U.S. COMMODITY FUTURES TRADING COMMISSION

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DIVISION OF
TRADING & MARKETS

96-20

February 27, 1996

Re: Rule 4.7(a); -- Request To Treat Certain Investors As Qualified Eligible Participants

Dear :

This is in response to your letter dated January 17, 1996, as supplemented by telephone conversations with Division staff, in which you request on behalf of "P" a registered commodity pool operator ("CPO")[1/] and general partner of (the "Fund"), confirmation that "P" may continue to claim relief under Rule 4.7[2/] with respect to its operation of the Fund despite the fact that certain investors in the Fund are not qualified eligible participants ("QEPs"), as that term is defined in the rule. In addition, you request on behalf of "P" relief from the restriction in Rule 4.7(a)(1)(ii)(B)(2)(xi) (the "ten percent restriction") which would prevent the Fund, 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").

The Fund has been operating on a "proprietary" basis since June 1994,[3/] but was opened to outside, "non-proprietary"

1/ Our records indicate that "P" is also registered with the Commission as a commodity trading advisor ("CTA"). Further, our records indicate that "P's" registration as both a CPO and CTA was effective on April 3, 1995.

2/ 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).

3/ You use "proprietary" to indicate that all investors in the Fund were employees or officers of "P" or of its affiliated companies, "Q", a registered CTA and CPO and a listed principal of "P", or "R", which is also a listed principal of "P", or relatives of such persons. Since all investors in the Fund were affiliated with "P" or its principals, "P" did not believe that the Fund was a "pool" as that term is defined in Rule 4.10(d)(1). The Division

(continued...)

investors effective January 1, 1996. Our records indicate that a notice of claim of exemption for the Fund under Rule 4.7 was filed with the Commission effective December 27, 1995. You indicate that except for certain investors, who had invested in the Fund prior to January 1, 1996 and are described more fully below ("the Non-QEP Investors"), all investors in the Fund will be QEPs as that term is defined in Rule 4.7(a).[4/] Accordingly, you are requesting that Division confirm that "P" will be able to treat the Non-QEP Investors as QEPs and to continue to claim relief under Rule 4.7(a) in connection with its operation of the Fund.

You represent that the Non-QEP Investors are as follows:

1. "A", who is the President of "R" and who has been associated with "R" since its founding in February 1994. "A", and two other "R" officers, make all investment decisions for

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3/ (...continued)
is noting "P's" view of the status of the Fund prior to January 1, 1996 for the purposes of clarifying the facts presented by your letter. By noting these facts, the Division is neither accepting nor rejecting "P's" interpretation of the Fund's pool status. Moreover, any relief granted by this letter would not prevent the Commission from taking action against "P" should it be determined that the Fund was a pool as that term is defined in Rule 4.10(d)(1) prior to January 1, 1996.

4/ We note that "P" filed its notice of a claim for exemption for the Fund despite the fact that certain investors were not QEPs and that "P" had not yet obtained relief to admit such investors to a Rule 4.7 exempt pool. Moreover, "P's" notice of a claim of exemption does not meet the criteria of the Division's Advisory concerning Rule 4.7 relief for pools with non-QEP investors since the notice did not contain the required statement indicating that the pool included non-QEP investors. See, CFTC Advisory for Interpretative Letters Nos. 93-1 and 93-2 (Two Interpretative Letters Concerning Rule 4.7 Relief for Pools with Non-QEPs), [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,935 (January 7, 1993).

In this regard, we note that the relief granted below does not prevent the Commission from taking action against "P" or any person connected therewith for any violation of the Commodity Exchange Act ("Act"), 7 U.S.C. § 1 et seq. (1994), or Commission rules promulgated thereunder that may arise from filing an inadequate notice of a claim of exemption under Rule 4.7. We further note that, notwithstanding the foregoing, it is not necessary for "P" to file a new notice of a claim of exemption for the Fund.

the Fund. From 1988 to 1994, "A" was a vice president of "S". Prior to 1988, he was employed for five years at "T". "A" graduated summa cum laude with a degree in accountancy. He is a certified public accountant ("CPA") and an accredited investor, as defined in Rule 501 under the Securities Act of 1933. Our records indicate that "A" is a registered associated person ("AP") and listed principal of "P".

2. "B", who has been an officer of "Q" since January 1992 and has been associated with that firm since March 1991. He is also a Vice President and the Assistant Secretary of "R". "B" is responsible for the administrative management of all of "Q's" investment Funds. He also has overall supervisory and management responsibility for the Fund. "B" received a J.D. degree cum laude from School of Law in 1987 and an undergraduate degree summa cum laude in accountancy. He is a CPA, a member of the bar and an accredited investor. Our records indicate that "B" is a registered AP and listed principal of "P", "Q" and "U".[5/]

3. "C", who is Director of Research for all of "Q's" investment funds. Although "C" is not directly involved in research for the Fund, he is consulted by persons responsible for the investment research for the Fund and has access to all information concerning the Fund and its investments. From 1986 until joining "Q" in 1994, "C" was Managing Director of "V", a software firm specializing in options analytic software and portfolio risk management systems for Wall Street firms. Prior to founding that company, he worked as a financial consultant and as a financial systems analyst. "C" received an M.B.A. in finance. He is an accredited investor. Our records indicate that "C" is a registered AP and listed principal of "Q".

5/ "U" is registered as both a CPO and CTA, and is a listed principal of "Q".

4. "D", who has been an analyst with "P" since the firm's inception in June 1994. "D", along with "E" (below), researches all potential investments by the Fund. His duties include reviewing relevant documentation and information concerning possible investments, visiting the operations and sites of possible investment targets, running any necessary calculations, and reporting any findings or recommendations to the persons responsible for making investment decisions on behalf of the Fund. From 1989 through 1991, he was an analyst for "W". He received a B.A. in economics from University in 1989, and an M.B.A. in real estate development from the University in 1993. "D" is an accredited investor.

5. "E", who has been employed as an analyst with "P" since January 1995. Along with "D" (above), "E" is responsible for conducting research concerning potential investments for the Fund. His duties are the same as those described for "D". "E" was a vice president with "X", from October 1993 until joining "P". From 1991 until October 1993 he was an Acquisitions Associate with "Z". He received a B.S. in economics.

6. "F", who is responsible for marketing at "Q" and who joined "Q" in 1992. He is in the process of becoming registered as an AP of "P". Once this registration becomes effective, his responsibilities will include finding outside investors for the Fund and making presentations concerning the Fund to potential investors. Because of these duties, he will have full access to information concerning the Fund including current information on the Fund's performance and the Fund's investment strategy. From 1988 to 1991, he was Vice President of "Z". Prior to joining "Z", "F" was Staff Assistant to the Undersecretary of the United States Department of Housing and Urban Development. He received a B.A. in Economics with honors in 1984. Our records indicate that "F" is a registered AP of "Q" and a registered AP and listed principal of "U".

Based upon the foregoing, it appears that granting the requested relief would not be contrary to the public interest and the purpose 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) "P" if the Non-QEP Investors remain investors in the Fund, and "P" treats each non-QEP investor as a QEP; and (ii) "P" or the CPO of any Rule 4.7 exempt pool in which the Fund is or becomes a participant based solely upon the Fund's investment of more than ten percent of the Fund's assets in a Rule 4.7 exempt pool. This relief is subject to the conditions that: (1) each Non-QEP Investor consents to being treated as a QEP; and (2) "P" notifies all Non-QEP Investors that the Fund 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 "P" or the Fund, including its membership composition, change in any way from those represented to us. Further, this letter is applicable to "P" solely in connection with its operation of the Fund and to the CPOs of Rule 4.7 exempt pools in which the Fund is a participant solely in connection with the Fund's participation therein.

We note that this letter relieves "P" solely from certain requirements of Rule 4.7 and does not excuse it from compliance with any other applicable requirements contained in the Act or in the Commission's regulations issued thereunder. For example, "P" remains subject to the antifraud provisions of Section 4o of the Act,[6/] 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

6/ 7 U.S.C. § 6o (1994).