DechertOnPoint

Dechert Follow-Up Comment Letter Regarding CFTC Proposed Rulemaking to Amend Regulation 4.5 and Rescind Regulations 4.13(a)(3) and (a)(4)

by M. Holland West, Julien Bourgeois and Audrey Wagner

Dechert LLP

July 2011

Dechert LLP

1095 Avenue of the Americas
New York, NY 10036-6797
+1 212 698 3500 Main
+1 212 698 3599 Fax
www.dechert.com

M. HOLLAND WEST

holland.west@dechert.com
+1 212 698 3527 Direct
+212 698 0453 Fax

July 26, 2011

David A. Stawick
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: CFTC Proposed Rulemaking to Amend Regulation 4.5 and Related Issues [RIN number 3033-AD30]

Dear Mr. Stawick:

Dechert LLP ("**Dechert**") appreciates this additional opportunity to comment on the proposed rulemaking of the Commodity Futures Trading Commission ("**CFTC**") regarding the modification of exclusionary relief and rescission of exemptive relief available to certain persons that would otherwise be required to register as commodity pool operators ("**CPOs**").[1] This comment letter focuses on the proposed changes to CFTC Regulation 4.5 ("**Regulation 4.5**"),[2] which currently excludes from the definition of CPO (among other persons) investment companies registered under the Investment Company Act of 1940 as amended ("**1940 Act**"),[3] and addresses the proposed changes to CFTC Regulation 4.13(a)(3) ("**Regulation 4.13(a)(3)**")[4] as it

[1] Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations, 76 Fed. Reg. 7976 (proposed Feb. 11, 2011) ("**Proposing Release"**) (announced by the CFTC at an open meeting on January 26, 2011).

[2] 17 C.F.R. § 4.5. *See also* 7 U.S.C. § 1a(5).

[3] 15 U.S.C. § 80a-1 *et seq*.

[4] 17 C.F.R. § 4.13(a)(3).

applies to private funds and to CFTC Regulation 4.13(a)(4) ("**Regulation 4.13(a)(4)**")[5] as it applies to private funds and registered investment company wholly-owned offshore subsidiaries ("**CFCs**") (collectively "**Proposed Part 4 Rule Changes**"). Dechert has previously commented on the CFTC's public notice regarding the National Futures Association's ("**NFA's**") petition for changes to Regulations 4.5 and 4.13(a)(3),[6] as well as the CFTC's Proposing Release.[7]

---

[5] 17 C.F.R. § 4.13(a)(4).

[6] Although the CFTC has stated that the Proposed Part 4 Rule Changes are related to other regulations it is required to adopt under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank Act**"), the NFA instead generated the rule proposal when in June 2010 it petitioned the CFTC to make almost identical amendments to Regulation 4.5 as those currently set forth in the Proposed Part 4 Rule Changes. Letter from Thomas W. Sexton, III, Senior Vice President and General Counsel, NFA, to David A. Stawick, Office of the Secretariat, CFTC (June 29, 2010), *available at* http://www.nfa.futures.org/news/newsPetition.asp?ArticleID=2491. On August 18, 2010, the NFA revised its proposed rule amendment to apply only to registered investment companies and not to the other persons eligible for exclusion under CFTC Regulation 4.5. Letter from Thomas W. Sexton, III, Senior Vice President and General Counsel, NFA, to David A. Stawick, Office of the Secretariat, CFTC (August 18, 2010), *available at* http://www.nfa.futures.org/news/newsPetition.asp?ArticleID=3630 ("**NFA Letter**"). For a discussion of the NFA Letter, refer to the August 2010 Dechert LLP OnPoint client alert available at http://www.dechert.com/files/Publication/74354d53-8723-48de-b075-03fcff78b805/Presentation/PublicationAttachment/05161d32-63d7-4ef8-89aa-0ae37ac269d2/FS_21-08-10-NFA_Petitions_for_Rulemaking.pdf. On September 17, 2010, the CFTC alerted the public to the NFA's petition and requested comments. Petition of the National Futures Association, Pursuant to Rule 13.2, to the U.S. Commodity Futures Trading Commission to Amend Rule 4.5, 75 Fed. Reg. 56997 (Sept. 17, 2010) ("**Notice of Petition**"). On April 12, 2011, the NFA commented on the Proposed Part 4 Rule Changes as a whole and further revised its proposed rule amendment regarding Regulation 4.5. Letter from Thomas W. Sexton, III, Senior Vice President and General Counsel, NFA, to David A. Stawick, Office of the Secretariat, CFTC (April 12, 2011), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=42160&SearchText= ("**NFA Revised Letter**").

[7] Letter from M. Holland West, Partner, Dechert LLP, to David A. Stawick, Office of the Secretariat, CFTC (October 18, 2010), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=26313&SearchText=, Letter from George J. Mazin, Partner, Dechert LLP, to David A. Stawick, Office of the

On July 6, 2011, staff of the CFTC ("**CFTC Staff**") held a public roundtable ("**July 6 Roundtable**") meeting to discuss issues related to the Proposed Part 4 Rule Changes with members of the domestic and international financial services industry that would be affected by the changes, as well as with staff ("**SEC Staff**") of the Securities and Exchange Commission ("**SEC**").[8] In connection with the July 6 Roundtable, the NFA submitted its fifth public statement which summarized the NFA Revised Letter. It was intended to "address both the CFTC and NFA's regulatory objectives, while at the same time not eliminating [mutual fund] products," as well as to request that the CFTC retract its proposed rescission of Regulation 4.13(a)(3) (together with the NFA Revised Letter, "**NFA Modified Proposal**").[9] Following the July 6 Roundtable and the submission of the NFA Modified Proposal, the CFTC temporarily reopened the comment period on the Proposed Part 4 Rule Changes and the NFA Modified Proposal.

Secretariat, CFTC (April 12, 2011), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=42176&SearchText=, Letter from Dechert LLP and Clients, to David A. Stawick, Office of the Secretariat, CFTC (April 12, 2011), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=42183&SearchText=.

[8] A list of July 6 Roundtable participants is available at http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/participants070611.pdf.

[9] Carol Wooding, Assistant General Counsel, NFA, Public Statement at the July 6, 2011 Roundtable: Proposed Changes to Registration and Compliance Regime for Commodity Pool Operators and Commodity Trading Advisors (July 6, 2011), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=46737&SearchText=.

Introduction

We respectfully believe that the CFTC's and NFA's concerns, efforts and resources should be focused on the fostering of open, competitive, financially sound and transparent markets. Providing the CFTC access to market and participant trading activity and position data, including data from companies registered with the SEC under the 1940 Act ("**RICs**") and private funds, serves those objectives. To achieve this aim, the CFTC should not also be focused on promulgating duplicative, conflicting, onerous, and costly disclosure and operating compliance regulation on RICs, America's favorite and most regulated investment vehicles, and on their investors already adequately protected by long-standing SEC regulation and for which there is no history or evidence of abuse identified by the NFA, CFTC or any other person.

Although investment vehicles excluded or exempt from CPO regulation are currently outside of much, if not all, of the CFTC's disclosure, document delivery, reporting, recordkeeping, advertising and personnel licensing and testing requirements, their trading activities in the commodity markets have always been, and continue to be, well within the CFTC's regulatory jurisdiction. The CFTC already has direct access to these market participants' trading data by way of large trader reporting,[10] special calls[11] and imposition and enforcement of speculative position limits.[12] In this respect, excluded and exempt CPO obligations to the CFTC are no different than any other commodity traders. In addition, SEC disclosure requirements require

---

10 17 C.F.R. Part 18.

11 17 C.F.R. Part 21.

12 17 C.F.R. Part 150.

RICs to make available significant and detailed amounts of information regarding commodity interest trading objectives, strategies and associated risks in their registration statements filed with the SEC at least annually on Form N-1A.[13] SEC reporting requirements also require RICs to report in detail their holdings, including commodity interests, to the SEC quarterly on Form N-Q[14] and to their investors on a semi-annual basis on Form N-CSR.[15] RIC registration statements and semi-annual shareholder reports are publicly available on-line through the SEC's Electronic Data Gathering, Analysis and Retrieval, in the SEC's public reading room in Washington, D.C. and through most RIC sponsors' public websites. SEC registration requirements for RIC investment advisers require the filing and annual updating of Form ADV. Part 2 of Form ADV, in particular, requires an investment adviser to file a brochure with the SEC that describes, in detail, the entity's advisory business, including types of investments, strategies and risks. Each registered investment adviser's Form ADV is publicly available on the SEC's Investment Adviser Public Disclosure system.[16] Additionally, the CFTC already has jurisdiction over excluded and

---

[13] Form N-1A, Items 4(a), 9(b), and 16(b). Specific disclosure of a mutual fund's policies with respect to commodity investing is also required. 15 U.S.C. § 8(b)(1)(F), Form N-1A, Item 16(c)(1)(v). There are similar requirements applicable to closed-end RICs that file their registration statements on Form N-2 and to their shareholder reports.

[14] 17 C.F.R. §270.30b1-5.

[15] 17 C.F.R. §270.30b1-1. Recently, the SEC reiterated the importance of specifying derivatives disclosure in shareholder communications in the form of disclosure and reports. Letter from Barry D. Miller, Associate Director, Office of Legal and Disclosure of the SEC Division of Investment Management, to Karrie McMillan, General Counsel, Investment Company Institute ("**ICI**") (July 30, 2010), *available at* http://www.sec.gov/divisions/investment/guidance/ici073010.pdf ("**SEC Derivatives Disclosure Letter**").

[16] 17 C.F.R. § 275.203-1. *See* Amendments to Form ADV, 75 Fed. Reg. 49234 (Aug. 12, 2010).

exempt CPOs to enforce violations by market participants affecting the commodity markets or of the Commodity Exchange Act as amended ("**CEA**")[17] and CFTC regulations.[18]

In 2003, when the CFTC removed the then-current operating restrictions from the Regulation 4.5 CPO exclusion,[19] its intention was "to encourage and facilitate participation in the commodity interest markets by additional collective investment vehicles and their advisers, with the added benefit to all market participants of increased liquidity."[20] The NFA strongly and actively endorsed and supported those objectives. Those goals have unquestionably been achieved. The volume and liquidity that collective investment vehicles, of which mutual funds are a significant subset, supply to the commodity markets supports and improves the proper and effective functioning of those markets and facilitates price discovery.[21] Since 2003, mutual funds have

---

17 7 U.S.C. § 1 *et seq.*

18 *E.g.*, 7 U.S.C. §§ 6b, 6o, 9, 13, 13b; *see also* Prohibition on Employment, or Attempted Employment, of Manipulative and Deceptive Devices and Prohibition on Price Manipulation, 76 Fed. Reg. 41398 (July 14, 2011).

19 The CFTC's amendments to Regulation 4.5 in 2003 expanded the scope and use of Regulation 4.5 by eliminating certain operating restrictions on qualifying entities. In particular, the CFTC eliminated the requirement that a qualifying entity use commodity futures or commodity options contracts solely for *bona fide* hedging purposes, although five percent or less of the liquidation value of the qualifying entity's portfolio could be allocated to the aggregate initial margin and premiums necessary to establish non-*bona fide* hedging positions ("**five-percent initial margin test**"). The CFTC also eliminated the language prohibiting a qualifying entity from marketing participations to the public as or in a commodity pool or otherwise as or in a vehicle for trading in the commodity futures or commodity options markets ("**marketing restriction**"). Additional Registration and Other Regulatory Relief for Commodity Pool Operators and Commodity Trading Advisors; Past Performance Issues, 68 Fed. Reg. 47221 (Aug. 8, 2003) ("**2003 Amendments**").

20 2003 Amendments, 68 Fed. Reg. at 47223.

21 Registration under the Advisers Act of Certain Hedge Fund Advisers, 69 Fed. Reg. 45172 ,45178 (proposed July 28, 2004) (stating, "We must also recognize the important role that hedge funds

increasingly participated in, and grown to rely upon access to, the commodity markets as an additional asset class and as additional instruments to replicate trading in securities and indices, benefiting both those markets and the funds' shareholders who desire access to such markets. The 2003 Amendments also made possible the availability of mutual funds that offer physical commodity exposure to retail investors in an efficient, cost-effective and liability-limiting manner. For most retail investors, investing in mutual funds is the only accessible means of diversifying their stock and bond portfolios with uncorrelated or negatively correlated physical commodity exposure, a beneficial practice for retail investors that the CFTC has recognized.[22]

---

play in our markets. Hedge funds contribute to market efficiency and liquidity. They play an important role in allocating investment risks by serving as counterparties to investors who seek to hedge risks." In this regard, mutual fund activity in the markets is not different from hedge funds.); *see also*, David Harris, General Counsel, Nasdaq Liffe Markets, LLC, Remarks at the CFTC Roundtable on Managed Funds (Sept. 19, 2002); Dr. Henry Jarecki, Chairman, Gresham Investment Management, Written Testimony for the CFTC Hearing on Speculative Position Limits in Energy Futures Markets (July 29, 2009).

The 2003 Amendments resulted, in part, from industry comments that the CFTC had received in conjunction with the CFTC's broader study mandated by Section 125 of the Commodity Futures Modernization Act of 2000, CFTC regulations and conduct of CFTC registrants. In the CFTC's report regarding the study, the CFTC noted that commenters had brought the issue of overlapping regulatory jurisdiction in the managed funds industry to the CFTC's attention. In response, the CFTC planned to hold a roundtable to address "ways in which this regulatory environment may be made less confusing and burdensome." CFTC, Report on the Study of the Commodity Exchange Act and the Commission's Rules and Orders Governing the Conduct of Registrants Under the Act 26 (June 2002), *available at* http://www.cftc.gov/files/opa/opaintermediarystudy.pdf. The study, in addition to the roundtable, informed the CFTC's decision to promulgate the 2003 Amendments. Additional Registration and Other Regulatory Relief for Commodity Pool Operators and Commodity Trading Advisors, 68 Fed. Reg. 12622, 12625 (proposed Mar. 17, 2003).

22 Risk Management Exemption from Federal Speculative Position Limits, 72 Fed. Reg. 66097, 66098 (proposed Nov. 27, 2007).

Jurisdictional Accommodation and Regulatory Deference

The SEC and its Division of Investment Management have long maintained a jurisdictional accommodation of, and regulatory deference to, public commodity pools that would otherwise be required to register as RICs, if those pools meet the conditions outlined in a line of SEC Staff no-action letters.[23] We believe that the CFTC likewise should afford a similar accommodation to RICs and their related persons that would otherwise be required to register as CPOs, rather than subjecting them to dual-registration, thus rendering the Proposed Part 4 Rule Changes and NFA Modified Proposal unnecessary.

However, if the CFTC determines not to afford RICs investing in commodity interests similar jurisdictional accommodation and regulatory deference as described above and as commented on by many persons in response to the Proposed Part 4 Rule Changes, we respectfully submit that the CFTC needs to consider the points outlined below.

Transparency and Market Protection

If the CFTC's overriding objective with regard to the Proposed Part 4 Rule Changes is transparency that would afford it access to additional commodity trading data to facilitate its mandate to oversee and protect the regulated commodity markets, we recommend that the CFTC consider, as an alternative to CPO registration, making it a condition for any person claiming a CPO registration exclusion under Regulation 4.5 (as well as any person, including CFCs,

---

[23] *Peavey Commodity Futures Fund I, II, III*, SEC No-Action Letter (pub. avail. June 2, 1983); *Dean Witter Principal Guaranteed III Fund L.P.*, SEC No-Action Letter (pub. avail. July 23, 1992); *Managed Funds Association*, SEC No-Action Letter (pub. avail. July 15, 1996).

claiming a CPO exemption under Regulations 4.13(a)(3) and (4)) to file additionally with the CFTC any reports already required of such persons to be provided to investors and/or to be filed with the SEC (described above, possibly with some additional items adopted jointly with the SEC after a rule proposal and industry consultation). Excluded and exempt CPOs would also continue to be subject to the CFTC's existing market regulation tools, such as large trader reporting and special calls. On the other hand, subjecting currently excluded and exempt CPOs to applicable registered CPO disclosure, reporting, recordkeeping, advertising, licensing and testing requirements would provide to the CFTC little additional transparency regarding commodity market activity than is already available to the public and/or the SEC as well as the CFTC itself. It would, however, result in significant, and not yet quantified, market costs to the detriment of U.S. investors and the American economy.

Rulemaking Process and Harmonization

In advance of any further CFTC rulemaking action in respect of the Proposed Part 4 Rule Changes, the CFTC should continue to gather data (including estimated cost data) and input to understand the RIC industry better. Until the Dodd-Frank Act swaps-related rules (including particularly margin requirements for both cleared and non-cleared swaps) have been finalized and implemented by the CFTC and the SEC,[24] this gathering of data could not be complete as the

[24] The CFTC has proposed a process for reviewing which swaps will be subject to mandatory exchange clearing. Process for Review of Swaps for Mandatory Clearing, 75 Fed. Reg. 67277 (proposed Nov. 2, 2010). The CFTC has proposed rules regarding margin requirements applicable to uncleared swaps. Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 76 Fed. Reg. 23732 (proposed Apr. 28, 2011). The CFTC has also sought public comments regarding segregation rules for margin for cleared swaps and initial margin for uncleared swaps. Protection of Cleared Swaps Customers Before and After Commodity Broker

Proposed Part 4 Rule Changes include commodity swap trading as a potential qualifying factor for CPO registration. Gathering such data, awaiting final rulemaking on swaps and conducting a thorough cost-benefit analysis would be especially important for the CFTC determining appropriate and workable asset-based or trading level tests for CPO registration. Data gathering can be achieved with a special call. With assistance from the SEC, the CFTC should also spend additional time to learn about the 1940 Act, mutual funds, their use of derivatives and their actual impact on the markets. If the CFTC were then to determine to proceed with the Proposed Part 4 Rule Changes as modified, the CFTC should re-propose the rules to permit further industry comment. We believe that seeking further industry comment after making changes to the Proposing Release would be consistent with the Administrative Procedures Act.[25]

RIC sponsors would want to see that any re-proposal affords RICs, at a minimum where applicable, the same regulatory compliance relief as the CFTC provided in its final rule ("**Commodity ETF Rule**") with regard to commodity exchange traded funds ("**Commodity ETFs**"), but would want the opportunity to comment on how the Commodity ETF Rule should translate and apply to RICs.[26] For example, the Commodity ETF Rule remains too restrictive on individual director/trustee CPO registration.[27]

Bankruptcies, 75 Fed. Reg. 75162 (Dec. 2, 2010) (advance notice of proposed rulemaking); Protection of Collateral of Counterparties to Uncleared Swaps: Treatment of Securities in a Portfolio Margining Account in Commodity Broker Bankruptcy, 75 Fed. Reg. 75432 (proposed Dec. 3, 2010).

25 5 U.S.C. §§ 551-559.

26 The Commodity ETF Rule exempts Commodity ETFs from the CFTC periodic account statement distribution requirements. Rather than distributing a monthly account statement to each pool

There are multiple major inconsistencies and conflicts between the two sets of regulations that will need to be harmonized to permit the operation of dually-registered RICs/commodity pools. Please refer to **Annex A** which details certain of the most significant inconsistencies and conflicts between the two regulatory regimes. Where inconsistent or conflicting items are close enough that one or the other regime could be used to achieve the same end (*e.g.*, the CPO disclosure document requirement that a break-even point be included versus the Form N-1A expense example chart that permits an investor to calculate a break-even point),[28] we believe that the CFTC should defer to the SEC regime which has effectively regulated RICs for 70 years. It is imperative that the CFTC Staff and the SEC Staff collaborate on any final rules to eliminate duplication and conflicts and avoid unnecessary and costly requirements.

---

participant, Commodity ETFs are permitted to maintain each account statement on their website for at least 30 days. The Commodity ETF Rule also exempts Commodity ETFs from the CPO disclosure document delivery requirements and, instead, requires CPOs to make their disclosure documents readily accessible on their website, inform prospective investors with whom the CPO has contact of their availability, and direct selling agents to do the same. Commodity Pool Operators: Relief From Compliance With Certain Disclosure, Reporting and Recordkeeping Requirements for Registered CPOs of Commodity Pools Listed for Trading on a National Securities Exchange; CPO Registration Exemption for Certain Independent Directors or Trustees of These Commodity Pools, 76 Fed. Reg. 28641 (May 18, 2011)("**Commodity ETF Rule Release**"). Mutual funds, like Commodity ETFs, also have a constantly changing investor base, making distribution of monthly reports both costly and unnecessary, especially given the fact that mutual funds already make publicly available their net asset value and provide semi-annual reports to investors. The Commodity ETF Rule is a starting point for the CFTC to consider certain issues related to mutual funds, as differences between mutual funds and Commodity ETFs do not justify more burdensome treatment of mutual funds.

[27] *Id*. at 28641.

[28] *Compare* 17 C.F.R. §§ 4.24 (d)(5), 4.10(j) *with* Form N-1A, Item 3.

Costs

The cost of mutual fund regulation, America's favorite collective investment vehicle, is already very high. The costs of the Proposed Part 4 Rule Changes have the potential to increase costs significantly per sponsor, per fund and industry-wide. Any additional regulation should carefully consider additional costs and benefits to the U.S. investing public and the commodity markets. We believe that it is imperative for the CFTC to determine the likely economic consequences of the Proposed Part 4 Rule Changes and their effect on the mutual fund industry. As the CFTC learned at the July 6 Roundtable, RICs typically consider disclosure preparation and filing and reporting to shareholders to be fund expenses because they are undertaken to comply with requirements directly applicable to the fund. As a result, these costs are, and will be, charged to shareholders rather than being covered by the sponsor or adviser. If the CFTC's priority is mostly transparency and commodity market integrity and protection, the costs of rule changes and dual registration will be disproportionally and inappropriately borne by U.S. investors. Making documents available electronically, as provided for in the Commodity ETF Rule,[29] would mitigate printing and mailing costs, but not the preparation costs associated with additional disclosure and reporting. The CFTC needs to balance the effect additional expenses will have on shareholder returns with any added benefit of any new disclosure, reporting and other additional regulatory requirements.

---

[29] Commodity ETF Rule Release, 76 Fed. Reg. at 28642, 28644-28645.

Responses to NFA Modified Proposal

We also take this opportunity to respond to the NFA Modified Proposal.

Clarification Regarding Persons to Register

The NFA has recommended that a RIC's investment adviser should be the entity required to register as the CPO rather than the RIC itself, which under current Regulation 4.5(a) is the excluded CPO. We generally agree with the NFA in this regard. The investment adviser registering as the CPO makes practical sense as it would limit the number of unique registered entities as well as account for the fact that a RIC could vary over time in meeting or not meeting the various asset-based or trading level tests (if any). Having the investment adviser register as the CPO instead of the fund would be analogous to the approach used with many public and private commodity pools and is consistent with prior CFTC positions and interpretations.[30] But, the CFTC will nevertheless need to reconcile the definitions of a CPO in the CEA and CFTC regulations with this practical approach and position.

As to the NFA's point regarding fund independent directors/trustees, we agree in part with the NFA, but we believe further that CPO registration of any fund directors/trustees individually (whether independent or non-independent or U.S. or non-U.S.) is not sensible, as these persons, in

---

30 *See* Commodity Pool Operators and Commodity Trading Advisors; Exemption from Registration and From Subpart 4 for Certain Otherwise Regulated Persons and Other Regulatory Requirements, 49 Fed. Reg. 4778, 4780 (proposed Feb. 8, 1984) (noting that, in determining who is the CPO of a given pool, "the staff typically looks at . . . who will be acting in the manner contemplated by the statutory definition of the term "commodity pool operator"—*e.g.*, who will be promoting the pool by soliciting, accepting or receiving from others, property for the purpose of commodity interest trading—and who will have the authority to hire (and to fire) the pool's CTA and to select (and to change) the pool's [futures commission merchant].").

the mutual fund context, perform a governance function and are not operating or advising the fund or soliciting participations in the fund.[31] Accordingly, we believe that even non-independent directors/trustees should not be required to register as CPOs.[32] Furthermore, CPO registration of directors/trustees, or allowing them to delegate functions to a registered CPO, would subject these persons individually to joint and several liability with the CPO for violations of the CEA.[33] Currently, the business judgment rule provides directors/trustees with significant liability protection. Accordingly, we do not believe that any directors/trustees individually should have to assume such joint or several liability with the RIC's investment adviser as the registered CPO. As has been repeatedly commented on by many people, requiring any natural person director/trustee of a RIC to register individually as a CPO or assume joint and several liability for

---

31 With regard to private funds, the CFTC also needs to provide the industry clarity on individual director/trustee CPO registration where the pool is organized as a corporation, trust or other entity with no separate operator. *See*, CFTC No-Action Letter No. 97-73 (Aug. 20, 1997) (granting no-action relief to directors of a fund who did not register as CPOs where the directors delegated the fund's operations, solicitation and supervision to a registered CPO and the registered CPO managed the fund); CFTC No-Action Letter No. 09-39 (Jul. 30, 2009) (granting no-action relief to trustees of a commodity pool organized as a trust who did not register as CPOs where the trustees had no authority to perform CPO functions and a separate registered CPO performed all CPO functions for the trust); CFTC No-Action Letter No. 10-06 (Mar. 29, 2010) (granting no-action relief to independent trustees of a commodity pool organized as a trust who did not register as CPOs where the independent trustees had no authority to perform CPO functions, the independent trustees were appointed solely to meet certain audit committee independent trustee membership requirements and a separate registered CPO was authorized to perform all CPO functions).

32 With regard to non-independent, investment adviser/sponsor directors/trustees, it may be appropriate for them to be named as principals of the CPO.

33 In some instances where the CFTC has granted no-action relief for fund trustees from CPO registration, a condition of the relief has been that the board of trustees and the registered CPO of the fund continue to accept joint and several liability for any violations of the CEA. *See, e.g.*, CFTC No-Action Letter No. 97-73 (Aug. 20, 1997).

CPO compliance is unworkable, will result in a fundamental and negative change in RIC governance and discourage individuals from serving on boards and will be inconsistent with SEC requirements. Further, a director/trustee should not be subject to taking any proficiency test (*e.g.*, Series 3) that does not bear on his/her function.

Five-Percent Initial Margin Test

As noted above, with regard to the CFTC setting any asset-based or trading level test, the CFTC should wait at least until the CFTC and the SEC finalize and implement exchange and over-the-counter margin rules and gather further industry input. Given that the definition of "commodity interests" will include an increased number of products (*i.e.*, both cleared and uncleared swaps which were not counted for the five-percent initial margin test in place before 2003) and higher margin requirements generally are expected pursuant to the Dodd-Frank Act related rules, the five-percent initial margin test should be adjusted to significantly increase the percentage threshold so as not to inadvertently capture more funds than is necessary and appropriate and with respect to which the CFTC and NFA have the time and resources to oversee meaningfully. Consideration should also be given to making available an alternate test such as an aggregate net notional value test similar to the one available to private commodity pools in current Regulation 4.13(a)(3)(ii)(B).[34] As the net notional value test is a legitimate test the CFTC currently uses to determine when it should require CPO registration based on the amount of commodity interest trading, there is no reason not to use it in the RIC context as well. Furthermore, the NFA believes

[34] 17 C.F.R. § 4.13(a)(3)(ii)(B).

that the alternative test is worthwhile since it has now recommended that Regulation 4.13(a)(3) continue in effect and not be rescinded, as discussed below.

However, we disagree with the NFA that, if a RIC exceeds the applicable threshold test and is marketed as a vehicle for trading commodity interests, the RIC and its CPO should be subject to the full panoply of CFTC Part 4 Regulations. Instead, because RICs are already adequately regulated by the SEC, if a RIC exceeds the applicable threshold test, its CPO should be exempt from certain of the CFTC's Part 4 Regulations relating to disclosure, reporting and recordkeeping, similar to CFTC Regulation 4.7 or 4.12.[35]

Marketing Restriction

As an initial matter, any marketing restriction has no bearing on a RIC's activities in the commodity markets. If the CFTC has prioritized commodity market transparency and data collection, there is no reason to include any marketing restriction in a revised Regulation 4.5. We strongly recommend that the marketing restriction be eliminated entirely from further consideration as it is fraught with vagueness, uncertainty and issues regarding breadth and application, has unintended consequences and directly conflicts with both SEC and CFTC disclosure requirements relating to investment objectives, strategies, activities and benefits, returns, exposures, risks and conflicts, as described in further detail in **Annex A**.

However, if the CFTC determines to maintain a marketing restriction, the test must be workable; otherwise the marketing restriction swallows any asset-based or trading level test and obligates

---

[35] 17 C.F.R. §§ 4.7, 4.12.

virtually every RIC that trades any commodity interests or incurs any commodity market exposure to comply with the CPO requirements. The currently proposed marketing restriction is too vague and too broad. It has the potential to inadvertently capture more funds than is necessary and appropriate. One absurd application would be a RIC that purchases securities of a mining company, financial services company or any other company whose business is in commodities or uses the commodity markets; that RIC could be considered to be "a vehicle for trading in (*or otherwise seeking investment exposure to) the commodity futures, commodity options, or swaps markets.*"[36] There are many other examples.

The NFA Modified Proposal recognizes that the marketing restriction included in the Proposed Part 4 Rule Changes is unworkable. However, the NFA Modified Proposal also falls short as it indicates that the NFA may not understand the type of disclosure obligations that apply to mutual funds. For example, the SEC Staff has made clear that mutual funds should, in order to comply with their disclosure obligations, disclose with specificity the derivatives they use and the purposes of their derivatives investments.[37] All mutual funds that invest in commodity interests and simply comply with their SEC disclosure obligations would likely trigger the "No Marketing Restriction." In this sense, the NFA Modified Proposal is still likely overbroad.

---

36 Proposing Release, 76 Fed. Reg. at 7989 (emphasis added).

37 *See generally* SEC Derivatives Disclosure Letter.

The other various criteria the NFA sets forth for objectively determining whether a fund "'should be' marketed as a commodity pool" are also problematic as well as broad, vague, subjective, risky and/or inapplicable:

- Several terms included in the criteria are not defined or explained, including "primary source of potential gains or losses," "consistently exceeds," "extent to which it does so," "normal trading activities" and "any commodity."
- The use of a wholly-owned or controlled subsidiary (*e.g.*, a CFC) for commodity interest trading purposes is a structural, not marketing, attribute. Some RICs that would fundamentally not be commodity pools set up these subsidiaries out of an abundance of caution due to the Internal Revenue Service ("**IRS**") rules on qualifying income.
- As discussed above, a net notional value test should be included as an alternative asset-based or trading level test. This is a trading, not a marketing, attribute.
- Having a "net short speculative exposure to any commodity" is too broad and vague as to amount, percentage, time, frequency and other relevant considerations.

Finally, the NFA's proposal that the CFTC "place the burden on the CPO to evaluate whether a pool that is a RIC is being appropriately marketed" opens the RIC's adviser to second-guessing and additional liability for making the determination with regard to a vague and overly-broad rule. Any marketing restriction the CFTC settles on must be a pragmatic, objective test that works, strikes the right balance for dual regulation and captures only a limited number of RICs.

Again, however, we believe that any marketing restriction is unnecessary to achieve the CFTC's objectives.

Commodity-Linked Notes

The NFA's proposal with regard to commodity-linked notes fails to acknowledge that RICs invest in these instruments for the same IRS rule reasons that they invest in wholly-owned subsidiaries: commodity-linked notes generally produce qualifying income.

Regulation 4.13(a)(3)

We agree with the NFA that the CFTC should not rescind the CPO exemption in Regulation 4.13(a)(3). We believe that it could be a reasonable condition to require that the fund's investment adviser (rather than the "fund" itself, as the NFA proposes) be subject to SEC oversight (*i.e.*, registration as an investment adviser) in order to claim the exemption. Requiring the fund to be regulated by the SEC is inconsistent with, and defeats the purpose of, Regulation 4.13(a)(3) and would make the exemption generally unavailable. Additionally, for the same reasons discussed above regarding the proposed five-percent initial margin test for the Regulation 4.5 exclusion, the test should be adjusted to significantly increase the percentage threshold. Likewise, the alternative aggregate net notional value test should be retained. Finally, for the same reasons discussed above regarding the CFTC's ability to gain additional transparency in commodity trading activity, the CFTC could introduce a further condition that any person claiming the CPO exemption under Regulation 4.13(a)(3) must file additionally with the CFTC

any reports already required of such person to be provided to investors and/or to be filed with the SEC.[38]

Regulation 4.13(a)(4)

For the same reasons discussed by the NFA and by us above with respect to not rescinding Regulation 4.13(a)(3), we likewise believe that the CFTC should not rescind the CPO exemption in Regulation 4.13(a)(4), particularly in view of the sophisticated and limited participants in a qualifying pool. In the NFA Modified Proposal, the NFA acknowledges that investors in pools for which the CPO is exempt from registration under Regulation 4.13(a)(3) are sophisticated and less in need of regulatory protection. It bears noting that the threshold for eligibility for investment in a pool for which the CPO is exempt from registration under Regulation 4.13(a)(4) is more stringent than that under Regulation 4.13(a)(3).[39] We also believe that the CFTC could add reasonable conditions to the availability of the exemption in Regulation 4.13(a)(4) as discussed above with respect to Regulation 4.13(a)(3), adjusted of course to the nature of the relevant pool participants.

---

38 *See* Annex A.

39 *Compare* 4.13(a)(3)(iii) *with* 4.13(a)(4)(ii).

* * *

Thank you for considering our additional views on this important topic. If you have questions or if we can provide additional information that may assist the CFTC and the CFTC Staff, please contact Holland West at 212.698.3527 or holland.west@dechert.com, Julien Bourgeois at 202.261.3451 or julien.bourgeois@dechert.com, or Audrey Wagner at 202.261.3365 or audrey.wagner@dechert.com.

Respectfully submitted,

/s/ M. Holland West_

M. Holland West
Partner

Annex A – Comparison of Significant CFTC/SEC Areas for Harmonization

ANNEX A

COMPARISON OF SIGNIFICANT CFTC/SEC AREAS FOR HARMONIZATION[40]

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
Disclosure (Including Past Performance)			
1.	A CPO is required to provide performance information for each other similar pool and account it operates and explain the material differences between the offered pool and the other pools and accounts. The CPO must also disclose the performance of any accounts (including pools) directed by a major CTA to the relevant pool.[41]	A mutual fund is only permitted to disclose the performance of other funds in limited circumstances, and even then only if they are substantively similar to the fund itself.[42]	Absent relief, this is a direct conflict. A registered investment company is permitted to include in its registration statement performance data for other accounts only in circumstances where the other account is managed in a substantially similar manner, among other requirements. In addition, Financial Industry Regulatory Authority rules generally prohibit broker-dealers from using sales literature for a registered investment company that includes the performance of other accounts.

---

40 This chart was prepared in part on comments previously provided by Dechert and other commenters, including the ICI. Letter from Karrie McMillan, General Counsel, ICI, to David A. Stawick, Office of the Secretariat, CFTC (Apr. 12, 2011), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=42191&SearchText=.

41 17 C.F.R. §§ 4.25(a)(3) and (c)(2)-(3).

42 *E.g.*, *Nicholas-Applegate Mutual Funds*, SEC No-Action Letter (pub. avail. Aug. 6, 1996).

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
2.	A commodity pool must include the rate of return presented on a monthly basis for the last five years and year-to-date.[43]	Mutual funds are required to provide their average annual returns on a calendar year basis for the last ten years, if available.[44]	If the intention is to present one set of returns, this is a direct conflict. Moreover, if an additional chart or graph showing monthly returns were included in the summary section/prospectus where the comparable mutual fund information is required to appear, it would conflict with the summary section/prospectus limit on content.[45]
3.	Commodity pool performance amounts are required to be net of all fees, expenses and allocations to the CPO.[46]	Mutual fund performance disclosures in the bar chart required by Form N-1A do not reflect sales loads. However, other performance disclosures are net of those charges.[47]	These different measurements appear to be in conflict with each other and could confuse investors.

43 17 C.F.R. § 4.25(a)(1)(i)(H).

44 Form N-1A, Item 4(b)(2)(ii)-(iii).

45 The SEC recently revised and rearranged Form N-1A, requiring that mutual funds provide a summary section at the beginning of their statutory prospectus and permitting the use of a summary prospectus for selling. 17 C.F.R. §270.498. The summary prospectus may be subject to further changes under the Dodd-Frank Act.

46 17 C.F.R. § 4.25 (a)(1)(i).

47 Form N-1A, Item 4(b)(2), Instruction 1.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
4.	Disclosure must include the largest monthly drawn-down (loss) in the last five years and year-to-date,[48] and include the worst peak-to-valley draw-down for the same time periods.[49]	A mutual fund is required to disclose the highest and lowest return for a quarter during the last 10 calendar years or for the life of the fund, if the fund does not have 10 calendar years of returns. If the fund's fiscal year is other than a calendar year, it must disclose the year-to-date return as of the end of the most recent quarter.[50]	These different requirements would be an additional disclosure burden and could confuse investors. Moreover, if the information were included in the summary section/prospectus where the comparable mutual fund information is required to appear, it would conflict with the summary section/prospectus limit on content.
5.	Commodity pool performance must include the aggregate gross capital subscriptions to the pool.[51]	There is no comparable mutual fund disclosure requirement.	For an open-end fund that continuously offers and redeems its shares, the aggregate gross capital subscriptions change daily. The measurement is meaningless to fund investors, as subscriptions will frequently be offset, in whole or in part, by redemptions. If the information were included in the summary section/prospectus, it would conflict with the section/summary prospectus limitation on content.

48 17 C.F.R. §§ 4.25 (a)(1)(i)(F), 4.10(k).

49 17 C.F.R. §§ 4.25 (a)(1)(i)(G), 4.10(l).

50 Form N-1A, Item (4)(b)(2)(ii).

51 17 C.F.R. § 4.25 (a)(1)(i)(D).

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
6.	A CPO is required to provide a break-even point, which is the trading profit the pool must realize in the first year of a participant's investment in order to recoup all fees and expenses. This break-even point must be expressed both as a dollar amount and as a percentage of the minimum unit of initial investment and must assume redemption of the initial investment at the end of the first year of investment.[52]	A mutual fund is required to provide an Example of Fund Expenses that shows the dollar amount of expenses an investor will pay after 1, 3, 5 and 10 years of investment assuming a 5% rate of return.[53]	The Example of Fund Expenses would allow a mutual fund investor to calculate his/her break-even point. Inclusion of a break-even point would be an additional disclosure requirement as the comparable mutual fund disclosure is a different measurement. If the information were included in the summary section/prospectus where the comparable mutual fund information is required to appear, it would conflict with the summary section/prospectus limit on content. Although CPO disclosure rules do not mandate an exact order of items, the requirement that the break-even analysis should appear in the "forepart" of the document may conflict with the SEC's summary prospectus requirements.

52 17 C.F.R. §§ 4.24 (d)(5), 4.10(j).

53 Form N-1A, Item 3.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
7.	On its disclosure document cover page, a CPO is required to provide a cautionary statement to the effect that the CFTC has not passed on the merits of participating in the pool or on the adequacy or accuracy of the disclosure document. It must also provide boiler-plate risk disclosure statement(s) addressing the general risk of trading commodity interests and, if applicable, the risks of investing in a pool that trades foreign commodity interests, <u>the risk that losses may not be limited to the amount of an investor's contribution</u> and/or the risk of investing in a pool that engages in off-exchange foreign currency trades.[54]	This would be an additional disclosure requirement to the mutual fund's cover page under applicable SEC rules.	The additional information could not appear on the mutual fund's summary prospectus cover page under applicable SEC rules. In addition, the SEC has stated that boiler-plate all-capital letter risk disclosure would violate the Plain English disclosure rule under the 1933 Act.[55] The underlined text does not apply to mutual fund investments.

54 17 C.F.R. § 4.24 (a)-(b) (emphasis added).

55 *See* Plain English Rule, 17 C.F.R. § 421(d) ("Using all capitalized letters for the legends does not give them proper prominence. Rather, it makes them hard to read." Plain English Disclosure, SEC Release No. 33-7497 at 11 (Jan. 28, 1998).

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
	Disclosure Document Delivery		
8.	A CPO must deliver a disclosure document to a prospective participant no later than the time it delivers a subscription agreement to such participant.[56]	Sales of a mutual fund's securities must be accompanied or preceded by the fund's then-currently effective prospectus. While investors often receive the prospectus before making their investment decision, it is customary for the prospectus to be sent with the confirmation which can be sent as late as 3 days after the trade date (T+3), which satisfies the delivery requirements.[57]	The CFTC should extend the regulatory relief recently provided to Commodity ETFs to registered investment companies or defer to the SEC requirements.[58]
9.	Any information delivered before a disclosure document is delivered must be consistent with, or amended by, the information contained in the disclosure document. If such previously delivered information is amended by the disclosure document in any material respect, the participant must receive the disclosure document at least 48 hours before its subscription is accepted.[59]	Any written information must be accompanied or preceded by the statutory prospectus,[60] unless eligible for an exemption (*e.g.*, Rule 482 omitting prospectus).	The CFTC should extend the regulatory relief recently provided to Commodity ETFs to registered investment companies or defer to the SEC requirements.

56 17 C.F.R. § 4.21(a)(1).

57 15 U.S.C § 77a-5(b)(2).

58 *Cf*. Commodity ETF Rule Release, 76 Fed. Reg. 28641.

59 17 C.F.R § 4.21(a)(1).

60 15 U.S.C § 77a-5(b)(1).

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
10.	A CPO may not accept funds from a prospective participant unless the CPO first receives from such participant an acknowledgment signed and dated by the participant stating that the participant received the disclosure document. If the disclosure document is delivered electronically, the CPO may receive the acknowledgment electronically through the use of a "unique identifier" to confirm the identity of the recipient of the disclosure document.[61]	There is no comparable requirement that the fund must receive a signed acknowledgement from an investor that the investor received the prospectus before the fund may accept a purchase order from the investor. The SEC permits electronic communication of regulatory materials, including the prospectus as well as other required reports, subject to the basic requirements of notice, access and evidence of delivery.[62]	The CFTC should extend the regulatory relief recently provided to Commodity ETFs to registered investment companies or defer to the SEC requirements.
11.	A CPO is required to provide a single disclosure document to prospective participants that includes certain information describing the pool.[63]	A registered investment company registration statement consists of three parts – the Prospectus, the SAI and the Wrapper/Part C; however, a sub-part of the prospectus called the "summary prospectus" is generally the only document that a registered investment company must deliver to prospective investors. The SAI is made available to investors upon request at no charge.[64]	Absent relief, this is a direct conflict.

61 17 C.F.R § 4.21(b).

62 *See* SEC Interpretation: Use of Electronic Media, Release No. 33-7856 (Apr. 28, 2000).

63 17 C.F.R. §§ 4.21, 4.24.

64 *See* Form N-1A, General Instructions, C(2).

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
12.	The NFA requires that the CPO of a commodity pool required to register its securities under the 1933 Act must deliver (or cause to be delivered) a separate SAI to a prospective participant prior to accepting or receiving funds from the prospective participant.[65]	A sub-part of the prospectus called the "summary prospectus" is generally the only document that a registered investment company must deliver to prospective investors. The SAI is made available to investors upon request at no charge.[66]	Absent relief, this is a direct conflict.
13.	The NFA must review a CPO disclosure document prior to use. Once it reviews the document, NFA informs the CPO that the document is accepted or deficient. The CPO is required to correct the deficiencies and re-submit the document to NFA for review before the document will be accepted.[67]	Mutual fund disclosure documents are subject to SEC pre-effective review so there need never be a stop to a continuous offering.[68]	The first time a mutual fund uses a CPO disclosure document, it may need to stop offering shares during the NFA review period. Registered investment companies should be deemed to have met the CFTC requirements if they satisfy the SEC requirements, and pre-clearance by the NFA should not be required.

65 NFA Compliance Rule 2-35.

66 *See* Form N-1A, General Instructions, C(2).

67 Disclosure Documents, A Guide for CPOs and CTAs, NFA at 44, *available at* http://www.nfa.futures.org/NFA-compliance/publication-library/disclosure-document-guide.pdf.

68 17 C.F.R. § 230.485.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
		Reporting to Investors	
14.	A CPO operating a pool with net assets of more than $500,000 must distribute to each pool participant an account statement on a monthly basis.[69]	Open-end mutual funds publicly disclose their net asset value daily, and provide semi-annual reports to investors that provide the same information as the account statement.[70] In addition, a mutual fund must file a quarterly report with the SEC on Form N-Q within 60 days after the close of the first and third quarters containing a schedule of investments and other disclosures.[71]	Monthly statements would be unnecessary and would only serve to increase fund operating expenses. Monthly reporting requirements could also impose major operational hurdles and additional costs for shareholders that hold mutual fund shares in omnibus accounts by introducing additional operational requirements on intermediaries that are not necessarily equipped to meet these requirements. The CFTC should extend the regulatory relief recently provided to Commodity ETFs to registered investment companies or defer to the SEC requirements.
15.	A CPO is required to distribute an annual report to each participant in each pool that it operates. The annual report must include, among other things, audited financial statements.[72]	A registered investment company is required to send to its shareholders at least semiannually a report containing financial statements and other required disclosures. The annual report must contain audited financial statements.[73] The reports to shareholders, along with certain additional information, must also be filed with the SEC on Form N-CSR.[74]	The CFTC should extend the regulatory relief recently provided to Commodity ETFs to registered investment companies or defer to the SEC requirements.

69 17 C.F.R. § 4.22.

70 17 C.F.R. § 270.30b1-1.

71 17 C.F.R. § 270.30b1-5.

72 17 C.F.R § 4.22(c).

73 17 C.F.R. § 270.30e-1.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
	Reporting to Regulators		
16.	Under the proposed CPO-PQR reporting form, a CPO would be required to report basic identifying information about the CPO, including its name, NFA identification number and assets under management.[75]	A registered investment company must report to the SEC information regarding the name of the investment company, its SEC file numbers and address, among other things.[76] It must also report information regarding assets under management.[77]	Registered investment companies should be deemed to have met the CFTC requirements if they satisfy the SEC requirements.

---

74 17 C.F.R. § 270.30b2-1.

75 Proposing Release, 76 Fed. Reg. at 7978-7980.

76 Form N-SAR, Item 1-6.

77 Form N-SAR, Item 75.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
17.	Under the proposed CPO-PQR reporting form, a CPO would be required to report information regarding each of its commodity pools, including the names and NFA identification numbers, position information for positions comprising 5% or more of each pool's net asset value, and the identification of the pool's key relationships with brokers, other advisers, administrators, custodians, auditors and marketers. A CPO would also be required to disclose each pool's quarterly and monthly performance information and information regarding participant subscriptions and redemptions.[78]	Investment companies must list on Form N-SAR: the name of each series of the registrant; the identification of key service providers; information regarding portfolio investments and positions; and information regarding subscription and redemption activity.[79] Performance information is not specifically required by the form, but performance information is available in other reports and registration statements filed with the SEC.[80]	Registered investment companies should be deemed to have met the CFTC requirements if they satisfy the SEC requirements. While there are some differences between the requirements of Form N-SAR and proposed Form CPO-PQR, these differences generally reflect the fact that Form CPO-PQR is intended to obtain information relating to systemic risk. The SEC proposed Form PF, which the CFTC has stated solicits information that is generally identical to that sought by Form CPO-PQR, is specifically designed to address the potential systemic risk raised by activities of advisers to private funds, not registered investment companies. Registered investment companies are subject to CFTC large trader reporting requirements and special calls like any other trader, which enables the CFTC to obtain information from those entities that it can use to assess systemic risk.

78 Proposing Release, 76 Fed. Reg. at 7980.

79 Form N-SAR, Item 7, 8-15, 28, 67-70.

80 *See* Form N-SAR.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
18.	A CPO that has assets under management equal to or exceeding $150 million would be required to file Schedule B, which would require the CPO to report detailed information for each pool. [81]	Investment companies must complete the entire Form N-SAR regardless of assets under management. In addition, the form must be completed on a series-by-series basis. In general, Form N-SAR requires: the name of each series; information regarding each series' investment strategies and positions; liabilities from borrowings and other portfolio management techniques; and information regarding brokerage transactions.[82]	The information required by CPO-PQR is comparable to that required by the corresponding provisions of Form N-SAR for funds and includes information regarding each pool's investment strategy, borrowings by geographic area and the identities of significant creditors, credit counterparty disclosure, and entities through which the pool trades and clears its positions. Registered investment companies should be deemed to have met the CFTC requirements if they satisfy the SEC requirements.

81 Proposing Release, 76 Fed. Reg. at 7980.

82 Form N-SAR, Item 7, 20-26, 62-70, 74.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
19.	A CPO that has assets under management equal to $1 billion or more would be required to file Schedule C. The proposed rules would require certain aggregate information about the commodity pools advised by a large CPO, such as the market value of assets invested, on both a long and short basis, in different types of securities and derivatives, turnover in these categories of financial instruments, and the tenor of fixed income portfolio holdings. A CPO would also be required to report detailed information regarding individual pools with at least $500 million in assets under management, including liquidity, concentration, material investment positions, collateral practices with significant counterparties and clearing relationships.[83]	A registered investment company must report investment and exposure information on a series-by-series basis in all cases. Rules generally do not require an investment company to report investment and exposure information on an aggregate basis or certain more detailed information required by Schedule C of Form CPO-PQR.[84]	Registered investment companies should be deemed to have met the CFTC requirements if they satisfy the SEC requirements. Registered investment companies are subject to CFTC large trader reporting requirements and special calls like any other trader, which enables the CFTC to obtain information from those entities that it can use to assess systemic risk. Accordingly, the more detailed information requested by Form CPO-PQR, Schedule C should not be necessary for registered investment companies.

[83] Proposing Release, 76 Fed. Reg. at 7980-7981.

[84] *See* Form N-SAR.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
	Recordkeeping		
20.	CFTC recordkeeping requirements provide that a CPO must maintain a ledger or other equivalent record for each participant in the pool, which is a record of each investor's name, address and all funds, securities or other property the pool has received or distributed to the investor.[85]	There is a common industry practice of allowing fund investors to hold their shares through omnibus accounts and Networking Level 3 accounts maintained by financial intermediaries, such as broker-dealers and banks. Omnibus accounts are an arrangement that provides for greater ease of management of investor accounts. Mutual fund shares are held in hundreds of thousands of omnibus accounts.[86]	If the relevant financial intermediaries are not considered the "investors" for purposes of this recordkeeping requirement, either the shares would not be able to be held in omnibus or Networking Level 3 accounts or the omnibus and Networking Level 3 accounts would need to be "pierced." Piercing omnibus accounts or discontinuing the practice of using omnibus accounts for mutual funds that invest in commodity interests would make mutual fund distribution impossible with no ascertainable additional shareholder protection.

85 17 C.F.R. § 4.23(a)(4).

86 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).

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
21.	A CPO is required to maintain required pool books and records at its main business office for a five-year period, the first two years of which the records must be "readily accessible."[87]	A registered investment company is required to preserve its books and records for specified periods of time, with more recent books and records typically preserved in an "easily accessible place."[88] A registered investment company is permitted to use a third party to prepare and maintain required records. Reliance on this rule is conditioned upon having a written agreement to the effect that the records are the property of the person required to maintain and preserve them, and that such records will be surrendered promptly on request.[89] A registered investment adviser must indicate whether it maintains its required books and records at a location other than its principal office and place of business,[90] and it must specify each entity that maintains its books and records, including the location of the entity, and a description of the books and records maintained at that location.[91]	A mutual fund adviser should not be subject to CPO requirements regarding the location of books and records if it satisfies the requirements of the 1940 Act rules and Form ADV. The CFTC should defer to the SEC on the content of the recordkeeping rules.

87 17 C.F.R. § 4.23, § 1.31.

88 17 C.F.R. § 270.31a-2.

89 17 C.F.R. § 270.31a-3.

90 Form ADV, Item 1(K).

91 Form ADV, Schedule D, Section 1.K.

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
22.	Under CFTC rules, shareholders in mutual funds subject to CFTC regulation would be given access to pool trading information and other proprietary information.[92]	Mutual funds must currently set and disclose policies regarding how often and to whom they divulge their portfolio holdings.[93] They are also required to disclose their holdings twice yearly in shareholder reports[94] and within 60 days of quarter end for the first and third fiscal quarters on Form N-Q.[95] Many mutual funds disclose their portfolio holdings more frequently, such as monthly. Mutual funds are generally prohibited from selectively disclosing their portfolio holdings information in contravention of their fund policies.[96]	If pool trading information captures a mutual fund's entire portfolio, it would raise portfolio holding disclosure and possible front-running issues and could allow competitors and others to have daily access to fund portfolio information simply by purchasing fund shares and demanding their rights under CFTC rules. This could lead to investors trying to "front run" fund trading in certain securities, taking advantage of anticipated price movements in assets susceptible to these activities by getting in front of fund trades. Having this information could also allow a competitor to reverse engineer a mutual fund's quantitative strategy. Mutual funds disclosing portfolio information to one shareholder under CFTC regulations would arguably be required to disclose publicly this information to all of their shareholders.

92 17 C.F.R. § 4.23. Information that must be made available to commodity pool participants for inspection and copying include, but is not limited to, the pool's itemized daily record of each commodity interest transaction of the pool, a record showing all receipts and disbursements of money, securities and property and copies of confirmations. 17 C.F.R. § 4.23(a)(1), (2) and (7).

93 Form N-1A, Item 16(f).

94 17 C.F.R. § 270.30e-1 and Form N-CSR, Item 6.

95 17 C.F.R. § 270.30b1-5; Form N-Q, General Instruction A.

96 Disclosure Regarding Market Timing and Selective Disclosure of Portfolio Holdings, 69 Fed. Reg. 22300, 22306 (Apr. 23, 2004).

	COMMODITY POOL	MUTUAL FUND	ANALYSIS
	Advertising and Hypothetical Performance		
23.	No comparable requirement.	Advisers are generally prohibited from using testimonials in advertisements, subject to certain exceptions (*e.g.*, partial client lists, certain third party ratings). Mutual fund advertisements are not subject to the Investment Advisers Act of 1940 and rules thereunder prohibition on testimonials. However, an adviser may not use mutual fund related testimonials in a such a manner as to promote other services or offerings of the adviser. [97]	Absent relief, this could be a direct conflict.
24.	Advertisements may present performance of simulated or hypothetical accounts or commodity interest transactions, subject to the use of a prominently disclosed statement that the performance is simulated or hypothetical and results have certain inherent limitations.[98]	Performance information for other funds managed by a mutual fund's investment adviser may be included in the fund's Rule 482 advertisements, but only in limited circumstances, such as the use of a predecessor fund's performance to represent performance prior to the date of the fund's registration statement, in master-feeder fund structures and in the launch of new classes.[99]	Absent relief, this is a direct conflict.

[97] 17 C.F.R. § 275.206(4)-1; Letter from C. Gladwyn Goins, Associate Director, Division of Investment Management, SEC, to R. Clark Hooper, Vice President, Advertising Regulation/Investment Companies, National Association of Securities Dealers (Oct. 19, 1993).

[98] 17 C.F.R. § 4.41(b), NFA Rule 2-29(c).

[99] *E.g.*, *Nicholas-Applegate Mutual Funds*, SEC No-Action Letter (pub. avail. Aug. 6, 1996).