



**COMMODITY FUTURES TRADING COMMISSION**

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93-59

**DIVISION OF  
TRADING AND MARKETS**

May 3, 1993

Re: Request for Relief from Commodity Pool Operator  
Regulation

Dear :

This is in response to your March 2, 1992 letter, as supplemented by Confidential Exhibits A, B and C thereto, by your April 14, May 13, July 28, 1992 and March 17, 1993 letters and by telephone conversations with Division staff, wherein, on behalf of "X" and its general partners, you request relief from commodity pool operator ("CPO") registration in connection with "X"'s investment in "Y".

Based upon the representations made in your letter, as supplemented, we understand the pertinent facts to be as follows. "X", a Delaware limited partnership, is a registered broker-dealer. "X" does not act as a broker-dealer on behalf of customers. "X" has two managing general partners "A" and "B", and nine other general partners.<sup>1/</sup> All, except four of the general partners who have no trading responsibility, are registered with the National Association of Securities Dealers, Inc. ("NASD") as registered representatives of "X". None of the general partners is subject to a statutory disqualification under Section 8a(2) or 8a(3) of the Commodity Exchange Act ("Act"), 7 U.S.C. §12a(2) or 12a(3) (1988), as amended by the Futures Trading practices Act of 1992, Pub. L. No. 102-546, 106 Stat. 3590 (October 28, 1992). "X"'s units of participation were sold in a private offering exempt from registration pursuant to Section 4(2) of the Securities Act of 1933 ("Securities Act"). "X" has presently sixty limited partners, each of whom, at the time of its purchase, was an accredited investor as that term is defined in Regulation D under the Securities Act. The average capital contribution of a limited partner exceeds \$1 million. Four of the sixty limited partners have current account balances of less than \$200,000 but

<sup>1/</sup> These other general partners are: "D" through "L".

are present or former senior employees of "X" or an affiliate thereof. All but four of the other limited partners, in addition to being accredited investors, have had a long relationship with "X", as they have been limited partners of "X" for no less than six years and up to eleven years. You represent that three of the four limited partners who have been limited partners of "X" for less than six years had an investment portfolio, at the time of their investment, including their investment in "X", of more than \$3 million. A fourth limited partner, admitted in June 1992 as an investor in "X", has an investment portfolio of more than \$2 million. New limited partners will be solicited in private offerings under Section 4(2) of the Securities Act. Except for officers of "X" or its affiliates, all new limited partners will be required to have a net worth of at least \$1 million at the time of his or her initial investment in "X". In total, "X" will have no more than one hundred limited partners at any time.

"X" primarily engages in risk arbitrage trading in the securities markets, including purchasing and selling securities of public issuers in connection with announced mergers, acquisitions, exchange offers, cash tender offers, corporate recapitalizations, liquidations and similar transactions. "X" also engages to a lesser extent in other activities such as short selling and conventional securities investing and trading. In connection with its securities trading, "X", from time to time, directly enters into commodity futures or options transactions for bona fide hedging purposes.<sup>2/</sup> "X" has not been and does not intend to be marketed as a commodity pool. While continuing to engage principally in securities risk arbitrage trading, "X" proposes to invest no more than five percent of its assets as a limited partner in "Y", a limited partnership that will be organized to conduct "X"'s proposed commodity futures and options trading activities. "X" will be the sole limited partner of "Y". "Y"'s general partner will be a registered commodity pool operator.<sup>3/</sup>

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<sup>2/</sup> For the purpose of this letter, we are presuming that these transactions will come within the definition of the term "bona fide hedging transactions and positions" in Rule 1.3(z)(1). You represent that for the years ended December 31, 1990 and 1991 and for the quarter ended March 31, 1992 the daily average aggregate amount of margin deposits and option premiums posted in connection with "X"'s bona fide hedging activity represents approximately .118%, .124% and .264% of "X"'s assets respectively.

<sup>3/</sup> It is expected that "C" will be the general partner and registered CPO of "Y". You represent that "C" "is recognized in the futures industry as an expert in the financial futures markets".

It is anticipated that "Y" will engage primarily in so-called volatility trading via spread and straddle transactions utilizing foreign currency options and options on futures. You represent that these transactions typically will be initiated in a "market-neutral" manner, i.e., the profitability of the transactions is not dependent upon the direction of exchange rate movements and that "Y"'s futures trading will be completely independent from "X"'s trading.

Based on the foregoing, you request that the Division not recommend any enforcement action against "X" or any of its general partners if they do not register as CPOs in connection with "X"'s investment in "Y". In support of your request, you represent that both "Y"'s CPO and "X" would qualify as "qualified eligible participants" under Rule 4.7.<sup>4/</sup> You also represent that the registered CPO of "Y" will comply with the disclosure, reporting and recordkeeping requirements for CPOs under Part 4 of the Commission's rules, as modified by the limited exemptions therefrom afforded under Rule 4.12(b).<sup>5/</sup> Although "X" will be the sole limited partner of "Y", the CPO of "Y" will treat the limited partners of "X" as if each were a limited partner of "Y" for purposes of meeting applicable disclosure and reporting requirements. The periodic and annual reports required under paragraphs (b) (2) (ii) and (b) (2) (iii) of Rule 4.12 will either be provided to the limited partners of "X" directly by the CPO of "Y" or be forwarded to such partners by "X". If the latter alternative is employed, this information may accompany or be incorporated into statements setting forth the financial results or other financial information relating to "X". In addition, you represent that each prospective limited partner of "X" will receive a disclosure document prepared by the CPO of "Y" meeting the requirements of Rule 4.12(b) (2) (i).

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<sup>4/</sup> Subject to the antifraud provisions of the Act and the regulations thereunder, pursuant to Rule 4.7, 57 Fed. Reg. 34853 (August 7, 1992), CPOs may claim relief from the disclosure requirements of Rule 4.21, certain reporting requirements of Rule 4.22 and the recordkeeping requirements of Rule 4.23 with respect to pools sold only to certain highly accredited investors termed "qualified eligible participants."

<sup>5/</sup> Commission rules referred to herein are found at 17 C.F.R. Ch. I (1992). Pursuant to Rule 4.12(b), a pool operator may claim relief from certain parts of Rules 4.21, 4.22 and from Rules 4.23(a) (10) and (a) (11) with respect to a pool it operates, subject to certain limitations relating, among other things, to the amount of pool assets committed to establish commodity interest positions.

Based on the foregoing, the Commission has determined that, subject to the conditions set forth below, it will not recommend that the Commission take any enforcement action against the general partners of "X" if such general partners do not register as CPOs in connection with their operation of "X". This position is based in part on your representations that the general partners of "X" are not subject to any statutory disqualification and that each general partner of "X" who has trading responsibility is registered with the NASD as a registered representative. This position is subject to the conditions that: (1) "X"'s commodity interest trading will be limited to: (a) directly investing no more than .5% of its assets in commodity futures or options thereon for bona fide hedging purposes; and (b) investing no more than five percent of its assets in "Y", a commodity pool formed specifically to trade commodity interests on behalf of "X"; (2) any new limited partner who is not an officer of "X" or its affiliates will have no less than \$1 million in net worth at the time of his or her initial investment in "X" and "X" will have no more than one hundred limited partners at any time; (3) "X"'s limited partners will be given the disclosures and reports as described above; and (4) within 30 days after issuance of this letter the Division receives a statement signed by each general partner of "X" confirming that each such general partner assumes liability under the antifraud provisions of Section 40 of the Commodity Exchange Act (the "Act"), 7 U.S.C. §60 (1988), as a CPO in connection with the operation of "X".

This letter is based on the representations that you have made to us. Any different, changed or omitted facts or circumstances may require us to reach a different conclusion. In this regard, we request that you notify us immediately in the event the operations of any of the entities referred to herein change in any way from those represented to us. The relief granted in this letter is applicable to "X"'s general partners solely in connection with their operation of "X" and is subject to compliance with the conditions set forth herein.

Further, this letter does not excuse "X"'s general partners from compliance with other applicable requirements contained in the Act or in the Commission's regulations thereunder. For example, they remain subject to the antifraud provisions of Section 40 of the Act (as indicated above), to the prohibitions of Rule 4.20 and to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations.

This letter represents the views of this Division only and does not necessarily represent the views of the Commission or of any other office or division of the Commission.

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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.

Very truly yours,

Susan C. Ervin  
Chief Counsel