

## CFTC Updates Regulation 4.7 Without Adopting the Proposed Disclosure Requirements

September 23, 2024

On September 12, 2024, the Commodity Futures Trading Commission (CFTC) adopted amendments to CFTC Regulation 4.7 (Reg. 4.7), a rule that provides exemptions from the broader compliance requirements under Part 4 of the CFTC regulations (Part 4) for registered commodity pool operators (CPOs) with respect to pools (4.7 pools) offered solely to “Qualified Eligible Persons” (QEPs) and registered commodity trading advisors (CTAs) that advise or manage commodity trading accounts of QEPs. The amendments (i) increase the financial thresholds in the “Portfolio Requirement” of the QEP definition and (ii) permit CPOs of fund of fund pools offered solely to QEPs to provide monthly account statements within 45 days of the month-end, rather than providing quarterly account statements within 30 days of the quarter-end. The CFTC chose not to adopt, at this time, the proposed minimum QEP disclosures.<sup>1</sup>

### Financial Thresholds in Portfolio Requirement Increased

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As noted above, Reg. 4.7 provides an exemption from certain compliance obligations for CPOs and CTAs who operate pools or offer trading programs for QEPs, who are deemed financially sophisticated so as not to require the protections of all of Part 4. Reg. 4.7(a) bifurcates the definition of QEP to:

- (i) persons who do not need to meet the so-called Portfolio Requirement,<sup>2</sup> and
- (ii) persons who do need to meet the Portfolio Requirement.<sup>3</sup>

Prior to the amendment, the Portfolio Requirement, which had not been modified since its adoption more than 30 years ago, meant that a person owned at least \$2,000,000 in securities or other assets, had on deposit with an FCM at least \$200,000 in margin or premiums for commodity interest transactions, or a combination of the two. Therefore, in order to reflect the effects of inflation and to harmonize the Portfolio Requirement with existing securities laws and regulations for sophisticated investors, the amendments essentially double the financial thresholds in the Portfolio Requirement. Specifically, Portfolio Requirement now requires a person to:

- own securities and other assets worth at least \$4,000,000;
- have on deposit with a futures commission merchant (FCM), for their own account at least \$400,000 in initial margin, option premiums, or minimum security deposits; or
- own a portfolio of funds and assets that, when expressed as a percentage of the two prior thresholds, have a combined value of at least 100 percent.

The increased financial thresholds take effect 60 days after publication of the adopting release in the Federal Register (Effective Date) and CPOs and CTAs must implement the increased financial thresholds for QEPs subject to the Portfolio Requirement within six months of such publication. While CPOs and CTAs would not be required to redeem existing pool participants or terminate advisory relationships with persons not meeting the updated Portfolio Requirement, the amendments prohibit CPOs and CTAs from selling any additional pool participations or opening any additional exempt account for such persons.

## Alternate Account Statement Schedule Permitted for Certain 4.7 Pools

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Reg. 4.7(b)(3) requires CPOs of 4.7 pools to distribute account statements “no less frequently than quarterly within 30 days after the end of the reporting period.” However, CPOs of 4.7 pools that are funds of funds have routinely sought and obtained exemptive relief from the CFTC to permit the distribution of account statements monthly within 45 days of the month-end (Alternate Account Statement Schedule). The amendments codify the Alternate Account Statement Schedule for 4.7 pools that are funds of funds.

The Alternate Account Statement Schedule will be available to CPOs as of the Effective Date.

### For More Information

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We are available at any time to answer questions, discuss scenarios, and provide guidance. If you would like further information concerning the matters discussed in this article, please contact any of the following attorneys or the Chapman attorney with whom you regularly work:

**Juan M. Arciniegas**  
Chicago  
312.845.3710  
arciniegas@chapman.com

**Curtis A. Doty**  
New York  
212.655.2512  
cdoty@chapman.com

**Peter M. Hong**  
Washington, DC  
202.478.6472  
phong@chapman.com

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- 1 For CPOs, the proposed minimum disclosures would have required disclosures regarding the principal risk factors for the exempt pool, the investment program and use of proceeds, fees and expenses, conflicts of interest, and performance information in a disclosure document, which is not currently required. Similarly, for CTAs, the proposed minimum disclosures would have required disclosures regarding principals of the CTA and intermediaries used, principal risk factors of the trading program, the trading program and its approach to offsetting positions, fees charged, conflicts of interest, and performance information.
  - 2 Pursuant to Reg. 4.7(a)(2), this list includes, but is not limited to: (1) registered futures commission merchants (FCMs), registered retail foreign exchange dealers, registered swap dealers, and principals thereof; (2) registered broker-dealers and principals thereof; (3) certain registered CPOs and principals thereof; (4) certain CTAs and principals thereof; (5) certain registered investment advisers and principals thereof; (6) “qualified purchasers” as defined under the Investment Company Act (ICA); (7) “knowledgeable employees” as defined under the ICA; (8) certain persons associated with exempt pools; (9) certain trusts; (10) 501(c)(3) entities for whom the person making the investment decisions is a QEP; (11) non-U.S. persons; and (12) exempt pools.
  - 3 Pursuant to Reg. 4.7(a)(3), this list includes, but is not limited to: (1) certain registered investment companies or business development companies; (2) banks as defined the Securities Act of 1933 (Securities Act) or any savings and loan association or other institution as defined in the Securities Act acting for its own account or for the account of a QEP; (3) certain insurance companies acting for their own account or that of a QEP; (4) certain employee state benefit plans; (5) certain ERISA plans; (6) private business development companies; (7) certain corporations or business trusts, partnerships, limited liability companies or similar business ventures; (8) natural persons who are “accredited investors”; (9) natural persons who would otherwise be deemed to be accredited investors; (10) certain pools, trusts, insurance company separate accounts or bank collective trusts; and (11) certain government entities.

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