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To: Jean Webb, Secretary of the Commission
From: Yves Balcer, FORT, Inc.
Ref: Comments on partially-funded accounts managed by CTAs.

First, the Concept Release of the CFTC is a significant step in the right direction as the Commission recognizes the lack of reliability of current guidelines in providing the investor-public with useful and comparable information across managers and asset classes (alternatives to CTAs' offerings)

Second, the invitation for further comments leaves open the door to further progress in that direction.

Before engaging in a technical debate on performance measurement, let us step back and ask ourselves what are we trying to accomplish with the regulations on performance reporting, and then, how best to accomplish those goals.

The true goal of standardized performance reporting is to allow the investors the possibility to compare across various CTAs their past returns (possibly inferring something about possible future ranking), and comparing CTAs returns to those of alternative assets. First and foremost, the reported performance should reflect the results that an investor would have earned had she chosen to invest with the CTA over the reporting period. Clearly, the best proxy for those results is the actual returns obtained by the manager for comparable accounts over the reported period, as everyone will attest from the commission on down to the lowliest of CTA.

In general, actual performance is true performance. This is surely true for fully funded accounts; and, as the Commission has recognized over the years, the way to insure true performance reporting was the fully-funded subset method. However, as investors became more savvy in the management of their cash (and sought more specialized managers for the investment of cash), and CTAs wanted to exhibit lower risk profile programs (with lower leverage and margin), the standard account is now partially-

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funded. This new development presents a problem as many CTAs, particularly emerging CTAs, have no fully funded accounts.

This problem was addressed by the Commission in its directive under review that for purpose of performance calculation, the notional size may be used as it is the size of funds upon which risk decisions are taken by the CTA.

If performance for all CTAs were reported ex-interest, (pure trading performance net of commissions and fees), the problem would be solved on two counts: performance would be actual, and comparable across all CTAs. This would be fine and be the end of it. However, CTAs do not operate in a vacuum: they must compete not just amongst each other but against asset classes (the main competition of our industry, as we represent less than 1% of total assets under management).

To fulfill our primary objective of insuring that the performance remains comparable both across CTAs and asset classes, interest earnings must be included in the computation of performance. This is not a problem for those CTAs with fully funded accounts. But for CTAs with partially funded accounts and for those who do not have any control on the investment of cash (and more often than not in those cases, returns from cash are not reported on the statements seen by CTAs), it is problematic. Their reported performance is not comparable and is seriously handicapped relative to their peers.

To illustrate the point, let us examine the reported performance of two CTAs with the same trading profits, commissions and fees. CTA-1 manages a fully funded account while CTA-2 manages a partially-funded account with no cash reported on the account. CTA-1 reports an actual net performance of 15% for the year, while CTA-2 reports an actual net performance of 12%. In addition, CTA-1 had a drawdown of 5% that lasted 3 months, while CTA-2 had a drawdown of 7% that lasted 6 months. Armed with that information, most investors would chose CTA-1 over CTA-2, but is the client well informed by the proposed regulation. Hypothetically, if CTA-2 had included an imputed interest on notional funds (4.8% per annum), he would have reported 16.8% returns with a drawdown 4.6%; clearly a better choice. Had it been so reported, the client would have more likely chosen CTA-2, assuming that client selects CTAs based on performance and risk-adjusted performance.

The facts are clear: inclusion of interest earnings is necessary for CTAs to be comparable to other asset classes; and therefore, imputed interest is necessary for CTAs to remain comparable to one another. However, how do we prevent misrepresentation (intentional or not) of the performance while allowing imputed interest on notional funds.

First, divulgence of the fact that imputed interest has been added to performance, and the percentage return attributable to imputed interest.

Second, standardization of imputed interest. Imputed interest can only be the rates of returns on 3-month T-bills minus 25 basis points (data series available daily from the fed).

Third, uniformity. If imputed interest method is chosen by a CTA, it should be applied uniformly to all accounts used in creating performance table.

Fourth, the notional size of the account shall not be increased by the amount of imputed interest.

In imposing these four steps, the commission could insure that reported results reflects the true performance that a client could have obtained using the services of that CTA.

In summary, allowing CTAs with some funded accounts to report their results including the returns from interest (currently 5% per annum, almost one third of the average returns of a typical CTA), while forcing other less fortunate CTAs who have only partially funded accounts with no control over the investment of the cash report their results without the benefits of interest investment is a great disservice to potential investors. How are they to compare the various CTA programs when the Commission cannot assure a uniform performance reporting?

We are confident that the Commission will allow those changes to take in order to provide clients with more representative information on CTA programs. We will be very happy to present our views in person to the Commission and to participate in the preparation of guidelines if the Commission wishes to avail itself of our services.