



DIVISION OF
TRADING AND MARKETS

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

May 6, 1986

Re: Petition for Exemption from Certain Registration and
Recordkeeping Requirements

Dear :

This is in response to your letters dated November 22, 1985 and December 30, 1985, to the Division of Trading and Markets ("Division"), as supplemented by subsequent telephone conversations and a letter dated February 14, 1986, on behalf of your client, ("Bank"). The Bank has determined to apply for registration with the Commodity Futures Trading Commission ("Commission") as a commodity pool operator ("CPO") and, based upon the facts as represented to the Division and as set forth below, has requested the Division to grant relief from certain of the registration and recordkeeping requirements under parts 3 and 4 of the Commission's regulations. 1/

1/ In addition, the Bank has requested that, pending registration as a CPO, relief be granted to permit the solicitation of plan sponsors of employee benefit trusts and to negotiate and execute Trust Agreements as described herein providing for the commingling of trust assets in collective investment funds to engage in futures trading, provided that no trading in commodity futures contracts on behalf of such collective investment funds commences prior to the effective date of the registration of the Bank as a CPO.

Based upon the representations set forth herein, the Division will not recommend that the Commission take any enforcement action against the Bank or its employees for failure to be registered as a CPO or as an associated person of a CPO, respectively, in connection with the solicitation of plan sponsors of employee benefit trusts as stated in your letter. This position is, however, subject to the condition that, in connection with the solicitation activities set forth above, the Bank remains responsible as a CPO for compliance with the antifraud provisions

(Footnote continued)

The Facts

The Division understands that the Bank acts as a fiduciary of a number of employee benefit trusts, including pension, welfare and governmental plans as defined under section 3 of the Employee Retirement Income Security Act ("ERISA"). The Bank enters into written agreements ("Trust Agreements") establishing its fiduciary relationships, which obligate the Bank to manage trust assets for the exclusive benefit of trust beneficiaries in accordance with the provisions of the Trust Agreements and applicable laws, including Title I, Subtitle A, Part 4 of ERISA. Pursuant to rules promulgated by the Comptroller of the Currency, 12 C.F.R. part 9, the Bank manages employee benefit trust assets either through Master Trusts (which may hold at least some assets that would not qualify for "non-pool" status under Commission rule 4.5, 17 C.F.R. §4.5 (1985)) and, subject additionally to express authorization provided in the Trust Agreements, one or more collective investment funds. Such Master Trusts and collective investment funds consist solely of employee benefit trust assets.

The Bank intends to engage in the trading of futures (and options on futures) on U.S. government securities and stock indices (collectively "financial futures") through the vehicle of several of these collective investment funds. In doing so, the Bank intends to pursue certain investment strategies using financial futures trading to enhance portfolio return or to facilitate the allocation of portfolio assets among equity, debt and cash instruments. Because these investment strategies may not necessarily fall within the Commission's interpretation of bona fide hedging, as defined in Commission rule 1.3(z), 17 C.F.R. §1.3(z) (1985), or the alternate test set forth in rule 4.5(c)(2)(i), 17 C.F.R. §4.5(c)(2)(i) (1985), the Bank does not qualify for exclusion from the definition of a CPO under Commission rule 4.5, 17 C.F.R. §4.5 (1985), with respect to these funds and, therefore, it has applied for registration as such. 2/

The activities in which the Bank will engage requiring registration as a CPO, including all solicitations of prospective customers, will be conducted through the Fiduciary Futures Management Department ("Department"), a division of the Investment Management Department of the Investment Bank, one of three operating banks within the Bank. In order to ensure compliance with

(Footnote continued)

of section 4o of the Commodity Exchange Act, 7 U.S.C. §6o (1985).

The Bank has also requested relief from certain other regulatory requirements applicable to CPOs under part 4 of the Commission's regulations. The Division's position with respect to these matters will be addressed separately.

2/ The Bank also manages other funds with respect to which it qualifies for exclusion from the definition of a CPO.

the fiduciary obligations imposed upon it, inter alia, by the relevant provisions of ERISA and the regulations of the Comptroller of the Currency -referenced above, the activities of the Department are governed by the Fiduciary Policies and Practices Manual of the Bank. This manual is designed to establish a "chinese wall" between the Department and the other divisions of the Bank, prohibiting the sharing of information that would enable any employee of the Bank or the Bank itself to profit from knowledge of the trading activities of the Department.

Part 3 of the Commission's Regulations

Commission rule 3.14(a)(2), 17 C.F.R. §3.14(a)(2) (1985), provides that an application for registration as a commodity pool operator must be accompanied by a Form 8-R and the fingerprints of each natural person who is a principal of the applicant. As defined in Commission rule 3.1(a), 17 C.F.R. §3.1(a) (1985), a principal includes any "officer, director, branch office manager or designated supervisor or person occupying a similar status or performing similar functions, having the power, directly or indirectly, through agreement or otherwise, to exercise a controlling influence over [the applicant's] activities which are subject to regulation by the Commission." Thus, all officers of the Department, any officers of the Bank having direct or indirect authority over the activities of the Department and the Bank's Board of Directors generally would be required to be identified as principals and to file a Form 8-R and fingerprints.

In addition, many of these principals would also be required to be registered as associated persons of the CPO in accordance with the provisions of Commission rule 3.16, 17 C.F.R. 3.16 (1985). An associated person of a CPO, as defined in section 4k(2) of the Commodity Exchange Act, includes any officer or employee of the CPO engaged in any activity that involves "(i) the solicitation of funds, securities or property for a participation in a commodity pool or (ii) the supervision of any person or persons so engaged." As interpreted by the Commission, the provisions of section 4k(2) would require the registration as an associated person of all individuals in the line of supervisory authority over the associated persons who solicit commodity pool participations, including positions up through that of the CPO's chief operating officer. 3/

On behalf of the Bank, you have requested the Division to adopt a no-action position with respect to the principals of the Bank who are not directly employed within the Department. Specifically, you have requested that the Division not recommend any enforcement action against such individuals for their failure to file a Form 8-R and fingerprints as required

3/ See Interpretative Statement Regarding the Scope of the Term "Supervision" in the Associated Person Requirement, 45 Fed. Reg. 54032 (August 14, 1980).

by Commission rule 3.14(a)(2). Moreover, with respect to those principals not directly employed within the Department who would also be required to be registered as associated persons of the CPO, you have requested an exemption from the requirements of the provisions of Commission rule 3.16. 4/

Based upon the representations set forth above, the Division has determined to adopt the no-action position you have requested with respect to the individual principals of the CPO who are not directly employed within the Department. This no-action position is based, in particular, upon the representation that all of the collective investment funds managed by the Bank requiring it to be registered as a CPO will be managed within the Department and that, as a result of its obligations under federal law, the management of these funds is autonomous from the activities of the other divisions of the Bank. Moreover, the Division notes that the Bank has conducted a fitness examination of each of the principals of the Bank in connection with his employment. 5/ Although this examination is not considered a substitute for the fitness examination required under the Commission's regulations, the Division believes that, in connection with the other factors discussed above, it would impose an unnecessary burden on such individuals to require an additional fitness examination.

This no-action position, however, is subject to the condition that the President, Chief Executive Officer or other officer of the Bank with authority to sign on behalf of and bind the Bank furnish the Commission a letter setting forth a list of officers (up to at least the level of Senior Vice President) responsible for supervising the Fiduciary Futures Management Department and certifying that none of these officers or any director of the

4/ Pursuant to rule 3.16(g), your request is being treated as a petition for exemption from rule 3.16(a). Rule 3.16(g)(1) provides that any person adversely affected by the operation of rule 3.16 may file a petition with the Secretary of the Commission requesting an exemption from any of the requirements of the rule. Rule 3.16(g)(1) further provides that the Commission may grant such a petition if it finds that the exemption is not contrary to the public interest and the purposes of the provision from which exemption is sought. By rule 3.16(g)(2)(i), the Commission has delegated to the Director of the Division of Trading and Markets, or the Director's designee, the authority to grant or deny petitions filed pursuant to this rule.

5/ A fitness examination is effectively required by the provisions of 12 U.S.C. §1829, which prohibits any bank insured by the Federal Deposit Insurance Corporation ("FDIC") from employing any person who has been convicted of a crime involving dishonesty or breach of trust without the prior consent of the FDIC. Such fitness examinations generally include the submission of a fingerprint card to the Federal Bureau of Investigation for identification and processing.

Bank could be refused registration with the Commission on the grounds stated in section 8a(2) of the Act. Appropriate documents evidencing the authority of the certifying officer to sign on behalf of and bind the Bank must also be furnished to the Division. 6/

For these same reasons, pursuant to the authority delegated by rule 3.16(g) (2) (i), the Division has determined to exempt from registration as an associated person of a CPO those principals not directly employed within the Department whose supervisory responsibilities might otherwise require them to be registered as associated persons. This exemption is conditioned upon receipt by the Division of a binding resolution or other appropriate document vesting final supervisory authority, including the authority to hire and fire, with respect to the futures-related activities of the CPO, as fiduciary of employee benefit trust assets, and its associated persons, in a named officer. 7/ Evidence of the authority of the officer signing the resolution or other appropriate document must also be furnished to the Division. 8/

Part 4 of the Commission's Regulations

The recordkeeping requirements applicable to CPOs are set forth in Commission rule 4.23, 17 C.F.R. §4.23 (1985). Specifically, rule 4.23(b) requires each CPO to make and keep: (1) an itemized daily record of each commodity interest transaction of the commodity pool operator and each principal thereof; (2) each confirmation of a commodity interest transaction, each purchase and sale statement and each monthly statement furnished by a futures commission merchant to (i) the commodity pool operator relating to a personal account of the pool operator and (ii) each principal of the pool operator relating to a personal account of such principal; and (3) books and records of all other transactions in all other activities in which the pool operator engages. Those books and records must include cancelled checks, bank statements, journals, ledgers, invoices, computer generated records of all other records, data and memoranda which have been prepared in the course of engaging in those activities.

The primary purpose of these recordkeeping requirements is to permit the Commission and the National Futures Association ("NFA") to determine in a routine audit whether a CPO, or any principal of a CPO, has used the information it has about the trading activities of the pool to enter into

6/ A copy of this certification and related documents should also be sent to Daniel A. Driscoll, Vice President-Compliance, National Futures Association, 200 West Madison Street, Chicago, Illinois 60606.

7/ The Division understands that initially this officer will be the Bank's Chief Investment Officer.

8/ A copy of these documents should also be sent to Mr. Driscoll.

transactions for its own benefit. With respect to the activities of the Bank, however, you have stated that, in light of the "chinese wall" that separates the activities of the Department from the activities of the other divisions of the Bank, the Bank will not be in a position to take advantage of the trading activities of the Department. Moreover, requiring the Bank to make available for audit all of the books and records that would otherwise be required under this rule would impose a significant burden on the Bank, given its size and scope of activities. Therefore, you have requested that the Division exempt the divisions of the Bank other than the Department from the requirements of Commission rule 4.23(b). In other words, for purposes of rule 4.23(b), the Department only would be treated as the CPO.

The Division understands that the Bank is otherwise required to maintain the records required under Commission rule 4.23(b). Nonetheless, the Division has determined that granting the requested exemption is not contrary to the public interest and the purposes of the rule, in particular because of the procedures the Bank has implemented to ensure that no other division of the Bank, or any employee of the Bank, will be able to benefit from knowledge of the trading activities of the Department. Therefore, pursuant to the authority delegated by Commission rules 4.12 and 140.93(a)(1), the Division hereby exempts from the requirements of Commission rule 4.23(b) every division of the Bank other than the Department. This exemption, of course, does not exempt the Bank from making and keeping such records as may otherwise be required under the Commodity Exchange Act and the regulations thereunder. ^{9/} Nor does the Division intend by this action to waive the Commission's authority under section 6(b) of the Act to "require the production of any books, papers, correspondence, memoranda, or other records that the Commission deems relevant or material to [an] inquiry." ^{10/}

The no-action positions adopted, and the exemptions granted, by the Division in this letter are based upon the representations that have been made to the Division and set forth herein. Any different, changed or omitted facts or conditions may require the Division to reach a different conclusion. Therefore, we ask that you notify us immediately in the event that the activities of the Bank or any of the individuals affected hereby change in any way. Finally, the no-action position adopted herein is that of the Division of Trading and Markets and does not necessarily represent the views of the Commission or any other office or division of the Commission.

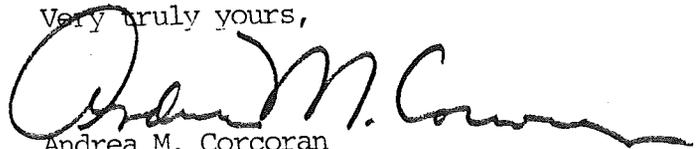
^{9/} See, e.g., parts 15 and 18 of the Commission's rules relating to reporting requirements of large traders.

^{10/} The Division, of course, has no authority to limit the Commission's statutory jurisdiction in this regard. Nor does the Division intend to limit in any way the authority of the National Futures Association to require production of such records pursuant to its compliance rule 3-1.

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If you have any questions about the positions adopted in this letter, please feel free to contact me or Kevin M. Foley, the Division's Chief Counsel, at 202/254-8955.

Very truly yours,

A handwritten signature in black ink, appearing to read "Andrea M. Corcoran". The signature is fluid and cursive, with a large initial "A" and "C".

Andrea M. Corcoran
Director

cc: Daniel A. Driscoll
Vice President-Compliance
National Futures Association