

MEMO# 24867

January 12, 2011

ICI Comment Letter Requesting Exemption from Position Limits for Diversified Funds

[24867]

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TO: CLOSED-END INVESTMENT COMPANY MEMBERS No. 2-11
ETF ADVISORY COMMITTEE No. 3-11
EQUITY MARKETS ADVISORY COMMITTEE No. 3-11
FIXED-INCOME ADVISORY COMMITTEE No. 3-11
SEC RULES MEMBERS No. 4-11
SMALL FUNDS MEMBERS No. 2-11 RE: ICI COMMENT LETTER REQUESTING EXEMPTION
FROM POSITION LIMITS FOR DIVERSIFIED FUNDS

The Institute has submitted a comment letter to the Commodity Futures Trading Commission on the use of position limits for derivatives. The letter advocates for an exemption from position limits for diversified registered investment companies (“RICs”) that comply with the leverage requirements of the Investment Company Act of 1940 (“Investment Company Act”) and that take passive, long-only positions (“diversified funds”). The letter is summarized below.

I. Exemption from Position Limits

In support of this position, the letter begins by establishing that the CFTC has the authority to grant an exemption from position limits for any person or class of persons. The letter then walks through some of the benefits of having diversified funds investing in the futures and swaps markets. It explains that diversified funds serve as a stable, long-term source of liquidity and facilitate efficient price discovery in these markets. It also explains that diversified funds are not speculators but rather are long-term investors, and that diversified funds provide small investors with a cost-effective means of diversifying their portfolio and investing in the commodity derivatives markets. As another justification for an exemption from position limits for diversified funds, the letter details some of the restrictions placed on RICs under the Investment Company Act, noting that these restrictions limit the ability of

diversified funds to speculate or contribute to systemic risk.

II. Aggregation

The letter recommends that, if the CFTC determines not to provide an exemption for diversified funds, it permit advisers to report the positions of each of their clients separately instead of requiring them to aggregate the positions of any fund with the positions of other funds managed by the same adviser or its affiliates. The letter explains that each fund is a separate client of a registered investment adviser, with a separate group of investors and independent investment objectives. Further, as a fiduciary, advisers to these funds must make decisions based on the objectives and needs of each individual diversified fund without taking into account other diversified funds' positions. The letter therefore states that there is no reason to believe diversified funds managed by the same adviser or its affiliates would inappropriately engage in manipulative trading activity.

III. Bona Fide Hedging

The letter urges the CFTC to define "bona fide hedging" as it is commonly understood in the investment industry and adopt a definition that encompasses both commercial and financial hedging.

IV. Position Points

The letter notes that the CFTC has recently discussed the implementation of a "position points" regime that would be implemented as an interim measure until the CFTC has gathered data to fully implement position limits. The letter questions whether the CFTC has the legal authority to pursue the "position points" concept absent a notice and comment rulemaking process. It also states that the criteria for when the CFTC may elect to enforce "position points" is vague and uncertain, which could have an adverse affect on market participants' interest in participating in the futures and swaps markets, thereby reducing market liquidity. The letter concludes by recommending that the Commission refrain from exercising enforcement of "position points" without providing the public an opportunity to provide input.

Heather L. Traeger
Associate Counsel

[Attachment](#)

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