CITADEL

August 21, 2013

Via Electronic Submission: http://www.sec.gov/rules/proposed.shtml

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

Re: Proposed Rules and Interpretive Guidance on Cross-Border Security-Based Swap Activities (Release No. 34–69490, File No. S7-02-13)

Dear Ms. Murphy:

Citadel LLC[1] ("Citadel") appreciates this opportunity to provide comments to the Securities and Exchange Commission (the "Commission") in response to the proposed rules and interpretive guidance on cross-border security-based swap activities (the "Proposal").[2]

We are unwavering in our conviction that Title VII's clearing and reporting requirements will mitigate systemic risk, increase transparency, promote competition, and otherwise improve the safety, stability and integrity of the security-based swap ("SBS") market, and the marketplace as a whole. A material percentage of SBS market activity is conducted by funds that are organized or incorporated outside of the U.S., but which have a U.S. nexus.[3] We therefore agree with the Commission's proposed application of the transaction-level requirements, including clearing and reporting, to SBS entered into by offshore funds that have a U.S. nexus. Failure to do so would undermine central objectives of the Dodd-Frank Act, create opportunities for regulatory arbitrage, and risk fragmenting the SBS market.

The Dodd-Frank Act states that its provisions applicable to SBS, as well as subsequent rulemaking, do not apply to "any person insofar as such person transacts a business in security-based swaps without the jurisdiction of the United States."[4] In our view, the SBS activity of the U.S. hedge fund industry is clearly not done *without* the jurisdiction of the U.S., notwithstanding the offshore domicile of certain funds. Thus, for the purposes of ensuring the effective application of Title VII in the cross-border context, the Commission has correctly proposed two

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[1] Established in 1990, Citadel is a leading global financial institution that provides asset management and capital markets services. With over 1,100 employees globally, Citadel serves a diversified client base through its offices in the world's major financial centers including Chicago, New York, London, Hong Kong, San Francisco and Boston.

[2] 78 Fed. Reg. 30968-31281 (May 23, 2013).

[3] Including, for example, those offshore funds that have their *principal place of business* in the U.S. or conduct their transactions within the U.S.

[4] Dodd-Frank Act, Sec. 772(b).

complementary approaches that together will ensure that the SBS activity of offshore funds with a U.S. nexus is appropriately subject to the transaction-level requirements:

- The *principal place of business* test within the U.S. person definition, and
- The definition of *transaction conducted within the United States*.

Background

The U.S. hedge fund industry typically employs master-feeder structures, in which trading and investment activity is conducted in an offshore master fund, at the direction of a U.S.-based investment manager, while the investors in the master fund are a combination of onshore feeder funds (which pool investments from U.S. investors) and offshore feeder funds (which pool investments from foreign and U.S. tax-exempt investors). Given such an arrangement, solely looking at the domicile or place of incorporation of the master fund – which is the legal counterparty to any SBS activity – would overlook where the trading activity is taking place and ignore the otherwise relevant connections to the U.S. Consequently, it is essential that the Commission adopt an approach that reflects market realities and ensures that SBS activity conducted by offshore funds with a U.S. nexus will be subject to the clearing, reporting, and other transaction-level requirements.

Principal Place of Business Test within the U.S. Person Definition

We believe that the Commission has correctly proposed (a) to incorporate a *principal place of business* test in the U.S. person definition, and (b) to apply the transaction-level requirements to SBS transactions where either counterparty is a U.S. person. This approach ensures that offshore funds managed by a U.S.-based investment manager are deemed to be U.S. persons, and are thereby required to clear and report their SBS transactions.

In the Proposal, the Commission sought input on if and how it should define the term *principal place of business*.[5] We urge the Commission to provide further clarity. We support the Commission's suggestion to define "principal place of business as the location of the personnel who direct, control, or coordinate the security-based swap activities of the entity."[6] In addition, we believe it would be useful in the final adopting release for the Commission to provide further guidance as to how its *principal place of business* test applies to collective investment vehicles, to parallel the CFTC's guidance in this regard.[7] The CFTC indicated it would consider, among others, the principal location of the "the senior personnel who implement the investment and trading strategy" and "those responsible for investment selections, risk management decisions, portfolio management, or trade execution."[8]

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[5] Proposal at 30999: "Should the Commission define the term ''principal place of business'' for purposes of the proposed definition of ''U.S. person''? If so, should the Commission define ''principal place of business'' as the location of the personnel who direct, control, or coordinate the security-based swap activities of the entity? If no, how should the Commission define it?"

[6] *Ibid.*

[7] 78 Fed. Reg. 45292-45374 (July 26, 2013). See specifically the discussion of the application of the principal place of business test to collective investment vehicles at 45309-45312.

[8] *Ibid.*, at 45310.

We also caution against any changes to the U.S. person definition that would result in offshore funds with a U.S. nexus falling outside the definition. For example, reliance on the Regulation S definition of U.S. person would not capture such offshore funds. We thus applaud the Commission's recognition that "adopting the definition of U.S. person in Regulation S without significant modifications would not achieve the goals of Title VII" since "Regulation S addresses specific policy concerns that are different from those addressed by Title VII."[9] The Commission is correct to conclude that "[i]n light of the specific objectives of Title VII … that a definition of U.S. person specifically tailored to the regulatory objectives it is meant to serve … is appropriate."[10]

Transaction Conducted Within the United States

We also believe that the Commission has correctly proposed (a) to define *transaction conducted within the United States* as any "security-based swap transaction that is solicited, negotiated, executed, or booked within the United States … regardless of the location, domicile, or residence status of either counterparty to the transaction"[11] and (b) to apply the transaction-level requirements to such transactions. Together, these provisions represent an additional important approach to ensuring that the SBS activity of offshore funds managed by U.S.-based investment managers is subject to the Commission's clearing and reporting requirements.

Conclusion

The *principal place of business* test within the U.S. person definition and the definition of *transaction conducted within the United States* should be included in the final rules in substantially the same form as proposed. They each embody an accurate recognition of actual market practices and represent a practical approach to identifying those market participants who are engaged in U.S. SBS market activity, and therefore, are both appropriate determinants of when the transaction-level requirements should apply in the cross-border context. Ensuring that SBS market activity conducted by offshore funds with a U.S. nexus is subject to clearing, reporting, and other transaction-level requirements is fundamental to achieving the goals of Title VII of the Dodd-Frank Act, as well as to meeting the commitments of the G-20 nations to reform the OTC derivatives markets.

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We appreciate the opportunity to provide comments on the Commission's proposed rule and interpretive guidance. Please feel free to call the undersigned at (312) 395-3100 with any questions regarding these comments.

Respectfully,

/s/ Adam C. Cooper

Senior Managing Director and Chief Legal Officer

[9] Proposal at 31007.

[10] *Ibid.*, at 31008.

[11] *Ibid.,* at 30999.