U.S. COMMODITY FUTURES TRADING COMMISSION

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DIVISION OF
TRADING & MARKETS

~~96-77~~ 96-76

October 21, 1996

Re: Section 4m(1) of the Act -- Relief from CPO and CTA Registration Requirements In Connection with Services Provided To OffShore Fund

Dear :

This is in response to your letter dated August 8, 1996 to the Division of Trading and Markets ("Division") of the Commodity Futures Trading Commission ("Commission"). By your letter, you requested relief on behalf of "U", an investment adviser registered under the Investment Advisers Act of 1940 ("IAA"), from the requirements of Section 4m(1) of the Commodity Exchange Act ("Act")[1/] that "U" register as a commodity pool operator ("CPO") and commodity trader advisor ("CTA") in connection with the services which it will provide to (the "Fund"), a fund organized in the Cayman Islands.

Based upon the representations made in your letter, as supplemented by telephone conversations with Division staff, we understand the pertinent facts to be as follows. "U" is a registered investment adviser under the IAA. It provides investment advice, principally to Mexican corporations and citizens investing in Mexican and other Latin American debt obligations. As of April 1, 1996, "U" had in excess of $200 million under management.

The Fund is organized in the Cayman Islands and will invest primarily in fixed income instruments issued by Mexican and Latin American governments, banks and corporations. Initially, these instruments will be dollar-denominated instruments but the Fund may invest a portion of its assets in Mexican-peso denominated obligations in the future. In order to protect the value of some portion of its holdings against currency risks, the Fund may enter into currency futures contracts for hedging purposes. It is anticipated that the value of any futures positions entered into on

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1/ 7 U.S.C. § 6m(1) (1994).

behalf of the Fund will not represent a material portion of the Fund's assets. In any event, the aggregate amount of initial margin deposits on the Fund's futures positions will not exceed five percent of the value of the Fund's total portfolio as provided in Rule 4.5(c)(2), and "U" expects that the value of the initial margin deposits on the Fund's futures positions will be substantially below that five percent limit. In essence, although the Fund does not qualify for relief pursuant to Commission Rule 4.5, it will be operated in a manner consistent with the provisions of Rule 4.5(c)(2).

"U" has assisted in organizing the Fund. In this regard, it obtained legal counsel to draft documents related to the organization of the Fund and chose the Administrator of the Fund.[2/] In addition, "U" will contract with non-United States persons and entities who will solicit participation in the Fund. No officer, director or employee of "U" will be a member of the Board of the Fund, solicit participation in the Fund, or engage in any marketing or promotional activity for the Fund. "U" will also act as investment adviser to the Fund. As investment adviser, "U" will have sole investment discretion for the Fund, will select investments for the Fund and will place purchase and sale orders for investments on behalf of the Fund. As a result of these activities, "U" will be acting as a CPO[3/] and CTA[4/] and, absent relief, will be required to register as such.[5/]

2/ Fees owed to the relevant entities for organizing the Fund will be paid from proceeds of the offering.

3/ In this regard, the Commission has stated that a pool's CPO typically is the person or persons who promote the pool, who have the authority to hire (and to fire) the pool's CTA and who select or change the pool's futures commission merchant ("FCM"). <u>See</u> 49 Fed. Reg. 4778, 4780 (February 8, 1984).

4/ <u>But see</u> Rule 4.14(a)(4), which provides an exemption from CTA registration for any person who is registered as a CPO and whose commodity trading advice is directed solely to, and for the sole use of, the pool(s) for which it is registered.

5/ "V", a Delaware limited partnership and part of the "W" group of companies, will serve as technical adviser to the Fund and "U". "V" is not affiliated with "U" or "U's" principals. "V" will advise "U" with respect to obtaining leverage financing for the Fund and to selecting investments for the Fund in Latin American debt obligations and derivatives on such Latin American debt obligations. "V" will not make investment decisions for the Fund (continued...)

The Administrator of the Fund will be "X", a Cayman Island corporation. The Administrator will be responsible for all administrative matters, including: (1) maintaining corporate and financial books and records of the Fund; (2) preparing periodic financial statements for the Fund; (3) making the various net asset calculations and the amount of dividends, if any, payable on the shares; (4) providing registrar and transfer agent services in connection with the issuance, transfer and redemption of the shares; and (5) performing all other accounting and clerical services necessary in administration of the Fund. "Y", the sole corporate director of the Fund and an affiliate of the Administrator, will have ultimate responsibility for managing the Fund. "X" and "Y" are unrelated to "U".

The Fund will not hold meetings or conduct any administrative activities within the United States. Shares in the Fund will not be offered to United States persons, nor will the Fund solicit in the United States. For the purposes of your request you employ a definition of "United States person" used in the Securities and Exchange Commission Regulation S, promulgated under the Securities Act of 1933.[6/] The Fund will require each subscriber to make an

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5/ (...continued)
or for "U". In a September 11, 1996 telephone conversation with Division staff, you represented that the Technical Advisory Agreement between "V" and "U" states that "V" will not provide advice concerning futures contracts or commodity option contracts or the use of such contracts by the Fund. We note that any relief granted "U" would not be applicable to "V".

6/ You represent that while the definition of United States person employed in Regulation S is similar to the definition usually used by this Division, the two are not the same. See, e.g., CFTC Interpretative Letter No. 92-3 [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,221 (Jan. 29, 1992)(defining United States person). Specifically, you represent that shares in the Fund will not be offered, sold or delivered, directly or indirectly, in the United States, its territories or possessions or any area subject to its jurisdiction, including the Commonwealth of Puerto Rico, or to any citizen or resident thereof (including any corporation, partnership or other entity organized or created under the laws of the United or any political subdivisions thereof) or to any estate or trust the income of which is subject to United States federal income taxation, regardless of its source or to any person, corporation, partnership or other entity qualifying as a "U.S. person" as defined in Rule 902(o) of Regulation S, 17 C.F.R. 230.902(o) (1996), under the Securities Act of 1933. However, the shares may be sold to persons deemed not to be United States
(continued...)

initial investment of $100,000.

In further support of your request, you represent that "U" does not and will not hold itself out generally as a CTA or a CPO. "U" also agrees to submit to such special calls as the Division may make of it in order to demonstrate compliance with the terms and conditions of any no-action relief granted herein.

Based upon the representations made by you, we do not believe that it would be contrary to the public interest or the purposes of the Act if the requested relief were granted. Accordingly, the Division will not recommend that the Commission take enforcement action against "U" for violations of the CPO and CTA registration requirements of Section 4m(1) of the Act solely based upon "X's" failure to register as the CPO and CTA of the Fund in connection with its advising on the purchase or its purchasing of foreign currency futures contracts on behalf of the Fund.[7/] Further, we confirm that based upon the relief from the CPO and CTA registration requirements provided herein, "U" is not subject to the Disclosure Document delivery requirements of Rules 4.21 or 4.31 or the recordkeeping requirements of Rules 4.23 or 4.33. This relief is, however, subject to the conditions that: (1) "U" remains duly registered as an investment adviser; (2) "U" submits to such special calls as the Division may make of it to assure compliance with the terms of the relief granted herein; and (3) the Fund, or any persons affiliated therewith, will not undertake any marketing activity for the purpose, or that could reasonably be expected to have the effect, of soliciting participation from United States persons, as used herein.

6/ (...continued)
persons under Rule 902(o)(2) and (o)(6) of Regulation S, namely, any discretionary account or similar account (other than an estate or trust) held for the benefit or account of a person that is not a United States person by a dealer or other professional fiduciary organized, incorporated or (if an individual) resident in the United States or to any branch or agency of a United States insurance company or bank located outside of the United States that operates for valid business reasons and is subject to substantive regulation in the jurisdiction where located.

7/ We note that in CFTC Interpretative Letter No. 95-67, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,497 (July 17, 1995), the Division provided no-action relief such that registered investment advisers were not required to register as CTAs or CPOs if their only futures-related activity consisted of providing advice to or exercising trading discretion on behalf of clients with respect to foreign currency futures or options traded on the Chicago Mercantile Exchange.

This letter is based upon the representations that have been made to us and is subject to compliance with the conditions set forth above. Any different, changed or omitted facts or conditions might require us to reach a different conclusion. In this connection, we request that you notify us immediately in the event that the activities of "U" or the Fund change in any way from those represented in your letter as supplemented. This letter is applicable to "U" solely in connection with its services to the Fund as described above and solely in connection with any foreign currency futures trading activities undertaken on behalf of the Fund for hedging purposes. Further, "U" remains subject to all otherwise applicable provisions of the Act and Commission rules, including the antifraud provisions of Sections 4b and 4o of the Act,[8/] the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission rules, and any applicable provisions of Part 4.

This letter represents the views of this Division only. It does not necessarily reflect the views of the Commission or of any other division or office of the Commission. If you have any questions concerning this letter, please contact me or Thomas E. Joseph, an attorney on my staff, at (202) 418-5450.

Very truly yours,

Susan C. Ervin
Chief Counsel

8/ 7 U.S.C. §§ 6b & 6o (1994).