

COMMENT LETTER

August 21, 2013

ICI and ICI Global Submit Letter on SEC Proposed Rules on Cross-Border Security-Based Swap Activities (pdf)

August 21, 2013 Ms. Elizabeth M. Murphy Secretary Securities and Exchange Commission
100 F Street, NE Washington, DC 20549 Re: Cross-Border Security-Based Swap Activities;
Re-Proposal of Regulation SBSR and Certain Rules and Forms Relating to the Registration of
Security-Based Swap Dealers and Major Security-Based Swap Participants Dear Ms. Murphy:
The Investment Company Institute (“ICI”)¹ and ICI Global² are submitting this letter in
response to the rules and interpretive guidance for parties to cross-border security-based
(“SB”) swap transactions proposed by the Securities and Exchange Commission (“SEC” or
“Commission”).³ The Proposal addresses the application of Title VII of the Dodd-Frank Wall
Street Reform and Consumer Protection Act (“Dodd-Frank Act”) to market intermediaries,
participants, and infrastructures for SB swaps. The Proposal also addresses certain
transaction-related requirements under Title VII in connection with reporting and
dissemination, clearing, and trade execution for SB swaps. Concurrently, the SEC re-opened
for comment all of its currently pending rule proposals related to Title VII of the Dodd-Frank
Act in light of the Proposal.⁴ 1 The Investment Company Institute is the national association
of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded
funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high
ethical standards, promote public understanding, and otherwise advance the interests of
funds, their shareholders, directors, and advisers. Members of ICI manage total assets of
\$14.9 trillion and serve over 90 million shareholders. 2 ICI Global is the global association of
regulated funds publicly offered to investors in leading jurisdictions worldwide. ICI Global
seeks to advance the common interests and promote public understanding of global
investment funds, their managers, and investors. Members of ICI Global manage total
assets in excess of US \$1 trillion. 3 Cross-Border Security-Based Swap Activities; Re-
Proposal of Regulation SBSR and Certain Rules and Forms Relating to the Registration of
Security-Based Swap Dealers and Major Security-Based Swap Participants, Release No.
34-69490, 78 FR 30967 (May 23, 2013), available at
<http://www.gpo.gov/fdsys/pkg/FR-2013-05-23/pdf/2013-10835.pdf> (“Proposal”). 4
Reopening of Comment Periods for Certain Rulemaking Releases and Policy Statement
Applicable to Security-Based Swaps Proposed Pursuant to the Securities Exchange Act of
1934 and the Dodd-Frank Wall Street Reform and Consumer Protection Act, Release No.
34-69491, 78 FR 30800 (May 23, 2013), available at
<http://www.gpo.gov/fdsys/pkg/FR-2013-05-23/pdf/2013-10836.pdf>. The re-opened
comment period for these pending proposals closed on July 22, 2013. ICI/ICI Global Letter to
Ms. Elizabeth M. Murphy August 21, 2013 Page 2 of 14 Background and Need for Regulatory

Coordination U.S. funds that are regulated under the Investment Company Act of 1940 (“ICA”) and non- U.S. regulated funds publicly offered to investors⁵ (collectively, “Regulated Funds”) use swaps and other derivatives in a variety of ways. Derivatives are a particularly useful portfolio management tool in that they offer Regulated Funds considerable flexibility in structuring their investment portfolios. Uses of swaps and other derivatives include, for example, hedging positions, equitizing cash that a Regulated Fund cannot immediately invest in direct equity holdings, managing a Regulated Fund’s cash positions more generally, adjusting the duration of a Regulated Fund’s portfolio, or managing a Regulated Fund’s portfolio in accordance with the investment objectives stated in a Regulated Fund’s prospectus. Therefore, as participants in the global derivatives marketplace, Regulated Funds have a keen interest in regulators reaching consensus on a rational and practical approach to regulating cross-border derivatives transactions. As the Commission well recognizes, the SB swap market is a global market and cross-border transactions involving counterparties in different jurisdictions are the “majority of security-based swaps.”⁶ Given the international nature of these transactions and efforts by regulators worldwide to regulate these activities, ICI and ICI Global have emphasized the importance of global coordination among regulators with respect to cross-border application of derivatives regulations to avoid imposing, at best, duplicative and, at worst, conflicting regulatory requirements on counterparties.⁷ We have

⁵ For purposes of this letter, the term “non-U.S. regulated fund” refers to any fund that is organized or formed outside the United States, is authorized for public sale in the country in which it is organized or formed, and is regulated as a public investment company under the laws of that country. Generally, non-U.S. regulated funds are regulated to make them eligible for sale to the retail public, even if a particular fund may elect to limit its offering to institutional investors. Such funds, like U.S. registered investment companies, typically are subject to substantive regulation in areas such as disclosure, form of organization, custody, minimum capital, valuation, investment restrictions (e.g., leverage, types of investments or “eligible assets,” concentration limits and/or diversification standards). For example, in Canada, shares issued by mutual funds are generally regulated as securities by Securities Acts in place in each province, and specifically regulated as funds in a series of detailed national instruments and their companion policies that apply across the country. Funds are primarily regulated by National Instrument (NI) 81-102, which includes portfolio investment rules (such as limits on leverage and borrowing) as well as requirements on custodianship, sales, redemptions, net asset value calculation, fundamental changes and sales communications, among others. Detailed disclosure rules governing form and content of prospectuses, annual information forms and Funds Facts (analogous to the U.S. summary prospectus) are set out in NI 81-101. Other substantive rules regulate areas such as sales practices (NI 81-105), continuous disclosure (NI 81-106) and independent review committees to consider conflict of interest matters (NI 81-107).

⁶ Proposal, *supra* note 3, at 30976.

⁷ See Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to Wayne Byres, Secretary General, Basel Committee on Banking Supervision, Bank for International Settlements, and David Wright, Secretary General, International Organization of Securities Commissions, dated Mar. 14, 2013; Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to Melissa Jergens, Secretary, CFTC, dated Feb. 6, 2013; Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to Wayne Byres, Secretary General, Basel Committee on Banking Supervision, Bank for International Settlements, and David Wright, Secretary General, International Organization of Securities Commissions, dated Sept. 27, 2012; Letter from ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 3 of 14 expressed our concern that there may be reluctance to engage in cross-border derivatives transactions with a dealer in a different jurisdiction, unless regulators coordinate the requirements that

would apply to such activities. International comity and practical considerations dictate that there be real and meaningful coordination among regulators on how cross-border transactions between counterparties in different jurisdictions should be appropriately regulated. We appreciate the SEC's thoughtful approach in the Proposal both in the careful consideration of the various issues and in the form by which the SEC proposes to impose its approach (i.e., by rule rather than by guidance). We also fully recognize the tremendous amount of work undertaken by the Commission and the staff on the Proposal. The SEC's approach to the regulation of cross-border activities differs, however, in significant ways from the approach adopted by the Commodity Futures Trading Commission ("CFTC") in its interpretive guidance regarding the cross-border application of the swap provisions of the Commodity Exchange Act ("CEA").⁸ Now that the CFTC has adopted its final guidance, we believe that consistency between the CFTC and the SEC in the outcome of whether an entity or transaction would be subject to the Dodd-Frank Act requirements (rather than the particular analysis or test) to the extent possible and reasonable should be the primary goal. We acknowledge that a common approach may be particularly challenging for the SEC given that the CFTC has finalized its guidance and the CFTC's approach was issued as guidance rather than as a rule (without the benefit of a cost-benefit analysis). Although it would have been preferable for the primary regulators of the U.S. derivatives market to have developed a similar set of rules at the same time, the SEC now should coordinate its approach with that of the CFTC given the significant global ramifications. To ensure certainty and simplicity, we urge the adoption of SEC rules that will produce outcomes similar to those under the CFTC's guidance. Global firms will face significant costs and burdens if the two regulatory approaches produce different outcomes regarding whether an entity or transaction would be subject to the Dodd-Frank Act. Attempting to analyze derivatives transactions differently for swaps and SB swaps that are traded typically by the same trading desk or desks of asset managers would be unworkable. Therefore, we suggest several modifications to the SEC's proposal both to address concerns with the SEC's proposed approach and to ensure that the outcome is broadly consistent with the CFTC's approach. Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to David Stawick, Secretary, CFTC, dated Aug. 23, 2012, ⁸ Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations, 78 FR 45292 (July 26, 2013) available at <http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2013-17958a.pdf> ("Final Cross-Border Guidance"); See Further Proposed Guidance regarding Compliance with Certain Swap Regulations, 78 FR 909 (Jan. 7, 2013), available at <http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-31734a.pdf>; Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 FR 41214 (July 12, 2012), available at <http://www.gpo.gov/fdsys/pkg/FR-2012-07-12/pdf/2012-16496.pdf> (together "CFTC Proposed Cross-Border Guidance"). ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 4 of 14 Generally, the Proposal would subject SB swap transactions to the requirements of Title VII if they are (1) entered into with a U.S. person or (2) otherwise conducted within the United States.⁹ The SEC notes the guiding principles for its approach to applying Title VII in the cross-border context, including risks to the U.S. financial system, transparency, counterparty protection, economic impacts, harmonization with other regulators, consistent international standards, and anti-evasion. We support these principles and believe our suggestions are consistent with those goals. In particular, we support the Commission's proposed definition of U.S. person but believe the "principal place of business" test is not appropriate for funds or other collective investment vehicles and suggest an alternative test for these vehicles. In addition, we believe that a broader exception is necessary for transactions between two non-U.S. persons that may be

considered “conducted in the United States” solely by virtue of the engagement of a U.S. investment adviser/asset manager by a counterparty. We also have some comments on the substituted compliance framework proposed by the Commission. Under the Proposal, U.S. investment managers to non-U.S. regulated funds would face an economic disadvantage if global market participants cease trading with such funds solely to avoid being subject to Title VII requirements. We particularly believe this disparate impact is unwarranted if these types of transactions do not raise risks to the U.S. financial system or undermine counterparty protection. Without modifications, the proposed approach could have unintended but substantial negative economic and competitive effects on U.S. entities, damage the U.S. financial markets and U.S. economy, and be potentially harmful to non-U.S. regulated funds and their investors. We describe our concerns and comments in more detail below.

Definition of U.S. Person Should Be Tailored for Non-U.S. Regulated Funds

The Proposal would define “U.S. person” as: (1) any natural person resident in the United States; (2) any partnership, corporation, trust, or other legal person organized or incorporated under the laws of the United States or having its principal place of business in the United States; or (3) any account (whether discretionary or non-discretionary) of a U.S. person. We generally support the proposed definition, with one exception. Under the second part of the proposed definition, an entity that is organized or incorporated in a jurisdiction outside the United States would be a U.S. person if it has its principal place of business in the United States. The Commission states that it has included the principal place of business provision because any risk to such entities arising from their SB swap activity is likely to manifest itself most directly within the United States and the provision would prevent entities from organizing outside the United States to avoid the costs of complying with Title VII.¹⁰ The Proposal, however, does not define or provide guidance on the term “principal place of business.”⁹ The SEC’s approach differs from the CFTC Final Cross-Border Guidance, which does not consider whether the transaction is conducted inside or outside the United States.¹⁰ Proposal, *supra* note 3, at 30997. ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 5 of 14 We believe the “principal place of business” test is not appropriate for funds and other collective investment vehicles, which are generally externally managed and have no employees or offices of their own. We urge the SEC not to apply the “principal place of business” provision to funds and other collective investment vehicles. U.S. funds registered with the SEC and regulated under the ICA are incorporated in the United States and would be considered a U.S. person without the application of the principal place of business provision.¹¹ If the SEC believes a test limited to the place of incorporation or organization is not sufficient to dissuade funds from incorporating outside the United States to avoid the burdens of Title VII, we suggest that the principal place of business test not apply to a non-U.S. regulated fund, as defined above.¹² We believe this approach would properly limit the SEC’s territorial reach to include only those non-U.S. regulated funds that intend to be active in the U.S. market, engage in derivatives transactions that could pose risks to the U.S. markets, or for which investors may have a reasonable expectation that U.S. law would apply. First, our suggestion would exclude from the definition of “U.S. person” non-U.S. regulated funds that are offered publicly to only non-U.S. persons. These funds have only a nominal nexus to the United States because they are marketed and sold publicly to retail investors outside the United States.¹³ These non-U.S. regulated funds are offered and sold in countries around the world (e.g., UCITS,¹⁴ Canadian mutual funds, Japanese investment trusts, etc.). Moreover, if the “U.S. person”¹¹ Under Section 7(d) of the ICA, an investment company organized in a foreign jurisdiction may offer publicly its securities only if the SEC finds by order that “it is both legally and practically feasible to effectively enforce” the provisions of the ICA against the fund. Since 1954, 15 orders have been granted by the SEC, but we are aware of only two funds that are currently operating under those orders and offer their

shares in the United States. 12 In response to the CFTC Proposed Cross-Border Guidance, we made a similar suggestion for determining whether a fund or collective investment vehicle is a U.S. person. See Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to Melissa Jurgens, Secretary, CFTC, dated July 5, 2013; Letter from Karrie McMillan, General Counsel, ICI, and Dan Waters, Managing Director, ICI Global, to David Stawick, Secretary, CFTC, dated Aug. 23, 2012. The CFTC has largely excluded these funds from the definition of “U.S. person.” Specifically, the CFTC provides 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 Final Cross-Border Guidance, *supra* note 8, at 45314 (emphasis added). 13 We also urge the SEC not to look to the location of the activities, employees, or offices of the “sponsor” or “adviser” of a non-U.S. fund for jurisdictional nexus under the Dodd-Frank Act because the risk of a transaction remains with the non- U.S. fund and would not migrate to the United States with the use of the services of a U.S. adviser or U.S. sponsor. Each fund is a separate pool of securities with its own assets, liabilities and shareholders, and the non-U.S. regulated fund’s U.S. adviser or promoter does not guarantee the fund’s transactions. 14 UCITS, or “undertakings for collective investment in transferrable securities,” are collective investment schemes established and authorized under a harmonized European Union (“EU”) legal framework, currently EU Directive 2009/65/EC, as amended (“UCITS IV”), under which a UCITS established and authorized in one EU Member State (“Member State”) can be sold cross border into other EU Member States without a requirement for an additional full registration. Detailed requirements applicable to UCITS include those related to disclosure and custody as well as ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 6 of 14 determination is made in this manner, systems are already in place to assess compliance with the standard. This approach also would provide certainty to counterparties at the outset of a swap transaction regarding which laws would govern. Therefore, both counterparties would be able to plan for, and address, the consequences of the “U.S. person” determination for their swap transactions. We recommend that the analysis to determine whether a non-U.S. regulated fund is making a public offshore offering to non-U.S. persons should be consistent with Regulation S under the Securities Act of 1933 (“Securities Act”). Global fund managers have long structured their activities to reflect the requirements of Regulation S to remain offshore and have policies and procedures in place to avoid making public offers to U.S. persons. Non-U.S. regulated funds commonly use the definition of “U.S. person” under Regulation S in their offering documents and procedures to prevent offers and sales to U.S. persons. In addition, our suggestion would exclude from the definition of U.S. person non-U.S. regulated funds that are publicly offered to only non-U.S. persons but offered privately to U.S. persons under Section 3(c)(1) or Section 3(c)(7) of the ICA as permitted by the SEC¹⁵ as well as certain non- U.S. regulated funds authorized to make a public offering but that elect only to offer privately to non- U.S. institutional investors.¹⁶ We believe the mostly institutional investors and non-U.S. institutional investors in these funds would not expect the protections of U.S. law to apply to such funds’ transactions. investment restrictions and limitations. See UCITS IV (requirements regarding simplified disclosure (key investor information document) (Art. 78), annual and semi-annual reports (Art. 68), appointing a depositary bank as a custodian and its responsibilities (Art. 22), redemption (Art. 76), diversification and issuer concentration (Art. 52 and Art. 56), permitted assets, including limitations relating to derivatives and leverage (Art. 50 and Art. 52)). 15 Although some non-U.S. regulated funds may, consistent with well-established positions of the staff of the SEC, make a limited private offering to U.S. investors in addition to their public offering to non-U.S. investors, this limited private offering does not increase the risk to U.S. investors or U.S. markets. The SEC staff permits such offerings to be made

only to a very limited number of U.S. investors or investors who are highly qualified, ameliorating investor protection concerns. See Goodwin, Procter & Hoar, SEC No-Action Letter (pub. avail. Feb. 28, 1997); Touche, Remnant & Company, SEC No-Action Letter (pub. avail. Aug. 27, 1984). Under the ICA, a foreign fund is prohibited from using any means of U.S interstate commerce to offer or sell its securities in connection with a public offering unless the SEC has issued an order permitting the foreign fund to register under the ICA, which orders are exceedingly rare. See *supra* note 11. The SEC staff takes the position that a non-U.S. regulated fund may, however, make a limited private offering of its shares in the United States to fewer than 100 beneficial owners resident in the United States or to highly sophisticated “qualified purchasers” (individuals must have more than \$5 million in investments) in the United States at the same time the fund publicly offers its shares overseas to non-U.S. investors. The existence of a limited private offering in the United States does not increase the risk to U.S. markets because the non-U.S. regulated fund remains subject to substantive regulation offshore, and the risks of the fund’s transactions remain within the fund and do not migrate to the United States as a result of the private offering. 16 We recognize that the CFTC’s definition of U.S. person does not exclude funds in these two categories. We intend to seek further guidance or relief for these non-U.S. funds that do not have a significant connection to the United States. ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 7 of 14 In crafting a tailored provision for funds and other collective investment vehicles, we caution the SEC not to incorporate parts of the definition adopted by the CFTC that look to the number or percentage of U.S. investors in a fund. This type of analysis is not workable for non-U.S. regulated funds that are publicly offered. First, many non-U.S. regulated funds are publicly traded in the secondary market, and the manager/operator of the fund and the fund would not know the composition of the investor base in the secondary market. Second, because of the distribution system for non-U.S. regulated funds and the use of omnibus accounts, the fund manager/operator (and its administrator/recordkeeper) would not know the ultimate beneficial owners of the funds even though their shares are not offered to U.S. persons. Investors in non-U.S. regulated funds that are publicly- offered only to non-U.S. 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.¹⁷ When shares are held through these types of omnibus accounts, the fund manager/operator (and its administrator/recordkeeper) typically does not have information regarding the underlying investors who are the customers of the intermediary.¹⁸ In fact, there may be multiple layers of omnibus intermediaries through which the ultimate investors may hold shares.¹⁹ Moreover, certain jurisdictions may prohibit disclosure by intermediaries of beneficial owner information such as, for example, personal addresses that may constitute “personal data” under European Union data protection laws. For these reasons, a fund manager/operator (and its administrator/recordkeeper) would not be able to verify whether underlying investors are U.S. persons in a non-U.S. fund that is publicly-offered only to non-U.S. persons. Finally, by not tying the definition of a U.S. person to the fund’s actual investor base, non-U.S. funds and their counterparties would know at the outset of a derivatives transaction whether they would be subject to Title VII requirements. If the determination of “U.S. person” status could evolve, however, over time because of investor changes that were beyond the control of a fund or its manager/operator, counterparties would have to reassess periodically the difficult issue of how swaps that were entered into before the change in U.S. person status occurred might later be subject to Title VII requirements. 17 See OECD, *The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles* (April 2010). 18 For non-U.S. regulated funds, beneficial owner positions are predominantly held in omnibus accounts on the books of the fund in the name of the financial intermediary (e.g., a financial institution or insurance

company), acting on behalf of its customers. An omnibus account includes the shares of multiple investors (sometimes numbering in the thousands) including both individual and institutional customers and represents the aggregate share balance of all the subaccounts for these investors. Omnibus accounts are a common way for funds to efficiently process purchases and redemptions of their shares and are growing in use. In limited circumstances, non-U.S. regulated funds also may have intermediary-controlled individual accounts in which the fund has no relationship or contact with the customer. These accounts are typically registered in the name of the intermediary for the benefit of a non-disclosed individual customer. 19 An intermediary's omnibus account with the fund may include other omnibus accounts for which the intermediary provides services and keeps records. The fund manager/operator (and its administrator/recordkeeper) would not have transparency or information about the beneficial investors that are customers of intermediaries held in omnibus accounts. ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 8 of 14 Proposed Exceptions for Transactions Conducted in the United States between Non-U.S. Persons Should Be Expanded The Proposal defines "transaction conducted within the United States" to mean any SB swap transaction that is "solicited, negotiated, executed, or booked within the United States, by or on behalf of either counterparty to the transaction, regardless of the location, domicile, or residence status of either counterparty to the transaction." If a transaction is conducted within the United States, certain transaction level requirements in Title VII in connection with reporting and dissemination, clearing and trade execution would apply and SB swap dealers ("SBSDs") would be required to comply with certain requirements with respect to their non-U.S. counterparties. We recognize that the SEC intends to cast a broad net regarding the type of transactions that should be subject to Title VII and then to provide limited exceptions from certain requirements in appropriate circumstances. We are concerned, however, that the formulation of the definition is so broad that the test as proposed may capture transactions of non-U.S. clients (including non-U.S. regulated funds) that retain U.S. asset managers to manage their investment portfolios. We believe imposing Dodd-Frank Act requirements should not be based solely on the retention of a U.S. asset manager. Such a result would be inconsistent with the expectations of investors in non-U.S. regulated funds and is unnecessary to protect U.S. markets or U.S. investors. With respect to an SB swap transaction that is "conducted within the United States," the SEC's proposed rule would not apply the mandatory clearing and trade execution requirements if (1) neither counterparty to the transaction is a U.S. person; (2) neither counterparty's performance under the SB swap is guaranteed by a U.S. person; and (3) neither counterparty to the transaction is a foreign registered SB swap dealer.20 As noted by the SEC, transactions between "two non-U.S. persons whose performance under a security-based swap are not guaranteed by a U.S. person do not pose the same risk to the U.S. financial system that is posed by transactions with U.S. person counterparties or transactions in which a U.S. person provides a guarantee."21 Moreover, the SEC recognizes that because the "financial risks of the transaction would reside with non-U.S. persons outside the United States," it is not necessary to apply the clearing and trade execution requirements. We agree with the policy rationale for these exceptions, which is equally true where one of the non-U.S. persons uses the services of an asset manager in the United States. We do not believe that transactions between two non-U.S. counterparties (for which a U.S. asset manager is managing the portfolio of one of the counterparties) should be subject to Title VII of 20 Under the SEC's proposed approach, these transaction-level requirements generally would not apply to transactions conducted outside the United States between, among others: (1) a foreign branch of a U.S. bank and an unregistered non- U.S. person that does not receive a guarantee from a U.S. person on its performance of its SB swap obligations; and (2) a non-U.S. person that is a registered SB swap dealer and a non-U.S. person that does not

receive a guarantee from a U.S. person on its performance of its SB swap obligations. 21 Proposal, *supra* note 3, at 31080. ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 9 of 14 the Dodd-Frank Act for several reasons. As an initial matter, the risk borne in these transactions would reside with non-U.S. persons outside the United States. The non-U.S. regulated funds (as we recommend to be defined above) would bear any risks associated with their derivatives transactions rather than the U.S. asset manager and the “risks of the transactions” would not migrate to the United States merely because of the use of a U.S. asset manager. Each fund is a separate pool of securities with its own assets, liabilities, and shareholders. A U.S. asset manager of a non-U.S. fund in the course of managing the portfolio of investments may be involved in assisting the non-U.S. fund in a derivatives transaction, but the asset manager would not be the counterparty to the transaction, nor would it guarantee the performance of the transaction. A non-U.S. regulated fund would not have any expectation of having its derivatives transactions with other non-U.S. counterparties subject to Title VII, nor would shareholders of that fund expect to receive the protections of U.S. regulation solely based on the engagement of a U.S. asset manager. Moreover, non-U.S. counterparties of a non-U.S. regulated fund would not expect to be subject to Title VII requirements merely because their counterparty was managed by a U.S. asset manager. Excluding these transactions from the Title VII requirements, therefore, would not reduce counterparty protection or reduce protection for the U.S. markets. Finally, imposing Title VII obligations on non-U.S. counterparties solely because of the engagement of a U.S. asset manager would disadvantage the U.S. asset management industry without furthering the SEC’s policy objectives. If the SEC does not provide an exception, U.S. asset managers to non-U.S. regulated funds would find themselves at a significant disadvantage to their non-U.S. counterparts, resulting in harm to U.S. business and potentially driving such asset management business overseas. Non-U.S. funds would be subject to significant and potentially overlapping derivatives regulations as a result of having an asset manager that is located in the United States. To avoid unnecessary costs and burdens, U.S. asset managers may be terminated from their engagements because their non-U.S. regulated fund clients prefer not to be disadvantaged vis-à-vis other non-U.S. regulated funds that do not retain a U.S. asset manager. Furthermore, non-U.S. entities may seek to avoid engaging in transactions with non-U.S. regulated funds deemed to be U.S. persons solely as a result of the engagement of a U.S. asset manager to eliminate the need to comply with certain requirements of the Dodd-Frank Act and SEC regulations. These disincentives would discourage a non-U.S. regulated fund from selecting a U.S. asset manager, even if the U.S. asset manager may have the best expertise to manage the fund. Such a result would be harmful to the fund, its investors, and the U.S. asset management industry.²² All U.S. asset managers advising non-U.S. funds may lose that portion of their business or be forced to move their business offshore. ²² If the Proposal were adopted without modification, these consequences would, therefore, likely result in significant costs and burdens to non-U.S. regulated funds and the U.S. asset management industry. ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 10 of 14 We, therefore, request that the SEC expand the exceptions proposed for clearing and trade execution requirements in several ways.²³ First, the SEC should extend the exception to all of the transactional requirements and exclude transactions between non-U.S. counterparties from the reporting and public dissemination requirements even if those transactions technically are conducted within the United States. In the Proposal, the SEC determined to delete the use of the phrase “through any means of interstate commerce” because the language could “unduly require a security-based swap to be reported if it had only the slightest connection with the United States.”²⁴ The new trigger – “conducted within the United States” – continues to be quite broad and would impose the regulatory reporting and public dissemination requirements on non-U.S.

counterparties even if the only connection to the United States is the retention of a U.S. asset manager.²⁵ We do not believe using the expertise of a U.S. asset manager alone should cause transactions between non-U.S. person funds to be subject to regulatory reporting or public dissemination. Where neither of the non-U.S. counterparties is an SBSD or MSBSP, a non-U.S. dealer counterparty to a non-U.S. regulated fund would not have the obligation to report even though the dealer would have a greater capacity to fulfill that responsibility. Non-U.S. regulated funds are unlikely to have the infrastructure in place to serve as the reporting party, and we are concerned that non-U.S. regulated funds may not have the economic leverage to require their non-U.S. dealers to report. Therefore, non-U.S. regulated funds using the services of a U.S. asset manager would have to incur considerable expense either to develop a reporting system or to contract with an outside vendor to satisfy this obligation. Either option could impose significant costs on these funds and their shareholders. Second, we urge the SEC not to impose the transaction-level requirements on non-U.S. registered SBSDs when transacting with non-U.S. regulated funds that are managed by U.S. asset managers. Transaction-level requirements primarily focus on protecting counterparties by imposing certain obligations on SBSDs (both U.S. and non-U.S. SBSDs), including standards of business conduct and segregation of customer funds. For the reasons discussed above, we do not believe it is necessary to extend these protections to non-U.S. regulated funds that are managed by U.S. asset managers. ²³ For the reasons articulated above, the SEC should eliminate the last condition proposed for the clearing and trade execution exception – “neither counterparty to the transaction is a foreign registered SB swap dealer.” Removing this condition would permit all transactions conducted by a non-U.S. registered SBSD with non-U.S. persons to be treated in the same manner. ²⁴ Proposal, *supra* note 3, at 31061. ²⁵ The SEC does not articulate in the Proposal a specific rationale for subjecting transactions “conducted in the United States” by two non-U.S. persons to regulatory reporting. For public dissemination, the SEC states that it intends to preserve the principle from the original proposal that an SB swap would be subject to public dissemination if it were “executed in the United States.” The new trigger covers, however, significantly more activities related to a derivatives transaction than execution and could include routine activities of an asset manager in managing the portfolio of its non-U.S. clients. ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 11 of 14 In the Proposal, the SEC preliminarily determined not to impose most of the external business conduct standards with respect to the “foreign business”²⁶ of a non-U.S. registered SBSD because: (1) “these requirements relate primarily to customer protection;” (2) the “Dodd-Frank Act’s counterparty protection mandate focuses on the United States and the U.S. markets;” and (3) “foreign counterparties typically would not expect to receive the customer protections of Title VII when dealing with a foreign security-based swap dealer outside the United States.”²⁷ We agree, but also believe that non-U.S. regulated funds would not expect to receive the protections of Title VII’s business conduct standards merely because they hire a U.S. asset manager.²⁸ The protections of Title VII for a non-U.S. counterparty of an SBSD should not depend on whether that non-U.S. counterparty retains the services of a U.S. asset manager. Moreover, we believe these requirements would disadvantage non-U.S. regulated funds and their U.S. asset managers because non-U.S. SBSDs may prefer to transact with non-U.S. funds managed by non-U.S. asset managers to avoid the imposition of these requirements. Substituted Compliance Framework Should Accommodate Different Regulatory Standards The SEC proposes a “substituted compliance” framework under which it would consider written applications to permit compliance with requirements in a foreign regulatory system to substitute for compliance with certain requirements of Title VII relating to SB swaps, provided that the corresponding requirements in the foreign regulatory system are comparable to the relevant provisions of the Securities Exchange Act of 1934. Under the Proposal, the SEC

would make a determination that a foreign jurisdiction has comparable requirements pursuant to the proposed procedures for considering applications for substituted compliance determinations. We applaud the SEC for proposing to make the substituted compliance determinations based on whether the foreign jurisdiction's requirements achieve regulatory outcomes comparable to those of Title VII in four major categories of requirements rather than based on a rule-by-rule comparison. We have several suggestions on the SEC's proposed approach. First, we request that foreign regulatory authorities be permitted to submit an application for substituted compliance for entities that would be subject to their regulations. We believe foreign regulators would have the most complete information about their framework and should not be precluded from seeking a substituted compliance determination directly from the SEC. 26 The SEC proposes to define "foreign business" as SB swap transactions entered into, or offered to be entered into, by or on behalf of a non-U.S. SBSB that do not include its "U.S. Business." The proposed rule would define "U.S. Business" for a non-U.S. SBSB as (i) any transaction entered into, or offered to be entered into, by or on behalf of such foreign SB swap dealer, with a U.S. person (other than with a foreign branch), or (ii) any transaction conducted within the United States. 27 Proposal, *supra* note 3, at 31017. 28 We request that the SEC revise the Proposal to eliminate the second prong of the definition of "U.S. Business" for foreign SBSBs - "(ii) any transaction conducted within the United States." ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 12 of 14 We also request that the SEC be mindful that the approach set forth by the SEC in making these determinations must be workable in the near future as well as in the longer term when G-20 countries have fulfilled their regulatory reform obligations. Regulators around the world are at different points of implementation of derivatives regulation,²⁹ but the extraterritorial approach adopted by the SEC must consider the fact that other jurisdictions at some point will fully implement their reforms. In this regard, although we agree in principle that certain conditions should be satisfied before the SEC can make such a determination, the SEC should not deny substituted compliance applications merely if the foreign regulatory regime differs technically from those requirements in the United States. Therefore, we urge the SEC not to apply its substituted compliance framework in an overly mechanical manner that could effectively preclude a substituted compliance determination with respect to a similar foreign regime. For example, one of the proposed conditions provides that the rules of a foreign jurisdiction must require the SB swap to be reported and publicly disseminated in a manner and timeframe comparable to those required by the SEC. Applied too strictly, technical differences in the timeframes for, or manner of, reporting could disqualify a foreign jurisdiction.³⁰ We encourage the SEC to look holistically at the foreign regulatory authority regulatory framework for reporting to determine whether it broadly achieves the G-20 goals of transparency of the derivatives markets. Moreover, the SEC's substituted compliance process should not pre-judge the determination before all the regulatory reform efforts have been fully adopted by international regulators. Specifically, the SEC has not proposed detailed rules for substituted compliance with respect to the clearing requirement because the SEC does "not expect a large number of requests for substituted compliance in this area due to the small number of security-based swap clearing agencies in the market."³¹ Although we acknowledge that there may only be a few SB swap clearing agencies at this time, clearing is an area in which counterparties could not practically comply with two sets of requirements and a workable solution must be developed to address these difficult issues. For example, how would a swap be cleared in a situation where both the SEC's as well as foreign regulator's rules require that the swap be cleared or in a situation where the U.S. central counterparty is not recognized by the foreign rules and/or the foreign central counterparty is not recognized by the SEC? Moreover, we do not think it would be possible to clear a transaction twice or to clear separate legs of a swap. We, therefore, urge the SEC

to develop more specific rules for making a substituted compliance determination for mandatory clearing. 29 CFTC and SEC, Joint Report on International Swap Regulation Required by Section 719(c) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Jan. 31, 2012), available at <http://www.sec.gov/news/studies/2012/sec-cftc-intlswapreg.pdf>. 30 It is unclear whether the reporting obligations imposed by the European Market Infrastructure Regulation (“EMIR”) would satisfy the SEC’s proposed condition if applied too strictly. Under EMIR, counterparties must report swap data to a trade repository no later than the next working day following the conclusion, modification, or termination of a contract. 31 Proposal, *supra* note 3, at 31099. ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 13 of 14 Finally, we urge the SEC also to consult closely, and to coordinate, with the CFTC in making its substituted compliance determinations. Inconsistent findings by the SEC and the CFTC with respect to the regulatory framework of a foreign jurisdiction would impose significant costs and burdens on market participants. As discussed above, non-U.S. regulated funds typically trade swaps and SB swaps from the same desk or desks. If economically similar instruments that trade on the same trading desk were subject to different regulatory regimes, non-U.S. regulated funds would face significant additional compliance costs and complexity. Furthermore, for most jurisdictions, swaps and SB swaps are not given separate regulatory treatment. Given that regulations for both the SEC’s SB swap and CFTC’s swap stem from the Dodd-Frank Act, we see no reason the SEC and CFTC should come to different conclusions regarding the comparability of the laws of a foreign jurisdiction. * * * * * We appreciate the significant effort and work undertaken by the SEC to provide a sensible framework for regulating cross-border derivatives transactions. We urge the SEC to modify certain aspects of the Proposal to tailor properly the territorial approach for non-U.S. regulated funds and non- U.S. regulated funds that are managed by U.S. asset managers and to ensure consistency with the outcome under the CFTC’s approach. If you have any questions on our comment letter, please feel free to contact the undersigned or Giles Swan at 011-44-203-009-3103, Sarah Bessin at 202-326-5835 or Jennifer Choi at 202-326-5876. ICI/ICI Global Letter to Ms. Elizabeth M. Murphy August 21, 2013 Page 14 of 14 Sincerely, /s/ Karrie McMillan /s/ Dan Waters Karrie McMillan Dan Waters General Counsel Managing Director Investment Company Institute ICI Global 202-326-5815 011-44-203-009-3101 kmcmillan@ici.org dan.waters@ici.org cc: The Honorable Mary Jo White The Honorable Luis A. Aguilar The Honorable Daniel M. Gallagher The Honorable Kara M. Stein The Honorable Michael S. Piwowar John Ramsay, Acting Director, Division of Trading and Markets, SEC Norm Champ, Director, Division of Investment Management, SEC The Honorable Gary Gensler The Honorable Bart Chilton The Honorable Scott D. O’Malia The Honorable Mark Wetjen Gary Barnett, Director, Division of Swap Dealer and Intermediary Oversight