

CFTC Letter No. 98-09**November 13, 1997****Division of Trading & Markets****Re: Rule 4.13(a)(2); Exemption from CPO Registration**

Dear :

This is in response to your letter dated August 25, 1997 to the Division of Trading and Markets ("Division") of the Commodity Futures Trading Commission ("Commission") as supplemented by telephone conversations among Division staff, you and your associate, "A". By this correspondence, you request that "B" may continue to claim an exemption from registration as a commodity pool operator ("CPO") under Rule 4.13(a)(2)¹ in connection with his operation of the "Company".

Based upon the representations made in your letter, as supplemented, we understand the relevant facts to be as follows. The Company was organized as a limited liability company under the laws of the State of New York. It has three members ("Members"):

(1) "B", who is registered with the Commission as a floor trader and has been an associate member of "R" since October 18, 1995.² He has over 12 years experience as a trader in currency option contracts and as a trader in commodity futures contracts. His net worth is approximately \$810,000, and he will receive 35% of the Company's profits and losses.

(2) "C", who is registered with the Commission as a floor broker and who has been a full member of "R" since October 27, 1995. He has known "B" professionally and socially for over seven years and first met him on the "R" trading floor. "C" has over eight years experience as a trader in commodity futures contracts. His net worth is approximately \$700,000. "C" and "B" will trade the Company's account on "R", and "C" will receive 35% of the Company's profits and losses.

(3) "S", a limited liability company organized under Delaware law, and registered with the Commission as a CPO and commodity trading advisor.³ "S's" net worth is approximately \$2,000,000. It is owned by "D" and his wife. "D" is an accredited investor and has a net worth of approximately \$3.5 million.⁴ He is registered with the Commission as an associated person and listed as a principal of "S". "D" has known "B" professionally and

socially for over ten years and first met him when "B" was a proprietary floor trader and "D" was an institutional equity broker at "T".⁵ "S" is engaged primarily in the business of investing in "investment-related ventures."⁶ It will receive 30% of the Company's profits and losses.

The Company is a full member of "R". It trades solely for its own account.

"B" filed a Notice of Claim of Exemption from CPO registration pursuant to Rule 4.13(a)(2), which was effective June 27, 1997.⁷ Rule 4.13(a)(2) provides an exemption from CPO registration where: (1) the aggregate gross capital contributions for all pools operated by the CPO do not exceed \$200,000; and (2) none of the pools operated by the CPO has more than fifteen participants at any time. At present, the Company's aggregate gross capital contributions are \$199,000, which consist of \$2,500 each from "B" and "C" and \$194,000 from "S". The Members would now like to contribute additional capital to the Company, which would make the Company's aggregate gross capital contributions exceed the \$200,000 maximum amount for relief from CPO registration under Rule 4.13(a)(2).⁸ It is intended that "B" and "C" will each contribute an additional \$2,500 and that "S" will contribute an additional \$195,000 to the Company. Thus, it is intended that the Company's aggregate gross capital contributions will be \$399,000.

In support of your request, you represent, among other things, that: (1) each Member is equally and actively involved in the management of the Company; (2) no intention exists to admit additional members; and (3) the Company is the only commodity pool operated by "B".

Based upon the foregoing representations, the Division will not recommend that the Commission take any enforcement action against "B" solely for failure to comply with the \$200,000 gross capital contributions criterion of Rule 4.13(a)(2).

This letter is applicable to "B" solely in connection with his operation of the Company and does not excuse him from compliance with any other applicable requirements contained in the Commodity Exchange Act (the "Act") or the Commission's regulations issued thereunder. For example, he remains subject to the antifraud provisions of Section 4o of the Act,⁹ to the reporting requirements for traders set forth in Parts 15, 18, and 19 of the Commission's regulations, and to the operational and advertising requirements of Rules 4.20 and 4.41, respectively.

This letter is based upon the representations that have been made to us. Any different, changed, or omitted facts or conditions might require us to reach a different conclusion. In this regard, we request that you notify us immediately in the event that the operations and activities of "B" or the Company, including the composition and contributions of the

Members, change in any way from those represented to us. Further, this letter represents the position of the Division only. It does not necessarily reflect 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 Monica S. Amparo, an attorney on my staff, at (202) 418-5450.

Very truly yours,

Susan C. Ervin

Chief Counsel

¹ Commission rules referred to herein are found at 17 C.F.R. Ch. I (1997).

² From January 17, 1991 to October 17, 1995, "B" was a full member of "R".

³ Currently, "S" provides commodity trading advice on a non discretionary basis to its clients.

⁴ Notwithstanding "D's" net worth, he is not a qualified eligible participant under Rule 4.7(a) because he does not meet the portfolio requirement of Rule 4.7(a)(1)(ii)(B).

⁵ In addition, "D" had business dealings with "B" in 1993 and 1995. In 1993, "B" executed various trades on "R" for "W", for which "D" served as an investment consultant. In 1995, "B" executed various trades on "R" for "D's" personal account.

⁶ "S" is a general partner of "U", which is not a registered investment company, a general partner of "V", also not a registered investment company, and a Member of the Company.

⁷ You have advised Division staff that the determination that "B", rather than either of the other two Members of the Company, would be the one to seek CPO registration relief was purely an arbitrary decision, as the Company does not have a "managing member" and all decisions are made by the Members. Pursuant to New York law, under which the Company was organized, management authority in a limited liability company may be held by a managing member or management authority may rest with all the Members, as is the case with the Company.

⁸ You initially sought confirmation that "B" would qualify for relief from registration as a CPO pursuant to Rule 4.13(a)(1), which does not limit the amount of gross capital contributions that may be collected from pool participants to claim relief thereunder. However, in order to claim that exemption, a person may not otherwise be required to register with the Commission. As noted above, "B" is a registered floor

trader. Consequently, "B" cannot qualify for an exemption from CPO registration pursuant to Rule 4.13 (a)(1).

⁹ 7 U.S.C. § 6o (1994).