

Client Alert

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The CFTC Proposes Broadening Exemptions from Registration for Non-U.S. Intermediaries

The Commodity Futures Trading Commission (“CFTC”) recently proposed amending CFTC Rule 3.10 with an objective of expanding exemptions from registration applicable to non-U.S. persons engaged in commodity interest transactions in U.S. markets on behalf of other persons located outside of the U.S. At the same time, the proposal also seeks to simplify the exemptions’ requirements.

In this Client Alert, we examine the proposed amendments to CFTC Rule 3.10 and the exemptions. In light of the proposal, a non-U.S. financial institution should determine whether it can meet the proposed requirements, and how reliance on the exemptions will allow it to participate in U.S. markets on behalf of its customers. In addition, a non-U.S. financial institution should consider whether any changes, or other suggestions, should be provided to the CFTC during the 30-day comment period. Comments in support of the proposal are also encouraged.

The proposed exemptions would apply to non-U.S. persons acting solely as a “foreign broker,” or otherwise acting as an intermediary only with persons located outside of the U.S., and exempt such non-U.S. persons from registration as futures commission merchants (“FCMs”), introducing broker (“IBs”), commodity trading advisors (“CTAs”) or commodity pool operators (“CPOs”).

Currently, CFTC Rule 3.10 (c)(3)(i) exempts non-U.S. persons from registration as an IB, CTA or CPO for certain non-U.S. activities involving commodity interest transactions (including commodity futures and swaps) executed bilaterally, or made on or subject to the rules of an exchange or a swap execution facility (“SEF”) in the U.S. if the following conditions are met: (1) the person is located outside of the U.S.; (2) the person acts only on behalf of persons located outside of the U.S.; and (3) the commodity interest transaction is submitted for clearing through a registered FCM. CFTC Rule 3.10 (c)(2)(i) provides similar exemptive relief for any non-U.S. person acting as an FCM. Generally, the proposal will remove the clearing requirement set forth in (3) above, and simply require that the person is located outside of the U.S. and acts only on behalf of persons located outside of the U.S.

As background, following the Dodd-Frank Act, swaps became subject to the jurisdiction of the CFTC. As a result, by its language, CFTC Rule 3.10 seemed to impose a clearing obligation on Non-U.S. persons seeking to rely upon exemptions set forth therein. In 2015 and 2016, the CFTC issued a series of no-action relief that permitted

Non-U.S. persons to rely upon the exemption set forth in CFTC Rule 3.10 (c)(3)(i) if their activities involved swaps that were not subject to a clearing requirement. In its no-action relief, the CFTC noted that its regulations do not require all swaps to be cleared and some swaps are not yet accepted for clearing. Thus, the CFTC did not seek to impose a greater obligation on Non-U.S. Persons seeking to rely upon the exemptive relief provided in CFTC Rule 3.10.

Based on various venues for execution and clearing requirements applicable to different swaps, the CFTC determined to amend CFTC Rule 3.10(c)(2)(i) and (3)(i) in order to essentially codify the no-action relief, and at the same time, simplify the requirements for exemptive relief.

In support of the proposal, the CFTC stated that it believes that “the focus on the exemption should be the activity of the [Non-U.S. Person], not its customer.” Additionally, the CFTC noted that the proposal is consistent with its “longstanding policy” to focus domestically on customer protection activities, and that where a Non-U.S. Person’s customers are located outside the U.S., the jurisdiction where the customer is located has the “preeminent interest” in protecting such customers.

While the CFTC’s proposal is a welcomed step, there are questions regarding the scope of the relief. For example, who is considered a “person located outside of the U.S.”? Would this include U.S. citizens temporarily residing outside of the U.S.? Questions such as these will need to be addressed during the comment period.