



## Disclosure Documents: A Guide for CPOs

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**February 2020 Revisions:** The Disclosure Documents Guide was previously serving both our CPO and CTA Members. In an effort to address the specific needs of each Member, NFA has created a separate Disclosure Document Guide tailored specifically to only CPOs. Along with the new guide, NFA updated the contents to incorporate the adoption of the Interpretive Notice regarding disclosure requirements for NFA Members engaging in virtual currency activities and updates to the Interpretive Notice regarding the preparation and presentation of a pool's break-even analysis.

February 2020

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## Who Must Prepare a Disclosure Document?

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Commodity pool operators (CPO) must deliver a disclosure document (Document) to a prospective pool participant prior to or when it delivers the pool subscription agreement to the participant. See [Filing Disclosure Documents and the Review Process](#) on page 36 for filing procedures.

**Note:** *This does not apply when the prospective pool participant is another pool operated by the same CPO, or by a CPO who controls, is controlled by or is under common control with the CPO. Additionally, certain CPOs registered under the Securities Act of 1933 or the Investment Company Act of 1940 may claim relief from the delivery of a disclosure document under CFTC Regulation 4.12(c) which provides for substituted compliance.*

**Exception.** A Document is not required to be delivered where the CPO is offering a pool exclusively to a Qualified Eligible Persons (QEPs) as defined by Commodity Futures Trading Commission (CFTC) Regulation 4.7 and the required exemption notice has been filed with NFA.

## General Disclosure Document Guidelines for Commodity Pools

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Documents for commodity pools must comply with NFA Compliance Rule 2-35. This rule limits the information that may be included in a pool disclosure document. For public commodity pools, the rule requires that Documents be prepared in two parts, consisting of a disclosure document and a Statement of Additional Information (SAI). The information which can be included in Part 1 of the Document is limited to the information required by the CFTC's Part 4 Regulations and any other information that the SEC or state securities administrators require to be included in Part 1 of a two-part disclosure document. Any information the CPO elects to disclose that is not specifically required by the CFTC, the SEC, or state securities administrators must appear in the SAI. The CPO of a public pool must provide both the disclosure document and the SAI to prospective clients prior to accepting or receiving any funds.

Documents for private placement commodity pools are not required to be prepared in two parts unless the CPO chooses to disclose information other than that required by the CFTC's Part 4 Regulations in which case such information must appear in an SAI. CPOs of private commodity pools are not required to deliver an SAI to all prospective clients but must inform clients that one exists and provide it to them upon request. The SAI may be either bound together with the disclosure document or provided separately.

If a CPO prepares an SAI, the cover page of the SAI should include a date as well as the name of the commodity pool. In addition, it should include the date of the disclosure document and a statement that it is the second part of a two-part document and should be read in conjunction with the pool's disclosure document. Finally, a table of contents should immediately follow the SAI cover page.

NFA Compliance Rule 2-35 also requires that disclosure documents for commodity pools be written using plain English principles. In particular, disclosure documents should be written:

- In the active voice;
- Using short sentences and paragraphs;
- Breaking up the document into short sections, using titles and subtitles that specifically describe the contents of each section;
- Using words that are definite, concrete, and part of everyday language;
- Avoiding legal jargon and highly technical terms;
- Using glossaries to define technical terms that cannot be avoided;
- Avoiding multiple negatives;
- Saying something once where it is most important rather than repeating information;
- Using tables and bullet lists, where appropriate.

Documents which adhere to the guidelines set forth pursuant to the Rule should generally be 30 pages or less. Documents for more complex pools; however, such as multi-advisor pools or principal-protected pools may be slightly longer. When reviewing Documents for compliance with this Rule, NFA wants to avoid making determinations on what information must be included in order for a prospective participant to understand the fundamental characteristics of a pool. NFA feels that the CPO of a pool is better able to make these decisions. However, at the same time, NFA will review the Documents to ensure they provide the information in a manner which is manageable and easy to understand.

**Additional NFA References:**

- [NFA Interpretive Notice 9035](#): Rule – 2-35: CPO/CTA Disclosure Documents

## Disclosure Document Requirements for Commodity Pools

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Documents for pools must include the following information:

### Cover Page

The cover page of the Document must prominently include the Cautionary Statement below. Prominently means displayed in CAPITAL letter and in **boldface** type.

**THE COMMODITY FUTURES TRADING COMMISSION HAS NOT PASSED UPON THE MERITS OF PARTICIPATING IN THIS POOL NOR HAS THE COMMISSION PASSED ON THE ADEQUACY OR ACCURACY OF THIS DISCLOSURE DOCUMENT.**

### Risk Disclosure Statement

The applicable Risk Disclosure Statement must be prominently displayed immediately after the cover page of the Document.

If the pool trades commodity interests, the following Risk Disclosure Statement is required:

#### **RISK DISCLOSURE STATEMENT**

**YOU SHOULD CAREFULLY CONSIDER WHETHER YOUR FINANCIAL CONDITION PERMITS YOU TO PARTICIPATE IN A COMMODITY POOL. IN SO DOING, YOU SHOULD BE AWARE THAT COMMODITY INTEREST TRADING CAN QUICKLY LEAD TO LARGE LOSSES AS WELL AS GAINS. SUCH TRADING LOSSES CAN SHARPLY REDUCE THE NET ASSET VALUE OF THE POOL AND CONSEQUENTLY THE VALUE OF YOUR INTEREST IN THE POOL. IN ADDITION, RESTRICTIONS ON REDEMPTIONS MAY AFFECT YOUR ABILITY TO WITHDRAW YOUR PARTICIPATION IN THE POOL.**

**FURTHER, COMMODITY POOLS MAY BE SUBJECT TO SUBSTANTIAL CHARGES FOR MANAGEMENT, AND ADVISORY AND BROKERAGE FEES. IT MAY BE NECESSARY FOR THOSE POOLS THAT ARE SUBJECT TO THESE CHARGES TO MAKE SUBSTANTIAL TRADING PROFITS TO AVOID DEPLETION OR EXHAUSTION OF THEIR ASSETS. THIS DISCLOSURE DOCUMENT CONTAINS A COMPLETE DESCRIPTION OF EACH EXPENSE TO BE CHARGED THIS POOL AT PAGE (insert page number) AND A STATEMENT OF THE PERCENTAGE RETURN NECESSARY TO BREAK EVEN, THAT IS, TO RECOVER THE AMOUNT OF YOUR INITIAL INVESTMENT, AT PAGE (insert page number).**

**THIS BRIEF STATEMENT CANNOT DISCLOSE ALL THE RISKS AND OTHER FACTORS NECESSARY TO EVALUATE YOUR PARTICIPATION IN THIS COMMODITY POOL. THEREFORE, BEFORE YOU DECIDE TO PARTICIPATE IN THIS COMMODITY POOL, YOU SHOULD CAREFULLY STUDY THIS DISCLOSURE**

**DOCUMENT, INCLUDING A DESCRIPTION OF THE PRINCIPAL RISK FACTORS OF THIS INVESTMENT, AT PAGE (insert page number).**

If the pool may trade foreign futures or options contracts on foreign exchanges, the Risk Disclosure Statement must further state:

**YOU SHOULD ALSO BE AWARE THAT THIS COMMODITY POOL MAY TRADE FOREIGN FUTURES OR OPTIONS CONTRACTS. TRANSACTIONS ON MARKETS LOCATED OUTSIDE THE UNITED STATES, INCLUDING MARKETS FORMALLY LINKED TO A UNITED STATES MARKET, MAY BE SUBJECT TO REGULATIONS WHICH OFFER DIFFERENT OR DIMINISHED PROTECTION TO THE POOL AND ITS PARTICIPANTS. FURTHER, UNITED STATES REGULATORY AUTHORITIES MAY BE UNABLE TO COMPEL THE ENFORCEMENT OF THE RULES OF REGULATORY AUTHORITIES OR MARKETS IN NON-UNITED STATES JURISDICTIONS WHERE TRANSACTIONS FOR THE POOL MAY BE EFFECTED.**

If the pool may engage in retail forex transactions, the Risk Disclosure Statement must further state:

**YOU SHOULD ALSO BE AWARE THAT THIS COMMODITY POOL MAY ENGAGE IN OFF-EXCHANGE FOREIGN CURRENCY TRADING. SUCH TRADING IS NOT CONDUCTED IN THE INTERBANK MARKET. THE FUNDS THAT THE POOL USES FOR OFF-EXCHANGE FOREIGN CURRENCY TRADING WILL NOT RECEIVE THE SAME PROTECTIONS AS FUNDS USED TO MARGIN OR GUARANTEE EXCHANGE-TRADED FUTURES AND OPTION CONTRACTS. IF THE POOL DEPOSITS SUCH FUNDS WITH A COUNTERPARTY AND THAT COUNTERPARTY BECOMES INSOLVENT, THE POOL'S CLAIM FOR AMOUNTS DEPOSITED OR PROFITS EARNED ON TRANSACTIONS WITH THE COUNTERPARTY MAY NOT BE TREATED AS A COMMODITY CUSTOMER CLAIM FOR PURPOSES OF SUBCHAPTER IV OF CHAPTER 7 OF THE BANKRUPTCY CODE AND THE REGULATIONS THEREUNDER. THE POOL MAY BE A GENERAL CREDITOR AND ITS CLAIM MAY BE PAID, ALONG WITH THE CLAIMS OF OTHER GENERAL CREDITORS, FROM ANY MONIES STILL AVAILABLE AFTER PRIORITY CLAIMS ARE PAID. EVEN POOL FUNDS THAT THE COUNTERPARTY KEEPS SEPARATE FROM ITS OWN FUNDS MAY NOT BE SAFE FROM THE CLAIMS OF PRIORITY AND OTHER GENERAL CREDITORS.**

If the pool may engage in swaps, the Risk Disclosure Statement must further state:

**SWAPS TRANSACTIONS, LIKE OTHER FINANCIAL TRANSACTIONS, INVOLVE A VARIETY OF SIGNIFICANT RISKS. THE SPECIFIC RISKS PRESENTED BY A PARTICULAR SWAP TRANSACTION NECESSARILY DEPEND UPON THE TERMS OF THE TRANSACTION AND YOUR CIRCUMSTANCES. IN GENERAL, HOWEVER, ALL SWAPS TRANSACTIONS INVOLVE SOME COMBINATION OF MARKET RISK, CREDIT RISK, COUNTERPARTY CREDIT RISK, FUNDING RISK, LIQUIDITY RISK, AND OPERATIONAL RISK.**

**HIGHLY CUSTOMIZED SWAPS TRANSACTIONS IN PARTICULAR MAY INCREASE**



**LIQUIDITY RISK, WHICH MAY RESULT IN A SUSPENSION OF REDEMPTIONS. HIGHLY LEVERAGED TRANSACTIONS MAY EXPERIENCE SUBSTANTIAL GAINS OR LOSSES IN VALUE AS A RESULT OF RELATIVELY SMALL CHANGES IN THE VALUE OR LEVEL OF AN UNDERLYING OR RELATED MARKET FACTOR.**

**IN EVALUATING THE RISKS AND CONTRACTUAL OBLIGATIONS ASSOCIATED WITH A PARTICULAR SWAP TRANSACTION, IT IS IMPORTANT TO CONSIDER THAT A SWAP TRANSACTION MAY BE MODIFIED OR TERMINATED ONLY BY MUTUAL CONSENT OF THE ORIGINAL PARTIES AND SUBJECT TO AGREEMENT ON INDIVIDUALLY NEGOTIATED TERMS. THEREFORE, IT MAY NOT BE POSSIBLE FOR THE COMMODITY POOL OPERATOR TO MODIFY, TERMINATE, OR OFFSET THE POOL'S OBLIGATIONS OR THE POOL'S EXPOSURE TO THE RISKS ASSOCIATED WITH A TRANSACTION PRIOR TO ITS SCHEDULED TERMINATION DATE.**

If the potential liability of a participant in the pool is greater than the amount of the participant's contribution for the purchase of an interest in the pool and the profits earned thereon, whether distributed or not, the Risk Disclosure Statement must prominently disclose the following as the **last** paragraph of the Risk Disclosure Statement:

**ALSO, BEFORE YOU DECIDE TO PARTICIPATE IN THIS POOL, YOU SHOULD NOTE THAT YOUR POTENTIAL LIABILITY AS A PARTICIPANT IN THIS POOL FOR TRADING LOSSES AND OTHER EXPENSES OF THE POOL IS NOT LIMITED TO THE AMOUNT OF YOUR CONTRIBUTION FOR THE PURCHASE OF AN INTEREST IN THE POOL AND ANY PROFITS EARNED THEREON. A COMPLETE DESCRIPTION OF THE LIABILITY OF A PARTICIPANT IN THIS POOL IS EXPLAINED MORE FULLY IN THIS DISCLOSURE DOCUMENT.**

## Table of Contents

The Document must contain a table of contents showing, by subject matter, the location of the disclosures made in the Document. The table of contents must appear immediately following the Risk Disclosure Statement.

## Introduction

The forepart of the Document must include the full name, address of the main business office, main business telephone number, and form of organization of both the pool and the CPO. If the mailing address of the main business office is a post office box number or is not within the United States, its territories or possessions, the Document must state where the books and records will be kept and made available for inspection.

If applicable, the forepart of the Document must state if the pool is:

- Privately offered pursuant to section 4(2) of the Securities Act of 1933, as amended or pursuant to Regulation D thereunder,

- A multi-advisor pool as defined in [CFTC Regulations 4.10\(d\)\(2\)](#),
- A principal-protected pool as defined in [CFTC Regulations 4.10\(d\)\(3\)](#) or
- Continuously offered. If the pool is not continuously offered, the closing date of the offering must be disclosed.

Finally, the date (month, day, and year) when the CPO first intends to use the Document and the break-even point per unit of initial investment must be included in the forepart of the Document. See [Break-Even Analysis](#) on page 17 for how the break-even point is calculated. The break-even point must be expressed as a dollar amount and a percentage of the minimum unit of initial investment. A CPO may not use a Document more than 12 months after the date of the Document.

For purposes of the Document, the forepart has been defined as the first few pages following the table of contents.

### The CPO and its Principals

The Document must identify, by name, the CPO and all its principals. The Document must also clearly identify those principals that will make trading decisions for the pool, or who supervises, or has authority to allocate pool assets to, persons so engaged.

### Business Background

The Document must disclose the business background of the CPO and any principal of the CPO who will participate in making trading or operational decisions for the pool, or who supervise persons so engaged, for the five years preceding the date of the Document. Officers and Directors are included among the principals whose business background is required.

The business background of the CPO should include the effective date of its NFA membership and CFTC registration(s). If the CPO was organized within the last five years, then its business background should include the date it organized. This section should also include a reference to the location in the Document where any of the required past performance disclosures for the CPO is presented. If the CPO has been previously registered under any other name, this information must also be included.

The business background for each required principal should include the starting and ending period (month and year) of each employment, the full name and main business of each employer (employer's CFTC registration may be used, if applicable), the principal's functions while so employed, and the principal's active CFTC registration and principal listing dates (month, day, and year). All gaps in employment must be explained. This section should also include a reference to the location in the Document where any of the required past performance disclosures for the principal is presented.

### **Additional NFA References:**

- [NFA Notice to Members: I-10-12](#): NFA provides guidance for disclosure of business background information by commodity pool operators and commodity trading advisors

## The Trading Manager

A trading manager is any person, other than the pool's CPO, who has sole or partial authority to allocate pool assets to commodity trading advisors (CTAs) or investee pools. If the pool will utilize a trading manager, the Document must identify the name of the trading manager and all of its principals and identify those principals that will make trading decisions for the pool. In addition, the business background of the trading manager and each principal who will participate in making trading or operational decisions for the pool or who supervise persons so engaged must be disclosed for the five years preceding the date of the Document.

## The Investment Program

The Document must disclose the types of commodity interests and other interests that the pool will trade, including:

- The approximate percentage of the pool's assets that will be used to trade commodity interests, securities and other types of interests, categorized by type of commodity or market sector, type of swap, type of security (debt, equity, preferred equity), whether traded or listed on a regulated exchange market, maturity ranges and investment ratings, as applicable.
- The extent to which such interests are subject to state or federal regulation, regulation by non-United States jurisdiction or rules of a self-regulatory organization.
- The custodian or other entity (e.g., bank or broker-dealer) which will hold such interests. In addition, if such interests will be held or if pool assets will be invested in a non-United States jurisdiction, the Document must disclose the jurisdiction in which such interests or assets will be held or invested.

The Document must include a description of the trading and investment programs and policies that will be followed by the pool, and any material restrictions or limitations on trading. This description must include, if applicable, an explanation of the systems used to select CTAs, investee pools, and types of investment activity to which pool assets will be committed.

In addition, if the CPO has chosen a method for how futures commission merchants (FCM) and/or retail foreign exchange dealers (RFED) carrying the pool's accounts treat offsetting positions other than to close out all offsetting positions or to close out offsetting positions on other than a first-in, first-out basis, then the description of the trading and investment programs must disclose the method.

### ***Use of Proceeds***

The Document must disclose the manner in which the pool will fulfill its margin requirements and the approximate percentage of the pool's assets that will be held in segregation pursuant to the Act and the CFTC's regulations thereunder. If the pool will fulfill its margin requirements with other than cash deposits, the nature of such deposits must be disclosed and, if assets deposited by the pool as margin or as security deposit generate income, the Document must state to whom that income will be paid.

### **Major CTA(s)**

The Document must identify, by name, each major CTA. A major CTA is any CTA that is currently or will be allocated 10% or more of the pool's assets. The Document must also disclose the names of all principals of these major CTAs as well as identify those principals that will make trading decisions for the pool.

The Document must disclose the business background(s) of the major CTA(s) and each principal who will participate in making trading or operational decisions for the pool, or who will supervise persons so engaged, for the five years preceding the date of the Document. The Document must also disclose the location in the Document where any of the required past performance disclosures for such principals is presented.

The Document must disclose a summary description of each major CTA, including:

- The respective percentage of pool assets allocated to each major CTA,
- A description of the nature and operation of the trading programs each major CTA will follow, including the types of interests traded pursuant to such programs, and
- Each major CTA's historical experience trading such programs including material information as to volatility, leverage and rates of return and the length of time during which the major CTA has traded such program.

If the pool is organized as a series pool, then a major CTA is determined based on whether the CTA is currently or will be allocated 10% or more of the series' assets.

### **Major Investee Pool(s)**

The Document must identify, by name, each major investee pool and the CPO of such investee pool. The Document must also disclose the names of all principals of the CPO(s) of the major investee pools as well as identify those principals that will make trading decisions for the pool. A major investee pool is any pool in which 10% or more of the offered pool's net asset value is invested.

The Document must disclose the business background(s) of each major investee pool's CPO and each principal of the investee pool's CPO who will participate in making trading or operational decisions for the pool, or who will supervise persons so engaged, for the five years preceding the date of the Document. The Document must also disclose the location in the Document where any of the required past performance disclosures for such principals is presented.

The Document must disclose a summary description of each major investee pool or fund, including:

- The percentage allocation of pool assets invested in each major investee pool and fund,
- A description of the nature and operation of such major investee pools and funds, including for each major investee pool or fund the types of interests traded, material information as to volatility, leverage and rates of return for such major investee pool or fund and the

period of its operation.

If the pool is organized as a series pool, then a major investee pool is determined based on whether the series has invested 10% or more of its assets into the investee pool.

### ***Inception of Trading***

The Document must disclose the minimum and maximum subscriptions that will be necessary for the pool to commence trading and the maximum subscriptions that may be contributed to the pool. The Document must disclose the maximum period of time the pool will hold funds prior to the commencement of trading and the disposition of funds received if the pool does not receive the necessary amount to commence trading, including the period of time within which the disposition will be made. The Document must state where the CPO will deposit funds received prior to the commencement of trading and to whom any income received from these deposits will be paid.

### **Ownership in the Pool**

The Document must disclose the extent of any ownership in the pool held by the CPO, the pool's trading manager, the pool's major CTAs, the operators of the pool's major investee pools and any principals of the foregoing.

### **The Futures Commission Merchant and/or RFED**

The Document must identify, if known, the name of the FCM and/or RFED through which the pool will execute its trades.

### **The Introducing Broker**

If the pool will use an introducing broker (IB) to introduce its trades, if known, the name of the IB must be disclosed in the Document.

### **Other Forex Counterparties**

If the pool will use a counterparty not registered as an FCM or RFED, the name of that counterparty must be disclosed in the Document. Other eligible counterparties are specified under Section 2(c)(2)(B)(i)(II) of the CEA and include U.S. financial institutions, certain FCM affiliates, and financial holding companies as defined under the Bank Holding Company Act of 1956.

### **Principal Risk Factors**

The Document must include a discussion of the principal risk factors of participation in the offered pool. This discussion must include, without limitation, the risks relating to volatility, leverage, liquidity, and counterparty creditworthiness, as applicable to the types of trading programs to be followed, trading structures to be employed and investment activity (including retail forex transactions) expected to be engaged in by the offered pool.

The CPO should examine all aspects of participation in the offered pool that may require disclosure of additional risk factors such as day trading, electronic trading issues, concentration risk, the use of options, the use of stops, foreign exchange risk, SFPs, forwards, EFPs, forex, swaps, underlying or spot virtual currency, virtual currency derivatives, etcetera.

### ***Additional Disclosures for Virtual Currency***

#### **Virtual Currency Disclosure Requirements for Pools that engage in Virtual Currency Derivatives**

NFA does not prescribe standardized disclosure language for CPOs engaging in virtual currency derivatives (i.e., futures, options and cleared swaps) transactions in a pool or exempt pool. However, the Document must address the number of unique features of virtual currency derivatives which may include:

- Virtual currency derivatives may experience significant price volatility and the initial margin for virtual currency derivatives may be set as a percentage of the value of a particular contract, which means that margin requirements for long positions can increase if the price of the contract rises;
- Some FCMs may pose restrictions on customer trading activity in virtual currency derivatives, such as requiring additional margin, imposing position limits, prohibiting naked shorting or prohibiting give-in transactions; and
- The rules of certain designated contract markets impose trading halts that may restrict a market participant's ability to exit a position during a period of high volatility

The risks associated with the unique features of engaging in virtual currency derivatives should be disclosed and the impact these risks may have on the pool's performance should be explained.

#### **Virtual Currency Disclosure Requirements for Pools that engage in Underlying or Spot Virtual Currency Transactions**

NFA does not prescribe standardized disclosure language for CPOs engaging in underlying or spot virtual currency transactions. However, the Document must address any of the following areas that are applicable to the pool's investments in underlying or spot virtual currency transactions:

- Unique Features of Virtual Currencies
- Price Volatility
- Valuation and Liquidity
- Cybersecurity
- Opaque Spot Market
- Virtual Currency Exchanges, Intermediaries and Custodians

- Regulatory Landscape
- Technology
- Transaction Fees

In addition, the Document must prominently display the following language:

**[NAME OF NFA MEMBER] IS A MEMBER OF NFA AND IS SUBJECT TO NFA'S REGULATORY OVERSIGHT AND EXAMINATIONS. [NAME OF NFA MEMBER] HAS ENGAGED OR MAY ENGAGE IN UNDERLYING OR SPOT VIRTUAL CURRENCY TRANSACTIONS IN A COMMODITY POOL. ALTHOUGH NFA HAS JURISDICTION OVER [NAME OF NFA MEMBER] AND ITS COMMODITY POOL, YOU SHOULD BE AWARE THAT NFA DOES NOT HAVE REGULATORY OVERSIGHT AUTHORITY FOR UNDERLYING OR SPOT MARKET VIRTUAL CURRENCY PRODUCTS OR TRANSACTIONS OR VIRTUAL CURRENCY EXCHANGES, CUSTODIANS OR MARKETS. YOU SHOULD ALSO BE AWARE THAT GIVEN CERTAIN MATERIAL CHARACTERISTICS OF THESE PRODUCTS, INCLUDING LACK OF A CENTRALIZED PRICING SOURCE AND THE OPAQUE NATURE OF THE VIRTUAL CURRENCY MARKET, THERE CURRENTLY IS NO SOUND OR ACCEPTABLE PRACTICE FOR NFA TO ADEQUATELY VERIFY THE OWNERSHIP AND CONTROL OF A VIRTUAL CURRENCY OR THE VALUATION ATTRIBUTED TO A VIRTUAL CURRENCY BY [NAME OF NFA MEMBER].**

#### **Any Other Activities in Underlying or Spot Virtual Currencies**

NFA Compliance Rule 2-22 prohibits a Member from, among other things, stating or implying that it has been sponsored, recommended or approved by NFA. To provide clear disclosure about the lack of NFA's regulatory oversight, any CPO engaging, in any manner, in activities with customers or counterparties involving underlying or spot virtual currencies other than those described above (e.g., initial coin offerings) must provide its customer or counterparty with the following disclosure language at or before the time the CPO engages in any underlying spot or virtual currency activities with the customer or counterparty:

**[NAME OF NFA MEMBER] IS A MEMBER OF NFA AND IS SUBJECT TO NFA'S REGULATORY OVERSIGHT AND EXAMINATIONS. HOWEVER, YOU SHOULD BE AWARE THAT NFA DOES NOT HAVE REGULATORY OVERSIGHT AUTHORITY OVER UNDERLYING OR SPOT VIRTUAL CURRENCY PRODUCTS OR TRANSACTIONS OR VIRTUAL CURRENCY EXCHANGES, CUSTODIANS OR MARKETS.**

#### **Additional NFA References:**

- [NFA Interpretive Notice 9073](#): Disclosure Requirements for NFA Members Engaging in Virtual Currency Activities (October 2018)

## Fees and Expenses

The Document must include a complete description of each fee, commission and other expense, which was incurred by the pool for its preceding fiscal year, and those expected to be incurred by the pool for its current fiscal year. This should include fees or other expenses incurred in connection with the pool's participation in investee pools and funds. The description must include, without limitation:

- Management fees;
- Brokerage fees and commissions, including interest income paid to FCMs and/or RFEDs, and any fees incurred to maintain an open position in retail forex transactions;
- Fees and commissions paid in connection with trading advice provided to the pool;
- Fees and expenses incurred within investments in investee pools, investee funds and other collective investment vehicles, which fees and expenses must be disclosed separately for each investment tier;
- Incentive fees;
- Any allocation to the CPO, or any agreement or understanding that provides the CPO with the right to receive a distribution, where such allocation or distribution is greater than a pro rata share of the pool's profits based on the percentage of capital contributions made by the CPO;
- Commissions or other benefits, including trailing commissions paid or that may be paid or accrue, directly or indirectly, to any person in connection with the solicitation of participations in the pool;
- Professional and general administrative fees and expenses, including legal and accounting fees and office supplies expenses;
- Organizational and offering expenses;
- Clearance fees and fees paid to national exchanges and self-regulatory organizations;
- For principal-protected pools, any direct or indirect costs to the pool associated with providing the protection feature;
- Any costs or fees included in the spread between bid and asked prices for retail forex transactions or, if known, swap transactions; and
- Any other direct or indirect cost.

In addition:

- Where any fee, commission or other expense is determined by reference to a base amount including, but not limited to, "net assets," "allocation of assets," "gross profits," "net profits" or "net gains," the Document must explain how such base amount will be calculated.
- Where any fee, commission or other expense is based on an increase in the value of the pool, the Document must specify how that increase is calculated, the period of time during which the increase is calculated, the fee, commission or other expense to be charged at



the end of that period and the value of the pool at which payment of the fee, commission or other expense commences.

- Where any fee, commission or other expense of the pool has been paid or is to be paid by a person other than the pool, the Document must disclose the nature and the amount of the fee, commission or other expense and the person who paid or is expected to pay the fee, commission, or other expense.

### Break-Even Analysis

In order to ensure participants are aware of the impact fees and expenses have on the potential profitability of their investments, CPOs are required to disclose in a tabular presentation a calculation of the pool's break-even point or the amount of trading income required for the pool's net asset value (NAV) per unit at the end of one year to equal the selling price per unit. The break-even point must be expressed as a dollar amount and a percentage of the minimum unit of initial investment.

The break-even analysis must include the pool fees and expenses required to be described in the Document. If the pool incurs fees and expenses in connection with the pool's participation in other investments (e.g., equities, mutual funds, REITs, private equity funds) such fees or expenses must be clearly shown, considered part of the total cost and reflected in the break-even analysis. All management, brokerage and other fees must reflect actual experience or contractual charges, if known. If not known, they must be based on good faith estimates.

The break-even analysis must be based on the minimum initial investment amount for a participant and the minimum total subscription amount required for the pool to commence trading. Additionally, if the CPO anticipates a higher amount of total funds raised that will affect the fees and expenses per participant, then the CPO may also provide a break-even analysis using the higher amount of anticipated total funds raised.

### ***Interest Income***

If pool participants receive some or all of the interest income generated by the pool, the expected interest income may be deducted from the expenses which must be covered by trading profits to return the participant to the level of his initial investment.

For purposes of the break-even analysis, CPOs may only offset expenses with interest income generated through the pool's investment in high credit quality short-duration instruments or deposits associated with the pool's buy-and-hold cash management strategies. For purposes of the break-even analysis, short-duration generally means instruments with a term of one year or less. Examples of such instruments or investments include, but are not limited to, Treasury Bills, cash on deposit at a bank or in a money market account, funds on deposit with brokerage firms and interest in a money market mutual fund. The estimate of this interest income must include the assumed interest rate, and that rate must reflect current cash market information. If any interest income is to be paid to the pool operator, or to anyone other than the pool participants, that fact and an estimate of the amount must also be clearly disclosed.

### ***Redemption Fees***

If a redemption fee is charged on the redemption of the initial investment at the end of the first year of investment, it must be clearly shown, considered a part of the total cost, and reflected in the break-even analysis. Any other redemption fee(s) (e.g., early withdrawal fees) must be disclosed in the explanatory notes to the break-even analysis.

### ***Incentive Fees or Performance Allocations***

If the pool and its participants may be subject to an incentive fee or performance allocation, the incentive fee must be clearly shown, considered a part of the total cost, and reflected in the break-even analysis. Incentive fees must be stated as a percentage of profits, and the method by which profits are calculated must be described in the explanatory notes to the break-even analysis.

Often the dollar amount of the incentive fee or performance allocation is reflected as zero because the fee will **not** be charged until the participant recovers their initial investment. However, in some situations, the CPO must calculate the additional trading profit necessary to overcome any incentive fees that would be incurred by a participant prior to the participant recovering the amount of their initial investment. This situation will arise whenever the pool expects to incur expenses which would **not** be deducted from the net performance that is the basis of the incentive fee calculation. This often arises when a CTA is trading a pool and the pool incurs expenses that are not deducted from the CTA's net performance in calculating the CTA's incentive fee.

In order to calculate the additional trading profit necessary to overcome an incentive fee, you must first sum all of the pool fees, expenses and interest income that will be excluded from the computation of the incentive fee and then divide that amount by  $(1 - \text{incentive fee rate})$ . The incentive fee dollar amount that must be shown in the break-even analysis is computed by multiplying this amount by the incentive fee rate. For example, if the incentive fee is 25%, the denominator would be  $(1 - .25)$ , which is then multiplied by the incentive fee rate of 25%.

In the example that follows, the pool would be subject to the Trading Advisor's incentive fees that total 15% of Trading Profits exclusive of interest income. In order to determine the Trading Advisor's incentive fee dollar amount for purposes of the break-even analysis, you should add all the costs and interest income that will **not** be taken into consideration when computing the incentive fee in question (i.e.,  $\$1,500 + \$200 + \$985 + \$1,034 - \$1,231 = \$2,488$ ) and divide that over the denominator of  $1 - .15$  or  $.85$  (i.e.,  $\$2,488 / .85$  or  $\$2,927$ ) and then multiply that amount by the incentive fee rate of  $.15$  (i.e.,  $\$2,927 * .15$  or  $\$439$ ).

### **Sample Break-Even Analysis**

As discussed above, the break-even presentation should be based on the minimum initial investment amount and the minimum total subscription amount required for the pool to commence trading. A sample break-even presentation is shown below:

Minimum Initial Investment (1)	<u>\$100,000</u>
Upfront Syndication and Selling Expense (2)	1,500
Initial Organizational Expenses (3)	200
General Partner's Management Fee (4)	985
Fund Operating Expenses (5)	1,034
Trading Advisor's Management Fees (6)	1,773
Trading Advisor's Incentive Fees on Trading Profits (7)	439
The General Partner's Performance Allocation (8)	0
Brokerage Commissions and Trading Fees (9)	1,724
Less Interest Income (10)	<u>(1,231)</u>
Amount of Trading Profits Required for a Participant's Capital Account (Redemption Value) at the End of One Year to Equal Its Initial Investment	<u>\$6,424</u>
Percentage of Minimum Initial Investment	<u>6.42%</u>

#### **Explanatory Notes:**

- (1) Investors will initially make an investment of \$100,000. The break-even presentation is based on the \$100,000 minimum initial investment and the minimum total subscriptions of \$5,000,000 for the Fund to commence trading.
- (2) A 1.5% upfront syndication and selling charge will be deducted from each subscription to reimburse the Fund, the General Partner and/or the Clearing Broker for the syndication and selling expenses incurred on behalf of the Fund.
- (3) The initial organizational costs for the Fund are \$10,000. Therefore, each participant's allocation of those costs based on a minimum initial investment of \$100,000 and minimum total subscriptions of \$5,000,000 will be \$200.
- (4) Fund's General Partner will be paid a monthly management fee of 1/12 of 1% of Net Asset Value.
- (5) The Fund's actual accounting, auditing, legal and other operating expenses will be borne by the Fund. These expenses are expected to amount to approximately 1.05% of the Fund's Net Asset Value.

- (6) The Fund's Trading Advisor will be paid a monthly management fee of 1/12 of 2% of Allocated Net Assets, which is anticipated to be 90% of the Net Asset Value.
- (7) The Trading Advisor will receive an incentive fee of 15% of Trading Profits exclusive of interest income. The \$439 of incentive fees shown above is equal to 15% of the net of total trading income of \$6,424, minus \$1,724 of brokerage commissions and trading fees and \$1,773 of Trading Advisor management fees.
- (8) In the above example, no performance allocation for the General Partner is included in the calculation. The General Partner charges a 20% quarterly performance allocation based upon New Net High Profits. New Net High Profits is net of all other fees and expenses and, as such, the General Partner does not receive a performance allocation until the Fund generates trading income sufficient to offset such expenses. Based on the above analysis, the General Partner would need to earn more than \$6,424 of gross trading income per unit before it would be entitled to an incentive fee.
- (9) Brokerage commissions (including any spread on forex transactions) and trading fees are estimated at 1.75% of Net Asset Value.
- (10) The Fund will earn interest on margin deposits with its Clearing Broker. Based on a current assumed interest rate of 2%, interest income is estimated at 1.25% of Net Asset Value.

**Additional NFA References:**

- [NFA Interpretive Notice 9023](#): Compliance Rule – 2-13: Break-Even Analysis

**Trading for its own Account**

If the CPO, the pool's trading manager, any of the pool's CTAs or any principals of the foregoing trades or intends to trade commodity interests for its own account, the Document must disclose whether participants will be permitted to inspect the records of such trades and any written policies related to such trading.

**Related Party Transactions**

The Document must contain a full description, including a discussion of the costs to the pool, of any material transactions or arrangements for which there is no publicly disseminated price between the pool and any person affiliated with a person providing services to the pool.

**Conflicts of Interest**

The Document must include a full description of any actual or potential conflicts of interest regarding any aspect of the pool on the part of:

- The CPO;
- The pool's trading manager, if any;

- Any major CTA;
- The CPO of any major investee pool;
- Any principal of the above; and
- Any other person providing services to the pool or soliciting participants for the pool, or acting as a counterparty to the pool's retail forex or swap transactions or acting as a swap dealer with respect to the pool.

The Document must also include any other material conflict involving the pool.

This includes a discussion of the conflicts of interest arising from typical incentive fee arrangements and from the trading of proprietary accounts. If the pool is subject to a fee that is based on a percentage of profits, then the Document must disclose that this fee may encourage a CPO/CTA charging the fee to take excessive risks to earn an outsized incentive fee and that such risk-taking may place the interests of the CPO/CTA, as applicable, in conflict with the interests of the pool. If the CPO and/or CTA or any of its principals trades or intends to trade commodity interests for its own account, then the Document must include a discussion of the specific conflicts of interest that arise from the trading of proprietary accounts. Specifically, the discussion should disclose that there is an incentive to give preferential treatment to proprietary accounts and to trade proprietary accounts ahead of or against client accounts.

Included in the description of such conflicts must be any arrangement whereby a person may benefit, directly or indirectly, from the maintenance of the pool's account with an FCM and/or RFED, from the maintenance of the pool's swap positions with a swap dealer, or from the introduction of such account to an FCM, RFED, and/or swap dealer by an IB (such as payment for order flow or soft dollar arrangements) or from an investment of pool assets in investee pools or funds or other investments. Some common conflicts include:

1. If the CPO or major CTA (or principal thereof) receives per-trade compensation, the Document must disclose that there is an incentive to overtrade the account to increase its compensation. This statement is required even if the CPO, the major CTA or a principal receives commission rebates in his capacity as an IB or AP.
2. If the CPO or major CTA (or principal thereof) is an AP of the FCM/RFED that the pool uses, the Document must disclose that there is an incentive to trade the account actively to increase the compensation that his employer will receive.
3. If the CPO or major CTA (or a principal thereof) receives office space or other soft dollar benefits from an FCM, RFED, or IB (e.g. charts, analysis software, etc.), the Document must disclose that this arrangement may dispose them to trade more actively.

**Additional NFA References:**

- [NFA Notice to Members: I-07-25](#): Disclosure of Conflicts of Interest by CPOs and CTAs
- [NFA Notice to Members: I-11-01](#): NFA provides guidance for disclosure of conflicts of interests arising from Typical Incentive Fee Arrangements by commodity pool operators and commodity trading advisors

## Litigation

The Document must disclose any material administrative, civil or criminal action, whether pending or concluded, within five years preceding the date of the Document, against the following persons (a concluded action that resulted in adjudication on the merits in favor of such person need not be disclosed):

- The CPO, the pool's trading manager, the pool's major CTAs, and the operators of the pool's major investee pools;
- Any principal of the foregoing; and
- The pool's FCMs, RFEDs, swap dealers, and IBs, if any.

With respect to an FCM, RFED, and/or swap dealer, or an IB, an action is material if:

- The action would be required to be disclosed in the notes to the FCM's, RFED's, swap dealer's or IB's financial statements prepared pursuant to generally accepted accounting principles;
- The action was brought by the CFTC (unless the action was concluded, did not result in civil monetary penalties exceeding \$50,000, and did not involve allegations of fraud or other willful misconduct); or
- The action was brought by any other federal or state regulatory agency, a non-United States regulatory agency or a self-regulatory organization and involved allegations of fraud or other willful misconduct.

Where a matter is material, its description must include a recital of the nature of the action, the parties involved, the allegations or findings, the status of the action and the size of any fine or settlement.

## Principal-Protected Pools

Principal-protected pools or "guaranteed pools" are those which are designed to limit the loss of the initial investment of participants. If the pool is a principal-protected pool, this must be stated in the forepart of the Document. In addition, the Document must describe the nature of the principal protection feature, the manner by which such protection will be achieved, including sources of funding, and what conditions must be satisfied for participants to receive the benefits of such protection. The Document must also specify when the protection feature becomes operative and disclose, in the break-even analysis, the costs of purchasing and carrying the assets to fund the principal protection feature or other limitations on risk, expressed as a percentage of the price of a unit of participation.

## Transferability and Redemption

The Document must include a complete description of any restrictions upon the transferability of a participant's interest in the pool and a complete description of the frequency, timing and manner in which a participant may redeem interests in the pool. The description must specify the following:

- How the redemption value of a participant's interest will be calculated;
- The conditions under which a participant may redeem its interest, including the cost associated therewith;
- The terms of any notification required and the time between the request for redemption and payment;
- Any restrictions on the redemption of a participant's interest, including any restrictions associated with the pool's investments; and
- Any liquidity risk relative to the pool's redemption capabilities.

### Liability of Pool Participants

The Document must disclose the extent to which a participant may be held liable for obligations of the pool in excess of the funds contributed by the participant for the purchase of an interest in the pool.

### Distribution of Profits and Taxation

The Document must disclose the pool's policies with respect to payment of distributions from profits or capital and the frequency of such payments. The Document must also disclose the federal income tax effects of such payments for a participant, including a discussion of the federal income tax laws applicable to the form of organization of the pool and to payments from the pool. If the pool is specifically structured to accomplish certain federal income tax objectives, the CPO must explain those objectives, the manner in which they will be achieved and any related risks.

### Reporting

The Document must state that the CPO is required to provide all participants with either monthly or quarterly statements of account (whichever applies) as well as a certified annual report. Account statements must be distributed at least monthly in the case of pools with net assets of more than \$500,000 at the beginning of the pool's fiscal year, otherwise at least quarterly.

### Required Performance Disclosures

All performance information presented in the Document must be current as of a date not more than three months preceding the date of the Document. All required performance information must be presented for the most recent five calendar years and the current year-to-date or for the life of the pool, account, or trading program, if less than this period.

Each page that includes past performance presentation must include the following statement, prominently displayed: **PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS.**

**If the offered pool has traded commodity interest for at least three years** and at least 75% of the contributions to the pool were made by people unaffiliated with the pool's CPO, CTA, trading

manager, or their principals for at least such three-year period, then the performance of the offered pool is all that is required to be disclosed in the Document.

**If the offered pool has less than a three-year operating history** the Document must include the following:

- The performance of the offered pool. If the offered pool has no operating history, the Document must include the following statement prominently displayed: **THIS POOL HAS NOT COMMENCED TRADING AND DOES NOT HAVE ANY PERFORMANCE HISTORY.**
- The performance of each other pool operated (in the format outlined for [Performance Presentation for Pools](#) on page 25) and account traded (in the format outlined for [Performance Presentation for Accounts](#) on page 26) by the CPO (and by the trading manager if the offered pool has a trading manager).
  - If the CPO or the trading manager has not operated any commodity pool for at least three years, the Document must disclose the performance of each other pool operated and account traded by the trading principals of the CPO (and the trading manager, if applicable).
    - In addition, if the CPO (and the trading manager, if applicable) has not operated for at least three years any commodity pool in which 75% or more of the contributions to the pool were made by persons unaffiliated with the CPO, the trading manager, the pool's CTAs or their respective principals, the CPO must also disclose the performance of each other pool operated by and account traded by the trading principals of the CPO (and of the trading manager, as applicable) unless such performance does not differ in any material respect from the performance of the offered pool and the CPO (and trading manager, if any) disclosed in the Document.
  - If neither the CPO or trading manager (if any), nor any of the principals thereof has operated any other pools or traded any other accounts, the Document must include the following statement prominently displayed: **NEITHER THIS POOL OPERATOR (TRADING MANAGER, IF APPLICABLE) NOR ANY OF ITS TRADING PRINCIPALS HAS PREVIOUSLY OPERATED ANY OTHER POOLS OR TRADED ANY OTHER ACCOUNTS.** If the CPO or trading manager is a sole proprietorship, reference to its trading principals may be deleted from the above statement.
- The performance of any accounts (including pools) directed by each major CTA in the format outlined for [Performance Presentation for Accounts](#) on page 26. If a major CTA has not previously traded accounts, the Document must include the following statement prominently displayed: **(name of the major commodity trading advisor), A COMMODITY TRADING ADVISOR THAT HAS DISCRETIONARY TRADING AUTHORITY OVER (percentage of the pool's funds available for commodity interest**



**trading allocated to that trading advisor) PERCENT OF THE POOL'S COMMODITY INTEREST TRADING HAS NOT PREVIOUSLY DIRECTED ANY ACCOUNTS.**

- The performance of any major investee pool. If the major investee pool has not commenced trading, the Document must include the following statement prominently displayed: **(name of the major investee pool), AN INVESTEE POOL THAT IS ALLOCATED (percentage of the pool assets allocated to that investee pool) PERCENT OF THE POOL'S ASSETS HAS NOT COMMENCED TRADING.**
- The Document must provide a summary description of the performance history of all other CTAs and investee pools not required above, including:
  - Monthly return parameters (highs and lows),
  - Historical volatility and degree of leverage, and
  - Any material differences between the performance of such advisors and pools as compared to that of the offered pool's major trading advisors and major investee pools.
  - **Note:** If the Document has a SAI, the summary description of the pool's non-major CTAs and investee pools may be provided in the SAI.

***Performance Presentation for Pools***

The performance disclosure for pools must include the following information and must be net of any fees, expenses or special allocations:

- The name of the pool;
- A statement as to whether the pool is privately offered, a multi-advisor pool, or a principal protected pool;
- The date (month, day, and year) of inception of trading;
- The aggregate gross capital subscriptions to the pool;
- The pool's current net asset value;
- The largest monthly draw-down during the most recent five calendar years and year-to-date, expressed as a percentage of the pool's net asset value and the month and year of the draw-down;
- The worst peak-to-valley draw-down during the most recent five calendar years and year-to-date, expressed as a percentage of the pool's net asset value, as well as the period the draw-down occurred. The period begins with the peak month and year and ends with the valley month and year;
- The annual and year-to-date rate of return for the pool's most recent five calendar years and year-to-date, computed on a compounded monthly basis; and
- A definition of the term draw-down must be included in the capsule that is consistent with [CFTC Regulation 4.10\(k\)](#).

### ***Performance Presentation for Accounts***

The performance disclosure for accounts must include the following information and must be net of any fees and expenses:

- The name of the CTA or other person trading the account;
- The name of the trading program;
- The date (month, day, and year) on which the CTA or other person trading the account began trading client accounts;
- The date (month, day, and year) when client funds began being traded pursuant to the trading program;
- The number of accounts directed by the CTA or other person trading the account pursuant to the trading program, as of the date of the Document;
- The total assets under the management of the CTA or other person trading the account, as of the date of the Document;
- The total assets traded pursuant to the trading program specified, as of the date of the Document;
- The largest monthly draw-down experienced by the trading program during the most recent five calendar years and year-to-date expressed as a percentage, as well as the month and year of the draw-down;
- The worst peak-to-valley draw-down experienced by the trading program during the most recent five calendar years and year-to-date, as well as the period the draw-down occurred;
  - The period begins with the peak month and year and ends with the valley month and year.
- The annual and year-to-date rate of return for the trading program for the most recent five calendar years and year-to-date, computed on a compounded monthly basis;
- A definition of the term draw-down must be included in the capsule that is consistent with [CFTC Regulation 4.10\(k\)](#) and;
- If the trading program will be used by the offered pool, then this must be prominently disclosed.

Unless the presentation would be misleading, the past performance of accounts required to be presented may be presented in composite form on a program-by-program basis. However, accounts that differ materially with respect to rates of return cannot be presented in the same composite. If there are other material differences amongst accounts in the same program composite, they must be disclosed.

### ***Performance of the Offered Pool***

The performance of the offered pool must be identified as such and presented first. The performance of the offered pool must also include monthly rates of return for the five most recent calendar years and year-to-date, either in a numerical table or in a bar graph.

**Note:** This applies even if the offered pool meets the definition of proprietary performance [below](#).

### ***Performance of Other Pools***

Performance data for pools of the same class as the offered pool for which performance is required to be presented must appear after the performance of the offered pool and be presented on a pool-by-pool basis.

**Note:** For purpose of this *Performance of Other Pools* discussion, these would be considered pools of different classes: (1) privately offered pools and public offerings; (2) principal-protected pools and non-principal-protected pools; and (3) multi-advisor pools and non-multi-advisor pools.

For example, if the offered pool is privately offered, the performance of all other privately offered pools for which performance is required to be presented must be presented on a pool-by-pool basis. Performance data for pools of a different class than the offered pool must be presented less prominently, and, unless such presentation would be misleading, may be presented in composite form. Only pools of the same class may be included in a composite and they may not differ materially with respect to rate of return. Furthermore, if pool performance is presented in a composite, the Document must disclose how the composite was developed and the material differences among the pools included in the same composites including differences in leverage and the different trading programs used by the pools. Monthly rates of return need not be presented for any pool or account other than the offered pool. Rather, only annual and year-to-date rates of return for the pools for the most recent five calendar years and year-to-date are required to be presented.

### ***Computing Aggregate Gross Capital Subscriptions***

The aggregate gross capital subscriptions is the total amount of all additions to the pool over its entire operating history. This should be a gross figure and not reduced by the withdrawals from the pool.

### ***Computing Rate of Return (ROR)***

All performance information presented in the Document, including performance information contained in any capsule and performance information not specifically required by CFTC rules, must be supported by the following amounts, calculated on an accrual basis of accounting in accordance with generally accepted accounting principles, as specified below or by a method otherwise approved by the CFTC:

- The beginning net asset value for the period, which shall be the same as the previous period's ending net asset value;
- All additions, whether voluntary or involuntary, during the period;
- All withdrawals and redemptions, whether voluntary or involuntary, during the period;
- The net performance for the period, which shall represent the change in the net asset value net of additions, withdrawals, and redemptions;
- The ending net asset value for the period, which shall represent the beginning net asset value plus or minus additions, withdrawals, redemptions and net performance;

- The rate of return for the period, which shall be calculated by dividing the net performance by the beginning net asset value or by a method otherwise approved by the CFTC; and
- The number of units outstanding at the end of the period, if applicable.

**Note:** For instructions on computing RORs for accounts, consult the Computing Rate of Return (ROR) section of the [Disclosure Documents: A Guide for CTAs](#) on NFA's website.

### **Annual and Year-to-Date Rates of Return**

Annual RORs should be calculated on a compounded monthly basis. This can be done using the Value Added Monthly Index (VAMI) method.

The VAMI method generally assumes an initial investment of \$1,000 and shows how such an investment would have fared over a certain period of time. In order to calculate annual ROR using VAMI, you must first calculate the value of the \$1,000 investment at the end of each subperiod or month based upon the monthly RORs computed in accordance with one of the above mentioned methods. The calculation would be as follows:

***In the first month of the period:***

$$\text{VAMI for month} = (1 + \text{ROR for month}) \times 1000$$

***For all subsequent months:***

$$\text{VAMI for month} = (1 + \text{ROR for month}) \times \text{VAMI for prior month}$$

***Annual ROR would then be calculated as follows:***

$$\text{Annual ROR} = (\text{year-end VAMI} - \$1,000) \text{ divided by } \$1,000.$$

When calculating the annual RORs for subsequent years, the value of the initial investment should be the prior year-end VAMI.

### **Computing Monthly and Peak-to-Valley Draw-Downs**

Draw-down means losses experienced by a pool or trading program over a specified period.

Worst monthly draw-down is simply the pool's or trading program's worst monthly percentage ROR.

Worst peak-to-valley draw-down is the greatest cumulative percentage decline in month-end net asset value (NAV) due to losses sustained by the accounts during any period in which the initial month-end NAV is not equaled or exceeded by a subsequent month-end NAV. In order to calculate this amount, the firm should calculate a continuous VAMI for the time period presented. Using this method the firm should determine the first month in which the VAMI is not followed by a VAMI that is greater than or equal to that month's VAMI. This would be the first peak. The next peak would be the next month in which the VAMI is greater than the previous peak's VAMI and is followed by a lower VAMI. Once all the peaks have been identified, determine all the months that have the lowest VAMIs during a period between two peaks. These would be the valleys. Then determine the percentage change between each peak and valley using the following calculation:

(Valley VAMI – Peak VAMI) divided by Peak VAMI

The worst peak-to-valley draw-down will be the largest percentage change from a peak to a valley. The peak month and the valley month should be reported in the capsule.

**Note:** A peak-to-valley draw-down that began prior to the beginning of the most recent five calendar years is deemed to have occurred during such five calendar year period.

**Sample Performance Capsule for Pools**

Below is a sample performance capsule for pools:

Name of Pool:	Sample Pool					
Type of Pool:	Privately offered					
Inception of Trading:	January 1, 2011					
Aggregate Subscriptions:	\$1,673,000					
Current Net Asset Value:	\$1,925,495					
Largest monthly draw-down:	-16.87% / December 2015					
Worst peak-to-valley draw-down:	-36.95% / July 2013 – April 2016					
<b>PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS</b>						
	<b>Rate of Return</b>					
<b>Month</b>	<b>2019</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>January</b>	3.08%	-2.43%	1.54%	-0.67%	-4.45%	0.69%
<b>February</b>	-0.36%	3.11%	-0.89%	-3.98%	0.71%	-0.82%
<b>March</b>	-1.54%	-0.23%	1.15%	1.82%	-0.64%	0.55%
<b>April</b>	-0.19%	1.16%	0.97%	-10.58%	1.03%	-12.06%
<b>May</b>	-3.60%	1.54%	-1.21%	3.82%	12.30%	0.90%
<b>June</b>	-6.72%	0.32%	5.82%	-0.23%	-2.51%	-4.12%
<b>July</b>	4.79%	-1.28%	0.11%	1.16%	0.32%	1.01%
<b>August</b>	2.86%	1.12%	-0.14%	1.54%	0.75%	-9.93%
<b>September</b>	-1.73%	-2.09%	-0.56%	0.33%	1.25%	3.99%
<b>October</b>	0.61%	1.34%	-0.23%	5.61%	-4.65%	1.01%
<b>November</b>	-0.28%	1.57%	1.11%	1.22%	2.12%	16.82%
<b>December</b>		1.04%	0.32%	-1.87%	-16.87%	1.14%
<b>Year</b>	-3.55%	5.14%	8.09%	-2.76%	-12.40%	-3.54%
<b>Draw-down:</b> Losses experienced by the pool over a specified period.						

(A bar chart may be substituted for the numerical table. The bar chart, if used, must show percentage rate or return on the vertical axis and one-month increments on the horizontal axis. It must be scaled in such a way as to clearly show month-to-month differences in rate of return and must separately display numerical percentage annual rates of return for the period covered by the bar graph.)

## Sample Performance Capsule for Accounts

Below is a sample performance capsule for managed accounts or trading programs:

Name of CTA (or person trading the account):	Sample CTA
Name of Trading Program:	Offered Trading Program
Inception of Trading by CTA (or person trading the account):	January 1, 2011
Inception of Trading in Offered Program:	February 1, 2012
# of accounts currently traded pursuant to the program:	145
Total nominal assets under management:	\$30,673,000
Total nominal assets traded pursuant to the program:	\$21,746,000
Largest monthly draw-down:	-16.87% / December 2015
Worst peak-to-valley draw-down:	-31.60% / May 2015 – April 2016
Number of profitable accounts that have opened and closed:	35
Range of returns experienced by profitable accounts:	1.12% – 20.33%
Number of losing accounts that have opened and closed:	23
Range of returns experienced by unprofitable accounts:	-0.43% – -24.57%

### PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS

Month	Rate of Return					
	2019	2018	2017	2016	2015	2014
January	3.08%	2.43%	1.54%	-0.67%	-4.45%	0.69%
February	-0.36%	3.11%	-0.89%	-3.98%	0.71%	-0.82%
March	-1.54%	-0.23%	1.15%	1.82%	-0.64%	0.55%
April	-0.19%	1.16%	0.97%	-10.58%	1.03%	1.06%
May	3.60%	1.54%	1.21%	3.82%	6.05%	0.90%
June	-6.72%	0.32%	0.51%	-0.23%	-2.51%	1.12%
July	4.79%	1.28%	0.11%	1.16%	0.32%	1.01%
August	-3.20%	1.12%	-0.14%	1.54%	0.75%	0.93%
September	-1.28%	2.09%	0.56%	0.33%	-1.25%	0.99%
October	3.67%	1.34%	0.23%	5.61%	-4.65%	1.01%
November	-2.91%	1.57%	1.11%	1.22%	2.12%	1.19%
December		1.04%	0.32%	-1.87%	-16.87%	1.14%
Year	-1.69%	18.07%	6.86%	-2.76%	-19.31%	10.20%

**Draw-down:** Losses experienced by the trading program over a specified period.

(A bar chart may be substituted for the numerical table. The bar chart, if used, must show percentage rate or return on the vertical axis and one-month increments on the horizontal axis. It must be scaled in such a way as to clearly show month-to-month differences in rate of return and must separately display numerical percentage annual rates of return for the period covered by the bar graph.)

## Material Information

A CPO is obligated to disclose all material information to existing or prospective pool participants even if not specifically required by CFTC or NFA rules.

## Supplemental Information

If any information other than that required by CFTC rules, the antifraud provisions of the Act, other federal or state laws or regulations, rules of a self-regulatory agency or laws of a non-United States jurisdiction, is provided, such information:

- Must be included in the SAI;
- May not be misleading in content or presentation or inconsistent with required disclosures;
- Is subject to the antifraud provisions of the Act, CFTC rules and NFA rules regarding the use of promotional material;
- May include supplemental non-performance information relating to a required disclosure with the related required disclosure provided that it is included after the related required disclosures;
- May include any other supplemental non-performance information as long as this information is presented after all required disclosures.

## ***Proprietary Trading Results***

Proprietary trading results are the performance of any pool or account in which 50% or more of the beneficial interest is owned or controlled by: (1) the CPO, Trading Manager (if any), CTA or any principal thereof, (2) an affiliate or family member of the CPO, trading manager (if any), or CTA, or (3) any person providing services to the pool.

Proprietary trading results may not be included in a Document unless it is ***clearly labeled*** as "Proprietary" and set forth separately after all required and non-required disclosures, together with a discussion of any differences between such performance and the performance of the offered pool, including, but not limited to, differences in costs, leverage and trading methodology.

Pro-forma adjustments must be made for fees and commissions and prepared on a conservative basis. Notes to the table should include complete information on the adjustments made and the performance must be ***clearly labeled*** as "Pro-Forma".

## ***Hypothetical Results***

Hypothetical performance results are any performance results derived with the benefit of hindsight. NFA generally discourages the use of hypothetical performance results. However, NFA also recognizes that in certain circumstances the presentation of these results may have some limited utility. Hypothetical or simulated results may not be shown for any pool for which the CPO has three months of actual trading results trading. In situations where a CPO elects to present hypothetical performance results for a pool which has less than three months of actual



performance, the CPO must adhere to the following requirements in order to prevent the over-emphasis of the hypothetical performance results:

- Hypothetical trading results must be **clearly labeled** as "Hypothetical".
- The hypothetical trading results must appear in the SAI (see [General Disclosure Document Guidelines for Commodity Pools](#) on page 5 for details on preparing an SAI and should appear after any supplemental client or proprietary performance).
- If the CPO has less than one year of experience in directing customer accounts, past performance results must be shown for any proprietary trading over the last five years or over the entire performance history if less than five years.
- Any hypothetical results must include a description of all material assumptions that were made in preparing the hypothetical results. At a minimum, this description must cover points such as the initial investment amount, reinvestment or distribution of profits, commission charges, management and incentive fees, and a general discussion of how performance was calculated (e.g., based on settlement prices, real time pricing, the method used to select and allocate assets among particular trading advisors, as applicable). Any disclosure which is necessary to place the hypothetical results in their proper context must be made. This may go well beyond the prescribed disclaimer.

**Note:** Hypothetical performance must be adjusted for the fees of the pool, including reasonable commission and slippage.]

- The following disclaimer must be prominently displayed. If the person for whom the hypothetical results are being shown has less than 12 months of actual results, then the disclaimer must immediately precede the hypothetical results, otherwise it may be displayed immediately following the results. If several pages of hypothetical results are shown, the disclaimer may need to be included more than once.

**HYPOTHETICAL PERFORMANCE RESULTS HAVE MANY INHERENT LIMITATIONS, SOME OF WHICH ARE DESCRIBED BELOW. NO REPRESENTATION IS BEING MADE THAT ANY ACCOUNT WILL OR IS LIKELY TO ACHIEVE PROFITS OR LOSSES SIMILAR TO THOSE SHOWN. IN FACT, THERE ARE FREQUENTLY SHARP DIFFERENCES BETWEEN HYPOTHETICAL PERFORMANCE RESULTS AND THE ACTUAL RESULTS SUBSEQUENTLY ACHIEVED BY ANY PARTICULAR TRADING PROGRAM.**

**ONE OF THE LIMITATIONS OF HYPOTHETICAL PERFORMANCE RESULTS IS THAT THEY ARE GENERALLY PREPARED WITH THE BENEFIT OF HINDSIGHT. IN ADDITION, HYPOTHETICAL TRADING DOES NOT INVOLVE FINANCIAL RISK, AND NO HYPOTHETICAL TRADING RECORD CAN COMPLETELY ACCOUNT FOR THE IMPACT OF FINANCIAL RISK IN ACTUAL TRADING. FOR EXAMPLE, THE ABILITY TO WITHSTAND LOSSES OR TO ADHERE TO A PARTICULAR TRADING PROGRAM IN SPITE OF TRADING LOSSES ARE MATERIAL POINTS WHICH CAN ALSO ADVERSELY AFFECT ACTUAL TRADING RESULTS. THERE ARE NUMEROUS OTHER FACTORS**

**RELATED TO THE MARKETS IN GENERAL OR TO THE IMPLEMENTATION OF ANY SPECIFIC TRADING PROGRAM WHICH CANNOT BE FULLY ACCOUNTED FOR IN THE PREPARATION OF HYPOTHETICAL PERFORMANCE RESULTS AND ALL OF WHICH CAN ADVERSELY AFFECT ACTUAL TRADING RESULTS.**

- If the CPO for whom the hypothetical results are shown has either less than one year of experience in directing customer accounts or trading proprietary accounts, then the disclaimer must also contain the following statement:

**(THE CPO) HAS HAD LITTLE OR NO EXPERIENCE IN TRADING ACTUAL ACCOUNTS FOR ITSELF OR FOR CUSTOMERS. BECAUSE THERE ARE NO ACTUAL TRADING RESULTS TO COMPARE TO THE HYPOTHETICAL PERFORMANCE RESULTS, CUSTOMERS SHOULD BE PARTICULARLY WARY OF PLACING UNDUE RELIANCE ON THESE HYPOTHETICAL PERFORMANCE RESULTS.**

- If the CPO includes or makes reference to a hypothetical composite performance record showing what a multi-advisor account portfolio or pool could have achieved in the past if assets had been allocated among particular trading advisors, the Document must include the following disclaimer:

**THIS COMPOSITE PERFORMANCE RECORD IS HYPOTHETICAL AND THESE TRADING ADVISORS HAVE NOT TRADED TOGETHER IN THE MANNER SHOWN IN THE COMPOSITE. HYPOTHETICAL PERFORMANCE RESULTS HAVE MANY INHERENT LIMITATIONS, SOME OF WHICH ARE DESCRIBED BELOW. NO REPRESENTATION IS BEING MADE THAT ANY MULTI-ADVISOR MANAGED ACCOUNT OR POOL WILL OR IS LIKELY TO ACHIEVE A COMPOSITE PERFORMANCE RECORD SIMILAR TO THAT SHOWN. IN FACT, THERE ARE FREQUENTLY SHARP DIFFERENCES BETWEEN A HYPOTHETICAL COMPOSITE PERFORMANCE RECORD AND THE ACTUAL RECORD SUBSEQUENTLY ACHIEVED.**

**ONE OF THE LIMITATIONS OF A HYPOTHETICAL COMPOSITE PERFORMANCE RECORD IS THAT DECISIONS RELATING TO THE SELECTION OF TRADING ADVISORS AND THE ALLOCATION OF ASSETS AMONG THOSE TRADING ADVISORS WERE MADE WITH THE BENEFIT OF HINDSIGHT BASED UPON THE HISTORICAL RATES OF RETURN OF THE SELECTED TRADING ADVISORS. THEREFORE, COMPOSITE PERFORMANCE RECORDS INVARIABLY SHOW POSITIVE RATES OF RETURN. ANOTHER INHERENT LIMITATION ON THESE RESULTS IS THAT THE ALLOCATION DECISIONS REFLECTED IN THE PERFORMANCE RECORD WERE NOT MADE UNDER ACTUAL MARKET CONDITIONS AND, THEREFORE, CANNOT COMPLETELY ACCOUNT FOR THE IMPACT OF FINANCIAL RISK IN ACTUAL TRADING. FURTHERMORE, THE COMPOSITE PERFORMANCE RECORD MAY BE DISTORTED BECAUSE THE**

**ALLOCATION OF ASSETS CHANGES FROM TIME TO TIME AND THESE ADJUSTMENTS ARE NOT REFLECTED IN THE COMPOSITE.**

- If the CPO for whom the hypothetical results are shown has less than one year of experience allocating assets among particular trading advisors, then the disclaimer must also contain the following statement:

**(THE CPO) HAS HAD LITTLE OR NO EXPERIENCE ALLOCATING ASSETS AMONG PARTICULAR TRADING ADVISORS. BECAUSE THERE ARE NO ACTUAL ALLOCATIONS TO COMPARE TO THE PERFORMANCE RESULTS FROM THE HYPOTHETICAL ALLOCATION, CUSTOMERS SHOULD BE PARTICULARLY WARY OF PLACING UNDUE RELIANCE ON THESE RESULTS.**

**Additional NFA References:**

- [NFA Interpretive Notice ¶9025](#) – Compliance Rule 2-29: Use of Promotional Material Containing Hypothetical Performance Results
- [NFA Interpretive Notice ¶9043](#) – Compliance Rule 2-29: Use of Past or Projected Performance; Disclosing Conflicts of Interest for Security Futures Products

***Extracted Performance***

Extracted performance is when a CPO chooses only one component of its overall past trading results to highlight to customers. The use of extracted performance results is permitted only when a CPO's previous disclosure document designated the percentage of assets which would be committed toward that particular component of the overall trading program. For example, if the previous disclosure document stated that 25% of a pool's assets would be dedicated to trading financial futures contracts and if 25% of the pool's assets were in fact dedicated to trading financial futures contracts, the CPO would be allowed to present the extracted performance of its financial futures trading based on net asset values equal to 25% of the pool's total net asset value. Extracted results must be ***clearly labeled*** as "Extracted" and the Document must also disclose in an equally prominent fashion the overall actual trading results from which the extracted results were drawn.

**Additional NFA References:**

- [NFA Interpretive Notice ¶9025](#) – Compliance Rule 2-29: Use of Promotional Material Containing Hypothetical Performance Results

## Filing Disclosure Documents and the Review Process

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NFA is responsible for reviewing all Documents, including Documents for CTAs, privately offered commodity pools, and certain public commodity pools (i.e., those that are required to register their securities under the Securities Act of 1933). Prior to using a disclosure document, a CPO must submit the Document to NFA and receive an acceptance letter from NFA confirming that the Document can be used to solicit.

All Documents must be filed through [NFA's Electronic Disclosure Document Filing System](#). NFA will not accept any Documents filed through any other mode (i.e., email, fax, or regular mail). Through this system, firms may track the status of their submissions online, in real-time, and have instantaneous access to NFA's comment and acceptance letters. Additionally, the system archives all correspondence, including filed Documents and NFA's comment or acceptance letters, creating an electronic file cabinet that is easily accessible to the CPO at any time. Firms will receive confirmation of receipt upon filing. Copies of all subsequent amendments or updated Documents must be submitted to NFA using the same procedures.

NFA's goal is to complete its initial review of a Document within 14 days after NFA receives it. Once the review is complete, NFA will inform the CPO that the Document is accepted or deficient. The CPO is required to correct the deficiencies and re-submit the Document to NFA for review before the Document will be accepted. NFA's review is designed to ensure that Documents contain all of the required information and that such information is consistent with information on record with NFA. However, NFA's review process does not attempt to verify the accuracy of the information contained in the Document. The CPO is responsible for ensuring it does not use a Document that it knows to be materially inaccurate or incomplete. During the course of an NFA examination, a CPO's Document may be reviewed again, with the objective of ensuring consistency between the firm's business operations and the information included in the Document. As a result, the receipt of an acceptance letter upon filing a Document with NFA may not prevent NFA or the CFTC from raising issues with regard to the Document in the future.

A staff member will be assigned to review a Document within 24 hours after receipt. Contact NFA's Information Center at (312) 781-1410 or (800) 621-3570 to speak with a member of NFA's Disclosure Document Team concerning Document preparation and other issues relating to CPOs and CTAs.

### Subsequent Filings

A CPO who resubmits a previously reviewed or accepted Document must submit two copies: a "clean" copy and a "marked" copy of the Document that identifies all deletions and additions that have been made to the Document previously filed with NFA. This may be done, for example, by striking through deletions and underlining additions. A "clean" copy is the same Document, except without the deletions and additions highlighted. NFA will refuse to review and accept any subsequent filings that fail to include with it a copy of the Document identifying the additions and deletions.

## Instant Filings

Once a CPO has filed a Document with NFA that has been accepted, subsequent Documents may be eligible for instant filing, which results in an expedited review process. Instant filing is available for:

- Documents that do not contain material changes from a previous filing that NFA has accepted,
- New pool offerings that are substantially similar to Documents of other pools operated by the CPO that NFA has accepted, or
- Pools that will be operated pursuant to an exemption under CFTC Regulation 4.12(b).

To qualify for instant filing relief, the CPO must check the appropriate responses during the filing process by requesting instant filing treatment of the Document and indicating that there are no material changes from a previous filing that NFA has accepted. Furthermore, the CPO must highlight any changes from the previous filing in the body of the Document. NFA usually reviews Documents that qualify for instant filing within three business days. In those cases, NFA relies on the CPO firm's representation of the changes made to the Document and generally limits its review to only those changes the firm identifies.