

CFTC Letter No. 99-17**April 5, 1999****No-Action****Division of Trading & Markets**

Dear :

This is in response to your letter of February 26, 1999 in which you request an exemption from the requirements of Rules 4.35(a)(7) and 4.34(n).

Based upon the representations made in your letter, the relevant facts are as follows. "A"'s trading program is called the "B" Program. The "B" Program is purely systematic and does not employ subjective analysis and as a result all accounts are traded exactly alike. Each account receives the same trade price as a result of the use of the Chicago Board of Trade's Average Pricing System. All accounts are maintained at the same futures commission merchant and are charged the same brokerage rates. "A" has only thirteen accounts, three of which fall under the definition of proprietary.

A currently has approximately \$\$\$\$000 under management. The three proprietary accounts represent 11 percent of the total assets under management. Two of these proprietary accounts are owned by "A"'s Branch Office Manager and the third is owned by a sibling of "A"'s president. One of these accounts was opened as a client account in January 1998, and became a proprietary account when the account owner became an associated person and branch office manager of "A." You request that the Commission grant no-action relief and allow the proprietary accounts to remain in the composite performance table of "A." In the alternative "A" requests relief from having to retroactively restate its tables to exclude these accounts and seeks permission to simply exclude these accounts prospectively.

The use of proprietary trading results in soliciting customer accounts is a practice which has long been of concern to the Commission. The Commission expressly addressed the issues raised by the inclusion of proprietary trading results in Disclosure Documents in extensive revisions to the disclosure requirements applicable to commodity trading advisors and commodity pool operators (the "Part 4 Revisions") which were adopted effective August 24, 1995.¹

In proposing and adopting the Part 4 Revisions, "several commenters suggested that if proprietary accounts are traded in a manner similar to pool and customer accounts, the rules should permit CPOs and CTAs to include the performance in a composite with customer accounts, provided *pro forma* adjustments are made for fees or other differences."² Your arguments in this area are well presented and provide a close case that has required careful staff analysis.

As a result of arguments, such as yours, the Commission regulation permits the use of proprietary trading results, subject to certain safeguards to ensure that past performance presentation is consistent across CTAs. However, in order to assure consistency of presentation of performance data across CTAs with varying levels of customer and proprietary trading, it was determined that Rule 4.34(n)(3)(iii) would be written to require that any proprietary trading results (together with any hypothetical, extracted, pro-forma or simulated trading results) be placed at the end of the Disclosure Document in order to minimize the likelihood that the proprietary results will be afforded undue weight.³

Thus, in order to ensure consistency in presentation among diverse CTAs, the circumstances presented by your request do not justify a waiver of the Commission's requirements, despite the individual circumstances discussed in your letter. This is particularly true since the Commission's rules do not preclude the presentation of proprietary trading results. Consequently, the Division will not grant no-action relief to enable you to consider these accounts as non-proprietary.

Further, there is no compelling reason advanced for permitting the restatement of the track record to only be prospective from the date of this letter. Rather, the tables need to be restated for all periods where the accounts are proprietary in nature. However, it should be noted that, for the period the affiliate's account was in fact a customer account (all times prior to the date the AP status became effective) it may be treated as such in the performance table.

If you have any questions concerning this letter, please contact Kevin P. Walek at (202) 418-5463.

Very truly
yours,

Robert B.
Wasserman

Associate
Director

cc: Daniel A. Driscoll

National Futures Association

¹ See 60 Fed. Reg. 38146 at 38167-38168 (July 25, 1995). Prior to the Part 4 Revisions, use of proprietary trading results was not specifically referenced in the Commission's rules, although Commission staff had advised registrants that any proprietary trading results presented in a Disclosure Document must be clearly labeled as such and presented in a separate table. See 59 Fed. Reg. 25351, 25360 (May 16, 1994).

² See 60 Fed. Reg. at 38167-38168.

³ See 60 Fed. Reg. 38146 at 38167.