

95-05



COMMODITY FUTURES TRADING COMMISSION

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DIVISION OF  
TRADING AND MARKETS

December 29, 1994

Re: Rule 4.7(a) -- Request That Non-QEP Pool  
Participants Be Deemed QEPs For Pool To  
Obtain Rule 4.7(a) "Exempt Pool" Treatment

Dear :

This is in response to your letter dated November 15, 1994, as supplemented by additional information provided by letter on December 21, 1994, and by telephone conversations with "A", your counsel. In your letter, you requested that the Division of Trading and Markets ("Division") of the Commodity Futures Trading Commission ("Commission") grant relief to (the "Limited Partnership Pool")<sup>1/</sup> and (the "General Partner") under Rule 4.7(a) adopted pursuant to the Commodity Exchange Act, 7 U.S.C. §§ 1 et seq. (1988 & Supp. IV 1992) (the "Act").<sup>2/</sup> Specifically, you requested that certain investors in the Limited Partnership Pool who are not "qualified eligible participants" ("QEPs") under Rule 4.7(a) (1) (ii) be deemed such so that the Limited Partnership Pool may be treated as an "exempt pool" by the General Partner under Rule 4.7(a) (1) (i).<sup>3/</sup>

<sup>1/</sup> Formerly, the Limited Partnership Pool was named "X".

<sup>2/</sup> Commission rules referred to herein are found at 17 C.F.R. Ch.I (1994).

<sup>3/</sup> Preliminarily, we note that by letter dated April 28, 1994, the Division granted relief to the Limited Partnership Pool from regulation as a commodity pool operator in connection with its operation of two partnerships referred to as the operating partnerships (the "Operating Partnerships"): (the "U.S. Operating Partnership") and (the "Cayman Operating Partnership"). These Operating Partnerships, are solely owned, for all practical purposes, by the Limited Partnership Pool, the only other owner being an affiliated entity holding only a nominal interest, for the sole purpose of permitting the Operating Partnerships to have a legal existence.

Based upon the representations made in the letters, as supplemented by telephone conversations with Division staff, we understand the relevant facts to be as follows. The Limited Partnership Pool, through its Operating Partnerships, invests in securities and commodity interest contracts. You specifically represented that a very small part of the overall business of the Limited Partnership Pool was the purchase and sale of commodity interest contracts, and certain transactions were hedging transactions: "As of September 30, 1994, less than 0.5% of the fair market value of the Pool's assets were represented by initial margin and premiums paid for commodity futures and commodity option contracts."<sup>4/</sup> Contracts in commodity interests in which the Limited Partnership Pool, through its Operating Partnerships, trades are primarily contracts on U.S. and European government securities. Some are contracts on financial indices and oil and metals.

The Limited Partnership Pool has been deemed to be a commodity pool. The General Partner is registered as a commodity pool operator ("CPO"). All Limited Partnership Pool participants received their interests pursuant to a private placement in accordance with Section 4(2) of the Securities Act of 1933.

Limited Partnership Pool participants are of two types: those holding limited partnership interests ("Limited Partners") and those with special limited partnership interests ("SLPs"). There are currently 38 Limited Partners, 37 of whom are also QEPs. None of the 11 SLPs are QEPs.

1 Limited Partner Who Is Not a QEP. The one Limited Partner, a natural person who is not a QEP, is an "accredited investor" as defined in Rule 501(a)(1) of Regulation D, adopted pursuant to the Securities Act of 1933.<sup>5/</sup> In addition, he manages the investment of one of the four founding Limited Partners of the Limited Partnership Pool. In view of his experience and status as an accredited investor, it is not inappropriate to grant the relief requested under Rule 4.7 as to this Limited Partner, provided he consents in writing to being treated as a QEP.

11 SLPs Who Are Not QEPs. The SLPs are each employees of the Limited Partnership Pool who received their SLP interests as bonus compensation. Pursuant to the terms of the Limited Partnership Agreement ("LP Agreement") with the Limited Partnership Pool, the

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<sup>4/</sup> Note 2, letter dated November 15, 1994.

<sup>5/</sup> The rules of the Securities Exchange Commission adopted pursuant to the Securities Act of 1933 and referenced herein are found at 17 C.F.R. Part 230 (1994).

SLPs are granted to employees at the discretion of the General Partner. Under the LP Agreement, an employee does not choose to receive such an SLP interest. Moreover, the LP Agreement provides that an employee does not have a vested right to the principal amount of such SLP interest until four years after it is granted, except in the event of the employee's death or termination of employment without cause.

a. 5 SLPs Have Not Contributed Any of Their Own Capital.

As noted above, none of the SLPs has a choice in receiving such bonus compensation. In addition, an SLP does not possess a vested right to such capital until a substantial period of time has passed, in the absence of extraordinary circumstances. In this regard, the bonus compensation package these SLPs receive is somewhat analogous to the financial interest an employee holds in a non-contributory pension plan, whether a defined benefit or defined contribution plan, covered under Title I of the Employee Retirement Income Security Act of 1974. Under Rule 4.5(a)(4), such plans are specifically excluded from the "pool" definition in Rule 4.10(d) and, therefore, the operators of such plans are excluded from the definition of "commodity pool operator". Given that these SLPs' interests and those defined in Rule 4.5 are analogous, and the factual representations of the General Partner with respect to the Limited Partnership Pool, it is not inappropriate to grant the relief requested under Rule 4.7 as to these 5 holders of SLPs, provided that each of the 5 holders of SLPs consents in writing to being treated as a QEP.

b. 6 SLPs Have Voluntarily Contributed Their Own Capital In Addition to Monies Contributed to the Limited Partnership Pool By Their Employer.

Six other persons are holding SLPs which represent, or in the past represented, in part, their personal, voluntary capital contributions to the Limited Partnership Pool. However, these SLPs have credentials, professional expertise in securities and/or commodity interest trading and access to information on a day-to-day basis on the operations of the Limited Partnership Pool as executives of the Limited Partnership Pool.<sup>6/</sup> Five executives of the Limited Partnership Pool are also persons who have invested in the Limited Partnership Pool

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<sup>6/</sup> For example, each of these persons has passed one or more commodities or securities licensing examinations and, with the exception of the commodity interest trader discussed below, have been employed by the Limited Partnership Pool for a minimum of 2.33 years.

limited amounts of their personal assets relative to their individual net worth. In each instance, the personal investment in the Limited Partnership Pool totalled less than seven percent (7%) of the person's net worth. The sixth person is intimately involved on a daily basis with assessing the risks of futures and commodity options trading; he is the risk analyst and commodity trader for the Limited Partnership Pool's Operating Partnerships. He has passed the Series 3 examination for registration with the National Futures Association, Inc., the Series 4 and 7 examinations for registration with the National Association of Securities Dealers, Inc., and the Series 63 examination for registration under state blue sky laws. Given the experience in the securities and commodities industry and the access to information that these 6 persons, as executives of the Limited Partnership Pool, have with respect to the Limited Partnership Pool, it is not inappropriate to grant the relief requested under Rule 4.7 as to these 6 holders of SLPs, provided that each of the 6 holders of SLPs consents in writing to being treated as a QEP.

As noted above, provided that each of the persons not QEPs will consent in writing to their being treated as QEPs, the Division will not recommend that the Commission take any enforcement action against the General Partner if it files a Rule 4.7(a) notice of claim for exemption as the CPO of the Limited Partnership Pool, notwithstanding the participation of the non-QEP participants discussed above. This is subject to the conditions that the General Partner comply with Rule 4.7(a)(3)(i)(I)(2) for previously offered pools.<sup>7/</sup>

This letter is based on the representations made in your letters, as supplemented, and is subject to compliance with the conditions set forth above. Any different, changed or omitted facts or circumstances might cause us to reach a different conclusion. In this connection, we request that you notify us immediately in the event that (i) the number, type or status of non-QEP participants changes, or (ii) the General Partner changes its operations or activities with respect to the Limited Partnership Pool. Moreover, this relief is applicable only to the General Partner in connection with its operation of the Limited Partnership Pool.

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<sup>7/</sup> See Interpretative Letter 93-1 [1992 - 1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) para. 25,531 (December 10, 1992) and CFTC Advisory 93-2 [1992 - 1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) para. 25,935 (January 7, 1993).

The relief issued by this letter does not excuse the General Partner from compliance with any other applicable requirements contained in the Act or the Commission's regulations thereunder. For example, the General Partner remains subject to the antifraud provisions of Section 40 of the Act,<sup>8/</sup> to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations, and to all other provisions of Part 4. The no-action relief provided herein is prospective only.

Finally, this letter represents the position of the Division of Trading and Markets only. It does not necessarily reflect the views of the Commission or any other office or division of the Commission. If you have any questions regarding this letter, please contact me or Sharon Zackula, a member of my staff, at (202) 254-8955.

Very truly yours,

Susan C. Ervin  
Chief Counsel

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<sup>8/</sup> 7 U.S.C. § 60 (1988 & Supp. IV 1992).