination	44
After the Examination	44
Appendix A: Securities Haircuts	46
Appendix B: Anti-Money Laundering Questionnaire	49
Appendix C: Business Continuity and Disaster Recovery Questionnaire	57
Appendix D: Ethics Training Policy Questionnaire	59
Appendix E: Privacy Policy Questionnaire	60
Sources of Additional Information	62

General Regulatory Requirements

This guide is an overview of the regulatory requirements that apply to NFA FCM, IB, CPO and CTA Members; it is not an in-depth discussion. Although the guide is intended to offer useful and practical information, it should not be used as a substitute for reading NFA's Rules. If any of the information in this guide is inconsistent with NFA's Rules—which could occur due to Rule changes taking place after this book has been printed—the Rules are the final word. This guide also does not cover those Rules that apply to security futures products. Those rules are discussed in NFA's "Security Futures Products: A Regulatory Guide" located on NFA's website.

Basic Records

Every FCM and IB registered or required to be registered with the CFTC must maintain, and have available for inspection, certain records that support and explain its activities. Such records must be maintained in an orderly fashion at the FCM's or IB's main business.

All required books and records must be kept for five years and must be readily accessible for the most recent two years of the five-year period. Members are allowed to store most required records on either micro-graphic (e.g., microfilm, microfiche and other similar media) or electronic storage media (i.e., any digital storage medium or system that preserves in a permanent format, indexes the data and records the data's date and can be converted to hard copy immediately) for the entire five-year maintenance period. However, trading cards and customer order tickets must be retained in hard copy form for the above required time period.

FCMs must maintain their books and records in an office located in the U.S. or in a Part 30 jurisdiction (e.g., Great Britain, Canada) if it is subject to regulation there. The office must be supervised by a person who is a listed principal and registered associated person present in that office. FCMs that maintain their books and records in a Part 30 jurisdiction are required to reimburse NFA for any additional travel and other expenses incurred travelling to the foreign jurisdiction.

FCMs and IBs are also required to prepare financial and other required reports in English, using U.S. dollars and U.S. accounting standards. FCMs and IBs must also maintain a general ledger in English using U.S. dollars.

All documents filed with NFA by NFA Members must be in English. All Members are also required to maintain English translations of foreign-related promotional material, maintain required procedures in English and provide English translations when NFA requests. NFA Members must also ensure that an English-speaking individual who is knowledgeable of the firm's business is available to assist NFA during an exam.

Customer Statements

Daily and monthly trade confirmation statements sent to customers must identify the FCM, and where applicable, indicate that the account is introduced and identify the IB introducing the account. If more than one IB will receive per-trade compensation on an account, the IB primarily involved in the order flow should be disclosed to the customers. The FCM is required to keep these statements, but NFA recommends that the IB also keep a copy.

An FCM can forward daily and monthly trade confirmations by means of electronic media to any customer who consents to delivery by that method, subject to certain conditions. Electronic media encompasses facsimiles, electronic mail, Internet websites and computer networks. The customer consent must contain sufficient information about the following:

- the electronic medium or source through which the statements will be delivered;
- the period through which the consent will be effective;
- the statements that will be delivered electronically;
- the costs, if any, charged to the customer to deliver statements via electronic medium; and
- a statement that gives the customer the right to revoke at any time the consent to receive statements by electronic medium.

For customers who are deemed “eligible customers,” a consent can be oral, by means of electronic medium or hard copy. The FCM should document the consent with a written confirmation and retain it as part of its records. Eligible customers include any person who: 1) is an eligible swap participant as defined by CFTC Regulation 35.1(b)(2); 2) is an institutional customer as defined by Federal Reserve Board Rule 225.2(g); or 3) is a Commission registrant. For “non-eligible” customers, the FCM must maintain the customer’s signed, hard-copy, revocable consent prior to transmission of any statements electronically.

Customer Orders

At the time an order is received, the FCM must time-stamp the order and note the account number and order number. Option orders must also be time-stamped upon transmittal for execution. Any IB involved in placing a customer order must make and keep the same written record of the order. If the account is an introduced account, but the IB is not involved in placing an order for the customer (e.g., the customer calls the FCM directly or a CTA has discretionary authority over the account and the CTA calls the FCM directly), then the IB is not required to make or keep a written record of the order.

A journal or record must be kept which shows, for each day, all commodity transactions executed for both futures and options. For IBs, the name of the carrying FCM must also be shown. A listing of daily trades received from the FCM is considered to be an acceptable record if it includes date, price, quantity, market,

commodity, contract month and the person for whom the transaction was made. For options, the put, call, strike price, premium, mark-up, commission and fees are acceptable.

Again, an exception is made for this requirement in the case of the IB who refers a customer to an FCM but is not involved in the order flow, though the IB may render advice, etc., to the customer. An IB who does not place orders for a particular customer would not be required to keep this journal for that customer. An IB who does place some orders for a particular customer would be required to keep a journal for all trades but would not be required to have the order ticket for orders which the IB did not place.

Operations and Activities of IBs

IBs must carry all accounts, including customer, proprietary and foreign futures, with an FCM on a fully disclosed basis. Accounts of customers of guaranteed IBs must be carried by the guarantor FCM.

IBs are also prohibited from accepting customer funds in the name of the IB. An IB may, however, accept checks made out in the name of the FCM if the FCM gives the IB written authorization to do so and the checks are forwarded to the FCM or deposited in a qualifying bank account on the day the checks are received. The IB must maintain this written authorization on file.

In order for a bank account to be a qualifying bank account, the account must be in the name of the FCM, must be titled "customer segregated funds" and must only allow the FCM to withdraw from the account. The FCM must obtain an acknowledgment from the bank stating the bank was informed that the account is a customer-segregated account.

Position Limits

Many futures and options contracts are subject to limits on the number of contracts that may be held or controlled by any one person. Certain limits are set forth in Part 150 of CFTC Regulations, while others are set by the exchange where the contract is traded. FCMs and IBs should be aware of these limits in order to properly monitor the positions of their customers as well as their own positions.

Reportable Positions

Part 15 of CFTC Regulations sets forth requirements for reporting "special accounts" to the CFTC. A "special account" is any account which has a reportable position as defined in Part 15. The quantities of each contract, which have been fixed for reporting, are listed in CFTC Regulation 15.03. FCMs must report to the CFTC and NFA any account in which the positions equal or exceed limits.

Doing Business with Non-Members

Mandatory membership in NFA is the cornerstone of NFA's regulatory structure. A meaningful and effective industry-wide self-regulatory organization would be impossible unless all persons required to be registered as FCMs, IBs, CPOs and

CTAs were required to be Members. NFA Bylaw 1101 prohibits Members from conducting customer business with non-Members unless such non-Member is notice-registered with the Commission as an FCM or IB and the account, order or transaction involves only security futures products.

Though it would be impossible to describe all of the situations which should put a Member on notice that a person is required to be a Member of NFA, there are certain minimal steps a Member should take to reduce the possibility of violating NFA Bylaw 1101.

- 1) FCM Members should ensure that all omnibus accounts they carry are held by FCM Members of NFA.
- 2) Each Member should review the list of CFTC registrants with which it does business to determine if they are NFA Members. This review can be done through BASIC (Background Affiliation Status Information Center), which is accessible through NFA's website. BASIC contains Commodity Futures Trading Commission registration and NFA membership information, as well as futures-related regulatory and non-regulatory actions contributed by NFA, the CFTC and the U.S. futures exchanges.
- 3) Each Member should review its list of customers and, if there is any indication that a customer may be engaged in the futures business, the Member should inquire as to its registration and membership status.
- 4) NFA Compliance Rule 2-8(d) requires Members who accept an order from a third party who is not an Associate of the Member to first obtain a copy of the account controller's written trading authorization or a written acknowledgment from the customer that this authorization has been given. The Member should check the account controller's membership status. If the account controller claims to be exempt from registration as a CTA, the Member should determine whether the exemption claim on its face is valid.
- 5) If any customer is operating a commodity pool but claims to be exempt from registration as a CPO, the Member should verify that the customer has made the required filings with the CFTC and NFA.
- 6) Members should monitor deposits to customer accounts to ensure they are received from customers and not third parties.
- 7) Members should ensure that their branch offices are doing business in the name of the Member and are not separately incorporated entities. Branch offices which are separately incorporated are required to be registered as IBs.
- 8) If a foreign broker with whom the Member does business solicits U.S. customers for transactions on U.S. exchanges, the Member should ensure the foreign broker is an NFA Member.

Customer Information and Risk Disclosure

NFA Compliance Rule 2-30 requires each Member or Associate soliciting all individual customers and any other customers who are not eligible contract participants to obtain certain information about each customer and to provide disclosure of the risks of futures trading in light of that information at or before the time the customer opens an account. The basic risk disclosure statements for futures, options, security futures products and non-cash margins must at a minimum be provided to the customer.

The rule provides that Members or Associates must collect certain information from all customers and more specific types of information depending on whether the customer is an individual or not. Members or Associates are required to obtain from all customers at least the customer's true name and address, principal occupation or business, an indication of the customer's previous investment and futures trading experience and any other information deemed appropriate by a Member or Associate to disclose the risks of futures trading. Furthermore, if the customer is an individual, the Member or Associate must also obtain the customer's current estimated annual income and net worth and the customer's approximate age or date of birth. In those cases where the customer is not an individual, the Member or Associate is also required to obtain the customer's net worth or net assets and current estimated annual income or where not available, the previous year's annual income.

In addition, a Member or Associate must obtain from each customer who is an individual if the customer trades security futures products whether the customer's account is for speculative or hedge purposes, employment status, estimated liquid net worth, marital status and number of dependents and such other information used or considered in making recommendations to the customer.

The rule further requires that for an active customer who is an individual the FCM Member carrying the customer account shall contact the customer, at least annually, to verify that the information previously obtained from that customer remains materially accurate, and provide the customer with an opportunity to correct and complete the information. Whenever the customer notifies the FCM Member carrying the customer's account of any material changes to the information, a determination must be made as to whether additional risk disclosure is required to be provided to the customer based on the changed information.

If another FCM or IB introduces the customer's account on a fully disclosed basis or a CTA directs trading in the account, then the carrying FCM must notify that Member of the changes to the customer's information. The Member or Associate who currently solicits and communicates with the customer is responsible for determining if additional risk disclosure is required to be provided based on the changed information. In some cases, this may be the Member introducing or controlling the account; in other cases, it may be the carrying FCM.

The Member or Associate is entitled to rely on the customer for information. If the customer declines to provide the information required under NFA Compliance Rule 2-

30, the Member may still agree to open the trading account, but only if the Member or Associate makes a record that the customer declined and only with the approval of a partner, officer, director, branch office manager or supervisory employee of the Member. If an account is intended to trade security futures products, this account must be approved or disapproved in writing by a designated security futures principal.

Under NFA Compliance Rule 2-30, once a Member or Associate "knows the customer," appropriate disclosures of the risks of futures trading must be made to the customer. The required risk disclosure must be supplemented by whatever additional disclosures may be necessary in a particular instance including, in appropriate cases, information that makes clear that futures trading is too risky for that particular customer. Once that has been done, and the customer has been given adequate risk disclosure, the customer is free to make the decision whether to trade futures (other than security futures) and the Member is permitted to accept the account. Members and Associates, however, are prohibited from making individualized recommendations to any customer for which the Member or Associate has or should have advised that futures trading is too risky for that customer.

The rule recognizes that the identification of customers who require additional risk disclosure can only be done on a case-by-case basis and that the determination of whether additional risk disclosure is required for a given customer is best left to the Member. The rule does not require Members to provide their APs with any sort of grid-like formula to identify those customers who require additional risk disclosure; however, it does require that a Member be able to articulate the general factors its APs are instructed to consider in determining whether additional risk disclosure is required.

Additional guidance on the Interpretation of Compliance Rule 2-30 may be gained from decisions of NFA's Business Conduct Committee (BCC). The most serious violations of the rule have involved either failing to provide additional risk disclosures when necessary or inducing customers to provide false information on their account opening forms. Though risk disclosure is the heart of the rule, certain recordkeeping and supervisory requirements are also imposed.

Anti-Money Laundering

The *International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001* (Title III), which was signed into law on October 26, 2001, imposes significant anti-money laundering requirements on all "financial institutions," as defined under the Bank Secrecy Act ("BSA"), including FCMs and IBs. In particular, Section 352 of Title III requires all financial institutions to establish an anti-money laundering program by April 24, 2002. CPOs and CTAs are also defined as "financial institutions" under the BSA; however, the Secretary of Treasury has deferred applications of these requirements for an unspecified period. Consequently, NFA adopted NFA Compliance Rule 2-9(c) to impose AML requirements on NFA Member FCMs and IBs. For further assistance in drafting an anti-money laundering program, see Appendix B.

NFA also issued an interpretive notice (i.e., 9044) to NFA Compliance Rule 2-9, which specifically highlights certain minimum standards that must be a part of any adequate program and provides Members with additional guidance on satisfying the requirements of NFA Compliance Rule 2-9(c). Although Members may tailor the anti-money laundering program based on the Member's type of business, size and complexity of its operations, breadth and scope of its customer base, number of firm employees and firm's resources, any adequate program must include certain key components. These key components include policies, procedures and internal controls; a designated compliance officer; an employee training program and an independent audit function to test the adequacy of the anti-money laundering program.

Developing AML Policies, Procedures and Internal Controls

Policy Statement

The Member should adopt a policy statement that clearly outlines the following:

- The firm is against money laundering and is committed to following all applicable laws and regulations to ensure its business is not used to facilitate money laundering.
- All employees are required to follow the firm's anti-money laundering procedures.
- Consequences of not following the anti-money laundering procedures.

Customer Identification Program

FCM and IB anti-money laundering programs must include a written customer identification program (CIP). The CIP must include procedures that enable the FCM or IB to form a reasonable belief that it knows the true identity of the customer. The CIP must specify the identifying information that the FCM or IB will require from its customers and the methods (documentary, non-documentary, combination of both) that it will use to verify the customer's identity. The CIP must include procedures related to recordkeeping, comparing customers to certain government lists, notifying customers that the firm is seeking information to verify their identity and, if applicable, relying on other firms to conduct the CIP.

At a minimum, the CIP must require the FCM or IB to obtain the customer's name, customer's date of birth and residential or business address (for individuals) or customer's principal place of business, local office or other physical location (for non-natural persons). The CIP must also require that the FCM or IB obtain the customer's social security number or taxpayer identification number for U.S. persons. For non-U.S. persons, the CIP must require that that FCM or IB obtain some type of government issued document evidencing nationality or residence and bearing a photograph or similar safeguard, such as a passport or alien identification card. For non-U.S., non-natural persons, the CIP must require the firm to obtain a government issued identification number.

Each firm's CIP should identify the documents that will be used for documentary verification, and firms are encouraged to obtain more than one document. The CIP should also identify the types of non-documentary methods the firm will use and the circumstances where these methods will be used.

The firm's CIP should also include a mechanism to identify potentially high-risk accounts in the account opening process. FCMs and IBs should consult the Financial Action Task Force's (FATF) Public Statements of jurisdictions with strategic anti-money laundering and combating the financing of terrorism deficiencies (AML/CFT) to determine whether a customer is from one of those countries or territories, and if so, what additional due diligence must be done before opening the account and what additional monitoring should be done if the account is accepted.

FCMs and IBs should also consult the Office of Foreign Assets Control (OFAC) lists of blocked persons, restricted countries and specially designated nationals. Firms should consult these lists both in the account opening process and throughout the life of the account.

An FCM and IB may share a customer relationship with other FCMs or IBs. In those situations, it may be appropriate for one of those FCMs or IBs to be responsible for all or part of the identification and verification process. An FCM or IB may use another FCM or IB to conduct some or all of the CIP in one of two ways. The FCM or IB may enter into a reliance agreement with the other FCM or it may enter into an allocation agreement with the FCM or IB or third party service provider.

An FCM or IB may rely on another FCM or IB and not be held responsible if the other FCM or IB does not fulfill its responsibilities under the following circumstances: (1) the reliance is reasonable under the circumstances; (2) the other FCM or IB is subject to an AML compliance program under the Bank Secrecy Act; and (3) the other FCM or IB enters into a contract requiring it to certify annually to the FCM or IB that it has implemented an AML program and that it will perform the specified requirements of its own CIP.

An FCM or IB may also delegate some or all of CIP implementation to another FCM or IB or third party service provider. The FCM or IB should have a written agreement with the other entity outlining the other entity's responsibilities. The FCM or IB, however, remains responsible for assuring that compliance with the CIP requirements and therefore should monitor the delegation.

The focus of the CIP procedures is different from the focus of NFA Compliance Rule 2-30. Rule 2-30 applies only to accounts owned by individuals and requires a Member to obtain sufficient information to provide adequate risk disclosure. In contrast, Rule 2-9 procedures apply to all accounts and are focused on learning the true identity of the account owner.

Detecting and Reporting Suspicious Activity

A Member's anti-money laundering program must include systems and procedures

designed to detect and require reporting of suspicious activity. A Member's procedures should specify how it will monitor for this activity. Examples of suspicious transactions are those that have no business or apparent lawful purpose, are unusual for the customer, or lack any reasonable explanation. A Member's familiarity with customer's business practices and trading activity and patterns will assist a firm in identifying activity that is unusual or inconsistent with a customer's practices. In addition, firms should provide employees with examples of behavior or activity that should raise a "red flag" and cause further inquiry. Each firm's program must require employees to promptly notify identified firm personnel of any potential suspicious activity. The appropriate supervisory personnel must evaluate the activity and decide whether a suspicious activity report should be filed with FinCEN.

FCMs and IBs are required to file form SAR with FinCEN to report suspicious transactions that are conducted, or attempted by, at, or through an FCM or IB, involve an aggregate of at least \$5,000 in funds or other assets, and the FCM or IB knows, suspects or has reason to suspect that the transaction or pattern of transactions:

- Involves funds that come from illegal activity or are part of a transaction designed to conceal that the funds are from illegal activity;
- Is designed, such as through structuring, to evade the reporting requirements of the BSA;
- Does not appear to serve any business or apparent lawful purpose; or
- Involves the use of the FCM or IB to facilitate a criminal transaction.

Generally, a SAR is due within 30 days after the firm becomes aware of the suspicious transaction. A copy of the SAR and all supporting documentation must be maintained for five years from the date the SAR was filed.

In most cases, FCMs and IBs are prohibited from disclosing that a SAR was filed, or any information that would reveal the existence of a SAR to the person involved in the transaction, as well as any other persons except as specifically authorized by regulation. Firms should develop additional risk-based measures to help ensure the confidentiality of SARs, including limiting access to a "need-to-know" basis, establishing restricted areas for reviewing SARs, maintaining a log of access to SARs, as well as other protective measures. Firms should also consider including information on SAR confidentiality and the penalties associated with unauthorized disclosure in its ongoing training.

If more than one FCM and/or IB is involved in a particular transaction, the firms may file one form provided that the form contains all the relevant information. The firms may also share information, including the form itself, in order to complete and file a single SAR. FCMs and IBs may also share information, including the SAR itself, with parent entities for the purpose of the parent entity fulfilling its obligation to review

compliance by its subsidiaries in meeting the legal requirements to identify and report suspicious activity. FCMs and IBs must have a written confidentiality agreement or other arrangement in place specifying that the parent entity (or entities) must protect the confidentiality of a SAR through appropriate internal controls.

FCMs and IBs may share a SAR, or any information that might reveal the existence of a SAR, with an affiliate, provided the affiliate is subject to a SAR regulation issued by FinCEN or another regulatory agency. The affiliate may not share the existence of a SAR, or any information that would reveal the existence of that SAR, with another affiliate, even if that affiliate is subject to a SAR rule. In addition, the FCM or IB, as part of its internal controls, must have policies and procedures in place which ensure that its affiliates protect the confidentiality of the SAR.

In the event an FCM or IB receives a request from an authorized law enforcement agency to keep open an account that has suspicious activity, FinCEN recommends that the firm ask for a written request from the law enforcement agency. This request should be issued by a supervisory agent or by an attorney within a U.S. Attorney's Office or the Department of Justice. If the request is made by a state or local law enforcement agency, the request should be from a supervisor of the state or local law enforcement agency or from an attorney within a state or local prosecutor's office. The request should indicate that the agency requested that the firm maintain the account and the purpose of the request. The request should also indicate the duration of the request, not to exceed six months; however, law enforcement may issue a subsequent request for a longer duration. FinCEN also recommends that the FCM or IB maintain the request for five years after the request has expired.

Section 314(a) Information Request

FCM Members are required to develop procedures to access and respond to FinCEN's 314(a) biweekly lists that are published on FinCEN's website. These lists identify individuals, entities or organizations that are suspected by various law enforcement agencies of engaging in money laundering or terrorist financing. FCMs are required to access FinCEN's website to obtain the most recent lists and search their records for any current accounts and accounts maintained by a named subject during the preceding 12 months and for transactions conducted by the named subject within the preceding 6 months. The firm must report any matches to FinCEN within 14 days of the list being posted on FinCEN's website. For matches involving introduced accounts, FCMs should inform FinCEN or the appropriate law enforcement agency. FCMs are not required to respond to FinCEN if no matches are found. At a minimum, FCMs should maintain the following records: a record of the date of request, the tracking numbers within the request and the date the request was searched; and the date the match was reported to FinCEN (if applicable). FCMs must ensure that FinCEN's requests are kept confidential.

FCMs are required to designate a point of contact (POC) person(s) to handle matters involving 314(a) and provide NFA with that information. Any changes to the firm's POC information must be immediately reported to NFA.

Foreign Correspondent and Private Banking Accounts

FCMs and IBs are required to establish due diligence programs for correspondent accounts established or maintained for foreign financial institutions and private banking accounts established or maintained for non-U.S. persons.

FCMs and IBs must establish appropriate, specific and risk based procedures and controls that will allow the firm to reasonably detect and report, on an ongoing basis, any known or suspected money laundering activity conducted through or involving a correspondent account of a foreign financial institution.

In determining the appropriate procedures, FCMs and IBs should consider a number of factors. These factors include: (1) the nature of the foreign financial institution's business and the markets it serves; (2) the type, purpose and anticipated activity of the correspondent account; (3) the nature and duration of the firm's relationship with the foreign financial institution; (4) the anti-money laundering and supervisory regime in which the foreign financial institution is chartered or licensed; and (5) information known or reasonably available to the firm about the foreign financial institution's anti-money laundering record. In addition, the firm's procedures should require the FCM or IB to conduct a periodic review of the activity in the correspondent account.

FCMs and IBs are required to apply enhanced due diligence measures to correspondent accounts maintained for a foreign bank operating under an offshore banking license issued by a country designated as having AML/CFT deficiencies by FATF, or under a license issued by a country that has been designated by the Secretary of Treasury as a primary money laundering concern and as warranting special measures under Section 311. At a minimum, the firm must take reasonable steps to (1) conduct risk-based enhanced scrutiny of correspondent accounts established or maintained for this type of foreign bank to guard against money laundering and to identify and report suspicious activity, (2) determine whether any such foreign bank maintains correspondent accounts for other foreign banks that enable those other foreign banks to gain access to the foreign bank's correspondent account with the FCM or IB, and if so, to take reasonable steps to obtain information to assess and mitigate the money laundering risks associated with such accounts, and (3) identify the owners of the foreign bank if the bank's shares are not publicly traded, and the nature of the extent of each owner's ownership.

An FCM's and IB's due diligence program should include procedures for situations where the FCM or IB cannot perform the enhanced due diligence, including when the FCM or IB refuses to open an account, suspend transaction activity, file a suspicious activity report or close the account.

Private Banking Rule

FCM and IB anti-money laundering programs must also include policies, procedures and controls that are reasonably designed to detect and report any known or suspected money laundering or suspicious activity conducted through or involving any private banking account that is established, maintained, administered or managed in the U.S. by the financial institution for a non-U.S. person. The

procedures should ensure that FCMs and IBs take reasonable steps to (1) ascertain the identity of all nominal and beneficial owners of a private banking account; (2) ascertain whether any owner of the account is a senior foreign political figure; (3) ascertain the source(s) of funds deposited into a private banking account and the purpose and expected use of the account; and (4) review the activity of the account to ensure that it is consistent with the information obtained about the client's source of funds and with the stated purpose and expected use of the account.

An FCM's and IB's due diligence program must include procedures for enhanced scrutiny of a private banking account where a senior foreign political figure is a nominal or beneficial owner. In addition, the due diligence program should also include procedures for situations where the FCM or IB cannot perform appropriate due diligence with respect to a private banking account, including when the FCM or IB refuse to open the account, suspend transaction activity, file a SAR or close the account.

Office of Foreign Assets Control

FCMs and IBs also have obligations under regulations issued by the Office of Foreign Assets Control (OFAC). FCMs and IBs are currently restricted from engaging in certain transactions with individuals or entities located in countries that are under a sanction program administered by OFAC. If the customer is located in one of these countries, the FCM or IB needs to review the sanctioning document or contact OFAC to determine the breadth of the restrictions. FCMs and IBs are also required to block funds from individuals or entities identified on OFAC's list of Specially Designated National and Blocked Persons (SDN list). If the customer's name appears on this list the firm should immediately notify OFAC. To avoid violating the economic sanctions laws administered by OFAC, FCMs and IBs need to check the OFAC lists for new customers and also recheck their existing customer base against the lists when the lists are updated and new countries or Specially Designated Nationals and Blocked Persons are added to the lists. Otherwise FCMs and IBs risk violating the laws by engaging in prohibited transactions with persons who were not subject to sanction when they became customers, but became subject to sanctions later.

Section 311 of the USA Patriot Act give the Secretary of the Treasury the authority to designate a foreign jurisdiction, institution(s), class(es) of transactions, or type(s) of account(s) as a "primary money laundering concern" and to impose certain "special measures" with respect to such jurisdiction, institution(s), class(es) of transaction, or type(s) of account(s). FCMs and IBs should monitor FinCEN's website (<http://www.fincen.gov/>) for information on foreign jurisdiction(s), institution(s), class(es) of transactions, or type(s) of account(s) that have been designated as a primary money laundering concern and any special measures that have been imposed.

Foreign Bank and Financial Accounts

FCMs and IBs are required to file a Report of Foreign Bank and Financial Accounts (FBAR) if they have a financial interest in, or signature authority over any financial

accounts which exceed \$10,000 in a foreign country at any time during the calendar year. This report must be filed with the Department of Treasury on or before June 30th of the following year.

International Transportation of Currency or Monetary Instruments

An FCM is required to file a Report of International Transportation or Monetary Instruments (CMIR) if the firm physically transports, mails or ships or causes to be physically transported, mailed or shipped an aggregate amount exceeding \$10,000 at any one time from the United States to any place outside of the United States or any place into the United States from outside the United States. A CMIR must also be filed if the firm receives in the United States any currency or other monetary instrument in aggregate exceeding \$10,000 at one time which has been transported, mailed or shipped from outside the United States. A CMIR does not need to be filed, however, if the FCM is a bank or broker-dealer, and the currency or other monetary instrument is mailed or shipped through the postal service or by a common carrier. CMIRs must be filed on or before the date of the shipment and must be filed within 15 days of the receipt of the currency/monetary instruments.

Hiring Qualified Staff

An adequate program for anti-money laundering compliance must ensure that the individuals that staff areas susceptible to money-laundering schemes are trained to work in the areas. A firm may want to perform background checks on key employees to screen employees for criminal and disciplinary histories.

Recordkeeping

A firm's program must also include written requirements for the following: the types of records that should be maintained; where the records should be maintained; and specify that the records must be maintained in accordance with CFTC Regulation 1.31 (i.e., maintained for five years and readily accessible for the first two years). The ultimate goal of the recordkeeping requirements is to provide an audit trail for law enforcement officials investigating money laundering schemes.

Designation of a Compliance Officer

FCMs and IBs are required to designate an individual or individuals to monitor the day-to-day operations and internal controls of its anti-money laundering program. The person may be the compliance officer that is responsible for other compliance areas of the firm but must be independent of functional areas where money laundering could occur. This person does not need to be a designated principal or Associate Member but must ultimately report to senior management.

Employee Training Program

Procedures must be in place to provide ongoing training to those employees who are involved in areas where money laundering could occur. The training program must be provided to appropriate personnel at least annually and include training on the firm's policies and procedures, relevant federal laws and NFA's guidance issued on this topic. Firms should also maintain records to evidence their compliance with this requirement.

Independent Audit Function

A Member must have an independent audit function to test the adequacy of the anti-money laundering program. This must be done at least annually. An internal audit staff or other internal employees independent from the anti-money laundering function, including compliance functions, can perform this review. Also, firms may hire an outside party with experience in this type of auditing. The results of these audits should be documented and reported to the firm's senior management or an internal audit committee or department. If deficiencies are noted, follow-up should be performed to ensure deficiencies are addressed and corrected.

Privacy Rules

All NFA Members must comply with the federal privacy laws and the CFTC's regulations applying those laws to futures firms. The CFTC's regulations restrict a Member's right to disclose non-public personal information about customers and other consumers. A consumer is any individual who obtains financial products or services from the Member primarily for personal, family or household purposes or who applies for those services (but not someone who merely provides name, address and areas of interest in order to receive information on the Member's services). A customer is any consumer with whom the Member has a continuing relationship.

Members must have written policies and procedures that describe their administrative, technical, and physical safeguards for protecting customer records and information. The procedures must be reasonably designed to 1) keep customer records and information secure and confidential, 2) protect against any anticipated hazards to the security or integrity of those records and 3) protect against unauthorized access to or use of the records or information.

Members should also have policies and procedures addressing when it will disclose nonpublic personal information to unaffiliated third parties and how it will notify customers about its disclosure policies. For further assistance in drafting these privacy procedures, see Appendix E on page 56. A Member must provide a customer with a privacy notice when the customer first establishes a relationship with the Member and annually after that. Your firm must also notify other consumers of its privacy policies before disclosing nonpublic personal information about those consumers.

Every Member who solicits or accepts individuals as customers (unless it only solicits or accepts individuals who use its products and services primarily for business purposes) must provide a privacy notice that identifies the categories of nonpublic personal information the Member collects and describes the Member's policies and procedures for protecting that information. This is true even if the Member does not share nonpublic personal information with nonaffiliated third parties.

If your firm does not disclose nonpublic personal information to nonaffiliated third parties, or does so only in very limited circumstances, the only additional information you must include in the privacy notice is a statement that your firm shares nonpublic personal information with third parties as permitted by law. CFTC Regulations

describe the limited circumstances where Members may disclose the information without having to provide a more detailed privacy notice (e.g., when necessary to process a transaction or provide a service to the customer or with the customer's specific consent).

If your firm discloses nonpublic personal information to nonaffiliated third parties for other reasons, the notice must inform the customer that the firm discloses or reserves the right to disclose nonpublic personal information to nonaffiliated third parties and that the customer has the right to opt out of that disclosure. The notice must identify the categories of nonpublic personal information that your firm discloses and the categories of affiliates and non-affiliates to whom your firm discloses the information. The notice must also inform customers that they may opt out of the disclosure and must provide a reasonable means for customers to exercise their opt-out rights.

Members must provide amended privacy and opt-out notices before disclosing information to unaffiliated third parties if either the information or the third party does not fall with a category already identified in the privacy notice.

All privacy and opt-out notices should be in writing. Members may deliver these notices electronically if the customer agrees.

Customer Protection

CFTC regulations establish certain standards which FCMs and IBs must follow in the conduct of their business. An FCM or IB may not represent that it will, in any way, guarantee a person against loss or limit their loss. This does not prohibit the FCM or IB from assuming or sharing a loss caused by an error or mishandling of an order. Also, an FCM or IB is prohibited from claiming that it will not call for, or attempt to collect, the margin required on each contract.

An FCM or IB must give written authorization to any FCM that carries an account for one of its affiliated persons. The carrying FCM must provide copies of statements and orders for affiliated persons' accounts to the FCM or IB.

An FCM or IB must adopt procedures and controls that ensure that orders for proprietary accounts and accounts of affiliated persons are not placed before customer orders which are executable at or near the market. An FCM or IB, or an FCM's or IB's affiliated persons, are prohibited from disclosing that an order of another person is being held by the FCM or IB unless such disclosure is necessary for the effective execution of the order. Also, an FCM or IB, or an FCM's or IB's affiliated person, cannot take the other side of a person's order it knows of because of its relationship with that person.

An affiliated person is defined as any general partner, officer, director, owner of more than 10 percent of the equity interest, AP or employee of the FCM or IB, any relative or spouse of any of the foregoing persons, or any relative of such spouse, who shares the same home as any of the foregoing persons.

An FCM must electronically notify the CFTC and the firm's designated self-regulatory organization (DSRO) of certain events, including material adverse events that could impact the firm's obligations and liquidity; material changes in operations or risk profile; other regulatory matters; and restrictions on omnibus accounts. Certain notices are due immediately while others are due within 24 hours. See [FCM Reporting Requirements](#) for additional details.

Risk Management Program

CFTC Regulation 1.11 requires each FCM that holds customer funds to establish maintain and enforce a system of risk management policies and procedures, known as a Risk Management Program, which is designed to monitor and manage the risks associated with the FCM's activities. Each FCM was required to file its initial Risk Management Program with the Commission by July 14, 2014 and must provide an updated copy upon request. Any FCM applying for registration must file a copy of the Risk Management Program as part of its application.

As part of the Risk Management Program, each FCM is required to provide to its senior management and governing body with a quarterly Risk Exposure Report (RER), as well as interim RERs at anytime the FCM detects a material change in the FCM's risk exposure. The quarterly RERs must set forth all applicable risk exposures of the FCM; any recommended or completed changes to the Risk Management Program; the recommended time for implementing recommended changes; and the status of any incomplete implementation of previously recommended changes. Each FCM is required to submit a copy of the quarterly RER and any interim RERs through WinJammer™ within five business days of providing the report to its senior management.

Additionally, CFTC Regulation 1.15 requires each FCM to electronically file through WinJammer™ an annual Risk Assessment Report containing a copy of the firm's organizational chart, copies of the financial and operational policies, procedures and systems, as well as fiscal year-end consolidated financial statements for certain affiliates. Each FCM must also report any material change in the FCM's organizational chart and/or financial and operational policies and procedures within 60 days after the end of the fiscal quarter where the change occurred.

Public Disclosures by FCMs

CFTC Regulation 1.55(i) requires FCMs to provide a Disclosure Document to each customer prior to opening an account, which discloses all information about the FCM including its business, operations, risk profile, and affiliates that would be material to the customer's decision to do business with the FCM. See CFTC Regulation 1.55(k) for specific topics required to be covered in this disclosure. The FCM must also publicly display the Disclosure Document on its website, and update the Disclosure Document annually and as needed, to keep it accurate and complete. .

FCMs are also required to post certain financial information on its website including:

- The daily segregated, secured, and cleared swap customer collateral computations for the most recent 12-month period;
- The summary schedule of month end net capital, adjusted net capital, and excess net capital for the 12 most recent months;
- The segregated, secured and cleared swaps customer collateral computations included in the firm's 1-FR-FCM for the most current 12-month period; and
- The most current certified financial statement including all applicable footnotes.

Further each FCM's website must contain a link to the CFTC's webpage for financial data—where additional financial information on all FCMs is available—and a link to NFA's BASIC system—where additional information on how it invests and holds customer funds is disclosed.

Discretionary Accounts

NFA Compliance Rule 2-8 contains specific requirements concerning FCM and IB discretionary accounts. First, an AP of an FCM or IB may not exercise discretion over a customer's account unless that AP has been continuously registered and working as an AP for at least two years. Anyone seeking a waiver of this rule must submit a written request to the Compliance Department.

Before an FCM or IB or one of its APs may exercise discretion over an account, the customer (or account controller) must authorize this discretion in writing. The FCM or IB must keep records which clearly show the accounts over which it or its APs have discretion. An officer, partner or branch office manager of the FCM or IB must regularly and diligently review these accounts and make a written record of the reviews. For discretionary security futures trading activity, review must be conducted and documented by a designated security futures principal. In addition, the FCM or IB must have written procedures, which address the supervision and review of discretionary accounts.

An FCM or IB also has a responsibility when that account is controlled by a third party. In such a case the FCM or IB must obtain a copy of the account controller's written trading authorization, or a written acknowledgment from the customer that the authorization has been given.

Any account for which discretionary authority is given to a family member is not subject to these rules except for the requirement that the grant of discretionary authority be in writing.

Disclosure of Costs Associated with Futures Transactions

If fees and charges associated with futures transactions are not determined on a per-trade or round-turn basis, an FCM or IB must provide the customer with a complete written explanation of such fees and charges, including a reasonable example or examples of the fees and charges on a per-trade or round-turn basis. Where the per-trade or round-turn equivalent of the fees and charges may vary widely, the most

appropriate disclosure would be to explain this fact and to provide examples demonstrating the reasonably expected range of the fees or charges.

Ethics Training

The CFTC's Statement of Acceptable Practices requires that all APs and any individuals registered as an FCM, IB, CPO, CTA, FB or FT receive ethics training to ensure they understand their responsibilities to the public under the Act, including responsibilities to observe just and equitable principles of trade, rules or regulations of the Commission, rules of any appropriate contract market, registered futures association, or other self-regulatory organization, or any other applicable federal or state law, rule or regulation.

Registrants must receive ethics training on a periodic basis as needed. Firms should determine the frequency and form of this based on the size of its operation and type of business.

All firms should implement written procedures that outline their ethics training programs. Acceptable procedures will cover the topics that will be included in the training program; who will provide the training; the format of the training; how often the firm expects its employees to obtain ethics training; and how the firm will document that it has followed its written procedures. For further assistance in drafting these ethics training procedures, see Appendix D on page 55.

Topics to be addressed in training should include:

- An explanation of the applicable laws and regulations, and the rules of self-regulatory organizations or contract markets and registered derivatives transaction execution facilities;
- The registrant's obligation to the public to observe just and equitable principles of trade;
- How to act honestly and fairly and with due skill, care and diligence in the best interests of customers and the integrity of the market;
- How to establish effective supervisory systems and internal controls;
- Obtaining and assessing the financial situation and investment experience of customers;
- Disclosure of material information to customers; and
- Avoidance, proper disclosure and handling of conflicts of interest.

Business Continuity and Disaster Recovery Planning

NFA Compliance Rule 2-38 requires each Member to adopt a business continuity and disaster recovery plan reasonably designed to enable it to continue operating, to reestablish operations or to transfer its business to other Members with minimal disruption. A Member's plan should cover all areas that are essential to its business operations and should be tailored to its individual needs. At a minimum, the Member's plan should address the following, as applicable:

- Establishing back-up facilities, systems and personnel that are located in one or more reasonably separate geographic areas from the Member's primary facilities, systems and personnel (e.g. primary and back-up facilities should be located in different power grids and different telecommunication vendors should be used), which may include arrangements for the temporary use of facilities, systems and personnel provided by third parties;
- Backing up or copying essential documents and data (e.g. general ledger) on a periodic basis and storing the information off-site in either hard-copy or electronic format;
- Considering the impact of business interruptions encountered by third parties and identifying ways to minimize that impact; and
- Developing a communication plan to contact essential parties such as employees, customers, carrying brokers, vendors and disaster recovery specialists.
- Each FCM Member must provide NFA with, and keep current, the name and contact information for all key management employees, as identified by NFA, in the form and manner prescribed by NFA. In addition, each FCM Member must provide NFA with the location, address and telephone number of its primary and alternative disaster recovery sites.

In order for a Member's plan to remain effective, the firm must update its plan as necessary to respond to material operational changes. Each Member must also periodically conduct reasonable reviews designed to assess the plan's effectiveness.

Communicating the plan is also essential. Each member should distribute and explain the plan to its key employees plus ensure that all employees are aware of the plan's essential components. The firm should maintain copies of the plan at one or more off-site locations readily accessible to key employees. For further assistance in drafting a business continuity and disaster recovery plan, see Appendix C of this Guide.

General Supervision

NFA Compliance Rule 2-9 places a continuing responsibility on every Member to diligently supervise its employees and agents in all aspects of their futures activities. NFA recognizes that, given the differences in the size and complexity of the operations of NFA Members, there must be some degree of flexibility in determining what constitutes "diligent supervision" for each firm. It is NFA's policy to leave the exact form of supervision to the Member, thereby providing the Member with flexibility to design procedures that are tailored to the Member's own situation. The Board of Directors adheres to this principal but feels that all Members should regularly review the adequacy of their supervisory procedures. In doing so, the Board of Directors has determined that NFA Members must complete, on a yearly basis, a self-examination checklist. This checklist is distributed by NFA's Information Center subsequent to registration or is available on NFA's website.

Other NFA Compliance Rules impose more specific supervisory duties on Members in connection with certain types of activities. For example, Rule 2-8 contains detailed requirements regarding the supervision of discretionary accounts. Rule 2-29(e) requires each Member to adopt and enforce written procedures regarding communications with the public, including advance review and approval of all promotional material by an appropriate supervisory person. Rule 2-30(h) requires each Member to adopt and enforce procedures regarding customer information and risk disclosure.

Supervision of Branch Offices and Guaranteed IBs

NFA has also issued an interpretive notice to NFA Compliance Rule 2-9, which specifically addresses the supervision of branch offices and guaranteed IBs. Though Members may tailor their supervisory procedures to meet their particular needs, any adequate program for supervision must include procedures for performing day-to-day monitoring and surveillance activities, conducting on-site visits of remote locations and conducting ongoing training for firm personnel. The firm's policies and procedures, including those for the supervision of branch offices and guaranteed IBs should be in writing and be on file with each branch office and guaranteed IB.

Day-to-Day Monitoring

On a regular basis, Members should perform a number of supervisory procedures in order to monitor the business being conducted in their remote locations. Repeated problems in any particular area should heighten the level of scrutiny and follow-up by the main office or guarantor. The procedures to review the day-to-day activities of an office should include the following areas.

Hiring

An adequate program for supervision must include thorough screening procedures for prospective employees to ensure they are qualified and to determine the extent of supervision required. The appropriate documentation to support any "yes" answers on the Form 8-R should be obtained and reviewed for potential disqualifying information. Information which applicants may have submitted in connection with any registrations should be obtained from NFA. Although this information is generally treated as non-public information, it is available to prospective employers.

A prospective employer should check with NFA for any futures-related disciplinary proceedings against any AP's prior employers or against the IB. This information should be used by the prospective employer to determine the extent of supervision required.

Due Diligence Check of Guaranteed IBs

Guarantor FCMs must do a due diligence inquiry before entering into a guarantee agreement. The due diligence review must include a check to ensure that the IB is properly registered. The FCM's due diligence review should also include inquiries concerning the disciplinary history of the IB and the disciplinary and employment history of the IB's principals and APs. This type of information could be helpful to a prospective guarantor in determining the types of difficulties, if any, experienced by

an IB, its principals and APs in the past and the extent of supervision which may be required of that IB under a guarantee agreement. Both registration and disciplinary information are readily available from NFA through BASIC.

Registration

Records of commissions payable to or generated by the branch office or guaranteed IB should be broken down by sales person and should be frequently reviewed to ensure that no commissions are being paid to unregistered individuals.

Customer Information

Procedures for opening new accounts should require that the appropriate account documentation be kept by both the main office and the remote location. The documentation should be reviewed to ensure that the appropriate supervisory personnel approved the account and that the customer received the appropriate risk disclosure. It may also be necessary to contact the customer to verify that the disclosure was provided and that the customer understood its meaning.

Account Activity

On a regular basis the trading activity in customer and AP personal accounts should be reviewed and analyzed in order to highlight those accounts which may require further scrutiny. Measures should be taken to follow up, such as reviewing order tickets and trade blotters, discussing the activity with the broker or contacting the customer.

Discretionary Accounts

NFA Compliance Rules contain detailed requirements concerning the supervision and review of discretionary accounts. In addition, the registration history of APs should be reviewed to ensure that they have been properly registered for the requisite two-year minimum.

Promotional Material

All promotional material should be submitted by the branch office or guaranteed IB to the home office or guarantor for review and approval prior to its first use. Review and approval of the material should be documented by the appropriate supervisory personnel.

Customer Complaints

A written record of all customer complaints should be maintained, and complaints which meet certain criteria should be sent to the main office or guarantor who should review the complaints for possible rule violations and for similarity to other complaints which may indicate a pattern of abuse. The status of unresolved complaints should also be periodically reviewed.

On-Site Visits

In addition to day-to-day supervisory procedures, adequate supervision must include periodic on-site inspections. ***As a general matter, NFA expects guaranteed IBs and branch offices to be inspected annually.***

Members should develop written procedures for the on-site review process including detailed steps to be followed during the visit. A Member's supervisory procedures should also address the number of visits to be made to a branch office or guaranteed IB.

Promptly after the completion of an on-site visit, a written report should be prepared and its findings discussed with the branch office managers or guaranteed IB's principals and supervisory personnel. Follow-up procedures should also be performed to ensure that any deficiencies revealed during an on-site visit are promptly corrected.

The written procedures for the on-site examination should include steps to review the following areas:

- Customer Account Files
- Customer Order Procedures
- Discretionary Accounts
- Sales Practices
- Customer Complaints
- Handling of Customer Funds
- Proprietary Trading

Ongoing Training

A Member's supervisory responsibilities include the obligation to ensure that its employees are properly trained to perform their duties. Procedures must be in place to ensure that employees receive adequate training to abide by industry rules and obligations and to properly handle customer accounts. The formality of a training program will depend on the size of the firm and the nature of its business.

Chief Compliance Officer

Each FCM must designate a chief compliance officer (CCO) and that person must be a listed principal of the firm. The CCO is required to prepare the CCO Annual Report, which includes the information outlined in CFTC Regulation 3.3 for the FCM's most recently completed fiscal year. The FCM must provide this report to its Board of Directors or senior officer and electronically file a copy of the report through WinJammer™ within 60 days of the FCM's fiscal year-end.

Although IBs, CPOs and CTAs are not required by CFTC Regulation 3.3 to designate an individual to serve as the firm's CCO, if a firm appoints a CCO, that person must be a listed principal of the firm.

Accounting for FCMs and IBs

This section is not intended to provide an all-inclusive discussion of accounting topics applicable to the operation of an FCM or independent IB. Rather, it is included as a starting point in the discussion of financial requirements and to provide an overview of accounting issues. FCMs and IBs may want to discuss the development and implementation of their accounting system with an independent public accountant or other qualified consultant. Certification by an independent public accountant is required under NFA Rules and CFTC Regulations for the firm's Annual Report. The conditions which impair an accountant's independence are discussed on page 23.

Generally, accounting for an FCM or IB should be the same as for any other type of business. Accounting records should be prepared in accordance with generally accepted accounting principles.

Financial Requirements

The basic calculation an FCM or independent IB must make in order to demonstrate compliance with NFA and CFTC financial requirements is as follows:

$$\text{Current Assets} - \text{Liabilities} - \text{Charges Against Net Capital} = \text{Adjusted Net Capital}$$

While basic accounting terms such as assets, liabilities and ownership's equity are necessary components of an FCM's and IB's accounting system, NFA Financial Requirements and CFTC Regulation 1.17 include further definitions which must be understood in order to properly prepare financial records. For example, the definition of current assets, such as receivables and prepaid expenses, under NFA and CFTC requirements is much more restrictive than under generally accepted accounting principles. Additionally, NFA and CFTC requirements exclude certain items, such as satisfactory subordinated loan agreements, from the definition of liabilities.

NFA and CFTC requirements also define charges against capital, which must be calculated in determining the FCM's or IB's compliance with minimum financial requirements. These charges include deductions based on the market value and time to maturity of securities owned by the FCM or IB, deductions based on any trading done by the FCM or IB for its own account and several other charges. FCMs must also take charges against capital for any under-margined accounts which it carries. See Appendix A on page 36 for a listing of securities charges.

An independent IB must maintain, at all times, adjusted net capital equal to the greater of:

- 1) \$45,000; or
- 2) for Member IBs with less than \$1,000,000 in adjusted net capital, \$6,000 per office operated by the IB (including the main office); or
- 3) for Member IBs with less than \$1,000,000 in adjusted net capital, \$3,000 for each AP sponsored by the IB (including each AP with a temporary

license); or

4) for securities broker-dealers, the amount of net capital required by Rule 15c3-1(a) of the Regulations of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

The minimum capital requirement for an FCM is the greater of:

1) \$1,000,000; or

2) for Member FCMs with less than \$2,000,000 in adjusted net capital, \$6,000 for each remote location (i.e., each proprietary branch office, guaranteed IB main office, and guaranteed IB branch office, including each guaranteed IB and branch office of a guaranteed IB with a temporary license); or

3) for Member FCMs with less than \$2,000,000 in adjusted net capital, \$3,000 for each AP sponsored (including each AP sponsored by a guaranteed IB and each AP with a temporary license); or

4) for securities broker-dealers, the amount of net capital specified in Rule 15c3-1(a) of the Regulations of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)); or

5) eight percent of domestic and foreign customer and non-customer (excluding proprietary) risk maintenance margin/performance bond requirements for all domestic and foreign futures, options on futures contracts and cleared over-the-counter derivative positions excluding the risk margin associated with naked long option positions. This requirement only applies to the FCM carrying the account.

If an FCM guarantees IBs, the FCM also has an eligibility capital requirement set at 150 percent of the greater of the amount calculated in sections 1, 2, 3, 4 or the amount in section 5 above. If its capital falls below the above requirement level, the FCM is subject to additional notice requirements and is prohibited from guaranteeing new IBs.

Any FCM whose capital falls below its minimum capital requirement must immediately give telephonic notice to the CFTC and its DSRO. Any independent IB whose capital falls below its minimum capital requirement must immediately give telephonic notice of that fact to NFA and any FCMs that carry accounts for the IB. Telephonic notice should be confirmed in writing by telegraphic or facsimile notice. An FCM has additional notice requirements when its adjusted net capital falls below the eligibility capital requirement for guaranteeing IBs or when any customer's account becomes under-margined by an amount equal to its adjusted net capital. Certain FCMs also must file written notice when their adjusted net capital decreases by more than 20 percent or their excess net capital decreases by more than 30 percent.

Required Accounting Records

NFA Compliance Rule 2-10 and CFTC Regulation 1.18 specify the minimum accounting records required to be prepared and kept current by an FCM and an independent IB. The FCM or IB must maintain ledgers or other similar records which show or summarize, with appropriate references to supporting documents, each transaction affecting its assets, liability, income, expense and capital accounts. These ledgers must be classified into the account classification subdivisions on the Form 1-FR (CFTC-required financial form) or FOCUS Report (SEC-required financial form). Generally, these records would include basic accounting documents such as a General Ledger and a Cash Receipts and Disbursements Journal.

Additionally, an FCM or independent IB must make and retain a formal computation of its adjusted net capital and minimum financial requirement as of the end of each month. This computation must be completed within 17 business days after the date for which the computation is made. Although a formal computation is required monthly, an FCM or IB must be able to demonstrate capital compliance at all times.

All required books and records must be kept for five years and must be readily accessible for the most recent two years of the five-year period. An FCM which fails to maintain current records must, within 24 hours, send telegraphic notice of that fact to the CFTC and its DSRO. An IB that fails to maintain current records must, within 24 hours, send telegraphic notice of that fact to NFA and any FCMs that carry accounts for the IB.

Financial Reporting

An FCM is required to prepare Form 1-FR-FCM and submit it to NFA and to the CFTC on a monthly basis. Independent IBs which are not securities broker-dealers must prepare and submit a Form 1-FR-IB to NFA and to the CFTC on a semi-annual basis. A Form 1-FR for the FCM's or IB's fiscal year-end must be certified by an independent public accountant. If the FCM or IB is also registered as a securities broker-dealer, a FOCUS Report may be filed in lieu of the Form 1-FR.

Although the Form 1-FR contains a number of different financial statements, it is not always necessary to prepare each statement.

Unaudited Forms 1-FR must contain:

- Statement of Financial Condition
- Statement of the Computation of Minimum Capital Requirements
- Statement of Changes in Ownership Equity
- Statement of Segregation Requirements and Funds in Segregation (FCMs only)
- Statement of Secured Amounts and Funds held in Separate Accounts (FCMs only)

- Statement of Changes in Liabilities Subordinated to the Claims of General Creditors
- Pursuant to a Satisfactory Subordination Agreement (if applicable)

The certified year-end Form 1-FR must also include:

- Statement of Income
- Statement of Cash Flows

The certified statement must also contain any necessary footnote disclosure, the accountant's opinion covering all statements and the accountant's supplemental report on material inadequacies. Financial statements must be received by NFA and the CFTC within a certain time period. For both FCMs and IBs, the unaudited Form 1-FR is due within 17 business days after the statement date. The certified Form 1-FR is due within 60 days after the statement date for FCMs and within 90 days after the statement date for IBs. Securities broker-dealers must file the certified Focus Report within 60 days after the statement date.

All FCMs, as well as IBs that are registered securities broker-dealers, must file their financial statement through WinJammer™, which accommodates filing of Form 1-FR-FCM, FOCUS II and FOCUS IIA Reports. IBs that are not also securities broker-dealers must file all financial statements electronically through NFA's web-based EasyFile system. WinJammer™ and EasyFile also include procedures for the appropriate representative of the NFA Member FCM or IB to attest to the completeness and accuracy of the financial report in order to comply with NFA and CFTC certification and attestation requirements. Each authorized signer using WinJammer™ must complete the User Identification Request Agreement and obtain NFA approval. Each authorized signer using EasyFile must be identified by the firm's manager in NFA's Online Registration System.

Full details about the software and electronic filing procedures are available by accessing the Electronic Filings section of NFA's website at www.nfa.futures.org or by contacting the Information Center at (312) 781-1410. Information also is available on the WinJammer™ website (<http://winjammer.futures.org>).

In order to certify an FCM's or IB's year-end Form 1-FR or FOCUS report, the public accountant must be independent of the FCM or IB. A public accountant is not considered independent if he or his firm has had any material relationship with the FCM or IB. Examples of a material relationship include:

- The public accountant or his firm had, or was committed to acquire, any financial interest or any material indirect financial interest in the FCM or IB; *or*
- The public accountant or his firm was connected as a promoter, under-writer, voting trustee, director, officer, or employee with the FCM or IB (former employees are excepted); *or*

- The public accountant or his firm performs manual or automated bookkeeping or assumes responsibility for maintaining accounting records including making classification decisions for the FCM or IB.

A certified public accountant engaged to certify an FCM's financial statements must be registered with the Public Company Accounting Oversight Board (PCAOB), must have undergone an examination by the PCAOB, and may not be subject to a permanent or temporary bar to engage in the examination of public issuers, brokers or dealers registered with the SEC as a result of a PCAOB disciplinary hearing.¹

Subordinated Loan Agreements

A subordinated loan agreement must be filed with and approved by a firm's DSRO before the proceeds from the loan will be deemed satisfactory for capital purposes. A signed copy of the agreement must be submitted to the firm's DSRO at least 10 days prior to its proposed effective date. For broker-dealers, the FCM or IB must file signed copies of the subordination agreement with both its DSRO and its securities industry designated examining authority (DEA) before the proposed effective date. The FCM or IB also must file copies of the DEA's approval with the DSRO immediately upon receipt.

The subordination agreement must include a statement setting forth the name and address of the lender, the business relationship of the lender to the FCM or IB and whether the FCM or IB carried funds or securities for the lender at or about the time the proposed agreement was filed. If a lender contributes 10 percent or more of an FCM's or IB's capital, then the lender must be listed as a principal of the FCM or IB.

In addition, prepayment or special prepayment of a subordination agreement must be approved by the DSRO and the DSRO must be given notice of any accelerated maturity of a subordination agreement. Any amendments to existing subordination agreements must be submitted to the DSRO for approval. For broker-dealers, prepayments, special prepayments and amendments must be submitted to the firm's DEA for approval. The agreement and DEA's notice of approval should also be filed with the firm's DSRO.

Again, these filing requirements do not relieve an FCM or IB of filing requirements with the CFTC or other regulatory agencies. Finally, NFA has developed standardized Cash Subordination Loan Agreements and Secured Demand Notes for use by FCMs and IBs. An FCM or IB may obtain a copy of these agreements by calling NFA's Compliance Department at (800) 621-3570.

¹ Compliance with this requirement is effective June 1, 2014; however, Certified Public Accountants have until December 31, 2015 to be inspected by the PCAOB.

Segregation Requirements

The Commodity Exchange Act and CFTC Regulation 1.20 require that all customer funds received by an FCM to margin futures and options on futures contracts trading on a futures market located in the United States be segregated from, and accounted for, separately from the FCM's own funds. CFTC Regulation 30.7 contains a related requirement for foreign futures and foreign options customer funds, and CFTC Regulation 22.2 contains a related requirement for cleared swaps customer collateral.

Customer funds received from customers trading on U.S. Exchanges must be deposited in an account that is clearly identified and titled as a customer segregated account. Similarly, customer funds received from U.S.-based customers trading on foreign exchanges must be deposited in an account that clearly identifies them as secured amount funds. Funds that customers deposit with an FCM, or that are otherwise required to be held for the benefit of customers, to margin, guarantee or secure a cleared swap must be segregated and held in accordance with CFTC Regulation 22.2 (either at an FCM physical location or a depository). Prior to or contemporaneously with opening an account, the FCM must obtain an acknowledgement from the depository holding customer funds stating that it has been informed that the account is a customer segregated, secured amount or cleared swaps customer collateral account. The FCM and its depositories, including derivatives clearing organizations where applicable and other FCMs holding customer funds, must file a copy of the acknowledgment letter with both the CFTC and FCM's DSRO within three business days of opening the account or executing a new written acknowledgement for an existing account. If the FCM holds cleared swaps customer collateral itself, then the FCM must physically separate the cleared swaps customer collateral from its own property, clearly identify each physical location as a "Location of Cleared Swaps Customer Collateral," ensure the physical location provides appropriate protection for the collateral and record in its books and records the amount of such cleared swaps customer collateral separately from its own funds.

An FCM is prohibited from using one customer's funds to meet the obligations of another customer. Therefore, if one customer does not have sufficient funds on deposit with an FCM to meet its obligation, the FCM must use its own funds to make up the deficiency in that customer's account. In order to ensure that there are sufficient funds in the customer segregated, secured amount or cleared swaps customer collateral accounts, an FCM is permitted to deposit its own funds in the customer segregated, secured amount or cleared swaps customer collateral account. The amount of these funds that is in excess of the amount required is referred to as the FCM's residual interest. While these funds are held in customer segregated, secured amount or cleared swaps customer collateral accounts, the funds are for the exclusive benefit of the FCM's customers. The FCM's books must reflect the amount of its interest in the segregated, secured amount or cleared swaps customer collateral account at all times.

Policies and Procedures

An FCM must maintain written policies and procedures that identify a target amount (either a percentage or dollar amount) that it will seek to maintain as its residual interest in customer segregated and customer secured amount funds, as well as in its cleared swaps customer collateral accounts. This target residual amount, as well as any changes to the amount or material changes to the written policies and procedures, must be approved in writing by the FCM's governing body, as part of the FCM's Risk Management Program. In establishing the target residual amount, the FCM's governing body, CEO, CFO, or other officer(s) specifically granted the authority and responsibility to fulfill the responsibilities of senior management by the governing body, must perform a due diligence inquiry related to the nature of the firm's business and create a written record that describes the factors used to determine its target residual amount.

Should an FCM fall below the target residual interest amount due to a disbursement that is not for the benefit of customers, it must either deposit funds into the segregated, secured amount or cleared swaps customer collateral accounts necessary to restore the account balance to the target amount or, if appropriate, revise the target amount by the close of business on the next business day. If any of the customer segregated, secured amount funds or cleared swaps customer collateral account(s) falls below the target residual interest amount, the FCM must file immediate notification through WinJammer™. Whenever an FCM makes a disbursement from customer segregated, secured amount funds or cleared swaps customer collateral account(s) that is not for the benefit of customers, the FCM must ensure that after making the disbursement the FCM maintains sufficient funds to remain in continued compliance with its segregated funds, secured amount or cleared swaps customer collateral requirements. Therefore, the FCM's internal procedures must require it to consider the most-current required segregated funds, secured amount or cleared swaps customer collateral calculation, as well as the impact of any known unsecured debits, deficits and previous disbursements that could cause material adjustments to its most-current segregated, secured amounts or cleared swaps customer collateral calculations.

Disbursements from Customer Funds

An FCM may not, by single or multiple transfers, withdraw, transfer or otherwise disburse funds from any customer segregated, secured amount funds or cleared swaps customer collateral accounts that exceed 25% of its residual interest in either customer segregated, secured amount funds or cleared swaps customer collateral accounts based on the daily segregated, secured amounts funds or cleared swaps customer collateral calculation, unless the FCM prepared the daily segregation calculation as of the close of business on the previous business day and its CEO, CFO or a financial principal with knowledge of the firm's financial position pre-approves the disbursement in writing. For purposes of calculating the 25% threshold, an FCM may exclude any segregated, secured amount funds or cleared swaps customer collateral disbursements made to or for the benefit of customers.

Immediately after an FCM's CEO, CFO or financial principal pre-approves the disbursement that results in the FCM exceeding the 25% threshold (either through the single disbursements or in combination with disbursements made since the last daily segregated, secured amount funds or cleared swaps customer collateral calculation), the FCM must file a written notice signed by the CEO, CFO or financial principal through WinJammer™. The notice must disclose that the FCM has made, or intends to make, such a disbursement, and describe the reasons, the amount and recipients of the disbursement (or series of disbursements). The notice must also confirm that the disbursement was properly pre-approved and provide a current estimate of the FCM's remaining total residual interest in the segregated, secured amount funds or cleared swaps customer collateral accounts, along with a representation from the CEO, CFO or financial principal that to the best of that person's knowledge and reasonable belief, after due diligence, the FCM remains in compliance with its segregated, secured amount funds or cleared swaps customer collateral requirement after the disbursement.

After an FCM makes a disbursement that requires the pre-approval and written notice, the FCM must obtain the pre-approval and file the required notice for any subsequent disbursements from the applicable customer segregated, secured amount funds or cleared swaps customer collateral accounts that are not made for the benefit of customers until the FCM completes its next daily segregated, secured amount funds or cleared swaps customer collateral calculation.

FCMs may hold customer segregated or secured amount funds in cash at an acceptable depository or may invest those funds in one of several investments permitted under CFTC Regulation 1.25(a).

Reporting Obligations

FCMs must make daily formal segregation, secured amount and cleared swaps customer collateral computations as of the close of each business day. These computations must detail the amount of customer funds required to be on deposit in segregated, secured amount and cleared swaps customer collateral accounts, the amount of funds on deposit in segregated, secured amount and cleared swaps customer collateral accounts and the FCM's residual interest in the funds on deposit. Calculations must be completed and submitted to NFA by noon of the following business day.

In addition, each Member FCM must instruct each depository, as required by NFA, holding customer segregated funds under CFTC Regulation 1.20, customer secured amount funds under CFTC Regulation 30.7 or cleared swaps customer collateral under CFTC Regulation 22.2 to report the balances in the FCM's customer segregated funds, customer secured amount funds and cleared swaps customer collateral accounts to a third party designated by NFA in the form and manner prescribed by NFA.

FCMs must also file a Segregated Investment Detail Report ("SIDR") through WinJammer™ on a semi-monthly basis on the 15th (or following business day should

the 15th fall on a weekend) and the last business day of each month. The report is due by 11:59 p.m. on the business day following the 15th and last business day of each month. The SIDR requires an FCM to provide a detailed breakdown of: an FCM's investment of customer segregated funds, customer secured amount funds and cleared swaps customer collateral accounts; each type of permitted investment identified in CFTC Regulation 1.25(a); customer owned securities held as margin and as securities under agreements to resell the securities (reverse repurchase transactions); and the identity and location of all depositories holding these funds.

If an FCM fails to complete the required segregated funds, secured amount funds or cleared swaps customer collateral calculations, it is prohibited from making any disbursements not for the benefit of customers from the accounts for which the calculation was not completed until the required calculation is completed and submitted to NFA.

FCMs are required on a monthly basis, within 17 business days after the end of each month, to submit certain financial information through WinJammer™ as of the close of business on the last business day of the month. The required information includes total adjusted net capital, minimum net capital and excess net capital, and the firm's measure of leverage using a calculation required by NFA.

Margins

All FCMs must collect margin for customer accounts in accordance with the rules established by the exchange on which the contract is traded. NFA Financial Requirements Section 7 requires that exchange margin procedures be followed by an FCM even if it is not a member of the exchange. Thus, any FCM must establish its margin levels and collection procedures in accordance with exchange rules.

Also, if an FCM carries an account for another FCM on an omnibus basis, CFTC Regulation 1.58 requires the carrying FCM to collect margin and the originating FCM to deposit margin on the gross positions in the account. This means that margin must be collected on each long and short position and those positions may not be netted against each other. In addition, if positions in an omnibus account are to be margined as spreads or hedges, the carrying FCM must receive a written representation from the originating FCM that the positions are entitled to the special rates.

If an FCM accepts other than immediately available funds from an omnibus account, it must notify its DSRO within 24 hours of such acceptance. NFA Compliance Rule 2-33 recognizes wire transfers and certified checks as immediately available funds. Acceptance of any other type of funds must be reported to the DSRO.

Finally, an FCM is required by CFTC Regulation 1.12 to provide immediate notification to the CFTC and the FCM's DSRO when its amount of residual interest is less than the sum of the undermargined amounts in its customer accounts as determined at the point in time that the firm is required to maintain the undermargined amounts.

Requirements for a Guarantee Agreement

An IB may satisfy the minimum financial and reporting requirements by entering into a Guarantee Agreement with the registered FCM. Generally, once an IB enters into a Guarantee Agreement, it must introduce all of its accounts to the guarantor FCM. A copy of the prescribed Agreement is attached as Part B of the Form 1-FR-IB. This is the only form which may be used under NFA Compliance Rule 2-23. As long as an Agreement remains in effect, an IB has no further financial reporting obligations. The Agreement does not have an expiration date and therefore continues to be in effect until terminated. The procedures necessary to terminate an agreement are explained below.

An Agreement must include the names of the FCM and the IB and an effective date. The form must be signed and dated by an appropriate person from both the FCM and IB. An appropriate person is the proprietor if the firm is a sole proprietorship, a general partner if the firm is a partnership and either the chief executive officer or the chief financial officer if the firm is a corporation.

An FCM that enters into a guarantee agreement is jointly and severally subject to discipline under NFA Compliance Rule 2-23 for acts and omissions of the IB that violate NFA rules while the guarantee agreement is in effect.

An FCM may not enter into a new guarantee agreement with an IB if the FCM's adjusted net capital is below the early warning capital level or has not been above the early warning level on at least three consecutive monthly financial reports filed with NFA and the CFTC. Additionally, if an FCM falls below the early warning level and cannot demonstrate that its capital is above early warning within 30 days, the FCM must notify all of its guaranteed IBs that the guarantee agreements will terminate in 30 days. If the FCM's adjusted net capital increases above early warning during this 30-day period, it may keep the guarantee agreements in effect.

Termination of a Guarantee Agreement

In order to terminate a guarantee agreement, either party must give written notice of its intent at least 30 days prior to the planned termination date. The notice must be filed with the other party, NFA, the CFTC and the DSRO for the FCM. If both parties agree in advance, they may file a mutual determination notice, signed by both parties, at any time prior to the termination date. Finally, if either party feels it has "good cause," it may terminate the agreement immediately upon written notice to the other party and NFA.

On the termination date, the IB must cease doing business until it has filed with NFA either a new guarantee agreement or the necessary financial reports. The financial filing requirement may be satisfied by filing either an audited Form 1-FR-IB or FOCUS Report which is less than 45 days old as of the date received by NFA; or an audited Form 1-FR-IB or FOCUS Report which is less than one-year-old as of the date received by NFA and an unaudited Form 1-FR-IB or Focus Report which is less than 17 business days old as of the date received by NFA. If the IB files the financial

reports, it must also include a statement describing the source of its current assets and representing that its capital has been contributed for the purpose of operating its business and will continue to be used for such purpose. The IB must also file a statement establishing a fiscal year-end or electing a calendar year.

Accounting for Commodity Pools

This section is not intended to provide an all inclusive discussion of accounting topics applicable to the operation of a commodity pool. Rather, it is included as a starting point in the discussion of financial requirements and to provide an overview of accounting issues. CPOs may want to discuss the development and implementation of their pool's accounting system with the independent public accountant they engage to certify their pool's Annual Report. Certification by an independent public accountant is required under NFA Rules and CFTC Regulations. The conditions which impair an accountant's independence are discussed on page 31.

Accounting refers to the system employed by a business to record its financial transactions. An accounting system has three major categories: assets, liabilities and ownership equity.

Assets

Assets are items of value which are owned by—or owed to—the commodity pool. For example, assets include cash, securities, equity at FCMs, interest receivable (interest earned but not yet received) and the pool's organizational costs (which will be amortized over a period of years).

Liabilities

Liabilities are the amounts that the commodity pool owes to others (such as for management fees and commissions).

Ownership Equity

Ownership Equity is the amount by which assets exceed liabilities. For purposes of accounting by commodity pools, ownership equity is also referred to as Net Asset Value (NAV).

Based on the foregoing definitions, the following equation can be stated.

$$\textbf{Assets - Liabilities = Ownership Equity}$$

This equation can be restated to follow the balance sheet format.

$$\textbf{Assets = Liabilities + Ownership Equity}$$

Ownership Equity is not determined in an accounting system by merely taking the amount by which assets exceed liabilities. Instead, ownership equity consists of the following three components: capital, revenue and expenses.

Capital

Capital is the amount of money invested in the commodity pool including capital additions less capital distributions.

Revenue

Revenue is the amount of income earned by the commodity pool, including but not limited to realized and unrealized trading gains and interest income.

Expenses

Expenses are the amount the commodity pool has paid or incurred to earned revenue, including but not limited to realized and unrealized trading losses, management and incentive fees and legal and accounting expenses.

Often, realized trading gains and losses, and unrealized trading gains and losses, are reflected together in a single account rather than in separate revenue and expense accounts.

The foregoing information can be expressed by the following equation.

$$\text{Ownership Equity} = \text{Capital} + \text{Revenue} - \text{Expenses}$$

Financial transactions are recorded in an accounting system by means of offsetting “debit” and “credit” entries. That is, for each debit entry, there must (at some place in the accounting system) be an equal and offsetting credit entry. When all transactions have been properly recorded, total debits and total credits will be equal.

- Debits increase assets, decrease liabilities or decrease ownership equity.
- Credits decrease assets, increase liabilities or increase ownership equity.

Required Accounting Records

All transactions are initially recorded in what are known as journals. A journal is simply a chronological record of each and every transaction. Two kinds of journals must be established and maintained for each commodity pool.

Cash Receipts and Disbursements Journal

This is a journal which records all transactions which involve receipts or disbursements of money, securities or other property.

General Journal

This is a journal which records all accounting entries that do not involve a receipt or disbursement of money, securities or other property. This pertains primarily to entries which are of an accrual rather than a cash nature, such as an adjustment for interest income earned but not yet received.

Ledgers

Once entries have been recorded in a journal, they are then transferred, either individually or as a total, to what are known as ledgers. A ledger consists of a group of accounts. Two kinds of ledgers must be established and maintained for each commodity pool:

General Ledger

A ledger consists of a group of individual accounts. The General Ledger for a

commodity pool must include all asset, liability, capital, income and expense accounts. Examples of the types of General Ledger accounts you might establish are:

- Escrow
- Cash — Checking
- Money Market Fund
- Broker Balance — Ledger Balance
- Broker Balance — Open Trade Equity
- Securities — T-Bills
- Investment in Commodity Pool
- Interest Receivable
- Organization Costs
- Management Fees Payable
- Accrued Commissions
- NFA, Exchange and other Fees
- Redemptions Payable
- Accounting Fees Payable
- Legal Fees Payable
- Partners' Equity
- Gross Realized Trading Gains (Losses)
- Change in Open Trade Equity—Gross
- Unrealized Gain (Loss) on Market Value of Securities
- Gain (Loss) on Investment in Commodity Pool
- Interest Income
- Other Income
- Commissions
- Incentive Fees
- Management Fees
- Change in Accrued Commissions and Fees
- Accounting Fees
- Legal Fees
- Amortization Expense
- Other Expenses

Participant Subsidiary Ledger

This ledger or equivalent record must include certain account information for each participant in the commodity pool. It must show the participant's name and address and all funds, securities and other property that the pool received from or disbursed to the participant.

Financial Statements

CPOs are required to prepare the following periodic financial statements:

- A Statement of Financial Condition. This statement, also known as a Balance Sheet, summarizes all asset, liability and partnership equity accounts contained in the General Ledger.
- A Statement of Income (Loss). This statement summarizes the income and expense accounts contained in the general ledger. The Statement of Income (Loss) must separately itemize the following information:
 - The total (gross) amount of realized gain or loss on commodity positions which were liquidated during the period.
 - The change in unrealized net gain or loss on commodity positions during the period. This balance can be computed from the Broker Balance — Open Trade Equity Account.
 - The total amount of net gain or loss from all other transactions in which the commodity pool engaged during the period, including interest and dividends earned or accrued.
 - Separate totals for all management fees, advisory fees, brokerage fees, and any other fees (in connection with commodity or investment transactions) during the period.
 - The total of all other expenses incurred or accrued by the commodity pool during the period, such as legal or accounting expenses.
- A Statement of Changes in Net Asset Value. This statement summarizes the change in the commodity pool's Net Asset Value (NAV) for the reporting period. The statement must separately itemize the following information:
 - The NAV of the commodity pool as of the beginning of the reporting period.
 - Total additions to the commodity pool during the reporting period.
 - Total withdrawals and redemptions during the reporting period.
 - Total net income or loss of the pool during the reporting period.
 - The NAV of the commodity pool as of the end of the reporting period.
 - Either (a) the NAV per outstanding participation unit as of the end of the participant's interest or (b) the share in the commodity pool as of the end of the reporting period.

If a commodity pool has net assets of more than \$500,000 at the start of its fiscal year, the required statements must be prepared *monthly*. If the net assets of the commodity pool at the start of its fiscal year are \$500,000 or less, the statements are required to be prepared at least *quarterly*. In both cases, however, the statements must be prepared within 30 days of the end of the month or quarter (whichever is applicable).

The following page describes and illustrates the required financial statements and indicates the distribution that must be made.

Sample Financial Statements for a Commodity Pool
Statement of Financial Condition as of March 31, 20xx

Assets

Cash — Checking and Money Market Accounts	\$31,368
Ledger Balance	74,232
Open Trade Equity.....	2,275
Securities on Deposit	104,867
Organization Cost	<u>9,666</u>
Total Assets	<u>\$222,408</u>

Liabilities & Ownership Equity

Liabilities

Management Fee Payable	\$1,109
Accrued Commissions	462
Redemption Payable	<u>5,386</u>
Total Liabilities.....	<u>\$6,957</u>

Units

Ownership Equity:

General Partner	25
Limited Partner	175
Total Ownership Equity.....	<u>\$215,451</u>
Total Liabilities & Ownership Equity.....	<u>\$222,408</u>

Statement of Income (Loss) For the Month ended March 31, 20xx

Income

Gross Realized Trading Gains (Losses)	\$17,690
Change in Unrealized Gains (Losses)	2,275
Unrealized Gain (Loss) on Market Value of Securities	2,230
Interest Income	<u>1,184</u>
Total Income.....	<u>\$23,379</u>

Expenses

Management Fee	\$3,266
Incentive Fee	2,690
Commissions	1,071
Exchange and NFA Fees	211
Amortization	334
Other Expenses	250
Total Expenses.....	<u>\$7,822</u>
Net Gain (Loss).....	<u>\$15,557</u>

Statement of Changes in Net Asset Value For the Month Ended March 31, 20xx

Net Asset Value Beginning of Period 3/1/xx (200 Units)	\$200,000
Additions (5 units)	5,280
Withdrawals (5 units)	(5,386)
Net Income	<u>\$15,557</u>
Net Asset Value End of Period 3/31/xx.....	\$215,451
Net Asset Value Per Unit (200 Units).....	\$1,077

Reports to Pool Participants

CPOs are required to distribute to pool participants an Account Statement and an Annual Report.

Account Statements

Each CPO Member must distribute account statements to pool participants at least monthly within 30 days of month end for pools with net asset value of more than \$500,000. For pools with net asset value less than \$500,000 or exempt pools under CFTC Regulation 4.7, the CPO must distribute account statements to participants at least on a quarterly basis within 30 days of the quarter end. However, a CPO is not required to be distribute an account statement for the final reporting period of the fiscal year if participants receive an Annual Report within 45 days of the end of the fiscal year which must include the Statements of Income (Loss) and Changes in Net Asset Value.

A CPO must disclose any material business dealings between the commodity pool, the commodity pool's operator, CTA, FCM, IB or the principals thereof, if the firm has not previously disclosed the information in the commodity pool's Disclosure Document, amendments, prior Account Statements or Annual Reports. Examples of such material business dealings include the addition or deletion of principals, CTAs, FCMs or IBs, any changes in compensation arrangements, any changes in investment strategy or the use of the commodity pool's funds, including loans. This list is not all inclusive, and the firm should ensure that it discloses all of the information required under CFTC Regulation 4.24 when it describes these dealings.

Finally, a signed oath or affirmation must accompany the Account Statement and must state that to the best of the knowledge and belief of the individual making the oath or affirmation the information contained in the document is accurate and complete.

The oath or affirmation must include the name of the CPO, the commodity pool and the name and capacity of the signatory. If the commodity pool is a sole proprietorship, the oath or affirmation must be made by the sole proprietor; if a partnership, by a general partner; and if a corporation, by the chief executive officer or chief financial officer.

Annual Reports

An Annual Report must contain information for two preceding fiscal years. It must be distributed to pool participants within 90 days after the end of the fiscal year or the permanent cessation of trading, whichever is earlier. In addition, the Annual Report must be filed with NFA.

CPOs are required to electronically file these pool Annual Reports with NFA via EasyFile, a web-based system available at NFA's website (www.nfa.futures.org). EasyFile involves uploading a PDF of the identical Annual Report provided to the pool's limited partners plus entering key financial balances into a standardized

schedule. Access to EasyFile is granted by the firm's security manager in NFA's Online Registration System.

The Annual Report must be prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP"). However, the CFTC may provide limited relief, on a case by case basis, to CPOs that operate offshore pools by allowing such pools to prepare and present pool financial statements in accordance with International Financial Reporting Standards, or United Kingdom or Irish accounting standards, instead of U.S. GAAP. The CPO must apply for this relief from the CFTC. The Annual Report must include the following:

- The NAV of the pool for the two preceding fiscal years.
- The NAV per outstanding participation unit in the pool as of the end of each of the pool's two preceding fiscal years, or the total value of the participant's interest or share in the pool as of the end of the pool's two preceding fiscal years.
- A Statement of Financial Condition (balance sheet) as of the end of the pool's fiscal year and the preceding fiscal year.
- The Statement of Income (Loss), Statement of Changes in Financial Condition and Statement of Changes in Net Asset Value. These statements must be included for the period starting with (a) the date of the last such statement filed with the CFTC and NFA or (b) the date of the formation of the pool, whichever is more recent, and ending with the pool's fiscal year end. The statements must also be included for the preceding fiscal year.
- Appropriate footnote disclosures and any additional material information as may be necessary to make the required statements not misleading.
- The same signed oath or affirmation required for Account Statements.
- ***The Annual Report must be certified by an independent certified public accountant.*** The Annual Report must include the auditor's opinion with respect to the financial statements and schedules and with respect to the consistency of application of accounting principles.
- The auditor's report must identify the financial statements audited in an opening (introductory) paragraph, describe the nature of an audit in a scope paragraph and express the auditor's opinion in a separate opinion paragraph. The basic elements of the report are the following:
 - a. A title that includes the word *independent*;
 - b. A statement that the financial statements identified in the report were audited;
 - c. A statement that the financial statements are the responsibility of the commodity pool operator and that the auditor's responsibility is to express an opinion on the financial statements based on his audit;
 - d. A statement that the audit was conducted in accordance with

generally accepted auditing standards;

- e. A statement that generally accepted auditing standards require that the auditor plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement;
 - f. A statement that an audit includes—
 - (1) Examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
 - (2) Assessing the accounting principles used and significant estimates made by management; and
 - (3) Evaluating the overall financial statement presentation.
 - g. A statement that the auditor believes that his audit provides a reasonable basis for his opinion;
 - h. An opinion as to whether the financial statements present fairly, in all material respects, the financial position of the commodity pool as of the balance sheet date and the results of its operation for the periods then ended in conformity with generally accepted accounting principles.
 - i. The manual or printed signature of the auditor's firm; and
 - j. The date of the audit report.
- To be independent, the auditor must be free from any obligation to or interest in the commodity pool or the commodity pool operator.

Quarterly Reporting Requirements

Each CPO Member must report on a quarterly basis with NFA or the CFTC specific information about the firm and the pools that it operates. These quarterly reports are due within 60 days after the end of the quarters ending March 31, June 30 and September 30. Reports for the quarter ending December 31 are due within 90 days of the calendar year-end for Small (less than \$150 million in assets under management (AUM)) or Mid-size CPOs (greater than \$150 million but less than \$1.5 billion in AUM) and within 60 days for Large CPOs (greater than \$1.5 billion in AUM). All Pool Quarterly Reports (PQR) must be filed electronically using NFA's EasyFile system regardless of whether the PQR is being filed to fulfill NFA or CFTC requirements. The content of the quarterly PQR filing will depend upon the CPO's highest AUM during the reporting period. All CPOs are required to file a quarterly report even if the CPO has not operated during the reporting period. CPOs that file a Form PF with the SEC will continue to be required to file a quarterly PQR with NFA for quarters ending March 31, June 30, September 30 and with the CFTC for the quarter ending December 31.

NFA Examinations

Once you become an NFA Member, you will be required to fully comply at all times with the rules and regulations of NFA and the CFTC. As a means of monitoring and assuring compliance, NFA conducts periodic on-site examinations. NFA generally notifies a Member of an upcoming exam by telephone shortly before the exam is scheduled to begin. FCMs which carry customer funds, and others at NFA's discretion, however, may be subject to unannounced exams.

At the outset of an exam, a member of the examination team will explain the purpose and scope of the exam and will indicate what books, statements and other information will be reviewed. During the course of the exam, additional records or documentation will be requested. Examination teams will review the Member's sales materials and practices, accounting procedures and financial records, and, if appropriate, disclosure documents, performance representations and trading records. NFA will observe the Member's operations and conduct interviews with Member personnel. A preliminary list of records needed for the exam is provided at the announcement of the exam, usually by facsimile or verbally over the telephone. The examiner will conduct a pre-exam interview with an individual of the firm that is knowledgeable of the firm's current operations. The interview will consist of a series of questions regarding the firm's business, including the type of customers the firm has, the solicitation methods used, the types of promotional material used, etc. Obtaining a clear understanding of the firm's operations will enable NFA to conduct a more effective examination. The length of time of this pre-exam interview will depend on the nature of the firm's operations.

Although NFA attempts to minimize the disruption of a Member's business operations, NFA's examination program is designed so that the examiners must perform a certain amount of work at the Member's office. Even though a Member may feel that its operations and records are in near-perfect condition, the examiners will still need to perform testing. In order to fully understand each Member's business operations and resolve any testing discrepancies, the examiners also need to obtain oral representations and documents from the appropriate firm personnel. Obviously, to the extent that this information is not readily available, NFA exams may take longer, inconveniencing the Member as a result. Additionally, if a firm, principal or AP is registered in another capacity, then the exam may take longer while the examiners perform certain required procedures for each separate category of registration. Examinations generally last from one day to five days depending on the nature of operations and areas of concern. Examinations of FCMs that carry customer funds generally last longer.

The fact that you are being examined does not hold a negative implication. All NFA Members are subject to an NFA examination. FCMs that carry customer accounts must be examined every year. There are several factors that contribute to decisions about when and how frequently Members are examined. Among these are: NFA's monitoring of the Member's promotional material, the receipt of customer complaints,

knowledge of the past history of the firm and its principals, the Member's fiscal year-end and the time elapsed since its last exam, potential effects of market moves and referrals from outside NFA. Other factors can include the amount of money CPOs and CTAs have under management and our review of disclosure documents and financial statements that must be filed with NFA.

NFA examinations have two major objectives:

- To determine whether the firm is maintaining records in accordance with NFA rules and applicable CFTC regulations.
- To ensure that the firm is being operated in a professional manner and that customers are protected against unscrupulous activities and fraudulent or high-pressure sales practices.

FCMs and independent IBs are also subject to examinations of their financial records as are CPOs for the pools they operate. The financial audit focuses on the preparation and presentation of the financial statement and internal accounting controls. The primary objective of the financial exam is to determine that the financial statements are complete, accurate, and prepared in accordance with NFA rules, CFTC regulations and generally accepted accounting principles.

How to Prepare for an Examination

There is only one way to be prepared for an NFA exam—by having properly prepared and maintained books and records available for review at all times. This will not necessarily expedite the completion of the exam but will enhance the likelihood of a satisfactory examination report.

There are several possible sources of advice and assistance available to help Members establish and maintain the required records. As a first step, Members should study the information contained in this booklet, the *NFA Manual* and CFTC Regulations. Also, the *Self-Examination Checklist*, which all NFA Members must complete on a yearly basis, is a valuable source of information concerning a Member's regulatory responsibilities and internal procedures. A copy of the *Self-Examination Checklist* is available under separate cover or on NFA's website at www.nfa.futures.org. If additional information or guidance is necessary, an accountant or attorney should be able to help, or assistance can be obtained by contacting NFA's Compliance Department.

After the Examination

After the exam has been completed, but before departing, the examiners generally meet with the Member in what is called an exit interview. The purpose of the exit interview is to discuss the findings of the exam, with emphasis on any deficiencies which were noted and ways in which they can be corrected. The examination team also will obtain representations from appropriate firm personnel on how the firm will correct the deficiencies.

Upon completion of the fieldwork, the examiners will prepare an Exam Report. If the

examiners find that the Member's books, records and other documents were without material deficiencies, the Exam Report will simply state that the exam has been completed and no material deficiencies were noted. If there were deficiencies, the Exam Report will note them. A written response to the Exam Report may be required.

If the results of an NFA exam disclose relatively few deficiencies, a Member cannot represent that it has been approved or recommended by NFA. In fact, NFA Compliance Rule 2-22 prohibits any representation that a Member's abilities have been passed upon by NFA or any federal or state regulatory body.

Should an exam indicate a serious or repeated violation of NFA rules, the Compliance Department will forward the matter to the Business Conduct Committee (BCC), which is composed of NFA Members. Depending on the seriousness of the violation, the BCC may direct that a Warning Letter be sent to the firm or it may issue a formal Complaint charging the Member with specific violations of NFA rules. If a Complaint is issued, the Member is given the opportunity to answer and is entitled to a hearing before members of NFA's Hearing Committee to determine whether the violations occurred. The Hearing Committee is also comprised of NFA Members. If the Hearing Committee finds that a Member violated NFA rules, the Member is subject to several possible disciplinary actions, including expulsion from NFA membership, suspension for a fixed period, prohibition from future association with any NFA Member, censure, reprimand and/or a fine of up to \$250,000 for each violation. A Member can appeal any adverse decision by the Hearing Committee to a committee of directors created by the Board—the Appeals Committee. Decisions of the Appeals Committee are final, subject to review by the CFTC.

In emergency cases, such as when an infraction is deemed to pose an imminent danger to markets, customers or other Members, the President of NFA with the concurrence of the Board of Directors or the Executive Committee may initiate what is known as a Member Responsibility Action (MRA). This summary action can require the firm to immediately cease doing business, restrict a firm's operation or impose other remedial actions. Any Member subject to an MRA will be offered a hearing before several members of the Hearing Committee as promptly as possible. An MRA may be initiated either following an exam or investigation, or if circumstances so dictate, during the course of an exam or investigation.

Appendix A - Securities Haircuts

Haircut charges on securities should be calculated in compliance with SEC Regulation 240.15c3-1. The charges below are a general summary of the haircuts to be taken on the more common securities.

A. Government Securities and Canadian Debt Obligations

- Haircut taken on the market value of the net long or short position in each category plus 50% of the lesser of the aggregate deductions on the long or short positions

Category 1

- (i) Less than 3 months to maturity—0%;
- (ii) 3 months but less than 6 months to maturity— 1/2 of 1%;
- (iii) 6 months but less than 9 months to maturity— 3/4 of 1%;
- (iv) 9 months but less than 12 months to maturity—1%.

Category 2

- (i) 1 year but less than 2 years to maturity—1 1/2 %;
- (ii) 2 years but less than 3 years to maturity—2%.

Category 3

- (i) 3 years but less than 5 years to maturity—3%;
- (ii) 5 years but less than 10 years to maturity—4%.

Category 4

- (i) 10 years but less than 15 years to maturity—4 1/2 %;
- (ii) 15 years but less than 20 years to maturity—5%;
- (iii) 20 years but less than 25 years to maturity—5 1/2 %;
- (iv) 25 years or more to maturity—6%.

B. Municipal Securities

- Haircut taken on the market value of the net long or short positions in each category
- Original maturity of 731 days or less
- Issued at par and pays interest at maturity or issued at a discount
- Not traded flat or in default as to principal or interest
 - (i) Less than 30 days to maturity—0%

- (ii) 30 days but less than 91 days to maturity—1/8 of 1%.
 - (iii) 91 days but less than 181 days to maturity—1/4 of 1%.
 - (iv) 181 days but less than 271 days to maturity—3/8 of 1%.
 - (v) 271 days but less than 366 days to maturity—1/2 of 1%.
 - (vi) 366 days but less than 456 days to maturity—3/4 of 1%.
 - (vii) 456 days but less than 732 days to maturity—1%.
- C. Municipal Securities other than those described above
- Haircut taken on the market value of the net long or short positions in each category
 - (i) Less than 1 year to maturity—1%.
 - (ii) 1 year but less than 2 years to maturity—2%.
 - (iii) 2 years but less than 3 1/2 years to maturity—3%.
 - (iv) 3 1/2 years but less than 5 years to maturity—4%.
 - (v) 5 years but less than 7 years to maturity—5%.
 - (vi) 7 years but less than 10 years to maturity—5 1/2%.
 - (vii) 10 years but less than 15 years to maturity—6%.
 - (viii) 15 years but less than 20 years to maturity—6 1/2%.
 - (ix) 20 years or more to maturity—7%.
- D. Money Market Funds
- Haircut is 2% of the market value of the money market fund.
- E. Commercial Paper, Bankers Acceptances and Certificates of Deposit
- Haircut taken on market value of the greater of the long or short positions in each category
 - (i) less than 30 days to maturity—0%;
 - (ii) 30 days but less than 91 days to maturity—1/8 of 1%;
 - (iii) 91 days but less than 181 days to maturity—1/4 of 1%;
 - (iv) 181 days but less than 271 days to maturity—3/8 of 1%;
 - (v) 271 days but less than 1 year to maturity—1/2 of 1%; and
 - (vi) 1 year or more to maturity—same as Government Securities.
- F. Non-convertible Debt Securities
- Haircut taken on the market value of the greater of the long or short positions in each category
 - (i) Less than 1 year to maturity—2%;

- (ii) 1 year but less than 2 years to maturity—3%;
- (iii) 2 years but less than 3 years to maturity—5%;
- (iv) 3 years but less than 5 years to maturity—6%;
- (v) 5 years but less than 10 years to maturity—7%;
- (vi) 10 years but less than 15 years to maturity—7 1/2%;
- (vii) 15 years but less than 20 years to maturity—8%;
- (viii) 20 years but less than 25 years to maturity—8 1/2 %; and
- (ix) 25 years or more to maturity—9%.

G. Convertible Debt Securities

- If market value is equal to or greater than principal amount, haircut is same as common stock.
- If market value is less than principal amount, haircut is the same as non-convertible debt securities.

H. Common Stock

- Haircut is 15% of the market value of the greater of the long or short position plus 15% of the lesser to the extent it exceeds 25% of the greater position.

I. Preferred Stock

- Haircut is 10% of the market value of the greater of the long or short position.

Appendix B - Anti-Money Laundering Questionnaire

National Futures Association (“NFA”) is dedicated to helping Member firms meet their regulatory requirements. Each Member firm must adopt a written anti-money laundering (“AML”) program tailored to its operations. NFA has developed the following questionnaire to assist firms in meeting that requirement.

The firm should maintain its AML program with other firm procedures. Having a written program is not enough to meet your regulatory requirements, however. You must also implement and follow the program and communicate it to your employees.

Please also consult the following NFA Rule and Interpretive Notice when designing your AML program:

NFA Rule 2.9. Supervision. NFA Interpretive Notice “NFA Compliance Rule 2.9: FCM and IB Anti-Money Laundering Programs”.

A Member firm's written AML program should answer all of the following questions as completely as possible. Although you may answer “not applicable” to particular questions, you should carefully consider the firm's operations before doing so.

General Questions

- A. What is the firm's policy statement regarding money laundering and terrorist financing?
- B. What are the consequences if an employee does not follow the firm's AML policy?
- C. Who in senior management is responsible for giving written approval of the firm's AML program?
- D. Has the firm designated one or more individuals to be responsible for overseeing the day to day operations of the firm's AML compliance program? Who has the firm designated?
- E. Does the AML Compliance officer/department report to senior management? If so, who do they report to?
- F. What are the AML Compliance Officer's duties and responsibilities?

Customer Identification Program (CIP)

- A. What identifying information (e.g., name, address, date of birth, tax identification number) does the firm obtain from its new customers?
- B. Does the firm rely on documentary methods to verify identity? If so:
 - What documents does the firm accept to verify the identity of new

customers who are individuals? Be specific.

- What documents does the firm accept to verify the identity of new customers that are not individuals (e.g., corporations, partnerships, trusts)? Be specific.
- C. Does the firm rely on non-documentary methods to verify identity? If so, what non-documentary methods does the firm use to verify a customer's identity? Be specific.
- D. Under what circumstances will the firm verify identity:
- Using documentary methods alone?
 - Using non-documentary methods alone?
 - Using a combination of both methods?
- E. Does the firm require non-documentary methods in the following situations:
- The customer is unable to present a current government ID with a photograph or similar safeguard (e.g., a thumbprint)?
 - The firm is not familiar with the documents the customer provides?
 - The firm opens an account without obtaining documents from the customer?
 - A customer opens an account without appearing in person?
 - Other circumstances that increase the risk that the firm will be unable to verify the identity of the customer through documents?
- If the firm does not use non-documentary methods in one or more of these situations, why has the firm concluded that non-documentary methods are not necessary?
- F. What is the firm's deadline for completing the verification process? How does the firm ensure that the customer's identity is verified within a reasonable time before or after the account is opened?
- G. Does the firm accept accounts from people who are applying for taxpayer identification numbers? If so, how does the firm confirm that an application for taxpayer identification number has been filed? How does the firm ensure that it obtains the taxpayer identification number within a reasonable period of time?
- H. Under what circumstances will the firm require customers that are not individuals (e.g., corporations, partnerships, trusts) to provide information about the account controller in order to verify the customer's identity?
- I. How does the firm handle an account if the firm does not have a reasonable belief that it knows the customer's identity? Specifically:
- When will the firm refuse to open an account?
 - What restrictions does the firm place on customer transactions while the firm is still verifying the customer's identity?

- Under what circumstances will the firm close an account after the firm's attempts to verify the customer's identity have failed?
 - In what situations will the firm file a suspicious activity report?
- J. Does the firm rely on other financial institutions to carry out its CIP requirements? If so, answer the following questions for each financial institution the firm intends to rely upon:
- What is the financial institution's name?
 - When will your firm rely on that financial institution to perform some or all elements of the CIP for your firm? If it will perform only some elements, which ones are they?
 - What steps did your firm take to ensure that the financial institution is required to have an AML Compliance program under the Bank Secrecy Act?
 - What Federal agency regulates the financial institution?
 - When did your firm enter into a written agreement with the financial institution requiring it to certify annually that it has implemented an AML program and that it will perform the specified requirements of its own CIP or perform the CIP functions described in the agreement? (You should attach the agreement to the firm's AML procedures.)
 - How does your firm ensure that it obtains a copy of the annual certification?
- K. Does the firm contractually delegate its CIP functions to other entities? If so, answer the following questions for each entity (including any financial institution not included above) that the firm intends to contractually delegate those functions to:
- What is the entity's name?
 - What elements of the firm's CIP are delegated to that entity?
 - When did you enter into a written agreement outlining each party's responsibilities? (You should attach the agreement to the firm's AML procedures.)
 - What does your firm do to monitor how the other entity implements the CIP and how effective the CIP is?
 - How does your firm ensure that regulators are able to obtain information and records relating to the CIP performed by that entity?
- L. How does your firm notify customers about why the firm requests information to verify identity before opening an account? What does the notice say?
- M. Where, in what form and for what time period does the firm keep the following information:
- Identifying information collected from customers (e.g., name, address,

date of birth, tax identification number)?

- Documents used to verify identity? Does the firm keep a copy of the documents or does it record the necessary information (e.g., identification number, place issued, date issued, expiration date)?
- Descriptions of the methods used and results obtained when non-documentary methods are used to verify identity?
- Descriptions of how discrepancies in particular customers' verifying information are resolved?

Identifying High-Risk Accounts

- A. How does the firm identify potentially high-risk accounts?
- B. What types of accounts does the firm characterize as high risk?
- C. How does the firm determine whether a customer/prospective customer appears on OFAC's list of Specially Designated Nationals and Blocked Persons (SDN list) identifying known or suspected terrorists and terrorist organizations?
- D. How does the firm determine whether a customer is located in a country on OFAC's list of sanctioned countries?
- E. How does the firm determine whether a customer appears on any list of known or suspected terrorists or terrorist organizations that is issued by the Federal Government and designated by the Treasury Department? How does the firm ensure that it follows all Federal directives issued in connection with the list? (Note: No other lists or federal directives have yet been issued).
- F. How does the firm determine whether a customer is from a country that appears on FATF's Public Statement of jurisdictions with AML/CFT deficiencies?
- G. What type of ongoing monitoring does the firm do to ensure that existing customers don't subsequently appear on the SDN list or come from a country on OFAC's sanctioned country list or FATF's Public Statement of jurisdictions with AML/CFT deficiencies?
- H. What kind of due diligence does the firm perform to determine whether to accept a high risk account?
- I. How does the firm determine whether additional monitoring of account activity is necessary for a high risk account?
- J. What additional monitoring does the firm perform for account activity in high risk accounts?
- K. What special steps will the firm take if the customer/prospective customer or its country appears on the following lists:
 - OFAC's SDN list?
 - OFAC's list of sanctioned countries?

- A list of known or suspected terrorists or terrorist organizations issued by the Federal Government?
- FATF's NCCT Public Statement of jurisdictions with AML/CFT deficiencies?

Suspicious Activity

- A. What systems and procedures does the firm use to detect and report suspicious activity:
 - During the account opening process?
 - While an account is open?
 - When an account closes?
- B. What type of transactions will require a firm to file a form SAR?
- C. How does the firm ensure that a form SAR is filed for a transaction or series of transactions that are conducted, attempted by, at or through the firm, involve an aggregate of at least \$5,000 in funds or other assets and the firm knows, suspects or has reason to suspect that transactions or pattern of transactions (1) Involves funds that come from illegal activity or are part of a transaction designed to conceal that the funds are from illegal activity (2) Are designed, such as through structuring, to evade the reporting requirements of BSA (3) Do not appear to serve any business or apparent lawful purpose (4) Use the firm to facilitate a criminal transaction. Generally, a SAR is due within 30 days after the firm becomes aware of the suspicious transaction.
- D. How does the firm monitor wire transfer activity for unusual transfers (e.g., unexpected or unusually frequent or large transfers by a particular account during a particular period, transfers involving certain countries identified as high risk or having AML/CFT deficiencies)?
- E. What examples of "red flags" does the firm provide its employees to alert them to suspicious activity?
- F. What kind of investigation does the firm do when a red flag occurs? Who does it?
- G. How promptly must employees report potential suspicious activity, and who do they report it to?
- H. What are the firm's procedures for filing a form SAR with FinCEN after the firm becomes aware of a suspicious transaction or if identity is unknown? Specifically, how promptly does the firm file a form SAR with FinCEN?
- I. Which supervisory personnel evaluate the activity and determine whether the firm is required to file a SAR with FinCEN?
- J. How does your firm ensure the confidentiality of SAR filings or any information that would reveal the existence of a SAR?
- K. Where and in what form does the firm keep the form SAR and any supporting

documentation, which must be maintained for five years from the date the SAR was filed?

- L. How does the firm maintain the confidentiality of the form SAR?
- M. If your firm shares a SAR with a parent entity (or entities), does it have a written confidentiality agreement in place specifying that the parent (or parent entities) must protect the confidentiality of the SAR through appropriate internal controls?

If your firm shares a SAR, or any information that might reveal the existence of a SAR, with an affiliate, does it have policies and procedures, as part of its internal controls, which ensure that its affiliate protects the confidentiality of the SAR? Note that any affiliate receiving a SAR from your firm must be subject to a SAR regulation and cannot share the SAR with another affiliate.

- N. What kind of due diligence does the firm do to ensure that any requests for SARs or SAR supporting documentation come from a representative of FinCEN or an appropriate law enforcement or supervisory agency? What procedures will the firm use to complete this verification?
- Q. Does the firm have additional risk-based measures to help ensure the confidentiality of SARs, including limiting access to the SARs, using cover sheets for SARs or supporting documentation that indicates the filing of a SAR, or using electronic notices that highlight confidentiality concerns before a person may access or disseminate the information? Does the firm include information on SAR confidentiality and the penalties associated with unauthorized disclosure in its ongoing training of employees?
- R. Does the firm obtain a written request from a law enforcement agency when the agency is requesting that the firm keep a particular account open? If so, what type of documentation is maintained and for what time period does the firm keep the documentation?

Other

- A. If your firm is an FCM, what steps does the firm take to respond to FinCEN information requests (e.g., 314(a) biweekly request)?
- B. If responsibilities for conducting AML compliance, other than CIP responsibilities, are divided between your firm and an FCM or IB, what documentation does your firm maintain to indicate how those responsibilities are divided? How does the firm ensure the other firm is adhering to the AML procedures?
- C. If your firm is an FCM that guarantees introducing brokers ("GIB"), how does it ensure that the firm's GIBs are adhering to their AML procedures?
- D. If your firm is an FCM, how does your firm comply with the currency transaction reporting and funds transfer recordkeeping requirements set forth in the Bank Secrecy Act?
- E. Does your firm accept private banking accounts maintained for non-U.S. persons? If so, what kind of special due diligence does the firm perform for

those accounts? If not, how does the firm screen new accounts to ensure that it does not accept this type of account?

- F. Does your firm accept private banking accounts maintained by or on behalf of senior political figures? If so, what enhanced scrutiny does the firm conduct for private banking accounts maintained by or on behalf of senior political figures? If not, how does the firm screen new accounts to ensure that it does not accept this type of account?
- G. Does your firm have a procedure to file the required FBAR report if it has a financial interest or signature authority over any financial accounts which exceed \$10,000 in a foreign country at any time during the calendar year?
- H. Does your firm (only FCMs) have a procedure to file a Report of International Transportation of Currency or Monetary Instruments (CMIR) if your firm transports amounts exceeding \$10,000 internationally under certain circumstances?
- I. Does the firm accept correspondent accounts established, maintained or administered by the firm in the US for a foreign financial institution. If so, what procedures or controls have the firm established over the account that will allow the firm to reasonably detect and report any known suspected money laundering activity conducted through or involving the correspondent account? If not, it is sufficient to indicate that the firm will not open any correspondent accounts.
- J. What are the firm's procedures regarding Section 311 Special Measures? Does the procedures require the firm to monitor FinCEN's website for information on foreign jurisdictions, institutions, classes of transactions, or types of account that have been designated as a primary money laundering concern and any special measures that have been imposed? Does the firm's procedure require the firm to follow any special measures that have been imposed?
- K. Which individuals or departments are trained, at least every 12 months, on the firm's overall AML program?
- L. Which individuals or departments are trained to monitor unusual trading activity to detect suspicious activity? How often do these employees take the training?
- M. Who conducts the training and what areas does it cover? Be specific for each group of employees who receive training.
- N. Other than documents obtained or made during the CIP process, what AML documents and records does the firm maintain? How long are they maintained? Be specific.
- O. Which independent firm personnel or experienced outside party will conduct annual testing on the adequacy of the firm's anti-money laundering program at least every 12 months?
- P. What areas are reviewed in the annual audit?

- Q. Who in senior management or on the audit committee receives the results of the independent audit?
- R. Who in senior management or on the audit committee reviews and signs off in writing on the independent audit report?
- S. How will the firm address deficiencies noted in the annual AML audit report?

Appendix C - Business Continuity & Disaster Recovery Plan Questionnaire

Each National Futures Association ("NFA") Member firm must adopt a written business continuity and disaster recovery plan tailored to its operations. NFA has developed the following questionnaire to assist firms in meeting that requirement.

The firm should maintain its business continuity and disaster recovery plan with other firm procedures. Having a written policy is not enough to meet your regulatory requirements, however. You must also implement and follow that policy and communicate it to your employees.

Please also consult the following NFA Rule and Interpretive Notice when designing your plan:

NFA Rule 2-38. Business Continuity and Disaster Recovery Interpretive Notice "NFA Compliance Rule 2-38: Business Continuity and Disaster Recovery Plan".

A Member firm's written policy should answer all of the following questions as completely as possible. Although you may answer "not applicable" to particular questions, you should carefully consider the firm's operations before doing so.

- A. Where are the firm's backup facilities (including systems and personnel) located? Are the backup facilities located in separate geographical areas from the primary facility? Are the backup facilities on a different power grid than the primary facility? Do they utilize a different telecommunication vendor?
- B. What are the firm's procedures for backing up or copying essential documents and data? How often is this done?
- C. Does the firm store the information in hard copy? In electronic format? Where is the backup information stored?
- D. What staff competencies or duties are critical to continuing your operations? How has your firm duplicated these competencies in order to minimize the effect on the firm's operations if it loses primary staff?
- E. What specific steps will the firm take to minimize the impact of business interruptions encountered by the following third parties:
 - Banks?
 - Carrying brokers?
 - Order routers?
 - Data providers?
 - Other third parties that are critical to continuing your operation? Be specific.

- F. Describe the firm's disaster-related communication plan. Specifically, how will the firm contact each of the following essential parties:
- Employees?
 - Customers?
 - Carrying brokers?
 - Vendors?
 - Other third parties that are essential to continuing your operation? Be specific.
- G. How often does management review the plan for needed updates? What evidence does the firm maintain as proof that a review was completed?
- H. How often is the plan tested for effectiveness? Describe the testing process, including whether the firm plans to participate in any industry-wide disaster recovery testing. What evidence does the firm maintain as proof that a test was completed?
- I. Where does the firm maintain copies of the plan? Is the plan kept at one or more off-site locations that are readily accessible to key employees? Be specific.
- J. List the key employees that have received the plan. Has the plan been explained to these employees? What essential components have been discussed with all other employees? How often will the plan be communicated or distributed to employees?
- K. What procedures are in place to ensure that any updated plan is distributed to key employees and that all other employees are notified of changes to essential components?
- L. Have FCM Members provided NFA with, and maintained the emergency contact information for, all key management employees? Additionally, have the firms provided NFA with the location, address and telephone number of its primary and alternative disaster recovery sites?
- If not, this information can be updated through the WinJammer™ Online Filing System.*
- M. Have IB, CPO, or CTA Member firms provided NFA with emergency contact information for one or more individuals whom NFA can contact in the event of an emergency?
- If not, this information can be updated in the firm's annual questionnaire. Go to NFA's website home page under the "Annual Update" heading Then click on "Annual Questionnaire." Members will need an ORS sign-on ID and password to gain access.*
- N. The components listed in letters A through N are the minimum areas that the plan should address. Please include additional information on any other areas that are essential to your operations.

Appendix D - Ethics Training Policy Questionnaire

Each National Futures Association (“NFA”) Member firm must adopt a written ethics training policy tailored to its operations. NFA has developed the following questionnaire to assist firms in meeting that requirement.

The firm should maintain its ethics training policy with other firm procedures. Having a written policy is not enough to meet your regulatory requirements, however. You must also implement and follow that policy.

Please also consult the following NFA Rule and Interpretive Notice when designing your plan:

NFA Rule 2-9. Supervision. Interpretive Notice “NFA Compliance Rule 2-9: Ethics Training Requirements”.

A Member firm’s written policy should answer all of the following questions as completely as possible.

- A. Who conducts the ethics training? If the firm conducts training in-house, who are the training personnel (by name or title)? If the firm utilizes an outside provider, what is the provider’s name?
- B. What are the training personnel’s or provider’s qualifications? What proof does the firm maintain that the training personnel or provider are qualified to conduct ethics training?
- C. What type of medium (e.g., Internet, audiotapes, computer software, video tapes, in-person courses) does the firm utilize for the ethics training course?
- D. How frequently are employees required to complete the training? Specifically, how soon and how often are new registrants required to complete ethics training? How often are other registrants required to complete ethics training?
- E. How long is the ethics training program for new registrants? For existing registrants?
- F. List the topics the ethics training program addresses.
- G. What type of written materials are distributed during training? How does the firm ensure that it maintains copies of those materials?
- H. What type of documentation or records does the firm maintain as proof that its employees have completed the ethics training?
- I. How often does management review the firm’s ethics training policy?

Appendix E - Privacy Policy Questionnaire

National Futures Association (“NFA”) has developed the following questionnaire to assist firms in meeting their obligations under the CFTC’s privacy rules.

Many elements of the firm’s privacy policy must be described in the privacy notice given to customers. The firm’s policy and procedures for protecting customer records and information (see Question C) must be in writing separate from the privacy notice and should be maintained with the rest of the firm’s written procedures. Although the firm is not technically required to have a separate document describing every aspect of its privacy policy and procedures, a comprehensive written policy is the best way to ensure that firm personnel know what the firm’s policy is. This is important because just having a policy is not enough to meet your regulatory requirements. You must also implement and follow that policy.

The questions listed below are very general and do not cover every aspect of the privacy rules. You should consult the following CFTC Regulations when designing your privacy policy:

CFTC Regulation 160 -- Privacy of Consumer Financial Information

A firm’s privacy policy should answer all of the following questions as completely as possible. Although you may answer “not applicable” to particular questions, you should carefully consider the firm’s operations before doing so.

- A. Does the firm solicit, accept, or have any clients or customers who are individuals and who use the firm’s products or services primarily for personal, family or household purposes?

[NOTE: If the answer to this question is “NO,” the firm is not required to have a privacy policy and does not need to answer the remaining questions.]

- B. What types of nonpublic personal information does the firm collect from clients or customers? Be specific. (NOTE: Nonpublic personal information includes account numbers, trading history, account balances, social security numbers and all financial information obtained from the customer. It also includes names and addresses when that information is included in a list derived in whole or in part from nonpublic personal information, such as a list of the firm’s customers.)
- C. What does the firm do – administratively, technically and physically – to maintain the confidentiality and security of customer information?
- How does the firm safeguard paper documents?
 - How does the firm safeguard electronic information?
 - Who has access to nonpublic personal information?
 - How does the firm protect against unauthorized access, disclosure or use of the information?

- D. Does the firm disclose information to nonaffiliated third parties? If so, what categories of nonaffiliated third parties does the firm disclose customer information to? For each category, what information does the firm disclose and under what circumstances does the firm disclose it? Be specific.
- E. What types of information are included in the firm's written privacy notice? (If the firm has written privacy procedures, you should attach a copy of the privacy notice to those procedures.)
- F. When does the firm provide new customers with the firm's privacy policy? How often does the firm provide its privacy policy to existing customers?
- G. Under what circumstances does the firm provide its privacy policy to consumers who do not become customers?
- H. How does the firm distribute its privacy policy to customers (e.g., electronically or mailed, included with account statements)?
- I. Does the firm give customers an opt-out notice? (If the firm has written privacy procedures, you should attach a copy of the opt-out notice to those procedures.) [NOTE: Your firm does not have to give customers an opt-out notice if it does not share nonpublic personal information with nonaffiliated third parties.]
- J. When does the firm provide customers with amended privacy and opt-out notices?

Sources of Additional Information

American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036
(212) 596-6200
www.aicpa.org

Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581
(202) 418-5000
www.cftc.gov

Futures Industry Association/Institution for Financial Markets
2001 Pennsylvania Avenue, N.W. Suite 600
Washington, D.C. 20006
(202) 466-5460
(202) 223-1528
www.futuresindustry.org
www.theifm.org

Managed Funds Association
2025 M Street, N.W. Suite 800
Washington D.C. 20036-3309
(202) 367-1140
www.mfainfo.org

Financial Industry Regulatory Authority
1735 K Street, N.W.
Washington, D.C. 20006
(202) 728-8000
www.finra.org

National Futures Association
300 South Riverside Plaza
Suite 1800
Chicago, IL 60606
(312) 781-1300
www.nfa.futures.org

National Introducing Brokers Association
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