

CLIENT ADVISORY



CFTC Proposed Amendments to Regulation 4.41

SEPTEMBER 2006

On August 23, 2006, the Commodity Futures Trading Commission (the “CFTC”) issued proposed amendments (the “Proposal”) to Regulation § 4.41, which governs advertising by commodity pool operators (“CPO”), commodity trading advisors (“CTA”) and the principals thereof. The amendments would (1) restrict the use of testimonials, (2) clarify the required placement of the prescribed simulated or hypothetical performance disclaimer, and (3) include within the regulation’s coverage advertisements made through electronic media.

Washington, DC
+1 202.942.5000

New York
+1 212.715.1000

London
+44 (0)20 7786 6100

Brussels
+32 (0)2 517 6600

Los Angeles
+1 213.243.4000

San Francisco
+1 415.356.3000

Northern Virginia
+1 703.720.7000

Denver
+1 303.863.1000

BACKGROUND

CFTC Regulation § 4.41 covers both oral and written communications and applies regardless of whether a CPO or CTA is exempt from registration under the Commodity Exchange Act, as amended (the “CE Act”), pursuant to CFTC Regulation §§ 4.13 or 4.14 or Sections 4m(1) or 4m(3) under the CE Act. Under Regulation § 4.41, CPOs, CTAs, or their principals have discretion over the presentation of their past performance results, as long as the format is not false, misleading or deceptive. However, when past performance results are simulated or hypothetical, Regulation § 4.41(b)(1) requires that they “be accompanied by” a prescribed statement (either from the text of the Regulation itself or prescribed by a registered futures association such as the NFA) to warn customers of the limitations inherent in such results. Furthermore, when that performance is presented other than orally, Regulation § 4.41(b)(2) requires the prescribed statement to be “prominently disclosed.”

THE PROPOSAL

Presentation of Actual Past Performance: Proposed Addition of Regulation § 4.41(a)(3)

The CFTC has proposed adding a new paragraph to Regulation § 4.41 to govern the use of testimonials by a CPO, CTA, or principal thereof. Proposed Regulation § 4.41(a)(3) would require advertisements utilizing a testimonial to prominently disclose: (i) that the testimonial may not be representative of the experience of other clients; (ii) that the testimonial is no guarantee of future performance or success; and (iii) if more than a nominal sum is paid, the fact that it is a paid testimonial.

This summary is intended to be a general summary of the law and does not constitute legal advice. You should consult with competent counsel to determine applicable legal requirements in a specific fact situation.

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It is the CFTC's belief that advertisements that do not contain this information may provide potential customers with a misleading assessment about the quality of services being offered or the motivation of the person providing the testimonial, thus rendering the advertisement false, misleading or deceptive.

Simulated or Hypothetical Performance Presentation: Proposed Amendments to Regulation § 4.41(b)

In light of the growing popularity of electronic means of communication not in existence 25 years ago when Regulation § 4.41 was first adopted, the CFTC is proposing to amend Regulation § 4.41(b)(1) to clarify the meaning of the term "accompanied by." The CFTC has discovered numerous instances where persons were not adequately identifying their trading results as simulated or hypothetical, or were not locating the prescribed disclaimer in an appropriate place. To rectify this situation, the CFTC proposes to amend Regulation § 4.41(b)(1)(i) by including in the prescribed disclaimer references to "these results" when discussing simulated or hypothetical

performance results. Additionally, the CFTC proposes to amend Regulation § 4.41(b)(2) by adding the requirement that the prescribed disclaimer be "in immediate proximity to the simulated or hypothetical performance being presented."

The Scope of Regulation § 4.41: Proposed Amendment to Regulation § 4.41(c)(1)

The term "commodity trading advisor," as originally adopted by Congress in 1974, included any person who provided commodity interest trading advice "either directly or through publications or writings." With the subsequent advent and increasing use of electronic media by CTAs, in 1982 Congress amended the CTA definition to include advice given through such electronic media. The CFTC recognizes that CPOs, like CTAs, routinely solicit customers based on their performance results through various forms of electronic media. Accordingly, the CFTC is proposing to amend Regulation § 4.41(c)(1) to explicitly clarify that advertisements by "electronic media, or otherwise, including information provided via internet or e-mail" fall within the scope of Regulation § 4.41.

If you have questions about this advisory, or other related issues, please feel free to contact your Arnold & Porter attorney or:

Michael F. Griffin
+1 212.715.1136
Michael.Griffin@aporter.com

J.P. Bruynes
+1 212.715.1135
JP.Bruynes@aporter.com

Rob Holton
+1 212.715.1137
Robert.Holton@aporter.com

William V. de Cordova
+1 212.715.1137
William.deCordova@aporter.com

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