

CFTC Letter No. 99-49**November 30, 1999****Exemption****Division of Trading & Markets**

Re: Rule 4.7(a); Request to Treat A as a Qualified Eligible Participant

Dear :

This is in response to your letter dated March 4, 1999, to the Division of Trading and Markets (Division) of the Commodity Futures Trading Commission (the Commission), as supplemented by your letter dated June 7, 1999, your facsimile dated June 10, 1999 and telephone conversations with Division staff. By your correspondence, you request on behalf of X , the commodity pool operator (CPO) of the Pool , an exemption from Rule 4.7 (a) ¹ so that X may treat the Trust as if it satisfies the qualified eligible participant (QEP) criteria of the rule.

The Facts

Based upon the representations you have made in your correspondence, we understand the facts to be as follows. The Pool is a common investment fund that was formed in 1991. Virtually all of its assets are invested in securities. However, the Pool does engage in commodity interest trading to hedge its securities portfolio and, to a limited degree, to conduct spread strategies in commodity interest contracts. In fact, since the inception of the Pool, less than 0.5% of the Pool s total assets have been committed to establish commodity interest trading positions. X is the CPO of the Pool, and it operates the Pool pursuant to a Claim for Exemption under Rule 4.7(a).² Accordingly, X is permitted to accept only persons who are QEPs as participants in the Pool.

X now would like to accept the Trust as a participant in the Pool. The Trust is not a QEP however, because it does not meet the requirements of Rule 4.7(a)(1)(ii)(B)(2)(xi), the QEP criteria applicable to trusts, that it has total assets in excess of \$5 million and its participation in the Pool is directed by a QEP.

In support of your request, you explain that the Trust is a living trust established by A , who is its sole trustee and beneficiary. The Trust owns securities and other investments

with a market value of approximately \$900,000. A individually owns securities with a market value of approximately \$500,000. Taken together, then, the market value of securities and other investments owned by the Trust and A is approximately \$1.4 million.

A is a certified public accountant with 25 years in the investment business, including 17 years as a partner in a registered investment adviser, and he is an accredited investor as that term is defined under Regulation D of the Securities Act of 1933. He received undergraduate and graduate degrees in accounting, finance and taxation and also has taught finance at the graduate school level for six years.

A has been intimately involved with the Pool from its inception. As your correspondence explains:

Since 1993, A has served as chief financial officer of Y, where he is responsible for managing investments worth more than \$1 billion. B [a QEP,] was one of the four founding limited partners of the Pool, providing approximately one-quarter of the Pool's initial capital. As a result of his founding investment in the Pool, B also owns direct interests in X and in the Pool's general partner. While providing investment advisory services to B in 1991, A was responsible for evaluating and structuring B's original investment in the Pool and for negotiating the Pool's original formation documents on behalf of B. Since that time, A has continued to oversee B's investment in the Pool, including negotiation of the documents under which X was formed and engaged to manage the Pool's investments.

You further represent that as the primary contact person concerning B's investment in the Pool, A has access to all relevant books and records of the Pool. In addition, the Trust has provided its written consent to be treated as a QEP with respect to the Pool.

Analysis

The Commission has stated that its objective in proposing (and subsequently adopting) Rule 4.7 is, consistent with its customer protection role, to reduc[e] unnecessary regulatory prescriptions for CPOs offering pool participations only to persons who, based upon the qualifying criteria in the rule, do not appear to need the full protections offered by the Part 4 framework.³ As you note, the criteria for QEPs is designed to insure, among other things, that such persons possess the investment expertise and experience necessary to understand the risks involved.⁴

Based upon the representations you have made to us, it does not appear that granting the

requested relief would be contrary to the public interest or the purposes of Rule 4.7. This is because of, among others, your representations that: (1) the sole grantor, trustee and beneficiary of the Trust is A ; (2) A has an extensive background and experience in finance and investment advisory matters; (3) A was responsible for evaluating and structuring the investment of one of the original four limited partners of the Pool, who is a QEP; (4) A was responsible for negotiating on behalf of the QEP the documents under which X was formed and engaged to manage the Pool s investments; and (5) A has continued to oversee the QEP s investment in the Pool, such that he is the primary contact person concerning the QEP s investment in the Pool. In addition, we note your representation that since the inception of the Pool, less than 0.5% of the Pool s total assets have been committed to establish commodity interest trading positions. Accordingly, by the authority delegated under Rule 140.93(a)(1), the Division hereby grants X an exemption permitting it to treat the Trust as a QEP and to continue to claim relief pursuant to Rule 4.7(a) with respect to the Pool, notwithstanding the Trust s investment in the Pool.

This letter, and the exemption granted herein, are based upon the representations made in your correspondence. 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 X or the Pool change in any material way from those represented to us.

This letter relieves X solely from the QEP criteria of Rule 4.7(a) with respect to the participation of the Trust in the Pool. It does not excuse X from compliance with any otherwise applicable requirements contained in the Commodity Exchange Act (Act⁵) or the Commission s regulations issued thereunder. For example, X remains subject to all antifraud provisions of Section 4o of the Act, to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission s regulations and to all other applicable provisions of Part 4. Moreover, the relief provided by this letter is prospective only. It does not prevent the Commission from taking action against X for any past violation of the Act or the Commission s regulations.

If you have any questions concerning this correspondence, please contact Barbara S. Gold, Assistant Chief Counsel, at (202) 418-5450.

Very truly yours,

John C. Lawton

Acting Director

¹ Commission rules referred to herein are found at 17 C.F.R. Ch. I (1999).

² Commission records indicate that a Notice of Claim for Exemption was filed with respect to the Pool on _____.

³ 57 Fed. Reg. 3148 at 3150 (January 28, 1992).

⁴ 57 Fed. Reg. 3148 at 3152.

⁵ 7 U.S.C. 1 et seq. (1994).