U.S. COMMODITY FUTURES TRADING COMMISSION

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95-107

DIVISION OF
TRADING & MARKETS

November 22, 1995

Re: Request for Relief Under Rule 4.7

Dear :

This is in response to your letter dated April 21, 1995, as supplemented by letters dated May 4, 1995, June 27, 1995, July 14, 1995 and September 25, 1995 and telephone conversations with Division staff, in which you request on behalf of "R", a registered commodity pool operator ("CPO") and general partner of (the "Partnership"), confirmation that "R" may claim relief under Rule 4.7[1/] despite the fact that certain limited partners in the Partnership will not be qualified eligible participants ("QEPs"), as that term is defined in the rule. In addition, you request on behalf of the Partnership relief from the restriction in Rule 4.7(a)(1)(ii)(B)(2)(xi) (the "ten percent restriction") that would prevent the Partnership, as a pool with non-QEP participants, from investing more than ten percent of its assets in other pools for which the CPOs thereof have claimed relief under Rule 4.7 ("Rule 4.7 exempt pools").[2/]

(a) General Representations.

Based upon the representations made in your correspondence, we understand the pertinent facts to be as follows. "R" is a closely

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1/ Commission rules referred to herein are found at 17 C.F.R. Ch. I (1995), as amended by 60 Fed. Reg. 38,146 (July 25, 1995).

2/ During a telephone conversation with Division staff on November 16, 1995, you withdrew your request in connection with the following potential investors in the Partnership: "C", "D", "E", "F", "G", "H", "I" and "J", and "K".

held corporation owned equally by "A" and "B".[3/] "R" is the general partner of the Partnership.

The Partnership is a fund of funds. None of the funds in which the Partnership invests will have significant exposure to commodity futures or commodity options contracts, although such funds may trade such commodity interests in a manner solely incidental to their securities trading activities. With the possible exception of certain persons described more fully in Section (b) below (the "Non-QEP LPs"), interests in the Partnership will be sold only to limited partners qualifying as QEPs, as defined in Rule 4.7. It is anticipated that total assets in the Partnership will be in excess of $5 million. In addition, you state that the Partnership may on occasion wish to invest more than ten percent of the fair market value of its assets in Rule 4.7 exempt pools.

Finally, you represent that if the relief requested herein is granted, each of the Non-QEP LPs will be required to consent to being treated as a QEP and to a waiver of the ten percent restriction and will be notified that more than ten percent of the fair market value of the assets of the Partnership may be invested in Rule 4.7 exempt pools.

(b) Non-QEP LPs.

Based on responses to questionnaires submitted by prospective limited partners, you have determined that the following persons do not qualify as QEPs. You claim that the potential investors who are non-QEPs possess the financial sophistication, investment experience and educational backgrounds necessary for them to fully evaluate the merits and risks of an investment in the Partnership. Accordingly, "R" desires to allow these persons to invest as limited partners in the Partnership. You describe the potential Non-QEP LPs as follows:

1. The "S" Trust, which has total assets of approximately $4 million, predominately invested in securities. The sole beneficiary and trustee of the trust is "L", who is a QEP. "L" makes all investment decisions for the trust.

2. The "U", which has total assets of approximately $3.7 million, predominately invested in securities. The sole

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3/ "A" and "B" are also the sole shareholders of "T", an investment consulting firm to over fifty clients with substantial assets under management. "T" is a registered investment adviser under the Investment Advisers Act of 1940.

beneficiary and trustee of the trust is "M", who is a QEP. "M" makes all investment decisions for the trust.

3. The "V" Foundation, which is a tax-exempt foundation that was founded by "L" and provides gifts and grants to charities involved in the arts or education. The foundation has assets of approximately $900,000. "L", a QEP, has primary responsibility for making investment decisions for the foundation.

4. The "W" Trusts, which consist of three irrevocable trusts created by "N" for the benefit of his two minor children for estate planning purposes. The total combined assets of the trusts are $700,000. "N's" brother, "O", is the trustee for all three trusts. "N" introduces investment ideas to his brother, but "O" makes all investment decisions for the trusts. Both "N" and "O" are QEPs.

5. "X", a limited partnership formed as an investment vehicle solely for the family members of "P", which owns securities with a fair market value of approximately $1.8 million. It currently has seven partners -- "P", his wife and their five children. "P", the general partner of "X", is a QEP and makes all investment decisions for "X".

6. The "Y" Foundation, a charitable foundation with assets of approximately $500,000. It has broad discretion to make gifts and grants, and was founded by "Q" and his father. "Q" is a QEP and makes all investment decisions for the foundation.

7. "A", who is co-founder and the managing director of "R", the Partnership's CPO. He is actively involved in the day-to-day operations of "R", including serving on its Investment Committee, selecting managers and monitoring results of its investment partnerships. "A" is an accredited investor as defined in Rule 501 of Regulation D under the Securities Act of 1933.[4/]

8. "RR", who is the President and Secretary of "R" and a member of its Investment Committee. He is actively involved in the day-to-day operations of "R" and has been employed by "R" for approximately one year. Before joining "R", "RR" was a Senior Tax Consultant with "Z" for over three years, and was an attorney "UU" where he

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4/ 17 C.F.R. § 230.501 (1995).

specialized in the taxation of new investment products offered by insurance companies, for three years.

9. "SS", who is the Vice President of "R". He has worked at "R" since its inception in 1990 and has been employed by the principals of "R" since his graduation from college in 1986. He is actively involved in the selection and monitoring of all money managers for "R". He is a member of the Partnership's Investment Committee.

10. "TT", who has been a consultant to "R" since its inception in 1990 and served on its board of directors from its inception until the end of 1991.[5/] "TT" has a Doctorate in Finance and Investments and is a Charted Financial Analyst. He was an assistant professor for over ten years and taught securities analysis, statistics and corporate finance. "TT" is an accredited investor.

(c) Relief.

Based upon the foregoing, it appears that granting the requested relief would not be contrary to the public interest and the purposes of Rule 4.7. Accordingly, subject to the conditions stated below, the Division will not recommend that the Commission take any enforcement action against: (i) "R" if "R" files a Rule 4.7(a) claim for exemption as the CPO of the Partnership, notwithstanding the participation in the Partnership of any of the Non-QEP LPs described in Section (b) above, and treats such Non-QEP LP as a QEP;[6/] and (ii) the CPO of any Rule 4.7 exempt pool in which the Partnership is or becomes a participant based solely upon the Partnership's investment of more than ten percent of the Partnership's assets in a Rule 4.7 exempt pool. This relief is subject to the conditions that each Non-QEP LP consents to being

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5/ In his role as consultant, "TT" has been primarily involved in conducting due diligence reviews for various hedge funds. Currently, "TT" serves as a consultant to "R" on a periodic basis.

6/ We note that we have granted similar relief to persons whose situations were similar to those of many of the non-QEP investors described in your letter. See, e.g., CFTC Interpretative Letter No. 94-13, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,994 (December 27, 1993) (Non-QEP trust where sole trustee and beneficiary is a QEP may be admitted to exempt pool and treated as QEP); CFTC Interpretative Letter No. 94-56, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,120 (May 6, 1994)(non-QEPs involved in day-to-day operations of an exempt pool's CPO may invest in exempt pool and be treated as QEPs).

treated as a QEP and that "R" notifies all Non-QEP LPs, before such Non-QEP LPs are allowed to invest in the Partnership, that the Partnership may invest more than ten percent of its assets in pools that are operated pursuant to a Rule 4.7 exemption.

This letter is based upon the representations made to us and is subject to compliance with the conditions stated 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 if the operations or activities of the Partnership, "R" or the other persons and entities referred to above change in any way from those represented to us. Further, this letter is applicable to "R" solely in connection with its operation of the Partnership and to the CPOs of Rule 4.7 exempt pools in which the Partnership is a participant solely in connection with the Partnership's participation therein.

We note that this letter relieves "R" solely from certain requirements of Rule 4.7 and does not excuse it from compliance with any other applicable requirements contained in the Commodity Exchange Act ("Act")[7/] or in the Commission's regulations issued thereunder. For example, "R" remains subject to the antifraud provisions of Section 4o of the Act,[8/] to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission regulations, and to all other applicable requirements of Part 4.

This letter represents the views of the Division only and does not necessarily represent the views of the Commission or any other office or division of the Commission. If you have any questions concerning this correspondence, please contact me or Thomas E. Joseph, an attorney on my staff, at (202)418-5450.

Very truly yours,

Susan C. Ervin
Chief Counsel

7/ 7 U.S.C. § 1 et seq. (1994).

8/ 7 U.S.C. § 6o (1994).