

CFTC Staff Issues Self-Executing Registration Relief for Certain Delegating CPOs

On October 15, 2014, the Commodity Futures Trading Commission (“CFTC”) staff issued [Letter 14-126](#) (the “October Letter”), which provides self-executing registration relief to a commodity pool operator (“CPO”) of a fund that delegates its rights and obligations as a CPO to another entity that will serve as the registered CPO of the fund, if certain conditions are met. The October Letter replaces [CFTC Letter 14-69](#) (the “May Letter”), which required each CPO to receive its own no-action letter to be able to delegate its CPO functions to a registered CPO (discussed in a previous Ropes & Gray Alert, available [here](#)). If the conditions of the October Letter are not met, a CPO will still need to obtain its own no-action letter. We recommend that private fund sponsors take this opportunity to review the CPO status of the parties that may be CPOs with respect to the fund (i.e., a fund’s general partner, manager, directors and/or trustees), and consider whether the fund can rely on the self-executing relief made available by the October Letter to avoid registration obligations otherwise applicable to each CPO.

Background

Historically, the CFTC staff has considered a private fund’s general partner, manager, directors or trustees to be the fund’s CPO. Accordingly, a fund sponsor that uses special purpose entities to serve as general partners or limited liability company managers of the funds it advises, or that has directors or trustees for its funds, may have multiple CPOs, each of which would be required (absent no-action relief from the CFTC) to register separately as a CPO or claim an applicable exemption. The May Letter established a streamlined process whereby the CFTC staff would grant relief on an expedited basis when certain criteria were met and a form of request was filed. For many, satisfying the criteria under the May Letter proved to be problematic. For instance, affiliated directors often could not use the streamlined process because they are involved in solicitation of investors or in portfolio management for the fund. Other CPOs could not use the streamlined process because they appointed trading advisors with investment management authority over fund assets. In addition, CPOs were reluctant to affirmatively attest that they would maintain the books and records of the fund in accordance with CFTC Rule 1.31 (which contains outdated technical provisions). Moreover, as it turned out, the CFTC staff actually granted only a small number of the requests they received based on the streamlined process.

The October Letter addresses many of the impediments to streamlined relief under the May Letter. Specifically, the October Letter revised the enumerated criteria to allow a CPO to appoint third-party trading advisors, to allow directors to participate in solicitation (as associated persons of the registered CPO) and in portfolio management (as principals or employees of the registered CPO), and to remove the attestation of compliance with Rule 1.31. Significantly, CPOs will no longer be required to submit requests for relief. So long as the criteria enumerated in the October Letter are satisfied, the relief under the October Letter is self-executing.

The Criteria for Relief

In the October Letter, the CFTC staff set forth specific criteria that must be met to qualify for the self-executing relief. In essence, there must be a legally binding document pursuant to which the delegating CPO has delegated to the designated CPO all of its investment management authority with respect to the fund (the CPO may in turn appoint third-party trading advisors). If a delegating CPO is not an individual, then the legally binding document must require the delegating and designated CPOs to be jointly and severally liable for any violation of the Commodity Exchange Act or the CFTC rules of the other in connection with the fund. Similarly, if a delegating CPO is an individual and is affiliated with the designated CPO, then the legally

binding document must require the delegating and designated CPOs to be jointly and severally liable for one another's violations of the Commodity Exchange Act or the CFTC rules with respect to the fund. If a delegating CPO is an individual but is not affiliated with the designated CPO, there is no such requirement. Affiliation for this purpose is based on being a member of management or an employee of the designated CPO (or an affiliate), having substantial beneficial ownership of the designated CPO (or an affiliate), or having an interest or relationship that could interfere with the ability to act independently of management of the designated CPO (or an affiliate).

The delegating CPO must not participate in the solicitation of investors except as an associated person of the registered CPO, and must not manage any property of the fund except as a principal or employee of the designated CPO or of a trading advisor for the fund. There must be a legitimate business purpose for the designated CPO being a separate entity from the delegating CPO. The designated CPO must be registered as a CPO and must maintain the books and records of the delegating CPO with respect to the fund, and the delegating CPO must not be subject to a statutory disqualification under the Commodity Exchange Act. Finally, if neither the delegating CPO nor the designated CPO is an individual, then one such CPO must control, be controlled by, or be under common control with the other CPO (criterion #6).

Many CPOs that did not previously qualify for the streamlined approach under the May Letter will now qualify for the relief under the October Letter. Issues remain, however, including those arising under criterion #6. As a result of criterion #6, unaffiliated entity directors, trustees, general partners or managing members that are delegating CPOs will be required to request no-action relief from the CFTC staff. We understand that the CFTC staff is aware that this issue remains and that the staff may consider addressing it in follow-on guidance or in a rulemaking process.

Next Steps

The October Letter does not affect the validity of any prior staff letter issued with respect to CPO registration relief for a delegating CPO, including any relief granted pursuant to the May Letter. However, the staff will no longer consider requests for relief under the May Letter, including any requests previously submitted that are still pending. If a CPO has not received a delegation no-action letter from the staff, it should consider taking advantage of the relief under the October Letter.

To take advantage of the relief under the October Letter, CPOs should first review the criteria and confirm that the criteria are satisfied. This process would include reviewing the applicable investment management or separate delegation agreements to ensure that they contain provisions addressing the requirements of the October Letter, and amending these agreements as needed. CPOs should also establish a process to make sure that agreements for future funds contain the necessary provisions to meet the criteria and that all agreements are updated as needed to reflect changes, including changes in directors.

A CPO that is unable to qualify for the relief set forth in the October Letter should prepare its own request for delegation no-action relief based on its specific facts and circumstances and submit it to the staff for consideration.

Please contact [Deborah Monson](#), [Jeremy Liabo](#), or the Ropes & Gray attorney who usually advises you with any questions you may have or if you would like additional information.

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