

# Morgan Lewis

## Summary of Proposed CPO/CTA Rule Changes

On October 9, 2018, the CFTC issued a proposal to codify existing no-action and other relief applicable to CPOs and CTAs, which is summarized in the table below:

Existing Relief	Proposed New Relief	Summary of Proposal
CFTC Advisory 18-96 (Advisory)	§ 4.13(a)(4)	<p><b><i>Relief for CPOs of Offshore Pools</i></b></p> <p>Registered CPOs with offshore pools with no US investors would be permitted to solicit or accept funds from non-US persons for participation in offshore pools and claim an exemption from CPO registration requirements with respect to such pools while simultaneously remaining registered as CPOs where the CFTC deems such registration is required.</p> <p>This proposed amendment would have the effect of expanding relief currently available under the Advisory such that CPOs solely operating offshore pools with no US investors would have an express exemption from registration with the CFTC. Importantly, by placing this relief within CFTC Regulation 4.13, CPOs of offshore pools will become exempt from the requirement to report information about those pools in Form CPO-PQR pursuant to CFTC Regulation 4.27. The Advisory, which was issued several years before Form CPO-PQR was adopted, does not provide relief from this reporting requirement.</p> <p><i>(We note that the National Futures Association (NFA)—the industry regulatory body for CFTC-registered firms—has an independent reporting obligation and its own Form PQR, which registered CPOs satisfy by filing a single report. As a result, the NFA may need to revise or provide relief from this requirement to align with the CFTC’s approach to offshore pools, assuming the CFTC ultimately adopts this proposed rule change.)</i></p> <p>A CPO relying on the proposed relief would be required to (1) affirm its current registration status with the CFTC; (2) ensure that the commodity pool for which it acts is, and will remain, organized and operated outside of the United States, will not hold meetings or conduct administrative activities within the United States, and will not have at any time any shareholder or partner of such pool who is considered a US person (including a strict prohibition on not receiving, holding, or investing any capital directly or indirectly contributed</p>

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		<p>from sources within the United States); (3) not engage in any marketing activity for the purpose, or that could reasonably have the effect, of soliciting participation from US persons; and (4) represent that neither itself nor any of its principals is subject to any statutory disqualification under the Commodity Exchange Act (CEA) unless such disqualification was previously disclosed in connection with a registration.</p> <p>In order to qualify for existing recordkeeping relief under the Advisory, a registered CPO with its main business office in the United States will be required to represent that original books and records of the pool are maintained at the main business office of the pool outside the United States in order to comply with IRS requirements for relief from US federal income taxation.</p> <p>The CPO will also be required to maintain duplicate books and records of the pool in the United States such that the original books and records of the pool can be made available within 72 hours after a request from the CFTC, US Department of Justice, or NFA.</p> <p>The CPO will remain subject to the CEA’s antifraud and anti-manipulation provisions to keep books and records for the exempt pools, and must submit to special calls to demonstrate eligibility and compliance with the conditions of the relief.</p>
<p>CFTC No-Action Letter Nos. 14-115 and 15-47</p>	<p>§ 4.27(b)</p>	<p><b><i>Relief for Registered CPOs and CTAs That Engage Solely in Exempt or Excluded Activities</i></b></p> <p>CPOs and CTAs that are registered but only operate pools for which they are excluded from the CPO definition or exempt from registration with respect to such pools or do not direct client accounts, as the case may be, are no longer required to submit Forms CPO-PQR and CTA-PR.</p> <p>In addition, the CFTC has proposed to expand relief from filing Form CTA-PR to firms that are registered as CPOs and provide commodity interest trading advice to pools for which they are so registered. Under the proposed rules, these types of firms would be exempt from CTA registration under Section 4.14(a)(4) because they are required to file Form CPO-PQR with regard to the relevant pool. Firms that direct the trading of pools for which the firm is</p>

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		<p>exempt from CPO registration would be similarly exempt from making a Form CTA-PR filing under the proposed rules notwithstanding any such firm's status as a registered CTA.</p>
<p>CFTC No-Action Letter No. 14-116</p>	<p>§§ 4.7(b)(1), 4.13(a)(3)(i)</p>	<p><b><i>Codifying JOBS Act Relief with Respect to Offerings of Commodity Pools Involving General Solicitations</i></b></p> <p>CFTC No-Action Letter 14-116 provides relief from certain provisions of CFTC Regulations 4.7(b) and 4.13(a)(3), which restrict marketing to the public. The letter was issued to harmonize these CFTC regulations with Securities and Exchange Commission (SEC) Rule 506(c) of Regulation D and SEC Rule 144A, which permit general solicitation or advertising, subject to specific conditions. The SEC rules were amended pursuant to the Jumpstart Our Business Startups Act of 2012 (the JOBS Act). CPOs currently wishing to rely upon this exemptive letter must, among other things, file a notice with the CFTC Division of Swap Dealer and Intermediary Oversight (DSIO).</p> <p>The CFTC has proposed to tailor the requirements in Sections 4.7(b) and 4.13(a)(3) to eliminate the language that restricted marketing the pool to the public and to be consistent with the JOBS Act relief provided in CFTC No-Action Letter No. 14-116.</p>
<p>CFTC No-Action Letter No. 12-40</p>	<p>§ 4.5(b)(1)</p>	<p><b><i>Including Business Development Companies (BDCs) in the Current Exclusion for Registered Investment Companies</i></b></p> <p>The CFTC has proposed to expand the CPO exclusion for investment companies under Section 4.5 to include BDCs. The investment manager of a BDC will be subject to the limits on commodity interest exposure that currently apply under Section 4.5, i.e., the 5% initial margin test and the 100% aggregate net notional value test (only one of which must be satisfied).</p> <p><i>(The CFTC elected not to modify the language in Section 4.5 that permits a CPO to exclude commodity interests held as bona fide hedging positions, such that they are not subject to the 5% and 100% tests noted above. This is true, even though the referenced rules that define bona fide hedging—Sections 1.3(z) and 151.5—were vacated by a federal court</i></p>

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		<p><i>decision years ago. In doing so, the CFTC has indicated that it will update cross references to Sections 1.3(z) and 151.5 in Section 4.5 after it adopts new bona fide hedging rules.)</i></p> <p>The CFTC also proposed to amend Section 4.5 to provide that the investment adviser to a registered investment company or BDC is the entity that must claim the CPO exclusion, which reflects a change from the current reference to the registered investment company itself. The CFTC explained that this rule change is consistent with the approach it has taken to CPO registration in this context, under which the investment adviser to a registered investment company (rather than its directors) must register as the CPO.</p> <p>If adopted, this change could require firms that have historically claimed the Section 4.5 exclusion based on its text, i.e., by filing the claim of exclusion in the name of the registered investment company as to itself or its series, to update their claims in the NFA's system absent any different accommodation by the CFTC for this historical practice.</p>
<p>CFTC No-Action Letter Nos. 12-37 and 14-143</p>	<p>§§ 4.13(a)(8), 4.14(a)(11)</p>	<p><b><i>Codifying Relief from CPO and CTA Registration for Family Offices</i></b></p> <p>The CFTC has proposed to codify the relief from registration applicable to CPOs and CTAs for family offices. In order to avail itself of the relief, a family office must submit a claim to the DSIO and remain in compliance with the exclusion for family offices from the definition of investment adviser, adopted by the SEC in 2011.</p> <p>The CFTC proposes to exempt from registration (1) CPOs of pools offered privately to family clients; and (2) CTAs who advise family clients. "Family client" would be defined by reference to SEC Rule 202(a)(11)(G)-1.1. Family offices would be required to make a filing with the NFA in order to claim this family office exemption.</p>