()nPoint

October 2013

A Legal Update from Dechert's Global Commodities and Derivatives Group*

CFTC Adopts New CPO Rules for Registered Investment Companies and Others

Introduction

The U.S. Commodity Futures Trading Commission ("CFTC") recently released its long-awaited "Final Rule" to harmonize CFTC disclosure, reporting, and recordkeeping requirements with parallel U.S. Securities and Exchange Commission ("SEC") requirements for registered investment advisers ("RIAs") also required to register as commodity pool operators ("CPOs")² with respect to their operation of certain investment companies ("registered funds") registered under the U.S. Investment Company Act of 1940 as amended ("1940 Act").³ In the Final Rule, the CFTC substantially changed course from the Proposed Rule. In summary, the Final Rule is "grounded in the concept of substituted compliance" but is not without some additional operational obligations, and it does not address all issues related to this new "harmonized" regime.

The Final Rule's simplified approach to CFTC disclosure, reporting, and recordkeeping obligations for registered fund CPOs is in stark contrast to the Proposed Rule, which had instead focused on removing existing barriers to duplicative disclosure and otherwise would have largely subjected registered fund CPOs to all of the same ongoing CFTC Part 4 CPO regulations as are applicable to CPOs of public commodity pools in addition to parallel obligations under the existing SEC regime. The Proposed Rule drew a broad spectrum of industry comments that were generally concerned that such a non-synchronized approach would result in increased costs that would ultimately be borne by registered fund investors and cause

The CFTC released its proposed harmonization rule in February 2012. Harmonization of Compliance Obligations for Registered Investment Companies Required to Register as Commodity Pool Operators, 77 Fed. Reg. 11345 (Feb. 24, 2012) ("Proposed Rule").

Section 1a(11) of the CEA (as defined below) and CFTC Regulation 1.3(cc).

Harmonization of Compliance Obligations for Registered Investment Companies Required to Register as Commodity Pool Operators, 78 Fed. Reg. 52308 (Aug. 22, 2013) ("Adopting Release"). The Final Rule was first publically announced by the CFTC on August 13, 2013.

For ease of reference, this OnPoint uses the term "registered fund" generally to refer to open-end management investment companies registered under the 1940 Act, as well as to registered closed-end investment companies and exchange-traded funds ("<u>ETFs</u>") that have registered as unit investment trusts under the 1940 Act.

⁴ Adopting Release at 52309.

⁵ See Proposed Rule at 11345-48.

investor confusion, without substantively improving upon the SEC's existing disclosure, reporting, and recordkeeping regime for registered funds.⁶

In particular, commenters expressed concern that:

- 1. CFTC regulations generally require a CPO to correct material misstatements in a "commodity pool's" disclosure document within 21 days of becoming aware of such misstatements" -- however SEC rules prohibit a registered fund from offering its shares pursuant to a prospectus that contains any materially misleading statements, effectively requiring any material inaccuracies to be updated immediately upon discovery;8
- 2. in connection with sales of commodity pool interests, CFTC regulations generally require a CPO to deliver the full disclosure document to a prospective investor and obtain an individually signed acknowledgment of receipt of the document prior to accepting funds from the investor -- whereas SEC rules allow for the delivery of a "summary" prospectus provided the longer "statutory" prospectus is made available to shareholders via a website, and also do not require a signed acknowledgment of receipt;⁹
- 3. CFTC regulations generally require that every pool be a discrete legal entity (rather than each a class or series) -- whereas SEC rules permit series trusts, an organizational structure that allows a registration statement for certain open-end registered funds to contain the registration statement for multiple funds; 10
- 4. CFTC regulations generally require certain boiler-plate risk disclosure, break-even calculations for a sample investor, and additional information about specific fees -- all of which registered funds, pursuant to SEC rules, are not permitted to include in their summary prospectuses and are either discouraged from using or are not required to use in their registration statements at all:¹¹
- 5. CFTC regulations generally require a CPO to maintain all books and records at the CPO's main business office and make them available for inspection by investors -- however SEC rules permit books and records to be maintained by third parties and do not generally require that they be made available to shareholders for inspection; 12
- 6. with respect to registered funds that utilize a trading subsidiary structured as a controlled foreign corporation ("<u>CFC</u>") to obtain exposure to commodity investments, strict application of current CFTC regulations would require CFCs to prepare separate disclosure documents, reports, and financial statements from the related registered fund even though the registered fund is its only shareholder -- whereas SEC rules permit the registered fund to consolidate CFC disclosure, reporting, and financial statements with those of the registered fund; ¹³ and

Brief for the Mutual Fund Directors Forum as Amicus Curiae in Support of Plaintiff's Motion for Summary Judgment, Chamber of Commerce v. CFTC, No. 1:12-cv-00612 (D.D.C May 25, 2012), available here.

CEA Section 1a(10) and CFTC Regulation 4.10(d).

⁸ Compare CFTC Regulation 4.26(d) with Sections 12(a)(2) and 17(a)(2) of the U.S. Securities Act of 1933 as amended ("Securities Act").

Compare CFTC Regulation 4.21 with Securities Act Sections (5)(b)(2) and 10(a) and Rule 493.

See Adopting Release at 52314 (discussing CFTC Regulation 4.20(a)(1) and substituted compliance in relation to registered funds organized as series entities).

¹¹ Compare CFTC Regulation 4.24 with Rule 481 under the Securities Act and SEC Form N-1A.

Compare CFTC Regulations 4.7(b)(4) and 4.23 with 1940 Act Rule 31a-3.

See Adopting Release at 52319.

7. CFTC regulations generally require a CPO to maintain a ledger containing the name, address, and capital account information for each investor -- whereas registered funds' customary use of market-standard transfer agent and omnibus account arrangements would be rendered impossible. 14

Importantly, the CFTC took into consideration the many concerns the industry had with the efficacy and efficiency of the Proposed Rule. Accordingly, the Final Rule allows registered fund CPOs to elect to comply with applicable CFTC Part 4 CPO regulations, subject to the few exceptions specified below under "Impact of Final Rule," by electing substituted compliance with existing parallel SEC rules. Substituted compliance will allow registered fund CPOs to avoid problematic discrepancies between, and duplication of, the CFTC and SEC disclosure, reporting, recordkeeping, and document delivery regimes (including those described above). Also, registered fund disclosure documents will not be subject to filing with, or review or approval by, the U.S. National Futures Association ("NFA") (although they will be subject to NFA inspection during a CPO examination).

Dechert has been extensively involved in commenting on the CFTC's Part 4 CPO amendments throughout the rulemaking process, in particular with respect to CFTC Regulation 4.5 and the harmonization of compliance obligations. ¹⁵ In our April 2012 comment letter, we advocated that the CFTC's stated objectives of (i) eliciting information to address certain sources of risk delineated in the U.S. Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd Frank Act") ¹⁶ and (ii) implementing "enhanced oversight" of the derivatives markets and registered fund commodity interest trading activities ¹⁷ would be better served by accepting the documentation that registered funds are already required to produce and deliver, and instead focusing the CFTC's resources on a collaborative effort with the SEC to determine what additional measures (if any) would actually serve investors' best interests and help them to make informed investment decisions. Now, registered fund investors will continue to benefit from plain-English disclosure in the SEC format and content that is familiar and has benefitted from extensive SEC study and implementation.

CFTC Regulation 4.23(a)(4). When the SEC adopted redemption fee rules in 2006 that related to omnibus accounts, commenters reported that hundreds of thousands of accounts could qualify as being held by financial intermediaries. Mutual Fund Redemption Fees, 71 Fed. Reg. 58257, 58264 n.62 (Oct. 3, 2006).

Over the course of this rulemaking process, Dechert submitted six comment letters to the CFTC and advised on several others, addressing various aspects of the proposals. See letter from M. Holland West, Partner, Dechert LLP, to David A. Stawick, Office of the Secretariat, CFTC (Oct. 18, 2010), available here. See letter from George J. Mazin, Partner, Dechert LLP, to David A. Stawick, Office of the Secretariat, CFTC (Apr. 12, 2011), available here. See letter from Dechert LLP and Clients, to David A. Stawick, Office of the Secretariat, CFTC (Apr. 12, 2011), available here. See letter from M. Holland West, Partner, Dechert LLP, to David A. Stawick, Office of the Secretariat, CFTC (July 26, 2011), available here. See letter from M. Holland West, Partner, Dechert LLP, to David A. Stawick, Office of the Secretariat, CFTC (Apr. 5, 2012), available here. See letter from M. Holland West, Partner, Dechert LLP, to David A. Stawick, Office of the Secretariat, CFTC (Apr. 25, 2012), available here. See also Brief for the Mutual Fund Directors Forum, supra note 5.

Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. Law 111-203, 124 Stat. 1376 (2010).

¹⁷ Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, 77 Fed. Reg. 11252, 11253 (Feb. 24, 2012) ("CFTC Regulation 4.5 Adopting Release"). The proposing release relating to these amendments stated that the CFTC was reevaluating its regulation of CPOs "in order to ensure that the [CFTC] can adequately oversee the commodities and derivatives markets and assess market risk associated with pooled investment vehicles under its jurisdiction." Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations, 76 Fed. Reg. 7976, 7977-78 (Feb. 11, 2011).

Background

Since its adoption in 1985 until 2003, CFTC Regulation 4.5 provided that a registered fund could qualify for an exclusion from the definition of a CPO (and thus be exempted from all CPO regulation under the CFTC's Part 4 CPO regulations) only if <u>both</u>: (i) any commodity interest trading above a fixed *de minimis* threshold was conducted solely for "bona fide hedging" purposes as defined by CFTC Regulation 1.3(z)(1); and (ii) the registered fund observed certain marketing restrictions. However in 2003, seeking to "modernize" Regulation 4.5 to allow registered funds greater direct access to the derivative markets and to increase commodity market liquidity, the CFTC amended Regulation 4.5 to create a broad-based CPO registration exclusion by removing both the *de minimis* trading threshold and the marketing restrictions. In 2010, in connection with passage of the Dodd-Frank Act and related expansion of the U.S. Commodity Exchange Act as amended ("CEA"), the NFA successfully petitioned the CFTC to reinstate the *de minimis* commodity interest trading thresholds and the marketing restrictions into Regulation 4.5 with respect to registered funds. The CFTC identified the RIA of a registered fund that cannot meet the new conditions in Regulation 4.5 as the appropriate entity to register and function as the CPO, not the registered fund itself nor its directors or trustees.

(i) with respect to exchange-traded commodity futures, options on futures, and commodity options and most over-the-counter swaps, forwards, options, and other derivatives ("commodity interests") used for purposes other than solely bona fide hedging purposes (as determined under CFTC Regulations 1.3(z)(1) and 151.5), either

the aggregate initial margin, collateral, and premiums (not variation or mark-to-market margin) required to establish the registered fund's commodity interest positions, determined at the time the most recent position was established, will not exceed 5% of the liquidation value (i.e., net asset value) of the registered fund's portfolio (after accounting for unrealized profits and unrealized losses on such positions and excluding the in-the-money amounts on options at the time of purchase), or

the aggregate net notional value of such commodity interest positions, determined at the time the most recent position was established, does not exceed 100% of the liquidation value of the registered fund's portfolio (after accounting for unrealized profits and unrealized losses on such positions):

<u>and</u>

(ii) the registered fund will not be, and has not been, marketing participations in the registered fund to the public as a commodity pool or otherwise as or in a vehicle for trading commodity interests. See also CEA Section 4m(3)(C) and CFTC Regulation 1.3(yy).

See CFTC Changes Rules Affecting Public and Private Funds, *Dechert OnPoint*, (March 1, 2012), available here.

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Prior to the expansion of the term "commodity interest" pursuant to the Dodd-Frank Act and the CFTC's implementing regulations, only exchange-traded futures contracts, options on futures, and commodity options were included in such term. See footnote 20 infra.

^{19 17} C.F.R. § 1.3(z)(1). Since adopting CFTC Regulation 1.3(z)(1) in 1977, the CFTC has clarified, interpreted, and reinterpreted what it means to be engaged in *bona fide* hedging. See Background on Position Limits and the Hedge Exemption, Statement of Dan M. Berkovitz, General Counsel, CFTC (Jan. 14, 2010), available here.

Now, in order to rely on the CPO registration exclusion in Regulation 4.5, a registered fund must represent that:

²¹ Because of the way CFTC Regulation 4.5(a)(i) and (b)(i) are worded, the registered fund continues to be the appropriate entity to claim the exclusion, if available. The CFTC regulates CPOs and commodity trading advisors ("<u>CTAs</u>") but not the actual commodity pools, so there is no concept of a "registered commodity pool" the way that there is a concept of a registered fund.

Impact of Final Rule

An RIA to a registered fund that is ineligible for the exclusion under CFTC Regulation 4.5 and is now dually registered as a CPO may comply with CFTC disclosure, investor reporting, and recordkeeping requirements with respect to the registered fund through substituted compliance with the existing SEC regime applicable to the registered fund, provided the CPO:

- 1. files a notice with the NFA of the CPO's intent to use the substituted compliance regime with regard to the CFTC's disclosure and reporting rules;²²
- files a notice with the NFA if the CPO uses or intends to use third-party service providers for recordkeeping purposes;²³
- 3. files with the NFA the applicable registered fund's annual report (including audited financial statements) that are prepared pursuant to SEC requirements (rather than needing to meet the CFTC annual report requirements in CFTC Regulation 4.22);
- adds specified (but very limited) CFTC-related disclosure to the front page legend of the registered fund's current prospectus;
- 5. for a registered fund with less than three years of operating history, the registered fund prospectus must include the performance of all of the CPO's other pools (*i.e.*, funds) and separately managed accounts that the CPO manages that are "substantially similar" in investment objectives, policies, and strategies to those of the offered registered fund; and 24
- to avoid preparing and providing monthly account statements to investors under CFTC Regulation 4.22, makes the registered fund's daily net asset value publicly available to investors and discloses how the information may be accessed and otherwise provides the SEC-mandated semi-annual and annual reports to investors and files them with the SEC.²⁵

In a coordination with the CFTC's release of the Final Rule, the SEC's Division of Investment Management ("IM Division") issued guidance that signaled that it supports the CFTC rulemaking and facilitated compliance with the joint SEC and CFTC requirements.²⁶ The IM Division stated that it would interpret the

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See CFTC Regulation 4.12(d)(1). The notice of the use of substituted compliance is filed through the NFA exemptions system as a CFTC Regulation 4.12(c)(3) exemption. As of October 1, 2013, the NFA system was open to receive these filings. Filing Requirements for Exemption Notices under CFTC's Recently Adopted Harmonization Rules, NFA Notice to Members I-13-28 (Sept. 30, 2013) ("NFA Notice Regarding Notice Filings"), available here.

See Letter from the Investment Company Institute ("ICI") to Gary Barnett, Director of CFTC Division of Swap Dealer and Intermediary Oversight (Aug. 28, 2013) at 5 ("ICI Harmonization Letter") (discussing informal guidance from the CFTC staff indicating that, with respect to utilizing alternate recordkeepers while complying with CFTC Regulation 4.23(c)(1)(iv)(D), open-end registered funds will also need to disclose the location of their books and records in Item 33 of SEC Form N-1A and closed-end registered funds will need to disclose the location of their books and records in Item 32 of SEC Form N-2).

See Adopting Release at 52318-19 (discussing substantially similar accounts). See also, e.g., Growth Stock Outlook Trust, Inc., SEC No-Action Letter (pub. avail. Apr. 15, 1986); Nicholas-Applegate Mutual Funds SEC No-Action Letter (pub. avail. Aug. 6, 1996); Bramwell Growth Fund SEC No-Action Letter (pub. avail. Aug. 7, 1996); Mass Mutual Institutional Funds SEC No-Action Letter (pub. avail. Sept. 28, 1995); and ITT Hartford Mutual Funds, SEC No-Action Letter (pub. avail. Feb. 7, 1997).

²⁵ SEC Form N-1A, Item 4(b)(2)(i) requires a registered fund to include a statement explaining that updated performance information is available (if applicable) and to provide a website address and/or toll-free (or collect) telephone number where the updated information may be obtained; however, the SEC does not require that access be given to daily net asset value.

Disclosure and Compliance Matters for Investment Company Registrants that Invest in Commodity Interests, SEC Division of Investment Management, Guidance Update, No. 2013-05 (Aug. 2013) ("IM Guidance"), available here.

items in the list above as being consistent with existing SEC rules and disclosure and compliance requirements and instructions.

Compliance Dates

The Final Rule does not explicitly state the date by which a currently registered CPO will be required to file the applicable notice with the NFA of its intent to satisfy its CFTC Part 4 CPO disclosure obligations via substituted compliance for a registered fund; however, informal guidance given to Dechert and the ICI by the CFTC staff indicates that registered fund CPOs will need to file the applicable notice by October 21, 2013.²⁷

The Final Rule, as applicable to registered fund CPOs, generally became effective 30 calendar days (i.e., September 23, 2013) following its publication in the U.S. Federal Register (which occurred on August 22, 2013). However, in accordance with the CFTC Regulation 4.5 Adopting Release, registered fund CPOs will have 60 calendar days from the effective date of the Final Rule (or until November 22, 2013) to comply with CFTC Part 4 CPO recordkeeping, reporting, and disclosure requirements.²⁸ Accordingly, registered fund prospectuses that are either initial registration statements or annual updates by way of post-effective amendments filed on or after (but not prior to) November 22, 2013 will need to include the modified front page legend, additional performance disclosure, and disclosure of how to obtain daily net asset value information (to the extent applicable) when the registered fund files either the initial registration statement or annual update of the registration statement. With respect to the Final Rule's requirement to file annual reports (including audited financial statements) beginning November 22, 2013, the CFTC staff has clarified that the filing of annual reports by a registered fund on SEC Form N-CSR in accordance with applicable SEC rules and filing the same annual reports with the NFA within 90 calendar days of such registered fund's fiscal year-end will satisfy CFTC Regulation 4.22. If the registered fund has a CFC, the annual report may consolidate the CFC's financial statements with those of the registered fund, but must also separately indicate in the report the holdings, gains and losses, and other financial statement amounts attributable to the CFC. To take advantage of the consolidated reporting, the CPO must file for no-action relief from the CFTC by the end of the registered fund's next fiscal year following November 22, 2013.²⁹ The no-action relief is effective upon filing so long as the request is materially complete. 30

In addition, registered fund asset reporting on CFTC Form CPO-PQR will begin 60 calendar days following effectiveness of the Final Rule (*i.e.*, November 22, 2013). The CFTC staff has informally confirmed that this effectively means that registered fund CPOs will be required to include registered fund assets on their Form

²⁷ See ICI Harmonization Letter at 3.

²⁸ ICI Harmonization Letter at 3 (discussing that registered fund CPOs must file the notice with the NFA that they intend to maintain their records with third-party service providers on or before November 22, 2013).

²⁹ CPOs seeking relief to consolidate CFC reporting in relation to <u>both</u> the registered fund's annual report <u>and</u> CFTC Form CPO-PQR must file for no-action relief from the CFTC by the earlier of the close of the registered fund's next fiscal year following November 22, 2013 or December 31, 2013. See footnotes 30 and 31 *infra*.

Request for Confirmation and No-Action Relief Regarding Application of Certain Reporting Obligations under Part 4 of the Commission's Regulations Concerning Certain Subsidiaries of Registered Investment Companies, CFTC No-Action Letter 13-51 (Sept. 5, 2013) ("Consolidation No-Action Letter").

Similarly, a registered fund's CFC will not be required to prepare and distribute a separate CFTC-compliant disclosure document, but rather its disclosure can be incorporated into the registered fund's prospectuses pursuant to the SEC rules as is the current industry practice.

CPO-PQR filing for the quarter ending December 31, 2013.³¹ Please refer to Appendix A for a summary timeline of the various compliance dates.

Substituted Compliance Not an Abdication of Jurisdiction

Registered fund CPOs should note that, while SEC rules will generally govern their ongoing reporting and disclosure obligations, registered fund CPOs are still subject to examination and/or oversight and enforcement by the CFTC and the NFA, and all commodity interest market participants are subject to the anti-fraud and anti-manipulation provisions of the CEA.³² Additionally, if a registered fund CPO fails to comply with the SEC-administered regime, the CPO will be in violation of the CFTC's Part 4 CPO regulations and subject to possible CFTC enforcement action. Of particular interest, both the Adopting Release and the IM Guidance explicitly highlight the importance of adopting robust compliance policies in relation to trading derivatives as well as routinely reevaluating derivatives-related risk disclosure in relation to the substantive concerns of both the CFTC and SEC.³³ As a best practice, registered fund CPOs should consider CFTC and NFA, as well as SEC, guidance directly applicable whenever reviewing and revising either their derivatives-related policies and procedures or derivatives-related registration statement disclosure.

What Final Rule Did Not Address

The Final Rule left unanswered some practical questions related to: permissible third-party (or alternate) recordkeepers;³⁴ whether registered fund CPOs will have any additional recordkeeping requirements pursuant to CFTC Regulation 4.23 in addition to those addressed in the Final Rule;³⁵ and what will be the process for approval and use of marketing materials by registered funds whose RIAs must dually register as CPOs.³⁶ The Adopting Release lists certain permissible third-party recordkeepers (administrators, distributors, custodians, or banks or registered broker-dealers acting in similar capacities); however, the relatively narrow list does not conform with registered fund industry practice. The CFTC staff has given informal guidance that it intends to conform CFTC Regulation 4.23 with current industry practice concerning third-party recordkeepers by expanding the permissible alternate recordkeepers to include record maintenance companies, data storage companies, and sub-advisory RIAs/CTAs.³⁷ With respect to whether

If a registered fund has a CFC, the registered fund and CFC may be consolidated as a single pool for CFTC Form CPO-PQR and NFA Form PQR reporting purposes. To take advantage of consolidated reporting, the CPO must file for no-action relief from the CFTC before December 31, 2013. Consolidation No-Action Letter at 6-7.

³² CEA Sections 4b and 4o.

³³ Compare Adopting Release at 52315-16 with IM Guidance at 2-3.

³⁴ See ICI Harmonization Letter at 6.

³⁵ Id

³⁶ See Adopting Release at 52322.

A CPO using one of the enumerated third-party recordkeepers must file a notice with the NFA at the time of CPO registration or the decision to use a third-party recordkeeper, whichever is later. The CPO must file both a CPO-level notice and a separate notice for each pool for which a third party will keep records if the third-party recordkeeper will keep both CPO and pool records. The CPO must also upload a statement from the third-party recordkeeper wherein the recordkeeper will make the acknowledgements specified in the applicable rule. All of this is accomplished through the NFA exemptions system, which is now ready to receive these notice filings. See NFA Notice Regarding Notice Filings.

registered fund CPOs are required to maintain any additional records pursuant to Regulation 4.23 beyond those required to be maintained pursuant to the Final Rule, the CFTC has informally clarified that they are not.

While the CFTC has offered clarification related to books and records, it has yet to address the open questions concerning how it will regulate applicable registered fund marketing materials. Accordingly, it remains to be seen what effect the CFTC harmonization efforts will have on registered fund advertising and sales literature. The CFTC and the NFA have rules that apply to commodity pool marketing and promotional materials used by CPOs and CTAs. The Proposed Rule did not address the application of the CFTC regulations to registered fund promotional materials, and the Final Rule does not do so either.³⁸ Registered fund industry practitioners, including the ICI staff, have raised questions as to whether and to what extent the NFA would seek to apply its rules on the use of promotional materials³⁹ to RIAs that are also required to register as CPOs or CTAs with respect to registered funds unable to rely on CFTC Regulation 4.5.⁴⁰

The ICI staff has advised its members that, on December 28, 2012, it sent a letter to the NFA to confirm conversations between the ICI staff and NFA officials which dealt in part with this issue ("ICI NFA Rules Letter"). In the ICI NFA Rules Letter, the ICI staff confirmed its understanding that, with respect to performance and marketing of registered funds as well as recordkeeping requirements, compliance with applicable SEC requirements will be deemed to constitute compliance with the requirements of the NFA rules relating to those topics, until the NFA amends its own rules to conform with the CFTC's harmonization requirements (although the letter recognized that compliance with the NFA's anti-fraud standards would not be deferred).

Additionally, the ICI NFA Rules Letter noted that registered fund promotional materials prepared by a registered fund's principal underwriter, a broker-dealer registered with the U.S. Financial Industry Regulatory Authority ("FINRA"), are prepared, reviewed, and approved for use in accordance with the procedures established under FINRA's extensive rules governing marketing materials, which incorporate the standards set forth in the SEC's advertising rules. On that basis, the ICI staff confirmed its understanding that, pending further NFA review of how NFA rules compare with the SEC and FINRA rules governing registered fund

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The Adopting Release noted the adoption by the U.S. Congress of the U.S. Jumpstart Our Business Startups Act ("JOBS Act"), which eliminated the prohibition on general solicitation and advertising in connection with the offering of private funds, and the fact that the JOBS Act amends certain provisions of the Securities Act but not the CEA or the CFTC's regulations. The Adopting Release noted the fact that there may be a disparity whereby "private funds may market to the public but private [commodity] pools may not." The Adopting Release states that, because this issue was not raised in the Proposed Rule and was not subject to notice and comment, the CFTC does not believe that the Final Rule is the appropriate mechanism for addressing the differences between the two regimes, but has asked its staff to evaluate the issue and make recommendations to the CFTC for future action. See Adopting Release at 52322.

The JOBS Act impacts the CFTC's regulations for certain CPO registration exemptions (such as CFTC Regulation 4.7), which require that the offering be made in reliance on Securities Act Section 4(a)(2) or Regulation D or S. Presumably because SEC Rule 506 remains a rule under Section 4(a)(2), those CPO registration exemptions should still be available with regard to commodity pools offered in accordance with the new SEC private offering regime. See U.S. JOBS Act Remakes the Standards for Offerings of Hedge Funds and Private Funds, *Dechert OnPoint*, (April 2012), available here.

In particular, NFA Compliance Rule 2-29 (Communications with the Public and Promotional Material). See also NFA Interpretive Notice 9025 (Discussing NFA Rule 2-29), available here, and A Guide to NFA Compliance Rules 2-29 and 2-36: Communications with the Public and Promotional Material, available here.

Letter from the ICI to the NFA, Application of NFA Rules to Registered Investment Companies Unable to Rely on CFTC Rule 4.5 and their Adviser (Dec. 31, 2012).

promotional materials, the NFA will deem compliance by a registered fund's principal underwriter or another broker-dealer with FINRA's review, approval, filing, recordkeeping, and supervision requirements with respect to registered fund promotional materials (including radio and television advertisements, emails that promote funds, and websites) to satisfy a CPO's or CTA's obligation to comply with NFA Compliance Rule 2-29. The NFA has not yet issued any formal guidance or rule proposals relating to these points.

Benefits for Non-Registered Fund CPOs

While the CFTC declined to take the suggestion of certain commenters that it extend the compliance relief granted to ETFs under CFTC Regulation 4.12(c)⁴¹ not only to registered funds but also to private commodity pools, the Final Rule does however provide certain relief to <u>all</u> registered CPOs of all funds (registered, public, or private). Specifically, all CPOs may now use certain third-party service providers as recordkeepers,⁴² and the CFTC has rescinded the individually signed disclosure document acknowledgment requirement under CFTC Regulation 4.21(b) in relation to offering ownership interests in commodity pools. Also, all CPOs may use fund disclosure documents (registered, public, or private) for up to 12 calendar months from the date of the document to offer commodity pool interests, instead of the previous limit of 9 months.⁴³ All Final Rule changes applicable to all CPOs were effective September 23, 2013, except for the rescission of the signed disclosure document acknowledgement requirement, which was effective on August 22, 2013.

. . .

ETFs that are also registered funds may rely on the Final Rule and related CFTC staff guidance discussed herein in lieu of CFTC Regulation 4.12(c) for non-1940 Act registered funds.

For information regarding how to take advantage of this relief, refer to footnote 37 *supra*.

Likewise, a CTA now may use a trading program disclosure document for up to 12 calendar months from the date of the document (instead of 9 months).



APPENDIX A

CFTC Harmonized Disclosure, Reporting, and Recordkeeping Requirements			
CPOs Affected	Regulatory Requirement	Effective/Compliance Date	
CPOs of Registered Funds	File an electronic notice with the NFA regarding the intent to use the SEC substituted compliance regime.	Beginning October 1, 2013, CPOs may file notice through the NFA's online Exemption System. ⁴⁴ Current CPOs should file notice by or before October 21, 2013. ⁴⁵	
	File an electronic notice with the NFA regarding the use of, or intent to use, third-party service providers for recordkeeping purposes.		
	File electronically with NFA the registered fund's annual reports that are prepared pursuant to SEC requirements.	Beginning November 22, 2013, an annual report will need to be filed (1) with the SEC pursuant to the requirements applicable to SEC Form N-CSR and (2) with the NFA within 90 days of the fund's fiscal yearend. 46	
	If the registered fund utilizes a CFC subsidiary, the annual report may consolidate the CFC's financial statements with those of the registered fund, but must also separately indicate in the report the holdings, gains and losses, and other financial statement amounts attributable to the CFC.	File for no-action relief from the CFTC by the end of the registered fund's next fiscal year following November 22, 2013. ⁴⁷ The no-action relief is effective upon filing so long as the request is materially complete. ⁴⁸	
	Add certain CFTC-related disclosure to the front page legend of the registered fund's current prospectus. Disclose that the registered fund's NAV is publicly available and the means for obtaining the information (this would allow the fund to avoid the CFTC's monthly account statement preparation and distribution requirements).	Any prospectus changes would need to be addressed in the next annual update or initial registration statement on or after November 22, 2013. ⁴⁹	

Similarly, a registered fund's CFC will not be required to prepare and distribute a separate CFTC-compliant disclosure document, but rather its disclosure can be incorporated into the registered fund's prospectuses pursuant to the SEC rules as is the current industry practice.

⁴⁴ NFA Notice Regarding Notice Filings.

We understand from informal guidance from the CFTC staff that the deadline to file these notices is October 21, 2013. See also ICI Harmonization Letter.

⁴⁶ ICI Harmonization Letter at 4.

⁴⁷ CPOs seeking relief to consolidate CFC reporting in relation to <u>both</u> the registered fund's annual report <u>and</u> CFTC Form CPO-PQR must file for no-action relief from the CFTC by the earlier of the close of the registered fund's next fiscal year following November 22, 2013 or December 31, 2013. See footnotes 5 and 9 *infra*.

Consolidation No-Action Letter at 7-8.

⁴⁹ ICI Harmonization Letter at 2.

CFTC Harmonized Disclosure, Reporting, and Recordkeeping Requirements		
CPOs Affected	Regulatory Requirement	Effective/Compliance Date
	For a registered fund with less than three years of operating history, the fund is required to disclose, in its prospectus, the performance of all other pools (<i>i.e.</i> , funds) and separately managed accounts that the CPO of the fund manages pursuant to substantially similar investment objectives, policies, and strategies as those of the offered fund.	Any prospectus changes would be addressed in the next annual update or initial registration statement on or after November 22, 2013. ⁵⁰
	Begin reporting the assets in the registered fund as a listed commodity pool on the CPO's CFTC Form CPO-PQR and NFA Form PQR. CFC assets may be consolidated with a registered fund's assets for reporting purposes if the CPO files for no-action relief	The CPO must include fund assets on its CFTC Form CPO-PQR or NFA Form PQR filing (as applicable for the given quarter) beginning with the calendar quarter ending December 31, 2013. ⁵¹
	from the CFTC.	File for no-action relief from the CFTC by December 31, 2013. The no-action relief is effective upon filing so long as the request is materially complete. 52
All CPOs	All CPOs will no longer be required to obtain an individually signed acknowledgment from investors of receipt of fund disclosure documents (registered, public, or private).	Effective August 22, 2013 (date of publication in the U.S. Federal Register).
	All CPOs may use certain third-party service providers to maintain their books and records. In order to do so, CPOs will need to file a notice with the NFA regarding the use of, or intent to use, third-party service providers for recordkeeping purposes.	Effective September 23, 2013. Beginning October 1, 2013, CPOs may file the notices regarding third-party recordkeepers through the NFA's online Exemption System. 53
	All CPOs may use a disclosure document (registered, public, or private) to offer commodity pool interests for up to 12 calendar months after the date of the document (instead of 9 months).	

⁵⁰ *Id*.

We understand from informal guidance from the CFTC staff that this effectively means registered fund assets will be included on the fourth quarter CFTC Form CPO- PQR for 2013 (i.e., as of December 31, 2013), which will be due either 60 or 90 calendar days following 2013 calendar year-end depending on the size of the CPO. See also ICI Harmonization Letter at 4.

⁵² Consolidation No-Action Letter at 6-7.

NFA Notice Regarding Notice Filings.



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