



U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Swap Dealer and
Intermediary Oversight

Gary Barnett
Director

CFTC Letter No. 14-113
Interpretation
September 8, 2014
Division of Swap Dealer and Intermediary Oversight

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**RE: Request for Interpretation of the Definition of “Commodity Pool” under
Section 1a(10) of the Commodity Exchange Act and Commission Regulation 4.10(d)**

Dear Mr. Wilkerson:

This responds to your letter dated April 15, 2014 (“Correspondence”), to the Division of Swap Dealer and Intermediary Oversight (“DSIO” or “Division”) of the Commodity Futures Trading Commission (“Commission”). By the Correspondence, you request, on behalf of the members of the American Council of Life Insurers (“ACLI”), an interpretation of the definition of “commodity pool” in Section 1a(10) of the Commodity Exchange Act (“CEA” or “Act”)¹ and Commission Regulation 4.10(d),² such that a General Account Entity,³ formed by state-regulated life insurance company affiliates by combining their general account assets, that invests directly or indirectly in commodity interests is not within the definition of “commodity pool,” and

¹ 7 U.S.C. 1a(10). The CEA is available through the Commission’s website, <http://www.cftc.gov>.

² 17 CFR 4.10(d). The Commission’s regulations are found at 17 CFR Part 1 *et seq.* Like the CEA, the Commission’s regulations may also be accessed through the Commission’s website, <http://www.cftc.gov>.

³ Commission Regulation 75.2(p) defines a general account as “all of the assets of an insurance company except those allocated to one or more separate accounts.” 17 CFR 75.2(p). As explained herein, a General Account Entity consolidates and manages the general account assets of multiple life insurance company subsidiaries belonging to the same parent company. Comparatively, Commission Regulation 75.2(bb) defines a separate account as “an account established and maintained by an insurance company in connection with one or more insurance contracts to hold assets that are legally segregated from the insurance company’s other assets, under which income, gains, and losses, whether or not realized, from assets allocated to such account, are, in accordance with the applicable contract, credited to or charged against such account without regard to other income, gains, or losses of the insurance company.” 17 CFR 75.2(bb); *see also* 17 CFR 4.5(b)(2).

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therefore, that the life insurance companies forming the General Account Entity would not be required by CEA Section 4m(1) to register as commodity pool operators (“CPOs”), as that term is defined in Section 1a(11) of the CEA.⁴

Background

Based upon the Correspondence, we understand the relevant facts to be as follows. ACLI is a national trade association with 300 members, who represent more than 90 percent of the assets and premiums of the life insurance and annuity industry. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance. The Correspondence requests from the Division an interpretation, which would affect any state-regulated life insurance company, that a General Account Entity formed by affiliated life insurance companies is not a commodity pool, and that the life insurance companies forming and operating a General Account Entity are therefore not CPOs.

In support of the request for interpretative guidance, the Correspondence provides the following background on the operation of life insurance companies and the purposes and structure of the General Account Entity, which the Division has summarized for the purposes of this letter. Insurance companies often establish subsidiary entities to conduct business in different states or jurisdictions, and each insurance company subsidiary is subject to regulation under state insurance law by the insurance commissioner of its respective state of domicile, as well as the insurance commissioner of other states where the company is a licensed insurer. Similarly, each foreign subsidiary that invests directly or indirectly in a General Account Entity will be subject to the insurance law of its applicable jurisdiction and any others in which it operates.

It is not uncommon for affiliated insurance companies under common ownership and control to establish a General Account Entity, in which each affiliated company, either directly or indirectly, contributes assets from its general account to a vehicle that will make various investments. The General Account Entity will not accept contributions from an investor that is not an insurance company controlled by the same parent insurance company and under no circumstances would assets held in an insurance company separate account be used to fund contributions to a General Account Entity. Insurance companies do not market insurance contracts or policies to the public as interests or participations in any such General Account Entity.

⁴ 7 U.S.C. 4m(1), 1a(11). Alternatively, you request that the Division not recommend enforcement action to the Commission against any state-regulated insurer operating a General Account Entity for failure to register with the Commission as a CPO with respect to such entity. In light of the position taken herein, it is unnecessary for the Division to separately consider this alternate request.

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The Correspondence also explains the rationale behind the formation of General Account Entities by affiliated insurance companies:

By pooling the insurance companies’ general account assets, the General Account Entity can serve as a limited liability conduit vehicle for the investment of such assets. Each insurance company affiliate could, if it chose, make direct investments with its assets. Forming a General Account Entity, however, permits an insurance company to achieve greater operational and accounting efficiencies than could be achieved by having each insurance company affiliate invest directly. [ACLI’s] members are also able to realize lower overall costs in managing and deploying their assets than would be the case if each insurance company affiliate invested directly.⁵

Need for Relief for Similarly Situated Life Insurance Companies

The Correspondence states that a General Account Entity may use the proceeds from the contributions it receives from affiliated insurance company general accounts to invest in a variety of investments, including, among others, private equity funds, hedge funds, real estate funds, venture capital funds, and securitization vehicles. Some of these underlying investment funds may trade or otherwise hold commodity interests and, thus, may themselves be commodity pools. Also, a General Account Entity may establish separately managed accounts to be advised by third party investment managers. Accordingly, depending upon its investments, a General Account Entity could become a commodity pool, and the insurance company affiliates who created it, its CPOs.

Life insurance companies forming General Account Entities met the qualifications for and formerly relied upon the CPO registration exemption in Regulation 4.13(a)(4). Since the rescission of that exemption by the Commission in 2012,⁶ ACLI, on behalf of its members and all life insurance companies forming General Account Entities, is seeking regulatory certainty for the General Account Entity structure through the instant request for interpretative relief.

⁵ Correspondence, p. 2.

⁶ See Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, 77 Fed. Reg. 11252 (Feb. 24, 2012).

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Analysis

In 1981, the Commission proposed and adopted the definition of “pool” in Commission Regulation 4.10(d), which provided that “pool” means “any investment trust, syndicate or similar form of enterprise operated for the purpose of trading commodity interests.”⁷ At that time there was no statutory definition of a commodity pool. The statutory definition of commodity pool, as it currently appears in Section 1a(10) of the CEA, is substantively identical to the Commission’s longstanding regulatory definition of the term “pool.”⁸

The Commission addressed the issue of insurance company general accounts in the 1985 Federal Register release adopting, among other regulations, the exclusions from the CPO definition contained in Regulation 4.5.⁹ Currently, Regulations 4.5(a)(2) and (b)(2) exclude from the CPO definition “an insurance company subject to regulation by any State” with respect to “a separate account established and maintained or offered by an insurance company pursuant to the laws of any State or territory in the United States, under which income gains and losses, whether or not realized, from assets allocated to such account, are, in accordance with the applicable contract, credited to or charged against such account, without regard to other income, gains, or losses of the insurance company.”¹⁰

Initially, in 1984, the Commission proposed to exclude from the CPO definition an insurance company subject to regulation by any state, with respect to its operation of “the assets of any trust, custodial account or other separate unit of investment for which it is acting as a fiduciary.”¹¹ The Commission noted in the Adopting Release that “[t]he commenters on this proposed provision strongly took issue with [the proposed exclusionary language]. Specifically, these commenters asserted that the provision would go far beyond the intended scope of the [Senate] Committee [on Agriculture, Nutrition, and Forestry] Report by, in effect, deeming the holding of commodity interests in an insurance company’s general assets as the operation of a commodity pool.”¹² In its discussion, the Commission quoted ACLI’s comment letter on the

⁷ See Revisions of Commodity Pool Operator and Commodity Trading Advisor Regulations; Delegation of Authority, 46 Fed. Reg. 26004, 26014 (May 8, 1981).

⁸ See, 7 U.S.C. §1(a)(10), and 17 CFR 4.10(d).

⁹ See Commodity Pool Operators; Exclusion for Certain Otherwise Regulated Persons From the Definition of the Term “Commodity Pool Operator; Other Regulatory Requirements, 50 Fed. Reg. 15868 (Apr. 23, 1985) (“Adopting Release”).

¹⁰ 17 CFR 4.5(a)(2) and (b)(2).

¹¹ Commodity Pool Operators and Commodity Trading Advisors; Exemption from Registration and From Subpart B of Part 4 for Certain Otherwise Regulated Persons and Other Regulatory Requirements, 49 Fed. Reg. 4778 (Feb. 8, 1984).

¹² Adopting Release, 50 Fed. Reg. at 15872.

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proposed regulations, which defined what life insurance companies’ general assets are and how the companies use them:

Life insurance companies use premiums to acquire assets such as real estate or corporate bonds, which satisfy contractual obligations under the life insurance product contract. Life insurance companies treat these contractual obligations as a liability, against which the company maintains a reserve representing the difference between the actuarially determined value of future benefits payable and future premiums receivable. Reserves are established as a way of determining or measuring the assets the company must maintain to meet its future commitments under the policies it has issued. The funds accumulated in support of these reserves are invested by the insurance company in assets that are the property of the company. Unlike some entities within the scope of the proposal’s relief, contractholders of traditional life insurance products do not own any interest in the general assets of a life insurance company. As a result of this significant distinction, a life insurance company’s general assets are not a pool in which policyholders participate.¹³

Essentially, ACLI explained that a life insurance company invests premiums paid to it by its policyholders, in order to maintain a reserve of assets, known as general assets or a general account, upon which the insurance company can rely to pay benefits to insurance policy beneficiaries, pursuant to the contractual requirements of the policies the company issues. In the same comment letter, ACLI further differentiated general accounts from insurance company separate accounts, which contain assets or investments whose value provides the basis for benefits paid pursuant to policies generally known as variable life insurance.¹⁴ ACLI argued that, if insurance companies needed relief from regulation as a CPO provided by Regulation 4.5, then “at most such relief was necessary with respect to such separate accounts.”¹⁵ The Commission agreed with ACLI’s comment on its proposal, stating explicitly in the Adopting Release that “the holding of commodity interests in an insurance company’s general assets should not make the insurance company a commodity pool,” and adopting “a provision that limits the availability of the rule – and therefore the need to seek the relief provided by the rule – to the operation of insurance company separate accounts.”¹⁶

¹³ Comment Letter of the American Council of Life Insurance, p. 5 (May 9, 1984), *quoted in* Adopting Release, 50 Fed. Reg. at 15872.

¹⁴ Adopting Release, 50 Fed. Reg. at 15872.

¹⁵ *Id.*

¹⁶ *Id.*

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In the request before the Division, ACLI is seeking interpretative relief such that life insurance companies under common ownership may contribute general account assets to a single vehicle, the General Account Entity, which may invest directly or indirectly in commodity interests, in order to achieve greater operational and accounting efficiency and lower costs, without the vehicle being deemed a commodity pool. The Division believes it significant that only affiliated life insurance companies under common control by the same parent company will contribute their general account assets to a given General Account Entity. Despite being contributed by multiple entities, the general account assets invested in a General Account Entity as described in the Correspondence ultimately are owned by the parent of the contributing affiliates, and it is the parent corporation, through its multiple subsidiaries, that bears the risk of the General Account Entity investments, including investments in commodity interests. As represented by ACLI, a General Account Entity will not accept contributions from an investor that is not an insurance company controlled by the same parent insurance company and under no circumstances would assets held in an insurance company separate account be used to fund contributions to a General Account Entity. Given the historical context of Regulation 4.5 and the Commission’s position regarding insurance company general accounts, as well as the consolidation of assets and risk of multiple commonly owned life insurance companies into a General Account Entity, the Division believes that General Account Entities, as described herein, are outside the definition of “commodity pool” under Section 1a(10) of the CEA and Commission Regulation 4.10(d). Therefore, based on the foregoing representations made by ACLI, pursuant to Commission Regulation 140.99, the Division hereby interprets the definition of “commodity pool” under Section 1a(10) of the CEA and Commission Regulation 4.10(d) to not include General Account Entities as delineated in this letter.

This letter, and the positions taken herein, represent the view of this Division only, and do not necessarily represent the position or view of the Commission or of any other office or division of the Commission. The relief issued by this letter does not excuse any entity relying upon its terms from compliance with any other applicable requirements contained in the Act or in the Commission’s regulations issued thereunder. Further, this letter, and the relief contained herein, is based upon the representations made to the Division, and applicable laws and regulations in their current form. Any different, changed or omitted material facts or circumstances might render this letter void.

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If you have any questions regarding this letter, please contact Amanda Olear, Associate Director, at 202-418-5283 or aolear@cftc.gov, or Elizabeth Groover, Special Counsel, at 202-418-5985 or egroover@cftc.gov.

Very truly yours,

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cc: Regina Thoele, Compliance
National Futures Association