

CFTC Letter No. 98-04**February 21, 1997****Division of Trading & Markets**

Re: Section 4m(1) -- Request for confirmation that "S" would not be a commodity pool operator ("CPO") as a result of providing certain services to registered CPOs.

Rule 4.23(a) -- Request to permit "T" and "B" to maintain certain required books and records concerning pools they operate at a location other than their main business office.

Dear :

This is in response to your letter dated December 13, 1996 to the Division of Trading and Markets (the "Division") of the Commodity Futures Trading Commission (the "Commission"), as supplemented by the prior letter of "A" of your firm on behalf of "S" dated November 11, 1996, by the December 24, 1996 facsimile transmission of "C" and "B", and by telephone conversations with Division staff. By your correspondence, you request on behalf of "T", "B" and "S": (1) confirmation that "S" would not be deemed to be a commodity pool operator ("CPO") as a result of providing certain services to "T" and "B" in connection with certain commodity pools they operate (the "Pools");¹ and (2) exemptive relief from Rule 4.23(a)² to permit the CPOs to keep certain books and records of the Pools at "S's" office. Based upon the representations made in your correspondence, we understand the relevant facts to be as follows. "T", a registered commodity trading advisor ("CTA"), became registered as a CPO effective December 12, 1996. "T" intends to operate and market two new commodity pools, "U" and "V". Additionally, as of December 31, 1996, "T" became a co-general partner and co-CPO with "B" of an existing pool, "W".

"S" is registered as a CPO and as a CTA, and it operates and provides commodity interest trading advice to several pools. An affiliate of "S", "X", is engaged in data processing and technological support for the financial services industry.³ "T", "B" and "S" intend to enter into a contract pursuant to which "S" will perform certain of the recordkeeping functions that "T" and "B" would otherwise be obligated to perform with respect to the Pools, as well as a range of other administrative services, as described below. Rather than develop internally the capability to perform these functions, "T" prefers to employ a service provider "S" already equipped to perform them.

Under the proposed arrangement, "S" would perform the following services ("Services") in lieu of, but subject to the supervision of, the respective Pool's CPO: (1) maintenance of certain of the original books and records of the Pool; (2) calculation of the Pool's net asset value; (3) preparation of monthly Account Statements; (4) processing of transactions from broker equity runs; (5) production of year-end financial statements and tax statements for review by the CPO and the Pool's accountants; (6) production of performance tables; (7) provision of daily estimated net asset value when requested by existing Pool participants and response to participants' technical inquiries about account statements and accounting matters; (8) payment to third parties of fees and expenses approved by the CPO; (9) processing of subscriptions and redemptions approved by the CPO; (10) mailing of monthly and annual reports and tax information to Pool participants; and (11) assisting in the preparation of, and maintenance of, all account and trading documentation (e.g., customer agreements, give-up agreements and swap agreements). To assist it in performing some or all of these functions, "S" may contract with "X" and possibly one or more additional third parties ("S" and such third parties are referred to collectively herein as the "Service Providers"). The Disclosure Document for each of the Pools will contain information concerning the nature of "S"'s administrative services, the amount of the administrative fee to be charged to the Pool, and the location at which "S" will maintain the original books and records for the pool.

"T" (and "B", as applicable) will remain responsible for compliance with all requirements of the Commodity Exchange Act (the "Act")⁴ and the Commission's regulations promulgated thereunder applicable to CPOs, including proper performance of the Services by the Service Providers. You note that for each of the Pools the CPO will: (1) have sole responsibility for the form and content of the Pool's Disclosure Document, subscription agreement and marketing materials; (2) conduct (and have sole responsibility for) solicitation of prospective pool participants, including delivery of the Disclosure Document;⁵ (3) receive and maintain original subscription documents, as well as the signed acknowledgments required pursuant to Rule 4.21(b); (4) determine pool participant suitability; (5) engage and terminate the engagement of persons performing services for the Pool; and (6) have sole responsibility for the selection, retention and termination of all CTAs for the Pool. In supervising the services provided by "S", the CPO will review and approve each report to pool participants before the report is distributed. "S" will permit the CPO to review any of the pool records and documentation maintained by "S" and to consult with "S" personnel involved in providing the Services, at any time. Pool records kept by "S" will be maintained (and shall be accessible to pool participants, the Commission and other authorities) in accordance with Rule 4.23 except as discussed below.

Based upon the representations made in your correspondence, it appears that "S" will be providing administrative assistance to, and acting as agents of, the CPOs in providing the Services. The CPOs remain responsible under the Act and Commission regulations for

compliance with the requirements of Part 4 and all other applicable statutory and regulatory requirements. Accordingly, we confirm that performance by "S" of the Services on behalf of "T" and "B" will not cause the Division to require "S" to register as a CPO with respect to any of the Pools. As an agent of "T" and "B", however, "S" (and any other Service Provider) is subject to the requirements of the Act and Commission rules with respect to their activities on behalf of the CPOs and the Pools.⁶ Furthermore, "S" is reminded that this position does not affect in any way "S's" obligation under Rule 4.23 to make and keep the books and records specified in Rule 4.23(b) concerning "S's" and its principals' commodity interest trading and all other activities of "S" (to which rule "S" is already subject as a registered CPO operating its own pools).

"T" and "B" also seek to have "S" maintain at "S's" office the books and records required by the following: Rule 4.23(a)(1) (itemized daily record of commodity interest transactions), Rule 4.23(a)(2) (journal of receipts and disbursements), Rule 4.23(a)(4) (participants' names and addresses and property received from or disbursed to participants), Rule 4.23(a)(5) (records forming the basis of any ledger entries), Rule 4.23(a)(6) (general ledger), Rule 4.23(a)(7) (confirmations, purchase and sale statements and monthly account statements), Rule 4.23(a)(8) (canceled checks, bank statements, journals, ledgers, invoices, and other pool operation records), Rule 4.23(a)(10) (statements of financial condition), and Rule 4.23(a)(11) (statements of income (loss)). Each of the Pools' respective CPOs will keep at its own office the records required to be maintained pursuant to Rule 4.23(a)(3) (written acknowledgment by participant of Disclosure Document receipt) and Rule 4.23(a)(9) (originals or copies of all materials distributed to participants or received from the pool's CTAs).

Based upon the representations in your correspondence, and pursuant to the authority delegated in Rule 140.93(a)(1), the Division hereby exempts "T" and "B" in connection with the operation of the Pools from the requirement of Rule 4.23 to keep the books and records required by Rules 4.23(a)(1) and (a)(2), 4.23(a)(4) through (a)(8) and 4.23(a)(10) and (a)(11) at their main business offices, subject to compliance with the conditions stated herein. "T" and "B" remain responsible for compliance with all other requirements of Rule 4.23. This relief is subject to the conditions that:

1. Duplicates of such books and records of the Pools will be kept by the respective CPOs at their main business offices;
2. Books and records subject to Rule 4.23 and maintained by "S" must be made available to pool participants for inspection and copying during normal business hours at "S's" office, and upon request of a participant, copies of such books and records must be sent by "S" by mail within five business days if the pool participant pays reasonable reproduction and distribution costs;

3. All books and records of the Pools, whether maintained at "S's" office or at the main business office of the Pool's CPO, must be open to inspection by any representative of the Commission or of the United States Department of Justice;

4. Upon request of a Commission or National Futures Association representative, "S" or the Pool's CPO, as applicable, will promptly provide copies of any Pool books or records maintained by them in accordance with Rule 1.31(b); and

5. The Disclosure Documents for the Pools will clearly apprise Pool participants of the location and accessibility of each Pool's records.

This letter is applicable to "T" and "B" only in connection with the operation of the Pools, and to "S" solely in connection with performance by "S" of the Services. Pursuant to Section 2(a)(1)(A) (iii) of the Act,⁷ "T" and "B" remain responsible for the acts of "S" and the other Service Providers. Furthermore, this letter does not excuse either "T", "S" or "B" from compliance with any other applicable requirements contained in the Act or in the Commission's regulations issued thereunder, including all other provisions of Part 4. For example, "S" remains subject to the antifraud provisions of Section 40 of the Act⁸ with respect to activities performed by the Service Providers on behalf of "T" and "B".

This letter is based upon the representations provided to us, and is subject to compliance with the conditions set forth above. Any different, changed or omitted facts or circumstances might require us to reach a different conclusion. In this connection, we request that you notify us immediately in the event the operations or activities of "T", "S" or "B" change in any way from those represented to us (including without limitation, any change in the location at which records of the Pools are kept).

Further, this letter represents the position of the Division of Trading and Markets 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 correspondence, please contact me or Christopher W. Cummings, an attorney on my staff, at (202) 418-5445.

Very truly yours,

Susan C. Ervin

Chief Counsel

¹ The Pools are "U" and "V", both of which are operated by "T", and "W", operated by "T" and "B" as

co-CPOs. For convenience, the term "CPO" when used in reference to the Pools refers to "T" in the case of "V" and "U", and to "T" and "B" in the case of "W".

² Commission rules referred to herein are found at 17 C.F.R. Ch. 1 (1996).

³ "S's" president, "D", is also Chairman of "X".

⁴ 7 U.S.C. § 1 et seq. (1994).

⁵ In response to staff inquiries you have represented that neither "S" nor any person associated or affiliated with "S" will be engaged to solicit participants for any of the Pools.

⁶ Moreover, an agent is a fiduciary with respect to matters within the scope of its agency. Restatement (Second) of Agency § 13 (1958).

⁷ 7 U.S.C. § 2 (1994).

⁸ 7 U.S.C. § 60 (1994).