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

September 29, 2017

Via Website Submission

Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: Project KISS

Dear Mr. Kirkpatrick:

Managed Funds Association[1] ("**MFA**") appreciates the opportunity to submit comments to the Commodity Futures Trading Commission (the "**CFTC**" or "**Commission**") in response to the Commission's request for input on simplifying CFTC rules.[2] MFA strongly supports the Commission's initiative on simplifying CFTC regulations to make them "less burdensome and less of a drag on the American economy."[3] The U.S. derivatives markets are important to the investment and hedging strategies of MFA members. In addition, their trading adds important liquidity to the marketplace for farmers, ranchers and other commercial end-users who use the derivatives markets to manage commercial risk. As such, MFA members support regulations that promote fair and efficient markets. We believe that many objectives of the Commodity Exchange Act ("**CEA**") and the Commission can be achieved in less burdensome ways that are at least as effective as current approaches. In addition to MFA's letter of June 6, 2017 to acting Chair

[1] Managed Funds Association (MFA) 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, North and South America, and many other regions where MFA members are market participants.

[2] CFTC Requests Public Input on Simplifying Rules, CFTC press release, May 3, 2017, available at: http://www.cftc.gov/PressRoom/PressReleases/pr7555-17.

[3] *See id.*

Giancarlo on regulatory recommendations[4] ("**MFA June 2017 Letter,**" attached as **Appendix**), MFA submits this letter to provide further recommendations for enhancing regulatory efficiency.

I. SUMMARY

In this letter, we raise several suggestions for regulatory improvements in a number of subject areas under the Project KISS initiative, which we believe will help the Commission achieve its regulatory objectives by making regulation simpler, more effective, and less costly and burdensome for compliance and oversight purposes. We would welcome the opportunity to discuss our suggestions in greater detail.

A. Registration

1. Avoiding Duplicative Registration

i. **Commodity Pool Operator ("CPO") Registration.** MFA recommends that the CFTC reinstate an exemption from CPO registration for a CPO of a private commodity pool, provided that such CPO is registered as an investment adviser with the Securities and Exchange Commission ("**SEC**") or affiliated with an SEC-registered investment adviser—a narrower exemption than former Rule 4.13(a)(4).

ii. **Commodity Trading Advisor ("CTA") Registration.** MFA recommends that the CFTC and the SEC should each adopt a rule or provide interpretive guidance that would subject a firm to advisor/adviser registration with either the CFTC or SEC, depending on whether it is primarily engaged in the business of advising on trading in commodity interests or securities.

2. **Reviewing Rule 4.13(a)(3).** As the CFTC and the SEC work to rationalize and avoid dual registration, MFA recommends that the Commission exclude compo swaps from calculation under Rule 4.13(a)(3) with respect to determining a pool's commodity interest position, and to issue related guidance. MFA recommends that the Commission issue guidance setting forth that in calculating the Rule 4.13(a)(3) *de minimis* trading exemption, a CPO should conduct the calculation for a commodity pool including any wholly owned subsidiary of the commodity pool; and that the CPO need not conduct the Rule 4.13(a)(3) exemption calculation with respect to a wholly owned subsidiary on its own.

[4] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to the Honorable J. Christopher, Chairman, CFTC, on June 6, 2017, regarding Managed Funds Association Regulatory Priorities, attached as **Appendix** and available at: https://www.managedfunds.org/wp-content/uploads/2017/06/MFA-Letter-to-Acting-Chair-Giancarlo-Appendix.pdf.

3. Simplifying Regulation Through Interpretive Guidance

i. **Registration & Interpretation of Commodity Pool Operator.** MFA recommends that the Commission: (1) adopt a more streamlined approach to registration or CPO delegation by issuing guidance analogous to the SEC's umbrella registration; and (2) provide consistent treatment to natural persons serving on the governing body of a commodity pool and issue guidance that members of an investment company's or commodity pool's board of directors or other governing body are not considered to be CPOs.

ii. Interpretation of Commodity Pool. MFA recommends that the Commission issue guidance providing that a wholly owned subsidiary of a commodity pool is not a separate commodity pool. In the alternative, MFA recommends that the Commission provide guidance that for purposes of CPO exemptions from registration or exclusions, and for regulatory reporting purposes, a wholly owned subsidiary of a commodity pool need not be considered a separate commodity pool.

iii. Updating Qualified Eligible Person ("QEP") Status. MFA recommends that the CFTC issue interpretive relief or guidance that an employee in certain technology-related roles at a firm with a technologically-driven trading model may satisfy the Rule 4.7(a)(2)(viii)(A)(4)(ii) prior work experience requirement through work experience at a technology company, rather than exclusively at a financial services company.

B. Reporting

1. Forms CPO-PQR and CTA-PR. MFA plans to submit in a separate submission to the Commission and the SEC detailed recommendations for a single and simpler systemic risk reporting form for CPOs, CTAs and investment advisers.

2. Reduce Complexity of Cleared Swap Reporting Requirements. MFA recommends that the CFTC eliminate alpha swap reporting requirements to reduce the reporting complexities of its cleared swaps reporting regime and to streamline the data actually reported to swap data repositories ("**SDRs**") without sacrificing the amount of information available to the CFTC regarding the entire life cycle of a swap. As an alternative to eliminating SDR reporting for cleared swaps, MFA suggests that the CFTC consider simplifying the regulatory reporting infrastructure by making registered derivatives clearing organizations *i.e.*, central counterparties ("**CCPs**") responsible for maintaining data on their cleared swaps, and have SDRs maintain data for uncleared swaps.

C. Executing. MFA recommends that the CFTC improve the legal framework for swaps trading on registered swap execution facilities ("**SEFs**") and designated contract markets ("**DCMs**") by:

1. Allowing investors more flexibility in how they trade swaps while: (i) enabling true impartial access to SEFs and execution methods for all eligible participants, and (ii) preserving crucial requirements for pre-trade price transparency, price competition, and a multiple-to-multiple trading system or platform;

2. Assuming responsibility for determining when particular swap contracts have to be SEF-traded while carefully considering the distinct liquidity issues for any such contract; and

3. Simplifying and codifying with certain changes, the existing universe of CFTC staff guidance and no-action relief that the CFTC used to smooth the implementation of the SEF framework.

4. Requiring SEFs to make public disclosures regarding important aspects of their offerings, including trading protocols, fees, and governance.

D. Miscellaneous

1. **Repeal Segregation Interpretation 10-1 for Futures and Options Transactions.** MFA recommends that the Commission repeal the Division of Clearing and Intermediary Oversight's ("**DCIO**") Amendment of Interpretation ("**Segregation Interpretation 10–1**")[5] to the Financial and Segregation Interpretation No. 10 on the Treatment of Funds Deposited in Safekeeping Accounts ("**Segregation Interpretation 10**")[6] for futures and options transactions (together, "**Futures**").

2. **Initial Margin Requirements Should be Tailored to the Risk of Certain Non-Clearable Swaps.** MFA recommends that the CFTC recalibrate and appropriately tailor its initial margin requirements for uncleared swaps to reflect the actual risk posed by certain non-clearable swap products, such as total return swaps for complex equity trades.

3. **Liquidation Periods Should be More Closely Calibrated to Product Liquidity.** MFA suggests that the CFTC work with the Working Group on Margining Requirements of the Basel Committee on Banking Supervision and the International Organization of Securities Commissions ("**Basel-IOSCO WGMR**"), the SEC, the Board of Governors of the Federal Reserve ("**Fed**") and the other U.S. prudential regulators to re-examine market practice and historical data to more accurately calibrate minimum liquidation time periods to account for a product's

[5] 70 Fed. Reg. 24768 (May 11, 2005), available at: http://www.gpo.gov/fdsys/pkg/FR-2005-05-11/pdf/05-9386.pdf.

[6] *See* Comm. Fut. L. Rep. (CCH) 7120 (May 23, 1984) available at: http://www.cftc.gov/tm/finseginterp_10.htm.

liquidity profile, regardless of whether the product is a futures contract, a cleared swap, or an uncleared swap.

4. **Organization of CFTC Staff Letters.** MFA recommends that the Commission enhance the organization of its website and CFTC staff letters to facilitate compliance of CFTC regulations by market participants.

II. DISCUSSION OF ISSUES

A. Registration

As the Commission is aware, many investment management firms are registered with the SEC as investment advisers and registered with the CFTC as CPOs and/or CTAs. The U.S. is in the minority jurisdiction in bifurcating the regulation of financial markets and subjecting investment management firms to overlapping and redundant systems of registration and oversight.[7] Subjecting investment managers to two similar, but slightly different, regulatory frameworks have made regulation inefficient and extremely burdensome. Similarly, we believe that such duplicative regulation is an unnecessary use of government resources. We believe the U.S. should adopt a regulatory framework in which investment management firms have a primary regulator, rather than register with both the CFTC and the SEC. To this end, we urge the CFTC and the SEC to rationalize registration and oversight of investment managers and provide recommendations to the Commission with respect to the CEA and CFTC regulations. In the same vein, we have also provided recommendations to the SEC with respect to the Investment Advisers Act of 1940 ("**Advisers Act**") and regulations thereunder.

1. Avoiding Duplicative Registration

i. CPO Registration

MFA believes the CFTC should reinstate an exemption from CPO registration for a CPO of a private commodity pool, provided that such CPO is registered as an investment adviser with the SEC or affiliated with an SEC-registered investment adviser—a narrower exemption than former Rule 4.13(a)(4).[8] Given the CPO and CTA framework under the CEA, it is important in

[7] Fund managers in other countries are only subject to one national regulator, such as the UK's Financial Conduct Authority, France's Autorité des Marchés Financiers, Hong Kong's Securities & Futures Commission, and Singapore's Monetary Authority of Singapore, amongst many others.

[8] Many investment advisers have affiliated entities, which may or may not be separately registered as investment advisers, CTAs, or CPOs, that provide services to private investment funds managed by the registered adviser. For example, a registered investment adviser that manages a private investment fund may have a separate, affiliated entity that is the general partner and CPO of the fund. The SEC has recognized that for a variety of reasons "advisers to private funds may be organized as a group of related advisers that are separate legal entities but effectively operate as—and appear to investors and regulators to be—a single advisory business." The SEC exempts a registered investment adviser's affiliates from independently registering as investment advisers, provided that certain conditions are met and the registered investment adviser makes an "umbrella registration" filing in its Form ADV. *See* Final Form ADV and Investment Advisers Act Rules, 81 Fed. Reg. 60,418 (Sept. 1, 2016), available at: https://www.gpo.gov/fdsys/pkg/FR-2016-09-01/pdf/2016-20832.pdf. The SEC's rulemaking on Final Form ADV

developing a regulatory structure with a primary regulator that regulators take into consideration all three registration constructs—CPO, CTA, and investment adviser—and generally how investment management firms are incorporated. In this way, an investment management firm, for example, that is structured as a limited partnership does not result in registering a limited partner with the SEC as an investment adviser and registering its general partner as a CPO. We believe that providing an investment management firm that is registered with the SEC as an investment adviser with an exemption from registration as a CPO with respect to private commodity pools may be the most straight forward type of exemption for registrants. Such exemption will reduce duplicative registration and regulatory requirements with the SEC as well as the corresponding regulatory expenses and make regulation efficient, effective, and appropriately tailored for investment managers.

MFA also recognizes that the current CPO registration framework is overly broad in its extraterritorial reach and encourages the CFTC to work with the Alternative Investment Management Association ("**AIMA**") and other industry associations and foreign investment advisers to adopt a reasonable exemption for foreign investment advisers that would not be covered by any relief granted in response to our request for relief for SEC-registered investment advisers or their affiliated entities. MFA discusses the above recommendation in the MFA June 2017 Letter and refers the Commission Staff to this letter, attached as an Appendix.[9]

ii. CTA Registration

In addition, we believe the CFTC and the SEC should each adopt a rule or provide interpretive guidance that would subject a firm to advisor/adviser registration with either the CFTC or SEC, depending on whether it is primarily engaged in the business of advising on trading in commodity interests or securities. This framework would promote efficiency, reduce overlap, help prioritize regulatory resources, and reduce compliance costs to managers and their customers.

Under current CFTC and SEC rules, many private fund managers register with both agencies due to their providing investment advice to clients with respect to securities and commodity interests. Such dual registration results in overlapping and duplicative regulatory requirements that impose unnecessary additional costs on managers and their investors with little additional benefit.

The current statutory framework is, in fact, designed for regulators to minimize dual registration. Section 4(m)(3) of the CEA provides an exemption from CFTC registration for a CTA that is registered with the SEC as an investment adviser and whose business does not consist

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and Investment Advisers Act Rules codified prior No-Action relief. *See ABA Subcommittee on Private Investment Entities*, SEC No-Action Letter (Dec. 8, 2005) and *American Bar Association Section of Business Law*, SEC No-Action Letter (Jan. 18, 2012). Similarly, the CFTC has allowed certain affiliated entities, to claim an exemption from CPO registration by delegating the CPO function to an affiliated registered CPO and meeting certain requirements. We believe the CFTC should include legal entities affiliated with a registered investment adviser that provide services to the same private investment fund to be within the scope of the exemption.

[9] MFA June 2017 Letter *supra* n. 4 at p. 7-10.

primarily of acting as a CTA. Section 203 of the Advisers Act provides an analogous exemption from SEC registration for a CFTC-registered CTA whose business does not consist primarily of acting as an investment adviser.[10]

In addition, Section 403 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank Act**") provided a new exemption from SEC registration for a CFTC-registered CTA that advises a private fund, unless the business of the CTA should become predominantly the provision of securities-related advice.[11] This exemption reflects Congress's recognition that CTAs to private funds or managed accounts, which are primarily engaged in the business of providing advice regarding commodity derivatives and are already subject to a comprehensive registration and regulatory framework, do not have to be dually registered.

Despite this clear statutory framework, however, the CFTC and SEC have not yet adopted rules or issued guidance to allow firms to avail themselves of these statutory exemptions. MFA encourages the Commission and the SEC to adopt rules or guidance to eliminate dual registration and clarify the criteria relevant to determining whether an entity is primarily engaged in the business of providing advice regarding commodity derivatives and subject to registration as a CTA or providing advice regarding securities and subject to registration as an investment adviser.[12]

In this regard, we recommend that the CFTC and SEC consider the factors addressed in the Peavey Commodity Futures Fund No-Action letter ("**Peavey**").[13] We believe the standard set in Peavey to determine the primary business engagement of a fund for purposes of determining whether it is an investment company under Section 3(b)(1) of the Investment Company Act of 1940 ("**Investment Company Act**") is a fair and flexible standard for determining whether an advisor registered with the CFTC is primarily acting as an investment adviser or its business has become predominantly the provision of securities-related advice. In addition, we believe the same analysis may be applied for purposes of determining whether an adviser registered with the SEC is primarily acting as a CTA pursuant to Section 4(m)(3) of the CEA.

Section 3(b)(1) of the Investment Company Act excludes from the definition of investment company any issuer engaged primarily in a business or businesses other than investing, reinvesting, owning, holding or trading in securities, either directly or through wholly-owned subsidiaries.

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[10] Advisers Act Section 203(b)(6)(A).

[11] Advisers Act Section 203(b)(6)(B).

[12] In advocating for the simplification of CFTC and SEC registration for private fund managers, MFA has made the analogous request to SEC Chairman Clayton. *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to the Honorable Walter J. Clayton, Chairman, SEC, on May 18, 2017, regarding Managed Funds Association Regulatory Priorities, available at: https://www.managedfunds.org/wp-content/uploads/2017/05/MFA-Regulatory-Priorities-Letter-to-SEC-Chairman-Clayton.pdf.

[13] *See* Peavey Commodity Futures Fund, SEC No-Action Letter (June 2, 1983) (determining the primary engagement of a fund for purposes of the Investment Company Act). *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).

Under the Peavey analysis, in determining whether an entity investing in futures was otherwise primarily engaged in the business of investing in securities so as to be an investment company, the SEC considered the composition of the entity's assets, the sources of its income, the area of business in which it anticipated realization of the greatest gains and exposure to the largest risks of loss, the activities of its officers and employees, its representations, its intentions as revealed by its operations, and its historical development. The SEC stated that of greatest importance in its analysis was the area of business in which the entity anticipated realization of the greatest gains and exposure to the largest risks of loss as revealed by its operations on an annual or other suitable basis.[14]

We believe the factors under the Peavey analysis are appropriate for determining the primary business activity of an advisor and whether it should be registered with the CFTC or SEC. Accordingly, we recommend that the CFTC and SEC, through rulemaking or guidance, indicate how a firm would be able to determine whether it is acting primarily as a CTA or an investment adviser, based on the Peavey analysis – the composition of the adviser's assets, the sources of its income, the area of business in which the adviser anticipates realization of the greatest gains and exposure to the largest risks of loss, the activities of its officers and employees, its representations, its intentions as revealed by its operations, and its historical development.[15]

2. Reviewing Rule 4.13(a)(3)

MFA believes that as the CFTC works with the SEC to rationalize and avoid dual registration the Commission should provide relief to investment advisers that might otherwise need to register as CPOs. MFA requests that the Commission exclude "compo" equity total return swaps ("**compo swaps**") from calculation under Rule 4.13(a)(3) with respect to determining a pool's commodity interest position; and to issue related guidance. MFA refers the Commission to the MFA June 2017 Letter for additional details. In addition, MFA supports the CFTC staff's continued provision of relief under Rule 4.13(a)(3) to operators of fund-of-funds as the Commission works with the SEC to rationalize registration of fund managers.[16] It will be important for a rationalized registration and reporting framework to take into consideration the treatment of operators and advisers of fund-of-funds, and where possible seek reporting information directly from operators of, or advisers to, underlying funds.

Notwithstanding MFA's request that the CFTC and the SEC rationalize registration of investment management firms, MFA believes that in interpreting Rule 4.13(a)(3) the Commission should not consider a wholly owned subsidiary of a commodity pool to be a separate commodity

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[14] For example, a company's anticipated gains and losses in futures trading as compared to its anticipated gains and losses on its government securities and other securities.

[15] *See also* Managed Futures Association, SEC No-Action Letter (July 15, 1996) (applying a "look through" analysis in determining the primary business of a commodity pool that invests in other commodity pools). Managed Futures Association subsequently changed its name to Managed Funds Association.

[16] *See* CFTC No-Action Letter No. 12-38 (Nov. 29, 2012), available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/12-38.pdf.

pool. Rather, the Commission should allow a CPO to make the Rule 4.13(a)(3) *de minimis* trading calculation with respect to all the assets of a commodity pool, including any wholly owned subsidiaries. As stated in the Commission's 2003 adopting release for Rule 4.13(a)(3), the purpose of the rule is to provide an exemption where commodity interest trading is limited and pool participants are sophisticated.[17] As such, we think it is appropriate to consider a pool participant's overall exposure to commodity interests, as opposed to the legal structure through which a CPO trades for a commodity pool. Otherwise, the operator of any commodity pool that has a wholly owned subsidiary that engages only in commodity interest trading needs to register as a CPO, even if the wholly owned subsidiary is only engaged in one futures contract. We do not believe this is a rational outcome. Please see below for further discussion and recommendations regarding wholly owned subsidiaries of commodity pools.

Accordingly, MFA recommends that the Commission exclude compo swaps from calculation under Rule 4.13(a)(3) with respect to determining a pool's commodity interest position, and to issue related guidance. MFA recommends that the Commission issue guidance setting forth that in calculating the Rule 4.13(a)(3) *de minimis* trading exemption, a CPO should conduct the calculation for a commodity pool including any wholly owned subsidiary of the commodity pool; and that the CPO need not conduct the Rule 4.13(a)(3) exemption calculation with respect to a wholly owned subsidiary of a commodity pool.

3. Simplifying Regulation Through Interpretive Guidance

i. Registration & Interpretation of Commodity Pool Operator

MFA believes the Commission should adopt a registration framework analogous to the SEC's "umbrella registration" system,[18] rather than require affiliated entities to delegate the CPO function to a registered CPO or individually register as a CPO.[19] For a variety of reasons, operators of privately-offered commodity pools may be organized as a group of related operators and/or advisers that are separate legal entities but effectively operate as—and appear to investors and regulators to be—a single CPO or investment management business. A streamlined registration system would simplify regulation and reduce administrative burden for investment management firms. In addition, the CFTC should take a consistent position with respect to how it treats members of an investment company's board of directors. Just as the Commission has concluded that a member or members of a registered investment company's board of directors would not be considered as CPOs, the Commission also should take the position and issue guidance that it will

[17] *See* Additional Registration and Other Regulatory Relief for Commodity Pool Operators and Commodity Trading Advisors, 68 Fed. Reg. 47,221 (Aug. 8, 2003), available at: https://www.gpo.gov/fdsys/pkg/FR-2003-08-08/pdf/03-20094.pdf.

[18] *See* SEC Final Form ADV and Investment Advisers Act Rules, 81 Fed. Reg. 60,418 (Sept. 1, 2016), available at: https://www.gpo.gov/fdsys/pkg/FR-2016-09-01/pdf/2016-20832.pdf.

[19] *See infra* n. 22.

not consider a member or members of a private investment company's board of directors to be CPOs.[20]

With umbrella registration, the SEC allows a single registration by a *filing adviser* and one or more *relying advisers* who advise only private funds and certain separately managed account clients and collectively conduct a single advisory business.[21] The SEC requires the filing adviser to file and update as required a registration statement relating to, and including all information concerning, the filing adviser and each relying adviser. Accordingly, the SEC has information about the various advisers, without the need to file individual Forms ADV for each entity. The CFTC staff, with respect to affiliated operators that operate or serve the same privately-offered commodity pool, has issued No-Action letters allowing a CPO to delegate the CPO function to a registered CPO under certain fact patterns.[22] While we appreciate the relief the CFTC staff has issued, we are concerned that the relief is limited and is only able to address certain fact patterns as evidenced by subsequent, individual, No-Action relief letters issued by the CFTC staff. We believe a more streamlined approach, analogous to the SEC's umbrella registration framework, would achieve the CFTC staff's objectives of ensuring that all relevant entities are subject to the Commission's authority and oversight in a more straight-forward and administratively efficient manner.

With respect to members of an investment company's board of directors, the CFTC staff has taken an inconsistent approach from the Commission on registration and/or delegation of the CPO function. In the CFTC 2012 Final Rule on CPOs and CTAs, the Commission provided that "[t]o require a member or members of the registered investment company's board of directors to register would raise operational concerns for the registered investment company as it would result in piercing the limitation on liability for actions undertaken in the capacity of director."[23] The Commission recognized that members of a registered investment company's board of directors are not CPOs of the fund. Nevertheless, with respect to members of a private investment company's board of directors, the CFTC staff has required that such persons either register or delegate the CPO function to a registered CPO.[24] Moreover, the CFTC staff requires a natural person, affiliated with the CPO of a privately-offered commodity pool, who is a voting member of the board of directors, board of trustees, board of managers or an equivalent governing body of a commodity pool, in delegating the CPO function to agree to joint and several liability as the CPO.[25] We have

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[20] *See* CFTC Final Rule on Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, 77 Fed. Reg. 11252 (Feb. 24, 2012), (hereinafter "**CFTC 2012 Final Rule on CPOs and CTAs**") available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2012-3390a.pdf.

[21] *See* SEC Final Form ADV and Investment Advisers Act Rules *supra* n. 18 at 60,463 (providing the circumstances under which umbrella registration is allowed).

[22] *See, e.g.*, CFTC Staff Letter No. 14-126, October 15, 2014, available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/14-126.pdf.

[23] *See* CFTC 2012 Final Rule on CPOs and CTAs *supra* n. 20 at 11,259.

[24] *See, e.g.*, CFTC Staff Letter No. 14-126, *supra* n. 22.

[25] *See id.*

strong concerns with such policy as it deters affiliated natural persons from serving on the governing body of a commodity pool and providing important expertise. We believe the CFTC staff should provide consistent treatment to natural persons serving on the governing body of a commodity pool, and issue guidance that members of an investment company's or commodity pool's board of directors or other governing body are not considered to be CPOs.

Accordingly, MFA recommends that the Commission: (1) adopt a more streamlined approach to registration or CPO delegation by issuing guidance analogous to the SEC's umbrella registration; and (2) provide consistent treatment to natural persons serving on the governing body of a commodity pool and issue guidance that members of an investment company's or commodity pool's board of directors or other governing body are not considered to be CPOs.

ii. Interpretation of Commodity Pool

MFA believes that the Commission should not consider a wholly owned subsidiary of a commodity pool to be a separate commodity pool. Such interpretation would significantly simplify regulation and reduce burden on market participants without reducing the effectiveness of the Commission's regulations or oversight.

The CFTC 2012 Final Rule on CPOs and CTAs took the position that a controlled foreign corporation was a commodity pool.[26] Subsequently, the CFTC staff issued guidance with respect to CPO/CTA compliance obligations, providing that a wholly owned trading subsidiary of a commodity pool was a commodity pool in and of itself.[27] As a result of such interpretation, a CPO must conduct the Rule 4.13(a)(3) *de minimis* trading calculation for CPO registration purposes with respect to wholly owned subsidiaries, as discussed above; and a registered CPO must file a Form CPO-PQR on behalf of each commodity pool, discussed further below. Interpreting a wholly owned subsidiary of a commodity pool has greatly increased the regulatory burden on CPOs, and made regulation complex and costly without additional benefits. MFA recommends that the Commission issue guidance providing that a wholly owned subsidiary of a commodity pool is not a separate commodity pool. In the alternative, MFA recommends that the Commission provide guidance that for purposes of CPO exemptions from registration or exclusions, and for regulatory reporting purposes, a wholly owned subsidiary of a commodity pool need not be considered a separate commodity pool.

iii. Updating QEP Status

MFA believes the Commission should provide interpretive guidance with respect to CFTC Rule 4.7(a)(2), persons who do not need to satisfy the Portfolio Requirement to be a QEP, recognizing that for a technology-driven trading firm, an employee may satisfy the exemption from

[26] *See* CFTC 2012 Final Rule on CPOs and CTAs *supra* n. 20.

[27] *See* Division of Swap Dealer and Intermediary Oversight Responds to Frequently Asked Questions – CPO/CTA: Amendments to Compliance Obligations, August 14, 2012, available at: http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/faq_cpocta.pdf.

the QEP portfolio requirement by having worked at a technology firm in lieu of a commodity interest, securities, or other financial services firm for at least 24 months.

CFTC Rule 4.7 allows certain insiders to invest in exempt pools without satisfying the QEP portfolio requirement. In particular, Rule 4.7(a)(2)(viii)(A)(4) allows an employee or agent engaged to perform (non-clerical or administrative) legal, accounting, auditing or other financial services for the exempt pool, CPO, CTA or other affiliate, to invest in the exempt pool, provided, that such employee or agent: (1) is an accredited investor; and (2) has been employed or engaged by the exempt pool, CPO, CTA, investment adviser or affiliate, or by another person engaged in providing commodity interest, securities or other financial services, for at least 24 months. The Commission explained in the adopting release that the purpose of the rule "was in furtherance of the intent of Rule 4.7: to reduce unnecessary regulatory prescriptions for CPOs and CTAs with respect to persons who do not appear to need the full protections offered by the Part 4 framework."[28]

As the Commission recognizes, "FinTech is driving innovation in financial markets across the globe."[29] Financial firms to varying degrees have become technology firms, and frequently attract talent from technology companies. Such employees may be intimately involved with the design and deployment of trading strategies, yet because they come from technology firms they may not be able to invest in the exempt pools to which they provide services for two years. We believe the Commission rules should recognize that an employee in certain technology-related roles at a firm with a technologically-driven trading model may satisfy the second prong of Rule 4.7(a)(2)(viii)(A)(4) by having worked at a technology company for at least 24 months. Similarly, the SEC has recognized that technology-related roles may be principal business functions within an investment manager that employs technologically-driven trading modes for purposes of being a "knowledgeable employee".[30]

Accordingly, MFA recommends that the CFTC issue interpretive relief or guidance that an employee in certain technology-related roles at a firm with a technologically-driven trading model may satisfy the Rule 4.7(a)(2)(viii)(A)(4)(ii) prior work experience requirement through work experience at a technology company rather than a financial services company.

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[28] CFTC Final Rules on Exemption from Certain Part 4 Requirements for Commodity Pool Operators with respect to Offerings to Qualified Eligible Persons and for Commodity Trading Advisors with respect to Advising Qualified Eligible Persons, 65 Fed. Reg. 47,848 (Aug. 4, 2000).

[29] *See* CFTC LabCFTC Overview regarding FinTech Innovation, available at: http://www.cftc.gov/LabCFTC/Overview/index.htm.

[30] *See Managed Funds Association*, SEC No-Action Letter (Feb. 6, 2014), available at: https://www.sec.gov/divisions/investment/noaction/2014/managed-funds-association-020614.htm.

B. Reporting

1. Forms CPO-PQR and CTA-PR

In the MFA June 6, 2017 letter, MFA recommended that the SEC and the CFTC rationalize and harmonize reporting, and for the SEC to administer a single, simpler, systemic risk form. MFA plans to submit in a separate submission to the Commission and the SEC detailed recommendations for a single and simpler systemic risk reporting form for CPOs, CTAs and investment advisers.

Notwithstanding the specific recommendations that we'll provide to the agencies, we believe the systemic risk form should request registrants to report on their commodity pools and investment funds on an aggregated basis, and not report separately on wholly owned subsidiaries of commodity pools/investment funds. This will greatly simplify reporting and provide regulators with a clearer understanding of the overall picture of a commodity pool and/or investment fund of a registrant. We understand from our members that it is extremely burdensome and time-consuming to provide reports to the CFTC and NFA on each wholly owned subsidiary of a commodity pool and to provide disaggregated reports with respect to master-feeder vehicles. Further, our members report that they receive regular quarterly calls from NFA staff as they cannot understand how the affiliated legal entities considered individual commodity pools relate to each other. Said another way, by requiring registrants to break up and report the activities of a commodity pool by its various legal entities or trading vehicles, regulators cannot understand the overall strategy of a commodity pool, nor effectively assess its risk. While it may be appropriate to have registrants list master-feeder vehicles and wholly owned subsidiaries of commodity pools, registrants should not need to file separate reports for each of these vehicles.

MFA will provide further recommendations in connection with Forms CPO-PQR, CTA-PR and PF. We raise the reporting aspect of wholly owned subsidiaries of commodity pools for the Commission's consideration as it reviews the interpretation of "commodity pool."

2. Reduce Complexity of Cleared Swap Reporting Requirements

MFA believes the CFTC should eliminate alpha swap reporting requirements to reduce the reporting complexities of its cleared swaps reporting regime and to streamline the data actually reported to SDRs without sacrificing the amount of information available to the CFTC regarding the entire life cycle of a swap. As Chairman Giancarlo noted in a recent interview with *Risk.net*,[31] the Commission only needs the final information reported by the CCP concerning the beta/gamma swaps comprising a cleared swap for effective oversight. As explained in MFA's prior comment letters, MFA believes there is no need for the reporting of an original "alpha" swap for any swap that is executed with the intention to be cleared.[32]

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[31] "Giancarlo orders review of CFTC rules", *Risk.net*, March 15, 2017.

[32] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, and Adam Jacobs, Director, Head of Markets Regulation, AIMA, to Melissa D. Jurgens, Secretary, CFTC, on May 27, 2014, on Review of Swap Data Recordkeeping and Reporting Requirements, available at:

MFA acknowledges that CFTC staff may prefer to retain alpha swap reporting to track compliance with timing and other compliance issues, such as counterparty interaction, price movements and whether trades are executed bilaterally off-venue or on-venue. As an alternative to eliminating SDR reporting for cleared swaps, MFA suggests that the CFTC consider simplifying the regulatory reporting infrastructure by making the CCPs responsible for maintaining data on their cleared swaps, and have SDRs maintain data for uncleared swaps. A CCP is party to every swap it clears and maintains comprehensive "golden source" data on such swaps for regulatory and risk management reasons, among others. Swap data reporting would be greatly simplified if the CCPs were responsible for maintaining SDR data for cleared swaps, rather than redundantly reporting such data to a third-party SDR (and subsequently updating and reconciling records with such SDR). Data aggregation would also be simplified for regulators, who could look to CCPs for SDR data on cleared swaps and to a separate SDR for data on uncleared swaps.

C. Executing

MFA urges the CFTC to improve the legal framework for trading on SEFs and DCMs. MFA believes the CFTC's work to promote swaps trading on SEFs has benefitted investors through increased pre-trade price transparency, competition, and liquidity. However, the implementation of the SEF framework can be refined and improved. MFA believes the CFTC should:

(1) Allow investors more flexibility in how they trade swaps while: (i) enabling true impartial access to SEFs and execution methods for all eligible participants, and (ii) preserving crucial requirements for pre-trade price transparency, price competition, and a multiple-to-multiple trading system or platform;

(2) Assume responsibility for determining when particular swap contracts have to be SEF-traded while carefully considering the distinct liquidity issues for any such contract; and

(3) Simplify and codify, with requested changes, the existing universe of CFTC staff guidance and no-action relief that the CFTC used to smooth the implementation of the SEF framework.

In October 2015, MFA submitted a petition to the CFTC to amend certain provisions of its regulations related to over-the-counter ("**OTC**") derivatives trading on SEFs, based on MFA members' experiences to date and the "lessons learned" through the implementation process.[33]

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https://www.managedfunds.org/wp-content/uploads/2014/05/CFTC-Swap-Data-Reporting-Rules-Final-MFA-AIMA-Letter.pdf; *see also* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, and Jiri Krol, Deputy CEO, Global Head of Government Affairs, AIMA, to Mr. Christopher Kirkpatrick, Secretary, CFTC, on October 30, 2015, on Amendments to Swap Data Recordkeeping and Reporting Requirements for Cleared Swaps, available at: https://www.managedfunds.org/wp-content/uploads/2015/11/CFTC-Proposed-Amendments-for-Cleared-Swap-Data-Reporting-MFA-AIMA-Final-Letter.pdf.

[33] *See* MFA Petition for Rulemaking to Amend Certain CFTC Regulations in Parts 1 (General Regulations under the Commodity Exchange Act), 39 (Derivatives Clearing Organizations, Subpart B – Compliance with Core Principles) and 43 (Real-Time Public Reporting), submitted to Mr. Christopher Kirkpatrick, Secretary of the Commission, on October 22, 2015 ("**MFA SEF Petition**"), available at: https://www.managedfunds.org/wp-

We outline below our updated positions and suggestions on key areas of regulatory reform for the CFTC's swaps trading framework raised in Chairman Giancarlo's White Paper,[34] as well as in his speeches earlier this year.[35]

1. Methods of Execution

MFA supports a broader variety of execution methods so long as: (i) true impartial access to SEFs and execution methods are provided to all eligible participants, and (ii) requirements for pre-trade price transparency, price competition and a multiple-to-multiple trading system or platform are preserved.

The promotion of pre-trade price transparency on SEFs is an express goal of the Dodd-Frank Act.[36] MFA is concerned that the potential regulatory elimination of the order book and request-for-quote ("**RFQ**")-to-3 execution protocols, which are designed to provide pre-trade price transparency, could undermine the pre-trade price transparency statutory goal for SEFs.

MFA is also concerned that the potential elimination of the current required methods of execution (*i.e.*, the order book and RFQ-to-3 execution methods) would remove pre-trade transparency in the U.S. SEF trading regime, and thereby raise a point of difference with the EU's MiFID II regulations governing pre-trade transparency of OTC derivatives trading on multilateral trading facilities ("**MTFs**") and organised trading facilities ("**OTFs**"). MFA encourages the CFTC to consider carefully introducing additional points of difference with the EU derivatives trading regime to avoid undermining equivalence and comparability determinations.

2. MAT Determination Process

MFA supports the CFTC assuming a more meaningful oversight role in the "made available to trade" ("**MAT**") determination process, including its ability to reject MAT determinations from SEFs. MFA strongly suggests that the CFTC keep the MAT determination process separate from the clearing determination, because clearing suitability does not assess adequately the liquidity features of the swap product in question. MFA believes the CFTC has an

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content/uploads/2015/10/CFTC-Petition-for-SEF-Rules-Amendments-MFA-Final-Letter-with-Appendix-A-Oct-22-2015.pdf.

[34] *See* "Pro-Reform Reconsideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank", White Paper, by Commissioner J. Christopher Giancarlo, issued on January 29, 2015 ("**Giancarlo White Paper**"), available at: http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/sefwhitepaper012915.pdf.

[35] *See* Keynote Address of CFTC Commissioner J. Christopher Giancarlo Before SEFCON VII, "Making Market Reform Work for America", January 18, 2017, available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo-19; *see also* "CFTC: A New Direction Forward," Remarks of Acting Chairman J. Christopher Giancarlo before the 42nd Annual International Futures Industry Conference in Boca Raton, FL, March 15, 2017, available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo-20.

[36] *See* section 733 of the Dodd-Frank Act, adding CEA section 5h(e); 7 U.S.C. 7b-3(e).

important role to play in carefully considering the distinct liquidity-related factors with respect to a clearing-mandated swap product before requiring it to trade on-SEF.

While expanding the methods of execution available on SEFs would be a welcome development, the CFTC's authorization of more flexible execution methods does not mean that all mandatorily cleared, non-MAT products will suddenly be suitable for SEF trading. In MFA's view, flexibility in execution alone is not enough to promote swaps trading on SEFs, as it would not address the sufficiency of a product's liquidity or the ability of all eligible market participants to access all SEFs that will offer broader methods of execution and diverse liquidity in trading the product.

MFA urges the CFTC not to adopt a simplistic construction of the trade execution requirement that would require any mandatorily cleared and listed swap product automatically to become subject to the trading mandate. MFA fears that such a construction would inextricably link the trading mandate to the clearing mandate and discourage the industry from bringing more products into central clearing.

In that connection, MFA reiterates the MFA SEF Petition request to provide a mandatory comment period for every MAT determination submission by a SEF or DCM under Part 40 of the Commission's regulations. MFA also reiterates the MFA SEF Petition request to establish a clear de-MAT determination process when a swap product no longer exhibits the requisite liquidity profile to trade on-SEF.

MFA agrees with Chairman Giancarlo's concerns with respect to package transactions.[37] MFA encourages the CFTC to consider the proposed amendments in the MFA SEF Petition as an alternative approach to resolve those concerns by requiring SEFs to make MAT determinations separately for a given swap when executed on a stand-alone basis and for different types of package transactions that include such a swap.

Taken together, MFA's proposed amendments in the MFA SEF Petition with respect to the MAT determination process would improve the CFTC's process and facilitate equivalence discussions with the EU by moving the CFTC's process a step closer in comparability to the European Securities and Markets Authority's ("**ESMA**") process for determining which mandatorily cleared OTC derivative products will become subject to the derivatives trading obligation under the MiFID II/MiFIR regime.

3. Impartial Access

MFA believes the buy-side should have fair, unbiased and unprejudiced access to SEFs that offer more execution modalities. More specifically, the buy-side needs true impartial access, without adverse commercial repercussions, to legacy interdealer broker ("**IDB**") SEF order books and voice-brokered IDB trading functionality in order to more efficiently trade package

[37] *See* Giancarlo White Paper at p. 26 (stating that "many package transactions are ill-suited to Order Book or RFQ System execution given their limited liquidity and complex characteristics.")

transactions and stand-alone swaps that are not MAT. Our position is based on the serious challenges MFA members continue to face trading such products using the RFQ system on dealer-to-customer SEFs, where they have lost the ability to place resting orders.

The CFTC should enforce true impartial access to all SEFs, in conjunction with authorizing more flexible execution methods on SEFs, by removing artificial barriers that hinder the achievement of the Dodd-Frank Act goals to promote swaps trading and pre-trade price transparency on SEFs.[38] MFA believes that the current bifurcated swaps market structure has not, and will not, achieve these statutory goals if such barriers to true impartial access persist in the U.S. SEF regime. We highlight examples of such barriers below.

As MFA explained in its position paper,[39] the legacy practice of post-trade name disclosure or "name give-up" on IDB SEFs that offer anonymous execution of cleared swaps is a key mechanism that continues to prevent the buy-side from accessing important pools of liquidity for cleared swaps, including the only liquid order books. The practice's exclusionary effect on otherwise qualified buy-side market participants is status-based discrimination and thus inconsistent with the impartial access mandate for SEFs. MFA believes that the practice also reduces pre-trade price transparency for otherwise qualified buy-side market participants and restricts their ability to trade certain swap products anonymously. The effects of this practice are anti-competitive and have been challenged in recent federal antitrust lawsuits brought in the U.S. District Court, Southern District of New York.[40] MFA believes that if the free market was going to address the effects of this anti-competitive practice organically, it would have done so by now. However, it is difficult for any one IDB SEF to disable post-trade name disclosure unilaterally, as traditional dealers that opposed such a change might easily shift their trading to other IDB SEFs. This is a classic case where the CFTC, as the primary regulator of the U.S. swaps market, can readily bring competition and fairness to the market.

With respect to the use of enablement mechanisms and breakage agreements for swaps that are intended to be cleared on SEFs, MFA reiterates the MFA SEF Petition request to prohibit such arrangements by codifying existing CFTC staff guidance around the implementation of the CFTC's impartial access requirements.

MFA members also remain concerned with the lack of transparency concerning SEF fee structures. As regulated entities, all SEFs should be required to publish their fee schedules. MFA understands that certain SEFs have pricing schemes and volume rebates that deter buy-side access, as pricing is only viable and affordable for certain firms to access such SEFs.

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[38] *See supra* n. 36.

[39] *See* MFA Position Paper: *Why Eliminating Post-Trade Name Disclosure Will Improve the Swaps Market*, dated March 31, 2015, available at: https://www.managedfunds.org/wp-content/uploads/2015/04/MFA-Position-Paper-on-Post-Trade-Name-Disclosure-Final.pdf.

[40] *See, e.g., In re Interest Rate Swaps Antitrust Litigation,* 16-MD-2704 (PAE) (S.D.N.Y.).

MFA also urges the CFTC to finalize dealer ownership restrictions or thresholds for SEF governance, as dealer-dominated SEFs create the risk of conflicts of interest.

Similar to the U.S. impartial access requirement, the European MiFID II legislation requires trading venues to provide non-discriminatory access to market participants.[41] ESMA recently issued Q&A guidance[42] to clarify particular types of arrangements on MTFs, OTFs and regulated markets that ESMA would consider as non-objective and discriminatory for purposes of access to such EU trading venues, which was similar in scope to prohibited arrangements cited in the CFTC's impartial access guidance for SEFs and DCMs[43]. As such, there should be no difference between the two regimes on this topic. MFA believes that ensuring equivalent standards with respect to the implementation of impartial access should be a key focus in future discussions regarding harmonization and regulatory equivalence.

4. STP and Void *Ab Initio*

MFA reiterates the MFA SEF Petition request to codify existing CFTC staff guidance around the CFTC's straight-through processing ("**STP**") requirements. MFA believes that STP is critical to a competitive, open and transparent market for swaps that are intended to be cleared.

STP benefits all market participants, especially smaller market participants and alternative liquidity providers that could otherwise encounter barriers to entry, in that it: (i) gives market participants certainty of clearing immediately following execution, which in turn, allows them to hedge more efficiently and effectively manage risk; (ii) is an important factor in encouraging the implementation of broad, mandatory clearing; (iii) is essential to electronic trading, particularly central limit order book trading, as it is not possible to enter into an electronic transaction on an anonymous basis without both the immediate confirmation of the execution of the transaction and its acceptance for clearing; and (iv) promotes accessible, competitive markets and access to best execution by ensuring parties to a cleared transaction have immediate confirmation that they will face the relevant CCP, thus eliminating the need to negotiate individual credit arrangements with each of their counterparties, as is required in bilateral derivatives markets.

MFA views void *ab initio* as an important part of the STP regime that should be preserved. More specifically, MFA reiterates the MFA SEF Petition Request to codify, with clarifying modifications, existing CFTC staff guidance and extended no-action relief under CFTC No-Action

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[41] *See* Article 18(3) of the MiFID II Directive governing MTFs and OTFs, and Article 53(1) of the MiFID II Directive governing regulated markets.

[42] Available at: https://www.managedfunds.org/wp-content/uploads/2017/09/ESMA-QA-on-MiFID-II-and-MiFIR-Market-Structures-Topics.pdf, p. 29-31.

[43] *See* "Division of Clearing and Risk, Division of Market Oversight and Division of Swap Dealer and Intermediary Oversight Guidance on Application of Certain Commission Regulations to Swap Execution Facilities", issued Nov. 14, 2013, available at: http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/dmostaffguidance111413.pdf.

Letter 17-27 ("**NAL 17-27**") around rejection of swaps from clearing and resubmission for operational and clerical errors.[44]

MFA notes that ESMA included both void *ab initio* and a resubmission procedure in its regulatory technical standards under the EU's MiFID II/MiFIR. As a result, codifying these points would further facilitate harmonization between SEFs/DCMs and MiFID II trading venues.

5. The "Occurs Away" Requirement for Block Trades

MFA believes the "occurs away" requirement is unnecessarily complex, and agrees with Chairman Giancarlo's views on this issue.[45] Accordingly, MFA reiterates the MFA SEF Petition request to modify the definition of "block trade" in Part 43 of the Commission's regulations to authorize on-SEF execution of a block trade as a Permitted Transaction, as defined in section 37.9(c), in order to facilitate pre-execution credit checks of block trades that are intended to be cleared.

6. Footnote 88 SEF Registration Mandate for FX PB Platforms

MFA requests CFTC guidance to clarify ambiguities surrounding SEF trade execution of FX prime brokerage transactions, in particular non-deliverable forward contracts, on multiple-to-multiple platforms that had to register as SEFs. The application of SEF requirements for cleared trades executed on these platforms is a point of ambiguity that continues to impede trading on these platforms. These registered SEFs do not list any clearing-mandated Required Transactions.

7. Uncleared Swaps Confirmations

MFA requests that the CFTC adopt a modified confirmation delivery requirement in section 37.6(b) for uncleared swaps that will respect confidentiality concerns of the counterparties. MFA appreciates the current no-action relief that will expire on the effective date of any changes in the regulation.[46] Without such relief, buy-side market participants would be required to disclose the terms of all of their ISDA Master Agreements to SEFs, which raises material concerns regarding confidentiality and practicality. MFA strongly agrees with Chairman Giancarlo's criticisms of the confirmation requirement as expressed in the Giancarlo White Paper.[47]

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[44] *See* CFTC Staff Letter No. 17-27, May 30, 2017, available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/17-27.pdf.

[45] *See* Giancarlo White Paper at p. 27-28 and n. 91.

[46] *See* CFTC Staff No-Action Letter No. 17-17, "Extension of No-Action Relief for Swap Execution Facility Confirmation and Recordkeeping Requirements under Commodity Futures Trading Commission Regulations 37.6(b), 37.1000, 37.1001, 45.2, and 45.3(a)", issued on March 24, 2017, available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/17-17.pdf.

[47] *See* Giancarlo White Paper at p. 34-36.

Accordingly, we support a rule amendment to section 37.6(b) that would make the confirmation delivery requirement workable for SEF market participants.

8. Automated SEF Error Processing

Under the most recent extension of CFTC no-action relief in NAL 17-27, SEFs and DCMs may permit a pre-arranged trade between the original or intended counterparties without having to comply with required execution methods when a trade has been cleared and the parties to the trade discover an operational or clerical error.[48] The relief is subject to a number of conditions, including that a SEF or DCM must make an affirmative finding that the trade or a trade term resulted from an error. This condition raises a question as to how a SEF or DCM makes such a finding and approves the submission to correct an error.

With respect to SEFs specifically, MFA members have observed error handling processes that are largely manual, subject counterparties to significant delays and market risk, and lack sufficient safeguards to ensure the SEF's findings and approvals (or lack thereof) are adequately documented. Specifically, MFA understands, based on its members' experience on two leading SEFs, that error trades are often flagged to a SEF via telephone, on lines which are not required to be recorded. SEF personnel then forward the request to compliance personnel, and generally rely on email to confirm the error and, if necessary, obtain counterparty consents. That process can sometimes take more than 30 minutes, during which counterparties are subject to market risk. Once the SEF approves an error request, traders on at least one leading SEF are instructed to initiate an RFQ ticket and to choose "Error Offset" or "Error Correction" from a drop-down menu before submitting an order. MFA understands that the "Error Offset" and "Error Correction" options in the drop-down menu are available to a trader at all times and are not restricted for use only with prior SEF approval.

The lack of automated error processing procedures on SEFs subjects market participants to significant delays and market risk, and effectively puts the onus on the counterparties to evidence that the SEF confirmed the trading error and approved the correcting trade submission. Accordingly, MFA recommends that the Commission codify NAL 17-27 with a requirement for SEFs and DCMs to build automated error processing controls into their trading systems. Such controls should be designed to streamline the SEF's confirmation of the trading error and approval to correct an erroneous trade, to ensure only pre-approved transactions are recorded as "Error Offset" or "Error Correction", and to generate for all interested parties reliable documentation of the resolution of an error in accordance with applicable rules. MFA believes that, with years of experience handling errors, SEFs and DCMs should be required to make modest improvements to their trading platforms since it would facilitate market surveillance in a manner consistent with their obligations as self-regulatory organizations.

[48] *See supra* n. 44.

9. Increased Mandatory Disclosure from SEFs regarding Trading Protocols, Fees, and Governance

In November 2015, the CFTC issued a notice of proposed rulemaking regarding "Regulation Automated Trading", which included a provision requiring a DCM to provide additional public information regarding its market maker and trading incentive programs. MFA supported such requirement and, in addition, recommended that the CFTC require SEFs to make similar types of market maker and trading incentive program disclosures.[49] Applying these transparency requirements to SEFs would level the playing field with DCMs, as DCMs may directly compete with SEFs by listing swaps or economically similar contracts. MFA believes that such disclosure requirements will provide investors and the broader public with more information and transparency into DCM and SEF market maker and trading incentive programs, and we agree with the CFTC that such disclosure will enhance market integrity.

Further, it is our view that market participants can benefit from greater transparency from SEFs regarding other important aspects of their offerings, including trading protocols, fees, and governance. Ensuring that this type of information is consistently provided to market participants, will level the playing field and ensure that all investors can make informed decisions regarding whether to join a particular platform.

D. Miscellaneous

1. Repeal Segregation Interpretation 10-1 for Futures and Options Transactions

MFA respectfully request that the Commission repeal DCIO Segregation Interpretation 10–1[50] to the Financial and Segregation Interpretation No. 10[51] for Futures. This change would simplify Commission rules by better aligning the Commission segregation regime for Futures customers with the regime for swap customers, and would allow Futures customers to have greater optionality as to the level of segregation protection that they could choose for their collateral.

i. Background

As the Commission knows, Section 4d(a)(2) of the CEA requires futures commission merchants ("**FCMs**") to maintain all customer collateral separate from the FCM's own funds, but permits an FCM to commingle assets of one customer with the assets of another. In 1984, the Commission's Division of Trading and Markets ("**DTM**") issued Segregation Interpretation 10 to provide DTM's view on the treatment under Section 4d(a)(2) of funds deposited in third-party custodial accounts. Pursuant to Segregation Interpretation 10, DTM permitted the use of third-

[49] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Christopher Kirkpatrick, Secretary, CFTC, on March 16, 2016, on Proposed Regulation Automated Trading, at p. 33, available at: https://www.managedfunds.org/wp-content/uploads/2016/03/MFA-RegAT-Letter-final.pdf.

[50] 70 Fed. Reg. 24,768 (May 11, 2005), available at: http://www.gpo.gov/fdsys/pkg/FR-2005-05-11/pdf/05-9386.pdf.

[51] *See* Comm. Fut. L. Rep. (CCH) 7,120 (May 23, 1984) available at: http://www.cftc.gov/tm/finseginterp_10.htm.

party custodial accounts so long as the accounts complied with certain enumerated standards.[52] However, in 2005, DCIO issued Segregation Interpretation 10-1, in part, in response to concerns that FCMs did not have "immediate and unfettered access" to customer collateral.[53] In Segregation Interpretation 10-1, DCIO stated that, with limited exception,[54] third-party custodial accounts were no longer permitted or appropriate, and that FCMs would not be "in compliance with the requirements of Section 4d(a)(2) if they deposit, hold or maintain margin funds for customer accounts in third-party custodial accounts".[55]

However, this prohibition of third-party custodial accounts for Futures is a departure from the Commission segregation rules that apply to swaps. Specifically, in 2012, in adopting the final segregation of collateral rules for cleared swaps, the Commission clarified that Segregation Interpretation 10–1 does not apply to those swaps.[56] In addition, in the Final Cleared Swap Rule Release, the Commission noted a commenter's request that the Commission repeal Segregation Interpretation 10-1 for Futures, but the Commission declined to address the commenter's request because "it [was] beyond the scope of this rulemaking".[57] However, the Commission also stated that "while the Commission does not believe it would be appropriate to address this request at this time . . . the Commission may address this concern in the future."[58]

Moreover, in 2013, the Commission adopted final rules of segregation collateral for uncleared swaps.[59] In those final rules, the Commission expressly provided customers with the option to segregate the initial margin that they post on uncleared swaps in a third-party custodial account.

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[52] *See id*., permitting third party custodial accounts if the accounts meet DTR's outlined standards with respect to: (1) account name, (2) liquidation of open positions, (3) withdrawal power, and (4) account location.

[53] *See* Segregation Interpretation 10-1 at 24,768. *See also id*., where DCIO bases its decision, in part, on changes to Rule 17f–6 of the Investment Company Act of 1940, as amended, which permitted registered investment companies to deposit customer margin directly with FCMs and futures clearinghouses.

[54] *See id*., where DSIO asserted that FCMs could continue to use third party custodial arrangements where existing law precludes FCMs from holding assets of registered investment companies.

[55] *Id*.

[56] *See* Commission final rule on "Protection of Cleared Swaps Customer Contracts and Collateral; Conforming Amendments to the Commodity Broker Bankruptcy Provisions", 77 Fed. Reg. 6,336 (February 7, 2012), at 6343, available at: http://www.gpo.gov/fdsys/pkg/FR-2012-02-07/pdf/2012-1033.pdf (the "**Final Cleared Swap Rule Release**").

[57] *Id*. at 6,343.

[58] *Id*.

[59] See Commission final rule on "Protection of Collateral of Counterparties to Uncleared Swaps; Treatment of Securities in a Portfolio Margining Account in a Commodity Broker Bankruptcy", 78 Fed. Reg. 66,621, available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2013-26479a.pdf.

MFA believes that, in light of the Commission's efforts to simplify its rules and the failures of MF Global, Inc. ("**MF Global**") and Peregrine Financial Group, Inc. ("**Peregrine**"), it is the appropriate time for the Commission to reconsider this matter and the foregoing commenter's request. Therefore, we respectfully request that the Commission repeal Segregation Interpretation 10-1 for Futures.

ii. FCM Immediate and Unfettered Access to Futures Customer Collateral

MFA's members are customers to FCMs and are fiduciaries to their investors. Thus, we were very troubled by the MF Global and Peregrine insolvencies, which resulted in Futures customers experiencing a delay in the return of their segregated Futures assets or incurring material losses of their Futures funds.[60] Therefore, we believe that repealing Segregation Interpretation 10-1 to permit third-party custodial accounts for Futures is an important step towards safeguarding investors' assets.

We understand that the Commission is concerned about maintaining FCM and market stability. Therefore, "any impediments or restrictions on the FCM's ability to obtain immediate and unfettered access to customer funds are not permitted"[61] because any potential delay in a customer margin payment could significantly disrupt the market, particularly in times of market stress. We also appreciate that DCIO issued Segregation Interpretation 10-1, in part, to address "evidence of significant risks that may impair immediate and unfettered access by FCMs".[62]

However, in Segregation Interpretation 10-1, DCIO's concern about restrictions to FCMs' access to customer collateral resulted from:

(1) A comment letter indicating that Futures customers, rather than FCMs, have the client relationship with the custodian banks, which limits FCMs ready access to the third-party custodial account;[63] and

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[60] *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.

[61] Segregation Interpretation 10-1 at 24,769.

[62] *Id*. at 24,768.

[63] *See id*. at 24,769, citing a comment letter from the Futures Industry Association dated April 4, 2005.

(2) Reports by Commission audit staff and the Joint Audit Committee[64] of instances where the custodian released significant amounts of customer assets from the third-party custodial account without the FCM's knowledge or permission.[65]

As described below, MFA strongly believes that the structure of typical third-party custodial account arrangements and the standard provisions in the related account agreements address these concerns and justify the Commission's repeal of Segregation Interpretation 10-1 for Futures. In addition, we remind the Commission that, following repeal of Segregation Interpretation 10-1 for Futures, the tri-party custodial accounts would remain subject to the standards enumerated in Segregation Interpretation 10.

a. Typical Third-Party Custodial Account Arrangements

Some of MFA's members have established third-party custodial accounts in the OTC derivatives market for collateral they have posted on uncleared swap positions. Typically, the related agreement is a tri-party agreement among the customer, its dealer counterparty and a third-party custodian bank.[66] Therefore, both the customer and its dealer counterparty have a relationship, and are in contractual privity, with the third-party custodian (*i.e.*, it is not only the customer that has a relationship with the custodian). Although the third-party custodial account holds the customer collateral, as discussed further below, the dealer counterparty has a secured interest in the posted customer collateral and has exclusive control over the account and related customer collateral, except when the FCM is in default. Limiting the FCM's exclusive control over the third-party custodial account upon its default is necessary because providing the FCM with exclusive control is what allows potential misuse and misappropriation of customer collateral.

b. UCC Control of Collateral by Dealer Secured Party

For third-party custodial accounts, a custody bank or other institutional custodian assumes responsibilities for safeguarding, investing, transferring and releasing customer posted collateral under the three-way contract among the custodian, the customer and the dealer counterparty.[67] The control agreement is in favor of the dealer and the collateral safeguarding covenants provided by the custodian to the dealer in that agreement allow the dealer to control the customer's

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[64] *See* The Joint Audit Committee website, available at: http://www.wjammer.com/jac/, which describes the Joint Audit Committee as a representative committee of U.S. futures exchanges and regulatory organizations, including the ACC, BTEC, CBOT, CME, COMEX, CSC, ELX Futures, KCBOT, MESL, MGE, NQLX, NYCE, NYFE, NYMEX, One Chicago, PBOT and the NFA.

[65] *See* Segregation Interpretation 10-1 at 24,769.

[66] *See* Memorandum, "Independent Amount Segregation: Summary of ISDA's Sample Tri-Party IA Provisions", published in 2011 by the International Swaps and Derivatives Association, Inc. ("**ISDA**"), available at https://www.managedfunds.org/wp-content/uploads/2013/02/ISDA-SampleTri-Party-IA-Provisions-Memorandum.pdf, which contains standard contractual provisions to facilitate negotiation of third-party custodial account agreements.

[67] *See id*.

collateral. The dealer becomes a secured party by obtaining and perfecting its valid security interest in the posted collateral by having "control" over the collateral assets under Article 8[68] and Article 9[69] of the Uniform Commercial Code ("**UCC**"). UCC Articles 8 and 9 have been widely adopted in the U.S. Subject to the UCC and the respective rights of the parties under the third-party custodial account agreement, the dealer (as the secured party) typically establishes the requisite degree of control under the UCC by virtue of its contractual ability to direct the custodian to follow its instructions (except when it is the defaulting party under the relevant agreements).

The dealer may also gain exclusive control over the collateral posted by the customer (in the event of the custodian's default or other specified condition) by issuing an "entitlement order" to the custodian. In particular, if the dealer issues a "Notice of Exclusive Control" to the custodian in such circumstances, it will eliminate any right of a defaulting customer to attempt to instruct the custodian to move its collateral.[70] The contractual terms would then require the custodian to cede possession of the collateral to the dealer, ensuring the dealer's timely access to the collateral. Such access facilitates the dealer's timely liquidation of the customer's non-cash collateral to cover its exposures.[71] In the event of the customer's bankruptcy, the dealer's contractual rights to liquidate, terminate or accelerate a derivatives contract would be unimpaired, as such contractual rights are not subject to the automatic stay.[72]

iii. Equal Protection of Swaps, Futures and Options Customers

Although Segregation Interpretation 10-1 reflects DCIO's prior views and concerns about third-party custodial accounts, as mentioned above, in adopting the final segregation of collateral rules for cleared swaps, the Commission demonstrated a willingness to reconsider Segregation Interpretation 10-1 and the extent to which third-party custodial accounts comply with Section 4d of the CEA.[73] In addition, in adopting the final rules for uncleared swaps, the Commission expressly allowed customers to utilize third-party custodial accounts with regard to their uncleared

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[68] Article 8 relates to "perfection by control over a certificated security, an uncertificated security, or a security entitlement is provided in §8-106).

[69] Article 9 relates to "perfection by control over deposit accounts is provided in §§9-104, 9-314 and 9-327".

[70] *See* "Independent Amounts", Release 2.0, dated March 1, 2010, a white paper produced jointly by ISDA, MFA and the Securities Industry and Financial Markets Association at 10, available at: https://www.managedfunds.org/wp-content/uploads/2013/02/Independent-Amount-WhitePaper-Final.pdf, which describes arrangements for holding initial margin in third party custodial accounts and control provisions for the secured party to achieve a perfected security interest in the collateral.

[71] *See id.* at 40, endnote 38.

[72] 11 U.S.C. sections 555 (securities contract) and 560 (swap agreement).

[73] *See* Final Cleared Swap Rule Release at 6,343, where the Commission clarified that subject to the conditions described therein, FCMs may deposit their cleared swaps customers' collateral in a third-party custodial account without the FCM being deemed in violation of Section 4d(f) of the CEA.

swap collateral.[74] As mentioned, some of our members have established third-party custodial account arrangements in the OTC derivatives market for protection of their uncleared swaps collateral, and MFA believes that the protections provided by third-party custodial accounts[75] should be available to all customers, including Futures customers.

Moreover, we believe that there is no difference between cleared and uncleared swaps on the one hand and Futures on the other that supports retaining Segregation Interpretation 10-1 and limiting the use of third-party custodial accounts for Futures. In fact, it was the Futures customers of MF Global and Peregrine that were harmed by MF Global and Peregrine's misuse and misappropriation of customer assets and subsequence insolvencies.[76] These events suggest a clear need to enhance protections of Futures customers' collateral, and we feel strongly that Futures customers should have protections that mitigate "fellow customer" risk[77] as well as FCM operational and investment risk for their collateral equal to those that the Commission permits a swaps customer to receive.

Therefore, we respectfully request that the Commission simplify its segregation regime across different all products by repealing Segregation Interpretation 10-1 for Futures and allowing the use third-party custodial accounts to ensure that Futures customers will have protections for the collateral that they post equal to those available to other derivatives customers.

2. Initial Margin Requirements Should be Tailored to the Risk of Certain Non-Clearable Swaps

MFA believes that the CFTC should work with the Fed and other U.S. prudential regulators to recalibrate and appropriately tailor initial margin ("**IM**") requirements for uncleared swaps to reflect the actual risk posed by certain non-clearable swap products, such as total return swaps ("**TRS**") for complex equity trades. Under the uncleared margin rules, swap dealers must charge higher margin for non-cleared swaps than for cleared swaps. One reason for this distinction is to encourage all market participants to clear as many derivatives trades as possible. MFA has been a strong supporter of Title VII of the Dodd-Frank Act and believes that clearing (as well as trading mandates) improve pricing and reduce systemic risk.

Unfortunately, market conditions make it unlikely that market participants will clear certain categories of derivatives, such as TRS. Many hedge funds trade such TRS to achieve exposure to equities. Therefore, the margin rules that will be coming into effect for many MFA members' uncleared trades on September 1, 2019 or 2020 will penalize hedge funds that use non-

[74] *See supra* n. 59.

[75] *See* Section C below for a brief discussion of the benefits of tri-party custodial accounts.

[76] *See supra* n. 60.

[77] "Fellow customer risk" is the risk that a derivatives clearing organization ("**DCO**") uses assets of an FCM's non-defaulting customers to satisfy losses of that FCM's defaulting customer in the event that those losses exceed the margin assets of the defaulting customer and the FCM.

clearable TRS by having to over-collateralize them based on the higher IM requirements. One of the underlying policy objectives for the higher uncleared margin requirements is to encourage clearing swaps that are suitable for clearing. That policy objective has a punitive and disproportionate effect on buy-side market participants who trade non-clearable TRS and collateralize them based on the actual risk posed by such products. Moreover, we note that, as banks do not trade such TRS among themselves, our requested tailored revision to IM requirements for such products would present relatively little systemic risk. Given that banks' risk-based initial margin models would remain subject to regulatory approval, there would still be ample regulatory oversight and validation of the margin methodologies and calculations for such products. Based on the foregoing, we urge the CFTC to reconsider IM requirements for certain non-cleared swaps, such as TRS, when market conditions make it unlikely that market participants will clear such swaps for the foreseeable future.

3. Liquidation Periods Should be More Closely Calibrated to Product Liquidity

Under the CFTC's uncleared margin rules, IM models are required to set IM at a level that covers at least 99% of price changes over at least a ten-day liquidation time period.[78] The CFTC's margin requirements for cleared financial swaps require a five-day liquidation time period and a one-day liquidation period for futures contracts[79] However, in our members' experience, this product-level disparity in liquidation time periods among futures, cleared swaps and uncleared swaps is arbitrary and unjustified.

Therefore, we suggest that the CFTC work with the Basel-IOSCO WGMR, the SEC, the Fed and the other U.S. prudential regulators to re-examine market practice and historical data to more closely calibrate liquidation periods based on the liquidity profile of the contract in question rather than setting arbitrary and risk-insensitive liquidation time periods based on broad product types (*i.e.*, futures contracts, cleared swaps, or uncleared swaps).

4. Organization of CFTC Website & Staff Letters

In the MFA June 6, 2017 letter, MFA recommended that the CFTC modernize and update the Part 4 regulations. In the meantime, we believe the CFTC should enhance the organization of its website and CFTC staff letters to facilitate compliance of CFTC regulations by market participants.

For example, we believe it would be helpful for each division to have a dedicated webpage with links to relevant "frequently asked questions" or "questions and answers" that the staff has issued in connection with important rulemakings; as well as division staff letters. Currently, many

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[78] *See* CFTC Final Rule, "Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap participants", 81 Fed. Reg. 636, 656-657 (Jan. 6, 2016), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2015-32320a.pdf.

[79] *See* CFTC Final Rule, "Derivatives Clearing Organization General Provisions and Core Principles," 76 Fed. Reg. 69,334, 69,438 (Nov. 8, 2011), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2011-27536a.pdf.

helpful Fact pages, FAQs or Q&As, which were issued in connection to the adoption of a final rule, can only be found linked to an archived CFTC press release. Further, we believe it would be helpful for the CFTC to organize CFTC staff letters by providing for No-Action, Exemptive and Interpretative letters: a subject category list of letters; an alphabetical list of letters; and a chronological list of letters. We believe that by enhancing the organization of regulatory materials on the CFTC's website, the Commission will help reduce compliance costs and improve compliance of its regulations by market participants.

MFA recommends that the Commission enhance the organization of its website and CFTC staff letters to facilitate compliance of CFTC regulations by market participants.

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MFA appreciates the opportunity to provide these suggestions under the Project KISS initiative. If you have any questions about these suggestions, or if we can provide further information, please do not hesitate to contact Associate General Counsels Jennifer Han, Laura Harper Powell, Carlotta King, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

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

CC: The Hon. J. Christopher Giancarlo, Chairman
The Hon. Brian D. Quintenz, Commissioner
The Hon. Rostin Behnam, Commissioner
Michael Gill, Chief of Staff, Chairman
Matthew B. Kulkin, Director, Division of Swap Dealer and Intermediary Oversight
Amir Zaidi, Director, Division of Market Oversight
Brian A. Bussey, Director, Division of Clearing and Risk

APPENDIX

June 6, 2017

Via Electronic Submission

The Hon. J. Christopher Giancarlo
Acting Chairman
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: Managed Funds Association Regulatory Priorities

Dear Acting Chairman Giancarlo:

Managed Funds Association[1] ("**MFA**") congratulates you on your nomination to become the new Chairman of the Commodity Futures Trading Commission (the "**CFTC**" or "**Commission**"). We very much appreciate the productive dialogue that we have had with you and other Commissioners in the past and look forward to continuing a constructive and cooperative relationship with the Commission under your leadership.

We wish to outline MFA's priority issues and related requests concerning the Commission's regulatory activity that affect the private fund industry. MFA represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair markets. MFA has over 3,000 members from firms engaging in many alternative investment strategies all over the world. Many of our members are commodity pool operators ("**CPOs**") and/or commodity trading advisors ("**CTAs**") either registered with the Commission or exempt from registration.

MFA members favor smart, effective regulation of derivatives markets, and have a strong interest in thoughtful and efficient regulation of hedge fund managers. We applaud your Project KISS—Keep It Simple Stupid—initiative, and support the agency-wide review of CFTC

[1] Managed Funds Association (MFA) 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, North and South America, and many other regions where MFA members are market participants.

APPENDIX

regulations and practices to make them simpler, less burdensome, and less costly.[2] MFA supported many aspects of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "**Dodd-Frank Act**"), such as the Title VII requirement for centralized clearing of certain swaps.[3] Passage of the Dodd-Frank Act was followed by several years of intensive regulatory and rulemaking activity by the CFTC, in part to implement the statutory requirements of the Dodd-Frank Act. We agree that now that the CFTC has developed many of the key regulatory requirements of the Dodd-Frank Act, the Commission should review the results of its rulemakings and refine aspects of these rulemakings to enhance efficiency and reduce burden for the Commission and market participants. In addition, we greatly support and welcome under your leadership a resumption of "normalized operations and practices [by the CFTC, which] means a return to greater care and precision in rule drafting, more thorough econometric analysis, less contracted time frames for public comment and a reduced docket of new rules and regulations to be absorbed by market participants."[4]

In this letter, we raise several recommendations for regulatory improvements, which we believe will help the Commission achieve its regulatory objectives while making regulation simpler, more effective, and less burdensome. We would welcome the opportunity to meet with you, Commissioner Bowen, and Commission Staff in due course to discuss the issues outlined below in greater detail.

I. SUMMARY OF PRIORITY ISSUES

A. Rationalize CPO & CTA Regulation by Reducing Redundancy with the SEC

In the spirit of the President's "Core Principles for Regulating the United States Financial System,"[5] we believe the CFTC and the Securities and Exchange Commission ("**SEC**") should rationalize investment manager registration and systemic risk/compliance reporting requirements between the CFTC and the SEC. Doing so will simplify and streamline regulation of investment managers, making regulation more efficient and less costly and burdensome for registrants.

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[2] "CFTC: A New Direction Forward," Remarks of Acting Chairman J. Christopher Giancarlo before the 42nd Annual International Futures Industry Conference in Boca Raton, FL, March 15, 2017 ("**Giancarlo Boca Speech**"), available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo-20.

[3] Pub. L. 111-203, 124 Stat. 1376 (July 21, 2010), available at: http://www.gpo.gov/fdsys/pkg/PLAW-111publ203/html/PLAW-111publ203.htm.

[4] *See supra* note 2.

[5] Presidential Executive Order on Core Principles for Regulating the United States Financial System, White House, February 3, 2017, available at: https://www.whitehouse.gov/the-press-office/2017/02/03/presidential-executive-order-core-principles-regulating-united-states.

APPENDIX

1. Reduce Redundant Oversight and Reinstate § 4.13(a)(4) for Investment Management Firms Overseen by the SEC; Reduce Extraterritorial Scope; and Modernize and Update Regulation for those Entities that Should Remain Subject to CFTC Oversight

MFA requests that the Commission reinstate § 4.13(a)(4) for U.S. investment firms with advisers registered with the SEC or affiliated with an SEC-registered investment adviser. Such exemption will reduce duplicative registration and regulatory requirements; and make regulation more efficient, effective, and appropriately tailored for investment managers. MFA also encourages the Commission to work with the Alternative Investment Management Association ("AIMA") and other industry associations and foreign investment advisers to adopt a reasonable exemption for foreign investment advisers that would not be covered by any relief granted for SEC-registered investment advisers. Further, the Commission should modernize and update regulation for those entities that should remain subject to CFTC oversight.

2. Unify and Streamline Systemic Risk Reporting with the SEC

MFA requests that the CFTC and the SEC simplify and streamline systemic risk reporting by using a single, shorter systemic risk report administered by the SEC. Such a report would greatly enhance regulatory efficiency, and drastically simplify and reduce the burden and costs associated with systemic risk reporting. MFA also requests that the CFTC allow the National Futures Association ("**NFA**") to amend Form PQR to its pre-Dodd-Frank Act version and to make similar amendments to Form PR. These changes would further reduce regulatory costs and burdens for registered CPOs and CTAs while continuing to provide NFA with information it needs.

B. Foster Economic Growth and Vibrant Financial Markets by Abandoning the Proposed CFTC Position Limits Framework

MFA urges the CFTC to abandon its reproposed position limits rule (the "**Reproposal**").[6] We are strongly concerned that without having made a finding that excessive speculation exists in the markets or that position limits are necessary in each of the core referenced futures contracts, the Commission has failed to justify the economic need or basis for the Reproposal. Imposing unnecessary or inappropriate position limits will impair economic growth and place a greater burden on interstate commerce by hindering the ability of derivatives markets to: ensure that the price discovery function of the underlying market is not disrupted; and perform their fundamental risk transfer and risk management functions—both of which depend on the existence of liquid, fair and competitive markets to ensure sufficient market liquidity for *bona fide* hedgers.

[6] Position limits for Derivatives, 81 Fed. Reg. 96,704 (proposed Dec. 30, 2016), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2016-29483a.pdf.

APPENDIX

C. Adopt Regulatory Refinements to Improve CFTC Swaps Trading Framework

MFA urges the CFTC to improve the legal framework for trading over-the-counter ("**OTC**") derivatives on registered swap execution facilities ("**SEFs**"). MFA believes the CFTC's work to promote swaps trading on SEFs has benefitted investors through increased pre-trade price transparency, competition, and liquidity. However, the implementation of the SEF framework can be refined and improved. MFA believes the CFTC should:

(1) Allow investors more flexibility in how they trade swaps while: (i) enabling true impartial access to SEFs and execution methods for all eligible participants, and (ii) preserving crucial requirements for pre-trade price transparency, price competition, and a multiple-to-multiple trading system or platform;

(2) Assume responsibility for determining when particular swap contracts have to be SEF traded while carefully considering the distinct liquidity issues for any such contract; and

(3) Simplify and codify the existing universe of CFTC staff guidance and no-action relief that the CFTC used to smooth the implementation of the SEF framework.

D. Enhance Data Security and Treatment of Confidential Information

MFA urges the Commission to continue using the subpoena process for requesting confidential, commercially valuable intellectual property, and to enhance its policies and procedures for protecting such information. MFA and its members are concerned about the high risk and threat of cyberespionage and data security at regulatory agencies. The Commission should adopt a policy to refrain from asking for highly confidential and commercially valuable intellectual property from a registrant or market participant unless absolutely necessary; and when it asks for such information, it should be through a Commission issued subpoena. The Commission should also have special procedures for protecting such information.

E. Simplify Regulation of Automated Trading

MFA urges the Commission to abandon Regulation AT, as proposed. We remain concerned that the underlying framework of Regulation AT is flawed. As an inefficient and ineffective regulation, Regulation AT will inhibit economic growth and impose inappropriate restraints on a large swath of market participants. We strongly believe that the Commission should fundamentally revise the underlying framework and, thus, abandon Regulation AT, including its supplemental proposal, as proposed. The Commission should simplify and modernize regulatory oversight of automated trading by adopting targeted regulatory solutions to address marketplace risk.

APPENDIX

Division of Swap Dealer and Intermediary Oversight

F. Reduce Administrative Burden by Amending Part 4 Regulations Regarding Third-Party Recordkeeping

MFA commends the Commission for its adoption of final § 1.31, a modernized and significantly improved recordkeeping rule. MFA requests that the Commission allow CPOs and CTAs to engage in third-party recordkeeping arrangements without the need to make notice filings. Discrepancies between CFTC recordkeeping regulations for CPOs and CTAs and the SEC's recordkeeping arrangements for investment advisers make regulation burdensome and more expensive for dual registrants.

G. Exclude Compo Swaps From Calculation Under § 4.13(a)(3)

MFA requests that the Commission exclude "compo" equity total return swaps ("**compo swaps**") from calculation under § 4.13(a)(3) with respect to determining a pool's commodity interest position; and to issue related guidance. For regulatory simplification, we believe the Commission should allow a CPO to treat compo swaps as security-based swaps and exclude such products from its calculation of commodity interest positions for purposes of qualifying for an exemption from registration under § 4.13(a)(3), the *de minimis* trading exemption.

Division of Clearing and Risk

H. Advocate for Congress to Amend the Bankruptcy Code to Facilitate Full Physical Segregation of Customer Collateral

MFA requests that the Commission advocate for Congress to amend the Bankruptcy Code to facilitate full physical segregation of customer collateral. Ensuring the protection of customers and their collateral was one of Congress's goals under the Dodd-Frank Act; however, the current treatment of "customer property" under the Bankruptcy Code prevents customers and their assets from being fully protected from the failure of an FCM or another of the FCM's customers.

I. Encourage European Regulators to Resolve Equivalence Issues under EMIR Article 13 and MiFIR Article 33

MFA requests that the Commission engage with European authorities and encourage them to resolve equivalence issues under Article 13 of the European Market Infrastructure Regulation ("**EMIR**") and Article 33 of the Markets in Financial Instruments Regulation ("**MiFIR**"). As written, the language of Article 13 of EMIR and Article 33 of MiFIR prevent certain U.S. persons from satisfying their regulatory obligations under EMIR and MiFIR by complying with equivalent U.S. rules because those U.S. persons are not "established" in the U.S. This issue deeply affects the fund industry and the European banks with which they trade derivatives, and will hamper the ability of these market participants to continue to trade derivatives on a cross-border basis.

APPENDIX

J. Protect the Assets and Interests of Customers in Regulations on CCP Recovery and Resolution

MFA believes that any regulations addressing the recovery or resolution of central counterparties ("**CCPs**") should protect the assets and interests of customers. As the Commission continues to consider whether it should issue regulations on this issue, we urge the Commission to ensure that it is protecting customers by allowing certain key principles to guide it. In particular, discussions of this issue have primarily taken place among regulators, CCPs, and FCMs, with customers being largely excluded, even though use of customer assets has been emphasized as a potential loss allocation tool. Because MFA's members manage the assets of their investor and taxpayer clients, any use of customer assets during a CCP's recovery or resolution results in losses to these investors and taxpayers, which is contrary to the core principles of the Dodd-Frank Act.

K. Recalibrate and Reduce Initial Margin Requirements to Better Reflect the Actual Risk of Certain Non-Clearable Swap Products

MFA believes that the Commission needs to recalibrate and appropriately tailor the initial margin ("**IM**") requirements for uncleared swaps to reflect the actual risk posed by certain non-clearable swap products, such as total return swaps ("**TRS**") for complex equity trades. Many hedge funds trade such TRS to achieve exposure to equities. However, as banks do not trade such TRS among themselves, our requested tailored revision to IM requirements for such products would present relatively little systemic risk. Therefore, funds that use non-clearable TRS should not be penalized by having to over-collateralize them based on the higher IM requirements that will be coming into effect for their uncleared trades on September 1, 2019 or 2020.

Division of Market Oversight

L. Reduce Complexity of Cleared Swap Reporting Requirements by Eliminating Alpha Swap Reporting

MFA believes the CFTC should eliminate alpha swap reporting requirements to reduce the reporting complexities of its cleared swaps reporting regime and to streamline the data actually reported without sacrificing the amount of information available to the CFTC regarding the entire life cycle of a swap. As you noted in a recent interview,[7] the Commission only needs the final information reported by the CCP concerning the beta/gamma swaps comprising a cleared swap for effective oversight.

[7] "Giancarlo orders review of CFTC rules", *Risk.net,* March 15, 2017.

APPENDIX

Bank Capital Regulations Affecting Customer Clearing

M. Recalibrate Leverage Ratio for Cleared Derivatives to Allow Offset for Segregated Client Initial Margin

MFA seeks the CFTC's help as a voting member of FSOC to achieve an important recalibration in the leverage ratio for cleared derivatives that will have a profound impact on customer clearing. As you noted in your recent public remarks, the CFTC has an influential role to play in achieving recalibrated bank regulatory capital requirements and leverage ratios to "better balance systemic risk concerns with healthy economic growth and American prosperity."[8] To ensure the continued affordability and robustness of customer clearing in the U.S., MFA suggests that bank regulators should recalibrate the leverage ratio rules to allow clearing members of CCPs to offset segregated IM when calculating exposure.

II. DISCUSSION OF ISSUES

In the spirit of refining and modernizing derivatives regulation to enhance efficiency and reduce regulatory burden, we have provided detailed discussions of our regulatory recommendations and the potential impact of these rule proposals. Please note that MFA has also previously submitted comment letters describing our recommendations in response to the CFTC's formal requests for comment. We would encourage you and the Staff to also refer to these letters, links to which are provided in the discussions.

A. Commodity Pool Operator & Commodity Trading Advisor Regulations

In the spirit of the President's "Core Principles for Regulating the United States Financial System,"[9] we believe that the CFTC and the SEC should rationalize investment manager regulation and systemic risk/compliance reporting requirements between the two agencies. Subjecting investment managers to two similar but slightly different regulatory frameworks have made regulation inefficient, ineffective, and extremely burdensome. SEC-registered investment management firms devote significant resources, including hundreds of thousands of hours, towards compliance with an additional regulatory regime. Similarly, we believe that such duplicative regulation is an unnecessary use of government resources. Thus, we propose that the Commission reinstate an exemption from CPO registration for investment firms registered with the SEC as investment advisers and unify and streamline systemic risk reporting with the SEC. In addition,

[8] *See* Giancarlo Boca Speech, *supra* note 2. *See also* "Changing Swaps Trading Liquidity, Market Fragmentation and Regulatory Comity in Post-Reform Global Swaps Markets," Remarks of Acting Chairman J. Christopher Giancarlo before the International Swaps and Derivatives Association 32nd Annual Meeting in Lisbon, Portugal, May 10, 2017 (expressing concerns with the "misguided application" of the supplementary leverage ratio (SLR) to swaps clearing and proposing suggested SLR rule changes to reduce capital costs for clearing members).

[9] Presidential Executive Order on Core Principles for Regulating the United States Financial System, *supra* note 5.

APPENDIX

we believe the Commission should reduce the extraterritorial scope of its CPO and CTA regulations, and modernize and update the Part 4 regulations, as discussed further below.

1. **Reduce Redundant Oversight and Reinstate § 4.13(a)(4) for Investment Management Firms Overseen by the SEC; Reduce Extraterritorial Scope; and Modernize and Update Regulation for those Entities that Should Remain Subject to CFTC Oversight**

MFA requests that the Commission reinstate CFTC § 4.13(a)(4), an exemption from registration for a CPO of a private commodity pool, for a CPO that is registered as an investment adviser with the SEC or affiliated with an SEC-registered investment adviser.[10] Such exemption will reduce duplicative registration and regulatory requirements with the SEC as well as the corresponding regulatory expenses and make regulation efficient, effective, and appropriately tailored for investment managers.[11] MFA also recognizes that the current CPO registration framework is overly broad in its extraterritorial reach and encourages the Commission to work with AIMA and other industry associations and foreign investment advisers to adopt a reasonable exemption for foreign investment advisers that would not be covered by any relief granted in response to our request for relief for SEC-registered investment advisers or their affiliated entities.

Reduce Redundant Oversight of Investment Managers

In 2012, not as a requirement, but in the "spirit" of the Dodd-Frank Act, the CFTC rescinded § 4.13(a)(4), which provided a person with an exemption from registration as a CPO if the interests in the pool were exempt from registration under the Securities Act of 1933 and the

[10] Many investment advisers have affiliated entities, which may be separately registered as investment advisers, CTAs, or CPOs, that provide services to investment funds managed by the registered adviser. For example, a private investment fund managed by a registered investment adviser may have a separate, affiliated entity that is the general partner and CPO of the fund. The SEC has recognized that an SEC-registered investment adviser may have affiliates that fall under the investment adviser definition and provides an exemption from registration under the Investment Advisers Act, provided certain conditions are met. *See generally ABA Subcommittee on Private Investment Entities*, SEC No-Action Letter (Dec. 8, 2005) and *American Bar Association Section of Business Law*, SEC No-Action Letter (Jan. 18, 2012). In these letters, the SEC staff has permitted special purpose entities ("SPVs") that act as general partners or managing members of private funds not to register under the Advisers Act if, among other conditions, the private funds are advised by a registered investment adviser and the SPVs are subject to the Advisers Act and the rules thereunder and subject to examination by the SEC. Similarly, the CFTC has allowed certain affiliated entities, to claim an exemption from CPO registration by delegating the CPO function to an affiliated registered CPO and meeting certain requirements. We believe the CFTC should include these types of entities affiliated with a registered investment adviser within the scope of the exemption.

[11] MFA has requested that the SEC adopt a rule or issue guidance that would subject firms to adviser registration with either the SEC or CFTC, depending on whether it is primarily engaged in the business of advising on trading in securities or futures, options, and/or swaps. *See* letter from Stuart J. Kaswell, Executive Vice President, Managing Director and General Counsel, MFA, to Jay Clayton, Chairman, SEC, dated May 18, 2017 on Regulatory Priorities, available at: https://www.managedfunds.org/wp-content/uploads/2017/05/MFA-Regulatory-Priorities-Letter-to-SEC-Chairman-Clayton.pdf.

APPENDIX

operator reasonably believes that the participants are all qualified eligible persons.[12] MFA does not believe that the Commission documented a clear record of abuse that justified its rescission of the exemption, nor do we believe that the Commission can point to any tangible record of benefits that have resulted as a consequence of the repeal. In 2011, MFA submitted comments in response to the Commission's proposal to rescind § 4.13(a)(4) and argued, among other things, that: (1) rescission was unnecessary to achieve the public policy objectives of the Dodd-Frank Act; (2) § 4.13(a)(4) was consistent with and embedded in current law and inter-agency comity; (3) the Commission would still receive information it needed of private pools; and (4) rescission of § 4.13(a)(4) would be costly for managers.[13] We attach a copy of this letter as **Appendix A**. Unfortunately, rescission of § 4.13(a)(4) has increased dramatically the cost of operating an investment adviser. MFA believes that the CFTC should reinstate § 4.13(a)(4) for investment firms with advisers registered with and overseen by the SEC whether based inside or outside the United States—a narrower exemption than the original § 4.13(a)(4) exemption. Under our proposal, operators that are not registered with the SEC or affiliated with an SEC-registered investment adviser to the pool would still be required to register with the CFTC as a CPO.

The CFTC's rescission of § 4.13(a)(4) created a series of follow-on problems that imposed regulatory requirements on additional entities in circumstances that did not serve a clear public policy purpose. For example, the repeal required investment advisers (or affiliated entities) of privately offered investment funds that were registered with the SEC also to register with the CFTC unless they met the terms of one of the substantially narrower available exemptions.[14] The CFTC's final rule release regarding the rescission of § 4.13(a)(4) required investment advisers of fund-of-funds, including advisers that only invested in securities, to look through the holdings of their independent investments to determine whether they had a registration requirement.[15] As a result

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[12] *See* Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, 77 Fed. Reg. 11252 (Feb. 24, 2012), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2012-3390a.pdf. One could argue that the CFTC's action was not consistent with the "spirit" of the Dodd-Frank Act since sections 403 and 749 amended the Investment Advisers Act of 1940 and the Commodity Exchange Act to more clearly exempt from registration an entity registered with one agency and not engaged primarily in trading products overseen by the other agency. In other words, the Dodd-Frank Act itself sought to reduce redundant regulation, not add to it.

[13] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to David A. Stawick, Secretary, CFTC, dated Apr. 12, 2011, on Proposal to Rescind Sections 4.13(a)(3) and (a)(4), available at: http://www.managedfunds.org/wp-content/uploads/2011/06/4.12.11-MFA-CTA_CPO-Amendments-final.4.12.11.pdf. This letter is attached as Appendix A.

[14] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to David A. Stawick, Secretary, CFTC, dated Apr. 12, 2011, on Proposal to Rescind Sections 4.13(a)(3) and (a)(4), available at: http://www.managedfunds.org/wp-content/uploads/2011/06/4.12.11-MFA-CTA_CPO-Amendments-final.4.12.11.pdf. This letter is attached as Appendix A. *See also* CFTC § 3.10(c)(3)(i), Exemption from registration for certain persons.

[15] MFA has raised the concern that managers of fund-of-funds generally do not have position-level transparency of the funds in which they invest and to the extent they receive any such information it is on a delayed basis (*e.g.*, quarter-end), which makes it difficult for a CPO to calculate whether the fund indirectly trades more than a *de minimis* level of commodity interests, pursuant to CFTC § 4.13(a)(3). *See* letter from Karen L. Barr, General Counsel, Investment Adviser Association, and Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel,

APPENDIX

of the rescission, many SEC-registered investment advisers (and/or affiliated entities) were required to be dually registered with both the SEC and CFTC, subject to two similar but different sets of regulatory requirements, and subject to multiple regulatory filings designed to achieve the same objectives (*i.e.*, Forms PF, CPO-PQR and CTA-PR). Further, the Commission's rescission of § 4.13(a)(4) greatly expanded the extraterritorial application of the CFTC's CPO and CTA regulations. Operators of a non-U.S. commodity pool with a single U.S. investor became subject to CPO regulation, as well as operators and/or advisors of non-U.S. commodity pools that engaged in even a single uncleared swap transaction with a U.S. counterparty.

Dual registrants have had to reconcile different regulatory requirements which has been extremely burdensome, especially as the CFTC has not had the resources to timely address regulatory interpretive issues. For example, we spent over two years urging the CFTC staff to provide relief with respect to the issue of CPO delegation,[16] and after the CFTC staff issued its initial No-Action relief,[17] following our request for further guidance and self-executing relief, the CFTC staff issued subsequent relief acknowledging that its prior letter posed too great a burden on the Division of Swap Dealer and Intermediary Oversight's limited resources.[18] While the CFTC staff has provided some relief, we continue to have concerns with how broadly it interprets the definition of CPO. Similarly, the CFTC has interpreted a broader number of related entities to a CPO registrant as "CPOs" or "commodity pools" for which a Form CPO-PQR needs to be filed, including pass-through vehicles that have no investors, creating additional filings and calculations which greatly increase compliance burdens but provide little additional regulatory value.

Managed Funds Association, 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, available at: https://www.managedfunds.org/wp-content/uploads/2012/11/IAA-MFA-Comment-Letter-to-CFTC-re-Extension-of-Compliance-Date-of-Former-Appendix-A-11-9-12.pdf; *and* CFTC Staff Letter No. 12-38 (Nov. 29, 2012), available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/12-38.pdf.

[16] The CFTC staff has held the view that a general partner, managing member or board of directors of a commodity pool, among others, may be considered a CPO and required to either register or delegate its rights and obligations as a CPO to a registered CPO. Initially, the CFTC staff took the position that each entity needed to seek individual no-action relief in order to delegate the CPO function, which we did not believe was a practical solution. Typically, large private investment companies have both domestic and offshore funds (*i.e.*, funds established outside the United States). Offshore funds are generally structured as corporate entities (rather than, for instance, as limited partnerships, as is common in the United States) and are governed by a board of directors. Such fund generally appoints a separate entity to serve as the fund's CPO (the "Designated CPO"). While the Designated CPO also may provide commodity interest trading advice and/or investment advice to the fund, often the Designated CPO appoints a separate entity (or entities) for this purpose. These arrangements can require multiple entities and individuals to either register as CPOs or seek No-Action relief to delegate the CPO function. *See* letter from Stuart J. Kaswell, EVP & Managing Director, General Counsel, MFA, to Mr. Gary Barnett, Director, Division of Swap Dealer and Intermediary Oversight, CFTC, July 15, 2014, available at: https://www.managedfunds.org/wp-content/uploads/2014/07/MFA-CPO-Delegation-Follow-up-to-Letter-14-69.final_.7.15.14.pdf.

[17] *See* CFTC Staff Letter No. 14-69, May 12, 2014, available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/14-69.pdf.

[18] *See* CFTC Staff Letter No. 14-126, October 15, 2014, available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/14-126.pdf.

APPENDIX

Modernize and Update the Part 4 Regulations

In addition, MFA believes that the CFTC's Part 4 regulations have not kept pace with industry changes and other developments concerning CPOs and CTAs. For example, CPOs and CTAs have had concerns with the CFTC's limitations with respect to the use of third-party recordkeepers.[19] We are pleased to see that the CFTC has recently amended § 1.31.[20] However, differences between the CFTC's and the SEC's regulations contribute to increased regulatory costs for registrants with no additional value. Separately, we believe the Commission needs to modernize its Part 4 regulations to streamline regulation and make compliance more accessible for entities that remain registrants. Currently, it is extremely difficult for a CPO or CTA to ensure compliance with the CFTC Part 4 rules without retaining outside counsel with CPO/CTA expertise because a significant amount of rulemaking is found in CFTC staff letters from the past 10 or more years. These are only some of the examples of the concerns we have relating to CFTC part 4 regulations and/or guidance and would be pleased to separately discuss updating the CFTC's part 4 regulations to make regulation more efficient and less costly.

We believe that regulators have alternative tools to assist with effective industry oversight, and that CPO registration of SEC-registered investment advisers or their affiliates is not necessary to achieve the public policy objectives of promoting transparency and oversight of market participants. For example, the Dodd-Frank Act requires the SEC to share systemic risk information collected under Form PF with the CFTC, as a member of the Financial Stability Oversight Council ("**FSOC**").[21] Moreover, pursuant to legislative and regulatory requirements with respect to reporting and recordkeeping of cleared and uncleared swaps, the CFTC has access to detailed transaction-level information of commodity interest contracts.[22] Thus, the CFTC would continue to have necessary information on firms that would heretofore be registered as CPOs or CTAs, but that are registered with the SEC as investment advisers. To minimize duplicative registration and regulatory requirements of such firms, and to reduce the associated costs for regulators and market participants, the CFTC should provide an exemption from CPO registration for investment advisers registered with the SEC or affiliated with an SEC-registered investment adviser.[23]

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[19] Petition for Rulemaking to Amend CFTC §§ 1.31, 4.7(b) and (c), 4.23 and 4.33, Managed Funds Association, Investment Adviser Association, and Alternative Investment Management Association (July. 21, 2014), available at: https://www.managedfunds.org/wp-content/uploads/2014/07/Final-Petition.pdf.

[20] Final Recordkeeping Rule 1.31, 82 Fed. Reg. 24,479 (May 30, 2017), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2017-11014a.pdf; *and* Proposed Amendments to § 1.31, 82 Fed. Reg. 6356 (Jan. 19, 2017). *See also* joint comment letter available at: https://www.managedfunds.org/wp-content/uploads/2017/03/MFA-AIMA-IAA-AMG-CFTC-Recordkeeping-Comment-Letter.final_.3.20.17.pdf.

[21] Section 404 of the Dodd-Frank Act.

[22] *See generally*, CFTC Parts 16 - 20, 45 and 49 Regulations.

[23] *See* discussion below on regulatory requirements.

APPENDIX

Accordingly, MFA recommends that the CFTC reinstate § 4.13(a)(4) for investment firms with advisers registered with the SEC or affiliated with an SEC-registered investment adviser; and encourages the Commission to work with AIMA and other industry associations and foreign investment advisers to adopt a reasonable exemption for foreign investment advisers that would not be covered by any relief granted in response to our request for relief for SEC-registered investment advisers or their affiliates. MFA also recommends that the Commission modernize and update the CFTC Part 4 regulations.

2. Unify and Streamline Systemic Risk Reporting with the SEC

MFA requests that the CFTC and the SEC simplify and streamline systemic risk reporting by using a single, shorter systemic risk report administered by the SEC. Such a report would greatly enhance regulatory efficiency, and drastically simplify and reduce the burden and costs associated with systemic risk reporting. MFA also requests that the CFTC allow NFA to amend Form PQR to its pre-Dodd-Frank Act version. This change would further reduce regulatory costs and burdens for registered CPOs and CTAs while continuing to provide NFA with information it needs.

The Dodd-Frank Act requires the SEC and the CFTC, after consultation with FSOC, to jointly promulgate rules to establish private fund reports to be filed by dual registrants.[24] Instead, the SEC, CFTC, and NFA each require registrants to file slightly different systemic risk reports.[25] Investment firms that are registered as investment advisers, CPOs and CTAs are required to routinely file Forms PF, CPO-PQR, CTA-PR, PQR and PR.[26] The SEC and CFTC forms request for similar information, such as a schedule of investments. However, because the SEC and CFTC use different definitions, instruct registrants to use different methodologies to calculate responses, and the SEC allows registrants to file Form PF for a fund on an aggregated basis (*i.e.*, reporting master-feeder and trading subsidiaries on an aggregated basis) while the CFTC requires registrants to file Form CPO-PQR on a legal entity-by-entity basis, dual registrants file different systemic reports with the SEC and CFTC. Separately, while the SEC and CFTC take into consideration the size of a firm in determining the frequency of the filing, NFA requires all CPOs and CTAs to file

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[24] Section 406 of the Dodd-Frank Act.

[25] The CFTC allows a CPO that is also registered with the SEC to satisfy a portion of its Form CPO-PQR filing requirements by filing Form PF with the SEC. However, such CPO still is required to file schedule A of Form CPO-PQR, which includes the burdensome and lengthy request for a schedule of investments. *See* Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, *supra* note 12 at 11,288 (providing reporting instructions).

[26] *See* Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, *supra* note 12; Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF, 76 Fed. Reg. 71,128 (Nov. 16, 2011), available at: https://www.gpo.gov/fdsys/pkg/FR-2011-11-16/pdf/2011-28549.pdf; *and* NFA Rule 2-46, CPO and CTA Quarterly Reporting Requirements, available at: http://www.nfa.futures.org/nfamanual/NFAManual.aspx?RuleID=RULE%202-46&Section=4.

APPENDIX

quarterly reports.[27] Implementing separate processes for collecting and compiling data required by the different forms has been extremely burdensome and costly for registrants, causing registrants to expend thousands of hours each quarter to prepare the reports and respond to follow-up questions from regulators.

Similarly, each regulator also likely expends significant resources replicating analyses performed by other regulators. In addition, the SEC and CFTC forms do not lend themselves to being aggregated by FSOC. It is not clear that the differences in, or vast amounts of, data received by regulators have provided any measurable regulatory benefits, while the costs to registrants and regulators have been substantial. The SEC's Private Funds Statistics Reports indicate that private investment funds are not a source of systemic risk.[28] It is not clear to us whether the CFTC has had resources to dedicate to routinely analyze the reports from CPOs and CTAs. We understand that many of the data that the CFTC requested in Forms CPO-PQR and CTA-PR are not necessary for NFA; and that the pre-Dodd-Frank Act quarterly reports would be sufficient for NFA's regulatory purposes.

To simplify regulation, make it more efficient, conserve government resources, and reduce burden on regulators and registrants alike, the CFTC and the SEC should unify systemic risk reporting and adopt a single, shorter report administered by the SEC. MFA believes it would be more efficient for the same regulatory staff to both request and administer the systemic risk form, as registrants have found it inefficient for the CFTC and NFA staffs to share the responsibility. Further, we believe a single form would be more helpful to FSOC as it would allow FSOC to aggregate data from both regulators. Finally, a single, uniform systemic risk form would greatly reduce regulatory inconsistency, support good governance, and reduce cost and burden on registrants. NFA's pre-Dodd-Frank Act quarterly report was shorter and narrower in scope than the Forms CPO-PQR or PQR, and served NFA's purposes. We believe NFA should return to using its pre-Dodd-Frank Act quarterly report.

Accordingly, MFA recommends that the SEC and CFTC simplify and streamline systemic risk reporting by using a single, shorter systemic risk report administered by the SEC. MFA recommends that the CFTC allow NFA to amend Form PQR to its pre-Dodd-Frank Act version.

B. Foster Economic Growth and Vibrant Financial Markets by Abandoning the Proposed CFTC Position Limits Framework

The CFTC should not adopt the Reproposal. We are strongly concerned that without having made a finding that excessive speculation exists in the markets or that position limits are necessary in each of the core referenced futures contracts, the Commission has failed to justify the economic need or basis for the Reproposal. Imposing unnecessary or inappropriate position limits

[27] *Id.*

[28] *See* SEC Division of Investment Management Private Fund Statistics Reports, available at: https://www.sec.gov/divisions/investment/private-funds-statistics.shtml.

APPENDIX

will impair economic growth and place a greater burden on interstate commerce by hindering the ability of derivatives markets to: ensure that the price discovery function of the underlying market is not disrupted; and perform their fundamental risk transfer and risk management functions—both of which depend on the existence of liquid, fair and competitive markets to ensure sufficient market liquidity for *bona fide* hedgers. MFA does not support the Reproposal and urges the Commission to abandon it and reconsider what, if any, additional regulations are needed to meet its statutory objectives.

MFA welcomes a return to regular order and your remarks regarding "a return to greater care and precision in rule drafting" and "more thorough econometric analysis."[29] Regulatory policy, especially a policy as significant and with such a profound market impact as position limits, should be designed based on sound market and economic principles. MFA is concerned that the regulatory steps in the Reproposal are flawed and are potentially harmful to the health of the markets as they will reduce liquidity in U.S. derivatives markets. Aside from the overall imposition of position limits, the Reproposal will also deter use of the U.S. futures markets due to the regulatory and administrative complexity and costs associated with it.

Position limits are a crude and inefficient tool for deterring market manipulation because it is difficult to set limits at a level that inhibits market manipulation without unduly affecting the ability of markets to efficiently transfer risk. The Commission has better alternatives than to use such a blunt instrument for deterring market manipulation. Through the use of the current position reporting and market surveillance regime, and the ability to impose penalties for disruptive market behavior, the Commission and exchange surveillance staffs can detect and prevent corners, squeezes, and other forms of manipulation. It is preferable, therefore, to use readily available market data and the Commission's statutory authority to investigate and prosecute aggressive traders that manipulate or attempt to manipulate the market, rather than to limit the trading activity of all other market participants through position limits. An effective enforcement regime will discourage manipulation and assure a proper balance – preventing excessive speculation and deterring market manipulation, while ensuring sufficient market liquidity and price discovery.[30]

Accordingly, MFA urges the Commission to abandon the Reproposal. MFA remains interested in working with the Commission to address its concerns through regulations that are practical and based on sound market and economic principles. If the Commission determines to move forward with implementing position limits, we respectfully urge that the Commission narrowly tailor the regulatory framework to achieve a specific market outcome, in a way that is designed to be minimally disruptive, practical, and not overly complicated to administer by market participants. A concern that we raised with the Reproposal and the Commission's final

[29] *See* Giancarlo Boca Speech, *supra* note 2.

[30] The CFTC has recognized that there is academic support for this notion, and has cited to a study by Craig Pirrong ("Squeezes, Corpses, and the Anti-Manipulation Provisions of the Commodity Exchange Act," Oct. 1, 1994). Position Limits for Derivatives, 78 Fed. Reg. at 75,695, available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2013-27200a.pdf.

APPENDIX

aggregation rule[31] is that both these regulations are drafted in ways that unnecessarily create operational and interpretive challenges, making compliance complex, expensive and burdensome. For specific comments on the Reproposal, we refer the Commission to MFA's letter in response to the Reproposal, linked below.[32]

C. Adopt Regulatory Refinements to Improve CFTC Swaps Trading Framework

MFA urges the CFTC to improve the legal framework for SEF trading. MFA believes the CFTC's work to promote swaps trading on SEFs has benefitted investors through increased pre-trade price transparency, competition, and liquidity. However, the implementation of the SEF framework can be refined and improved. MFA believes the CFTC should:

(1) Allow investors more flexibility in how they trade swaps while: (i) enabling true impartial access to SEFs and execution methods for all eligible participants, and (ii) preserving crucial requirements for pre-trade price transparency, price competition, and a multiple-to-multiple trading system or platform;

(2) Assume responsibility for determining when particular swap contracts have to be SEF traded while carefully considering the distinct liquidity issues for any such contract; and

(3) Simplify and codify the existing universe of CFTC staff guidance and no-action relief that the CFTC used to smooth the implementation of the SEF framework.

In October 2015, MFA submitted a petition to the CFTC to amend certain provisions of its regulations related to OTC derivatives trading on SEFs, based on MFA members' experiences to date and the "lessons learned" through the implementation process.[33] We outline below our

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[31] Aggregation of Positions, 81 Fed. Reg. 91,454 (Dec. 16, 2016), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2016-29582a.pdf.

[32] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Christopher Kirkpatrick, Secretary, CFTC, on Feb. 28, 2017, on Position Limits for Derivatives, available at: https://www.managedfunds.org/wp-content/uploads/2017/02/Final_Position-Limits-Comment-Letter-2017-MFA-AIMA-SIFMA-AMG.pdf.

[33] *See* MFA Petition for Rulemaking to Amend Certain CFTC Regulations in Parts 1 (General Regulations under the Commodity Exchange Act), 39 (Derivatives Clearing Organizations, Subpart B – Compliance with Core Principles) and 43 (Real-Time Public Reporting), submitted to Mr. Christopher Kirkpatrick, Secretary of the Commission, on October 22, 2015 ("**MFA SEF Petition**"), available at: https://www.managedfunds.org/wp-content/uploads/2015/10/CFTC-Petition-for-SEF-Rules-Amendments-MFA-Final-Letter-with-Appendix-A-Oct-22-2015.pdf.

APPENDIX

updated positions and requests on key areas of regulatory reform for the CFTC's swaps trading framework raised in your White Paper,[34] as well as in your recent speeches earlier this year.[35]

1. Methods of Execution

MFA supports a broader variety of execution methods so long as: (i) true impartial access to SEFs and execution methods are provided to all eligible participants, and (ii) requirements for pre-trade price transparency, price competition and a multiple-to-multiple trading system or platform are preserved.

The promotion of pre-trade price transparency on SEFs is an express goal of the Dodd-Frank Act.[36] MFA is concerned that the potential regulatory elimination of the order book and request-for-quote ("**RFQ**")-to-3 execution protocols, which are designed to provide pre-trade price transparency, could undermine the pre-trade price transparency statutory goal for SEFs.

MFA is also concerned that the potential elimination of the current required methods of execution (*i.e.*, the order book and RFQ-to-3 execution methods) would remove pre-trade transparency in the U.S. SEF trading regime, and thereby raise a point of difference with the EU's MiFID II regulations governing pre-trade transparency of OTC derivatives trading on multilateral trading facilities ("**MTFs**") and organised trading facilities ("**OTFs**"). MFA encourages the CFTC to consider carefully introducing additional points of difference with the EU derivatives trading regime to avoid undermining equivalence and comparability determinations.

2. MAT Determination Process

While expanding the methods of execution available on SEFs would be a welcome development, the CFTC's authorization of more flexible execution methods does not mean that all mandatorily cleared, non-MAT products will suddenly be suitable for SEF trading. In MFA's view, flexibility in execution alone is not enough to promote swaps trading on SEFs, as it would not address the sufficiency of a product's liquidity or the ability of all eligible market participants to access all SEFs that will offer broader methods of execution and diverse liquidity in trading the product.

MFA supports the CFTC assuming a more meaningful oversight role in the "made available to trade" ("**MAT**") determination process, including its ability to reject MAT determinations from SEFs. MFA strongly suggests that the CFTC keep the MAT determination process separate from the clearing determination, because clearing suitability does not assess

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[34] *See* "Pro-Reform Reconsideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank", White Paper, by Commissioner J. Christopher Giancarlo, issued on January 29, 2015 ("**Giancarlo White Paper**"), available at: http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/sefwhitepaper012915.pdf.

[35] *See* Keynote Address of CFTC Commissioner J. Christopher Giancarlo Before SEFCON VII, "Making Market Reform Work for America", January 18, 2017, available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo-19; *see also* Giancarlo Boca Speech, *supra* note 2.

[36] *See* section 733 of the Dodd-Frank Act, adding Commodity Exchange Act (CEA) section 5h(e); 7 U.S.C. 7b-3(e).

APPENDIX

adequately the liquidity features of the swap product in question. MFA believes the CFTC has an important role to play in carefully considering the distinct liquidity-related factors with respect to a clearing-mandated swap product before requiring it to trade on-SEF. MFA urges the CFTC not to adopt a simplistic construction of the trade execution requirement that would require any mandatorily cleared and listed swap product automatically to become subject to the trading mandate. MFA fears that such a construction would inextricably link the trading mandate to the clearing mandate and discourage the industry from bringing more products into central clearing.

In that connection, MFA reiterates the MFA SEF Petition request to provide a mandatory comment period for every MAT determination submission by a SEF or a designated contract market ("**DCM**") under Part 40 of the Commission's regulations. MFA also reiterates the MFA SEF Petition request to establish a clear de-MAT determination process when a swap product no longer exhibits the requisite liquidity profile to trade on-SEF.

MFA agrees with many of your concerns with respect to package transactions.[37] MFA encourages the CFTC to consider the proposed amendments in the MFA SEF Petition as an alternative approach to resolve those concerns by requiring SEFs to make MAT determinations separately for a given swap when executed on a stand-alone basis and for different types of package transactions that include such a swap.

Taken together, MFA's proposed amendments in the MFA SEF Petition with respect to the MAT determination process would improve the CFTC's process and facilitate equivalence discussions with the EU by moving the CFTC's process a step closer in comparability to the European Securities and Markets Authority's ("**ESMA**") process for determining which mandatorily cleared OTC derivative products will become subject to the derivatives trading obligation under the MiFID II regime.

3. Impartial Access

MFA believes the buy-side should have fair, unbiased and unprejudiced access to SEFs that offer more execution modalities. More specifically, the buy-side needs true impartial access, without adverse commercial repercussions, to legacy interdealer broker ("**IDB**") SEF order books and voice-brokered IDB trading functionality in order to more efficiently trade package transactions and stand-alone swaps that are not MAT. Our position is based on the serious challenges MFA members continue to face trading such products using the RFQ system on dealer-to-customer SEFs, where they have lost the ability to place resting orders.

The CFTC should enforce true impartial access to all SEFs, in conjunction with authorizing more flexible execution methods on SEFs, by removing artificial barriers that hinder the achievement of the Dodd-Frank Act goals to promote swaps trading and pre-trade price transparency on SEFs. MFA believes that the current bifurcated swaps market structure has not,

[37] *See* Giancarlo White Paper at p. 26 (stating that "many package transactions are ill-suited to Order Book or RFQ System execution given their limited liquidity and complex characteristics.")

APPENDIX

and will not, achieve these statutory goals if such barriers to true impartial access persist in the U.S. SEF regime. We highlight examples of such barriers below.

As MFA explained in its position paper,[38] the legacy practice of post-trade name disclosure or "name give-up" on IDB SEFs that offer anonymous execution of cleared swaps is a key mechanism that continues to prevent the buy-side from accessing important pools of liquidity for cleared swaps, including the only liquid order books. The practice's exclusionary effect on otherwise qualified buy-side market participants is status-based discrimination and thus inconsistent with the impartial access mandate for SEFs. MFA believes that the practice also reduces pre-trade price transparency for otherwise qualified buy-side market participants and restricts their ability to trade certain swap products anonymously. The effects of this practice are anti-competitive and have been challenged in recent federal antitrust lawsuits brought in the U.S. District Court, Southern District of New York. MFA believes that if the free market was going to address the effects of this anti-competitive practice organically, it would have done so by now. However, it is difficult for any one IDB SEF to disable post-trade name disclosure unilaterally, as traditional dealers that opposed such a change might easily shift their trading to other IDB SEFs. This is a classic case where the CFTC, as the primary regulator of the U.S. swaps market, can readily bring competition and fairness to the market.

With respect to the use of enablement mechanisms and breakage agreements for swaps that are intended to be cleared on SEFs, MFA reiterates the MFA SEF Petition request to prohibit such arrangements by codifying existing CFTC staff guidance around the implementation of the CFTC's impartial access requirements.

MFA members also remain concerned with the lack of transparency concerning SEF fee structures. As regulated entities, all SEFs should be required to publish their fee schedules. MFA understands that certain SEFs have pricing schemes and volume rebates that deter buy-side access, as pricing is only viable and affordable for certain firms to access such SEFs.

MFA also urges the CFTC to finalize dealer ownership restrictions or thresholds for SEF governance, as dealer-dominated SEFs create the risk of conflicts of interest.

Similar to the U.S. impartial access requirement, the European MiFID II legislation requires trading venues to provide non-discriminatory access to market participants.[39] As such, there should be no difference between the two regimes on this topic, though European regulators may be required to issue additional guidance (similar to the CFTC's impartial access guidance[40])

[38] *See* MFA Position Paper: *Why Eliminating Post-Trade Name Disclosure Will Improve the Swaps Market*, dated March 31, 2015, available at: https://www.managedfunds.org/wp-content/uploads/2015/04/MFA-Position-Paper-on-Post-Trade-Name-Disclosure-Final.pdf.

[39] *See* Article 18(3) of the MiFID II Directive governing MTFs and OTFs, and Article 53(1) of the MiFID II Directive governing regulated markets.

[40] *See* "Division of Clearing and Risk, Division of Market Oversight and Division of Swap Dealer and Intermediary Oversight Guidance on Application of Certain Commission Regulations to Swap Execution Facilities", issued Nov.

APPENDIX

in order to ensure that the non-discriminatory access requirement is properly implemented. MFA believes that ensuring equivalent standards with respect to the implementation of impartial access should be a key focus in future discussions regarding harmonization and regulatory equivalence.

4. STP and Void *Ab Initio*

MFA reiterates the MFA SEF Petition request to codify existing CFTC staff guidance around the CFTC's straight-through processing ("**STP**") requirements. MFA believes that STP is critical to a competitive, open and transparent market for swaps that are intended to be cleared.

STP benefits all market participants, especially smaller market participants and alternative liquidity providers that could otherwise encounter barriers to entry, in that it: (i) gives market participants certainty of clearing immediately following execution, which in turn, allows them to hedge more efficiently and effectively manage risk; (ii) is an important factor in encouraging the implementation of broad, mandatory clearing; (iii) is essential to electronic trading, particularly central limit order book trading, as it is not possible to enter into an electronic transaction on an anonymous basis without both the immediate confirmation of the execution of the transaction and its acceptance for clearing; and (iv) promotes accessible, competitive markets and access to best execution by ensuring parties to a cleared transaction have immediate confirmation that they will face the relevant CCP, thus eliminating the need to negotiate individual credit arrangements with each of their counterparties, as is required in bilateral derivatives markets.

MFA views void *ab initio* as an important part of the STP regime that should be preserved. More specifically, MFA reiterates the MFA SEF Petition Request to codify, with clarifying modifications, existing CFTC staff guidance and extended no-action relief under CFTC No-Action Letter 17-27 around rejection of swaps from clearing and resubmission for operational and clerical errors.[41]

MFA notes that ESMA included both void *ab initio* and a resubmission procedure in its regulatory technical standards under the EU's MiFID II/MiFIR. As a result, codifying these points would further facilitate harmonization between SEFs/DCMs and MiFID II trading venues.

5. The "Occurs Away" Requirement for Block Trades

MFA believes the "occurs away" requirement is unnecessarily complex, and agrees with your views on this issue. Accordingly, MFA reiterates the MFA SEF Petition request to modify the definition of "block trade" in Part 43 of the Commission's regulations to authorize on-SEF execution of a block trade as a Permitted Transaction, as defined in section 37.9(c), in order to facilitate pre-execution credit checks of block trades that are intended to be cleared.

14, 2013, available at: http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/dmostaffguidance111413.pdf.

[41] *See* CFTC Staff Letter No. 17-27, May 30, 2017, available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/17-27.pdf.

APPENDIX

6. Footnote 88 SEF Registration Mandate for FX PB Platforms

MFA requests CFTC guidance to clarify ambiguities surrounding SEF trade execution of FX prime brokerage transactions, in particular non-deliverable forward contracts, on multiple-to-multiple platforms that had to register as SEFs. These registered SEFs do not list any clearing-mandated Required Transactions. The application of SEF requirements for cleared trades executed on these platforms is a point of ambiguity that continues to impede trading on these platforms.

7. Uncleared Swaps Confirmations

MFA requests that the CFTC adopt a modified confirmation delivery requirement in section 37.6(b) for uncleared swaps that will respect confidentiality concerns of the counterparties. MFA appreciates the current no-action relief that will expire on the effective date of any changes in the regulation.[42] Without such relief, buy-side market participants would be required to disclose the terms of all of their ISDA Master Agreements to SEFs, which raises material concerns regarding confidentiality and practicality. MFA strongly agrees with your criticisms of the confirmation requirement as expressed in the Giancarlo White Paper. Accordingly, we support a rule amendment to section 37.6(b) that would make the confirmation delivery requirement workable for SEF market participants.

D. Enhance Data Security and Treatment of Confidential Information

MFA urges the Commission to continue using the subpoena process for requesting for confidential, commercially valuable intellectual property, and to enhance its policies and procedures for protecting such information. MFA and its members are concerned with the high risk and threat of cyberespionage and data security at regulatory agencies. Information security vulnerabilities at a regulator will jeopardize not only market participants and their investors, but the U.S. economy through the loss of domestic trade secrets and confidence in the integrity of the regulatory framework. Over the last several years, due to both statutory mandates and regulatory discretion, the Commission has expanded the scope and breadth of the types of information that it requests of registrants. It has, however, generally continued to rely on the same framework for information collection and protection. MFA believes that the Commission needs to reexamine and rethink its policies and processes for collecting and protecting non-public and confidential information. We are aware of statutory provisions designed to protect the confidential and proprietary information of registrants, but without robust, updated policies and procedures at the CFTC, we are concerned that the Commission is unable to adequately protect such information.[43]

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[42] *See* CFTC Staff No-Action Letter No. 17-17, "Extension of No-Action Relief for Swap Execution Facility Confirmation and Recordkeeping Requirements under Commodity Futures Trading Commission Regulations 37.6(b), 37.1000, 37.1001, 45.2, and 45.3(a)", issued on March 24, 2017, available at: http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/17-17.pdf.

[43] *See, e.g.*, Section 8 of the Commodity Exchange Act; *and* Federal Information Security Modernization Act of 2014, 44 U.S.C. § 3551 (2014). *See also* 18 U.S.C. § 654 (1996) (prohibiting an officer or employee of United States

APPENDIX

MFA was highly alarmed with the Commission's 2015 proposal through Regulation AT to allow regulators to inspect a registrant's algorithmic trading source code. We are concerned that regulators, at times, unnecessarily request highly confidential and commercially valuable information, without exhausting other less sensitive means of understanding a firm's activities, and then do not have robust procedures for protecting such information. We support regulators having the information they need to oversee registrants and to surveil markets; however, this authority needs to be balanced with the potential risk of irrevocable harm (*e.g.*, unauthorized disclosure or misappropriation of trade secrets) to registrants and their due process rights.[44] To be clear, MFA has never disputed the Commission's authority to obtain confidential materials that it needs to enforce the law. However, the CFTC should adopt a general policy to refrain from asking for highly confidential and commercially valuable intellectual property from a registrant or market participant unless absolutely necessary; and when it asks for such information, it should be through a Commission issued subpoena. We believe that the Commission itself, and not the staff, should have to make the necessary determination that the CFTC needs access to such sensitive materials to discharge properly the Commission's regulatory responsibilities. We strongly agree and support your view that the subpoena process provides a fair compromise between the rights of property owners and the government's right to seize their property.[45]

In addition, we think the CFTC needs to have an information security policy in which the protections and security requirements are heightened or tiered depending upon the level of sensitivity of the data collected, including how to dispose of or return the data, if no wrongdoing is found, at the end of the examination, investigation or query. The Dodd-Frank Act imposed heightened confidentiality protections with respect to systemic risk information that the SEC collects from managers of private funds.[46] Similarly, we think the CFTC should impose heightened procedures and standards with respect to Forms CPO-PQR and CTA-PR and other highly sensitive and confidential information that it receives. The Commission should also consider industry practices and standards with respect to protecting confidential intellectual property. Market participants go to great lengths to protect sensitive intellectual property, implementing practices shaped by case law from intellectual property cases. We think it is only appropriate for the Commission to apply consistent protections.

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converting property of another); *and* 18 U.S.C. § 1905 (2008) (prohibiting public officers and employees of disclosure of confidential information generally).

[44] *See* Statement of Dissent by Commissioner J. Christopher Giancarlo Regarding Supplemental Notice of Proposed Rulemaking on Regulation Automated Trading, November 4, 2016, (expressing that allowing the CFTC to inspect algorithmic source code "would strip owners of intellectual property of due process of law" and that the "subpoena process provides property owners with due process of law before the government can seize their property.") available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/giancarlostatement110416.

[45] *Id.*

[46] *See* section 404 of the Dodd-Frank Act.

APPENDIX

Accordingly, MFA respectfully urges the Commission to continue using the subpoena process for requesting for confidential, commercially valuable intellectual property, and to enhance its policies and procedures for protecting such information. Specifically, the Commission should adopt a policy to refrain from asking for highly confidential and commercially valuable intellectual property from a registrant or market participant unless absolutely necessary; and when it asks for such information, it should be through a Commission issued subpoena. The Commission should also have special procedures for protecting such information. MFA would be pleased to discuss with the Commission common industry practices for protecting confidential intellectual property.

E. Simplify Regulation of Automated Trading

MFA urges the Commission to abandon its notice of proposed rulemaking on the regulation of automated trading[47] ("**NPRM**") and its supplemental notice of proposed rulemaking on Regulation AT[48] ("**Supplemental Proposal**") (together with the NPRM, "**Regulation AT**"), as proposed. While we believe that the CFTC Staff has attempted to incorporate comments it received on the NPRM into the Supplemental Proposal, we remain concerned that the underlying framework of Regulation AT is flawed. Regulation AT will inhibit economic growth, create inefficient and ineffective regulation, and impose inappropriately tailored regulation on a large swath of market participants. We strongly believe that a fundamental revision is necessary. The Commission should simplify and modernize regulatory oversight of automated trading by adopting targeted regulatory solutions to address marketplace risk.

Contrary to the Commission's intention, we believe that, as drafted, Regulation AT would create new risks, impose inefficient and ineffective requirements and burdens on the CFTC, DCMs, and market participants. In our view, Regulation AT proposes to apply a very prescriptive, unnecessary, one-size-fits-all regulatory framework on many different types of market participants. For example, the definitions under Regulation AT continue to be so broad that almost all trading by market participants will fall under the definitions of Algorithmic Trading and Direct Electronic Access. Subjecting market participants to Regulation AT for the use of third-party Algorithmic Trading systems places them in the untenable position of being responsible for systems and processes for which they have no technical expertise and to which they have no access. We are also concerned that in prescribing rigid controls and standards, Regulation AT does not provide enough flexibility for the markets and market participants to innovate or adjust controls or processes, as they deem appropriate or necessary, to address new technologies and circumstances in the future.

We believe the Commission should modernize regulatory oversight of automated trading by adopting targeted regulatory solutions to address marketplace risk. In doing so, we support the

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[47] *See* Proposed Regulation Automated Trading, 80 Fed. Reg. 78,824 (Dec. 17, 2015), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2015-30533a.pdf.

[48] *See* Supplemental Notice of Proposed Rulemaking: Regulation Automated Trading, 81 Fed. Reg. 85,334 (Nov. 25, 2016), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2016-27250c.pdf.

APPENDIX

Commission developing a regulatory framework that establishes baseline risk controls among "gatekeepers" such as DCMs and executing futures commission merchants ("**FCMs**") or clearing firms to address the risk of market disruption. We believe that the Commission should add any regulations by integrating them into the existing regulatory framework. Attempting to "modernize" oversight by simply layering another level of regulation on market participants and subjecting them to multiple DCM oversight creates an unwieldy and inefficient regulatory regime.

To the extent that the Commission believes it needs more information from CTAs or CPOs, or that these registered entities need enhanced controls, we would strongly urge the Commission to direct the NFA to amend its Annual Questionnaire. From the data NFA collects through its Annual Questionnaire, the Commission would be able to assess whether additional requirements are necessary to address risk concerns. We think that such a targeted approach would more precisely achieve the Commission's goals at lower cost.[49]

Finally, we strongly concur that the Commission has adequate authority through the subpoena process to seek Algorithmic Trading Source Code and that the Commission should continue relying on this authority rather than circumvent an intellectual property owner's right to due process of law.[50]

Accordingly, we recommend that the Commission abandon Regulation AT, as proposed, and instead to: (1) reduce electronic trading risk by implementing a risk control framework at the marketplace gatekeeper levels—DCMs and executing FCMs or clearing firms; and (2) build on the existing regulatory framework, as necessary, to oversee registrants, such as CTAs and CPOs.[51]

DIVISION OF SWAP DEALER AND INTERMEDIARY OVERSIGHT

F. Reduce Administrative Burden by Amending Part 4 Regulations Regarding Third-Party Recordkeeping

MFA commends the Commission for its adoption of final § 1.31, a modernized and significantly improved recordkeeping rule.[52] MFA requests that the Commission amend the CFTC

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[49] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Christopher Kirkpatrick, Secretary, CFTC, on Mar. 16, 2016, on Proposed Regulation Automated Trading, available at: https://www.managedfunds.org/wp-content/uploads/2016/03/MFA-RegAT-Letter-final.pdf.

[50] *See* Statement of Dissent by Commissioner J. Christopher Giancarlo Regarding Supplemental Notice of Proposed Rulemaking on Regulation Automated Trading, November 4, 2016 (hereinafter "Giancarlo Statement of Dissent"), available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/giancarlostatement110416.

[51] *See* letter from Stuart J. Kaswell, Executive Vice President, Managing Director and General Counsel, MFA, to Christopher Kirkpatrick, Secretary, CFTC, dated May 1, 2017 on the Supplemental Proposal on Regulation AT, available at: https://www.managedfunds.org/wp-content/uploads/2017/05/MFA.AIMA_.Reg-AT.Supp_.pdf.

[52] Final Recordkeeping Rule 1.31, 82 Fed. Reg. 24,479 (May 30, 2017), available at: http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2017-11014a.pdf. *See* Recordkeeping Proposal, 82 Fed. Reg. 6,356 (Jan. 19, 2017), available at:

APPENDIX

Part 4 regulations to allow CPOs and CTAs to engage in third-party recordkeeping arrangements without the need to make notice filings. Discrepancies between CFTC recordkeeping regulations for CPOs and CTAs and the SEC's recordkeeping arrangements for investment advisers make regulation burdensome and more expensive for dual registrants.

In 2014, MFA, jointly with other associations, submitted a petition to the Commission to modernize CFTC recordkeeping § 1.31 and other regulations ("**Recordkeeping Petition**"), as we were concerned that the regulations' incorporation of outdated technology and incongruity with standard market practices exposed registrants to security risks and increased compliance costs.[53] We are pleased that the Commission has amended § 1.31 in a technology neutral manner, and appreciate that the rule text is straight-forward and easy to understand. As we raised in our Recordkeeping Petition and in our comments on the Commission's proposed amendments to § 1.31, we continue to urge the Commission to amend the CFTC Part 4 regulations to permit records entities to maintain records at locations other than their main business office and to engage third parties, use certain facilities or cloud-based applications, or enter into any other desired recordkeeping arrangements with third parties.[54] We believe that the Part 4 regulations can be amended with a simple fix by simply not specifying the "where" with respect to records maintenance, similar to regulations pertaining to FCMs and other registrants. We appreciate that the CFTC staff has issued exemptive relief permitting CTAs to use third-party recordkeepers. Nevertheless, amending the Part 4 regulations would greatly reduce administrative burden for CPOs and CTAs. Otherwise, registrants expend significant resources navigating the CFTC regulations to understand staff guidance and available exemptive relief, and amending or updating notice filings.

Accordingly, MFA requests that the Commission amend the CFTC Part 4 regulations to permit records entities to maintain records at locations other than their main business office and to engage third parties, use certain facilities or cloud-based applications, or enter into any other desired recordkeeping arrangements with third parties.

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http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2017-01148a.pdf; *and* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, Karen Barr, President and Chief Executive Officer, Investment Adviser Association, Jiří Król, Deputy CEO, Global Head of Government Affairs, Alternative Investment Management Association, and Laura Martin, Managing Director and Associate General Counsel, SIFMA Asset Management Group, to Christopher Kirkpatrick, Secretary, CFTC, on Mar. 20, 2017, on Recordkeeping (hereinafter "**Comments on Proposed Recordkeeping**", available at: https://www.managedfunds.org/wp-content/uploads/2017/03/MFA-AIMA-IAA-AMG-CFTC-Recordkeeping-Comment-Letter.final_.3.20.17.pdf.

[53] Petition for Rulemaking to Amend CFTC §§ 1.31, 4.7(b) and (c), 4.23 and 4.22, Managed Funds Association, Investment Adviser Association, and Alternative Investment Management Association (Jul. 21, 2014), available at: https://www.managedfunds.org/wp-content/uploads/2014/07/Final-Petition.pdf.

[54] *See also* Comments on Proposed Recordkeeping, *supra* note 52.

APPENDIX

G. Exclude Compo Swaps from Calculation Under § 4.13(a)(3)

MFA requests that the Commission exclude compo swaps from calculation under § 4.13(a)(3) with respect to determining a pool's commodity interest position; and to issue related guidance. For regulatory simplification, we believe the Commission should allow a CPO to treat compo swaps as security-based swaps and exclude such products from its calculation of commodity interest positions for purposes of qualifying for an exemption from registration under § 4.13(a)(3), the *de minimis* trading exemption.

Market participants transact in total return swaps that allow one party to gain equity exposure to a stock or a narrow-based index of stocks that trade outside the United States; and generally, desire for payments under such total return swaps to be made in U.S. dollars ("**foreign equity total return swaps**"). Compo swaps are foreign equity total return swaps, in which the currency translation is effected using the prevailing "spot" exchange rate at the time of such valuation or payment. While the Commission has held the view that compo swaps are mixed swaps,[55] we believe for purposes of calculating commodity interest positions under § 4.13(a)(3), the Commission should allow CPOs to treat compo swaps as security-based swaps and exclude compo swaps from the *de minimis* trading test under § 4.13(a)(3). The foreign exchange component of a compo swap is relatively minimal compared to the equity component; and these products are already regulated as security-based swaps. For regulatory simplification, we believe the Commission should exclude compo swaps from calculation under § 4.13(a)(3), and issue corresponding guidance.

DIVISION OF CLEARING AND RISK

H. Advocate for Congress to Amend the Bankruptcy Code to Facilitate Full Physical Segregation of Customer Collateral

MFA respectfully requests that the Commission advocate for Congress to amend the Bankruptcy Code to facilitate full physical segregation of customer collateral. Ensuring the protection of customers and their collateral was one of Congress's goals under the Dodd-Frank Act; however, the current treatment of "customer property" under the Bankruptcy Code prevents customers and their assets from being fully protected from the failure of an FCM or another of the FCM's customers.

MFA appreciates that the Commission remains vigilant about protection of investors and has adopted rules to address the regulatory issues revealed by the MF Global, Inc. ("**MF Global**")

[55] Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement;" Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 Fed. Reg. 48,208 (Aug. 13, 2012), available at: https://www.gpo.gov/fdsys/pkg/FR-2012-08-13/pdf/2012-18003.pdf.

APPENDIX

and Peregrine Financial Group, Inc. ("**Peregrine**") insolvencies.[56] Our members are fiduciaries to their investors and are customers themselves, and as counterparties to swaps transactions must post collateral to ensure performance of the contract.[57] Thus, the protection of such collateral is one essential element to preserving the financial integrity of the markets. 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.[58] Accordingly, we support thoughtful legislative and regulatory changes to strengthen protections of FCMs' customers.

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 ask that the Commission 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"[59] 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 Commission has adopted the "legally segregated operationally commingled" model ("**LSOC**") for cleared swaps,[60] which is intended to protect the assets of non-defaulting customers from *pro rata* distribution. However, LSOC is a relatively new and untested segregation model. If a bankruptcy trustee or FCM's

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[56] *See* Commission final rule on "Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations", 78 Fed. Reg. 68506 (Nov. 14, 2013), available at: https://www.gpo.gov/fdsys/pkg/FR-2013-11-14/pdf/2013-26665.pdf.

[57] 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.

[58] *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.

[59] *See* 11 U.S.C. §§752 and 766.

[60] *See* Commission 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 ("C**ommission Segregation Rules**"). 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.

APPENDIX

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 "customer property" and is not shielded from *pro rata* distribution. By so amending the Bankruptcy Code as discussed above, Congress 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.[61] MFA appreciates the Commission's efforts to enhance customer protections[62] 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 OTC derivatives market. Therefore, MFA believes that, if the Commission encouraged Congress to amend 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.

I. Encourage European Regulators to Resolve Equivalence Issues under EMIR Article 13 and MiFIR Article 33

MFA requests that the Commission engage with European authorities and encourage them to resolve equivalence issues under Article 13 of the European Market Infrastructure Regulation ("**EMIR**")[63] and Article 33 of the Markets in Financial Instruments Regulation ("**MiFIR**"),[64] which prevent certain U.S. persons from satisfying their regulatory obligations under EMIR and MiFIR by complying with equivalent U.S. rules because those U.S. persons are not "established" in the U.S. This issue deeply affects the fund industry and the European banks with which they

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[61] 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.

[62] *See supra* note 56.

[63] 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, available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:201:0001:0059:en:PDF.

[64] Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012, available at: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0600&from=EN.

APPENDIX

trade derivatives, and will hamper the ability of these market participants to continue to trade derivatives on a cross-border basis.

MFA applauds the efforts of the Commission and regulators in other jurisdictions to harmonize the scope of their derivatives rules and to recognize the equivalent rules of other jurisdictions to ensure that the trading of derivatives can continue to occur unimpeded on a cross-border basis. However, language in the text of Article 13 of EMIR and Article 33 of MiFIR could result in regulatory conflicts or duplication between European and U.S. rules. These regulatory conflicts may unintentionally prevent trading between European banks and funds organized in the Cayman Islands that have a U.S.-based manager or a U.S. principal place of business, and thus, are regulated in the U.S. as "U.S. persons" ("**Cayman Funds**"). As the vast majority of U.S.-based managers establish funds in the Cayman Islands or other offshore jurisdictions, this unintended consequence could impair a significant volume of business in the derivatives market.

Article 13(3) of EMIR provides as follows:

> *An implementing act on equivalence... shall imply that counterparties entering into a transaction subject to this Regulation shall be deemed to have fulfilled the obligations contained in Articles 4, 9, 10 and 11 where at least one of the counterparties is established in that third country.*

Similarly, Article 33(2) of MiFIR ("**Article 33**") provides as follows:

> *An implementing act on equivalence... shall have the effect that counterparties entering into a transaction subject to this Regulation shall be deemed to have fulfilled the obligation contained in Articles 28 and 29 where at least one of the counterparties is established in that third country.*[65]

MFA believes that the European policymakers intended Article 13 and Article 33 to prevent circumstances from arising where parties to a derivative contract are required to comply with two separate regulatory regimes (*e.g.*, EMIR and the Dodd-Frank Act[66]). Specifically, these Articles seek to avert two undesirable regulatory outcomes. The first is where parties might be subject to directly conflicting rules in two jurisdictions if they enter into a trade and, accordingly, would be unable to trade with each other because by complying with one regime they would breach the requirements of another regime. The second is where parties to the trade may be subject to duplicative requirements in the two jurisdictions that achieve the same objectives but may have important substantive differences. Compliance with such duplicative rules creates inefficiencies, unnecessary expense and is contrary to the stated intention of Article 13 and Article 33.

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[65] MFA notes that the Articles of MiFIR referred to in the foregoing address the following regulatory obligations: (1) obligation to trade on regulated markets, multilateral trading facility, or organised trading facility (Article 28); and (2) clearing obligation for derivatives traded on regulated markets and timing of acceptance for clearing (Article 29).

[66] *See supra* note 3.

APPENDIX

Despite the intentions behind Article 13 and Article 33, a problem arises under both because of the notion of where a fund is "established" such that it can rely on an equivalence determination issued by the European Commission with respect to U.S. regulations. Specifically, the Commission regulates Cayman Funds (*i.e.*, non-U.S. funds with a U.S.-based manager or a U.S. principal place of business) as "U.S. persons".[67] However, based on a strict reading of EMIR and MiFIR, it is doubtful that market participants can treat these Cayman Funds as "established" in the U.S., since, even though these funds are subject to U.S. regulations, they are not organized in the U.S. As a result, if such Cayman Funds are not deemed "established" in the U.S., the consequence is that, when Cayman Funds trade derivatives with European dealers, neither the Cayman Funds nor their European dealer counterparties would be able to benefit from Article 13 or Article 33 and rely on such equivalence acts with respect to U.S. regulations.

MFA emphasizes that these fact patterns are reflective of a significant volume of business in the derivatives market, and has raised this concern with the European Commission, ESMA, the SEC, and the Cayman Islands Monetary Authority. Therefore, this issue should not be underestimated and could have serious consequences on the business of European banks and Cayman Funds as they may cease transacting with each other in order to avoid duplicative or conflicting rules. Such unintended consequences would be contrary to the interests of global trading as well as ease of access to markets. Accordingly, we emphasize that resolution of this equivalence issue is of equal importance to, and affects both, Cayman Funds as well as European dealers. We would appreciate any assistance that the Commission can provide in urging European authorities to resolve this issue.

J. Focus on and Protect the Interests of Customers in Regulations on CCP Recovery and Resolution

MFA believes that any regulations addressing the recovery or resolution of CCPs should protect the assets and interests of customers. As the Commission continues to consider whether it should issue regulations on this issue, we urge the Commission to ensure that it is protecting customers by allowing certain key principles to guide it. In particular, discussions on this issue have primarily taken place among regulators, CCPs, and FCMs, with customers being largely excluded, even though use of customer assets has been emphasized as a potential loss allocation tool. Because MFA's members manage the assets of their investor and taxpayer clients, any use of customer assets during a CCP's recovery or resolution results in losses to these investors and taxpayers, which is contrary to the core principles of the Dodd-Frank Act.

Issues related to the recovery and resolution of CCPs have become an area of focus for regulators in the U.S. and other jurisdictions. Because CCPs are financial market infrastructures that allow central clearing to occur, as clearing has risen in importance so too has the focus on the safety and soundness of CCPs, as well as the steps that should be taken in the circumstances,

[67] MFA notes that we support the Commission regulating such funds as "U.S. persons".

APPENDIX

however rare, where a CCP experiences material financial distress. Because customers are significant users of CCPs and their clearing services (albeit indirect users), customers' capital is at risk if a CCP fails. Thus, customers warrant substantial protection and have a significant interest in having their views taken into account on these issues. Given the implications that a CCP's failure would have on customers, we think it extremely important for relevant authorities to consult, reflect the views of, and balance the assumed risks of, all market participants, including customers, as discussions and rulemaking around these issues progress.

Set forth below are key principles that MFA believes should guide the Commission and other authorities across the globe as they consider what requirements they will impose on CCPs with respect to their recovery or resolution. These key principles reflect our views as to where we believe the appropriate balance is between the safety and soundness of CCPs and the protection of customers and their assets. MFA believes that each key principle is a critical component of ensuring the continued functioning of the financial markets while any CCP is in distress.

(1) CCPs should not use customer assets as part of any loss allocation tool.

Regardless of whether a failing CCP will seek recovery or begin resolution, a central question is whose assets the CCP will use to bolster its recovery or facilitate its resolution. Some clearing members are recommending that CCPs use customer assets (in particular customer variation margin ("**VM**") haircutting) as a preferred solution. MFA strongly objects to use of customer IM or VM during a CCP recovery or resolution. Policy makers and regulators seem to agree that IM haircutting is not a viable option, since it is impermissible under the rules and law of many jurisdictions.[68] However, we are aware that, despite our strong objections, policy makers or regulators have contemplated permitting a stressed CCP to use VM haircuts to allocate losses to its participants more broadly after the CCP has used all other financial resources available to it.[69] In discussions about using VM haircutting as a loss allocation tool, we believe that the mechanism by which CCPs would allocate any such VM haircuts has been overlooked, and could have severe consequences with respect to how losses are actually distributed among market participants (as recognized by at least one clearing member).[70] Therefore, we emphasize that, if policy makers or regulators ever permit a stressed CCP to employ haircuts with respect to its

[68] *See e.g.*, U.S. Bankruptcy Code, 7 U.S.C. §741-753 and §761-766; Sections 724 and 763 of the Dodd-Frank Wall Street Reform and Consumer Protection Act; and Commission Segregation Rules *supra* note 60.

[69] *See* Committee on Payments and Market Infrastructures and the Board of the International Organization of Securities Commissions principles for "Recovery of financial market infrastructures" dated October 2014, at 18-19, discussing CCPs' possible use of VM haircutting as a loss allocation tool and the reasons why clearing members prefer CCPs to use gains-based methods, available at: http://www.bis.org/cpmi/publ/d121.pdf.

[70] *See* JPMorgan Chase & Co. Perspectives, *What is the Resolution Plan for CCPs?*, September 2014, at 2, explaining that VM gains haircutting "is equally flawed as a sole solution to resolution" because it could have unexpected consequences. In particular, the Whitepaper asserts that end users who expected cash payments would be likely to liquidate assets in order to raise funds, which would depress the value of these assets and weaken the market, creating a pro-cyclical scenario that could further destabilize a collapsing market. Available at: http://www.jpmorganchase.com/corporate/About-JPMC/document/resolution-plan-ccps.pdf.

APPENDIX

participants' VM, such VM haircuts: (1) should be used as a last resort, (2) should not affect customers disproportionately as compared to other CCP participants, and (3) should only be applied using equitable approaches that allocate losses to participants in proportion to their use of the CCP.

(2) Customers must have certainty as to whether a failing CCP will be recovered or resolved.

A core, polarizing issue in the debate around CCPs in distress is whether to allow such CCPs to fail and be resolved or whether to encourage the CCP's recovery. A question underlying this debate is whether a systemically important CCP is "too big to fail". MFA believes that there is no universal right answer to this question.

Whether the CCP will resolve or seek recovery, we emphasize that the overarching goal must be to provide market participants with prompt certainty. Currently, CCP rulebooks are the only established guidelines around whether a distressed CCP must seek recovery or go into resolution. However, our understanding is that the rulebooks provide CCPs with significant flexibility. The rulebooks allow the CCPs to determine, for example, when to conduct an auction and who can participate or what the timeframe is after becoming distressed for the CCP to decide whether to seek recovery or be resolved. Therefore, it is important that CCP rulebooks have less flexibility and instead include clear, robust, pre-determined criteria that enable CCPs to make prompt determinations between recovery and resolution. Such criteria will allow the CCP to make prompt determinations, and thus, provide market participants with the certainty they need to be able to manage their own portfolios and assets accordingly.

(3) Customers must have affirmative representation on CCP decision-making bodies.

The imposition of mandatory central clearing and the potential magnitude of losses that customers would suffer if a CCP fails (especially if CCPs use customer assets as a loss allocation tool) emphasize the need for customers to have affirmative representation on CCP governing bodies, including CCP boards, risk committees, and default management committees.

Customers should have their views reflected in the critical decisions of CCP governing bodies. Customers are crucial stakeholders in the cleared derivatives markets and have interests that are aligned with the core CCP goals of mitigating systemic risk and increasing transparency, efficiency, and competition. Customers also have sophisticated derivatives product and risk management expertise and significant knowledge about the issues market participants encounter when seeking access to clearing and best execution. Therefore, MFA strongly believes that, to address imbalances in CCP governance and act as a counterbalance to historically aligned and concentrated clearing member interests, regulations should mandate that customers have affirmative representation on CCP boards and committees and that no group's representation may constitute a controlling majority.

APPENDIX

(4) Customers must be allowed to participate in CCP default management auctions.

It is important for regulators to take steps to expand opportunities for customer participation in CCP default management auctions. A CCP's auction is a critical piece of its default management process, which is typically open only to clearing members (*i.e.*, customers are excluded from participation). In particular, in the case of a clearing member default, a CCP may use an auction to coordinate the orderly transfer of defaulted trades by allowing non-defaulting participants to bid on those trades.

At a fundamental level, it makes sense to allow customers to participate in these auctions. First, based purely on the principle of supply-and-demand, the more demand that can be generated for the auctioned trades, the higher the likelihood that a market clearing auction price is achieved, and the more likely the auction will be successful for the CCP. Second, allowing customers to participate in CCP auctions ensures that more sources of private capital are available, which helps to minimize potential negative externalities of the CCP's distress, such as the possibility that the CCP would need to access public capital to facilitate its recovery or resolution. Lastly, customer participation in CCP auctions increases the likelihood that there are market participants in a sufficiently strong position to robustly bid in the auction (as compared to only allowing a relatively homogenous group of clearing members to participate that may be similarly impaired by market events).

(5) CCPs should have substantial "skin in the game" to align their incentives.

It is important that a CCP be exposed to the loss of its own funds as part of its default waterfall.[71] The guarantee fund consisting of clearing member contributions and the separate CCP contributions that form part of the CCP's default waterfall are the CCP's principal mechanisms for protecting itself from the failure or default of one of its participants. While each clearing member must contribute a certain amount of resources to a CCP's guarantee fund, the CCP's assets are included to a more limited extent.

Therefore, requiring CCPs to pre-fund capital contributions to the guarantee fund (*i.e.*, have "skin in the game") would have important benefits. Most importantly, it would align the incentives of the CCP with its direct and indirect participants by ensuring that the CCP has as significant an interest as its participants in avoiding default. In addition, contributing such additional capital would increase the CCP's financial resources, and thus, would reduce the potential for the CCP to default in the event of a participant failure.

[71] For purposes of this principle, when we refer to CCP "skin in the game", we mean CCP capital from all available resources, such that the incentives of the CCP, its shareholders, and its participants are all aligned.

APPENDIX

(6) Regulators should set standards for, and have robust oversight of, CCP stress testing.

Stress testing is an essential component of CCP risk management that allows the CCP to verify the adequacy of its financial resources (*i.e.*, posted margin, guarantee fund contributions, and CCP capital contributions) and financial stability during extreme or stressed market situations. Although CCPs currently engage in stress testing, each CCP is able to design and conduct its own stress tests, which includes determining the scope, frequency, and duration of such tests. Therefore, stress testing procedures can vary from CCP to CCP and may not be sufficiently robust in all areas (*e.g.*, may not test sufficiently for certain stressed situations).

MFA believes that to augment such regulatory enhancements, regulators should impose specific minimum criteria and standards for CCPs' stress tests as part of CCPs' ordinary business as well as CCPs' recovery planning. We believe it important that regulators impose a uniform, minimum set of standards that all CCPs must apply on a periodic (but sufficiently frequent) basis and regulators should include review of those procedures and stress tests as part of regular CCP exams.

K. Recalibrate and Reduce Initial Margin Requirements to Better Reflect the Actual Risk of Certain Non-Clearable Swap Products

MFA believes that the Commission needs to recalibrate and appropriately tailor the IM requirements for uncleared swaps to reflect the actual risk posed by certain non-clearable swap products, such as total return swaps ("**TRS**") for complex equity trades. Many hedge funds trade such TRS to achieve exposure to equities. However, as banks do not trade such TRS among themselves, our requested tailored revision to IM requirements for such products would present relatively little systemic risk. Therefore, funds that use non-clearable TRS should not be penalized by having to over-collateralize them based on the higher IM requirements that will be coming into effect for their uncleared trades on September 1, 2019 or 2020. The underlying policy objective for the higher uncleared margin requirements is to encourage clearing swaps that are suitable for clearing. That policy objective has a punitive and disproportionate effect on buy-side market participants who trade non-clearable TRS and collateralize them based on the actual risk posed by such products.

DIVISION OF MARKET OVERSIGHT

L. Reduce Complexity of Cleared Swap Reporting Requirements by Eliminating Alpha Swap Reporting

MFA believes the CFTC should eliminate alpha swap reporting requirements to reduce the reporting complexities of its cleared swaps reporting regime and to streamline the data actually reported without sacrificing the amount of information available to the CFTC regarding the entire

APPENDIX

life cycle of a swap. As you noted in a recent interview with *Risk.net*,[72] the Commission only needs the final information reported by the CCP concerning the beta/gamma swaps comprising a cleared swap for effective oversight. As explained in MFA's prior comment letters, MFA believes there is no need for the reporting of an original "alpha" swap for any swap that is executed with the intention to be cleared.[73]

BANK CAPITAL REQUIREMENTS AFFECTING CUSTOMER CLEARING

M. Recalibrate Leverage Ratio for Cleared Derivatives to Allow Offset for Segregated Client Initial Margin

MFA seeks the CFTC's help as a voting member of FSOC to achieve an important recalibration in the leverage ratio for cleared derivatives that will have a profound impact on customer clearing. As you noted in your recent public remarks, the CFTC has an influential role to play in achieving recalibrated bank regulatory capital requirements and leverage ratios to "better balance systemic risk concerns with healthy economic growth and American prosperity."[74] While MFA supports the Basel Committee on Banking Supervision's ("**Basel Committee**") proposed revision to use the Standardized Approach for Measuring Counterparty Credit Risk Exposures ("**SA-CCR**") for its Basel III leverage ratio ("**Leverage Ratio**") framework, we are concerned with the Leverage Ratio's treatment of segregated IM for centrally cleared derivatives exposure, which does not recognize the exposure-reducing effect of customers' segregated IM. To ensure the continued affordability and robustness of customer clearing in the U.S., MFA suggests that the leverage ratio rules should be recalibrated to allow clearing members of CCPs to offset segregated IM when calculating exposure.

The Basel Committee's transition from the Current Exposure Method to the SA-CCR method should be a positive for end-clients, because SA-CCR more accurately captures exposures that clearing members face when providing clearing services to clients. However, MFA has strong concerns about the Basel Committee's treatment of segregated IM for centrally cleared derivatives exposure under the Leverage Ratio, because it will significantly increase clearing costs, cause

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[72] *See supra* note 7.

[73] *See* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, and Adam Jacobs, Director, Head of Markets Regulation, Alternative Investment Management Association (AIMA), to Melissa D. Jurgens, Secretary, CFTC, on May 27, 2014, on Review of Swap Data Recordkeeping and Reporting Requirements, available at: https://www.managedfunds.org/wp-content/uploads/2014/05/CFTC-Swap-Data-Reporting-Rules-Final-MFA-AIMA-Letter.pdf; *see also* letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, and Jiri Krol, Deputy CEO, Global Head of Government Affairs, AIMA, to Mr. Christopher Kirkpatrick, Secretary, CFTC, on October 30, 2015, on Amendments to Swap Data Recordkeeping and Reporting Requirements for Cleared Swaps, available at: https://www.managedfunds.org/wp-content/uploads/2015/11/CFTC-Proposed-Amendments-for-Cleared-Swap-Data-Reporting-MFA-AIMA-Final-Letter.pdf.

[74] *See* Giancarlo Boca Speech, *supra* note 2.

APPENDIX

customers to reduce their hedging activities to levels that are inadequate to manage their risks, and make central clearing of derivatives increasingly less accessible and less affordable for end-users.

CCPs' risk management methodologies are predicated on the collection of IM and VM from clearing members and customers in order to collateralize potential exposure. In addition, direct clearing members guarantee payment of their customers' obligations to the CCP. Because the IM is the customer's money, CFTC rules require clearing members to segregate customer funds from the clearing member's own assets.

While the Basel Committee's framework captures a clearing member's guarantee to the CCP as an off-balance sheet exposure, the Leverage Ratio fails to provide an offset that recognizes the exposure-reducing effect of customers' segregated IM. According to the Basel Committee, the reason for the lack of an offset for customer IM is that segregated customer IM not only offsets exposures, but also can be used by the clearing member for further leverage.

In the U.S., segregation rules severely restrict the ability of IM to be held in anything other than extremely low-risk and extremely liquid assets, assuring that it is always available to absorb losses ahead of the bank. Moreover, the substantial majority of segregated IM is posted to the CCP, and therefore, is entirely outside the control of the clearing member.

The Leverage Ratio's failure to recognize the purpose of segregated IM is a threat to the use of cleared derivatives by customers. Because of the lack of offset, clearing members will incur large Leverage Ratio exposures, which will likely raise prices for customer clearing significantly. This substantial cost increase may cause customers to reduce their hedging activities, which could result in price increases and volatility for food, gasoline, and other consumer goods.

On November 3, 2016, MFA joined a coalition letter signed by 14 other industry bodies representing clearing members, asset managers, insurance companies, commodity end-users, hedge funds, derivatives exchanges, and CCPs.[75] The letter expressed the coalition's concerns that the Leverage Ratio will harm the strength and stability of the cleared derivatives markets worldwide, unless it is amended to recognize the exposure-reducing effect of the segregated IM that clearing banks collect from their clients. The coalition sent the letter to the Chairman of the Basel Committee, as well as to the Chairman of the FSB and the Chairman of the Group of Governors and Heads of Supervision.

In the letter, the coalition expressed its willingness to accept further conditions that the Basel Committee may impose for client segregated IM, or a limited recognition so that money that goes to the CCP may be recognized under the Leverage Ratio. The coalition also expressed concerns that the Leverage Ratio could raise barriers to porting client positions from a failing clearing member, because the ported clients' segregated IM would increase a transferee clearing member's capital requirements at a time of system-wide stress, when firms would already face

[75] Available at: https://www.managedfunds.org/wp-content/uploads/2016/11/Letter-to-BCBS-GHOS-FSB-from-Participants-in-Cleared-Derviatives-Markets-Final.pdf.

APPENDIX

capital and liquidity challenges. Lastly, the coalition noted that a clearing member's inability to recognize the segregation of client IM in the Leverage Ratio inappropriately increases the capital cost of client clearing, which undermines a key reform goal to use the safeguards of central clearing for standardized derivatives contracts.

Separately, on November 23, 2016, the EC proposed changes to the EU capital requirement regulation and directive that would, among other things, allow clearing firms to reduce the Leverage Ratio exposure measure by the IM received from clients for cleared derivatives. MFA applauds this EC proposal.

To ensure the continued affordability and robustness of customer clearing in the U.S., MFA seeks the CFTC's help in its capacity as a voting member of FSOC to encourage the Board of Governors of the Federal Reserve, the Federal Deposit Insurance Corporation, and the Office of Comptroller of the Currency to consider the EC's proposal and industry-wide concerns in their rulemaking processes, and provide an offset for clearing members to the extent that customer IM is posted to the CCP, or is segregated under the U.S. regulatory regime.[76]

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MFA appreciates the opportunity to provide these comments, and we look forward to continuing to provide what we intend as useful and constructive comments on pending and future Commission rulemakings. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact Jennifer Han, Associate General Counsel, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

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Mike Gill, Chief of Staff, Acting Chairman
Eileen Flaherty, Director, Division of Swap Dealer and Intermediary Oversight
John Lawton, Acting Director, Division of Clearing and Risk
Amir Zaidi, Director, Division of Market Oversight

[76] MFA notes that Federal Reserve Governor Jerome Powell recently called for a recalibration of the Leverage Ratio in the U.S.at its Global Finance Forum in Washington, D.C. on April 20, 2017, pointing to the damaging impact the SLR is having on client clearing.