CFTC Letter No. 00-67

May 26, 2000

No-Action

Division of Trading & Markets

Re: Rules 4.7(a) and 4.7(a)(1)(ii)(B)(*2*)(*xi*)-- Request for confirmation of continuing effectiveness of prior relief if the permissible range of non-QEPs that may participate in a CPO's pools is expanded to include employees of the CPO's parent company who are not accredited investors as defined in SEC Regulation D

Dear :

This is in reference to your letter dated March 30, 2000 to the Division of Trading and Markets (the "Division") of the Commodity Futures Trading Commission (the "Commission"), as supplemented by your letters dated April 17, 2000, May 4, 2000 and May 10, 2000 and by telephone conversations with Division staff. By your correspondence you request on behalf of "P" confirmation that certain no-action letters issued by the Division with respect to the activities of "P" will remain in effect if "P" expands the permissible range of participants in pools operated by it ("Q", "R" and "S", collectively "Investment Vehicles") to include employees of "P's" parent company "T" who are neither qualified eligible participants ("QEPs") as defined in Commission Rule 4.7(a),[1] nor accredited investors as defined in Regulation D[2] under the Securities Act of 1933.[3]

Based upon the representation in your correspondence, we understand the facts to be as follows. "P" is registered with the Commission as a commodity pool operator ("CPO") and is a wholly-owned subsidiary of "T", a privately-held corporation which (together with its subsidiaries) you describe as an internationally known business consulting and management firm. "P" operates and administers the Investment Vehicles (as well as other investment funds that are not commodity pools) for the benefit of certain eligible employees of "T" ("Eligible Employees"), to whom the funds are offered as a benefit of their employment. Eligible Employees presently include "T's" shareholders (all of whom are senior professionals or senior administrators of "T"), certain retired Directors of "T", the director of "T's" Investment Programs and the director of "T's" European Investment Programs.

Neither "P" nor any principal thereof is paid a fee or commission in connection with solicitations for the Investment Vehicles. "P" does not receive a management or incentive fee from the Investment Vehicles. However, fees and expenses incurred by or allocable to the Investment Vehicles, including legal and accounting fees and transaction-related fees, are generally borne by the Investment Vehicles. You indicate that "P" receives a partial expense reimbursement from each Investment Vehicle in an amount equal to up to 0.50 percent of the Investment Vehicle's net asset value, subject to the disclosure of this arrangement to, and receipt of consent from, each participant in the affected Investment Vehicle. Certain employees of "T" provide administrative support to the Investment Vehicles and are compensated by "T" for their services in this regard.

The Division previously has issued a number of no-action letters for the benefit of "P" in connection with its structuring and implementing investment opportunities for Eligible Employees (the Prior No-Action Letters).[4] Among the representations made by "P" in connection with the Prior No-Action letters is that each of the employees participating in the pools for which relief was sought was an accredited investor. Now, in order to attract and retain essential employees, "T" has asked "P" to make participation in the Investment Vehicles available to persons who are neither QEPs nor

accredited investors. Participation is entirely voluntary. Specifically, the following modifications are proposed:

Employees who are accredited investors will continue to be required to meet the income requirements of Rule 501(a)(6) of Regulation D under the Securities Act of 1933, but no other specific restrictions. Such employees will no longer be required to have a net worth of $250,000, to have a graduate degree or to be a "T" management group member.

Employees who are not accredited investors will be required to have reportable income from all sources of at least $100,000 in the most recent year and a reasonable expectation of income from all sources of at least $140,000 in each year in which such person makes (or commits to make) investments in the relevant Investment Vehicle. Such employee will further be required to have either:

(a) a graduate degree (or foreign equivalent) in business, law, accounting, finance, economics, marketing, engineering, government, science, mathematics, or another business, scientific, technical or analytical field, and a minimum of three years of consulting, investment banking or other professional business or similar experience; or

(b) an undergraduate degree (or foreign equivalent) and a minimum of five years of consulting, investment banking or similar business or professional experience.

Furthermore, no person who is not an accredited investor will be permitted to invest in any year more than fifteen percent of his or her income from "T" and its affiliates for the immediately preceding year in the aggregate in the Investment Vehicles.

Pursuant to Section 6(b) of the Investment Company Act of 1940 (the "IC Act")[5] one of the Investment Vehicles (Partners Income Fund) has obtained from the Securities and Exchange Commission ("SEC") exemptive relief for all of the Investment Vehicles from the provisions of the IC Act, on the basis that the Investment Vehicles are "employees' security companies" as contemplated by IC Act Section 6(b). "P" expects that the order issued pursuant to IC Act Section 6(b) (the "6(b) Order") will be modified by the SEC to permit the change in employee eligibility standards set forth above.

In support of your request that the Division confirm the positions taken in the Prior No-Action Letters, you state that your client would agree to the following conditions and undertakings:

1. "P" will continue to comply with all of the conditions and undertakings set forth in the Prior No-Action Letters except with respect to the changes in eligibility requirements for participation in the Investment Vehicles (as described above);

2. "P" will cause each Investment Vehicle using the modified eligibility requirements outlined above to comply with the audit requirement set forth in Rule 4.22(c), and will cause an annual report to be distributed to participants in the Investment Vehicles, and will file such annual reports with the Commission, as required by Rule 4.22(c);[6]

3. "P" will cause each participant in any Investment Vehicle using the modified eligibility requirements outlined above to receive an offering memorandum relating to such Investment Vehicle setting forth the material terms of investment prior to participation by such person; and

4. "P" will provide the Division with a copy of its amended 6(b) Order following receipt thereof, and will

inform the Division of any modifications required by the SEC to the eligibility requirements set forth above, in connection with granting the 6(b) Order, and "P" will comply with any conditions imposed by the SEC in connection with granting the 6(b) Order.

You further represent that all employees participating in the Investment Vehicles will receive full disclosures as to the nature and type of investments, and that each such employee can obtain access to the Investment Vehicles' books and records upon request.

Based upon the representations made in your correspondence and the conditions and undertakings proposed by "P", the Division believes that continued effectiveness of the Prior No-Action Letters is appropriate, in light of, among others, your representations concerning: (1) the purpose of expanding the class of Eligible Employees; (2) fees; (3) restrictions as to the percentage of income that may be contributed; (4) the voluntary nature of contributions to the Investment Vehicles; and (5) treatment of the Investment Vehicles by the SEC as exempt employees' securities companies. Accordingly, subject to compliance with the conditions and undertakings set forth above, the Division will not recommend that the Commission commence any enforcement action against "P" in connection with any of the activities specified in the Prior No-Action Letters if "P" modifies the requirements for participation in the Investment Vehicles in the manner specified above.

This letter does not excuse "P" or "T" from compliance with any other applicable requirements contained in the Commodity Exchange Act[7] or in the Commission's regulations issued thereunder. For example, each remains subject to all of the antifraud provisions of the Act and the Commission's regulations, to the reporting requirements for traders set forth in parts 15, 18 and 19 of the Commission's regulations and to all otherwise applicable provisions of Part 4.

This letter and the no-action positions confirmed herein are based upon the representations you have made to us and are applicable to "P" solely in its capacity as operator of the Investment Vehicles. Any different, changed or omitted material facts or circumstances might render these positions void. Also, the no-action positions confirmed herein are subject to compliance with any conditions set forth in the Prior No-Action Letters, as well as compliance with the conditions and undertakings set forth above. In this connection, we request that you notify us immediately in the event that the operations or activities of "P", "T" or the Investment Vehicles change in any material way from those represented to us. Further, the no-action positions taken herein are solely those of the Division and do not necessarily represent the views of the Commission or those of any other division or office of the Commission.

If you have any questions concerning this correspondence, please contact Chris Cummings, an attorney on my staff, at (202) 418-5445.

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 17 C.F.R. §230.501 - 508 (1999).

3 15 U.S.C. §§77a *et seq.* (1994).

4 *See* CFTC Staff Letter 97-12, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH)¶ 26,985 (March 7, 1997) (enforcement action would not be recommended if Security Benefit Life Insurance Company failed to register as a CPO in connection with offering a diversified income subaccount to eligible employees of "T" and if "P" claimed relief under Rule 4.7(a) for the diversified income subaccount, irrespective of the ten percent limitation in Rule 4.7 on assets invested in a Rule 4.7(a) exempt pool by a QEP pool with non-QEP members (the "10 Percent Limitation")); CFTC Staff Letter 96-61, [1994-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH)¶ 26,779 (August 6, 1996) (permitting "P" to claim relief under Rule 4.7(a) with respect to "U" notwithstanding participation by non-QEPs, and notwithstanding the 10 Percent Limitation); CFTC Staff Letter 96-53, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH)¶ 26,758 (June 26, 1996) (permitting eligible employees to transfer their interests in "V" to a trust for the benefit of the employee and/or spouse or immediate family member); CFTC Staff Letter 94-72, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH)¶ 26,161 (May 6, 1994) (permitting investment of more than ten percent of the assets of any of the Investment Vehicles in other Rule 4.7 exempt pools irrespective of the 10 Percent Limitation); and CFTC Staff Letter 94-11, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH)¶ 25,992 (December 17, 1993) (granting relief similar to Rule 4.7(a) in connection with operation of the Investment Vehicles, irrespective of participation by non-QEPs).

5 15 U.S.C. § 80a-6(b) (1994).

6 Inasmuch as relief under Rule 4.7(a) has been claimed with respect to each of the Investment Vehicles, audited annual reports would not ordinarily be required to be delivered to the participants of the Investment Vehicles.

7 7 U.S.C. § 1 *et seq*. (1994).