

COMMODITY POOLS AS ECPs AFTER THE DODD-FRANK ACT

Since 2000, the definition of eligible contract participant¹ in the Commodity Exchange Act has included a commodity pool with at least \$5 million in total assets that was formed by a person subject to regulation by the Commodity Futures Trading Commission or a similar foreign regulator, regardless of whether each investor in the commodity pool is itself an ECP. The Dodd-Frank Act amended the definition of ECP as it applies to commodity pools engaging in off-exchange (or “over-the-counter” (“OTC”)) foreign currency transactions. The definition now includes a “look through” requirement with respect to such transactions, such that a commodity pool with any non-ECP participants will not be considered an ECP with respect to its OTC foreign currency transactions. A commodity pool in which at least one investor is not an ECP² will be restricted from engaging in OTC foreign currency transactions unless the commodity pool’s counterparty is one of certain specifically enumerated types of entities.³

Another subsection of the ECP definition provides that an entity with total assets exceeding \$10 million is an ECP.⁴ In connection with the revised ECP test for commodity pools, in December 2010 the CFTC proposed to affirmatively prohibit a commodity pool from qualifying as an ECP under the \$10 million test.⁵ If the proposed rule is adopted, a collective investment vehicle that is a commodity pool, which includes many hedge funds, would not be permitted to rely on the \$10 million test to qualify as an ECP, regardless of its size.

¹ Eligible contract participant (“ECP”) was originally defined in Commodity Exchange Act (“CEA”) § 1a(12)(A)(iv), which has been amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (the “Dodd-Frank Act”), and renumbered as CEA § 1a(18)(A)(iv).

² For example, the definition of ECP for individuals generally requires that such persons have at least \$10 million invested on a discretionary basis (in certain cases, this requirement is reduced to \$5 million). Any commodity pool with even a single individual who does not meet this threshold may not satisfy the definition of ECP with respect to its OTC foreign currency transactions.

³ The list of permitted types of entities includes, among others, United States financial institutions, broker-dealers, futures commission merchants, financial holding companies and retail foreign exchange dealers. *See* CEA § 2(c)(2)(B)(i)(II). Certain of these types of entities, however, may only enter into OTC foreign currency transactions with non-ECPs pursuant to, and in accordance with regulations promulgated by such entities’ respective federal regulators. Such federal regulators are not obligated to promulgate such rules. *See* CEA § 2(c)(2)(E)(ii). In addition, if the transaction is a swap, other issues arise concerning whether the transaction must be executed on a swap execution facility, whether the transaction must be cleared and what reporting requirements apply.

⁴ CEA § 1a(18)(A)(v).

⁵ Joint Proposed Rule; Proposed Interpretations: Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant” and “Eligible Contract Participant,” 75 Fed. Reg. 80174 (Dec. 21, 2010) at 80185.

If a commodity pool engages in OTC foreign currency transactions but does not qualify as an ECP (either generally or solely with respect to such transactions), its operator will be subject to the CFTC's new Part 5 Rules. These rules generally require the operator to register with the CFTC as a commodity pool operator and comply with certain disclosure, recordkeeping and reporting requirements with respect to the commodity pool.

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