

- 2. New Rule 4.22(i): Distributing Account Statements and Annual Reports Electronically
- E. Amendments to Rules 4.5, 4.7, 4.12, 4.13, 4.14 and 4.22: Conforming Signature Requirements
- F. Effect of Final Rulemaking
 - 1. Effect on Prior Claimants
 - 2. Effect of Withdrawal from CPO Registration on Rule 4.22(c) Annual Report Requirement
- G. Continued Availability of No-Action Relief from Commission Staff
- III. Past Performance Presentation Issues
 - A. Range of Rates of Return for Closed Accounts
 - B. Use of Composite Draw-down
 - C. Treatment of Additions and Withdrawals in Computing Rate of Return
 - D. New Appendix B to Part 4
- IV. Other Matters
 - A. Regulatory Flexibility Act
 - B. Paperwork Reduction Act
 - C. Cost-Benefit Analysis
 - D. Administrative Procedure Act

I. Background on the Proposal for Additional Registration and Other Regulatory Relief for CPOs and CTAs

A. Statutory and Regulatory Authorities

Section 1a(5) of the Commodity Exchange Act (Act) defines the term "commodity pool operator" to mean:

[A]ny person engaged in a business that is of the nature of an investment trust, syndicate, or similar form of enterprise, and who, in connection therewith, solicits, accepts, or receives from others, funds, securities, or property, either directly or through capital contributions, the sale of stock or other forms of securities, or otherwise, for the purpose of trading in any commodity for future delivery on or subject to the rules of any contract market or derivatives transaction execution facility.* * *

Section 4m(1) of the Act² provides, in relevant part, that it is unlawful for any CPO, "unless registered under (the Act), to make use of the mails or any means or instrumentality of interstate commerce" in connection with its business as a CPO. Rules 4.5 and 4.13,

provide exemptions from CPO registration.

Section 1a(6)(A) of the Act defines the term *commodity trading advisor* to mean any person who:

(i) For compensation or profit, engages in the business of advising others, either directly or through publications, writings or electronic media, as to the value of or the advisability of trading in—

(I) any contract of sale of a commodity for future delivery made or to be made on or subject to the rules of a contract market or derivatives transaction execution facility;

(II) any commodity option authorized under section 6c of this title; or

(III) any leverage transaction authorized under section 23 of this title; or

(ii) For compensation or profit, and as part of a regular business, issues or promulgates analyses or reports concerning any of the activities referred to in clause (i).³

Section 4m(1) of the Act also requires CTAs to register as such with the Commission and, along with section 4m(3) and Rule 4.14, provides exemption from CTA registration.

If a person is exempt from registration as a CPO or CTA, its associated persons (APs) are not required to register as such. Further, neither the exempt CPO or CTA, nor any of its APs, is required to become a member of a registered futures association.

Generally, CPOs and CTAs who are, or who are required to be, registered with the Commission, must provide prospective pool participants or advisory clients, as the case may be, with a Disclosure Document containing specified information⁴—e.g., the business background of the CPO or CTA and its principals, past performance, fees and other expenses, and conflicts of interest—and they must make and keep specified books and records.⁵ These CPOs also must provide unaudited periodic financial reports and certified annual reports to participants in their pools.⁶ Additionally, regardless of registration status, all persons who come within the CPO or CTA definition are subject to certain operational⁷ and advertising requirements⁸ under part 4,

to all other provisions of the Act and the Commission's rules prohibiting fraud that apply to CPOs and CTAs, and to all other relevant provisions of the Act and the Commission's rules that apply to all commodity interest market participants, such as the general antifraud provisions, prohibitions on manipulation and the trade reporting requirements.

B. The Proposal

On March 17, 2003, the Commission published proposed revisions to Rules 4.5, 4.13, and 4.14 and various other rules under part 4 of its regulations (Proposal).⁹ The Commission based the Proposal on a prior Rule 4.5 proposal;¹⁰ an Advance Notice of Proposed Rulemaking (ANPR) setting forth additional CPO and CTA registration exemptions submitted by the National Futures Association (NFA) and an additional CPO registration exemption submitted by the Managed Funds Association (MFA);¹¹ the Commission's Roundtable on CPO and CTA Issues (Roundtable);¹² and generally on its staff's experience in administering part 4 of the regulations (Part 4 Rules).

Specifically, the Commission proposed to amend: (1) Rule 4.5, by deleting from the rule any trading criteria and corresponding disclosure requirement for eligibility for an exclusion from the CPO definition; (2) Rule 4.13, by expanding the availability of existing relief from CPO registration and providing for additional CPO registration exemptions thereunder; (3) Rule 4.14, similarly by expanding the availability of existing relief from CTA registration and providing for additional CTA registration exemptions thereunder; (4) Rules 4.21 and 4.31, by permitting certain communications with prospective pool participants and managed account clients, respectively, prior to Disclosure Document delivery; (5) Rules 4.21 and 4.22, by removing duplicative disclosure and reporting requirements in the "master/feeder fund" context; (6) Rule 4.22, by providing for electronic distribution of Account Statements and Annual

¹ 7 U.S.C. 1a(5) (2000). Section 1a(5) also provides the Commission with authority to exclude persons from the CPO definition.

Commission Rule 4.10(d)(1) correspondingly defines the term "pool" to mean "any investment trust, syndicate or similar form of enterprise operated for the purpose of trading commodity interests." Unless otherwise noted, Commission rules cited to herein are found at 17 CFR Ch. I (2003). Both the Act and the Commission's rules issued thereunder can be accessed through the Commission's Web site, at: <http://www.cftc.gov/cftc/cftclawreg.htm>.

CFTC Staff Letters issued since 1995 may be accessed through <http://www.cftc.gov/opaletters.htm>.

² 7 U.S.C. 6m(1) (2000).

³ 7 U.S.C. 1a(6)(A) (2000).

Section 1a(6) also excludes certain persons not at issue here from the CTA definition, and provides the Commission with authority to exclude additional persons from that definition.

⁴ Rule 4.21 for CPOs and Rule 4.31 for CTAs.

⁵ Rule 4.23 for CPOs and Rule 4.33 for CTAs.

⁶ Rule 4.22.

⁷ Rule 4.20 for CPOs and Rule 4.30 for CTAs.

⁸ Rule 4.41.

While Rules 4.7 and 4.12(b) provide relief for certain registered CPOs from the Disclosure Document, periodic and annual reporting, and recordkeeping requirements of Rules 4.21, 4.22, and 4.23, they do not affect the applicability of Rules 4.20 and 4.41 to these CPOs. Similarly, CTAs who have claimed relief under Rule 4.7 continue to remain subject to Rules 4.30 and 4.41.

⁹ 68 FR 12622. The Proposal may be accessed through <http://www.cftc.gov/foia/fedreg03/foi030317b.htm>.

¹⁰ 67 FR 65743 (Oct. 28, 2002). Both the prior Rule 4.5 proposal and the comment letters the Commission received thereon may be accessed through <http://www.cftc.gov/foia/fedreg02/foi021028a.htm>.

¹¹ 67 FR 68785 (Nov. 13, 2002). Both the ANPR and the comment letters the Commission received thereon may be accessed through <http://www.cftc.gov/foia/fedreg02/foi021113a.htm>.

¹² See 68 FR 12622, 12624–25 for a discussion of the origin and outcome of the Roundtable. Comments received in connection with the Roundtable may be accessed through <http://www.cftc.gov/opa/press02/opa4700-02.htm>.