December 11, 1986

Re: Request by a National Bank for Relief from Regulation as a CTA.

Dear Mr. :

This is in response to your letter dated October 23, 1986, as supplemented by your letter dated October 24, 1986 and telephone conversation with Division staff held on November 18, 1986, whereby you requested on behalf of "A", a national bank, confirmation that the Division will not recommend that the Commission take any enforcement action against "A" if it fails to register as a commodity trading advisor ("CTA") under the circumstances set forth below.

Based upon the representations you made in your October 22, 1986 letter, as supplemented, we understand the facts to be as follows:

> "A" is the principal banking subsidiary of "B". "A" is a commercial bank that has provided comprehensive banking and trust services to individuals, government entities and businesses since 1933. Pursuant to agreement, "A" acts as the Investment Administrator to two portfolios of the Trust, which is registered as an investment company with the Securities and Exchange Commission ("SEC") under the Investment Company Act of 1940 [the "1940 Act"].
>
> The Trust is a diversified, open-end investment company established under Massachusetts law as a Massachusetts business trust. The Declaration of Trust permits the Trust to offer one or more separate series of units of beneficial interest ("units") representing interests in separate port-

> folios of securities. Each unit of each portfolio represents an equal proportionate interest in that portfolio. Although the Trust currently consists of three separate series, "A" acts as Investment Administrator only with respect to two Portfolios.
>
> One of the Portfolios is authorized to enter into stock index futures contracts. . . .
>
> It has not yet commenced trading in stock index futures contracts. Prior to and throughout such trading, the Trust intends to comply fully with 17 C.F.R. §4.5, including the advance filing of a Notice of Eligibility thereunder, in order to be exempt from registration as a commodity pool operator.

As you have acknowledged, in providing commodity interest trading advice to the Trust "A" would appear to come within the definition of the term "commodity trading advisor" in Section 2(a)(1)(A) of the Commodity Exchange Act (the "Act"), 7 U.S.C. §2 (1982), 1/ and, absent any relief, would be required to register as a CTA pursuant to Section 4m(1) of the Act, 7 U.S.C §6m(1) (1982).

As you also are aware, in connection with its recent consideration of amendments to the Act, the House of Representatives Committee on Agriculture urged the Commission to issue rules which would provide relief from CTA regulation for, among other persons, registered investment advisers to Rule 4.5 trading vehicles. 2/ As the Committee Report states:

> [W]here the advisor advises an entity that is excluded from registration as a commodity pool under Rule 4.5 or is a Rule 4.5 qualifying entity and <u>such advisor is subject to appropriate regulation under the Investment Advisers Act</u>, that advisor should ordinarily be exempted from commodity trading advisor registration if its commodity advice is solely incidental to its

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1/ You further acknowledged that Section 2(a)(1)(A) of the Act excludes from the CTA definition such persons as a bank or trust company, provided that the furnishing of commodity interest trading advice is solely incidental to the conduct of their business or profession. You stated, however, that "A" is not requesting at this time any Division interpretation on the availability of this exclusion.

2/ H.R. Rep. No. 624, 99th Cong., 2d Sess. 46-48 (1986).

> business of providing securities advice to such entity and the advisor is not otherwise holding itself out as a commodity trading advisor. Therefore, the Committee urges the Commission to exercise its authority to adopt regulations in regard to these matters. [Emphasis added.]
>
> . . . .
>
> The Committee understands that rulemaking addressing these concerns may take some time for the Commission to develop and promulgate. Individual requests for exclusions or exemptions, consistent with the above guidelines, however, should be processed by the Commission as expeditiously as practicable. The Commission's experience with individual cases should facilitate the formulation of more general rulemaking.

The Committee Report also provides in pertinent part:

> [T]he Committee does not expect the Commission to grant exempted commodity trading advisors any relief from the antifraud provisions of section 4o of the Act. 3/

In furtherance of the foregoing, the Division recently issued registration "no-action" relief of the nature that you seek to certain registered investment adviser subsidiaries of a State-licensed insurance company in connection with the providing by those subsidiaries of commodity interest trading advice to certain registered investment companies which met (or would meet) the requirements of Rule 4.5. 4/

In support of the instant request, we note your representations, among others, that "A" will provide commodity interest trading advice to a Rule 4.5 qualifying entity (the Trust, a registered investment company) and that it

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3/ Id.

4/ Division of Trading and Markets Interpretative Letter No. 86-24, Comm. Fut. L. Rep. (CCH) ¶23,292 (October 1, 1986). See also Division of Trading and Markets Interpretative Letter No. 86-25, Comm. Fut. L. Rep. (CCH) ¶23,332 (October 9, 1986).

will not hold itself out as a CTA. 5/ We further note, however, that "A" is not registered as an investment adviser in light of the fact that, and as you have explained, it is excluded from the definition of the term "investment adviser" pursuant to Sections 202(a)(2) and (a)(11) of the Investment Advisers Act of 1940 (the "Advisers Act"), 15 U.S.C. §§80b-2(a)(2) and (11) (1982). 6/

In further support of the instant request, then, you represented the following:

> Requiring "A" to register as a CTA would undermine the legislative intent of exempting banks from registration under the Advisers Act. Congress clearly determined that the pervasive oversight of banks, including their investment advisory activities, precluded the need for duplicative regulation in the form of SEC registration. Preventing banks from qualifying under the staff's no-action position due solely to their reliance on this statutory exemption would contradict Congressional intent and place banks at an unwarranted competitive disadvantage vis a vis non-bank investment advisers.
>
> Moreover, "A" is subject to the substantial regulation applied to investment company advisers under the 1940 Act because banks are not exempt from the "investment adviser" definition in that act. It is the 1940 Act -- and not the Advisers Act -- which imposes the primary restrictions on the activities of investment advisers with registered investment companies. . . . . .

With respect to disclosure obligations in particular you explained:

> Section 15(c) of the 1940 Act in pertinent part provides as follows:

5/ For the purpose of the position we are taking below, we are assuming that this latter representation will meet the criteria established for "not holding out" as a CTA in Interpretative Letter No. 86-24, id.

6/ Unlike the CTA exclusion for banks and trust companies in Section 2(a)(1)(A) of the Act, the investment adviser exclusion does not contain a "solely incidental" requirement.

> [I]t shall be unlawful for any registered investment company having a board of directors to enter into, renew, or perform any contract or agreement, written or oral, whereby a person undertakes regularly to serve or act as investment adviser of . . . such company unless the terms of contract or agreement and any renewal thereof have been approved by the vote of a majority of directors. . . .
>
> It shall be the duty of the directors of a registered investment company to request and evaluate, and the duty of an investment adviser to such company to furnish, such information as may reasonably be necessary to evaluate the terms of any contract whereby a person undertakes regularly to serve or act as investment adviser of such company. (Emphasis added.)

In short, the 1940 Act imposes the precise same disclosure requirements on every adviser to an investment company -- including "A" -- regardless of whether the adviser is registered under the Investment Advisers Act of 1940. Accordingly, prior to the initial approval of "A" by the Trust's Board of Trustees, "A" provided the Board with all relevant information, including (1) the experience of "A" in managing portfolio assets in general and indexed assets in particular, (2) the identities and experience of the particular "A" employees who would be primarily responsible for managing the Trust's account, (3) the proposed method by which "A" intends to implement the Trust's stated investment objectives and policies, (4) the basis for "A"'s proposed fees, and (5) any other information requested by the Board. Section 15(c) requires that "A" provide such information at each annual renewal of the contract between the Trust and "A".

You also explained that, like the principals of an applicant for registration as an investment adviser, the principals of a bank insured by the Federal Deposit Insurance Corporation ("FDIC"), such as "A", are subject

to a fitness examination in that the bank effectively is prohibited from employing any person who has been convicted of a crime involving dishonesty or breach a trust without the prior consent of the FDIC. 7/

Accordingly, based upon the foregoing and in furtherance of the House Committee Report, the Division will not recommend that the Commission take any enforcement action against "A" if it fails to register as a CTA in connection with providing commodity interest trading advice to the Trust as set forth above. 8/

You should be aware that this position does not excuse "A" from compliance with any otherwise applicable requirements contained in the Act or in the Commission's regulations thereunder. For example, it remains subject to the antifraud provisions of Section 4o of the Act, 7 U.S.C. §6o (1982), and the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations, 17 C.F.R. Parts 15, 18 and 19 (1986). 9/

The position adopted herein is based upon the representations that you have made to us, as stated above. Any different, changed or omitted facts or conditions might require us to reach different conclusions. In this connection, we request that you notify us immediately in the event the operations and activities of "A" change in any way from that as represented to us. Finally, this position is that of the Division of Trading and Markets and does not necessarily represent the views of the Commission or any other office or division of the Commission.

If you have any questions about this letter, please feel free to contact me or Barbara R. Stern, the Division's Assistant Chief Counsel, at 202/254-8955.

Very truly yours,

Andrea M. Corcoran
Director

cc: Daniel A. Driscoll, National Futures Association

7/ Compare Section 203(e) of the Advisers Act, 15 U.S.C. §80b-3(e) (1982), to Section 19 of the Federal Deposit Insurance Act, 12 U.S.C. §1829 (1982).

8/ See supra, n. 5. Similarly, and as you have requested, the Division will not recommend that the Commission take any enforcement action against the associated persons ("APs") of "A" if they fail to register as such in connection with such activity.

9/ The APs of "A" similarly remain subject to Section 4o.