

# Public Statements & Remarks

## Statement of Chairman Heath P. Tarbert in Support of Amending the Registration Exemption for Foreign CPOs

October 15, 2020

When the Commission considered the proposal to amend the registration exemption for foreign commodity pool operators (CPOs),<sup>[1]</sup> I noted that, in his second inaugural address in 1893, President Grover Cleveland remarked “[u]nder our scheme of government the waste of public money is a crime against the citizen.”<sup>[2]</sup> The CFTC is a taxpayer-funded agency, and Congress expects us to deploy our resources to serve the needs of American taxpayers. That is why as Chairman and Chief Executive, I have sought to revisit our agency’s regulations where there does not appear to be a clear connection to furthering the interests of the United States or our citizens.<sup>[3]</sup>

The CFTC’s framework for regulating foreign commodity CPOs protects U.S. investors who put their money in commodity investment funds run from outside the United States. But, in some instances, the only benefit of CFTC regulation of offshore CPOs is to *foreign* investors. There is no statutory mandate for the CFTC to regulate pools never offered or sold to U.S. investors. To do so absent a compelling reason would be—in President Cleveland’s words—a waste of public money.

Consequently, I am pleased to support today’s final rule to amend the exemption for CPOs in regulation 3.10(c) (3.10 Exemption). The final rule eliminates the potential need for the CFTC to require the registration and oversight of non-U.S. CPOs whose pools have no U.S. investors. The final rule additionally exempts U.S.-based affiliates of pool sponsors who put seed money into offshore funds that have only foreign investors. In so doing, the final rule provides much-needed regulatory flexibility for non-U.S. CPOs operating offshore commodity pools, without compromising the CFTC’s mission to protect U.S. investors.

### ***Exemption for Foreign CPOs Sponsoring Funds without U.S. Investors***

The final rule amends the conditions under which a foreign CPO, in connection with commodity interest transactions on behalf of persons located outside the United States, will qualify for an exemption from CPO registration and regulation with respect to an offshore pool. Specifically, through amendments to our regulation 3.10(c), a non-U.S. CPO will be able to operate pools offered to U.S. persons as either a registered or exempt CPO, while simultaneously claiming the 3.10 Exemption with respect to its qualifying offshore commodity pools.<sup>[4]</sup>

Absent a compelling reason, the CFTC should be focused on U.S. markets and U.S. investors, and refrain from extending our reach outside the United States.<sup>[5]</sup> The protection of non-U.S. customers of non-U.S. firms is best left to foreign regulators with the relevant jurisdiction and mandate.<sup>[6]</sup> Therefore, I believe it is appropriate for the final rule to allow foreign CPOs to rely on the 3.10 Exemption for their foreign commodity pools when they have no U.S. investors. Where a foreign CPO does have U.S. investors, other exemptions or exclusions from registration might be available.

Unfortunately, under a strict construction of the current rule, if a foreign CPO has one fund with U.S. investors, then the foreign CPO must register all its funds or rely on some other exemption besides the 3.10 Exemption. This “all or nothing” reading of the rule has produced two competing consequences—neither of which makes for good regulatory policy. First, if the CPO chooses to register with respect to *all* its funds, the CFTC ends up regulating some foreign-based funds without any U.S. investors. Second, if the CPO refuses to register for any of its funds, then U.S. investors are effectively denied the liquidity and investment opportunities offered by foreign commodity pools.

In the last decade, statutory and regulatory developments have produced a growing mismatch between the Commission’s stated policy purposes underlying the 3.10 Exemption (that focus the CFTC’s resources on the protection of U.S. persons) and the strict construction of the 3.10 Exemption (that leads to its “all or nothing” application). To address this mismatch, the final rule amends the 3.10 Exemption to align the plain text of the exemption with our longstanding policy goal of regulating foreign CPOs only when they offer their funds to U.S. investors. In effect, the Commission’s walk finally conforms to our talk.<sup>[7]</sup>

### ***Affiliate Investment Exemption***

The final rule also permits U.S. affiliates of a non-U.S. CPO to contribute capital to that CPO’s offshore pools as part of the initial capitalization without rendering the non-U.S. CPO ineligible for the 3.10 Exemption. In other words, the final rule allows a U.S. affiliate of a foreign CPO to invest in the offshore fund without triggering registration requirements because of the nature of the relationship between the affiliate and the non-U.S. CPO.

It is hard to imagine how an entity that controls, is controlled by, or is under common control with, a given foreign CPO could lack a sufficient degree of transparency with respect to its own contribution of initial capital to an offshore commodity pool run by that very same foreign CPO. In short, a U.S. affiliate’s initial investment in its affiliated non-U.S. CPO’s offshore pool does not raise the same investor protection concerns as similar investments in the same pool by unaffiliated persons located in the United States. In many cases, moreover, the affiliate is itself regulated by other U.S. regulators—for instance, state insurance departments in the case of insurance companies that wish to deploy their own general account assets as they best see fit, in keeping with their separate regulatory regimes. Accordingly, I see no reason to deploy the limited, taxpayer-funded resources of the CFTC to protect U.S. affiliates of foreign CPOs who are far better positioned than us to safeguard their own interests.

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

[2] Statement of Chairman Heath P. Tarbert in Support of Amending the Registration Exemption for Foreign CPOs (May 28, 2020), available at:

<https://www.cftc.gov/PressRoom/SpeechesTestimony/tarbertstatement052820b>. See Second Inaugural Address of Grover Cleveland (Mar. 4, 1893), reprinted in *American History Through Its Greatest Speeches: A Documentary History of the United States* 278 (Courtney Smith, et al., eds. 2016).

[3] See Statement of Chairman Heath P. Tarbert in Support of Amending the Registration Exemption for Foreign CPOs, *supra* note 2.

[4] The final rule adds a safe harbor as new regulation 3.10(c)(3)(iv) for non-U.S. CPOs that have taken what the Commission preliminarily believes are reasonable steps designed to ensure that participation units in the operated offshore pool are not being offered or sold to persons located in the United States.

[5] For example, section 2(i) of the Commodity Exchange Act provides that the swap provisions of Title VII of the Dodd-Frank Act shall not apply to activities outside the United States unless those activities (1) have a direct and significant connection with activities in, or effect on, commerce of the United States; or (2) contravene such rules or regulations as the Commission may prescribe or promulgate as are necessary or appropriate to prevent the evasion of Title VII. In interpreting this provision, the Commission has taken the position that “[r]ather than exercising its authority with respect to swap activities outside the United States, the Commission will be guided by international comity principles and will focus its authority on potential significant risks to the U.S. financial system.” Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants, 85 Fed. Reg. 56924, 56928 (Sep. 14, 2020).

[6] The Commission also cited this policy position in the initial proposal for what ultimately became Commission regulation 3.10(c)(3)(i). See 72 Fed. Reg. 15637, 15638 (Apr. 2, 2007).

[7] Apart from policy incoherence inside the CFTC, the mismatch has also caused confusion among CPOs and their investors. A number of foreign CPOs have not adopted the strict “all or nothing” reading of the 3.10 Exemption, but have instead quite sensibly latched on to the Commission’s stated policy behind the rule to conclude that a foreign CPO may rely on the current 3.10 Exemption for non-U.S. pools with only non-U.S. investors even if the foreign CPO operates other non-U.S. pools with U.S. investors. Given that the confusion largely stems from the Commission’s own doing, I would not support any enforcement action against foreign CPOs whose interpretation followed the spirit, if not the letter, of the 3.10 Exemption. Furthermore, today’s final rule conforms to their reading.

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