NATIONAL FUTURES ASSOCIATION

April 12, 2011

David A. Stawick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations
RIN No. 3033-AD30

Dear Mr. Stawick:

National Futures Association (NFA) appreciates the opportunity to comment on the Commodity Futures Trading Commission's (CFTC or Commission) proposed rulemaking related to Commodity Pool Operator (CPO) and Commodity Trading Advisor (CTA) compliance obligations. Although NFA fully supports the Commission's ultimate goals with this rulemaking, we offer the following comments on particular aspects of the rulemaking.

Proposed New Regulation 4.27 – Data Collection for CPOs and CTAs

Under proposed Regulation 4.27, any CPO or CTA that is registered or required to be registered must complete and submit proposed form CPO-PQR and CTA-PR, respectively, with NFA. CPOs and CTAs would be required to file the appropriate schedules of each report (depending on the size of the CPO or CTA) on a quarterly basis, within 15 days of the quarter end, except that mid-sized CPOs will be required to file Schedule B of Form CPO-PQR on an annual basis, within 90 days of the end of the calendar year.

As the Commission is aware, NFA implemented Compliance Rule 2-46 in March 2010. This rule requires CPOs to file a quarterly report with NFA containing much of the information required under the Commission's proposed Schedule A of Form CPO-PQR. CPOs must file the quarterly reports required under Compliance Rule 2-46 within 45 days after the end of each quarterly reporting period.

NFA is concerned that the proposed 15 day deadline set forth in the Commission's regulation does not provide CPOs and CTAs with sufficient time to assemble the information that must be reported, especially based on NFA's experience with its quarterly reporting deadline Although the vast majority of CPOs file the information required under Compliance Rule 2-46 within the 45 day period, most information is received at the end of the time period, and there are a number of funds (primarily funds of funds) that have difficulty meeting this deadline. Given the increase in information that the Commission will require, particularly with respect to Schedules B and C of Form PQR, NFA recommends that the Commission consider extending the filing deadline to the 45 day period currently provided under Compliance Rule 2-46. NFA also believes that this time period should be applied to CTA reporting requirements.

Proposed Amendment to Regulation 4.7 – Removing Exemptive Relief from Annual Report Certification Requirement

The Commission's proposal would also amend Commission Regulation 4.7 to remove the exemption from the requirement that CPOs provide a certified annual report to the participants in a 4.7 exempt pool. NFA fully supports this change to Regulation 4.7. As the Commission noted in the Federal Register release, the vast majority of CPOs that operate pools under Regulation 4.7 file certified annual reports for these pools. NFA believes that requiring that the annual reports be certified by an independent public account will better ensure the transparency and accuracy of this information for pool participants.

Proposed Amendments to Regulations 4.5, 4.13 and 4.14 – Requiring Annual Filings of Notices of Claims for Exemptions

As the Commission notes in the Federal Register release, persons claiming exclusionary or exemptive relief related to CPO and CTA registration requirements are required to file a notice of the claim with NFA. Those entities that claim relief under Regulations 4.5, 4.13 and 4.14 are not required to provide the Commission or NFA with any follow up information once the notice is filed. Under the Commission's proposal, persons claiming exemptive or exclusionary relief under Regulations 4.5, 4.13 or 4.14 would be required to confirm their notice of claim for exemption or exclusion on an annual basis.

NFA fully supports the requirement that these entities be required to confirm their exemption notice on an annual basis. As of March 18, 2011, NFA had over 12,000 effective exemptions for funds or fund advisors filed under Regulations 4.5,

4.13(a)(1) and (2) and 4.14.[1] However, because there is no follow-up requirement, NFA has no way of tracking how many of these funds are still operating, or ever started operations. With the Commission's proposed requirement, the Commission and NFA will have much better information on the number of entities currently operating under exemptive relief.

NFA recommends, however, that the Commission change the due date of the notice confirmation from an annual requirement based on the exemption's original filing date to a calendar year due date for all filers. NFA believes that requiring the notices to be filed by all filers at the same time each year will make it much easier for the CFTC and/or NFA to follow up with entities that have missed the filing deadline and to notify other NFA Members that because an entity did not file its annual notice, the entities exemption or exclusion has been deemed to have been withdrawn.

Finally, NFA recommends that the Commission provide a 60 day window from the time the notice confirmation is due until the time the exemption or exclusion would be deemed to have been withdrawn. This 60 day period would provide sufficient time for NFA to notify any entity that misses its deadline and for that entity to file the notice. Without this 60 day window, NFA anticipates that there would be a number of unnecessary withdrawals that will subsequently be "reversed."

Proposed Amendments to Regulation 4.13 – Rescission of "*De minimis*" Exemption from Registration

The Commission is also proposing to rescind the exemption from registration under Regulation 4.13(a)(3). This exemption is available to a CPO that operates a privately offered pool that is offered only to qualified eligible participants, accredited investors or knowledgeable employees and which does a *de minimis* amount of futures trading (initial margin and premiums are limited to five percent of the liquidation value of the pool's portfolio).

NFA was a proponent of the 4.13(a)(3) exemption at the time the Commission originally adopted it, and we continue to be staunch supporters of it today. As NFA noted in 2003, the exemption allows both the Commission and NFA to focus their resources on those entities that are more directly involved in the futures markets and away from investment vehicles that are sold only to sophisticated investors and use futures trading in a limited manner to hedge their risks and diversify their investments,

[1] NFA became the sole custodian of these exemptions on January 1, 2003. Therefore, NFA may not have complete records regarding exemptions filed prior to that date.

rather than as vehicles for futures trading. Given that regulatory resources are being stretched more than ever today, NFA believes that the 2003 underlying rationale for the 4.13(a)(3) exemption remains appropriate. However, NFA believes that the Commission going forward should ensure that persons offering these investment vehicles are exempt under this rule only if they are regulated in the alternative by the Securities Exchange Commission (SEC). Therefore, NFA suggests that the Commission add registration with the SEC pursuant to the Investment Advisers Act of 1940 as an investment adviser or a private fund investment adviser as an additional criteria for persons claiming an exemption from CPO registration for pools pursuant to CFTC Regulation 4.13(a)(3).

If the Commission determines to rescind this exemption, as well as the 4.13(a)(4) exemption, NFA encourages the Commission to provide these entities with sufficient time to come into compliance with the Part 4 requirements. The Commission should be mindful that many non-exempt funds have direct investments in one or more of these 4.13(a)(3) and (a)(4) funds and an insufficient amount of time could have a detrimental effect on the participants in these non-exempt funds if the funds needed to divest their holdings pending regulatory compliance.[2]

Proposed Amendments to Regulation 4.5

The Commission's rulemaking also proposes to reinstate certain operating restrictions that were in place prior to 2003 for entities seeking to be excluded from the definition of CPO under Regulation 4.5. The Commission's impetus for this proposal may be NFA's August 18, 2010 Petition for Rulemaking that sought to amend Regulation 4.5 as now proposed by the Commission. For the reasons explained in NFA's Petition, we continue to support the proposed amendments to Regulation 4.5. However, as explained below and in light of further consideration of this issue, NFA believes that the Commission's proposal should be further amended to more precisely achieve the regulatory objectives set forth in NFA's Petition and the Commission's proposal.

At the outset, the Commission should be aware that in order to guide NFA in making recommendations on this proposal, NFA assembled an informal group of representatives from public commodity pools, those who currently operate commodity[3]-

[2] Currently, NFA has almost 4,500 effective exemptions filed under 4.13(a)(3) and over 22,000 effective exemptions file under 4.13(a)(4).

[3] Commodity refers to both physical and financial related derivatives.

related registered investment companies (RICs), and private counsel who specialize in both the Commission's Part 4 Regulations and the Investment Company Act of 1940. This group considered the Commission's proposed rulemaking, including the proposed operating restrictions and their impact if they were reinstated, and the type of regulatory relief that would be necessary for the CPOs offering these RICs to operate under a dual SEC/CFTC regulatory regime.[4] This group proved invaluable in helping NFA formulate its recommendations on the issues described below.

Prior to addressing the proposed operating restrictions, NFA believes it appropriate to address a threshold issue—who should register pursuant to the Commission's proposed amendments to Regulation 4.5. Certainly, a fair reading of the Commission's proposal and current Rule 4.5 would be that the RIC itself must register as the CPO. Some may argue that this outcome is problematic because a RIC's independent directors would, without relief, have to presumably be listed principals of the RIC/CPO. Additionally, to further blur this issue, some have also noted that the RIC's independent directors may have to register as CPOs themselves since they act to delegate functions to the RIC's investment adviser and oversee the investment adviser's activities in relation to the RIC.

NFA believes that two approaches exist to resolve this issue. First, the Commission could require that the RIC itself register as the CPO, and provide appropriate registration relief to the RIC's independent directors. NFA has spoken to several commodity-related RIC's regarding this issue and believes that a better approach is for the Commission to specify that the RIC's investment adviser and not the RIC itself is permitted to register as the CPO. The CPO/investment adviser would simply list the RIC as a commodity pool with NFA. The RIC's investment adviser is the entity that furnishes continuous investment supervision and management to the RIC's investment strategy and portfolio. Therefore, this function appears consistent with how a CPO acts in relation to operating a traditional commodity pool.

The Proposed Operating Restrictions

The Commission proposes to amend Regulation 4.5 to impose two types of operating restrictions that were in place prior to 2003. These operating conditions are often referred to as the "Five Percent Test" and "No Marketing Restriction." Specifically, the Commission proposes that in order for a person to claim an exclusion from CPO

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4 As indicated in both NFA's Petition and our October 18, 2010 comment letter to the Commission on the Petition, NFA's purpose in submitting the Petition was not to eliminate these RIC product offerings, provided they are subject to appropriate regulatory oversight and applicable Part 4 Regulations.

registration for a RIC, the person must represent that the RIC's use of commodity futures, commodity options and swaps (initial margin and premiums used to establish the positions) may not exceed 5% of the liquidation value of the fund's portfolio, and the RIC may not market the fund as a commodity pool or as a vehicle for trading in (or otherwise seeking investment exposure to) the commodity futures, commodity options, or swaps markets. As further discussed below, the Commission's proposal would also require that the commodity futures, commodity options and swaps positions be held by the RIC itself and not a wholly-owned subsidiary.

In proposing these operating restrictions, the Commission's release cited at least four regulatory objectives. Notably, the Commission stated that the operating restrictions would: (1) stop the practice of RICs offering futures-only investment products without Commission oversight;[5] (2) limit the possibility of entities engaging in regulatory arbitrage whereby operators of otherwise regulated entities that have significant holdings in commodity interests would avoid registration and compliance obligations under the Commission's regulations; (3) ensure consistent treatment of operators of commodity pools regardless of registration status with other regulators; and (4) ensure that entities that operate funds that are *de facto* commodity pools are required to report the activities of the pool on the proposed form CPO-PQR.

As noted above, NFA believes that the Commission's proposal can be further structured to more precisely achieve these four regulatory objectives. To do so, NFA strongly encourages the Commission to consider applying the operating restrictions in a manner that creates the bifurcated structure discussed below.

A. <u>The Five Percent Test</u>

In March 2003, the Commission proposed to amend Regulation 4.5 to eliminate the Five Percent Test. As a significant rationale for eliminating this operating restriction, the Commission stated that it was proposing to provide additional relief from CPO registration pursuant to proposed Regulation 4.13(a)(4) based solely on the sophistication of the pool participants, without any requirement that the pool operator be subject to another regulatory scheme and without any restriction whatsoever on the purpose or scope of the pool's commodity interest trading. The Commission further stated that since the Rule 4.5 eligible persons and qualifying entities are "otherwise regulated," the Commission believes that, like the unregulated CPOs for whom it is

[5] As explained more fully below, NFA believes that the amendments to Regulation 4.5 should be directed not only to RICs offering futures-only investment products but also to RICs that have commodity futures, commodity options and swap investments exceeding the Five Percent Test.

proposing relief, these persons and entities may not need to be subject to any commodity interest trading criteria to qualify for relief under Rule 4.5.

To the extent the Commission is now proposing to rescind Regulation 4.13(a)(4)—which served as a rationale for eliminating Rule 4.5's Five Percent Test in 2003—NFA believes that the Commission should also amend Regulation 4.5 to re-impose the Five Percent Test in place prior to 2003. As stated in its February 11, 2011 Federal Register release, in connection with rescinding Regulation 4.13(a)(4), the Commission proposes to eliminate this exemption because it contains no limits on the amount of commodity interest trading in which these pools can engage. Similarly, as evident by these new RIC commodity-related product offerings, there is currently no limit placed upon these RICs as to the amount of commodity interest trading in which they can engage. NFA believes that the issue is even more problematic with regard to these RIC product offerings since unlike current Regulation 4.13(a)(4) there is also no limitation on the presumed sophistication level of their investors.

Currently, NFA believes that five percent of the liquidation value of the portfolio attributable to *non-bona fide* hedging positions in commodity futures, commodity options and swaps is the appropriate threshold in which to set this operating restriction. Although NFA's October 18, 2010 comment letter to the Commission encouraged the Commission to carefully consider comments relating to whether five percent is the appropriate threshold, NFA believes that this threshold percentage is entirely consistent with our position for maintaining the *de minimis* exemption pursuant to current Regulation 4.13(a)(3). NFA believes that RICs that engage in more than a *de minimis* amount of trading subject to the Commission's jurisdiction should be subject as CPOs to the appropriate regulatory requirements and oversight by regulatory bodies with primary expertise in commodity futures.

The Commission's proposed changes to Regulation 4.5 would require a RIC to register as a CPO and be subject to the Part 4 Requirements if it exceeds the Five Percent Test. Certainly, one of NFA's regulatory objectives would be met in that these RICs would be required to register and be subject to oversight by regulatory bodies with primary expertise in commodity futures. At this time, although NFA believes that registration is appropriate, NFA questions whether all RICs that exceed the Five Percent Test should be subject to the full panoply of the CFTC's and NFA's CPO regulatory requirements. Specifically, we believe there may be investment advisers for RICs that exceed the Five Percent Test that do not operate the types of funds that should be subject to the full Part 4 requirements, particularly those related to the content and use of disclosure documents, monthly account statements and recordkeeping.

Therefore, NFA recommends that the final amendments to Regulation 4.5 provide that the investment adviser for any RIC that exceeds the Five Percent Test be required to register as a CPO with the CFTC. This proposal would accomplish two of the Commission's objectives with regard to all RICs that exceed the Five Percent Test—it would limit the possibility of entities engaging in regulatory arbitrage whereby operators of otherwise regulated entities that have significant holdings in commodity interests would avoid registration and compliance obligations under the Commission's regulations; and ensure that entities that operate funds that have significant holdings in commodity interests be required to report the activities of the pool on the proposed form CPO-PQR.

As discussed below, however, unless the CPO marketed the RIC as a vehicle for directly or indirectly trading in the commodity futures, commodity options or swaps markets, the RIC's CPO would be exempt from certain Commission Part 4 requirements, particularly those relating to the content and use of disclosure documents, monthly account statements and recordkeeping.[6] Instead, the CPO would be required to ensure that the RIC/pool complied with the securities industry's requirements in these areas.

B. No Marketing Restriction

In addition to the Five Percent Test, the Commission also proposes that in order for a person to claim an exclusion from CPO registration for a RIC, the person may not market the RIC as a commodity pool or as a vehicle for trading in (or otherwise seeking investment exposure to) the commodity futures, commodity options or swaps markets. NFA clearly supports the requirement that the investment adviser for any RIC that is marketed as a vehicle for trading in (or otherwise seeking investment exposure to) the commodity futures, commodity options or swaps markets should be required to register with the Commission and fully comply with the Part 4 Requirements. Additionally, NFA believes that the vast majority of investment advisers for these newly offered commodity related RICs would not be eligible for a Rule 4.5 exclusion for the RIC if a No Marketing Restriction were in place since these RICs are clearly marketed to the retail public as investments in the commodity markets.

As the Commission's current release notes, the Commission in adopting the final amendments to Regulation 4.5 in 2003 explained that its decision to delete the prohibition on marketing was driven by comments claiming that "the 'otherwise

[6] Although NFA believes it would be an unlikely occurrence, a fund that markets (or should market) itself as a commodity pool would be required to register and comply with the full Part 4 requirements even if it did not trigger the 5% non-hedge limitation.

regulated' nature of the qualifying entities...would provide adequate customer protection and, further, that compliance with the subjective nature of the marketing restriction could give rise to the possibility of unequal enforcement where commodity interest trading was restricted." The Commission's current release also specifically requests comment regarding whether the term "marketing" needs to be clarified. As the Commission is aware, NFA opposed the elimination of the No Marketing Restriction in 2003 since Rule 4.5 is an exclusion rather than an exemption from registration and, therefore, the anti-fraud provisions of Section 4(o) of the CEA do not apply. NFA pointed out that while the sale of these investment vehicles is subject to the anti-fraud provisions in other statutes, unsophisticated customers should also have the benefit of Section 4(o) if the investment is marketed as a commodity pool.

While NFA remains steadfast in its belief that the No Marketing Restriction is appropriate, we have given consideration to those commenters who argue that the restriction is subjective in nature and could give rise to unequal enforcement action. NFA believes that several responses exist to this argument. Initially, NFA believes that the Commission's adopting release should clarify that a RIC does not trigger the No Marketing Restriction simply because its promotional material and/or prospectus either generally mentions that the fund may invest in commodity futures, commodity options or swaps or lists these instruments as a fund's investments. On the other hand, the Commission's release should also make clear that if a fund highlights the benefits or returns of investing in futures, or if the fund's name or marketing materials indicate it is a vehicle for investing in (or otherwise seeks investment exposure to) the commodity futures/options/swaps markets, the fund would trigger the No Marketing Restriction.

NFA is concerned, however, that if the sole determination of whether a fund is marketed as a commodity pool is how it is described in its marketing materials and prospectus, an investment adviser could tailor these materials so as not to trigger the No Marketing Restriction. Certainly, if investment advisers for RICs are required to register as CPOs if they exceed the Five Percent Test, then the CFTC and NFA could review their marketing materials to determine if they appropriately describe a fund's investment strategies to potential investors. If the CPO's marketing materials for the RIC are deemed materially misleading, then the CPO could be subject to an enforcement action.

NFA believes, however, that an enforcement action should be the last resort to address this issue. Instead, NFA strongly encourages the Commission to provide clarity in its adopting release for CPOs to evaluate whether a RIC should be marketed as a commodity pool or as a vehicle for trading in (or otherwise seeking investment exposure to) the commodity futures, commodity options or swaps markets.

Although language in the adopting release should be sufficient, NFA has no objection if the Commission decided to amend the No Marketing Restriction to clarify that the restriction also applies to a fund that "should be" marketed as a commodity pool.

Obviously, in order for a CPO to evaluate whether it should be marketing a RIC as a commodity pool or as a vehicle for trading in (or otherwise seeking investment exposure to) the commodity futures, commodity options or swaps markets, certain criteria must be provided. Although NFA does not believe that there is any one objective test that will drive this determination, we have identified a few factors to serve as indicia as to whether a CPO should be marketing a RIC as a vehicle for trading in (or otherwise seeking investment exposure to) the commodity futures, commodity options or swaps markets. Certainly, if any of these criteria were provided as guidance, then the Commission would be providing more clarity than existed prior to 2003 regarding the application of the No Marketing Restriction. These factors include whether:

- Futures/options/swaps transactions engaged in by the fund or on behalf of the fund will directly or indirectly be its primary source of potential gains and losses;
- Futures/options/swaps trading engaged in by the fund or on behalf of the fund is done through a wholly-owned and controlled subsidiary;
- The fund's objective is correlated or tied to a commodity or managed futures index or benchmark;
- The net notional value of the futures/options/swaps positions engaged in by the fund or on behalf of the fund consistently exceeds 100% of the fund's net liquidating value and the extent to which it does so;
- The normal trading activities by the fund or on behalf of the fund result in it having a net short speculative exposure to any commodity through a direct or indirect investment in futures or other derivatives.[7]

At this time, NFA does not recommend that the Commission attempt to provide an exact formula or specific combinations of the aforementioned factors to conclusively resolve whether a CPO should be marketing a RIC as a commodity pool. Rather, these factors are designed to provide clarity in response to those who argued

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[7] Depending on the Department of Treasury's determination with regard to currency swaps under Dodd-Frank, the Commission may have to consider how to treat transactions in currency swaps by CPOs pursuant to Regulation 4.5's Five Percent Test.

that the No Marketing Restriction was subjective when in place prior to 2003, and NFA believes that the burden should be placed on the CPO to evaluate whether a pool that is a RIC is being appropriately marketed to potential investors in the context of the overall operation of the fund.

NFA is also cognizant of the fact that a RIC could try to avoid the Five Percent Test by indirectly accessing returns from commodity futures, options or other derivatives by utilizing commodity linked notes in place of futures, options and swaps. NFA strongly believes that a RIC's migration to this type of investment strategy is undesirable since it would expose retail participants to not only the risks of the futures markets but also counterparty risk. Therefore, NFA believes it is appropriate for the No Marketing Restriction to retain the proposed parenthetical language so that if a person is marketing participations in a RIC to the public as or in a vehicle for trading in (or otherwise seeking investment exposure to) the commodity futures, commodity options or swaps markets, then the person would be required to register as a CPO.

Pursuant to NFA's proposed bifurcated structure, if a RIC fails the No Marketing Restriction, then there would be additional regulatory requirements beyond simply requiring the investment adviser to register as a CPO. In particular, investment advisers for these RICs would be required to comply with the Commission's Part 4 Regulations, including those relating to the content and use of disclosure documents. As discussed below, however, NFA believes that the Commission and SEC would need to harmonize certain regulatory requirements for the RIC's investment adviser to register as a CPO.

NFA believes that this approach would further accomplish the Commission's other two objectives—stop the practice of RICs offering futures-only investment products without Commission oversight since these RICs would no doubt have to be marketed as a vehicle for trading in the commodity futures, commodity options or swaps markets; and ensure consistent treatment of operators of commodity pools regardless of registration status with other regulators since these CPOs would be subject to the Part 4 Regulations. Specifically, if a RIC is marketed (or should be marketed) as an investment in a commodity pool or as a vehicle for trading in (or otherwise seeking investment exposure to) the commodity futures, commodity options or swaps markets, then the RIC's investment adviser would not only have to register as a CPO[8] but the CPO would have to comply with the harmonized Part 4 Regulations.

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[8] The investment adviser would most likely also have to register as a CPO since it could not meet the Five Percent Test.

Wholly-Owned and Controlled Subsidiary

The Commission's proposal also requires that all non-hedge commodity futures, commodity options and swaps positions be held by the RIC. This requirement effectively prohibits RICs from using a wholly-owned and controlled subsidiary for futures/options and swaps trading. NFA understands that RICs use this type of structure to provide exposure to certain futures and commodities in a manner consistent with the limitations of the federal tax requirements in Sub-chapter M of the IRS Code.

NFA included this requirement in its Petition because we were concerned about the lack of transparency associated with the RIC's commodity futures trading being done via an entity that is neither a commodity pool regulated by the CFTC and NFA nor an SEC registered investment company. After discussing this issue with RICs that currently use this structure and the Investment Company Institute, NFA recommends that the Commission consider permitting RIC's to use these subsidiary entities provided one essential condition is met. In particular, NFA believes that a CPO should be permitted to use this type of structure only if the Commission adopts a requirement within Regulation 4.5 whereby the CPO agrees without condition to make the RIC's subsidiary's books and records available for full inspection by the CFTC and NFA.

Harmonization Issues

The Commission's proposal also asks for specific comments identifying CFTC and SEC requirements regarding the operation of these funds under a dual regulatory structure that conflict, as well as the best way to address these conflicts. In NFA's view, this question is extremely important because as we stated in our October 18, 2010 comment letter, NFA's August 2010 Petition did not seek to eliminate these RIC product offerings. To that end, we specifically encouraged the Commission to not only provide adequate time for CPOs offering these RICs as pools to comply with the Commission's applicable regulations if certain operating restrictions are re-imposed but more importantly consider as part of any proposed rulemaking what, if any, relief may be appropriate for CPOs offering these RICs as pools subject to the CFTC's jurisdiction. In granting such relief, NFA also encouraged the Commission to consider granting similar relief to public commodity pools to avoid giving one structure a competitive regulatory advantage over other similar structures in the marketplace.

Over the past few months, NFA worked very closely with its informal group to identify a number of regulatory requirements that need to be harmonized if these RICs are to operate as pools under a dual regulatory structure, and we believe workable

solutions that maintain appropriate customer protections exist to these issues. In deriving these possible solutions, NFA was mindful of advances in technology that have occurred since many of the Part 4 Regulations were adopted. These advances have impacted the manner in which mutual fund and pool investments are sold to the public and the manner in which investors obtain information about these funds. Therefore, as discussed above, NFA believes that if the Commission grants relief from certain regulatory requirements to CPOs offering these RICs, then the same relief should be offered to CPOs offering public commodity pools, especially with respect to the disclosure document delivery and acknowledgement requirements.

A. Disclosure Document Issues

(i) Delivery – Commission Regulation 4.21 requires a CPO to deliver a Disclosure Document to a prospective participant no later than the time the CPO delivers the subscription agreement. Section 5(b)(2) of the Securities Act of 1933 requires that a Prospectus accompany the sale of a mutual fund share, however, this delivery requirement is deemed satisfied if the Prospectus is delivered with the trade confirmation, which may be sent as many as 3 days after the trade date. Therefore, the securities industry's distribution channel used by RICs would make it very difficult to deliver a pool disclosure document prior to an investor making a RIC investment.

NFA recommends that the Commission consider adopting relief from this requirement, which is similar to the relief the Commission has recently afforded and formally proposed with respect to commodity exchange traded funds (Commodity ETFs). In particular, NFA recommends that CPOs offering pools that are also RICs would be deemed to have delivered the Disclosure Document to participants if the CPO keeps a current copy of the Disclosure Document on its Internet Web Site and clearly informs prospective participants of the Web Site address. Moreover, given today's use of the Internet, NFA believes that this interpretation of Regulation 4.21's delivery requirement should also be afforded to a CPO of a pool registered under the Securities Act of 1933 that maintains a current disclosure document on its Web Site and clearly informs prospective participants of the Web Site address. Of course, a CPO could always deliver a disclosure document by another method if requested by a participant.

(ii) Acknowledgement – Commission Regulation 4.21 also requires a CPO to obtain a written acknowledgement of receiving the Disclosure Document from a prospective participant prior to accepting any funds. The SEC has no comparable requirement and again the current distribution channel for RICs

makes it nearly impossible to obtain an acknowledgement. In evaluating this requirement, NFA questions whether it continues to provide a meaningful customer protection benefit and notes that the Commission must agree since in the context of Commodity ETFs it does not require a CPO to obtain an acknowledgement once the participations reach the secondary securities markets. Therefore, at this time, NFA believes that the Commission should consider eliminating this requirement altogether for CPOs for any type of pool investment, including RICs and pools registered under the Securities Act of 1933.

(iii) Amendments – CFTC and SEC requirements related to the timing of amendments to Disclosure Documents/Prospectuses are materially different in one key area. CFTC Regulation 4.26 requires that a Disclosure Document be updated every 9 months, whereas the SEC requires that a Prospectus be updated every 12 months. The SEC also requires that the updated Prospectus be accompanied by the fund's annual certified financial statements dated no more than 4 months earlier. These separate timing requirements have raised logistical issues for pools registered under the Securities Act of 1933 for years and often lead to unnecessary confusion in the operation of these pools in complying with the SEC's and CFTC's update requirements. Obviously, these logistical issues will also impact CPOs offering RICs and pose a significant problem over time because the 9 month cycle will be at odds with the RIC's audited financial date. As a result, pools that are also RICs would be required to update their Disclosure Documents and Prospectuses far more frequently in order to satisfy both the CFTC's 9 month requirement and the SEC's requirement that the updated Prospectus be accompanied by the fund's audited financial statements.[9]

Because these CPOs must meet both the SEC's and CFTC's filing requirements, NFA strongly suggests that the Commission move to a 12 month update cycle for pools that are also RICs and those registered under the Securities Act of 1933. Although we believe pool participants and potential investors should obtain timely information to make their investment decisions, we also believe safeguards are already in place to meet this customer protection objective. In particular, since CPOs are required pursuant to Commission Regulation 4.26(c) to amend a pool's Disclosure Document to reflect any material changes and distribute it within 21 days, NFA believes that existing and potential participants receive a document that is current in all material respects. In addition, with the use of the Internet

[9] Since the fund's audited financial statements would not be completed when the first 9 month update was due, the fund would be required to file supplemental/post-effective amendments with the SEC to add the audited financial statements.

over the past several years, RICs and many pools registered under the Securities Act of 1933 provide daily NAV information on their Web Sites so that both existing and prospective participants always have access to current performance information.

At this time, NFA also raises another issue in connection with Disclosure Document amendments filed pursuant to Regulation 4.26(c) for pools that are also RICs. Specifically, CPOs currently file an amended Disclosure Document with NFA and cannot distribute the document until approved by NFA. This is problematic in the context of pools that may be RICs since they provide daily liquidity to investors and, therefore, these investors may not know all the information relevant to an investment decision if the document remains in the review process at NFA. To resolve this issue, NFA encourages the Commission to consider whether it may be appropriate to allow pools that provide for daily liquidity to post the Disclosure Document with the highlighted changes on its Web Site for pool participants at the same time the CPO files it for approval with NFA. The CPO could then post the Disclosure Document on the Web Site upon completion of NFA's review.

(iv) Content –There are several material differences between the CFTC's Disclosure Document and the SEC's Prospectus content requirements. To resolve these differences, NFA encourages the CFTC and SEC to engage in further discussions regarding these commodity-related RICs and their respective agency's Disclosure Document and Prospectus requirements. NFA remains optimistic that these issues can be resolved and notes that pools registered under the Securities Act of 1933 have for many years operated under a dual regulatory regime that permits the use of offering materials that meet both the SEC's Prospectus and the CFTC's Disclosure Document requirements. NFA believes that an overriding regulatory objective should be that CPOs offering these RICs as pools should be allowed to provide one document to potential participants since NFA questions whether a potential investor would understand why both a Prospectus and Disclosure Document are being delivered in the first place and, moreover, would take the time to read and understand the two documents.

In comparing the CFTC's Part 4 content requirements to the content of the Prospectuses for these commodity-related funds, NFA believes that several areas (e.g., potential conflicts of interest, risk disclosure, description of futures commission merchants, and further background information for those persons investing money directly or indirectly on behalf of the RIC or its subsidiaries) may

need further discussion but this most likely is supplemental (not conflicting) information that can be added without issue to the Prospectus. However, there are two areas, discussed below, that conflict and will need to be addressed by the two Commissions.

Fee Disclosure. CFTC Regulation 4.24 requires that the Disclosure Document include a complete description of all fees and expenses, including those incurred in connection with the pool's participation in investee pools and funds. Regulation 4.24(i)(2) sets forth a non-exhaustive list of fees that must be included and requires a break-even analysis per unit of initial investment. Form N-1A under the Securities Act of 1933 requires RICs to provide a fee table that discloses shareholder fees and annual fund operating expenses. NFA is concerned that the current fee disclosures made by these commodity-related RICs do not contain a complete description of all fees and expenses, particularly those incurred at the wholly-owned subsidiary level and trading costs associated with operating the RIC. Moreover, because of the differences in these fee disclosure requirements, a prospective investor is not able to appropriately compare the fees associated with a pool registered under the Securities Act of 1933 and a commodity-related RIC.

NFA does not, however, recommend that the CFTC permit CPOs that operate a RIC to replace the Part 4 fee disclosure requirements with those of the SEC. Rather, two possible alternative solutions exist to this issue. First, if the CFTC and SEC agree, these funds could be required to include both types of mandated fee disclosures—including the break-even analysis—in their Prospectus. In the alternative, CPOs offering these RICs could discuss with the SEC whether they can treat their underlying wholly-owned subsidiaries and any investment vehicles held by those subsidiaries as acquired funds, which NFA understands from an accounting perspective mandate the fee disclosures for these wholly-owned subsidiaries (and any investment vehicles held by these subsidiaries) required under Part 4. The regulatory objective is to ensure that all fees are disclosed for each investment vehicle down through each level. Of course, CPOs would still also have to provide the mandated break-even analysis as supplemental information within the Prospectus. By using either of these formats, potential investors will be able to accurately compare fees between a pool registered under the Securities Act of 1933 and a pool that is a commodity-related RIC, and between two pools that are commodity-related RICs.

Past Performance Disclosure. CFTC Regulation 4.25 requires that the CPO provide the offered pool's past performance information. If the pool has less than

3 years of operating history, the CPO must include performance information related to the other pools operated by the CPO, and in some instances the CTA, if applicable. The Staff of the SEC's Division of Investment Management has published guidance that indicates that it is inherently misleading to include performance of other RICs in the Prospectus unless the other RIC's investment objectives, policies and strategies are substantially similar to those of the offered RIC. Clearly, this issue will require compromise by both the CFTC and the SEC. NFA recommends, however, that a possible solution may be that the CFTC permit commodity pools that are also RICs to provide any performance information related to other pools or managed accounts required by CFTC Regulation 4.25 in the pool's Statement of Additional Information, which is made available contemporaneously with the pool's prospectus on the CPO's Web Site.

B. Reporting Issues

(i) Monthly Account Statement – CFTC Regulation 4.22(a) requires that a CPO distribute a monthly account statement to participants in any pool with net assets exceeding $500,000. Although RICs are not required to provide monthly statements to shareholders, these funds are subject to other regular reporting requirements. SEC Rule 30e-1 requires a RIC to send each shareholder of record, at least semi-annually within 60 days after the close of the period, a report containing: a balance sheet accompanied by a statement of the aggregate value of investments on the date of the balances sheet; a list showing the amounts and values of securities owned by the RIC; an itemized income statement; an itemized surplus statement; a statement of aggregate remuneration paid to officers and directors during the period covered by the report; and a statement regarding purchases and sales of securities. Additionally, since mutual funds are sold through a principal underwriter that is a registered broker-dealer, the broker-dealer is required to provide a quarterly account statement to its customers under FINRA Rule 2340. Lastly, because RICs are subject to daily redemption requests, NAVs are calculated daily and are readily available on the RIC's Web Site.

NFA believes that the discrepancy between reporting requirements may be resolved in one of two ways. First, since RICs provide daily liquidity and the vast majority of customers have access to their position's value daily via the Internet, the Commission could adopt relief similar to Regulation 4.12(b)(2)(ii), which permits certain pools to distribute account statements no less frequently than quarterly. In the alternative, the Commission could adopt relief similar to that afforded and now formally proposed for Commodity ETFs, which would permit

the CPO to make the monthly Account Statement available on the CPO's Web Site within 30 days after the last day of the applicable reporting period and maintain it on the Web Site for no less than 30 calendar days.

(ii) Annual Report Certification – The CFTC requires that a CPO certify the accuracy and completeness of the pool's monthly Account Statement and the Annual Report. Similarly, the SEC requires that the RIC's principal executive and principal financial officers certify the annual and semi-annual reports. The language required by the CFTC and the SEC in their respective certifications is not identical. NFA encourages the Commission to work with the SEC to either accept one language in lieu of the other or develop agreed upon language for these certifications. In addition, since the CPO is required to attach the certification to the monthly Account Statement, NFA recommends that the Commission permit the CPO to meet this requirement by posting the certification on its Web Site along with the Account Statement.

C. Recordkeeping

Although both CPOs and RICs are subject to extensive recordkeeping requirements, unlike RICs, CFTC Regulation 4.23 requires that the CPO maintain books and records at its main business office. This poses a significant problem for RICs because their books and records are generally maintained by one or more of its professional service providers, such as the administrator, distributor or custodian, or bank or registered broker-dealer that provides services that are similar to those provided by the administrator or distributor. Again, a similar issue is faced by Commodity ETFs and NFA recommends that the Commission adopt the same relief that it has afforded and now formally proposed for Commodity ETFs, including the requirement that the CPO obtain an acknowledgement from each person keeping the pool's books and records that that the person will be keeping the books and records identified by the CPO, and that the person will make those books and records available in accordance with CFTC Regulation 4.23.

In closing, NFA reiterates its support of the Commission's regulatory objectives with this rulemaking and encourages the Commission to address this issue in a prompt manner. This is an extremely important customer protection issue and as stated in NFA's August 2010 Petition, NFA believes that the CFTC alone has the Congressional mandate to regulate retail managed futures trading and products and over the years has developed the specialized body of skill and knowledge necessary to fulfill this mandate. We believe the proposed bifurcated application of the operating restrictions along with the proposed solutions to the Part 4 harmonization issues would

permit the CFTC to regulate the investment advisers of these commodity-related RICs as CPOs and impose the appropriate regulatory requirements upon their operations. If the Commission desires, NFA is willing to participate in further discussions in the future with Commission staff to achieve this result.

Lastly, although NFA's August 2010 Petition was limited to RICs, NFA believes the Commission in finalizing rules in this area should consider whether another type of person under Regulation 4.5(a) could offer an investment vehicle with a strategy identical to these commodity-related RICs. Specifically, NFA believes that persons described in Regulation 4.5(a)(3)—banks or trust companies—may be able to offer similar investment vehicles.

If you have any questions concerning this letter, please do not hesitate to contact the undersigned at (312) 781-1413 or tsexton@nfa.futures.org or Carol Wooding at (312) 781-1409 or cwooding@nfa.futures.org.

Respectfully submitted,

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