CADWALADER

Cabinet **News and Views**

Informed analysis for the financial services industry

CFTC Issues Proposed Rule to Modify Regulation 4.7 Exemptions


By **Peter Y. Malyshev**
Partner | Financial Regulation


By **Nikita B. Cotton**
Associate | Financial Regulation


By **Hayden Stark**
Law Clerk

On October 2, 2023, the Commodity Futures Trading Commission (the "Commission" or "CFTC") published a notice of proposed rulemaking (the "Proposed Rule") to amend CFTC Regulation 4.7, which provides exemptions to registered commodity pool operators ("CPOs") and commodity trading advisors ("CTAs") that solely operate or advise (as applicable) private pools from compliance with certain requirements related to disclosure, reporting, and recordkeeping (the "4.7 Exemption"). Specifically, the 4.7 Exemption is available for CPOs and CTAs whose prospective and actual commodity pool participants and/or advisory services are restricted to qualified eligible persons ("QEPs"). The comment period on the Proposed Rule will remain open until December 11, 2023.

The significant features of the Proposed Rule are as follows:

- The Proposed Rule would raise the financial requirements for qualifying as a QEP by increasing the monetary thresholds for the "Portfolio Requirement" of the QEP definition in § 4.7(a)(1)(v) to account for 30 years of inflation. The proposal would double the securities portfolio test to $4,000,000 and the initial margin and premium test to $400,000 – figures which the Commission consulted the CPI index to come up with and is seeking comment as to whether the CPI index or an alternative would be the "most appropriate" measure to assess how to modify the thresholds to account for inflationary effects.

- The Proposed Rule would establish new minimum disclosure requirements, including descriptions of a pool's principal risk factors, investment program, use of proceeds, custodians, fees and expenses, conflicts of interest, and performance.

- The Proposed Rule would codify exemptive relief that has historically been granted to allow CPOs of funds of funds to elect monthly rather than quarterly reporting schedules.

CFTC Commissioner Kristin N. Johnson stated that the amendments in the Proposed Rule are necessary to “address[] regulatory gaps that have arisen due to . . . changing dynamics in the derivatives markets” and to provide “robust customer protections” with respect to the determination of QEPs. Commissioner Summer K. Mersinger, in her dissent, expressed that the Commission has not adequately evaluated whether the Proposed Rule’s elimination of certain disclosure exemptions would address the Commission’s stated concerns.