Client Update
CFTC Proposes Amendments on Registration Relief for Foreign CPOs, CTAs and IBs

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The Commodity Futures Trading Commission (the "CFTC") recently proposed amendments[1] to Section 3.10(c) of the CFTC regulations for the purpose of implementing registration relief for certain intermediaries located outside of the United States acting in the capacity of a commodity pool operator ("CPO"), commodity trading advisor ("CTA"), or introducing broker ("IB").[2] If adopted, the amendments would remove the condition in Section 3.10(c)(3)(i) that currently requires that commodity interest transactions be submitted for clearing through a registered futures commission merchant ("FCM") in order to qualify for exemptive relief under such Section. The proposed amendments implement and codify relief granted pursuant to no-action letters that were issued by the CFTC's Division of Swap Dealer and Intermediary Oversight (the "DSIO") in 2015 ("Letter 15-37")[3] and earlier in 2016 ("Letter 16-08").[4] The proposing release also clarifies the rationale for the adoption of such amendments.

CFTC REGULATION 3.10(c)(3)(i)

With respect to commodity interest transactions executed bilaterally or made on or subject to the rules of any designated contract market ("DCM") or swap execution facility ("SEF"), CFTC Regulation 3.10(c)(3)(i) provides an exemption from registration as a CPO, CTA or IB if that intermediary and the transaction meet the following conditions:

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[1] 81 Fed. Reg. 51824 (August 5, 2016).

[2] The proposed amendments also relate to registration requirements for a futures commission merchant. However, the scope of this Client Update is limited to CPOs, CTAs and IBs.

[3] Available at: http://www.cftc.gov/LawRegulation/CFTCStaffLetters/15-37.

[4] Available at: http://www.cftc.gov/LawRegulation/CFTCStaffLetters/16-08.

- The intermediary is located outside the United States;
- The intermediary acts only on behalf of persons located outside the United States; and
- The commodity interest transaction is submitted for clearing at a derivatives clearing organization ("DCO") through a registered FCM.

Commodity interests include swaps, whether executed bilaterally or on or subject to the rules of a DCM or SEF, futures and retail forex transactions.

The remainder of this memorandum refers to CPOs, CTAs and IBs who meet the first two requirements summarized above as "Foreign Intermediaries."

NO-ACTION POSITION IN LETTER 16-08

The DSIO states in Letter 16-08 that CFTC Regulation 3.10(c)(3)(i) was not intended to impose an independent clearing requirement on commodity interest transactions involving Foreign Intermediaries that the Commodity Exchange Act and the CFTC regulations do not otherwise require to be cleared and that, accordingly, it will not recommend an enforcement action against a person located outside the United States that is engaged in the activity of a CPO, CTA or IB, in connection with swaps not subject to a CFTC clearing requirement entered into only on behalf of persons located outside the United States for failure to register in such capacity. Letter 16-08 indicates that it will expire on the later of the effective date or compliance date of any final rule amending CFTC Regulation 3.10(c)(3)(i).

NO-ACTION POSITION IN LETTER 15-37

The DSIO states in Letter 15-37 that it will not recommend enforcement action against a person located outside the United States: (1) for failure to register as an IB solely with regard to activities involving swaps for a customer that is an international financial institution ("IFI") or (2) for failure to register as a CTA in connection with providing advice solely incidental to those activities. IFIs include the International Monetary Fund, International Bank for Reconstruction and Development, European Bank for Reconstruction and Development, International Development Association and similar institutions that have been identified as IFIs in the CFTC's previous rulemakings and staff no-action letters. While IFIs may have headquarters or another significant presence in the United States, the DSIO recognizes that the unique attributes and multinational status of such institutions does not warrant treating them as domestic persons. Letter 15-37 indicates that it will expire on the later of the effective date or the compliance date of any final rule or final order of the CFTC providing relief from

IB and CTA registration for persons located outside the United States who facilitate swap transactions for IFIs with offices in the United States.

PROPOSED AMENDMENTS TO CFTC REGULATION 3.10(c)(3)(i)

In order to codify the registration relief set forth in Letter 16-08 and Letter 15-37, the CFTC is proposing to amend CFTC Regulation 3.10(c)(3)(i) to indicate that a person located outside the United States, its territories or possessions (a "foreign located person") engaged in activity that meets the definition of an IB, CTA or CPO is not required to register as such if such activity is either solely on behalf of foreign located persons or IFIs. In addition, the proposed amendments include a new subparagraph (3.10(c)(6)) expressly defining the list of institutions that are currently recognized by the CFTC as IFIs and indicating that any other international financial institution that the CFTC may designate as such will also constitute an IFI.

In proposing the amendments, the CFTC indicates that it has come to the view that the focus of the exemption should be the activity of the Foreign Intermediary, not its customer. Accordingly, the CFTC believes that the proposed amendments are consistent with its long-standing policy to focus its customer protection activities upon domestic firms and upon firms soliciting or accepting orders from domestic participants. Where a Foreign Intermediary's customers are located outside the United States, the CFTC believes the jurisdiction where the customer is located has the preeminent interest in protecting such customers. Unlike the relief under Letter 16-08 (which only addresses swaps), the relief provided by the proposed amendments would apply to foreign futures (which do not clear through DCOs) and retail forex transactions (which are uncleared, bilateral trades) in addition to swaps.

The CFTC notes that the registration exemption for a Foreign Intermediary does not in itself exclude any person from compliance with any provision of the Commodity Exchange Act or the CFTC regulations otherwise applicable to such person, including any requirement that a swap be cleared by a registered or exempt DCO.

FURTHER COMMENTS

In a prior Client Update regarding Letter 16-08,[5] we noted that while the relief for Foreign Intermediaries provided by Letter 16-08 was welcomed, in our view,

[5] Available at: http://www.debevoise.com/insights/publications/2016/02/cftc-registration-relief-for-foreign-cpos.

the CFTC's basis for the no-action relief was misguided in that it focused on the view that CFTC Regulation 3.10(c)(3)(i) was not intended to impose an independent clearing requirement on commodity interest transactions involving Foreign Intermediaries that the Commodity Exchange Act and the CFTC regulations do not otherwise require to be cleared. While this is true, it does not necessarily lead to the conclusion that relief under the Regulation should be available if a Foreign Intermediary trades swaps bilaterally or on a DCM or SEF that are not required to be cleared through a DCO. Rather, in our view, the requirement for registration should not be imposed on a Foreign Intermediary in such circumstances in light of the regulatory objective of the related registration requirement, which, in the case of a CPO, CTA or IB, is to protect customers of such CPO, CTA or IB. The United States has no regulatory interest in protecting foreign customers of a Foreign Intermediary. In particular, foreign customers of a Foreign Intermediary have no expectation for protection under the Commodity Exchange Act, and the registration of such Foreign Intermediary would not help achieve the protection of market integrity or other policy objectives of the CFTC. The rationale provided by the CFTC for the proposed amendments and summarized above is more in line with this view.

However, certain concerns that we raised in our Client Update regarding Letter 16-08 are still unresolved. In particular, we believe it would be appropriate for the CFTC to provide further guidance on the meaning of the phrase "person located outside the United States, its territories or possessions" (which, pursuant to the proposed amendments, would be used in defining "foreign located person"). The scope of such phrase may need to be different with respect to a foreign CPO, on the one hand, and a foreign CTA or IB, on the other hand.

We also noted in our Client Update regarding Letter 16-08 that we believed the CFTC should consider the interaction between CFTC Regulation 3.10(c)(3) and the definition of eligible contract participant ("ECP") (within the meaning of section 1(a)(18) of the Commodity Exchange Act and CFTC Regulation 1.3(m)). The relief set forth in Letter 16-08 is limited to a person located outside the United States that is engaged in the activity of a CPO, CTA or IB in connection with swaps not subject to a CFTC clearing requirement entered into only on behalf of persons located outside the United States. A "swap" in a foreign currency traded by a foreign CPO or CTA on behalf of a foreign pool will be a retail forex transaction under sections 2(c)(2)(B) and 2(c)(2)(C) of the Commodity Exchange Act if the foreign pool is not an ECP. The proposed amendments resolve this concern since they do not limit the relief to Foreign Intermediaries executing swaps for foreign located persons but instead apply to any activity of a Foreign Intermediary that meets the definition of a CPO, CTA or IB if such activity is solely on behalf of foreign located persons or IFIs. Thus

retail forex transactions entered into by a Foreign Intermediary on behalf of a foreign pool are within the scope of the proposed amended version of CFTC Regulation 3.10(c)(3)(i).

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Please do not hesitate to contact us with any questions.