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April 12, 2011

VIA ELECTRONIC MAIL

Mr. David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581
agswapsANPR@cftc.gov

Re: RW3038-AD30 – Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations

Dear Mr. Stawick:

The Commodity Futures Trading Commission ("CFTC" or "Commission") has requested public comment on its proposal to repeal certain exemptions from rules requiring registration as a Commodity Pool Operator ("CPO") and Commodity Trading Advisor ("CTA") currently provided in Rules 4.13 and 4.14 of the CFTC's regulations.[1] As the CFTC has noted in the proposing release, over 10,000 exemption notices under Rules 4.13(a)(3) and 4.13(a)(4) alone have been filed since 2003.[2] Many of these notices have been filed by our clients. Skadden, Arps, Slate, Meagher & Flom LLP ("Skadden") appreciates the opportunity to express our views on this issue of importance to our clients and the private funds community generally.

In 2003, the CFTC adopted these exemptions because, without jeopardizing investor protection, they would "encourage and facilitate participation in the commodity interest markets [that will] benefit . . . all market participants [through] increased liquidity."[3] The Commission's 2003 policy judgment remains valid today, a conclusion that is confirmed by the Commission's failure accompany its proposed repeal of its 2003 judgment with sufficient justification.

1 Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations, 76 Fed. Reg. 7,976 (Feb. 11, 2011) (the "Proposed Rules").

2 76 Fed. Reg. 7,986, n. 69.

3 Additional Registration and Other Regulatory Relief for Commodity Pool Operators and Commodity Trading Advisors; Past Performance Issues, 68 Fed. Reg. 47,221, 47,223 (Aug. 8, 2003).

Accordingly, we request that the Commission withdraw its proposed repeal of these exemptions. If the CFTC disagrees and decides to repeal the exemptions in Rules 4.13 and 4.14, as discussed below, we request that the CFTC (i) provide an exemption for family offices; (ii) grandfather previously exempt entities; and (iii) provide *de minimis* exceptions, including an exception for registered investment advisors of pools with less than 50% of their assets invested in commodity interests.

Current Registration Exemptions Under Rules 4.13 and 4.14 that the Commission Proposes to Repeal

Rule 4.13(a)(3) currently exempts a person from registration as a CPO for a pool if (1) the pool's interests are exempt from registration under the Securities Act of 1933, as amended (the "Securities Act"); (2) the pool's interests are offered only to certain sophisticated persons, including Qualified Eligible Persons under Rule 4.7 ("QEPs") and accredited investors as defined in Regulation D of the Securities Act; and (3) the pool's aggregate initial margin and premiums attributable to futures and options on futures do not exceed five percent of the liquidation value of the pool's portfolio and the aggregate notional value of such positions does not exceed 100 percent of the liquidation value of the pool's portfolio. Under Rule 4.13(a)(4), persons are exempt from registration as a CPO for a pool if (1) the interests in the pool are exempt from registration under the Securities Act and (2) the operator reasonably believes that all participants are QEPs or accredited investors (and participants that are natural persons must hold at least $2 million in portfolios of securities or similar investments).

Rule 4.14(a)(8)(i)(D) currently exempts a person from registration as a CTA for a pool if, among other requirements, the advised pool has a CPO that qualifies for exemption from registration under Rules 4.13(a)(3) or 4.13(a)(4), as long as the advisor does not hold itself out as a CTA.[4]

No policy purpose is served by repealing these exemptions. If these exemptions are repealed, many thousands of persons will be required to register with the CFTC.

The CFTC Should Not Repeal the Private Fund Exemptions – The CFTC Has Not Stated Sufficient Reasons for Repealing the Exemptions

Before rescinding a rule, an agency must "examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.'" *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 42 (1983). An agency must articulate good cause for departing from a standing policy, which is presumed to have been adopted for valid reasons. *See id.*; *see also Western States Petroleum Ass'n v. E.P.A.*, 87 F.3d 280, 284 (9th Cir. 1996).

[4] For convenience, we refer to the exemptions in 4.13(a)(3), 4.13(a)(4) and 4.14(a)(8) as the "private fund exemptions."

Here, the CFTC has not established the "rational connection" or a rulemaking record that justifies rescission of the exemptions. The CFTC proposal cites no enforcement actions, fraud concerns or other facts suggesting any regulatory problems with private funds whose CPOs and CTAs have relied on these exemptions. Instead, the CFTC cites a handful of reasons to justify its new policy. Once analyzed, none of these reasons offers an adequate basis for repeal.

The first reason cited by the CFTC for proposing the exemption repeal is that the repeal will help bring the CPO and CTA regulatory structure into alignment with the stated purposes of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), Pub. L. 111-203 (2010), by improving transparency and oversight of large private investment funds.[5] If Congress was concerned that exempt CPOs and CTAs should be registered, Congress could have amended the Commodity Exchange Act (the "CEA") in Dodd-Frank to require exempt CPOs and CTAs to register, but did not. Similarly, if Congress thought that the private offering requirement in the exemptions now subject to the CFTC's proposed repeal was too broad, Congress could have narrowed or eliminated the private offering exemption in the Securities Act, but did not. In contrast, by enacting Dodd-Frank, Congress demonstrated that, when it determines an exemption no longer serves the public interest, Congress will amend that exemption, as it did when it eliminated the 15-client private adviser exemption in the Investment Advisers Act of 1940, as amended (the "Advisers Act").[6] Congress took no such action with regard to the exemptions the CFTC now proposes to repeal and nothing in Dodd-Frank requires, or, even by implication, supports eliminating these exemptions.[7]

In relying on Dodd-Frank for support, the CFTC states that the repeal will help ensure consistent regulation of similarly situated entities among federal agencies in order to limit regulatory arbitrage.[8] Again, however, Dodd-Frank evidences the opposite. For example, Dodd-Frank eliminated the 15-client private adviser exemption in the Advisers Act, but retained the 15-client exemption for CTAs in the CEA, indicating a Congressional recognition that similarly situated entities should be treated differently.[9]

Another reason offered by the CFTC for repealing the private funds exemptions is that the repeal will improve accountability and transparency of the activities of pools.[10] An example

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5 76 Fed. Reg. 7,985-86.

6 Dodd-Frank § 403, amending Advisers Act § 203(b)(3).

7 The only changes Dodd-Frank made to the CEA in respect of CPOs and CTAs are the definitional changes to 'commodity pool', CPO and CTA to include swaps and similar changes to CEA § 4m to include swaps. Dodd-Frank §§ 721(a) and 749(b). The amendments to § 4m(3) also underscore the exception from CTA registration for CTAs who advise pools not primarily engaged in commodity interest trading. Dodd-Frank § 749(b), amending CEA § 4m(3).

8 76 Fed. Reg. 7,986.

9 *Compare* Dodd-Frank § 403, amending Advisers Act § 203(b)(3) *with* CEA § 4m(1).

10 76 Fed. Reg. 7,985.

offered by the CFTC was that, under the current exemption in Rule 4.13(a)(3), an exempt commodity pool with less than five percent of its liquidation value committed to margin could nevertheless be large enough to be "a major participant in the futures market."[11] Accountability and transparency of market participants with large futures positions already are addressed by the CFTC's large trader reporting requirements, which will soon include large swap positions as well.[12] This long-standing and well-respected foundation of the Commission's surveillance program provides transparency for all major participants in the futures markets, whether a single person, private fund or public corporation. The Commission has stated no reason why its large trader reporting system – which applies to pools and all other market participants – is not adequate to address its accountability and transparency concerns. Nor has the Commission explained why registration of the CPO of a private fund would fill a perceived gap in its existing surveillance system or the additional new reporting and transparency provisions contemplated by Dodd-Frank.

In fact, to the extent swaps are traded by private funds with CPOs and CTAs eligible for the exemptions the CFTC proposes to repeal, Dodd-Frank already addressed accountability and transparency by adding swaps to the CFTC's large trader reporting mandate and creating the 'major swap participant' and 'major securities-based swap participant' categories. Congress also required the registration of these major participants in swaps in order to protect against systemic risk.[13] Notably, in requiring major participant registration, Congress did not require or suggest that any major participants needed to be otherwise regulated in order to improve transparency or accountability. The proposed repeal will not protect against systemic risk and will not provide additional accountability or transparency.

Finally, the CFTC has stated that expanding the universe of registered CPOs and CTAs will help "facilitate a collection of data that will assist the [Financial Stability Oversight Council ("FSOC")] . . . in the event that the FSOC requests and the Commission provides such data."[14] Any information the FSOC could need from private funds' CPOs and CTAs already is available to the CFTC, or will be available to it once Dodd-Frank is implemented. Under its general special call authority under CFTC Rule 21.03, the Commission can obtain a range of information as broad as it could obtain from a registered CPO or CTA if there is any threat of a market disruption. This special call for information would supplement the information the CFTC already receives on a regular basis through large trader reports. The CFTC would also have special call authority under Proposed Rule 20.5, which would require persons holding or controlling reportable positions (certain large positions in specified contracts) to make a 40S filing. A 40S filing would require the reporting person to submit a Form 40 (modified to include

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11 *Id.*

12 Position Reports for Physical Commodity Swaps, 75 Fed. Reg. 67,258 (proposed Nov. 2, 2010) (proposing 17 C.F.R. Part 20).

13 Dodd-Frank § 731, adding new CEA § 4s; *and* Dodd-Frank § 763, adding new Exchange Act § 15F.

14 76 Fed. Reg. 7,987.

swaps and swaptions) reporting certain large positions.[15] Moreover, there also is information provided in filings with the Securities and Exchange Commission (the "SEC") by advisers to private funds, as well as the information provided in the current private fund exemption filings made to the National Futures Association by private funds. Indeed, the CFTC itself does not cite any kinds of information beyond already available data that the CFTC needs for its enforcement or oversight duties.

In sum, the CFTC does not provide any facts or rationale that are adequate to support the repeal of these well-established private fund exemptions on which numerous people rely. In lieu of a supporting rationale, the CFTC appears to equate the need for accountability and transparency with registration. Decades of CFTC large trader reporting experience belie this central supporting theme of the CFTC's proposal. Even under Dodd-Frank, many futures and swap market participants (beyond private funds) with sizeable trading positions will not need to register in any capacity with the CFTC. But these same entities will be subject to the accountability and transparency afforded by the larger trader reporting system. Private funds will be part of that process, just as they are today. Registration for registration's sake is not an adequate basis for the CFTC, in effect, to revoke more than 10,000 notices of claims for exemptive relief that have been filed under Rules 4.13(a)(3) and 4.13(a)(4).[16] Based upon the foregoing, we urge the CFTC to withdraw its proposal.

Family Offices Should Be Afforded a Special Exemption From Registration

We represent a variety of family offices that already have been relieved from CPO registration in reliance on the exemptions from registration provided by Rules 4.13(a)(3) and 4.13(a)(4). We have received a number of inquiries from these family office clients regarding the proposed repeal of Rules 4.13(a)(3) and 4.13(a)(4) and the potential need for each of them to register as a CPO absent another exemption, exclusion or other form of relief. Should the Commission proceed with its repeal of these exemptions, we respectfully request that the CFTC consider the suggestions presented below and, prior to such repeal, take action to ensure that family offices are not required to register as CPOs or CTAs.

Family offices are multi-purpose entities that are intended to provide a broad range of services, including investment management services, to members of an extended family. Family offices employ a broad range of organizational, management, and employment structures and arrangements to manage the family's assets and achieve economies of scale. In particular, many family offices operate collective investment vehicles primarily owned by family members for the purpose of, among other things, trading, directly or indirectly, commodity interests. As a result, absent an exemption, exclusion or other form of relief, these family investment vehicles and the

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[15] The special call authority under Rule 21.03 and Proposed Rule 20.5 is in addition to the CFTC's authority to issue special calls under Rule 4.13 regarding eligibility and compliance with the exemption.

[16] 76 Fed. Reg. 7,986, n. 69.

family offices that operate them would constitute "pools" and "commodity pool operators," respectively, and the family offices would be required to register as CPOs.[17]

To their credit, the staff of the Division of Clearing and Intermediary Oversight and the staff of the former Division of Trading and Markets have repeatedly interpreted the definition of "pool" in Rule 4.10(d) to exclude certain types of family investment vehicles from its scope, typically where all direct or indirect participants were members of the same immediate or extended family, trusts for their benefit or the benefit of their issue and, in certain instances, long-time business associates of the applicable family.[18] The applicable interpretative,

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[17] Rule 4.10(d) defines the term "pool" to mean "any investment trust, syndicate or similar form of enterprise operated for the purpose of trading commodity interests." CEA § 1a(5) and Rule 1.3(cc) define "commodity pool operator" in a similarly broad fashion. The CFTC has stated that whether a particular entity is operated "for the purpose" of trading commodity interests and, therefore, is a commodity pool within the meaning and intent of Rule 4.10(d) depends on "an evaluation of all facts relevant to the entity's operation." Revision of Commodity Pool Operator and Commodity Trading Advisor Regulations, 46 Fed. Reg. 26,004, 26,006 (May 8, 1981).

[18] *See, e.g.*, *Rule 4.10(d)(1):--Request for Interpretation That Family Limited Partnerships are Not Commodity Pools, and Section 4m(1) of the Act:--Request for Interpretation That General Partners of Family Limited Partnerships are Not CPOs or CTAs*, CFTC Interpretative Letter No. 00-98 (May 22, 2000) (several family limited partnerships were not commodity pools and the general partners were not CPOs thereof where each member of the partnerships, including the general partners, was a member of the same extended family – i.e., three cousins and their immediate families), or trusts for their benefit or the benefit of their issue); *Section 4m(1) of the Act;--Request for No-Action Position From CPO Registration*, CFTC No-Action Letter No. 99-45 (Sept. 15, 1999) (a limited liability company was not a commodity pool whose members consisted of immediate family members and a long-term business associate of the family); *Section 4m(1) of the Act;-Request for No-Action Position From CPO Registration*, CFTC No-Action Letter No. 99-43 (Sept. 15, 1999) (a limited partnership was not a commodity pool whose partners consisted of immediate family members and a long-term business adviser to the family); *Request for Confirmation That General Partnership is Not a Commodity Pool Under Rule 4.10(d)(1) and Managing General Partner is Not a Commodity Pool Operator Under Section 1a(4) of the Act*, CFTC Interpretative Letter No. 97-50 (June 23, 1997) (enforcement action was not recommended against the managing general partner of a general partnership for failing to register as a CPO thereof, where a general partnership previously not found to be a commodity pool added three new general partners, two of whom were sons of a founding partner and the third was a close friend and long-time colleague of the managing general partner); *Rule 4.10(d): Confirmation That the Partnership is Not a Commodity Pool Where Participants are Immediate Family Members and One Long-Term Adviser*, CFTC Interpretative Letter No. 95-21 (Mar. 7, 1995) (a general partnership was not a commodity pool where the partners were immediate family members, trusts beneficially owned by these immediate family members and a long-term advisor to the family); *Request for Interpretation of Rule 4.10(d)*, CFTC Interpretative Letter No. 93-72 (July 26, 1993) (a limited partnership was not a commodity pool where the partnership consisted of the general partner, his wife, and a friend of over 30 years); *Request for Relief From Commodity Pool Operator Regulation*, CFTC Interpretative Letter No. 93-46 (May 19, 1993) (a limited partnership was not a commodity pool where all participants were immediate family members or long-term family friends (and their immediate families) of the general partner) ; *Re: "X"*, CFTC Interpretative Letter No. 93-48 (May 19, 1993) (a limited partnership was not a commodity pool and the general partner was not a CPO thereof where the participants were family members – i.e., the general partner and his wife, sister, brother-in-law, father, mother, grandmother and uncle or entities wholly owned by the these family members); *Interpretation of the Term "Pool" in Rule 4.10(d)*, CFTC Interpretative Letter No. 86-10 (Apr. 24, 1986) (a limited partnership was not a commodity pool where the partners consisted of two limited partnerships with partners from two unrelated families (including a 20-plus year associate of one family) and an individual unrelated to the families).

exemptive and no-action letters were all premised on the grounds that the family investment vehicles described therein were not within the meaning and intent of the commodity "pool" definition under Rule 4.10(d) and that the registration of the CPOs thereof would not further the primary purpose of the CPO registration requirements, which is to protect unsophisticated investors from undesirable managerial and trading practices.[19]

Nevertheless, countless family offices have still found it necessary or desirable to file notices of exemption under Rule 4.13(a)(3) or 4.13(a)(4) and to use, in effect, such exemptions as safe harbors. The reasons family offices make these filings are, at least, twofold. First, exemptive and no-action letters may only be relied on by the beneficiaries thereof, and interpretative letters are binding only upon the CFTC division issuing it, and not upon the CFTC itself.[20] Second, family offices employ a broad range of organizational, management, investment and employment structures and arrangements that vary from family to family. Consequently, many family pools and family offices do not fit squarely within the four corners of the facts and circumstances set forth in the previously issued interpretative letters and are therefore not comfortable relying on such letters. For example, many family pools include, as participants, employees of the family office that are not long-time (e.g., more than 10 year) business associates of the applicable family.

If Rule 4.13(a)(3) or 4.13(a)(4) is repealed without the CFTC taking other appropriate action, many family offices that have filed notices of exemption under such Rules, not to mention an endless number of future family offices, will be required to register or to seek their own "not a pool" interpretative or no-action letters notwithstanding the fact that the regulation of such persons is outside the intent and purpose of the CPO registration rules. Not only would such an outcome be unduly burdensome for both these family offices and the Commission[21], but it would be inconsistent with the clear and stated intent of Congress when enacting Dodd-Frank. In connection with Dodd-Frank, Congress recognized that there is no federal interest in regulating family offices that generally provide advice only to members of a family and that the application of the Advisers Act to family offices "would unnecessarily intrude on the privacy" of family members.[22] Accordingly, when eliminating the 15-client exemption under the Advisers

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[19] "[L]egislative history of [the CPO registration requirements] indicated that it was intended to bring CPOs within the Commission's jurisdiction for the purpose of protecting unsophisticated investors from undesirable managerial and trading practices." *See Request for Interpretation of Rule 4.10(d)*, CFTC Interpretative Letter No. 86-17 (June 24, 1986) (*citing* Statement of Dr. Clayton Yeutter, Assistant Secretary of Agriculture, House Committee of Agriculture Report on Commodity Futures Trading Commission Act of 1974, H.R. REP. NO. 975, 93rd Cong., 2d Sess. 79 (1974)).

[20] *See* Rule 140.99(a).

[21] Although some of these family offices could claim relief under Rules 4.7 or 4.12, any requirement to register would still unnecessarily intrude upon the privacy of family members and impose increased administrative costs on family offices without providing any corresponding benefit to the participants in family pools or the public and would still be inconsistent with the intent of the CPO and CTA registration requirements.

[22] S. Rep. No. 111-176, at 75 (2010); SEC Proposed Rule, Family Offices, 75 Fed. Reg. 63,753, 63,754-55 & n.13 (Oct. 18, 2010).

Act, Congress directed the SEC to provide family offices with a broad exemption from registration as an investment adviser that "recognizes the range of organizational, management, and employment structures and arrangements employed by family offices."[23] It would be ironic for the Commission to eliminate the ability of family offices to rely on Rules 4.13(a)(3) and 4.13(a)(4) based on the purpose and intent of Dodd-Frank in the face of Dodd-Frank's clear mandate regarding family offices and lack of any attention to these CFTC rules. Most importantly, Dodd-Frank's explicit recognition of the validity of the family office exemption under the Advisers Act cannot be reconciled with the CFTC's rationale for repealing the private fund exemption (including its application to family offices), which relies on Congressional silence not affirmative legislative action.

We therefore respectfully request that, if the CFTC proceeds to repeal Rule 4.13(a)(3) or 4.13(a)(4), the CFTC exempt a wide variety of family offices from the CPO and CTA registration requirements, whether through (i) the issuance of a clarification, (ii) the adoption of a new rule, (iii) the adoption of an exemption from CPO and CTA registration that is substantially similar to the exclusion of family offices from the definition of "investment adviser" under § 202(a)(11) of the Advisers Act that is ultimately adopted by the SEC,[24] or (iv) other means. Any such "exemption" should be broad enough to apply to:

- family offices (*i.e.*, operators of family pools) that are not wholly-owned by the family members (*e.g.*, many operators are owned in whole or in part by the employees);
- operators of family pools whether or not they receive compensation;[25]
- family pools whose ownership extends beyond immediate family members; for example, many family pools include the following as participants:
    - members of the extended family (such as grandparents, parents, siblings, aunts, uncles, cousins and descendants of the foregoing);

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[23] *See* Dodd Frank § 409(b)(2).

[24] *See Family Offices*, Investment Advisers Act Release No. 3098 (Oct. 12, 2010).

[25] *See, e.g., Interpretation of the Term "Pool" in Rule 4.10(d)*, CFTC Interpretative Letter No. 86-10 (Apr. 24, 1986) (a limited partnership was found not to be a commodity pool and the general partners were not CPOs thereof even though the general partners received an "override" on the limited partners' share of the profits); *Section 4m(1) of the Act; Request for No-Action Position From CPO Registration*, CFTC No-Action Letter No. 99-43 (Sept. 15, 1999) (a limited partnership was found to be a family investment vehicle and not a commodity pool and consequently, the general partner was not a CPO thereof even though the general partner received an annual fee equal to 1% of the partnership's assets and 20% of the partnership's net profits); *Rule 4.10(d)(1):--Request for Interpretation That Family Limited Partnerships are Not Commodity Pools, and Section 4m(1) of the Act:--Request for Interpretation That General Partners of Family Limited Partnerships are Not CPOs or CTAs*, CFTC Letter No. 00-98 (May 22, 2000) (three family limited partnerships were found not to be commodity pools and, consequently, the general partners of the partnerships were not CPOs thereof even though they received either reimbursement for operating expenses or an annual fee for management services).

- trusts established by or for the benefit of family members;
- foundations established by family members;
- estates of family members and other involuntary transferees (e.g., a charity that has a contingent interest under a family trust) of interests in the family pool;
- family members that are in-laws, adopted, step-parents, step-siblings, etc.;
- former family members (*e.g.,* ex-spouses);
- key employees (such as investment professionals, executive officers, directors and other persons occupying a similar status or performing similar functions) of the family pool or any related family office (such persons are clearly not unsophisticated investors in need of protection from undesirable managerial and trading practices);
- other employees of the family pool or any related family office that are granted profit interests in the family pool (these employees would not require the protection of the CEA since they would not be making investment decisions);
- family members, etc. of employees;
- former employees;
- long-time friends or business associates of the applicable family;
- persons owned by any of the foregoing; and

- operators of pools that otherwise meet the criteria set forth in the "not a pool" interpretative letters previously issued in the family office context.[26]

Responses to Specific Requests for Comment

1. The CFTC should grandfather previously exempt entities

The CFTC requests comment as to whether previously exempt entities should be grandfathered from registering as CPOs and CTAs. Such previously exempt entities should be grandfathered. Since 2003, thousands of people have spent time and resources to structure their business activity carefully and legitimately in justifiable reliance on the expectation that they could rely on the private fund exemptions in Rules 4.13(a)(3) and 4.13(a)(4). It is fundamentally unfair, burdensome and disruptive to require these persons to restructure their businesses and now become subject to regulation as CPOs and CTAs.

2. The CFTC should allow at least 18 months for previously exempt entities to comply with the proposed changes

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[26] *Infra*, footnote 18.

The CFTC requests comment regarding the amount of time previously exempt entities will need to come into compliance with the proposed changes. Should the CFTC proceed with the repeal and decide against grandfathering previously exempt entities, we ask that the CFTC provide previously exempt entities at least 18 months to come into compliance with the proposed changes.

First, numerous regulations are being promulgated by several federal agencies under Dodd-Frank. The burden on the CFTC and the entities involved in the derivatives markets to promulgate, comment upon, and ultimately comply with the upcoming regulations is already putting a strain on resources and will continue to be substantial. Given these resource constraints and the volume of new regulatory burdens, entities that would be required to register for the first time as CPOs and CTAs should be allowed the maximum amount of time possible to comply with the rules. This is particularly important as, unlike most of the other regulations currently under consideration, the registration consequences of this proposed repeal are not mandated or even contemplated by Dodd-Frank.

Second, certain private funds may be eligible for other CFTC exemptions, but may need to modify their operations in order to qualify for a different exemption from registration as a CPO. For example, by redeeming two investors from a 17 investor pool, reducing total gross capital contributions to $400,000 and meeting other conditions, the CPO of a small pool could comply with the 15-investor exemption in Rule 4.13(a)(2). The CFTC should give these entities sufficient time to qualify for these other exemptions.

3. The CFTC should not require entities to file a notice in order to avoid registration

The CFTC asks how it should treat entities whose activities do not require registration and whether those entities should be required to file a notice with the CFTC to avoid registration. We appreciate the CFTC's recognition that a number of the exemption filings were made as a prophylactic measure out of an abundance of caution by operators of, and advisors to, private funds.

Operators who have claimed exemptions but whose activities do not require them to register should have no further regulatory obligations. Many operators that might have filed a protective exemption notice are far removed from the derivatives industry. Those entities would likely not even be aware of the rule changes or any requirement to file such a notice. Such a requirement would create rule violations, the enforcement of which will not further in any way the regulatory goals of Dodd-Frank or the CEA, nor would they serve any other useful regulatory purpose.[27]

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[27] In the event that the CFTC proceeds with repealing Rules 4.13(a)(3) and 4.13(a)(4), it should not draw any negative inferences about an entity's status from the fact that an entity previously filed an exemption but, after the repeal, does not register.

4. <u>The CFTC should provide a *de minimis* exception for private funds</u>

The CFTC asks whether there should be a *de minimis* exemption under Rule 4.13, and, if so, what the *de minimis* threshold should be. We strongly believe that there should be a *de minimis* exception.

In the 2003 preamble to the proposed rules creating the exemption, the CFTC acknowledged that a *de minimis* exception was appropriate.[28] The exemption was proposed to the CFTC by the National Futures Association, which recommended a five percent of liquidation value threshold.[29] At that time, the CFTC gave serious consideration to using a lower threshold, but after due deliberation, followed the recommendation of numerous commenters and promulgated the five percent threshold.[30] In this proposing release, the CFTC has failed to explain why it is completely abandoning its prior position that a *de minimis* exemption is appropriate.

Accordingly, the Commission should restore the *de minimis* exemption, acknowledging that there is a level of trading that is so modest that registration as a CPO is of no regulatory significance. Further, the CFTC should consider *increasing* the level of *de minimis* trading above the current 5% level to provide a cushion so that persons who have already organized private funds to have a *de minimis* amount of commodity interest trading are not inadvertently required to register solely because the definition of commodity interest has been expanded to include swaps, which are traded by many private funds. The inclusion of swaps in the definition of commodity will result in an increase in the percentage of trading in commodity interests in the existing portfolios of many private funds. A corresponding increase in the *de minimis* trading threshold is appropriate. Moreover, whatever *de minimis* level the CFTC chooses, commodity interests that are for hedging and risk mitigation purposes should be excluded for the same reasons hedging and risk mitigation are given deference elsewhere in Dodd-Frank and the Commission's regulations.[31]

The Commission also should consider raising the current 5% threshold -- up to 50% of a portfolio's liquidation value -- where the fund is advised by an SEC-registered investment adviser. The notion that these kinds of funds should not be regulated by the CFTC is supported by CEA § 4m(3), which provides that the CPO and CTA registration requirements shall not apply to CTAs that are SEC-registered investment advisers whose business do not consist

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[28] Notice of Proposed Rulemaking, Additional Registration and Other Regulatory Relief for Commodity Pool Operators and Commodity Trading Advisors, 68 Fed. Reg. 12,622, 12,626 (Mar. 17, 2003).

[29] *Id.*

[30] 68 Fed. Reg. 47,223.

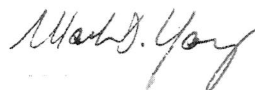
[31] *E.g.*, Dodd-Frank § 721(a)(16), adding new CEA § 1(a)(33)(A).

primarily of acting as a CTA and that does not act as a CTA to any pool engaged primarily in trading commodity interests. Similarly, the Advisers Act does not require SEC registration of investment advisers of CFTC-registered CTAs whose business does not consist primarily of acting as an investment adviser (and does not act as an investment adviser to certain registered investment companies).[32] This approach is also supported by the January 2011 Executive Order on regulation, which calls for consistency among regulators.[33] Both Congressional action and Presidential directives make clear that the Commission should not expend its resources on funds with SEC-registered investment advisers that are not "primarily" engaged in commodity interest trading.

* * *

We appreciate the opportunity to comment on this proposal and look forward to working with the Commission throughout this rulemaking process.

Sincerely,



Mark D. Young
Partner

cc: Chairman Gary Gensler
Commissioner Michael Dunn
Commissioner Bart Chilton
Commissioner Jill Sommers
Commissioner Scott O'Malia

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[32] Advisers Act § 203(b)(6), as amended by Dodd-Frank.

[33] Improving Regulation and Regulatory Review, Executive Order 13563, 76 Fed. Reg. 3,821, Section 3 (Jan. 21, 2011).