INVESTMENT ADVISER
ASSOCIATION

August 21, 2013

VIA ELECTRONIC MAIL

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

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, Rel. No. 34-69490; File Nos. S7-02-13; S7-34-10; S7-40-11

Dear Ms. Murphy:

The Investment Adviser Association[1] appreciates the opportunity to comment on the Securities and Exchange Commission's ("Commission" or "SEC") proposed rulemaking under the Securities Exchange Act of 1934, as amended ("Exchange Act") for purposes of determining the application of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") to cross-border activities.[2] We appreciate the SEC initiative to address how Title VII and implementing regulations will apply to security-based swap transactions involving U.S. persons and non-U.S. persons. We recognize the SEC's need to balance the important policy goals of achieving the benefits of the Dodd-Frank Act and of facilitating a well-functioning global security-based swap market by taking into

[1] The Investment Adviser Association ("IAA") is a not-for-profit association that represents the interests of investment adviser firms registered with the SEC. Founded in 1937, the IAA's membership consists of more than 500 firms that collectively manage in excess of $11 trillion for a wide variety of individual and institutional investors, including pension plans, trusts, investment companies, private funds, endowments, foundations, and corporations. For more information, please visit our website: www.investmentadviser.org.

[2] *See 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, Proposed Rule,* SEC Rel. No. 34-69490, 78 Fed. Reg. 30968 (May 23, 2013) ("Proposal"), available at: http://www.gpo.gov/fdsys/pkg/FR-2013-05-23/pdf/2013-10835.pdf. Under the Proposal, "cross-border activities" means the application of Title VII to a security-based swap transaction involving (i) a U.S. person and a non-U.S. person, (ii) two non-U.S. persons where one or both are located within the United States, or (iii) two non-U.S. persons conducting a security-based transaction that otherwise occurs in relevant part within the United States, including by negotiating the terms of the security-based swap transaction within the United States or where performance by one or both counterparties under the security-based swap is guaranteed by a U.S. person. Proposal at 30971-72, n. 3. The SEC is also re-proposing Exchange Act rules 900-911 (Regulation SBSR).

account counterparty protection, transparency, systemic risk, liquidity, efficiency, and competition in the market. We also appreciate the SEC's efforts in its substituted compliance provisions to avoid having market participants subject to conflicting or duplicative compliance obligations between SEC regulation and other global regulation.[3]

Section 772(b) of the Dodd-Frank Act amends Section 30 of the Exchange Act to provide that "[n]o provision of [Title VII] . . . shall apply to any person insofar as such person transacts a business in security-based swaps without the jurisdiction of the United States," unless that business is transacted in contravention of rules prescribed to prevent evasion of Title VII. To implement this provision, the SEC proposes that its Title VII regulations would apply to security-based swaps activity involving U.S. persons or involving a "transaction conducted within the United States." We comment with respect to these two jurisdictional tests.

I. "U.S. Person" Definition and Exemptions

The SEC has proposed in rule 3a71-3(7) that the term U.S. person for purposes of Title VII means: (a) any natural person resident in the United States; (b) 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 (c) any account (whether discretionary or non-discretionary) of a U.S. person.[4] We note the CFTC recently adopted interpretive guidance under the Commodity Exchange Act, as amended ("CEA"), defining the term U.S. person for purposes of cross-border application of swaps regulation under Title VII.[5]

[3] In this regard, we encourage the SEC and the Commodity Futures Trading Commission ("CFTC") to coordinate their determinations with respect to ways in which a foreign financial regulatory system achieves comparable results to Title VII.

[4] The SEC proposed that under an entity-level approach, a foreign branch, agency, or office of a U.S. person would be treated as a U.S. person under the Proposal because the legal obligations and economic risks associated with the transactions directly affect a U.S. person, of which the branch, agency or office is a part. The accounts would be U.S. persons regardless of whether the entity at which the account is held or maintained is a U.S. person. Proposal, *supra* note 2, at 30997.

[5] CFTC, *Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations; Rule*, 78 Fed. Reg. 45292 (July 26, 2013) ("CFTC Guidance"), available at: http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2013-17958a.pdf. For purposes of the treatment of collective investment vehicles or other pooled funds, the CFTC Guidance states that under the application of CEA section 2(i), the CFTC will interpret the term "U.S. person" generally to include, but not be limited to, under prong (iii): any corporation, partnership, limited liability company, business or other trust, association, joint-stock company, fund or any form of enterprise similar to any of the foregoing (other than an entity described in prongs (iv) or (v)) (a "legal entity"), in each case that is organized or incorporated under the laws of a state or other jurisdiction in the United States or having its principal place of business in the United States; or under prong (vi): any commodity pool, pooled account, investment fund, or other collective investment vehicle that is not described in prong (iii) and that is majority-owned by one or more persons described in prong (i), (ii), (iii), (iv), or (v). The CFTC also exempts from the U.S. person definition any commodity pool, pooled

We recognize that the SEC has proposed rules rather than guidance and is taking a somewhat different overall approach than the CFTC. Nevertheless, given that the CFTC's guidance is now final, we request that the SEC modify its proposal in a number of respects to be more consistent with the CFTC's definition of "U.S. person." For example, as discussed more fully below, we urge the SEC to adopt the same exemption from the CFTC's definition of U.S. person for collective investment vehicles that are publicly offered only to non-U.S. persons and not offered to U.S. persons generally. We believe it important that market participants operate under the certainty and clarity that would be provided by a consistent U.S. person definition used by U.S. regulators in applying Title VII. Registered investment advisers and others may not differentiate between security-based swaps and swaps in management of client portfolios to achieve client investment objectives. Further, it would be burdensome and costly to develop separate compliance systems and operations for these two types of instruments for purposes of Title VII.

In addition to our recommendation for consistency with the CFTC approach, we also address below several prongs of the U.S. person definition where the SEC seeks comment in the Proposal.

Principal Place of Business

The SEC seeks comment on whether it should define the term "principal place of business" for purposes of the proposed definition of "U.S. person" and if so, whether it should be defined as the location of the personnel who direct, control, or coordinate the security-based swap activities of the entity. The SEC notes that this focus would be generally consistent with the focus of the definition of "principal office and place of business" in the Investment Advisers Act of 1940 ("Advisers Act"), where it is defined as "the executive office of the investment adviser from which the officers, partners, or managers of the investment adviser direct, control, and coordinate the activities of the investment adviser."[6]

We urge the SEC, if it does adopt a "principal place of business" test, to coordinate with the CFTC in developing a consistent definition. While we have concerns with the CFTC's interpretation of the term principal place of business, particularly with regard to the ambiguities in the definition, we urge the SEC to work with the CFTC to harmonize the two approaches to this aspect of the U.S. person definition between the agencies. Otherwise, it will be overly burdensome to implement two separate definitions.

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account, investment fund, or other collective investment vehicle that is publicly offered only to non-U.S. persons and not offered to U.S. persons. CFTC Guidance at 45316-17.

[6] Proposal, *supra* note 2, at 30999, n. 306 (citing rule 222-1(b) of the Advisers Act).

We also request that the SEC adopt an approach consistent with the CFTC guidance with respect to entities that are not collective investment vehicles but that hire an asset manager in the United States. Thus, the SEC should confirm, as is provided by the CFTC, that a non-U.S. individual, institution, pension plan or operating company that is not otherwise within any prong of the U.S. person definition will not come within the definition of "U.S. person" solely because it retains an asset management firm located in the United States to manage its assets or provide other financial services.[7]

Ownership

The SEC seeks comment on whether an account of one U.S. person and one or more non-U.S. persons should be treated as a U.S. person, or whether the SEC should instead establish a *de minimis* threshold amount or otherwise allows some U.S. person ownership without triggering U.S. person status for the account. As an initial matter, we do not believe that the SEC definition of "U.S. person" should focus on ownership (direct or indirect) because such a definition would capture non-U.S. funds that are not created for the purpose of pooling U.S. assets and would include non-U.S. entities with little nexus to the U.S. or the U.S. security-based swap market or impact upon U.S. commerce or the U.S. financial system.[8] An ownership test would focus on the activities of investors rather than the purposeful activities of the fund. A non-U.S. fund may have U.S. investors without engaging in marketing or offering to U.S. persons. Indeed, non-U.S. funds may not be aware that there are U.S. investors in their funds.

Many types of collective investment vehicles face ownership verification obstacles. Many non-U.S. funds do not know their direct or indirect owners because such interests may be purchased through an intermediary or may be held in omnibus accounts. If fund shares are held through an intermediary or in an omnibus account, the intermediary or omnibus account holder may or may not be willing or able to provide representations regarding the status of the ultimate beneficial owners. Such third parties may also face additional layers that they would have to look through. Similarly, it would be very difficult to determine ultimate "indirect" ownership in a number of fund structures (*e.g.*, fund of funds). Further, ownership in a non-U.S. fund alone does not necessarily indicate that the non-U.S. fund is within the jurisdiction of the United States under Section 30(c) of the Exchange Act.

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[7] *See* CFTC Guidance, *supra* note 5, at 45311-12.

[8] We had also requested the CFTC not include a majority-ownership prong in its U.S. person definition during the CFTC proposal's comment period. *See IAA Comment Letter to CFTC re: Further Proposed Guidance Regarding Compliance with Certain Swap Regulations (Cross Border)* (Feb. 6, 2013), available on the IAA website. The CFTC did not adopt the IAA's comment but made other changes that somewhat mitigated the broad reach of the provision.

If, however, the SEC determines to include an ownership test, we encourage the SEC to apply the same ownership test as adopted by the CFTC to avoid the burden of applying different ownership tests. In particular, the CFTC Guidance states that a collective investment vehicle that is majority-owned by one or more U.S. persons would be deemed a U.S. person.[9] Under the CFTC Guidance, majority ownership is determined by beneficial ownership of more than 50 percent of the equity or voting interests in the vehicle. However, if the vehicle is owned in part by an unrelated investor collective investment vehicle, the vehicle need not "look through" the unrelated investor entity, but may reasonably rely upon written, bona fide representations from the unrelated investor entity regarding whether it is a U.S. person, unless the vehicle has reason to believe otherwise. The SEC's provision, if any, should be consistent with and no more restrictive than the CFTC's provision.

Exemption for Investment Funds that are Publicly Offered to Non-U.S. Persons Only

We urge the SEC to adopt the same exemption from the definition of U.S. person for certain collective investment vehicles that was adopted by the CFTC. Specifically, the CFTC stated in its Guidance that, "[i]n addition, 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.'"[10] In particular, investment funds that are publicly offered and not offered to U.S. persons should be able to rely on the same definition and exemption to address the concerns regarding obtaining ownership verification. As discussed, a non-U.S. collective investment fund may not be able to determine its ownership because (i) its interests are held at an omnibus level by other financial intermediaries that cannot or will not provide ownership information to the fund, or (ii) its interests are traded on an exchange and ownership changes for the shares of such funds on a regular basis without the knowledge of the fund. Further, this exception more accurately reflects the types of non-U.S. funds that have little to no nexus to the United States or the U.S. security-based swaps market. Moreover, an adviser's non-U.S. client would have no reasonable expectation that U.S. law would govern its transaction in these situations, and such transactions would not present systemic risk concerns to the United States.

II. "Transaction Conducted Within the United States" Test

Under the Proposal, provisions of Title VII would also be applicable to any "transaction conducted within the United States."[11] Proposed rule 3a71-3(5)(i) defines

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[9] *See* CFTC Guidance, *supra* note 5, at 45313.

[10] CFTC Guidance, *supra* note 5, at 45314.

[11] *See, e.g.*, SEC proposed rule 3a71-3(a)(7) and proposed Regulation SBSR rule 908 (reporting is required for a security-based swap if: (i) the security-based swap is a transaction conducted within the United States; (ii) there is a direct or indirect counterparty that is a U.S. person on either side of the transaction; or (iii) there is a direct or indirect counterparty that is a security-based swap dealer or major security-based swap participant on either side of the transaction). We recommend that the SEC reconsider including the term "indirect" counterparty in this

"transaction conducted within the United States" as any security-based 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."[12] The SEC preliminarily believes that when a non-U.S. person engages in dealing activity with another non-U.S. person from within the United States either through an agent, branch, or office, or otherwise engages in security-based swap dealing activity within the United States (such as by soliciting persons within the United States from outside the United States), the solicitation, negotiation, or execution activity that occurs within the United States constitutes dealing activity that is described by the security-based swap dealer definition.[13] The SEC seeks comment as to whether the proposed approach toward determining whether dealing activity is conducted within the United States is appropriate and if it identifies appropriate factors in determining whether a transaction has been conducted within the United States.

We believe the proposed definition is too broad and may capture unnecessary parties beyond those that engage in transactions with a substantive nexus to the U.S. For example, we do not believe the provisions of Title VII should apply where a non-U.S. counterparty retains an investment adviser in the United States to manage its assets, and no other "transaction" triggers the appropriate nexus with the United States. For example, a U.S. investment adviser assisting a non-U.S. client entering into a security-based swap transaction with a non-U.S. counterparty should not trigger Title VII jurisdiction.[14] If the purposes of Title VII, as stated in the Proposal, require that its provisions apply to the person who actually bears the risk arising from the security-based swap transaction, then applying Title VII to non-U.S. persons who rely on the expertise of an agent such as an investment adviser in the United States does not satisfy the stated purpose. While the investment adviser may, pursuant to an investment management agreement, determine whether a non-US client or fund should enter into a transaction, it does not guarantee, itself enter into, or otherwise become subject to the risk of the non-U.S. counterparty client's security-based swap transaction. Accordingly, the SEC should exclude from the scope of this provision the activities of an investment adviser in

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proposed rule. Market participants may face significant challenges in determining the definition and the identity of an "indirect" counterparty in many circumstances. Instead, an anti-evasion provision could alleviate the SEC's concern that market participants may seek to avoid certain requirements.

[12] *See* Proposal, *supra* note 2, at 31061.

[13] The SEC does not propose to include submitting a transaction for clearing in the United States or reporting a transaction to an SDR in the United States as an activity that would cause a transaction to be conducted in the United States, nor does it propose to treat activities related to collateral management (*e.g.*, exchange of margin payments) that may occur in the United States or involve U.S. banks or custodians as activity conducted within the United States for these purposes. Proposal, *supra* note 2, at 31000.

[14] Other U.S. agents may be impacted by the SEC's approach as well, such as lawyers, accountants, or other service providers to non-U.S. counterparties that are engaged in transactions that do not otherwise trigger the appropriate nexus with the United States.

the United States managing assets, including security-based swaps, for its non-U.S. person clients when transacting with non-U.S. counterparties.

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We appreciate the opportunity to comment on the SEC's Proposal under Title VII of the Dodd-Frank Act addressing cross-border application of security-based swaps regulation, and we appreciate the SEC's consideration of our comments. Please do not hesitate to contact the undersigned or Karen Barr, IAA General Counsel, at (202) 293-4222 if we may provide any additional information about our comments.

Respectfully submitted,

/s/ Monique S. Botkin
IAA Associate General Counsel

cc: The Honorable Mary Jo White, Chair
The Honorable Luis A. Aguilar, Commissioner
The Honorable Daniel M. Gallagher, Commissioner
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner

Mr. John Ramsay, Acting Director, Division of Trading and Markets, SEC
Mr. Norm Champ, Director, Division of Investment Management, SEC
Mr. Gary Barnett, Director, Division of Swap Dealer and Intermediary Oversight, CFTC