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CFTC Amends Regulations Applicable to Asset Managers Including Excluded and Exempt CPOs and CTAs; Action May Be Required

The United States Commodity Futures Trading Commission (“CFTC” or the “Commission”) recently amended Part 4 of its regulations (the “Amendments”)¹ (available [here](#) and [here](#)). The Amendments may affect many asset managers, including those that are excluded or exempt from registration as commodity pool operators (“CPOs”) and commodity trading advisors (“CTAs”). At a high level, the amendments:

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- Update Rule 4.5 to specify that the registered investment adviser (“RIA”) of an investment company registered under the Investment Company Act of 1940, as amended (“RIC”) is the entity that is required to claim the exclusion from the definition of CPO with respect to a qualifying RIC;
- Codify existing no-action relief regarding CPO and CTA registration with respect to family offices;
- Update Rules 4.13(a)(3) and 4.7 to permit the general solicitation of pool participants as contemplated by the JOBS Act;
- Remove the filing requirements for Forms CPO-PQR and CTA-PR for certain CPOs and CTAs;
- Codify existing no-action relief from CPO registration with respect to business development companies (“BDCs”); and
- Update Rule 4.13(a)(3) to explicitly add Qualified Eligible Persons (“QEPs”), including non-U.S. persons, to the list of permitted pool participants.

The Amendments will go into effect on January 9, 2020. In advance of the effective date, asset managers should review the Amendments, which are discussed in greater depth below, to evaluate their operational impact and determine what additional actions, if any, are required to remain in compliance with the CFTC’s revised regulations. Action items could include making filings with the National Futures Association (“NFA”), revising NFA Bylaw 1101 questionnaires, amending registration statements, and revising policies and procedures.

Updates to the Rule 4.5 Exclusion for Registered Investment Companies

Rules 4.5(a)(1) and 4.5(b)(1) provide an exclusion from the CPO definition for operators of RICs that trade only a *de minimis* amount of commodity interests and do not market the RIC as a vehicle for trading in commodity interests. Prior to the Amendments, many RICs had been listed as both the excluded CPO in Rule 4.5(a)(1) and a “qualifying entity” with respect to which a CPO may claim an exclusion under Rule 4.5(b)(1). However, the CFTC determined in 2012, in

¹ Registration and Compliance Requirements for Commodity Pool Operators and Commodity Trading Advisors: Registered Investment Companies, Business Development Companies, and Definition of Reporting Person, 84 Fed. Reg. 67343 (Dec. 10, 2019); Registration and Compliance Requirements for Commodity Pool Operators (CPOs) and Commodity Trading Advisors: Family Offices and Exempt CPOs, 84 Fed. Reg. 67355 (Dec. 10, 2019).

connection with the adoption of Rule 4.12(c)(3), that the RIA of a RIC is the appropriate entity to register as the CPO of such pool.² The CFTC did not update Rule 4.5 at that time.

In the years since, the inconsistencies between Rule 4.5 and Rule 4.12(c)(3) have created uncertainty for RICs and their sponsors about which entity should claim the Rule 4.5 exclusion. The CFTC has addressed this issue by amending Rule 4.5 to specify that the RIA of a qualifying RIC is the entity that is required to claim the exclusion from the definition of CPO.

If a person other than a RIC's RIA has claimed the Rule 4.5 exclusion, the RIA must file a notice of exclusion with the NFA by March 1, 2021, allowing the RIC's claim under Rule 4.5 to expire. In addition, RICs affected by the amendments to Rule 4.5(a)(1) should consult counsel to determine whether the change constitutes a material change necessitating an off-cycle amendment to the RIC's registration statement.

Codification of No-Action Relief for Family Offices

In 2011, the Securities and Exchange Commission ("SEC") adopted a regulatory exclusion (the "SEC Family Office Rule") from the definition of "investment adviser" under the Investment Advisers Act of 1940, as amended (the "Advisers Act") for persons meeting the definition of "family office."³ At the time, the CFTC rules had no corresponding rule providing relief from registration requirements for family offices falling under the CPO and CTA definitions.

Thereafter, the CFTC staff issued two no-action letters, Letter Nos. 12-37⁴ and 14-143⁵ (the "Family Office Letters"), providing relief from registration as a CPO and CTA on terms similar to the SEC Family Office Rule.

The Amendments codify the substance of the relief provided by the Family Office Letters, subject to certain conditions.

In order for a CPO to qualify for the exemption under new Rule 4.13(a)(6) with respect to a commodity pool:

- Interests in the pool must be exempt from registration under the Securities Act of 1933, as amended ("Securities Act");
- Interests in the pool must be offered and sold only to "family clients" as defined in the SEC Family Office Rule, 17 C.F.R. § 275.202(a)(11)(G)-1;
- The CPO must qualify as a "family office" as defined in the SEC Family Office Rule;
- The CPO must reasonably believe, at the time of investment, or in the case of an existing pool, at the time of conversion to a Rule 4.13(a)(6) pool, that each person who participates in the pool is a "family client" of the "family office"; and
- The CPO must keep books and records related to their CPO activities for five years and submit to special calls from the CFTC to demonstrate eligibility for and compliance with the applicable criteria of the exemption.⁶

In order for a CTA to qualify for the exemption under new Rule 4.14(a)(11) the CTA's commodity interest trading advice must be solely directed to, and for the sole use of, "family clients," as defined in the SEC Family Office Rule.

² Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, 77 FR 17328 (Mar. 26, 2012).

³ Family Offices, 76 FR 37983 (June 29, 2011).

⁴ Letter No. 12-37, available [here](#) (Nov. 29, 2012).

⁵ Letter No. 14-143, available [here](#) (Nov. 5, 2014).

⁶ See 84 FR 67355, 67357-67360.

The CPO and CTA exemptions provided by Rules 4.13(a)(6) and 4.14(a)(11) are both self-executing. No initial or ongoing notice filings are required for qualifying family offices to claim the exemptions.

Once effective, the new rules will supersede the no-action relief previously provided by the Family Office Letters. Family offices that qualify for the exemptions should create and maintain an internal record documenting their intent to rely on the relevant exemption(s) and the basis on which they qualify. The Amendments, however, do not supersede prior staff letters providing that a particular entity is “not a pool.”

Other relief may be available for CPOs or CTAs that are unable to meet the requirements of Rules 4.13(a)(6) and 4.14(a)(11).

Form CPO-PQR and CTA-PR Reporting Relief

Rule 4.27 requires each registered CPO and CTA who is a “Reporting Person” to file Forms CPO-PQR and CTA-PR, respectively.⁷ Prior to the Amendments, the definition of “Reporting Person” included all CPOs regardless of whether they operate only exempt or excluded pools, and all CTAs regardless of whether they direct trading in commodity interest accounts. This definition created burdens for CPOs and CTAs whose filings would be of limited utility to the CFTC due to the status of the relevant pools or accounts.

Prior to the Amendments, the CFTC staff issued Letter No. 14-115, which provided exemptive relief to CPOs that operate only Rule 4.5 or Rule 4.13(a)(3) pools,⁸ and Letter No. 15-47, which provided exemptive relief to registered CTAs that do not direct trading in commodity interest accounts.⁹

The Amendments codify and expand the relief provided by Letters 14-115 and 15-47. Accordingly, the following persons are not “Reporting Persons” under Rule 4.27(b) as amended and do not need to file Forms CPO-PQR or CTA-PR, as applicable:

- A CPO that is registered, but operates only pools for which it maintains an exclusion from the definition of the term “commodity pool operator” under Rule 4.5 and/or an exemption from registration as a commodity pool operator under Rule 4.13;
- A CTA that is registered, but does not direct, as that term is defined in Rule 4.10(f), the trading of any commodity interest accounts;
- A CTA that is registered, but directs only the accounts of commodity pools for which it is registered as a CPO and, though registered, complies with Rule 4.14(a)(4);
- A CTA that is registered, but directs only the accounts of commodity pools for which it is exempt from registration as a CPO, and though registered, complies with Rule 4.14(a)(5).

Updates Related to the JOBS Act

The Jump-start Our Business Startups Act of 2012 mandated that the SEC relax certain marketing restrictions on securities that are privately offered, or resold pursuant to Rule 144A of the Securities Act. Accordingly, the SEC amended Regulation D under the Securities Act in 2013 to permit general solicitation in connection with private

⁷ See 17 CFR § 4.27

⁸ CFTC Letter No. 14-115, available [here](#) (Sep. 8, 2014).

⁹ CFTC Letter No. 15-47, available [here](#) (Jul. 21, 2015).

offerings, so long as all purchasers are verified accredited investors.¹⁰ Similar amendments to Rule 144A removed comparable marketing restrictions on resales to qualified institutional buyers (“QIBs”)¹¹ (collectively, the “JOBS Act”).

In response, the CFTC staff issued Letter No. 14-116 (the “JOBS Act Relief Letter”), which granted no-action relief to CPOs from the prohibition on marketing to the public pools that are operated pursuant to Rules 4.7 or 4.13(a)(3), provided that any general solicitation is done in accordance with the JOBS Act.¹²

The Amendments codify and supersede the JOBS Act Relief Letter. Once effective, pools operated pursuant to amended Rules 4.7 and 4.13(a)(3) may use general solicitation pursuant to SEC Rule 506(c) without any Rule 506(c) notice filings.

Codification of No-Action Relief for Business Development Companies

The Amendments also codify existing no-action relief with respect to business development companies (“BDCs”). BDCs are entities created by, and subject to regulation under, the Investment Company Act of 1940 as amended (“ICA”).¹³ As a technical matter, a BDC is not a RIC, but instead is an entity exempt from registration under the ICA by virtue of the filing of an election to be treated as a BDC. Despite the similarities between RICs and BDCs, operators of BDCs did not historically qualify for the exclusion from the definition of CPO under Rule 4.5.

To facilitate the operation of BDCs, the CFTC staff issued a Letter in 2012 (the “BDC Letter”) which provided relief from CPO registration for BDC operators, subject to certain conditions.¹⁴

The Amendments largely codify the relief granted through the BDC Letter by amending Rule 4.5 to permit the RIA of a BDC to claim an exclusion from CPO registration with respect to the BDC. Once claimed, the Rule 4.5 exclusion must be renewed on an annual basis.

Amended Rule 4.5 will supersede the BDC Letter. Accordingly, the operator of a BDC that previously relied on the BDC Letter should file a notice of exclusion under Rule 4.5 as soon as practicable once the Amendments are effective. Asset managers relying on the amended Rule 4.5 should update their compliance procedures to account for the annual renewal requirement.

Permitting Non-U.S. Person Investors in *De Minimis* Exempt Private Pools

The CFTC also adopted a technical amendment to Rule 4.13(a)(3). The amendment clarifies that QEPs, including non-U.S. persons (as such terms are defined in Rule 4.7), are permitted to invest in pools operated pursuant to Rule 4.13(a)(3). The amendment to Rule 4.13(a)(3) is consistent with existing CFTC guidance and is not intended to affect the substance of the exemption.¹⁵

Changes from the Proposal

The CFTC notably did not adopt proposed amendments to Rule 4.13 that would: (i) generally codify Advisory 18-96 pertaining to non-U.S. pools and (ii) add a requirement that any person claiming or affirming an exemption from CPO registration pursuant to Rule 4.13 certify that neither the claimant nor its principals are subject to statutory disqualification. (The proposed amendments are available [here](#).) The CFTC, in adopting the Amendments, noted that many commentators objected to the 18-96 exemption proposal because it could significantly increase compliance

¹⁰ Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings, 78 FR 44771 (July 24, 2013).

¹¹ See 17 CFR § 230.144A.

¹² CFTC No-Action Letter No. 14-116, available [here](#) (Sep. 9, 2014).

¹³ See CFTC Letter No. 12-40, available [here](#) (Dec. 4, 2012).

¹⁴ Id.

¹⁵ See 84 FR 67355, 67362.

burdens on CPOs operating outside the United States. Based on the comments received and the recommendations of CFTC staff, the Commission withdrew the proposed exemption. In doing so, the Commission reserved the option to reconsider the issue in the future as part of a more comprehensive review of the extraterritorial application of CFTC regulations in the CPO/CTA space. Likewise, in light of comments received, the Commission determined that the statutory disqualification proposal requires further consideration and intends to reconsider the proposal in a future rulemaking.

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