investee pools, any principal of the foregoing, and the pool's FCMs and IBs (if any). Disclosure of actions that were concluded by adjudication on the merits in favor of the listed persons would not have been required. Proposed Rule 4.33(k) would have required similar disclosure with respect to the CTA and with respect to the FCM and IB required to be used by the CTA's client.

Former Rule 4.21(a)(13) required disclosure of any action against a pool's CPO, CTA, FCM, IB or any of their principals within five years preceding the Document date without regard to the outcome. Former Rule 4.31(a)(7) required similar disclosure with respect to the CTA, any FCM or IB the client is required to use, and any principal of those persons. If there had been no actions against any of the listed persons, the former rules required a statement to that effect.

In addition to eliminating the requirement to disclose actions resolved on the merits in favor of one of the identified persons, the proposed rules would have substantially reduced required litigation disclosures concerning FCMs and IBs. First, the basic determinant of whether FCM or IB litigation would be material would be the extent of potential impact of the proceeding upon the FCM or IB, unless the proceeding were brought by the Commission or another regulatory or self-regulatory organization. The proceeding would be disclosable only if it would be required to be disclosed in the notes to the FCM's or IB's financial statements prepared pursuant to generally accepted accounting principles.[173] Disclosure of actions brought by the Commission and other regulatory agencies was also proposed to be streamlined. Commission actions would have been deemed material except for concluded actions which did not result in civil monetary penalties exceeding $50,000 and did not involve allegations of fraud or willful misconduct or which was adjudicated on the merits in favor of the specified person. Actions brought by other federal or state regulatory agencies or domestic or foreign self-regulatory organizations would have been required to be disclosed either if they were required to be disclosed in the notes to financial statements as discussed above or if they involved allegations of fraud or willful misconduct. Proposed Rule 4.24(*l*) also would expressly have required disclosure of litigation against a pool's trading manager, if any, and its principals, a requirement previously encompassed within the former requirement for disclosure of litigation against CTAs.

Proposed Rules 4.24(*l*) and 4.33(k) thus represented a reduction of required litigation disclosure, particularly with respect to FCMs and IBs. The scope of previously required litigation disclosures as to CTAs would have been limited under proposed Rule 4.24(*l*) to major, as opposed to all, CTAs for the pool, and only litigation against operators of major investee pools would be included.[174] Litigation involving FCM and IB principals was not included in the proposed rule.

Commenters generally supported the proposed changes but suggested certain further revisions. One commenter urged that *all* Commission and other regulatory matters concluded favorably with respect to the respondent (whether or not involving allegations of fraud or willful conduct) should be considered *not* material. Several commenters contended that litigation against FCMs is immaterial because such litigation generally does not jeopardize customer funds and virtually all FCMs have been subject to litigated customer claims. One commenter stated that only litigation required to be disclosed in the FCM's financial statements (and not the regulatory matters required by Rule 4.24(*l*)(2) (ii) and (iii)) is material and should be required in CPO and CTA Documents. Other commenters contended that CPOs and CTAs must rely upon the FCM to furnish its litigation history and are unable to verify independently the information that is provided. Consequently, commenters recommended, variously, that litigation disclosures be limited to those actions against an FCM that the FCM reasonably believes are likely to have a material adverse effect on the FCM's ability to provide brokerage services to the pool or managed account program or upon the investor's decision to place his funds with that FCM, or actions *actually* disclosed in an FCM's or IB's financial statements. Another commenter asserted that the impact of the litigation disclosure requirement upon funds-of-funds is unclear.

The Commission is adopting Rules 4.24(*l*) and 4.33(k) as proposed (renumbering proposed Rule 4.33(k) as 4.34(k)) with the exception that the rule is clarified to make explicit that actions involving an FCM or IB brought by a non-United States regulatory agency and involving allegations of fraud or willful misconduct will be considered material. The requirement to disclose actions that would be required to be disclosed in an FCM's or IB's financial statements is being retained. Since FCMs carry funds of the pool or managed account, their financial status and reliability are matters of material importance to prospective investors.

Except for events occurring subsequent to the issuance of the latest certified financial statements, litigation required to be disclosed would already have been disclosed in the FCM's or IB's latest certified financial statements. Generally, the CPO or CTA will be able to rely, under a reasonable diligence standard, upon these pre-existing disclosures as to matters covered by such statements. A CPO should exercise reasonable diligence in determining which subsequent actions are required to be so disclosed. Generally, absent facts placing the CPO or CTA on notice of special circumstances, the CPO or CTA should be able to rely upon representations by the FCM or IB as to what litigation is required to be disclosed in the firm's financial statements.

Actions brought by the Commission are treated differently from those brought by other regulatory agencies due to the presumptively greater relevance of such actions to the investment decision being made. All actions brought by the Commission are considered material other than concluded actions that did not result in civil monetary penalties exceeding $50,000 and did not involve allegations of fraud or other willful misconduct or which were adjudicated on the merits in favor of the specified person. Actions brought by any other federal or state agency, by a non-United States regulatory agency or by a self-regulatory organization, whether domestic or foreign, are material if they involve allegations of fraud or other willful misconduct. In all cases, subject to the general materiality standard, concluded actions resulting in an adjudication on the merits in favor of such persons would not be required to be disclosed.

As in the case of other provisions of the final rules, Rule 4.24(*l*) provides parallel treatment of litigation against CTAs for the pool and the operators of

[173] Proposed Rules 4.24(*l*)(2)(i) and 4.33(k)(2)(i). Under generally accepted accounting principles, certain information regarding litigation must be disclosed if the potential of a financial loss from the litigation is either probable (*i.e.*, likely to occur) or reasonably possible (more than remote but less than likely). *See* ACCOUNTING FOR CONTINGENCIES, Statement of Financial Accounting Standard No. 5, (Financial Accounting Standards Board, 1975) relating to disclosure of contingencies, including litigation.

[174] *See* Rules 4.10(i) and (d)(5), which define the terms ''major commodity trading advisor'' and ''major investee pool.'' Of course, as noted above with respect to conflicts of interest on the part of FCM and IB pricnipals, the requirement to disclose all material information may require disclosure of litigation involving persons not expressly designated in the rules.