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

January 18, 2011

Via Electronic Submission: http://comments.cftc.gov

David A. Stawick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: RIN No. 3038-AC96: Notice of Proposed Rulemaking on Implementation of Conflicts of Interest Policies and Procedures by Swap Dealers and Major Swap Participants; Notice of Proposed Rulemaking on Regulations Establishing and Governing the Duties of Swap Dealers and Major Swap Participants; Proposed Rule regarding Designation of a Chief Compliance Officer; Required Compliance Policies; and Annual Report of a Futures Commission Merchant, Swap Dealer, or Major Swap Participant.

Dear Mr. Stawick:

Managed Funds Association ("**MFA**")[1] appreciates the opportunity to provide comments on the following on the rulemakings proposed by the Commodity Futures Trading Commission related to the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**") (the "**Commission**"):

(i) Notice of Proposed Rulemaking regarding the Regulations Establishing and Governing the Duties of Swap Dealers and Major Swap Participants,[2]

(ii) Notice of Proposed Rulemaking on the Implementation of Conflicts of Interest Policies and Procedures by Swap Dealers and Major Swap Participants,[3] and

(iii) Proposed Rule regarding the Designation of a Chief Compliance Officer; Required Compliance Policies; and Annual Report of a Futures Commission Merchant, Swap Dealer, or Major Swap Participant.[4]

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[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 $1.7 trillion invested in absolute return strategies. MFA is headquartered in Washington, D.C., with an office in New York.

[2] 75 Fed. Reg. 71397 (Nov. 23, 2010) (the "**Proposed Duties Rules**").

[3] 75 Fed. Reg. 71391 (Nov. 23, 2010) (the "**Proposed Conflicts Rules**").

MFA supports the Commission's general approach to establish business conduct standards with which swap dealers ("**SDs**") and major swap participants ("**MSPs**") must comply. We believe the Rulemakings are useful measures that will help to reduce risk, increase transparency and promote market integrity within the financial system. We look forward to working closely with the Commission to promulgate rules that serve the public interest by establishing a regime that imposes appropriate duties and reduces conflicts of interest for SDs and MSPs.

I. Summary

MFA urges the Commission to adopt rules and guidance that effectively clarify the rights and obligations of market participants. We believe that greater guidance will clarify the lines between permissible and impermissible conduct and allow market participants to develop proper internal controls. To that end, we recommend that:

(i) With respect to the Proposed Duties Rules, the Commission clarify that the rule does not impose any new (a) fiduciary obligations or duties (*i.e.*, duties beyond those to which participants in the futures and derivatives markets would otherwise be subject to by agreement or by operation of common law) or (b) supervisory duties on market participants;

(ii) With respect to the Proposed Conflicts Rules, the Commission establish a clear separation between the research and trading departments, so that the criteria for clearing membership are objective and risk-based; and

(iii) With respect to the CCO Proposed Rules, the Commission clarify that the chief executive officer ("**CEO**") or the firm itself must certify and submit the annual report, not the chief compliance officer ("**CCO**") individually.

II. Proposed Duties Rules

MFA respectfully requests that the Commission explicitly clarify and confirm that the Proposed Duties Rules do not impose any new duties, including duties of disclosure, inquiry, diligence or supervision, other than those that exist or are created under contract, under other laws or by operation of common law. In particular, proposed Section 23.602[5] (the "**Diligent Supervision Rule**") provides that each SD and MSP must diligently supervise, and must establish and maintain a system to supervise, all activities relating to its business performed by its employees. In addition, such system must be reasonably designed to achieve compliance with the requirements of the CEA and Commission regulations. This rule is similar to the National Futures Association's ("**NFA**") Supervision Rule[6] with respect to futures commission merchants ("**FCMs**").

We are concerned that without the requested clarification, the Proposed Duties Rules, and in particular the Diligent Supervision Rule, may impose fiduciary and supervisory obligations on MSPs, and in some cases SDs, similar to those that the NFA imposes on FCMs with respect to third parties.

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[4] 75 Fed. Reg. 70881 (Nov. 19, 2010) (the "**CCO Proposed Rules**" and, collectively with the Proposed Duties Rules and the Proposed Conflicts Rules, the "**Rulemakings**").

[5] Proposed Section 23.602 implements Section 4s(h)(1)(B) of the Commodity Exchange Act, as amended (the "**CEA**"), added by Section 731 of the Dodd-Frank Act.

[6] NFA Compliance Rule 2-9.

Further, the Commission should make it explicitly clear that an MSP that is not an SD is not subject to *any* of the counterparty duties to which an SD is subject. The Proposed Duties Rules imply equivalence between an MSP and an SD, but this should not be the case. Although the Dodd-Frank Act imposes similar obligations on SDs and MSPs,[7] it does not state that the Commission must subject SDs and MSPs to identical regulation. SDs and MSPs are entirely different entities, as the definitions of such terms in the Dodd-Frank Act[8] make clear. Generally, SDs are market makers, while MSPs are non-dealers with substantial positions in swaps. Thus, since there are fundamental differences in the businesses, structures and other characteristics of SDs and MSPs, the Commission should not use the same regulatory regime to oversee such different market participants. Rather, the Commission should focus MSP regulation on default risk and focus SD regulation on market making and pricing and sales practices, in addition to default risk.

Moreover, simply because a market participant is an MSP and has a large portfolio in a given asset class, should not mean it has customers to whom it owes any duty. For example, if the MSP is merely an investor who becomes an MSP due to the size of its position in a particular asset class, it should not be treated any differently from any other investor that does not come within the MSP designation. Accordingly, MSPs should not bear the burdens of an SD that has customers – the entire apparatus from know-your-customer to best execution. Such a result would create barriers to competition and the evolution of an open trading marketplace.

We believe the imposition of the same duties on MSPs (or SDs acting on an arm's-length basis) as those the Commission or the NFA requires from FCMs and other SDs would be inappropriate. Because an MSP can conduct its business on an arm's-length basis with counterparties and not enter an advisory role, in such circumstances, the Commission should not hold it to a fiduciary standard similar to that of an FCM or an SD that is not acting at arm's-length. It is a tenet of basic corporate law that fiduciary duties normally do not arise in situations where the parties conduct business at arm's-length.[9]

An MSP that is not also an SD does not act in any sort of advisory role with its counterparties and generally does not create a relationship of higher trust with its counterparties. It is merely a counterparty engaging in an arm's-length transaction. To the extent that an MSP transacts at arm's-length, we believe the Commission should explicitly clarify that no new duties flow from any of the Proposed Duties Rules beyond those traditionally understood.

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[7] *See* Section 731 of the Dodd-Frank Act, which imposes various registration and business conduct requirements on SDs and MSPs.

[8] *See* Section 721(a)(21) of the Dodd-Frank Act, which defines the term "Swap Dealer"; *see also* Section 721(a)(16) of the Dodd-Frank Act, which defines the term "Major Swap Participant".

[9] EBC I, Inc. v. Goldman Sachs & Co., 5 N.Y.3d 11, 20 (2005) (internal citations omitted), which states that a fiduciary relationship "exists between two persons when one of them is under a duty to act for or to give advice for the benefit of another upon matters within the scope of the relation". Such a relationship, necessarily fact-specific, is grounded in a higher level of trust than normally present in the marketplace between those involved in arm's-length business transactions. Generally, where parties have entered into a contract, courts look to that agreement "to discover . . . the nexus of [the parties'] relationship and the particular contractual expression establishing the parties' interdependency". "If the parties . . . do not create their own relationship of higher trust, courts should not ordinarily transport them to the higher realm of relationship and fashion the stricter duty for them". However, it is fundamental that fiduciary "liability is not dependent solely upon an agreement or contractual relation between the fiduciary and the beneficiary but results from the relation".

III. Proposed Conflicts Rules

With respect to SDs, MFA supports the informational partitions between the research and trading departments in the Proposed Conflicts Rules. We believe those partitions will help to achieve the Commission's goal of constructing "structural and institutional safeguards" to minimize the potential conflicts of interest that could arise with SDs. In addition, we agree with the Commission's view that such partitions are necessary to the extent that SDs prepare research reports that are publicly disseminated.

However, although we support the Proposed Conflicts Rules, we seek additional guidance from the Commission regarding the scope of the informational partitions. The Proposed Conflicts Rules speak in terms of, among other things: (i) the communication between non-research personnel and research analysts; (ii) research analysts not subject to the supervision or control of any employee in the business trading unit or clearing unit; and (iii) the lack of influence or control by employees engaged in pricing, trading or clearing activities over the evaluation or compensation of research analysts. We suggest that the Commission provide more clarity around these rules by further describing the bright lines of separation. For example, may an SD house its research department and trading department in the same building or on the same floor? Must there be different key cards for entry into each department?

MFA supports the portions of the Proposed Conflicts Rules that would prohibit SDs and MSPs from directly or indirectly interfering with, or attempting to influence, the decision of any affiliated clearing member of a derivatives clearing organization with regard to clearing services and activities. Further, we support the Proposed Conflicts Rules' informational partitions required between business trading personnel and personnel of an affiliated clearing member. We believe that these requirements will result in an objective and risk-based evaluation of market participants to determine their appropriateness to become clearing members. We believe the best way to create non-discriminatory fair access to clearing membership is to ensure that such decisions are made objectively based on the risk such proposed clearing member poses, rather than based on biased, anti-competition factors. In our view, such clearing membership access is crucial because of its significance to the greater mandatory clearing required by the Dodd-Frank Act.

IV. CCO Proposed Rules

The CCO Proposed Rules provide that SDs and MSPs must furnish to the Commission an annual report describing, among other things, compliance with the CEA, the Commission's regulations and each of the registrant's compliance policies. MFA respectfully suggests that the Commission provide in the final rules that the CEO or the firm itself must submit and certify the annual report, rather than the CCO individually. To the extent submission and certification of the annual report is an obligation, it should be an obligation of the entity itself.

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MFA thanks the Commission for the opportunity to provide comments regarding the Rulemakings. Please do not hesitate to call Carlotta King or the undersigned at (202) 730-2600 with any questions or comments the Commission or its staff might have regarding this letter.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President & Managing Director,
General Counsel

cc: The Hon. Gary Gensler, Chairman
The Hon. Michael Dunn, Commissioner
The Hon. Bart Chilton, Commissioner
The Hon. Jill E. Sommers, Commissioner
The Hon. Scott D. O'Malia, Commissioner