

MEMO# 35486

October 16, 2023

CFTC Proposes Revisions to the Regulation 4.7 Exemption for CPOs and CTAs

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TO: Registered Fund CPO Advisory Committee RE: CFTC Proposes Revisions to the Regulation 4.7 Exemption for CPOs and CTAs

On October 2, 2023, the CFTC published a proposed rule ("Proposal") that would significantly revise CFTC Regulation 4.7, a provision that provides exemptions from certain compliance requirements for commodity pool operators (CPOs) with respect to commodity pool offerings to qualified eligible persons (QEPs) and for commodity trading advisors (CTAs) with respect to trading programs advising QEPs.

Comments on the Proposal are due on December 11, 2023. ICI will hold a member call on this Proposal on October 23, 2023, from 3-4:00 pm ET. We will circulate a call invite and agenda closer to that date. It is our understanding that the Proposal is likely to impact members, particularly as it relates to how advisers comply as CPOs and CTAs under Regulation 4.7 with respect to controlled foreign companies (CFCs) wholly owned by registered funds. Please feel free to reach out to Kevin Ercoline, at kevin.ercoline@ici.org, or Sarah Bessin, at sarah.bessin@ici.org, with any comments or questions prior to the call.

The Proposal would amend Regulation 4.7 in three primary ways:

- (1) Doubling the "Portfolio Requirement" monetary thresholds within the "QEP" definition to account for the effects of inflation;
- (2) Requiring new minimum disclosure requirements for CPOs and CTAs operating pools and trading programs in reliance on Regulation 4.7 ("Regulation 4.7 CPOs and CTAs"); and
- (3) Codifying routinely issued exemptive relief allowing CPOs of "Funds of Funds"[\[2\]](#) that rely on Regulation 4.7 to choose to distribute monthly account statements within 45 days of

the month-end.

While each of these amendments will affect CPOs and CTAs that rely on Regulation 4.7, it is the minimum disclosure requirements that are the most significant and substantial. A summary of the Proposal is below.

Updating Financial Thresholds in the "Portfolio Requirement" of the "Qualified Eligible Person" Definition

Regulation 4.7(a) bifurcates the definition of QEP into two different categories: 1) those that do not need to meet the "Portfolio Requirement" to be a QEP and 2) those that do. The Portfolio Requirement has remained unchanged since 1992, and the CFTC is proposing to update the financial amounts to reflect inflation. The "Securities Portfolio Test" will be doubled to \$4,000,000 and the "Initial Margin and Premium Test" will be doubled to \$400,000. The CFTC would continue to permit persons to meet the Portfolio Requirement through a combination of the two, as is currently allowed.

The CFTC recognizes that these increases will likely result in a certain portion of currently qualifying QEPs no longer meeting the Portfolio Requirement. Current Regulation 4.7(a)(3) provides that CPOs must assess a person's QEP status, including satisfaction of the Portfolio Requirement, at the time of sale of any pool participation units, and that CTAs must make a similar assessment at the time that a person opens an exempt account. The CFTC intends to maintain this "time of assessment" aspect of the rule so that the new thresholds would only apply to new sales of pool participation units or new accounts and not cause advisory relationship terminations or forced divestitures.

Establishing Minimum Disclosure Requirements Under Regulation 4.7

A. Minimum Disclosure Requirements for Regulation 4.7 CPOs

Under the Proposal, Regulation 4.7(b)(2)(i) would be amended to no longer provide an exemption from Regulation 4.21, which requires distribution of a disclosure document. However, instead of requiring full compliance with Regulations 4.24 and 4.25, which detail the disclosure to be provided in the document, the Proposal would provide for more limited disclosure, detailed in new proposed Regulations 4.7(b)(2)(i)(A)-(E). These proposed disclosures include the pool's principal risk factors, investment program, use of proceeds, custodians, fees and expenses, conflicts of interest, and certain performance disclosures, including past performance. Related to the Commission's proposal to require new disclosures for QEP investors, it proposes to remove the exemption from disclosing the past performance of pools whose operators rely on Regulation 4.7 in the disclosure documents of pools whose operators do not rely on Regulation 4.7. The CFTC is also proposing to retain, but reformat, the existing disclosure language currently required by Regulation 4.7.

The CFTC would require that QEP disclosures used and distributed by Regulation 4.7 CPOs be kept current and that they be maintained as business records to ensure compliance and to facilitate CFTC and NFA oversight. Finally, the Proposal would continue to exempt CPOs from NFA's filing and pre-approval requirements for disclosure documents.

B. Minimum Disclosure Requirements for Regulation 4.7 CTAs

Similar to the amendments for Regulation 4.7 CPOs discussed above, the CFTC proposes to

eliminate the exemption for Regulation 4.7 CTAs from providing a disclosure document to QEP clients. Instead of requiring these CTAs to comply fully with Regulations 4.34 and 4.35, which detail the disclosure to be provided in the disclosure document, the CFTC proposes more limited disclosures for QEPs. Proposed Regulation 4.7(c)(1)(i) would include new paragraphs (c)(1)(i)(A)-(F), which require descriptions of certain persons to be identified, the principal risk factors of the investment, the CTA's trading program, fees, conflicts of interest, and performance disclosures. Additionally, the CFTC is proposing to retain, but reformat, the existing language currently required by Regulation 4.7.

The CFTC also proposes to eliminate the exemption for CTAs from disclosing past performance of Regulation 4.7 CTA trading programs in the disclosure documents of non-4.7 trading programs. As with CPO disclosures, the CFTC would continue to exempt CTAs relying on Regulation 4.7 from NFA's filing and pre-approval requirements for disclosure documents but would require that QEP disclosures of Regulation 4.7 CTAs be kept current and be maintained as business records of the CTA to ensure compliance and to facilitate CFTC and NFA oversight.

Permitting Monthly Account Statements for Pools Under Regulation 4.7 Consistent with Commission Exemptive Letters

CPOs relying on Regulation 4.7 currently are required to distribute account statements to pool participants no less frequently than quarterly, within 30 days after the end of the reporting period.^[3] Regulation 4.7 CPOs of pools that are Funds of Funds are often unable to comply with this quarterly account statement schedule because they cannot control the timing of when they receive the financial information of the underlying funds. The CFTC has routinely granted exemptive letter requests permitting these Regulation 4.7 CPOs to distribute monthly, rather than quarterly, account statements for their pools that are Funds of Funds within 45 days of the month-end. The CFTC proposes to codify this exemptive relief by amending Regulation 4.7 to provide that the CPO of a Fund of Funds may choose instead to prepare and distribute to its pool participants statements on a monthly basis within 45 days of the month-end, provided that the CPO notifies its QEP pool participants so that they are aware of the account statement distribution schedule.

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Notes

^[1] Commodity Pool Operators, Commodity Trading Advisors, and Commodity Pools: Updating the 'Qualified Eligible Person' Definition; Adding Minimum Disclosure Requirements for Pools and Trading Programs; Permitting Monthly Account Statements for Funds of Funds; Technical Amendments, 88 Fed. Reg. 70852 (Oct. 12, 2023), available at <https://www.cftc.gov/sites/default/files/2023/10/2023-22324a.pdf>. CFTC Commissioner Mersinger dissented and issued a [statement](#) raising concerns about the process by which the Proposal was issued and the disclosure obligations it would impose. She poses 10

questions on which she requests public comment. Commissioner Pham voted in favor of the Proposal but issued a separate [concurring statement](#).

[2] As defined in the Proposal, "Funds of Funds" means pools that invest in unrelated funds, pools, or other collective investment vehicles.

[3] As it relates to registered funds using a CFC, the CFTC has stated that it views the CFC and registered fund relationship as akin to a master-feeder structure for the purposes of complying with Part 4 of the CFTC's regulations and therefore the CPO of the CFC is exempt from providing the required documents to the registered fund. See CFTC Division of Swap Dealer and Intermediary Oversight Responds to Frequently Asked Questions - CPO/CTA: Amendments to Compliance Obligations (Aug. 14, 2012), http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/faq_cpocta.pdf.

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