

# CLIENT UPDATE

## CFTC ISSUES RELIEF REGARDING INSURANCE COMPANY GENERAL ACCOUNT ENTITIES, CPO USE OF THIRD-PARTY RECORDKEEPERS, AND FORM CPO-PQR FILING REQUIREMENTS

### NEW YORK

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The Commodity Futures Trading Commission's ("CFTC") Division of Swap Dealer and Intermediary Oversight ("DSIO") recently issued a series of letters providing relief to commodity pool operators ("CPOs") including, as further detailed below, (i) interpretive relief situating certain life insurance company subsidiaries outside the definition of "commodity pool," (ii) exemptive relief permitting expanded use of third-party recordkeepers, and (iii) exemptive relief from filing Form CPO-PQR for certain CPOs that operate pools pursuant to a claim of exemption or exclusion from registration.

### EXCLUSION OF LIFE INSURANCE COMPANY GENERAL ACCOUNT ENTITIES FROM THE DEFINITION OF COMMODITY POOL

In a letter (the "Insurance Letter")<sup>1</sup> responding to a request for relief from the American Council of Life Insurers (the "ACLI"), the DSIO provided an interpretation of Section 1a(10) of the CEA and of CFTC Regulation 4.10(d) that excludes certain life insurance company subsidiaries from the definition of "commodity pool" and advised that it would not require such entities to register as CPOs.

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<sup>1</sup> Available at: <http://www.cftc.gov/LawRegulation/CFTCStaffLetters/14-113>

## *Background*

General Account Entities are subsidiaries established by insurance companies to conduct business in different states or jurisdictions.<sup>2</sup> Each such insurance company subsidiary is subject to regulation under state insurance law by the insurance commissioner of its respective state of domicile, as well as the insurance commissioner of other states where the company is a licensed insurer.

The Insurance Letter notes that affiliated insurance companies under common ownership and control frequently establish a General Account Entity where each affiliated company contributes assets from its general account to a vehicle that will make various investments. ACLI claims that by pooling the insurance companies' general account assets, the General Account Entity can serve as a limited liability conduit vehicle for the investment of such assets; forming a General Account Entity permits an insurance company to achieve greater operational and accounting efficiencies than could be achieved by having each insurance company affiliate invest directly, and ACLI's members are able to realize lower overall costs in managing and deploying their assets than if each insurance company affiliate invested directly.

## *Relief*

Given the historical context of Regulation 4.5,<sup>3</sup> where the CFTC stated in the adopting release that the holding of commodity interests in an insurance company's general account should not make the insurance company a commodity pool, the DSIO finds that General Account Entities are outside the definition of "commodity pool," and will not require the insurance company affiliates that create such entities to register as CPOs where each of the following conditions are met:

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<sup>2</sup> CFTC Regulation 75.2(p) defines a general account, upon which the insurance company can rely to pay benefits to insurance policy beneficiaries, as "all of the assets of an insurance company except those allocated to one or more separate accounts." A General Account Entity consolidates and manages the general account assets of multiple life insurance company subsidiaries belonging to the same parent company. Comparatively, a "separate account," which contain assets or investments whose value provides the basis for benefits paid pursuant to variable life insurance policies, is an account established and maintained by an insurance company in connection with one or more insurance contracts to hold assets that are legally segregated from the insurance company's other assets, under which income, gains, and losses, whether or not realized, from assets allocated to such account, are, in accordance with the applicable contract, credited to or charged against such account without regard to other income, gains, or losses of the insurance company.

<sup>3</sup> CFTC Regulations 4.5(a)(2) and (b)(2) exclude from the definition of CPO "an insurance company subject to regulation by any State" with respect to "a separate account established and maintained or offered by an insurance company pursuant to the laws of any State or territory in the United States, under which income gains and losses, whether or not realized, from assets allocated to such account, are, in accordance with the applicable contract, credited to or charged against such account, without regard to other income, gains, or losses of the insurance company."

- Only affiliated life insurance companies under common control by the same parent company contribute their general account assets to the relevant General Account Entity.
- Despite being contributed by multiple entities, the general account assets invested in the General Account Entity ultimately are owned by the parent of the contributing affiliates, and it is the parent corporation, through its multiple subsidiaries, that bears the risk of the General Account Entity investments, including investments in commodity interests.
- The General Account Entity will not accept contributions from an investor that is not an insurance company controlled by the same parent insurance company and under no circumstances will assets held in an insurance company separate account be used to fund contributions to the General Account Entity.

#### **EXEMPTIVE RELIEF TO USE ADDITIONAL THIRD-PARTY RECORDKEEPERS IN CFTC REGULATIONS 4.7(B)(4) AND 4.23(C)**

In a letter (the “Recordkeeper Letter”)<sup>4</sup> responding to requests from multiple parties, the DSI0 provides exemptive relief to permit CPOs to use third-party recordkeepers beyond those enumerated in CFTC Regulations 4.23(c) and 4.7(b)(4), subject to certain requirements.

##### *Background*

In August 2013, the CFTC revised Regulations 4.23(c) and 4.7(b)(4) to provide that required books and records that are not kept at the main business office of the CPO may be alternately kept at the pool’s administrator, distributor or custodian, or a bank or registered broker or dealer acting in a similar capacity with respect to the pool (the “Main Business Office Exception”). The requested relief would permit the use of third-party recordkeepers other than those enumerated in the Main Business Office Exception.

##### *Relief*

In light of current data management practices in use by CPOs (e.g., specialized data centers and services, or unenumerated affiliates that have day-to-day control over that data to manage records), and the fact that CPOs remain ultimately responsible for fulfilling the CFTC’s recordkeeping obligations, the Recordkeeper Letter provides exemptive relief

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<sup>4</sup> Available at: <http://www.cftc.gov/LawRegulation/CFTCStaffLetters/14-114>

from the main business office requirement to allow a CPO to use any third-party recordkeeper, provided that:

- the CPO's timely access to such records is maintained, such that the CPO will satisfy the obligations of the applicable CFTC regulations, particularly with respect to providing such records for inspection; and
- the CPO timely and completely files the statements required pursuant to Regulations 4.23(c) or 4.7(b)(5), as applicable (i.e., that the CPO identify the recordkeeper, the recordkeeper's contact information, which records shall be so kept, and representations regarding the continued and proper keeping of those records).

The DSIO notes that, regardless of the third-party recordkeeper's condition or failures, the CPO remains responsible for ensuring that all books and records required to be kept are maintained in accordance with CFTC regulations, and producing them upon request, within the time specified by the regulations.

### **EXEMPTIVE RELIEF FROM THE OBLIGATION TO FILE FORM CPO-PQR WITH RESPECT TO CERTAIN REGISTERED CPOs**

In a letter (the "CPO-PQR Letter")<sup>5</sup> responding to a request from the National Futures Association, the DSIO provides relief from the obligation to file Form CPO-PQR to those CPOs that are registered with the CFTC but otherwise have no reporting obligations under Part 4 of the CFTC's regulations.

#### *Background*

Pursuant to CFTC Regulation 4.27(b)(1), any CPO that is registered or required to be registered under the CEA and the CFTC's regulations thereunder must file Form CPO-PQR (such CPOs, "Reporting Persons"), and Regulation 4.27(c) requires such Reporting Person to file Form CPO-PQR with the NFA. The CPO-PQR Letter states that a plain reading of Regulation 4.27(b)(1) would require any CPO that is registered or required to be registered to file a Form CPO-PQR with the NFA, irrespective of whether the CPO claims an exemption or exclusion with respect to its operated pools or if the CPO has registered despite not operating any commodity pools.

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<sup>5</sup> Available at: <http://www.cftc.gov/LawRegulation/CFTCStaffLetters/14-115>

*Relief*

The DSIO notes that requiring CPOs that only operate pools pursuant to CFTC Regulations 4.5 or 4.13(a)(3) to report on Form CPO-PQR would provide limited additional information regarding that CPO beyond that already available to the CFTC as part of the registration process and the CPO's ongoing obligations as a registrant.

Accordingly, the DSIO provides exemptive relief from Regulation 4.27(c) such that a CPO is not required file a Form CPO-PQR where the CPO is registered but only operates pools pursuant to a claim of exemption from registration or for which they maintain an exclusion from the definition of a CPO.

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Please do not hesitate to contact us with any questions.

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