

## Alert

### CFTC Finalizes Significant Rule Changes Affecting Fund Managers and Investment Companies

February 10, 2012

Yesterday, the Commodity Futures Trading Commission ("CFTC") issued a final rule that rescinds the exemption from CFTC registration for commodity pool operators ("CPOs"), which is currently provided in CFTC Rule 4.13(a)(4). The CFTC also: amended CFTC Rule 4.5 to impose new conditions on the ability of mutual funds and other registered investment companies to effect transactions in futures and swaps without the need for CPO registration; imposed new data reporting requirements under Forms CPO-PQR and CTA-PR; rescinded the relief provided in CFTC Rule 4.7(b)(3), under which the annual reports of certain commodity pools were not required to be certified; instituted a new requirement that CPOs and CTAs annually file notices claiming an exemption from registration; and imposed additional risk disclosure requirements upon CPOs and CTAs that engage in swap transactions.

#### Rescission of CPO Registration Exemption

CFTC Rule 4.13(a)(4), which was adopted in 2003, generally exempts from CFTC registration CPOs of funds whose natural person investors are "qualified eligible persons" ("QEPs") within the meaning of CFTC Rule 4.7(a)(2) (a category that includes "qualified purchaser" investors in funds offered pursuant to Section 3(c)(7) of the Investment Company Act of 1940) and whose non-natural person investors are either QEPs or "accredited investors" as defined in Securities Exchange Commission ("SEC") Regulation D. The CFTC's rescission of the Rule will become effective 60 days after publication in the Federal Register. CPOs who have claimed the exemption (which includes the general partners of a large number of Section 3(c)(7) funds) and cannot avail themselves of any other exemption, must register with the CFTC by Dec. 31, 2012. It should be noted that the CFTC proposed, during 2011, to amend the definition of "commodity interest" in CFTC Rule 1.3 to include swaps. If this proposal is adopted, CPOs of funds that engage in swaps activity also may be required to register with the CFTC unless another exemption applies.

#### Registration Lite for CPOs of 3(c)(7) Funds

CPOs of funds whose investors are all QEPs may be able to avail themselves of "registration lite" under CFTC Rule 4.7, which provides relief from certain disclosure and periodic reporting requirements applicable to registered CPOs. A [Client Alert](#) providing a summary of Rule 4.7 and a checklist of key CFTC registration steps and requirements was issued on March 10, 2011.<sup>1</sup>

The CFTC is still considering possible exemptions from registration for family offices and foreign advisers that might be similar to the SEC registration exemptions for these types of advisers.

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<sup>1</sup> See *Client Alert* (March 10, 2011), available at: [http://www.srz.com/031011\\_CFTC\\_Proposes\\_to\\_Discontinue\\_Registration\\_Exemptions/](http://www.srz.com/031011_CFTC_Proposes_to_Discontinue_Registration_Exemptions/).

### Continued Availability of “De Minimis” Exemption

At the time that the CFTC issued its proposal to rescind Rule 4.13(a)(4) in February 2011, it also proposed to rescind Rule 4.13(a)(3), which exempts from registration CPOs of funds that have “de minimis” futures activity (i.e., either: (1) aggregate initial margin on futures positions and premiums on options on futures does not exceed five percent of the liquidation value of the fund’s portfolio (including unrealized gains and losses); or (2) aggregate notional value of such positions does not exceed 100 percent of the liquidation value of the pool’s portfolio (including unrealized gains and losses)). The CFTC has *not* rescinded 4.13(a)(3); accordingly, general partners of funds that use futures, but only within the defined minimum amounts, can continue to use this exemption. General partners of funds that previously relied on 4.13(a)(4) who find that in practice their funds do not actually trade futures above the 4.13(a)(3) minimums could consider switching to the 4.13(a)(3) exemption. In its Adopting Release, the CFTC notes that swaps activity will count toward the de minimis thresholds for purposes of determining the applicability of this exemption.

### Amendment of Rule 4.5 — Registered Investment Companies

The CFTC has also amended Rule 4.5, which is the exclusion from the definition of CPO that investment companies registered under the 1940 Act have relied on to avoid the need for CPO registration. Rule 4.5 as amended imposes significant new conditions on claiming the exclusion. These changes will result in the need for CPO registration in situations where an investment company’s investment program has a significant commodities component or an investment company makes more than limited use of commodities and swaps for other than bona fide hedging purposes. Recognizing that the amendment of Rule 4.5 would subject investment companies and their advisers to possibly duplicative, inconsistent and conflicting disclosure and reporting requirements, the CFTC also proposed the adoption of various rule amendments intended to harmonize the compliance obligations arising under CFTC rules with those imposed by the 1940 Act and the rules adopted thereunder. Compliance with amended Rule 4.5 is required by the later of Dec. 31, 2012, or 60 days after the effective date of final rulemaking defining the term “swap.” Entities required to register due to the amendment of Rule 4.5 will become subject to CFTC recordkeeping, reporting and disclosure requirements 60 days following the effectiveness of the proposed rule amendments relating to investment companies.

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