

CFTC Letter No. 98-32**April 28, 1998****Division of Trading & Markets**

Re: Request for Exemptive Relief from Rules 4.21, 4.22 (a) and (b), 4.25, and 4.26

Dear :

This is in response to your letter, dated March 10, 1998, to the Division of Trading and Markets of the Commodity Futures Trading Commission ("Commission"), as supplemented by facsimiles dated March 23, 1998, March 24, 1998, April 7, 1998 and telephone conversations with Division staff. By your correspondence, you request a continuation of the exemptive relief from the requirements of Rules 4.21, 4.22(a) and (b), 4.25 and 4.26 ("Rules")¹ that the Division previously issued to "J", a registered commodity pool operator ("CPO"),² with regard to ("Insider Fund"), a commodity pool operated by "J", notwithstanding the addition of certain additional participants in the Insider Fund.

Based upon the representations made in your correspondence, we understand the relevant facts concerning the Insider Fund to be as follows. The Insider Fund began trading as of January 1, 1996 and was formed for the purpose of permitting investment by the principals and employees of "J" and its affiliate, "K",³ and certain members of their immediate families. By letters dated November 4, 1996, March 24, 1997, June 2, 1997, October 29, 1997, and February 27, 1998, the Division granted "J's" requests for exemption from compliance with the Rules in connection with the Insider Fund.⁴ You now seek confirmation that "J" may continue to claim relief from the Rules if it admits six additional investors into the Insider Fund (the "Proposed Participants").

You assert that each of the Proposed Participants is an investment manager for "K" who makes trading decisions for one or more of the subaccounts through which the Insider Fund invests in securities, and is a "sophisticated investor fully capable of evaluating the risks of an investment in the Insider Fund without the full disclosure and reporting safeguards of the Commodity Exchange Act ['Act']⁵ and the Commission's regulations." You further state that each of the Proposed Participants will have access to the Insider Fund's books and records on an ongoing basis and has received or will receive: (1) a copy of the Insider Fund's Limited Partnership Agreement and Private Placement Memorandum; (2) quarterly financial statements; and (3) audited annual financial statements. Finally, you represent that "J" will obtain the consent of each Proposed Participant to be treated as a QEP. The Proposed Participants are the following:

(1) "A", who has been an investment manager for "K" since 1997. Prior to joining "K", "A" worked for three and a half years as a wire clerk for a member firm on the floor of "L". He has a BS degree in Psychology and has passed the Series 7 and 63 exams. Though not an accredited investor, "A" has a net worth of approximately \$100,000 and is expected to earn at least \$200,000 this year.

(2) "B", who joined "K" as an investment manager in 1996. A listed principal of "K", "B" has worked in the securities industry since 1985 and has passed the Series 7 and 63 exams. Prior to joining "K", "B" traded securities and commodities for "M", a hedge fund, and "N", a broker-dealer. Though not an accredited investor, "B" earned in excess of \$200,000 last year and is expected to earn at least \$200,000 this year.

(3) "C", who joined "K" as an investment manager in 1995. "C" has worked in the securities industry for the past 18 years. Prior to joining "K", he traded equities at "O", a broker-dealer, "P", a defunct broker-dealer, and "H", a limited partnership hedge fund. "C" is an accredited investor and has passed the Series 7 and 63 exams.

(4) "D", who joined "K" as an investment manager in 1993. "D" has worked in the securities industry for the past six years. Before joining "K", "D" was a retail broker with "Q", a broker-dealer. He has a BS degree in Psychology and has passed the Series 7 and 63 exams. Though not an accredited investor, "D" earned in excess of \$200,000 last year and is expected to earn at least \$200,000 this year.

(5) "E", who joined "K" as an investment manager in 1995. "E" has worked in the securities industry since 1994. Before joining "K", "E" was an associate financial advisor for "R", a broker-dealer, and an assistant trader at "S", a hedge fund limited partnership. "E's" duties at "R" included analyzing portfolios. At "S", "E" helped maintain low risk portfolios in short term equities and futures. "E" has a B.A. in history and philosophy and has passed the series 7 and 63 exams. Though not an accredited investor, "E" has a net worth of \$600,000. He also earned in excess of \$200,000 last year and is expected to earn at least \$200,000 this year.

(6) "F", who joined "K" as an investment manager in October 1997. "F" has worked in the securities industry since 1988. Before joining "K", "F" was a trader for "T", an entity that managed hedge funds, and "U", a broker-dealer that traded proprietary capital. "F" also was a retail stock broker for "V", a broker-dealer, and an institutional salesman for "W", another broker-dealer. "F" is an accredited investor and has passed the Series 7 and 63 exams.

Based upon the foregoing representations, it appears that granting the requested relief

would not be contrary to the public interest or the purposes of Rule 4.7(a). Accordingly, under authority delegated to it by Rule 140.93(a)(1), the Division hereby confirms that "J" may continue to claim exemptive relief from the Rules in connection with its operation of the Insider Fund notwithstanding the participation therein of "A", "B", "C", "D", "E", and "F". This relief is subject to the conditions that "J" will: (1) obtain from each Proposed Participant written confirmation that the Participant has received, read, and understood the Private Placement Memorandum; (2) notify each Proposed Participant that the Insider Fund is being operated pursuant to exemptive relief granted by the Division; (3) explain to each Proposed Participant the nature and purpose of the exemptive relief; (4) obtain written acknowledgment from each Proposed Participant that the Participant does not object to the Insider Fund's operation pursuant to exemptive relief or to the Proposed Participants' treatment as a QEP; and (5) provide each Proposed Participant with access to the Insider Fund's books and records.

The relief granted by this letter does not excuse "J" from compliance with any otherwise applicable requirements contained in the Commodity Exchange Act (the "Act") or in the Commission's regulations thereunder. For example, "J" remains subject to all antifraud provisions of the Act and Commission regulations, the reporting requirements for traders set forth in Parts 15, 18, and 19 of the Commission's regulations, and all other provisions of Part 4. Moreover, this relief is applicable to "J" solely in connection with its operation of the Insider Fund, as discussed above.

This letter, and the exemption granted herein, are based both upon the representations you have made to us and any conditions stated above, and are applicable to "J" solely in connection with its service as the CPO of the Insider Fund. Any different, changed or omitted material facts or circumstances might render this exemption void. You must notify us immediately in the event the operations or activities of "J" or the Insider Fund, including the composition of the Insider Fund's investors, change in any material way from those as represented to us.

If you have any questions concerning this correspondence, please contact Helene D. Schroeder, an attorney on my staff, at (202) 418-5450.

Very truly yours,

I. Michael Greenberger

Director

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

² "J" also is registered as a commodity trading advisor ("CTA").

³"K" is registered as a CTA and CPO and serves as co-investment manager of the Insider Fund. Its sole managing member is "G", who also is "J's" sole managing member and is individually registered as a CPO.

⁴ Initially, because interests in the Insider Fund had been privately offered and sold under Section 4(2) of the Securities Act of 1933, as amended, and Regulation D thereunder, the Insider Fund was operated pursuant to an exemption under Rule 4.12(b). As such, the Insider Fund could not invest more than ten percent of its assets in commodity interests. On November 4, 1996, "J" obtained exemptive relief from Rules 4.21, 4.22(a) and (b), 4.24, 4.25 and 4.26 because it wished to invest more than ten percent of its assets in commodity interests and still be exempt from certain disclosure and monthly reporting requirements of Part 4. CFTC Interpretative Letter No. 96-82, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,911 (November 4, 1996). Thereafter, on March 24, 1997, June 2, 1997, October 29, 1997, and February 27, 1998, "J" obtained confirmation of this exemptive relief notwithstanding investment in the Insider Fund of certain additional limited partners. *See* CFTC Interpretative Letters No. 97-18, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,010 (March 24, 1997), No. 97-90, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,192 (October 29, 1997), No. 98-14, to be published in Comm. Fut. L. Rep. (CCH) (February 27, 1998). In the February 27 letter, "J" also obtained confirmation of the relief in connection with the requests of a former employee and the spouse of another former employee to maintain their investments after employment had terminated.

⁵ 7 U.S.C. § 1 *et seq.* (1994).