

CLIENT ALERT

CFTC Proposes to Amend and Clarify Registration Exemptions for Non-U.S. CPOs

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In a unanimous vote, the Commodity Futures Trading Commission has proposed to amend a registration exemption widely used by commodity pool operators located outside the United States.¹ CFTC Rule 3.10(c)(3) (the “3.10 Exemption”) is available to non-U.S. CPOs who execute commodity interest transactions on behalf of persons located outside the United States. The proposal would amend the 3.10 Exemption to (i) permit reliance on a pool-by-pool basis; (ii) clarify that generally both the pool and its participants must be outside the United States; (iii) incorporate a safe harbor for non-U.S. CPOs that are unable to identify all pool participants; and (iv) provide for an exception for seed investments made by U.S. controlling affiliates.²

¹ Exemption From Registration for Certain Foreign Persons Acting as Commodity Pool Operators of Offshore Commodity Pools, 85 FR 35820 (June 12, 2020).

² The proposal also reopens the comment period on previous amendments related to the clearing requirements in the 3.10 Exemption proposed by the CFTC in July 2016. Exemption from Registration for Certain Foreign Persons, 81 FR 51824 (Aug. 5, 2016).

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Stacking of the 3.10 Exemption

In an October 2018 rule proposal relating to CFTC Staff Advisory 18-96,³ the CFTC stated that a CPO could not rely on the 3.10 Exemption while simultaneously claiming other registration exemptions with respect to its U.S. commodity pools (a practice known as “stacking” exemptions). In response to comments and suggestions from industry experts, the CFTC’s current proposal would now expressly permit a non-U.S. CPO relying on the 3.10 Exemption to stack it alongside other exemptions. In other words, a non-U.S. CPO would be permitted to rely upon the 3.10 Exemption for its non-U.S. pools with non-U.S. participants, while concurrently registering with the CFTC or relying on other exemptions with respect to pools it offers or sells to U.S. persons.⁴ This practice of stacking exemptions is consistent with the practice of U.S. domiciled registered CPOs, which are permitted to operate qualifying commodity pools pursuant to the exemption provided in Rule 4.13(a)(3) while simultaneously operating Rule 4.7 or full Part 4 pools.

3.10 Exemption Safe Harbor

The CFTC recognizes that it may be impossible for a non-U.S. CPO to be certain that all participants are located outside the United States. For example, if a pool is traded in an offshore secondary market, a CPO may not have the ability to ensure that purchasers are limited to persons located outside the United States. The CFTC is thus proposing to add a safe harbor permitting a non-U.S. CPO to rely on the 3.10 Exemption with respect to a non-U.S. pool provided the following conditions are satisfied:

1. The pool’s offering documents and any distribution agreements include clear prohibitions on offering to and ownership by U.S. persons.
2. The pool’s governing and offering documents are reasonably designed to preclude U.S. persons from participating therein and include mechanisms reasonably designed to enable the non-U.S. CPO to exclude U.S. persons attempting to participate in the pool.
3. The non-U.S. CPO uses only non-U.S. intermediaries to distribute interests in the pool.
4. The non-U.S. CPO employs reasonable due diligence methods to preclude U.S. persons from participating.
5. Interests in the pool are directed and distributed to participants outside the United States.

³ For more information on this rule proposal, please see our client memoranda entitled “CFTC Proposes to Codify Prior Relief for CPOs and CTAs” (October 10, 2018), available [here](#), and “CFTC Adopts Family Office Exemption, BDC Exclusion, JOBS Act Consistency” (December 6, 2019), available [here](#).

⁴ Unlike certain other exemptions, the 3.10 Exemption is self-executing. Thus, a non-U.S. CPO need not make any filing in order to claim it.

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The CFTC would expect non-U.S. CPOs to keep adequate records to exhibit compliance with the above conditions.

Exception for Initial Contributions by U.S. Controlling Affiliates

Subject to certain conditions, the CFTC's proposal would permit a non-U.S. CPO to rely on the 3.10 Exemption with respect to a pool even if a U.S. controlling⁵ affiliate of the CPO provides seed capital to such pool. The proposal indicates that this exception is preliminarily intended to apply to those contributions made at or near a pool's inception, although the U.S. controlling affiliate's contributed capital can remain in the pool. The proposal emphasizes that the exception may not be used as a vehicle for evading the CFTC's general CPO compliance requirements with respect to non-U.S. pools. In addition to general comments, the CFTC is seeking specific input on conditions that should be added to the proposed exception that would serve to prevent any such evasion.

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If you have any questions regarding this client alert, please contact one of the authors, any member of our CFTC team listed below, or the Willkie attorney with whom you regularly work.

⁵ The proposal defines "control" as "the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting shares, by contract, or otherwise."

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Willkie has a dedicated team of attorneys with extensive knowledge and experience in all aspects of the Commodity Exchange Act and the CFTC regulatory regime. We would be pleased to assist on your matters.

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