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April 12, 2011

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

Re: Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations; RIN Number 3038-AD30

Dear Mr. Stawick:

Fidelity Investments[1] ("Fidelity") welcomes the opportunity to comment on the Commodity Futures Trading Commission's (the "CFTC" or the "Commission") proposed rules (the "Proposed Rules") relating to amendments to compliance obligations for Commodity Pool Operators and Commodity Trading Advisors, which were published in the Federal Register on February 11, 2011 (the "Release").[2]

Fidelity acts as an investment manager to private funds and accounts ("private pools") and mutual funds. Various of these private pools and mutual funds from time to time utilize futures, options or swaps subject to the Commission's jurisdiction ("Swaps") for *bona-fide* hedging and other investment purposes.

The Proposed Rules follow a petition for proposed rulemaking ("NFA Petition") submitted by National Futures Association ("NFA")[3] regarding the exclusion of specified entities from the definition of commodity pool operator ("CPO") under CFTC Regulation 4.5 ("Rule 4.5"). As discussed in Fidelity's October 18, 2010 letter to the Commission in response to the NFA Petition (the "October Letter"),[4] Fidelity does not believe it is necessary or appropriate to amend Rule 4.5 to require mutual funds that utilize commodity

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[1] Fidelity Investments is one of the world's largest providers of financial services, with assets under administration of more than $3.3 trillion, including managed assets of $1.5 trillion. The firm is a leading provider of investment management, retirement planning, portfolio guidance, brokerage, benefits outsourcing and many other financial products and services to more than 20 million individuals and institutions, as well as through 5,000 financial intermediary firms.

[2] *See* Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations, 76 Fed. Reg. 7976 (proposed Feb. 11, 2011).

[3] Letter from Thomas W. Sexton, III, Senior Vice President and General Counsel, NFA, to David A. Stawick, Office of the Secretariat, CFTC (August 18, 2010), available at http://www.cftc.gov/stellent/groups/public/@requestsandactions/documents/ifdocs/nfapetitionamend4-5.pdf.

[4] Letter from Scott C. Goebel to David A. Stawick, Secretary, CFTC (Oct. 18, 2010), available at http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=26305&SearchText=.

futures, commodity options or Swaps to register as CPOs. We also oppose the Commission's proposal to eliminate the exemptions that certain private pools rely on under CFTC Regulation 4.13(a)(3) and (a)(4) (collectively, "Rule 4.13").

I. Summary

As discussed in some detail later in our letter, Fidelity believes the Proposed Rules would result in substantial costs and administrative burdens that would far outweigh any benefits to investors or the marketplace. We are particularly concerned about the dramatic increase in the scope of the Commission's Proposed Rules to cover entities that use Swaps, which we strongly oppose. If the Commission nevertheless proceeds with changes to Rule 4.5 and Rule 4.13, we believe that some mutual funds and private pools will cease or limit their use of certain investment strategies, thereby restricting the options available to investors. To avoid such an outcome, we offer several suggestions to minimize the negative impact of the Proposed Rules, which are summarized below.

- The Commission should narrow registration requirements by 1) exempting certain commodity funds or pools and funds-of-funds, 2) significantly narrowing the marketing restriction, 3) clarifying the breadth of the hedging exemption, and 4) expanding the quantitative non-hedging limit.

- The Commission should harmonize its rules with conflicting or inconsistent regulations and should provide appropriate relief to mutual funds and private pools from certain Commission rule provisions.

- The Commission should eliminate or significantly reduce the proposed new reporting obligations for CPOs and Commodity Trading Advisers ("CTAs").

II. Swaps should not be included in any changes made to Rule 4.5 and Rule 4.13.

Title VII of the Dodd-Frank Act imposes a number of new requirements on participants in the Swaps market, with the goals of increasing transparency and reducing market risk. For example, a large portion of the Swaps market will be centrally cleared and exchange traded, thereby substantially reducing the potential risks that could exist in the market today and rendering additional regulation of investment vehicles that use these instruments unnecessary. The Commission will have available to it extensive information on the market because of new recordkeeping and reporting requirements for all Swap market participants as well as the means to access data regarding Swaps executed on swap execution facilities. [5]

[5] *See* Section 723(a) of the Dodd-Frank Act, 7 U.S.C. § 2; Section 727 of the Dodd-Frank Act, 7 U.S.C. § 2(a); Reporting, Recordkeeping, and Daily Trading Records Requirements for Swap Dealers and Major Swap Participants, 75 Fed. Reg. 76,666 (proposed Dec. 9, 2010); Swap Data Recordkeeping and Reporting Requirements, 75 Fed. Reg. 76,573 (proposed Dec. 8, 2010) (proposing Swap data recordkeeping and reporting requirements for swap data repositories, derivatives clearing organizations, designated contract

Furthermore, Congress specifically directed the CFTC to regulate a specific sub-set of Swap users whose Swap positions could create systemic risk, major swap participants ("MSPs").[6] Pursuant to a series of rules that the Commission is adopting, MSPs will be subject to registration with, and additional oversight by, the CFTC.[7] The Dodd-Frank Act also prohibits various practices and conduct that are disruptive to fair and equitable Swaps trading, and the CFTC has proposed an interpretive order to provide additional guidance in determining what conduct may constitute disruptive trading.[8]

Given the comprehensive rulemaking that the Commission is undertaking pursuant to the Dodd-Frank Act, altering the Rule 4.5 exclusion and Rule 4.13 exemptions and requiring registration of entities that use Swaps is not necessary. Additionally, we are not aware of the Commission having identified any harm to the market caused by mutual funds or private pools resulting from their use of Swaps. Even the NFA Petition that initiated the proposed changes to Rule 4.5 did not suggest any harm to the market resulting from mutual funds or private pools utilizing Swaps. Instead, NFA's focus appeared to be on managed futures products that are structured as mutual funds. In the absence of such harm, and in light of the extensive new regulation of Swaps under the Dodd-Frank Act, we urge the Commission to exclude Swaps from its consideration of changes to Rule 4.5 and Rule 4.13.

III. The Commission should not adopt the Proposed Rules.

A. The Commission should not make any changes to current Rule 4.5.

As we discussed in detail in our October Letter, we do not believe it is appropriate to eliminate or restrict the categorical exclusion from CPO registration that is afforded to

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markets, swap execution facilities, swap dealers, major swap participants, and swap counterparties who are neither swap dealers nor major swap participants); Real-Time Public Reporting of Swap Transaction Data, 75 Fed. Reg. 76,139 (proposed Dec. 7, 2010; Core Principles and Other Requirements for Swap Execution Facilities, 76 Fed. Reg. 1214 (proposed Jan. 7, 2011).

[6] Section 731 of the Dodd-Frank Act, 7 U.S.C. § 6s; *see* Registration of Swap Dealers and Major Swap Participants, 75 Fed. Reg. 71,379 (proposed Nov. 23, 2010). As the use of Swaps by mutual funds does not create a high degree of risk due to the extensive regulatory requirements with which mutual funds must comply, we have advocated for the exclusion of mutual funds from the MSP status determination. See Letter from Scott C. Goebel to David A. Stawick, Secretary, CFTC and Elizabeth M. Murphy, Secretary, SEC (Feb. 22, 2011), available at http://www.sec.gov/comments/s7-39-10/s73910-41.pdf.

[7] For example, MSPs will be subject to specific duties and business conduct standards, enhanced recordkeeping and reporting requirements and additional compliance responsibilities. *See, e.g.,* Section 731 of the Dodd-Frank Act, 7 U.S.C. § 6s; Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 75 Fed. Reg. 80,637 (proposed Dec. 22, 2010); Reporting, Recordkeeping, and Daily Trading Records Requirements for Swap Dealers and Major Swap Participants, 75 Fed. Reg. 76,666; Regulations Establishing and Governing the Duties of Swap Dealers and Major Swap Participants, 75 Fed. Reg. 71,397 (proposed Nov. 23, 2010).

[8] Section 747 of the Dodd-Frank Act, 7 U.S.C. § 6c(a); Antidisruptive Practices Authority, 76 Fed. Reg. 14,943 (proposed Mar. 18, 2011).

mutual funds under current Rule 4.5.[9] Mutual funds are already perhaps the most heavily regulated investment vehicle in the United States. In particular, the primary statute governing mutual funds, the Investment Company Act of 1940, together with the rules promulgated thereunder, provides a comprehensive set of regulation that encompasses investor protection, stringent limits on conflicts of interest,[10] extensive disclosure requirements[11] and restrictions on a mutual fund's ability to create risk through leverage (including through the use of derivatives),[12] investment concentration or other means, among other things.[13] In addition, mutual fund investors are afforded protections under state law and other federal statutes, such as the Investment Advisers Act of 1940 (the "Advisers Act"),[14] the Securities Act of 1933 (the "Securities Act") and the Securities Exchange Act of 1934 (the "Exchange Act").

The various anti-fraud provisions in these statutes are good examples of these protections. The 1940 Act and its rules contain numerous provisions designed to protect investors from fraud, such as the requirement that mutual funds and their investment advisers adopt written codes of ethics prohibiting fraudulent or manipulative conduct.[15] The Advisers Act also contains strong anti-fraud safeguards, including additional requirements related to advertising.[16] Mutual funds are also subject to the anti-fraud provisions contained in the Securities Act and the Exchange Act.[17] In light of these

[9] We would also strongly oppose any further restriction of Rule 4.5 to require registration by other types of entities that may rely on the current exclusion.

[10] For example, Section 17 of the 1940 Act imposes strict limits on transactions between mutual funds and their affiliates. *See* Section 17 of the 1940 Act, 15 U.S.C. §80a-17. In addition, a mutual fund's board generally must be composed of a majority of independent directors or trustees. *See* Section 10 of the 1940 Act, 15 U.S.C. §80a-10.

[11] Form N-1A requires mutual funds to make a vast array of disclosures that provide protection to investors that is substantially equivalent to that provided by the CFTC's disclosure regime. Among other required disclosures, a fund must disclose its principal investment strategies and principal investment risks in its prospectus. If a mutual fund's trading in, or exposure to, the commodity futures, commodity options or Swaps markets is a principal strategy and/or presents principal investment risks, the fund must provide prospectus disclosure; investment strategies used by a fund and not considered to be principal strategies or to raise principal investment risks would be disclosed in a fund's statement of additional information. Form N-1A also requires disclosure of certain performance data. *See* Items 2, 4, 9, and 16 of Form N-1A.

[12] Mutual funds are required to segregate liquid assets or hold offsetting positions against obligations that could otherwise result in a "senior security," including derivatives obligations, thereby restricting the amount of leverage mutual funds may obtain. *See* Section 18 of the 1940 Act, 15 U.S.C. §80a-18; *see also* Securities Trading Practices of Registered Investment Companies, Investment Company Act Release No. 10666 (Apr. 18, 1979); *Merrill Lynch Asset Management, L.P.*, SEC No-Action Letter (July 2, 1996); *Dreyfus Strategic Investing & Dreyfus Strategic Income*, SEC No-Action Letter (Mar. 30, 1987).

[13] Mutual funds are subject to rigorous advertising requirements. *See, e.g.*, Rule 482 under the Securities Act of 1933, 17 C.F.R. § 230.482. They are also required to produce audited financial statements, make periodic reports to the SEC and to fund shareholders and follow exhaustive recordkeeping requirements. *See* Section 30 of the 1940 Act, 15 U.S.C. §80a-30; and Section 31 of the 1940 Act, 15 U.S.C. §80a-31.

[14] Advisers to mutual funds are required to register with the SEC under the Advisers Act.

[15] *See* Section 17(j) of the 1940 Act, 15 U.S.C. §80a-17(j).

[16] *See* Section 206 of the Advisers Act, 15 U.S.C. § 80b-6.

[17] For example, *see* Section 17(a)(3) of the Securities Act 15 U.S.C. § 77q(a)(3) and Section 10-b of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5.

protections, the concern expressed by NFA in the NFA Petition that mutual fund investors do not benefit from the CFTC's anti-fraud protections seems misplaced.

Given these ample protections afforded to mutual fund investors under statutes and regulations administered by the Securities and Exchange Commission (the "SEC"), it is not necessary for similar, but different, CFTC regulations to be applied to mutual funds. Neither the CFTC nor NFA has produced any evidence that investors in mutual funds are being harmed by the lack of CFTC oversight. We fail to see the tangible benefits or additional protection to investors from requiring CPO registration for certain mutual funds and remain concerned about the potential costs associated with such registration.[18]

B. The Commission should not make changes to Rule 4.13.

The Release references the requirements to improve transparency of private fund advisers contained in Title IV of the Dodd-Frank Act as support for eliminating the private pool exemptions under Rule 4.13. On the same day the Commission approved the Proposed Rules, the Commission, jointly with the SEC, separately proposed another rule ("Regulation PF") to address the concerns identified in Title IV relating to the transparency of private fund advisers.[19] While Fidelity has concerns with portions of Regulation PF, including certain of its proposed reporting requirements, we believe that the disclosure reporting structure required by this rule appropriately addresses concerns associated with advisers to private commodity pools. If the Commission believes that advisers to private pools should be subject to greater transparency, then we suggest Regulation PF be applied to private pool advisers that rely on the Rule 4.13 exemption and that meet the Regulation PF asset thresholds, rather than eliminating the exemption for private pools under Rule 4.13.

The Rule 4.13 exemptions apply only to funds whose investors meet certain thresholds of sophistication, and therefore, do not require the same level of investor protection as ordinary retail investors.[20] The SEC has recognized this distinction in

[18] As explained in our October Letter, these costs may result from, among other things: the requirements of at least one "associated person" of the CPO (as defined in 17 C.F.R. §1.3(aa)), including all persons in the line of supervisory authority, to pass the National Commodity Futures Examination (known as the Series 3 Exam) and NFA fitness examinations, and pay membership fees to NFA; CFTC and NFA registration; increased reporting requirements to NFA and fund shareholders; and the costs of compliance with an additional regulatory regime, including the provisions of a revised Rule 4.5 itself and submission of the proposed new forms CPO-PQR and CTA-PR.

[19] Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF, Investment Company Act Release No. 3145, 76 Fed. Reg. 8068 (proposed Jan. 26, 2011) available at http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2011-2175a.pdf.

[20] Rule 4.13(a)(4) is only available to pools in which each investor is either: (i) an "accredited investor," as defined in Regulation D of the Securities Act or (ii) a "qualified eligible person," as defined in CFTC Rule 4.7(a)(2). Rule 4.13(a)(3) is only available to pools in which the adviser reasonably believes each investor is (i) an "accredited investor" or a trust formed by an accredited investor for the benefit of a family member, (ii) a "knowledgeable employee," as defined in Rule 3c-5 under the 1940 Act, (iii) a "qualified eligible person,"

providing exemptions for certain private funds in various contexts.[21] NFA acknowledged the justification for an exemption for funds marketed to sophisticated investors in the NFA Petition,[22] which did not seek any changes to Rule 4.13. The case for retaining the Rule 4.13 exemptions is even stronger for private pools that are managed by registered investment advisers ("RIAs"), as investors in these pools will be afforded similar protections under the Advisers Act as the CFTC's CPO requirements.[23] Consequently, we do not believe the stated rationale for eliminating the Rule 4.13 exemptions justifies the costs and burdens that such action would impose on private pools and their investors, and strongly urge the Commission to reconsider its proposal.

IV. If the Commission proceeds with changes to Rule 4.5 and Rule 4.13, the changes should be more narrowly tailored.

A. Possible Changes to Rule 4.5

As proposed, the changes to Rule 4.5 have the potential to require CPO registration by a wide range of mutual funds. Although we believe that no changes should be made to Rule 4.5, if the Commission proceeds with modifications, the changes should be refined to require registration only for mutual funds[24] that are "managed futures products" or "futures-only investment products."[25] In other words, any changes to Rule 4.5 should only apply to that limited universe of mutual funds that use futures or options to take active positions on a referenced investment[26] as all or the most substantial portion of their

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as defined in CFTC Rule 4.7(a)(2)(vii)(A) or (iv) a person eligible to participate in a pool under Rule 4.13(a)(4).

[21] *See, e.g.*, Section 3(c)(7) under the 1940 Act, 15 U.S.C. § 80a–3.

[22] NFA cites the "qualifications of fund participants" as a "critical distinction" in not pursuing a change to Rule 4.13. *See* NFA Petition at 9.

[23] *See., e.g.*, Section 206 of the Advisers Act, 15 U.S.C. § 80b-6 (containing anti-fraud protections and advertising requirements); and Section 204 of the Advisers Act, 15 U.S.C. § 80b–4 (containing record-keeping requirements). Many advisers to private pools that have been exempt from registration under the Advisers Act in the past will now be required to register as RIAs as a result of the Dodd-Frank Act's recent elimination of the private investment adviser exemption. *See* Section 403 of the Dodd-Frank Act (amending Section 203(b) of the Advisers Act), 15 U.S.C. § 80b-3(b).

[24] There is a question as to which entity would be required to register as a CPO if Rule 4.5 is modified. Although it does not appear to be completely clear from the Proposed Rules, we believe that it would be more appropriate for the investment adviser of a mutual fund, as opposed to the fund itself, to register as a CPO if the rule is changed. However, for purposes of this letter, we refer to the mutual fund itself as the registrant. The same applies to the registrant for purposes of Rule 4.13; in this letter, we refer to private pools as the registrant, but we believe it would be more appropriate for the adviser to register if the rule is changed.

[25] We believe that if changes to Rule 4.5 were to be made, this proposal would strike the right balance between our view that mutual funds are already sufficiently regulated and NFA's perceived need to oversee mutual funds that sell managed futures strategies to retail investors. *See* NFA Petition at 4. *See also* Release at 7984.

[26] "Active positions" generally includes actively trading in and out of these derivative instruments to express a view on an underlying investment, but it does not include, among other things, using these instruments to hedge (including managing portfolio duration or risk), manage cash positions, or obtain overall exposure tied to a commodity or securities index.

investment strategy. In order to implement this standard, the Commission should import the following concepts to any final rule.

1. Any amendment to Rule 4.5 should not apply to mutual funds that directly, or through a wholly-owned subsidiary, utilize futures, options or Swaps to provide investors with returns tied to a physical commodity index.

Mutual funds that provide investors with exposure to an index of physical commodities through the use of futures, options or Swaps should remain excluded from the definition of CPO, as long as the use of these instruments is tied to the returns of an underlying commodity index. These funds do not take active positions or use futures, options or Swaps to express views on particular commodities. Instead, their positions shift only to the extent of changes in the underlying index or as a result of investors moving into or out of the fund. The passive nature of the use of futures, options or Swaps by mutual funds, and thus the limited risk level attached to their strategies, should not result in CPO registration.

This same principle should apply to mutual funds that employ wholly-owned subsidiaries to access exposure to a referenced commodities index. As explained in our October Letter, mutual funds that invest in commodities through subsidiaries do so merely to satisfy requirements related to tax law limits on the character of income produced by mutual fund investments, and not to evade regulations.[27] Accordingly, wholly-owned subsidiaries of mutual funds that use derivatives to gain returns that are tied to a commodity index should continue to be able to rely on the Rule 4.13 exemption from CPO registration.

Although mutual funds have relatively limited means to access commodity markets,[28] Fidelity believes that mutual funds that use futures, options or Swaps to provide exposure to commodities are a cost-effective and efficient means for ordinary retail

[27] Many mutual funds have obtained private letter rulings from the Internal Revenue Service permitting their use of subsidiaries. *See, e.g.*, I.R.S. Priv. Ltr. Rul. 200743005 (July 20, 2007). These private letter rulings require the subsidiaries to follow SEC guidelines set forth in Section 18(f) of the 1940 Act and all related guidance regarding coverage and the use of leverage by mutual funds. 15 U.S.C. §80a-18(f); *see also supra* note 12. More broadly, the SEC has issued several no-action letters that require mutual funds with subsidiaries to comply collectively with the 1940 Act. *See, e.g., South Asia Portfolio* SEC No-Action Letter (Mar. 12, 1997), *Templeton Vietnam Opportunities Fund, Inc.* SEC No-Action Letter (Sep. 10, 1996), *The Spain Fund, Inc.* SEC No-Action Letter (Mar. 28, 1988) and *The Scandinavia Fund* SEC No-Action Letter (Nov. 24, 1986). Also, the SEC has taken the view that consolidation of a mutual fund's subsidiary in the parent fund's financial statements would give fund shareholders a more accurate picture of the mutual fund's financial position and structure and, as a result, mutual funds usually report holdings and financial statements of their subsidiaries on a consolidated basis. *See Fidelity Select Portfolio*, SEC No-Action Letter (Apr. 29, 2008).

[28] Gaining exposure to the physical commodity markets has barriers to entry that might otherwise make it difficult for retail investors to obtain commodity market exposure. Mutual funds should not be unduly restricted in their mode of investment by unnecessary regulation.

investors to diversify their portfolios. Requiring CPO registration of mutual funds that access commodity markets through derivatives for the limited purpose of trading to replicate an index would impose unnecessary costs that would be ultimately borne by investors in those mutual funds. To the extent those costs are determined to be prohibitive, retail investors may be left with very limited ability to include commodities in their overall investment portfolios.

Commodity-based mutual funds, together with their wholly-owned subsidiaries, also generally are considered long-term liquidity providers to the commodity options, futures and Swaps markets. If mutual funds (or their wholly-owned subsidiaries) that employ these instruments cease doing so in the face of CPO registration, this could impair liquidity in the commodity futures, options and Swaps markets and could potentially have a destabilizing effect on commodity prices and commodities markets.[29] In order to prevent these undesirable results, the CFTC should continue to exempt from CPO registration mutual funds that utilize futures, options or Swaps as a means to take passive positions that track the performance of a commodity index.

2. Mutual funds that do not utilize commodity futures, commodity options or Swaps directly, or through a subsidiary, should be exempt from registration.

It is possible that the Commission may require mutual funds that invest more than a certain percentage of their assets in other funds to become CPOs if the underlying funds are themselves CPOs. We believe that this would be an inappropriate result for funds that do not use commodity futures, commodity options or Swaps directly (or through a wholly-owned subsidiary), as the top-level mutual fund would have no ability to manage or influence the use of these instruments by the funds in which it invests. Instead, the top-level mutual fund's exposure to these instruments would be passive. As the Commission already would have oversight over the underlying CPO(s) that controls the futures, options or Swap investments, it would be unnecessarily duplicative for the Commission to also require registration by the top-level fund.

We believe that treating a fund-of-funds mutual fund as a CPO would be a particularly inappropriate result where the mutual fund is a target date or asset allocation fund. Many of these mutual funds invest in other funds to gain exposure to physical commodities, but typically only for a relatively small portion of the target date or asset allocation fund's overall investment portfolio. Nevertheless, exposure to physical commodities as an asset class is an important element of the strategies that these funds employ. Requiring CPO registration would impose added regulatory burdens on these funds, and could even lead funds to cease investing in this asset class if CPO registration proves too costly. In turn, investors would have less ability to hold diversified portfolios

[29] Any decreased liquidity could leave commodity producers and commercial end users with unmatched demand, higher costs of hedging and increased risks, as mutual funds and their subsidiaries often take the long side of hedging transactions with these commodity producers and end users.

that can mitigate particular risks, such as inflation and adverse movements in foreign exchange rates.[30] Accordingly, we believe that any revisions to Rule 4.5 should clarify that CPO registration would not be required for funds-of-funds, including target date funds and asset allocation funds.

3. The proposed marketing restriction should be eliminated or significantly narrowed so as to only apply to mutual funds that hold themselves out as being managed futures vehicles.

As currently drafted, the marketing restriction in the Proposed Rules could potentially apply to a wide range of mutual funds that offer investors exposure to physical commodities or that market their use of derivatives. The proposed marketing restriction would require CPO registration for any mutual fund that markets itself as "otherwise seeking investment exposure to" the commodity futures, commodity options or Swaps markets.

In addition to applying to mutual funds that use wholly-owned subsidiaries to gain exposure to commodity futures, commodity options or Swaps, this language could capture a much broader range of funds. For example, if not otherwise exempted, the proposed restriction potentially could apply to asset allocation mutual funds or target date or other funds-of-funds mutual funds that market their investment in other funds that use futures, options or Swaps, or even other instruments, to gain exposure to physical commodities markets or for other legitimate investment or risk management purposes, even if the underlying funds are not themselves CPOs. It would be a perverse result to require CPO registration for such a mutual fund where the underlying funds are not themselves CPOs or the underlying investments are not futures, options or Swaps.[31]

A better approach would be to eliminate the marketing restriction altogether or alternatively, to tailor the marketing restriction to apply specifically only to those funds that hold themselves out as "managed futures products" or "futures-only investment products" (that is, mutual funds that use futures or options - or Swaps, if ultimately included - to take active positions on a referenced investment as all or the most substantial portion of their investment strategy). Under the Proposed Rules, if a mutual fund marketed itself[32] as a vehicle for trading commodity futures, commodity options or Swaps (or as

[30] Reduced exposure to commodities in mutual funds could also translate into the potential loss of global purchasing power for these funds and their investors.

[31] For example, registration should not be required where a mutual fund advertises exposure to commodities through investments in notes where the returns are linked to commodity futures, commodity options or Swaps, as we do not believe that the CFTC has jurisdiction over such investments.

[32] Fidelity also requests that the term "marketing" be defined to clarify that it does not include disclosures made in a mutual fund's registration statement. Importantly, as mentioned in our October Letter, requiring mutual funds that disclose their use of commodity futures, commodity options or Swaps in their registration statements to register as CPOs would provide a disincentive for funds to fully disclose the use of these instruments and would run counter to the SEC's recent initiative to improve transparency and disclosure of the use of derivatives in mutual fund disclosure documentation. *See* Letter to Karrie McMillan, General Counsel, Investment Company Institute, from Barry D. Miller, Associate Director, Division of Investment

otherwise providing exposure to these instruments), then it would be required to register as a CPO, even if it only used these instruments for *bona-fide* hedging purposes or in relatively small amounts. The Proposed Rules would also have the potential to pick up a large number of mutual funds that utilize futures, options or Swaps for a wide variety of legitimate investment or risk management purposes. Mutual fund companies should retain the freedom to market mutual funds that use derivatives to achieve efficient fund management strategies without the need to register these mutual funds as CPOs. Any other rule could result in subjective and inconsistent outcomes among mutual funds.[33]

4. <u>The proposed bona-fide hedging exemption should include economic risk management strategies employed by mutual funds.</u>

Under the Proposed Rules, commodity futures, commodity options or Swaps used for *bona-fide* hedging, as defined in CFTC Rule 1.3(z)(1), would be disregarded in assessing whether a mutual fund could remain exempt from CPO registration. In the past, the CFTC has interpreted *bona-fide* hedging to include portfolio risk reduction.[34] We believe that it would be appropriate to include the use of commodity futures, commodity options or Swaps for all economic risk reduction purposes in the hedging exemption contained in any revised Rule 4.5. We, therefore, request that the Commission explicitly include such activity in defining the hedging exception in any rule change.

5. <u>The quantitative limit for non-hedging activity should be higher than five percent of a mutual fund's adjusted liquidation value.</u>

The Proposed Rules would allow a mutual fund to invest in commodity futures, commodity options or Swaps for non-*bona-fide* hedging purposes without having to register as a CPO if the initial margin or premiums for such transactions do not exceed five percent of the fund's liquidation value, as adjusted for unrealized profit or loss.[35] While we agree that if Rule 4.5 is modified it would be appropriate to include a quantitative

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Management, Securities and Exchange Commission, July 30, 2010 (the "ICI Letter") available at http://www.sec.gov/divisions/investment/guidance/ici073010.pdf.

[33] In removing the previous marketing restriction from Rule 4.5 in 2003, the CFTC acknowledged the subjective nature of the restriction when it stated that "[c]ompliance with the subjective nature of the marketing restriction could give rise to the possibility of unequal enforcement where commodity interest trading is restricted." Additional Registration and Other Regulatory Relief for Commodity Pool Operators and Commodity Trading Advisers; Past Performance Issues, CFTC Final Rule Release, 68 Fed. Reg. 47221, 47223 (Aug. 8, 2003).

[34] *See* Clarification of Certain Aspects of the Hedging Definition, 52 Fed. Reg. 27195 (July 20, 1987). Also the CFTC's Form 40, Statement of Reporting Trader, Part B, Item 3 includes instructions that treat "asset/liability risk management, security portfolio risk management, etc." as hedging. Futures exchanges have also adopted rules recognizing risk-reduction transactions as hedging. *See, e.g.*, Board of Trade of the City of Chicago, Inc. Rules 559A-C; Chicago Mercantile Exchange Inc. Rules 559A-C.

[35] We request clarification around the terminology "liquidation value of the qualifying entity's portfolio, after taking into account unrealized profits and unrealized losses" in the text of proposed Rule 4.5. In the mutual fund context, we interpret this to mean a fund's total net asset value, but would appreciate certainty on this point.

threshold in determining whether a mutual fund's use of these instruments would be significant enough to merit CPO registration, we do not think that a threshold for initial margin or premiums of five percent of a fund's adjusted liquidation value is sufficient. We note that the five percent threshold was initially adopted by the Commission in 1985 and the commodity futures and commodity options markets have developed considerably during past twenty-five years.[36] Accordingly, we request that the CFTC re-examine margin requirements in these markets and include a considerably higher threshold based on aggregate initial margin or premiums in any revised rule it may adopt.

A higher threshold would be even more important if Swaps are included in any further rule proposal or final rules, as the CFTC has not yet adopted rules regarding margin requirements for Swaps and Swap clearinghouses have not yet established initial margin levels for cleared Swaps.[37] Furthermore, as of the date of this letter, it is still uncertain as to whether "foreign exchange forwards" (as defined in the Dodd-Frank Act) will be included as Swaps.[38] As a result, it is not possible at this time to determine the full impact of any proposed rule change relating to Swaps that are utilized for non-hedging purposes.

B. <u>The same exemptions from registration that are adopted for Rule 4.5 should be applied to any changes to Rule 4.13.</u>

If the Commission makes changes to Rule 4.13, instead of leaving the Rule 4.13(a)(3) and (a)(4) exemptions in place, we request that the Commission adopt the same exceptions to registration that are ultimately adopted as exceptions from Rule 4.5. We see no reason to treat mutual funds and private pools differently in this regard. Private pools that use commodity futures, commodity options or Swaps for hedging purposes or within any quantitative limit applied to Rule 4.5 should be similarly exempted from CPO registration under Rule 4.13. Also, any private pool currently eligible for a Rule 4.13 exemption that uses futures, options or Swaps to provide investors with exposure to physical commodities in a manner that is tied to a commodity index should be exempt from registration. The same considerations apply to private pools that use these instruments to provide investors access to commodity market returns tied to an index as apply to mutual funds that employ this strategy.

C. <u>If the Commission proceeds with changes to Rule 4.5 and Rule 4.13, it should provide the public with another opportunity to comment before adopting final rules.</u>

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[36] In the 1985 adopting release, the Commission stated that the quantitative limit "generally should not pose any serious or regular impediments to the use of commodity interests." *See* 50 Fed. Reg. 15868-01 (Apr. 23, 1985).

[37] We note, however, that the Commission at its open meeting held on the date of this letter proposed a rule on margin requirements for uncleared Swaps for Swap dealers and MSPs.

[38] Section 721 of the Dodd-Frank Act, 7 U.S.C. § 1a. This determination will have a significant bearing on mutual funds and private pools that use these instruments for non-hedging purposes but would otherwise fall outside of the definition of a CPO.

As the CFTC states in the Release with regard to Rule 4.5, the "Commission believes that NFA's proposed language is an appropriate point at which to *begin discussions*…"[39] If the Commission elects to proceed with changes to either Rule 4.5 or Rule 4.13, we agree with the characterization of the Proposed Rules as a starting point. Consequently, we respectfully request that the Commission re-propose for public comment any changes it believes should be made to these rules before moving to final adoption.

V. If CPO registration of mutual funds or private pools is required, the CFTC should harmonize its rules with SEC regulations and provide appropriate relief from certain CFTC requirements, including the proposed mandatory Swap disclosure.

As indicated above, mutual funds are subject to extensive SEC regulation that is duplicative and inconsistent with CFTC regulations in many respects. The same is true for private pools that are advised by RIAs subject to the Advisers Act. As a result, for any mutual funds or RIA-advised private pools that may be required to register with the Commission as CPOs, we request that the CFTC harmonize its regulations with corresponding SEC regulation.[40] We understand that Dechert LLP is submitting a letter on behalf of certain of its clients (the "Dechert Letter") today, which details the areas in which the Commission should work to harmonize its rules with SEC counterparts applicable to mutual funds. We agree with Dechert that these areas need to be harmonized and, to the extent that there are inconsistencies between the CFTC rules and the SEC's approach to mutual funds, we ask that the CFTC exempt mutual funds from having to comply with these CFTC regulations. Also, where there is overlap with Advisers Act rules, we would request the same harmonization apply to any RIA-advised private pools that would be required to register as CPOs under any revisions adopted to Rule 4.13. Without proper harmonization and relief from these additional regulatory obligations, mutual funds and private pools that may be required to register as CPOs would face tremendous additional, unwarranted expense.

We also ask that the Commission clarify that the individual members of the board of directors or trustees of mutual funds are not required to register with the Commission as CPOs even though they collectively have the ability to hire or fire the funds' investment adviser.[41] The same relief should apply to individual members on the board of any private

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[39] Release at 7984, emphasis added.

[40] In the NFA Petition, NFA has also encouraged the Commission to consider harmonization between CFTC and SEC regulations if the proposed Rule 4.5 changes were to be adopted. *See* NFA Petition at 11.

[41] *See, e.g.*, CFTC No-Action Letter No. 10-06 (Mar. 29, 2010). The CFTC has taken a similar position with respect to directors of a pool. *See, e.g.*, CFTC No-Action Letter No. 97-73 (Aug. 20, 1997). There is precedence for the CFTC to provide such requested relief. *See, e.g.*, CFTC No-Action Letter No. 10-06; CFTC No-Action Letter No. 09-39 (Jul. 30, 2009); CFTC No-Action Letter No. 97-73 (all granting no-action relief to directors or trustees of a fund or trust where the directors or trustees had no authority to perform CPO functions or delegated them to a separate registered CPO). Also, last year, the Commission proposed similar relief to independent directors and trustees of commodity ETFs. *Commodity Pool Operators: Relief From Compliance With Certain Disclosure, Reporting and Recordkeeping Requirements for Registered*

pool that could be required to register as a CPO under any revisions to Rule 4.13. Alternatively, to the extent that the Commission agrees that the adviser to the mutual fund or private pool, and not the fund or pool itself, would be required to register as a CPO, this would be a moot point.

In addition, we request that the CFTC not adopt the proposed changes to CFTC Rules 4.24(b) and 4.34(b), which would require uniform Swap disclosure. Swaps are used by funds and accounts for a variety of purposes and the risks attendant in the use of a particular Swap may differ based upon the type of Swap, the duration and the use of the Swap. While we support clear and comprehensive disclosure of the risks associated with the use of Swaps, we do not agree with the notion of "one-size-fits-all" risk disclosure for funds or accounts that use Swaps. Also, to the extent that any mutual fund would be required to register as a CPO, standardized risk disclosure would not be consistent with recent SEC initiatives to improve disclosure of the use of derivatives by mutual funds, including customizing disclosures for specific funds rather than utilizing standard language.[42] Finally, the required disclosure that any increased liquidity risk from the use of Swaps may "result in a suspension of redemptions" is particularly problematic for mutual funds as the 1940 Act generally does not permit mutual funds to suspend redemptions without obtaining a specific order from the SEC.[43]

VI. The Commission should eliminate or substantially revise the Form CPO-PQR and CTA-PR reporting requirements set forth in the Release.

Fidelity is separately submitting a letter today to the Commission and the SEC on proposed Regulation PF. With respect to the substantive requirements regarding the timing of implementation, the frequency and timing of reporting, the dollar thresholds for disclosure and the data requested for Form CPO-PQR and Form CTA-PR (collectively, "PQR") filings, please refer to our Regulation PF letter. Because of the substantial overlap between the Form PF requirements and the PQR requirements proposed in the Release, our comments on Regulation PF apply equally to the PQR requirements in the Proposed Rules.

We agree with the CFTC and SEC that funds or advisers that have assets under management below a particular level do not present systemic risk, and therefore should not be subject to the additional reporting requirements under Regulation PF. Fidelity also believes that the additional PQR reporting by smaller CPOs and CTAs is not warranted.

CPOs of Commodity Pools Listed For Trading on a National Securities Exchange: CPO Registration Exemption for Certain Independent Directors or Trustees of These Commodity Pools, 75 Fed. Reg. 54794 (Sept. 9, 2010) (the "Commodity ETF Relief"). To the extent that a mutual fund or private pool may be required to register as a CPO, we request relief from CPO registration for all directors or trustees of the mutual fund or private pool, irrespective of whether they are independent and without the conditions imposed in the Commodity ETF Relief, as requiring these individuals to register as CPOs would serve no purpose in benefiting investors or in providing transparency to investment advisers to private pools.

[42] *See* the ICI Letter.

[43] *See* Section 22(e) of the 1940 Act, 15 U.S.C. §80a-22(e), and Rule 22c-1 thereunder, 17 C.F.R. § 270.22c-1.

Therefore, we suggest that the proposed PQR reporting requirements should be eliminated entirely, as the significant cost and burdens on CPOs and CTAs from this added reporting provides very little corresponding benefit to the marketplace or the Financial Stability Oversight Council in its efforts to monitor and assess systemic risk.

If the Commission nevertheless proceeds with the proposed PQR requirements, it should limit the number of CPOs and CTAs required to make PQR filings and streamline the information required to be provided by these entities. At a minimum, the Commission should clarify that no PQR reporting should be required for any CPO or CTA that is required to submit Form PF. In light of the substantial amount of overlap between the proposed PQR forms and Form PF, we believe that it is unnecessarily duplicative to require CPOs or CTAs that are required to submit Form PF also to file Schedule A of the PQRs.

Specifically with regard to the proposed PQR filing, the Commission should not base the CPO and CTA filing requirements on assets under management. A more relevant measure would be commodity pool assets under management. In addition, the Commission should look to the proportion of those assets that represent commodity futures, commodity options or Swaps. Otherwise, it is possible that a large fund with very limited commodity future, commodity option or Swap exposure could be required to make substantial PQR submissions.

If PQR filing requirements are adopted, we believe that the Commission should only require the information in Schedule A of each PQR form for any market participants that are ultimately required to file. These participants would be below the Regulation PF thresholds, already file (or have advisers that file) Form ADV with the SEC on an annual basis and will be subject to the Commission's Large Trader Reporting System on Form 40 for reporting certain large positions. In light of these other reporting requirements, mandating yet another substantial reporting obligation would be unnecessary.

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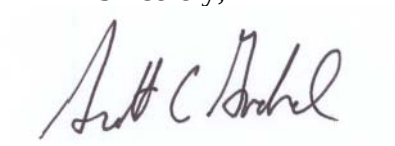
We thank the Commission for considering our comments on this important matter and would be pleased to provide any further information or respond to any questions that the Commission or the staff may have.

Sincerely,



cc: The Honorable Gary Gensler, Chairman
The Honorable Michael V. Dunn, Commissioner
The Honorable Jill E. Sommers, Commissioner
The Honorable Bart Chilton, Commissioner
The Honorable Scott D. O'Malia, Commissioner
Daniel S. Konar II, Attorney-Advisor
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