

MEMO# 27052

February 26, 2013

ICI Submits Request to CFTC Staff for Fund of Funds Guidance

[27052]

February 26, 2013

TO: CLOSED-END INVESTMENT COMPANY MEMBERS No. 23-13
COMPLIANCE MEMBERS No. 14-13
DERIVATIVES MARKETS ADVISORY COMMITTEE No. 22-13
ETF (EXCHANGE-TRADED FUNDS) COMMITTEE No. 14-13
ETF ADVISORY COMMITTEE No. 13-13
SEC RULES MEMBERS No. 27-13
SMALL FUNDS MEMBERS No. 17-13
UNIT INVESTMENT TRUST MEMBERS No. 7-13 RE: ICI SUBMITS REQUEST TO CFTC STAFF
FOR FUND OF FUNDS GUIDANCE

ICI and the Investment Adviser Association (IAA) have jointly submitted to the Division of Swap Dealer and Intermediary Oversight (Division) of the Commodity Futures Trading Commission a request for revised guidance on how the de minimis thresholds in CFTC Rules 4.5 and 4.13(a)(3) will be applied to a fund of funds (FOF). The letter is attached and briefly described below.

Background

In July 2012, ICI and IAA submitted an initial request for FOF guidance, based on former Appendix A to Part 4 of the CFTC's rules. That request sought to apply the Appendix A principles to advisers to registered investment companies along with private funds (together, funds), as well as expand the breadth of situations to which revised FOF guidance would apply. Since that time, we have had several discussions with the CFTC staff about possible revised guidance in this area. Last November, the Division granted temporary no-action registration relief for managers of FOFs (FOF Managers) while it continues to develop revised FOF guidance.

The need for clear guidance has become more important in light of the Division's indications that a fund's investments in securities issued by securitization vehicles, REITs and business development companies (collectively, Non-Traditional Pools) could cause an investing fund to be deemed a FOF. If followed, this approach could significantly increase the number of fund advisers that may be required to register as commodity pool operators (CPOs) based on their funds' investment in such securities.

ICI / IAA Letter

The letter requests that the Division develop FOF guidance that is sufficiently broad to cover a range of FOFs, including (1) funds that invest in other registered and/or private funds, (2) funds that engage sub-advisers to manage one or more portions of the fund's assets (each a Sub-Advised Sleeve) or that are structured as multi-manager funds, (3) funds that invest in securities issued by Non-Traditional Pools, and (4) funds pursuing a combination of these approaches. After offering insights regarding FOF investor expectations and the difficulty that FOF Managers have in obtaining information on commodity interest trading by underlying funds and Non-Traditional Pools, the letter sets forth recommendations for how the Division's guidance can be made flexible and workable for FOF Managers and still achieve what we understand the Division's objective to be—to exclude from regulation only those FOF Managers whose direct and indirect commodity interest trading is below a certain level.

The letter recommends that the Division's guidance:

1. be crafted broadly to cover a range of FOFs;
2. permit a specified level of investment, without a look-through, in underlying funds managed by registered CPOs and commodity trading advisors that are acting in a registered capacity with respect to these underlying funds and (b) Non-Traditional Pools;
3. clarify the treatment of direct trading in commodity interests by the FOF Manager;
4. clarify the treatment of a Sub-Advised Sleeve, both as a portion of a "true" FOF and in a multi-manager fund;
5. include a "reasonable belief" standard for FOF Managers that must look through certain underlying funds;
6. permit periodic testing for compliance with the de minimis limitations by the FOF Manager;
7. provide a transition period for a FOF Manager that can currently rely on Rule 4.5 or 4.13(a)(3) and then subsequently determines that it needs to register as a CPO;
8. provide relief for FOFs that invest in underlying funds that do not issue interests/shares that are periodically redeemable; and
9. provide relief for FOFs that cannot easily change their investments once formed.

Rachel H. Graham
Senior Associate Counsel

Sarah A. Bessin
Senior Counsel

[Attachment](#)