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Consumer Federation of America

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COMMENT

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OFC. OF THE SECRETARIAT

Jean A. Webb
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: Performance Data and Disclosure for Commodity Trading Advisors

Dear Ms. Webb:

I am writing on behalf of the Consumer Federation of America (CFA)[1] to express our strong opposition to the proposed rules to change the way past performance is calculated and disclosed to prospective investors in trading programs offered to the public by commodity trading advisors (CTAs). We opposed a similar proposal when it was issued in 1999 on the grounds that it would diminish the value of performance data in supplying information to investors about investment risks and in allowing investors to make meaningful comparisons among various investment options. That continues to be our position. With investors battered by more than a year of relentless corporate scandals and most policymakers looking for ways to rebuild investor confidence, it is frankly incomprehensible that the commission would choose this time to revive this anti-investor proposal.

The proposal would change the way rate of return is calculated for CTA accounts by substituting nominal account size for actual cash funding as the denominator in the calculation. The commission argues that this would provide a more accurate picture of the CTAs' past trading results.[2] This may be so, but it would also provide a far less accurate picture of the real life experience of investors in those accounts, a growing number of whom, according to the

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[1] Consumer Federation of America is a non-profit association of roughly 300 pro-consumer groups. It was founded in 1968 to

[2] The commission also argues that the change is needed because CTAs may not always be able to determine actual cash funding of accounts. The obvious solution to that problem, however, is to require the information sharing that would make such a determination possible. This would seem to be well within the commission's authority. But if it is not, the commission should seek that authority from Congress.

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commission, participate through partial funding.

The proposal appears to be based on a fundamental misunderstanding of the purpose of performance disclosure. The underlying view seems to be that the primary value of this disclosure is to allow traders to showcase their past trading results. While that view is understandable coming from an industry trade association, it is disturbing coming from a regulator, which should be warning investors of the dangers of relying on past performance in selecting investments, not making it easier for industry to tout their services on this basis.

In fact, the primary benefit of disclosing past performance to prospective investors is its ability to elucidate the volatility that a particular investment has experienced in the past and, thus, the risks the investor runs of losing some or all of his money. When investors weigh a decision between investing a sum of money in a mutual fund, a REIT, individual stocks, or an account managed by a CTA, the relevant performance comparison involves the return they might expect to get, and the size of the losses they could conceivably suffer, on the money put up. When losses could even exceed the initial investment, clear and comparable disclosures of those risks are even more essential.

Because it relies on a number -- nominal account size -- in calculating past performance that is totally irrelevant to the actual cash put up by the majority of participants in CTA accounts, the proposed rule would make it far more difficult for investors to make such assessments. Furthermore, because nominal account size is generally far larger than actual cash funding, the proposed rule would have the effect of reducing the appearance of volatility for such accounts. And, because the commission proposes to use the nominal account size method for calculating key risk information, such as peak-to-valley drawdown figures, this misleading information would be incorporated throughout the disclosures designed to warn investors of potential risks.

The commission argues that required disclosures in performance tables showing the effect of partial funding on worst monthly and peak-to-valley drawdowns will counteract this effect. But that is like arguing that a disclosure statement in tiny type at the bottom of an ad (that a particular type of brokerage account is not an advisory account, for example) will counteract a multi-million dollar advertising campaign designed to create exactly the opposite effect. It fails to answer the fundamental question: why should the only relevant information about the real risks the majority of participants in such accounts are likely to face be relegated to a few lines in a performance table, while the bulk of performance information provided to investors serves to minimize or mask those risks?

Despite the rule release's statements to the contrary, the proposed rule would not even make it easier to compare various CTA accounts on the basis of past performance. This is because, as the rule release clearly states, "there is no standard among CTAs for the setting of nominal account sizes," and the commission has no intention of setting such a standard. It doesn't take a mathematical genious to realize that, if you use non-standardized figures in a calculation, the results will not be comparable. This would be like trying to compare miles per gallon on different makes of car if the manufacturers were free to perform the calculations using their own definitions of what constitutes a gallon. In short, the rule would create the illusion of

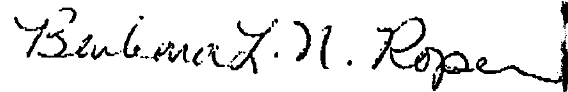
comparability without the reality. For the commission to claim otherwise is both disingenuous and disturbing.

The only thing likely to produce *less* comparable disclosures would be adoption of a "core principles" approach to performance disclosures as contemplated in the rule release. Furthermore, such an approach would leave the commission with few enforcement tools to prosecute misleading disclosures, except in the case of the most egregious violations. The commission should not go down this road.

With neither interest rates nor stock markets today providing particularly attractive alternatives, today's investors are highly vulnerable to pitches that offer the promise of a decent return. Having been burned by both the bursting of the tech stock bubble and the recent wave of corporate scandals, however, today's investors are also newly sensitive to the risks that investing can carry. In the current environment, regulators have a clear obligation to ensure that investors receive the information that will allow them to make sound risk-reward determinations.

This rule proposal fails that test. It places industry's interest in touting trading results over investors' need for sound risk disclosures. It should be scrapped in its entirety. Instead, the commission should focus on ways to improve the current system of performance disclosure, based on the only concrete number that reflects investors' real world experience -- actual cash funding of accounts.

Respectfully submitted,



Barbara Roper
Director of Investor Protection