INVESTMENT COMPANY INSTITUTE

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September 28, 2017

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

Re: Project KISS (RIN 3038-AE55)

Dear Mr. Kirkpatrick:

The Investment Company Institute[1] commends the Commodity Futures Trading Commission for undertaking its "Project Kiss" initiative to determine how the Commission's rules, regulations, or practices can be applied in a simpler, less burdensome manner.[2] ICI and its members have a strong interest in the CFTC and its staff rationalizing CFTC rules to reduce unnecessary burdens on market participants, particularly by recognizing the critical differences between registered investment companies ("registered funds") and traditional participants in the commodity markets. As participants in the derivatives markets, registered funds support regulation designed to maintain orderly, competitive, and efficient derivatives markets. Derivatives are a particularly useful portfolio management tool in that they offer registered funds considerable flexibility in structuring their investment portfolios.[3]

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[1] ICI is a leading global association of regulated funds, including mutual funds, exchange-traded funds, closed-end funds, and unit investment trusts in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's members manage total assets of US$20.4 trillion in the United States, serving more than 95 million US shareholders, and US$6.7 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC.

[2] *Project Kiss*, 82 Fed.Reg. 23765 (May 24, 2016), *available at* http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2017-10622a.pdf.

[3] A registered fund uses derivatives, among other things, to hedge positions, equitize cash, adjust the duration of its portfolio, and generally manage the portfolio in accordance with the investment objectives stated in its prospectus.

Registered funds are subject to CFTC regulation in two separate capacities. First, funds are buy-side participants in the derivatives market and are subject to rules such as the clearing mandate and the trading obligation. Second, registered funds are subject to CFTC regulation as a result of the CFTC's 2012 amendments to Regulation 4.5 under the Commodity Exchange Act (CEA), which required many registered fund advisers to register with the CFTC as commodity pool operators (CPOs).

We welcome this opportunity to provide our recommendations as the Commission reconsiders the application of its rules. We believe our recommendations are consistent with the agenda Chairman Giancarlo recently articulated for the CFTC,[4] particularly his goals of:

- Reducing regulatory burden, consistent with President Trump's executive orders;[5]
- Returning the CFTC to "regular order," and
- Resetting the CFTC's focus on its core mission, including leveraging its cooperation with parallel federal market regulators such as the Securities and Exchange Commission.

We recognize that some of our recommendations may, or would, require the Commission to engage in rulemaking. We discuss those issues in our letter, however, because we believe they are critical issues for the Commission's further consideration, and hope this discussion will be the beginning of a further and more in-depth dialogue.

We have organized our recommendations, below, according to each of the topics on which the Commission seeks comment.[6] For your convenience, our attached recommendations are summarized briefly below:

- **The CFTC should amend Regulation 4.5 to eliminate unnecessary regulatory overlap for registered funds and their advisers.** The CFTC should amend the rule to exclude registered funds advisers from being treated as CPOs, just as they were immediately prior to the rule's 2012

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[4] Acting Chairman J. Christopher Giancarlo, *CFTC: A New Direction Forward, Remarks before the 42nd Annual International Futures Industry Conference,* Boca Raton, Florida (March 15, 2017), *available at* http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo-20.

[5] *See* Exec. Order, Reducing Regulation and Controlling Regulatory Costs (Jan. 30, 2017), *available at* https://www.whitehouse.gov/the-press-office/2017/01/30/presidential-executive-order-reducing-regulation-and-controlling; *see also* Exec. Order, Enforcing the Regulatory Reform Agenda (Feb. 24, 2017), *available at* https://www.whitehouse.gov/the-press-office/2017/02/24/presidential-executive-order-enforcing-regulatory-reform-agenda.

[6] Consistent with the electronic filing requirements, we are filing this cover letter, along with an Appendix that corresponds to the topic of the respective Commission filing portal (registration, reporting, clearing, executing). *See* https://comments.cftc.gov/KISS/KissInitiative.aspx.

amendments.

- **Until the CFTC amends Regulation 4.5, it should take a substituted compliance approach to regulating registered fund CPOs and CTAs.** We suggest that the CFTC and its staff take a pragmatic, outcomes-based substituted compliance approach to addressing regulatory overlap for registered fund CPOs and CTAs in areas that were not adequately addressed by harmonization, and take such an approach as new issues arise in the future. We provide, as examples, Forms CPO-PQR and CTA-PR, liquidation statements, and recordkeeping.

- **The CFTC should adopt its rulemaking proposal that would provide relief to CPOs and CTAs acting on behalf of non-US persons.** We urge the CFTC promptly to adopt its 2016 rulemaking proposal that would, among other things, amend Regulation 3.10(c)(3) to eliminate unnecessary conditions, consistent with prior staff no-action relief.

- **The CFTC should amend its definition of "US person" to exclude certain non-US funds**. For purposes of the cross-border application of the CFTC's swaps provision, the CFTC should exclude from its definitions of "US person" non-US regulated funds that are authorized to be publicly offered to non-US persons but are not offered publicly to US persons.

- **The CFTC should retain the strong asset protections for cleared swaps provided by the "LSOC" model.** As the CFTC considers any recommendations for reform it may receive in the clearing area, we urge it to retain the "legal segregation with operational commingling," or LSOC, model for the protection of customer collateral and extend these protections to other cleared derivatives.

- **The CFTC should strengthen the process for making a swap "available to trade."** The CFTC should engage in a rulemaking that would address the risks and weaknesses inherent in the current "made available to trade," or MAT, process. We recommend that this process ensure that only those swaps that are liquid enough to support mandatory execution on a swap execution facility or designated contract market become MAT.

We also share Chairman Giancarlo's interest in reforming the CFTC's swap trading rules to foster a vibrant and liquid swaps market. To that end, we are preparing a separate letter—that we expect to submit soon—which will contain a set of recommendations designed to improve swaps trading.

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We appreciate the Commission's consideration of our recommendations. If you have questions or require further information, please contact me at (202) 218-3563, Sarah Bessin at (202) 326-5835, Jennifer Choi at (202) 326-5876, or Rachel Graham at (202) 326-5819.

Sincerely,

/s/ Dorothy M. Donohue

Dorothy M. Donohue
Acting General Counsel

cc: The Honorable J. Christopher Giancarlo
The Honorable Brian D. Quintenz
The Honorable Rostin Benham

Matthew B. Kulkin, Director
Division of Swap Dealer and Intermediary Oversight
Commodity Futures Trading Commission

Thomas W. Sexton, III, President and CEO
Regina G. Thoele, Senior Vice President, Compliance
National Futures Association

Appendix: Executing Recommendation

Recommendation: The CFTC Should Strengthen the Process for Making a Swap "Available to Trade"[1]

Background: The Dodd-Frank Act amended the Commodity Exchange Act to require that any swap subject to the clearing requirement must be executed on a swap execution facility (SEF) or a designated contract market (DCM) unless no SEF or DCM "makes the swap available to trade."[2] Based on this language, the CFTC has adopted rules setting out the process to determine when a swap is "made available to trade" (MAT).[3] The implications of the MAT determination are critical, as that process determines whether a swap will be subject to mandatory execution. If a swap is deemed "available to trade," it generally must be traded on a DCM or SEF, and nearly all bilateral trading in that swap must cease.

The current MAT process, however, is fundamentally flawed and is in critical need of reform. It provides the CFTC no meaningful role in determining which swaps will be subject to mandatory trading and turns over this process to SEFs and DCMs. The MAT process also does not adequately establish criteria to ensure that there is sufficient liquidity of the swap to trade on the SEF or DCM, or sufficient operational readiness of market participants to support mandatory trading in the swap.[4] This process fails to protect adequately against the financial incentives of DCMs and SEFs to subject a swap to mandatory trading, even when there is insufficient liquidity to support mandatory trading in that swap.

Recommendation: The CFTC should engage in a rulemaking that would address the risks and weaknesses inherent in the current MAT process. We recommend that the MAT process ensure that only those swaps that are liquid enough to support mandatory SEF or DCM execution become MAT. The process should include an assessment of the market structure to verify that it can support SEF or DCM trading of a swap, including the number of market participants presently providing liquidity on trading platforms and the capacity of these liquidity providers/makers and trading platforms to manage additional volume arising from the application of the trading mandate to the swap. The Commission should have adequate authority to ensure that a swap will be subject to mandatory SEF or DCM

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[1] We recognize that addressing this recommendation would require the Commission to engage in rulemaking.

[2] Section 2(h)(8) of the Commodity Exchange Act.

[3] *See Process for a Designated Contract Market or Swap Execution Facility To Make a Swap Available to Trade, Swap Transaction Compliance and Implementation Schedule, and Trade Execution Requirement Under the Commodity Exchange Act*, 78 Fed. Reg. 33606 (June 4, 2013).

[4] *See* Letter to Mr. Christopher Kirkpatrick, Secretary, CFTC, from David W. Blass, General Counsel, ICI, dated Aug. 17, 2015, *available at* https://www.ici.org/pdf/29262.pdf; Letter to Mr. David A. Stawick, Secretary, CFTC, from Karrie McMillan, General Counsel, ICI, dated Feb. 13, 2012, *available at* https://www.ici.org/pdf/25910.pdf.

execution only if the swap is sufficiently liquid and the infrastructure supports adequately the trading of the swaps on a SEF or DCM. In addition, no swap should become MAT until the SEF(s) or DCM(s) listing that swap are operationally ready to support the execution requirement.