84-11

COMMODITY FUTURES TRADING COMMISSION
2033 K STREET, N.W., WASHINGTON, D.C. 20581

DIVISION OF
TRADING AND MARKETS

July 17, 1984

Re:
Regulation as a commodity pool operator.

Dear :

This is in response to your letter dated June 15, 1984, as supplemented by the letter of your associate, , dated June 27, 1984 and the draft prospectus dated June 22, 1984 (the "Prospectus") enclosed therewith, in which you requested an opinion that (the "Fund") would not be a "pool" as defined in Rule 4.10(d) of the Commission's regulations, 17 C.F.R. §4.10(d) (1983).

From the representations made in your letter, as supplemented, we understand the facts to be as follows: The Fund is a Maryland corporation which has applied for registration as an open-end investment management company under the Investment Company Act of 1940. The investment objective of the Fund is "to provide investors with a high current return by investing in [Federal] debt obligations . . . and by writing covered call options and secured put options against such securities." In addition, the Fund may also engage in transactions involving interest rate futures contracts and options on such contracts "in order to hedge against changes in interest rates."

These commodity interest transactions would, however, be subject to certain limitations. The Prospectus, at page 13, sets forth, among others, the following limitations:

> The Fund will not engage in transactions in futures contracts or related options for speculative purposes but only as a hedge against changes resulting from market conditions in the values of debt securities held in the Funds's portfolio or which it intends to purchase. . . In addition, the Fund may not purchase or sell futures contracts or purchase or sell related options if immediately thereafter the sum of the amount of margin deposits on the Fund's existing futures and related options positions and the amount of premiums paid for related options would exceed 5% of the Fund's total assets.

> [The Fund will] sell futures contracts, purchase put options on futures contracts and write call options on futures contracts solely for the purpose of protecting its portfolio against declines in value. In addition, the Fund expects that in the normal course upon sale (or other termination) of long futures contracts, long call options on futures contracts and written put options on futures contracts, it will have purchased or will purchase the debt securities covered by such futures contracts or options a substantial majority of the time, but under unusual market conditions it may terminate any of such positions without a corresponding purchase of securities.

On February 2, 1984, the Commission issued proposed Rule 4.5, which would exempt certain otherwise regulated persons from registration as a commodity pool operator ("CPO") and from the provisions of Subpart B of Part 4 of the Commission's regulations. 1/ See 49 Fed. Reg. 4778 (February 8, 1984), 49 Fed. Reg. 6910-11 (February 24, 1984). Based upon our review of the representations made in your letter, as supplemented, it appears that the Fund would be eligible for this proposed exemption inasmuch as the Fund: (1) is among the persons and qualifying entities covered by the proposal -- i.e., a registered investment company; (2) will engage in commodity interest transactions solely for bona fide hedging purposes; (3) will not deposit as initial margin or premiums for its commodity interest transactions more than 5% of its total assets; (4) will not be, and has not been, marketed as a commodity pool or otherwise as a vehicle for trading in the commodity interest markets; and (5) will disclose in writing to its prospective participants the purpose of and the limitations on the scope of its commodity interest trading.

Accordingly, this Division will not recommend that the Commission take any enforcement action against
for failure to register as a CPO or to comply with the provisions of Subpart B of Part 4 of the Commission's regulations.2/ This position is, however, subject to the condition that the Fund will comply with Rule 4.5 as adopted by the Commission or with any other such rule that the Commission may adopt

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1/ Section 4m(1) of the Act, 7 U.S.C. §6m(1) (1982), requires each person who comes within the CPO definition to register as a CPO with the Commission. The provisions of Subpart B of Part 4 concern the operational, disclosure, reporting and recordkeeping requirements of registered CPOs. See 17 C.F.R. §§4.20-4.23 (1983), as amended by 48 Fed. Reg. 35248 (August 3, 1983).

2/ Inasmuch as proposed Rule 4.5 would provide exemption for a registered investment company and any principal or employee thereof, the position we are taking herein also would apply to any principal or employee of the Fund -- e.g., its officers.

to exempt certain otherwise regulated persons from regulation as a CPO.3/ Therefore, this position will cease upon the effective date of Rule 4.5 or of such other rule.

In this connection, we note that previously we have issued opinions to certain registered investment companies that they would not be pools within the meaning and intent of Rule 4.10(d) based upon representations similar to those made by the Fund.4/ However, in light of the Commission's recent proposal in this area, we believe that such a "no-action" position is the appropriate relief that should be afforded at this time. We further note that with respect to such investment companies and the filing of certain notices proposed in Rule 4.5, the Commission has stated:

> [We do] not believe that it should be necessary for the recipients of such interpretative letters to, in effect, "re-submit" an application for exemption -- i.e., to file an initial notice of eligibility -- in the event the proposal is adopted. However, to insure that these persons (and entities) would be in compliance with the requirements of the proposed rule, the Commission intends to take the position that such persons must file supplemental notices in the event that any of the representations they previously had made to the Commission changed or that, to the extent that the proposal would require any additional representations, they were not in compliance with them. This position would ensure equal treatment of all persons claiming exemption under the rule. 49 Fed. Reg. 4778 at 4782-83.

3/ For example, the rule as adopted may or may not contain the same standards and indicia of bona fide hedging transactions and positions contained in the rule as proposed. Moreover, to the extent that the rule as adopted is less restrictive than the rule as proposed -- with respect to the standards and indicia of bona fide hedging transactions and positions or to any other aspect of the proposal -- the Fund would be able to trade commodity interests subject to such other restrictions provided, of course, that such trading is conducted in accordance with the rule as adopted.

4/ See _____, Comm. Fut. L. Rep. (CCH) ¶21,908 (available November 3, 1983); _____, Comm. Fut. L. Rep. (CCH) ¶21,906 (available October 21, 1983); _____, Comm. Fut. L. Rep. (CCH) ¶21,905 (available September 13, 1983). See also _____, Comm. Fut. L. Rep. (CCH) ¶21,910 (available November 21, 1983).

We believe, and intend to recommend, that the Commission should take this same position with respect to the Fund. 5/

You should be aware that the position we have taken in this letter does not excuse the Fund from compliance with any otherwise applicable requirements contained in the Act or in the Commission's regulations thereunder. For example, it remains subject to the anti-fraud provisions of Section 4o of the Act, 7 U.S.C. §6o (1982), and to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations, 17 C.F.R. Parts 15, 18 and 19 (1983), as amended.

The position we have taken herein is based upon the representations that have been made to us. Any different, changed or omitted facts or conditions might require us to reach different conclusions. In this connection, we request that you notify us immediately in the event the Fund's operations and activities change in any way from that as represented to us.

Very truly yours,

Andrea M. Corcoran
Director

5/ We historically have treated registered investment companies and their officers and directors as those persons subject to CPO regulation. You have requested our opinion, however, that neither the Fund's registered investment adviser, (the "Adviser"), nor its registered broker-dealer, (the "Distributor"), nor any officer, director or employee of the Adviser or Distributor is a CPO. Proposed Rule 4.5 does not contemplate that any such person would be a CPO. See, e.g., Rule 3.16(a)(5), which generally exempts from registration as an associated person of a CPO persons registered with the National Association of Securities Dealers as a registered representative or registered principal. 48 Fed. Reg. 35248 (August 3, 1983). Accordingly, we do not believe that any such opinion is necessary at this time.

However, in the unlikely event that Rule 4.5 or any other such rule as the Commission adopts includes investment advisers to and broker-dealers of registered investment companies among the persons who could be considered to be CPOs but does not also include provision for exemption from regulation as a CPO for such persons, the Division will not recommend that the Commission take any enforcement action against the Adviser, the Distributor, or any officer, director or employee thereof pending such persons' compliance with such requirements as the rule may impose. Of course, this position assumes that such persons will endeavor to achieve such compliance as promptly as possible.