

**CFTC Letter No. 97-30****April 21, 1997****Division of Trading & Markets**

Re: Commodity Exchange Act Section 4m(1) -- Request for Commodity Pool Operator Registration Relief in Connection with the Operation of "P" Whose Limited Partners are Current or Former Commission Registrants or Chicago Board Options Exchange Members

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Dear :

This is in response to your letter dated July 17, 1996 to the Division of Trading and Markets (the "Division") of the Commodity Futures Trading Commission (the "Commission"), as supplemented by your memorandum dated January 21, 1997, and by telephone conversations with Division staff. By your correspondence you request on behalf of "O", a registered futures commission merchant ("FCM"), and "P", a registered broker-dealer and member of the Chicago Board Options Exchange ("CBOE"), confirmation that (1) "P" is not a commodity pool; and (2) "Q", in its capacity as general partner of "P", is not required to register as a commodity pool operator ("CPO").<sup>1</sup>

Based upon the representations made in your correspondence, we understand the relevant facts to be as follows. "P", an Illinois limited partnership, is registered with the Securities and Exchange Commission ("SEC") as a broker-dealer. The sole general partner of "P" is "Q", which is owned by "A" and "U".<sup>2</sup> In addition to being a member of the Chicago Mercantile Exchange ("CME"), "A" is a registered floor broker, an accredited investor as defined in Regulation D<sup>3</sup> under the Securities Act of 1933,<sup>4</sup> a qualified eligible participant ("QEP") as defined in Rule 4.7(a), and a listed principal of three other Commission registrants.<sup>5</sup> "B" and "C" are co-trustees of "U". "B" is a former CBOE member, an accredited investor and a QEP. "C" is a registered floor trader.<sup>6</sup> The five limited partners of "P" are: "A"; "U"; "D", a former CBOE member, accredited investor and QEP; "E", also a former CBOE member, accredited investor and QEP; and "C".<sup>7</sup>

"P" acts as a market maker on the CBOE, trading through its nominee, "F".<sup>8</sup> "Q" and "A" are responsible for "P's" trading decisions. Its trading activity is primarily in Standard & Poor's 100 Index ("OEX") options on the CBOE. "P" hedges its OEX option positions with Standard & Poor's 500 Index ("SPX") futures positions on the CME. "P" occasionally trades futures contracts on United States Treasury instruments on the Chicago Board of Trade. You acknowledge that while the latter trades may not qualify as bona fide hedging transactions within the meaning of Commission Rule 1.3(z), "P" considers such trading to be part of its risk management program. At

various times, as much as forty percent of "P's" total equity has been used for initial margin for commodity interest trading. "P" maintains a trading account at "O" for trading SPX futures contracts.

In support of your request you state, among other things, that: (1) "Q" does not solicit investors in "P" nor will any additional investors be accepted in "P"; (2) none of the partners of "P" is in need of the protections afforded by Part 4 of the Commission's regulations; (3) no management fee is paid by "P" or its investors to "Q" or to any other person; and (4) none of "A" or "B", "D", "E", "C", "Q" or "P" is subject to statutory disqualification pursuant to Section 8a(2) or 8a(3) of the Commodity Exchange Act (the "Act").<sup>9</sup>

Section 1a(4) of the Act defines "commodity pool operator" as follows:

The term "commodity pool operator" means any person engaged in a business that is of the nature of an investment trust, syndicate, or similar form of enterprise, and who, in connection therewith, solicits, accepts, or receives from others, funds, securities, or property, either directly or through capital contributions, the sale of stock or other forms of securities, or otherwise, for the purpose of trading in any commodity for future delivery or commodity option on or subject to the rules of any contract market, except that the term does not include such persons not within the intent of the definition of the term as the Commission may specify by rule, regulation or order.<sup>10</sup>

Rule 4.10(d)(1) defines a pool as "any investment trust, syndicate or similar form of enterprise operated for the purpose of trading commodity interests."

Inasmuch as capital contributed by its partners is used to trade commodity interests, "P" is a pool and its general partner is a commodity pool operator. Nevertheless, based upon the representations made in your correspondence, we believe that your request has merit. Accordingly, the Division will not recommend that the Commission take any enforcement action against "Q" as general partner of "P" solely for failure to register as a CPO in accordance with Section 4m(1) of the Act<sup>11</sup> and to comply with the disclosure, reporting and recordkeeping requirements of Commission Rules 4.21 through 4.26 in connection with the operation of "P". This position, however, is subject to the conditions that: (1) "P" remains duly registered as a securities broker-dealer; (2) no solicitation of additional limited partners or investors of "P" is conducted and no additional limited partners or investors are admitted into "P" or "Q"; and (3) the trading of commodity interests by "P" remains limited to hedging and risk management in connection with CBOE option positions.

This letter is applicable to "Q" solely in connection with the operation of "P". Furthermore, this letter does not excuse "Q" from compliance with any other applicable requirements contained in the Act or in the Commission's regulations issued thereunder. For example, it remains subject to

the antifraud provisions of Section 40 of the Act<sup>12/</sup> and to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations. The no-action relief provided herein is prospective only, and the Division is not excusing, or in any way limiting, the Commission's ability to proceed against "Q" for any past violations of the Act or the Commission's regulations promulgated thereunder.

This letter is based upon 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 that: (1) the operations or activities of "Q" or "P" including their respective principals or limited partners, change in any way from those represented to us; or (2) "T" resumes trading.

Further, this letter represents the position of the Division of Trading and Markets only. It does not necessarily reflect the views of the Commission or of any other division or office of the Commission. If you have any questions concerning this correspondence, please contact me or Christopher W. Cummings, an attorney on my staff, at (202) 418-5445.

Very truly yours,

Susan C. Ervin

Chief Counsel

<sup>1</sup> You have provided the Division with a copy of a letter dated January 16, 1997 to you from "A" on behalf of "Q" authorizing you to submit this request and to make representations on behalf of "Q" as general partner of "P". Your July 17, 1996 letter also sought confirmation that "R" (since renamed "S" and referred to herein as "T"), also a registered broker-dealer and CBOE member, was not a commodity pool and that "T's" general partner was not required to register as a CPO. "T" has since ceased operations and you have withdrawn your request with respect to "T".

<sup>2</sup> "U" was established by "A" for the benefit of his father, "B". "B" is a principal and an owner of "Y", a former CBOE member and broker-dealer, which is not an active company at this time.

<sup>3</sup> 17 C.F.R. 230.501 (1996).

<sup>4</sup> 15 U.S.C. § at et seq. (1994).

<sup>5</sup> "A" is listed as a principal of "V" (a registered introducing broker ("IB")), "W" (a registered CPO), and "W" (also a registered CPO).

<sup>6</sup> "C" has been registered as a floor trader for more than three years, and he was formerly listed as

a principal of "V" (a registered IB of which "A" is currently a principal). "C" holds an IDEM (index, debt and energy markets) seat on the Chicago Board of Trade.

<sup>7</sup> "D" traded on the CBOE for thirteen years and "E" did so for fourteen years.

<sup>8</sup> "F" is registered with the Commission as a floor broker.

<sup>9</sup> 7 U.S.C. § 12a(2) or § 12a(3) (1994).

<sup>10</sup> 7 U.S.C. § 1a(4) (1994).

<sup>11</sup> 7 U.S.C. §§ 6m(1) (1994).

<sup>12</sup> 7 U.S.C. § 6o (1994).