WHITE PAPER:

Commodity Customer Protections and Regulations History and Potential Solutions for the Future 1938-2012

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I. Executive Summary

The October 31, 2011 bankruptcy of MF Global, among the 10 largest brokerage firms in the futures industry, sent shockwaves throughout the industry because of an alleged "missing" $600 million – $1.2 billion of customer segregated funds. As a result, an estimated 38,000 customers with futures trading accounts at MF Global have had their account funds frozen, and transferred only in part to receiving FCMs, with at least 28% of pre-bankruptcy balances still held in the bankrupt firm's estate and subject to bankruptcy proceedings and trustee decisions.

Violation of the sanctity of customer segregated funds – the regulatory requirement that customer monies must be held separately from brokerage firm assets and 100% available to the customer – by MF Global, one of the largest firms in the business, has shaken industry professionals and customers to their core. Thus, the call for improving the protection of customer funds in the futures industry.

Interestingly, the National Futures Association (NFA) conducted a 15-month study of customer account protections that it delivered to the Commodity Futures Trading Commission (CFTC) in 1986. Although 25 years old, its enumeration of customer protections and findings concerning alternative methods, such as an insurance fund, remain largely relevant. To use the 1986 Study as a starting point for further examination in today's environment, which reflects continued industry consolidation and public-company exchanges, would be valuable.

SIPC and FDIC Models

This report examines two other financial customer protection systems in the United States for insights into their history, structure, protections offered, funding and success. Most relevant is the securities customer account protection up to $500,000 ($250,000 in cash) via the Securities Investor Protection Corporation (SIPC). Formed in 1970 as a non-profit, member-funded organization, SIPC has helped recover $109 billion (with the SIPC Fund responsible for $1 billion) in missing assets due to securities firm failures for an estimated 739,000 investors.

The Federal Deposit Insurance Corporation (FDIC), a federal government corporation formed in 1934, guarantees the safety of deposits in member banks up to $250,000 per depositor per bank. No depositor has lost any insured funds as a result of a bank failure in FDIC's history.

NFA Customer Account Protection Study

In 1986, the four-year-old NFA prepared a report at the behest 15 months earlier of the CFTC to examine "whether insurance could play a role in reducing the impact of financial failures." The 122-page Study, although 25 years old, remains largely relevant to the issues facing the futures industry today in light of the MF Global bankruptcy. Although the key points have been summarized for this report's purpose, the entire NFA Study (attached in the Appendix) would be valuable for any interested party to the current discussion surrounding futures customer account protection.

The NFA Study examined the following areas: (1) history and analysis of the industry's insolvency risk from 1938 - 1985; (2) risk-reduction mechanisms currently in place as well as other possible risk-reduction measures; (3) insurance provided commercially or by industry self-insurance; (4) various contribution methods for generating income to support an insolvency response mechanism; and (5) potential administrative structures.

The NFA Study concluded that, in 1986, the "substantial and wide ranging" customer account protections in place – including net capital, segregation, FCM internal control systems, customer creditworthiness, industry margining systems, clearing association protections, information sharing and protections from bank failure – had been effective given the historically low incidence of loss. Indeed, over the 1938 - 1985 period, insolvency losses to commodities customers totaled less than $10 million, the majority of that the result of failures of non-exchange member FCMs surrounding the sale of "London options" and "deferred delivery contracts" from 1977 - 1980. (At the time, exchanges monitored exchange member firms only. Since then, the NFA was formed in 1982 and is charged with monitoring non-exchange member FCMs.)

Commodity Customer Coalition (CCC)

In order to ensure customer confidence in the futures industry, the Commodity Customer Coalition (CCC), formed by MF Global customers affected by the firm's bankruptcy, proposes six ideas that would protect customer assets from brokerage insolvency. CCC members include not only futures industry customers – varying from retail speculators to high-frequency traders to true hedgers – but also brokerage firms, regulators and legislators.

CCC proposes six low-cost changes to regulation, policies and bankruptcy law that would bolster the already robust financial protections in place for commodity customers. These include: (1) correct the tierd approach to regulating FCM categories; (2) bring financial oversight for all brokers under the purview of CME Group; (3) require daily customer fund segregation reports for all FCMS; (4) establish commodity customers as the first in line for recovered segregated funds in a bankrupt FCM's estate; (5) encourage CME Group to double and broaden its Protection Fund, with industry support, and encourage other exchanges to make similar efforts; and (6) research protection of other customer fund types, including foreign and forex.

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II. Current Situation

(As of February 3, 2012)

While there have been many examples of FCM failures over the years (mostly non-exchange member FCMs) in which no (or relatively few) customer funds were lost, the MF Global bankruptcy may be the first time in the modern history of the futures industry that customers lose money due to the failure of a clearing member firm. Indeed, when most portions of Refco went into bankruptcy in 2005, the company's structure kept the FCM Refco, Inc. out of those proceedings, which enabled business-as-usual while an orderly sale of the FCM assets and transfer of customer positions, funds and accounts could be made.

The other notable clearing member firm default was that of Volume Investors Corporation at the Comex Clearing Association (CCA) in New York in 1985. The inability of Volume customers to meet a margin call on naked short gold options precipitated the firm's failure. Although potential customer losses were $3.6 million in that case, all non-defaulting customers were made whole by: (1) Volume's house-account margin on deposit at CCA; (2) Volume's share of the CCA guaranty fund; and (3) the CCA's surplus funds.[1]

CME Protections

CME Group initiated two measures in reaction to the MF Global bankruptcy in addition to the Clearing House Guaranty Fund that ensures performance of a futures trade. On November 11, 2011, CME Group offered $300 million, including nearly the entire $50 million in capital from the CME Trust to cover customer losses, as a guarantee to the estate Trustee to accelerate the release of MF Global customer assets. Eleven days later, CME increased its guarantee to the Trustee to $550 millon from $250 million.

On February 2, 2012, CME Group announced a $100 million insurance fund to protect certain U.S. customers from similar FCM failures in the future. The Family Farmer and Rancher

[1] Customer Account Protection Study. National Futures Association. November 1986. Page 77.

Protection Fund would insure participating hedgers up to $25,000 per account for individuals and up to $100,000 per account for cooperatives against trades placed on CME Group markets. FCM customer fund losses greater than $100 million will result in the group receiving a pro-rata share of the fund amount. The fund will be backed by insurance, and is set to start on March 1, 2012.

Effect on Trading Volume

MF Global's bankruptcy on October 31, 2011 appears to have precipitated a surge in trading volume in November, a drop-off in December and a slow start to trading in January 2012. All three months show a decline in volume compared with the comparable year-earlier periods.

CME Group Volume						
Month	Total volume (million contracts)			Avg. Daily Volume (million contracts)		
	2010	2011	% Change	2010	2011	% Change
October	240	261	+8.8	11.4	12.4	+8.8
November	297	276	-7.1	14.2	13.2	-7.0
December	232	201	-13.4	10.5	9.6	-8.6
	2011	2012		2011	2012	
January	246	232	-5.7	12.3	11.6	-5.7

Source: CME Group data

MF Global Timeline

The following highlights are largely selected from a list tallied by John Lothian Newsletter. Please see www.johnlothiannewsletter.com/tag/mf-global-news/ for continued updates.

2011

October 25 Poor earnings, bond position revealed

October 26 Firm for sale

October 27 Credit downgraded to junk

October 31 Funds missing & Bankruptcy declared

November 4 CME Group completes account transfer & Corzine resigns

November 10 CFTC launches investigation

November 11 1,066 employees fired, lawsuits follow

November 11 CME Group guarantees $300 million

November 17	Judge OKs $520 million payout
November 21	Shortfall could exceed $1.2 billion
December 2	Remaining directors resign
December 5	CFTC approves “MF Global Rule”
December 8	Corzine testifies before Congress

2012

January 10	First plea deal request
January 12	Trustee says $3.8 billion distributed
January 18	SROs address seg fund safeguards
January 31	“Missing money” reportedly found, but not disclosed
February 2	CME announces $100 million fund for farmers/ranchers

Industry Task Forces

Three industry groups and the United States Senate Committee on Agriculture, Nutrition and Forestry (U.S. Senate Ag Committee) have gathered resources to recommend improvements in systems and regulations that were found lacking due to MF Global’s bankruptcy.

The CCC, incorporated as a non-profit organization on December 28, 2011, first met on January 4, 2012 in Chicago with 40 attendees, representing customers, FCMs, exchanges and regulators. Its goal is to make recommendations that will protect the customers of FCMs in any insolvency.

On January 17, 2012, Debbie Stabenow, chairwoman of the U.S. Senate Ag Committee , invited 20 “important participants in derivative markets” to provide “your evaluation of current policies and any recommendations you would like to make to this Committee on changes that would create stronger, safer markets and provide customers with greater protections.” The Committee will be considering policies that could help customer recover money, protect customer collateral and prevent similar bankruptcies.

On January 18, 2012, the five self-regulatory organizations in the futures industry formed a joint committee to address customer segregation issues. Initiated by CME Group and the NFA, members also include the InterContinental Exchange, Kansas City Board of Trade and Minneapolis Grain Exchange. The committee will make its recommendations by the end of March 2012 on new rules or ways that firms can demonstrate compliance with rules to prevent customer losses due to an FCM's insolvency.

The Futures Industry Association (FIA) established the Futures Market Financial Integrity Task Force on January 24, 2012 to develop and recommend specific measures that can be implemented though both industry best practice and regulatory change to restore customer confidence in the futures markets. The task force will consider areas such as: (1) enhanced financial recordkeeping and reporting requirements; (2) greater transparency regarding the investment of customer funds; (3) internal control standards for the customer funds segregation process; and (4) the adequacy of customer funds protections in the U.S. and abroad. The steering committee includes representatives from Bank of America Merrill Lynch, Barclays Capital, Citigroup Global Markets, CME Group, Credit Suisse Securities, Deutsche Bank, Getco, Goldman Sachs, HSBC, InterContinental Exchange, J.P. Morgan Securities, Morgan Stanley, Newedge and R.J. O'Brien & Associates. It expects to release its initial findings at the FIA Annual Meeting in Boca Raton, Florida in mid-March 2012.

III. Banking and Securities Industry Solutions

Certain customers in both banking and securities are covered by solutions that protect their assets, up to a limited amount, in the event of bank or brokerage insolvency. Both plans were developed to bolster retail customer confidence in their respective financial institutions. However, the two systems differ in their structure and funding, mainly due to the differences in the risk profile of the activities involved.

Federal Deposit Insurance Corporation (FDIC)

The FDIC guarantees the safety of deposits in member banks, up to $250,000 per depositor per bank (as of January 2012). It is a U.S. government corporation created by the Banking Act of 1933 in response to the losses sustained by individuals due to widespread bank failures during the Great Depression. Since the start of FDIC insurance on January 1, 1934, no depositor has last any insured funds as a result of a bank failure.

Deposits at an FDIC member bank are "backed by the full faith and credit of the United States Government." The FDIC was originally funded by a $289 million loan from the U.S. Treasury and Federal Reserve in order to provide deposit insurance of $2,500 per depositor per bank. Those limits have increased seven times to their current $250,000, and are now mandated to be reviewed every five years for potential adjustment.

Securities Investor Protection Corporation (SIPC)

SIPC protects investors in certain securities up to $500,000 of a customer's net equity balance, including up to $250,000 in cash. It is a federally mandated, non-profit, member-funded corporation created by the Securities Investor Protection Act of 1970 (SIPA). Following the "Paperwork Crunch" of the late 1960s, when securities brokerage firms were under pressure to invest in automated solutions to handle a massive increase in trading volume – and the failure of many firms as a result – U.S investors had little confidence in the securities industry.

Sen. Edward Muskie introduced SIPA to the Senate with these words: "The economic function of the securities markets is to channel individual institutional savings to private industry and thereby contribute to the growth of capital investment. Without strong capital markets it would be difficult for our national economy to sustain continued growth…The continued financial well-being of the economy thus depends, in part, on public willingness to entrust assets to the securities industry."

Although not every investor is protected by SIPC, its track record shows that 99% of eligible investors get their investments back from a failed brokerage. To receive the benefit, the customer's broker must have been a SIPC member. In addition to providing customer account insurance, SIPC also takes the lead in resolving asset distribution of a failed broker-dealer. Importantly, SIPC does not insure the underlying value of the financial assets at stake, and customers continue to bear market risk.

The current member assessment is one-fourth (1/4) of one (1) percent per annum of net operating revenues from securities business, as defined in SIPA, in order to maintain a target balance in the SIPC Fund of $2.5 billion. SIPC has authority to change the formula of member assessment in terms of both percentage and gross vs. net revenues based on the level of the SIPC Fund. SIPC also earns revenue for the Fund via interest on investments in U.S. Government securities. As a final backstop, the Securities Exchange Commission (SEC) has the authority to lend SIPC up to $2.5 billion, which it would borrow from the U.S. Treasury.

In late 2008, SIPC led two liquidation proceedings of monumental size and importance – Lehman Brothers Inc., the largest bankruptcy in U.S. history at $639 billion, and Bernard L. Madoff Investment Securities, a $50 billion Ponzi scheme. As of December 31, 2010, nearly all of Lehman's retail customer claims had been resolved, with SIPC advancing $8.4 million to cover investor losses. It may take several years to resolve remaining claims, and SIPC may have to make additional advances of as much as $1 billion. In the Madoff situation, the Trustee has recovered about $8.7 billion, about 50% of the principal estimated to have been lost by customers who filed claims with

SIPC. From its inception through 2010, SIPC has advanced $1.6 billion to make possible the recovery of $109 billion in assets for an estimated 739,000 investors.

The Lehman and Madoff cases created a spike in SIPC customer protection expenses, to nearly $1.5 billion in 2008, exceeding substantially the previous high of about $100 million in 2001. As a result, SIPC increased its member assessment to 0.25% of net operating revenues, effective April 1, 2009, from $150 annually since 1996, in order to build the SIPC Fund to $2.5 billion. The Fund stood at more than $1.5 billion in 2008, but fell to about $1 billion in 2009.

(See Appendix for supporting tables sourced from the SIPC 2010 Annual Report.)

IV. Customer Account Protection Study of 1986

In November 1986, the NFA completed a 15-month study of commodity customer account protections as well as the possibility of establishing a customer insurance fund to protect against brokerage insolvency losses. The most important observation of this work was that "substantial and wide ranging customer account protections" were already in place. In addition, the history of customer losses had been low and willingness to commit resources to regulation high.

The NFA did not make recommendations to the CFTC as a result of this Study, but clearly the report suggested that there was no perceived need to construct a customer insurance protection fund akin to SIPC.

Introduction

The idea of establishing commodity account insurance has been debated for nearly 40 years. Indeed, such a program (patterned after SIPC, formed four years earlier in 1970) was discussed during the Congressional debate that resulted in formation of the CFTC in 1974. The concern was that there "would be the need to protect the liquidity of the markets by preventing an erosion of public confidence."

However, instead of making an insurance plan part of the new agency's directives, Congress asked for further study on the matter. This resulted in a CFTC study by the Division of Trading and Markets known as the "417 Report." It concluded that there was no need for account insurance given the low ratio of benefits to costs that resulted from a statistical analysis of prior losses in the industry. In 1980, the Division again looked at the matter of customer account insurance, but did not complete its study.

The issue came up again in 1985 following the failure of Volume investors Corporation. That report, "Volume Investors Corporation: Report of the Division of Trading and Markets" of July 1985, according to the 1986 NFA Study, concluded that "there are ways other than SIPC-type insurance to protect customer funds from the dangers of an FCM insolvency." The NFA report

concluded: "…a failure on the part of a firm's internal control system or the relevant regulatory organizations may neutralize the benefits of the best protective mechanisms."

The 1986 NFA Study also addressed several misconceptions, including: (1) Is insurance the only way to protect customer funds? No. Many measures are in place and further ones would have to be justified on an analysis of benefit vs. cost.; (2) Does the loss history in the futures industry show a trend toward more frequent and larger losses? No. The trend prior to 1985 was for failures by firms not subject to exchange supervision.; (3) What do we mean by insurance? Besides SIPC-type insurance, protection could be seen as (a) facilitating transfer of positions; (b) varying payout formulas for small and large customers; and (c) voluntary response, as was the case in Volume Investors.; (4) Who is the "customer" whose account needs protecting? NFA suggests that less than 5% of volume comes from retail customers, those who presumably would need the most protection. Insurance for other futures market participants – exchange members, hedgers and financial institutions – was deemed to "have minimal relevance in view of their private arrangements to protect funds and the small likelihood that an insurance program could be scaled large enough to address failures of significance to them."; and (5) If insurance is deemed necessary, what should be its administrative structure? NFA concludes that the question is unanswerable until the protection scheme is devised.

Risk Analysis

The NFA compiled a complete list of insolvencies in the commodities industry from 1938 - 1985, based on data from CFTC reports. These are shown in Table A, which is replicated from the NFA Study. Note that the "dollars in jeopardy" column indicates funds that were not properly segregated at the insolvent FCM; the "actual losses" column shows about $10 million in customer losses over this 48-year period.

The NFA summarizes that "almost all of the failed FCMs were thinly capitalized, closely held firms with few principals. A majority of the failures involved some sort of malfeasance by

insiders. In many instances principals were prosecuted criminally for converting customer funds to their own use."

One case, in particular, sounds strikingly familiar to the MF Global situation – that of Weis Securities, Inc., which failed with $105,312 in jeopardy, but ultimately had no customer losses. The NFA Study says:

> Weis was an FCM and Broker/Dealer located in New York. In May, 1973 the New York Stock Exchange suspended Weis for failing to meet capital requirements. The SEC charged the firm with fraud as well as capital and recordkeeping violations. The firm was apparently properly segregated until just prior to the collapse. At that point the firm withdrew $90,000 from its customer omnibus account and the funds were deposited into one of the firm's general bank accounts where it was promptly used by the bank to offset a loan. The trustee was nevertheless able to pay the "regulated" commodity customers 100% of their balances because certain of these customers had debit balances in their security or "non-regulated" commodity accounts which could be netted. In addition, the trustee brought suit against the bank alleging that the $90,000 transaction was a preferential transfer. The trustee eventually prevailed and the $90,000 was returned to the estate.

It is clear that the MF Global bankruptcy, which put an estimated $600 million to $1.2 billion of customer funds at risk, is the tsunami of all previous FCM failures. With $41.05 billion in assets, it is among the 10 largest U.S. bankruptcies since 1980 (Table 1). Its closest futures industry comparison is Refco Inc., which failed in 2005 with $33.33 billion in assets. However, Refco's customer segregated funds were completely intact, so the ultimate sale of the FCM (to MF Global's predecessor Man Financial) and transfer of customer accounts and funds for exchange-traded products was completed with little customer disruption.

In what may bode well for the ultimate outcome with MF Global, the 1986 NFA Study of 48 years of brokerage insolvencies notes that it is "unusual in FCM failures for all of the customer funds to be missing, even in situations where funds have been converted by insiders. Receivers, trustees and regulatory authorities have had fairly good success at recovering or otherwise obtaining full or partial reimbursement to customers even when there is a shortfall of funds in segregation. In fact, it appears

that of customer funds actually missing, on average, one-half of that amount has eventually been recovered.

Table A Incidence of Insolvency Loss[2]			
Year	Number of Failures	Dollars in Jeopardy[3]	Actual Losses (dollars)
1938	1	35,000	35,000
1939	14	71,290	34,201
1940	4	102,084	100,834
1941	2	0	0
1942	1	0	0
1945	1	160,701	0
1946	2	0	0
1947	1	1,900	0
1961	2	0	0
1963	4	60,372	60,372
1965	1	8,174	8,174
1968	2	17,600	1,600
1969	4	572,109	172,109
1970	1	48,215	48,215
1973	2	122,930	76,472
1974	1	59,011	59,011
1976	1	160,000	0
1977	1	191,000	191,000
1978	11	3,143,000	1,775,000
1979	6	5,343,000	1,000,000
1980	5	7,954,000	6,319,000
1982	2	2,300,000	300,000
1983	1	93,000	0
1984	1	515,000	0
1985	2	3,700,000	100,000[4]

Source: NFA Customer Account Protection Study, Nov. 20, 1986

[2]The sources of the data contained in this table are: 1938 through 1974, the 417 Report; 1975 through 1985, the Division Study. Subsequent information referred to, infra, indicates that actual losses in 1980 are $1 million less than amount shown above.

[3]The term "jeopardy" is applied to funds which were not properly segregated and subject to misuse by the carrying FCM. The amount of actual loss by customers is always less than or equal to the amount of funds in jeopardy with the difference between such amounts being equal to the individual and industry efforts to reimburse customers.

[4] All non-defaulting customers of Volume have since been compensated for the entire amount of their equity balances which amounted to $3,600,000. U.S.A. Commodity Futures, Inc. is currently in receivership. The potential insolvency loss is approximately $100,000.

TABLE 1	
COMPANY/YEAR	**TOTAL ASSETS**
Lehman Brothers Holdings Inc (2008)	$639.00 billion*
WorldCom Inc (2002)	103.91 billion
General Motors Corp (2009)	91.05 billion
CIT Group Inc (2009)	80.45 billion
Enron Corp (2001)	65.50 billion
Conseco Inc (2002)	61.39 billion
MF Global Holdings Ltd (2011)	41.05 billion*
Chrysler LLC (2009)	39.30 billion
Thornburg Mortgage Inc (2009)	36.52 billion
Pacific Gas and Electric Co (2001)	36.15 billion
Texaco Inc (1987)	34.94 billion
Financial Corp of America (1988)	33.86 billion
Refco Inc (2005)	33.33 billion
Washington Mutual Inc (2008)	32.90 billion*
IndyMac Bancorp Inc (2008)	32.73 billion

* - from court documents
Source: Thomson Reuters

During these nearly 50 years of various FCM failures, the largest of which put $7.9 million of customer segregated monies in jeopardy, the NFA notes that "there has been a general willingness on the part of the exchanges to reimburse customers if the funds could not be otherwise recovered." In two periods, 1960 - 1977 and 1980 - 1985, the industry averaged one failure per year and $67,000 in losses. Between 1978 and 1980, there were 22 failures (all of them non-exchange members) with just over $9 million in customer losses – mainly due to dealing in London commodity options or illegal off-exchange deferred delivery contracts.

The NFA Study points out two primary reasons for FCM insolvency. First, the theft or conversion of assets by FCM insiders – often by principals – which indicates that prevention measures are tied to preventing that type of conduct. Second is the failure of risk management systems inside the FCM, often precipitated by customer deficits. Bank failure and clearing association default also could cause FCM insolvency, but had not during the years studied.

In the 1986 Study, the NFA came up with an approach to estimate the size of an insurance fund required to meet insolvency losses in an average year, based on the history of the industry to date. The assumptions were:

1. Firms that fail hold less than 50% of the per FCM average of segregated funds.
2. Missing funds are less than 50% of the segregation required of the failed firm.
3. 50% of missing funds are ultimately recovered.

Here's how those assumptions looked as of September 30, 1985 and August 31, 2011 (the last month that MF Global was included on the CFTC reports of FCM Financials).

Calculating an Estimated Response Mechanism		
	September 30, 1985	**August 31, 2011**
FCMs reporting to CFTC	223	126
Average segregated funds per FCM	$28.5 million	$1.7 billion [includes 4d(a)(2) and Pt.30]
50% of average seg funds	$14.25 million	$850 million
Missing funds = 50% of average seg funds	$7.125 million	$425 million
Recovered funds = 50% of missing funds	$3.5 million	$213 million
Annual availability of response mechanism to compensate customers	$3.5 million	$213 million

Risk Reduction Mechanisms

In 1986, at the time of the NFA Study, the CFTC had been in operation for 12 years and the NFA for four years. Thus, many regulations for risk-reduction had been established and implemented in the futures industry. The Study discussed six measures already in place as well as nine additional possibilities.

Risk Reduction Mechanisms Currently in Place

1. Net capital requirements

At the time of this Study, CFTC Rule 1.17 required FCMs to maintain adjusted net capital equal to at least the greatest of: (1) 4% of segregated funds; (2) the applicable SEC requirement if registered as a broker/dearler; or (3) $50,000. An FCM with a ratio of capital to segregated funds of 4%-6%, was considered on early warning and required to file financial statements monthly rather than quarterly. In practice, FCMs in 1985 typically had adjusted net capital equal to 80% of total segregation requirements.

2. Segregation requirements

The segregation requirement is straightforward: FCMs are required to segregate customer monies in special customer segregated funds depository accounts. The NFA Study points out: "FCMs must keep customer funds separate from firm assets and, unlike securites broker/dealers and banks, cannot use the funds or property of customers in any way to help finance their own business operations."

3. Internal control systems

Although many internal controls – as well as independent audits of such systems—are outlined, the NFA Study acknowledges the importance of the integrity of a firm's management. "Any system of internal control will be ineffective if management has overridden controls which are in place," the Study observes.

The internal controls outlined include: (1) competent, trustworthy personnel with clear lines of authority and responsibility; (2) adequate segregation of duties; (3) proper procedures for authorization; (4) adequate documents and records; (5) proper procedures for recordkeeping; (6) physical control over assets; and (7) independent checks on performance.

4. Customer creditworthiness procedures

The primary defense against defaults of customers that could precipitate insolvency is the "diligent and prompt collection of margins." In addition, the NFA Study reported that FCMs also

took steps to verify at least some of the financial information provided by prospective customers, and often set trading limits for customers.

5. Exchange clearing systems

Because futures trading is not a credit system like securities, clearing organizations that are the counterparty to every trade use daily pay/collects on all positions, original margin and daily price limits to protect against the risk of a clearinghouse default. They also can use capital-based position limits for clearing members as well as capital requirements related to concentration of positions and intraday margin calls.

6. Federal structures to remedy effects of bank failures

In the event that an FCM held deposits at an FDIC-member bank that failed, it would not suffer any losses if the deposits were assumed by a healthy bank. If that were not the case, then each individual customer of the FCM would be insured to the extent offered by FDIC insurance. At the time of the Study, it was estimated that about 75% of customer accounts had less than $100,000 equity and thus would be fully covered by the FDIC limits at the time. For larger accounts, the Study noted that FCMs typically hold less than 20% of customer property in cash, with more than 50% in securities that would be returned in full if the bank failed.

Additional Possible Risk Reduction Measures

1. Gross margining

Gross margining would require clearing member firms to deposit margin on each position rather than on the net long/short position. Hence, gross margining shifts funds to a clearinghouse and from an FCM. This reduces the risk of FCM malfeasance, increases diligence in collecting margin deficits from customers, facilitates transfer of accounts between FCMs and reduces interest income to the FCM. However, in the case of an FCM default, customer losses might actually increase because the clearinghouse would have more funds available from the FCM with which to satisfy obligations.

2. Changes in capital requirements

At the time of this Study, industry and regulatory discussions already were underway concerning an increase in minimum net capital requirements for an FCM.

3. Improvement in internal controls

These controls, for example, might include a minimum number of employees to satisfy segregation of duty responsibilities.

4. Improved creditworthiness standards

The Study concluded that it was best for FCMs to determine their own customer creditworthiness requirements rather than impose new regulations.

5. Separation of floor traders as a distinct class of customers

This idea held little appeal, particularly because it was assumed that the value of a trader's exchange membership provided security against a potential debit.

6. Information sharing

Pay/collect data, margins deposited and position information could be shared among exchanges and clearing associations. The Study notes that the Board of Trade Clearing Corp. (BOTCC) and CME, clearing 80% of U.S. futures, already shared daily pay/collect information.

7. Common clearing

Whether the risks to the industry would increase or decrease with consolidation into a single, centralized clearing organization were being debated at the time of this Study. Does having a single entity result in increased risk due to a presumed reduction in margin held, or decreased risk due to access and insight into a larger number of firms?

8. Futures contracts held in the name of the customer

This idea would mean that customer margin funds would be held in their individual names at the clearing association, essentially making the clearinghouse a large FCM and the FCM an introducing broker. It also was concluded that this system would be "enormously expensive and

difficult to maintain" and would take "immense data processing and recordkeeping facilities and manpower."

9. Fidelity bonding

The NFA found that it already was common practice to FCMs to bond their employees, but that those who might need it the most (small and new FCMs) may find it difficult or impossible to obtain. To require bonding was seen as putting small firms out of business and barring new firms from entering the industry.

Alternative Possible Responses to Insolvency

In addition to compensating customers of an insolvent firm with an insurance scheme like SIPC, the NFA Study considered two other responses – a transfer of open positions and a compensation program. The orderly transfer of customer positions to a healthy FCM was seen as beneficial not only to customers (hedgers, in particular), but also in facilitating the continued orderly operation of the futures markets and avoidance of forced liquidation of positions. "Immediate availability" of sufficient funds was considered key. Under the compensation alternatives, the NFA Study noted a variety of methods for distribution: (1) total compensation, with each customer's equity restored in full; (2) compensation limit per account, like SIPC; (3) limit per FCM insolvency; and (4) compensation limited to a percentage of funds in the account; however, because that likely would not result in pro rata distributions to customers it would require "substantive changes to the Part 190 Regulations."

Methods of Providing Resources Necessary to Respond to Insolvencies

The NFA looked at four types of insurance – two each from commercial and the industry – that could provide the resources deemed necessary to have available in the event of an FCM bankruptcy.

Commercial Insurance

At the time of the NFA Study, the insurance industry was under pressure from seven consecutive years of underwriting losses, to the point that Congress was holding hearings on the high

cost and scarcity of liability insurance. It was the opinion of two insurers interviewed by the NFA that a customer compensation policy would not be well-received by the insurance industry, would likely be limited to $10 million (about three times the estimated, potential annual average payout of $3.5 million), would require a deductible and would be dependent upon availability of reinsurance.

Another option would be "fronting" insurance, whereby the insurance company pays the initial claims and then receives total repayment from another entity, e.g., NFA; the insurance company assumes the risk of time in exchange for a fee.

Both commercial alternatives were considered such remote possibilities that no further study was conducted.

Industry Self-Insurance

An accumulated cash fund or letters of credit were considered as ways in which the industry could self-insure against customer losses due to FCM insolvency.

Many questions were raised regarding the accumulated cash fund, which was seen as a way to make funds readily available and increase the confidence of the investing public. However, an accumulated cash fund was seen as a "significant added burden" to firms already supporting self-regulation and federal regulation. In addition, there were concerns about how quickly it could be replenished if tapped, the cost of administering the fund, how to ensure equitable contributions, and whether it would require relief via federal legislation to not be considered to be conducting the business of insurance.

The outlook for providing letters of credit as an industry self-insurance solution was "not bright." Indeed, it would likely tap the same banks that already issue letters of credit to worthy FCMs, thereby increasing pressure on the same sources of funding.

Methods for Generating Income to Support an Insolvency Response Mechanism

The form of contribution to support a customer insurance program boiled down to three avenues: (1) a flat annual fee per firm, which has a regressive effect on small firms; (2) a per transaction cost, which is how NFA is funded and is generally favored due to the ease of which it can

be passed on to customers; and (3) a percentage of gross revenue, which places the largest burden on the largest firms. SIPC has used both a flat annual fee and a percentage of gross revenue (ranging from 1/8 of 1% to ½ of 1%) to raise funds.

In particular to the futures industry, the NFA Study outlined three methods for adjusting the contributions among FCMs – capital, risk of open positions and risk ranking.

In the first method, an FCM's contribution would be based on the ratio between capital and segregation requirements. As the percentage of capital to segregation requirements increased, the assessment would decrease proportionately. Or, it could be devised to be calculated on absolute values rather than percentages.

The second method, based on risk of open positions, reflected the idea that those firms that carry more risk should also do more to support a compensation fund. The definition of "risk" could be underlying market value, margin requirements or volatility. Also, would the defiition be based on gross or net positions? Would it be treated differently for spread, hedge or omnibus accounts? Would it be reduced by excess margin in a customer's account?

The third method, which would base contributions on a risk ranking, could take into consideration a combination of compliance history, management expertise, internal control, capital ratios and creditworthiness of the largest customers. However, the design and administration of such a scheme could be substantial. One solution would be to entrust ranking power to the designated self-regulatory organizations (DSROs).

Alternative Administrative Structure

The NFA Study outlined the pros and cons of two types of structures that could administer an insurance-type recovery program. The first would be a governmental/quasi-governmental organization such as SIPC, a federally mandated, non-profit, member-funded corporation regulated by the SEC or FDIC, which is a U.S. government-owned corporation.

The SIPC model would be inappropriate for the futures industry, according to the NFA Study. First, it was designed to bolster public confidence in markets in which many members of the

public are direct participants. Second, it was designed to serve an industry that is more prone to insolvency losses than is the futures industry. In addition, SIPC management "strongly opposed" adding futures accounts to its scope during a Commission hearing on the matter in July 1976.

Three organizations existed in 1986 (at the time of the NFA Study) that were seen as candidates to administer a customer account protection fund: the exchanges and their clearing organizations individually, the Futures Industry Association (FIA), and the NFA. In addition, the Study suggested that a new account protection agency could be created.

Individual mechanisms across several exchanges and clearing organizations were seen as unwieldy presuming that accounts may have positions on multiple exchanges. In addition, the NFA Study noted that the exchanges already have guaranty funds in place that can be dispensed in emergency at the behest of its leadership boards.

Because the FIA is not a mandatory membership organization and insurance is not consistent with its trade association role, it was deemed unsuitable. In NFA's favor, it already was a mandatory membership organization and had administrative functions and organization in place. However, adding insurance to its efforts would likely subject it to multiple and complicated state insurance regulations.

Analysis of Account Protection Mechanisms on Decision Making by Management of FCMs, SROs and by Customers

One of the directives the CFTC posed to the NFA in conducting this Study was whether an account protection program might subsidize bad management or result in reduced oversight by self-regulatory organizations (SROs). The short answer is, "No."

Indeed, FCMs surveyed by the NFA said internal controls for securities and futures were about the same already. Exchanges already employ risk-management techniques to preserve the financial integrity of the market and have been self-regulating since the mid-1800s. Similarly, the industry supports self-regulation via NFA to ensure professionalism and technical competence.

In the securities world, the head of SIPC told NFA that the fund likely has made the self-regulators stronger rather than weaker because it can help identify potential problems earlier. In banking, however, the opinion existed that FDIC had encouraged bank management to take greater risks because customers had a safety net.

Summary

The 1986 NFA Study concluded that "substantial and wide ranging customer account protections" already were in place in the futures industry and had resulted in a "historically low incidence of loss in the futures industry." It also noted the differences among banking, securities and futures:

> The large public commitment to insurance programs in the banking and securities industries were born out of the importance of the retail customer in those sectors. Aside from any considerations of the "justice" of compensation for insolvency loss, the need for retail investor confidence in those capital formation industries mandated huge investment in, and government backing of, public well-advertised compensation structures when that confidence was threatened by widespread failures. That need for confidence is underscored by the apparent willingness to ignore even the advertised limits on compensation when a large uncompensated loss would otherwise come to public attention.
>
> The needs of the futures industry and the expectations of most of its customers are different…because the customers of these risk shifting markets derive their confidence not from a bailout scheme but instead from an understanding, whether specific or general, of the protections afforded by the industry as a whole and the firm with whom they choose to deal. They are also different because the retail customer, although important to the futures industry, is not its lifeblood.

V. CCC Proposal

The Commodity Customer Coalition (CCC) recognizes the substantial safeguards already in place in the futures industry as it concerns protecting market integrity and customer accounts. However, it also recognizes how the MF Global bankruptcy has revealed flaws in the system that could be improved with relatively little time or expense.

PFGBEST commissioned industry veteran Susan Abbott Gidel[5] to research customer fund protections and prepare this report. Based on these findings, PFGBEST recommends that CCC pursue the following changes and regulations, all of which are both sensible and executable.

1. Correct tiered approach to regulating FCM categories.

The regulatory distinction between non-clearing FCMs and all other types of FCMs has its roots deep within the evolution of the futures industry. However, it now is apparent that this distinction has created an unintended consequence of creating tiers of oversight as well as opened loopholes for how customer segregated funds can be employed by different categories of FCMs. Thus, CCC advocates for all FCM categories – non-clearing, clearing, broker/dealer and bank –to have equal treatment, particularly as it concerns the use of capital.

2. Bring financial oversight for all U.S. regulated brokers under the purview of CME Group.

As an exchange that has monitored the financial status of clearing member firms and monitored real-time risk for decades, the CME Group is eminently qualified to perform those duties for all types of FCMs, including the non-clearing FCMs that currently are monitored by the NFA. To bring non-clearing FCMs under CME's purview would not only bring consistency to the financial reporting status for all brokers, but also free up NFA resources to focus on its area of expertise, i.e., governing sales practices and supervision of FCMs.

---

[5] Susan Abbott Gidel, owner of Susan Gidel Consulting in Chicago, has witnessed the evolution of the futures industry from a variety of angles. Starting as an editor at Futures Magazine in the late 1970s, she spent the past 11 years in charge of retail marketing at Lind-Waldock and MF Global.

3. Require daily customer fund segregation reports for all FCMs.

Currently, only non-clearing FCMs are required to submit daily segregation reports. All other types of FCMs (clearing, broker/dealer and bank) are required to submit this data only monthly. The size or type of FCM should not be the qualifier on maintaining an eye on the safety of customer segregated funds.

4. Establish that commodity customers as the first recipient of recovered segregated funds in a bankrupt FCM's estate.

Bankruptcy law does not recognize owners of segregated funds to be the first recipients of those funds when they are recovered from a bankrupt broker's estate. As with the protections available in banking and securities, the customer in futures should be protected to the utmost and be first in line to be made whole.

5. Encourage CME Group to double and broaden its Protection Fund, with industry support. Encourage other exchanges to make similar efforts.

The CME Group has made substantial headway in customer protection by establishing the $100 million Family Farmer and Rancher Protection Fund. However, based on the Estimated Response Mechanism formula devised by NFA in 1986, that Fund's calculation equals $213 million (see table on page 18 of this report). This Fund, which could then be expanded to a broader set of customers than farmers, ranchers and cooperatives, would be funded from clearing and exchange fees charged to all customers of the CME. These changes would most likely reduce the NFA fee and increase the exchange fee nominally.

Similarly, other exchanges acting as the Designated Self-Regulatory Organization (DSRO) for FCMs would establish funds that protect their customers based on the Estimated Response Mechanism. It is likely that their Estimated Response Mechanism calculation would be lower, due to a smaller group of FCMs using the other exchanges as a DSRO; however, this method allows for growth or changes in the future.

6. Research protection of other customer fund types.

It is important that the work toward protecting customers does not stop at customer segregated funds for futures and options, but also includes protections of 30.7 funds (foreign customers in futures and options) and Forex segregated funds. Protection for these types of funds should be researched as a follow-up to this analysis.

VI. Appendix

Customer Account Protection Study
By National Futures Association, Nov. 20, 1986
http://www.pfgbest.com/common/docs/NFACustomerProtectionStudy1986.pdf
Securities Investor Protection Act of 1970
www.sipc.org/pdf/SIPA.pdf
Bylaws of Securities Investor Protection Corporation
Revision #14, January 2011
http://www.sipc.org/pdf/SIPC%20BYLAWS%202011%20-%20Revision%20Fourteen.pdf
Associated tables and information from the SIPC 2010 Annual Report:

PART A: Customer Claims and Distributions Being Processed[a]

Member and Trustee By Date of Appointment	Date Registered as Broker-Dealer	Filing Date	Trustee Appointed	Customers[b] To Whom Notices and Claim Forms Were Mailed	Responses[b] Received	Customers[b] Receiving Distributions
North American Clearing Inc. Longwood, FL (Robert N. Gilbert, Esq.)	11/15/95	05/27/08	07/28/08	43,383	1,699	1,125
Great Eastern Securities, Inc. New York, NY (SIPC)	03/01/72	08/26/08	09/03/08	16,102	358	7
Lehman Brothers Inc. New York, NY (James W. Giddens, Esq.)	03/27/65	09/19/08	09/19/08	905,000	124,980	110,000
Bernard L. Madoff Investment Securities LLC New York, NY (Irving H. Picard, Esq.)	01/19/60	12/11/08	12/15/08	8,110	16,518*	2,372
TOTAL 4 MEMBERS: PART A				**972,595**	**143,555**	**113,504**

* Includes duplicate claims filed for 3,385 Active Accounts.

The increase from the prior year represents an adjustment for the customer distributions made by the court appointed receiver prior to SIPC's involvement in the proceeding.

December 31, 2010

Distribution of Assets Held by Debtor[c]			SIPC Advances				
Total	For Accounts of Customers	Administration Expenses	Total Advanced	Administration Expenses	Contractual Commitments	Securities	Cash
$ 285,007,271	$ 283,000,000#	$ 2,007,271	$ 10,285,000	$ 8,685,000			$1,600,000
			480,314	71,188		$ 409,126	
92,798,121,067	92,300,000,000	498,121,067	8,453,416			6,700,605	1,752,811
16,891,848	7,621,990	9,269,858	1,055,326,754	300,026,454		755,300,300	
$93,100,020,186	**$92,590,621,990**	**$509,398,196**	**$1,074,545,484**	**$308,782,642**		**$762,410,031**	**$3,352,811**

PART B: Customer Claims Satisfied, Litigation Matters Pending[a]

Member and Trustee By Date of Appointment	Date Registered as Broker-Dealer	Filing Date	Trustee Appointed	Customers[b] To Whom Notices and Claim Forms Were Mailed	Responses[b] Received	Customers[b] Receiving Distributions
Continental Capital Investment Services, Inc. and Continental Capital Securities, Inc. Sylvania, OH (Thomas S. Zaremba, Esq.)	10/09/59	08/25/03	09/29/03	19,636	325	81
Financial World Corporation Overland Park, KS (SIPC)	09/13/96	01/12/06	01/18/06	1,383	112	26
Hanover Investment Securities, Inc. Madisonville, LA (SIPC)	08/30/82	02/28/08	02/28/08	826	92	43
TOTAL 3 MEMBERS: PART B				**21,845**	**529**	**150**

December 31, 2010

Distribution of Assets Held by Debtor[c]			SIPC Advances				
Total	For Accounts of Customers	Administration Expenses	Total Advanced	Administration Expenses	Contractual Commitments	Securities	Cash
$2,332,898	$1,993,273	$339,625	$ 8,723,573	$6,974,568		$ 632,650	$1,116,355
			877,798	61,639		770,140	46,019
120,696	105,610	15,086	4,150,984	54,103		3,968,184	128,697
$2,453,594	**$2,098,883**	**$354,711**	**$13,752,355**	**$7,090,310**		**$5,370,974**	**$1,291,071**

PART C: Proceedings Completed in 2010

Member and Trustee By Date of Appointment	Date Registered as Broker-Dealer	Filing Date	Trustee Appointed	Customers[b] To Whom Notices and Claim Forms Were Mailed	Responses[b] Received	Customers[b] Receiving Distributions
Adler, Coleman Clearing Corp. New York, NY (Edwin B. Mishkin, Esq.)	12/27/84	02/27/95	02/27/95	102,000	19,848	59,650
Paul L. Forchheimer & Co., Inc. New York, NY (SIPC)	08/08/52	12/12/06	12/12/06	109	14	11
TOTAL 2 MEMBERS 2010				**102,109**	**19,862**	**59,661**
TOTAL 313 MEMBERS 1973–2009[d]				**2,036,334**	**426,407**	**565,467**
TOTAL 315 MEMBERS 1973–2010				**2,138,443**	**446,269**	**625,128**

December 31, 2010

Distribution of Assets Held by Debtor[c]			SIPC Advances				
Total	For Accounts of Customers	Administration Expenses	Total Advanced	Administration Expenses	Contractual Commitments	Securities	Cash
$ 933,430,275	$ 884,022,385	$ 49,407,890	$ 4,446,358			$ 2,223,179	$ 2,223,179
1,165,695	1,124,749	40,946	992,483	$ 25,000		967,483	
934,595,970	**885,147,134**	**49,448,836**	**5,438,841**	**25,000**		**3,190,662**	**2,223,179**
15,023,249,836	**14,749,278,962**	**273,970,875**	**495,301,677**	**190,262,237**	**$1,388,427**	**175,003,822**	**128,647,191**
$15,957,845,806	**$15,634,426,096**	**$323,419,711**	**$500,740,518**	**$190,287,237**	**$1,388,427**	**$178,194,484**	**$130,870,370**

PART D: Summary

	Customers[b] To Whom Notices and Claim Forms Were Mailed	Responses[b] Received	Customers[b] Receiving Distributions
Part A: 4 Members — Customer Claims andDistributions Being Processed	972,595	143,555	113,504
Part B: 3 Members — Customer Claims Satisfied, Litigation Matters Pending	21,845	529	150
Sub-Total	994,440	144,084	113,654
Part C: 315 Members — Proceedings Completed	2,138,443	446,269	625,128
Total	**3,132,883**	**590,353**	**738,782**

Notes:

(a) Based upon information available at year-end and subject to adjustments until the case is closed.

(b) SIPA requires notice to be mailed to each person who appears to have been a customer of the debtor with an open account within the past twelve months. In order to be sure that all potential claimants have been advised of the liquidation proceeding, trustees commonly mail notice and claim forms to all persons listed on the debtor's records, even if it appears that their accounts have been closed. As a result, many more claim forms are mailed than are received.
Responses Received usually exceeds Customers Receiving Distributions because responses are commonly received from customers whose accounts were previously delivered to another broker or to the customer. Responses are also received from persons who make no claim against the estate, or whose accounts net to a deficit, or who file late, incorrect, or invalid claims. The number of Customers Receiving Distributions can exceed Responses Received when the trustee transfers accounts in bulk to other brokers before claims are filed.

(c) Includes assets marshalled by Trustee after filing date and does not include payments to general creditors.

(d) Revised from previous reports to reflect subsequent recoveries, disbursements and adjustments.

December 31, 2010

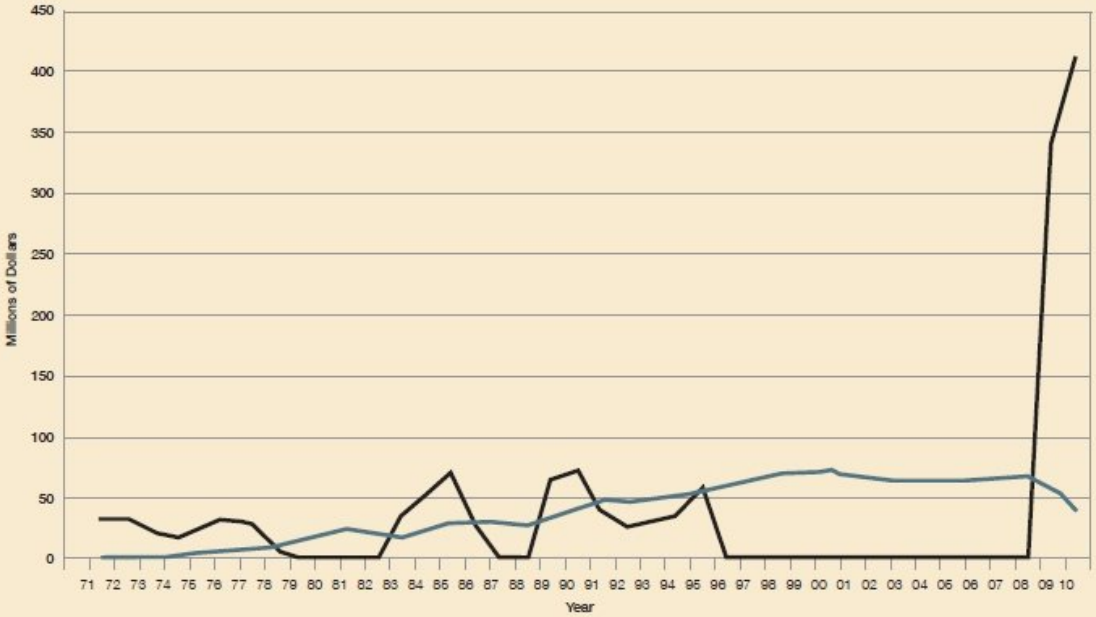
Distribution of Assets Held by Debtor[c]			SIPC Advances				
Total	For Accounts of Customers	Administration Expenses	Total Advanced	Administration Expenses	Contractual Commitments	Securities	Cash
$ 93,100,020,186	$ 92,590,621,990	$509,398,196	$1,074,545,484	$308,782,642		$762,410,031	$ 3,352,811
2,453,594	2,098,883	354,711	13,752,355	7,090,310		5,370,974	1,291,071
93,102,473,780	92,592,720,873	509,752,907	1,088,297,839	315,872,952		767,781,005	4,643,882
15,957,845,806	15,634,426,096	323,419,711	500,740,518	190,287,237	$1,388,427	178,194,484	130,870,370
$ 109,060,319,586	**$ 108,227,146,969**	**$ 833,172,618**	**$ 1,589,038,357**	**$506,160,189**	**$1,388,427**	**$945,975,489**	**$135,514,252**

TABLE 3

SIPC Revenues for the Forty Years Ended December 31, 2010

■ Member assessments and contributions: $1,492,407,646

■ Interest on U.S. Government securities: $1,572,833,970



History of Member Assessments*

1971: ½ of 1% plus an initial assessment of 1/8 of 1% of 1969 revenues ($150 minimum).

1972–1977: ½ of 1%.

January 1–June 30, 1978: ¼ of 1%.

July 1–December 31, 1978: None.

1979–1982: $25 annual assessment.

1983–March 31, 1986: ¼ of 1% effective May 1, 1983 ($25 minimum).

1986–1988: $100 annual assessment.

1989–1990: 3/16 of 1% ($150 minimum).

1991: .065% of members' net operating revenues ($150 minimum).

1992: .057% of members' net operating revenues ($150 minimum).

1993: .054% of members' net operating revenues ($150 minimum).

1994: .073% of members' net operating revenues ($150 minimum).

1995: .095% of members' net operating revenues ($150 minimum).

1996–March 31, 2009: $150 annual assessment.

April 1, 2009–December 31, 2010: .25% of members' net operating revenues.

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* Rates based on each member's gross revenues (net operating revenues for 1991–1995 and April 1, 2009 to present) from the securities business.

TABLE 4

SIPC Expenses for the Forty Years Ended December 31, 2010

- Customer protection proceedings: $2,860,038,357 (Includes net advances of $1,589,038,357 and $1,271,000,000 of estimated costs to complete proceedings.)
- Other expenses: $219,849,451

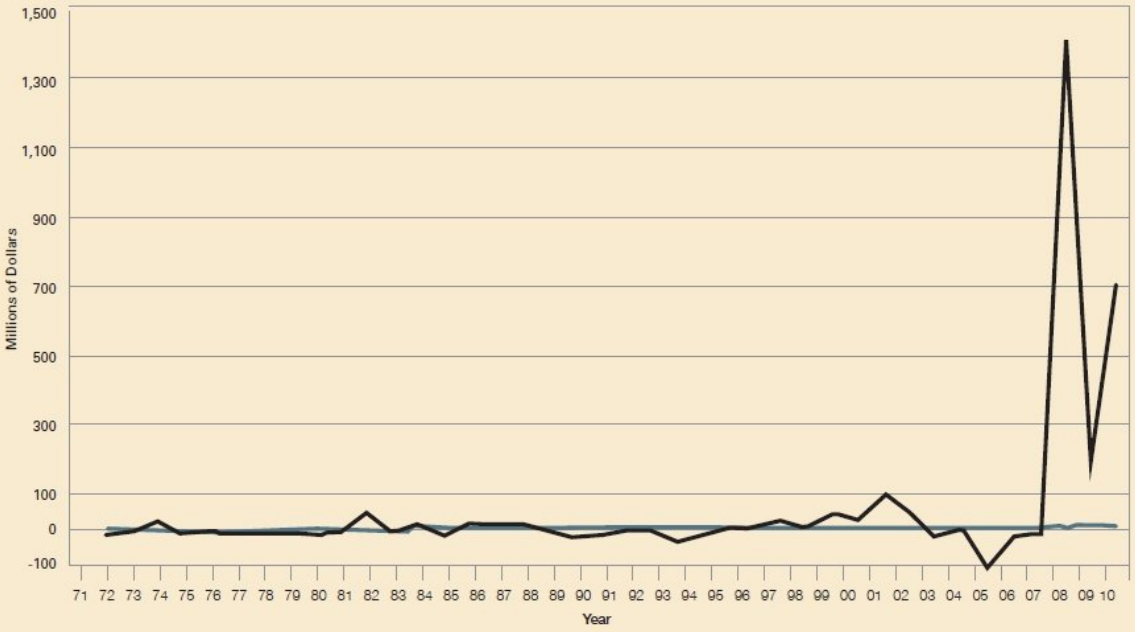
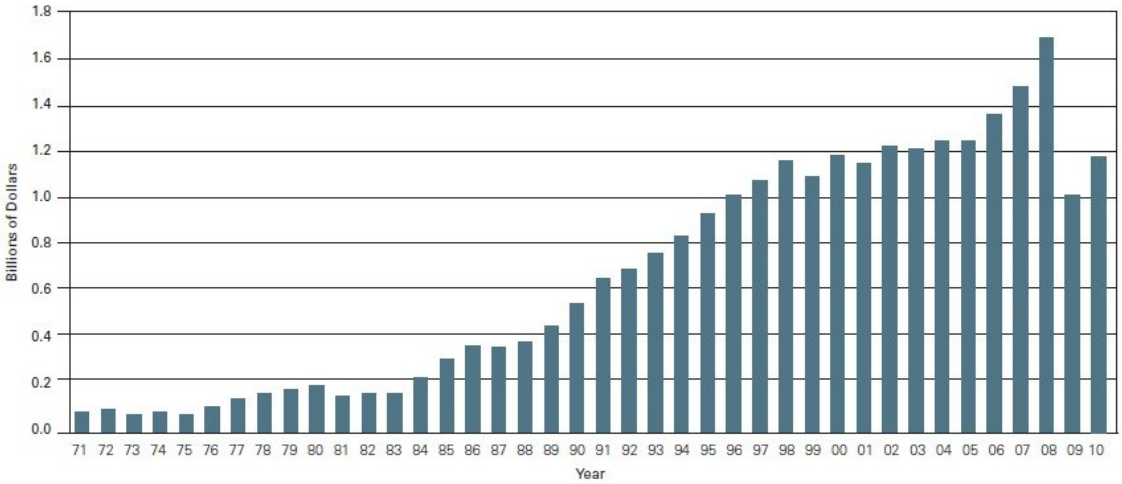


TABLE 5

SIPC Fund Comparison
Inception to December 31, 2010



APPENDIX 1 DISTRIBUTIONS FOR ACCOUNTS OF CUSTOMERS
for the Forty Years Ended December 31, 2010 (In Thousands of Dollars)

	From Debtor's Estates	From SIPC			
	As Reported by Trustees	Advances*	Recoveries*	Net	Total
1971	$ 271	$ 401		$ 401	$ 672
1972	9,300	7,347	$ (4)	7,343	16,643
1973	170,672	35,709	(4,003)	31,706	202,378
1974	21,582	4,903	(5,125)	(222)	21,360
1975	6,379	6,952	(2,206)	4,746	11,125
1976	19,901	1,292	(528)	764	20,665
1977	5,462	2,255	(2,001)	254	5,716
1978	1,242	4,200	(1,682)	2,518	3,760
1979	9,561	1,754	(6,533)	(4,779)	4,782
1980	10,163	3,846	(998)	2,848	13,011
1981	36,738	64,311	(1,073)	63,238	99,976
1982	28,442	13,807	(4,448)	9,359	37,801
1983	21,901	52,927	(15,789)	37,138	59,039
1984	184,910	11,480	(13,472)	(1,992)	182,918
1985	180,973	19,400	(11,726)	7,674	188,647
1986	28,570	14,886	(4,414)	10,472	39,042
1987	394,443	20,425	(2,597)	17,828	412,271
1988	72,052	8,707	(10,585)	(1,878)	70,174
1989	121,958	(5,481)	(10,244)	(15,725)	106,233
1990	301,237	3,960	(4,444)	(484)	300,753
1991	1,943	6,234	(2,609)	3,625	5,568
1992	34,634	7,816	(230)	7,586	42,220
1993	115,881	4,372	(9,559)	(5,187)	110,694
1994	(14,882)†	(1,283)	(3,829)	(5,112)	(19,994)
1995	585,756	17,850	(4,196)	13,654	599,410
1996	4,770	(1,491)	(10,625)	(12,116)	(7,346)
1997	314,813	22,366	(4,527)	17,839	332,652
1998	3,605	4,458	(1,571)	2,887	6,492
1999	477,635	47,360	(7,460)	39,900	517,535
2000	364,065	26,330	(3,413)	22,917	386,982
2001	10,110,355	200,967	(87,538)	113,429	10,223,784
2002	606,593	40,785	(5,812)	34,973	641,566
2003	(643,242)▲	22,729	(4,425)	18,304	(624,938)
2004	209,025	(11,662)▲	(37,700)	(49,362)	159,663
2005	(24,245)#	1,175	(4,342)	(3,167)	(27,412)
2006	1,635,006	2,653	(51,942)	(49,289)	1,585,717
2007	1,167	7,054	(6,624)	430	1,597
2008	144,265,058	1,982	(709)	1,273	144,266,331
2009	(52,025,582)●	543,280	(213)	543,067	(51,482,515)
2010	579,035	217,842	(1,824)	216,018	795,053
	$ 108,227,147	$1,433,898	($351,020)	$1,082,878	$ 109,310,025

* Advances and recoveries not limited to cases initiated this year.

† Reflects adjustments to customer distributions in the John Muir & Co. customer protection proceeding based upon Trustee's final report.

▲ Reflects adjustments to customer distributions in the MJK Clearing, Inc. customer protection proceeding based upon Trustee's revised allocation.

\# Reflects adjustment to distribution of customers assets subsequently determined not held by Donahue Securities, Inc.

● Reflects adjustment to customer distributions in the Lehman Brothers Inc. customer protection proceeding based upon Trustee's revised allocation.

APPENDIX 2 ANALYSIS OF SIPC REVENUES AND EXPENSES
for the Five Years Ended December 31, 2010

	2010	2009	2008	2007	2006
Revenues:					
Member assessments and contributions	$ 409,200,016	$346,299,978	$ 816,322	$ 852,025	$ 894,941
Interest on U.S. Government securities	38,160,886	56,636,031	67,597,794	67,670,369	65,487,278
Interest on assessments	170,336	304,378	3,337	3,531	2,929
	447,531,238	403,240,387	68,417,453	68,525,925	66,385,148
Expenses:					
Salaries and employee benefits	8,254,272	8,259,757	6,461,396	5,818,841	5,439,474
Legal fees	346,375	56,255	88,987	51,033	257,329
Accounting fees	331,901	521,581	84,817	75,962	72,277
Credit agreement commitment fee	83,330	907,501	1,686,889	1,698,657	2,164,497
Professional fees—other	309,931	212,141	179,957	342,549	179,575
Other:					
Assessment collection cost	29,679	20,848	9,127	15,416	9,492
Depreciation and amortization	273,758	112,345	148,640	160,201	160,453
Directors' fees and expenses	42,470	70,379	101,207	71,107	67,492
Insurance	35,529	31,245	32,544	32,184	30,970
Investor education	342,766	247,317	1,907,599	369,927	324,029
Imaging expenses	771,556	348,856	104,760	115,200	57,440
Office supplies and expense	164,894	91,027	143,778	70,629	85,457
EDP and internet expenses	743,819	274,081	366,148	435,441	352,902
Postage	13,164	12,557	16,814	9,619	11,165
Printing & mailing annual report	38,443	39,625	31,493	30,965	32,793
Publications and reference services	156,760	175,277	160,067	173,713	155,887
Rent—office space	747,231	720,442	707,604	663,850	678,667
Telephone	104,201	71,229	73,258	66,890	70,127
Travel and subsistence	223,391	271,242	283,452	92,668	122,258
Personnel recruitment	46,000	10,000	10,625		
Miscellaneous	74,236	23,924	72,819	21,111	16,813
	3,807,897	2,520,394	4,169,935	2,328,921	2,175,945
	13,133,706	12,477,629	12,671,981	10,315,963	10,289,097
Customer protection proceedings:					
Net advances to (recoveries from):					
Trustees other than SIPC:					
Securities	212,738,676	547,280,342	296,456	(2,435,817)	(48,468,436)
Cash	213,380	(5,100,190)	(2,610,108)	(816,131)	(2,452,686)
	212,952,056	542,180,152	(2,313,652)	(3,251,948)	(50,921,122)
Administration expenses	177,227,833	135,564,649	9,884,474	2,098,243	(31,319,949)
	390,179,889	677,744,801	7,570,822	(1,153,705)	(82,241,071)
Net change in estimated future recoveries	1,900,000	(100,000)	(1,400,000)	6,000,000	85,300,000
	392,079,889	677,644,801	6,170,822	4,846,295	3,058,929
SIPC as Trustee:					
Securities	(1,689)	1,468,579	3,862,296	2,237,551	1,382,472
Cash	(24,211)	(580,770)	(276,003)	1,391,181	249,601
	(25,900)	887,809	3,586,293	3,628,732	1,632,073
Administration expenses	(8,586)	172,689	1,194,506	(97,104)	454,596
	(34,486)	1,060,498	4,780,799	3,531,628	2,086,669
Direct payments:					
Securities				52,561	
Cash					
				52,561	
Administration expenses			639	4,828	188,282
			639	57,389	188,282
Net change in estimated cost to complete proceedings	314,100,000	(468,700,000)	1,413,000,000	(8,700,000)	(11,000,000)
	706,145,403	210,005,299	1,423,952,260	(264,688)	(5,666,120)
	719,279,109	222,482,928	1,436,624,241	10,051,275	4,622,977
Total net (expenses) revenues	(271,747,871)	180,757,459	(1,368,206,788)	58,474,650	61,762,171
Realized and unrealized gain (loss) on U.S. Government securities	32,321,095	(102,463,159)	132,368,130	63,088,803	(18,597,798)
Effect of adoption of recognition provisions of FASB Guidance					(3,861,167)
Pension and postretirement benefit changes other than net periodic benefit costs	(280,274)	2,538,599	(5,752,428)	(1,007,696)	
(Decrease) increase in net assets	$(239,707,050)	$ 80,832,899	$(1,241,591,086)	$120,555,757	$39,303,206

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