CFTC Letter No. 02-03
December 20, 2001
No-Action
Division of Trading and Markets

Re: Section 4m(1) -- Request for relief from CPO and CTA registration requirements for "V" as the operator and advisor of a collective investment vehicle for investment of assets of ERISA and government pension plans.

Dear :

This is in response to your letter dated December 11, 2000, to the Division of Trading and Markets (the "Division") of the Commodity Futures Trading Commission (the "Commission"), as supplemented by your letters dated May 17, 2001 and July 27, 2001, by the letter of "A" dated October 22, 2001, and by telephone conversations with Division staff. By this correspondence, you request that the Division not recommend that the Commission commence any enforcement action against "V" in connection with the operation of the "Company" if "V" does not register under Section 4m(1) [1] of the Commodity Exchange Act (the "Act")[2] as a commodity pool operator ("CPO") and a commodity trading advisor ("CTA").

Based upon your representations, we understand the facts to be as follows.

"V"

"V", the sponsor of the Company, was formed in 1999 to acquire and operate the fixed-income investment management business of "W".[3] "V" is wholly-owned by "X", a corporation established in ____, which, with its predecessors, has been engaged in the banking business since ____. Although it is registered with the Securities and Exchange Commission ("SEC") under the Investment Advisers Act of 1940 (the "IAA")[4] as an investment adviser ("IA"), "V" is not registered with the Commission as a CPO or as a CTA, and you represent that it does not hold itself out to the public as a CPO or as a CTA. None of "V" or its principals or officers is subject to statutory disqualification under Section 8(a)(2) or 8 (a)(3) of the Act.[5]

"V" is the Managing Member of the Company. Besides the Company, "V" currently provides commodity interest trading advice to five clients. "V" relies upon a claim of exemption from CTA registration under Commission Rule 4.14(a)(8)[6] with respect to these other clients.

The Company

The Company was organized June 18, 1999 to allow "V" to achieve certain efficiencies by placing together in one trading vehicle the assets of certain advisory clients, namely, qualified employee pension and profit sharing plans subject to Title I of the Employee Retirement Income Security Act of 1974 ("ERISA") and governmental plans as defined in Section 3(32) of Title I of ERISA (each a "Plan"). The Company comprises multiple investment portfolios (each called a "Series"), some or all of which may trade commodity interests as a hedge against changes in interest rates, market prices and currency fluctuations. A Series will engage in commodity interest trading solely for bona fide hedging purposes as defined in Rule 1.3(z)(1), and with respect to each Series the aggregate initial margin and premiums paid to establish positions in commodity interest contracts generally will not exceed 5 percent of the liquidation value of such Series' respective portfolio. The Company is the only investment fund sponsored by, or advised by, "V" that trades or intends to trade commodity interests.

Membership interests in each Series are offered on a continuing basis to a maximum of 100 persons. The minimum initial investment is $1 million and the minimum subsequent investment is $100,000, subject to waiver at the discretion of "V". Each Member will be: (1) either a "qualifying entity" under Commission Rule 4.5(b) or excluded from the definition of "pool" under Commission Rule 4.5(a)(4)(i)-(iii); and (2) a "qualified eligible person" as defined in Rule 4.7. Members receive monthly statements of net asset value, monthly transaction statements, an annual Schedule K-1, and, upon request, the Company's annual report, which contains certified financial statements.

Analysis

CPO Registration Relief

As you acknowledge in your correspondence, in operating the Company "V" would be acting as a CPO and, absent relief, it would be required to be registered as such. This is because the Company does not fall within the definition of "qualifying entity" under Rule 4.5, nor is it one of the types of entities excluded from the "pool" definition under Rule 4.5(a)(4)(i)-(iii). The Company is not a pension plan itself, but rather an investment vehicle whose participants are various unaffiliated Plans.

In support of your claim for CPO registration relief, you note certain prior Staff Letters issued to registered investment advisers acting as sponsors of group trusts. In Letter 97-94,[7] the investment vehicle involved was a group trust in which other trusts participated, each consisting of pension plan assets. The entity directing the investment of the group trust's assets was a state-regulated insurance company (and SEC-registered IA), and the investment fund through which the group trust's assets were invested was an account of the bank that acted as the group trust's trustee. Commodity interests were to be used solely for bona fide hedging purposes within the meaning of Rule 1.3(z)(1). Letters 94-52 and 93-91[8] each involved a group trust sponsored by a registered IA for employee benefit plans, and a bank or trust company unaffiliated with the group trust or its sponsor serving as the group trust's trustee. In each of these three letters the Division took a CPO (and a CTA) registration no-action position with respect to the sponsor conditioned upon compliance with the operating requirements of Rule 4.5. In the facts you present, although there is a registered IA ("V"), there is no group trust (and therefore, no

trustee), but rather an LLC (the Company), of which the sponsor ("V") is the managing member. Nevertheless, a similar pattern is present: assets have been combined into a single trading vehicle from plans which, if advised and managed individually by "V", would be qualifying entities within the meaning of Rule 4.5(b) or excluded from the pool definition under Rule 4.5(a)(4).

CTA Registration Relief

You also acknowledge that, in connection with providing commodity interest trading advice to the Company, "V" would be acting as a CTA and, absent relief, it would be required to register as such. This is because "V" cannot claim exemption from CTA registration under Rule 4.14(a)(8) with respect to advising the Company since that relief is available only to SEC-registered IAs who advise only Rule 4.5 qualifying entities or entities excluded from the "pool" definition under Rule 4.5. In support of your request for CTA registration relief the Division notes that: (1) "V" is registered with the SEC as an IA; and (2) "V" will be providing essentially the same commodity interest trading advice to the Company that it would be able to provide individually to each of the plans that are Members of the Company if "V" were advising them individually under a Rule 4.5 notice of eligibility (except that "V" will be restricting the Company's commodity interest trading to bona fide hedging transactions, and will not engage it in speculative commodity interest trading, a limited amount of which is permitted under Rule 4.5(c)(2)).[9]

Based upon the representations made in your correspondence and subject to the conditions set forth below, the Division will not recommend that the Commission commence any enforcement action against "V" based solely upon the failure of "V" to register as a CPO or as a CTA under Section 4m(1) of the Act.[10] This position is conditioned upon compliance with the conditions: (1) that "V" maintain at its main business address all books and records prepared in connection with its activities as the CPO and CTA of the Company, and (2) that it make such books and records available to any representative of the Commission, the National Futures Association and the United States Department of Justice in accordance with the provisions of Rule 1.31.

The position taken in this letter does not excuse "V" from compliance with any other applicable requirements contained in the Act or in the Commission's regulations issued thereunder. For example, "V" remains subject to all antifraud provisions of the Act, to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's rules and to all otherwise applicable provisions of Part 4. Moreover, this letter is applicable to "V" solely in connection with its serving as the CPO and the CTA of the Company.

This letter is based upon the representations you have made to us and is subject to compliance with the conditions set forth above. Any different, changed or omitted facts or circumstances might render the positions taken herein void. You must notify us immediately in the event that the operations or activities of "V" or the Company change in any material way from those represented to us. Further, this letter represents the views of this Division only and does not necessarily represent the views of the Commission or of any other office or division of the Commission.

If you have any questions concerning this correspondence, please contact me or Christopher W. Cummings, an attorney on my staff, at (202) 418-5450.

Very truly yours
John C. Lawton
Acting Director

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[1] 7 U.S.C. § 6m(1) (1994).

[2] 7 U.S.C. § 1 *et seq*. (1994), as amended by the Commodity Futures Modernization Act of 2000 ("CFMA"), Pub. L. No. 106-554, 114 Stat. 2763 (to be codified as amended in scattered sections of 7 U. S.C.).

[3] "W" is registered with the Commission as a CPO and a CTA, and with the Securities and Exchange Commission as an investment adviser.

[4] 15 U.S.C. § 80b-1 *et seq*. (1994).

[5] 7 U.S.C. § 12a(2) or § 12a(3) (1994), as amended.

[6] Commission rules referred to herein are found at 17 C.F.R. Ch I *et seq*. (2001).

[7] [1996-98 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,198 (November 21, 1997).

[8] [1992-94 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,116 (June 1, 1994) and [1992-94 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,857 (September 7, 1993), respectively.

[9] Thus, the Company will be held to a more restrictive limitation on commodity interest trading than is permitted for qualifying entities under Rule 4.5.

[10] This letter is not, and should not be understood as, creating a *de minimis* exception to the "pool" definition of Rule 4.10(d). On the contrary, the CPO registration no-action position taken herein is based upon, among other factors, the similarity of the facts represented and the undertakings made by "V" and the Company to the framework of Rule 4.5, including the IA registration status of "V" and, as discussed above, the nature of the Company's Members.