ICI Global

110 Bishopsgate
19th Floor, Suites 19-06 and 19-07
London EC2N 4AY, UK
+44 (0) 207 961 0830
www.iciglobal.org

Suite 715–717, Level 7
Two Exchange Square
8 Connaught Place
Central, Hong Kong
+852 2168 0882

1401 H Street, NW
Suite 1200
Washington, DC 20005, USA
+001 202 326 5800
www.ici.org

December 19, 2016

Mr. Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: *Cross-Border Application of the Registration Thresholds and External Business Conduct Standards Applicable to Swap Dealers and Major Swap Participants (RIN 3038-AE54)*

Dear Mr. Kirkpatrick:

ICI Global[1] appreciates the opportunity to comment on the proposed rules and interpretations of the Commodity Futures Trading Commission ("CFTC" or "Commission") on the cross-border application of the registration thresholds and external business conduct standards for swap dealers and major swap participants.[2] The proposed rules specify when the CFTC would require US and non-US persons to include their cross-border swap dealing transactions or swap positions in their swap dealer or major swap participant registration threshold calculations and the

[1] ICI Global carries out the international work of the Investment Company Institute, serving a fund membership that includes regulated funds publicly offered to investors in jurisdictions worldwide, with combined assets of US$19.8 trillion. ICI Global seeks to advance the common interests and promote public understanding of regulated investment funds, their managers, and investors. Its policy agenda focuses on issues of significance to funds in the areas of financial stability, cross-border regulation, market structure, and pension provision. ICI Global has offices in London, Hong Kong, and Washington, DC.

[2] *See* Cross-Border Application of the Registration Thresholds and External Business Conduct Standards Applicable to Swap Dealers and Major Swap Participants, 81 Fed. Reg. 71946 (Oct. 18, 2016), available at https://www.gpo.gov/fdsys/pkg/FR-2016-10-18/pdf/2016-24905.pdf.

extent to which swap dealers and major swap participants would be required to comply with the CFTC's business conduct standards in cross-border transactions.[3]

Importantly, the CFTC proposes to define certain terms, including the definition of "US person." Our letter focuses on this key term, which the CFTC indicates will apply to any subsequent rulemakings addressing the cross-border application of other swap requirements. Given the importance of this definition, we are gravely concerned that the Commission does not provide in the proposed rule an exclusion from the definition of "US person" for certain non-US regulated funds, which was part of the Commission's cross-border guidance.[4] Without the exclusion, the proposed definition of US person could impose significant regulatory obligations on non-US regulated funds that have only a tangential nexus to the United States. Moreover, a definition that could transform a non-US fund into a US person because it is managed by a US firm would disadvantage US asset managers compared to their non-US counterparts, resulting in harm to US business and potentially driving asset management business overseas. In adopting a definition of "US person" that will trigger the application of the US swap requirements to cross-border transactions, we urge the CFTC to exclude explicitly certain non-US regulated funds from the definition and, as proposed, to remove the majority US ownership test from the definition. We discuss our recommendations and concerns in more detail below.

I. The CFTC Should Exclude Certain Non-US Regulated Funds from the "US Person" Definition

Lack of an Exclusion for Certain Non-US Regulated Funds Could Extend Inappropriately the Territorial Reach of the CFTC's Swap Rules

Under the proposed rules, a collective investment vehicle would be "US person" if its principal place of business is in the United States. Departing from the CFTC's Cross-Border Guidance, the proposed rules do not explicitly exclude from the definition funds that are publicly offered only to non-US persons and not offered to US persons.[5]

Given that the swaps market is global in nature and swap transactions are routinely entered into between counterparties located in different jurisdictions, we continuously have urged the Commission to develop a practical definition of "US person" for non-US regulated funds to avoid extending inappropriately the application of the US regulations to entities that have only a nominal

---

[3] In addition, the proposed rules outline whether and to what extent these thresholds and standards would apply to swap transactions that are arranged, negotiated, or executed using personnel located in the United States.

[4] *See* Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations, 78 Fed. Reg. 45292 (July 26, 2013) ("Cross-Border Guidance"), available at https://www.gpo.gov/fdsys/pkg/FR-2013-07-26/pdf/2013-17958.pdf.

[5] In the Cross-Border Guidance, the Commission stated that "a collective investment vehicle that is publicly offered only to non-U.S. persons and not offered to U.S. persons generally would not fall within any of the prongs of the interpretation of the term 'U.S. person.'" *See*, *id*, at 45314 (emphasis added).

nexus to the United States.[6] As Section 2(i) of the Commodity Exchange Act ("CEA") states, swap rules related to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act") shall not apply to activities outside the United States unless, among other things, those activities "have a direct and significant connection with activities in, or effect on, commerce of the United States."[7] When the Commission provided an exclusion from the definition of "US person" for funds that are publicly offered only to non-US persons and not offered to US persons in the Cross-Border Guidance, it properly recognized that non-US regulated funds do not have a "direct and significant connection" with US commerce and should not be subject to the substantive provision of the Dodd-Frank Act.[8]

We therefore disagree with the CFTC's current proposal to reverse this determination and to remove this clear exclusion for non-US regulated funds from the proposed rules. Non-US regulated funds publicly offered only to non-US persons and not offered to US persons (such as a UCITS that are not marketed to investors in the United States) do not have a "direct and significant connection" with US commerce, and subjecting those funds or those funds' transactions to the CFTC's swap requirements would go beyond the intent and scope of the Dodd-Frank Act. These funds do not intend to be active in the US markets, the risks of their related transactions reside outside the United States, and investors have no reasonable expectation that US laws would apply to them. Nevertheless, a non-U.S. regulated fund the portfolio of which is being managed by a US investment adviser or that is sponsored by a US entity may be considered to have its principal place of business in the United States, and accordingly would be a US person. Under the proposed rules, those funds would be deemed US persons unnecessarily and would be subject to the full set of external business conduct rules. Further, the CFTC expects to apply this definition of "US person" to subsequent rulemakings specifically addressing the cross-border application of other swap requirements.

Defining Non-US Regulated Funds with a Nominal Nexus to the United States as "US Persons" Could Disadvantage US Asset Managers

The CFTC's "US person" definition without an exclusion for non-US regulated funds could significantly disadvantage US asset managers to non-US regulated funds vis-à-vis their non-US counterparts, resulting in harm to US business and potentially driving asset management

---

[6] ICI Global and the Investment Company Institute have made similar comments to the CFTC on a number of occasions. *See* Letter from Dan Waters, Managing Director, ICI Global, to Christopher Kirkpatrick, Secretary, CFTC, dated Sept. 14, 2015; Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to Melissa Jergens, Secretary, CFTC, dated July 5, 2013; Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to Melissa Jergens, Secretary, CFTC, dated February 6, 2013; Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to David Stawick, Secretary, CFTC, dated August 23, 2012.

[7] *See* Section 2(i) of the CEA. Similarly, such swap rules shall not contravene CFTC rules or regulations adopted to prevent the evasion of any provision of the Dodd-Frank Act. *Id.*

[8] *Id. See also* Cross-Border Guidance, *supra* note 4, at 45314.

business overseas. A non-US regulated fund with a US asset manager could be considered a US person under the proposed rules and be subject to US regulations. To avoid the unnecessary costs and burdens of potentially having to comply with the rules of two separate jurisdictions – those of the fund's home jurisdiction as well as CFTC regulations – these non-US regulated funds may terminate the US asset manager and/or avoid hiring a US asset manager. These disincentives could dissuade a non-US regulated fund from selecting a US asset manager, even if the US asset manager has the expertise to manage the fund. In addition, non-US dealers may seek to avoid engaging in transactions with non-US regulated funds that could be US persons to avoid having to comply with the Dodd-Frank swap requirements. These results would be harmful to the fund, its investors, and the US asset management industry.

Crafting an Exclusion for Non-US Regulated Funds Should be Based on Workable Systems and Appropriate Regulatory Interest

We urge the Commission to define "US person" focusing on whether an entity makes an "offering to US persons," which has two distinct advantages. First, if the "US person" determination is made by how a fund conducts its offerings, funds already have systems in place to comply with the standard.[9] This approach would provide certainty to counterparties at the outset of a swap transaction regarding which jurisdiction's rules will govern. Second, focusing on the "offering to US persons" would look to whether the fund is attempting to target the US market or US investors and should be appropriately subject to US laws. Our recommendation would exclude non-US regulated funds that have little US nexus and do not target the US market or US investors and therefore present little risk to the US markets or US investors.

We recognize that the CFTC has adopted already the proposed definition of "US person" for the cross-border margin rule, but we believe that the deficient definition should be amended and should not be carried forward to all of the other substantive provisions of the CFTC's swap requirements. We therefore urge the Commission to adopt a definition of "US person" that specifically excludes pools, funds or other collective investment vehicles that are publicly offered only to non-US persons and not offered to US persons.

II. The CFTC Should Exclude the US Majority-Owned Fund Test from the "US Person" Definition

In the proposed rules, the CFTC would remove from the definition of "US Person" the majority-ownership test that would deem commodity pools, pooled accounts, investment funds or other collective investment vehicles that are majority-owned by one or more US persons as US persons. The Commission explains that it removed this portion of the requirement, which appeared in the Cross-Border Guidance, over concerns about identifying and tracking a fund's

[9] For example, global fund managers have long structured their activities to reflect the requirements of Regulation S under the Securities Act of 1933 to remain offshore and have policies and procedures in place to avoid making offers to US persons.

beneficial ownership. We fully support the Commission's determination to exclude this test from the definition as we have urged previously.[10]

Over the last decade, use of omnibus structures, in which an intermediary registers and holds accounts on behalf of its customers at a fund's transfer agent in the intermediary's name and maintains the customer data underlying the accounts on its own books, have become much more prevalent.[11] In fact, there may be multiple layers of omnibus intermediaries through which the ultimate beneficial investors may hold shares. Often, funds do not have access to data underlying the omnibus positions, and intermediaries have no regulatory obligation to provide this information to funds. Moreover, certain jurisdictions may prohibit intermediaries from disclosing beneficial ownership information, such as personal addresses that may constitute "personal data" under EU data protection laws. Given these structural and operational challenges to verifying the status of shareholders, we fully support the Commission's determination to remove the majority US ownership test from the "US person" definition.

* * * * * * *

[10] *See* Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to Melissa Jergens, Secretary, CFTC, dated July 5, 2013; Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to Melissa Jergens, Secretary, CFTC, dated February 6, 2013; Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to David Stawick, Secretary, CFTC, dated August 23, 2012. The Cross-Border Guidance would have interpreted "majority-owned" in this context to mean the beneficial ownership of more than 50 percent of the equity or voting interests in the collective investment vehicle. *See* Cross-Border Guidance, *supra* note 4, at 45314.

[11] Investors in non-US regulated funds that are publicly offered only to non-US persons typically purchase shares through intermediaries (not directly from the fund), and these shares are registered and held in nominee/street name accounts by the recordkeeper.

We appreciate the opportunity to provide our comments to the Commission. If you have any questions about our comment letter, please feel free to contact the undersigned, Jennifer Choi, Associate General Counsel, at (202) 326-5876, or Kenneth Fang, Assistant General Counsel, at (202) 371-5430.

Sincerely,

/s/Dan Waters

Dan Waters
Managing Director
ICI Global
+44-203-009-3101

cc: The Honorable Timothy G. Massad
The Honorable Sharon Y. Bowen
The Honorable J. Christopher Giancarlo