

UNITED STATES OF AMERICA  
Before the  
COMMODITY FUTURES TRADING COMMISSION

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CAPITAL MARKET SERVICES LLC

v.

NATIONAL FUTURES ASSOCIATION

CFTC Docket No. CRAA 09-02

OPINION AND ORDER

Capital Market Services LLC (“CMS”) filed a notice of appeal from a decision by the National Futures Association’s (“NFA”) Telemarketing Procedures Waiver Committee (“TPWC”) denying CMS’s request for a full waiver from the enhanced supervisory procedures imposed on some NFA member firms under NFA Compliance Rule 2-9. NFA filed a motion to dismiss for lack of subject matter jurisdiction, arguing that its decision is a non-appealable regulatory action. CMS opposes NFA’s motion to dismiss, arguing that the imposition of enhanced supervisory requirements upon it is in effect an appealable disciplinary action or alternatively a member responsibility action. The parties’ positions are fully set forth in their pleadings filed to date and no further briefing is required. While the parties disagree on how to characterize certain facts, there is no dispute as to the operative facts bearing on the Commission’s jurisdiction in this matter.

Section 17 of the Commodity Exchange Act (“CEA”), 7 U.S.C. § 21, provides for Commission appellate review of certain NFA decisions, as do the Commission’s Part 171 Rules, 17 C.F.R. §§ 171.1-171.50. Appealable decisions include NFA disciplinary actions and member responsibility actions. Section 17(h) of the CEA, 7 U.S.C. § 21(h). CMS does not dispute that the TPWC’s decision to impose enhanced supervisory requirements on CMS did not occur

through the NFA's well-established disciplinary and member responsibility procedures. Instead, CMS argues that NFA's imposition of enhanced supervisory requirements was effectively a disciplinary or member responsibility action that is subject to appeal. The record reveals that NFA had an adequate factual basis for imposing enhanced supervision and did so in accordance with its rules in a manner that does not appear to be a *de facto* disciplinary action. On this record, we find that the TPWC's enhancement of supervision of CMS is neither a *de facto* disciplinary action nor a member responsibility action. Based on this finding, we conclude that NFA's imposition of enhanced supervisory requirements in this case was not an appealable decision under the Commodity Exchange Act and the Commission's Part 171 rules.

Accordingly, we grant NFA's motion to dismiss.

## BACKGROUND

### I.

NFA is designated as a self-regulatory organization by the CFTC. NFA's responsibilities include registration and frontline review of sales practices of its member-registrants. NFA requires futures commission merchants such as CMS to train and properly supervise their sales staff, including registered associated persons ("APs"). NFA's rules require a registrant "to adopt supervisory procedures specified by the [NFA Board of Directors] for the supervision of telemarketing" when the employment history of the APs hired by the registrant fit certain criteria. Compliance Rule 2-9(b) ("Rule 2-9(b)"). See Record ("R.") Tab 14. The NFA's long-standing interpretive statement issued under Rule 2-9(b) specifies the criteria that trigger the enhanced supervision requirements and the additional steps that the firm must take in overseeing telemarketing. See R. Tab 14, Interpretive Notice 9021. As relevant here, NFA's enhanced supervision requirements are triggered when a firm has at least 20 associated persons and at least

20 percent of those APs having previously worked for a "Disciplined Firm." *Id.*, Interpretive Notice 9021, § II(B), at 3-4. An NFA member firm is designated by NFA as a "Disciplined Firm" when:

1. the firm has been formally charged by either the CFTC or NFA with deceptive telemarketing practices or promotional material;
2. those charges have been resolved; and
3. the firm has either been permanently barred from the industry at any time as a result of those charges or has been sanctioned in any way within the preceding five years as a result of those charges.

*Id.* at 3. Members are advised that the "obligation to adopt the enhanced supervisory requirements is conclusively established on any day on which its sales force meets," in particular, this 20-percent rule. *Id.* at 5, n.1.

## II.

CMS is a registered futures commission merchant and a forex dealer. Prior to October 14, 2008, CMS employed 16 registered APs. On October 14, 2008, Joseph Kim, a CMS compliance officer, entered the registration applications of four newly hired APs into NFA's Online Registration System ("ORS"). All formerly were employed by IFX Markets, Inc., a Disciplined Firm found liable for sales practice violations. The addition of these four names caused CMS to reach the NFA's threshold for enhanced supervision by NFA. That is, as of close of business on October 14, 2008, the firm had 20 associated persons and at least 20 percent of its APs had previously worked for a Disciplined Firm.

## III.

NFA's Rule 2-9 informs NFA's member registrants, including CMS, that NFA may request it to "adopt supervisory procedures specified by the Board for the supervision of telemarketing." R. Tab 14, Rule 2-9 at 1. On October 16, 2008, NFA's Compliance Department



notified CMS that the firm was subject to enhanced supervisory requirements under NFA's Rule 2-9. R. Tab 1. These enhanced supervision procedures included making audio records of all telephone conversations between CMS APs and existing or prospective customers. *Id.* In its October 16, 2008 notice, NFA staff advised CMS of the procedures it was required to implement, its right to request that some or all such procedures be waived, and various factors considered by NFA in deciding waiver requests. *Id.* at 2-3.

CMS applied for a complete waiver from NFA enhanced supervision on November 14, 2008, arguing that it should not be deemed to have exceeded the 20 percent threshold and that its current supervisory programs already satisfied "most" of the enhanced supervision procedures NFA imposed. R. Tab 2. CMS stated that five associated persons were supposed to be added to ORS at the same time on October 14, but that Mr. Kim did not enter the fifth name, that of Alexandra Shainskaya, on October 14 because he was interrupted by another work task. R. Tab 2, at 1-2. Mr. Kim entered Ms. Shainskaya's name into NFA's ORS on the afternoon of October 15, 2008. CMS contended that the submission of Ms. Shainskaya's name on October 15 resolved any issue with CMS's trigger of the 20-percent threshold on October 14. *Id.* CMS reasoned that Ms. Shainskaya's registration had brought CMS's total number of APs to 21, placing CMS under the 20 percent threshold.

CMS contended that Ms. Shainskaya's name was not added to dilute or circumvent the 20 percent triggering factor under NFA's Rule 2-9 procedures. *Id.* at 2 (stating that her "AP registration has no correlation to the employment of the four APs" from a Disciplined Firm). Ms. Shainskaya had worked at CMS since 2005. *Id.* at 1. She held the position of business development manager. *Id.* at 2. CMS acknowledged that Ms. Shainskaya's job did not require registration, but represented that she might need to be registered in the future. *Id.* CMS

maintained that it should not be burdened with heightened supervisory requirements based on the random sequence of data entry, contending that if Ms. Shainskaya's name had been the first, second or third name entered by Mr. Kim the previous day, the enhanced supervisory requirements would not have been triggered. *Id.* at 2. In its request for a waiver of enhanced supervision from NFA, CMS also described in summary fashion its then-current supervisory program for monitoring the sales practices of the APs it employed. *Id.* at 2-3. CMS represented to NFA that CMS's supervisory programs "already satisfy most of the requirements of the enhanced supervision." *Id.* at 2-3.

The NFA's Telemarketing Procedures Waiver Committee (TPWC) is NFA's designated decisionmaker for such waiver requests. R. Tab 1 at 2. NFA's Compliance Department informed the TPWC that it thought CMS's waiver request should be denied. R. Tab 3. NFA Compliance staff reasoned that CMS pierced the 20 percent threshold on October 14, 2008, and the fact that the ratio went down the next day with the addition of Ms. Shainskaya's name was "immaterial" to the triggering of Rule 2-9 under NFA's guidance protocol. R. Tab 3, at 6. NFA Compliance staff also observed that CMS's ongoing supervision of its APs was not "an entirely adequate substitute" for the NFA requirements. *Id.* at 6-7.

#### IV.

On May 6, 2009, the TPWC issued a decision that relieved CMS of one aspect of the NFA's enhanced supervision requirements (the obligation to maintain enhanced net capital), but let stand the remaining elements of heightened supervision (including audiotaping of AP phone calls with customers). Record Tab 8 (modifying enhanced supervision requirement of NFA's October 16, 2008 notification of enhanced supervisory requirements (Tab 1)). Specifically, the TPWC's decision meant that CMS was required to:

- make complete audio recordings of all telephone conversations between APs and customers or prospective customers and retain these for five years;
- catalog the recordings by AP and date; have APs maintain a daily solicitation log; and
- file monthly reports with NFA regarding its compliance.

See R. Tabs 1, 8. These requirements are forms of enhanced supervision available under NFA's Rule 2-9 and associated interpretative guidance. R. Tab 14.

NFA's TPWC addressed and rejected CMS's contention that NFA's decision to enhance supervision of CMS was unfair, concluding that imposition of the requirements was "neither inappropriate nor unduly burdensome to CMS's operations as a futures commission merchant and forex dealer member." R. Tab 8, at 1.

#### V.

CMS's appeal to the Commission followed on June 10, 2009. R. Tab 9. NFA moved for the CFTC to decline to accept the appeal or, in the alternative, to dismiss CMS's appeal. R. Tab 10. NFA also sought a stay in filing a record before the Commission until the Commission considered its request to decline to accept the appeal. CMS opposed this Motion to Dismiss. R. Tab 11. By Order dated July 14, 2009, the Commission denied NFA's request to stay NFA's obligation to file the administrative record with the CFTC. R. Tab 13.

### DISCUSSION

#### I.

The Commission's appellate authority with respect to decisions of registered futures associations is set forth in Section 17 of the CEA, 7 U.S.C. § 21. The CEA authorizes Commission review of final disciplinary actions and membership responsibility actions taken by a registered futures association such as NFA. Section 17(h) of the CEA, 7 U.S.C. § 21(h). The



CEA also sets forth the minimum procedural requirements that NFA must follow in taking such actions and the standards of review that the Commission must apply. Section 17(i) of the CEA, 7 U.S.C. § 21(i). *See also* Section 17(b)(9) of the CEA, 7 U.S.C. § 21(b)(9) (requiring the rules of a registered futures association to “provide a fair and orderly procedure” with respect to disciplinary actions). This statutory authority is implemented through the Commission’s Part 171 Rules, 17 C.F.R. §§ 171.1-171.50. Rule 171.1(a) limits the Commission’s review of NFA decisions to those issued in disciplinary, membership denial, registration and member responsibility actions. *See* 17 C.F.R. §§ 171.2(b), (g), (h) and (l) (defining disciplinary action, member responsibility action, membership denial action and registration action).

The NFA enhanced supervision procedures at issue here are distinct from these disciplinary and member responsibility actions. Congress mandated that self-regulatory organizations such as NFA establish special supervisory guidelines. *See* Section 17(p)(4) of the CEA, 7 U.S.C. § 21(p)(4) (providing that a self-regulatory association’s rules must include “special supervisory guidelines to protect the public interest relating to the solicitation by telephone . . . and make such guidelines applicable to those members determined to require such guidelines”). In particular, Congress made express that the type of supervisory requirements that NFA can impose included enhanced procedures for taping AP phone calls:

For example, firms which have previously been the subject of enforcement actions involving telemarketing or firms whose sales force or management structure includes a large percentage of persons who previously worked for and received training from such firms could be required to adopt enhanced supervisory procedures. Enhanced procedures could include, for example, the tape recording or outside monitoring of all telephone sales solicitations.

S. Rep. No. 101-191, 1st. Sess. 62 (Nov. 6, 1989).

## II.

In moving to dismiss CMS's appeal, NFA argues that its decision to impose enhanced supervisory requirements on CMS is not within the scope of our appellate jurisdiction. R. Tab 10 (NFA Motion to Decline Acceptance of Appeal or, in the Alternative, to Dismiss). CMS argues in opposition that the imposition of any enhanced supervisory requirements against it is the equivalent of an appealable disciplinary action or member responsibility action. R. Tab 12, CMS Opposition to Motion to Dismiss at 2. CMS asserts that the TPWC's decision was a "narrow concentration on a mere technical error," rendering NFA's action "nothing short of an unjust disciplinary action." *Id.* at 5. Based on facts that are undisputed, we disagree with CMS.

First, the TPWC's decision was not overly "narrow" in focusing on the 20 percent trigger. The decision of NFA's TPWC is consistent with NFA's longstanding articulation of the conditions under which it places one of its member registrants under enhanced supervision, including exceeding the 20 percent threshold. There is nothing unjust about the NFA enforcing a rule which, under published interpretive guidance, does not give leeway generally for a registrant to "unring" the bell by bringing itself back under the 20 percent threshold. NFA's Rule 2-9 supervisory enforcement procedures are "technical" in the sense that they have an arithmetic trigger, but that clarity does not render NFA's approach hypertechnical, let alone unjust. CMS does not dispute that it met the 20 percent threshold – it had a sufficient percentage of APs with a history at Disciplined Firms to warrant enhanced supervision – as of close of business on October 14, 2008.<sup>1</sup> From all that appears in the record before us, CMS has not presented any evidence that NFA applied its published guidance inconsistently, let alone punitively, when NFA

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<sup>1</sup> This employment history, under NFA's well-established guidance, indicated to NFA's TPWC that CMS had a potential for sales practice problems based on inadequate or inappropriate training or supervision by previous employers. R. Tab 14; NFA Rule 2-9; *see* 7 U.S.C. § 21(p).



imposed the requirements on October 16, 2008, and when the TPWC in part denied CMS's waiver request on May 6, 2009. *See* R. Tab 14, Interpretive Guidance at 5 n.1 ("obligation to adopt the enhanced supervisory requirements is conclusively established on *any day* on which its sales force meets one of the listed numerical criteria") (emphasis added).

Second, the TPWC decision was not a disciplinary one. A disciplinary action is a "proceeding brought by NFA to enforce its rules that may result in expulsion, suspension, censure, bar from association with a member, fine in excess of \$100 or any comparable sanction being imposed on a member or a person associated with a member." 17 C.F.R. § 171.2(b). No such sanctions have been imposed upon CMS. The automatic triggering of enhanced supervision under Compliance Rule 2-9, based on the 20 percent rule, is not a proceeding based on a suspected rule violation that may result in a sanction, but a prophylactic measure designed to prevent possible future misconduct. Far from being a sanction, NFA's enhanced supervision procedures may help registrants avoid sanctions by requiring better supervision of APs. *See* R. Tab 14 (NFA Interpretative Notice explaining that an AP from a Disciplined Firm may have "received inadequate or inappropriate training and supervision," including having "learned improper sales tactics," and that enhanced supervision is designed to ensure that improper training does not "taint their sales efforts"). The enhanced measures are a "supervisory tool used to prevent future misconduct, not a disciplinary measure to remediate past misconduct." *American Financial Corp. v. NFA*, [2005-2007 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 30,381 at 58,717, 2006 WL 3770772 (CFTC Dec. 21, 2006) (rejecting the claim that a firm's placement on the Disciplined Firms list is a sanction).

CMS asserts that NFA's decision was the result of a "mechanical, rigid, and unjustified" application of NFA's "triggering" software. R. Tab 12, at 14-15. That NFA had an internal

process to consider a waiver of the enhanced supervisory requirements and in fact the TPWC granted partial relief indicates this is not true. Moreover, CMS cannot establish the existence of a punitive motive by NFA, where it applied a clear rule to a set of facts to which the rule indisputably applies.

CMS also contends that its supervisory programs already complied with “most” of the enhanced supervision requirements. R. Tab 2, at 3. As NFA compliance staff observed, CMS’s undocumented assertion that it already recorded and monitored its APs’ sales communications was unaccompanied by any details on the frequency, focus, and duration of such monitoring. R. Tab 3, at 6. Moreover, this undocumented assertion, even if true, does not establish that the NFA action was disciplinary in nature. To the contrary, CMS’s position that NFA’s approach was unduly burdensome to the point of being punitive is undercut by CMS’s assertion that it already does “most” of what NFA required.

For these reasons, no appellate review is available to CMS under the Commission’s Rules for review of disciplinary actions. 17 C.F.R. §§ 171.23(a), 171.30-34.<sup>2</sup>

We are also not persuaded by CMS’s alternative argument that NFA’s imposition of enhanced supervisory requirements can be viewed as a member responsibility action under our decisions. A member responsibility action requires a finding by NFA that there is reason to believe summary action is necessary to protect the markets, and can involve NFA’s suspension of a party’s membership or a requirement that it restrict operations. 17 C.F.R. § 171.2(g). The

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<sup>2</sup> Because we decline jurisdiction, we do not reach the ultimate question whether the TPWC abused its discretion in not permitting CMS to avoid all enhanced supervisory procedures by, after-the-fact, registering Ms. Shainskaya. We do not resolve the factual question of whether Ms. Shainskaya’s name was added to the NFA database as an AP to attempt to undo the Rule 2-9 trigger or, as CMS insists, for unrelated reasons. A decision not to grant a full waiver based on these facts is not a disciplinary decision for the reasons NFA argues persuasively and thoroughly. CMS presents no legal authority to suggest that the Commission has ever held otherwise.

Commission has explained that such membership responsibility actions must comply with the procedures in the CEA for other disciplinary proceedings. *American Financial Corp. v. NFA*, [2005-2007 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 30,381 at 58,717 n.6, 2006 WL 3770772 (CFTC Dec. 21, 2006), *citing* 7 U.S.C. § 21(i). CMS does not explain how NFA's decision could properly be shoehorned within the language of 17 C.F.R. § 171.2(g). The TPWC's discretionary, partial denial of CMS's request for a waiver of enhanced supervisory requirements was not a "summary action" entered on an injunctive or emergency basis. *See* 17 C.F.R. § 171.2(g). Accordingly, no appellate review is available to CMS under 17 C.F.R. §§ 171.40-46 (appeals of membership responsibility actions).

In sum, because NFA has not taken a disciplinary or member responsibility action within the meaning of 7 U.S.C. § 21 and the Commission's Part 171 Rules, CMS may not seek appellate review before the Commission.<sup>3</sup>

### III.

We do not decide whether an NFA supervisory action could ever be so unjust as to be a pretext for a disciplinary action triggering Commission appellate jurisdiction. On this administrative record, it is sufficient to find that there is no evidence that NFA's TPWC acted outside of its supervisory enhancement authority or that NFA acted punitively in its imposition of enhanced supervisory measures. Accordingly, there is no legal basis for Commission

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<sup>3</sup> Because the Commission finds that the NFA action is not appealable, the Commission does not reach NFA's further argument that, even if it were, CMS would first be required to exhaust administrative remedies before NFA. *See* R. Tab 10, at 3-10. NFA takes the position that should CMS fail to comply with NFA's enhanced supervisory requirements, and be disciplined for doing so, then after exhausting administrative remedies before NFA's Business Conduct Committee, it could appeal any adverse decision to the Commission. *Id.*; *see* 17 C.F.R. § 171.1(b)(1) (excluding from Commission appellate review disciplinary actions where the aggrieved party has knowingly failed to pursue its internal right to appeal before NFA).



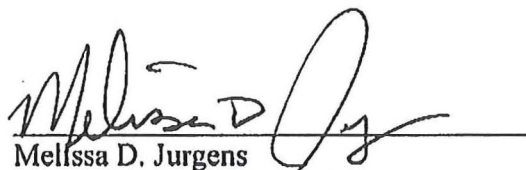
appellate review of the merits of the TPWC's discretionary decision not to grant CMS a full waiver from enhanced supervision.

**CONCLUSION**

Based on the foregoing, we decline to take jurisdiction of this matter. NFA's motion to dismiss CMS's appeal is granted, and this appeal is dismissed.

**IT IS SO ORDERED.**

By the Commission (Chairman GENSLER and Commissioners SOMMERS, CHILTON, O'MALIA and WETJEN).

  
Melissa D. Jurgens  
Secretary of the Commission  
Commodity Futures Trading Commission

Dated: May 15, 2013