

CFTC Letter No. 00-54

March 30, 2000

Exemption

Division of Trading and Markets

Re: Rule 4.7(a) - "X"

Dear :

This is in response to your letter dated February 15, 2000, to the Division of Trading and Markets ("Division") of the Commodity Futures Trading Commission ("Commission"). By your correspondence, you request on behalf of "X", a registered commodity pool operator ("CPO"), that the Division permit "X", in connection with its operation of the "Fund", to continue to treat "Y" as if it satisfies the qualified eligible participant ("QEP") criteria of Rule 4.7(a) for the purposes of the participation of "Y" in the Fund and to permit "X" to continue to claim relief from Rules 4.21 through 4.26 in connection with "X's" operation of "Y", notwithstanding the addition of two non-QEP investors to "Y".¹

Preliminarily, we note that by letter dated December 27, 1999 ("Prior Letter"), the Division permitted "X" to continue to claim relief from the specific requirements of Rules 4.21 through 4.26 in connection with its operation of "Y", notwithstanding the participation of a non-QEP investor in "Y", and permitted "X" to continue to claim relief pursuant to Rule 4.7(a) in connection with its operation of the Fund, notwithstanding the investment of "Y" in the Fund. The Division issued the Prior Letter based upon representations, among others, that the non-QEP investor was a research analyst for the manager of the fund, ("Fund Manager"),² had over two years' experience in the financial services industry, and was an "accredited investor" as that term is defined in Rule 501(a)(6) under the Securities Act of 1933.³

Based upon the representations made in your correspondence, we understand the relevant facts to be as follows. "X" serves as the CPO of the Fund and "Y". Pursuant to a Notice of Claim for Exemption filed under Rule 4.7(a), interests in the Fund may be sold only to QEPs.⁴ "X" now wishes to admit two additional non-QEP investors ("Non-QEPs") as members of "Y". Specifically, the Non-QEPs are "B" and "C", each of whom is an accredited investor under Rule 501(a)(6) and has been employed as a portfolio manager or a research analyst for at least the two preceding years. Each currently is employed as an analyst by the Fund Manager.

The purpose of Rule 4.7 is to "reduc[e] unnecessary regulatory prescriptions for CPOs offering pool participations only to persons who, based upon the qualifying criteria in the rule, do not appear to need

the full protections offered by the Part 4 framework."⁵ As noted above, the Non-QEPs do not meet the applicable QEP criteria. However, as also noted above, the Non-QEPs: (1) are employed by the Fund Manager as analysts; (2) have over two years' experience in the financial services industry; and (3) are accredited investors under Rule 501(a)(6).

Based upon the foregoing representations, it appears that granting your request would not be contrary to the public interest or the purposes of Rule 4.7(a).⁶ Accordingly, by the authority delegated under Rule 140.93(a)(1), the Division hereby confirms that "X" may continue to claim relief pursuant to Rule 4.7(a) with respect to the Fund, notwithstanding the participation of the Non-QEPs in "Y". Further, by the authority delegated under Rule 140.93(a)(1), "X" may also continue to claim relief from the specific requirements of Rules 4.21 through 4.26 in connection with its operation of "Y".

This letter does not excuse "X" from compliance with any other applicable requirements contained in the Commodity Exchange Act ("Act")⁷ and the Commission's regulations issued thereunder. For example, "X" remains subject to all of the antifraud provisions of the Act and the Commission's regulations, the reporting requirements for traders set forth in Parts 15, 18, and 19 of the Commission's regulations and all otherwise applicable provisions of Part 4. Moreover, this relief is applicable to "X" solely in connection with its operation of the Fund and "Y", as discussed above.

This letter, and the relief provided by this letter, are based upon the representations you have made to us. Any different, changed or omitted material facts or circumstances might render the relief provided by this letter void. You must notify us immediately in the event the operations or activities of "X", the Fund Manager, the Fund, or "Y", including the composition of participants, change in any material way from those as represented to us.

If you have any questions concerning this correspondence, please contact Matthew W. Lisle, an attorney on my staff, at (202) 418-5450.

Very truly yours,

John C. Lawton
Acting Director

1 While your letter sought approval of additional members to "Y" in accordance with the conditions set forth in a previously issued "no-action" letter dated September 15, 1997 from the Division to "X", we are treating it as a request for exemption from the QEP criteria of Rule 4.7(a) and as a matter that needs to be addressed separately from the relief granted in the "no-action" letter. *See* CFTC Staff Letter No. 97-86, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶27,183 (September 15, 1997). Commission rules referred to herein are found at 17 C.F.R. Ch.1 (1999).

2 The Fund Manager and the CPO are both controlled by "A".

3 17 C.F.R. § 230.501(a)(6) (1999) defines an "accredited investor" as a person who "had an individual income in excess of \$200,000 in each of the two most recent years or joint income with that person's spouse in excess of \$300,000 in each of those years and has a reasonable expectation of reaching the same income level in the current year."

4 "X" filed a Notice of Claim of Exemption pursuant to Rule 4.7(a) in connection with its operation of the Fund on _____.

5 57 Fed. Reg. 3148 at 3150 (January 28, 1992). Among other things, Part 4 specifies disclosure, reporting and recordkeeping requirements for CPOs.

6 The Commission recently has proposed revisions to Rule 4.7 that would include in the QEP definition, among other persons, any employee of a Rule 4.7 exempt pool, CPO or an affiliate of the foregoing (other than an employee performing solely clerical, secretarial or administrative functions with regard to such person or its investments), provided that such employee is an accredited investor as defined in Rule 501(a)(5) or (6) and has been employed in the financial services industry for at least 24 months. *See* 65 Fed. Reg. 11253, 11260 (Mar. 2, 2000).

7 7 U.S.C. § 1 *et seq.* (1994).