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

January 24, 2011

Via Electronic Mail: rule-comments@sec.gov

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

Re: Managed Funds Association Comments on Exemptions for Certain Advisers; File No. S7-37-10

Dear Ms. Murphy:

Managed Funds Association ("MFA")[1] appreciates the opportunity to provide comments on the Securities and Exchange Commission's (the "SEC") proposed rule, "Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than $150 Million in Assets Under Management, and Foreign Private Advisers," Investment Advisers Act Release No. IA-3111 (the "Exemptions Release). Throughout the legislative process leading up to enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") MFA consistently expressed its strong support for a comprehensive registration framework for investment advisers. We believe that the Exemptions Release generally provides a reasonable framework for implementation of the private fund registration provisions in Title IV of the Dodd-Frank Act.

Though we are generally supportive of the approach taken in the Exemptions Release, we encourage the SEC to consider providing additional guidance regarding the application of the proposed exemptions. We believe the proposed interpretations set out below are consistent with the registration framework as contemplated by the Dodd-Frank Act and the Exemptions Release. In that regard, we request additional guidance from the SEC with respect to the new statutory exemption for commodity trading advisors; the registration

[1] MFA is the voice of the global alternative investment industry. Its members are professionals in hedge funds, funds of funds and managed futures funds, as well as industry service providers. Established in 1991, MFA is the primary source of information for policy makers and the media and the leading advocate for sound business practices and industry growth. MFA members include the vast majority of the largest hedge fund groups in the world who manage a substantial portion of the approximately $1.9 trillion invested in absolute return strategies. MFA is headquartered in Washington, D.C., with an office in New York.

obligations for certain entities affiliated with a registered investment adviser; single investor private funds; and the proposed definition of "investor."

Commodity trading advisor exemption

Section 403 of the Dodd-Frank Act provides a new exemption from registration with the SEC under new Section 203(b)(6)(B) of the Investment Advisers Act of 1940 (the "Advisers Act") for an investment adviser that "is registered with the Commodity Futures Trading Commission as a commodity trading advisor and advises a private fund, provided that, if after the date of enactment of the [Dodd-Frank Act], the business of the advisor should become predominately the provision of securities-related advice, then such adviser shall register with the Commission."[2] In determining whether the new exemption is available, an investment adviser that is currently registered as a commodity trading advisor ("CTA") must assess whether its business is, or becomes, "predominately the provision of securities-related advice." Such a determination depends in significant part on the definition of the term "predominately," but that term is not defined in the Dodd-Frank Act.

The language in Section 403 of the Dodd-Frank Act reflects Congress's recognition that CTAs to private investment funds, which are primarily engaged in the business of providing advice regarding futures and are already subject to a comprehensive registration and regulatory framework, do not have to be dually registered. It further reflects the view that requiring these CTAs to register with both the SEC and the Commodity Futures Trading Commission (the "CFTC") would, at best, subject them to a duplicative regulatory framework and, at worst, subject them to potentially inconsistent regulatory requirements.

MFA believes that it is important to clarify the criteria relevant to determining whether an investment adviser that is registered with the CFTC can rely on either of the relevant exemptions from registration under Section 203(b)(6) of the Advisers Act. We request that the SEC provide guidance as to the appropriate scope of the exemptions in Section 203(b)(6). In this regard, in September of 2009, MFA filed a comment letter with the SEC and the CFTC recommending that they consider the factors addressed in the *Peavey Commodity Futures Fund* no-action letter.[3] We continue to believe that the

[2] In addition to the new exemption in Section 203(b)(6)B), the Dodd-Frank Act also retained the exemption for registered commodity trading advisors in prior Section 203(b)(6) (now Section 203(b)(6)(A)) of the Advisers Act.

[3] *See* Peavey Commodity Futures Fund, SEC No-Action Letter (pub. avail. June 2, 1983), 1983 SEC No-Act. LEXIS 2576 (determining the primary engagement of a fund for purposes of the Investment Company Act of 1940, as amended). *See also,* Tonopah Mining Co. of Nevada, 26 S.E.C. 426 (1947) (adopting a five factor analysis for determining an issuer's primary business for purposes of assessing the issuer's status under the Investment Company Act of 1940, as amended) (the "1940 Act").

A copy of MFA's comment letter is available at http://www.managedfunds.org/downloads/MFA%20response%20to%20SEC.CFTC.9.25.09.pdf.

factors addressed in the letter provide an appropriate framework for determining the primary (or predominant) business of an investment adviser that is also a CTA.

Registration of subadvisers, subsidiary advisers and affiliated entities

The Advisers Act registration provisions of the Dodd-Frank Act were intended to create a comprehensive registration framework that reduced gaps in the SEC's regulatory authority over the investment adviser industry. We do not believe the Dodd-Frank Act was intended to alter the SEC's authority to provide exemptions to or limitations on the application of the Advisers Act to entities, as appropriate in light of the intended purposes of the Advisers Act. In the Exemptions Release, the SEC asks for comment on whether the activities of subadvisers, subsidiary advisers, and affiliates should be considered in determining whether an entity is eligible for an exemption. We recognize that there are circumstances when the SEC or its staff would need to consider the relevant facts on a case-by-case basis. As discussed in more detail below, however, we encourage the SEC to address in the final rule release some additional circumstances beyond those addressed in the Exemptions Release in which we believe it would be appropriate to provide an exemption from registration for entities affiliated with a registered investment adviser.

An investment adviser may seek to assign or delegate management of a portion of its client's assets to an affiliated entity such as a subadviser, including, for instance, when an investment adviser seeks exposure to regions, strategies or products in which a subadviser has specialized expertise. The Exemptions Release provides guidance with respect to a number of circumstances involving foreign advisers and subadvisers (by designating them as exempt reporting advisers), some of which are formalizations of previous SEC staff guidance provided in no-action letters to individual advisers. We believe that the SEC should clarify in its final rule the circumstances under which an affiliate, subsidiary adviser or subadviser would be required to register separately as an investment adviser under the Advisers Act as a consequence of its relationship to the investment adviser. In particular, we request that the SEC indicate whether, in each case set out below, the affiliated entity would be required to register under the Advisers Act.

<u>Affiliated entities in a control relationship with a registered adviser</u>

A registered investment adviser may control, be controlled by, or be under common control with, other domestic or non-U.S. investment advisory firms.[4] The registered investment adviser and other advisers or affiliated entities are typically part of the same organization and subject to the same or similar compliance and management structures. Such affiliated entities typically are, for tax or other purposes, organized as separate legal entities rather than branch offices. Each of the affiliated entities typically has authority to manage assets for clients.

[4] Section 202(a)(12) of the Advisers Act defines "control" to mean the power to exercise a controlling influence over the management or policies of a company, unless such power is solely the result of an official position with such company.

We believe that the public policy purposes of the Dodd-Frank Act and the Advisers Act can be achieved without requiring each such affiliate to register and that requiring registration of each affiliate would simply add costs to the industry without additional public policy benefits. Under the SEC's current policy, non-registered advisers operating under "participating affiliate" agreements with registered advisers are not required to register with the SEC as long as: (1) the registered entity treats each non-registered entity as a “participating affiliate” as described in *Mercury Asset Management plc* and in prior and subsequent no-action letters issued by the staff (the “Affiliate Letters”);[5] (2) the registered and non-registered entities act substantially in accordance with the factual representations cited by the SEC staff in the Affiliate Letters; and (3) the registered entity treats as its “associated persons” and subjects to its supervision all of the employees of the non-registered entities that provide advice to U.S. clients or have access to any information concerning which securities are recommended to U.S. clients prior to the effective dissemination of the recommendations. This approach currently gives the SEC full regulatory access and oversight over the U.S. activities of each such non-registered adviser and avoids the imposition of unnecessary burdens on multi-jurisdictional advisory firms. This approach also, in the case of non-U.S. advisers, recognizes in the spirit of international comity that the non-U.S. activities of non-U.S. advisers are less likely to implicate U.S. regulatory interests. Consistent with the SEC's current position, we believe the SEC should reaffirm that affiliated entities may continue to rely on the Affiliate Letters. This will ensure that the SEC retains appropriate regulatory oversight of the U.S. activities of a multi-jurisdictional advisory firm and will help facilitate the collection of systemic risk information as it would reduce the likelihood of double counting that could result from having multiple advisers report information about the activities of a single fund or client.

The position described above is consistent with the SEC staff guidance provided in connection with the adoption of the hedge fund adviser registration rules,[6] in which staff concluded that affiliated investment advisers could rely on the Affiliate Letters.[7] For the reasons set out above, and particularly in light of the number of affiliated entities that we believe will be required under the Dodd-Frank Act to register with the SEC as investment advisers, we request that the SEC formalize in the final rules or otherwise confirm that its positions in the Affiliate Letters apply to a registered adviser and its U.S. and non-U.S. advisory affiliates.

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[5] SEC No-Action Letter (Apr. 6, 1993). *See also União de Banco de Brasileiros S.A.*, SEC No-Action Letter (Jul. 28, 1992); *Kleinwort Benson Investment Management Limited, et al.*, SEC No-Action Letter (Dec. 15, 1993); *Murray Johnstone Holdings Limited, et al.*, SEC No-Action Letter (Oct. 7, 1994); *ABN AMRO Bank N.V., et al.*, SEC No-Action Letter (Jul. 1, 1997); and *Royal Bank of Canada, et al.*, SEC No-Action Letter (Jun. 3, 1998).

[6] SEC Investment Advisers Act Release No. IA-2333.

[7] *See ABA Subcommittee on Private Investment Entities*, SEC No-Action Letter (Dec. 8, 2005).

Affiliated entities not in a control relationship with a registered adviser

There are also circumstances when registered investment advisers may be affiliated with entities that are not part of the same compliance and management structures. To the extent that the goals of regulatory access, oversight and reporting can be achieved with respect to non-control, affiliated entities,[8] we believe it would be appropriate to exempt such affiliated persons from registration. Accordingly, we request that the SEC provide guidance in the final rules or otherwise confirm that an affiliated, but non-registered and non-controlled subadviser (whether formed under U.S. or non-U.S. law) that meets the definition of "affiliated person" in Section 202(a)(12) of the Advisers Act and is engaged by a registered investment adviser to manage a portion of the assets of a private fund managed by the registered adviser would not be required to register with the SEC; provided, that the unregistered affiliate is listed on the registered adviser's Form ADV; complies with the record keeping requirements of the Advisers Act; agrees to comply with SEC requests for information or examinations; and provides (directly or indirectly through the registered adviser) such information as the SEC deems appropriate. We believe that providing this limited exemption from registration is consistent with the goals of the Dodd-Frank Act and provides the SEC with oversight authority in an effective and efficient way.

Single investor private funds

Section 203(m) of the Advisers Act contains, among other things, a requirement that an investment adviser seeking to rely on the exemption provided by that Section must act "solely as an adviser to private funds." The term "private fund" is defined under the Dodd-Frank Act as "an issuer that would be an investment company, as defined in Section 3 of the [Investment Company Act of 1940], but for Section 3(c)(1) or 3(c)(7) of that Act." By its express terms, Section 203(m) would not permit an investment adviser to rely on the exemption if it provides investment advice to, among others, any other type of investment company exempted or excluded from the Investment Company Act of 1940's (the "Investment Company Act") definition of "investment company" or an individual client separate account.

We are aware that many advisers provide investment advice to private funds that have only a single investor. Such a fund may, for example, serve as a specialized feeder fund in a master-feeder structure. An investment adviser may also use a single investor private fund when making an investment in a side-by-side structure in which a number of private funds co-invest following the same investment objective and strategy. Such

[8] Section 202(a)(12) of the Advisers Act defines "affiliated person" by reference to the definition of that term in the Investment Company Act of 1940. Section 2(a)(3) of the Investment Company Act defines "affiliated person" to include: "(A) any person directly or indirectly owning, controlling, or holding with power to vote, 5 per centum or more of the outstanding voting securities of such other person; (B) any person 5 per centum or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by such other person; (C) any person directly or indirectly controlling, controlled by, or under common control with, such other person; (D) any officer, director, partner, copartner, or employee of such other person."

structures are often created at the request of institutional investors. We note in this regard that neither Section 3(c)(1) nor Section 3(c)(7) requires a fund to have a minimum number of investors.

As recently as March 5, 2010, the staff of the SEC recognized that a "pooled investment vehicle," in certain circumstances, is not required to have a minimum number of investors. Rule 206(4)-2 under the Advisers Act provides that a "limited partnership (or limited liability company, or another type of pooled investment vehicle)" is exempt from the independent verification of assets requirement under the Rule. In responding to a question relating to amendments to the Rule, the staff agreed that an entity was not required to have a minimum number of investors to rely on the exemption.[9] The question asked cited instances in which a limited partnership, limited liability company or other pooled vehicle would only have one member, including a pooled investment vehicle "formed where the general partner has only a nominal capital account and there is a single limited partner," and "a limited liability company [that] may have a single member."[10] We request that the SEC confirm in the final rule release that, to the extent an investment adviser meets the requirements of Section 203(m), that the investment adviser would not lose its exemption solely because it provides advice to a private fund having a single investor.[11]

Definition of "investor"

The Exemptions Release generally defines the term "investor" by reference to persons who would be considered a beneficial owner of a fund for purposes of Sections 3(c)(1) and 3(c)(7) of the Investment Company Act. The Exemptions Release specifically states that a third party that holds "any instrument, such as a total return swap, that effectively transfers the risk of investing in the private fund from the record owner" would be the beneficial owner for purposes of Sections 3(c)(1) and (7) of the Investment Company Act and for purposes of the foreign private adviser exemption under the Advisers Act.

Section 766 of the Dodd-Frank Act authorizes the SEC to determine that the owner of a security-based swap is the beneficial owner of the equity security only "to the extent that the Commission, by rule, determines after consultation with the prudential regulators and the Secretary of the Treasury, that the purchase or sale of the security based swap, or class of security-based swap, provides incidents of ownership comparable to direct ownership of the equity security."

We believe the proposed definition in the Exemptions Release is not consistent with this approach because the proposed definition would deem the swap owner to be the

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[9] *Staff Responses to Questions About the Custody Rule*, Question VI.11., available at http://sec.gov/ divisions/investment/custody_faq_030510.htm (updated as of Sep. 9, 2010).

[10] *Id*.

[11] We note that Section 208(d) of the Advisers Act should address concerns about the potential for abuse of such a position.

beneficial owner because of the transfer of economic risk, which we believe does not rise to the level of "incidents of ownership comparable to direct ownership." The swap owner, for example, does not have voting rights with respect to the fund, nor would it necessarily have the same types of redemption or transparency rights that a direct owner would have. Though Section 766 does not expressly limit the SEC's authority to determine that a swap holder is a beneficial owner for purposes of the Advisers Act or the Investment Company Act, we believe the SEC should adopt a consistent test for determining when the owner of a swap is the beneficial owner of the underlying security.[12]

We further note that, in applying such a standard, private funds and the investment advisers to those funds will need to rely on representations made by investors in their subscription agreements to purchase interests in a private fund. As such, we request that the SEC confirm in the final rule that a private fund adviser or private fund may rely on good faith on the representations made by investors, so long as the adviser and fund do not know or have reason to know that a representation is not correct.

Calculation of "regulatory assets under management"

Investment advisers that wish to rely on the *de minimis* exemption from registration found in Section 203(m) of the Advisers Act will be required to calculate their regulatory assets under management in accordance with the rules proposed in the companion SEC release, "Rules Implementing Amendments to the Investment Advisers Act of 1940" (the "Implementation Release").[13] MFA is submitting a separate comment letter to the SEC in response to the Implementation Release.[14] As discussed in more detail in that letter, we recommend that the SEC continue to permit investment advisers to determine whether to include in their calculation of regulatory assets under management the types of assets and advisory services that generally would not subject a firm to regulation under the Advisers Act, including family accounts, proprietary accounts, and accounts for which the manager receives no compensation. Advisers should be permitted to make this determination with respect to such accounts that are managed as part of a pooled investment vehicle (*e.g.*, a private fund interest of a principal of the manager, that is not charged a fee) or as a separate account structure. Further, we believe that this critical determination should continue to be based on a straightforward, easy to use calculation of a manager's net assets rather than a gross assets calculation, because the latter is likely to be complex and could lead to significant uncertainty as to whether an adviser has to register with the SEC. Finally, we believe that advisers to

[12] To the extent the SEC is concerned about investment advisers or their funds using swap agreements to evade the application of the Advisers Act or the Investment Company Act, Section 208(d) of the Advisers Act and Section 48(a) of the Investment Company Act, respectively, address those concerns by prohibiting persons from doing things indirectly that would violate the statute if done directly.

[13] Investment Advisers Act Release No. 3110 (Nov. 19, 2010).

[14] A copy of MFA's letter in response to the Implementing Release is available at: www.managedfunds.org.

calculate regulatory assets under management for a private fund that it manages using fair value, or in accordance with the valuation methodology that is described in a private fund's offering materials.

Conclusion

MFA appreciates the opportunity to comment on the Exemptions Release. We strongly support a comprehensive registration framework for investment advisers that limits gaps in SEC oversight. We encourage the SEC to consider providing additional guidance along the lines discussed above, which we believe will help achieve this shared goal in an effective and efficient manner.

If you have any questions regarding any of these comments, or if we can provide further information with respect to these or other regulatory issues, please do not hesitate to contact Stuart J. Kaswell or me at (202) 730-2600.

Respectfully submitted,

/s/ Richard H. Baker

Richard H. Baker

President and CEO