March 28, 2016

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Use of Derivatives by Registered Investment Companies (File Number S7-24-15)

Dear Mr. Fields:

AssetMark, Inc. ("AssetMark") appreciates the opportunity to comment on the Securities and Exchange Commission's (the "Commission") Proposed Rule 18f-4 (the "Proposed Rule") under the Investment Company Act of 1940 (the "1940 Act") regarding the use of derivatives by registered investment companies. While we welcome many of the elements of the Proposed Rule, we feel strongly that the 150% exposure limit on leverage should be refined in order to avoid a negative impact on investors. We appreciate the comprehensiveness and clarity of the Proposed Rule as well as the questions posed by the Commission in the proposing release (the "Release"). We believe our answers to some of these questions provide the opportunity to explain why the Proposed Rule should be refined, and we offer suggestions for how this can be accomplished.

Background

By way of background, AssetMark is an independent provider of investment and consulting solutions to independent financial advisers, with approximately $28.5 billion in combined assets on its platform. Over 6,500 advisors maintain more than 120,000 accounts on AssetMark's platform with an average account size of roughly $230,000. The platform utilizes an open architecture environment, which enables advisors to offer a choice of proprietary and third-party solutions, including AssetMark's proprietary mutual funds, to their clients. It is important to note that less than 10% of the assets on AssetMark's platform are in its proprietary mutual funds, because we believe our perspective on the Proposed Rule is informed less by our commercial interests than by our role as a consultant with the responsibility to provide high-level portfolio construction advice to advisors for the benefit of their clients.

The Importance of Managed Futures in Overall Portfolio Construction

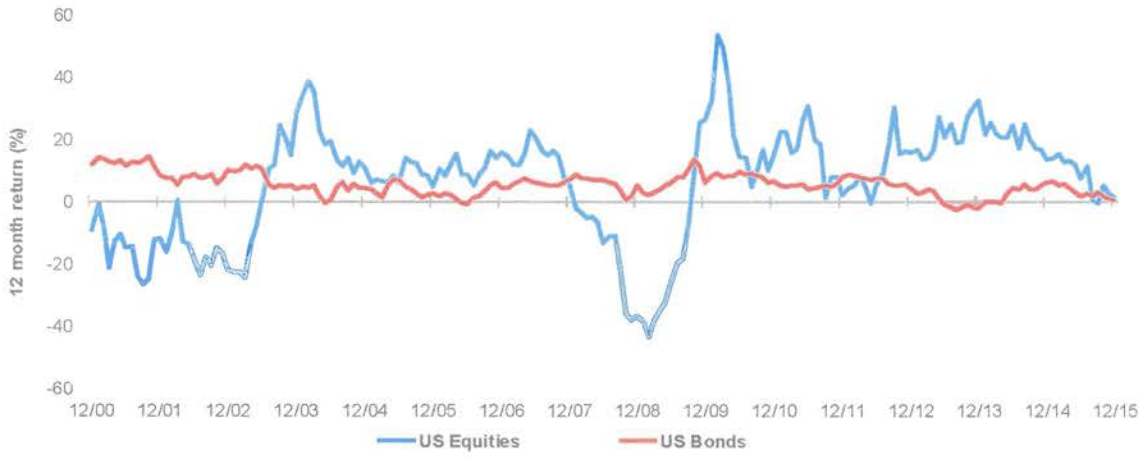
Managed futures strategies are generally trend-following strategies that use exchange-traded futures contracts to gain long exposure to markets with prices that have been trending up and to gain short exposure to markets where prices have been trending down. They are broadly diversified across assets and asset classes with exposure to equity indices, government bonds and notes, short-term interest rates, currencies, precious metals, industrial metals, oil and gas, crops and livestock. This diversification helps a fund manager to control risk and to provide more consistent returns since the trend can be observed more clearly across related assets than in any single asset. Diversifying across asset classes reduces portfolio risk and allows the fund manager to tilt toward markets where price trends can be most clearly observed.

Most managed futures fund managers actively manage portfolio risk (i.e., volatility) by monitoring short-term price volatility and adjusting market exposures daily to stay within a relatively narrow volatility band comparable to the long-term average price volatility of a broad-based equity market index. The asset classes in which managed futures strategies invest generally have very different levels of price volatility. Without the flexibility to maintain exposures greater than 150%, a managed futures fund cannot effectively diversify its positions by including lower-volatility assets. For example, because 3-month Treasury Bills exhibit much less volatility than a stock market index (e.g., the S&P 500), far greater notional exposure through futures would be required to approach the risk associated with an unleveraged investment in a stock market index. By effectively excluding lower volatility assets, the proposed 150% exposure limit would mean that naturally high-volatility assets such as stock market indices and commodities would consistently dominate the portfolio's returns, undermining the key benefit of managed futures to investors and their financial advisers.

Managed futures mutual funds are a uniquely valuable category of mutual funds for investors and their advisors because they enable more efficient and effective overall portfolio diversification with the potential for higher long term returns and less severe declines in overall portfolio value during stock market crises. Managed futures strategies historically have displayed very low correlations to traditional stock and bond investments. For the 15 years ended December 31, 2015, the correlation of the SG Trend Index (comprised of the ten largest managed futures trend-followers) with the S&P 500 was -0.14%. Its correlation for the same time-period with the

Barclay's US Aggregate Bond Index was only 0.21%, making managed futures a truly diversifying tool for equity and fixed income portfolios.

Consistent with Modern Portfolio Theory, the lack of correlation provided by managed futures strategies reduces portfolio risk (i.e., volatility) without a systematic or material reduction in long-term return. It is believed that the low correlation between managed futures strategies and stock market returns is due to the fact that markets can "trend" most strongly during periods of high market volatility, and periods in which markets experience extreme or extended declines tend to be the most volatile. The combination of the low correlation of managed futures returns to stock market returns and the fact that managed futures funds generally target an overall risk level comparable to the long term average volatility of stock indexes means that managed futures are likely to produce positive returns when stock markets are in decline, and the magnitude of their returns can offer a material offset to the losses experienced by investors in their stock market investments.



Source: Zephyr Style Advisor. US Equities represented by S&P 500, US Bonds represented by Barclays US Aggregate

Source: Zephyr Style Advisor. US Equities represented by S&P 500, Managed Futures represented by SG Trend (BarclayHedge Systematic Traders prior to 2000)

Although managed futures returns have frequently been positive when stock market returns were materially negative, the potential for managed futures to offset stock market losses in diversified portfolios was clearly demonstrated during the Financial Crisis of 2007 – 2009, when the S&P 500 Index lost 41.39% between 11/01/07 and 02/28/09, and most other assets and alternative strategies were down. As the chart below illustrates, only bonds (as measured by the Barclays U.S. Aggregate Bond Index) and managed futures (and the closely-related global macro) strategies were spared.

Source: Zephyr Style Advisor. US Equities represented by S&P 500, Diversified Hedge Fds represented by HFRI Fund of Funds Composite, Global Macro represented by HFRI Macro (Total), Equity Market Neutral represented by HFRI: EH Equity Market Neutral, Relative Value represented by HFRI Relative Value (Total), Managed Futures represented by SG Trend (BarclayHedge Systematic Traders prior to 2000), Merger Arbitrage represented by HFRI ED: Merger Arbitrage

The value of a managed futures component in portfolio construction is further enhanced by the fact that its "downside assistance" is available to investors without depressing what would otherwise be their long-term return. For the 15-year period ended December 31, 2015, the compound average annual return for managed futures (based on the SG Trend Index) was 6.12%, while the return for U.S. stocks was 5.00% (based on the S&P 500 Total Return Index).

Impact of the Proposed Rule on Managed Futures Mutual Funds

Because of the unique value of managed futures to investors and advisors when constructing portfolios, we have focused our comments on the impact

the Proposed Rule is likely to have on managed futures mutual funds, and the disadvantages to investors of the proposed 150% exposure limit.

In the Discussion section of the Release, the Commission acknowledges that the proposed notional exposure limits may be inconsistent with the flexibility needed by mutual funds employing managed futures strategies, but points out that such mutual funds represent a mere 0.09% of all mutual fund assets. While the assets in mutual funds employing managed futures strategies are small relative to asset levels across all mutual funds, we believe that this is not a reflection of the value of these managed futures strategies or investor interest in them, but of their relative newness in the mutual fund space. The Chicago Board of Trade did not introduce futures contracts on Treasury bonds and notes until 1977, and the first managed futures fund registered under the 1940 Act (the Rydex Managed Futures Strategy Fund) was not launched until 2007. As a result, the behavior of managed futures funds was not seriously appreciated until the recent Financial Crisis, when it caught the public's attention. Managed futures strategies in mutual funds have had only eight years since their introduction to accumulate assets in contrast to the more than 75 years for equity and fixed income mutual funds.

Alternatives for Investors to Access Managed Futures Strategies

As the Commission observes, there are alternative vehicles available to investors through which managed futures strategies can be accessed, including private funds and publicly-offered commodity pools. Indeed, until 2007 these were the only vehicles outside of individually-managed accounts through which such strategies were available. However, private funds generally are only open to accredited investors and often require high minimum investments, putting them out of reach for the average investor. In addition, private funds and public commodity pools generally generate a Form K-1 for their investors in lieu of a Form 1099, adding perceived complexity and potential delays in tax filing, making them less attractive to the average investor. Furthermore, fees on public commodity pools and private funds with managed futures strategies generally include both management and performance fees, making them significantly more expensive than managed futures mutual funds, at least historically. For these reasons, the available alternative vehicles for managed futures strategies are either inaccessible to most individual investors or come with prohibitive disadvantages.

Mutual fund sponsors with managed futures strategies could choose to conform to the 150% exposure limit, however they would need to either dramatically lower their overall notional exposure. This would diminish the portfolio diversification benefits of the strategy because it would either significantly lower volatility (i.e., impact) or dramatically narrow the set of asset classes to include only those that require the lowest notional exposure because they have the highest natural volatility (i.e., market risk). If such a strategy offered improved returns or portfolio diversification, it would already be offered by managed futures managers. In fact, the 150% exposure limit is likely to materially impair both returns and diversification.

Grandfathering

At a minimum, if the Commission decides to impose a 150% exposure-based limit on all mutual funds, managed futures mutual funds in operation today should be grandfathered to preserve the availability of this uniquely valuable strategy, and more importantly, to protect investors in these funds from having their overall portfolio diversification materially diminished. Only the higher exposure limit would need to be grandfathered as managed futures mutual funds should be able to comply with all other elements of the Proposed Rule without compromising the benefits of their return characteristics.

Recommended Refinements to the Proposed Rule

Beyond grandfathering, we recommend that an exception to the 150% exposure limit be made for managed futures and any other strategy that exclusively employs simple exchange-traded derivatives with daily liquidity and margin requirements, such as futures contracts, provided that: 1) such strategies conform to all other elements of the Proposed Rule; 2) are actively managed to remain within a specified volatility range over all time periods, with a targeted maximum no greater than 20% annualized, and 3) the non-derivative portion of the fund is invested exclusively in high-quality cash equivalents.

Such an exception appropriately recognizes both the importance of the portfolio diversification benefits offered by managed futures strategies to investors, as well as the ability for such strategies to be managed consistent with the Commission's desire to discourage undue speculation and to ensure asset adequacy.

Recommended refinements to the 150% exposure limit

The strength of an across-the-board 150% exposure limit is its simplicity. However, the weakness of such a limit is that by not distinguishing between derivatives based on assets with different degrees of market risk, or between derivatives that are liquid and illiquid, or based on how the non-derivative portion of a fund is invested, the rule is both overly and inadequately restrictive. For example, an S&P 500 index fund that also has a derivatives allocation with additional equity market exposure could have a total notional exposure to the stock market approaching 250%. At such an exposure level, there would have been multiple periods in recent history where investors in such a fund would have lost the entirety of their investment. In contrast, a fund that seeks to balance the risk of investing half its assets in stocks with a comparable risk allocation to Treasury bills and notes could be restricted from doing so by the very same rule (even with the VaR-based 300% alternative limit).

If the Commission decides that a 150% exposure limit is acceptable for even the riskiest assets, we recommend the Commission create three categories of assets with different exposure limits but comparable levels of volatility:

Category 1
For derivatives based on high-volatility reference assets, such as stocks and commodities. The exposure limit could be 150%, as currently proposed by the Commission.

Category 2
For derivatives based on lower-volatility reference assets, such as government obligations with maturities greater than 3 years and currencies. The exposure limit for such derivatives could be 500%.

Category 3
For derivatives based on reference assets with the lowest volatility, such as interest rate contracts and government obligations with maturities shorter than 3 years. An exposure limit of 1000% could be applied to such derivatives, and their volatility would still likely be less than that of 150% exposure to a broadly-diversified stock index.

A rule such as the one above, which categorizes derivatives by their reference assets into three categories and applies a different exposure limit to each based on the volatility of the referenced asset, would allow distinctions between assets without sacrificing simplicity of application. It

would give much greater flexibility to fund managers than a blunt 150% exposure limit, while still addressing the Commission's concerns regarding undue speculation and asset sufficiency. To further address the Commission's concerns, the applicability of the volatility-based three-category construct could be limited to simple derivatives such as exchange-traded futures contracts with daily liquidity and daily margin requirements, and funds where the non-derivatives portion of the fund's holdings are invested exclusively in cash equivalents. These restrictions, combined with the Commission's recommendations for an asset coverage calculation based on a derivative's market value plus some "cushion", (e.g., a simultaneous three standard deviation unfavorable move on each derivative position in the fund), would provide investors with ample protection. The exposure limit for complex derivatives or illiquid derivatives that do not have daily margin requirements could be maintained at 150%.

Unequal Access for Mutual Fund Investors

The unfortunate consequence of the Proposed Rule is, that while the benefits of managed futures will remain available to certain types of investors through private funds and commodity pools, the portfolio diversification benefits of managed futures strategies will be denied to many mutual fund investors who can least afford to be exposed to volatile markets without the tempering influence of managed futures strategies.

Conclusion

The Commission's Proposed Rule is welcome. A comprehensive updating of the rules governing the use of derivatives by registered investment companies is necessary and extremely helpful. We support most of the elements of the Proposed Rule, specifically a formal board-approved derivative risk management program, the designation of a derivatives risk officer who reports to the mutual fund board, the maintenance and daily monitoring of qualifying coverage assets, and the definition of qualifying coverage assets.

Our primary concern with the Proposed Rule is its across-the-board application of a single notional exposure limit for derivatives regardless of: 1) how the non-derivatives portion of a fund is invested; 2) whether the derivatives in question are simple or complex, liquid or illiquid, with or without daily margining; and 3) the market volatility of the asset referenced by the derivative. This overly simple approach to restricting undue speculation and ensuring asset sufficiency is inadequate to accomplish its

goals while effectively eliminating a unique and important tool in managing overall portfolio risk. The proposed 150% exposure limit would strip the value from managed futures strategies in mutual funds, denying mutual fund investors access to one of the very few investment strategies that did not lose money during the Financial Crisis of 2007-2009. Given that managed futures strategies will continue to be available to wealthy and sophisticated investors without restriction in private funds and public commodity pools, it is distressing that the average mutual fund investor might lose access to these same managed futures strategies in his portfolio. These issues can be easily avoided with the simple amendment we propose. We sincerely hope the Commission will address these concerns by incorporating our proposed refinements into the final rule.

Thank you again for this opportunity to share our comments on this important piece of regulation for funds and their investors.

Sincerely,

Jerry Chafkin
Chief Investment Officer
AssetMark, Inc.