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Management Alert

New Commodity Pool Rules May Require Immediate Action by 401(k) Plans

New regulations adopted in 2012 by the Commodity Futures Trading Commission ("CFTC") may require 401(k) plans that had previously registered as exempt from CFTC regulation to renew their exemption on an annual basis, with the first renewal being due by March 1. In addition, some plans which have not previously registered may need to do so.

In addition to traditional agricultural commodities, the CFTC regulates financial futures, including the type of futures contracts often used for hedging purposes by stock and bond funds. Under the CFTC rules, any investment fund that invests in futures contracts is potentially classified as a "commodity pool", and any person engaged in the operation of a commodity pool may be considered a "commodity pool operator", required to be registered with and regulated by the CFTC.

A 401(k) investment fund whose advisers use futures as part of their trading strategy (other than solely through investment in a mutual fund) could be considered a "commodity pool" under this definition, which would make the fiduciaries of the 401(k) plan subject to regulation as commodity pool operators. The CFTC regulations provide that the fiduciaries of a retirement plan subject to ERISA are generally exempt from registration as commodity pool operators. However, if the plan provides for employee contributions, such as a 401(k) plan, the plan fiduciaries are required to file a statement with the CFTC claiming the exemption.

Prior to 2012, this was a one-time filing. However, in 2012 the CFTC changed the regulations to require any person claiming an exemption from regulation to file an annual statement within 60 days after the end of each year confirming that it still qualifies for the exemption. The first annual statement for calendar year 2012 should be filed by March 1, 2013. Failure to confirm a plan's exempt status may result in the plan fiduciaries being required to register as commodity pool operators.

As part of the same regulation update, the CFTC also eliminated an exemption for commodity pools that are limited to large sophisticated investors. Some plans may have relied on this exemption on the theory that the plan itself, rather than the participants, was the investor. If a plan relied on this exemption, it needs to confirm that it is still exempt under the rule applicable to ERISA plans.

The following types of plans are exempt *without the need to file an exemption* with the CFTC:

- Plans that don't provide for any employee contributions, whether defined benefit or defined contribution.
- Defined benefit plans that provide for employee contributions, but that limit the contributions so that they can't be invested in futures contracts.
- Welfare plans.
- Church and governmental plans.

A plan may also be exempt from registration if it does not invest directly in commodity futures, but only invests in mutual funds or similar investment vehicles that invest in commodity futures, but which are themselves exempt.

Also in 2012, the CFTC adopted regulations implementing the registration requirements for "major swap participants" as added by the Dodd-Frank Act. Although employee benefit plans are exempt from these rules if they engage in commodity swaps for the primary purpose of hedging risks, plan fiduciaries should confirm with their trading advisers that the plan's funds will be operated in accordance with these rules.

Steps to take:

- If your 401(k) plan has previously filed a statement with the CFTC that the plan fiduciaries are exempt from registration as commodity pool operators, a confirmation must be filed not later than March 1, 2013. All statements are filed online through the National Futures Association website.
- If your plan accepts employee contributions and uses commodity futures as part of its trading strategy (other than solely by investing in a mutual fund that uses futures) and has not previously registered, you need to determine whether the plan is exempt, and file the appropriate exemption statement or registration if applicable.
- If any of your plan's investment advisers utilize strategies that involve commodity swaps, review the investment advisory agreement to insure that it requires them to comply with the new regulations governing major swap participants.

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