**Managed Funds Association**
The Voice of the Global Alternative Investment Industry
Washington, D.C. | New York | Brussels

December 5, 2022

**Via Electronic Submission**

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549-1090

**Re: Notice of Proposed Rulemaking on Further Definition of "As a Part of a Regular Business" in the Definition of Dealer and Government Securities Dealer, File No. S7-12-22**

Dear Ms. Countryman:

Managed Funds Association ("**MFA**")[1] submits these comments to the Securities and Exchange Commission ("**Commission**" or "**SEC**") on the proposed rulemaking to revise and expand the definitions of "dealer" and "government securities dealer" under Sections 3(a)(5) and 3(a)(44), respectively, of the Securities Exchange Act of 1934 ("**Exchange Act**").[2] These comments supplement our comment letter dated May 27, 2022, on the Proposal ("**May Comment Letter**"),[3] and are in furtherance of meetings we and our members have had with SEC Commissioners and staff.

At the outset, we want to emphasize that we support ensuring that entities that engage in genuine dealing activities are registered and appropriately regulated.[4] However, we continue to

[1] MFA represents the global hedge fund and alternative asset management industry and its investors by advocating for regulatory, tax, and other public policies that foster efficient, transparent, and fair capital markets. MFA's more than 150 member firms collectively manage nearly $2.6 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has a global presence and is active in Washington, Brussels, London, and Asia. www.managedfunds.org

[2] SEC Release No. 34-94524 (Mar. 28, 2022), 87 Fed. Reg. 23,054 (Apr. 18, 2022) ("**Proposal**"), available at: https://www.govinfo.gov/content/pkg/FR-2022-04-18/pdf/2022-06960.pdf.

[3] *See* Letter from Jennifer W. Han, Executive Vice President, Chief Counsel & Head of Global Regulatory Affairs, MFA, to Vanessa Countryman, Secretary, SEC (May 27, 2022), available at: https://www.sec.gov/comments/s7-12-22/s71222-20129911-296085.pdf.

[4] By contrast, private funds are customers that do not engage in dealing activity and their advisers are already subject to extensive regulation by the Commission. In particular, registered investment advisers are subject to a comprehensive regulatory regime that covers, among other things, recordkeeping (17 C.F.R. § 275.204-2), reporting (*id.*), compliance programs (17 C.F.R. § 275.206(4)-7), custody (17 C.F.R.

believe that the proposed rulemaking is unnecessary and, unless revised, harmful to markets and market participants. As explained in our May Comment Letter, we are particularly concerned that the proposed quantitative and qualitative tests for who is a dealer or government securities dealer ("**Proposed Rules**") are vague, open-ended, and, in the case of the quantitative test, unprecedented and overbroad. As such, if adopted, the Proposed Rules would potentially capture many entities that are not dealers but are simply investors. Among the many problematic elements of the Proposal, this would subject alternative asset managers and their investors to a dealer regime that is not designed for, and is ill-suited to, private funds, which are not operating companies and have no employees or customers.[5]

The Proposal is not only an unjustified overreach, but it would also have significant negative unintended consequences on investors and markets, in particular the U.S. Treasury market, which is in an already fragile state. If the Proposed Rules are adopted as proposed, many hedge funds will exit or reduce participation in the U.S. Treasury market rather than register as dealers. This could lead to further concentration in the U.S. Treasury market, decrease market resilience and stability, increase government financing costs, and lead to increased systemic risk—which are at odds with the Inter-Agency Working Group on Treasury Market Surveillance principles.[6] Liquid Treasury markets are essential to the proper functioning of U.S. and global markets, and reduced participation in the Treasury markets will lead to less liquidity and greater volatility, which could result in significant damage to the financial markets and the real economy in the United States.[7] Therefore, our members are concerned that, if not carefully calibrated, the

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§ 275.206(4)-2), regulatory examinations and inspections, and antifraud rules (*e.g.*, 17 C.F.R. § 275.206(4)-8). Private funds managed by registered investment advisers are also subject to extensive reporting requirements on Form PF, which the Commission has proposed to amend. *See* Form PF; Reporting Requirements for All Filers and Large Hedge Fund Advisers, 87 Fed. Reg. 53,832 (Sep. 1, 2022), available at: https://www.govinfo.gov/content/pkg/FR-2022-09-01/pdf/2022-17724.pdf; Amendments to Form PF To Require Current Reporting and Amend Reporting Requirements for Large Private Equity Advisers and Large Liquidity Fund Advisers, 87 Fed. Reg. 9,106 (Feb. 17, 2022), available at: https://www.govinfo.gov/content/pkg/FR-2022-02-17/pdf/2022-01976.pdf.

[5] In the May Comment Letter, we explain the various reasons why the SEC's dealer regime is ill-suited to pooled investment vehicles. *See* pp. 9 to 11 (discussing, among other examples, Loss of Customer Protection, Loss of SEC and FINRA Sales Practice Protections, Loss of Liquidity Rights, Lost Access to the U.S. IPO Market, Lost Access to Certain Investment Strategies, and Increased Personnel and Infrastructure Costs).

[6] *See* IAWG, *Recent Disruptions and Potential Reforms in the U.S. Treasury Market: A Staff Progress Report* (Nov. 8, 2021), available at: https://home.treasury.gov/system/files/136/IAWG-Treasury-Report.pdf.

[7] *See, e.g.*, https://www.ft.com/content/3218c8b4-76bc-4690-9a17-1cfa52eeb0ac); https://www.wsj.com/articles/rocky-treasury-market-trading-rattles-wall-street-11667086782; https://www.bloomberg.com/opinion/articles/2022-10-14/fed-s-next-crisis-is-brewing-in-us-treasuries#xj4y7vzkg. *See also* IAWG, Enhancing the Resilience of the U.S. Treasury Market: 2022 Staff

Proposed Rules could create conditions in the U.S. Treasury markets that cause similar market stress to that which presented itself in the United Kingdom earlier this year, albeit on a larger scale.

The Commission should not proceed with this unnecessary proposal. However, if the Commission decides to do so, it should, at the very least, revise the Proposed Rules to mitigate the damage the rule, as drafted, will cause. To assist the Commission, in the Annex to this letter, we offer suggested changes to the Proposed Rules that generally reflect the positions set forth in our May Comment Letter and are intended to offer the Commission alternative approaches to address its policy concerns, as we understand them, while addressing some of the negative, unintended consequences of the Proposed Rules. These suggestions should not be read to imply that MFA or its members agree with the Commission's interpretation of the Exchange Act or that the Commission has authority to promulgate the Proposed Rules. We continue to believe that even with the suggested changes, the Proposed Rule are unnecessary, counterproductive, and unlawful.

* * *

MFA appreciates the opportunity to provide additional comments to the Commission on the Proposed Rules. We welcome the opportunity to discuss our views with you in greater detail. Please do not hesitate to contact Matthew Daigler, Vice President & Senior Counsel, or the undersigned, at (202) 730-2600, with any questions that you, your respective staffs, or the Commission staff might have regarding this letter.

Very truly yours,

/S/ Jennifer W. Han

Jennifer W. Han
Executive Vice President
Chief Counsel & Head of Global Regulatory Affairs

cc: The Hon. Gary Gensler, SEC Chairman
The Hon. Hester M. Peirce, SEC Commissioner
The Hon. Caroline A. Crenshaw, SEC Commissioner
The Hon. Mark T. Uyeda, SEC Commissioner
The Hon. Jaime Lizárraga, SEC Commissioner
Dr. Haoxiang Zhu, Director, Division of Trading and Markets
Dr. Jessica Wachter, Chief Economist and Director of the Division of Economic and Risk Analysis

Progress Report (Nov. 10, 2022), available at: https://home.treasury.gov/system/files/136/2022-IAWG-Treasury-Report.pdf.

**Annex**

Qualitative Tests

*Test 1*

~~Routinely making roughly comparable purchases and sales of the same or substantially similar securities in a day.~~

***Notes:***

- ***Qualitative Test 1 is inconsistent with the statutory definitions of "dealer" and "government securities dealer."***
- ***It also inappropriately departs from the Commission's own longstanding approach to determining dealer status, which has traditionally looked to whether a person facilitates customer trades, provides quotes, or otherwise holds oneself out as a market maker.***
- ***Contrary to the intended purpose, Qualitative Test 1 would encompass many customers engaged in normal course investing (not dealing) activity, including many private funds that do not engage in dealing activity.***
- ***It is particularly problematic given that many private funds operate multiple independent strategies in a given asset class. While each strategy may be directional, we struggle to see how a private fund could ensure that the aggregate exposure of independent strategies ends up directional on a "routine" basis (or how this could be monitored on an ex ante basis).***
- ***The Proposal states that routinely "means more frequent than occasional but not necessarily continuous." This standard is unclear, defined with reference to another undefined concept ("occasional") and distinguished from a concept ("continuous") that market participants actually understand and have experience applying.***
- ***The "roughly comparable" standard is unclear as drafted and will cause confusion for market participants. Indeed, determining whether this standard has been met will be just as uncertain for market participants as it was for the Commission in its economic analysis.***
- ***The "substantially similar" standard is fatally arbitrary and vague. Not only is the standard unclear, but the enumerated factors that are supposed to aid market participants in applying the standard would themselves require subjective determinations—for example, it is not always clear whether changes in the fair market value of one security are "reasonably expected" to approximate changes in the fair market value of another security.***

*Test 2*

> ~~Routinely~~ ~~expressing~~ ~~trading~~ ~~interests~~ Primarily expressing firm two-sided quotations on a continuous or near continuous basis that are at or near the best available prices on both sides of the market for the same security and that are communicated and represented by a person that holds itself out in a way that makes them accessible to other market participants; or

***Notes:***

- ***We question why merely expressing trading interests on both sides of the market and seeking to get the best price when doing so is indicative of dealing activity. Nearly any active investor or trader might engage in this activity just to get best execution, for example when using an order book protocol.***
- ***Unless this test is limited to continuous or near continuous quotations on both sides of the market for the same security, it will be extraordinarily overbroad. Accordingly, we have revised the rule text to refer to expressing "firm two-sided quotations on a continuous or near continuous basis."***
- ***As a technical change, we added "for the same security" to clarify that a person needs to be on both sides of the market for the same security, not just securities generally.***
- ***We added "by a person that holds itself out" to further refine the rule text so that it only captures entities that communicate firm quotes in a way that makes them accessible to other market participants as part of a regular business.***

*Test 3*

Earning ~~revenue~~ profits primarily from (a) capturing bid-ask spreads, by buying at the bid and selling at the offer, or (b) capturing any incentives offered by ~~trading venues~~ a national securities exchange or alternative trading system to liquidity-supplying trading interests; and

***Notes:***

- ***Qualitative Test 3 focuses on revenue earned by market participants, rather than profits, despite the fact that, in the Commission's view, dealers trade in a manner designed to profit from (and not merely earn revenue from) spreads or liquidity incentives.***
- ***We suggest textual changes to clarify that "primarily" applies to both parts of this prong.***
- ***We are concerned that the proposed breadth of the term "trading venue" could present implementation challenges to market participants. A more workable test that would capture the most significant trading activity and reduce the compliance burdens on market participants would be for the test to limit trading activity to the most liquid trading venues, including those where liquidity incentives are most likely to be offered and where trading to profit from the spread occurs most often.***

Quantitative Test

~~(2) In each of four out of the last six calendar months, engaged in buying and selling more than $25 billion of trading volume in government securities as defined in Section 3(a)(42)(A) (15 U.S.C. 78c(a)(42)(A)) of the Act;~~

***Notes:***

- ***The proposed $25 billion threshold is arbitrary. It also inappropriately departs from the Commission's own longstanding approach to determining dealer status, as it is not indicative of market-making (or even significant, relative to other firms) activity absent other activity.***
- ***In no instance has the Commission indicated that any single factor is determinative. There has never been a purely quantitative test for dealer or government securities dealer status.***
- ***While we believe that there is not a dollar threshold that would be appropriate with respect to defining a dealer, we note that the proposed $25 billion threshold is clearly inappropriate, because it represents a miniscule fraction of the average monthly transaction volume in the U.S. Treasury market.***
- ***Furthermore, the Commission has not adequately considered the consequences that the Quantitative Test could have on government securities markets. The bright-line threshold will inevitably decrease certain firms' participation in the Treasury market in order to avoid dealer status, may lead some to leave the Treasury market altogether, and may discourage new firms from entering the market. This could lead to further concentration in the market, decrease market resilience and stability, and lead to increased systemic risk.***

Common Control Provision

The proposed rule text in 3a44-2(b)(2), as revised, is set forth below:

(2) A person's "own account" means any account~~:~~

~~(i)~~ ~~H~~held in the name of that person.~~; or~~

~~(ii) Held in the name of a person over whom that person exercises control or with whom that person is under common control, provided that this paragraph (b)(2)(ii) does not include:~~

~~(A) An account in the name of a registered broker, dealer, or government securities dealer, or an investment company registered under the Investment Company Act of 1940; or~~

~~(B) With respect to an investment adviser registered under the Investment Advisers Act of 1940, an account held in the name of a client of the adviser unless the adviser controls the client as a result of the adviser's right to vote or direct the vote of voting securities of the client, the adviser's right to sell or direct the sale of voting securities of the client, or the adviser's capital contributions to or rights to amounts upon dissolution of the client; or~~

~~(C) With respect to any person, an account in the name of another person that is under common control with that person solely because both persons are clients of an investment adviser registered under the Investment Advisers Act of 1940 unless those accounts constitute a parallel account structure; or persons identified in paragraphs (b)(2)(i) and (ii) of this section.~~

~~(3) The term ''control'' has the same meaning as prescribed in § 240.13h–1 (Rule 13h–1), under the Act.~~

~~(4) The term ''parallel account structure'' means a structure in which one or more private funds (each a ''parallel fund''), accounts, or other pools of assets (each a ''parallel managed account'') managed by the same investment adviser pursue substantially the same investment objective and strategy and invest side by side in substantially the same positions as another parallel fund or parallel managed account.]~~

***Notes:***

- ***We generally question whether it is appropriate, in the context of the "dealer" and "government securities dealer" definitions, to adopt such broad aggregation rules. We are not aware of any judicial or agency precedent interpreting the phrase "own account" in any similar manner.***
- ***The Proposal appears to assume that all trading activity taking place within a single legal entity or commonly controlled group of legal entities takes place on an integrated and coordinated basis. However, it is quite common that a single entity (including a fund) or group of entities engage in trading through substantially (for all relevant purposes) independent portfolio managers.***

- ***For example, an investment adviser might delegate trading authority among multiple portfolio managers (sometimes separate sub-advisers, but sometimes part of the same investment adviser), who, in turn, trade independently of each other. If the trading activity of these independent portfolio managers were aggregated with each other, the aggregate appearance could be viewed, inappropriately, as being in the nature of market making as discussed above.***
- ***To avoid this issue, the Commission should adopt a definition of "person" that treats separate trading activity conducted by separate decision-makers without coordination of trading or cooperation among or between them. This treatment would be consistent with the treatment of truly separate accounts for other securities law purposes.***
- ***However, we understand the Commission's concerns about evasion. We believe the Commission can address such concerns through a more tailored measure. Specifically, the Proposal should be modified to require aggregation among commonly controlled entities solely in circumstances where such entities, acting together or at the direction of a person controlling them both, engage in coordinating trading activity, willfully structured to evade the rule.***