



March 14, 2011

Via Electronic Mail: pubcom@finra.org

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: FINRA Proposed Rule 5122; Private Placements of Securities

Dear Ms. Asquith:

Managed Funds Association (“MFA”)¹ appreciates the opportunity to provide comments in response to FINRA’s Notice-to-Members 11-04 (“Notice”) on proposed amendments to FINRA Rule 5122 to address member firm participation in private placements (the “Proposed Rule”).

Scope of Proposed Rule

The amendments proposed in the Notice expand FINRA Rule 5122 from covering private placements where a member firm (or its control entity) is the issuer to all private placements in which a member firm participates. MFA appreciates FINRA’s efforts to protect investors from abusive and fraudulent member private offerings. However, we are concerned that the Proposed Rule, as drafted, would frustrate the general public policy goals behind private placements and lead to unintended consequences. We believe the Proposed Rule should be drafted in a way that more narrowly targets FINRA’s specific concerns and does not make it more arduous for sophisticated investors to access and invest in private placements.

We do not believe that it is necessary for FINRA to regulate the substance of privately offered commodity pools and investment funds. Privately offered commodity pools and investment funds are offered pursuant to section 4 of the Securities Act of 1933 (“Securities Act”) and Regulation D thereunder.² Congress recognized in passing the federal securities laws that registration of a security is a long and expensive process, and that in some circumstances the costs of compliance with registration greatly exceeded any public benefit. Thus, Congress wrote

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 \$1.9 trillion invested in absolute return strategies. MFA is headquartered in Washington, D.C., with an office in New York.

² See Regulation D under the Securities Act of 1933; 17 CFR 230.501.

exemptions from the burdens of registration into the Securities Act as originally enacted in 1933. The Securities and Exchange Commission (“SEC”) also recognized in adopting Regulation D that sophisticated or “accredited investors” could sufficiently fend for themselves and adopted Regulation D with limited disclosure requirements.

Most recently, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). The Dodd-Frank Act mandates the registration of investment advisers to private funds,³ and raises the “accredited investor” standard.⁴ Nevertheless, it maintains the existing private placement regime.

Comments and Recommendations

We recognize that the Proposed Rule provides exemptions from the requirements of the Proposed Rule. In our view, the Proposed Rule should clarify that it does not apply to offerings pursuant to Section 3(c)(7) of the Investment Company Act of 1940 (the “Company Act”). We believe it makes sense to streamline the exemption to reflect the statutory provision in the Company Act, a well-developed area of law.

While the Proposed Rule exempts offerings sold solely to “qualified purchasers”, we are concerned that it may not capture or consider other persons who may invest in an investment fund exempt from being an investment company under Section 3(c)(7) of the Company Act (a “3(c)(7) Fund”). For example, Section 3(c)(7) of the Company Act also covers persons who receive shares in a 3(c)(7) Fund as a gift or bequest from a qualified purchaser who owned the 3(c)(7) Fund shares,⁵ as well as non-U.S. persons in an offshore transaction.⁶ Moreover, Section 3(c)(7) of the Company Act is a well-developed area of law with established caselaw and no-action letters. For regulatory consistency, we believe FINRA’s exemption in the Proposed Rule should clarify that it exempts offerings sold pursuant to Section 3(c)(7) of the Company Act. Accordingly, we recommend that the Proposed Rule exempt offerings sold pursuant to Section 3(c)(7) of the Company Act.

In addition, we believe that the Proposed Rule should not apply to private investment funds, such as hedge funds that are exempt under Section 3(c)(1) of the Company Act (“3(c)(1) Funds”). The Dodd-Frank Act raised the “accredited investor” standard by adjusting the net worth standard for an accredited investor “so that the individual net worth of any natural person, or joint net worth with the spouse of that person, at the time of purchase, is more than \$1,000,000 (as such amount is adjusted periodically by rule of the Commission), excluding the value of the primary residence of such natural person”⁷ MFA favors raising the accredited investor

³ See Section 403 of the Dodd-Frank Act.

⁴ See Section 413 of the Dodd-Frank Act.

⁵ See Section 3(c)(7) of the Company Act.

⁶ See Rule 902(h) of Regulation S under the Securities Act of 1933; 17 CFR 230.901.

⁷ See Section 413 of the Dodd-Frank Act.

standard and supports the SEC's proposed rule on the "Net Worth Standard for Accredited Investors".⁸ The Dodd-Frank Act amendment to the definition of accredited investor will safeguard that only sophisticated investors are invested in such funds. Furthermore, as a result of the elimination of the private adviser exemption under the Dodd-Frank Act,⁹ the advisers of 3(c)(1) Funds and 3(c)(7) Funds (together "Private funds") will generally be overseen by the SEC and subject to examination. Privately offered commodity pools that are Private Funds are already well regulated by the Commodity Futures Trading Commission ("CFTC") and the National Futures Association ("NFA").¹⁰ Additional regulation by FINRA of these entities would be duplicative.

While we do not believe it is necessary or appropriate for FINRA to regulate the substance of private placements, FINRA, at a minimum, should exempt from the Proposed Rule offerings sold pursuant to Section 3(c)(1) of the Company Act where the adviser is registered with the SEC or CFTC/NFA. Accordingly, we recommend that the Proposed Rule exempt offerings sold pursuant to Section 3(c)(1) of the Company Act where the adviser is registered with the SEC or CFTC/NFA.

* * * * *

MFA appreciates the opportunity to provide comments on the Proposed Rule, and would be pleased to meet with FINRA staff to discuss our comments further. Please do not hesitate to contact Jennifer Han or the undersigned at (202) 730-2600 with any questions you may have regarding this letter.

Respectfully submitted,

/s/ Stuart J. Kaswell

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

⁸ See letter from Richard H. Baker, President and CEO, MFA to Elizabeth M. Murphy, Secretary, SEC, dated March 11, 2011, available at: <http://www.managedfunds.org/files/MFA.Letter.on.Accredited.Investor.pdf>.

⁹ See Section 403 of the Dodd-Frank Act.

¹⁰ See Part 4 of the CFTC Regulations.