



U.S. COMMODITY FUTURES TRADING COMMISSION

Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581
Telephone: (202) 418-5430
Facsimile: (202) 418-5547
aradhakrishnan@cftc.gov

Division of Clearing and
Intermediary Oversight

CFTC Letter No. 08-01
January 11, 2008
Exemption
Division of Clearing and Intermediary Oversight

Re: Regulations 4.21, 4.22 and 4.23 –
Request for exemption from certain Disclosure Document, reporting and
recordkeeping requirements in connection with the operation of the Fund.

Dear :

This is in response to your letter dated December 21, 2007, to the Division of Clearing and Intermediary Oversight (the “Division”) of the Commodity Futures Trading Commission (the “Commission”), as supplemented by subsequent letters¹ and e-mail messages (the “correspondence”). By the correspondence, you request, on behalf of “A”, a registered commodity pool operator (“CPO”), exemption from certain provisions of Commission Regulations 4.21, 4.22, and 4.23,² which concern, respectively, the disclosure, reporting and recordkeeping requirements applicable to registered CPOs, in connection with “A” serving as the registered CPO of the Fund.

Background

Based upon the representations made in the correspondence, we understand the relevant facts to be as follows. Interests (“Shares”) in the Fund will be offered and sold to the public, pursuant to an effective registration statement filed with the Securities and Exchange Commission (“SEC”) (the “Registration Statement”).³ The Shares of the Fund will be both

¹ Specifically, those letters were dated December 26, 2007 and January 2, 2008.

² Commission regulations referred to in this letter are found at 17 C.F.R. Ch. I (2007). They can be accessed through the Commission’s website, at: <http://www.cftc.gov/>.

³ Prior to making the instant request, “A” filed the relevant offering materials for review with both the National Futures Association (“NFA”) and the SEC.

publicly-offered and listed for trading on the “X”, and it is this latter fact that causes “A” to seek the requested exemption.⁴

The Fund is being structured, and will be offered and listed, in a manner substantially similar to an exchange-traded fund, or ETF.⁵ The Fund will seek to track the performance of a futures index (the “Index”), which is described in your correspondence.⁶ To this end, and as more fully described in your correspondence, the Fund will establish positions in the futures contracts tracked by the Index.

Shares will be issued only in one or more blocks of Shares (“Baskets”), and in the first instance, only to an initial purchaser, anticipated to be “B” (the “Initial Purchaser”), a registered broker-dealer.⁷ The Initial Purchaser will commit to purchase the entire initial public offering of the Fund. The Initial Purchaser will not solicit or actively seek purchasers for Shares, and no person (other than the Initial Purchaser) will have any opportunity to purchase Shares prior to

⁴ Your request assumes, and the Registration Statement states, that the Shares constitute securities for purposes of the U.S. federal securities laws and will be offered, sold and transferred as such. While we may not necessarily agree with your categorization on this issue, the Division will not recommend that the Commission commence any enforcement action against a Fund or market participants in connection with the offer, sale and transfer of Shares in the manner contemplated by your request and the Disclosure Document for the Fund.

Further, we note that “X” listing will not affect “A’s” obligation to comply with any other provision of the Commodity Exchange Act (the “Act”) or the Commission’s regulations issued thereunder applicable to CPOs in particular or to persons in general. The Act is found at 7 U.S.C. §1, *et seq.* (2000), and also may be accessed through the Commission’s website, at: <http://www.cftc.gov/cftc/cftclawreg.htm>.

⁵ Unlike a typical ETF, however, the Fund will trade indirectly through a corresponding second fund, the Master Fund. The units of participation in the Master Fund are owned by “A” and the Fund.

The purpose of a two-tiered structure is to permit the Fund, which, as a commodity pool, would otherwise have to report its income to direct investors on a Form K-1, to provide information on a Form 1099 or substantially similar form, and thus in a format more akin to that given to ETF investors. You state that although the two-tier structure creates additional costs to investors, such costs are expected to be minimal.

For the purpose of this letter, the Division is treating the Fund and the Master Fund as a single commodity pool.

⁶ The Fund will seek to track the performance of the “C” sponsored by “D”, which is not affiliated with “A”.

⁷ “B” also is registered with the Commission as a futures commission merchant.

effectiveness of the Registration Statement and the listing of the Shares on the “X”.⁸ Subsequent to effectiveness of the Registration Statement, the Initial Purchaser will accept and fill orders and make an orderly market for the Shares. Additionally, the Fund may sell Baskets to “Authorized Participants” (certain registered broker-dealers who are also participants in the Depository Trust Corporation (“DTC”)), rather than directly to the public.

Investors will be able to purchase Shares in different contexts, then. First, upon effectiveness of the Registration Statement, from the Initial Purchaser, or if Authorized Participants decide to create additional Baskets, investors may purchase Shares from those Baskets. Second, investors may purchase Shares on the “X” in the secondary market.

Discussion

Regulation 4.21

Regulation 4.21(a) requires each registered CPO to deliver a Disclosure Document to prospective pool participants at or before the time the CPO delivers a subscription agreement for the pool. Regulation 4.21(b) requires the CPO to obtain a signed and dated acknowledgment that a prospective pool participant has received a Disclosure Document before the CPO may accept money or other property in exchange for shares or other units of interest in the pool. The purpose of the regulation is “to protect pool participants – particularly those who are unsophisticated in financial matters – by ensuring that they are informed about the material facts regarding the pool before they commit their funds.”⁹

The sale of Shares to the Initial Purchaser or to any Authorized Participant will be conducted in compliance with Regulation 4.21. The Initial Purchaser or Authorized Participant, as the case may be, will receive (and will acknowledge such receipt in writing) a Disclosure Document, which will comply in full with the requirements in Part 4 of the Commission’s regulations, and which “A” will update in accordance with Commission requirements.¹⁰

You request exemption from the Disclosure Document delivery requirement of Regulation 4.21 in the case of sales by the Initial Purchaser to the public and to the extent, if any, that Authorized Participants may subsequently create additional Baskets and sell those Shares to the public. In support of your request for exemption, you state that the Internet websites maintained by the Fund and the “X” (the “Website Sources”) will contain a current Disclosure Document for the Fund. You further state that “A” expects that prospective or actual investors will utilize the services of a registered broker-dealer, who will either inform them where they can

⁸ There will be no “road show” or other selling effort with respect to the Shares prior to the Registration Statement’s effectiveness and the Shares’ listing on the “X”.

⁹ 44 Fed. Reg. 1918, 1920 (Jan. 8, 1979).

¹⁰ See, e.g., Regulation 4.26, which contains various Disclosure Document updating requirements.

obtain the current Disclosure Document, or, upon request, will deliver a copy of the current Disclosure Document.¹¹

With respect to secondary market purchases on the “X”, you conclude that “A” is not subject to Regulation 4.21. The Division agrees with this conclusion.¹²

Regulations 4.22(a) and (b)

Regulation 4.22(a) requires a registered CPO to distribute to pool participants periodic unaudited Account Statements, which must include, among other information, Statements of Income (Loss) and of Changes in Net Asset Value. Regulation 4.22(b) provides that Account Statements be distributed monthly for pools with net assets of more than \$500,000 and otherwise at least quarterly.¹³ The purpose of these rules is to “ensure that participants have a reasonably current knowledge of the pool’s trading performance and operating costs.”¹⁴

An issuer of exchange-traded shares held in book-entry form through DTC (such as the Fund) typically does not readily know the identities of its ultimate beneficial owners. You request exemption from the Account Statement distribution requirement on the grounds that it would be unduly burdensome and costly to require “A” to ascertain on a monthly basis the identities of purchasers of Shares in the secondary market in order to comply with the requirement under Rules 4.22(a) and (b) to distribute monthly Account Statements to participants in each Fund.¹⁵ In this regard, you explain that, because of the secondary market for each Fund’s

¹¹ The only instances where the services of a registered broker-dealer would not be utilized would be where an investor has an account with a bank or trust company that is exempt from the requirement to register as a broker-dealer.

¹² The CPO’s obligation to deliver a Disclosure Document (and the requirement to obtain a signed acknowledgment of receipt) extends to the direct purchaser of units of participation, and not to persons who purchase from that purchaser. In this regard, the Commission has stated that, with respect to the transfer of a participation unit in a commodity pool, the CPO of the pool “is not required to provide a Disclosure Document (Rule 4.21) to a person who purchases a unit of participation or interest in the pool from a pool participant if the pool operator did not solicit the purchase.” 44 Fed. Reg. 25658, 25659 (May 2, 1979).

¹³ Regulation 4.22(c) requires a registered CPO to distribute a certified Annual Report to pool participants. You have not requested exemption from Regulation 4.22(c) in connection with the operation of the Fund, and, in fact, you represent that “A” will comply with Regulation 4.22(c) in connection with its operation of the Fund. Distribution of the Annual Report is required once a year, whereas distribution of monthly Account Statements requires continuous monitoring of changes in ownership of shares.

¹⁴ 44 Fed. Reg. at 1922 (Jan. 8, 1979).

¹⁵ You make this request not only with respect to investors purchasing Shares in the secondary market, but also with respect to purchasers from the Initial Purchaser or from an Authorized Participant. Once an investor has purchased Shares, whether directly from the Initial

shares on the “X”, ownership of a Fund’s shares is expected to change frequently on a daily basis.

In support of your request, you note that the same information that would otherwise be provided in each Fund’s monthly Account Statements, including the Fund’s net asset value via the Website Sources, and that monthly and annual reports conforming to the form and content requirements of Regulation 4.22, including the certification required by Regulation 4.22(h), will be posted on the Fund’s website, of which availability the Disclosure Document will advise participants.¹⁶ In this regard, you state that the expense of distributing an Account Statement is about the same as the expense of distributing the Annual Report and that, if the requested exemption is granted, the distribution expense of each Fund (an expense that is passed on to shareholders) will be significantly reduced.

Regulation 4.23

Rule 4.23 specifies the types of books and records a registered CPO must make in the course of operating a pool, and requires that those books and records be kept at the CPO’s main business office. The books and records must be available to pool participants for inspection and copying during normal business hours, and must be open and available for inspection by any representative of the Commission or the United States Department of Justice. The purpose of the regulation is “to enable pool participants and the Commission to ascertain whether the CPO is dealing properly with pool funds.”¹⁷

You request exemption from the location requirement of Regulation 4.23(a) such that books and records of the Fund (including those of the Master Fund) may be kept by its administrator, the “E”, a banking corporation subject to regulation by the “F” and the Federal Reserve Board, and, pursuant to delegation by “E”, by “G”, a registered broker-dealer that provides certain distribution-related services to the Fund (with respect to records related to Basket creations and redemptions and certain other functions), at their respective addresses as specified in your December 21, 2007 letter.¹⁸

Purchaser, from an Authorized Participant, or on the “X”, the Shares can be freely sold on the secondary market, and the same difficulties will be encountered in tracking the current owner.

¹⁶ Pursuant to Regulation 4.22(h), a representative duly authorized to bind the CPO must sign an oath or affirmation that, to the best of the knowledge and belief of the individual making the oath or affirmation, the information contained in the Account Statement is accurate and complete.

¹⁷ 44 Fed. Reg. at 1922.

¹⁸ Each of “E” and “G” has provided the Division with signed acknowledgments that the books and records of the Fund (including those of the Master Fund) may be inspected and copied by any representative of the Commission or the United States Department of Justice and may be inspected and copied during normal business hours by Fund participants. Included are schedules

You further ask for confirmation that neither “E” nor “G” will be deemed to be acting as a CPO solely by reason of keeping Fund records in the manner described in your correspondence, which the Division hereby so confirms. In this regard, the Division notes that neither firm will be acting in the manner contemplated by the statutory definition of a “commodity pool operator” – *e.g.*, neither will be promoting the pool by soliciting, accepting or receiving from others property for the purpose of commodity interest trading, and neither will have the authority to hire (and to fire) a Fund’s commodity trading advisor, and to select (and to change) a Fund’s futures commission merchant.¹⁹

Conclusion

Based upon the representations made in the correspondence, the Division believes that granting your request would not be contrary to the public interest and to the purposes of the regulations at issue. Accordingly, pursuant to the authority delegated in Regulation 140.93(a)(1), the Division hereby exempts “A” in connection with the operation of the Fund from: (1) the requirement of Regulation 4.21(b) to obtain a signed acknowledgment of receipt of a Disclosure Document before accepting funds, securities or property from a prospective pool participant with respect to sales of Shares by the Initial Purchaser and by Authorized Participants when Authorized Participants create additional Baskets, subsequent to effectiveness of the Registration Statement, provided that the information required to be contained in the Disclosure Document is maintained and kept current on the Website Sources; (2) the requirement of Regulation 4.22 to distribute monthly Account Statements to purchasers of Shares, provided that the information that would otherwise be contained in such reports is maintained on the Fund’s website; and (3) the requirement of Regulation 4.23 to keep required books and records at “A’s” main business office to the extent that such books and records are maintained at the offices of “E” or “G”.

Consistent with prior practice,²⁰ the exemption from the books and records location requirement of Regulation 4.23 is subject to the conditions that: (1) “A” notify the Division if the location of any of the books and records required to be kept by Regulation 4.23 changes from that as represented to the Division; (2) “A” remain responsible for ensuring that all books and records required by Regulation 4.23 are kept in accordance with Regulation 1.31 and for assuring the availability of such books and records to the Commission, NFA, and any other agency

specifying the classes of books and records, by subparagraph of Regulation 4.23, that each of “E” and “G” will be keeping.

¹⁹ See, *e.g.*, 49 Fed. Reg. 4778, 4780 (Feb. 2, 1984) (Commission acknowledged staff practice of employing these criteria in determining whether a person is, or is not, a CPO); and CFTC Staff Letter No. 06-27 [2005-2007 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶30,397 (Sep. 26, 2006) (Division granted a CPO an exemption to keep pool books and records with the pool’s administrator and its distributor, neither of which was thereby deemed to be acting as a CPO of the pool.)

²⁰ See, *e.g.*, Staff Letter 06-27.

authorized to review such books and records in accordance with the Act and Commission regulations; (3) within forty-eight hours after a request by a representative of the foregoing, “A” obtain the original books and records from “E’s” offices in _____ or from “G’s” offices in _____, as the case may be, and will provide them for inspection at “A’s” main business office in _____; (4) “A” disclose in the Fund’s Disclosure Document the location of its books and records that are required under Regulation 4.23; and (5) “A” remain fully responsible for compliance with Regulation 4.23.

This letter exempts “A” from Regulations 4.21, 4.22 and 4.23, as stated above. It does not excuse “A” from compliance with any other aspect of the Commission’s disclosure, reporting and recordkeeping requirements for registered CPOs, nor does it excuse “A” from compliance with any other applicable requirements contained in the Act or in the Commission’s regulations issued thereunder. For example, “A” remains subject to Regulation 1.31, and the Commission maintains its right under that regulation to inspect the required books and records of “A” at “E’s” offices in _____ and at “G’s” offices in _____. Additionally, “A” remains subject to all antifraud provisions of the Act and the Commission’s regulations, to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission’s regulations, and to all other applicable provisions of Part 4.

This letter is based upon the representations made to us and is subject to compliance with the conditions set forth above. Any different, changed or omitted material facts or circumstances might render this letter and the exemptions granted herein void. In this connection, you must notify us immediately in the event that the operations of “A”, the Fund, or the Master Fund change in any material way from those represented to us.

If you have any questions concerning this correspondence, please contact me or Christopher W. Cummings, Special Counsel, at (202) 418-5445.

Very truly yours,

Ananda Radhakrishnan
Director