

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 170

RIN Number 3038-AE09

Membership in a Registered Futures Association

AGENCY: Commodity Futures Trading Commission.

ACTION: Notice of Proposed Rulemaking.

SUMMARY: The Commodity Futures Trading Commission (“Commission”) proposes to amend its regulations to require that all persons registered with the Commission as introducing brokers (“IBs”), commodity pool operators (“CPOs”), and commodity trading advisors (“CTAs”) must become and remain members of at least one registered futures association (“RFA”).

DATES: Comments must be received on or before **[INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

ADDRESSES: You may submit comments, identified by RIN number 3038-AE09, by any of the following methods:

- The agency’s website, at <http://comments.cftc.gov>. Follow the instructions for submitting comments through the website.
- Mail: Melissa D. Jurgens, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.
- Hand Delivery/Courier: Same as mail above.

- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.

Please submit your comments using only one method.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to <http://www.cftc.gov>. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that you believe is exempt from disclosure under the Freedom of Information Act, a petition for confidential treatment of the exempt information may be submitted according to the procedures established in § 145.9 of the Commission's regulations.¹

The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse or remove any or all of your submission from <http://www.cftc.gov> that it may deem to be inappropriate for publication, such as obscene language. All submissions that have been redacted or removed that contain comments on the merits of the rulemaking will be retained in the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under the Freedom of Information Act.

FOR FURTHER INFORMATION CONTACT: Andrew Chapin, Associate Director, Division of Swap Dealer and Intermediary Oversight, 202-418-5465, achapin@cftc.gov; Jason Shafer, Attorney Advisor, Division of Swap Dealer and Intermediary Oversight, (202) 418-5097, jshafer@cftc.gov; or Hannah Ropp, Economist, 202-418-5228,

¹ 17 CFR 145.9. Commission regulations referred to herein can be found on the Commission's website, www.cftc.gov.

hropp@cftc.gov, Office of the Chief Economist, Commodity Futures Trading
Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.

SUPPLEMENTARY INFORMATION:

I. Background

Part 170 of the Commission's regulations pertains to RFAs. RFAs serve a vital self-regulatory role by functioning as frontline regulators of their members subject to Commission oversight. Regulations 170.15 and 170.16 require each registered futures commission merchant ("FCM"), and each registered swap dealer ("SD") and major swap participant ("MSP"), respectively, to become a member of an RFA, subject to an exception for certain notice registered brokers or dealers.² However, there is no such mandatory membership requirement for other registrants. In the absence of a mandatory membership requirement, those registrants not already members of an RFA are nevertheless subject to the rules and regulations of the Commission,³ and, absent this proposal, the Commission would assume the role performed by the RFA for this class of registrants. Currently, the National Futures Association ("NFA") is the sole RFA under Section 17(a) of the Commodity Exchange Act ("CEA"),⁴ and it is also a self-regulatory organization ("SRO").⁵

² 17 CFR 170.15 and 170.16. See also Registration of Swap Dealers and Major Swap Participants, 77 FR 2613 (Jan. 19, 2012).

³ See 7 U.S.C. 21(e), which specifies that any person registered under the CEA, who is not a member of an RFA, shall be subject to such other rules and regulations as the Commission may find necessary to protect the public interest and promote just and equitable principles of trade.

⁴ 7 U.S.C. 21(a).

⁵ SROs include designated contract markets ("DCMs" or "exchanges"), swap execution facilities ("SEFs"), registered futures associations, and derivatives clearing organizations ("DCOs"). Among other things, SROs maintain and update a standardized audit program and coordinate audit and financial statement surveillance activities over firms that are members of more than one SRO.

II. Proposed Regulation

Section 8a(5) of the CEA authorizes the Commission to promulgate such regulations as, in the judgment of the Commission, are reasonably necessary to effectuate any of the provisions, or to accomplish any of the purposes, of the CEA.⁶ Section 17(m) of the CEA permits the Commission to require membership in an RFA if the Commission determines that mandatory membership is necessary or appropriate to achieve the purposes and objectives of the CEA.⁷ Pursuant to its statutory authority, the Commission hereby proposes to amend Part 170 by adding § 170.17 to require each person registered as an IB, CPO, or CTA to become and remain a member of an RFA based on its preliminary belief that such membership is necessary or appropriate to ensure comprehensive and effective market oversight which is applied consistently to all registered intermediaries.

The Commission previously promulgated § 170.15 to require, subject to an exception for certain notice registered securities brokers or dealers, that all persons registered with the Commission as FCMs must become and remain members of at least one RFA.⁸ NFA Bylaw 1101 states that no member of NFA may “carry an account, accept an order or handle a transaction” in commodity futures contracts for, or on behalf of, any non-member of NFA that is required to be registered with the Commission as, inter alia, an IB, CPO, or CTA.⁹ Accordingly, any IB, CPO or CTA required to be registered that desires to conduct business directly with an FCM must become a member

⁶ 7 U.S.C. 12a(5).

⁷ 7 U.S.C. 21(m).

⁸ Membership in Registered Futures Association, 72 FR 2614 (Jan. 22, 2007).

⁹ NFA Bylaw 1101 is available at:

<http://www.nfa.futures.org/nfamanual/NFAManual.aspx?RuleID=BYLAW%201101&Section=3>.

of NFA, and derivatively, must ensure that it conducts business only with those IBs, CPOs or CTAs that also are NFA members. Therefore, given the NFA's status as the sole RFA under Section 17(a) of the CEA, at the time it was proposed, the Commission noted that § 170.15 would operate in conjunction with NFA Bylaw 1101 to assure essentially complete NFA membership from the universe of commodity professionals: FCMs, CPOs, CTAs and IBs.¹⁰

In proposing new Regulation 170.17, the Commission recognizes that due to recent changes to the CEA, § 170.15 and NFA Bylaw 1101 will no longer assure NFA membership for all IBs, CPOs or CTAs. In particular, the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") amended the CEA to establish a comprehensive new regulatory framework for swaps.¹¹ The new regulatory framework provides that, among other things, entities that engage in regulated activity with respect to swaps will be required to register with the Commission as IBs, CPOs, or CTAs, as appropriate. However, due to the unique nature of swap transactions, it may be possible for these Commission registrants to serve clients without interacting with a firm that "carries an account," e.g., an FCM or an SD who accepts customer funds. For example, a CTA may advise a "special entity" on swaps in the capacity of an "independent advisor," pursuant to section 4s(h)(5) of the CEA,¹² or a CPO may operate a pool that trades only swaps that are not cleared through a DCO. As a result, these registrants would not be

¹⁰ Membership in a Registered Futures Association, 71 FR 64171 at n.7 (proposed Nov. 1, 2006). The Commission notes that proposed § 170.17, like § 170.15 and § 170.16, does not directly require associated persons ("APs") to join a RFA. This is because APs must be sponsored by one of the aforementioned entities.

¹¹ Public Law 111-203, 124 Stat. 1376 (2010).

¹² See, e.g., Business Conduct Standards for Swap Dealers and Major Swap Participants with Counterparties, Final Rule, 77 FR 9734, 9825 (Feb. 17, 2012).

captured by the intersection of §§ 170.15 or 170.16, and NFA Bylaw 1101, and would not be required to become members of NFA.

Proposed § 170.17 would eliminate existing gaps in the regulatory oversight programs established by the Commission and NFA. The proposed rule would advance the Commission's effort to create an oversight regime that levels the playing field by ensuring consistent treatment of all its registered intermediaries, including FCMs, SDs, MSPs, IBs, CPOs, and CTAs.

In sum, consistent with Sections 8a(5) and 17m of the CEA, the Commission preliminarily believes that the proposed rule is necessary or appropriate to facilitate comprehensive and effective market oversight by NFA in its capacity as an SRO. By mandating membership in an RFA by each person registered as an IB, CPO, or CTA, the proposed rule would enable NFA to ensure compliance with Section 17 of the CEA, and rules and regulations thereunder. As the only RFA, NFA serves as the frontline regulator of its members, subject to Commission oversight. Without mandatory membership in NFA or another RFA, effective implementation of the programs required by Section 17 of the CEA and NFA's self-regulatory programs could be impeded.

III. Request for Comment

To ensure that the proposed rule would, if adopted, achieve its stated purpose, the Commission requests comment generally on all aspects of the proposed rule.

Specifically, the Commission requests comment on the following:

(1) Regulation 4.14(a)(9) was adopted on March 10, 2000.¹³ Regulation 4.14(a)(9) provides that a person is not required to register as a CTA if it does not: (i) direct any client accounts; or (ii) provide commodity trading advice based on, or tailored to, the commodity interest or cash market positions or other circumstances or characteristics of particular clients. This exemption from CTA registration generally pertains to persons only providing advice to the general public, such as in a newsletter, and not to specific clients. When adopted, Regulation 4.14(a)(9) did not require CTAs to de-register who were, at the time, registered with the Commission, but who could avail themselves of 4.14(a)(9). Therefore, many CTAs are currently registered with the Commission even though they qualify for an exemption from Commission registration pursuant to 4.14(a)(9). Should entities who are currently registered with the Commission but otherwise qualify for a Rule 4.14(a)(9) exemption be required to become members of NFA? If not, why?

(2) The Commission has not identified an impact on the risk management decisions of market participants as a result of the proposed regulation, but seeks comment as to any potential impact. Will proposed § 170.17 impact, positively or negatively, the risk management procedures or actions of intermediaries?

The Commission further requests comment on the specific questions included throughout this release.

IV. Administrative Compliance

A. Paperwork Reduction Act.

¹³ Exemption from Registration as a Commodity Trading Advisor, 65 FR 12938 (March 10, 2000).

The Paperwork Reduction Act of 1995 (“PRA”)¹⁴ imposes certain requirements on Federal agencies, including the Commission, in connection with their conducting or sponsoring any collection of information, as defined by the PRA. This proposed rulemaking would result in an amendment to existing collection of information OMB Control Number 3038-0023.¹⁵ The Commission is therefore submitting this proposal to the Office of Management and Budget (“OMB”) for review. If adopted, responses to this collection of information would be mandatory. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number.

Registration with the Commission requires each applicant for registration to, among other things, file a Form 7-R providing basic background and contact information.¹⁶ The proposed regulation would not require affected IBs, CPOs, and CTAs to register with the Commission, but only to become a member of the NFA.

As of April 11, 2013, NFA has indicated that 53 CPOs, CTAs, and IBs have applied for or have been approved for Commission registration solely because of their activity in the swaps market.¹⁷ Furthermore, NFA indicated to the Commission that, as of April 11, 2013, there are 756 non-FCM registrants that are currently registered with

¹⁴ 44 U.S.C. 3501 *et seq.*

¹⁵ See OMB Control No. 3038-0023, <http://www.reginfo.gov/public/do/PRAOMBHistory?ombControlNumber=3038-0023>.

¹⁶ The Commission has designated NFA to receive Form 7-R submissions on its behalf. The Commission notes that application for NFA membership is incorporated in Form 7-R.

¹⁷ Data provided by NFA was used in estimating this figure. Specifically, the data shows that, on April 11, 2013, there were 5 IBs, 1 IB/CTA, 30 CPOs, 8 CTAs, and 9 CPO/CTAs who indicated that they transact exclusively in swaps.

the Commission, but are not NFA members.¹⁸ Therefore, based on current information provided by NFA, the Commission estimates that there may be a total of 809 respondents affected by this proposed rule, and accordingly, the Commission preliminarily believes that OMB Collection 3038-0023 needs to be adjusted to account for an increase in the number of respondents. The proposed regulation would otherwise not impact the burden estimates currently provided for Collection 3038-0023.

The Commission seeks comment about the total number of respondents that it estimates may be impacted by the proposed rule, i.e., the Commission's preliminary estimate of 809 potential respondents. In particular, the Commission seeks comment as to the number of persons who have registered or plan to register as CTAs, CPOs, and IBs in order to serve the swap market exclusively and would be required to register with the Commission as a result of their activity in uncleared swaps (i.e., would not otherwise be captured by the aforementioned interplay of CFTC §§ 170.15 and 170.16 and NFA Bylaw 1101).

Information Collection Comments

The Commission invites the public and other Federal agencies to comment on any aspect of the reporting burdens discussed above. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments in order to: (1) evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including the information will have practical utility; (2) evaluate the accuracy of the Commission's estimate of the burden of the proposed collection of

¹⁸ Data provided by NFA was used in estimating this figure. Specifically, the 756 figure is calculated by adding the following (as of April 11, 2013, the total number of registered firms without NFA membership): 20 IBs, 1 IB/CPO, 2 IB/CTAs, 59 CPOs, 628 CTAs, and 46 CPO/CTAs.

information; (3) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (4) minimize the burden of the collection of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Comments may be submitted directly to the Office of Information and Regulatory Affairs, by fax at (202) 395-6566 or by e-mail at OIRASubmissions@omb.eop.gov. Please provide the Commission with a copy of submitted comments so that all comments can be summarized and addressed in the final rule preamble. Refer to the **ADDRESSES** section of this notice of proposed rulemaking for comment submission instructions to the Commission. A copy of the supporting statements for the collections of information discussed above may be obtained by visiting RegInfo.gov. OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication of this document in the Federal Register. Therefore, a comment is best assured of having its full effect if OMB receives it within 30 days of publication.

B. Regulatory Flexibility Act.

The Regulatory Flexibility Act¹⁹ requires that agencies consider whether the rules they propose will have a significant economic impact on a substantial number of small entities and, if so, provide a regulatory flexibility analysis respecting the impact.

1. CPOs

The Commission has previously determined that CPOs are not small entities for purposes of the Regulatory Flexibility Act.²⁰ Accordingly, the Chairman, on behalf of

¹⁹ 5 U.S.C. 601 et seq.

²⁰ Policy Statement and Establishment of Definitions of “Small Entities” for Purposes of the Regulatory Flexibility Act, 47 FR 18618, 18619 (Apr. 30, 1982).

the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that the proposed rules will not have a significant economic impact on a substantial number of small entities with respect to these entities.

2. IBs and CTAs

The Commission has previously determined to evaluate within the context of a particular rule proposal whether all or some IBs or CTAs should be considered to be small entities and, if so, to analyze the economic impact on them of any such rule.²¹

Since there could be some small entities that register as IBs or CTAs, the Commission is considering whether this rulemaking would have a significant economic impact on these registrants. The proposed rules would require all CTAs and IBs who register with the Commission to become members of an RFA. As previously noted, this would require CTAs and IBs to “check a box” on Form 7-R and ensure they are prepared for an NFA audit.²² However, as discussed below, the Commission preliminarily believes that any costs associated with preparing for an audit by the NFA should not be substantially different from, or significantly exceed, the costs associated with preparing for an audit by the Commission, which every registered entity would already be responsible to do.²³ To the extent that this proposed rule only pertains to CFTC

²¹ See, with respect to commodity trading advisors, 47 FR at 18620, and see, with respect to IBs, Introducing Brokers and Associated Persons of Introducing Brokers, Commodity Trading Advisors and Commodity Pool Operators; Registration and Other Regulatory Requirements, 48 FR 35276 (Aug. 3, 1983).

²² See infra note 28. As stated in the booklet titled “NFA Regulatory Requirements: For FCMs, IBs, CPOs, and CTAs,” NFA audits have two major objectives: (1) To determine whether the firm is maintaining records in accordance with NFA rules and applicable CFTC regulations; and (2) 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.

²³ The Commission believes that many of the recordkeeping obligations associated with preparing with a NFA audit are already required for Commission registrants. For example, Sections 4.23

registrants, the Commission preliminarily believes that any audit-related costs incident to NFA membership would be minimal, and should not have a significant economic impact on IBs, CPOs, or CTAs that are small entities. Consequently, the Commission finds that there is no significant economic impact on IBs or CTAs resulting from this rulemaking.

Accordingly, for the reasons stated above, the Commission preliminarily believes that the proposal will not have a significant economic impact on a substantial number of small entities. Therefore, the Chairman, on behalf of the Commission, hereby certifies, pursuant to 5 U.S.C. 605(b), that the proposed regulations being published today by this Federal Register release will not have a significant economic impact on a substantial number of small entities.

C. Considerations of Costs and Benefits

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing an order. Section 15(a) further specifies that the costs and benefits shall be evaluated in light of the following five broad areas of market and public concern: (1) protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations.

1. Background

As discussed above, prior to the Dodd-Frank Act, the intersection of § 170.15 and NFA Bylaw 1101 effectively required most CFTC-registered intermediaries to be

and 4.33 of the Commission's Regulations are recordkeeping requirements associated with registered CPOs and CTAs, respectively. Moreover, given the average periodicity for NFA audits, the magnitude of annual audit-related costs is limited.

members of NFA. Because NFA Bylaw 1101 provides that NFA members transacting futures business on behalf of customers cannot transact with non-members, and § 170.15 requires all FCMs to be NFA members, any IB, CPO, or CTA that engages with an FCM is required to maintain NFA membership in order to transact in futures.

In assessing the costs and benefits of the proposed rule, the Commission, in consultation with the NFA, has identified the following typical scenarios in which, under the current Commission regulations and NFA rules, a firm is registered with the Commission, but is not an NFA member:

- A firm that is no longer in business, but subject to Commission action, is prohibited from withdrawing its registration with the Commission until after the Commission action is resolved, but, since the firm no longer actively participates in the futures markets, it has withdrawn its NFA membership (in other words, a firm has a “withdrawal hold”);
- A firm that is not ready to commence business as a CTA and/or CPO first becomes registered in order to complete the more complex process of being properly vetted for registration, and then adds membership later when it is preparing to commence trading and to submit a disclosure document to NFA for review;
- When an NFA member firm no longer has at least one principal who is registered as an AP of the firm, NFA rules provide that the firm’s membership can be withdrawn if the situation is not corrected. If the firm does not re-attain NFA membership by adding a new principal who is an AP of the firm, typically the firm’s registration is subsequently withdrawn as well;

- CTAs that do not manage accounts consistent with the parameters of § 4.14(a)(9) register with the Commission, but are not required to become members of NFA and thus do not become members of NFA.

Moreover, the Dodd-Frank Act amended the CEA to establish a comprehensive new regulatory framework for swaps markets. Accordingly, an intermediary that was previously not required to register with the Commission because its activities were limited to swaps may now be required to register with the Commission. However, unlike futures transactions, because some swaps can be entered into bilaterally and not be cleared through a central counterparty (in other words, will not necessarily require the use of an FCM, SD, or MSP), the intersection of §§ 170.15 and 170.16 and NFA Bylaw 1101 may not require an IB, CPO, or CTA who transacts only in uncleared swaps to become a member of an RFA.²⁴

Proposed § 170.17 would eliminate these gaps in the regulatory oversight programs established by the Commission and NFA. In conjunction with § 170.15, which requires all FCMs to become members of an RFA, and § 170.16, which requires all SDs and MSPs to become members of an RFA, the Commission is intending to create an oversight regime that levels the playing field by ensuring consistent treatment of all its registered intermediaries. The Commission preliminarily believes that the proposed regulation is necessary to ensure comprehensive regulation and equal oversight of all intermediaries.

²⁴ Under the current Regulations and NFA bylaws, a IB, CPO, and CTA who transacts only in uncleared swaps with another IB, CPO, or CTA who similarly limits its transactions to uncleared swaps, will not be required to become a member of NFA so long as both parties are (1) not members of NFA and (2) continue to transact only in uncleared swaps with similarly-situated entities.

2. Costs

There would be certain costs associated with the proposed regulation. First, affected CFTC registrants would be required to become NFA members. The Commission understands that the process for a current CFTC registrant to become an NFA member amounts to checking a box on the CFTC registration form and updating some contact information; thus, the Commission preliminarily believes the cost of filing for membership to be less than one half-hour of labor.²⁵

Affected entities would also be subject to certain membership fees. The Commission understands that NFA imposes initial membership dues and annual membership dues for IBs, CPOs, and CTAs. Currently, the initial membership dues to become an NFA member are \$750 for the first year, and the annual dues to maintain membership are \$750 per year thereafter.²⁶

The Commission preliminarily believes that the rule may impose certain compliance costs on affected entities. However, such costs should not be substantially different from or significantly exceed the costs associated with current Commission regulations. NFA members are subject to periodic audits by NFA. The Commission understands that NFA audits CPOs, CTAs and IBs every three to four years, but the frequency may vary depending on NFA's risk analysis.²⁷ The Commission also

²⁵ See Form 7-R, <http://www.nfa.futures.org/nfa-registration/templates-and-forms/form7-r.HTML>. Applications forms for NFA membership and Associate membership are incorporated in Forms 7-R and 8-R. See NFA Membership and Dues, <http://www.nfa.futures.org/nfa-registration/NFA-membership-and-dues.HTML>.

²⁶ See NFA Membership and Dues, <http://www.nfa.futures.org/nfa-registration/NFA-membership-and-dues.HTML>.

²⁷ The Commission notes that the NFA states that it seeks to audit all new registrants within the first year of NFA membership, and periodically thereafter. See <http://www.nfa.futures.org/nfa-faqs/compliance-faqs/audits/index.HTML>.

understands that while the direct cost of the audit is covered by the annual membership dues, members may incur indirect costs associated with an on-site audit, e.g., preparing for the audit and providing staff to assist NFA staff during the audit. The Commission has authority to ensure all IBs, CTAs, and CPOs, registered with the Commission are in compliance with Commission regulations applicable to IBs, CTAs and CPOs as Commission registrants and to conduct on-site examinations of the operations and activities of IBs, CTAs, and CPOs as Commission registrants. Given the existing costs associated with ongoing compliance and examinations under the Commission regulations currently in effect, the Commission preliminarily believes that the costs associated with preparing for an audit by the NFA should not be substantially different from or significantly exceed the costs associated with preparing for an audit by the Commission, which every registered entity is already responsible to do (e.g., have properly prepared and maintained books and records available for examination at all times).²⁸ All affected entities should expect to incur costs necessary to work with NFA to facilitate regulatory audits.²⁹ Therefore, the Commission preliminarily believes that IBs, CPOs, and CTAs covered by the proposed rule may incur few, if any, additional audit-related costs by virtue of their NFA membership.

Likewise, with respect to general, ongoing compliance costs, the Commission preliminarily believes that NFA membership would impose few additional costs on

²⁸ Entities that will become Commission registrants for the first time should expect to incur the costs of ensuring they are adequately prepared for an on-site examination by the Commission. Such costs, however, are not attributable to the present rule proposal.

²⁹ NFA provides a booklet titled “NFA Regulatory Requirements: For FCMs, IBs, CPOs, and CTAs,” the NFA Manual, CFTC Regulations, and the “Self-Examination Checklist,” which all NFA must complete on a yearly basis. All are available on NFA’s website at www.nfa.futures.org.

subject IBs, CPOs, and CTAs, because as Commission registrants, these participants would already be subject to the majority of regulations that NFA is responsible to enforce. Specifically, in its capacity as an SRO, NFA would act, in respect of entities subject to the proposed rule, as the frontline regulator for the programs required by Section 17 of the CEA and the regulations thereunder. Section 17 and those regulations, however, are applicable to subject entities, independent of whether they are NFA members. Accordingly, in the main, entities would not incur any additional general, ongoing compliance costs as a result of NFA membership. However, in certain limited situations, there may be costs associated with being an NFA member in excess of those costs incurred for being registered with the Commission. For example, the Commission's capital rules require that registered IBs maintain adjusted net capital equal to or in excess of the greatest of \$45,000 [or] the amount of adjusted net capital required by a registered futures association of which it is a member.³⁰ However, section 5 of the NFA Manual sets forth the following capital requirements for member IBs:

- (a) Each Member IB, except an IB operating pursuant to a guarantee agreement which meets the requirements set forth in CFTC Regulation 1.10(j), must maintain Adjusted Net Capital (as defined in CFTC Regulation 1.17) equal to or in excess of the greatest of:
 - (i) \$45,000;
 - (ii) 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);
 - (iii) For Member IBs with less than \$1,000,000 in Adjusted Net Capital, \$3,000 for each AP sponsored by the IB.³¹

Therefore, while the Commission preliminarily believes, as noted above, that comprehensive and effective market oversight conducted by NFA would enhance market

³⁰ See 17 CFR 1.17(a)(1)(iii).

³¹ NFA's manual is available at <http://www.nfa.futures.org/nfamanual/NFAManual.aspx?RuleID=SECTION%205&Section=7>.

oversight and promote effective implementation of the CEA, the Commission recognizes that in certain limited situations, the requirements to be an NFA member may be more stringent, and potentially most costly to comply with, than the requirements associated with being registered with the Commission. The Commission requests comment on whether there are any additional situations similar to the example described above where the costs associated with NFA membership diverge from the costs of Commission registration.

The Commission contacted NFA to determine the number of IBs, CPOs, and CTAs that would be directly impacted by this rule (i.e., currently registered with the Commission, but not currently members of NFA). NFA indicated to the Commission that, as of April 11, 2013, there were 756 non-FCM firms that are registered with the Commission, but are not NFA members.³² Large percentages of the identified IBs, IB/CPOs, IBs/CTAs, and CPOs — 90%, 100%, 100% and 66%, respectively — are firms that are subject to a withdrawal hold. A smaller percentage of CPOs/CTAs (46%) and CTAs (4%) also fit within this category. This category of entities — i.e., those intermediaries that are subject to a withdrawal hold — should not be affected by the proposed regulations because they are, in the majority of cases, no longer in business, and, in any case, are not actively trading.

Relying on the information provided by NFA, the Commission estimates that a combined 652 entities are CFTC registrants because of the activities that qualify them as a CPO, CTA or IB, but are not NFA members, equating to an initial cost to the industry

³² See supra note 18.

of approximately \$489,000.³³ In addition, the Commission anticipates a small cost to each firm to update the firm's registration statement and other paperwork necessary to become an NFA member. The Commission estimates annual ongoing cost to the industry of the same amount (\$489,000)³⁴ plus the indirect costs of the periodic audits, which the Commission cannot estimate at this time due to the entity-specific nature of the indirect costs incurred.

The Commission also asked NFA for estimates regarding the number of future IBs, CPOs, and CTAs who will be required to register for the first-time with the Commission because of their swaps activity. NFA indicated that 53 firms that have applied for or have been approved for Commission registration have indicated they participate exclusively in the swaps markets.³⁵ However, the Commission estimates that this number may increase after certain regulations affecting the registration status of swaps entities come into effect.³⁶ Moreover, as described above, this regulation would directly affect the subset of these new entities required to register for the first time because they are active exclusively in the uncleared swaps market and engage with similarly-situated entities. The Commission preliminarily believes that many entities

³³ See *supra* note 18. Specifically, the 652 figure is calculated by adding the following (as of April 11, 2013): 2 IBs, 20 CPOs, 605 CTAs, and 25 CPO/CTAs. To arrive at the monetary estimate, the 652 figure was multiplied by the \$750.00 per-entity initial cost. The Commission notes, however, that some entities currently registered with the Commission may withdraw their registration because they are inactive in derivatives markets or for some other reason. As a result, the total number of affected entities may be reduced, and corresponding total costs associated with the proposed rule may be lower.

³⁴ *Id.*

³⁵ See *supra* note 17. NFA indicated that on April 11, 2013, it had approved 52 firms that deal exclusively in swaps for registration as an IB, CPO, or CTA and that the IB, CPO, or CTA registration of 1 additional firm that deals exclusively in swaps is currently pending.

³⁶ For example, the Commission's final definition of the term "U.S. Person" as it relates to cross-border swap transactions could dramatically affect the number of market participants required to register with the Commission.

have yet to apply for registration under the Commission's new swaps market regime, and as such the Commission is not yet able to accurately determine the exact number of new registrants that will be affected by the proposed regulation.

The Commission requests comment on all aspects of its preliminary consideration of costs. Has the Commission accurately identified the costs of this proposed regulation? Are there other costs to the Commission, market participants, and/or the American public that may result from the adoption of the proposed regulation that the Commission should consider? The Commission seeks specific comment on the following:

- How many IBs, CPOs, and CTAs will be affected by the proposed regulation?
- How many entities are active only in the uncleared swaps markets and plan to register with the Commission — and so would need to become members of NFA as a result of the proposed regulation?
- What are the costs of an NFA audit? Please identify and, where possible, quantify such costs. Do the types of costs or amount of costs vary depending on whether the audit is online or onsite? Do market participants bear different costs with respect to NFA's periodic audits versus daily audits?
- Would the proposed rule result in ongoing compliance costs beyond those an entity would face as a result of being registered with the Commission? Are there any costs of NFA membership beyond those an entity would face as a result of being registered with the Commission?
- Are there other costs of NFA membership that the Commission should consider?

3. Benefits

The proposed regulation would enable the Commission to carry out its obligations pursuant to Section 17 of the CEA to delegate certain oversight responsibility for intermediaries, including IBs, CPOs, and CTAs, to an RFA. As described above, the NFA cannot enforce its rules over registrants who do not become NFA members, and existing regulations would not require all IBs, CPOs, and CTAs to become NFA members. Thus, the Commission proposed new § 170.17 to require IBs, CPOs, and CTAs to become NFA members analogously to how § 170.15 presently requires FCMs to become NFA members and how § 170.16 requires the same of SDs and MSPs. In so doing, the Commission preliminarily believes it would ensure a level regulatory playing field for all registered intermediaries. The proposed rule would enable the NFA to apply its experience as a SRO to oversee all registered IBs, CPOs, and CTAs.

In addition, the Commission preliminarily believes that by requiring membership in an RFA, the proposed rule would result in a more efficient deployment of agency resources which would otherwise have to be used to oversee these registrants who would, without this rule, not be overseen by NFA.

Moreover, by requiring all registered IBs, CPOs and CTAs to become NFA members, the public would benefit from NFA's developed set of rules and oversight capabilities to ensure the integrity of the swaps market and its participants. This increase in market integrity may lead to a corresponding increase in market participation as the public and market participants grow more confident in the safety of these markets. The Commission preliminarily believes that the proposed regulation would ensure that NFA

has the authority necessary to fulfill its delegated responsibilities to provide regulatory oversight and promote market integrity.

The Commission requests comment on all aspects of its preliminary consideration of benefits. Has the Commission accurately identified the benefits of this proposed regulation? Are there other benefits to the Commission, market participants, and/or the public that may result from the adoption of the proposed regulation that the Commission should consider?

4. Section 15(a)

Section 15(a) of the CEA requires the Commission to consider the effects of its actions in light of the following five factors:

a. Protection of Market Participants and the Public

The proposed regulation would protect the public by ensuring that all registered intermediaries are subject to the same level of comprehensive NFA oversight. Because the entities affected by the proposed regulation act as intermediaries for clients, it is imperative that these entities be subject to proper oversight in order to protect customers from wrongdoing.

The Commission seeks comment as to how market participants and the public may be protected by the proposed regulation.

b. Efficiency, Competitiveness, and Financial Integrity of
Markets

The proposed regulation would act to create a more level playing field for intermediaries, ensuring that all such registered entities are subject to the same level of

oversight and regulatory responsibility. In so doing, the Commission preliminarily believes the integrity of markets would be enhanced.

The Commission seeks comment as to how the proposed regulation may promote the efficiency, competitiveness, and financial integrity of markets.

c. Price Discovery

The Commission has not identified an impact on price discovery as a result of the proposed regulation, but seeks comment as to any potential impact. Will proposed § 170.17 impact, positively or negatively, the price discovery process?

d. Sound Risk Management

The Commission has not identified an impact on the risk management decisions of market participants as a result of the proposed regulation, but seeks comment as to any potential impact. Will proposed § 170.17 impact, positively or negatively, the risk management procedures or actions of intermediaries?

e. Other Public Interest Considerations

The Commission preliminarily believes that proposed § 170.17 may promote public confidence in the integrity of derivatives markets by ensuring consistent and adequate regulation and oversight of all intermediaries. Will proposed § 170.17 impact, positively or negatively, any heretofore unidentified matter of interest to the public?

List of Subjects in 17 CFR Part 170

Authority delegations (Government agencies), Commodity futures, Reporting and recordkeeping requirements.

For the reasons stated in the preamble, the Commodity Futures Trading Commission proposes to amend 17 CFR part 170 as follows:

PART 170 – REGISTERED FUTURES ASSOCIATIONS

1. The authority citation for part 170 is revised to read as follows:

Authority: 7 U.S.C. 6p, 12a, and 21.

2. In subpart C, add §170.17 to read as follows:

Subpart C – Membership in a Registered Futures Association

§170.17 Introducing Brokers, Commodity Pool Operators, and Commodity Trading Advisors.

Each person registered as an introducing broker, commodity pool operator, or commodity trading advisor must become and remain a member of at least one futures association that is registered under Section 17 of the Act and that provides for the membership therein of such introducing broker, commodity pool operator, or commodity trading advisor, as the case may be, unless no such futures association is so registered.

Issued in Washington, DC, on November 5, 2013, by the Commission.

Melissa D. Jurgens,

Secretary of the Commission.

Appendix to Membership in a Registered Futures Association – Commission Voting Summary

NOTE: The following appendix will not appear in the Code of Federal Regulations.

Appendix – Commission Voting Summary

On this matter, Chairman Gensler and Commissioners Chilton, O’Malia, and Wetjen voted in the affirmative; no Commissioner voted in the negative.