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

December 16, 2010

VIA EMAIL

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: SEC Study on Enhancing Investment Adviser Examinations under Section 914 of the Dodd-Frank Wall Street Reform and Consumer Protection Act

Dear Ms. Murphy:

Managed Funds Association ("MFA")[1] and its members appreciate the opportunity to provide comments to the Commission on Section 914 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank" or the "Act"), which requires the Commission to, among other things, study the extent to which the establishment of a self-regulatory organization ("SRO") to augment the Commission's oversight of investment advisers would improve the frequency of examinations of investment advisers. We are pleased that the Commission has approached the study in such a deliberate and thoughtful manner, and we hope that our perspective can assist it in conducting this important analysis.

MFA members favor smart, effective regulation of securities markets generally, and have a strong interest in thoughtful and efficient regulation of hedge fund managers. A significant proportion of our members are currently registered as investment advisers with the SEC, and we expect that most will be registered with the SEC (or CFTC) as of the effective date of Dodd-Frank. We offer these comments on the future oversight of the private fund manager industry in light of this perspective.[2]

Based on our experience, we strongly believe that the existing framework of SEC regulation of private fund managers, as enhanced by Dodd-Frank, is effective in fulfilling the SEC's mission to protect investors, maintain fair, orderly and efficient markets and facilitate

[1] MFA is the voice of the global alternative investment industry. Its members are professionals in hedge funds, funds of funds and managed futures funds, as well as industry service providers. Established in 1991, MFA is the primary source of information for policy makers and the media and the leading advocate for sound business practices and industry growth. MFA members include the vast majority of the largest hedge fund groups in the world who manage a substantial portion of the approximately $1.5 trillion invested in absolute return strategies. MFA is headquartered in Washington, D.C., with an office in New York.

[2] *See also* Letter from Richard H. Baker, President and CEO, MFA, to Elizabeth Murphy, Secretary, Securities and Exchange Commission (Sept. 22, 2010), available at: http://www.managedfunds.org/downloads/MFA%20SEC%20Letter.9.22.10.pdf.

capital formation.[3] As described below, an SRO would lack experience in regulating private fund managers, create inconsistent regulation for investment advisers, face difficult conflicts of interest, increase regulatory costs, and ultimately diminish the quality of regulatory oversight of the industry.[4]

I. The SEC Currently Performs the Potential Oversight Functions of an SRO

The range of activities engaged in by private fund managers is subject to comprehensive, long-standing federal securities laws and regulatory oversight. The SEC regulates private fund managers as investors, like other market participants, under the Securities Act of 1933 ("Securities Act") and Securities Exchange Act of 1934 ("Exchange Act"), and regulates investment advisers managing client assets under the Investment Advisers Act of 1940 ("Advisers Act"). In broad terms, this statutory framework, as enhanced in a number of respects by Dodd-Frank and upcoming regulatory implementation of the Act, subjects private fund managers to oversight with respect to their trading and investment activities, their effects on markets and financial stability, and their management of client assets. In its entirety, this framework applies to all areas of a private fund manager's business.

Securities and Derivatives Trading Activities

Private fund managers, like other investors, are subject to extensive rules governing trading activities that involve securities. Such rules include, for example, prohibitions on insider trading,[5] restrictions on short selling,[6] disclosure requirements,[7] and limitations on the purchase and sale of unregistered securities.[8] More generally, the SEC has broad authority to investigate and punish any type of manipulative trading activity involving securities. Pursuant to Rule 10b-5 under the Exchange Act, market participants are prohibited from using any device or scheme to defraud, from making any untrue statement of a material fact, or from engaging in any fraudulent act, practice, or course of business. The SEC regularly enforces the prohibitions in Rule 10b-5 against investors of all types that engage in inappropriate conduct, including private fund managers.

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[3] We have limited our discussion in this letter to the regulation and oversight of private fund managers, and the potential effects of an SRO on the private fund industry.

[4] MFA strongly respects the role of SROs as securities associations with respect to broker-dealers, exchanges with respect to member firms, and clearing agencies with respect to participants. Our comments relate only to the question of whether an SRO is appropriate for oversight of private fund managers.

[5] *E.g.,* Exchange Act Rule 10b5-1 and Rule 10b5-2.

[6] Regulation SHO, Rule 200 *et seq.* The SEC has recently adopted a number of new requirements relating to short selling.

[7] *E.g.*, Exchange Act Section 13 and Section 16.

[8] *E.g.*, Securities Act Section 4(2); Regulation D, Regulation S, and Rule 144A under the Securities Act.

In addition to these long-standing rules governing transactions in securities, Dodd-Frank creates a new, comprehensive regulatory regime for investing activities involving over-the-counter derivative instruments. Prior to Dodd-Frank, over-the-counter derivatives were generally not subject to the type of direct regulatory oversight applicable to transactions in securities. Title VII of Dodd-Frank establishes an extensive new framework for the regulation of over-the-counter derivatives. The rules to be adopted by the SEC and CFTC under Title VII will, among other things: (i) require certain standardized transactions to be cleared and exchange traded; (ii) require "swap dealers" and "major swap participants" to register with the SEC or CFTC, and subject them to significant requirements; (iii) impose initial and variation margin requirement on both cleared and uncleared transactions; and (iv) provide for significant incremental transparency, including transaction reporting, to market participants and regulators. Many private fund managers, like other investors, transact in over-the-counter derivatives as part of their investment strategy, and together these new rules will implement a broad framework of CFTC and SEC oversight of such activities.

Systemic Risk Framework

Dodd-Frank also subjects hedge fund managers to new regulations designed to allow policy makers to monitor investment activities of funds they manage and the impact of the industry and any individual firm on the financial system. Under the Act, private fund managers will be required to maintain records and make reports to the SEC for the protection of investors or the assessment of systemic risk. Such records and reports will include detailed information about the activities of private funds and managers, including assets under management, use of leverage, trading positions, arrangements with counterparties, and the types of assets held in its portfolio. The SEC will also have authority to request additional information from managers as it deems necessary.[9] By receiving this information from private funds and their managers, the SEC will have the ability to assess if the investment activities of a particular firm, whether due to size or other factors, create significant risk to the financial system.

Along with this system of recordkeeping and reporting by private fund managers, Dodd-Frank also creates a new Financial Stability Oversight Council ("FSOC"), and assigns it the duties of determining which financial institutions pose a threat to financial stability, imposing restrictions on certain activities, and, if necessary, providing for the orderly liquidation of such financial institutions.[10] Together, these systemic risk provisions in Dodd-Frank create another layer of regulation and oversight of private funds and their managers. This type of systemic risk oversight and analysis is not a function that can or should be delegated to an SRO.

Investor Protection

Finally, private fund managers are subject to SEC regulation as investment advisers under the Advisers Act, which applies broadly to an advisory firm's investment activities and relationship with clients. Private fund managers registered under the Advisers Act must, among

[9] Section 404 of Dodd-Frank.

[10] Title I and Title II of Dodd-Frank.

other things, meet standards of conduct as fiduciaries to their clients, provide detailed disclosure to clients and the SEC, maintain books and records relevant to their business, be subject to periodic inspections and examinations by SEC staff, adopt and implement written compliance policies and procedures, designate a chief compliance officer, and establish a written code of ethics that sets standards of conduct for employees.[11] Together, these provisions ensure that investment advisory clients are treated with the highest standard of care. Significantly, Dodd-Frank maintains the Advisers Act as the primary framework for the regulation of private fund managers. We strongly agree with this approach and believe that the Advisers Act, as enhanced by SEC staff interpretations and guidance, is an effective, comprehensive framework for regulating the activities of private fund managers and other investment advisers.

Dodd-Frank not only continues to subject the private fund industry to SEC oversight under the Advisers Act, it expands the Act's application to private fund managers by requiring certain managers to register with the SEC. Currently, many private fund managers are registered with the SEC and subject to the substantive provisions of the Advisers Act, and many rely on an exemption from SEC registration provided for in the Act.[12] Dodd-Frank eliminates the existing exemption and requires all private fund managers with at least $150 million in assets under management to register under the Advisers Act. As a result, as of the effective date of Dodd-Frank, many private fund managers that are currently not registered will register with the SEC and become subject to the Advisers Act. Throughout consideration of Dodd-Frank, MFA consistently supported registration requirements for private fund managers.[13]

The regulatory framework for private fund managers described above addresses all areas of a manager's business – securities and derivatives trading activities, the effects of its investment activities on financial stability, registration with the SEC, and the protection of investors – and leaves no gaps in oversight.[14] In contrast, policy makers in the past established existing SROs for the financial services industry in response to incomplete or ineffective

[11] *See e.g.,* Section 206 of the Advisers Act and rules thereunder.

[12] Section 203(b)(3) of the Advisers Act. Managers not registered under the Advisers Act are nevertheless subject to the broad anti-fraud prohibitions in Section 206 of the Advisers Act. The SEC regularly uses its authority under this Section to investigate and punish any inappropriate conduct by unregistered investment advisers, including private fund managers.

In many respects, Section 206 has broader application than the anti-fraud provisions in the other federal securities laws. For example, unlike Rule 10b-5 under the Exchange Act, Section 206 is not limited to situations involving the purchase or sale of a security. In addition, in certain instances *scienter* may not be required to find a violation of Section 206 or rules thereunder, in contrast to a Rule 10b-5 violation. *See e.g.*, Lemke, Lins, *et al,. Hedge Funds and Other Private Funds: Regulation and Compliance* (2009-2010 ed.) at §3:17.

[13] *See e.g.,* Testimony of Richard H. Baker, President and CEO, MFA, Hearing on Industry Perspectives on the Obama Administration's Financial Regulatory Reform Proposals, Committee on Financial Services, U.S. House of Representatives (July 17, 2009).

[14] In addition to the areas of SEC regulation described above, hedge fund managers are subject to a number of other rules, including, among others, those adopted by the CFTC, the Department of Labor, and the Department of Treasury.

regulatory environments. For example, the precursor to the NASD was developed in the 1930's in response to the need to regulate the over-the-counter securities markets. At the time, the lack of regulation of the over-the-counter securities markets created a significant gap in the regulatory scheme.[15] The existing framework for the regulation of private fund managers leaves no such gap to be filled by an SRO.

SEC Inspection and Examination Resources

A critical feature of the SEC's regulation of private fund managers is its inspection and examination program. We believe the additional resources provided by Dodd-Frank will substantially enhance the SEC's capability to inspect and examine private fund managers. Dodd-Frank increases the authorized funding level for the SEC for the next five years by approximately 15% per year, which would double the Commission's authorized budget to $2.25 billion by fiscal year 2015. The Act also allows the SEC to establish and maintain a reserve fund of up to $100 million.[16] The increased funding will enable the SEC to enhance its oversight of private fund managers by hiring staff, upgrading its technology infrastructure, and applying additional resources to its Office of Compliance Inspections and Examinations ("OCIE").[17] Furthermore, the upgraded technology, additional information from advisers, and improved risk-based exams will enable the SEC to perform its oversight function more efficiently.

Specifically, we believe the funding levels authorized by Dodd-Frank will allow the SEC to regularly inspect and examine private fund managers that become registered with the Commission as a result of the Act. We recognize, however, that making this determination prior to the effective date of Dodd-Frank is difficult because the total number of private fund managers that will be registered at that time is uncertain. As explained above, the Act will require unregistered private fund managers with at least $150 million in assets under management to register with the SEC. There are no data on the number of managers that fall into this category, however, and the exact number will not be known until managers register with the SEC in advance of the effective date of Dodd-Frank. At the same time, Dodd-Frank will preclude many small private fund managers and other investment advisers from registering with the SEC, by increasing to $100 million the current *de minimis* threshold of $25 million in assets under management for SEC registration.[18] The SEC estimates that this new threshold will require approximately 4,100 investment advisers currently registered with the SEC to deregister

[15] *See* SEC Special Study of the Securities Markets (1963), Chapter XII at 603-4 ("While comparatively little was known about these markets in 1934 when the Exchange Act became law, it was early recognized that their regulation was necessary, since 'to leave the over-the-counter markets out of a regulatory system would be to destroy the effects of regulating the organized exchanges").

[16] Section 991 of Dodd-Frank.

[17] With the increased budget for fiscal year 2011, the SEC plans to fill 1,033 examination positions in OCIE, an increase of 100 positions from FY 2010. The Commission estimates that the additional staff will enable it to conduct 50 additional exams of advisers, 25 additional mutual fund exams, and 75 exams of newly registered private fund managers. *SEC FY2011 Congressional Justification In Brief* (Feb. 2010) ("SEC FY2011 Justification").

[18] Section 410 of Dodd-Frank.

and register in the state in which they are located.[19] In addition, Section 408 of the Act provides for a new exemption from SEC registration for managers solely to private funds with less than $150 million in assets under management, which will further limit the number of new registrants.

In our view, the uncertainty surrounding the number of private fund managers and other investment advisers that will be registered with the SEC at the time of the effective date of the registration provisions of Dodd-Frank suggests that policy makers should take a deliberative approach to evaluating the SEC's capacity to oversee newly registered managers. As the SEC implements many of the required rulemakings and studies under Dodd-Frank, and investment advisers prepare for the new registration requirements, we expect that it will be easier over the coming months to fully assess whether the Act provides the SEC with sufficient resources for its inspection and examination program, or whether additional resources may be needed.[20]

In addition to adequate funding, equally important to an effective inspection and examination program is an experienced examination staff, smart, efficient information gathering procedures, and methods for regulators to identify registrants that present increased risks. We believe OCIE has recently made substantial improvements in these areas by adding senior staff with backgrounds in the private fund industry, and hiring new examination staff with skill sets applicable to examining private fund managers, including trading, portfolio management, valuation, complex products, sales, compliance and forensic accounting.[21] MFA has sought to assist OCIE in training its staff by offering to serve as an educational resource about practices within the private fund industry. Many MFA members have had the opportunity to engage in dialogue with OCIE staff about ways to improve inspections of private fund managers and other industry issues. Members have also participated in training sessions for examination staff about legal and compliance issues in the industry. MFA believes the steps taken by OCIE over the last two years, and those it intends to make over the coming months, together will strengthen its regulation of the private fund industry.

In addition to enhancing its staff's knowledge of the private fund industry, OCIE is continuing to develop techniques to gather relevant, timely information about private fund managers and use the information to identify managers that present increased compliance risk. Through this risk-based approach to examinations, OCIE seeks to obtain targeted information

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[19] Rules Implementing Amendments to the Investment Advisers Act of 1940, Investment Advisers Act Release No. 3110 (Nov. 19, 2010). *See also* Investment Adviser Association and National Regulatory Services, *Evolution/Revolution 2010: A Profile of the Investment Advisory Profession* (Sept. 2010) (estimating that approximately 4,000 SEC-registered investment advisers will shift to state registration as a result of Dodd-Frank).

[20] It is worth noting that the SEC has made substantial progress to date in implementing reforms under Dodd-Frank. For example, based on the SEC's most recent estimate, since the enactment of Dodd-Frank in July, it has issued approximately 15 rule proposals, adopted at least 8 final rules or interpretive positions, and undertaken numerous other actions. The SEC has published a schedule of its activities under Dodd-Frank that indicates completion of its implementation program by mid-2011, available at: http://www.sec.gov/spotlight/dodd-frank/accomplishments.shtml.

[21] *See Examinations by the SEC, Office of Compliance Inspections and Examinations* (Feb. 2010), available at http://www.sec.gov/about/offices/ocie/ocieoverview.pdf.

that may indicate that a registrant presents a greater likelihood of inappropriate conduct.[22] MFA believes a risk-based approach is an effective method for OCIE to allocate its resources to inspections of private fund managers and other investment advisers that require enhanced scrutiny.

A critical component of OCIE's risk-based approach is its ability to gather key information from registrants. Dodd-Frank makes significant enhancements to OCIE's capacity to gather such information from private fund managers by providing the SEC with broad authority to require managers to maintain records and submit reports of detailed investment information to the SEC for investor protection or the assessment of systemic risk. We fully expect that the SEC will implement these provisions of Dodd-Frank to obtain additional information about private fund managers and enhance the effectiveness of its inspection and examination program.[23]

In addition to upcoming reforms under Dodd-Frank, the SEC has already taken steps to gather more detailed information from private fund managers and other investment advisers. The SEC, for example, recently amended Part 2 of Form ADV, the form that SEC-registered investment advisers must file with the SEC, by replacing the existing "check-the-box" format with a requirement that advisers provide a narrative disclosure about their business, investment strategy, clients, compliance practices and other information.[24] These disclosures, which will also be made publicly available, will provide regulators and investors with substantial additional information about the businesses of private fund managers. The SEC has also recently proposed amendments to Part 1 of Form ADV that would require managers to disclose a substantial amount of information about each private fund that they manage.[25] In addition to these changes to Form ADV, OCIE is expanding its gathering of targeted information about private fund managers through request letters that seek information about specific industry practices. We believe the combined effect of the expanded Form ADV and the increased use of request letters will meaningfully enhance the type of information about private fund managers that OCIE will receive and incorporate into its risk-based examination approach.

We believe the steps the SEC has taken to strengthen its inspection and examination program for investment advisers, including private fund managers, along with additional funding, will lead to enhanced oversight of the private fund industry. If the Commission were to determine, even after the implementation of Dodd-Frank, that it requires additional resources to

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[22] *Id.* ("OCIE's Risk Assessment staff sorts and analyzes this risk information and generates management-level reports that identify and provide insight on potential high-risk areas. The information is used by management in prioritizing risks for examination attention and in allocating program resources.")

[23] *See, e.g.,* SEC FY2011 Justification ("In fiscal year 2011, OCIE plans to significantly expand and enhance its oversight of registered advisers").

[24] Amendments to Form ADV, Investment Advisers Act Release No. 3060 (July 28, 2010).

[25] Rules Implementing Amendments to the Investment Advisers Act of 1940, Investment Advisers Act Release No. 3110 (Nov. 19, 2010). The proposed amendments would also require certain private fund managers that are exempt from SEC registration to report information on Form ADV.

conduct examinations of all registered investment advisers with the appropriate frequency, we believe the Commission should work with policy makers to ensure that it receives such resources.

II. An SRO Would Face Challenges to Effectively Regulating Private Fund Managers

In addition to the concern that an SRO for private fund managers only would serve to carry out a function that is already being performed effectively by the SEC, we are concerned that an SRO could diminish the quality of regulation of private fund managers.

An SRO Would Lack Experience in Overseeing Private Fund Managers

An effective private fund industry SRO must have extensive knowledge of the industry, and experience in interpreting and applying the Advisers Act and its rules to private fund managers. We are not aware of any organization with these necessary competencies, and we are concerned that an SRO's lack of experience in overseeing private fund managers could lead to inconsistent regulation and uncertainty for managers in operating their businesses. In particular, the nature of the Advisers Act as a principles-based statute would present difficult challenges to a new SRO, or an SRO that instead has experience in administering a rules-based regulatory framework.

An important example of the principles-based approach to regulation under the Advisers Act is the fiduciary duty that an investment adviser owes to its client. For more than forty years, the SEC has brought enforcement actions against investment advisers for violations of their fiduciary duty to clients under Section 206 of the Advisers Act. The Commission has broadly interpreted the scope of an investment adviser's fiduciary duty to apply to various aspects of an adviser's management of client assets. For example, investment advisers must, among other things, make full and fair disclosure of all material facts to their clients, provide impartial advice, disclose conflicts of interest, allocate securities fairly, and achieve best execution in connection with securities transactions. These and other standards of conduct are generally not set out in the Advisers Act or its rules, but rather are applied by the SEC staff based on its interpretations of the scope of an adviser's fiduciary duty. They have functioned effectively for many years, and are an integral part of how investment advisers conduct their business. We have strong concerns with an SRO assuming responsibility for interpreting and applying this fundamental aspect of investment adviser regulation.

Moreover, the fiduciary duty investment advisers owe to their clients is unique in the securities industry. For example, although broker-dealer firms provide investment advice to clients in the course of their business, these firms generally rely on an exclusion from the definition of investment adviser in the Advisers Act, and as a result are not subject to its provisions.[26] Instead, broker-dealer firms providing investment advice to clients are subject to a different, lower standard of conduct that generally requires only reasonable grounds for believing

[26] Advisers Act Section 202(a)(11)(C).

that a recommendation is suitable for a client.[27] An SRO accustomed to this standard for broker-dealer firms would have difficulty applying the investment adviser fiduciary standard of conduct and keeping such standards distinct.[28]

An SRO for private fund managers would have difficulty hiring experienced personnel to quickly acquire the necessary expertise. The private fund industry is small in comparison to other types of financial firms, and individual private fund managers typically rely on small staffs. As a result, the pool of personnel experienced with the operations and legal requirements of hedge fund managers is quite limited. Despite the small size of the industry, an SRO would need to be of sufficient size and scale to effectively oversee the industry, and we are concerned that an SRO would have difficulty establishing and maintaining such a staff.

An SRO Would Subject Different Types of Investment Advisory Firms to Inconsistent Oversight

The investment advisory industry is made up of extremely diverse firms, including independent advisers, financial planners, traditional asset management firms, wealth managers, large financial institutions, small advisers, private fund managers, mutual fund advisers, pension consultants and others. Under the Advisers Act, each of these types of investment advisory firms is currently subject to consistent regulation by the SEC. Creating an SRO exclusively for one type of investment advisory firm, such as private fund managers, would seem to undermine the intent of the Advisers Act by creating separate, and potentially inconsistent, oversight of investment advisers. Moreover, the creation of an SRO for private fund managers could subject a single advisory firm, such as a private fund manager or a traditional asset management firm that manages private funds in addition to other types of accounts, to two different regulatory frameworks. We are concerned that subjecting private fund managers to oversight that is separate from other investment advisory firms would create uncertainty, and could have the unintended consequence of leading to uneven playing field among advisory firms.

An SRO Would Face Inherent Conflicts of Interest in Overseeing Private Fund Managers and other SRO Members

An SRO overseeing both private fund managers and other types of firms would face difficult conflicts of interest in overseeing all of its members fairly and equitably. Private fund managers are active participants throughout the securities markets, and interact with other financial firms in numerous capacities, including engaging them as service providers to funds they manage, entering into counterparty arrangements with them, and competing with them for

[27] NASD Rule 2310. *See also* FINRA Rule 2114.

[28] Section 913 of Dodd-Frank requires the SEC to study the standards of care for brokers, dealers and investment advisers when providing investment advice to retail customers, and permits it to establish a fiduciary duty for brokers and dealers when providing investment advice to retail customers. If the SEC were to establish a new fiduciary duty, it would more closely resemble the existing fiduciary duty standard for investment advisers, rather than the suitability standard for broker-dealers. We do not expect this process to affect the fiduciary duty applicable to managers to institutional clients and private funds.

investment opportunities. These natural and healthy relationships would create challenges for an SRO to oversee private fund managers and other types of firms in an impartial manner.

An example of the type of interactions that could give rise to potential conflicts of interest for an SRO is the relationships between private fund managers and broker-dealer firms. In implementing their investment strategies, hedge fund managers engage one or more broker-dealer firms to serve as a prime broker for funds they manage. Prime brokers provide a number of important services to hedge funds, including custody of assets, clearing of securities transactions, securities lending, financing and reporting. In addition, hedge fund managers enter into arrangements with broker-dealer firms in which they serve as a counterparty to a financial transaction with the hedge fund. While counterparty arrangements take various forms, depending on the type of financial transaction, each arrangement is an arm's length transaction between a fund manager and a broker-dealer firm in which the interests of the two parties are generally not aligned. The features of prime brokerage and counterparty arrangements are complex, and hedge fund managers and broker-dealers generally negotiate their terms. We are concerned that the overlapping and sometimes competing interests between hedge fund managers and broker-dealer firms created by these arrangements would present challenges to an SRO responsible for overseeing these types of firms fairly and equitably.[29]

An SRO Would be More Costly than Enhancements to OCIE

The expense of establishing a new SRO would exceed the cost of providing additional resources to OCIE, and would place an undue burden on private fund managers. As noted above, the private fund industry is small, and an SRO would not benefit from economies of scale that would reduce costs to a wider membership. Because many private fund managers are also relatively small firms, fees paid to an SRO would constitute a higher percentage of revenue than other industries. We believe the additional resources provided by Dodd-Frank will ensure that the Commission is able to continue serving its oversight function. If the SEC requires additional resources to permit OCIE to conduct examinations of registered investment advisers with the appropriate frequency, the SEC should work with policy makers to ensure that it receives such resources.

An SRO Could Create Uncertainty for Managers and Reduce Accountability

The current regulatory framework ensures that a single entity has authority for rulemaking, examinations and inspections, and enforcement with respect to private fund managers and other investment advisers. The creation of an SRO would upset this structure, and potentially create regulatory uncertainty and reduce accountability. A structure in which an SRO was given authority to inspect and examine private fund managers, and the SEC retained policy

[29] Broker-dealer firms also interact with private fund managers in a number of other capacities, including as market makers, dealers, syndicators, and underwriters of securities issuances. Many of these roles raise similar potential conflicts of interest with respect to private fund managers. Despite the very best of intentions, it might be difficult for an SRO with a large broker-dealer membership to balance those responsibilities with its responsibilities for private fund managers. Moreover, an SRO might find itself in the awkward position of having to favor one class of regulatee over another. We do not believe that placing an SRO in such a conundrum would serve investors well.

making authority, for example, would add an extra layer of regulation for managers to comply with the Advisers Act. This dual regulatory structure would raise the risk of managers being confused as to how to comply with guidance from both entities, and could also lead to inconsistent policies. If instead, an SRO were provided with broad inspection and policy making authority over private fund managers, the SEC would no longer have direct oversight responsibility for private fund managers. We believe that to avoid either of these results, it is important for an independent, governmental agency to be accountable for such oversight.

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For the reasons described above, we are concerned that an SRO for private fund managers would reduce the quality of regulatory oversight of the industry. The long-standing practice of SEC oversight, as strengthened by Dodd-Frank, is a comprehensive framework that applies to all areas of a private fund manager's activities, and is the most effective approach for the regulation of industry. Should you have any questions, please contact Stuart Kaswell or the undersigned at (202) 367-1140.

Respectfully submitted,

/s/ Richard H. Baker

Richard H. Baker
President and CEO

cc: The Honorable Mary Schapiro
The Honorable Kathleen L. Casey
The Honorable Elisse B. Walter
The Honorable Luis A. Aguilar
The Honorable Troy A. Paredes