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Client Alert | Investment Management

CFTC Staff Permits Registered CPO to Treat Certain Employees as Qualified Eligible Persons

The Market Participants Division (Division) of the U.S. Commodity Futures Trading Commission (CFTC) issued [CFTC Letter 24-05](#) on May 7, providing exemptive relief to Two Sigma Investments LP and its affiliates (collectively, Two Sigma), a registered commodity pool operator (CPO), pursuant to which certain employees of Two Sigma may be considered qualified eligible persons (QEPs) under CFTC Regulation 4.7(a)(2)(viii)(A)(4) (the QEP tenure conditions).

Two Sigma sought the exemptive relief so that it could continue to operate commodity pools that are “employees’ securities companies” (ESCs) pursuant to CFTC Regulation 4.7 while accepting investments from certain senior employees who do not currently meet QEP tenure conditions, which require an employee or agent to be (1) an accredited investor and (2) to have “been employed or engaged by the exempt pool, commodity pool operator, commodity trading adviser, investment adviser or affiliate, or by another person engaged in providing commodity interest, securities or other financial services, for at least 24 months.” Two Sigma could not deem the employees to be QEPs by virtue of being “knowledgeable employees,” pursuant to CFTC Regulation 4.7(a)(2)(vii), because neither of the employees (1) was an executive officer, director, trustee, general partner, advisory board member or person serving in a similar capacity or (2) participated in the investment activities of Two Sigma, or engaged in substantially similar activities for another company, for at least 12 months.

Two Sigma, a quantitative investment management firm, recruits heavily from the technology industry, particularly for Two Sigma’s Modeling and Engineering Division, which is responsible for critical activities similar to Two Sigma’s research and development personnel. The two senior officers (the modeling and engineering officers) for whom the exemptive relief was requested “perform a variety of tasks and functions that are routine duties of financial services sector employees and that are critical to Two Sigma’s operations, like equities and macro research, portfolio management, trading, trading engineering, modeling engineering and data engineering,” according to the exemptive letter. Accordingly, Two Sigma argued that the modeling and engineering officers, while not meeting the QEP tenure conditions, possess advanced education, other prior work experience and deep knowledge of Two Sigma’s operations and trading activities such that considering them QEPs, for the limited purpose of investing in the ESCs, is appropriate. In support of its request, Two Sigma pointed to prior relief

granted by CFTC staff in similar situations when the facts and circumstances merited exemptive relief.¹

In granting the exemptive relief, the Division recognized the specific education and professional expertise of the modeling and engineering officers, as well as their deep knowledge and involvement with respect to Two Sigma and the highly technical nature of its fund operations, as reasonably equivalent to the work experience required by the QEP tenure conditions. The Division also noted the small number of individuals who would be covered by the requested exemptive letter and that the modeling and engineering officers were also financially sophisticated accredited investors who possess actual knowledge, familiarity and significant involvement in Two Sigma's trading and fund operations. The officers also receive detailed ESC disclosures, as well as periodic and annual reporting that meets or exceeds the requirements in CFTC Regulation 4.7, from Two Sigma. Finally, the Division noted that the QEP treatment of certain modeling and engineering officers would be temporary, in that as soon as an individual officer gains the requisite 24 months of work experience with Two Sigma or a combination of employers engaged in financial services, that person would be able to meet the QEP tenure conditions on his or her own.

The exemptive relief was granted subject to the following conditions:

- The exemptive relief is limited to Two Sigma's modeling and engineering officers, as well as trusts or other vehicles (organized for the benefit of such persons) meeting the conditions of CFTC Regulation 4.7(a)(2)(ix),² who are accredited investors and able to meet the seniority and other conditions of Two Sigma's ESC application and participation agreement.
- Two Sigma will operate the ESCs in a manner consistent with its ESC application, which was approved by the U.S. Securities and Exchange Commission in 2020, and as described in the requesting letter.
- Modeling and engineering officers participating in the ESCs are not permitted to sell, assign or otherwise transfer their interests without the prior written consent of such ESC's managing member. Any such sales, assignments or transfers are only permitted to other QEPs (including gifts, bequests or transfers pursuant to legal separation, divorce or death), to persons who may be considered QEPs by virtue of the exemptive relief, or to the ESCs, for purposes of redemption.

¹ See CFTC Letter 24-05 (May 7, 2024) citing CFTC Letter 94-01 "(permitting a corporate and securities lawyer, who acted as engagement counsel for the CPO and pool and was also an accredited investor, to make additional investments after the CPO claimed a Regulation 4.7 exemption for the pool, notwithstanding that he was not a QEP, due to his lengthy legal career and involvement in the pool's formation); CFTC Letter 00-06 (permitting a CPO's Director of Information and Technology, who was responsible for software development for the CPO and pool and had built computer models based on his research in commodities pricing, to be considered a QEP); CFTC Letter 00-17 (permitting a CPO to operate its pools pursuant to Regulation 4.7 exemptions, notwithstanding the participation of non-QEP employees, two of whom had been employed by the CPO for less than 24 months); CFTC Letter 00-68 (permitting a CPO to treat several non-QEP employees, who included its Managing Members, Systems Manager, and Software Manager, as QEPs because they would be considered 'knowledgeable employees' as defined by SEC regulations)."

² See CFTC Regulation 4.7(a)(2)(ix) (requiring that "(A) the trust not be formed for the specific purpose of either participating in the exempt pool or opening an exempt account; and (B) the trustee or other person authorized to make investment decisions with respect to the trust, and each settlor or other person who has contributed assets to the trust, is a QEP").

- Participation in the ESCs is voluntary, and Two Sigma will obtain the consent of any non-QEP modeling and engineering officers prior to treating them as QEPs.
- If an existing participant in the ESCs ceases to be an employee of Two Sigma, the exemptive relief provided will no longer apply to such person, and that person will not be permitted to make additional ESC contributions.
- Offering memoranda and Two Sigma's frequently asked questions regarding the ESCs, as well as the periodic and annual reports specified in CFTC Regulations 4.7(b)(3) and (b)(4), are provided to all prospective and actual ESC participants. Copies of such promotional materials and reports must be maintained at Two Sigma's main business office in accordance with CFTC Regulations 1.31 and 4.7(b)(5).
- Two Sigma will notify the Division staff if the operations of the ESCs materially change from the facts represented in the requesting letter.

As with other CFTC exemptive letters, this exemptive letter is solely applicable to Two Sigma with respect to the operations of the ESCs. Other CPOs seeking similar exemptive relief will be required to submit their own requests for exemptive relief.

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