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17 C.F.R. §1.35(a)

April 17, 2014

Mr. Gary Barnett
Director, Division of Swap Dealer and Intermediary Oversight

Mr. Vincent A. McGonagle
Director, Division of Market Oversight

Ms. Melissa Jurgens
Secretary

Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: CFTC Staff Public Roundtable to Discuss Dodd-Frank End-User Issues and Request for Interpretative Guidance and Relief on Application of Rule 1.35(a) to Asset Managers

Dear Mr. Barnett, Mr. McGonagle and Ms. Jurgens:

The Asset Management Group ("**AMG**")[1] of the Securities Industry and Financial Markets Association ("**SIFMA**") appreciates the opportunity to provide additional comments on Commodity Futures Trading Commission Rule §1.35(a) (the "**Rule**") in connection with the CFTC Staff Public Roundtable to Discuss Dodd-Frank End-User Issues held on April 3, 2014 (the "**Roundtable**"). AMG is submitting this letter both to provide additional information to the Commodity Futures Trading Commission (the "**Commission**") relating to the Request for Interpretative Guidance, submitted by AMG and the Managed Funds Association, on December 10, 2013 (a copy of which is attached) (the "**December 2013 Letter**") and renew its request to exempt Asset Managers[2] that are

[1] AMG's members represent U.S. asset management firms whose combined assets under management exceed $30 trillion. The customers of AMG member firms include, among others, registered investment companies, ERISA plans and state and local government pension funds, many of whom invest in commodity futures, options and swaps as part of their respective investment strategies.

[2]While we acknowledge that "Asset Manager" is not a registration category or defined term under the Commodity Exchange Act of the regulations promulgated pursuant thereto, as the staff noted in Commission Letter No. 13-77, dated December 20, 2013, we would define this term to include any person in the business of giving advice to others regarding the value of commodity interests or securities for compensation. This includes persons registered with the Securities and Exchange Commission (the "**SEC**") or any U.S. state as

members of swap execution facilities ("**SEFs**") or members of designated contract markets ("**DCMs**")[3] (together with members of SEFs, "**Members**") from the oral and written recordkeeping requirements of the Rule. At the very least, pending evaluation of the foregoing request, we request that the Commission staff issue relief to postpone the compliance date for Asset Managers that are Members until December 31, 2014.

As we mentioned in our meeting with Commissioner Wetjen and members of the staff on March 26, 2014, application of the Rule to Asset Managers raises substantial cost and compliance issues. Costs include not only set-up costs for recording and storage of oral conversations but also on-going procedures to insure that written records are searchable and identifiable and comply with record preservation requirements contained in Commission Rule §1.31.[4]

As a general matter, we believe that the costs associated with requiring Asset Managers that are Members to comply with the written and oral recordkeeping requirements of the Rule significantly outweigh the benefits of the Rule. The stated goals of the Rule, which are to " promote… market integrity and protect customers"[5] as well as to enhance the capability of the Commission's Division of Enforcement,[6] can be met by applying the Rule exclusively to swap intermediaries and not to Asset Managers. From a cost-benefit perspective, we note that the Commission already has access to tape recordings of substantially all conversations by Asset Managers that are Members through intermediaries such as swap dealers ("**Dealers**"), major swap participants ("**MSPs**"), futures commission merchants ("**FCMs**"), SEFs and DCMs. Relying on existing sources

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an investment adviser under the Investment Advisers Act of 1940 (the "**Advisers Act**"), any person registered with the Commission as a commodity trading advisor ("**CTA**"), or commodity pool operator ("**CPO**"), any person regulated by a foreign regulatory authority as an investment adviser and any person operating pursuant to an exemption or exclusion from registration with or regulation by any such regulator.

[3] We have included DCM members as part of our request based on the staff's recent provision of no-action relief to trueEX, which is both a DCM and a temporarily-registered SEF. *See* Time-Limited No-Action Relief for Certain members of a Designated Contract Market from the Requirement to Record Oral Communications, Pursuant to Commission Regulation 1.35(a), in connection with the Execution of Swap Transactions, CFTC Letter No. 14-33 (March 21, 2014).

[4] *See, e.g.,* Rule §1.31(b)(1)(ii)(A)(providing that any digital storage medium or system must "preserve… the records exclusively in a non-rewritable, non-erasable format.") The non-rewritable, non-erasable format is referred to as "write once, read many," or "WORM."

[5] *See* Adaptation of Regulations to Incorporate Swaps, 77 Fed. Reg. 75,523 (December 21, 2012) (the "**Adopting Release**") *75,528.

[6] In the Roundtable, Chairman Wetjen explained that the Rule was designed to enhance the capability of the Commission's Division of Enforcement, deter potential bad actors in the market and assist the staff in conducting investigations.

of oral records and not requiring Asset Managers that are Members to separately maintain these records would be consistent with the Commission's guidance in the Adopting Release allowing entities subject to the Rule to rely on records maintained by others to satisfy the participants' own recordkeeping obligations.[7] In that regard, we note that the SEC, when considering amending its own record-keeping requirements for registered investment advisers ("**RIAs**") and registered investment companies ("**RICs**"), expressly rejected a proposal to apply record preservation requirements similar to those contained in Commission Rule §1.31 on the basis that the costs associated with preserving records in that manner outweighed the benefits.[8]

We are also concerned that imposition of both oral and written recordkeeping requirements on participants in the SEF market could have a significant chilling effect on the willingness of Asset Managers and end-users to trade swaps directly on SEFs. As a result, application of the Rules would arguably undermine the statutory goals of promoting SEF trading and pre-trade price transparency in the swaps market.

Finally, we believe that the Rule will be costly and difficult to interpret and apply because it was not designed for Asset Managers. Instead, the Rule calls for maintenance of records that Asset Managers do not use in their business[9] and speaks in terms of entities that are engaged in a "dealing" business, which would not seem to be applicable to Asset Managers. As discussed at the Roundtable, there are also a host of questions that remain open for interpretation. As a result, there is a significant risk that compliance practices will differ and the goals that the Rule was intended to achieve will not be met.

In light of these considerations, we believe that the Asset Managers should be exempted from all aspects of the Rule. Any benefits provided by applying the Rule to Asset Managers are modest and do not serve a sufficiently important public policy

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[7] Adopting Release *75531 and 75532 n.82 ("While complying with the final rule is the responsibility of the covered participant and the covered participant will be liable for failure to comply, depending on the type of record and arrangements made for access, covered persons may reasonably rely on a DCM, SEF or other Commission registrant to maintain certain records on their behalf.")

[8] Electronic Recordkeeping by Investment Companies and Investment Advisers, SEC Rel. Nos. IC-24991, and IA-1945 (May 31, 2001) at http://www.sec.gov/rules/final/ic24991.htm *12 n.7 ("Based on our consideration of costs, benefits, and other factors described in the proposing release we are not adopting .. a requirement [to preserve records in a WORM format] at this time. We recognize that the standards for electronic recordkeeping we are adopting for funds and advisers are different from the rules that we have adopted for broker-dealers, which require brokerage records to be preserved in a WORM format. We have not experienced any significant problems with funds or advisers altering stored records.")

[9] Examples of records required to be maintained under the rule that are inapposite to Asset Managers include: order blotters, trading cards, street books, cancelled checks (because Asset Managers typically do not custody client assets), signature cards, and communications provided concerning quotes, bids and offers.

purpose that justifies the significant costs and negative impact that applying the Rule to Asset Managers is likely to have on other important policy considerations such as SEF liquidity. As support for our position, we offer the following additional information for the Commission and staff to evaluate in acting on our request.

A. Substantially all Conversations covered by the Rule are Already Taped by Dealers and FCMs and such Records are Accessible by the Division of Enforcement

The Commission's recordkeeping requirements, including those imposed by the Rule, require Dealers and FCMs (in addition to registered CTAs that are Members) to make and retain records of all oral communications provided or received concerning "quotes, solicitations, bids, offers, instructions, trading and prices that lead to the execution of a transaction in a commodity interest." Conversations around "related" hedging transactions in the cash market are excluded. As a result, conversations that would be expected to be picked up by the recordings made by a registered CTA would be conversations seeking quotes or providing trading instructions for swap trades on SEFs or for block trades executed pursuant to SEF rules ("**Covered Conversations**"). Based on discussions with our members, who include most of the country's largest and mid-sized, traditional, real-money asset managers, Covered Conversations currently are conducted exclusively with Dealers and FCMs. As a result, these Covered Conversations would already be subject to taping by Dealers and FCMs since the compliance date for those entities has passed. Given this practice and the current structure of the SEF marketplace, it is highly unlikely that a Covered Conversation with an Asset Manager would have been held with a market participant other than with a Dealer or FCM.

We believe that substantially all Covered Conversations are currently taped by Dealers or FCMs, and we expect that status quo to continue into the foreseeable future. Asset Managers and other end users do not to "hold [themselves] out" as Dealers or make a market in swaps. They do not trade on a proprietary basis with customers or regularly enter into swaps as an ordinary course of business for their own account. Doing so would not be consistent with their core business of managing assets for clients. In addition, for various regulatory and risks management reasons, Asset Managers generally trade commodity interests for their clients only with or through Dealers and FCMs.

In addition, there is not currently a developed crossing market between end users for trades on SEFs. Even if a crossing market were to develop on SEFs in the future, the market would very likely operate electronically and/or on an anonymous basis, thereby obviating the need for oral records. Counterparties would prefer to transact electronically in those circumstances for competitive reasons and in order to avoid the risk that the prospective counterparties would replicate or front run the trade idea of the originating party.

Applying a duplicative requirement on Asset Managers would be inconsistent with the Commission's stated objective of drafting regulation so as to eliminate duplicative regulatory burdens. For example, in the context of adopting the swap reporting rules, the Commission expressly rejected the idea that both parties to a swap would be required to report. In the context of real time reporting, the Commission drafted the rules to provide that parties may rely on DCMs and SEFs to report all on-exchange trades. The swap reporting rules do not mandate separate reporting requirements for participants. With respect to selection of the reporting party, the Commission noted that it had drafted the rules specifically to assign a greater burden to Dealers and MSPs.[10] Furthermore, the Commission together with National Futures Association ("**NFA**") have traditionally designed recordkeeping requirements to be efficient for participants and avoid duplicative reporting.[11]

B. The Direct and Indirect Costs Associated with Taping are High and Disproportionate to the Expected Benefits

In order to assess the costs associated with complying with the Rule's oral taping requirement, we asked members to provide estimates and also spoke with other Asset Managers. The feedback we received demonstrated that the operational implementation costs of taping varied based on the anticipated compliance program, the number of people who would be subject to taping and the sophistication of the storage and filing equipment requested by the firms. In all cases, the estimated costs of implementing an oral recording program was in the six-figure range, with further on-going annual expense. In addition, our members emphasized that they would incur significant additional costs associated with the requirement, which were difficult to quantify, such as training, planning and overseeing the filing and storage systems for the oral records, designing and maintaining search and production capabilities and pulling tapes when requested or required to do so.

The taping requirement imposes an unreasonably high cost burden on firms that transact in only a small amount of swaps each year, in particular. We believe that the

[10] *See* Swap Data Recordkeeping and Reporting Requirements: Pre-Enactment and Transition Swaps, 77 Fed, Reg. 1188 (Jan. 9, 2012) *1199 ("The reporting framework [which allocates reporting responsibility to only one swap counterparty] …strikes an appropriate balance from a cost-benefit perspective…In the Commission's view, it is appropriate to assign a greater cost burden to SDs and MSPs than to the buy-side (including end-users), as SDs and MSPs are likely to be larger, more sophisticated and more active in swap markets and thus more able to realize economies of scale in carrying out reporting responsibilities.")

[11] *See, e.g.*, NFA/CFTC Eliminate Duplicate Filing Requirements for CPOs and CTAs, NFA Notice 1-03-02 (March 12, 2003) ("These changes mean that CPOs and CTAs no longer have to file duplicate copies of certain records with both the CFTC and NFA…These actions reflect NFA's commitment to making the regulatory process more efficient and to reducing Members' regulatory burdens without lessening customer protection.")

costs associated with compliance with the taping requirement may lead some firms to avoid entering into swap transactions that are mandated for SEF execution or not access a SEF directly. Avoiding SEF mandated swaps would mean that an Asset Manager would use alternative risk management and investment products – even though the foregone swaps may provide the most efficient means of satisfying a hedging or investment need.

As the Commission and staff already have access to recordings of substantially all Covered Conversations through the Commission's oversight of Dealers and FCMs, there seems to be no compelling reason, from a cost-benefit perspective, to apply the oral recordkeeping requirements under the Rule to Asset Managers that are Members. As described above, in our view, the direct and indirect costs associated with the taping requirement significantly outweigh any benefits of applying the Rule to Asset Managers that are Members. In light of our assessment of the costs and benefits, as well as countervailing public policy concerns such as promoting trading activity on SEFs, we do not believe that applying the Rule to Asset Managers that are Members would be in the public interest.

C. Written Records Regarding Swaps Executed on SEFs are Already Available to the Staff in Written Form from the SEFs and Dealers and, thus, should not be required to be maintained by Asset Managers

Commission Rule §45.2 requires SEFs, as well as DCMs, designated clearing Organizations ("**DCOs**"), Dealers and MSPs to "keep full, complete, and systematic records, together with all pertinent data and memoranda, of all activities relating to the business of such entity or person with respect to swaps."[12] During the life of a swap and for a period of two years thereafter, all of these entities, including SEFs, must have real time electronic access to the records that are required to be retained. Afterwards, the entities must be able to retrieve these records within three business days for the remaining three years of the retention period. All records covered by the regulation must be open for inspection by the Commission, as well as by the Department of Justice, the SEC and any prudential regulator authorized by the Commission.

As the Commission emphasized in the adopting release for Commission Rule §45.2, these requirements are and were intended to be comprehensive for regulated entities, such as SEFs and Dealers. The Commission and the staff have access to these records. Given the broad scope of the existing requirements, it would be duplicative for the Commission to require Asset Managers that are Members as well to maintain "full, complete, and systematic records, which include all pertinent data and memoranda, of all

[12] *See* Commission Rule §45.2.

transactions relating to its business of dealing in commodity interests and related cash or forward transactions."[13]

We note that the general swap recordkeeping rule (Commission Rule §45.2) also imposed recordkeeping requirements on end-users. In that context, however, the Commission noted that the end-user recordkeeping requirements were intentionally "narrower" because the Commission had determined that it would be appropriate to "place lesser burdens on non-SD/MSP counterparties to swaps, where this can be done without damage to the fundamental systemic risk mitigation, transparency, standardization, and market integrity purposes of the legislation."[14] The adopting release for Commission Rule §45.2 expressed a "policy choice" of the Commission not to burden end users with extensive recordkeeping but to rely, instead, on SEFs, DCMs, Dealers, MSPs and DCOs to maintain a comprehensive set of records. Instead, end users were required simply to maintain sufficient records to risk manage their portfolios and satisfy their contractual obligations.[15] We believe that the Commission should reevaluate the written recordkeeping requirements under Commission Rule §1.35(a) applicable to Asset Managers that are Members in light of the policy choice taken by the Commission in adopting Commission Rule §45.2 and the records already available to the Commission with respect to the same commodity interest transactions by SEFs, DCMs, DCOs, Dealers and FCMs.

D. Existing SEC Recordkeeping Rules for RIAs establish Comprehensive Requirements and should satisfy the Commission's Policy Goals

Asset Managers that are registered as RIAs are subject to extensive recordkeeping requirements under the federal securities laws.[16] RIAs to RICs are also subject to heightened recordkeeping requirements with respect to the transactions of those RICs under the Investment Company Act of 1940 (the "**1940 Act**") and the rules promulgated thereunder.[17] SEC rules require books and records to be preserved for up to five years in the case of RIAs[18] and up to six years[19] or, in some cases, permanently[20], in the case of

[13] *See* Commission Rule §1.35(a).

[14] Swap Data Recordkeeping and Reporting Requirements, 17 CFR Part 45 (December 14, 2011) *23.

[15] *Id.* *26 ("…the final rule provides less onerous recordkeeping requirements and less onerous retrievability requirements for non-SD/MSP counterparties, in order to ameliorate recordkeeping burdens for them.")

[16] *See* SEC Advisers Act Rule 204-2.

[17] *See* SEC Rule 31a-1 under the 1940 Act.

[18] *See* SEC Advisers Act Rule 204-2 (e).

RICs. Records are required to be accessible and to be organized to permit easy access and retrieval. The SEC requirements include retention of transactional and execution records, and the obligations are customized by reference to a firm's advisory or fund business, which is more appropriate for the business of Asset Managers.[21]

While we believe that it would be most appropriate to exempt Asset Managers that are Members from the Rule altogether, the staff could make such an exemption from application of the written and oral recordkeeping requirements of the Rule conditional on maintaining written transactional records of commodity interest transactions, including information regarding price quotes and execution instructions, in accordance with the SEC's recordkeeping rules under the Advisers Act. As highlighted by the SEC itself, its existing recordkeeping requirements provide the ability for regulators to oversee RIAs and, thus, protect clients and enhance the integrity of the marketplace generally.[22]

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For all of the reasons discussed in this Letter and the December 2013 Letter, we request that the staff provide relief that exempts Asset Managers that are Members from application of both written recordkeeping and the oral recordkeeping requirements of the Rule. At the very least, pending evaluation of the foregoing request for relief, we further request the Commission staff postpone the compliance date for the Rule as it applies to Asset Managers that are Members until December 31, 2014.

The Commission is authorized to issue this guidance and relief under its general regulatory authority granted under §§4 and 5h of the Commodity Exchange Act.

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[19] *See* SEC 1940 Act Rule 31a-2(a)(2)-(6).

[20] SEC 1940 Act Rule 31a-2(a)(1), requiring RICs to retain permanently certain transactional records and ledgers as well as certain other records.

[21] *See, e.g.,* SEC Advisers Act Rule 204-2(a) relating to maintenance of books and records relating to an adviser's "*investment advisory business"* and SEC 1940 Act Rule 31a-1(a) requiring maintenance of records relating to the RIC's business.

[22] *See* Final Rule: Electronic Recordkeeping by Investment Companies and Investment Advisers, SEC Rel. Nos. IC-24991 and IA-1945 (May 31, 2001)("The recordkeeping requirements are a key part of the commission's regulatory program for funds and advisers, as they allow us to monitor fund and adviser operations, and to evaluate their compliance with federal securities laws.")

Should you have any questions, please do not hesitate to contact Tim Cameron of AMG at 212-313-1389, Matt Nevins of AMG at 212-313-1176 or Georgia Bullitt of Willkie Farr & Gallagher LLP at 212-728-8250.

Sincerely,

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Timothy W. Cameron, Esq.
Managing Director, Asset Management Group
Securities Industry and Financial Markets Association

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Matthew J. Nevins, Esq.
Managing Director and Associate General Counsel, Asset Management Group
Securities Industry and Financial Markets Association

cc: Hon. Mark Wetjen, Chairman, Commodity Futures Trading Commission
Hon. Scott O'Malia, Commissioner, Commodity Futures Trading Commission
Frank Fisanich, Chief Counsel, Division of Swap Dealer and Intermediary Oversight
Erik Remmler, Deputy Director, Division of Swap Dealer and Intermediary Oversight
Nancy Markowitz, Deputy Director, Division of Market Oversight
Katherine Driscoll, Associate Director, Division of Swap Dealer and Intermediary Oversight
Scott Reinhart, Office of the Chairman
Joseph Cisewski, Office of the Chairman
Ted Serafini, Office of the Chairman

Certification Pursuant to Commission Regulation §140.99(c)(3)

As required by Commission Regulation §140.99(c)(3), we hereby (i) certify that the material facts set forth in the attached letter dated April 17, 2014 are true and complete to the best of our knowledge; and (ii) undertake to advise the Commission, prior to the issuance of a response thereto, if any material representation contained therein ceases to be true and complete.

Sincerely,

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Timothy W. Cameron, Esq.
Managing Director, Asset Management Group
Securities Industry and Financial Markets Association

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Matthew J. Nevins, Esq.
Managing Director and Associate General Counsel, Asset Management Group
Securities Industry and Financial Markets Association