

ICI VIEWPOINTS

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CFTC Decision Imposes Inconsistent Requirements on Funds, Hurts Shareholders

The Commodity Futures Trading Commission (CFTC) recently finalized a rule—[known as Rule 4.5](#)—that will require many advisers to mutual funds that invest in commodity futures, commodity options, and swaps to register with the agency. This development is deeply troubling for at least two reasons:

1. It will impose duplicative and fundamentally inconsistent requirements on these funds.
2. Shareholders will pay the ultimate price for this rule in the way of increased fees and fewer investment options.

Some context is necessary to explain why we are so concerned about the implications of the CFTC's decision and its ultimate impact on shareholders. Mutual funds can use options, futures, swaps, and other derivatives to efficiently manage their portfolios and to provide exposure to the commodity markets for shareholders that seek diversification. Funds have for many years used derivatives to hedge the currency risks associated with investing in foreign markets. They use them to fine-tune the risk profiles of fixed income portfolios without constantly buying and selling bonds, which can be very expensive. And derivatives allow funds to gain investment exposures to asset classes that are too difficult or costly to access directly, such as some foreign markets. All of these uses of derivatives assist mutual funds to provide shareholders with investment products and choices that meet their needs in an efficient manner.

As we explained in our [April 12, 2011 comment letter](#), the CFTC's new amendments to Rule 4.5 will unnecessarily subject potentially thousands of mutual funds to duplicative and fundamentally inconsistent regulatory requirements. While we respect the CFTC's authority to regulate the derivatives markets, we believe Rule 4.5 represents an unnecessarily broad and unjustified overreach by the CFTC into the oversight of mutual funds, which already are comprehensively regulated by the Securities and Exchange Commission (SEC). In fact, mutual funds are the only investment products that are regulated under all four of the major federal securities laws.

Furthermore, the CFTC has not adequately justified the need for the additional regulatory burdens that Rule 4.5 will impose on funds. As Commissioner Sommers points out in her [dissenting statement](#) to the Rule, the CFTC also has failed to explain why the extensive

information reporting it will now require of mutual funds is justified for systemic risk purposes. We agree with Commissioner Sommers that the Rule's cost-benefit analysis is "sorely lacking."

The CFTC also proposes to "harmonize" certain CFTC and SEC rules that would apply to mutual funds investing in commodities. In reality, this proposal offers more duplication than harmonization. For example, the additional disclosure requirements that would be imposed by this rule would result in lengthy and confusing prospectus disclosures to fund shareholders. This end result is inconsistent with the SEC's focus in recent years on making mutual fund prospectuses simpler and more readable for shareholders.

Unfortunately, mutual fund shareholders will bear the brunt of the additional regulatory burdens the CFTC has imposed upon funds. Subjecting funds to duplicative and burdensome regulatory requirements will increase costs for fund shareholders, as funds seek to meet increased reporting obligations that are more likely to create confusion than clarity. These additional regulatory burdens ultimately are likely to result in fewer choices for mutual fund shareholders who seek to gain exposure to commodities as a component of a diversified investment portfolio. As a result of Rule 4.5, mutual fund advisers may be forced to either limit their commodity investments, or seek that exposure through more costly means. Neither of these results is in the best interests of fund shareholders.

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