

CFTC Letter No. 97-05**February 12, 1997****Division of Trading & Markets**

Re: Request for Relief from Registration as a Commodity Trading Advisor

Dear :

This letter is in response to your letter dated May 24, 1996, to the Division of Trading and Markets ("the Division") of the Commodity Futures Trading Commission (the "Commission"), as supplemented by your letters dated July 2, 1996, July 15, 1996, August 19, 1996, October 16, 1996, and January 31, 1997 as well as telephone conversations with Division staff. By your correspondence, you request relief from registration as a commodity trading advisor ("CTA") under Section 4m(1) of the Commodity Exchange Act (the "Act")¹ for "X", a Colorado corporation, in connection with providing advisory services to (the "Fund").

Based upon the representations made in your letter, as supplemented, we understand the facts to be as follows. The Fund is an exempted company with limited liability,² incorporated in the Cayman Islands, and will be operated as an offshore fund. The investment objective of the Fund is long-term capital appreciation through investments in equity securities. Interests in the Fund will not be offered, sold, or transferred to any United States person, as that term is defined in Rule 4.7.³ Interests in the Fund will only be offered to high net worth individuals and institutions. The minimum subscription will be \$250,000.

"A", the Chairman and President of "X", will sit as a director of the Fund on behalf of "X", but you represent that he "will not be involved in any aspect of portfolio management for the Fund." All other directors of the Fund will be non-United States persons. "X" owns neither voting nor participatory shares in the Fund. Moreover, "X" is not involved in marketing or soliciting participations in the Fund, nor is it involved in administrative matters or distribution of shares for the Fund.⁴

"X" is not registered with the Commission in any capacity,⁵ but is registered with the Securities and Exchange Commission ("SEC") as an investment adviser under the Investment Advisers Act of 1940, and as such, provides investment advice to a number of companies registered with the SEC. "X" provides commodity interest trading advice to the Fund that is intended to be solely incidental to its business of providing securities advice to the Fund. Commission Rule 4.14(a)(8) provides an exemption from registration as a CTA for an investment adviser registered under the

Investment Advisers Act of 1940 ("IAA") that provides commodity interest trading advice that (i) is solely incidental to its business of providing securities advice, (ii) is directed solely to, or for the sole use of, entities which are excluded from the definition of the term "pool" under Section 4.5 or are qualifying entities under Section 4.5; and (iii) employs only such strategies as are consistent with eligibility status under Section 4.5. The Fund, because of its foreign nature, will not (and absent an exemption from the SEC, cannot) register as an investment company under the Investment Company Act of 1940. Thus, it is neither an "otherwise regulated entity" nor a "qualifying entity" as specified in Rule 4.5. Consequently, "X" cannot rely on an exemption from CTA registration under Rule 4.14(a)(8). Nonetheless, you state that the Fund seeks to use commodity interest contracts and "X" seeks to provide commodity interest trading advice in a manner consistent with eligibility status under Rules 4.5 and 4.14(a)(8).

In support of your request, you represent that the Fund will be operated in a manner consistent with Rule 4.5(c)(2) and, specifically, will use commodity futures and commodity option contracts solely for bona fide hedging purposes within the meaning and intent of Rule 1.3(z)(1), or to the extent that such positions do not come within the meaning and intent of Rule 1.3(z)(1), the aggregate initial margin and premiums required to establish such positions will not exceed five percent of the liquidation value of the Fund's portfolio, after taking into account unrealized profits and losses on any such contracts it has entered into. You also represent that "X", in accordance with certain requirements of Rule 4.14(a)(8): (1) will provide commodity interest trading advice to the Fund in a manner solely incidental to its furnishing of securities advice to the Fund; (2) will employ only those strategies which are consistent with eligibility status under Rule 4.5 (c)(2); and (3) will not otherwise hold itself out as a CTA.

Based upon our review of this matter, it appears that granting the requested relief would not be contrary to the public interest and the purposes of the Commodity Exchange Act ("Act").⁶ Accordingly, based upon the foregoing representations, and consistent with our prior practice in this area,⁷ the Division will not recommend that the Commission take any enforcement action against "X" for a violation of Rule 4.14(a)(8)(i)(A) or the registration requirements of Section 4m (1) of the Act based solely upon its offering of commodity trading advice to the Fund if it continues to rely on the CTA registration exemption under Rule 4.14(a)(8) to offer commodity trading advice to the Fund. This position is subject to the condition that "X" will submit to such special calls as the Division may make to demonstrate compliance with the terms and conditions of this "no-action" position.

The views stated herein are based, in part, upon your representations that: (1) the Fund is organized outside of the United States and shares in the Fund will not be owned or transferred to any United States person; (2) the Fund's stated investment strategy is to invest primarily in equity securities; (3) "X" is already highly regulated due to its registration with the SEC as an investment adviser under the Investment Advisers Act of 1940; (4) the Fund will be operated in a manner consistent with Rule 4.5(c)(2); and (5) "X", which is registered as an investment adviser under the IAA, will comply with the requirements of Rule 4.14(a)(8) with respect to the manner in which

commodity interest trading advice is rendered to the Fund.

The relief granted by this letter does not excuse "X" from compliance with any other applicable requirements contained in the Act or the Commission's regulations issued thereunder. For example, it remains subject to the antifraud provisions of Section 40 of the Act,⁸ the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations, and all other applicable provisions of Part 4.

This letter is based upon the representations that you have 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 regard, we request that you notify us immediately in the event that the operations or activities of "X" or the Fund change in any way from those as represented to us. Moreover, this letter represents the position of the Division only, and does not necessarily represent the views of the Commission or any other division or office of the Commission.

If you have any questions concerning this correspondence, please contact me or Monica S. Amparo, an attorney on my staff, at (202) 418-5450.

Very truly yours,

Andrea M. Corcoran

Director

¹ 7 U.S.C. § 6m(1) (1994).

² You represent that under the laws of the Cayman Islands investment funds are organized as "exempted companies." Such companies are exempt from certain of the requirements of the Companies' Law and are entitled to obtain a tax exemption certificate.

³ Commission rules referred to herein are found at 17 C.F.R. Ch. I (1996).

⁴ Based on your representations, it does not appear that "X" acts as the commodity pool operator of the Fund.

⁵ Our records indicate that "X" filed a claim of exemption from registration as a CTA pursuant to Rule 4.14(a)(8), effective May 13, 1994.

⁶ 7 U.S.C. § 1 et seq. (1994).

⁷ See Division of Trading and Markets Interpretive Letter No. 95-77, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,523 (July 10, 1995). [Fund would be operated in a manner consistent with Rule 4.5(c)(2) and would use commodity interests solely for bona fide hedging purposes, or to the extent that such positions did not constitute bona fide hedging, then no more than five percent of the Fund's portfolio would be devoted to speculative positions.]

⁸ 7 U.S.C. § 60 (1994).