

September 20, 2016

Via Electronic Submission: <http://comments.cftc.gov>

Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW
Washington, DC 20581
Attn: Mr. Christopher Kirkpatrick, Secretary

RE: Commodity Pool Operator Annual Report; RIN 3038-AE47

Dear Mr. Kirkpatrick:

Willkie Farr & Gallagher LLP appreciates the opportunity to comment on the Commodity Futures Trading Commission's (the "Commission" or "CFTC") proposal to amend certain aspects of the reporting requirements in CFTC Rule 4.22.¹ We have numerous clients that have an interest in this issue. Willkie advises commodity pool operators ("CPOs"), their single and multi-advisor commodity pools, asset allocators, commodity trading advisors and administrators, among other participants in the commodity futures and swaps markets.

Our comments are limited to certain technical points on the Proposal and recommendations that, if followed, could further conserve the Commission's limited resources.

I. Introduction and Summary of Comments

We note that funds of funds ("FoF") started to become popular in the mid-1990s as a way for investors to obtain exposure to multiple trading advisors through the convenience of one investment vehicle. For many investors, a FoF became the way to access successful advisors with high minimum investments. A no-action letter issued by the SEC interpreting the Investment Company Act of 1940, as amended, and that related to commodity pools, also contributed to the growth of FoFs.² As the Commission is aware, FoF CPOs may claim an

¹ 81 Fed. Reg. 51828 (Aug. 5, 2016) (the "Proposal").

² Managed Futures Association, SEC No-Action Letter, 1996 SEC No-Act. LEXIS 623 (Jul. 15, 1996).

extended period of time to prepare and distribute their annual financial statements.³ Similar relief does not currently exist for FoF CPOs with respect to monthly account statements (or quarterly statements, in the case of a FoF operated pursuant to Rule 4.7).

We note also that certain private funds, such as private equity funds, have significant holdings in hard-to-value, illiquid assets. Many of such funds have been rendered commodity pools due to the relatively recent inclusion of swaps in the definition of commodity interest. We note, further, that the commodity pool reporting rules were written at a time when the vast majority of commodity pools limited their trading to liquid exchange-traded futures contracts, which generally are easier to value within the time frames provided in the Commission's Part 4 rules.

In light of the foregoing, and in connection with the Proposal, the Commission may want to consider the following:

- **Periodic reports.** The CPO of a FoF may encounter administrative difficulties in connection with delivering a periodic account statement within 30 days of the end of the applicable reporting period, because the CPO must first obtain rate of return information from the FoF's investee pools. The Commission could alleviate this issue in part by amending Rules 4.22 and 4.7 to give FoF CPOs additional time to prepare and deliver periodic account statements.

Similarly, the CPO of a private fund that invests in illiquid assets may find it difficult to deliver a periodic account statement within 30 days of the end of the applicable reporting period due to the length of time typically required to value such assets. The Commission could address this issue by amending Rules 4.22 and 4.7 to give the CPO of a pool that invests in illiquid assets additional time to prepare and deliver periodic account statements.

- **Aggregate gross capital contributions.** We note that the Commission may want to clarify whether "aggregate gross capital contributions," as used in the Proposal, has the same meaning as "aggregate gross capital subscriptions," as used in Rule 4.25.
- **Form CPO-PQR.** As the Commission knows, financial information on Form CPO-PQR currently must be presented and computed in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") consistently applied. We recommend that the Commission consider permitting a CPO that elects to use International Financial Reporting Standards ("IFRS") or one of the proposed alternatives to U.S. GAAP for a pool's periodic and annual reports to apply a consistent accounting methodology on the CPO's Form CPO-PQR with respect to that pool. Permitting such consistency, among other things, could reduce the risk of inadvertent errors.

³ See generally Rule 4.22(f)(2) (17 C.F.R. § 4.22(f)(2) (2016)).

II. Periodic Reports

In light of the fact that the Commission is proposing to amend Rule 4.22 and codify certain relief that was previously granted by the Staff on a case-by-case basis, we recommend that the Commission take this opportunity to consider additional relief to address certain administrative difficulties faced by CPOs to FoFs and pools that hold hard-to-value, illiquid assets (such as private equity funds) in connection with preparing periodic account statements for such pools. As described in more detail below, such relief would give these CPOs additional time to prepare and distribute periodic account statements.

As the Commission is aware, Rule 4.22 generally requires that registered CPOs deliver monthly account statements to pool participants (or quarterly statements in the case of pools with less than \$500,000 in net assets) within 30 calendar days of the end of the applicable reporting period. Rule 4.7 exempts the CPO of a pool operated pursuant to Rule 4.7 from the specific requirements of Rule 4.22(a) and (b), but generally requires that the CPO distribute to investors quarterly account statements within 30 calendar days of the end of each reporting period.

A. Funds of Funds

In order to meet the requirements of Rule 4.22 or 4.7, as the case may be, and prepare accurate account statements, the CPO of a FoF must obtain rate of return information from the vehicles through which the FoF invests (i.e., the investee funds). Once received, the relevant information from each such entity must be incorporated into the account statement of the FoF before such account statement can be distributed to the FoF's participants. Each underlying entity provides periodic account statements pursuant to the legal and regulatory requirements to which it (or its operator) is subject. Generally, an underlying investment vehicle that is a commodity pool operated by a registered CPO would be required to distribute its account statement to the FoF within 30 days of the end of the applicable reporting period. Such account statement may not be received by the FoF until the last few days of that period. Thus, even if it were the case that all of a FoF's investments were in pools operated by registered CPOs, the FoF CPO may still find it difficult to incorporate the relevant data from investee fund statements into the FoF's account statement and distribute such account statement to FoF pool participants within the prescribed 30-day period.

Importantly, a FoF frequently will invest a portion of its assets in investee funds or other entities whose operators are not subject to the CFTC's periodic account statement distribution deadlines (such as where the investee fund is not a commodity pool, is operated pursuant to an exemption from CPO registration, or is an entity otherwise outside of the CFTC's jurisdiction). Investments in such vehicles may be desirable to increase diversification or for a number of other purposes. Under the laws and regulations applicable to them, such entities may be permitted to distribute rate of return information less frequently than would be required if they were operated by a registered CPO. In such cases, strict compliance by the FoF CPO with the 30-day distribution requirement can present serious administrative difficulties and may simply be impracticable.

The Commission has previously acknowledged the difficulty in obtaining financial information from investee funds in sufficient time for the CPO of a FoF to prepare, file and distribute the

annual reports required by Rule 4.22(c). As a solution, in 2000 the Commission adopted Rule 4.22(f)(2), which provided an automatic 60-day extension to the CPO of a FoF with respect to the distribution and filing of the FoF's annual report.⁴ The extension provided in Rule 4.22(f)(2) was subsequently increased to 90 days.⁵ Thus, the CPO of a FoF that claims this relief currently has 180 days to distribute an annual report to investors, twice the amount of time allocated to non-FoF CPOs. The Commission adopted Rule 4.22(f)(2) in part to provide standardized relief to FoF CPOs in response to the significant number of requests for an extension that were submitted by such CPOs on the basis of "substantial undue hardship" under Rule 4.22(f)(1).⁶ The Commission could similarly codify the process for granting extensions by means of exemptive letters with respect to periodic account statements by amending Rules 4.22 and 4.7(b) to provide the CPO of a FoF additional time to prepare and distribute such account statements.⁷ Such an amendment could help conserve agency resources that might otherwise be expended by the Staff in granting extensions on a case-by-case basis.

In light of the foregoing, we recommend that the Commission consider, in connection with finalizing the Proposal or by separate rulemaking, revising Rules 4.22 and 4.7 to allow a FoF CPO additional time to prepare and deliver periodic account statements to the FoF's participants.⁸ We note that pool participants would continue to receive all information to which they are currently entitled.

⁴ See 65 Fed. Reg. 81333 (Dec. 26, 2000).

⁵ See 74 Fed. Reg. 57585 (Nov. 9, 2009).

⁶ See 65 Fed. Reg. 66663, 66663-64 (Nov. 7, 2000).

⁷ We note that the Staff has previously recognized the administrative difficulty that a CPO operating a FoF encounters with regard to providing periodic account statements to pool participants. For example, in a series of exemptive letters in 2002, the Staff provided exemptions to certain FoF CPOs from the 30-day reporting requirement of Rule 4.7, provided certain conditions were satisfied. See CFTC Staff Letters 02-13, 02-14, 02-15, 02-16, 02-17 (each dated Feb. 27, 2002), 02-60 (May 31, 2002), 02-95 (Aug. 13, 2002), and 02-97 (Aug. 21, 2002). These conditions generally included that (i) quarterly account statements were distributed within 45 calendar days from end of the applicable reporting period and (ii) the pool's current and prospective investors were informed that the pool's account statements would be distributed within 45 calendar days of the end of the applicable reporting period (in the case of Staff Letter 02-95, the relief was also conditioned on the CPO continuing to provide monthly valuation reports to participants approximately 30 to 45 days after the end of the reporting month). In each letter, the Staff noted that the CPO was unable to provide investors with the account statement within 30 calendar days due to reasons beyond the CPO's control; namely, that despite the CPO's best efforts, the financial information received from the investee funds did not arrive early enough to permit the CPO time to prepare and distribute quarterly account statements within the required period. As noted above, due to the increase in the number of FoFs in the past 20 years, more CPOs encounter difficulties in meeting such reporting requirements.

⁸ As noted above in footnote 7, the Staff has previously granted case-by-case relief to the CPOs of FoFs operated pursuant to Rule 4.7 that gave such CPOs up to 45 calendar days from the end of the applicable reporting period to deliver a quarterly report. We also note that the Staff has granted exemptive relief to two CPOs of Rule 4.7 FoFs that permitted such CPOs to prepare and distribute monthly account statements within 45 days of the end of each month, in lieu of the quarterly statements required by Rule 4.7(b). See CFTC Staff Letter 14-142 (Nov. 6, 2014); see also CFTC Staff Letter 15-44 (May 6, 2015) (granting similar relief). Providing for an extension longer than 45 days would further reduce the need for bespoke relief for FoF CPOs that may need additional time to prepare and deliver account statements. We note that a 60-day extension would be consistent with Rule

B. Commodity Pools Invested in Illiquid Assets

As the Commission is aware, the definition of commodity interest was expanded to include swaps as a result of the Dodd-Frank Act. Accordingly, many collective investment vehicles that traded swaps, but no other commodity interests, were no longer excluded from the definition of commodity pool. The inclusion of swaps within the definition of commodity interest resulted in many CPOs no longer being able to rely on the de minimis trading exemption in Rule 4.13(a)(3). In addition, in 2012, the Commission determined to rescind the exemption from CPO registration in Rule 4.13(a)(4). As the Commission is aware, a CPO exempt from registration with the CFTC is not subject to the requirements of Rules 4.22 or 4.7. As a result of all of these changes, however, the sponsors of many collective investment vehicles had to register as CPOs and, for the first time, became subject to the periodic account statement requirements in Rules 4.22 or 4.7. When formed, most, if not all, of these pools likely were not structured to comply with CFTC requirements.

Certain of such commodity pools invest in hard-to-value, illiquid assets. The CPOs of such pools, therefore, face the same general type of administrative difficulties as CPOs in the FoF context with respect to the timely delivery of periodic account statements. Some commodity pools, such as private equity funds, invest in assets for which values are not based on readily available quoted prices in an active market. In such instances, a CPO will have to value the assets and/or rely on an independent third party to provide a valuation. In the latter case, the CPO is dependent upon such third party's valuation being completed in time for the CPO to process and include the financial information in the pool's periodic account statements.

In the case of a CPO to a pool that invests in illiquid assets, either the CPO or the valuation firm(s) on which it relies are sometimes unable to complete the valuation process and provide the necessary data in time for the CPO to process the data and prepare and distribute the required account statements within the required 30-day period. In our experience, CPOs to such pools wish to deliver to their investors diligently produced, reasoned valuations for the pool's illiquid investments that have been prepared by an independent third party or that otherwise affirm the reasonableness of the CPO's own valuations.

In light of the foregoing, we recommend that the Commission consider amending Rules 4.22 and 4.7 to allow the CPO of a commodity pool that invests in illiquid assets additional time to prepare and deliver periodic account statements to pool participants.⁹ Although we acknowledge that it may be difficult to define an illiquid asset, the Commission could consider using as a point of reference an investment that would be considered a Level 3 asset under U.S. GAAP or similar criteria under any of the approved accounting methodologies.

4.22(f)(2), which provides an extension of 90 days for the delivery of an annual report (i.e., twice the time normally permitted under Rule 4.22(c)).

⁹ Any such amendments could be consistent with the case-by-case relief that has been granted by the Staff previously with respect to FoFs, as discussed above in footnotes 7 and 8, or the Commission could grant the CPO to a fund that invests in illiquid assets 60 calendar days in which to deliver periodic account statements, in light of the particular difficulties encountered in connection with valuing the highly illiquid assets generally held by certain private funds, such as private equity funds, and the fact that many such funds were not originally structured to comply with CFTC requirements.

III. Calculation of Aggregate Gross Capital Contributions

It would be helpful for the Commission to clarify whether “aggregate gross capital contributions,” for purposes of proposed Rule 4.22(g)(2)(ii)(A), is intended to have the same meaning as “aggregate gross capital subscriptions” under current Rule 4.25(a)(1)(i)(D). While not defined in the Part 4 rules, we note that the National Futures Association has interpreted “aggregate gross capital subscriptions” to mean the “total amount of all additions to the pool over its entire operating history” and that it “should . . . not [be] reduced by the withdrawals from the pool.”¹⁰

IV. Use of U.S. GAAP Alternatives for Reporting on CFTC Form CPO-PQR

The Commission’s proposal to permit the CPOs of certain non-U.S. commodity pools to use the additional alternatives to U.S. GAAP listed in the Proposal when preparing annual reports or periodic account statements for such pools recognizes the evolution of commodity pools and the participation therein that has occurred over the past few decades.

We anticipate that a number of CPOs will choose to take advantage of the relief to prepare financial statements in accordance with such U.S. GAAP alternatives (including IFRS) and may no longer compute financial information in accordance with U.S. GAAP in the ordinary course of business.¹¹ In light of that fact, we would recommend that the Commission consider permitting such CPOs to utilize consistent accounting principles when preparing their Forms CPO-PQR.¹² An amended Rule 4.27 or Rule 4.22(d) could also provide that a CPO that has filed the notice required under proposed Rule 4.22(d)(2)(iii) is not required to make any additional filing to use the same accounting principles with respect to the reporting of such pool in its Form CPO-PQR. Permitting a CPO to employ the same accounting method as it employs for periodic and annual reports would obviate the need for a reconciliation, which can lead to inadvertent errors and add expense to the overall process.

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We appreciate the opportunity to provide comments on the Proposal and would be pleased to address our comments or further discuss any aspects of the Proposal with the Commissioners or the Staff.

¹⁰ See National Futures Association, *Disclosure Documents: A Guide for CPOs and CTAs*, at 38 (Apr. 2015).

¹¹ We note that, after the Commission amended Rule 4.22(d) in 2009 to permit the use of IFRS when preparing a commodity pool’s annual report or periodic account statements, many CPOs of non-U.S. pools began preparing their annual reports and periodic account statements in accordance with IFRS. As a result, many CPOs currently do not, in the ordinary course, compute the financial information requested in Form CPO-PQR with respect to certain pools in accordance with U.S. GAAP.

¹² As the Commission is aware, CFTC Rule 4.27 provides that all financial information included in Form CPO-PQR must be reported in accordance with generally accepted accounting principles consistently applied. Form CPO-PQR further specifies that such financial information must be reported in accordance with U.S. GAAP. This requirement was reiterated in a Staff FAQ last year. See CFTC Division of Swap Dealer and Intermediary Oversight Responds to Frequently Asked Questions Regarding Commission Form CPO-PQR (Nov. 5, 2015).

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Respectfully submitted,

/s/ Rita M. Molesworth

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cc: The Hon. Chairman Timothy G. Massad
The Hon. Commissioner Sharon Y. Bowen
The Hon. Commissioner J. Christopher Giancarlo
Eileen T. Flaherty, Director, Division of Swap Dealer and Intermediary Oversight