INVESTMENT ADVISER
ASSOCIATION

April 24, 2012

VIA ELECTRONIC MAIL

Mr. David Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: Regulation 4.5 Harmonization, 17 CFR Part 4

Dear Mr. Stawick:

The Investment Adviser Association[1] appreciates the opportunity to submit comments on the proposed amendments ("Proposal")[2] to harmonize the disclosure, reporting and recordkeeping requirements of the Commodity Futures Trading Commission ("CFTC" or "Commission") and the Securities Exchange Commission ("SEC") applicable to investment companies registered under the Investment Company Act of 1940 ("RICs") whose advisers will be subject to registration as commodity pool operators ("CPOs") under CFTC Regulation 4.5. We write primarily with respect to the Commission's request for comment on whether any of the harmonization provisions should be applied to operators of private funds that are not registered investment companies ("private fund advisers"). Many of our members are private fund advisers that will be required to register as CPOs and/or commodity trading advisors ("CTAs") and we believe that certain of the harmonization provisions should also be available to them. Accordingly, we urge the Commission to apply certain harmonization provisions to all CPOs and CTAs as discussed below.

The primary objective of the Proposal is to minimize the risk and burden of duplicative, inconsistent and potentially conflicting disclosure, reporting and recordkeeping requirements of the CFTC and SEC on RICs and their advisers that will be subject to CFTC jurisdiction as CPOs. Accordingly, for such RICs, the CFTC proposes to (i) offer relief from

[1] The Investment Adviser Association is a not-for-profit association that represents the interests of SEC-registered investment adviser firms and private fund advisers. Founded in 1937, the IAA's membership consists of more than 500 advisory firms that collectively manage in excess of $10 trillion for a wide variety of individual and institutional investors, including pension plans, trusts, investment companies, private funds, endowments, foundations, and corporations. For more information, please visit our web site: www.investmentadviser.org.

[2] *Harmonization of Compliance Obligations for Registered Investment Companies Required to Register as Commodity Pool Operators*, 17 CFR Part 4 (Feb. 24, 2012) ("Proposal"), available at http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-3388a.pdf.

various CFTC disclosure document content, delivery, performance, updating, and acknowledgment requirements, (ii) grant relief from certain periodic reporting obligations, so long as the required information is available on the CPO's web site, and (iii) permit required books and records to be maintained at the CPO's main office or at the offices of a third-party, under certain conditions.

We fully support the goal of minimizing duplicative, inconsistent and potentially conflicting disclosure, reporting and recordkeeping requirements by the CFTC and SEC. Accordingly, we recommend several important changes to the Proposal that are consistent with this goal. First, we urge the Commission to permit all CPOs and CTAs to maintain required books and records at third party locations. Second, we suggest that the Commission extend the deadline for CPOs filing annual reports in order to harmonize the CFTC's reporting deadlines with those of the SEC. Third, we recommend that the Commission harmonize its past performance reporting requirements with those of the SEC for SEC-registered advisers. Fourth, we support the Commission's proposal to permit all CPOs and CTAs (including private fund advisers) to file updates to disclosure documents twelve months from the date of the document. Finally, we request the Commission to extend the proposed relief for disclosure document and account statement delivery requirements to all CPOs. Our concerns are further discussed below.

Introduction

In considering the application of its requirements to SEC-registered investment advisers, the Commission should consider the regulations to which such advisers are already subject. Our members are all SEC-registered investment adviser firms subject to the SEC's regulatory and oversight framework under the Investment Advisers Act of 1940 ("Advisers Act"). Under the Advisers Act, investment advisers are fiduciaries that must act in the best interests of their clients. As we described in our comment letter on the Commission's proposal to rescind CFTC Regulations 4.13(a)(3) and (a)(4),[3] SEC-registered advisers are required to provide substantial disclosures to both the SEC and to clients on Form ADV, which is publicly available on the SEC's web site.[4] In addition, investment advisers are subject to substantive requirements under the Advisers Act intended to protect investors and ensure compliance with applicable law. For example, advisers are required to appoint a chief compliance officer, adopt a code of ethics, and develop and implement a robust compliance program.[5] In addition, registered investment advisers must maintain specified books and records and must comply with the SEC's advertising rules and guidance.[6] Further, investment

[3] Letter from Karen Barr, General Counsel, IAA to David Stawick, Secretary, CFTC (April 12, 2011).

[4] *See* Advisers Act Rule 203-1, 204-1 (requiring initial and annual filing of Form ADV and interim amendments).

[5] Advisers Act Rules 204A-1 and 206(4)-7.

[6] Advisers Act Rules 204-2 and 206(4)-1.

advisers must comply with the "custody rule," which is intended to ensure the safekeeping of client assets.[7]

1. The Commission should permit all CPOs and CTAs to maintain required books and records at third party locations.

The Commission should permit all CPOs and CTAs (including, but not limited to, those operating or managing RICs) to maintain required books and records at third party locations. Under CFTC Regulations 4.23 and 4.33, CPOs and CTAs are required to maintain books and records at their main business offices. Strict adherence to this requirement would prevent CPOs and CTAs from utilizing the services of third parties to manage, store and secure their books and records. However, prevailing technologies and current market practices enable companies that use third parties to retain complete visibility, security, and access to all their business records, regardless of format or location, often at a cost lower than maintaining the books and records themselves. Indeed, the Commission has long permitted futures commission merchants and introducing brokers to utilize third parties to maintain required books and records. Given these realities, we see no policy reasons for prohibiting CPOs and CTAs from using third parties to maintain books and records.

CFTC Regulation 4.12(c) currently permits the CPO of a Commodity ETF to claim relief from the requirement to keep the CPO's books and records at its main business address in CFTC Regulation 4.23. The Proposal seeks to amend CFTC Regulation 4.12(c) to, among other things, permit RICs and their CPOs to maintain their records with third parties, subject to certain conditions. In particular, the books and records that the CPO will not keep at its main business office must be maintained by the RIC's administrator, distributor, or custodian (or a bank, registered broker or dealer acting in a similar capacity). We recommend that the Proposal include similar relief to permit all CPOs and CTAs to maintain their books and records with third parties. Our recommendation is supported by prevailing technologies, market practices, and recent actions by the Commission, and would harmonize CFTC requirements for private fund advisers with SEC guidance.[8]

We further request the Commission to broaden the type of third parties that may maintain books and records for CPOs and CTAs. We note that the SEC permits registered investment advisers and RICs to keep their required records at a wider range of third parties than does current CFTC Regulation 4.12(c). For example, a registered investment adviser may keep records with administrators, distributors, custodians, sub-advisers, banks, broker-

[7] Advisers Act Rule 206(4)-2.

[8] Advisers Act Rule 204-2 generally requires investment advisers to maintain books and records "in an easily accessible place for a period of not less than five years….the first two years in an appropriate office of the investment adviser." The SEC permits records required by this rule to be maintained by third parties under certain conditions. *See, e.g.*, ABA Subcommittee on Private Investment Entities, SEC No-Action Letter (Dec. 8, 2005); First Call Corporation, SEC No-Action Letter (Sept. 6, 1995).

dealers and/or futures commission merchants as well as with other third parties under certain conditions (*e.g.*, the adviser has ready access to the records and the third party agrees to certain undertakings including retaining the records for up to six years).[9] In addition, SEC-registered investment advisers are required to identify the various locations of their books and records in Form ADV, Part 1A, which is publicly available on the SEC's web site. Similar relief should be available to all CPOs and CTAs.

This relief would be consistent with relief previously granted by the Commission staff. For example, the Commission staff previously granted exemptive relief to allow books and records to be maintained with a third party where a registered CPO contracted with two firms to perform administrator, registrar, and transfer agent functions, including keeping and maintaining required books and records.[10] The CFTC staff indicated that the exemptive relief would apply to any additional pool that the CPO may operate in the future. The CFTC staff conditioned the relief on compliance with various conditions, including that the records are accessible for inspection, that the location of the records is disclosed, and that the CPO remains responsible for compliance with CFTC regulations.

On the basis of the foregoing, we see no policy reason why similar relief should not be granted to all CPOs and CTAs, including private fund advisers. Accordingly, we urge that the Commission permit greater flexibility in the maintenance of books and records beyond the confines of CPOs' and CTAs' main offices, provided that such books and records are secured and easily accessible and the location of the records is disclosed to the Commission and the National Futures Association ("NFA") by, for example, referencing the disclosure on Form ADV, Part 1A.

2. The Commission should extend the deadline for CPOs filing annual reports in order to harmonize the CFTC's reporting deadlines with those of the SEC.

CPOs must prepare periodic reports detailing the financial condition and performance of the pools they operate. The reporting obligations are specified in CFTC Regulation 4.22 (and CFTC Regulation 4.7 for exempt funds). The reports are due quarterly (within 45 days after the end of each quarter) and annually (within 90 days after the pool's fiscal year-end). The annual report also must be filed electronically with the NFA. The Commission mandates strict adherence to its reporting deadlines, and imposes disciplinary action on firms that are delinquent. In order to avoid a potential disciplinary action, CPOs of non-fund-of-funds must generally request an extension[11] by filing a hardship request with the NFA prior to the report's

[9] *See, e.g.*, ABA Subcommittee on Private Investment Entities, SEC No-Action Letter (Dec. 8, 2005); First Call Corporation, SEC No-Action Letter (Sept. 6, 1995).

[10] CFTC Letter No. 08-04.

[11] CFTC Regulation 4.22(f)(1).

original due date.[12] However, under Regulation 4.22(f)(2), a CPO that operates a pool that is a fund-of-funds may claim a 90-day automatic extension, subject to certain conditions, for the annual report for the pool. Once the extension is claimed, there is no need to re-file for the extension on an annual basis and the extension continues to apply as long as the fund remains a fund-of-funds.

The SEC's reporting deadline is different from the CFTC's. To comply with the "audit provision" of Rule 206(4)-2 (the "Custody Rule") promulgated under the Investment Advisers Act of 1940, a private fund adviser must distribute to pool investors audited financial statements prepared in accordance with generally accepted accounting principles within 120 days of the pool's fiscal year end.[13] However, the SEC has afforded some flexibility in its reporting regime. The underlying policy reason for its flexibility stems from the recognition that there are circumstances under which auditors might not be able to complete their work within the specified timeframes. For example, the auditor of a fund-of-funds would not be able to complete its work until the audit reports of the underlying funds are available. Accordingly, the SEC has indicated that it would not recommend enforcement action against an adviser of a fund-of-funds or a top-tier fund (a fund-of-funds-of-funds), if the audited financial statements are distributed to investors within 180 days of the end of its fiscal year.[14] Under certain circumstances, the SEC will further allow advisers to top-tier funds up to 260 days of a pool's fiscal year to distribute audited financial statements to investors.[15]

Accordingly, advisers that fall within the jurisdiction of both the CFTC and SEC would be subject to inconsistent deadlines. To avoid this problem, we suggest that the Commission (i) harmonize its annual reporting requirements and deadlines with those of the SEC, or (ii) provide that advisers that are in compliance with the SEC's requirements under the "audit provision" of the Custody Rule will also be deemed to be in compliance with the CFTC's requirements. We believe this approach would further the Commission's goal of minimizing inconsistent and conflicting requirements.

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[12] However, if the CPO is requesting an extension beyond 180 days after the pool's fiscal year-end, it must file its request directly with the CFTC.

[13] The vast majority of private fund advisers use the audit provision to comply with the Custody Rule.

[14] *See* SEC Staff Responses to Questions About the Custody Rule (December 13, 2011), Questions VI.7 and VI.8.A, available at: http://www.sec.gov/divisions/investment/custody_faq_030510.htm .

[15] *Id.*, Question VI.8B.

3. The Commission should harmonize mandatory performance reporting requirements.

CPOs and CTAs are subject to mandatory performance reporting requirements in their disclosure documents.[16] The Commission requires that operators of commodity pools that have less than a three-year operating history disclose performance data for each other pool and account operated by the CPO. Performance data may also be required for certain other persons associated with the pool.[17] For CTAs, a CTA disclosure document must generally show the performance of all accounts advised by the CTA.

The Commission recognizes that its disclosure obligations may conflict with the SEC's position concerning the use of past performance by investment advisers and RICs.[18] For example, the SEC staff has consistently taken positions indicating that adviser and RIC advertising that includes past performance for pools or accounts with investment objectives, styles and strategies not substantially similar to the pool being marketed may be deemed misleading.[19]

The CFTC suggests that the SEC staff may be able to address these regulatory conflicts on an individual firm-by-firm basis by way of no-action relief.[20] We submit, however, that such an approach would be slow, cumbersome, and highly inefficient, resulting in a significant drain on the SEC's limited resources. Accordingly, we urge the Commission to amend CFTC Regulations 4.25(c) and 4.35 to provide that investment advisers registered with the SEC will satisfy the requirements of these regulations by presenting performance information for pools and accounts with substantially similar investment objectives, policies, and strategies that would otherwise meet the standards for disclosure set forth in SEC staff positions.[21] Alternatively, the Commission should work with the SEC to issue joint rules applicable to investment advisers registered with both Commissions regarding the

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[16] CFTC Regulations 4.25(c) and 4.35.

[17] Under the Proposal, with regard to CPOs of RICs, the Commission is proposing that performance data for such other pools and accounts may be presented in the RIC's Statement of Additional Information.

[18] *See* Proposal n.27 and accompanying text.

[19] *See* Growth Stock Outlook Trust, Inc., SEC No-Action Letter (Apr. 15, 1986) ("Growth Stock"). The SEC staff provided no-action relief permitting the presentation in a mutual fund prospectus of an adviser's prior performance for private accounts managed by the adviser. The staff explicitly conditioned such relief with the requirement that, among other things, accounts "not managed in a substantially similar manner" to the fund must not be included in the performance. *See also* Nicholas-Applegate Mutual Funds, SEC No-Action Letter (Aug. 6, 1996 and Feb. 7, 1997); ITT-Hartford Mutual Funds, SEC No-Action Letter (Feb. 7, 1997); GE Funds, SEC No-Action Letter (Feb. 7, 1997).

[20] *See* Proposal n.27.

[21] This relief is needed with respect to CPOs and CTAs of pools that would not be able to claim relief under CFTC Regulation 4.7, either because they do not meet all of the conditions or because certain transition issues raised by the repeal of Regulation 4.13(a)(4) have not been resolved appropriately.

presentation of past performance information for pools or accounts other than the pool being offered.

4. We support the Commission's proposal to permit all CPOs and CTAs (including private fund advisers) to file updates to disclosure documents twelve months from the date of the document.

The Commission permits disclosure documents to be used for nine months from the date of the document before a new disclosure document must be prepared and filed with the NFA.[22] On the other hand, the SEC generally requires that prospectuses within its jurisdiction be updated annually.[23] Therefore, an SEC-registered CPO would be subject to inconsistent duties to update its disclosures. To resolve the inconsistency, the Commission has proposed that CPOs and CTAs be permitted to update their disclosure documents up to twelve months from the date of the document, in a manner consistent with the SEC's approach. The rule amendments appear to apply to all CPOs and CTAs (including private fund advisers), which is appropriate and consistent with the disclosure document timing requirements applicable to SEC-registered investment advisers under the Advisers Act.[24] We agree that the disclosure document deadlines should be the same for advisers to RICs and advisers to other pools and accounts.

5. **The Commission should extend the proposed relief for delivery requirements for disclosure documents and account statements to all CPOs.**

The Commission proposes to relieve CPOs to RICs from the requirement that a CPO distribute account statements monthly for pools with net assets in excess of $500,000 and at least quarterly for all other pools if the account statements are available on the CPO's web site.[25] The Commission proposes similar relief with respect to the delivery and acknowledgment requirements for disclosure documents for CPOs relying on the exemption in CFTC Regulation 4.12. We see no compelling reason to permit the use of web sites to satisfy delivery requirements for some CPOs and not others. Accordingly, we request that the Commission amend its regulations to permit all CPOs to comply with the disclosure document and account statement delivery requirements if such documents are available on the CPO's web site, subject to the same conditions proposed for CFTC Regulation 4.12(c)(2)(i) (*i.e.*, keeping the disclosure document current and informing prospective pool participants of the web site address).[26]

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[22] CFTC Regulation 4.26.

[23] Section 10(a)(3) of the Securities Act of 1933, as amended.

[24] *See* Advisers Act Rule 204-1 requiring annual amendments to Form ADV.

[25] CFTC Regulation 4.12(c).

[26] The web site would be password-protected as appropriate.

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We appreciate the Commission's consideration of our comments on the Proposal and our recommendation to apply certain of the harmonization provisions to all CPOs and CTAs, including private fund advisers. Please do not hesitate to contact me if we may provide any additional information regarding our comments or any other matters.

Sincerely,

Karen L. Barr
IAA General Counsel

cc: The Honorable Gary Gensler, Chairman
The Honorable Jill E. Sommers, Commissioner
The Honorable Bart Chilton, Commissioner
The Honorable Scott D. O'Malia, Commissioner
The Honorable Mark P. Wetjen, Commissioner

The Honorable Mary L. Schapiro, Chairman, SEC
The Honorable Elisse B. Walter, Commissioner, SEC
The Honorable Luis A. Aguilar, Commissioner, SEC
The Honorable Troy A. Paredes, Commissioner, SEC
The Honorable Daniel M. Gallagher, Commissioner, SEC