6351-01-P

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 4

RIN 3038-AD75

Harmonization of Compliance Obligations for Registered Investment Companies Required to Register as Commodity Pool Operators

AGENCY: Commodity Futures Trading Commission.

ACTION: Final rule.

SUMMARY: The Commodity Futures Trading Commission ("Commission" or "CFTC") is adopting final regulations with respect to certain compliance obligations for commodity pool operators ("CPOs") of investment companies registered under the Investment Company Act of 1940 ("registered investment companies" or "RICs") that are required to register due to the recent amendments to § 4.5. The Commission is also adopting amendments to certain provisions of part 4 of the Commission's regulations that are applicable to all CPOs and Commodity Trading Advisors ("CTAs"). This rulemaking is related to the final rule adopted under RIN 3038-AD30.

DATES: Effective Dates: Sections 4.12, except for § 4.12(c)(3)(i), and 4.21will become effective upon publication in the Federal Register. Sections 4.7(b)(4), 4.12(c)(3)(i), 4.23, 4.26, and 4.36 will become effective [INSERT DATE THAT IS 30 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]. Compliance Dates: Registered CPOs seeking exemption under these rules shall be required to comply with the conditions adopted in § 4.12(c)(3)(i) when the associated registered investment company updates its prospectus as described in Section II.F., below, and files the prospectus with the SEC. Moreover, the publication of these rules trigger the conditional compliance date that was established in the Commodity Pool Operators and

Commodity Trading Advisors: Compliance Obligations rulemaking. 77 FR 11252, 11252 (Feb. 24, 2012). With the publication of these rules, registered CPOs of RICs must comply with § 4.27 on or before [INSERT DATE THAT IS 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER].

FOR FURTHER INFORMATION CONTACT: Amanda Lesher Olear, Special Counsel, Telephone: (202) 418–5283, Email: aolear@cftc.gov, or Michael Ehrstein, Attorney-Advisor, Telephone: 202–418–5957, Email: mehrstein@cftc.gov, Division of Swap Dealer and Intermediary Oversight, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.

SUPPLEMENTARY INFORMATION:

I. Background

A. Recent Amendments to § 4.5 as Applicable to RICs

The Commodity Exchange Act ("CEA")[1] provides the Commission with the authority to require registration of CPOs and CTAs,[2] to exclude any entity from registration as a CPO or CTA,[3] and to require "[e]very commodity trading advisor and commodity pool operator registered under [the CEA] to maintain books and records and file such reports in such form and manner as may be prescribed by the Commission."[4] The Commission also has the authority to "make and promulgate such rules and regulations as, in the judgment of the Commission, are reasonably necessary to effectuate the provisions or to accomplish any of the purposes of [the CEA]."[5]

[1] 7 U.S.C. 1, et seq.

[2] 7 U.S.C. 6m.

[3] 7 U.S.C. 1a(11) and 1a(12).

[4] 7 U.S.C. 6n(3)(A). Under part 4 of the Commission's regulations, unless otherwise provided by the Commission, entities registered as CPOs have reporting obligations with respect to their operated pools. See 17 CFR 4.22.

[5] 7 U.S.C. 12a(5).

In February 2012, the Commission adopted modifications to the exclusions from the definition of CPO that are delineated in § 4.5 ("2012 Final Rule").[6] Specifically, the Commission amended § 4.5 to modify the exclusion from the definition of "commodity pool operator" for those entities that are investment companies registered as such with the Securities and Exchange Commission ("SEC") pursuant to the Investment Company Act of 1940 ("'40 Act").[7] This modification amended the terms of the exclusion available to CPOs of RICs to include only those CPOs of RICs that commit no more than a de minimis portion of their assets to the trading of commodity interests that do not fall within the definition of bona fide hedging and who do not market themselves as a commodity pool or other commodity investment.[8] Pursuant to this amendment, any such CPO of a RIC that exceeds this level, or markets itself as such, will no longer be excluded from the definition of CPO. Accordingly, except for those CPOs of RICs who commit no more than a de minimis portion of their assets to the trading of commodity interests that do not fall within the definition of bona fide hedging and who do not market themselves as a commodity pool or other commodity investment, an operator of a RIC that meets the definition of

[6] 17 CFR 4.5. See 77 FR 11252 (Feb. 24, 2012); correction 77 FR 17328 (March 26, 2012). Prior to this Amendment, all RICs, and the principals and employees thereof, were excluded from the definition of "commodity pool operator," by virtue of the RICs registration under the Investment Company Act of 1940. The 2012 amendment to § 4.5 maintained this exclusion for those RICs that engage in a de minimis amount of non-bona fide hedging commodity interest transactions. *See id.* Specifically, the amendment to § 4.5 retained this exclusion for RICs whose non-bona fide hedging commodity interest transactions require aggregate initial margin and premiums that do not exceed five percent of the liquidation value of the qualifying pool's portfolio, or whose non-bona fide hedging commodity interest transactions' aggregate net notional value does not exceed 100 percent of the liquidation value of the pool's portfolio.

[7] 15 U.S.C. 80a-1, et seq. "SEC" as used herein means the Securities and Exchange Commission or its staff, as the context requires.

[8] 17 CFR 1.3(yy).

"commodity pool operator" under § 4.10(d) of the Commission's regulations and § 1a(11) of the CEA must register as such with the Commission.[9]

B. Harmonization Proposal

In response to the Commission's February 2011 proposal to amend the § 4.5 exclusion with respect to CPOs of RICs,[10] as well a staff roundtable held on July 16, 2011 ("Roundtable"),[11] and meetings with interested parties, the Commission received numerous comments expressing concern about the relationship between part 4 of the Commission's regulations applicable to CPOs of RICs and the SEC rules and guidance under the '40 Act, the Securities Act of 1933 ("Securities Act"),[12] and the Securities Exchange Act of 1934[13] regarding disclosure, reporting and recordkeeping by RICs (collectively, "SEC RIC Rules").[14] Commenters asserted variously that the two sets of requirements touched upon similar areas, imposed undue burdens on CPOs of RICs, or conflicted such that CPOs of RICs could not comply with both. On this basis, some commenters argued that CPOs of RICs should not be required to comply with the full set of requirements under part 4. Several previously received comments, which were noted in the Proposal, suggested that the Commission make relief available, with respect to document and

[9] Pursuant to the terms of § 4.14(a)(4), CPOs are not required to register as CTAs if the CPOs' commodity trading advice is directed solely to, and for the sole use of, the pool or pools for which they are registered as CPOs. 17 CFR 4.14(a)(4).

[10] 76 FR 7976 (Feb. 11, 2011).

[11] See Notice of CFTC Staff Roundtable Discussion on Proposed Changes to Registration and Compliance Regime for Commodity Pool Operators and Commodity Trading Advisors, available at http://www.cftc.gov/PressRoom/Events/opaevent_cftcstaff070611.

[12] 15 U.S.C. 77a, et seq.

[13] 15 U.S.C.78a, et seq.

[14] The Commission understands that that SEC provides guidance in a variety of ways to market participants, including interpretive guidance, no action letters, frequently asked questions, and staff feedback in response to document submissions. The Commission also notes that RICs may be subject to separate requirements imposed by the Financial Industry Regulatory Authority.

report distribution, similar to that which it has recently adopted with respect to exchange-traded funds ("ETFs").[15]

Some commenters suggested ways in which the two agencies' requirements could be harmonized to eliminate the inconsistencies between the two compliance regimes with respect to those entities subject to dual registration as a result of the recent amendments to § 4.5. Specific areas of focus identified by the commenters include: the timing of delivery of Disclosure Documents to prospective participants; the signed acknowledgement requirement for receipt of Disclosure Documents; the cycle for updating Disclosure Documents; the timing of financial reporting to participants; the requirement that a CPO maintain its books and records on site; the required disclosure of fees; the required disclosure of past performance; the inclusion of mandatory certification language; and the SEC-permitted use of a summary prospectus for open-ended registered investment companies.

Commenters advocated different approaches to harmonization. Some suggested that where requirements are inconsistent, the Commission should defer to SEC requirements.[16] A few commenters made recommendations about the treatment of specific disclosures, such as presenting both SEC and CFTC-required fee information and presenting certain performance information required by the CFTC in the Statement of Additional Information ("SAI").[17] One

[15] See 76 FR 28641 (May 18, 2011). The Commission adopted rules to relieve individual CPOs of publicly offered, ETFs of certain requirements in part 4 of the Commission's regulations. Specifically, the Commission adopted amendments to § 4.12 providing exemptive relief from §§ 4.21, 4.22, and 4.23 for operators of ETFs. Such relief includes providing disclosure and periodic accounts statements to participants through the Internet and permitting the use of third-party service providers for recordkeeping obligations. Previously, Commission staff had issued relief to ETFs only on a case-by-case basis. ETFs that are also RICs may rely on the relief provided herein.

[16] See, e.g., Comment letter from the Investment Company Institute (April 12, 2011) (ICI Letter).

[17] See, e.g., Comment letter from the National Futures Association (April 12, 2011) (NFA Letter).

commenter noted that CPOs of RICs should be required to comply with all disclosure and other requirements applicable to registered CPOs.[18]

Sections 4n(3) and (4) of the CEA[19] authorize the Commission to adopt regulations requiring that CPOs maintain books and records and file reports with the Commission in the manner and form it prescribes. Such compliance obligations for CPOs are set forth in part 4 of the Commission's regulations and include a set of requirements that address disclosure, recordkeeping, and reporting obligations. The regulations are designed to promote market integrity and transparency, facilitate necessary Commission oversight, and provide important information to prospective participants. The requirement to comply with the full panoply of obligations set forth in part 4 of the Commission's regulations does not, however, follow inexorably from registration under the 2012 Final Rule requiring CPOs of RICs to register. The Commission determined, after consideration of the comments received, that further consideration was warranted concerning whether and to what extent CPOs of RICs ought to be subject to various part 4 requirements, and in the 2012 Final Rule suspended the obligations of CPOs of RICs with respect to most of the requirements of part 4 until further rulemaking.[20] The Commission's 2012 Final Rule imposed upon CPOs of RICs that do not otherwise qualify for an exemption only the requirement to register.[21] The Commission also finalized, but suspended

[18] See Comment letter from Steben & Company, Inc. (April 25, 2012) (Steben letter).

[19] 7 USC 6n(3) and (4).

[20] See 2012 Final Rule, supra note 6, 77 FR at 11252, 11255. The Commission exercised its authority under §§ 4 and 8a of the CEA, 7 U.S.C. §§ 6 and 12a, and § 4.12(a) of its regulations thereunder, which provides that the Commission may exempt any person or class of persons from any or all of part 4 requirements if the Commission finds that the exemption is not contrary to the public interest or the purposes of the provision from which the exemption is sought. 17 CFR 4.12(a).

[21] The Commission's regulations also provide for exemptions from registration for CPOs of privately offered pools that engage in a de minimis amount of commodities trading (17 CFR 4.13(a)(3)), CPOs whose total capital contributions for all operated pools do not exceed $400,000 and whose total participants do not exceed 15 (17 CFR

compliance with, pending the completion of further rulemaking, a requirement that CPOs of RICs file certain information on form CPO-PQR, pursuant to § 4.27. At the same time, consistent with the Commission's authority under § 4.12(a), the Commission commenced a new rulemaking to evaluate the necessity and reasonableness of additional requirements and, where possible, to devise ways in which the Commission's requirements for CPOs of RICs could be harmonized with applicable requirements of the SEC.[22]

The Commission therefore published for comment in the *Federal Register* proposed amendments to part 4 of the Commission's regulations designed to address potentially conflicting or duplicative compliance obligations administered by the Commission and the SEC regarding disclosure, reporting and recordkeeping by CPOs of RICs (the "Proposal").[23] The Commission proposed changes to part 4 designed to better harmonize the Commission's compliance obligations for CPOs with those of the SEC for entities that are subject to both regimes in such a way that would allow the Commission to fulfill its regulatory mandate while, at the same time, avoiding unnecessary regulatory burdens on dually-regulated CPOs of RICs with respect to disclosure, annual and periodic reporting to participants, and Commission recordkeeping requirements.[24]

The Proposal to harmonize the Commission's regulatory regime with that of the SEC as it applies to CPOs of RICs is grounded in the concept of substituted compliance. That is, insofar as

---

4.13(a)(2)),and CPOs that do not advertise and who do not receive any incentive or management fees (17 CFR 4.13(a)(1)).

[22] See 2012 Final Rule, supra note 6, 77 FR at 11260 ("Entities required to register due to the amendments to § 4.5 shall be subject to the Commission's recordkeeping, reporting, and disclosure requirements set forth in part 4 of the Commission's regulations within 60 days following the effectiveness of a final rule implementing the Commission's proposed harmonization effort pursuant to the concurrent proposed rulemaking.").

[23] 77 FR 11345 (Feb. 24, 2012).

[24] The Commission issued its proposal under the authority of §§ 4m, 4n, and 8a(5) of the CEA. 7 U.S.C. 6m, 6n, and 12a(5).

the disclosure, reporting, and recordkeeping regime administered by the SEC under SEC RIC Rules were designed to achieve substantially similar goals to those of the Commission's part 4 regulations, then CPOs of RICs that maintain compliance under the SEC regime would be deemed to fulfill their obligations under part 4 of the Commission's regulations. At the same time, in the event that a CPO of a RIC fails to comply with the SEC administered regime, the CPO will be in violation of its obligations under part 4 of the Commission's regulations and thus subject to enforcement action by the Commission. As such, the Proposal contemplated an alternative means for a CPO of a RIC to comply with its obligations under part 4 of the Commission's regulations by modifying certain of the requirements. These proposed modifications included: the timing of the delivery of Disclosure Documents to prospective participants; the signed acknowledgement requirement for receipt of Disclosure Documents; the cycle for updating Disclosure Documents; the timing of financial reporting to participants; the requirement that a CPO maintain its books and records on site; the required disclosure of fees; the required disclosure of past performance; the inclusion of mandatory certification language; and the SEC-permitted use of a summary prospectus for open-ended registered investment companies.

As stated in the 2012 Final Rule, the justification for the amendments to § 4.5 was to enable the Commission to adequately discharge its duties to oversee the commodity interest markets. Therefore, the Commission determined to require the CPOs of RICs that exceeded a de minimis threshold of commodity interest trading, excluding bona fide hedging, or which marketed themselves as a commodity pool or other commodity investment, to register with the Commission. The Commission recognizes, however, that its understanding of RICs and their use of commodity interests continues to evolve as it gains experience regarding RICs, and their regulation and operation. Thus, at this time, the Commission believes that the prudent approach is to provide a

substituted compliance regime based largely upon adherence to the regime administered by the SEC as it continues to expand its knowledge of RICs and their use of commodity interests.

Therefore, in this final rule, the Commission has determined to broaden the approach set forth in the Proposal. The Commission is adopting a substituted compliance regime for CPOs of RICs largely premised upon such entities' adherence to the compliance obligations under SEC RIC Rules, whereby the Commission will accept compliance by such entities with the disclosure, reporting, and recordkeeping regime administered by the SEC as substituted compliance with part 4 of the Commission's regulations. The Commission has concluded that this is appropriate because, as the Commission continues to gain experience regulating CPOs of RICs, it believes that general reliance upon the SEC's compliance regime, with minor additional disclosure, should provide market participants and the general public with meaningful disclosure, including for example, with regard to risks and fees, provide the Commission with information necessary to its oversight of CPOs, and ensure that CPOs of RICs maintain appropriate records regarding their operations. As noted, in the event that the operator of the RIC fails to comply with the SEC administered regime, the operator of the RIC will be in violation of its obligations under part 4 of the Commission's regulations and subject to enforcement action by the Commission.

C. Comments on the Proposal

The Commission received 66 comment letters regarding the Proposal from a wide range of entities, including trade and public interest organizations, family offices, a registered futures association, individuals, currently registered CPOs, RICs, and law firms.[25] Generally,

[25] See http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1161. The Commission notes that it received six duplicate comment letters; thus, the Commission received 60 unique comments. Of the comments received, many focused on the advisability of an exemption for single-family pools ("Family Offices"). The Commission's Division of Swap Dealer and Intermediary Oversight issued a letter on November 29, 2012, providing that it would not recommend enforcement action against the operator of a "family office" as that term has been

commenters favored the Commission's effort to harmonize for CPOs of RICs the Commission's part 4 regulations with SEC-administered rules.[26] Commenters particularly focused on disclosure issues, including the "break-even" disclosure, required statements of risk, cycle for updating Disclosure Documents, financial reporting including periodic account statements, and books and records requirements.[27] In addition, some commenters advocated modifications to part 4 requirements that they believed were necessary to maintain suitable regulatory requirements for all CPOs.[28] Commenters also addressed potential costs and benefits of harmonizing CFTC and SEC rules applicable to RICs.[29]

Beginning in 2011, Commission staff has engaged in ongoing substantive discussions with SEC staff regarding possible areas of harmonization between the compliance regimes of the two commissions as applicable to RICs and their CPOs, including disclosure to prospective investors and financial reporting. Such consultations occurred throughout the process culminating in this final rule and have informed the Commission's understanding of RICs and the SEC's regulation thereof.

D. Significant Changes from the Proposal

In the Proposal, the Commission stated its intent to facilitate compliance by CPOs of RICs with the Commission's disclosure, reporting, and recordkeeping requirements. As a result, the

---

defined in the SEC's regulations. See, CFTC Staff Letter, 12-37, available at http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/12-37.pdf. The Commission further notes that it has considered additional comments, including those received at and following the Roundtable, see supra note 11, regarding the harmonization of CFTC and SEC regulation applicable to operators of RICs.

[26] See, e.g., NFA Letter; Comment letter from Campbell & Company, Inc. (April 24, 2012) (Campbell Letter).

[27] See, e.g., Comment letter from New York City Bar Association (May 30, 2012) (NYCBA Letter); Comment letter from Securities Industry and Financial Markets Association Asset Management Group (April 24, 2012) (SIFMA AMG Letter); Comment letter from Fidelity Management and Research Company (April 24, 2012) (Fidelity Letter).

[28] NFA Letter; Campbell Letter; Comment letter from the Managed Funds Association (April 24, 2012) (MFA Letter).

[29] ICI Letter.

Commission proposed various alternative mechanisms to enable dually registered operators of RICs to comply with the Commission's part 4 requirements.[30] After consideration of the comments received and further deliberation, the Commission is adopting rules that effectively implement a substituted compliance approach for dually registered CPOs of RICs, whereby such CPOs, largely through compliance with obligations imposed by the SEC, will be deemed compliant with the Commission's regulatory regime. This is consistent with the Commission's conclusion that substituted compliance is appropriate because it believes that the regime administered by the SEC under SEC RIC Rules, with minor additional disclosure, should provide market participants with meaningful disclosure as required under part 4, enable the Commission to discharge its regulatory oversight function with respect to the derivatives markets, and ensure that CPOs of RICs maintain appropriate records regarding their operations.

The Commission is also modifying certain part 4 requirements that are applicable to all CPOs to recognize certain technological improvements and operational efficiencies that have developed since part 4 was last revised. The key changes from the Proposal that the Commission is making in the rules it is adopting today are as follows: (1) operators of RICs will be deemed to be in compliance with §§ 4.21, 4.22(a) and (b), 4.24, 4.25, and 4.26 if they satisfy all applicable SEC RIC Rules as well as certain other conditions; (2) all CPOs will be permitted to use third-

[30] In five of the eleven areas of potential redundancy, inconsistency, or conflict addressed in the Proposal, the Commission proposed allowing substituted compliance by adherence to SEC regulations. Under the proposal, CPOs of RICs would be exempt from disclosure requirements under §§ 4.21, 4.22, and 4.23. See Proposal, supra note 23, 77 FR at 11346. CPOs of RICs would also be exempt from more frequent disclosures required by § 4.26, and the oath or affirmation required by § 4.22(h). Id. For four other areas of potential conflict, the Commission proposed allowing the requested information to be disclosed instead in SEC filings. Specifically, the proposal provides alternative methods of satisfying §§ 4.24(a), 4.25(d)(5), 4.25(d), and 4.24(i), which ordinarily require a cautionary statement, break-even points, and disclosure of fees and expenses, and requires that they be located in the forepart of the document. With respect to the last two areas – the frequency of the provision to customers of account statements and the content of disclosures regarding past performance of commodity pools less than three years old – the Commission proposed maintaining its own standards, but also solicited comments on how it could harmonize those last two areas.

party service providers to maintain their books and records; and (3) the signed acknowledgement requirement is being rescinded for all CPOs. The reasoning underlying each of the enumerated changes is discussed infra.

Accordingly, a CPO of a RIC may comply with part 4 requirements applicable to all CPOs or elect to comply through substituted compliance, subject to the conditions specified in amended § 4.12(c). In the latter case, the CPO of a RIC will be subject to the following requirements:

- The CPO of a RIC will be required to file notice of its use of the substituted compliance regime outlined in § 4.12 with NFA;
- The CPO of a RIC with less than three years operating history will be required to disclose the performance of all accounts and pools that are managed by the CPO and that have investment objectives, policies, and strategies substantially similar to those of the offered pool;
- The CPO of a RIC will be required to file the financial statements with the National Futures Association ("NFA") that it prepares pursuant to its obligations with respect to the SEC; and
- If the CPO of a RIC uses or intends to use third-party service providers for recordkeeping purposes, it will be required to file notice with NFA.

In light of the requirements applicable to RICs under SEC RIC Rules, the Commission has endeavored to harmonize its regulations to achieve a reasonable balance that serves the Commission's regulatory goals under part 4 of its regulations.[31] In addition, the Commission has

[31] 7 U.S.C. § 19(a). It is the Commission's intent that if any portion of this rulemaking is held invalid, such invalidity shall not affect other provisions or applications of the Commission's regulations which can be given effect without the invalid provision or application, including without limitation other amendments to part 4 in this or the February 2012 Final Rule, and to this end each provision of this final rule is severable.

determined to modify certain part 4 requirements applicable to all CPOs, including CPOs of RICs. In particular, this final rule will permit a CPO of a RIC to use a third-party service provider for recordkeeping purposes. A CPO electing to do so will be required to file a notice with the NFA. Additionally, all CPOs and CTAs will be permitted to use a Disclosure Document for up to 12 months.

II. Discussion

A. Scope and Timing

The Commission received many comments that pertained to the scope and timing of the Proposal. For example, some commenters expressed displeasure with the Commission's recent amendments to § 4.5 and § 4.27.[32] One commenter said the Proposal is unripe and should be withdrawn pending the judicial challenge of the § 4.5 amendments.[33] Another commenter suggested the Commission withdraw its Proposal and re-propose harmonized compliance obligations for RICs.[34] Other commenters requested broad exemptions from all part 4

[32] ICI Letter, comment letter from U.S. Chamber of Commerce (April 24, 2012) (Chamber Letter); comment letter from Dechert LLP and Clients (April 24, 2012) (Dechert Letter).

[33] Chamber Letter. This commenter also stated that harmonization is unripe because, among other things, regulations needed to complete the implementation of Title VII of Dodd-Frank are still not finalized. To the extent this commenter was referring to the finalization of the Commission and SEC's further definition of "swap," that definition has now been finalized. This commenter and others have stated that the Commission could not, prior to the adoption of that final definition, properly consider the costs and benefits of the amendments to § 4.5 and proposed, therefore, the exclusion of swaps from the thresholds above which the operator of a RIC must register as a CPO. As the Commission explained in the 2012 Final Rule amending § 4.5, however, the costs and benefits were sufficiently clear at that time. The Commission explained that swap trading above a de minimis threshold implicates its regulatory interests, whereas trading below the threshold may not. To permit unlimited swap trading without registration would undermine the regulatory interest described throughout the 2012 Final Rule release. Consistent with the Commission's expectation at the time of the 2012 Final Rule amending § 4.5, the 2012 Final Rule further defining "swap" did not further define the term "swap" in a manner that would have materially affected the Commission's decision to amend § 4.5. On December 12, 2012, the U.S. District Court for the District of Columbia affirmed the 2012 Final Rule's amendments to § 4.5 and adoption of § 4.27 as applicable to CPOs of RICs. The District Court's opinion is available at https://ecf.dcd.uscourts.gov/cgi-bin/show_public_doc?2012cv0612-42.

[34] ICI Letter.

regulations.[35] One commenter, for example, suggested that the Commission more narrowly tailor the part 4 requirements to those funds that use derivatives as a primary investment strategy and exempt from registration funds that only use derivatives for diversification and/or hedging purposes.[36] Another commenter contended that the rules must take into account the differences between open-ended funds (which continuously offer shares and redeem through the company) and closed-ended funds (which generally have an initial offering and then trade shares on an exchange).[37] Some commenters suggested that the Commission work with the SEC in order to more effectively harmonize the requirements of the two regimes, and in particular, ensure that compliance with the one regulatory regime would not cause a violation of the other.[38]

The Commission is aware that some commenters do not believe that CPOs of RICs should be required to register with the Commission. The CPO registration requirement in § 4.5, however, is outside the scope of this rulemaking. The Commission previously determined that, given its new responsibilities under the Dodd-Frank Act, and the changes in the markets within the Commission's responsibilities in recent years, the operator of a RIC that engages in more than a de minimis amount of non-bona fide hedging commodity interest transactions or markets itself as a commodity pool or other commodity investment must register as a CPO and file form CPO-PQR.[39]

---

[35] ICI Letter; comment letter from American Bar Association Federal Regulation of Securities Committee, Business Law Section (April 24, 21012) (ABA Letter); comment letter from AXA Equitable Funds Management Group, LLC (April 24, 2012) (AXA Letter); comment letter from The Association of Institutional Investors (April 24, 2012) (AII Letter); comment letter from Investment Adviser Association (April 24, 2012) (IAA Letter); NYCBA Letter; Fidelity Letter.

[36] Comment letter from Katten Muchin Rosenman LLP (April 24, 2012) (Katten Letter).

[37] SIMFA AMG Letter.

[38] Fidelity Letter; NYCBA Letter; ICI Letter.

[39] See, 2012 Final Rule, supra note 6, 77 FR 11252 (Feb. 24, 2012); corrected by 77 FR 17328 (Mar. 26, 2012); affirmed by U.S. District Court for the District of Columbia (Dec. 12, 2012), available at https://ecf.dcd.uscourts.gov/cgi-bin/show_public_doc?2012cv0612-42.

Regarding obligations of registered CPOs, the Commission notes the concerns of commenters that dual registrants may be unable, or encounter substantial difficulty trying, to comply with both the CFTC and SEC regulatory regimes were they both required in their current state. The Commission believes that harmonization will reduce or eliminate such difficulty.

This rule release is focused on the harmonization of the Commission's compliance obligations under part 4 of its regulations with the requirements under the SEC RIC Rules. To that end, the Commission has considered the various provisions of part 4 and sought to address conflict, inconsistency, and duplication with SEC-administered disclosure, reporting and recordkeeping by RICs. Commission staff has also engaged in ongoing discussions with their counterparts at the SEC. The Commission believes that, with the final rules being adopted today, it has harmonized its compliance obligations with those of the SEC to the fullest extent practicable consistent with achieving the regulatory objectives of its part 4 regulations and its experience to date with CPOs of RICs.

B. Disclosure Requirements

a. Filing and Updating Disclosure Documents

Currently, § 4.26(a)(2) states that "[n]o commodity pool operator may use a Disclosure Document or profile document dated more than nine months prior to the date of its use." An identical provision applying to CTAs can be found in § 4.36(b). These provisions are designed to ensure that required disclosure materials remain current, complete, and accurate over time. Similarly, § 10(a)(3) of the Securities Act effectively requires an annual update of an open-end

RIC's registration statement, and provides 4 months after the end of the fiscal year in order to do so.[40]

Additionally, § 4.26(c) states that if a CPO becomes aware of any incompleteness or material inaccuracy in its Disclosure Document, the CPO must correct the defect and distribute the correction to participants within 21 days of becoming aware of the defect. Section 4.26(c)(2) lists acceptable means of distributing the correction. The federal securities laws prohibit the offer or sale of a security, including shares of a RIC, by means of a materially misleading prospectus and impose liability for the use of such a prospectus.[41] Section 4.26(d) requires a CPO to submit all Disclosure Documents to NFA prior to distributing the document to participants and to submit updates to Disclosure Documents to NFA that correct material inaccuracies or incompleteness within 21 days of becoming aware of any defects. Registration statements for RICs are required to be filed with the SEC prior to becoming effective,[42] and the RIC Rules prescribe the timeframes for effectiveness of registration statement amendments after filing with the SEC.[43]

In the Proposal, to facilitate compliance with part 4 requirements for CPOs of RICs, the Commission proposed amending § 4.26 and § 4.36 to allow CPOs and CTAs to use Disclosure Documents up to twelve months from the date of the document. In response to comments received, the Commission is also addressing in this final rule § 4.26(c), which governs the time

[40] Section 10(a)(3) of the Securities Act provides generally that when a prospectus is used more than nine months after the effective date of a registration statement, the information contained in the prospectus shall be as of a date not more than sixteen months prior to its use.

[41] Section 12(a)(2) of the Securities Act. See also, Section 17(a)(2) of the Securities Act (unlawful to obtain money or property by means of materially misleading statements and omissions in the offer or sale of securities).

[42] See, e.g., Section 8(a) of the Securities Act (effective date of registration statement shall be the twentieth day after filing or an earlier date determined by the SEC).

[43] See, Securities Act Rule 285, 17 CFR 230.485.

period for correcting materially inaccurate or incomplete disclosure, and § 4.26(d), which requires Disclosure Documents and updates to be filed with NFA.

1. Effective Time Period for Disclosure Documents

Commenters were generally supportive of the Commission's proposed amendments to §§ 4.26 and 4.36,[44] but also expressed concerns. Regarding the timing of disclosure, for example, some commenters suggested that the Commission extend the deadline applicable to all CPOs for using Disclosure Documents to sixteen months from the date of the document in order to accommodate the SEC's 120-day allowance under Rule 8b-16.[45] One commenter stated that the Proposal "provides no rationale for imposing the updating requirements of § 4.26(a)(1) on RICs" and does not "address the substantial costs these updates would impose."[46]

After careful consideration, the Commission has determined to adopt the amendment of §§ 4.26(a) and 4.36 as proposed. CPOs and CTAs will be permitted to use a Disclosure Document for up to 12 months. In addition, for CPOs of RICs, the Commission has determined that compliance with the applicable timeframes under the regime administered by the SEC under SEC RIC Rules will be deemed to satisfy the timing requirements in §§ 4.26(a) and 4.36.

As a general matter of policy, the Commission believes that sixteen months is not an optimal time period for providing updated information to participants. This is of particular concern with respect to past performance information and financial statements. The more distant the update of disclosure from the date of the pool's most recent financial statements, the less meaningful the information becomes to prospective participants deciding whether to invest. The Commission does believe, however, that efficiency can be gained by extending the time within

[44] AXA Letter; Steben Letter; IAA Letter.

[45] NYCBA Letter SIFMA AMG Letter; AII Letter.

[46] SIFMA AMG Letter.

which CPOs must update their Disclosure Documents from nine months to twelve months, as that time period aligns with the time period mandated for filing annual financial statements, which must be disclosed within the Disclosure Document. In the Commission's judgment, such efficiency justifies some delay in updating the Disclosure Document and the currency of the information thus available to participants. The Commission believes that the information available to participants will be sufficiently timely to enable participants to make informed investment decisions. Consistent with this determination that a twelve month updating cycle provides participants with information in a sufficiently timely manner, while also aligning with the larger CPO-industry twelve month regulatory calendar, the Commission is extending to twelve months the Disclosure Document update cycle requirement for all CPOs.

The Commission recognizes, however, that, absent harmonization, dual registrants may be required to comply with the disparate deadlines applicable under § 4.26 and the updating process implemented by the SEC pursuant to § 10(a)(3) of the Securities Act[47] and SEC Rule 485[48] thereunder. As noted above, § 4.26, as amended, requires a CPO to update a pool's Disclosure Document within 12 months of that Document's date of first use. As described above, § 10(a)(3) of the Securities Act and Securities Act Rule 485 requires open-end RICs to amend their registration statements annually and provides four months after the end of the fiscal year to do so.

Because the Commission is declining to adopt a sixteen-month update period for Disclosure Documents, absent other relief, CPOs of open-end RICs would have two different filing deadlines which would limit the ability for the CPO to take advantage of operational efficiencies that might be available if the Commission's deadlines coincided with those of the

[47] 15 U.S.C. 77j-24.

[48] 17 CFR 230.485.

SEC. The Commission believes that the burden associated with requiring CPOs of open-end RICs to comply with two different updating schedules for their Disclosure Documents is not justified by the benefit of more frequent disclosures. Thus, the Commission has determined to permit CPOs of open-end RICs to satisfy these obligations through substituted compliance in accordance with the timeframe administered by the SEC. The Commission believes that this is appropriate because the past performance information required to be disclosed by CPOs of open-end RICs will differ from that generally required of CPOs, and, as discussed infra, CPOs of open-end RICs will not be required to separately submit their disclosures documents for review by the NFA.

2. Interim Updating of Disclosure Documents

Section 4.26(c) requires a CPO to correct material inaccuracies in a Disclosure Document within 21-days of the date upon which the CPO first becomes aware of the defect. The purpose of the 21-day window in which to correct material inaccuracies is to provide participants with timely corrected information. As described above, the federal securities laws prohibit the offer or sale of the shares of a RIC by means of a materially misleading prospectus and impose liability for the use of such a prospectus.

One commenter noted that the 21-day period under § 4.26(c)(1) is not required under SEC RIC Rules and that RICs which do not normally supplement their prospectuses would be required to do so in order to comply with § 4.26.[49] Another commenter suggested that existing securities law obligations for RICs regarding material misstatements or omissions should satisfy § 4.26, and thus "a simple exemption from the Part 4 requirements is appropriate."[50] Another commenter

[49] SIFMA AMG Letter.

[50] ABA Letter.

suggested that RICs that are in compliance with SEC updating rules should be deemed compliant with § 4.26(a) and (c).[51]

In light of the substantively similar goals of the two regulatory regimes to ensure that participants receive accurate information in a timely manner, and recognizing that, absent relief from § 4.26(c), CPOs of RICs could be required to provide an additional mailing to participants, the Commission has determined to deem CPOs of RICs that adhere to the disclosure requirements under SEC RIC Rules compliant with § 4.26(c). Subject to additional experience that the Commission expects to acquire regarding the operation and oversight of CPOs of RICs, the Commission, at this time, believes that correcting any inaccuracies within this pre-scheduled and near-term update should be considered to be timely. Moreover, the Commission does not believe that the schedule for updates imposed by the SEC will impair the Commission's regulatory interest in ensuring that prospective and current participants in a commodity pool receive accurate and complete information. As such, the Commission believes that substituted compliance is appropriate with respect to the updating of disclosures to participants and, therefore, the Commission has determined to deem CPOs of RICs compliant with the provisions of § 4.26, provided that they are in compliance with the regime administered by the SEC under SEC RIC Rules.

3. Review of Disclosure Documents by NFA

Many commenters who addressed § 4.26 were concerned that NFA's review process (§ 4.26(d)) is unnecessary and duplicative, and thus should not be required.[52] Commenters said that this additional review process could result in regulatory delays, create investor confusion, tax

[51] SIFMA AMG Letter.

[52] AXA Letter; ABA Letter; Katten Letter; ICI Letter; SIFMA AMG Letter.

NFA's resources, prevent funds from issuing shares, and potentially subject funds to conflicting reviews from securities and derivatives regulators.[53] Some commenters noted that NFA's review process would be particularly challenging for RICs that make offerings through variable insurance products, as the distribution and updating of prospectuses for such RICs must be coordinated with their affiliated insurance companies, and that the Proposal does not address this issue.[54] One commenter also requested confirmation that "sticker" supplements—supplements tacked onto existing Disclosure Documents—would not be subject to NFA review, as § 4.26(d)(2) provides that updates may be filed with NFA at the same time they are distributed to participants.[55] Another commenter stated that the timelines for review between the SEC and CFTC requirements are different and conflicting. For example, if the NFA requests material changes, a CPO of a RIC may have to file the amendment with the SEC, triggering SEC review and potentially disrupting the issuance of shares. The commenter suggested that, should the CFTC decide to retain the NFA review requirement, it should limit the scope of the review to the part 4 disclosure requirements. This commenter further suggested that the SEC, CFTC, and NFA coordinate policies and processes to "avoid conflicting comments and prevent multiple filings and back-and-forth" during the review process.[56]

The Commission has determined that, although such disclosures must be made available to NFA to enable NFA to discharge its duty to monitor and examine CFTC registrants during an examination, it will not be necessary to file those documents with NFA according to the schedules provided in part 4 of the Commission's regulations or concurrent with their filing with the SEC,

[53] AXA Letter; ABA Letter; NYCBA Letter; ICI Letter; SIFMA AMG Letter.

[54] AXA Letter; ICI Letter.

[55] ABA Letter.

[56] SIFMA AMG Letter.

and those documents will not be subject to NFA approval. The Commission has decided that CPOs of RICs that take advantage of the relief provided under this rule must file a notice with NFA so that NFA and the Commission can identify which CPOs are claiming such relief and are not required to comply with the specific provisions of §§ 4.21, 4.24, 4.25, and 4.26. Providing this notice to NFA will facilitate compliance by market participants, assist the Commission's monitoring of the compliance of its registrants over time, and facilitate the enforcement of its rules with respect to all CPOs.

In sum, the Commission has determined to deem CPOs of RICs compliant with the provisions of § 4.26, provided that they are in compliance with the regime administered by the SEC under SEC RIC Rules.

b. Delivery and Acknowledgement of Disclosure Documents

Currently, § 4.21 requires a CPO to deliver a Disclosure Document to each participant, and obtain from that prospective participant a signed acknowledgment of receipt of the Disclosure Document before accepting or receiving funds from that participant. The federal securities laws require delivery of a "statutory" prospectus to each RIC investor no later than the confirmation of the transaction and do not require signed acknowledgment prior to receipt of funds from an investor.[57]

The Commission proposed to modify § 4.12(c) to allow the CPO of a RIC to claim relief from § 4.21. The proposed revisions to § 4.12(c) would enable CPOs of RICs to claim relief from

[57] Securities Act § 5(b)(2) (unlawful to carry through the mails or in interstate commerce any security for the purpose of sale or delivery after sale unless accompanied or preceded by a "statutory" prospectus, i.e., a prospectus that meets the requirements of § 10(a) of the Securities Act). Open-end RICs may satisfy the prospectus delivery obligation by sending or giving a summary prospectus to investors and providing the statutory prospectus on an Internet website. Rule 498 under the Securities Act. 17 CFR 230.498.

§ 4.21 provided that the Disclosure Document is readily available on the RIC's website, or that of its designee.

Some commenters suggested a broad exemption from § 4.21 for all CPOs of RICs.[58] Another commenter noted that a listed, closed-end RIC does not normally post its prospectus or annual report online when not conducting an offering, and suggested that such funds should be fully exempted from § 4.21. This commenter also requested confirmation that: (a) the website may be the main website for the RIC's fund family or the RIC's distributor, so long as the Disclosure Document page is readily available from the main website; (b) password-protected websites (used by privately-offered funds) will remain acceptable under the Commission's rules; and (c) the distributor for a RIC would be permitted to maintain the website for a RIC under the Commission's rules.[59]

One commenter did not support the proposed amendments. This commenter claimed that the requirements are duplicative, as the information required to be posted on a website is already provided to investors through various SEC regulations. The commenter also suggested that compliance with § 4.12 may harm investors by broadly disclosing a fund's trading strategy.[60]

The Commission has determined to deem CPOs of RICs compliant with the provisions of § 4.21 provided that the CPO provides disclosure to participants and prospective participants consistent with the regime administered by the SEC under SEC RIC Rules. The SEC RIC Rules permit open-end RICs to send or give a summary prospectus, provided that the statutory prospectus and other information are available on an Internet website, the address of which is

[58] Katten Letter; ABA Letter.

[59] SIFMA AMG Letter.

[60] AII Letter.

provided on cover page or at the beginning of the summary prospectus.[61] Any website permitted under the SEC RIC Rules will also be deemed compliant with the provisions of § 4.21 SEC regulations further provide that the RIC must provide paper copies of the statutory prospectus, SAI, and shareholder reports upon request at no cost to the requestor.[62] As the SEC RIC rules require that a participant receive substantial information about the fund (information that, as discussed above, would be deemed compliant with Commission regulations under part 4), the Commission believes that this SEC requirement is commensurate with the provisions of § 4.21 in that it provides a mechanism through which information about the investment in the RIC is disseminated to prospective participants. Under both part 4 of the Commission's regulations and the SEC's disclosure regime, information is made readily available to prospective investors in the pools. Therefore, the Commission believes it is appropriate to deem entities that comply with SEC disclosure delivery requirements to be compliant with their disclosure delivery obligation under part 4.

With respect to closed-end funds, under the Commission's regulations, CPOs are not required to maintain a current Disclosure Document for a pool if they are not soliciting participants for that pool.[63] Consistent with the Commission's reasoning regarding open-end RICs, provided that the closed-end fund is operated consistent with its obligations under SEC RIC Rules, the Commission believes that it is appropriate to deem CPOs of closed-end funds compliant with the requirements of § 4.21.

---

[61] See, 17 CFR 230.498.

[62] Id.

[63] See, 17 CFR 4.21 (requiring delivery of a Disclosure Document concurrent with the delivery of a subscription agreement to prospective participants).

Additionally, for those funds that are organized as series entities with inter-series limitation of liability, the SEC permits multiple series to be included in a single registration statement, but permits reporting and disclosure to be accomplished on a series by series basis. Under the Commission's regulations, the pool is considered to be the discrete legal entity.[64] As such, the Commission's regulations would require any such filings to be prepared at the legal entity level, not at the series level. The Commission recognizes that under part 4, RICs would be required to undertake substantial efforts to reorganize their filings to comply with both regimes.[65] However, because the Commission has already determined to accept compliance with the regime administered by the SEC as substituted compliance with the Commission's compliance program, the Commission believes that such entities will continue to be able to make such filings consistent with SEC guidance regarding the same.

c. Use of the Summary Prospectus

Commenters also expressed concern about continuing to use the Summary Prospectus adopted by the SEC.[66] Because the SEC limits the information allowed in the Summary Prospectus, a commenter requested clarification that the CFTC is not requiring that any of the specific part 4 disclosure requirements be included in that document.[67] Another commenter suggested that the Commission allow registrants the option of providing a combined document or

[64] The Commission has determined that, per Regulation 4.20(a)(1), a pool is considered to be a separately cognizable legal entity. See, CFTC Staff Interpretative letter 10-29, available at http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/10-29.pdf.

[65] The Commission reaffirms its position with respect to the entity qualification of "pool" as embodied in CFTC Staff Interpretative letter 10-29, available at http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/10-29.pdf.

[66] 17 CFR 230.498.

[67] SIFMA AMG Letter.

maintaining separate SEC- and CFTC-required disclosures.[68] Several commenters urged the Commission to provide assurances to CPOs of RICs that Summary Prospectus documents may still be utilized by funds in the format they currently use.[69] Another commenter expressed concern that requiring RICs to highlight new and amended disclosures under § 4.26 "would add unnecessary costs to the update process and could prove confusing to RIC shareholders" because such requirements are "not consistent with past practices."[70]

The Commission has determined to deem CPOs of RICs compliant with the provisions of §§ 4.24 and 4.25, provided that they are in compliance with the disclosure requirements of the Securities Act, the '40 Act, and the applicable SEC RIC Rules. By deeming such CPOs compliant, the ability to use a statutory prospectus and/or Summary Prospectus in a format recognizable to both funds and their participants has not been disturbed.

d. Risk Statements and Legends

Section 4.24(a)-(b) details specific disclosure statements that must appear in a CPO's Disclosure Document. The Commission requires a specific Cautionary Statement (§ 4.24(a)) to appear prominently on the cover page of the Disclosure Document.[71]

The Commission also requires certain Risk Disclosure Statements to be displayed immediately following any disclosures required to appear on the cover page. The disclosures most relevant to this rulemaking are found in § 4.24(b)(1).[72]

---

[68] MFA Letter.

[69] ABA Letter; Katten Letter; NYCBA Letter.

[70] AXA Letter.

[71] The Cautionary Statement reads as follows: THE COMMODITY FUTURES TRADING COMMISSION HAS NOT PASSED UPON THE MERITS OF PARTICIPATING IN THIS POOL NOR HAS THE COMMISSION PASSED ON THE ADEQUACY OR ACCURACY OF THIS DISCLOSURE DOCUMENT.

[72] Section 4.24(b)(1) reads as follows:

1. The Standard Cautionary Statement

The Commission proposed that, in lieu of the standard Cautionary Statement, the cover page of the RIC's prospectus may contain a statement that combines the language required by § 4.24(a) and Rule 481(b)(1) under the Securities Act.[73] The Proposal required the Risk Disclosure Statements to be presented concomitantly with SEC-required information in the RIC's prospectus.

One commenter claimed that the SEC must also grant relief to permit inclusion of the Cautionary Statement mandated in § 4.24(a) on the cover page of a prospectus; the commenter suggested the Commission ensure that the SEC has issued such relief before imposing the combined statement requirement.[74]

Other commenters objected to the disclosure statements, including the Cautionary Statement in § 4.24(a), as being "boilerplate," "technical," and "duplicative."[75] Commenters stated that such language is inconsistent with the SEC's "Plain English" disclosure requirements,

---

YOU SHOULD CAREFULLY CONSIDER WHETHER YOUR FINANCIAL CONDITION PERMITS YOU TO PARTICIPATE IN A COMMODITY POOL. IN SO DOING, YOU SHOULD BE AWARE THAT COMMODITY INTEREST TRADING CAN QUICKLY LEAD TO LARGE LOSSES AS WELL AS GAINS. SUCH TRADING LOSSES CAN SHARPLY REDUCE THE NET ASSET VALUE OF THE POOL AND CONSEQUENTLY THE VALUE OF YOUR INTEREST IN THE POOL. IN ADDITION, RESTRICTIONS ON REDEMPTIONS MAY AFFECT YOUR ABILITY TO WITHDRAW YOUR PARTICIPATION IN THE POOL.

FURTHER, COMMODITY POOLS MAY BE SUBJECT TO SUBSTANTIAL CHARGES FOR MANAGEMENT, AND ADVISORY AND BROKERAGE FEES. IT MAY BE NECESSARY FOR THOSE POOLS THAT ARE SUBJECT TO THESE CHARGES TO MAKE SUBSTANTIAL TRADING PROFITS TO AVOID DEPLETION OR EXHAUSTION OF THEIR ASSETS. THIS DISCLOSURE DOCUMENT CONTAINS A COMPLETE DESCRIPTION OF EACH EXPENSE TO BE CHARGED THIS POOL AT (insert page number) AND A STATEMENT OF THE PERCENTAGE RETURN NECESSARY TO BREAK EVEN, THAT IS, TO RECOVER THE AMOUNT OF YOUR INITIAL INVESTMENT, AT PAGE (insert page number).

[73] The proposed rules provided suggested language in two examples; for instance, one example states: "The Securities and Exchange Commission and the Commodity Futures Trading Commission have not approved or disapproved these securities or this pool, or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense." See Proposal, supra note 23, 77 FR at 11351.

[74] ICI Letter.

[75] ABA Letter; Dechert Letter; Fidelity Letter; AII Letter; SIFMA AMG Letter.

which are designed to make prospectuses easier for investors to read, and thus their inclusion may create investor confusion.[76]

With respect to the prescribed cautionary statement required under § 4.24(a), the Commission finds that the statement as required by the SEC[77] performs a similar function as that required by the Commission, and has concluded that the cautionary statement prescribed in SEC Rule 481 under the Securities Act,[78] with minor modifications, addresses the Commission's concerns regarding the need for CPOs to adequately apprise investors that the Commission has not approved a particular disclosure that is provided to prospective participants. Therefore, the Commission has determined that it would be acceptable for CPOs of RICs to include the CFTC in the statement prescribed by the SEC under Securities Act Rule 481,[79] such that the statement would read either:

The Securities and Exchange Commission and the Commodity Futures Trading Commission have not approved or disapproved these securities or passed upon the adequacy of this prospectus. Any representation to the contrary is a criminal offense.

or

The Securities and Exchange Commission and the Commodity Futures Trading Commission have not approved or disapproved these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

2. The Standard Risk Disclosure Statement

[76] AXA Letter; ABA Letter; Dechert Letter; AII Letter.

[77] Securities Act Rule 481 (17 CFR 230.481) requires that the outside front cover page of a prospectus contain a legend that indicates that the SEC has not approved or disapproved the securities or passed upon the accurace or adequacy of the disclosure in the prospectus and that any contrary representation is a criminal offense. The legend may be one of the two following statements in clear and concise language:

The Securities and Exchange Commission has not approved or disapproved these securities or passed upon the adequacy of this prospectus. Any representation to the contrary is a criminal offense; or

The Securities and Exchange Commission has not approved or disapproved these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

[78] 17 CFR 230.481(b)(1).

[79] 17 CFR 230.481(b)(1).

Commenters also objected to the inclusion of the standard Risk Disclosure Statements found in § 4.24(b).[80] Several commenters remarked that the CFTC-required disclosures, designed for commodity pools, are not appropriate for funds because (a) SEC regulations prohibit a fund from maintaining high degrees of leverage; and/or (b) SEC regulations do not allow funds to restrict redemption rights.[81] These commenters contended that requiring such "inappropriate" disclosures would be misleading and confusing for investors.

In addition, one commenter contended that because the risks described in § 4.24(b) are non-principal risks for most mutual funds, and because the SEC has indicated that only principal risks should be disclosed in the summary prospectus, RICs should be exempt from these requirements. This commenter also noted that "[e]xhaustion of a fund's assets is essentially impossible" under the '40 Act.[82] Another commenter requested clarification about the placement of required disclosures. Specifically, the commenter noted that putting the standard CFTC risk disclosures in a RIC's summary prospectus may violate SEC Rule 498, which prohibits information other than that prescribed by that Rule from inclusion in the summary prospectus.[83]

Commenters also requested that the Commission allow RICs to use the term "fund" instead of "pool" in the Cautionary Statement as well as any mandated disclosure statements, as fund investors are unfamiliar with the term "pool" and may be confused by such language.[84]

The standard risk disclosure statement under § 4.24(b) sets forth standard disclosures of risks associated with the use of commodity interests, including generic discussions of liquidity,

---

[80] AXA Letter; ABA Letter; Dechert Letter; Fidelity Letter; AII Letter; NYCBA Letter; SIFMA AMG Letter.

[81] AXA Letter; ABA Letter; Dechert Letter; NYCBA Letter; SIFMA AMG Letter; ICI Letter.

[82] Dechert Letter.

[83] AXA Letter.

[84] AXA Letter; Dechert Letter; SIFMA AMG Letter; comment letter from Invesco Advisers, Inc. (April 24, 2012) (Invesco Letter); ICI Letter.

counterparty creditworthiness, and limits on the ability to alter the terms of certain swap agreements.[85] Because open-end RICs are required to honor redemption requests within 7 days,[86] the Commission believes that, absent information to the contrary, the generic discussion of risks required as part of the standard risk disclosure statement under § 4.24(b) may differ with respect to RICs, in that investor liquidity is necessarily required as a function of fulfilling the redemption obligations under the '40 Act. Therefore, the risk that a participant will be unable to redeem in a timely manner appears to be mitigated. Further, with respect to closed-end funds, because interests in such funds are generally not redeemed directly from the fund, but rather are traded in the secondary market, it would appear that the risks discussed in the prescribed risk disclosure statement under § 4.24(b) may not be precisely applicable to their operation. For the foregoing reasons, the Commission believes that the specific risks delineated in the prescribed cautionary statement may not reflect those associated with investment in a RIC, and therefore, has determined not to require CPOs of RICs to include the standard risk disclosure statement required under §4.24(b).[87] Having considered the comments received as well as the redemption requirements of RICs under the '40 Act, the Commission has determined to deem CPOs of RICs compliant with the requirements of § 4.24(a) and (b) provided that the CPO complies with the related regime administered by the SEC pursuant to the SEC RIC Rules, including disclosure requirements in Section 10 of the Securities Act and other provisions of the Securities Act and '40 Act,, Rule 498 [88] under the Securities Act, and forms N-1A and N-2.

---

[85] 17 CFR 4.24(b).

[86] 15 U.S.C. 80a-22(e).

[87] Because the Commission has determined not to require CPOs of RICs to include the Standard Risk Disclosure statement in their Disclosure Documents, the Commission does not have to address the issue of using the term "fund" in lieu of "pool" within the risk disclosure statement.

[88] 17 CFR 230.498.

e. Risk Disclosure

Section 4.24(g) requires a discussion of the principal risk factors of participation in the offered pool. It further requires that the discussion must include, without limitation, risks relating to volatility, leverage, liquidity, and counterparty creditworthiness, as applicable to the trading programs followed, trading structures used, and investment activities of the offered pool.

One commenter suggested that the risks required to be disclosed pursuant to the SEC's disclosure requirements provide comparable information to that mandated by the Commission's regulations.[89] That commenter also suggested that the Commission should exempt CPOs of RICs from the risk disclosure requirements set forth in § 4.24(g) because they are generic and are required to appear in a single section of the Disclosure Document rather than in various sections of the disclosure as permitted by the SEC.

The Commission believes that, although the CPOs of RICs may elect to comply with §§ 4.24, 4.25 and 4.26 through substituted compliance, the disclosure provided by CPOs of RICs to prospective participants should include true, accurate, and complete information describing the commodity-interest activities of the pool, including a discussion of the material risks of those assets and activities. The Commission understands that SEC forms N-1A and N-2 require disclosure of the principal risks associated with investment in the RIC and that, to the extent that the use of commodity interests creates such a risk, it must be disclosed to prospective investors. This is consistent with the requirements set forth in § 4.24(g), which also requires the disclosure of the principal risks of investing in the pool, and which mandates that such disclosures be appropriately tailored to reflect the risks associated with the investment strategy and instruments traded by the offered pool. Moreover, the Commission does not believe that the fact that the

[89] ICI Letter.

disclosures may appear in multiple places under the SEC's disclosure requirements is inconsistent with the Commission's regulations, as such regulations do not require that such disclosures appear in a single section of the Disclosure Document. The Commission believes that the disclosure requirements on SEC forms N-1A and N-2, consistent with guidance from SEC staff, including the letter issued by the Division of Investment Management in 2010,[90] should satisfy the Commission's concern that participants receive complete and accurate disclosure about the risks associated with investment in commodity interests. CPOs of RICs must likewise comply with any applicable SEC guidance, including guidance that may be issued hereafter, concerning these disclosure requirements, which the Commission will evaluate for consistency with its own regulatory interests. The Commission understands, for example, that the Division of Investment Management at the SEC intends to issue additional guidance to RICs regarding compliance with certain aspects of the SEC RIC Rules.

f. Break Even Disclosure

Section 4.24(d)(5) requires CPOs to include in the forepart of the Disclosure Document the break-even point per unit of initial investment. Section 4.10(j) defines the break-even point as "the trading profit that a pool must realize in the first year of a participant's investment to equal all fees and expenses such that such participant will recoup its initial investment, as calculated pursuant to rules promulgated by a registered futures association pursuant to section 17(j) of the Act."

The Commission proposed to consider the "forepart" of the document to be the section immediately following all disclosures required by SEC form N-1A. The Commission did not

[90] Letter from the Division of Investment Management, Securities and Exchange Commission, to the Investment Company Institute, July 30, 2010, available at http://www.sec.gov/divisions/investment/guidance/ici073010.pdf.

propose to relieve RICs of the requirement to provide the break-even point disclosure, however, stating that "[the] Commission continues to believe that the inclusion of…the break-even point…is a necessary disclosure because, among other requirements, it mandates a greater level of detail regarding brokerage fees and does not assume a specific rate of return."

One commenter supported the Commission's position that the break-even table should be included in the prospectus of an investment company.[91]

However, other commenters generally believed that RICs should be exempt from disclosing the break-even point.[92] Some commenters claimed that the break-even point and analysis serves the same purpose as the tabular presentation of fees required by SEC regulations, and thus including such information would be duplicative and unnecessary.[93] One commenter believed that the current SEC-required disclosures are better suited to funds "given that they are continually offered and have daily changing asset levels." This commenter also believed that the CFTC did not identify why the break-even point is necessary or why the fact that it does not assume a rate of return makes the disclosure more meaningful for investors.[94] Some commenters contended that including the break-even point and analysis may undermine the SEC's goal of providing comparable disclosures and make it harder for potential investors to compare information across funds.[95] Another commenter argued that the Commission is incorrect in

[91] Steben Letter.

[92] AXA Letter; ABA Letter; Dechert Letter; ICI Letter; NYCBA Letter.

[93] AXA Letter; ABA Letter; ICI Letter.

[94] Dechert Letter.

[95] AXA Letter; NYCBA Letter.

suggesting that the SEC's fee table requirements are based on assumed rate of return, as form N-1A requirements for fee disclosure in general do not assume a specific rate of return.[96]

The Commission understands that the same types of fees and costs are disclosed through SEC-required disclosures, even if in a different format.[97] For example, § 4.24(i) requires a full and complete discussion of all management fees. Form N-1A, item 3 requires similar disclosure. The Commission is persuaded by the commenters that the information required by the SEC achieves substantially the same purposes as the break-even point analysis. The Commission has concluded that the disclosure required by the SEC is sufficient to communicate the fees and costs associated with a RIC that engages in derivatives. Therefore, the Commission has determined to deem the CPOs of RICs compliant with the requirements under § 4.24(d)(5) of the Commission's regulations contingent upon their compliance with the SEC RIC Rules.

g. Past Performance Disclosure

Section 4.24(n) requires CPOs to disclose past performance information in accordance with § 4.25. Section 4.25(a) requires various disclosures, including, but not limited to: aggregate gross capital subscriptions to the pool; the pool's current net asset value; the largest monthly draw-down during the most recent five calendar years and year-to-date; the worst peak-to-valley draw-down during the most recent five calendar years and year-to-date; and the annual and year-to-date rate of return for the pool for the most recent five calendar years and year-to-date, including a bar graph depicting such rates of return. Similar information is required for each account traded by the CPO or CTA on behalf of a client.

[96] ICI Letter.

[97] See generally SEC form N-1A, Item 3.

Section 4.25(c) states that when the offered pool has less than a three-year operating history, the CPO must disclose the past performance of each other pool it operates.
By contrast, the SEC's regulations do not require RICs to disclose past performance for any fund other than the offered fund. Most of the other performance-related disclosures are similar between the two regulatory regimes. However, some information is presented in a different manner. For example, whereas § 4.25 requires disclosure of the pool's performance for the year-to-date and the most recent five calendar years, Item 4(b)(2)(iii) of Form N-1A requires disclosure of average annual total returns for the previous year, five years, and ten years (or the life of the fund, if shorter than five or ten years).

The Commission proposed to maintain the past performance disclosure requirements, but requested comment on the advisability of doing so. Most commenters suggested that the Commission exempt RICs from disclosing past performance information.[98] Some commenters claimed that the SEC generally does not permit disclosure of the past performance of funds other than the offered fund, and that the CFTC's requirement to do so would cause funds to be in a position of having to choose which regulator's rules to violate.[99]

Numerous commenters highlighted a footnote in the Proposal that said the Commission had had preliminary discussions with the SEC regarding past performance disclosures and that the SEC may consider no-action relief for dually-registered RIC/CPOs. These commenters argued that it would unreasonable for the CFTC to expect hundreds of funds (according to one commenter) to apply for no-action relief, stressing the inefficiencies and burdens for RICs and for

[98] AXA Letter; ABA Letter; Dechert Letter; Katten Letter; IAA Letter; Fidelity Letter; NYCBA Letter; SIFMA AMG Letter.

[99] AXA Letter; Dechert Letter; Katten Letter; SIFMA AMG Letter; ICI Letter.

the SEC to comply with such a volume of requests.[100] Some commenters noted that the SEC is under no obligation to grant such relief, and that even if it did, no-action letters are typically non-binding.[101] Other commenters noted that even if the SEC does grant no-action relief for this provision, such an action may create disparate treatment between RICs and RIC/CPOs that would confuse investors who are accustomed to the SEC's provisions on performance disclosure. These commenters further noted that the dual requirements may complicate the registration process for RICs subject to the dual disclosure requirement, which could operate to their competitive disadvantage.[102]

One commenter expressed concern that this provision does not accomplish the CFTC's stated objective of providing material information while reducing duplicative disclosure.[103] Another commenter suggested that funds with fewer than three years' performance should be required to disclose information only for other funds with substantially similar objectives and strategies that are managed by the same adviser.[104]

Other commenters disagreed. One commenter suggested that while allowing CPOs of RICs to show only the results of similar pools (as permitted by the SEC) would lessen the burden on such firms, it "would also create interpretive questions" and allow funds to exclude the performance of relevant pools.[105] Another commenter recommended that the Commission maintain the requirement, but limit the scope of the disclosure to include past performance information only for other commodity pools listed with NFA by the RIC/CPO. This commenter

[100] Dechert Letter; IAA Letter; Fidelity Letter; SIFMA AMG Letter; ABA Letter.

[101] Dechert Letter; Fidelity Letter.

[102] ABA Letter; Katten Letter.

[103] Dechert Letter.

[104] ICI Letter.

[105] Steben Letter.

suggested that the Commission encourage the SEC to provide no-action relief and to do so on a "global" basis, as opposed to a case-by-case basis.[106]

Some commenters suggested that the CFTC exempt RICs from the requirement to disclose aggregate gross capital subscriptions.[107] One commenter stated that such a requirement is not practicable for open-ended RICs, which are publicly-offered.[108] Another commenter stated that the measurement "is meaningless to fund investors, as subscriptions are frequently offset…by redemptions."[109]

One commenter believed that the differences in how the charts required by SEC and CFTC regulations are calculated could result in an additional preparation burden for RICs and additional confusion for investors, and suggested that the CFTC harmonize this requirement to the SEC's disclosure. Similarly, the commenter suggested the Commission harmonize the different methodologies of the CFTC- and SEC-reporting requirements to avoid duplicative and confusing information. For example, the commenter noted that past performance disclosures are required for different timeframes (the SEC requires 1, 5, and 10 year disclosure; the CFTC requires each of the most recent 5 years to be disclosed).[110]

After consideration, and in light of the comments received, the Commission has determined to deem CPOs of RICs with less than three years of performance history to be compliant with § 4.25(c), provided that the CPO disclose the performance of all accounts and

[106] NFA Letter, Campbell Letter.

[107] SIFMA AMG Letter, Dechert Letter.

[108] SIFMA AMG Letter.

[109] Dechert Letter.

[110] Id.

pools that are managed by the CPO and that have investment objectives, policies, and strategies substantially similar to the offered pool.[111]

The requirements for disclosure of commodity pools' past performance exist because the Commission, drawing on its experience, believes they provide prospective participants with useful information. The markets for commodity interests are highly complex and require specialized knowledge to manage funds effectively. The Commission continues to believe that the presentation of past performance provides investors with information regarding the experience of a CPO of a relatively new pool. A prospective investor will, as a result of this requirement, be better able to assess the experience and expertise of the CPO as a result of this disclosure. As summarized by participants in the rulemaking process in which the Commission adopted § 4.25, while "past performance data alone are not directly predictive of future trading results, . . . past performance data provide information that is important in evaluating a contemplated pool offering or trading program. For example, patterns of volatility and other trading patterns in various market conditions may be evident."[112]

Although the SEC does not mandate the disclosure of the performance of other funds and accounts, guidance provided by the SEC's Division of Investment Management indicates that a RIC is permitted to show the performance of funds and accounts that are managed by the same investment adviser as the RIC and that have investment objectives, policies, and strategies substantially similar to those of the RIC.[113] Recognizing that the SEC approaches this issue

[111] With respect to the commenter that suggested requiring the disclosure of other pools that trigger registration as a CPO with the Commission, the Commission is concerned that it may result in requiring the CPO of a RIC to disclose the performance of a pool or account that does not have investment objective, policies, and strategies substantially similar to those of offered pool, thereby causing the CPO of the RIC to violate the restrictions imposed by the SEC.

[112] 60 FR 38148 (July 25, 1995); see also 68 FR 42964 (July 21, 2003).

[113] See, e.g., ITT Hartford Mutual Funds (pub. avail. Feb. 7, 1997) (fund may include in marketing materials performance information for other funds managed by the same adviser with investment objectives, policies, and

differently, and would not allow the performance disclosures of each other pool the CPO operates, the Commission understands that the SEC's Division of Investment Management would permit a subset of that information to be disclosed. Notably, it would permit all the disclosure of past performance that is most germane to that of the offered pool and provide precisely the information that a prospective investor would need to evaluate the historical behavior of the markets and instruments in which the offered pool invests. As such, the Commission has made the judgment to confine this requirement for CPOs of RICs with less than three years operating history to disclose information concerning pools or accounts that are managed by the CPO and that have substantially similar investment objectives, policies, and strategies because it provides prospective participants with additional information regarding the historical performance of accounts and pools traded pursuant to the trading strategy used by the offered pool, and provides data regarding the experience of the CPO trading substantially similar instruments and trading strategies.

The Commission believes that this requirement appropriately addresses the Commission's concerns about ensuring that prospective participants have the information that the Commission believes is essential to making informed decisions, prior to investing in a commodity pool, while respecting the limitations on disclosure imposed by the SEC. CPOs of RICs with less than 3 years performance history will be required to identify which other accounts and pools have investment objectives, policies, and strategies substantially similar to those of the offered pool. In contrast to § 4.25 as applied to CPOs generally, the Commission's acceptance of substituted compliance for CPOs of RICs introduces a mildly subjective element that is otherwise absent under the regulation. The Commission believes that any such subjectivity is tightly constrained due to the

---

strategies substantially similar to those of the fund); Nicolas-Applegate Mutual Funds (pub. avail. Aug. 6, 1996) (fund may include in prospectus information for private accounts managed by the fund's adviser with investment objectives, policies, and strategies substantially similar to those of the fund).

guidance that SEC staff has provided in this area. The Commission believes that the result will be reasonably tailored to provide prospective participants with materially useful information that otherwise would not be mandatorily disclosed under the SEC's regulatory regime.[114]

Additionally, the Commission has determined to deem CPOs of RICs compliant with the remainder of § 4.25, which includes the requirement to disclose aggregate gross capital subscriptions, to the extent that the CPOs comply with applicable SEC Rules. The Commission has reached this decision after considering the requirements imposed by the SEC and concluding that the compliance obligations, with the limited exception noted above for CPOs of RICs with less than three years of performance history, generally achieve the same disclosure objective. For example, although the timeframes for performance disclosure differ, with the Commission requiring 5 years of performance, whereas the SEC requires up to 10 years performance, the Commission believes that the disclosure required by the SEC provides a reasonable means for ensuring effective disclosure of a pool's past performance to a prospective participant as the information provided under the SEC's regulatory regime includes that required under part 4 of the Commission's regulations. Additionally, the Commission recognizes the challenges that a continuously offered RIC might face in determining its aggregate gross capital subscriptions. It may not be possible for the CPO of a continuously offered RIC to make such a determination given the continually variable number of subscriptions and redemptions. Therefore, the Commission is deeming CPOs of RICs compliant with the requirements of § 4.25 subject to compliance with the regime set forth under SEC RIC Rules, with the exception of those pools

[114] See, the Commission's discussion of costs and benefits, infra, regarding the costs associated with this disclosure requirement.

which have a less than three year operating history, the CPO of which must make the additional disclosures as discussed supra.

h. Fee Disclosure

Section 4.24(i) requires CPOs to include in the Disclosure Document a complete description of each fee, commission, and other expense which the CPO knows has been incurred or expects to be incurred. This description must include management fees, brokerage fees and commissions, any fees and commissions paid for trading advice, fees incurred within investments in investee pools and funds, incentive fees, any allocations paid out to the CPO, commissions or other benefits paid to any person in connection with soliciting participation in the pool, administrative fees and expenses, offering expenses, and clearance, exchange, and SRO fees, along with certain other fees as applicable.

Many of these fees are disclosed by RICs in SEC form N-1A. Item 3 of that form requires a table of fees to be presented. The Commission proposed to require any such expenses not included in the fee table in Item 3 of Form N-1A to be disclosed in the prospectus in addition to those fees and expenses required by both the CFTC and the SEC.

Commenters generally contended that the CFTC's requirement under § 4.24(i)(2)(ii) to disclose brokerage fees and commissions should not apply to RICs as such disclosures may be misleading and/or confusing for fund investors.[115] One commenter noted that if RICs decide that the inconsistent disclosures warrant changing existing practices, the process of separating out prospectuses would carry "inevitable initial and ongoing operational, legal, compliance, and marketing costs."[116] Another commenter stated that the SEC has determined its fee disclosure

[115] ABA Letter; Dechert Letter; Katten Letter; SIFMA AMG Letter.

[116] ABA Letter.

regime to be adequate and that the CFTC has not identified any reason why additional disclosure is necessary to protect investors. This commenter also noted that expected fees, required to be disclosed under § 4.24(i)(1), are predictive and could be misleading if projected expenses are more favorable than the actual expenses incurred.[117]

The Commission understands that the same types of fees and costs are disclosed through SEC-required disclosures, although perhaps in a different format, as discussed *supra*, with respect to the break-even information. The Commission, moreover, is persuaded by the commenters that the information required under its break-even point and table is not meaningfully different from what the SEC already requires. For example, the SEC-required disclosure permits brokerage fees to be included in the cost of securities, whereas the Commission requires such fees to be disclosed separately. In both cases, information regarding such fees is being provided to the investor. Moreover, item 21 of SEC form N-1A requires a discussion of brokerage commissions paid by the RIC during its three most recent fiscal years.[118] The Commission believes that the disclosure required by the SEC is sufficient to communicate the fees and costs associated with a RIC that engages in derivatives, notwithstanding the fact that the format is different from that generally prescribed by the Commission with respect to CPOs and CTAs. Therefore, the Commission has determined to deem the CPOs of RICs compliant with the requirements under § 4.24(d)(5) of the Commission's regulations, provided that they comply with the SEC's required disclosures.

i. Controlled Foreign Corporations (CFCs)

In the 2012 Final Rule, the Commission explained its position on the use of CFCs by RICs, stating that, although the Commission does not oppose the use of CFCs by RICs, it

[117] Dechert Letter.

[118] See SEC form N-1A, item 21.

nevertheless believes that CFCs that fall within the statutory definition of commodity pool may necessitate the registration of a CPO.[119] As such, operators of such entities, whether or not the RIC that owns the CFC may be excluded under § 4.5, may be required to register as CPOs with the Commission.

As stated in the 2012 Final Rule, the Commission understands that a RIC may invest up to 25 percent of its assets in a CFC, which then engages in actively managed derivatives strategies, either on its own or under the direction of one or more CTAs. [120]

One commenter agreed with the Commission's position that RICs should be permitted to use CFCs under appropriate circumstances. This commenter further articulated their belief that in certain situations additional disclosures regarding CFCs may be necessary, as the relationship between a RIC and related CFCs is "significantly different than a typical fund-of-funds structure." The commenter suggested that the Commission clarify that the RIC's Disclosure Document must contain a full discussion of this relationship and the impact of the CFC on the pool/RIC, including on the performance of the pool/RIC.[121]

Another commenter noted that a CFC may constitute a major investee pool and, as such, the CPO of a RIC would have to include certain disclosures regarding the CFC in its Disclosure Document pursuant to the Commission's regulations. However, this commenter suggested the Commission require additional "extensive, particularized disclosure regarding [CFCs] used by investment companies" and claimed that "[s]uch information is needed…to help investors and regulators identify and understand the expenses…and risks" associated with CFCs.[122]

---

[119] See 2012 Final Rule, supra note 6, 77 FR at 11260.

[120] See 2012 Final Rule, supra note 6, 77 FR 11252 (Feb. 24, 2012) for a discussion of CFCs and their use by RICs.

[121] NFA Letter.

[122] Steben Letter.

One commenter requested that the Commission exempt a CFC that is wholly owned by a RIC from the detailed disclosure and reporting requirements under part 4 because the only recipients of such information would be the RIC that owns the CFC.[123]

The Commission reaffirms its earlier statements in the 2012 Final Rule that RICs may continue to use CFCs and that such CFCs, depending on their investment activities, may fall within the statutory and regulatory definitions of "commodity pool."[124] The provisions of SEC forms N-1A and N-2 require a discussion of the investment strategies of the offered funds and the principal risk factors associated with investment in the fund.[125] The Commission understands that if a RIC is using a CFC to effectuate its investment strategy, the RIC is required to disclose in its prospectus filed with the SEC information about the RIC's investment in the CFC and the principal risks associated with the CFC investment, including those related to swaps and other commodity interests. Accordingly, the Commission has determined that, if the RIC provides full disclosure of material information regarding the activities of its CFC through its obligations to the SEC, the CFC will not be required to separately prepare a Disclosure Document that complies with part 4 of the Commission's regulations. Moreover, provided that the RIC consolidates the financial statements of the CFC with those of the RIC in the financial statements that are filed by the RIC with the NFA, the CFC will not be required to file separate financial statements.[126] Given the foregoing, the Commission does not believe that additional relief pertaining to CFCs is necessary.

---

[123] SIFMA AMG Letter.

[124] See 2012 Final Rule, supra note 6, 77 FR at 11260

[125] See Items, 4, 9, and 16(b) of SEC form N-1A; and Item 8 and 17 of SEC form N-2.

[126] 17 CFR 4.22(c)(8).

C. Financial Reporting

a. Periodic Financial Statements

Section 4.22 requires that every CPO must periodically distribute to each participant in each pool that it operates an Account Statement in the form and with the content prescribed therein. Further, § 4.22(b) requires that Account Statements must be distributed at least monthly for pools with net assets greater than $500,000 and at least quarterly for all other pools.

The '40 Act requires open-end RICs to sell and redeem their shares based on the current net asset values of those shares,[127] and these net asset values may be posted on the RIC's website or otherwise made available to investors. RICs are also required to furnish semi-annual and annual reports, including financial statements, to investors, as well as to file quarterly schedules of portfolio holdings and semi-annual and annual reports, including financial statements, with the SEC (which are publicly available to investors via the EDGAR system).[128]

The Commission proposed to exempt the CPO of any RIC from the distribution requirements of § 4.22, provided the Account Statements are readily accessible on the RIC's website. The Commission also proposed to exempt such entities from the requirement under § 4.26(b) to attach the Account Statements to the Disclosure Document, again provided such materials are readily accessible on the RIC's website. The Commission did not propose to alter the requirement that Account Statements be distributed at least monthly.

Commenters generally appreciated the proposed relief under § 4.12(c) but requested a broader exemption from the requirements in § 4.22(a)-(b), which require monthly statements to be

[127] 15 U.S.C. 80a-22; 17 CFR 270.2a-4; 17 CFR 270.22c-1(a).

[128] See 17 CFR 270.30b1-5 (quarterly schedule of portfolio holdings on Form N-Q); 17 CFR 270.30b2-1 (semi-annual and annual reports on Form N-CSR); 17 CFR 270.30e-1 (semi-annual and annual reports to shareholders).

prepared and provided to participants.[129] Alternatively, others suggested that the Commission allow RICs to file quarterly statements, rather than monthly, as such a requirement is more in line with the SEC's requirements under the federal securities laws.[130] One commenter suggested that the Commission permit RICs to satisfy the requirements of § 4.22(a)-(b) by posting on its public website all reports to shareholders in compliance with and as required by SEC RIC Rules.[131] Some commenters noted that RIC investors have ready access to daily performance information, which, according to one commenter, achieves the "key purpose of the Account Statement" on a more current basis.[132] Some commenters noted that there are significant similarities between the publicly available disclosures required by the SEC and the information required in § 4.22, making the CFTC's requirement redundant.[133]

Several commenters contended that requiring Account Statements would create a substantial burden on RICs that would ultimately be passed on to shareholders without any corresponding benefit.[134] Another commenter was concerned that CPOs will now be required to create and maintain an online reporting regime to provide information that is already available to investors.[135] One commenter recommended that the Commission change the number of days that a CPO registered under § 4.7 has to prepare and distribute quarterly statements from 30 days to 45 days.[136]

---

[129] AXA Letter; SIFMA AMG Letter; ICI Letter; ABA Letter.

[130] NFA Letter; ABA Letter.

[131] Katten Letter.

[132] NFA Letter; SIFMA AMG Letter.

[133] Katten Letter; NYCBA Letter.

[134] SIFMA AMG Letter; NYCBA Letter; AXA Letter.

[135] AII Letter.

[136] MFA Letter.

The Commission has been persuaded by commenters and has concluded that providing relief to CPOs of RICs from the requirement to send monthly financial statements is appropriate, provided that the RIC's current net asset value per share is available to investors, and provided that the RIC furnishes semi-annual and annual reports to investors and files periodic reports with the SEC as required by the SEC. When current net asset value per share is available to investors, coupled with more detailed periodic reports as described above, the Commission believes that the decision not to require monthly statements would not reduce the transparency available to investors. Importantly, a fund investor could calculate his/her position in the fund using the current net asset value per share.

The Commission does not believe that its interest in ensuring that financial information is provided to pool participants is negatively impacted if such information is made available through the website of the RIC or its designee. This is consistent with § 4.1(c) of the Commission's regulations, wherein the Commission permits the distribution of information to participants through electronic means.[137] In accordance with the permitted use of electronic distribution, the Commission does not believe that electronic delivery meaningfully changes the information available to participants and may, in fact, make the information more readily accessible to participants and the public in general. The Commission also believes that such relief will eliminate the costs of preparing monthly financial statements and thereby eliminate any marginal impact on CPOs of RICs related to compliance with § 4.22.

[137] 17 CFR 4.1(c).

D. Books and Records

a. Location of Records

Sections 4.23 and 4.7(b)(4) require that all CPOs maintain full books and records at the main business office of the CPO. Such books and records must include the following: a detailed and itemized daily record of each commodity interest transaction of the pool; all receipts and disbursements of money, securities, and other property; a participant ledger; copies of each confirmation of a commodity interest transaction; and other relevant records.

The records of RICs are often maintained by third parties, such as administrators. Because of this, the Commission proposed extending the same type of relief currently available to ETFs through § 4.23 to RICs. The relief in § 4.23 allows maintenance of records at certain third party sites, such as those of an administrator or custodian.

Commenters suggested that the Commission extend the proposed relief to include not only RICs but all CPOs and CTAs, including private pools or funds; these commenters claimed such an extension would be more consistent with prevailing technologies, current market practices, and SEC requirements.[138] Commenters also suggested that the Commission remove the limitation on which entities are permitted to maintain books and records, because SEC rules permit a wider range of entities to do so.[139]

The Commission understands the current practice for RICs, as well as many other CPOs, to maintain their books and records with a third party vendor, or other such record-keeper, to be part of efficient management practices regarding such records.[140] Such practice allows the CPO to

[138] MFA Letter; IAA Letter.

[139] MFA Letter; IAA Letter; Dechert Letter; ICI Letter; SIFMA AMG Letter.

[140] See, 17 CFR 270.31a-3 (person maintaining required records on behalf of a RIC must agree that records are the property of the RIC).

avail itself of the lower cost and increased record security of a third party vendor, as such vendors often specialize in such services. The Commission acknowledges that its requirement to keep such books and records at the main business address of a CPO is rooted in the timely and certain access of that data. However, to the extent that such data is readily accessible to a CPO, the Commission believes that the requirement that such data be maintained at the main business address of a CPO is similarly met so long as timely and complete access to that data is available. Further, as suggested by the comments, the Commission believes that the advantages of such recordkeeping practices are applicable to all CPOs. Accordingly, the Commission has determined that so long as at the time that such CPO registers with the Commission, or delegates its recordkeeping obligations, whichever is later, the CPO files a statement with the Commission describing the delegated record keeper, and maintains timely access to those records in such manner as set forth by the Commission, that CPO will be permitted to utilize the services of third-parties with respect to the maintenance of books and records.

b. Other Recordkeeping Obligations

Section 4.23 also requires that a CPO's books and records be made available to participants for inspection and/or copying at the request of the participant.[141] The Commission did not propose altering this requirement. The SEC does not have a comparable requirement. Indeed, disclosure of non-public information to some, but not all, participants is prohibited where

[141] Certain confidential or proprietary information, including participants' personal information and subscription information as well as the records of the CPO's personal investments, are not required to be made available for inspection by pool participants.

inconsistent with the antifraud provisions of the federal securities laws and the fund's or adviser's fiduciary duties ("selective disclosure").[142]

Additionally, § 4.23(a)(4) requires a ledger (or other record) to be kept for each participant in the pool that shows the participant's name, address, and all funds received from or distributed to the participant.

One commenter noted that the investor access provision is inconsistent with SEC regulations, which the commenter claimed are sufficient to provide investors with information.[143] Some commenters suggested the Commission exempt RICs from the requirement to make available a CPO's books and records at the request of an investor.[144] These commenters noted the possibility of investors accessing trading and position information to use in trading against the pool/fund, leading to unfair competition and front-running.

Commenters were concerned with the ledger requirement in § 4.23(a)(4) because they noted that most shares are held in omnibus accounts or through intermediaries and that transfer agents typically keep records of investors.[145] These commenters requested clarification that a transfer agent's maintenance of records and/or a list of relevant intermediaries would be deemed to satisfy the information requirements regarding pool participants under § 4.23(a)(4).

The Commission recognizes the concerns that, if a participant were to inspect such books and records of a pool, SEC requirements may then compel the pool to publicly disclose such information to avoid prohibitions against selective disclosure. Even in the absence of wide

[142] See SEC Regulation FD (17 CFR 243.100-103) (with respect to closed-end RICs); Items 9(d) and 16(f) of SEC form N-1A (open-end RICs required to disclose policies and procedures with respect to disclosure of portfolio securities and ongoing arrangements to make available information about portfolio securities.

[143] ABA Letter.

[144] Katten Letter; ABA Letter; ICI Letter; AII Letter.

[145] Dechert Letter; Katten Letter; SIFMA AMG Letter.

disclosure of such positions, which would at a minimum require substantial effort to compile and distribute such information to all fund participants at unplanned intervals, disclosure of transaction level data on a real time or near real-time basis to even a single participant may make such a pool vulnerable to front-running or market manipulation. Accordingly, to remove these risks, a registered CPO that operates a RIC will not be required to make its records available for inspection and copying.

The Commission recognizes that the practice of many RICs to hold account shares in an omnibus account, with such records of participant information being kept by a transfer agent or financial intermediary, such as a broker-dealer or bank, would make the requirement that the CPO keep custody of such records both duplicative and unduly burdensome on the CPO of a RIC. Because a subsidiary ledger of largely the form and substance required by the Commission is kept by those transfer agents and financial intermediaries, the Commission agrees that in such instances, the maintenance of these records by a transfer agent or financial intermediary, in such form that complies with that as set forth by the Commission, shall satisfy the requirement of § 4.23(a)(4).

The Commission has also determined to amend § 4.23 to permit all CPOs to use third-party service providers to maintain their books and records. The Commission believes that expansion of the relief previously limited to exchange traded funds appropriately recognizes technological advances in recordkeeping and the ability to make books and records readily available to regulatory agencies. The Commission will continue to require CPOs of RICs to file with the NFA (1) a notice providing information about the third-party service provider, and (2) a statement from the service provider agreeing to maintain the pool's books and records consistent with the Commission's regulations. This requirement is identical to the notices previously

required under § 4.12(c)(iii). Therefore, the Commission is adopting final amendments to § 4.23 permitting all registered CPOs to use third party service providers to maintain their books and records.

E. Broader Applicability

The Commission proposed harmonization of compliance obligations for CPOs of RICs only. The Commission did not propose extending relief to other CPOs or other SEC-registered entities, such as investment advisers to private funds. However, the Commission did request comment on whether it should consider applying any of the harmonization provisions to operators of pools that are not RICs.

One commenter supported the Commission's proposal to amend § 4.12(c) to extend relief to RICs similar to the relief granted to ETFs, as well as the Commission's proposal to extend the same relief to operators of all publicly offered pools, regardless of whether they are traded on a securities exchange.[146] Several commenters requested the Commission extend relief under 4.12(c) to privately offered pools.[147]

The Commission believes that publicly offered pools that are not traded on an exchange should be afforded the same relief as ETFs. Both are subject to regulation under the Securities Act, and therefore, required to comply with certain disclosure and reporting obligations. Accordingly, the Commission adopts as final the proposed extension of relief under § 4.12(c) to all publicly offered pools, regardless of whether such pools are traded on an exchange.

[146] NFA Letter.

[147] MFA Letter; IAA Letter; SIFMA AMG Letter; Campbell Letter; Steben Letter.

Unlike publicly offered pools, privately offered pools avail themselves of an exemption from registration under the Securities Act.[148] Ownership interests in privately offered pools are not subject to the same types of regulatory obligations under the securities laws as publicly offered pools. As a result, CPOs of privately offered pools are not subject to the prospect of being required to comply with two different compliance regimes. Therefore, the Commission will not extend the full scope of the exemptions provided under § 4.12(c) to all CPOs. However, the Commission has determined to liberalize the third party recordkeeping and document distribution requirements under part 4 of the Commission's regulations, as discussed supra, for all CPOs.

With respect to the specific compliance obligations under part 4, one commenter requested that the Commission extend the relief from the Disclosure Document delivery and acknowledgment requirements in § 4.21 to any CPO of a private pool/fund, so long as the pool/fund has an investment advisor registered with the SEC and is either registered under § 4.7 or would have been exempt under rescinded § 4.13(a)(4). [149] The commenter noted that because the participants in these private pools would be sophisticated investors, the Commission should not deny these pools the same relief granted to CPOs of RICs, whose investors are less sophisticated retail investors.[150]

The Commission has determined to rescind the signed acknowledgement requirement under § 4.21(b) for all registered CPOs. Through its expansion of § 4.12(c) to exempt all publicly offered funds, the Commission has recognized that publicly offered pools that are not exchange

[148] See, e.g., 17 CFR 230.501 ("Reg. D); 15 USC 77d ("Section 4(2)").

[149] Commission Regulation 4.7 and former Regulation 4.13(a)(4) provide for an exemption of certain Part 4 requirements, or an exemption from registration as a CPO, respectively, for, among other things, operating a pool of which all the participants therein are qualified eligible persons. 17 CFR 4.7 and 17 CFR 4.13(a)(4). See 2012 Final Rule, supra note 6, 77 FR 11252 (Feb. 24, 2012); correction 77 FR 17328 (March 26, 2012).

[150] SIFMA AMG Letter.

traded are similarly situated with respect to the requirements under § 4.21 as ETFs. The Commission believes that because participants in privately offered pools are not retail participants but are sophisticated persons, the concerns underlying the signed-acknowledgment requirement are not present. Moreover, the elimination of this requirement would align the Commission's requirements regarding the offering of ownership interests in commodity pools with the requirements imposed on the offerings of interests in other types of funds. Therefore, the Commission is rescinding the signed acknowledgement requirement under § 4.21(b) for all CPOs.

One commenter requested that the Commission amend § 4.7(b) and § 4.13(a)(3)[151] in response to the Jumpstart Our Business Startups Act ("JOBS Act"), which eliminates the prohibition on general solicitation in connection with private funds.[152] The JOBS Act amends certain sections of the Securities Act, but does not change similar provisions in the CEA or under part 4 of the Commission's regulations. The commenter contended that this disparity will create a situation in which private funds may market to the public but private pools may not.

The Commission recognizes that there may be some disparity between the treatment of privately offered funds under the securities laws and the Commission's regulations; however, this issue was not included in the Proposal and was not subject to notice and comment. Therefore, the Commission does not believe that this final rule is the appropriate mechanism for addressing the difference between the two regimes. The Commission has directed Commission staff to evaluate the issue and make recommendations to the Commission for future action.

[151] See supra footnote 149.

[152] Comment letter from Managed Futures Association (July 17, 2012) (MFA II Letter).

F. Effective Dates and Implementation

The harmonized compliance obligations for CPOs of RICs under § 4.12, except for § 4.12(c)(3)(i), will become effective upon publication in the Federal Register. Section 4.12(c)(3)(i) will become effective 30 days after publication in the Federal Register. Compliance will be required with the conditions adopted herein in § 4.12(c)(3)(i) for open-end RICs beginning when a RIC files with the SEC an initial registration statement on form N-1A or, for an existing RIC, its first post-effective amendment that is an annual update to an effective registration statement on form N-1A. For CPOs of closed-end RICs, compliance will be required when the closed-end RIC files an initial registration statement with the SEC, or, for existing closed-end RICs, when the closed-end RIC is required to update its registration statement. Consistent with the Commission's statements in the 2012 Final Rule, CPOs of RICs must begin to comply with § 4.27, which implements Commission forms CPO-PQR and CTA-PR, 60 days following the effective date of this rulemaking.[153] Accordingly, initial reporting on forms CPO-PQR for CPOs of RICs will begin [INSERT DATE THAT IS 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER].[154] Section 4.21 will become effective upon publication in the Federal Register. With respect to the amendments to §§ 4.7(b)(4), 4.23, 4.26, and 4.36 that are applicable to all registered CPOs, these amendments will become effective 30 days after publication in the Federal Register and CPOs may comply upon the effective date.

[153] See 2012 Final Rule, supra note 6, 77 FR 11252 (Feb. 24, 2012); correction 77 FR 17328 (March 26, 2012).

[154] The instructions for form CPO-PQR specify different dates by which CPOs must file the form, depending on the amount of assets under management by the pool operator. 77 FR at 11288. CTAs must file form CTA-PR annually. 77 FR at 11339.

III. Related Matters

A. Paperwork Reduction Act

The Paperwork Reduction Act ("PRA") imposes certain requirements on Federal agencies in connection with their conducting or sponsoring any collection of information as defined by the PRA.[155] An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number from the Office of Management and Budget ("OMB"). This final release affects OMB Control Numbers 3038-0023 and 3038-0005 to reflect the obligations associated with the registration of new CPOs that were previously excluded from registration under § 4.5. Specifically, this final release is amending Collection 3038-0005 to accommodate the modified compliance obligations under part 4 of the Commission's regulations.

a. Estimated Number of Affected Entities

In the Proposal, the Commission derived the number of estimated entities affected and the number of burden hours associated with this proposal through the use of statistical analysis. According to the single and limited source of data available to the Commission, in 2010, there were 669 sponsors of 9,719 registered investment companies, including mutual funds, closed end funds, exchange traded funds, and unit investment trusts.[156] In the comment letter submitted by the Investment Company Institute ("ICI") in response to the Commission's proposed amendments to § 4.5, the ICI stated that it surveyed its membership and 13 sponsors responded representing 2,111 registered investment companies. Of those 2,111 registered investment companies, the 13

[155] See 44 U.S.C. 3501 et seq.

[156] See 2011 Investment Company Fact Book, Chap. 1 and Data Tables, Investment Company Institute (2011), available at http://www.icifactbook.org/.

sponsors estimated that 485 would trigger registration and compliance obligations under § 4.5 as amended. This constituted approximately 23% of the reported registered investment companies.

The Commission then deducted the 2,111 registered investment companies discussed in the ICI comment letter from the 9,719 entities comprising the universe of registered investment companies, and deducted the 13 sponsors surveyed by the ICI from the universe of 669 fund sponsors to arrive at a balance of 656 fund sponsors operating 7,608 registered investment companies. This resulted, for the calculated remainder, in an average of 11.6 registered investment companies being offered per sponsor.

The Commission then calculated 23% of the 7,608 registered investment companies not covered by the ICI survey, resulting in 1,750 additional registered investment companies that the Commission would expect to trigger registration under amended § 4.5. The Commission then divided this number by the previously calculated average number of registered investment companies operated per sponsor to which it added the 13 sponsors from the ICI survey to reach 164 sponsors expected to be required to register under amended § 4.5. Because the Commission could not state with certainty that only 164 entities would be required to register the Commission indicated that the number of sponsors or advisors required to register were somewhere between 164 and 669 entities. For PRA purposes, the Commission concluded that it was appropriate to use the midpoint between the outer bounds of the range, which was 416 entities.

Pursuant to the request for comments on the Proposal, the Investment Company Institute ("ICI") submitted a comment letter in response which provided additional and differing information that it obtained through a further survey of its membership.[157] In its letter, the ICI

[157] ICI Letter.

stated that in its return, 42 advisers reported operating 4,188 funds, which constituted 43 percent of the universe of RICs.[158] Therefore, the total universe of RICs can be calculated to equal 9,740.

The ICI further stated that of these 42 advisers, 33 stated that they operated 551 funds that would trigger registration.[159] Therefore, according to the ICI's data, 13 percent of the surveyed funds would trigger registration of their operators.[160] Applying this percentage to the total universe of RICs less the 4188 surveyed RICs, results in an estimated 5552 non-surveyed RICs and an estimated total of 722 non-surveyed RICs with operators required to register.[161] The total number of surveyed and non-surveyed RICs with operators required to register is approximately 1,266.[162]

As stated above, the ICI also noted that 33 advisers would be required to register as CPOs due to the activities of 551 RICs.[163] According to the 2012 ICI Fact Book, there were 713 advisers to RICs in 2011.[164] The Commission deducted the 42 surveyed advisers from the total universe of 713 advisers to find a total of 671 non-surveyed advisers. When the Commission compared the number of non-surveyed RICs with the number of non-surveyed advisers, the Commission determined that each adviser advises an average of 8 RICs. The Commission then applied the average of 8 RICs per adviser to the 722 estimated number of non-surveyed RICs required to register, and obtained an estimate of 90 non-surveyed advisers being required to register. The Commission then added the 33 surveyed advisers to its estimate, and determined

---

[158] Id.

[159] Id.

[160] Percentage obtained by dividing 551 by 4,188 surveyed RICs.

[161] Total of non-surveyed RICs subject to registration obtained by multiplying 5552 non-surveyed RICs by .13

[162] Total obtained by multiplying 9740 by .13.

[163] ICI Letter.

[164] See 2012 Investment Company Fact Book at 13, available at http://www.icifactbook.org/2012_factbook.pdf.

that an estimated 123 advisers may be required to register. Because the Commission cannot state with certainty that only 123 entities would be required to register, the Commission believes that the number of sponsors or advisors required to register to be somewhere between 123 and 713 entities, the midpoint of which is 418 entities.

b. OMB Control Number 3038-0023

On February 24, 2012, the Commission finalized amendments to Collection 3038-0023, titled "Part 3 – Registration," to allow for an increase in response hours for the rulemaking resulting from the amendments to § 4.5 that the Commission recently adopted.[165] Collection 3038-0023 affects part 3 of the Commission's regulations that concern registration requirements. The Commission amended existing Collection 3038-0023 to reflect the obligations associated with the registration of new entrants, i.e., CPOs that were previously exempt from registration under § 4.5 that had not previously been required to register.[166] Because the registration requirements are in all respects the same as for current registrants, the collection was amended only insofar as it concerns the estimated increase in the number of respondents and the corresponding estimated annual burden. These burdens were associated with the 2012 Final Rule amending § 4.5, which was published in the Federal Register on February 24, 2012. Responses to this collection of information are mandatory. The total burden associated with registration including the registration of operators of RICs was as follows:

Estimated number of respondents: 75,425.

Annual responses by each respondent: 75,932.

Estimated average hours per response: 0.09.

[165] See 2012 Final Rule, supra note 6, 77 FR at 11272.

[166] See 2012 Final Rule, supra note 6, 77 FR at 11273.

Annual reporting burden: 6,833.9.

In the Proposal, the Commission published a proposed amendment to Collection 3038-0023 that inadvertently reflected an additional amendment to the collection arising from the registration of additional CPOs that were previously excluded from the definition of CPO under § 4.5.[167] As stated above, the Commission amended existing Collection 3038-0023 in the 2012 Final Rule to reflect the obligations associated with the registration of new CPOs that were previously excluded from registration under § 4.5. Thus, these entities were already included in the Commission's final amendment to Collection 3038-0023 associated with the 2012 Final Rule, and therefore, the additional amendments to Collection 3038-0023 in the Proposal resulted in those entities being erroneously double counted. Accordingly, the burden hours previously estimated for Collection 3038-0023 in the 2012 Final Rule that amended § 4.5 and the estimates for this collection remain unchanged from the 2012 Final Rule.

c. OMB Control Number 3038-0005

Also, on February 24, 2012, the 2012 Final Rule amended Collection 3038-0005 to allow for an increase in response hours for the rulemaking resulting from the amendments to § 4.5.[168] Collection 3038-0005 affects part 4 of the Commission's regulations that concern compliance obligations of CPOs and CTAs, and the circumstances under which they may be exempted or excluded from registration. The estimated average time spent per response was not altered in the 2012 Final Rule; however, adjustments were made to the collection to account for the new burden expected under the rulemaking. The total burden associated with Collection 3038-0005, in the aggregate, was as follows:

[167] See Proposal, supra note 23, 77 FR at 1349. The Proposal stated that there were 75,841 estimated number of respondents, 76,350 annual responses by each respondent and 6,871.6 annual reporting burden.

[168] See 2012 Final Rule, supra note 6, 77 FR at 11272.

Estimated number of respondents: 43,168.

Annual responses for all respondents: 61,868.

Estimated average hours per response: 8.77.

Annual reporting burden: 257,635.8.

In the Proposal, the Commission proposed changes to part 4 that were designed to better harmonize the Commission's compliance obligations for CPOs and minimize the burden imposed on those dually-regulated by the Commission and the SEC while still enabling the Commission to fulfill its regulatory goals.[169] The Proposal was designed to, where possible, minimize the regulatory burden on these entities with respect to disclosure, annual and periodic reporting to participants and the Commission, recordkeeping requirements, and ensure that requirements among the SEC and CFTC did not conflict such that compliance with one regime would cause a violation of another. With respect to the PRA, the Proposal increased the number of estimated entities that would be subject to the compliance obligations of CPOs and CTAs,[170] which are part of Collection 3038-0005.[171] The Proposal specifically added the following burden with respect to compliance obligations other than Form CPO–PQR:

Estimated number of respondents: 416.

Annual responses by each respondent: 5.

---

[169] The Commission issued its proposal under the authority of §§ 4m, 4n, and 8a(5) of the CEA. 7 U.S.C. 6m, 6n, and 12a(5).

[170] See Proposal, supra note 23, 77 FR at 11349, finding that 416 entities would be required to register under amended § 4.5.

[171] See Proposal, supra note 23, 77 FR at 11349, which, to account for the increased number of entities, proposed that the total burden associated with Collection 3038-0005, in the aggregate, including the burden imposed by regulations that were not proposed to be amended by that rulemaking, was expected to be, as follows:

Estimated number of respondents: 44,142.

Annual responses by each respondent: 62,121.

Estimated average hours per response: 4.22.

Annual reporting burden: 262,347.8.

Estimated average hours per response: 2.

Annual reporting burden: 4160.

As further discussed below, the Commission in this final release is amending Collection 3038-0005 to accommodate the modified compliance obligations under part 4 of the Commission's regulations resulting from these revisions. The title for this collection is "Part 4 – Commodity Pool Operators and Commodity Trading Advisors" (OMB Control number 3038-0005). Responses to this collection of information will be mandatory. The new total burden associated with Collection 3038-0005, in the aggregate, including the burden imposed by regulations that are not being amended by this rulemaking, is as follows:

Estimated number of respondents: 49,008.

Annual responses for all respondents: 69,382.

Estimated average hours per response: 3.99.[172]

Annual reporting burden: 276,540.3.[173]

The new total burden associated with Collection 3038-0005, as a result of the amendments adopted in this rulemaking, is as follows:

Estimated number of respondents: 5,894.

Annual responses for all respondents: 7,694.

Estimated average hours per response: 2.66.[174]

Annual reporting burden: 20,464.5

[172]The Commission rounded the average hours per response to the second decimal place for ease of presentation.

[173] This total estimate for Collection 3038-0005, in the aggregate, has been increased from the Proposal to accurately reflect the average under Collection 3038-0005. While the total annual reporting burden has increased, the total annual reporting burden reflects the decreased burden associated with the preparation of Disclosure Documents by CPOs under the amendments to §§ 4.26 and 4.36.

[174] The Commission rounded the average hours per response to the second decimal place for ease of presentation.

The Commission will protect proprietary information according to the Freedom of Information Act ("FOIA") and 17 CFR part 145, "Commission Records and Information." In addition, section 8(a)(1) of the CEA strictly prohibits the Commission, unless specifically authorized by the CEA, from making public "data and information that would separately disclose the business transactions or market position of any person and trade secrets or names of customers."[175] The Commission is also required to protect certain information contained in a government system of records according to the Privacy Act of 1974.[176]

d. Changes Resulting from Harmonization and Additional Information Provided by CPOs and CTAs

1. OMB Control Number 3038-0023.

This rule does not impact the burden hours previously estimated for Collection 3038-0023 in the 2012 Final Rule that amended § 4.5 and the estimates for this collection have not been changed by this rule.

2. OMB Control Number 3038-0005

The Commission is amending Collection 3038-0005 to increase the estimated total number of respondents, total annual responses for all respondents, and annual reporting burden from the estimates that appeared in the Proposal. These amendments are in response to comments that the Commission received regarding the burdens imposed by the Proposal and also reflect the differences between the Proposal and the final rule. Thus, the new total burden in the 2012 Final Rule associated with Collection 3038-0005, listed in the aggregate above, has increased to account

[175] See 7 U.S.C. 12.

[176] See 5 U.S.C. 552a.

for the burdens associated with the various information collections in this final rule, as discussed below.

i. Amendments to Timeframe for Updating Disclosure Documents

In this release, the Commission is finalizing the collection of information regarding the frequency with which CPOs and CTAs must update their Disclosure Documents under §§ 4.26 and 4.36, respectively. While the total annual reporting burden has increased to account for the total annual reporting by CPOs for the various information collections in this final release, the Commission believes that the amendments to §§ 4.26 and 4.36 will result in a reduction of the burden on CPOs and CTAs. [177] The Commission estimates the burden associated with the amendments to §§ 4.26 and 4.36 to be as follows:

Section 4.26:

Estimated number of respondents: 160.

Annual responses by each respondent: 1.8.

Estimated average hours per response: 3.25

Total Annual reporting burden hours: 936.

Section 4.36:

Estimated number of respondents: 450.

Annual responses by each respondent: 1.

Estimated average hours per response: 1.85.

Total Annual reporting burden hours: 832.5.

[177] To facilitate compliance with part 4 requirements for CPOs of RICs, the Commission amended § 4.26 and § 4.36 to extend the period that CPOs and CTAs may use Disclosure Documents from nine months to twelve months from the date of the document. Section 4.26(a)(2) in this final release now provides that no commodity pool operator may use a Disclosure Document or profile document dated more than twelve months prior to the date of its use. Section 4.36 (b) provides that no commodity trading advisor may use a Disclosure Document dated more than twelve months prior to the date of its use.

ii. Past Performance for Pools with Less than Three Years Performance

The Commission is adopting a rule in § 4.12(c) of this release that would require operators of RICs with less than three years performance history to disclose the performance of all pools and accounts that are managed by the CPO and that have investment objectives, policies, and strategies substantially similar to those of the offered pool.[178] Not all RICs will fall into this category and therefore, not all RICs will be subject to this disclosure requirement.

Based on information provided by the ICI in its comment letter, of the 551 RICs in the survey that would trigger registration of their advisor, 159 of those RICs had less than three years operating history.[179] This constitutes approximately 30 percent of the RICs in the survey whose CPOs would not be excluded under § 4.5. The RICs with less than three years operating history that would require registration in the ICI survey were operated by 29 of the 33 advisers that expected to register, which constitutes 88 percent of the surveyed sponsors expecting to register. Applying these percentages to the Commission's estimated number of 418 sponsors required to register, the Commission expects approximately 368 pool operators to be subject to the disclosure requirements for substantially similar accounts and funds with respect to 380 pools. The Commission is not aware of any source of data to assist it in estimating the number of operators of RICs with substantially similar pools or accounts or to assist in estimating the number of those substantially similar pools or accounts that do not independently have regulatory obligations requiring the preparation of past performance data. To be conservative, therefore, the

[178] Section 4.12(c)(3)(i) states that "The commodity pool operator of a pool whose units of participation meet the criteria of paragraph (c)(1)(ii) of this section may claim the following relief: (i) The pool operator of an offered pool will be exempt from the requirements of §§ 4.21, 4.24, 4.25, and 4.26; *Provided, that* (A) The pool operator of an offered pool with less than a three-year operating history discloses the performance of all accounts and pools that are managed by the same pool operator and that have investment objectives, policies, and strategies substantially similar to those of the offered pool;…."

[179] ICI Letter.

Commission will assume that all operators of RICs with less than three years operating history will have multiple pools or accounts that are substantially similar in all material respects and that such substantially similar pools or accounts do not have separate compliance obligations requiring preparation of past performance information.

The ICI, in its comment letter, estimated that costs associated with prior performance disclosure required under the Proposal for funds with less than a three year operating history would amount to 34 hours per fund initially, and 25.5 hours per fund each year in ongoing compliance requirements.[180] The ICI's estimates are based on the requirement in the Proposal to include past performance information for all other funds operated by the sponsor of the fund with less than a three year operating history. As noted supra, the Commission has altered this provision to require disclosure of only those funds and accounts that are substantially similar in all material respects to the fund with less than a three year operating history. In so doing, the Commission believes that it has significantly reduced the requirements regarding past performance disclosure. As such, the Commission believes it can reasonably reduce the number of hours required both initially and in ongoing compliance. The Commission anticipates initial and ongoing cost of approximately 15 hours per fund.[181] The Commission believes that 15 hours is a reasonable estimate for the preparation of past performance information for a substantially similar pool or account. The total burden associated with the past performance assessment and disclosure is:

Estimated number of respondents: 368.

Annual responses by each respondent: 1.

[180] ICI Letter.

[181] The burden estimate assumes that all RICs with less than three years performance are newly formed and have no performance history, whereas some of these RICs likely have anywhere from no past performance to just less than three full years. Therefore, the Commission believes that this calculation overestimates the ongoing burden to these CPOs.

Estimated average hours per response: 15.

Total Annual reporting burden hours: 5,520.

iii. Notice to Claim Substituted Compliance

This final rule requires a notice to be filed for operators of RICs to claim relief under revised § 4.12(d) to enable the Commission to know which entities are claiming this relief.[182] The notice is effective upon submission and must only be filed once per pool. The Commission estimates the burden associated with this filing to be as follows:

Estimated number of respondents: 418.

Annual responses by each respondent: 3.

Estimated average hours per response: 2.

Total Annual reporting burden hours: 2,508.

The Commission does not believe that the requirement that operators of RICs discuss the risks associated with the derivative activities of the operated pools as adopted by this final rule imposes a burden beyond that already imposed by the Securities and Exchange Commission through SEC forms N-1A and N-2.[183]

iv. Filing Annual Financial Statements by CPOs of RICs

The final rule requires that operators of RICs file annual financial statements with the NFA, pursuant to the terms of § 4.22(c),[184] which is applicable to all CPOs. It permits operators of RICs to file the same financial statements that it prepares for its compliance obligations with the SEC. The Commission anticipates that the additional requirement imposed by the rule in §

[182] Section4.12(d)(1)(iv) requires pool operators to specify the relief sought under paragraph (b)(2), (c)(2), or (c)(3) of this section, as the case may be.

[183] See Items, 4, 9, and 16(b) of Form N-1A; and Item 8 and 17 of Form N-2.

[184] Section 4.22(c) has not been amended by this rule. The information collection is being amended only to reflect the increase in the numbers of new CPOs registering.

4.22(c) necessitates only addressing any potential formatting changes—i.e. making sure the document is in PDF form as required by NFA—and uploading the document via NFA's Easy File system (to which advisers should already have access by virtue of their registration). Thus, the Commission anticipates at most 2 hours per fund per sponsor. With respect to the filing of annual financial statements by operators of RICs with the NFA, the Commission estimates the burden to be as follows:

Estimated number of respondents: 418.

Annual responses by each respondent: 3.

Estimated average hours per response: 2.

Total Annual reporting burden hours: 2,508.

v. Notice of Use of Third-Party Record Keepers

The final rule adopts amendments to §§ 4.7(b)(4) and 4.23 to permit the use of third-party recordkeepers by any CPO that files a notice with NFA. The estimated number of respondents is derived from the estimates finalized as part of the 2012 Final Rule adopting amendments to § 4.5 and §4.13, and reflects the additional registrants expected due to the changes in those rules. Because the Commission cannot be sure how many CPOs will use third-party service providers, the Commission estimates that all CPOs will take advantage of the amendments to the record-keeping requirements under § 4.23 and § 4.7.[185] With respect to the filing of the notice under revised § 4.23 to permit the use of third-party recordkeepers, the Commission estimates the burden to be as follows:

[185] The Commission has previously estimated that each CPO that subject to § 4.23 had a burden of approximately 50 hours associated with recordkeeping obligations and that each CPO subject to § 4.7(b)(4) had a burden of approximately 40 hours associated with recordkeeping obligations. Because the Commission is estimating that all registered CPOs will use third-party service providers for recordkeeping purposes, the Commission expects that burdens associated with §§ 4.7(b)(4) and 4.23 will be reduced, although the reduction cannot be quantified at this time.

For CPOs of RICs subject to § 4.23:

Estimated number of respondents: 418.

Annual responses by each respondent: 1.

Estimated average hours per response: 2.

Total Annual reporting burden: 836.

For all other CPOs subject to § 4.23:

Estimated number of respondents: 160.

Annual responses by each respondent: 1.

Estimated average hours per response: 2.

Total Annual reporting burden: 320.

With respect to the filing of the notice under revised § 4.7(b)(4) to permit the use of third-party recordkeepers, the Commission estimates the burden to be as follows:

Estimated number of respondents: 3,502.

Annual responses by each respondent: 1.

Estimated average hours per response: 2.

Total Annual reporting burden: 7,004.

vi. Compliance with Form CPO-PQR by CPOs of RICs

CPOs of RICs were not required to comply with its filing obligations under § 4.27 or file form CPO-PQR until the finalization of this rulemaking. The reporting obligations for CPOs of RICs with respect to form CPO-PQR under the PRA and the costs and benefits were addressed in the 2012 Final Rule,[186] and restated in the Proposal only for informational purposes.[187] To the

[186] See 2012 Final Rule, supra note 6, 77 FR at 11273.

[187] See Proposal, supra note 23, 77 FR at 11349.

extent that this rule does not impact the burden hours previously estimated in the 2012 Final Rule for Form CPO-PQR, the estimates for Collection 3038-0005 associated with form CPO-PQR have not been changed by this rule.

B. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA)[188] requires that agencies, in proposing rules, consider the impact of those rules on small entities. The Commission has previously established certain definitions of "small entities" to be used by the Commission in evaluating the impact of its rules on such entities in accordance with the RFA.[189]

CPOs: The Commission has previously determined that registered CPOs are not small entities for the purpose of the RFA.[190] With respect to CPOs exempt from registration, the Commission has determined that a CPO is a small entity if it meets the criteria for exemption from registration under current § 4.13(a)(2).[191] Based on the requisite level of sophistication needed to comply with the SEC's regulatory regime for registered investment companies, and the fact that registered investment companies are generally intended to serve as retail investment vehicles and do not qualify for exemption under § 4.13(a)(2), the Commission believes that registered investment companies are generally not small entities for purposes of the RFA analysis. Moreover, this final rule will reduce the burden of complying with part 4 for CPOs of registered investment companies. The Commission has determined that the final rule will not create a significant economic impact on a substantial number of small entities.

---

[188] See 5 U.S.C. 601, et seq.

[189] 47 FR 18618 (Apr. 30, 1982).

[190] See 47 FR 18618, 18619 (Apr. 30, 1982).

[191] See 47 FR at 18619-20.

CTAs: The Commission has previously decided to evaluate, within the context of a particular rule proposal, whether all or some CTAs should be considered to be small entities, and if so, to analyze the economic impact on them of any such rule.[192] The sole aspect of the final rule that affects CTAs that are registered with the Commission is the timeframe that permits Disclosure Documents to be used for 12 months rather than 9 months, thereby reducing the frequency with which updates must be prepared. While the Commission considers the reduced frequency with which these CTAs must prepare updates to their Disclosure Documents as reducing the overall burden on affected entities, it is of the view of the Commission that the reduction in updates mitigates the rule's economic impact. Over the course of three calendar years, the change from a 9 month update period to a 12 month update period eliminates 1 filing per CTA. This results in a change from 1.33 filings per year to 1 filing per year. In addition, because the eliminated filing would be an update of a document that was already prepared and reviewed by NFA, the Commission does not believe that the eliminated filing would result in a significant economic impact. As indicated above, it would reduce any impact that the rule would otherwise have. Moreover, the amended time period for updating Disclosure Documents for CTAs also aligns this requirement with other regulatory obligations that registered CTAs must comply with, including the filing of form CTA-PR pursuant to § 4.27 of the Commission's regulations.[193] The Commission believes that this will enable registered CTAs to avail themselves of operational efficiencies in satisfying its regulatory obligations as the information required under form CTA-PR is relevant to the preparation or updating of Disclosure Documents. Therefore, the Commission has determined that the final rule will not create a significant economic impact on a

[192] See 47 FR at 18620.

[193] 17 CFR 4.27.

substantial number of small entities. Accordingly, the Chairman, on behalf of the Commission hereby certifies pursuant to 5 U.S.C. 605(b) that the final rule will not have a significant impact on a substantial number of small entities.

C. Cost Benefit Analysis

a. Consideration of Costs and Benefits

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the Act or issuing certain orders.[194] Section 15(a) further specifies that the costs and benefits shall be evaluated in light of the following five broad areas of market and public concern: (1) protection of market participants and the public; (2) efficiency, competitiveness and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations.[195]

Generally, the Commission believes that, by avoiding the imposition of potentially duplicative, inconsistent, or conflicting regulatory requirements on CPOs of RICs subject to federal securities laws and SEC rules, the final harmonization rule should generate important benefits while mitigating the costs on market participants.

In the following discussion, the Commission summarizes the key aspects of the final rule, and considers the benefits and costs, taking account of public comments received in response to the Proposal and the February Final Rule regarding harmonizing the compliance regime of the

[194] 7 U.S.C. 19(a).

[195] 7 U.S.C. 19(a)(2).

Commission with that of the SEC. The Commission then evaluates the final rule in light of the aforementioned § 15(a) public interest considerations.[196]

1. Background

In February 2012, the Commission adopted modifications to the exclusions from the definition of CPO that are delineated in § 4.5.[197] Specifically, the Commission amended § 4.5 to modify the exclusion from the definition of "commodity pool operator" for those entities that are investment companies registered as such with the SEC pursuant to the '40 Act.[198] This modification amended the terms of the exclusion available to CPOs of RICs to include only those CPOs of RICs that commit no more than a de minimis portion of their assets to the trading of commodity interests that do not fall within the definition of bona fide hedging and who do not market themselves as a commodity pool or other commodity investment.[199] Pursuant to this amendment, any such CPO of a RIC that exceeds this level will no longer be excluded from the definition of CPO. Accordingly, except for those CPOs of RICs who commit no more than a de minimis portion of their assets to the trading of commodity interests that do not fall within the definition of bona fide hedging and who do not market themselves as a commodity pool or other commodity investment, an operator of a RIC that meets the definition of "commodity pool

[196] The discussion of costs and benefits in this section should be read in conjunction with the discussion of the effects of the rule and the choices made by the Commission in the remainder of this preamble, all of which entered into the Commission's consideration of costs and benefits in connection with its decision to promulgate this rule.

[197] 17 CFR 4.5. See 2012 Final Rule, supra note 6, 77 FR 11252 (Feb. 24, 2012); correction 77 FR 17328 (March 26, 2012). Prior to this Amendment, all RICs, and the principals and employees thereof, were excluded from the definition of "commodity pool operator," by virtue of the RICs registration under the Investment Company Act of 1940. The 2012 amendment to § 4.5 maintained this exclusion for those RICs that engage in a de minimis amount of non-bona fide hedging commodity interest transactions. See id. Specifically, the amendment to § 4.5 retained this exclusion for RICs whose non-bona fide hedging commodity interest transactions require aggregate initial margin and premiums that do not exceed five percent of the liquidation value of the qualifying pool's portfolio, or whose non-bona fide hedging commodity interest transactions' aggregate net notional value does not exceed 100 percent of the liquidation value of the pool's portfolio.

[198] 15 U.S.C. 80a-1, et seq.

[199] 17 CFR 1.3(yy).

operator" under § 4.10(d) of the Commission's regulations and § 1a(11) of the CEA must register as such with the Commission.[200]

In promulgating the revisions to § 4.5, the Commission received numerous comments that operators of RICs that also would be required to register as CPOs would be subject to duplicative, inconsistent, and possibly conflicting disclosure and reporting obligations. The Commission determined, after consideration of the comments received, that further consideration was warranted concerning whether and to what extent CPOs of RICs ought to be subject to various part 4 requirements, and in the 2012 Final Rule suspended the obligations of CPOs of RICs with respect to most of the requirements of part 4 until further rulemaking.[201] Therefore, concurrent with the 2012 Final Rule that amended § 4.5, the Commission issued the Proposal which was designed to address potentially conflicting or duplicative compliance obligations administered by the Commission and the SEC regarding disclosure, reporting and recordkeeping by CPOs of RICs.[202]

As set forth in the Proposal, the harmonization rulemaking sought to address a number of areas identified by commenters, including: the timing of the delivery of disclosure documents to prospective participants; the signed acknowledgement requirement for receipt of disclosure documents; the cycle for updating disclosure documents; the timing of financial reporting to participants; the requirement that a CPO maintain its books and records on site; the required

[200] Pursuant to the terms of § 4.14(a)(4), CPOs are not required to register as CTAs if the CPOs' commodity trading advice is directed solely to, and for the sole use of, the pool or pools for which they are registered as CPOs. 17 CFR 4.14(a)(4).

[201] See 2012 Final Rule, supra note 6, 77 FR at 11252, 11255. The Commission exercised its authority under § 4.12(a), which provides that the Commission may exempt any person or class of persons from any or all of part 4 requirements if the Commission finds that the exemption is not contrary to the public interest or the purposes of the provision from which the exemption is sought. 17 CFR 4.12(a).

[202] See, Proposal, supra note 23.

disclosure of fees; the required disclosure of past performance; the inclusion of mandatory certification language; and the SEC-permitted use of a summary prospectus for open-ended registered investment companies.

In the Proposal, the Commission considered the costs and benefits of harmonizing the Commissions' regimes and requested comment on its considerations of costs and benefits, including a description of any cost or benefit the Commission had not considered.

After consideration of the comments received and further deliberation, the Commission is adopting rules that effectively implement a substituted compliance approach for dually registered CPOs of RICs, whereby such CPOs, largely through compliance with obligations imposed by the SEC, will be deemed compliant with the Commission's regulatory regime. This is consistent with the Commission's conclusion, based on the information currently available, that substituted compliance is appropriate because it believes that the regime administered by the SEC under SEC RIC Rules, with minor additional disclosure, should provide market participants with meaningful disclosure as required under part 4, enable the Commission to discharge its regulatory oversight function with respect to the derivatives markets, and ensure that CPOs of RICs maintain appropriate records regarding their operations.[203]

2. Summary of The Final Rules

As discussed in greater detail in this section, the Commission believes that the rules finalized herein enable the Commission to discharge its regulatory oversight function with respect

[203] As discussed further below, the Commission has determined, in light of public comments, to modify certain elements of the Proposal. For example, the Commission is adopting a substituted compliance regime with respect to providing disclosures to prospective participants, whereby, with minor modification, the CPO of a RIC can rely upon the disclosures made pursuant to the SEC RIC Rules as satisfying its obligations under the Commission's regulations. Additionally, CPOs of RICs will satisfy the obligations to provide periodic account statements pursuant to §4.22, provided that the RIC's current net asset value per share is available to investors, and provided that the RIC furnishes semi-annual and annual reports to investors and files periodic reports with the SEC as required by the SEC.

to the commodity interest markets and ensure that CPOs of RICs maintain appropriate records regarding their operations in a manner that avoids imposing unnecessary costs on such entities.

The final rules represent several significant changes from the Proposal. The Commission is allowing CPOs of RICs to elect to comply with the majority of the provisions under §§ 4.21, 4.22(a) and (b), 4.23, 4.24, 4.25 and 4.26 through a system of substituted compliance. That is, subject to certain conditions as delineated in § 4.12(c)-(d), a CPO of a RIC may be deemed compliant with those enumerated portions of the CFTC's regulatory regime through compliance with obligations already imposed by the SEC.

Although the final rule relies primarily on a substituted compliance approach, it imposes certain obligations on CPOs of RICs beyond what is otherwise required by the federal securities laws and SEC rules. These are as follows:

- The CPO of a RIC will be required to file notice of its use of the substituted compliance regime outlined in § 4.12 with NFA;
- The CPO of a RIC with less than three years operating history will be required to disclose the performance of all accounts and pools that are managed by the CPO and that have investment objectives, policies, and strategies substantially similar to those of the offered pool; and
- The CPO of a RIC will be required to file the financial statements that it prepares pursuant to its obligations with respect to the SEC with NFA and may file notice requesting an extension to align the Commission's filing deadline with that of the SEC.

In addition, the Commission has, after consideration of the issues presented in the comment letters, determined to modify three provisions of part 4 for all CPOs, including CPOs of RICs. Specifically, the Commission is deleting a provisions in §§ 4.23 and 4.7(b)(4) that require

books and records to be kept at the "main business location" of the CPO. The Commission is updating §§ 4.23 and 4.7(b)(4) to allow all CPOs to use third-party service providers to manage their recordkeeping obligations, provided that each CPO electing to do so notifies the Commission through NFA as required under amended §§ 4.23(c) and 4.7(b)(4). The Commission has also determined to rescind the signed acknowledgement requirement in § 4.21(b). Finally, the Commission has amended §§ 4.26(a)(2) and 4.36(b) to allow the use of Disclosure Documents for a twelve-month cycle, rather than the current nine-month cycle, for both CPOs and CTAs.

In the following sections, the Commission considers the benefits and costs of the final rules, as well as the comments received regarding the costs and benefits associated with the Proposal, and evaluates the final rules in light of the five factors enumerated in Section 15(a)(2) of the CEA.[204]

3. Benefits

As explained throughout this release, the basic approach the Commission has taken to harmonization of disclosure and recordkeeping requirements for CPOs of RICs under the securities and commodities laws is substituted compliance. With very limited exceptions, a CPO of a RIC will satisfy its disclosure and recordkeeping obligations by maintaining compliance with applicable securities law requirements and SEC regulations. This approach offers benefits over possible alternatives, which, though not readily reduced to a dollar amount, the Commission believes are significant.

The Commission will benefit from the information gathered from the annual financial statements submitted to NFA. Though the reports filed with the SEC are publicly available and could be manually accessed by the Commission, the Commission believes that requiring CPOs of

[204] 7 U.S.C. 19(a)(2).

RICs to file a copy of their annual financial statements with NFA is a more efficient and expedient means of gathering required information necessary to monitor CPO activity and the markets. By having all CPO financial statements in one centralized database, the Commission will be better able to quickly and effectively access information about all CPOs trading in the markets overseen by the Commission, allowing for a faster and better informed response to any concerns that may arise regarding the trading of CPOs in derivatives markets. The submission of annual financial statements to NFA will also enable the Commission to gain a broader understanding of the financial stability and status of the RICs that use derivatives markets in a significant way.

NFA will also benefit from the information submitted by CPOs of RICs as part of their annual financial statements. This information will assist NFA in allocating its examinations resources more effectively through the scheduling of examinations based upon risk analysis of the annual financial data.

The Commission also believes that requiring CPOs of RICs to comply either with the full panoply of provisions in part 4 of the Commission's regulations or the substituted compliance regime adopted in this release will provide the Commission with additional information that it needs to monitor participants in markets subject to its oversight and enforce both the CEA and the Commission's regulations. This ability will not only provide investors with better access to a post-incident remedy, but will also act as a deterrent to behavior that is violative of the CEA and/or the Commission's regulations, and may reduce the frequency with which investors are harmed.

The Commission also believes that investors in RICs that hold commodity interests will benefit from this final rule as well. The Commission believes that the disclosure of prior performance for similar funds and accounts by CPOs of RICs with less than a three year operating

history provides valuable information to investors. Pursuant to SEC guidance, RICs are currently permitted, but not required, to report past performance information for funds and accounts with investment objectives, policies, and strategies substantially similar to those of the offered RIC in the disclosure required by the SEC, therefore, many entities may not be accustomed to reporting such information. However, the Commission believes that for funds with less than three years of operating history, the disclosure of past performance information to potential investors is necessary for a comprehensive understanding of the risks of investing in a fund that trades above a de minimis amount in commodity interests. Derivative markets are highly complex and require specialized knowledge in order to manage funds effectively. The Commission continues to believe that the presentation of past performance provides investors with important information regarding the experience of the adviser of a relatively new fund. A prospective investor will, as a result of this requirement, be better able to assess the prior performance of other funds the adviser has managed. The Commission believes that this additional information will give prospective investors a more complete sense of the ability of the adviser to trade in derivatives markets. For these reasons, the Commission is requiring prior performance of a CPO of a RIC with less than three years operating history to be disclosed as permitted by SEC disclosure regulations and guidance.

The CPO industry will also benefit from the amendments that the Commission has made to provisions applicable to all CPOs. First, the Commission removed the requirement in § 4.21 that a CPO receive a signed acknowledgement of receipt of a Disclosure Document before accepting funds from a new participant. Given the electronic and web-based solicitation strategies used by most entities today, the Commission believes that that requirement may be outdated, and extended the exemption proposed for registered investment companies to include all CPOs.

Second, the Commission removed the requirement in §§ 4.23 and 4.7(b)(4) that all books and records must be maintained at the main business office of the CPO. Originally intended to ensure that books and records were readily accessible to the Commission, if necessary, the Commission believes that this requirement, in the age of electronic recordkeeping, may also be outdated. Eliminating that requirement should relieve costs for market participants without compromising the Commission's regulatory objectives. The notice filing under § 4.23 allows the Commission to have accurate information on hand should it need to access the books and records of any CPO (including CPOs of RICs).

Finally, the Commission has determined to finalize the proposed amendments regarding the cycle for updating Disclosure Documents, outlined in § 4.26 for CPOs and § 4.36 for CTAs, to allow for a twelve-month cycle instead of the current nine-month cycle. In the Commission's opinion, the additional operational and cost efficiencies gained by these amendments justify the three-month delay for investors in receiving updated disclosure information. The Commission believes that the information provided in the Disclosure Document will be sufficiently timely for pool participants to make informed investment decisions. At the same time, the extended cycle allows Disclosure Document reporting to align with annual financial statement reporting. Further, with a nine-month cycle, a CPO or CTA would need to file and distribute two Disclosure Documents in the same calendar year approximately once every three years. The Commission believes the changes finalized within § 4.26 and § 4.36 eliminate the need to file more than one Disclosure Document in any given year, reducing the costs on CPOs and CTAs.

Overall, the Commission believes the final regulations will benefit CPOs of RICs by permitting these entities to rely on the filings made with the SEC to comply with many Commission regulations. Further, the Commission believes that all CPOs and CTAs will benefit

from the amendments to requirements under §§ 4.7(b)(4), 4.21, 4.23, 4.26(b), and 4.36(b). The Commission also believes that the final regulations provide the public with additional information that is vital to informed participation in derivative markets through investment in RICs. Because many participants in RICs are retail participants, the Commission believes that participants in RICs should be given additional information to help gauge the risks associated with derivatives trading and relevant past performance information in order for them to make better informed decisions. As at least one commenter remarked, these vehicles are important investment vehicles for many retirement plans, college savings plans, and other investment goals. The Commission believes that the final rules provide flexibility and cost-efficiency for dual registrants at the same time that the rules increase the ability for investors to participate in these vehicles in a more informed and responsible manner. As such, the Commission believes the final rules achieve the goal enumerated in the Proposal: to mitigate the costs associated with compliance without compromising the effectiveness of the Commission's regulatory regime.

4. Costs

i. Costs Associated with Substituted Compliance

In this final rule, the Commission has determined to adopt a substituted compliance regime for CPOs of RICs. The Commission is adopting a compliance regime for CPOs of RICs largely premised upon such entities' adherence to the compliance obligations under SEC RIC Rules, whereby the Commission will accept compliance by such entities with the disclosure, reporting, and recordkeeping regime administered by the SEC as substituted compliance with part 4 of the Commission's regulations. The Commission has concluded that this is appropriate because it believes that general reliance upon the SEC's compliance regime, with minor additional disclosure, should provide market participants and the general public with meaningful disclosure,

including for example, with regard to risks and fees, provide the Commission with information necessary to its oversight of CPOs, and ensure that CPOs of RICs maintain appropriate records regarding their operations. As noted, in the event that the operator of the RIC fails to comply with the SEC administered regime, the operator of the RIC will be in violation of its obligations under part 4 of the Commission's regulations and subject to enforcement action by the Commission.

The substituted compliance regime adopted by the Commission in these final rules provides that a CPO of a RIC will be deemed compliant with §§ 4.21, 4.22(a) and (b), 4.23, 4.24, 4.25, and 4.26 under the amendments to § 4.12, provided that the CPO comply with all applicable SEC RIC Rules.

Section 4.12 also provides that an entity must file a notice with the NFA to take advantage of the Commission's substituted compliance program for CPOs of RICs. The notice is effective upon submission and must only be filed once per pool. For purposes of calculating costs of the final rule, the Commission has estimated that each pool may require 2 hours to complete the notice and file the notice with NFA at an average salary cost of $76.93 per hour[205]. The Commission further estimates that 418 sponsors may be affected, [206] each with an average of 3

[205] The Commission staff's estimates concerning the wage rates are based on 2011 salary information for the securities industry compiled by the Securities Industry and Financial Markets Association ("SIFMA"). The $76.93 per hour is derived from figures from a weighted average of salaries across different professions from the SIFMA Report on Management & Professional Earnings in the Securities Industry 2011, modified to account for an 1800-hour work-year, adjusted to account for the average rate of inflation in 2012, and multiplied by 1.3 to account for overhead and other benefits. The Commission anticipates that compliance with the part 4 provisions would require the work of an information technology professional (to provide necessary information); a compliance manager (to determine whether or not an entity is eligible for an exemption in accordance with the Commission's regulations); and an associate general counsel (to prepare notices of exemption). Thus, the wage rate is a weighted national average of salary for professionals with the following titles (and their relative weight); "programmer (senior)" (30% weight), "compliance manager" (45%), and "assistant/associate general counsel" (25%). The Commission uses this wage estimate in estimating costs for provisions that were not included in commenters' assessments of costs and benefits; for provisions that were included in the commenters' assessments of costs and benefits, the Commission utilizes the estimates provided by the commenters. All estimates have been rounded to the nearest hundred dollars.

[206] There currently is no source of reliable information regarding the general use of derivatives by registered investment companies. Because of this lack of information, in the Proposal, the Commission derived the estimated entities affected and the number of burden hours associated with this proposal through the use of statistical analysis.

pools subject to the notice requirement. On this basis, the Commission anticipates a one-time cost per-entity of approximately $500.[207] Across all affected entities, the Commission estimates a total one-time cost of approximately $192,900.[208] The Commission believes that this is the extent of the costs associated with the substituted compliance regime.

The Commission received many comments regarding the costs of the Proposal.[209] Generally, commenters expressed concern about the cost imposed by the Proposal with respect to the compliance obligations of RICs and the Commission's consideration thereof.[210] Specifically, commenters stated that RICs were already subject to extensive regulation, and that additional compliance obligations required of CPOs under part 4 of the Commission's regulations may conflict with, or potentially be duplicative of, requirements under the SEC RIC Rules.[211] Commenters further cited specific market problems that may occur as a result of the rule, including reduced liquidity and potential price impacts should funds determine to reduce their

---

The Commission estimated that 1,266 pools would require 418 entities to register as CPOs due to the amendments to § 4.5. To determine the average number of pools per entity, the Commission divided the estimated number of pools by the estimated number of entities to arrive at about 3 pools per entity. The methodology used to determine this estimate is fully explained supra in this release. The Commission understands from NFA that as of February 1, 2013, there were six new registered CPOs and five CPOs whose registration pre-dates the amendments to § 4.5 that have compliance obligations for 149 RICs that are commodity pools. Due to limitations on this data arising from other actions taken by the Commission or divisions thereof, the Commission does not believe that the data is sufficiently finalized to use as the basis for its PRA or cost benefit calculations. Therefore, the Commission has determined to use the numbers derived through the methodology used in the Proposal. Notwithstanding the limitations in the data to date, the Commission believes that these numbers are useful in considering the likely impact on the final rule on industry.

[207] The Commission calculates this amount as follows: (3 pools per sponsor) x (2 hours per pool) x ($76.93 per hour) = $461.58.

[208] The Commission calculates this amount as follows: ($461.58 per sponsor) x (418 sponsors) = $192,940.44.

[209] The Commission also received several comments regarding the costs of the amendments to §4.5 that were finalized in the February Final Rule and asserting that the Commission should not have considered the costs of compliance separately from those of registration. See, SIFMA AMG Letter, Dechert Letter, ICI Letter, Invesco Letter. The Commission notes that it considered those costs related to the registration of CPOs of RICs under § 4.5 in the rules adopting such amendments and such comments are outside the scope of this rulemaking.

[210] See, ICI Letter; Dechert Letter; Katten Letter; NYCBA Letter; ABA Letter; Fidelity Letter; AII letter; Invesco Letter; SIFMA AMG Letter; AXA Letter.

[211] See, e.g., ICI Letter; SIFMA AMG Letter.

positions in derivatives in order to avoid additional compliance obligations.[212] Commenters also stated that RIC shareholders would bear many of the costs of these rules in several ways, including but not limited to, higher fees and lower returns.[213]

In adopting a broad substituted compliance regime wherein CPOs of RICs will be deemed compliant with §§ 4.21, 4.22(a) and (b), 4.23, 4.24, 4.25, and 4.26 under the amendments to § 4.12, provided that the CPO comply with all SEC RIC Rules, the Commission expects that it has reduced or eliminated any impetus for RICs to reduce their positions in markets overseen by the Commission and subsequently any negative impact on market quality indicators. The Commission also believes it has greatly reduced, and in many cases eliminated, the costs CPOs of RICs face, which could be passed through to investors in such RICs.

The Commission also received comments from ICI and Invesco regarding the costs associated with discrete provisions in part 4 that would have been imposed under the Proposal.[214] These letters enumerated specific costs associated with three general areas addressed in the Proposal: (1) general disclosure requirements under § 4.24; (2) performance disclosure requirements under § 4.25; and (3) financial reporting requirements under § 4.22(a) and (b).[215]

---

[212] Katten Letter; Dechert Letter; Fidelity Letter; NYCBA Letter.

[213] ABA Letter; Dechert Letter; Invesco Letter; Katten Letter; SIFMA AMG Letter; AXA Letter: AII Letter.

[214] See, ICI Letter; Invesco Letter. The Commission believes that the industry survey conducted by ICI provides useful insight about potential costs associated with various part 4 requirements, and as described further therein, has used the results in its consideration of costs associated with the final rules.

[215] ICI Letter. ICI reported that of the 42 advisers who responded to their survey, 33 advisers representing 551 funds with total net assets of $773 billion anticipated having to register under the newly amended § 4.5. ICI rounded all of its aggregate cost estimates to the nearest $100.

ICI calculated the initial costs of prior performance disclosure required for all funds under § 4.25 as follows: (18 hours per fund for initial compliance) x ($227 per initial compliance hour) = $4,086 per fund. ICI also calculated the ongoing costs of prior performance disclosure required for all funds under § 4.25 as follows: (9.5 hours per fund for ongoing compliance) x ($225 per ongoing compliance hour) = $2,137.50 per fund.

ICI calculated the aggregate initial costs for the surveyed funds as follows: ($4,086 initial cost per fund) x (551 surveyed funds) = $2,251,400. ICI also calculated the aggregate ongoing costs for the surveyed funds as follows: ($2,137.50 ongoing costs per fund) x (551 surveyed funds) = $1,177,800.

ICI also provided estimated costs associated with revising registration statements to include CFTC-required disclosures under the Proposal and costs associated with filing prospectuses with NFA.[216]

The final rules provide in § 4.12(c) that CPOs of RICs may take advantage of the Commission's substituted compliance provisions for all requirements under §§ 4.24, 4.25, and 4.22(a) and (b). The final rules do not require the disclosures contemplated under the Proposal nor do they require CPOs of RICs to file Disclosure Documents with NFA for review. Because the Commission anticipates that all CPOs of RICs will take advantage of the substituted compliance program to avoid any additional cost, the Commission estimates that none of the costs identified by commenters that are associated with complying with §§ 4.24, 4.25, and 4.22 (a) and (b) will be incurred by CPOs of RICs.

ICI, as well as other commenters, also identified the following additional costs of the Proposal: (1) costs to registrants if, because of complications associated with a different review process and/or more than one reviewing entity, their Disclosure Documents are not approved in a

---

With respect to the preparation of account statements under § 4.22(a) and (b), ICI calculated a one-time cost associated with the separate calculation of brokerage commissions as follows: (42 hours per fund) x ($171 per hour) = $ 7,182 per fund. ICI calculated the aggregate costs associated with brokerage commissions for all surveyed funds as follows: ($7,182 cost per fund) x (551 surveyed funds) = $3,957,300.

ICI calculated the costs for each fund associated with preparing and distributing account statements per § 4.22(a) and (b) as follows: (5.75 hours per fund) x ($122.40 average cost per hour) = $703.84 per fund per statement.. ICI calculated that the aggregate costs associated with the preparation and distribution of account statements for all surveyed funds as follows: ($703.84 costs per fund) x (551 surveyed funds) x (12 monthly statements) = $4,653,800.

In total, for all § 4.24 provisions, ICI estimated the 551 responsive funds would incur a cost of $5.8 million initially and $2.4 million annually. This was derived from hour and cost estimates for 5 different categories of disclosure that ICI developed from its survey data. For the industry as a whole, ICI estimated that these costs could be as high as $13.3 million initially and $5.5 million on an ongoing annual basis.

[216] ICI Letter. ICI calculated a one-time cost associated with the revision of prospectuses for all surveyed funds as follows: (15 hours per fund) x ($215 per hour) x (551 surveyed funds) = $1,777,000 to revise their prospectuses. ICI also calculated the initial cost of filing prospectuses with NFA as follows: (29.5 hours per fund) x ($199 per hour) = $5,870.50 per fund. ICI calculated the aggregate initial cost for the surveyed funds as follows: ($5,870.50 cost per fund) x (551 surveyed funds) = $3,234,600. ICI calculated the ongoing cost of filing prospectuses with NFA per fund as follows: (15.5 hours per fund) x ($195 per hour) = $3,022.50 per fund. ICI calculated the aggregate ongoing cost for all surveyed funds as follows: (551 surveyed funds) x ($3,022.50 cost per fund) = $1,665,400.

timely fashion and the RIC must temporarily stop issuing shares;[217] (2) costs associated with seeking relief from the SEC, CFTC, or NFA to comply with CFTC disclosure and reporting regulations, where conflicts exist;[218] (3) costs to the CFTC, SEC, and NFA of reviewing the additional filings, including the potential for multiple reviews of each filing in the early stages, as registrants seek to develop disclosures that are acceptable to all regulators; (4) likely significant investor confusion due to inconsistent and at times inapplicable disclosures;[219] and (5) costs associated with undoing decades of effort by the SEC to develop its fund disclosure regime for RICs.[220] Commenters also raised concerns about the costs associated with modifications to their internal compliance controls and additional systems that may be necessary to comply with the provisions of the Proposal.[221]

Additionally, one commenter stated that the legal conflicts and operational costs that would result from the application of the Proposal to CPOs of RICs would be substantial.[222] According to that commenter, many RICs belong to large fund families that may include dozens, if not hundreds, of funds.[223] This commenter further stated that significant economies of scale exist with respect to compliance with SEC regulations, because the advisers to these fund families are able to operate multiple funds on similar timetables and comply with similar filing and disclosure requirements.[224] The commenter contended that complying with the CFTC rules as

[217] ICI Letter. See also, Katten Letter; ABA Letter; AXA Letter; NYCBA Letter.

[218] ICI Letter. See also, Dechert Letter; IAA Letter; Fidelity Letter; SIFMA AMG Letter; ABA Letter; Katten Letter; AXA Letter; NYCBA Letter.

[219] ICI Letter. See, MFA Letter.

[220] ICI Letter. See, AXA Letter.

[221] NYCBA Letter; Dechert Letter; AXA Letter; ABA Letter; SIFMA AMG Letter.

[222] SIFMA AMG Letter.

[223] Id.

[224] Id.

described in the Proposal would not only impose significant new costs on the RICs that are subject to such rules, but also impede the ability of advisers to efficiently manage other funds that are not subject to CFTC requirements.[225]

The Commission does not anticipate these qualitative concerns to be applicable as a result of the substituted compliance regime provided in the final rules. Registrants will not be required to submit to multiple review processes, eliminating the costs associated with (1)-(3) above. The items that will be required of CPOs of RICs in addition to what is required by the SEC, which are discussed infra, will be disclosed in accordance with SEC regulations, which are familiar to investors and should largely eliminate any costs associated with (4) and (5) above. Moreover, because the Commission has adopted in these final rules a substituted compliance regime wherein CPOs of RICs will be deemed compliant with §§ 4.21, 4.22(a) and (b), 4.23, 4.24, 4.25, and 4.26 under the amendments to § 4.12, provided that the CPO comply with all SEC RIC Rules, the Commission does not believe that significant modifications to CPOs of RICs' compliance and disclosure infrastructures will be necessary.

ii. Costs Associated with Certain Additional Requirements for CPOs of RICs and Other Amendments

Although the final rule largely adopts a substituted compliance approach, the Commission acknowledges that there will be some costs associated with the final rule that will be borne by dually registered entities. In particular, CPOs of RICs with less than a three-year operating history will also have to provide disclosure regarding the past performance of all accounts and pools that are managed by the CPO and that have investment objectives, policies, and strategies substantially similar to those of the offered pool in accordance with SEC regulations and

[225] Id.

guidance. Additionally, CPOs of RICs will still be subject to § 4.22(c) and (d), requiring the CPO of a RIC to submit to NFA a copy of the annual financial statements the RIC provides to the SEC. Finally, all CPOs that use a third-party provider to maintain books and records are required to submit a notice with NFA with the name of the third-party provider, among other details, to ensure that the Commission has full access to the books and records of the CPO.

The Commission anticipates that CPOs of RICs will incur costs to disclose past performance information for substantially similar funds and accounts, if the fund has been in operation for less than three years. The ICI, in its estimates of costs and benefits, estimated that costs associated with prior performance disclosure for funds with less than a three year operating history would amount to 34 hours per fund at $265 per hour initially, and 25.5 hours per fund at $233 per hour each year in ongoing compliance requirements.[226] The ICI's estimates are based on the requirement in the Proposal to include past performance information for all other funds operated by the sponsor of the fund with less than a three year operating history. As noted above, the Commission has altered this provision to require disclosure of only those pools and accounts that are managed by the CPO and that have investment objectives, policies, and strategies substantially similar to those of the offered pool with less than a three year operating history. In so doing, the Commission has significantly reduced the requirements regarding past performance disclosure. As such, the Commission believes it can reasonably reduce the number of hours required both initially and in ongoing compliance. The Commission anticipates initial and ongoing cost of approximately 15 hours per fund. The Commission anticipates that 368 sponsors will need to provide additional past performance disclosure for an average of 1 fund per sponsor at

[226] ICI Letter.

15 hours per fund.[227] Using ICI's hourly cost estimates, described above, the Commission estimates an initial annual cost of $4,000 per entity[228] and an ongoing annual cost of $3,500 per entity.[229] Across all affected entities, the Commission estimates an initial annual cost of $1,462,800[230] and an ongoing annual cost of $1,286,200.[231]

The Commission also anticipates that CPOs of registered investment companies will incur small costs for each fund due to the requirement that the CPO of each registered investment company must submit a copy of the fund's annual financial statements to the Commission via NFA.[232] The Commission anticipates that the cost to submit each fund's financial statements to be relatively small because the Commission is requiring only a copy of the statements required to be submitted to the SEC under the SEC RIC Rules to be submitted to NFA. The Commission

[227] Based on information provided by the ICI in its comment letter, of the 551 surveyed funds that would trigger registration of their advisor, 159 of those funds had less than three years operating history. This constitutes approximately 30 percent of the surveyed funds that would not be excluded under § 4.5. The funds were operated by 29 of the 33 sponsors that expected to register, which constitutes 88 percent of the surveyed sponsors expecting to register. Applying these percentages to the Commission's estimated number of 1,266 pools and 418 sponsors, the Commission expects approximately 368 pool operators to be subject to the disclosure requirements for substantially similar accounts and funds with respect to 380 pools. With respect to the estimated hours required to prepare the past performance disclosure, the Commission has made an informed estimate premised upon the information provided by ICI and that it believes reflects the reduced disclosure obligations under the final rule as compared to the Proposal.

[228] The Commission calculates the amount as follows: (1 RIC per CPO) x (15 hours per RIC) x ($265 initial costs per hour) = $3,975.

[229] The Commission calculates the amount as follows: (1 RIC per CPO) x (15 hours per RIC) x ($233 ongoing costs per hour) = $3,495.

[230] The Commission calculates the amount as follows: ($3,975 estimated initial cost per CPO) x (368 estimated number of CPOs of RICs with less than 3 years performance) = $1,462,800.

[231] The Commission calculates the amount as follows: ($3,495 estimated ongoing cost per CPO) x (368 estimated number of CPOs of RICs with less than 3 years performance) = $1,286,160. This ongoing cost estimate assumes that all RICs with less than three years performance are newly formed and have no performance history. Many RICs subject to the disclosure requirement, however, may have operated for one or two years and thus incur a lower total cost. The Commission's estimate therefore may overstate the actual costs that past performance disclosure entails.

[232] The Commission notes that all CPOs are required to submit an annual report to NFA. Though the reports filed with the SEC are public domain could be manually accessed by the Commission, the Commission believes that requiring a copy of said reports to be filed with NFA is a more efficient and expedient means of gathering required information. By having all CPO financial statements in one centralized database, the Commission will be better able to quickly and effectively access information about all CPOs trading in the markets overseen by the Commission, allowing for a faster and better informed response to any concerns that may arise regarding the trading of CPOs in derivatives markets.

anticipates that the additional requirement imposed by the rule in § 4.22 necessitates only addressing any potential formatting changes—i.e. making sure the document is in PDF form as required by NFA—and uploading the document via NFA's Easy File system (to which advisers should already have access by virtue of their registration). Thus, the Commission anticipates that CPOs of RICs will require no more than 2 hours per fund to comply with § 4.22. The Commission estimates that each CPO has an average of 3 RICs. Thus, at a rate of $76.93 per hour,[233] the Commission estimates an initial cost of approximately $500[234] and an annual ongoing cost of approximately $500.[235] As described in the PRA section of this release, the Commission estimates that approximately 418 sponsors will register as a result of the amendments to § 4.5.[236] Using this figure, the Commission anticipates a total initial cost of $192,900[237] and an annual total ongoing cost of $192,900.[238] The Commission believes this to be a conservative estimate, allowing for the maximum amount of time necessary to upload the fund's financial statements and submit them to NFA.

Finally, the Commission anticipates a small burden to be incurred by all CPOs, including registered investment companies required to be registered as CPOs under § 4.5, that wish to keep their books and records with a third-party service provider. Under §§ 4.23 and 4.7(b)(4), such entities must file a notice with NFA to inform the Commission and NFA of the entity's intent to

---

[233] See, supra note 205.

[234] The Commission calculates the amount as follows: (6 hours per entity) x ($76.93 average salary cost per hour) = $461.58.

[235] The Commission calculates this amount as follows: (6 hours per entity) x ($76.93 average salary cost per hour) = $461.58.

[236] See supra note 206.

[237] The Commission calculates this amount as follows: ($461.58 estimated initial cost per CPO) x (418 estimated number of CPOs of RICs) = $192,940.44.

[238] The Commission calculates this amount as follows: ($461.58 estimated ongoing cost per CPO) x (418 estimated number of CPOs of RICs) = $192,940.44.

utilize a third-party service provider as well as the name and contact information of the third party. Because the Commission cannot be sure how many CPOs will use third-party service providers, the Commission estimates that all CPOs will take advantage of the amendments to the record-keeping requirements under § 4.23 and § 4.7.[239] The Commission estimates that CPOs, including registered investment companies, will incur a one-time per-entity cost of $200.[240] The Commission anticipates that most CPOs will take advantage of this provision, and thus estimates a one-time estimated cost of $627,700 for all CPOs.[241]

The Commission expects that all dually-registered entities will take advantage of the substituted compliance regime available under the final regulations. The Commission thus expects that the total initial costs associated with the final rules will be $5,100 per entity[242] and

[239] The Commission has previously estimated that each CPO that subject to § 4.23 had costs associated with approximately 50 hours associated with recordkeeping obligations and that each CPO subject to § 4.7(b)(4) had costs associated with approximately 40 hours associated with recordkeeping obligations. Because the Commission is estimating that all registered CPOs will use third-party service providers for recordkeeping purposes, the Commission expects that costs associated with §§ 4.7(b)(4) and 4.23 will be reduced, although the reduction cannot be quantified at this time.

[240] The Commission calculates this amount as follows: (2 estimated hours per notice) x ($76.93 estimated cost per hour) = $153.86.

[241] The Commission calculates this amount as follows: ($153.86 estimated cost per notice) x (4,080 estimated total number of registered CPOs) = $627,748.80.

[242] The Commission calculates the per-entity initial cost by summing the per-entity initial costs of the provisions described supra. Estimates may not sum to total due to rounding effects.

Notice of Substituted Compliance, § 4.12 = (3 pools per sponsor) x (2 hours per pool) x ($76.93 per hour) = $461.58.

Inclusion of Past Performance, § 4.25 = (1 pool per sponsor) x (15 hours per pool) x ($265 per hour) = $3,975.00.

Submission of Annual Report, § 4.22(c) = (3 pools per sponsor) x (2 hours per pool) x ($76.93 per hour) = $461.58.

Notice of Third Party Record-keeper, §§ 4.23, 4.7(b)(4) = (2 hours per sponsor) x ($76.93 per hour) = $153.86.

Total per-entity initial cost = ($461.58) + ($3,975.00) + ($461.58) + ($115.40) + ($153.86) = $5,061.02.

See supra notes 207, 228, 234, and 240.

$2,476,400 in the aggregate.[243] Likewise, the Commission expects annual ongoing costs associated with the final rules to be $4,000 per entity[244] and $1,479,100 in the aggregate.[245]

b. Section 15(a) Considerations

Section 15(a) of the CEA requires the Commission to consider the effects of its actions in light of the following five factors:

1. Protection of Market Participants and the Public

The Commission believes the rules promulgated in this release protect market participants by mitigating the costs associated with compliance. The rules maintain the effectiveness of the consumer protections of the Commission's regulatory regime while reducing costs for dually-registered entities. Though some costs are anticipated as a result of the final rules in order to

---

[243] The Commission calculates the aggregate initial cost by summing the aggregate initial costs of the provisions described supra. Estimates may not sum to total due to rounding effects.

Notice of Substituted Compliance, § 4.12 = (461.58 per sponsor) x (418 sponsors) = $192,940.44.

Inclusion of Past Performance, § 4.25 = ($3,975.00 per sponsor) x (368 sponsors) = $1,462,800.00.

Submission of Annual Report, § 4.22(c) = ($461.58 per sponsor) x (418 sponsors) = $192,940.44.

Notice of Third Party Record-keeper, §§ 4.23, 4.7(b)(4) = ($153.86 per operator) x (4,080 operators) = $627,748.80.

Total aggregate initial cost = ($192,940.44) + ($1,462,800.00) + ($192,940.44) + ($48,235.11) + ($627,748.80) = $2,476,429.68

See supra notes 208, 229, 237, and 241.

[244] The Commission calculates the per-entity ongoing cost by summing the per-entity ongoing costs of the provisions described *supra*. Estimates may not sum to total due to rounding effects.

Inclusion of Past Performance, § 4.25 = (1 pool per sponsor) x (15 hours per pool) x ($233 per hour) = $3,475.00.

Submission of Annual Report, § 4.22(c) = (3 pools per sponsor) x (2 hours per pool) x ($76.93 per hour) = $461.58.

Total per-entity ongoing cost = ($3,475.00) + ($461.58) = $3956.55.

See supra notes 235 and 238.

[245] The Commission calculates the aggregate ongoing cost by summing the aggregate ongoing costs of the provisions described supra. Estimates may not sum to total due to rounding effects.

Inclusion of Past Performance, § 4.25 = ($3,475.00 per sponsor) x (368 sponsors) = $1,286,160.00.

Submission of Annual Report, § 4.22(c) = ($461.58 per sponsor) x (418 sponsors) = $192,940.44.

Total aggregate ongoing cost = ($1,286,160.00) + ($192,940.44) = $1,479,100.44.

See supra notes 235 and 242.

provide additional information beyond that required by the SEC, the Commission believes such costs are necessary because the information the Commission is requiring of CPOs of RICs should provide additional insight for potential investors in deciding whether to invest in a fund that commits more than a de minimis portion of its assets to derivative trading.

In addition, the Commission believes the final rules provide a benefit to all CPOs by updating and modernizing certain provisions that may be outdated in the electronic age. CPOs will not be required to incur costs to comply with regulations that, in the absence of information to the contrary and in light of the Commission's current understanding, may not be necessary to ensure the effectiveness of the Commission's regulatory regime.

Furthermore, by lessening the regulatory costs RICs face, shareholders of these vehicles should not see much of an increase in fees or a decrease in returns, protecting the viability of these vehicles that are utilized by millions of families for their investment needs.

2. Efficiency, Competitiveness, and Financial Integrity of Markets

In light of the fact that these harmonizing regulations will not pose significant costs on CPOs of RICs, the Commission does not believe that these regulations will have a negative impact on the efficiency, competitiveness, or financial integrity of markets.

3. Price Discovery

The Commission has not identified a specific effect on price discovery as a result of these harmonizing regulations.

4. Sound Risk Management

The Commission has not identified a specific effect on sound risk management as a result of these harmonizing regulations.

5. Other Public Interest Considerations

The Commission has not identified other public interest considerations related to the costs and benefits of these harmonizing regulations.

List of Subjects in 17 CFR Part 4

Advertising, Brokers, Commodity futures, Commodity pool operators, Commodity trading advisors, Consumer protection, Reporting and recordkeeping requirements.

PART 4—COMMODITY POOL OPERATORS AND COMMODITY TRADING ADVISORS

1. Revise the authority citation for part 4 to read as follows:

Authority: 7 U.S.C. 1a, 2, 6(c), 6b, 6c, 6l, 6m, 6n, 6o, 12a, and 23.

2. In § 4.7, revise paragraph (b)(4) and add paragraph (b)(5) to read as follows:

§ 4.7 Exemption from certain part 4 requirements for commodity pool operators with respect to offerings to qualified eligible persons and for commodity trading advisors with respect to advising qualified eligible persons.

* * * * *

(b) * * *

(4) Recordkeeping relief. Exemption from the specific requirements of § 4,23; Provided, That the commodity pool operator must maintain the reports referred to in paragraphs (b)(2) and (b)(3) of this section and all books and records prepared in connection with his activities as the pool operator of the exempt pool (including, without limitation, records relating to the qualifications of qualified eligible persons and substantiating any performance representations). Books and records that are not maintained at the pool operator's main business office shall be maintained by one or more of the following: the pool's administrator, distributor or custodian, or a bank or registered

broker or dealer acting in a similar capacity with respect to the pool. Such books and records must be made available to any representative of the Commission, the National Futures Association and the United States Department of Justice in accordance with the provisions of § 1.31.

(5) If the pool operator does not maintain its books and records at its main business office, the pool operator shall:

(i) At the time it registers with the Commission or delegates its recordkeeping obligations, whichever is later, file a statement that:

(A) Identifies the name, main business address, and main business telephone number of the person(s) who will be keeping required books and records in lieu of the pool operator;

(B) Sets forth the name and telephone number of a contact for each person who will be keeping required books and records in lieu of the pool operator;

(C) Specifies, by reference to the respective paragraph of this section, the books and records that such person will be keeping; and

(D) Contains representations from the pool operator that:

(1) It will promptly amend the statement if the contact information or location of any of the books and records required to be kept by this section changes, by identifying in such amendment the new location and any other information that has changed;

(2) It remains responsible for ensuring that all books and records required by this section are kept in accordance with § 1.31;

(3) Within 48 hours after a request by a representative of the Commission, it will obtain the original books and records from the location at which they are maintained, and provide them for inspection at the pool operator's main business office; Provided, however, that if the original books and records are permitted to be, and are maintained, at a location outside the United States,

its territories or possessions, the pool operator will obtain and provide such original books and records for inspection at the pool operator's main business office within 72 hours of such a request; and

(4) It will disclose in the pool's Disclosure Document the location of its books and records that are required under this section.

(ii) The pool operator shall also file electronically with the National Futures Association a statement from each person who will be keeping required books and records in lieu of the pool operator wherein such person:

(A) Acknowledges that the pool operator intends that the person keep and maintain required pool books and records;

(B) Agrees to keep and maintain such records required in accordance with § 1.31 of this chapter; and

(C) Agrees to keep such required books and records open to inspection by any representative of the Commission, the National Futures Association, or the United States Department of Justice in accordance with § 1.31 of this chapter.

3. In § 4.12

a. Revise paragraphs (c)(1) and (c)(2);

b. Remove paragraph (c)(2)(iii);

c. Add paragraph (c)(3); and

d. Revise paragraphs (d)(1)(iii) and (d)(1)(iv).

The revisions and additions read as follows:

§ 4.12 Exemption from provisions of part 4.

* * * * *

(c) Exemption from Subpart B for certain commodity pool operators based on registration under the Securities Act of 1933 or the Investment Company Act of 1940. (1) Eligibility. Subject to compliance with the provisions of paragraph (d) of this section, any person who is registered as a commodity pool operator, or has applied for such registration, may claim any or all of the relief available under paragraph (c)(2) of this section if, with respect to the pool for which it makes such claim:

(i) The units of participation will be offered and sold pursuant to an effective registration statement under the Securities Act of 1933; or

(ii) The pool is registered under the Investment Company Act of 1940.

(2) Relief available to pool operator claiming relief under paragraph (c)(1)(i). The commodity pool operator of a pool whose units of participation meet the criteria of paragraph (c)(1)(i) if this section may claim the following relief:

* * * * *

(3) Relief available to pool operator claiming relief under paragraph (c)(1)(ii). The commodity pool operator of a pool whose units of participation meet the criteria of paragraph (c)(1)(ii) of this section may claim the following relief:

(i) The pool operator of an offered pool will be exempt from the requirements of §§ 4.21, 4.24, 4.25, and 4.26; Provided, that

(A) The pool operator of an offered pool with less than a three-year operating history discloses the performance of all accounts and pools that are managed by the pool operator and that have investment objectives, policies, and strategies substantially similar to those of the offered pool; and,

(B) The disclosure provided with respect to the offered pool complies with the provisions of the Investment Company Act of 1940, the Securities Act of 1933, the Securities Exchange Act of 1934, the regulations promulgated thereunder, and any guidance issued by the Securities and Exchange Commission or any division thereof.

(ii) Exemption from the Account Statement distribution requirement of §§ 4.22(a) and (b); Provided, however, that the pool operator:

(A) Causes the current net asset value per share to be available to participants;

(B) Causes the pool to clearly disclose:

(1) That the information will be readily accessible on an Internet Web site maintained by the pool operator or its designee or otherwise made available to participants and the means through which the information will be made available; and

(2) The Internet address of such Web site, if applicable; and

(iii) Exemption from the provisions of § 4.23 that require that a pool operator's books and records be made available to participants for inspection and/or copying at the request of the participant.

* * *

(d)(1) * * *

(iii) Contain representations that:

(A) The pool will be operated in compliance with paragraph (b)(1)(i) of this section and the pool operator will comply with the requirements of paragraph (b)(1)(ii) of this section;

(B) The pool will be operated in compliance with paragraph (c)(1) of this section and the pool operator will comply with the requirements of paragraph (c)(2) of this section; or

(C) The pool will be operated in compliance with paragraph (c)(1) of this section and the pool operator will comply with the requirements of paragraph (c)(3) of this section;

(iv) Specify the relief sought under paragraph (b)(2), (c)(2), or (c)(3) of this section, as the case may be;

* * * * *

4. Add § 4.17 to read as follows:

§ 4.17 Severability.

If any provision of this part, or the application thereof to any person or circumstances, is held invalid, such invalidity shall not affect other provisions or application of such provision to other persons or circumstances which can be given effect without the invalid provision or application.

5. Amend § 4.21 by removing paragraph (b).

6. Amend § 4.23 and add paragraph (c) to read as follows:

§ 4.23 Recordkeeping

Each commodity pool operator registered or required to be registered under the Act must make and keep the following books and records in an accurate, current and orderly manner. Books and records that are not maintained at the pool operator's main business office shall be maintained by one or more of the following: the pool's administrator, distributor or custodian, or a bank or registered broker or dealer acting in a similar capacity with respect to the pool. All books and records shall be maintained in accordance with § 1.31. All books and records required by this section except those required by paragraphs (a)(3), (a)(4), (b)(1), (b)(2) and (b)(3) must be made available to participants for inspection and copying during normal business hours. Upon request, copies must be sent by mail to any participant within five business days if reasonable reproduction and distribution costs are paid by the pool participant. If the books and records are maintained at the commodity pool operator's main business office that is outside the United States, its territories or possessions, then upon the request of a Commission representative, the pool operator must

provide such books and records as requested at the place in the United States, its territories or possessions designated by the representative within 72 hours after the pool operator receives the request.

(a) * * *

(4) A subsidiary ledger or other equivalent record for each participant in the pool showing the participant's name and address and all funds, securities and other property that the pool received from or distributed to the participant. This requirement may be satisfied through a transfer agent's maintenance of records or through a list of relevant intermediaries where shares are held in an omnibus account or through intermediaries.

* * * * *

(c) If the pool operator does not maintain its books and records at its main business office, the pool operator shall:

(1) At the time it registers with the Commission or delegates its recordkeeping obligations, whichever is later, file a statement that:

(i) Identifies the name, main business address, and main business telephone number of the person(s) who will be keeping required books and records in lieu of the pool operator;

(ii) Sets forth the name and telephone number of a contact for each person who will be keeping required books and records in lieu of the pool operator;

(iii) Specifies, by reference to the respective paragraph of this section, the books and records that such person will be keeping; and

(iv) Contains representations from the pool operator that:

(A) It will promptly amend the statement if the contact information or location of any of the books and records required to be kept by this section changes, by identifying in such amendment the new location and any other information that has changed;

(B) It remains responsible for ensuring that all books and records required by this section are kept in accordance with § 1.31;

(C) Within 48 hours after a request by a representative of the Commission, it will obtain the original books and records from the location at which they are maintained, and provide them for inspection at the pool operator's main business office; *Provided, however,* that if the original books and records are permitted to be, and are maintained, at a location outside the United States, its territories or possessions, the pool operator will obtain and provide such original books and records for inspection at the pool operator's main business office within 72 hours of such a request; and

(D) It will disclose in the pool's Disclosure Document the location of its books and records that are required under this section.

(2) The pool operator shall also file electronically with the National Futures Association a statement from each person who will be keeping required books and records in lieu of the pool operator wherein such person:

(i) Acknowledges that the pool operator intends that the person keep and maintain required pool books and records;

(ii) Agrees to keep and maintain such records required in accordance with § 1.31 of this chapter; and

(iii) Agrees to keep such required books and records open to inspection by any representative of the Commission or the United States Department of Justice in accordance with § 1.31 of this

chapter and to make such required books and records available to pool participants in accordance with this section.

7. Amend § 4.26 by revising paragraph (a)(2) to read as follows:

§ 4.26 Use, amendment and filing of Disclosure Document.

(a) * * *

(2) No commodity pool operator may use a Disclosure Document or profile document dated more than twelve months prior to the date of its use.

* * * * *

8. Amend § 4.36 by revising paragraph (b) to read as follows:

§ 4.36 Use, amendment and filing of Disclosure Document.

* * * * *

(b) No commodity trading advisor may use a Disclosure Document dated more than twelve months prior to the date of its use.

* * * * *

Issued in Washington, DC, on August 12, 2013, by the Commission.

Melissa D. Jurgens,

Secretary of the Commission

Appendix to Final Rule on Harmonization of Compliance Obligations for Registered Investment Companies Required to Register as Commodity Pool Operators—Commission Voting Summary

Note: The following appendix will not appear in the Code of Federal Regulations

Appendix 1 – Commission Voting Summary

On this matter, Chairman Gensler and Commissioners Chilton, O'Malia, and Wetjen voted in the affirmative.