

# MANAGED FUNDS ASSOCIATION

The Voice of the Global Alternative Investment Industry

WASHINGTON, DC | NEW YORK



May 15, 2015

**Via Electronic Submission:** [regs.comments@occ.treas.gov](mailto:regs.comments@occ.treas.gov);  
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Deputy Director, Office of Regulatory  
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Mr. Robert deV. Frierson  
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Board of Governors of the  
Federal Reserve System  
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Mr. Alfred M. Pollard  
General Counsel  
Attention: Comments/RIN 2590-AA45  
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Mr. Robert E. Feldman  
Executive Secretary  
Attention: Comments  
Federal Deposit Insurance Corporation  
550 17th Street, NW  
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Mr. Christopher Kirkpatrick  
Secretary of the Commission  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street NW  
Washington, DC 20581

**Re: Margin and Capital Requirements for Covered Swap Entities, Proposed Rule;  
Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap  
Participants, Proposed Rule**

Ladies and Gentlemen:

Managed Funds Association (“MFA”)<sup>1</sup> is providing the prudential regulators (the “Prudential Regulators”)<sup>2</sup> and the Commodity Futures Trading Commission (“CFTC”) with

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<sup>1</sup> 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

additional comments to supplement MFA's comment letter to the Prudential Regulators dated November 24, 2014 (the "**MFA PR Letter**") and MFA's comment letter to the CFTC dated December 2, 2014 (the "**MFA CFTC Letter**", and together with the MFA PR Letter, the "**MFA Letters**")<sup>3</sup>. The MFA Letters were in respect of the re-proposed rules on "Margin and Capital Requirements for Covered Swap Entities" (the "**PR Proposed Rules**")<sup>4</sup> and the "Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants"<sup>5</sup> (the "**CFTC Proposed Rules**" and together with the PR Proposed Rules, the "**Proposed Rules**") related to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**").<sup>6</sup>

In response to a request from CFTC and Fed staffs during a conference call with MFA on February 9, 2015, MFA's additional comments relate to only one aspect of the Proposed Rules: the proposed application of initial margin ("**IM**") thresholds to investment funds, with a suggested definition of "investment fund" for this purpose.

## **I. Proposed Definitional Changes to Ensure Fund-Level Application of IM Thresholds**

As explained in the MFA Letters, we are concerned that the proposed definition of "affiliate"<sup>7</sup> and the related proposed definition of "control"<sup>8</sup> could lead to consolidated treatment of funds in a firm's structure for purposes of applying the IM thresholds. We believe the proposed control definition would not allow separate treatment of funds in the same manner as described in the international margin framework issued by the Basel Committee for Banking

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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, the Americas, Australia and many other regions where MFA members are market participants.

<sup>2</sup> Collectively, the Office of the Comptroller of the Currency, Treasury; Board of Governors of the Federal Reserve System; Federal Deposit Insurance Corporation; Farm Credit Administration and the Federal Housing Finance Agency.

<sup>3</sup> See MFA PR Letter, available at: [https://www.fdic.gov/regulations/laws/federal/2014/2014-covered\\_swap\\_entities-c\\_39.pdf](https://www.fdic.gov/regulations/laws/federal/2014/2014-covered_swap_entities-c_39.pdf); and MFA CFTC Letter, available at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60037>.

<sup>4</sup> Notice of Proposed Rulemaking on "Margin and Capital Requirements for Covered Swap Entities", 79 Fed. Reg. 57348 (Sept. 24, 2014).

<sup>5</sup> Notice of Proposed Rulemaking on "Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants", 79 Fed. Reg. 59898 (Oct. 2, 2014).

<sup>6</sup> Pub. L. 111-203, 124 Stat. 1376 (2010).

<sup>7</sup> The Proposed Rules define "affiliate" to mean "any company that controls, is controlled by, or is under common control with another company". See PR Proposed Rules at 57389, Section \_\_.2; see CFTC Proposed Rules at 59926, Section 23.151.

<sup>8</sup> The Proposed Rules define "control" of another company to mean: (i) ownership, control, or power to vote 25% or more of a class of voting securities of the company, directly or indirectly or acting through one or more other persons; (ii) ownership or control of 25% or more of the total equity of the company, directly or indirectly or acting through one or more other persons; or (iii) control in any manner of the election of a majority of the directors or trustees of the company. See PR Proposed Rules at 57389, Section \_\_.2; see CFTC Proposed Rules at 59926, Section 23.151.

Supervision and the International Organization of Securities Commissions on September 2, 2013 (the “**Basel-IOSCO Standards**”).<sup>9</sup>

The Basel-IOSCO Standards treat investment funds separately for purposes of applying the IM threshold “as long as the funds are distinct legal entities that are not collateralized by or otherwise guaranteed or supported by other investment funds or the investment adviser in the event of fund insolvency or bankruptcy”.<sup>10</sup>

We are thus very concerned that the Proposed Rules would introduce new control criteria for determining affiliates of a fund, thus creating a significant discrepancy with the criteria in the Basel-IOSCO Standards. We strongly believe such a discrepancy will lead to inconsistent application of IM thresholds to funds in different jurisdictions. Accordingly, we request that the Prudential Regulators and the CFTC make certain suggested definitional modifications in the Proposed Rules to eliminate such discrepancy.

**A. Add New Definition of “Investment Fund”**

MFA requests that the Prudential Regulators and the CFTC add the following definition of “investment fund” in their final rules:

“Investment fund” means any financial end user, as defined in the rule, that is:

- (1) An investment company as defined in Section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3); or an entity that would be an investment company but for the exclusion in Section 3(c)(5)(C) of that Act; or an entity that is deemed not to be an investment company pursuant to Investment Company Act Rule 3a-7 (17 CFR 270.3a-7) of the U.S. Securities and Exchange Commission;
- (2) A private fund as defined in clause (vii) of the definition of “financial end user” in the rule;
- (3) A commodity pool, as defined in section 1a(10) of the Commodity Exchange Act (7 U.S.C. 1a(10));
- (4) A company that elects to be regulated as a business development company under section 54 of the Investment Company Act of 1940; or
- (5) An entity formed under the laws of a jurisdiction other than the United States that would be an investment fund, as defined in clauses 1 through 4 above, if it were organized in the United States or a State thereof.

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<sup>9</sup> The Basel-IOSCO Standards require all covered entities to exchange IM with a threshold not to exceed €50 million. The IM threshold generally applies on a consolidated group basis, except with respect to investment funds meeting certain criteria that are not based on affiliate status or indicia of control. See Basel-IOSCO Standards at 9, footnote 10. Available at: <http://www.bis.org/publ/bcbs261.pdf>.

<sup>10</sup> Id.

## **B. Modify Definition of “Control”**

MFA suggests the following amendment to the proposed definition of “control” for purposes of applying the initial margin thresholds to an investment fund, as defined above:

The definition of “control” should be amended to add the following sentence after clause (3) thereof:

For purposes of determining the “initial margin threshold amount”, with respect to any financial end user, an investment fund shall not be deemed to control, be controlled by, or be under common control with, its investment adviser, as defined in section 202(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)), commodity pool operator, as defined in section 1a(11) of the Commodity Exchange Act (7 U.S.C. 1a(11)), commodity trading advisor, as defined in section 1a(12) of the Commodity Exchange Act (7 U.S.C. 1a(12)), general partner or board of directors (or any affiliate of such person or entity), or any other investment fund, as long as such investment fund is a distinct legal entity that is not guaranteed by its investment adviser, commodity pool operator, commodity trading advisor, general partner or board of directors (or any affiliate of such person or entity), or any other investment fund, in the event of its insolvency or bankruptcy.

MFA notes certain terms used in the Basel-IOSCO criteria, such as “supported” and “collateralized” are undefined and vague in meaning. We used the term “guaranteed” in the proposed amendment above because it has a clear legal meaning. MFA would be pleased to address other credit support arrangements that may concern staff at the CFTC and the Prudential Regulators for purposes of our proposed amendment.

MFA believes that the proposed definitional changes in the final margin rules would distinguish funds from other entities for purposes of the appropriate application of the IM thresholds to financial end users, thus avoiding the inclusion of unknown and unexpected affiliate relationships based on a control test. More specifically, the proposed definitional changes would be used in determining whether an investment fund exceeded any of the following IM thresholds: the \$65 million initial margin threshold amount<sup>11</sup>, the material swaps exposure<sup>12</sup> threshold; and the phase-in threshold<sup>13</sup> for compliance dates. Unlike related entities in holding company or other similar structures, the different investment funds managed by a

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<sup>11</sup> The Proposed Rules define “initial margin threshold amount” as “aggregate credit exposure of \$65 million resulting from all uncleared swaps and uncleared security-based swaps between a covered swap entity and its affiliates, and a [counterparty/covered counterparty] and its affiliates”. PR Proposed Rules at 57390, Section \_\_.2; see CFTC Proposed Rules at 59927, Section 23.151.

<sup>12</sup> The Proposed Rules define “material swaps exposure” for an entity as follows: “an entity and its affiliates have an average daily aggregate notional amount of non-cleared swaps, non-cleared security-based swaps, foreign exchange forwards and foreign exchange swaps with all counterparties for June, July and August of the previous calendar year that exceeds \$3 billion, where such amount is calculated only for business days.” See PR Proposed Rules at 57391, Section \_\_.2; see CFTC Proposed Rules at 59927, Section 23.151.

<sup>13</sup> PR Proposed Rules at 57389, Section \_\_.1(d)(2)-(5); CFTC Proposed Rules at 59932, Section 23.159.

common manager do not typically have the kind of intercompany financial guarantees that can create interconnectedness and tie the risks and exposures associated with one company to other companies in the same ownership structure. We strongly believe that the appropriate risk-based analysis for applying IM thresholds to investment funds is the level of the individual fund. Our proposed definitional changes are intended to facilitate such risk analysis.<sup>14</sup>

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<sup>14</sup> For further discussion of the lack of cross-fund interconnectedness and guarantees in fund structures, please see MFA's letter to the Financial Stability Oversight Council, dated March 25, 2015.

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MFA appreciates the opportunity to comment on the Proposed Rules and respectfully submits these comments for the CFTC's and the Prudential Regulators' consideration. If the CFTC, the Prudential Regulators or their respective staffs have any questions, please do not hesitate to call Laura Harper Powell or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

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

cc:

**CFTC:**

The Hon. Timothy G. Massad, Chairman  
The Hon. Mark P. Wetjen, Commissioner  
The Hon. Sharon Y. Bowen, Commissioner  
The Hon. J. Christopher Giancarlo, Commissioner

**Prudential Regulators and Other Members of the Basel-IOSCO Working Group on  
Margining Requirements:**

Mr. Michael Gibson, Board of Governors of the Federal Reserve System  
Mr. Bobby Bean, Federal Deposit Insurance Corporation  
Mr. Sean Campbell, Board of Governors of the Federal Reserve System  
Mr. Nicolas Gauthier, European Commission  
Mr. John Lawton, U.S. Commodity Futures Trading Commission  
Mr. Thomas McGowan, U.S. Securities and Exchange Commission  
Mr. Matthew Osborne, UK Financial Services Authority  
Ms. Heather Pilley, UK Financial Services Authority  
Mr. Graham Young, Bank of England  
Mr. Kurt Wilhelm, U.S. Office of the Comptroller of the Currency

**SEC:**

The Hon. Mary Jo White, Chairman  
The Hon. Luis A. Aguilar, Commissioner  
The Hon. Daniel M. Gallagher, Commissioner  
The Hon. Michael S. Piwowar, Commissioner  
The Hon. Kara M. Stein, Commissioner