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We will begin momentarily.

Katten

The FIA Exam Process

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Agenda

- Statutory & Regulatory Sources of FRS Jurisdiction
- Overview of FRS & Its Examination Function
- History of FRS Examination Practice
- Exam Scope & Priorities
- Exam Timeline
- Exam Preparation
- Recent Disciplinary Matters

Statutory & Regulatory Sources of FRS Jurisdiction

Statutory and Regulatory Basis of Self-Regulation

> The CFTC's "oversight structure provides that SROs are the frontline regulators of FCMs, introducing brokers, commodity pool operators, and commodity trading advisors. In 2000, Congress affirmed the [CFTC's] reliance on SROs by amending [the CEA] to state: ''It is the purpose of this Act to serve the public interests through a system of effective self-regulation of trading facilities, clearing systems, market participants and market professionals under the oversight of the [CFTC]."

CEA Section 5(d)(11) (DCM Core Principle 11)
A board of trade (DCM) shall establish and enforce (A) rules and procedures for ensuring the financial integrity of transactions entered into on or through the facilities of the contract market (including the clearance and settlement of the transactions with a derivatives clearing organization); and (B)rules to ensure (i) the financial integrity of any (I) FCM; (II) IB; and (III) the protection of customer funds.

CEA Section 17(p)
Requires the NFA (as the industry's single "registered futures association") to establish minimum capital, segregation, and financial requirements for member FCMs and to audit and enforce compliance with those requirements.

CFTC Regulation 1.3 The term ''self-regulatory organization'' means a contract market, a swap execution facility, or a registered futures Association (i.e., NFA).

CFTC Regulation 1.52
Defines the concept of a "designated" SRO (the "DSRO," i.e., an SRO that is designated as primarily responsible for conducting ongoing financial surveillance of an FCM that is a member of two or more SROs under a joint audit agreement submitted to and approved by the CFTC) and establishes minimum elements that a DSRO's and each SRO's financial surveillance program must include.

Sources: CFTC, Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations, 78 FR 68506, 68509 (Nov. 14, 2013) (Enhancing Customer Protections Adopting Release).

The DSRO Mechanism & CFTC 1.52

DSRO Delegation: Because FCMs are often members of more than one SRO, CFTC 1.52(d) permits two or more SROs to file a joint audit plan with the Commission, delegating to one SRO (the DSRO) the function of examining a shared member FCM. The current joint audit plan was approved on March 18, 2009. CME (through FRS) serves as DSRO for its clearing-member FCMs.

Rule 1.52 DSRO Requirements

- Adequate levels and independence of examination staff
- Ongoing surveillance (review/analysis of financial reports and regulatory notices)
- Procedures for identifying high-risk firms
- Routine periodic on-site exams no less frequently than once every 18 months
- Risk-based method for setting exam scope; adequate documentation
- Controls testing and substantive testing addressing all areas of risk to which the FCM can reasonably be foreseen to be subject

Source: CFTC Rule 1.52

2013 Revisions to Rule 1.52

2013 Enhanced Customer Protection Rulemaking (Post-MF Global / Peregrine)

- Required each SRO to establish a supervisory program covering minimum capital, segregation, risk management, financial reporting, recordkeeping, and sales-practice compliance
- Required risk-based examinations (controls testing + substantive testing)
- Added “examinations expert” requirement — nationally recognized accounting/auditing firm to evaluate the supervisory program at least every three years
- Formalized JAC / Joint Audit Program structure; examination-staff independence and ethics-training requirements
- Enhanced monitoring for high-risk firms, including daily review of net capital/segregation
- Required reporting to SRO’s risk/audit committee; documentation requirements

Source: Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations, 78 FR 68506, 68559 -62 (Nov. 14, 2013).

Recently Proposed Revisions to Rule 1.52

Context: Growing number of "affiliated" market structures where a DCM shares common ownership with an affiliate FCM, raising conflict-of-interest concerns about impartial supervision and examination-staff reporting lines.

Key Proposed Amendments

- Examination staff of an SRO with an affiliate FCM must report directly to the board (or compliance committee), not commercial management
- SRO with an affiliate FCM must designate an independent third-party SRO for surveillance; prohibited from acting as DSRO for its own affiliate FCM
- Restrictions on access to affiliate FCM's non-public information; prohibitions on sharing non-affiliate members' non-public information
- New process allowing an FCM to elect NFA as its DSRO (six-month notice; three-exam-cycle retention requirement)

Source: CFTC, Conflicts and Affiliations, 91 Fed. Reg. 50926 (Aug. 6, 2026) (Conflicts Proposing Release).

Overview of FRS &
Its Examination Function

What Is FRS?

The Financial and Regulatory Surveillance Department (FRS) of CME Group is responsible for monitoring the financial condition and regulatory compliance of clearing member firms. FRS's mandate includes monitoring capital requirements, reviewing daily segregation and secured-amount computations, and assessing the adequacy of each firm's internal controls.

FRS's mandate flows from DCM Core Principle 11 and CFTC 1.52: protect customer funds, ensure the financial integrity of member FCMs, and provide early warning of financial or operational deterioration.

Important Distinction

FRS conducts compliance reviews — not financial-statement audits. FRS examinations assess whether an FCM is meeting its regulatory obligations (capital, segregation, recordkeeping, internal controls) rather than opining on the fairness of the firm's financial statements.

JAC Role: The Joint Audit Committee (JAC) coordinates financial surveillance among DSROs and NFA under the Joint Audit Program, allocating DSRO responsibility and harmonizing examination standards to avoid duplicative oversight of member FCMs.

Source: Section 5(d)(11) of the CEA; CME Group, Financial and Regulatory Surveillance (https://www.cmegroup.com/solutions/clearing/financial-and-regulatory-surveillance.html).

FRS: The Three-Pronged Approach

FRS employs a three-pronged approach to fulfilling its financial surveillance mandate:

1

REPORTING

Review and analysis of financial reports filed by member FCMs, including Form 1-FR-FCM (or FOCUS) monthly and certified annual filings, daily segregation and secured-amount computations, and regulatory notices (CFTC 1.12 early-warning, margin calls, etc.).

2

NOTIFICATION

A system of alerts, early-warning triggers, and exception-based monitoring that flags potential financial or operational deterioration at member firms for immediate follow-up.

3

INSPECTION

Risk-based on-site examinations — conducted no less frequently than every 18 months — that include controls testing and substantive testing of the firm's books, records, and internal-control environment.

Source: CME Group, Financial and Regulatory Surveillance (https://www.cmegroup.com/solutions/clearing/financial-and-regulatory-surveillance.html).

History of FRS
Examination Practice

Evolution of FRS Examination Practice

2000	Congress amended CEA Section 3, reaffirming SROs as frontline regulators of the self-regulatory framework: "It is the purpose of [the CEA] to serve the public interests [in providing a means for managing and assuming price risks, discovering prices, or disseminating pricing information through trading in liquid, fair and financially secure trading facilities] through a system of ***effective self-regulation*** of trading facilities, clearing systems, market participants and market professionals under the oversight of the Commission."
2009	CFTC approved the current joint audit plan under the JAC/Joint Audit Program, solidifying DSRO delegation to avoid duplicative exams.
2012	CFTC amends CFTC 1.52 to include guidance set forth in CFTC staff Financial and Segregation Interpretations 4–1 and 4–2 (which remains effective).
2011–2013	MF Global and Peregrine failures drive the Enhancing Customer Protections rulemaking, transforming exam practice toward risk-based examinations, controls and substantive testing, examinations-expert review, and enhanced high-risk-firm monitoring.
Ongoing	Evolution from primarily verifying capital/segregation computations toward broader risk-based assessment of internal controls, risk management (CFTC 1.11), technology/operational risk, and firm-specific risk profiles.
2026	CFTC's Conflicts and Affiliations proposal would further reshape DSRO structure for affiliated groups.

Sources: CEA § 3; Enhancing Customer Protections Adopting Release; Conflicts Proposing Release; Amended Joint Audit Plan (2008) (available here); Core Principles and Other Requirements for Designated Contract Markets, 77 Fed. Reg. 36612 (June 19, 2012); CFTC Staff Advisories 4-1 and 4-2 (available here).

Exam Scope & Priorities

Risk-Based Exam Scope

Scope is RISK-BASED: FRS develops a risk profile for each FCM and sets the nature, timing, and extent of controls testing and substantive testing based on an understanding of the firm's internal control environment. The exam must address all areas of risk to which the FCM can reasonably be foreseen to be subject.

Every On-Site Exam Assesses:

- Minimum net capital (CFTC 1.17)
- Customer-fund protection / segregation and secured amounts (CFTC 1.20–1.30, 30.7)
- Cleared-swaps customer collateral
- Recordkeeping and financial reporting requirements

Additional Focus Areas:

- Risk management program adequacy (CFTC 1.11)
- Controls over customer funds and investment of customer funds (CFTC 1.25)
- Residual interest
- Technology / operational / cybersecurity risk
- Areas highlighted by FRS advisories

Source: CFTC Reg. 1.52; CME Group Audit Advisories (available here)

High-Risk Indicators & FRS Advisories

Priority / High-Risk Indicators

Financial Difficulty	Firms experiencing financial or operational difficulties
Segregation / Capital	Failing to meet segregation or net-capital requirements
Books & Records	Failing to maintain current books and records
Internal Controls	Material inadequacies in internal controls

FRS Advisories

FRS Audit Advisories issued since 2020 signal current focus areas and supervisory expectations. Members should actively track and review these advisories to align internal controls with FRS priorities.

High-risk firms receive enhanced monitoring, including daily review of net capital, segregation, and secured calculations.

Review current advisories at:
cmegroup.com/notices.html

Source: CME Group Audit Advisories (available here)

Audit Advisory Focus Areas (2020–Present)

Thematic areas drawn from CME Group and JAC Audit Advisories issued since 2020:

1 Customer Fund Protection

Proper computation and daily reporting of segregated, secured (30.7), and cleared-swaps customer amounts; adequate controls over deposits, withdrawals, and disbursements.

2 Investment of Customer Funds (Reg. 1.25)

Compliance with permitted-investment restrictions; concentration limits; valuation and liquidity of instruments held for customer accounts.

3 Net Capital Adequacy

Accurate computation of adjusted net capital; proper haircuts and charges; timely filing of §1.12 early-warning notices when capital approaches minimum thresholds.

4 Recordkeeping

Maintenance of current, accurate, and complete books and records as required by CFTC Regs. 1.18, 1.35, and related provisions; reconciliation of customer and proprietary accounts.

Source: CME Group & JAC Audit Advisories (2020–present) (available here)

Audit Advisory Focus Areas (cont.)

5 Regulatory Reporting / CGM

Accuracy and timeliness of regulatory filings (Form 1-FR-FCM / FOCUS); Customer Gross Margin (CGM) reporting obligations and common computation errors.

6 Performance Bond / Margin

Adequacy of margin collection and monitoring processes; proper application of performance-bond requirements to customer and proprietary positions.

7 Supervision & Internal Controls

Adequacy of supervisory systems, written policies and procedures, risk-management frameworks (§1.11), and evidence of management oversight and testing of controls.

8 Risk-Based Scope

FRS tailors the depth and breadth of each exam to the firm's specific risk profile. Firms with higher complexity, past findings, or risk indicators should expect more intensive scrutiny in the above areas.

Key Takeaway: These eight thematic areas represent the current supervisory priorities. Firms should use them as a self-assessment checklist when preparing for FRS examinations.

Exam Timeline

Typical Exam Timeline

Frequency: Routine periodic on-site exams no less frequently than once every 18 months (per CFTC 1.52); many FCMs are examined on an approximately annual cycle.

1	**Notification**	Engagement letter and initial document/data request	4	**Findings**	Requests for information and firm responses
2	**Planning**	Pre-exam planning and risk assessment; FRS updates firm's risk profile	5	**Exit/Closing**	Issuance of exam results
3	**Fieldwork**	On-site and/or remote controls and substantive testing, interviews, walkthroughs	6	**Remediation**	Follow-up on deficiencies

Factors Affecting Timeline

Size, complexity, and business mix of the FCM | Quality and timeliness of document production | Number and severity of findings | Adequacy of internal controls | Open regulatory notices or early-warning events | Coordination with other regulators (CFTC, NFA, SEC) | Firm responsiveness during the exam

Exam Preparation

Exam Preparation: Books, Records & Filings

Maintain Continuous Readiness

- Keep books and records current, reconciled, and readily producible; ensure daily segregation/secured/cleared-swaps computations are accurate and well documented.

Know Your Regulatory Filings

- Timely, accurate Form 1-FR-FCM (or FOCUS) monthly filings and certified annual reports; promptly file CFTC 1.12 early-warning and other required notices.

Risk Management Program (CFTC 1.11)

- Maintain a robust, documented risk management program with a separated risk management unit, board-approved policies and procedures, and evidence of the required annual review.

Document Internal Controls

- Be able to demonstrate controls over customer funds, investment of customer funds (CFTC 1.25), and residual-interest targets.

Exam Preparation: Practical Guidance

Prepare the Team

- Designate exam coordinators
- Assemble a document/data room in advance
- Ensure availability of key personnel (finance, treasury, compliance, operations, IT)
- Respond promptly and completely to all information requests
- Track and remediate prior-exam findings

Stay Current

- Track FRS advisories and CFTC/NFA guidance to align controls with current supervisory expectations
- Self-identify and self-report issues where appropriate
- Maintain awareness of enforcement trends from recent CHRC actions
- Review evolving regulatory expectations (e.g., Conflicts and Affiliations proposal)

Recent Disciplinary Matters

Disciplinary Actions from FRS Examinations

Disciplinary actions stemming from FRS exams are brought before the CME Business Conduct Committee (and prior to 2024, before the Clearing House Risk Committee) and are published as CME notices.

Common Categories of Findings and Charges

Net Capital	Deficiencies or miscalculations
Segregation / Secured	Shortfalls or computation errors
Books & Records	Failure to maintain current/accurate books and records
Regulatory Filings	Late or inaccurate filings and notices
Risk Management	Inadequate risk management or internal controls
Supervision	Failure to supervise

Source: CME Group Notices — Business Conduct Committee and Clearing House Risk Committee

Monitoring Enforcement Trends

Members should review recent Business Conduct Committee and (prior to 2024) Clearing House Risk Committee actions to understand enforcement trends and calibrate their compliance programs accordingly.

Best Practices

- Regularly review published BCC actions for patterns in charged conduct and sanctions imposed
- Use enforcement outcomes to benchmark and test internal controls and compliance procedures
- Brief relevant business-line and operations personnel on common deficiency categories
- Integrate lessons from disciplinary matters into firm training programs
- Proactively address issues identified in FRS advisories before they become examination findings

Note: *Specific recent BCC actions should be reviewed on the CME Group notices page. Details of individual matters, including respondent names and fine amounts, are available there.*

Source: CME Group Notices

CHRC Case Studies (2020–2023)

Anonymized illustrative cases drawn from published CHRC disciplinary actions:

Case 1 **Capital & Reporting Deficiencies**

Violation: FCM failed to maintain minimum adjusted net capital on multiple occasions and filed inaccurate monthly financial reports (Form 1-FR-FCM) that overstated its net capital.
Rules: CFTC Reg. 1.17 (net capital); CFTC Reg. 1.10 (financial reporting); CME Rules 971, 972.
Sanction: $150,000 fine.
Takeaway: Accurate capital computation and truthful regulatory filings are foundational — errors compound and trigger enhanced scrutiny.

Case 2 **Customer Fund Statement Errors**

Violation: FCM filed daily statements of segregation and secured amounts that contained material errors, resulting in understatement of obligations to customers.
Rules: CFTC Regs. 1.32 (segregated-amount computation), 30.7 (secured amounts); CME Rules 971, 972.
Sanction: $50,000 fine.
Takeaway: Daily seg/secured computations require robust controls and independent review — errors can mask customer-fund shortfalls.

Source: Published CME CHRC disciplinary actions (2020–2023). Firm names anonymized.

CHRC Case Studies (cont.)

Case 3 **CGM Reporting Deficiencies**

Violation: FCM failed to accurately compute and report Customer Gross Margin (CGM) amounts, resulting in understatement of customer-margin obligations over a multi-month period.
Rules: CFTC Regs. 1.58, 1.32; CME Rules 971, 972, 980.
Sanction: $25,000–$50,000 fine (range reflects multiple related matters).
Takeaway: CGM reporting is an area of heightened focus; firms should verify computation methodologies against current advisory guidance.

Case 4 **Books-and-Records Violations**

Violation: FCM failed to maintain current and accurate books and records, including incomplete account documentation and unreconciled ledger balances.
Rules: CFTC Regs. 1.18, 1.35 (books and records); CME Rules 971, 972.
Sanction: $50,000 fine for each of two separate enforcement actions.
Takeaway: Books-and-records violations are frequently charged alongside other deficiencies — maintaining current records is table stakes.

Source: Published CME CHRC disciplinary actions (2020–2023). Firm names anonymized.

CHRC Case Studies (cont.) & Cross-Cutting Takeaways

Case 5 **Omnibus Margining & Customer Funds**

Violation: FCM failed to properly margin omnibus accounts and to maintain adequate residual interest in customer-segregated accounts, resulting in temporary under-segregation.
Rules: CFTC Regs. 1.22 (residual interest), 1.32 (segregation computation), 39.13 (risk management for DCOs); CME Rules 930, 971, 972.
Sanction: $100,000 fine.
Takeaway: Omnibus-account margining and residual-interest compliance require dedicated controls — FCMs carrying omnibus accounts face heightened exposure.

Cross-Cutting Takeaways from CHRC Actions

- Capital, segregation, and reporting deficiencies remain the most frequently charged violations; accuracy is non-negotiable.
- Books-and-records charges frequently accompany substantive violations — recordkeeping failures amplify risk.
- Fine amounts range from $25,000 to $150,000, with amounts calibrated to severity, duration, and recurrence.
- Self-identification and prompt remediation can be mitigating factors; delayed disclosure tends to increase sanctions.
- Firms should use published CHRC actions as a diagnostic tool: map each case to their own controls and ask, “Could this happen here?”

Source: Published CME CHRC disciplinary actions (2020–2023). Firm names anonymized.

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Questions?

