



U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Swap Dealer and
Intermediary Oversight

Gary Barnett
Director

CFTC Letter No. 14-49
Exemption
March 31, 2014
Division of Swap Dealer and Intermediary Oversight

Re: “A” and “B”, registered commodity pool operators for certain proprietary funds

Dear :

This is in response to your letter (the “Letter”), dated May 17, 2013, to the Division of Swap Dealer and Intermediary Oversight (the “Division”) of the U.S. Commodity Futures Trading Commission (the “Commission”). On behalf of the members of the “A” and its affiliate, “B” (“B,” and, together with “A”, the “Firms”), you requested no-action relief for each Firm if such Firm files with the National Futures Association (“NFA”) and distributes to participants of certain proprietary funds (“Proprietary Funds”) that are wholly owned by current owners of such Firm, close relatives of owners of such Firm, senior employees of such Firm, or portfolio managers of the applicable Proprietary Fund (collectively, “Personnel”) an annual report with financial statements that are not audited by an independent public accountant as required under Commission regulations 4.7(b)(3) and 4.22(d).¹

Background Facts

Based on the representations made in the Letter and other supplemental correspondence (collectively, the “Correspondence”), the Division understands the facts to be as follows. You request, on behalf of the members of the Firms, no-action relief for each Firm if such Firms files with NFA and distributes to participants of Proprietary Funds that are wholly owned by Personnel an annual report with financial statements that are not audited by an independent public accountant as required under Commission regulations 4.7(b)(3) and 4.22(d). You state that the no-action relief request applies to the financial statements for fiscal year 2013 and future fiscal years, as well as to any similarly situated Proprietary Fund that mirrors the facts provided in the Letter that may be created or operated by a Firm in the future.

“A”

¹ The Commission’s regulations can be found at 17 CFR part 4 (2013).

“A” and “B”

Page 2

You state that “A” is the commodity pool operator (the “CPO”) to a number of proprietary funds (each, an “A Proprietary Fund”), which are wholly owned by Personnel of “A” (“A Personnel”) and established by “A” to test new trading systems or strategies before determining whether to launch a new fund. You state that each “A” Proprietary Fund is operated pursuant to the exemption provided in Commission regulation 4.7(b). You also state that all “A” Personnel who invest in “A” Proprietary Funds have access to the trading records of the applicable “A” Proprietary Fund(s), as well as to unaudited annual financial statements of the applicable “A” Proprietary Fund(s). Also, you state that, although a former founding principal of “A” had invested in several of the “A” Proprietary Funds, he has been redeemed from the relevant funds. You state that all “A” Proprietary Fund investors have agreed in writing to waive the right to receive audited financial statements for the applicable “A” Proprietary Fund(s). Furthermore, you state that no “A” Proprietary Fund pays performance or management fees to “A” or “C”, which is the general partner of each “A” Proprietary Fund.²

You also state that if an “A” Proprietary Fund investor is no longer an “A” principal, or the trustee of a trust is no longer an “A” principal or a close relative of an “A” principal, that investor will be permitted to remain invested in the “A” Proprietary Fund(s) in which such investor is already invested, but generally will not be allowed to invest in future “A” Proprietary Funds. However, you state that if a senior employee or portfolio manager is no longer employed at “A”, that senior employee or portfolio manager will be required to redeem the interest in the applicable “A” Proprietary Fund(s) within a reasonable time and, unless such individual is also a principal of “A”, will no longer be allowed to invest in any future “A” Proprietary Funds.

Furthermore, you state that when the trading system or strategy testing of an “A” Proprietary Fund is complete, the “A” Proprietary Fund is either dissolved or the system or strategy is made available for investment by certain outside qualified eligible persons (“QEPs”), as defined in Commission Regulation 4.7, through either the existing “A” Proprietary Fund or a new fund pursuing the trading system or strategy. If the latter is the case, then such fund will comply with the full requirements of Commission Regulation 4.7(b), including having the financial statements in the annual report audited by an independent public accountant.

“B”

With respect to “B”, you state that “B” intends to establish a number of proprietary funds (each, a “B Proprietary Fund”) to test new trading systems or strategies before determining whether to launch a new fund, similar to “A”. You state that if the general partner, manager, or managing members of a “B” Proprietary Fund (the “MM”) is not registered with the Commission, the MM will delegate all CPO responsibilities and obligations with respect to the “B” Proprietary Funds to “B”, while agreeing to remain jointly and severally liable with “B” for

² You state that the “C” has delegated all CPO responsibilities and obligations with respect to the “A” Proprietary Funds to “A”. The Division has received a delegation no-action relief request letter to the Division on July 19, 2013 with respect to all of the “A” Proprietary Funds that receive relief pursuant to this letter.

any breaches of the Commodity Exchange Act (the “Act”). You state that, currently, there are no “B” Proprietary Funds, but “B” may establish such funds in the future.

You state that each “B” Proprietary Fund will be wholly owned by “B” principals or close relatives of current principals of “B” (or an entity owned by such persons), who will have access to the trading records and unaudited financial statements of the relevant “B” Proprietary Fund(s). You state that “B” will ensure that all “B” Proprietary Fund investors will waive in writing their right to receive audited financial statements for the applicable “B” Proprietary Fund. You state that “B” does not intend to allow employees who are not also principals of “B” to invest in any “B” Proprietary Funds. You state that all “B” Proprietary Fund investors will be QEPs and that each “B” Proprietary Fund will be operated pursuant to the exemption provided in Commission Regulation 4.7(b). Furthermore, you state that neither “B” nor the MM of the “B” Proprietary Funds will receive any performance or management fees for its services to the “B” Proprietary Funds.

You also state that if a “B” Proprietary Fund investor is no longer a “B” principal, or the trustee of a trust is no longer a “B” principal or a close relative of a “B” principal, that investor will be permitted to remain invested in the “B” Proprietary Fund(s) in which such investor is already invested, but generally will not be allowed to invest in future “B” Proprietary Funds. You also state that if an employee is no longer employed at “B”, that employee will be required to redeem such employee’s interest in the applicable “B” Proprietary Fund(s) within a reasonable time.

You state that when the trading system or strategy testing of a “B” Proprietary Fund is complete, the “B” Proprietary Fund will either be dissolved or the system or strategy will be made available for investment by certain outside QEPs.

Regulatory Background

Commission Regulation 4.7(b)(3) provides a CPO an exemption from filing and distributing an annual report in accordance with Commission Regulation 4.22(c) with respect to an exempt pool it operates in accordance with Commission Regulation 4.7; provided, that the CPO files with NFA and distributes to each participant an annual report for the exempt pool that complies with Commission Regulation 4.7(b)(3) within 90 calendar days after the end of the exempt pool’s fiscal year or the permanent cessation of trading, whichever is earlier. Commission Regulation 4.22(d) requires, among other things, financial statements in such annual reports to be audited by an independent public accountant. The principal purpose of financial reporting required by Commission regulations 4.7(b)(3) and 4.22(d) is to ensure that pool participants receive accurate, fair and timely information on the overall trading performance and financial condition of the pool.

Relief Granted

Based upon the representations made in the Correspondence, the Division believes that granting relief is neither contrary to the purpose of Commission regulations 4.7(b)(3) and 4.22(d)

nor to public interest. Accordingly, pursuant to the authority delegated by Commission regulations 140.93 and 4.12(a), the Division hereby grants “A” relief from the requirement pursuant to Commission regulation 4.22(d) to have an independent public accountant audit the financial statements for the following “A” Proprietary Funds:

1. “D”
2. “E”
3. “F”
4. “G”
5. “H”
6. “I”
7. “J”
8. “K”
9. “L”
10. “M”
11. “N”
12. “O”
13. “P”
14. “Q”
15. “R”
16. “S”
17. “T”
18. “U”
19. “V”
20. “W”

This relief is conditioned on the following:

1. If a current “A” Proprietary Fund investor is no longer an “A” principal, senior employee or portfolio manager, or the trustee of a trust is no longer an “A” principal or a close relative of an “A” principal, that investor must be redeemed out at the next regular redemption date.
2. The only new investors that each “A” Proprietary Fund listed above may take on are current “A” principals, senior employees or portfolio managers.

The Division declines to grant “A” relief with respect to any “A” Proprietary Funds that are not listed by name in the Letter, including the “A” Proprietary Funds that have yet to exist, as such relief would be contrary to the provisions of Commission regulation 140.99. For similar reasons, the Division declines to grant “B” relief with respect to any future “B” Proprietary Funds.

This letter, and the positions taken herein, represents the view of this Division only, and does not necessarily represent the position or view of the Commission or of any other office or division of the Commission. The relief issued by this letter does not excuse persons relying on it from compliance with any other applicable requirements contained in the Act or in the Commission regulations issued thereunder. Further, this letter, and the relief contained herein, is based upon the representations made to the Division. Any different, changed or omitted material facts or circumstances might render this interpretation void.

Should you have any questions, please do not hesitate to contact Amanda Olear, Associate Director, at 202-418-5283, or Chang Jung, Attorney-Advisor, at 202-418-5202.

Very truly yours,

Gary Barnett
Director
Division of Swap Dealer and
Intermediary Oversight