

CFTC Letter No. 97-88**October 10, 1997****Division of Trading & Markets**

Re: Request for Relief from Registration as a Commodity Trading Advisor under § 4m(1)

Dear :

This is in response to your letter dated September 9, 1997 to the Division of Trading and Markets ("the Division") of the Commodity Futures Trading Commission (the "Commission"), as supplemented by your letters dated September 26, 1997 and September 30, 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 V , a Colorado corporation, in connection with providing advisory services to W and X (the "Funds"²).

Based upon the representations made in your correspondence, we understand the pertinent facts to be as follows. The Funds are open-end mutual fund trusts established under the laws of the Province of Ontario, Canada pursuant to a Declaration of Trust made by the Funds' trustee, Y . The investment objective of X is to seek long-term growth of capital, which is accomplished by investing primarily in stocks of major, established U.S. corporations. The investment objective of W is to seek long-term growth of capital and to generate income as a secondary objective. It seeks to achieve this objective through a diversified portfolio of securities which consists mainly of common and preferred stocks of Canadian, United States ("U.S.") and other international issuers.

Interests in the Funds will not be offered, sold, or transferred to any U.S. person, as that term is defined in Rule 4.7.³ However, interests in the Funds will be offered outside of the U.S. and will be available to members of the non-U.S. public for a minimum subscription price of \$500. V owns neither voting nor participatory shares in the Fund, nor will any employees of V serve as directors of the Funds. Moreover, V is not involved in marketing or soliciting participations in the Funds, nor is it involved in administrative matters or distribution of shares for the Funds. The Funds' investment adviser, the "Manager", is a Canadian corporation. V is not affiliated in any way with the Manager. V has entered into agreements as of July 31, 1997 with the Manager under which V will act as subadvisor to the Funds.

The Funds may also invest in or use derivative instruments that are consistent with the investment

objectives of the Funds to the extent, and for the purposes, permitted by Canadian securities regulators from time to time. The Funds may only make use of "permitted derivatives" as defined in, and to the extent allowed by, National Policy No. 39 of the Canadian Securities Administrators ("Canadian Policy No. 39"). Such purposes include offsetting or reducing a risk associated with an investment, reducing transaction costs, achieving greater liquidity, creating effective exposure to international financial markets or increasing speed and flexibility in making portfolio changes. The Funds may use derivatives to position portfolios so that they may profit from declines in financial markets.

V is not registered with the Commission in any capacity⁴ but is registered with the Securities and Exchange Commission ("SEC") as an investment adviser under the Investment Advisers Act of 1940 (the "IAA"), and as such, provides investment advice to a number of investment companies registered with the SEC. V provides commodity interest trading advice to the Funds that is intended to be solely incidental to its business of providing securities advice to them. Commission Rule 4.14(a)(8) provides an exemption from registration as a CTA for an investment adviser registered under the 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 Rule 4.5 or are qualifying entities under Rule 4.5; and (iii) employs only such strategies as are consistent with eligibility status under Rule 4.5.

The Funds, because of their foreign nature, will not (and absent an exemption from the SEC, cannot) register as investment companies under the Investment Company Act of 1940. Thus, neither fund is an "otherwise regulated entity" nor a "qualifying entity" as specified in Rule 4.5. Consequently, V cannot rely on an exemption from CTA registration under Rule 4.14(a)(8). Nonetheless, you state that the Funds seek to use commodity interest contracts and V seeks to provide commodity interest trading 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 Funds 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 each Funds' portfolio, after taking into account unrealized profits and losses on any such contracts it has entered into. You also represent that V, in accordance with certain requirements of Rule 4.14(a)(8): (1) will provide commodity interest trading advice to the Funds in a manner solely incidental to its furnishing of securities advice to the Funds; (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").⁵ Accordingly, based upon the foregoing representations, and consistent with our prior practice in this area,⁶ the Division will not recommend that the Commission take any enforcement action against V for 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 Funds in reliance upon the CTA registration exemption of Rule 4.14(a)(8). This position is subject to the condition that V 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 Funds are organized outside of the U.S. and shares in the Funds will not be owned or transferred to any U.S. person; (2) the Funds' stated investment strategy is to invest primarily in equity securities; (3) V is already regulated due to its registration with the SEC as an investment adviser under the IAA; (4) the Funds will be operated in a manner consistent with Rule 4.5(c)(2); and (5) V, 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 Funds.

The relief granted by this letter does not excuse V 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 4o of the Act,⁷ 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 V or the Funds 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,

Susan C. Ervin

Chief Counsel

¹ 7 U.S.C. § 6m(1) (1994).

² The Division previously granted CTA registration no-action relief to V in connection with providing advisory services to U, which was incorporated in the Cayman Islands, and operated as an offshore fund. Division of Trading and Markets Interpretative Letter No. 97-5, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,972 (Feb. 12, 1997).

³ Commission rules referred to herein are found at 17 C.F.R. Ch. I (1997).

⁴ Our records indicate that V filed a claim of exemption from registration as a CTA pursuant to Rule 4.14(a)(8), effective May 13, 1994.

⁵ 7 U.S.C. § 1 *et seq.* (1994).

⁶ See Division of Trading and Markets Interpretative 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, no more than five percent of the Fund's portfolio would be devoted to speculative positions). *See also* Division of Trading and Markets Interpretative Letter No. 97-5, referenced in note 2 above.

⁷ 7 U.S.C. § 6o (1994).