COMMODITY FUTURES TRADING COMMISSION
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DIVISION OF
TRADING AND MARKETS

94-34

March 25, 1994

Re: Relief from Rule 4.7 "Ten Percent Limitation"

Dear :

This is in response to your letter dated February 8, 1994, as supplemented by your letter dated February 16, 1994 and telephone conversations with Division staff, in which, on behalf of "W", a registered commodity pool operator ("CPO"), you request relief from certain requirements of Rule 4.7[1/]. Specifically, in connection with "W"'s operation of "X", "Y" and "Z" (collectively, the "Pools"), you request relief from the Rule 4.7(a)(1)(ii)(B)(xi) provision ("ten percent limitation") that a pool may not invest more than ten percent of its assets in Rule 4.7 exempt pools unless all its participants are qualified eligible participants ("QEPs").

Based upon the representations made in your letter, as supplemented, we understand the pertinent facts to be as follows. "W" is the CPO of the Pools. The Pools, which primarily trade securities, follow a multi-manager investment approach, with "W" allocating their assets among numerous investment managers operating through managed accounts and collective investment vehicles, including commodity pools. "X", "Y" and "Z" currently have approximately $92, $23 and $66 million in assets, respectively. By letter dated December 24, 1992 (the "Relief Letter"), subject to certain conditions[2/], the Division permitted "W" to file a Rule 4.7 notice of claim for exemption for "X".[3/] Pur-

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1/ Commission rules referred to herein are found at 17 C.F.R. Ch. I (1993).

2/ The Relief Letter is incorporated herein by reference. The relief was based upon the conditions that, among other things, "W" would follow the Rule 4.7(a)(3)(i)(I)(2) procedure for operating pools claiming relief under Rule 4.7, continue to provide the full protections of Part 4 to "X"'s non-QEPs and accept no additional non-QEPs as participants in "X".

3/ This notice was filed March 11, 1993.

suant to Advisory 2-93[4/], "W" filed a notice of claim for exemption under Rule 4.7 for "Y" on November 15, 1993 and for "Z" on March 14, 1994.

Many of the Pools' investment managers have elected to operate some of their pools as Rule 4.7 exempt pools. As a result, almost ten percent of "X"'s and "Z"'s assets are currently invested in Rule 4.7 exempt pools. After the conversion to Rule 4.7 exempt pool status of some pools in which "Y" was already invested, "Y" has approximately forty-nine percent of its assets invested in Rule 4.7 exempt pools. You expect more of the Pools' existing managers and many of the managers "W" may wish to engage as managers for the Pools to claim Rule 4.7 relief. The Pools are QEPs, as defined in Rule 4.7(a)(1)(ii)(B)(xi), but not all their participants are QEPs. Thus, absent exemption, the Pools may not invest more than ten percent of their assets in Rule 4.7 exempt pools.

You represent that a total of twenty-three participants in the Pools are not QEPs, and that all but eight of them were participants in the Pools prior to July 1, 1992, that is, prior to the date when Rule 4.7 became effective. These non-QEPs are as follows.

With respect to "X":

"C", a vice-president of "W" who has worked in the futures industry for fifteen years and is one of the principals of "W" responsible for allocating the assets of the "W" funds.

With respect to "Y":

1) An accredited investor with $4,000 invested in "Y". This non-QEP is the child of "A", himself a QEP and investor in "Y". "A" is a consultant to "W" who coordinates the marketing approach of "Y" and is intimately familiar with all aspects of "Y";

2) An accredited investor with $450,000 invested in "Y". This non-QEP is the adult child of a QEP of "Y"; and

3) An accredited investor with approximately $495,000 invested in "Y".

4/ Advisory 2-93 (January 7, 1993), which is based on the Relief Letter, permits other CPOs to claim relief from Rules 4.21 and 4.22 under Rule 4.7 for previously offered pools in which some participants are not QEPs, subject to conditions similar to those in the Relief Letter. See note 2 supra.

With respect to "Z":

1) An accredited investor with $430,000 invested in "Z". This non-QEP is the adult child of ""B", himself a QEP and investor in "Z". "B", the former general partner of "Z", is now a consultant to "W" for "Z";

2) An accredited investor with $250,000 invested in "Z". This non-QEP is the adult child of a QEP of "Z";

3) A non-accredited investor with approximately $260,000 invested in "Z". This non-QEP is the mother of a QEP of "Z"; and

4) A non-accredited investor with approximately $173,000 invested in "Z". This non-QEP is the mother-in-law of a pension plan consultant who has substantial futures expertise and a long-term business relationship with "W".

You claim that no existing non-QEP investor would be adversely affected if the Division grants the requested relief. This is because "W" complies, and will continue to comply, with the reporting and recordkeeping requirements of Rules 4.22 and 4.23, respectively, including the requirements of Rule 4.22 to provide quarterly and certified annual reports to the Pools' participants, and will provide existing participants and file with the Commission all amendments to the Pools' Disclosure Documents required by Rule 4.21(b). Accordingly, you request relief from the ten percent limitation on investments in Rule 4.7 exempt pools ("Investee Pools") by the Pools.

Based upon the representations you have made and subject to the conditions set forth below, the Division will not recommend that the Commission take any enforcement action against "W" or the CPO of any Investee Pool if the Pools invest more than ten percent of their assets in Investee Pools notwithstanding the participation of the non-QEPs discussed above. This relief is subject to the conditions that: (1) "W" continues to comply with the terms and conditions of the Relief Letter with respect to "X" and Advisory 2-93[5/] with respect to "Y" and "Z"; (2) no additional non-QEPs are admitted as participants in the Pools; and (3) "W" notifies the Pools' participants who are not QEPs that their Pool has invested or may invest over ten percent of its assets in Investee Pools that are operated pursuant to a grant of exemptive relief and provides them an opportunity to redeem their interests in the Pool within ten days of the receipt of such notice. The no-action relief granted herein does not waive or in any respect limit the Commission's authority to take action with respect to any past violation of the Commodity Exchange Act ("Act"), 7 U.S.C. § 1 et seq. (1988 & Supp. 1992), or the Commission's regulations issued thereunder.

5/ See notes 2 and 4 supra.

This letter is based on the representations provided to us. 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 "W" in connection with the Pools change in any way from those as represented to us. Further, this letter is applicable to "W" solely in connection with its operation of the Pools and to the CPOs of any Investee Pools solely in connection with the Pools' investment in them.

We note that this letter relieves "W" and the CPOs of Investee Pools solely from certain requirements of Rule 4.7 and does not excuse them from compliance with any other applicable requirements contained in the Act or in the Commission's regulations issued thereunder. For example, each remains subject to the antifraud provisions of Section 4o of the Act, 7 U.S.C. § 6o (1988 & Supp. 1992), 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 (1993), and to all other provisions of Part 4.

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.

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