

CLIENT ALERT

CFTC Raises Qualification Threshold in Rule 4.7

Agency declines to mandate new disclosures at this time

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The Commodity Futures Trading Commission last week adopted amendments to Rule 4.7 that will double the monetary thresholds of the portfolio requirement for a “qualified eligible person.” Private fund managers should review their offering documents to ensure compliance with the new requirements, which become effective six months following publication in the Federal Register. The CFTC also adopted its proposal to permit managers of Rule 4.7 funds of funds to follow an alternative schedule for periodic reporting. The agency did not adopt the portions of the proposal that would have imposed new disclosure and recordkeeping requirements similar to those currently required for commodity pool operators (“CPOs”) and commodity trading advisors (“CTAs”) that do not avail themselves of the Rule 4.7 exemption.

Background on Rule 4.7

The CFTC adopted Rule 4.7 in 1992 to better align its rules with the SEC’s rules with respect to offerings to sophisticated investors pursuant to Regulation D. Rule 4.7 exempts an eligible CPO or CTA from many of the disclosure, reporting and recordkeeping requirements under Part 4 of the CFTC rules that are generally applicable to registered CPOs and CTAs. The CFTC noted that, in recent years, an increasing number of CPOs and CTAs rely on Rule 4.7. In October 2023, the CFTC proposed amendments to Rule 4.7 that would have: (1) doubled the monetary thresholds of the portfolio requirements for a qualified eligible person (“QEP”); (2) required CPOs operating pools and CTAs advising accounts under Rule 4.7 to deliver, and regularly update, an offering memorandum or disclosure document, which would include performance information and a break-even table, conflicts of interest, risks and information regarding fees and expenses; and (3) codified the ability of CPOs of 4.7 funds of funds to follow an alternative periodic account statement reporting schedule.¹ The CFTC

¹ See, 88 Fed. Reg. 70852 (Oct. 12, 2023). For a discussion of the October 2023 rule proposal, please see our Client Alert, available [here](#).

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stated that the proposed amendments were intended to ensure that investors in the complex derivatives markets receive relevant and comprehensive information. Many of the comments to the proposal supported increasing the monetary thresholds to reflect the effects of inflation since Rule 4.7 was adopted. The commenters generally opposed the CFTC's proposed prescriptive disclosure regime for Rule 4.7 CPOs and CTAs. While the final rule does not include amendments to the disclosure obligations, the CFTC noted that it will continue to consider the issue and other regulatory alternatives.²

Portfolio requirement thresholds for QEPs

As amended, the definition of QEP will include a person who (1) owns securities and other investments worth at least \$4,000,000; (2) has on deposit with an FCM, generally, at least \$400,000³ in initial margin and option premiums; or (3) owns a portfolio of funds and assets that, when expressed as percentages of the first two thresholds, has a combined value of at least 100%.⁴

Consistent with the requirements of current Rule 4.7, the QEP status determination will continue to be made at the time of subscription or initiation of a managed account. A CPO will not be required to redeem existing investors who do not satisfy the higher thresholds; a CTA will not be required to terminate advisory relationships with clients who are currently QEPs but who would not satisfy the increased threshold. Notably, however, investors that satisfied the prior QEP standard when making an initial investment will *not* be permitted to contribute additional amounts to a Rule 4.7 pool or account if they no longer satisfy the updated portfolio requirement thresholds under the final rule.

Alternative periodic reporting schedule for 4.7 fund of funds CPOs

CPOs of funds of funds often have difficulty complying with the quarterly account statement schedule in Rule 4.7(b)(3). That rule requires distribution of quarterly performance information within 30 days after the end of the reporting period. Such CPOs have regularly requested, and the CFTC has routinely issued, exemptive relief to permit these CPOs to follow an alternate account statement schedule wherein *monthly* account statements are delivered to investors within 45 days of month end. Among other reasons for such relief, CPOs of funds of funds cannot control the timing of when they receive financial information from underlying funds that is necessary to prepare the fund of funds account statements.

As amended, Rule 4.7 codifies the prior exemptive relief, and a CPO of a fund of funds will be permitted to distribute to investors an account statement within 45 days of each month end in lieu of a quarterly statement within 30 days of each

² Commissioner Summer K. Mersinger issued a statement supporting the final rule, noting that it achieved the balance that she believed was missing in the proposal, from which she dissented.

³ The current thresholds for the portfolio requirement in Rule 4.7 are \$2,000,000 in securities and investments, and \$200,000 in initial margin and option premiums.

⁴ It is worth noting that Rule 4.7 commodity pools are one category of funds included in the Volcker Rule's definition of a "covered fund." Consequently, the rule change may impact any Volcker analysis with respect to a 4.7 pool.

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quarter end. The CFTC noted that this approach would provide such CPOs with additional time to gather necessary account statement information and would actually provide pool participants with more frequent and accurate reporting.

Effective Dates

The increased portfolio requirement thresholds will be effective six months after publication in the Federal Register. The optional monthly account statement reporting schedule for funds of funds CPOs will be available to CPOs 60 days after publication in the Federal Register. Compliance is required upon election of that schedule by the CPO.

If you have any questions regarding this client alert, please contact one of the authors, any member of our CFTC team listed below, or the Willkie attorney with whom you regularly work.

Willkie has a dedicated team of attorneys with extensive knowledge and experience in all aspects of the Commodity Exchange Act and the CFTC regulatory regime. We would be pleased to assist on your matters.

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