



Advisory: 2-93

For Release: January 7, 1993

# Advisory

## Two Interpretative Letters Concerning Rule 4.7 Relief for Pools With Non-QEPs

The Commodity Futures Trading Commission's Division of Trading and Markets has issued CFTC Interpretative Letters 93-1 and 93-2. Subject to certain conditions, CFTC Interpretative Letter 93-1 allows filing of a claim for exemption under Rule 4.7 by the commodity pool operators (CPO) of two pools in which some existing participants are not Qualified Eligible Participants (QEPs). The Division's letter permits the CPO to claim Rule 4.7 relief from the disclosure and reporting requirements of Rules 4.21 and 4.22, under the procedure set forth in Rule 4.7(a)(3)(i)(I)(2) for previously offered pools, provided that, among other things, non-QEPs and existing QEPs who have objected as provided in Rule 4.7(a)(3)(i)(I)(2) ("objecting QEPs") continue to receive the full protections of Part 4.

Other CPOs may claim relief from Rules 4.21 and 4.22 under Rule 4.7 for previously offered pools in which some participants are not QEPs ("Pools") by filing the notice of claim for exemption required by Rule 4.7(a)(3) and using the procedure set forth in Rule 4.7(a)(3)(i)(I)(2) provided that: (1) all new participants in the Pools will be QEPs; (2) the CPO will continue to provide non-QEPs and objecting QEPs who are already participants in the Pools with the disclosure and reporting, and will maintain the books and records, required under Part 4 for pools that are not operated pursuant to Rule 4.7; (3) the CPO will modify the statement required by Rule 4.7(a)(2)(i) to read as follows: "PURSUANT TO RELIEF FROM THE COMMODITY FUTURES TRADING COMMISSION IN CONNECTION WITH THIS OFFERING TO QUALIFIED ELIGIBLE PARTICIPANTS AN OFFERING MEMORANDUM FOR THIS POOL IS NOT REQUIRED TO BE, AND HAS NOT BEEN FILED, WITH THE COMMISSION"; the CPO will not claim exemption from disclosing in the Disclosure Document of non-exempt pools the past performance of the Pools so long as the Pools have any participants who were not QEPs when Rule 4.7 relief was claimed; and (4) the notice of claim for exemption states that the pool for which relief is claimed includes non-QEPs and that the CPO will comply with the applicable requirements of Rule 4.7 as modified by, and under the conditions set forth in, this Advisory.

In CFTC Interpretative Letter 93-2, the Commission's Division of Trading and Markets granted no-action relief to the CPO of a pool that would qualify for Rule 4.7 relief but for the fact that one pool participant is not a QEP. This non-QEP participant is not only an accredited investor, as defined in SEC's Regulation D, but also has been employed by the CPO for sixteen years, is registered with the National Association of Securities Dealers, Inc. as a registered representative, and has consented to being treated as a QEP.



**COMMODITY FUTURES TRADING COMMISSION**  
2033 K Street, NW, Washington, DC 20581  
(202) 254 - 8955  
(202) 254 - 8010 Facsimile

**DIVISION OF  
TRADING AND MARKETS**

December 10, 1992

Re: Application of Rule 4.7 to Pools with Non-OEPs

Dear Ms. :

This is in response to your letter dated October 1, 1992, as supplemented by telephone conversations with Division staff, in which, on behalf of ("X"), a registered commodity pool operator ("CPO"), and ("Y"), a registered commodity trading advisor ("CTA"), you request that the Division permit a claim for exemption under Rules 4.7(a) and 4.7(b), respectively,<sup>1/</sup> with respect to A and B ("Pools"), under the circumstances set forth in your letter as supplemented.

Based upon the representations made in your letter, as supplemented, we understand the pertinent facts to be as follows. X is the CPO and Y the CTA of the Pools. Many, but not all, of the present participants in each Pool are qualified eligible participants ("QEPs") as defined in Rule 4.7 and X intends to accept only QEPs as new participants in the Pools. You represent that neither X or Y, nor any of their principals, is subject to a statutory disqualification under Section 8(a)(2) or 8(a)(3) of the Commodity Exchange Act ("Act"), 7 U.S.C. §12a(2) or 12a(3) (1988).

X seeks to claim the following relief under Rule 4.7(a):  
(1) with respect to new investors, all of whom will be QEPs, relief from the disclosure requirements of Rule 4.21;<sup>2/</sup> all existing participants, including existing QEPs, would continue to

<sup>1/</sup> Rules 4.7(a) and (b), recently adopted by the Commission, 57 Fed. Reg. 34853 (August 7, 1992), provide that registered CPOs in connection with specified pools serve only "qualified eligible participants" and registered CTAs in connection with clients who are "qualified eligible clients" as those terms are defined in the rules, may claim relief from certain Part 4 requirements by filing a notice of claim for exemption.

<sup>2/</sup> Other than Rule 4.7, Commission rules referred to herein are found at 17 C.F.R. Ch. I (1992).

receive amendments to the Pools' Disclosure Documents to show material changes and inaccuracies as required by Rule 4.21(b); (2) with respect to existing participants and future participants who are QEPs, consistent with Rule 4.7(a)(2)(ii), relief from the requirement to give QEPs the periodic unaudited reports specified by Rule 4.22(a); non-QEPs would continue to receive the periodic reports as required by Rule 4.22(a) and QEPs would receive simplified periodic reports as specified by Rule 4.7(a)(2)(ii)<sup>3/</sup>; and (3) relief from the recordkeeping requirements of Rule 4.23.

Pursuant to Rule 4.7(a)(3)(i)(I)(2) the CPO of a pool that has been offered or sold in full compliance with Part 4 may file a notice of claim for exemption under Rule 4.7 provided, among other things, that the CPO has notified the pool's existing participants of its intention to claim a Rule 4.7 exemption, absent objection within twenty-one days after the date of the notification by the holders of a majority of the units of participation in the pool who are unaffiliated with the CPO. You represent that X will follow the Rule 4.7(a)(3)(i)(I)(2) procedure.

Y seeks to claim relief under Rule 4.7(b) from the recordkeeping requirements of Rule 4.32 in connection with its serving as the CTA of the Pools.

The basis for the Rule 4.7 exemption is that participants in a Rule 4.7 exempt pool "possess either the investment expertise and experience necessary to understand the risks involved . . . or have an investment portfolio of a size sufficient to indicate that the participant has substantial investment experience and thus a high degree of sophistication with regard to investments as well as financial resources to withstand the risks of their investments". 57 Fed. Reg. 3148 at 3152 (January 28, 1992). Accordingly, Rule 4.7 relief is available solely for pools whose participants are limited to QEPs. Thus, because the Pools have non-QEPs, absent relief, Rule 4.7 is not available to X in connection with the Pools.

However, after careful consideration, the Division believes that, inasmuch as: (1) X will accept no non-QEPs in the future; and (2) the Pools' non-QEPs will continue to receive the full protections of Part 4, your request has merit. Accordingly, based on the representations made in your letter, as supplemented, and subject to the conditions set forth herein, the Division has determined that it will not recommend that the Commission take any enforcement action against X if X claims relief from the

---

<sup>3/</sup> We note that all participants and the Commission would continue to receive the audited annual reports required by Rule 4.22(c).

disclosure and reporting requirements of Rules 4.21 and 4.22(a) by filing a Rule 4.7 notice of claim for exemption for the Pools, notwithstanding the present participation of non-QEPs in the Pools, and using the procedure set forth in Rule 4.7(a)(3)(i)(I)(2) for previously offered pools. This position is subject to the conditions that: (1) if X provides an offering memorandum to prospective participants in the Pools, X modifies the statement required by Rule 4.7(a)(2)(i) to reflect that the Pools include non-QEPs so that the first sentence of the statement reads as follows: "PURSUANT TO RELIEF FROM THE COMMODITY FUTURES TRADING COMMISSION IN CONNECTION WITH THIS OFFERING TO QUALIFIED ELIGIBLE PARTICIPANTS AN OFFERING MEMORANDUM FOR THIS POOL IS NOT REQUIRED TO BE, AND HAS NOT BEEN FILED, WITH THE COMMISSION"; (2) X continues to provide its existing participants with, and file with the Commission, all amendments to its Disclosure Document required by Rule 4.21(b); (3) with respect to reporting, X continues to provide non-QEPs and existing QEPs who have objected to the claim for Rule 4.7 relief within twenty-one days after the date of the notice required by Rule 4.7(a)(3)(i)(I)(2) with all reports required by Rule 4.22.<sup>4/</sup> With respect to recordkeeping, the Division has determined that, inasmuch as the Pools have non-QEP participants, relief from the requirements of Rule 4.23 is not appropriate.

As to the relief requested by Y the Division has determined that no relief is appropriate so long as the Pools are not QECs as defined in Rule 4.7(b). As noted above, Rule 4.7(b) allows a CTA to claim relief from certain Part 4 requirements with respect to the accounts of QECs. Based upon the information you have provided us, it does not appear that the Pools are QECs -- e.g., that they are exempt pools or entities in which all of the participants, other than Y are QEPs as specified in Rule 4.7(b)(1)(ii).<sup>5/</sup> Accordingly, this portion of your request is hereby denied.

We note that this letter relieves X solely from certain Part 4 requirements as set forth herein and does not otherwise excuse it from compliance with any applicable requirements contained in the Act or in the Commission's regulations thereunder. For example, it remains subject to the antifraud provisions of Section 40 of the Act, 7 U.S.C. §60 (1988), to the reporting

---

<sup>4/</sup> We note that you have not requested, and therefore this letter does not contain our opinion with respect to, relief under Rule 4.7(a)(2)(i)(B) from X including the Pools' past performance in the Disclosure Document of any non-exempt pool it may, now or in the future, operate.

<sup>5/</sup> See paragraphs 4.7(b)(1)(ii)(C) and (D) of the QEC definition.

Esq.  
Page 4

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 (1992), and to all other applicable provisions of Part 4.

This letter is based on the representation made to us and is subject to compliance with the conditions set forth above. Any different, changed or omitted facts or circumstances might require us to reach a different conclusion. In this connection, we request that you notify us immediately in the event the operations or activities of X or the Pools change in any way from those as represented to us. This letter represents the views of this Division and does not necessarily represent the views of the Commission or of any other office or division of the Commission.

If you have any questions concerning this correspondence, please contact me or France M.T. Maca, an attorney on my staff, at (202) 254-8955.

Sincerely,

Andrea M. Corcoran  
Director

FMTM/bgb

cc: Daniel Driscoll  
National Futures Association