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DIVISION OF
TRADING & MARKETS

April 29, 1997

Re: Section 4m(1) -- Request of "J" on behalf of its subsidiary "L" for relief from the requirement to register as a commodity pool operator ("CPO") in connection with "L's" acquisition of the general partner interests in three investment partnerships, one of which invests assets in partnerships that trade commodity interests, and the simultaneous acquisition by another "J" subsidiary of the investment adviser to such investment partnerships.

Dear :

This is in response to your letter dated April 15, 1997 to the Division of Trading and Markets (the "Division") of the Commodity Futures Trading Commission (the "Commission"), as supplemented by telephone conversations with Division staff. On behalf of "J", you request relief from the requirement of Section 4m(1) of the Commodity Exchange Act (the "Act")[1] to register as a commodity pool operator ("CPO") as applicable to "J's" subsidiary "L" in connection with a proposed transaction by which "L" will succeed to the general partner interests in certain limited partnerships (the "Investment Partnerships"), and another "J" subsidiary ("K"), will acquire the assets of the investment adviser to the Investment Partnerships. A portion of the assets of one of the Investment Partnerships is invested in partnerships engaged in commodity interest trading.[2]

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[1] 7 U.S.C. § 6m(1) (1994).

[2] Although you have not sought relief on behalf of "K" from the requirement to register as a commodity trading advisor ("CTA") we believe that under the circumstances you describe, either registration or relief from the requirement to register is

Based upon the representations made in your correspondence, we understand the relevant facts to be as follows.

The Acquiring Companies.

"J" is a bank holding company registered under the Bank Holding Company Act of 1956[3] and subject to supervision and regular inspection by the Board of Governors of the Federal Reserve System. "K" is a national bank supervised by the Office of the Comptroller of the Currency ("OCC") and wholly-owned by "J" through an intermediate holding company.[4] "L" is a subsidiary of "J" and is also wholly-owned by "J", but through a second intermediate holding company.[5] You represent that neither "J", "K", "L", nor either of the intermediate holding companies has ever been subject to statutory disqualification pursuant to Section 8a(2) or 8a(3) of the Act.[6]

The Target Entities.

The existing general partner of each of the Investment Partnerships is "O". The general partners of "O" are Messrs. "A" and "B.[7] "O" is not (and has not ever been) registered with the

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necessary. You argue in your letter that pursuant to Section 1a(5) of the Act (7 U.S.C. § 1a(5)(B)(i) and (C) (1994)) "K" is excluded from the definition of CTA and is thus not required to register as a CTA. Among persons excluded from the CTA definition is "any bank or trust company or any person acting as an employee thereof" if the furnishing of services by such person "is solely incidental to the conduct of their business or profession". You contend that advising the Investment Partnerships will be a minor part of "K's" overall business and that, accordingly, "K" is not a CTA. Because we are treating your letter as a request for no-action relief, it is not necessary for us to decide whether "K" is a CTA. Pursuant to Section 202(a)(11) of the Investment Advisers Act of 1940 (15 U.S.C. § 80b-2(a)(11) (1994) the "IAA")), "K" is excluded from the definition of "investment adviser," and is not required to register as such under the IAA.

[3] 12 U.S.C. § 1841 et seq. (1994). You represent that based on total assets, "J" is one of the thirteen largest banking organizations in the United States.

[4] "M".

[5] "N".

[6] 7 U.S.C. § 12a(2) or 12a(3) (1994).

[7] You represent that although "O" is organized as a limited partnership, "A" is the sole limited partner.

Commission in any capacity. "O" is not registered with any other agency or authority.

"P", an investment adviser registered as such with the Securities and Exchange Commission ("SEC") under the Investment Advisers Act of 1940 (the "IAA"),[8] is the sole investment adviser to the Investment Partnerships. "A" is the sole shareholder of "P", and "B" is an employee. You represent that "P" has never been registered with the Commission in any capacity.[9] "A" was registered as an associated person of "Q" from March 31, 1982 to February 27, 1987. "B" has never been registered with the Commission. You state that you have been advised that neither "O", "P", "A" nor "B" has ever been the object of any administrative, civil or criminal action and you represent that neither "O", "P", "A" nor "B" is subject to statutory disqualification pursuant to Section 8a(2) or 8a(3) of the Act.

The Investment Partnerships are "R, "S" and "T". Limited partnership interests in each of the Investment Partnerships have been offered and sold in private offerings pursuant to Rule 506 of Regulation D under the Securities Act of 1933 (the "Securities Act").[10] You represent that pursuant to Section 3(c)(1) of the Investment Company Act of 1940 (the "ICA"),[11] each of the Investment Partnerships is exempt from registration with the SEC as an investment company. You further represent that the present limited partners of the Investment Partnerships come almost entirely from the approximately sixty clients of "P". You state that in certain instances (such as the non-QEP employee of "P" described below) persons other than "P" clients have been permitted to become limited partners in the Investment Partnerships.

Existing Activities Subject to Regulation under the Act

You represent that the Investment Partnerships invest portions of their assets in other partnerships, referred to for purposes of your letter as "Portfolio Partnerships." You represent that the Investment Partnerships do not, and in the future will not, directly trade commodity interests, although certain Portfolio

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[8] 15 U.S.C. § 80b-1 et seq. (1994).

[9] You represent that the "P" that was registered with the Commission as a CPO from August 28, 1991 to September 22, 1993 (National Futures Association ID number "Z") is an unrelated entity.

[10] 17 C.F.R. § 230.506 (1996) promulgated under 15 U.S.C. § 77a et seq. (1994).

[11] 15 U.S.C. § 80a-1 et seq. (1994).

Partnerships in which "T" participates may engage in commodity interest trading.[12] At the present time and upon closing of the contemplated transaction, "T" is the only Investment Partnership with assets invested in Portfolio Partnerships that hold futures contract or commodity option positions.

You represent that "T's" purpose, as stated in its private placement memorandum, is to "seek capital appreciation primarily by investing in securities of non-U.S. companies." At the present time and upon closing of the contemplated transaction, a total of twenty-eight percent of "T's" assets will be invested in four Portfolio Partnerships that have incidental futures positions.[13] Of that twenty-eight percent, twenty-two percent is allocated to three offshore funds (the "Offshore Funds") of a British Virgin Islands investment company.[14] You have been advised that the Offshore Funds' futures exposure currently consists of short positions in stock index futures on exchanges located outside of the United States. No Offshore Fund commits more than ten percent of the fair market value of its assets as initial margin and premiums for commodity interests (after taking into account unrealized profits and unrealized losses for any futures contract it has entered into). Six percent of "T's" assets will be invested in a domestic pool operated by "W", a registered CPO, pursuant to a claim of exemption pursuant to Commission Rule 4.7[15] (the "Domestic

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[12] You note that "T's" private placement memorandum states that it not only invests in Portfolio Partnerships, but also engages "Direct Portfolio Managers" to manage a portion of "T's" assets. You state that the other Investment Partnerships are also permitted to engage Direct Portfolio Managers. You represent that none of such Direct Portfolio Managers use Investment Partnership assets to trade commodity interests or provide commodity interest trading advice to Investment Partnerships.

[13] This letter does not address the legality of any past activities of "O", "P" or their respective principals.

[14] Not more than ten percent of the participants in, and the value of the assets of, the fund shares may be held by or on behalf of U.S. persons. You state that the British Virgin Islands investment company represents that it is exempt from registration under the ICA. You further state that "U", the investment manager responsible for operating the Offshore Funds, is incorporated in the United Kingdom and regulated by the Investment Management Regulatory Organization.

[15] Commission rules referred to herein are found at 17 C.F.R. Ch. I et seq. (1996). We note that if more than ten percent of the fair market value of the assets of "T" are used to purchase units in Rule 4.7 exempt pools, including the Domestic Pool, the validity of each such exempt pool's claim of exemption under Rule 4.7 may be jeopardized. Pursuant to Rule 4.7(a)(1)(ii)(B)(2)(xi)

Pool"). The Domestic Pool invests primarily in foreign securities and you have been advised that the Domestic Pool's futures exposure currently consists of short positions in stock index futures on foreign exchanges. The Domestic Pool does not commit more than ten percent of the fair market value of its assets as aggregate initial margin and premiums for commodity interests (after taking into account unrealized profits and unrealized losses on any futures contracts it has entered into).

All but five of "T's" investors are qualified eligible participants ("QEPs") within the meaning of Rule 4.7(a).[16] You represent that henceforth only existing investors, QEPs and senior executives of "V" ("V Executives" will be permitted to participate in "T".[17]

The Offshore Funds and the Domestic Pool provide "T" with certified annual financial statements, unaudited monthly performance reports and unaudited monthly allocation reports (which disclose, as of month-end, the extent to which the pool uses futures).[18] "T's" net asset value is calculated quarterly, based on the information received from Portfolio Partnerships and Direct Portfolio Managers. "T" investors are provided with a quarterly review three weeks after the end of the calendar quarter covered by the review. Investors are permitted to redeem their interests in

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4.7(a)(1)(ii)(B)(2)(xi) and 4.7(a)(1)(ii)(D) a pool with one or more non-QEP participants may not itself be a QEP if it invests more than ten percent of its assets in Rule 4.7 exempt pools.

[16] You represent that the non-QEP participants in "T" include "C", an employee of "P" responsible for marketing and familiar with securities investing; a partner in a major law firm who specializes in securities-related matters; a managing director of a registered broker-dealer; and two long-time (19-year) clients of "P" (each of whom has a securities portfolio valued at approximately $1 million and neither of whom is dependent upon his securities for living expenses). All but the "P" employee are "accredited investors," as defined in SEC Regulation D, 17 C.F.R. § 230.501 et seq. (1996).

[17] You state that "V" is focused on coordinating financial services for the families of the bank's wealthiest customers in such areas as tax and estate planning, and administrative and fiduciary functions. Senior executives in "V" are equivalent in qualifications and responsibilities to senior executives in other divisions of "K".

[18] You represent that "T" typically receives the month-end allocation reports within a week after the end of the subject month.

"T" quarterly, upon sixty days notice.[19] Unless waived by the general partner, the minimum investment in "T" is $100,000.

The Transaction.

Upon closing of the contemplated transaction, "L" will replace "O" as the general partner of each of the Investment Partnerships. "K" will acquire all of the assets of "P" and will replace "P" as the investment adviser to the Investment Partnerships.[20] "P" will withdraw its SEC registration as an investment adviser, and "A" and "B" will become employees of "K".[21]

You represent that "L" intends to continue to operate the Investment Partnerships and to establish additional Investment Partnerships in the future.

Federal Reserve Commitments.

You represent that in accordance with the provisions of the Bank Holding Company Act, "J" has provided detailed information (the "Notice") to the Federal Reserve Board concerning the proposed substitution of "L" for "O" as the general partner of each of the Investment Partnerships and the acquisition of "P" by "K".[22] You state that on April 7, 1997, the Board of Governors of the Federal Reserve System approved the transaction. "J" has represented to the Federal Reserve Board that "L's" operation of the Investment

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[19] You note that "T's" private placement memorandum states that the general partner of "T" may defer an investor's distribution for up to three calendar quarters after the quarter in which notice to redeem is given. If the distribution is not made within that time period, "T" is required to be dissolved and its assets liquidated.

[20] You note that not all of the liabilities of "O" and of "P" will be assumed by "J" and/or its subsidiaries.

[21] "B" and "A", together with another "J" employee, will become co-managing directors of "V". Their primary responsibilities will be to advise wealthy individuals, in addition to which duties they will advise the Investment Partnerships. "B" will be named chief investment officer of "V", and "A" will sit on the Management Committee of the "J" asset management group line of business.

[22] You indicate that "J" has filed the Notice with the Federal Reserve Bank of Cleveland pursuant to Section 1843(j) of the Bank Holding Company Act (12 U.S.C. § 1843(j) (1994)), as amended by Section 2208 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (Pub. L. 104-208, Div. A, Title II, 110 Stat. 3009 September 30, 1996).

Partnerships will be subject to thirty-eight regulatory commitments ("Federal Reserve Commitments") which are part of the Notice. In your correspondence, you call particular attention to several of the Federal Reserve Commitments:

1. "L" may act as general partner for existing or future Investment Partnerships that are excluded from the definition of "investment company" under the ICA and that are exempt from the registration and prospectus delivery requirements of the Securities Act.

   a. Investment Partnership interests will have minimum denominations of $100,000 (except that "V Executives" and persons who have $500,000 or more under the management of "J" and its subsidiaries may invest less than $100,000 in an Investment Partnership). With the exception of "V Executives", only "accredited investors" as defined in SEC Regulation D[23] will be permitted to invest in Investment Partnerships. Existing limited partners of Investment Partnerships who are not accredited investors or whose investments therein are less than $100,000 will be permitted to continue as limited partners following the closing of the contemplated transaction.

2. No general solicitation or general advertising will be made for limited partnership interests in Investment Partnerships.[24]

3. Each new investor (and each existing investor making an additional investment) will be required to execute a notarized subscription agreement acknowledging that he or she has received and read the private placement memorandum for the Investment Partnership, including a special disclosure statement, and that he or she understands, among other things, that:

   a. The Investment Partnership interests involve a high degree of risk;

   b. The Investment Partnership interests are not deposits or other obligations of "J" or its subsidiary bank or trust companies, and are not guaranteed in any way by "J" or its subsidiaries;

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[23] 17 C.F.R. § 230.501 et seq. (1996).

[24] You state that Investment Partnership interests may be marketed pursuant to "customary private placement practice" in accordance with state Blue Sky laws. "J's" subsidiary banks or its broker-dealer subsidiary may approach existing "K" customers or prospective "K" customers.

c. The Investment Partnership interests are not insured by the Federal Deposit Insurance Corporation or guaranteed by any government agency; and

d. The Investment Partnership interests are illiquid and are subject to fluctuation in value and subject to risk of loss of the principal amount invested.

4. The Investment Partnerships will not be permitted to invest directly in futures or commodity option contracts.

5. "L" will restrict investments by the Investment Partnerships in Portfolio Partnerships that might constitute commodity pools to:

a. Less than 5% of any class of voting securities of a Portfolio Partnership; and

b. Less than 25% of the total equity of a Portfolio Partnership.

Federal Reserve Audits.

You have been informed that after the closing of the contemplated transaction, the Federal Reserve will conduct audits of "L" at least once every two years, which will include reviews of "L's" accounting and risk management policies and procedures, as well as an examination of "L's" compliance with the Federal Reserve Commitments. You represent that the audits will assure compliance with the Federal Reserve Commitments and will include evaluation of the manner in which "K" selects and monitors investments chosen for the Investment Partnerships.

Other Operational Restrictions.

You state that "L" will operate "T" under restrictions in addition to the Federal Reserve Commitments.

a. Restrictions on "T".

1. "T" will have as its purpose investing in securities.

2. Investors in "T" will be restricted to QEPs, "V Executives" and those current investors who are not QEPs.

3. "T" will not be marketed as a commodity pool.

4. "T" will not directly trade commodity interests.

5. The only compensation "L" will receive for operating "T" will be amounts intended to reimburse "L" for its administrative expenses.

6. "L" will operate "T" only in accordance with advice provided by "K" as investment adviser to the Investment Partnerships. "L" will provide no advice to "T" on the value or advisability of trading in commodity interests.

7. Investments received from "T's" investors (whether new subscriptions or additions to an investor's existing investment) will be deposited in a custody account in the name of "T" at "K" or in a money market account with an SEC-registered broker-dealer for the short period of time such investments are not invested in Portfolio Partnership interests or other securities. "T" will provide investors with at least quarterly disclosure of the net asset value of their partnership interests.[25]

8. "T" will permit investors to redeem their interests at the end of any calendar quarter upon sixty days notice and subject to the right of "L" to defer a distribution for up to three quarters after the quarter in which the notice to redeem is given. If "L" does not make the distribution within that time period, "T" will be required to be dissolved and its assets liquidated.

9. "T's" losses will be restricted to the amount invested in Portfolio Partnerships and direct investments in securities selected by Direct Portfolio Managers. Direct Portfolio Managers will not trade commodity interests for Investment Partnerships.

10. "T" will not invest more than 50% of its assets in Portfolio Partnerships that trade commodity interests. "T" will be required to withdraw from any Portfolio Partnership that commits more than 10% of the fair market value of its assets to initial margin and premiums for commodity interests. Thus, using the formula set forth in Interpretative Letter 91-6, the portion of "T's" assets committed to commodity interest trading will be restricted to 5%.[26]

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[25] You state that "O" receives reliable information from the Portfolio Partnerships quarterly. Interim information received from the Portfolio Partnerships is only an estimate and is not passed on to Investment Partnership investors.

[26] You refer to the Division's Interpretative Letter No. 91-6, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,069 (June 13, 1991) which permits the CPO of a pool that is operated pursuant to a claim of exemption under Rule 4.12(b) and that invests in a second Rule 4.12(b) pool to multiply by .10 the amount of the first pool's assets invested in the second pool for purposes of testing compliance with the 10% restriction in Rule

11. "L" will obtain annual certified financial statements from each of the Portfolio Partnerships, and as soon as practicable after the end of each month, the unaudited monthly performance reports and monthly allocation reports of Portfolio Partnerships that trade commodity interests. Copies of the monthly allocation reports of Portfolio Partnerships that trade commodity interests will be provided to "T" investors (after redacting the name of the Portfolio Partnership).

b. Restrictions Upon "T's" Investments in Portfolio Partnerships.

1. Each Portfolio Partnership will have as its purpose investment in securities.

2. No Portfolio Partnership will be marketed as a commodity pool.

3. Each Portfolio Partnership will be operated by a registered CPO or by a person exempt from registering as, or excluded from the definition of, a CPO.

4. Each Portfolio Partnership will be registered as an investment company pursuant to the ICA and have its securities registered under the Securities Act or it will be exempt from such registration.

5. No Portfolio Partnership will enter into commodity interest transactions for which the aggregate initial margin and option premiums exceed ten percent of the fair market value of the Portfolio Partnership's assets, after taking into account unrealized profits and unrealized losses on any such contracts; provided, however, that in the case of an option that is in-the-money at the time of purchase, the in-the-money amount as defined in Rule 190.10(x) may be excluded in computing such ten percent ("Ten Percent Test"). "L" will monitor this condition as follows:

   a. "L" will advise each Portfolio Partnership that it has represented to the Commission as a condition of obtaining no-action relief that "T" will invest in only those Portfolio Partnerships that meet the Ten Percent Test and that, accordingly, "L" will withdraw "T's" investment in any Portfolio Partnership that exceeds the Ten Percent Test; and

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4.12(b) on the amount of a pool's assets that may be committed to initial futures margin and option premium.

b. "L" will obtain monthly reports from each Portfolio Partnership that trades commodity interests.[27] Such monthly reports will disclose the month-end use of commodity interests by the respective Portfolio Partnerships. If a report indicates that a Portfolio Partnership has exceeded the Ten Percent Test, "L" will notify the Portfolio Partnership in writing as soon as practicable. "L" will cause "T" to withdraw from such Portfolio Partnership unless the Portfolio Partnership promptly reduces the amount of its assets committed to initial margin and/or commodity option premiums to ten percent of the fair market value of the Portfolio Partnership's assets.

Based upon the representations made in your correspondence, and subject to compliance with the conditions set forth below, the Division will not recommend that the Commission take any enforcement action against (1) "L" for failure to register as a CPO pursuant to Section 4m(1) of the Act; or (2) "K" for failure to register as a CTA pursuant to Section 4m(1).[28]

<u>Conditions</u>

This position is subject to compliance with the following conditions:

1. "J" complies with (and causes its subsidiaries including "M", "N", "L" and "K", as applicable, to comply with) the Federal Reserve Commitments, as well as the other operational restrictions on Investment Partnerships and Portfolio partnerships described above;

2. The Division is notified in writing of the name of any new Investment Partnership as soon as the name is selected;

3. Unless relief is granted by the Division, or "L" becomes a registered CPO or subject to a valid exemption or exclusion, "L" will not invest assets of any Investment Partnership other than "T" in a Portfolio Partnership that trades commodity interests;

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[27] "L" will also conduct intra-month spot checks of the futures positions held by the Portfolio Partnerships as it deems appropriate.

[28] In view of the no-action position taken herein with respect to "L" and "K", we need not address the issue whether persons associated with "L" or "K" must register as associated persons of such entities.

4. Any Portfolio Partnership that trades commodity interests must be operated by a registered CPO and, if it is advised by a third party, that third party must be a registered CTA, unless a valid exemption or exclusion applies to such CPO or CTA; and

5. "J", "L" and "K" will be subject to such special calls as the Division may make to demonstrate compliance with the conditions upon which relief is granted hereby.

This letter is applicable to "L" and "K" in connection with the operation of the Investment Partnerships and the provision of investment advice thereto. The position taken hereby relieves "L" and "K" from registration requirements solely in connection with the operation of "T". Furthermore, this letter does not excuse "L" or "K" from compliance with any other applicable requirements contained in the Act or in the Commission's regulations issued thereunder, including all other provisions of Part 4. For example, "L" and "K" remain subject to the antifraud provisions of Section 4o of the Act[29] and to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations.

This letter is based upon the representations provided to us and is subject to compliance with the conditions set forth 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 in the event the operations or activities of "J", "K", "L", the Investment Partnerships or the Portfolio Partnerships change in any way from those represented to us.

Moreover, nothing in this letter should be construed as limiting in any way the Commission's ability to proceed against "O", "P", or their respective principals (or against "L" or "K" as successors in interest, respectively, to "O" and "P") for any past violation of the Act or of the Commission's regulations thereunder. If you have any questions concerning this correspondence, please contact me or Susan C. Ervin, the Division's Chief Counsel, at (202) 418-5450.

Very truly yours,

Andrea M. Corcoran
Director

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[29] 7 U.S.C. § 6o (1994).