MANAGED FUNDS ASSOCIATION
The Voice of the Global Alternative Investment Industry
WASHINGTON, DC | NEW YORK

April 30, 2013

**Via Electronic Mail:** cftcreauthorization@ag.senate.gov

The Hon. Debbie Stabenow
Chairwoman
Committee on Agriculture, Nutrition and Forestry
U.S. Senate
Washington, DC 20510-6000

The Hon. Thad Cochran
Ranking Member
Committee on Agriculture, Nutrition and Forestry
U.S. Senate
Washington, DC 20510-6000

**Re: Reauthorization of the Commodity Futures Trading Commission**

Dear Chairwoman Stabenow and Ranking Member Cochran:

Managed Funds Association ("**MFA**")[1] acknowledges the receipt of your letter[2] and appreciates the opportunity to provide the U.S. Senate Committee on Agriculture, Nutrition and Forestry (the "**Committee**") with recommendations related to reauthorization of the Commodity Futures Trading Commission ("**CFTC**") to regulate futures, swaps, and options markets pursuant to the Commodity Exchange Act ("**CEA**"). Our members, as investors and market participants in the derivatives markets, have a strong interest in ensuring that the CEA provides a modern regulatory framework to protect customers and foster economic growth. Accordingly, we respectfully submit a number of recommendations, which we believe will strengthen the CEA, and thereby, the markets and financial stability.

[1] Managed Funds Association represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, the Americas, Australia and many other regions where MFA members are market participants.

[2] Letter from Debbie Stabenow, Chairwoman and Thad Cochran, Ranking Member, Committee on Agriculture, Nutrition, and Forestry, United States Senate, to Richard Baker, President and Chief Executive Officer, MFA, March 7, 2013.

## I. Dodd-Frank Act-like Protections for Sensitive or Proprietary Information

### A. Reports of Commodity Pool Operators and Commodity Trading Advisors

MFA believes that Congress should strengthen the confidentiality protections for proprietary data in possession of the CFTC. MFA consistently has supported reasonable reporting requirements to ensure that regulators have meaningful data upon which to make policy decisions. Strong confidentiality protections help foster an atmosphere of trust to ensure that reporting entities are as forthcoming as possible. As you know, market participants—whether hedgers or investors—invest significant research, time and resources into developing proprietary hedging or investment strategies. Such trading strategies are trade secrets; the CEA and other statutes have recognized the legitimate commercial need to protect the confidentiality of such secrets.[3] The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "**Dodd-Frank Act**") in providing regulators with new authorities to collect sensitive and proprietary data also included important provisions to ensure that the confidentiality of such information was fully protected.

MFA believes that the confidentiality protections under section 8 of the CEA should be further enhanced to be consistent with these important protections in the Dodd-Frank Act.

The Dodd-Frank Act created the Financial Stability Oversight Council ("**FSOC**"), requiring the members of FSOC, including the CFTC, to collect sensitive and confidential data for the purpose of assessing financial stability. The Dodd-Frank Act included important provisions directing FSOC members to maintain the confidentiality of such data.[4] Specifically, the Dodd-Frank Act amended the Investment Advisers Act of 1940 ("**Advisers Act**")[5] to protect the confidentiality of reports that the Securities and Exchange Commission ("**SEC**") requires for SEC-registered investment advisers. We believe that Congress should make similar Dodd-Frank Act amendments to the CEA for CFTC reports. Such amendments would be appropriate and helpful to ensure that consistent confidentiality protections would extend to the reports, documents, records and information of commodity pool operators ("**CPOs**") and commodity trading advisors ("**CTAs**"). This is particularly important given that the CFTC requires both CPOs and CTAs to file reports that include sensitive and proprietary information.

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[3] *See* Section 8(a)(1) of the CEA (providing that in connection with investigations that the CFTC "may not publish data and information that would separately disclose the business transactions or market positions of any person and trade secrets or names of customers). *See e.g.*, Freedom of Information Act, 5 USC §552 (b)(4) (exception for "trade secrets and commercial or financial information obtained from a person and privileged or confidential….").

[4] Section 112(b)(5)(A) of the Dodd-Frank Act.

[5] *See* Section 112(b)(5) of the Dodd-Frank Act; and Section 204(b) of the Advisers Act. The amendments to the Advisers Act, among others, provide that: (1) the SEC may not be compelled to disclose any report or information, except that it may not withhold information from Congress, upon an agreement of confidentiality; (2) any department, agency, or self-regulatory organization that receives reports or information from the SEC shall maintain the confidentiality of such materials in a manner consistent with the level of confidentiality established for the SEC by statute; and (3) with respect to any adviser report or materials required to be filed with the SEC, the SEC and any other regulatory entity that receives such report or materials shall be exempt from section 552 of title 5.

The current inconsistency creates two potential difficulties. First, it may expose data from CFTC-regulated entities to greater risk of public disclosure. Second, it creates a potential unlevel regulatory playing field, disadvantaging the CFTC in its efforts to collect, analyze, and share data.[6] To afford confidential information consistent treatment for CPOs and CTAs as well as investment advisers, we recommend that the Committee consider amending the CEA by extending these important Dodd-Frank Act protections for sensitive or proprietary information to CPOs and CTAs.

### B. Additional Protections

In addition to the above statutory protections for sensitive or proprietary information, we believe the CFTC also needs to enhance its policies and controls with respect to the use of non-public data and internal controls. For example, we are alarmed at reports that academics have had access to, and have used confidential trading data and trading messages from, the CFTC to reverse engineer trading strategies and to have published their findings in academic journals.[7] We commend CFTC Chairman Gary Gensler for requesting that the CFTC Inspector General investigate this matter.[8] Section 8(a)(1) of the CEA in connection with investigations, as well as Section 552 of the Freedom of Information Act, prohibit disclosure of business transactions/commercial information and trade secrets regardless of whether it is in connection with the identity of the market participant.[9] We believe this disclosure is a fundamental violation of confidentiality and urge the Committee to review the CFTC Inspector General's findings and the steps the CFTC agrees to take to enhance its policies and controls with respect to non-public information.

We also believe that Congress should amend the CEA to strengthen the confidentiality requirements for swap data repositories ("**SDRs**") to protect both the identity of traders and the nature of their trading activities. In particular, our concerns with confidentiality protections extend to swap transaction data that market participants are reporting to SDRs under the CFTC's data reporting rules. Under the CFTC's final SDR rules,[10] an SDR must protect the confidentiality of reported swap data and may not disclose it to market participants. The final SDR rules provide an exception to this prohibited access rule, allowing a party to a particular swap to have access to "data and information" related to such swap. The final SDR rules do not define the broad phrase "data and information". For swaps that are traded anonymously on designated contract markets ("**DCMs**") and swap execution facilities ("**SEFs**") and then cleared

[6] For example, we note that the SEC and CFTC have jointly adopted Form PF for certain reporting obligations. A dually registered entity filing Form PF with the SEC would have greater confidentiality protection than if the entity filed the exact same report with the CFTC.

[7] *See e.g., Academic Use of CFTC's Private Derivatives Data Investigated,* Bloomberg, Mar. 7 2013 available at*:* http://www.bloomberg.com/news/2013-03-06/academic-use-of-cftc-s-private-derivatives-data-investigated-1-.html; and Exploratory Trading, Adam D. Clark-Joseph, January 13, 2013.

[8] *Id.*

[9] *See supra* n. 3.

[10] CFTC Final Rule on "Swap Data Repositories: Registration Standards, Duties and Core Principles", 76 Fed. Reg. 54538 (Sept. 1, 2011), available at: http://www.gpo.gov/fdsys/pkg/FR-2011-09-01/pdf/2011-20817.pdf.

in accordance with the CFTC's straight-through processing ("**STP**") requirements,[11] the derivatives clearing organization ("**DCO**") or DCM/SEF must report the swap transaction data and information to the SDR, which includes the legal entity identifiers ("**LEIs**") or the "CFTC Interim Compliant Identifiers" ("**CICIs**") of the original counterparties. If an original counterparty has the LEI or CICI of the other original counterparty from the SDR, such original counterparty can also determine its counterparty's identity by accessing DTCC's CICI database utility. This determination, in turn, could allow an original counterparty to a cleared swap to obtain transaction-level data about its original executing party's trades. Such disclosure should be prevented, because it could reveal proprietary information, could be used to introduce non-competitive distortions into the marketplace, and, in particular, could be damaging to the evolution of anonymous trading on DCMs and SEFs. Accordingly, we raised our concerns with Staff in the CFTC's Division of Market Oversight, noting that the loss of counterparty anonymity for cleared swaps is an unintended outcome of the broad reference to "data and information" in the final SDR rules. We have asked CFTC staff to issue formal guidance to clarify that SDR "data and information" that may be accessed by a party to any cleared swap should never include the LEI of its original executing counterparty or that counterparty's clearing member, or any other information that would identify these entities.

We have also become aware of other instances in which the confidentiality of trade data at SDRs has been compromised. We understand that as a result of the failure of confidentiality protections, competitors and other market participants may have had access to, and traded upon the basis of, confidential information. The potential for confidential swap data leakage is heightened when SDRs face inevitable technology malfunctions and internal control deficiencies. In addition to SDR data disclosure risks, we believe the sheer volume of data that the CFTC must begin digesting and analyzing from SDRs presents an opportunity for unprecedented regulatory transparency into the derivatives markets, but also another source of disclosure risk of market participants' LEIs and proprietary trading data if data confidentiality and integrity are not rigorously protected by the CFTC's policies, procedures and internal controls.

Accordingly, we believe the Committee should consider amending the CEA to clarify an SDR's obligations to maintain the confidentiality and integrity of swap trade data and the consequences of failures to perform this obligation. MFA believes that both the CFTC and industry market utilities, such as SDRs, DCOs, DCMs and SEFs, must provide appropriate safeguards to ensure the confidentiality of sensitive market secrets, particularly under circumstances in which regulations require market participants to furnish such data to regulators, SDRs, DCOs, DCMs and SEFs.

## II. Protection of Customer Collateral

MFA supports efforts to strengthen the legal framework for customers of futures commission merchants ("**FCMs**") and believes that Congress should amend the Bankruptcy

[11] *See* CFTC Final Rules on "Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management", 77 Fed. Reg. 21307 (April 9, 2012), available at: http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-7477a.pdf.

Code to bolster such protection. MFA appreciates that Congress remains vigilant about protection of investors and has held numerous hearings related to the MF Global, Inc. ("**MF Global**") and Peregrine Financial Group, Inc. ("**Peregrine**") insolvencies.[12] Our members are fiduciaries to their investors and are customers themselves. As a result, we were very troubled by the MF Global and Peregrine events because the misuse or misplacement of customer funds in those situations resulted in customers experiencing a delay in the return or loss of substantial amounts of their assets.[13] Accordingly we support thoughtful legislative and regulatory changes to strengthen protections of FCMs' customers.

As the Committee knows, counterparties to swaps transaction must post collateral to ensure performance of the contract.[14] The protection of such collateral is one essential element to preserving the financial integrity of the markets.

Under current law, if an FCM becomes insolvent, it is possible a court might conclude that the customers' collateral is subject to the claims of all the FCM's customers on a *pro rata* basis (*i.e.*, non-defaulting customers would share equally in any shortfall). MFA believes that such treatment defeats the very purpose of collateral, *i.e.*, to provide assurance as to the integrity and performance of individual contracts. To remedy this concern, we urge Congress to amend Chapter 7 of the Bankruptcy Code so that customer assets posted as collateral on cleared derivatives transactions are not considered "customer property"[15] subject to *pro rata* distribution upon an FCM's insolvency. Such an amendment would ensure that a customer receives prompt return of all of its assets upon such insolvency, rather than sharing in any shortfall due to the FCM's or another customer's default.

An amendment to the Bankruptcy Code would also enhance the effectiveness of existing and potential customer segregation protections. For example, the CFTC has adopted the "legally segregated operationally commingled" model ("**LSOC**") for cleared swaps,[16] which is intended

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[12] *See e.g.*, Committee hearing "Investigative Hearing on the MF Global Bankruptcy" (December 3, 2011), available at: http://www.ag.senate.gov/hearings/investigative-hearing-on-the-mf-global-bankruptcy; Committee hearing "Examining the Futures Markets: Responding to the Failures of MF Global and Peregrine Financial Group", August 1, 2012, available at: http://www.ag.senate.gov/hearings/examining-the-futures-markets-responding-to-the-failures-of-mf-global-and-peregrine-financial-group.

[13] *See* Complaint, Commodity Futures Trading Commission v. Peregrine Financial Group, Inc., and Russell R. Wasendorf, Sr., No. 12–cv–5383 (N.D. Ill. July 10, 2012), available at: http://www.cftc.gov/ucm/groups/public/@lrenforcementactions/documents/legalpleading/enfpfgcomplaint071012.pdf. *See also* Report of the Trustee's Investigation and Recommendations, In re MF Global Inc., No. 11– 2790 (MG) SIPA (Bankr. S.D.N.Y. Jun. 4, 2012), available at: http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/mfglobaliinvestreport060412.pdf.

[14] On uncleared swap trades, customers post initial margin to their dealer counterparties, and customers and their dealer counterparties exchange variation margin on a daily basis, depending on changes in the value of the swap.

[15] 11 U.S.C. §766.

[16] *See* CFTC final rule on "Protection of Cleared Swaps Customer Contracts and Collateral; Conforming Amendments to the Commodity Broker Bankruptcy Provisions", 77 Fed. Reg. 6336 (February 7, 2012), available at: http://www.gpo.gov/fdsys/pkg/FR-2012-02-07/pdf/2012-1033.pdf. LSOC requires an FCM to segregate its customers' collateral from its own property, but permits the FCM to commingle in an omnibus account all collateral of its customers.

to protect the assets of non-defaulting customers from *pro rata* distribution. However, LSOC is a new and untested segregation model. If a bankruptcy trustee or FCM's creditors challenge LSOC's intended protections in court after a customer's default leads to an FCM's insolvency, it is possible that a Bankruptcy Court judge will agree and hold that non-defaulting customers' collateral is not "customer property" and is shielded from *pro rata* distribution. If Congress amends the Bankruptcy Code as discussed above, it would help to alleviate this uncertainty and protect customers.

In addition, market participants are continuing to consider other enhancements to customer protections, such as optional full physical segregation of customer collateral.[17] MFA appreciates the CFTC's efforts to enhance customer protections[18] by making valuable regulatory adjustments to reduce the likelihood of events similar to MF Global and Peregrine occurring in the future. However, we emphasize that work remains to ensure that customers receive appropriate and the same level of protections in the cleared market as some currently enjoy in the over-the-counter ("**OTC**") derivatives market. Therefore, MFA believes that, if Congress amended the Bankruptcy Code, it would significantly accelerate and enhance progress of customer protections and ultimately would facilitate customers' ability to customize and choose the level of protection that is appropriate for them.

## III. International Aspects of Regulation

### A. International Coordination

MFA urges U.S. policymakers and regulators to enhance their coordination with their European, Asian, and other counterparts to ensure that derivatives regulatory reform is consistent, where applicable, and addresses counterparty and systemic risk, while permitting access to, and competition among, central counterparties ("**CCPs**") organized in countries outside of the relevant jurisdiction.

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[17] Full physical segregation is an arrangement that allows a customer to put its collateral in an account with a custodian or other third party in the customer's name, rather than have the customer's FCM hold its collateral, and thus, protects the customer in the event that its FCM or another customer becomes insolvent.

MFA notes that, even if LSOC is tested in a Bankruptcy Court proceeding and determined that customers' collateral is not "customer property" subject to *pro rata* distribution, LSOC still relies on the accuracy of an FCM's books and records to be effective. Under LSOC, if the FCM's books and records are not up-to-date or contain errors, an issue remains that there might be a delay in return of customer collateral or customer collateral might incorrectly be designated as FCM or another customer's property. For this reason, market participants continue to pursue full physical segregation options to provide the most robust protection of their collateral.

[18] *See* CFTC notice of proposed rulemaking on "Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations", 77 Fed. Reg. 67866 (November 14, 2012), available at http://www.gpo.gov/fdsys/pkg/FR-2012-11-14/pdf/2012-26435.pdf (proposing to ensure adequate protection of customers and their funds by amending and augmenting the requirements for FCMs and derivatives clearing organizations, and enhancing the oversight of FCMs by their designated self-regulatory organizations).

As the Committee is aware, European,[19] Asian,[20] and other policymakers are currently finalizing or beginning to implement their regulatory reforms with respect to OTC derivatives. While MFA expects these regulations to complement the U.S. market reform to a certain extent, the scope is not identical to the U.S. regulations and they are proceeding at different paces. Therefore, we are concerned that, without sufficient coordination and harmonization as to timing and scope of these different initiatives, conflicting rules will impair market participants' ability to manage their portfolios and regulatory obligations, and present market participants with opportunities for regulatory arbitrage to the detriment of U.S. markets.

One example of an area that highlights the need for international coordination is the regulatory framework for capital and margin requirements for uncleared derivatives. MFA strongly believes that an internationally uniform set of margin requirements will facilitate orderly collateral management practices and minimize regulatory arbitrage in the uncleared swaps and uncleared security-based swap markets. MFA applauds the formation of the Working Group on Margining Requirements of the Basel Committee of Banking Supervision and the International Organization of Securities Commissions to develop a unified international framework for margining uncleared derivatives. In the absence of such uniformity, market participants, including MFA members, will have to monitor and comply with multiple margin regimes, which would be administratively difficult, costly and burdensome, and may increase the likelihood for errors and instances of non-compliance.

Similarly, STP is a critical aspect of mandatory clearing that requires CCPs to accept or reject trades that dealers submit for clearing as quickly as technologically practicable. STP is important because it provides counterparties with immediate certainty as to whether or not their trade has cleared and whether they will face the CCP as their counterparty rather than each other. The CFTC has exhibited strong leadership and has finalized and implemented STP rules.[21]

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[19] *See* Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories European Market Infrastructure Regulation (EU) No 648/2012 ("**EMIR**"), available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:201:0001:0059:EN:PDF; and European Commission Delegated Regulation (EU) No 148/2013 of 19 December supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories with regard to regulatory technical standards on the minimum details of the data to be reported to trade repositories, 2013 O.J. (L 52) (September 27, 2012), available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:052:FULL:EN:PDF.

[20] *See* Hong Kong Monetary Authority and the Securities and Futures Commission joint "Consultation paper on the proposed regulatory regime for the over-the-counter derivatives market in Hong Kong" (October 2011), available at: http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/openFile?refNo=11CP6; and Monetary Authority of Singapore "Consultation Paper on Proposed Regulation of OTC Derivatives" (February 2012), available at: http://www.mas.gov.sg/~/media/resource/publications/consult_papers/2012/13%20February%202012%20Proposed%20Regulation%20of%20OTC%20Derivatives.pdf.

[21] *See* CFTC Final Rules on "Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management", 77 Fed. Reg. 21307 (April 9, 2012), available at: http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-7477a.pdf, which became effective October 1, 2012.

However, other U.S. and non-U.S. regulators have yet to propose similar rules mandating STP.[22] We believe it is necessary for STP to become an international mandate to ensure: (1) market participants' ability to reduce their global counterparty credit risk without delay; (2) market participants' unrestricted access to the broadest range of executing counterparties; and (3) liquidity and competitive pricing of derivatives transactions.

Lastly, it is important that approval by U.S. and non-U.S. regulators of CCPs organized outside their jurisdiction (*i.e.*, third country CCPs) not become unreasonably difficult to obtain. Because of mandatory requirements for clearing of derivatives, it is important to ensure that market participants have sufficient access to, availability of, and competition among, CCPs organized in U.S. and non-U.S. jurisdictions. Otherwise, there is potential that the derivatives market will become fragmented along jurisdictional lines. Such fragmentation could cause significant harm to the markets by, among other things, impeding competition, impairing portability and eventual interoperability, limiting participant access to clearing and their ability to operate in certain jurisdictions, and ultimately creating artificial barriers across a global marketplace and instrument type.

While MFA recognizes that the regulatory regimes of different countries may need to diverge to a certain extent to reflect local concerns, inconsistent regulations will be costly, burdensome and, in some cases, make it impossible for market participants to comply with both regimes. We are appreciative of the ongoing joint efforts of U.S. and non-U.S. regulators to avoid any disharmony between the regulations, to the extent possible, as well as the imposition of duplicative regulation, and encourage continued efforts in this regard. We urge the Committee to continue its oversight of these issues and encourage regulators to work together.[23]

### B. Extraterritorial Application of International Regulations

MFA encourages U.S. and non-U.S. regulators to harmonize the extraterritorial scope and substituted compliance frameworks of their derivatives regulatory regimes. The extraterritorial application of the U.S. and non-U.S. derivatives regulations (particularly EMIR[24]) remains a significant area of focus and concern for MFA. Unfortunately, considerable uncertainty continues to exist with regard to this issue. We appreciate the need to ensure that where a market

[22] The SEC has yet to propose a rule mandating STP. From our discussions with European policymakers and regulators, we expect them to include an STP mandate in either the legislative text of the Markets in Financial Instrument Directives or the EMIR Level 3 guidance. However, we do not know how soon any STP mandate will take effect in Europe.

[23] MFA is not aware of any legal impediments that preclude greater cooperation. Nonetheless, MFA urges the Committee to monitor cooperative efforts and consider legislative action, should such discussions identify legal roadblocks.

[24] *See* the European Securities and Markets Authority ("**ESMA**") final report on "Draft technical standards under the Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC Derivatives, CCPs and Trade Repositories" (September 27, 2012), at 6, available at: http://www.esma.europa.eu/system/files/2012-600_0.pdf (indicating that in the future ESMA will issue separate draft regulatory technical standards on contracts that are considered to have a direct substantial and foreseeable effect in the Union).

participant's activities have a direct and significant effect on a jurisdiction, that market participant is subject to adequate regulation in that jurisdiction. However, because the derivatives market is a global market, market participants and their transactions will be subject to regulation in multiple jurisdictions. Thus, we urge harmonization of these regulations to ensure that the extraterritorial scope of the various international reforms will not be duplicative and that related substituted compliance regimes will give sufficient deference to comparable regulations. We believe it important to ensure that, together, the final regulations will provide certainty to market participants, ensure the continued robustness of the derivatives markets and further the progress of international harmony and consistency.

## IV. Oversight of Commodity Pool Operators

### A. Re-Focusing CPO Registration

MFA believes that Congress should consider enacting amendments to the CEA that would better focus regulatory attention on the entities that are meaningfully engaged in trading commodity interests. Some of the CFTC's recent actions have caused market participants that seek to comply fully with CFTC rules to consider registering many entities that only peripherally are related to CPO activities or technically fall within the relevant legal definitions. MFA believes that it would be a better use of regulatory resources to focus on registration and oversight of CPOs that are operators of entities that are "engaged primarily" [25] in or formed "for the purpose of trading commodity interests."[26]

While we have the utmost respect for the CFTC and its Staff, we believe the CFTC's repeal of Regulation 4.13(a)(4), the CPO registration exemption for a CPO of a private pool, overly broadened the registration mandate for CPOs of private vehicles. As a result, a wide variety of business models, which do not fit or match the CPO regulatory framework, now fall within CPO registration obligations; and the CFTC and National Futures Association ("**NFA**") have and continue to spend substantial resources addressing regulatory issues with respect to entities whose business models do not fit the commodity pool regulatory framework, that are subject to different regulatory regimes, engage in minimal trading of commodity interests, or have indirect exposure to commodity interests.

The combination of Dodd-Frank Act changes to the definition of commodity pool and CPO to include swaps transactions,[27] the CFTC's repeal of Regulation 4.13(a)(4)[28] and CFTC staff interpretations[29] greatly expanded the number and types of entities that fall within the meaning of commodity pool. These entities include SEC-registered investment advisers, securitization vehicles, real estate investment trusts, private equity firms, fund-of-funds, family

[25] *See* Section 4m(3)(B) of the CEA.

[26] *See* Sections 1a(10) and (11) of the CEA (defining "commodity pool" and "commodity pool operator").

[27] *See id.*

[28] 77 Fed. Reg. 11252 (Feb. 24, 2012).

[29] *See id.* (interpreting a collective vehicle with even a single swap to be a commodity pool, as well as a fund-of-funds that invests in a fund with commodity interest exposure).

offices, foreign pool operators and business development companies. The CFTC's repeal of Regulation 4.13(a)(4) generated a substantial number of requests for interpretive and compliance relief as investment managers and other entities struggled to rationalize and adapt to different, overlapping regulatory regimes. MFA, in an effort to streamline federal regulation of investment managers, submitted numerous requests to the CFTC for clarifications, no-action or interpretive relief, petition for rulemaking, and guidance.[30] Many of our requests are outstanding; and we continue to work on new requests for regulatory relief.

The CFTC's Regulation 4.13(a)(3) provides an exemption from CPO registration for a CPO of a private pool that has very limited exposure, including from *bona fide* hedging, to commodity interests.[31] In calculating commodity interest exposure, the CFTC staff is of the view that an entity must calculate indirect commodity interest exposure even if the vehicle itself does not trade commodity interests. As a consequence, many fund-of-funds and private investment funds that do not trade commodity interests are swept into the definition of commodity pool. The limited availability of an exemption from registration has created CFTC regulatory obligations for many SEC-registered investment advisers and other types of entities with minimal commodity interest trading or indirect commodity interest exposure.

We believe the CEA does contemplate a broader exemption from CPO registration. The CEA provides that "[t]he term 'commodity pool' means any investment trust, syndicate, or similar form of enterprise ***operated for the purpose of trading in commodity interests***," (***emphasis added***).[32] Also, Section 4m(3) of the CEA introduces the concept of "engaged primarily" with respect to CTA registration, and excepts a CTA that is:

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[30] *See, e.g.*, letter from MFA, Alternative Investment Management Association, and Investment Adviser Association ("**IAA**"), to David A. Stawick, Secretary, CFTC, dated April 30, 2012, on "Request for an Extension of Time for Compliance with Registration as a Result of the Amendments to § 4.13"; letter from Stuart J. Kaswell, Executive Vice President & Managing Director, MFA, to Gary Barnett, Director, CFTC, dated August, 27, 2012, on "Request for Interpretive Guidance – Transition Period under § 4.13(a)(3)"; letter from Stuart J. Kaswell, Executive Vice President & Managing Director, MFA, to David Stawick, Secretary, CFTC, dated August 30, 2012, on "Petition for Rulemaking to Amend CFTC Rule 4.10(d)(1) & Request for Interim Relief"; letter from MFA and IAA to Sauntia S. Warfield, Assistant Secretary, CFTC, dated November 9, 2012, on "Request for Delayed Compliance Date of Amended Part 4; Former Appendix A of the CFTC's Part 4 Regulations, 17 CFR Part 4"; and letter from MFA, IAA, Asset Management Group of the Securities Industry and Financial Markets Association ("**SIFMA AMG**"), and the Investment Company Institute ("**ICI**"), to Gary Barnett, Director, CFTC, dated November 30, 2012, on "Request for a Temporary Exclusion of an Investment in a Securitization Vehicle as a "Commodity Interest" for Purposes of CPO and CTA Registration and Compliance"; letter from Stuart J. Kaswell, Executive Vice President & Managing Director, MFA, to Sauntia S. Warfield, Secretary, CFTC, dated December 19, 2012, on "Proposed Guidance with respect to § 4.13(a)(3)"; and letter from MFA, IAA, ICI and SIFMA AMG, to Gary Barnett, Director, CFTC, dated January 25, 2013, on "Compliance with Registration Requirements Under Amended Regulations 4.5 and 4.13(a)(3)." *See also note* 39. In addition, MFA has made several informal submissions to the CFTC staff with respect to questions for the CFTC's FAQs on CPO and CTA compliance obligations, and questions regarding Forms CPO-PQR and CTA-PR (still pending with CFTC staff). These letters are available on MFA's website: www.managedfunds.org.

[31] *See* CFTC Regulation 4.13(a)(3).

[32] Section 1a(10) of the CEA.

> registered with the Securities and Exchange Commission as an investment adviser whose business does not consist ***primarily of acting*** as a commodity trading advisor, as defined in section 1a, and that does not act as a commodity trading advisor to any commodity pool that is ***engaged primarily*** in trading commodity interests (***emphasis added***).

Section 4m(3)(B) of the CEA provides that:

> a commodity trading advisor or a commodity pool shall be considered to be "engaged primarily" in the business of being a commodity trading advisor or commodity pool if it is or holds itself out to the public as being engaged primarily, or proposes to engage primarily, in the business of advising on commodity interests or investing, reinvesting, owning, holding, or trading in commodity interests, respectively.

Given that regulatory resources are limited, we believe Congress should direct the CFTC to focus registration oversight of CPOs on entities that are engaged primarily or operated for the purpose of trading commodity interests rather than overseeing entities with minimal or indirect exposure to commodity interests. Accordingly, we recommend that Congress consider amending the CEA by providing a registration exemption for operators of entities that are not engaged primarily in trading commodity interests or formed for the purpose of trading commodity interests.

### B. CFTC-SEC Coordination on Regulation Pertaining to Private Fund Operators/Advisors

As a majority of the new CPO registrants are registered investment advisers of private funds, we believe Congress should direct the CFTC and SEC to streamline regulations for operators of private funds and to ensure consistency among regulations. We are concerned that the differences between the CFTC's and the SEC's regulatory frameworks for operators/advisers of private funds creates significant burden on the private fund industry. For example, we are concerned that a private fund manager registered as an investment adviser, CPO and CTA faces three different systemic risk reporting obligations—filing Form PF with the SEC, filing Form CPO-PQR and CTA-PR with the CFTC, and filing quarterly PQR and PR reports with NFA. The overlapping but distinct reporting requirements are a substantial burden on the fund industry.[33] We believe the regulation of private fund managers between the CFTC and SEC should be consistent where there is overlap. Accordingly, we recommend that Congress direct the CFTC and the SEC to collaborate in ensuring that their private fund regulations are consistent.

[33] We note that the CFTC worked with the SEC and other regulators in formulating the systemic risk forms. However, the end-product has been different forms requesting for similar information in different ways.

### C. Conforming Amendments with respect to Private Pools and the Rescission of the Prohibition on General Solicitation and Advertising

MFA believes that amendments to the CEA are needed to provide for consistent regulation of private pools and investment funds. The Jumpstart Our Business Startups Act of 2012 ("**JOBS Act**") directed the SEC to amend the securities regulations to eliminate the prohibition on general solicitation and advertising with respect to private offerings under Regulation D.[34] Privately-offered investment funds and commodity pools are also subject to Regulation D. The CFTC adopted regulations concerning privately-offered commodity pools to be consistent with the securities regulations, and included provisions prohibiting "public marketing".[35] The CFTC regulations concerning CPOs of privately-offered commodity pools are now inconsistent with the JOBS Act. We believe this situation creates an unreasonable dichotomy between the regulation of advisers of private funds and CPOs of privately-offered commodity pools. Accordingly, we recommend that the Committee amend the CEA to direct the CFTC to ensure that regulations concerning CPOs of privately-offered commodity pools are consistent with the JOBS Act and the relevant securities regulations.[36]

## V. Position Limits

MFA urges the Committee to oversee carefully any new CFTC efforts to impose position limits. MFA continues to have significant reservations about the efficacy of position limits; nonetheless we have sought to work constructively with the CFTC on its efforts to implement them. Accordingly, we believe that the CFTC, in promulgating position limit rules, should regulate based on quantitative findings, including the size and depth of markets. We are concerned that inappropriate limits could reduce hedging activity, decrease market liquidity, and artificially raise commodity prices. Most importantly, we believe that persons with independently controlled accounts should be able to treat such accounts separately and not aggregate the positions of such accounts for position limit purposes. We respectfully urge the Committee to encourage the CFTC to take a data-driven approach in setting position limits if it finds that limits are appropriate.

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[34] Section 201 of the JOBS Act, P.L. 112-106. Section 201 provides that "the prohibition against general solicitation or general advertising . . . shall not apply to offers and sales of securities made pursuant to section 230.506, provided that all purchasers are accredited investors."

[35] *See e.g.,* 68 Fed. Reg. 47221 (Aug. 8, 2003) (Adopting Release for Regulation 4.13(a)(3)), available at: http://www.gpo.gov/fdsys/pkg/FR-2003-08-08/pdf/03-20094.pdf; and 57 Fed. Reg. 34853 (Aug. 7, 1992) (Adopting Release for Regulation 4.7).

[36] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to David A. Stawick, Secretary, CFTC, dated July 17, 2012, on "Harmonization of Compliance Obligations and the Jumpstart Our Business Startups Act and CFTC Regulations" *available at:* https://www.managedfunds.org/wp-content/uploads/2012/07/CFTC-JOBS-Act-final-7-17-12.pdf.

MFA appreciates the opportunity to provide our comments and concerns to the Committee related to reauthorization of the CFTC. We would welcome the opportunity to discuss our comments in greater detail. Please do not hesitate to contact me or Roger Hollingsworth at (202) 730-2600 with any questions you, the Committee, or your staffs might have regarding this letter.

Respectfully submitted,

/s/ Richard H. Baker

Richard H. Baker
President and Chief Executive Officer