



## U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Clearing and  
Intermediary Oversight

February 2, 2011

**To: All Commodity Pool Operators**  
**Attention: Chief Financial Officer**  
**Subject: Annual Reporting for Commodity Pools**

The Division of Clearing and Intermediary Oversight (“DCIO” or “Division”) of the Commodity Futures Trading Commission (“CFTC” or “Commission”) is issuing this letter to assist commodity pool operators (“CPOs”) with the preparation and filing of commodity pool annual financial reports required under the Commodity Exchange Act (“Act”) and Commission regulations.<sup>1</sup> This letter highlights current regulatory changes affecting CPOs with respect to financial filings and provides reminders of regulatory requirements in response to common deficiencies observed in prior years’ annual reports. CPOs, including those that operate in non-U.S. jurisdictions, are encouraged to provide this letter to their public accountants and others assisting in the preparation of commodity pool annual financial statements.

The Division has issued similar guidance letters in prior years, which are available at the Commission’s website.<sup>2</sup> Those letters should be consulted as they contain information relevant for many commodity pools, including the following topics:

- Reports of Series Funds Structured with a Limitation on Liability Among the Different Series (2009 letter)
- American Institute of Certified Public Accountants’ (“AICPA”) Statement of Position (“SOP”) 03-04, *Reporting Financial Highlights and Schedule of Investments by Nonregistered Investment Partnerships: An Amendment to the Audit and Accounting Guide, Audits of Investment Companies* ( Accounting Standards Codification (ASC) 946-210-50-4) (2005 letter); an illustration of the investments schedule can be found in Attachment B of this letter);
- A CPO’s reporting obligation when claiming relief under Regulation 4.13 for a pool

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<sup>1</sup> The Act is codified at 7 U.S.C. §1 et seq. The Commission’s regulations are found in Title 17 of the Code of Federal Regulations. The Commission’s internet website, [www.cftc.gov](http://www.cftc.gov), provides links to both the Act and Commission regulations.

<sup>2</sup> Prior letters from 1998 forward are available at the Commission’s website at <http://www.cftc.gov/industryoversight/intermediaries/guidancecporeports.html>.

- previously operated without exemptive relief (2006 letter);
- A CPO's obligation to provide notice of replacement of accountant (2006 letter);
- Notice regarding election of a fiscal year other than the calendar year (2006 letter); and
- Process for requesting confidential treatment of commodity pool annual reports (2006 letter).

In addition, CFTC interpretations and other staff letters that provide written guidance concerning the Act and the Commission's regulations are available on the Commission's website. In particular, an illustrative example regarding Regulation 4.22(e)(2) is available in CFTC Interpretative Letter 94-3, *Special Allocations of Investment Partnership Equity*.

## **I. Recent Regulatory Activity**

The CFTC issued final forex rules, which became effective on October 18, 2010. Any firm acting as a counterparty to certain off-exchange forex transactions involving retail persons is required to register as a Retail Foreign Exchange Dealer. In addition, any individual acting as a forex solicitor, account manager and/or pool operator is required to register with the Commission as an Introducing Broker, Commodity Trading Advisor (CTA) or CPO, as appropriate, and to become a member of the National Futures Association (NFA).

NFA also adopted compliance rules applicable to CPOs as follows:

- Rule 2-45 prohibits a CPO from permitting a commodity pool to use any means to make a direct or indirect loan or advance of pool assets to the CPO or any person or entity affiliated with the CPO.
- Rule 2-46 requires each CPO that is a member of NFA to file, on a quarterly basis, with NFA, the following information for each pool the CPO operates that is subject to a reporting requirement under Regulation 4.22 (which includes exempt pools under Commission Regulation 4.7):
  - the identity of the pool's administrator, carry broker(s), trading manager(s) and custodian(s);
  - a statement of changes in net asset value for the quarterly reporting period;
  - monthly performance for the three months comprising the quarterly reporting period; and
  - a schedule of investments identifying any investment that exceeds 10% of the pool's net asset value at the end of the quarterly reporting period.

Such information must be filed with NFA within 45 days of the end of the quarterly reporting period, and must be filed using NFA Easyfile electronic filing system.

NFA also updated the Self Examination Checklist for CPOs and CTAs as of September 2010. NFA Compliance Rule 2-9 (Supervision) requires members to review their operations on a yearly basis using the NFA self-examination checklist

## II. Filing Deadlines and Procedures for Commodity Pool Annual Reports

Commission regulations establish the dates by which commodity pool annual reports must be provided to pool participants and received by the NFA.

Specifically, Commission regulations provide that:

- **Commodity pool annual reports must be distributed to pool participants and filed with NFA within 90 calendar days of the pool's fiscal year end.** The filing date for annual reports with a year end of December 31, 2010 is March 31, 2011. Copies of the annual reports must be filed with the NFA. A CPO should not file copies of the annual reports with the Commission.
- **CPOs must submit annual reports to NFA electronically in accordance with NFA's EasyFile electronic filing system and procedures.**
- **An annual report may be distributed in hardcopy or electronically to pool participants. The CPO, however, must obtain a participant's prior consent to distribute an annual report in electronic format.**
- **Applications for an extension of time to file an annual report must be submitted to NFA prior to the annual report due date and must include the information required by Regulation 4.22(f)(1). Any request for an extension of time that exceeds 90 days from the original due date must be submitted to the Commission, and a copy filed with NFA. The Commission generally does not grant extensions that would exceed 90 days from the original due date.**
- **CPOs of commodity pools that invest in other collective investment vehicles may obtain an "automatic" 90-day extension of the distribution and filing due date by submitting the information specified by Regulation 4.22(f)(2) to NFA prior to the original due date.** In subsequent years, the CPO will be presumed to operate the pool as a fund of funds and continue to qualify for the automatic extension. However, the CPO is obligated to inform the NFA if those circumstances change and to begin filing within the standard 90-day time frame. In addition, this extension of time has been made available to Regulation 4.7 exempt pools, even if the report is not audited by a certified public accountant.
- **Draft financial statements.** Some CPOs have filed incomplete, or "draft," unaudited financial statements for pools exempt under Regulation 4.7 to meet the due dates for such filings. CPOs are reminded that although Regulation 4.7 provides exemption from certain requirements, including the requirement that financial statements be subject to an audit by a certified public accountant, annual reports filed with NFA and distributed to pool

participants must include all required information and be in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”) or, in some instances, International Financial Reporting Standards (“IFRS”) to be considered timely filed. Draft unaudited financial statements do not satisfy the filing requirements.

### **III. Master/Feeder and Fund of Funds**

**Master/Feeder Structures.** FASB ASC 946-205-45-6 permits nonpublic feeder pools either to follow the disclosure and reporting provisions of FASB ASC 946-210, or to present a complete set of master financial statements with each feeder financial statement.

**Fund of Funds.** Year end pool financial statements must disclose specific income and fee information for investee pools as specified in Regulation 4.22(c)(5). CPOs must disclose amounts of income and fees associated with investments in investment partnerships that exceed five percent of the commodity pool’s net assets. Illustrative disclosures are in Attachment B to this letter.

If a commodity pool’s annual financial statements are found deficient with respect to compliance with GAAP, the CPO may be required to revise the commodity pool’s financial statements, distribute the revised statements to participants, and re-file the statements with NFA.

### **IV. Requests for Limited Relief from U.S. GAAP Compliance for Certain Offshore Commodity Pools**

Regulation 4.22(d)(2), applicable to year end annual reports, permits CPOs that operate commodity pools organized under the laws of a non-U.S. jurisdiction to prepare financial statements for such pools using IFRS, provided that:

- The use of IFRS does not conflict with any representations made in the pool’s offering memorandum or other operative document;
- The IFRS financial statements contain a condensed schedule of investments as required by U.S. GAAP (FASB ASC 946-210-50), or, if required, a full schedule of investments;
- The IFRS financial statements report any special allocations of partnership equity in accordance with Commission Regulation 4.22(e)(2); and
- If IFRS would require that the pool consolidate its financial statements with another entity, such as a feeder fund consolidating with its master fund, all applicable disclosures required by U.S. GAAP for the feeder fund must be presented with the reporting pool’s consolidated financial statements.

To claim the relief to use IFRS accounting standards, the CPO must file a notice with NFA within 90 days after the end of the pool’s fiscal year. Furthermore, Regulations 4.22(a)(5) and 4.7(b)(2) permit a CPO to present a pool’s periodic account statements and other disclosure documents on the same basis as that of its annual report.

In addition, Division staff has, on a case-by-case basis, provided limited relief to CPOs that operate offshore pools by allowing such commodity pools to prepare and to present their financial statements in accordance with another comprehensive basis of accounting other than IFRS, such as United Kingdom or Irish accounting standards, instead of U.S. GAAP. In each case, the Division’s

relief to use accounting standards other than U.S. GAAP was conditioned upon the offshore pool following the additional elements now required by Regulation 4.22(d)(2)(i).

CPOs seeking to prepare and present their offshore pools' financial statements on another comprehensive basis of accounting other than IFRS may request relief from the U.S. GAAP requirement by submitting their requests, enumerating compliance with each of the elements specified in Regulation 4.22(d)(2), to the undersigned at the address shown on this letterhead. If you have any further questions, contact Ronald Carletta, Branch Chief, or Al Goll, Auditor, at the phone numbers or addresses listed in Attachment A.

## **V. Reports of Liquidating Pools**

Commission Regulation 4.22(c)(7) provides for the filing and distribution of a final annual report within 90 days of a pool's permanent cessation of trading. Alternatively, the CPO of a liquidating pool may provide the following information within 90 days of the permanent cessation of trading in lieu of an otherwise required final annual report:

- Statements of Operations and Changes in Net Assets for the relevant period as contained in the regulation; and,
- An explanation of the winding down of the pool's operations with written disclosure that all interests in, and assets of, the pool have been redeemed, distributed, or transferred on behalf of participants; or
- In the event that all interests in, and assets of, the pool have not been distributed, redeemed, or transferred to participants by the time the final report is issued, the CPO must disclose the value of assets remaining to be distributed and an approximate timeframe for when the CPO expects distribution to occur. If the CPO is unable to complete distribution within the estimated timeframe, the CPO must update the above detailed information to both NFA and the pool's participants in writing.

If the CPO is not able to liquidate the pool's assets within time to prepare, file, and distribute the final annual report as prescribed by the regulation, Commission Regulation 4.22(c)(7) requires the CPO to provide written notice to each participant and NFA, disclosing the following:

- The value of assets remaining to be liquidated, the timeframe within which liquidation is expected to occur, any impediments to liquidation and any fees or expenses that will be charged to the pool prior to final distribution;
- Which financial reports the CPO will continue to provide to participants from the time of the cessation of trading until the final annual report is distributed, and the frequency of such reports, pursuant to the pool's constitutive documents; and
- The timing of the final annual report.

Additionally, a CPO who is availing itself of the alternative filing in lieu of a final annual report may file unaudited information provided that the CPO obtains waivers from all participants and certifies the same to NFA when the final report is filed.

This relief also is applicable for pools that have claimed an exemption under Regulations 4.7

or 4.12.

## **VI. Accounting Resources**

### **A. FASB Accounting Standards Codification**

On July 1, 2009 the Financial Accounting Standards Board (FASB) launched the *FASB Accounting Standards Codification* (the Codification) as the single source of authoritative nongovernmental U.S. GAAP. Although the FASB does not provide guidance in how specific requirements of GAAP are referred to in footnotes of financial statements, it notes that prior to the issuance of the Codification it was not unusual for footnotes to refer to specific standard numbers (for example, “as required by Statement 133”). Because these references are no longer the source of GAAP, such references will change. The FASB encourages the use of plain English to describe broad Topic references in the future. For example, to refer to the requirements of the Derivatives and Hedging Topic, they suggest a reference similar to “as required by the Derivatives and Hedging Topic of the FASB Accounting Standards Codification” and not use the specific numeric reference.

### **B. AICPA Commodities Audit Practice Aid**

The AICPA Audit Practice Aid, *Audits of Futures Commission Merchants, Introducing Brokers, and Commodity Pools Second Edition* (product number 006639), is a useful tool for auditors and accountants of commodity entities. It can be purchased at the AICPA website: <http://www.CPA2biz.com>. CPOs and public accountants should also ensure that they monitor the Commission for recent developments which may not be reflected in the Audit Practice Aid.

### **C. AICPA Audit Risk Alert**

The AICPA 2010 Audit Risk Alert (“ARA”) *Financial Institutions Industry Developments, Including Depository and Lending Institutions and Brokers and Dealers in Securities* contains sections on the commodities industry. The ARA can be purchased at the AICPA website: <http://www.CPA2biz.com>.

### **D. FASB ASC Topic 820 (Formerly FAS 157, Fair Value Measurements)**

Resources that may be helpful in understanding and applying FASB ASC Topic 820 are:

- *Measurements of Fair Value in Illiquid (or Less Liquid) Markets*, issued by the AICPA Center for Audit Quality available at <http://www.thecaq.org/resources/pdfs/MeasurementsIlliquidMarkets.pdf>
- ASC 275-10-50, *Risks and Uncertainties* (AICPA Statement of Position 94-6, *Disclosure of Certain Significant Risks and Uncertainties*, when auditing financial statements that contain complex fair value measurements);
- ASC 820-10, *Fair Value Measurements and Disclosure: Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)* - (guidance that generally the net asset value reported by investee investment companies will continue to be an acceptable fair value indicator, with certain exceptions.)

## E. AICPA Technical Guidance

Beginning at paragraph 8.23, the AICPA Audit and Accounting Guide, *Investment Companies* (May 1, 2010 edition) discusses organization and offering costs. The AICPA issued technical guidance regarding accounting treatment of offering costs incurred by investment partnerships.<sup>3</sup> This guidance:

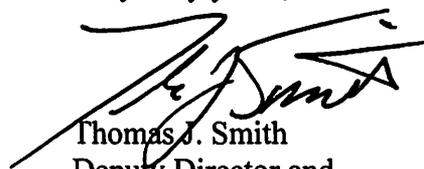
- Provides that investment partnerships that continually offer interests should defer offering costs incurred prior to commencement of operations and then amortize such costs, generally on straight-line basis, over the time period that it continually offers interests, up to a maximum of 12 months; and
- Defines the phrase “continually offer interests.”

Registrants are reminded that organization costs are not affected by this guidance and must be charged to expense as incurred as required by FASB Codification Section 720-15-25-1 (AICPA SOP No. 98-5, *Reporting on the Costs of Start-up Activities*.) However, if appropriately disclosed to investors and potential investors, net asset value used to compute investment entrance and exit values, may be adjusted to amortize such costs differently, but generally not to exceed a period of 60 months.

## IX. DCIO and NFA Contact Information

If a CPO, a public accountant, or other member of the public has any questions on the foregoing, please feel free to contact the DCIO staff or NFA staff listed in Attachment A to this letter.

Very truly yours,



Thomas J. Smith  
Deputy Director and  
Chief Accountant

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<sup>3</sup> See paragraph 8.33 of the AICPA Audit and Accounting Guide, *Investment Companies* (May 1, 2010 edition).

**ATTACHMENT A**

**CFTC DIVISION OF CLEARING AND INTERMEDIARY OVERSIGHT CONTACT INFORMATION**

<b>Regional Office Locations</b>	<b>Contacts</b>	<b>Location of CPO's Principal Office</b>
<b>Eastern Region</b>		
140 Broadway, 19th Floor New York, NY 10005-1146	Ronald A. Carletta Phone: (646)-746-9726 E-Mail: <a href="mailto:rcarletta@cftc.gov">rcarletta@cftc.gov</a>  Al Goll Phone: (646)-746-9723 E-Mail: <a href="mailto:agoll@cftc.gov">agoll@cftc.gov</a>  Fax: (646)-746-9937	All states east of the Mississippi River, <i>except</i> Illinois, Indiana, Michigan, Ohio, and Wisconsin. Any location outside of the United States
<b>Central Region</b>		
525 West Monroe Street Suite 1100 Chicago, IL 60661	Lisa M. Marlow Phone: 312-596-0566 Fax: 312-596-0711 E-Mail: <a href="mailto:lmарlow@cftc.gov">lmarlow@cftc.gov</a>	Illinois, Indiana, Michigan, Ohio, and Wisconsin
<b>Southwestern Region</b>		
Two Emanuel Cleaver II Boulevard, Suite 300 Kansas City, MO 64112	Kurt Harms Phone: 816-960-7711 Fax: 816-960-7750 E-Mail: <a href="mailto:kharms@cftc.gov">kharms@cftc.gov</a>	All states west of the Mississippi River

<b>National Futures Association Contact Information</b>	
National Futures Association 300 South Riverside Plaza, Suite 1800 Chicago, IL 60606	Tracy Hunt, Senior Manager, Compliance Phone: 312-781-1284 Fax: 312-559-3453 E-Mail: <a href="mailto:thunt@nfa.futures.org">thunt@nfa.futures.org</a>

## ATTACHMENT B

### ILLUSTRATION – Fund of Funds Additional Disclosures

#### Note X. Investments

As of December 31, 200X, ABC Fund invested in other funds, none of which were related parties.

The following table summarizes ABC Fund's investments in other funds as of December 31, 200X. Funds in which ABC Fund invested more than 5% of its net assets are individually identified, while smaller investments in three other funds are aggregated. The management agreements of the investee funds provide for compensation to the managers in the form of fees ranging from 1% to 3% annually of net assets and performance incentive fees ranging from 5% to 25% of net profits earned.

Investment	% of ABC's Net Assets	Fair Value	Income (Loss)	Fees Mgmt	Incentive	Investment Objective	Redemptions Permitted*
Airjo Fund Ltd.	5.1	\$ 2,550,000	\$200,000	\$ 25,000	\$ 30,000	Emerging market	Quarterly
Carron Int'l Fund	5.2	2,600,000	210,000	26,000	42,000	Sector investment	Monthly
Vital Fund NV	5.6	2,800,000	(30,000)	28,000	0	International equity	Semi-Annual
Other funds:	<u>4.2</u>	<u>2,100,000</u>	<u>100,000</u>	<u>24,000</u>	<u>25,000</u>	Other	Monthly-Annually
<b>Total</b>	<b><u>20.1%</u></b>	<b><u>\$10,050,000</u></b>	<b><u>\$480,000</u></b>	<b><u>\$103,000</u></b>	<b><u>\$97,000</u></b>		

An alternative illustrative table, for *unusual cases*, where the fee information cannot be obtained is shown below:

Investment	% of ABC's Net Assets	Fair Value	Income (Loss)	Fees Mgmt	Incentive	Investment Objective	Redemptions Permitted♦
Airjo Fund Ltd.	5.1	\$ 2,550,000	\$200,000	\$ 25,000	\$ 30,000	Emerging market	Quarterly
Carron Int'l Fund	5.2	2,600,000	210,000	26,000	42,000	Sector investment	Monthly
Other funds:	<u>4.2</u>	<u>2,100,000</u>	<u>100,000</u>	<u>24,000</u>	<u>25,000</u>	Other	Monthly-Annually
Subtotal	14.4	7,200,000	510,000	<u>\$75,000</u>	<u>\$97,000</u>		
Vital Fund NV	<u>5.6</u>	<u>2,800,000</u>	<u>(30,000)</u>	*	*	International equity	Semi-Annual
<b>Total</b>	<b><u>20.1%</u></b>	<b><u>\$10,050,000</u></b>	<b><u>\$480,000</u></b>				

\* = The fund operator is not able to obtain the specific fee amounts for this fund and does not know what those amounts are. However, management fees are computed based on 1% per year of net asset balances at the beginning of each month; incentive fees are computed based on 20% per year of net income.

♦ Note any funds in which redemptions have been suspended.