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June 3, 2011

### VIA ELECTRONIC MAIL

Mr. David A. Stawick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, N.W.  
Washington, DC 20581

Ms. Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

Re: RW3038-AD06 – Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and Eligible Contract Participant"

Dear Mr. Stawick and Ms. Murphy:

The Commodity Futures Trading Commission ("CFTC") has extended the public comment period on its jointly proposed rules to further define the terms "swap dealer," "security-based swap dealer," "major swap participant," "major security-based swap participant" and "eligible contract participant."<sup>1</sup> As noted in the proposing release, the CFTC and the Securities and Exchange Commission ("SEC," and together with the CFTC, the "Commissions") are aware of the need to craft the proposed rules to achieve the purposes of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act" or "Dodd-Frank").<sup>2</sup> To that end, the Commissions are soliciting recommendations as to how their proposed rules may be

<sup>1</sup> Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant," 75 Fed. Reg. 80,174 (Dec. 21, 2010).

<sup>2</sup> 75 Fed. Reg. at 80,175, proposing changes to the Dodd-Frank Act, 12 U.S.C. § 5301.

improved consistent with the intent of the Dodd-Frank Act.<sup>3</sup> Skadden, Arps, Slate, Meagher & Flom LLP ("Skadden") appreciates the opportunity to express our views on the Commissions' proposed definition of "eligible contract participant" ("ECP"), as this is an issue of importance to our investment management clients.

When the provisions of Title VII of the Dodd-Frank Act take effect, a person's status as an ECP will continue to be important for many reasons including eligibility to engage in certain over-the-counter ("OTC") forex transactions. Unless the Commissions revise their proposed rules concerning ECP status for commodity pools, many pools that operate legitimately under CFTC exemptions will no longer be able to use OTC forex as they have in the past, a result that Congress did not intend. As discussed below, we believe that the Commissions' proposed rules can be revised to avoid this result and to better effectuate the intent of Congress without compromising the Commissions' regulatory objectives.

### **The Current Definition of "ECP" and its Dodd-Frank Act Amendments**

The ECP definition in Section 1a(12) of the Commodity Exchange Act ("CEA") currently provides for two different categories under which a pool typically qualifies as an ECP.<sup>4</sup> First, subparagraph (A)(iv) of the ECP definition provides that a commodity pool, acting for its own account, qualifies as an ECP if it has total assets exceeding \$5 million and it is "formed and operated by a person subject to regulation under" the CEA.<sup>5</sup> Under this category now, a commodity pool may qualify as an ECP regardless of whether each investor in the commodity pool is itself an ECP. Second, subparagraph (A)(v) of section 1a(12), provides, in relevant part, that an entity, acting for its own account, qualifies as an ECP if it has total assets exceeding \$10 million.<sup>6</sup> Under the current statutory language, a commodity pool may rely upon subparagraph (A)(iv) or subparagraph (A)(v) to qualify as an ECP.

In Section 741(b)(10) of the Dodd-Frank Act, Congress amends subparagraph (A)(iv) of the ECP definition to include a limited "look-through" requirement.<sup>7</sup> This new look-through requirement is limited to commodity pools relying upon subparagraph (A)(iv) and limited only for purposes of determining such pools' ECP status under CEA sections 2(c)(2)(B)(vi) and 2(c)(2)(C)(vii).<sup>8</sup> For this limited purpose alone, a commodity pool that relies upon amended

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<sup>3</sup> *Id.*

<sup>4</sup> 7 U.S.C. § 1a(12).

<sup>5</sup> 7 U.S.C. § 1a(12)(A)(iv).

<sup>6</sup> 7 U.S.C. § 1a(12)(A)(v)(I).

<sup>7</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111-203, § 741, 124 Stat. 1376, 1732 (2010). Section 741(b)(10) also renumbers the ECP definition as CEA section 1a(18).

<sup>8</sup> Section 2(c)(2)(B)(vi) states that the CEA applies to and the CFTC shall have jurisdiction over any pooled investment vehicles that engage in the retail foreign currency transactions described in Section 2(c)(2)(B)(i). 7 U.S.C. § 2(c)(2)(B)(vi). Similarly, section 2(c)(2)(C)(vii) states that the CEA applies to and the CFTC shall have jurisdiction over any pooled investment vehicles that engage in foreign currency transactions described in Section 2(c)(2)(C)(i). 7 U.S.C. § 2(c)(2)(C)(vii).

subparagraph (A)(iv) will be required to "look-through" to its participants, each of whom must otherwise qualify as an ECP, in order for the pool itself to qualify as an ECP. For all purposes not related to the OTC forex provisions in CEA sections 2(c)(2)(B)(vi) and 2(c)(2)(C)(vii), a commodity pool, irrespective of a pool participant's status, with total assets exceeding \$5 million that is formed and operated by a person subject to regulation under the CEA will continue to qualify as an ECP under amended subparagraph (A)(iv).

Congress did not amend subparagraph (A)(v) of the ECP definition in the Dodd-Frank Act to include look-through language, thereby continuing to allow a commodity pool to be able to rely upon subparagraph (A)(iv) (subject to the new look-through requirement) or subparagraph (A)(v) to qualify as an ECP, whether for OTC forex or for any other kinds of transactions.

### **The Commissions' Proposed Further Definition of the Term "ECP"**

On December 21, 2010, the Commissions jointly proposed Rule 1.3(m) to further define the term "ECP."<sup>9</sup> Under proposed Rules 1.3(m)(5) and 1.3(m)(6), the definition of "ECP" would be further narrowed with respect to commodity pools. Rule 1.3(m)(5) proposes to extend the limited look-through requirement that Congress added to section 1a(18)(A)(iv) such that a commodity pool could not qualify as an ECP for purposes of sections 2(c)(2)(B)(vi) and 2(c)(2)(C)(vii) of the CEA if it has any "direct or indirect" participant that is not an ECP.<sup>10</sup> This would expand Congress' limited look-through requirement in two significant ways. First, by its plain language the proposal expands the application of the OTC forex look-through requirement from those commodity pools that are relying upon subparagraph (A)(iv) to qualify as ECPs to all commodity pools relying upon any category of the definition to qualify as ECPs. Second, the Commissions extend the look-through requirement to include a pool's direct or indirect participants "at any investment level (*e.g.*, a participant in the pool itself (a direct participant), an investor or participant in a fund or pool that invests in the pool in question (an indirect participant), an investor or participant in a fund or pool that invests in that investor fund or pool (also an indirect participant), *etc.*)."<sup>11</sup>

Proposed Rule 1.3(m)(6) proposes that a commodity pool with total assets of less than \$5 million *or* that is not operated by a person subject to regulation under the CEA will not qualify as an ECP under subsection (A)(v).<sup>12</sup> This could effectively prohibit pools operating under a CFTC exemption (and therefore not operated by a CFTC-registered person), even where they have \$10 million or \$10 billion in total assets, from qualifying as ECPs for OTC forex purposes.

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<sup>9</sup> 75 Fed. Reg. at 80,184.

<sup>10</sup> 75 Fed. Reg. at 80,211-12.

<sup>11</sup> 75 Fed. Reg. at 80,185.

<sup>12</sup> 75 Fed. Reg. at 80,212.

The Commissions apparently proposed Rules 1.3(m)(5) and 1.3(m)(6) because of the Commissions' concerns that retail forex<sup>13</sup> commodity pools (pools that trade predominantly in forex) may circumvent the limited look-through requirement of subparagraph (A)(iv) by relying instead on other categories of the ECP definition.<sup>14</sup> For the reasons discussed below, we believe that Rules 1.3(m)(5) and 1.3(m)(6) are inconsistent with the Dodd-Frank amendments to the ECP definition and extend beyond what is reasonably necessary for the Commissions to effectuate their stated intent of prohibiting OTC forex pools from escaping appropriate regulation.

**Congress Did Not Intend Commodity Pools to Be Excluded from Subparagraph (A)(v) of the ECP Definition**

As evidenced by the statute's plain meaning, Congress did not intend subparagraph (A)(v) of the ECP definition to be available only to those commodity pools that satisfy subparagraph (A)(iv) of the ECP definition. Section 1a(18)(A)(v)(I) makes clear that "any corporation, partnership, proprietorship, organization, trust, or other entity that has total assets exceeding \$10,000,000" and that is acting for its own account qualifies as an ECP for any purpose under the CEA.<sup>15</sup> Most pools are structured privately as partnerships or limited liability companies and commonly have total assets exceeding \$10 million. Operators of pools have long structured pools to qualify for many of the legitimate exclusions and exemptions from regulation under the CEA. Many of these pools regularly use OTC forex in the course of their risk management and investment dealings.

As evidenced by the plain language of amended section 1a(18), Congress chose not to amend subparagraph (A)(v) of the ECP definition. Congress could not reasonably have intended that its decision to leave section 1a(18)(A)(v) unchanged would be subsequently interpreted to effectively exclude qualifying pools from the list of entities that may rely upon section 1a(18)(A)(v). Had Congress intended such a result, it would have simply excluded commodity pools from the enumerated list of entities in subparagraph (A)(v). The absence of any change to the language of subparagraph (A)(v), especially in light of the changes to the language in subparagraph (A)(iv), is clear evidence of Congress' intent that commodity pools should continue to be able to qualify as ECPs under subparagraph (A)(v) for all investment purposes, irrespective of whether they are able to qualify as ECPs under subparagraph (A)(iv).

We therefore request that proposed Rule 1.3(m)(6) be withdrawn.<sup>16</sup>

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<sup>13</sup> Retail foreign currency or retail FX is a term of art describing transactions in which one of the parties is not an ECP and the other party is listed in Section 2(c)(2)(B)(i)(II), generally otherwise regulated U.S. financial institutions, CFTC-registered futures commission merchants or CFTC-registered retail forex dealers. On January 20, 2010 the CFTC adopted rules setting out extensive regulation of retail FX transactions, effective October 18, 2010. 75 Fed.Reg. 55409 (Sept. 10, 2010)

<sup>14</sup> 75 Fed. Reg. at 80,185.

<sup>15</sup> 7 U.S.C. §1a(12) (proposed as §1a(18) by Dodd-Frank)

<sup>16</sup> If the Commissions decide not to withdraw proposed Rule 1.3(m)(6), they should at least confirm that it applies only in the context of retail FX transactions.

**Congress Did Not Intend for the Look-Through Requirement to Apply to Commodity Pools Outside of Amended Section 1(a)(18)(A)(iv) of the CEA**

Congress did not intend the look-through requirement of amended subparagraph (A)(iv) of the ECP definition to be extended to all commodity pools relying upon any category of the ECP definition. In Section 741 of the Dodd-Frank Act, Congress added the look-through requirement to subparagraph (A)(iv) for the limited purpose of determining the ECP status of a commodity pool for the OTC forex transactions addressed in CEA sections 2(c)(2)(B)(vi) and 2(c)(2)(C)(vii). This look-through requirement was added only to subparagraph (A)(iv) and was not added to subparagraph (A)(v) or any other category of the ECP definition. If Congress intended the look-through requirement to be applied to commodity pools qualifying as ECPs under all ECP categories, Congress could have included a look-through requirement in all of the other ECP categories, which Congress did not do. That Congress only amended subparagraph (A)(iv) to include a look-through demonstrates that Congress only intended the look-through requirement to apply to pools qualifying as ECPs under subparagraph (A)(iv), that is, Congress intended the look-through requirement to apply to only those pools with less than \$10 million in total assets.

Applying the look-through requirement to all commodity pools, irrespective of size or sophistication, at all investment levels as proposed by Rule 1.3(m)(5), would create numerous issues for existing pools. Many thousands of pools that use OTC forex were and will continue to be structured to include knowledgeable employees, family members and others who are permitted to be investors under the various CFTC exemptions on which they rely. In this regard we note that, while thousands of pools have been structured in reliance on CFTC Rules 4.13(a)(3) and (4), many other pools are and will continue to be structured under Rule 4.7, Rule 4.13(a)(1) and (2) as well as exemptions that the CFTC may well develop in the future. If the Commissions extend the look-through in (A)(iv) to all ECP categories, many of these pools that otherwise would have qualified as ECPs under subparagraph (A)(v) will be precluded from ECP status by the presence of a non-ECP investor at some investment level.

In the context of knowledgeable employees, this sweeping application of the look-through requirement is at odds with the Commissions' otherwise thoughtful extensions of investor sophistication requirements. Many privately offered commodity pools allow or require participation by sophisticated or knowledgeable employees, who might not otherwise qualify as ECPs. Participation by knowledgeable employees is permitted and recognized in a number of contexts, including in the definition of accredited investor under the Securities Act of 1933, as amended,<sup>17</sup> in the context of the exemption under section 3(c)(7) of the Investment Company Act of 1940, as amended,<sup>18</sup> and in the definition of Qualified Eligible Participants ("QEP") under

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<sup>17</sup> 17 C.F.R. § 230.501(a) (2011).

<sup>18</sup> 15 U.S.C. § 80a-3(c)(7).

Rule 4.7 of the CEA.<sup>19</sup> In fact, many investors in private investment funds and fund advisers require the participation of investment professionals in the fund in order to ensure that the interests of the investment professionals are aligned with the interests of the investors. This participation is also important for fund advisers to offer to investment professionals as a matter of recruiting and retaining the best talent because participation in the profits of the fund is seen as an important compensation element.

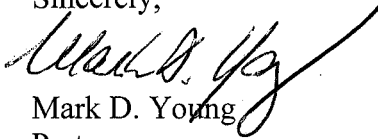
Proposed Rule 1.3(m)(5) would unnecessarily complicate the operations of innumerable established commodity pools, many of which would be forced to exclude or redeem their knowledgeable employees simply to qualify as an ECP, and would provide little protection to retail investors that could not otherwise be provided through a more narrowly tailored proposal. To effectuate the plain intent of Congress' selective amendments to the ECP definition, we respectfully request that the Commissions eliminate proposed Rule 1.3(m)(5).

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<sup>19</sup> 17 C.F.R. § 4.7 (2011).

We appreciate the opportunity to comment on this proposal and look forward to working with the Commissions throughout this rulemaking process.

Sincerely,



Mark D. Young  
Partner

Cc: Chairman Gary Gensler  
Chairman Mary Schapiro  
Commissioner Michael Dunn  
Commissioner Bart Chilton  
Commissioner Jill Sommers  
Commissioner Scott O'Malia  
Commissioner Kathleen Casey  
Commissioner Elisse Walter  
Commissioner Luis A. Aquilar  
Commissioner Troy A. Paredes