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June 16, 2000

COMMENT

Jean A. Webb, Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N. W.
Washington, D. C. 20581

Re: Proposed Rule 4.27 --Public Reporting by Operators of Certain Large Commodity Pools

Dear Ms. Webb:

The Committee on Futures Regulation of this Association (the "Committee") respectfully submits this comment letter to the Commodity Futures Trading Commission (the "Commission") in response to its request for comments concerning its proposed Rule 4.27 (the "Proposed Rule"), which was published in the Federal Register on April 17, 2000 (65 F. R. 20395). The Association is an organization of approximately 21,000 lawyers. Most of its members practice in the New York City area. However, the Association also has members in 48 states and 51 countries. The Committee consists of attorneys knowledgeable in the field of futures regulation and has a history of publishing reports analyzing critical regulatory issues which affect the futures industry and related activities.

For the reasons discussed below, the Committee believes that the Proposed Rule would not achieve its stated purpose: to facilitate the exercise of market discipline by other market participants in their dealing with commodity pools that, because of their size, could potentially have systemic risk effects. The Committee's concerns fall into the general categories of timeliness of information, uniformity of reported information, an imbalance of information and potential liability related to disclosure of such information.

First, the Proposed Rule would require the submission of information on a quarterly basis to the Commission. Many observers familiar with the operation of these markets have pointed out that financial and other risk information that is dated is of little value to market participants in evaluating the risk of current transactions or an institution's risk profile. Such information rapidly diminishes in value as time elapses from the reporting date.

Moreover, the Proposed Rule is likely to trigger requests for relief based on the burdens of providing timely reports. For example, funds of funds can only report on their activities after they have received reports from each of the funds in which they invest. The filing of annual

reports by these entities is frequently the source of requests for no-action relief due to the difficulty they encounter in complying with filing deadlines. The Committee anticipates that funds of funds subject to the reporting requirements of the Proposed Rule will have even greater difficulty in complying with the proposed requirements.

Second, the Proposed Rule does not succeed as a regulatory approach and would, if adopted, create confusion for market participants and uncertainty for pool operators attempting to comply with its imprecise standards. The information that would be made available to the public through the Commission by different commodity pool operators would not likely be comparable because the Proposed Rule fails to establish clear standards for compliance. Thus, the Committee anticipates that a substantial amount of additional analysis would be required to assess not only the reported data, but also the underlying methodologies that produced it, before the reported information could be of real value to market participants. In fact, the Commission expressly notes that it considered and rejected any requirements that would render reported VAR information comparable across multiple firms. Instead, it has elected to defer to internal policies of reporting firms. While it is commendable that the Commission seeks to ease the burden of new regulation by declining to mandate a particular method or model that should be used to calculate VAR, registrants subject to the Proposed Rule must still attest, under Rule 4.22 (h), to the accuracy and completeness of the reported information. Many pool operators are likely to experience difficulty in reconciling their desire to protect proprietary and confidential information regarding their risk management programs with their obligations under the Proposed Rule to provide an accurate and complete narrative summary of those programs. Given that penalties could be imposed for breaching the reporting standards, the Committee believes that they are insufficiently precise.

The Committee believes that the Proposed Rule attempts to harmonize a mandatory but imprecise reporting system with sufficient flexibility to permit the pool operators that are subject to the Proposed Rule to disclose any additional information they might believe necessary to provide full and complete disclosure. The Commission notes that, if such additional information is deemed to be inadequate, it would then be up to the reporting person's counterparties to determine whether or not the reporting person's risk management efforts were adequate, and the appropriate steps to take in light of that determination. Ultimately the Proposed Rule falls back on a negotiated counterparty-- to-- counterparty disclosure approach. This result underscores the conclusion that assessment of counterparty risk management is, and should be, the responsibility of the counterparties themselves, and raises the fundamental question of the propriety and effectiveness of public disclosure as proposed in the Proposed Rule.

Third, since the Proposed Rule is limited in its application to only Commission pool operator registrants meeting the specified size threshold levels, it would not provide a uniform basis for risk analysis. A great deal of information about the trading practices of certain Commission registrants would be available, but it would not be matched by comparable mandatory disclosures of information by other similar participants in these markets. The Committee believes that these limitations would substantially impair the effectiveness of the Proposed Rule in reducing systemic risk. In addition, the segment of the market composed of registrants would be exposed to greater legal liability in the event that reported information was inaccurate or incomplete.

Fourth, adoption of the Proposed Rule would likely create a new standard for disclosure in the disclosure documents and offering memoranda of all commodity pool operators, going well beyond the requirements of the Commission's Part 4 rules. The Proposed Rule would have implications for registrants who would not be reporting persons thereunder because the Proposed Rule could be viewed as a Commission determination that the listed information is material to counterparties and to the market generally. Although the Proposed Rule is applicable only to pool operators managing substantial amounts of capital, smaller pool operators may be forced to produce similar disclosures in an attempt to provide all material information, as generally required by Part 4. The Committee is concerned that adoption of the Proposed Rule would make the process of determining the adequacy of their disclosure considerably more difficult for registrants and for attorneys practicing in this area. As noted above, the reporting requirements in the Proposed Rule lack specificity. Thus, registrants will struggle with which portions of the information made publicly available through the Commission are material to investors. The required disclosures may serve only as a threshold level of disclosure, particularly when the proposed reporting standards themselves seem capable of considerable individual interpretation.

Overall, the Committee believes that greater emphasis should be placed on encouraging approaches for market wide counterparty-- to--counterparty disclosures. These disclosures could be tailored to the needs of the individual market participants in regard to specific transactions, and would be more timely, coinciding with the life span of a transaction. The Committee believes that such an approach corresponds more closely to the recommendations made by the various groups that have examined systemic risk resulting from the activities of highly leveraged institutions and other large institutional traders.[1] In any event, the Committee does not support adoption of the Proposed Rule while Congress is debating the same subject matter and may develop a more comprehensive approach to the problem.

The Committee appreciates the opportunity to comment on the Proposed Rule and stands ready to assist the Commission and its staff if further clarification is required on any of the points raised in this letter.

Sincerely yours,

Emily M. Zeigler

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1 The Committee submits that the appropriate role of the Commission in this area may be to encourage registrants to adopt risk management policies appropriate to the size and complexity of their organizations, rather than to convert non-standardized information into reports to regulators which will be publicly disclosed and consequently carry potential liability for reporting persons.

Association of the Bar the City of New York

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** Chair of Subcommittee who drafted this letter of comments.

* Member of Subcommittee who drafted this letter of comments.

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Joyce M. Hansen - abstain
Lenel Hickson, Jr. - abstain
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