crowell moring

CLIENT ALERT

CFTC Begins to Discuss Risk Management with Investment Funds

Mar.20.2014

On March 18, 2014, the Commodities Futures Trading Commission's (CFTC) Division of Swap Dealer and Intermediary Oversight and Division of Clearing and Intermediary Oversight hosted a public roundtable to discuss risk management practices by commodity pool operators. The roundtable focused on risk management procedures in various types of commodity pools, including registered investment companies, public commodity pools, private funds and funds of funds.

The CFTC staff noted that as banks are retreating from certain businesses that are affected by new regulations, investment funds (including funds registered as commodity pool operators) are in some cases stepping into the void. While not explicitly stated, the key question of the roundtable seemed to be whether current regulatory oversight adequately addresses the new risks posed by these funds. The CFTC staff did not have a proposal before the group to discuss. Rather, they asked very basic questions on how investment funds currently create and implement risk metrics and procedures.

The general message to the CFTC from participants was that funds are already at the forefront of risk management, including through regulatory examinations, investor due diligence and external audits and fund administration, because of the demands made upon them by their own investors. Therefore, they view no further regulation is needed. Throughout the session, participants generally repeated the message that to be competitive in soliciting investments from large institutional investors, investment funds must have the most sophisticated risk management tools available. Participants also noted that because investment fund risk management is rapidly innovating, risk management regulations would impose unnecessary rigidity and deter rapid response to new risks and market conditions. The participants also stressed that risks vary from fund to fund and therefore, in their belief, no template risk management structure or regulation would be able to account adequately for risks specific to each investment fund.

In addition to commodity pools, SEC and FCA-registered investment funds also participated in the roundtable. These funds made the point that they are continually hoping for more symmetry in regulatory efforts by agencies and described varying methods and practices they must undertake to satisfy different regulators.

Commodity pool operators are already obligated as part of their continuing supervisory responsibilities under NFA Compliance Rules 2-9, 2-36 and 2-39 to review their operations on a yearly basis using NFA's Self-Examination Questionnaire. This self-assessment, however, does not explicitly address many of the CFTC staff's queries expressed at the roundtable. In addition, the CFTC's Form CPO-PQR requires additional information gathering relevant to risk management. While new regulations are perhaps not imminent, understanding and management of risks appears to be an increasingly important focus area for regulators (whether at the CFTC, SEC, NFA, FINRA or otherwise), in particular risks posing potential systemic implications. We continue to counsel advance preparation to enable investment funds to be able to properly respond at any time to regulatory inquiries relating to risk management practices.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

Richard B. Holbrook Jr.
Partner – Washington, D.C.
Phone: +1 202.508.8779
Email: rholbrook@crowell.com