



COMMODITY FUTURES TRADING COMMISSION
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DIVISION OF
TRADING AND MARKETS

September 9, 1994

Re: Rules 4.31 and 4.32; Rule 3.12 -- Registered
CTA/Investment Adviser Providing Commodity Advice to
Foreign Investment Companies

Dear :

This is in response to your letter dated July 19, 1994, as supplemented by telephone conversations with staff of the Division of Trading and Markets (the "Division") of the Commodity Futures Trading Commission (the "Commission"), in which you request, on behalf of "X", that the Division not recommend that the Commission take any enforcement action against "X" if it provides commodity interest trading advice to certain foreign investment companies (as defined below) and (1) fails to comply with the disclosure and recordkeeping requirements of Commission Rules 4.31 and 4.32;^{1/} and (2) permits persons to become associated with "X" without such persons being registered as associated persons ("APs") of "X".

Based upon the representations made in your letter, as supplemented, we understand the relevant facts to be as follows. "X" is registered with the Commission as a commodity trading advisor ("CTA") and is also registered with the Securities and Exchange Commission ("SEC") as an investment adviser under the Investment Advisers Act of 1940. Subsequent to "X's" registration as a CTA, the Commission proposed and adopted Rule 4.14(a)(8) which, among other things, exempts a registered investment adviser from registering as a CTA, provided certain conditions are met. As a registered investment adviser, "X" desired to avail itself of the relief provided by Rule 4.14(a)(8) without abandoning its CTA registration. Accordingly, "X" sought, and by letter dated October 19, 1987 the Division granted, relief from the disclosure and recordkeeping requirements of Rules 4.31 and 4.32 (the "1987 Relief").

^{1/} Commission rules referred to herein are found at 17 C.F.R. Ch. 1 (1994).

The 1987 Relief was conditioned upon "X" limiting its commodity interest trading advice as follows:

1. It would direct its commodity interest trading advice solely to, and for the sole use of, entities which are excluded from the definition of the term "pool" under Rule 4.5 or are qualifying entities under Rule 4.5 for which notices of eligibility would be filed;
2. Its commodity interest trading advice would be solely incidental to its business of providing securities trading advice to such entity;
3. It would employ only such strategies which are consistent with eligibility status under Rule 4.5; and
4. It would not hold itself out as a commodity trading advisor.

As part of the 1987 Relief, "X" was allowed to permit persons to become associated with "X" after the date of the letter (October 19, 1987) without registering as APs of "X", (provided that the name of each such AP would be provided to the Division along with a representation that the AP is not subject to statutory disqualification under Section 8a(2) or 8a(3) of the Commodity Exchange Act (the "Act")^{2/}). "X" was further required to contact the Division for guidance in the event that "X" decided to provide commodity interest trading advice other than in accordance with the restrictions set forth in the Division's October 19, 1987 letter.^{3/}

By letter dated July 7, 1994, the Division modified the 1987 Relief to permit "X" to continue to provide commodity interest trading advice to entities which are excluded from the definition of the term "pool" under Rule 4.5 or are qualifying entities under Rule 4.5 for which notices of eligibility have been filed ("Rule

^{2/} 7 U.S.C. §§ 12a(2) or 12a(3) (1988 & Supp. IV 1992).

^{3/} Previously, by letter dated January 23, 1986, the Division had exempted all of the general partners of "X", with the exception of the partner designated (in a letter signed by a person with authority to bind the partnership) as having final supervisory authority, including authority to hire and fire, with respect to the futures and commodity option activity of "X", from the AP registration provisions of Rule 3.16(a). The exemption thus granted was conditioned upon registration as an AP of every employee or partner of "X" actually soliciting futures or commodity option accounts or supervising such activity.

4.5 Entities"), while also providing commodity interest trading advice to "qualified eligible clients" ("QECs") in reliance upon the exemption provided by Rule 4.7(b).^{4/}

"X" now seeks to have the 1987 Relief further modified to permit "X" to provide commodity interest trading advice to foreign investment companies ("Foreign Investment Companies"), which term "X" defines to mean:

investment companies that: (1) are not registered under the Investment Company Act [of 1940, as amended (the "Investment Company Act")], (2) are organized under the laws of a jurisdiction other than the United States or any state thereof, (3) maintain their principal place of business outside of the United States and (4) do not offer their securities to "United States persons." (Emphasis in original)^{5/}

You represent that the prospectus of each Foreign Investment Company and the policies of its management would prohibit ownership of its shares, either directly or indirectly, by any United States person. Investors in such Foreign Investment Companies are required to certify that they are not United States persons and are required to give notice if they establish residence in the United States. The Foreign Investment Companies which "X" intends to advise do not direct their marketing or sales efforts to United States persons or in the United States (as defined). You further represent that "X" "reasonably believes" that no more than 5% of the beneficial interests in each Foreign Investment Company is held by United States citizens residing abroad.

Because the Foreign Investment Companies which "X" intends to advise are not registered under the Investment Company Act (or otherwise within the categories specified in Rule 4.5), they are not eligible persons or qualifying entities under Rule 4.5(a) or (b). Accordingly, providing commodity interest trading advice to the Foreign Investment Companies would be outside the scope of the 1987 Relief as modified.

^{4/} Inasmuch as QECs are not necessarily Rule 4.5 Entities, "X" would not be limiting its commodity trading advice exclusively to Rule 4.5 Entities as required by the terms of the 1987 Relief.

^{5/} For purposes of the preceding definition and its request for relief, "X" uses the definitions of "United States" and "United States person" adopted by the Division in Interpretative Letter No. 92-3, [1990-92 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25221 (January 29, 1992).

In further support of your request you have represented that:

- (1) Each Foreign Investment Company will be operated in accordance with the criteria set forth in Rule 4.5(c)(2)^{6/} and "X" will employ only strategies that are consistent with eligibility status under Rule 4.5;
- (2) "X" will provide commodity interest trading advice to a Foreign Investment Company in a manner solely incidental to "X"'s business of providing securities advice to such Foreign Investment Company;
- (3) "X" will not hold itself out as a CTA to any Foreign Investment Company;
- (4) "X" will submit to such special calls as the Division may make of it to demonstrate compliance with the terms and conditions of this "no-action" position; and
- (5) The name of each person associated with "X" after October 19, 1987, and whose activities as an AP are limited to dealing with (a) Rule 4.5 Entities or (b) Foreign Investment Companies, will be provided to the Division along with a representation that the AP is not subject to statutory disqualification under Section 8a(2) or 8a(3) of the Act.^{7/}

Based upon compliance with the foregoing representations, and consistent with our prior practice in this area^{8/} the Division will not recommend that the Commission take any enforcement action

^{6/} Although because of its foreign nature, the Foreign Investment Company would not be registered (and absent an exemption from the Securities and Exchange Commission could not register) as an investment company under the Investment Company Act of 1940 and therefore the Foreign Investment Company would not be an eligible person or a qualifying entity under Commission Rule 4.5(a) or (b).

^{7/} Persons involved in the solicitation (or supervision of the solicitation) of discretionary accounts of QECs under Rule 4.7(b), however, will be registered as APs. You have informed Division staff that "X" intends to request relief from this requirement. The Division will consider whether to grant such relief at the time the request is made.

^{8/} See, e.g., Division of Trading and Markets Interpretative Letter No. 88-5, [1987-90 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,166 (February 2, 1988); and Interpretative Letter No. 93-108 [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,900 (November 3, 1993).

against "X" if it provides commodity interest trading advice to Foreign Investment Companies and (1) fails to comply with the disclosure and recordkeeping requirements of Rules 4.31 and 4.32 with respect to Rule 4.5 Entities and Foreign Investment Companies; and (2) permits persons to become associated with it whose activities are limited to dealing with (a) Rule 4.5 Entities or (b) Foreign Investment Companies without such persons being registered as APs of "X".

The position taken herein is based upon the representations that you have made to us. Any different, changed or omitted facts or circumstances might require us to reach a different conclusion. Therefore, we request that you notify us immediately in the event that the operations or activities of "X" or of any Foreign Investment Company advised by "X" change in any way from those as represented to us. Further, this letter does not excuse "X" from compliance with any otherwise applicable requirements contained in the Act^{9/} or the Commission's regulations thereunder. For example, "X" remains subject to the antifraud provisions of Section 40 of the Act,^{10/} to the reporting requirements set forth in Parts 15, 18 and 19 of the Commission's regulations and to all other applicable provisions of Part 4.

This letter represents the position of the Division only and does not necessarily reflect the position of the Commission or 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) 254-8955.

Very truly yours,

Susan C. Ervin
Chief Counsel

^{9/} 7 U.S.C. § 1 et seq. (1988 & Supp. IV 1992).

^{10/} 7 U.S.C. § 60 (1988 & Supp. IV 1992).