

CFTC Letter No. 99-13

March 12, 1999

Interpretation

Division of Trading & Markets

Dear:

This is in response to your letters dated January 29, February 3, and February 8 1999, as supplemented by telephone conversations with staff of the Division of Trading and Markets ("Division") of the Commodity Futures Trading Commission ("Commission"), wherein you requested guidance on how to represent the performance of the "B" Program in one capsule.

In your letter dated January 29, 1999, you indicated that you entered into a special arrangement with "C" under which "A" would run the B Program ("Trading Program") which started trading in 1993. Performance figures for this program were, until November 1998, calculated using the Fully-Funded Subset ("FFS") method approved in Commission Advisory 93-13¹. However, in November 1998, the fully funded subset, which was comprised of one account, had dropped to less than five percent of the nominal assets in the Trading Program², and thus no longer met the requirement of 93-13 that actual funds in the FFS must be at least 10% of the aggregate of the Nominal Account Sizes of the accounts comprising the composite performance table.³

In order to assess adequately the performance presentation, staff requested several items of information regarding the accounts comprising the performance table. You provided this information in your February 3, 1999 letter. In reviewing this information it appears that one account which was not included in the FFS in your analysis was funded at a level in excess of 90 percent of the nominal account size.

Following a subsequent conversation regarding this account, you explained in your letter dated February 8, 1999, that "The client wants the trading balance of each month to begin with \$\$\$,000 [dollars]. Therefore, at the end of every month the balance is adjusted by adding back any loss and subtracting any gains that occurred during the month." The table that you presented indicates that this has been the case since November 1998 and staff note that since November 1998 the account meets the GTPR⁴ test contained in Commission Advisory 93-13. We believe that an account funded at 90 percent or greater is not materially different from an account which is funded at 100 percent and thus may be treated as part of the FFS. Under this interpretation and the facts as represented to us in your letters, this \$\$\$,000 account can be included as part of the Fully-Funded Subset, on a

going forward basis, so long as it is funded at 90 percent or greater.

It should be noted that the interpretation contained in this letter solely applies to compliance with the Fully-Funded Subset method approved in Commission Advisory 93-13 it does not excuse A from compliance with any other applicable requirements contained in the Act or in the Commission's regulations issued thereunder.

This letter, and the interpretation contained herein, is based upon the representations provided to us. Any different, changed or omitted material facts or circumstances might render this interpretation void. You must notify us immediately in the event that A's operation of the Trading Program changes in any material way from that represented to us. Further, you should be aware that the Commission recently published, for public comment, a concept release regarding the presentation of past performance for CTAs and CPOs. The Commission may, as a result of comments received, propose and ultimately adopt a regulatory change. If a regulatory change is adopted, it may supercede the interpretation herein.

We hope that this letter and the enclosed information are responsive to your inquiries. If you have any further questions, please do not hesitate to contact the undersigned, at (202) 418-5463.

Very truly yours,

Kevin P. Walek

Assistant Director

¹ Commission Regulation 4.35(a)(6)(i) provides that performance information presented in a disclosure document must be calculated based on actual funds "or by a method otherwise approved by the Commission." In Commission Advisory 93-13, the Commission approved the "Fully-Funded Subset" method of calculating performance. 58 F.R. 8226 (February 12, 1993). The Fully-Funded Subset is comprised of all Fully-Funded accounts, other than certain accounts that may be excluded according to criteria set forth in Advisory 93-13. Advisory 93-13 defines Fully Funded Account as "an account which at its inception contains an amount of Actual Funds equal to its Nominal Account Size."

² It should be noted that, this event did not necessarily mean that the FFS method could no longer be used. In order to allow CTAs who adopted the FFS method to maintain consistency in their performance presentation, Advisory 93-13 provides that the FFS method may continue to be used even if the accounts to be included in the composite table do not meet both tests in every period presented, provided that ". . . failures to meet the first test, if any, were for a limited number of periods. . . ."

Based upon the information you have provided it appears that the Trading Program has failed to meet

the first test of the FFS for a period of only three months to date, out of a Trading Program life of over 72 months. Thus, the FFS method could still be validly used at this time.

³ The Fully-Funded Subset must meet the following two tests: 1) The aggregate of the Subset's Actual Funds must be at least 10% of the aggregate of the Nominal Account Sizes of the accounts which make up the composite performance table; and 2) The Gross Trading Profit (Loss) Ratio ("GTPR") of the aggregate of the accounts contained in the Subset based on Actual Funds must be materially the same as the GTPR for the aggregate of accounts contained in the composite performance table based upon the Nominal Account Size.

⁴ A GTPR is computed by dividing gross trading profits by the account size for any single account or by the aggregate of the account sizes for any subset of accounts (notional or actual funds).