

# CFTC Rule 3.10(c)(3): CFTC proposed amendments

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On July 27, 2016 the Commodity Futures Trading Commission (“**CFTC**”) released proposed amendments to the exemption from registration as an IB, a CTA or a CPO contained in CFTC Rule 3.10(c)(3) that remove the clearing requirement and expand the exemption to include international financial institutions.

## Background

As swaps became subject to regulation under the Commodity Exchange Act (“**CEA**”) under the regulatory framework established by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “**Dodd-Frank Act**”), the universe of entities that were required to register as introducing brokers (“**IB**”), commodity trading advisors (“**CTA**”) or commodity pool operators (“**CPO**”) was significantly expanded. One of the primary exemptions from registration utilized by non-US entities that would otherwise be required to register in such a capacity is the exemption in CFTC Rule 3.10(c)(3).

CFTC Rule 3.10(c)(3), in its current form, exempts a person from registration as an IB, a CTA or a CPO where all of the following requirements are satisfied:

1. the person seeking the exemption is located outside the US, its territories or possessions;
2. the person seeking the exemption acts only on behalf of persons located outside of the US, its territories or possessions; and
3. the commodity interest transaction (the definition of which now includes “swaps” following enactment of the Dodd-Frank Act) was submitted for clearing through a futures commission merchant registered under Section 4d of the CEA (“**FCM**”).

## Clearing Requirement (prong (3))

CFTC Rule 3.10(c)(3) was adopted a number of years ago, well before the CEA was most recently amended under the Dodd-Frank Act, and originally only applied to futures and listed option contracts. Those contracts, unlike swaps, are cleared through a FCM. As the requirement to clear the commodity interest transaction through a FCM (see prong (3) above) was retained following the inclusion of swaps within the definition of “commodity interest transaction”, there is a concern with the current drafting of CFTC Rule 3.10(c)(3) where a person that satisfies prongs (1) and (2) above transacts a swap (as opposed to a futures or listed option contract). The text provides that in such circumstances the person seeking exemption from registration under CFTC Rule 3.10(c)(3) would only be able to benefit from the exemption if the applicable swap was submitted for clearing through a FCM.

The problem with this requirement is that swaps which are executed bilaterally, subject to the rules of a swap execution facility (or SEF) or not yet accepted for clearing by any derivatives clearing organization would not

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satisfy the requirement in prong (3) above. Therefore, even if a person met all the other requirements for the exemption in CFTC Rule 3.10(c)(3), it would be unable to rely on the exemption where the applicable swap is not submitted for clearing through a FCM.

## International Financial Institutions (prong(2))

Many international financial institutions (e.g., the International Monetary Fund) have offices within the US in New York City or Washington, DC. As such, even where a person satisfies prongs (1) and (3) above, it would not be able to benefit from the exemption in CFTC Rule 3.10(c)(3) when acting on behalf of an international financial institution that has an office in the US as this would not satisfy the requirement in prong (2) above. The concern with this outcome is that international financial institutions, which are operated to satisfy public purposes, have multinational status and have as their members sovereign nations, are being treated the same as other domestic persons merely because they have a presence in the US.

## Exemptive Relief

The CFTC's Division of Swap Dealer and Intermediary Oversight has issued two no-action letters relating to registration as an IB, a CTA and/or a CPO. The first, [CFTC No-Action Letter 15-37](#), provided relief from registration as an IB or CTA for persons located outside the US with respect to their swaps activity for international financial institutions (i.e. various international development banks including, but not limited to, the International Monetary Fund). The second, [CFTC No-Action Letter 16-08](#), provided relief from registration as an IB, a CTA or a CPO for persons located outside the US engaged in an activity of an IB, a CTA or a CPO in connection with swaps not subject to a clearing requirement for person located outside the United States.

## Proposed Amendments

The proposed amendments to the exemption in CFTC Rule 3.10(c)(3) would (i) expand the exemption to include international financial institutions (as defined<sup>1</sup>), (ii) remove the references to the manner in which the commodity interest transaction is executed (bilaterally or on a designated contract market (DCM) or swap execution facility (SEF)) and (iii) remove the clearing requirement. Therefore, if the amendments were finalized as proposed, CFTC Rule 3.10(c)(3) would exempt persons located outside the US from registering with the CFTC as an IB, a CTA or a CPO if such a person, in connection with a commodity interest transaction, only acts on behalf of:

- persons located outside of the US, its territories or possessions; or
- international financial institutions.<sup>2</sup>

These amendments would codify the no-action relief set out in [CFTC No-Action Letter 15-37](#) and [CFTC No-Action Letter 16-08](#).

The CFTC noted that these amendments were consistent with its longstanding policy to focus its customer protection activities upon domestic firms and upon firms soliciting or accepting orders from domestic participants, and that where both parties to a commodity interest transaction are located outside the US, the jurisdiction of the customer should have the preeminent interest in protecting that customer.

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<sup>1</sup> The proposed amendments define "international financial institution" to mean each of the following and any other international financial institution that the CFTC may designate: Int'l Monetary Fund, Int'l Bank for Reconstruction and Development, European Bank for Reconstruction and Development, Int'l Development Association, Int'l Finance Corp., Multilateral Investment Guarantee Agency, African Development Bank, African Development Fund, Asian Development Bank, InterAmerican Development Bank, Bank for Economic Cooperation and Development in the Middle East and North Africa, Inter-American Investment Corp., Council of Europe Development Bank, Nordic Investment Bank, Caribbean Development Bank, European Investment Bank and European Investment Fund.

<sup>2</sup> Similar amendments were also proposed to CFTC Rule 3.10(c)(2) which provides an exemption for foreign intermediaries acting as a FCM.

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