



## U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Swap Dealer and  
Intermediary Oversight

Gary Barnett  
Director

CFTC Letter No. 13-51  
No-Action  
September 5, 2013  
Division of Swap Dealer and Intermediary Oversight

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**Re: Request for Confirmation and No-Action Relief Regarding Application of Certain Reporting Obligations under Part 4 of the Commission's Regulations Concerning Certain Subsidiaries of Registered Investment Companies**

Dear Ms. McMillan and Messrs. Cameron and Nevins:

This letter is in response to your correspondence, dated April 10, 2013, to the Division of Swap Dealer and Intermediary Oversight ("Division") of the U.S. Commodity Futures Trading Commission ("Commission")<sup>1</sup> on behalf of the members of the Investment Company Institute ("ICI") and the Asset Management Group of the Securities Industry and Financial Markets

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<sup>1</sup> See letter from Investment Company Institute and Securities Industry and Financial Markets Association Asset Management Group to Gary Barnett, Director of the Division of Swap Dealer and Intermediary Oversight, dated April 10, 2013 ("Correspondence").

Association (“SIFMA AMG”) for whom you requested confirmation and no-action relief regarding the application of certain reporting obligations under Part 4 of the Commission’s regulations (“Regulations”) to commodity pool operators (“CPOs”) of registered investment companies (“registered funds”)<sup>2</sup> that trade in commodity interests through wholly-owned subsidiaries<sup>3</sup> (known as controlled foreign corporations or “CFCs”) that are consolidated with such registered funds for financial reporting purposes.<sup>4</sup>

### **Request for Confirmation and No-Action Relief**

#### Regulation 4.27(c)

In the Correspondence, you requested confirmation that CPOs of registered funds that consolidate their CFCs for financial reporting purposes may report for a registered fund and its CFCs on a consolidated basis under Commission Regulation 4.27(c).<sup>5</sup>

In support, you noted that, in most cases, registered funds that trade in commodity interests through CFCs consolidate the financial statements of the CFC into the registered fund’s financial statements for financial reporting purposes, which results in the financial statements’ disclosing the CFC’s investments as if the registered fund held them directly, and that this practice is permitted by U.S. generally accepted accounting principles (“U.S. GAAP”) and has been explicitly permitted by the U.S. Securities and Exchange Commission (“SEC”) staff for SEC reporting purposes.<sup>6</sup> You also noted that, recently, the SEC has required registered funds to consolidate wholly-owned subsidiaries when that subsidiary is an extension of the parent investment company’s operations.<sup>7</sup>

In addition, you noted that registered fund complexes that consolidate their funds’ CFCs have established financial reporting systems that combine the assets, liabilities, income, and expenses of the registered fund and the CFC for reporting purposes.<sup>8</sup> You noted that, in order to gather the CFC’s data, CPOs of such registered funds would need to either manually isolate the CFC’s data, which may increase the likelihood of error, or implement, on a temporary basis,

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<sup>2</sup> The Correspondence does not explicitly indicate what constitutes “registered funds.” For purposes of this Division letter, “registered funds” means investment companies registered as such under the Investment Company Act of 1940 (“Investment Company Act”).

<sup>3</sup> The Correspondence does not explicitly indicate what constitutes “wholly-owned subsidiaries.” For purposes of this Division letter, the term “wholly-owned subsidiary” incorporates the definition provided in section 2 of the Investment Company Act. 15 U.S.C. 80a-2.

<sup>4</sup> See Correspondence, *supra* n.1.

<sup>5</sup> Correspondence, at 4. To illustrate the timing under your request, you noted that if the Compliance Date (defined below) is August 1, 2013, a quarterly Form CPO-PQR filer would file its first Form CPO-PQR with respect to the quarter ending September 30, 2013.

<sup>6</sup> Correspondence, at 3.

<sup>7</sup> *Id.*

<sup>8</sup> Correspondence, at 4.

financial reporting systems that would isolate the CFC's data until the date upon which the CPOs of registered funds are required to comply with Part 4 of the Regulations following the adoption of a final rule harmonizing the Commission's compliance regime with that of the SEC ("Compliance Date"),<sup>9</sup> at which point the CPOs would have to revert to the previous consolidated financial reporting system.<sup>10</sup>

In addition, you requested in a footnote that the relief be extended to CPOs that are in the process of converting from separate financial reporting to consolidated financial reporting for the registered funds and the CFCs they operate, and that such relief should apply to a CPO that operates at least one registered fund that consolidates its CFC for financial reporting purposes; provided that such CPO's remaining registered funds' next audited financial statements consolidate their CFCs for financial reporting purposes.<sup>11</sup>

Regulation 4.22(c)

In the Correspondence, you also requested that the Division provide no-action relief to permit CPOs of registered funds that consolidate their CFCs for financial reporting purposes to file with the National Futures Association ("NFA") an annual report for the CFC, to the extent required by Regulation 4.22(c), that contains audited consolidated financial statements of the registered fund, in lieu of a separate annual report for the CFC.<sup>12</sup> In addition, you requested that the Division permit registered fund CPOs to file the CFC's first such annual report with respect to the fiscal year of the registered fund that ends after the Compliance Date.<sup>13</sup>

In support, you noted that preparing the annual report in this manner would be consistent with how these registered funds provide financial information in their audited financial statements, as included in annual reports provided to shareholders and filed with the SEC.<sup>14</sup> You also noted that the annual reports to shareholders must contain audited financial statements prepared in accordance with U.S. GAAP.<sup>15</sup>

You also stated, as discussed above, that most registered funds that own CFCs prepare their audited financial statements on a consolidated basis, and such registered funds would not

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<sup>9</sup> To illustrate the timing under your request, you noted that if the Compliance Date is August 1, 2013, a quarterly Form CPO-PQR filer would file its first Form CPO-PQR with respect to the quarter ending September 30, 2013. Note, that the harmonization final rule was published in the Federal Register starting at 78 FR 52308 on August 22, 2013.

<sup>10</sup> *Id.*

<sup>11</sup> Correspondence, at 3

<sup>12</sup> Correspondence, at 4.

<sup>13</sup> *Id.* To illustrate the timing under your request, you noted that if the Compliance Date is August 1, 2013, and a registered fund's fiscal year end is September 30, then the first such annual report would be for the fiscal year ending September 30, 2013.

<sup>14</sup> *Id.*

<sup>15</sup> Correspondence, at 5.

prepare separate audited financial statements for the CFCs.<sup>16</sup> You further noted that preparing separate audited financial statements for the CFC would require registered funds to incur unnecessary and redundant costs associated with preparing financial statements for the CFC, as well as costs associated with an audit of the CFC's financial statements.<sup>17</sup> You noted that it would be costly and inefficient, and would provide no additional benefit to the Commission to require the CPO to such CFC to file an annual report with the NFA that includes separate audited financial statements of the CFC, as the registered fund's audited consolidated financial statements would include all required financial information for the registered fund, including the holdings, gains and losses, and other financial statement amounts attributable to the CFC.<sup>18</sup>

### **Regulatory Background**

The Commodity Exchange Act ("Act")<sup>19</sup> defines "commodity pool" as follows:

The term "commodity pool" means any investment trust, syndicate, or similar form of enterprise operated for the purpose of trading in commodity interests, including any—

- (i) commodity for future delivery, security futures product, or swap;
- (ii) agreement, contract, or transaction described in section 2(c)(2)(C)(i) of this title or section 2(c)(2)(D)(i) of this title;
- (iii) commodity option authorized under section 6c of this title; or
- (iv) leverage transaction authorized under section 23 of this title.<sup>20</sup>

A definition of a "pool" is also provided in Regulation 4.10(d), which is substantively identical to the statutory definition of a commodity pool.<sup>21</sup>

A definition of CPO is provided in section 1a(11) of the Act, which states, in part:

The term "commodity pool operator" means any person—

- (i) engaged in a business that is of the nature of a commodity pool, investment trust, syndicate, or similar form of enterprise, and who, in connection therewith, solicits, accepts, or receives from others, funds, securities, or property, either

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<sup>16</sup> *Id.*

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> 7 U.S.C. § 1 *et seq.*

<sup>20</sup> 7 U.S.C. § 1a(10).

<sup>21</sup> *See* 17 CFR § 4.10(d).

directly or through capital contributions, the sale of stock or other forms of securities, or otherwise, for the purpose of trading in commodity interests, including any—

(I) commodity for future delivery, security futures product, or swap;

(II) agreement, contract, or transaction described in section 2(c)(2)(C)(i) of this title or section 2(c)(2)(D)(i) of this title;

(III) commodity option authorized under section 6c of this title; or

(IV) leverage transaction authorized under section 23 of this title; or

(ii) who is registered with the Commission as a commodity pool operator.<sup>22</sup>

A CPO is also defined in Regulation 1.3(cc), which is substantively identical to the statutory definition of a CPO.<sup>23</sup>

Thus, as recently stated by the Commission, a CFC that is used for the purpose of trading in commodity interests and is a wholly-owned subsidiary of a registered fund is considered to be a separate “commodity pool” or a “pool” apart from the parent registered fund.<sup>24</sup> If a person is a CPO of a registered fund that uses a CFC meeting the definition of “commodity pool” or “pool,” that CPO is required to register with the Commission as the CPO of such CFC and is subject to compliance with Part 4 of the Regulations with respect to such CFC, unless such CFC can satisfy the criteria for an exemption or exclusion for its CPO from registration. Moreover, the analysis of whether a CPO of a CFC is subject to registration and compliance with Part 4 of the Regulations is independent of whether the activities of the parent registered fund trigger registration of such parent registered fund’s CPO. Therefore, it is possible for a CPO of a CFC to be required to be registered and subject to Part 4 of the Regulations, even if the CPO of the parent registered fund is excluded from the definition of a CPO pursuant to Regulation 4.5.

Under the Regulations, a registered CPO has various reporting and filing requirements. Regulation 4.27(c) requires, among other things, a registered CPO to file with NFA a report with respect to the directed assets of each pool under the advisement of the registered CPO consistent with Appendix A of Part 4 of the Regulations (*i.e.* Form CPO-PQR).<sup>25</sup>

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<sup>22</sup> 7 U.S.C. § 1a(11).

<sup>23</sup> See 17 CFR § 1.3(cc).

<sup>24</sup> See 77 FR 11260. Such CFCs are typically not eligible for exclusion under the terms of Regulation 4.5, because CFCs, by virtue of being foreign entities, are generally not eligible for registration under the Investment Company Act. See 15 U.S.C. § 80a-7(d). You do not dispute that the CFC is a separate legal entity, which the Commission considers to be a commodity pool, and that, absent relief, the CPO of the CFC would be required to report to the Commission independent of any exemption or exclusion applicable to the CPO of the parent registered fund.

<sup>25</sup> 17 CFR § 4.27(c)(1).

Also, Regulation 4.22(c) requires that, “[e]xcept as provided in paragraph... (c)(8) of this section, each commodity pool operator registered or required to be registered under the Act must distribute an Annual Report to each participant in each pool that it operates, and must electronically submit a copy of the Report and key financial balances from the Report to the National Futures Association pursuant to the electronic filing procedures of the National Futures Association, within 90 calendar days after the end of the pool’s fiscal year...”<sup>26</sup> Regulation 4.22(c)(8) states that, “[f]or the purpose of the Annual Report distribution requirement..., the term ‘participant’ does not include a commodity pool operated by a pool operator that is the same as, or that controls, is controlled by, or is under common control with, the pool operator of a pool in which the commodity pool has invested; *Provided*, That the Annual Report of such investing pool contain financial statements that include such information as the Commission may specify concerning the operations of the pool in which the commodity pool has invested.”<sup>27</sup>

Consequently, with respect to the requirements of Regulation 4.27(c), a registered CPO of a wholly-owned CFC is required to file a Form CPO-PQR with NFA with respect to the CFC for each reporting period as defined in Regulation 4.27 and the instructions to Form CPO-PQR (“Reporting Period”), independent of any obligations of the CPO of the parent registered fund. With respect to the requirements of Regulation 4.22(c), although the CPO of a CFC does not have to distribute an annual financial statement to the CFC’s parent registered fund where such CPO is also the CPO of the parent registered fund,<sup>28</sup> the CPO of the CFC must still file an annual financial statement with NFA pursuant to Regulation 4.22(c).

### **No-Action Relief Granted**

#### Regulation 4.27(c)

Based on the foregoing and the representations made in your correspondence requesting confirmation and no-action relief, the Division believes that granting no-action relief is warranted with respect to certain requirements of Regulation 4.27(c). Accordingly, the Division will not recommend that the Commission take an enforcement action against a CPO of a registered fund that uses a wholly-owned CFC for the purpose of trading in commodity interests for failure to provide a report with respect to such CFC to NFA pursuant to Regulation 4.27(c) until the deadline for the next applicable Reporting Period following the Compliance Date, where the CPO of the CFC is also the CPO of the parent registered fund;<sup>29</sup> provided that:

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<sup>26</sup> 17 CFR § 4.22(c).

<sup>27</sup> 17 CFR § 4.22(c)(8).

<sup>28</sup> *Id.*

<sup>29</sup> This relief does not apply in a scenario where an entity operating both a CFC and a registered fund is excluded from the definition of CPO with respect to the operation of that registered fund.

(i) the CPO provides a consolidated report for the registered fund that includes the data for its CFCs to NFA pursuant to Regulation 4.27(c) for the next applicable Reporting Period following the Compliance Date; and

(ii) the CPO either:

(I) currently consolidates the registered fund's wholly-owned CFC's financial statements with those of the parent registered fund's financial statements for financial reporting purposes; or

(II) is in the process of converting from separate financial reporting to consolidated financial reporting for the registered fund and CFCs it operates; provided that:

(1) such CPO operates at least one registered fund that currently consolidates its CFC for financial reporting purposes; and

(2) such CPO's other registered funds consolidate their CFCs for financial reporting purposes for the next applicable Reporting Period following the Compliance Date.

For all subsequent Reporting Periods after the Compliance Date, the CPO must either file a consolidated report consistent with the relief provided herein or make a separate filing on behalf of the CFC pursuant to Regulation 4.27(c).

This no-action relief is not self-executing. Rather, a CPO that is eligible for this relief must file a claim to perfect the use of this relief consistent with the procedures set forth below. A claim submitted by a CPO will be effective upon filing, so long as the claim is materially complete, and must be filed by before the end of the next applicable Reporting Period following the Compliance Date.

Regulation 4.22(c)

Based on the foregoing and the representations made in your correspondence requesting confirmation and no-action relief, the Division also believes that granting no-action relief is warranted with respect to certain requirements of Regulation 4.22(c). Accordingly, the Division will not recommend that the Commission take an enforcement action against a CPO of a registered fund that uses a wholly-owned CFC for the purpose of trading in commodity interests for failure to distribute an annual report with respect to such CFC to NFA pursuant to Regulation 4.22(c) where the CPO of the CFC is also the CPO of the parent registered fund,<sup>30</sup> provided that:

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<sup>30</sup> *Id.*

(i) the CPO prepares an annual report of the registered fund that contains consolidated audited financial statements for the registered fund that includes, and also separately indicates, the holdings, gains and losses, and other financial statement amounts attributable to the CFC; and

(ii) the CPO submits such annual report of the registered fund to NFA, in lieu of a separate annual report of the CFC, for the next fiscal year of the registered fund that ends after the Compliance Date, and, going forward, for all subsequent fiscal years (as applicable).

This no-action relief is not self-executing. Rather, a CPO that is eligible for this relief must file a claim to perfect the use of this relief consistent with the procedures set forth below. A claim submitted by a CPO will be effective upon filing, so long as the claim is materially complete, by the end of the next fiscal year of the registered fund that ends after the Compliance Date.

#### Procedures to Claim No-Action Relief

To obtain the no-action relief provided in this letter, the notice of claim must:

(i) state the name, main business address, and main business telephone number of the CPO claiming the relief;

(ii) state the capacity (*i.e.* CPO) and the name of the CFC(s) for which the claim is being filed and the name of the parent registered fund matched with each CFC;

(iii) be signed by the CPO;<sup>31</sup> and

(iv) be filed with the Division via email using the email address *dsionoaction@cftc.gov* with the subject line of such email “CFC Letter 13-51).”

The no-action relief provided herein contains a collection of information, as that term is defined in the Paperwork Reduction Act.<sup>32</sup> Therefore, a control number for the collection must be obtained from the Office of Management and Budget. In accordance with 44 U.S.C. § 3507(d) and 5 C.F.R. §§ 1320.8 and 1320.10, the Division will, by separate action, prepare an information collection request for review and approval by OMB, and will publish in the *Federal Register* a notice and request for public comments on the collection burdens associated with the no-action relief.

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<sup>31</sup> This may be accomplished by attaching a PDF with a signature of the CPO.

<sup>32</sup> 44 U.S.C. § § 3501 *et. seq.*



This letter, and the positions taken herein, represent the view of this Division only, and do not necessarily represent the position or view of the Commission or of any other office or division of the Commission. The relief issued by this letter does not excuse persons relying on it from compliance with any other applicable requirements contained in the Act or in the Regulations issued thereunder. Further, this letter, and the relief contained herein, is based upon the representations made to the Division. Any different, changed or omitted material facts or circumstances might render this no-action relief void.

Should you have any questions, please do not hesitate to contact Amanda Olear, Associate Director, at 202-418-5283, or Chang Jung, Attorney-Advisor, at 202-418-5202.

Very truly yours,

Gary Barnett  
Director  
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cc: Regina Thoele, Compliance  
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