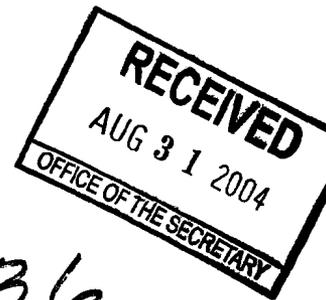




DENALI ASSET MANAGEMENT, LLLP



36

Friday, August 27<sup>th</sup> 2004

Mr. Jonathan G. Katz, Secretary  
U.S. Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20546-0609

Re: File No. S7-30-04  
Proposed Rule: Registration Under The Advisers Act of Certain Hedge Fund Advisers

Ladies and Gentlemen:

We are submitting the following comments in response to the recent proposal from the SEC's staff to require registration of certain hedge fund advisers. By way of background, Denali Asset Management, LLLP is a registered Commodity Trading Adviser and Commodity Pool Operator that currently manages approximately \$500 million in assets. While the vast majority of our trading occurs in the futures and foreign exchange markets, we also invest on a limited basis in individual equities, equity mutual funds and over-the-counter derivatives products. As such, it appears that we would be subject to the proposed regulation in its current form.

While we are sympathetic to the need for the Commission to require registration of those hedge fund advisers who are unregistered with any investment regulator, we respectfully disagree with the staff's contention that those hedge fund advisers already registered with the Commodity Futures Trading Commission (CFTC) and the National Futures Association (NFA) should also be required to register with the SEC. Please allow us to explain the reasons we believe this position is wrong:

1. Currently, we undergo an extensive audit from the National Futures Association approximately every two to three years. This audit covers everything from evaluating investor suitability and how we market our funds to the manner in which performance is calculated. Based upon the SEC's annual report for 2003, in the last year the Commission's staff audited 1,556 investment advisers of the 8,000 registered, for a frequency of roughly one audit per adviser every 5.14 years. It is difficult to see how subjecting an adviser already registered with the CFTC/NFA to this extra layer of review every four or five years is going to improve upon the regulatory procedures already in place.
2. The staff's assertion that the CFTC and the NFA would not bring adequate expertise outside of the area of futures and foreign exchange begs the question of whether the SEC is committed to training its own examiners how to value futures, foreign exchange positions, exotic foreign exchange options, over-the-counter derivatives, and the like. In fact, many of the more exotic instruments traded by some hedge funds are much more similar to those instruments already regulated in the futures and foreign exchange markets. Consequently, we believe that futures regulators may be better equipped to evaluate these positions.
3. The observation made by the staff that the CFTC is taking steps to reduce its oversight of certain types of hedge funds is irrelevant to whether the SEC should require those funds already registered with the CFTC to be subject to SEC oversight. If a hedge fund is



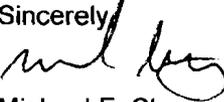
DENALI ASSET MANAGEMENT

structured intentionally to avoid CFTC regulation, then by all means the fund should be regulated by the SEC.

In lieu of the staff's proposal, we suggest an exemption from the proposed registration for those advisers who are already registered with the NFA and CFTC and who have less than 25% of assets under management invested in securities which fall under the SEC's authority. In order to ensure that advisers are honest with this ratio, the NFA and/or CFTC could require a periodic filing from advisers indicating the amount invested in these securities. This ratio could then be audited along with other information as required by current regulations. This framework will serve not only to provide the SEC with regulatory authority over those advisers whose strategies participate significantly in the securities markets, but also to provide some insight into the extent of adviser participation in these markets.

Again, we appreciate the Commission's efforts to increase oversight of unregistered investment advisers. Nevertheless, we do not believe it serves the interests of the investing public to unduly subject those advisers already registered with the CFTC and the NFA to additional registration and audit requirements as proposed. While it is unclear how the proposed regulation will improve upon the regulatory framework in place for advisers already registered with the CFTC and the NFA, it is clear that the SEC will be taxing its already strained resources to duplicate an activity that has already been paid for by the American investing public.

Thank you for providing us with this opportunity to share our thoughts.

Sincerely,  
  
Michael E. Strupp  
Vice President

Denali Asset Management, LLLP

---