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COMMENT

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MANAGED FUNDS ASSOCIATION

OFFICE OF THE SECRETARY

*The Association for investment professionals in futures, hedge funds and other alternative investments.*

August 18, 1998

COMMODITY FUTURES  
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By facsimile and E-mail

Ms. Jean A. Webb  
Secretary  
Commodity Futures Trading Commission  
1155 21<sup>st</sup> Street, N.W.  
Washington, DC 20581

Re: Recordkeeping

Dear Ms. Webb:

Managed Funds Association ("MFA") appreciates the opportunity to provide comments in response to the Notice of Proposed Rulemaking (the "Release"), 63 Fed. Reg. 30668 (June 5, 1998) by the Commodity Futures Trading Commission (the "Commission") which would amend the Commission's current recordkeeping requirements as contained in its Regulation 1.31. The Commission's objective is to expand the category of records which may be retained electronically and to eliminate the requirement for certain records that they be retained in hard copy for two years.

MFA is a national trade association of almost 700 members. MFA's membership is made up of a diverse group of alternative investment professionals, including hedge fund and commodity trading managers, commodity pool operators and fund of funds managers. These fund managers are responsible for a significant portion of the nearly \$250 billion invested in hedge funds and the vast majority of the over \$35 billion invested in managed futures funds. MFA members also include brokers, exchanges, cash managers, foreign exchange dealers, banks and other professionals who provide support services such as accountants, lawyers, consultants and academics. Accordingly, MFA and its members have a vital interest in the proposed rule changes set forth in the Release.

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MFA has worked closely with the Commission in obtaining relief to permit its CPO and CTA members to distribute required disclosure information electronically to their clients.<sup>1</sup> MFA commends the Commission's ongoing efforts to amend its rules to facilitate the use of electronic media by its registrants. Authority to distribute and to satisfy disclosure obligations electronically, however, can not be fully utilized if the Commission's rules do not permit and facilitate storage of such records in the same media for purposes of compliance with the Commission's recordkeeping requirements. Accordingly, in each of these advisories and interpretations, the Commission acknowledged the need to amend its existing regulations and permitted registrants to maintain records created pursuant to such advisories and interpretations in the manner currently permitted by the Securities and Exchange Commission's (the "SEC") record retention rules. In general, the SEC standards have worked well.

MFA is fully supportive of the Commission's current focus to provide a long term cohesive solution that will facilitate use of electronic recordkeeping systems and maximize the cost-reduction and time-savings arising from its use while not only maintaining, but in many cases, enhancing the safety, integrity and security of retained records. As is apparent from the existing regulations which are technology-specific, a technology standard enunciated today will simply be outdated tomorrow. Accordingly, specifications relating to specific storage media should be eliminated in favor of performance standards necessary for the integrity of the records kept or for Commission accessibility to such records.

In this regard, we believe it is essential that the Commission's proposed rule be amended to make electronic storage a feasible, not just a permissible, option for all records required to be retained and for the entire period record retention is required, without specific limitation of the storage media; *provided*, the registrant can ensure that the retained record can meet the appropriate performance standard. Because technology has advanced, and continues to advance, so rapidly in this field, Commission adoption of performance standards which

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<sup>1</sup> See *Electronic Filing of Disclosure Documents With the Commission*, 62 Fed. Reg. 18265 (April 15, 1997) in which the CFTC adopted a program permitting CPOs and CTAs to file required disclosure documents with the CFTC electronically. See *Advisory: Alternative Method of Compliance*, 62 Fed. Reg. 31507 (June 10, 1997) permitting FCMS, with customer consent, to deliver confirmation, purchase and sale and monthly statements to clients by electronic media. See *Interpretation Regarding Use of Electronic Media by Commodity Pool Operators and Commodity Trading Advisors for Delivery of Disclosure Documents and Other Materials*, 62 Fed. Reg. 39104 (July 22, 1997), permitting CPOs and CTAs to deliver required disclosure documents to clients electronically.



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protect the security and integrity of the records and the Commission's access to them, rather than adoption of rules specifying the type of technology that must be used to meet the standards provides the necessary flexibility for registrants to utilize the most efficient form of record retention. This enhanced efficiency should shorten the timeframe and lower the cost for production of documents and permit production of documents in a more useable and multiple use format which should also enhance the Commission's ability to choose selectively from voluminous documents, lowering the Commission's cost of oversight, investigation and enforcement.

### **Differing Regulatory Treatment for Handwritten and Electronic Order Tickets and Trading Cards**

MFA believes the efficacy of the proposed regulatory changes would be diminished if the Commission adopts rules for different types of records, such as order tickets and trading cards. It is not efficient, and does not seem rational, to apply two different record retention requirements (and systems): one applicable to orders and trading cards that have originated as handwritten and the other applicable to electronically generated orders and trading cards and all other documents required to be retained by the registrant. The significant cost entailed in implementing a bifurcated record retention process would probably not be justified for most firms. In addition, such a rule could significantly add to the cost of retention and increase the possibilities of errors, loss of records and opportunities for record tampering by segregating certain records from the system applicable to the majority of the records required to be retained. For records that originate as handwritten documents, the current state of technology with enhanced image quality and security of electronic formats and the far greater accessibility and lower costs that may be achieved with electronic storage of information more than outweigh the possibility of manual alteration of records prior to their electronic storage. Further, MFA believes the latter risk is just as great with respect to documents stored as hard copy as those stored electronically.

Pursuant to the Commission's 1997 Advisories and Interpretations noted above, the Commission has permitted registrants who have prepared or distributed documents electronically over the past 14 months, to retain such records electronically in accordance with the record retention requirements adopted by the SEC. We believe these rules provide a good model for the current rulemaking. To the extent the Commission now adopts more onerous or more restrictive record keeping requirements, such as segregating handwritten order tickets and trading cards, registrants who have developed systems and procedures in the interim in reliance on that relief will be detrimented. For MFA members who are not only registrants of



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the Commission and thus required to comply with the Commission's final rules but also registrants of the SEC, to the extent the Commission's final rules are inconsistent with SEC requirements, there will be increased costs to comply with both sets of criteria.

### Conversion to "Approved Machine Readable" Format

For registrants who store their records electronically, the Commission's proposed rules require not only that such records be able to be downloaded and preserved onto an acceptable storage media, but also that the registrants be ready at all times, at the registrant's expense, upon request, to have available facilities allowing for: (i) immediate, easily readable projection or production of electronic storage media images, (ii) easily readable hard-copies of the records, and (iii) "copies on compatible machine-readable media approved by the Commission" in a format and coding structure specified in the Commission's request made at the time the records are to be reproduced. It is unclear why electronic records should be singled out from the identified media by requiring that such records be capable of being "translated" at least two other different ways, neither of which may be particularly compatible with the original electronically created and delivered transmission. This requirement may be especially impracticable if the Commission is not required to specify the format and coding structure prior to the date of the request. In addition to being costly and difficult, in the case of transmissions originally designed and delivered electronically, these differing requirements may produce a fairly unsatisfactory 'translation'. Embedded images can be retained but do not necessarily reproduce identically, (although materially the same) depending upon the viewer through which the information is viewed. In its proposed interpretation of the use of electronic media by CPOs and CTAs dated August 14, 1996, the Commission noted the impracticability of a requirement that electronic images be stored in ASCII because such images are normally not written in ASCII format<sup>2</sup>, yet the Commission indicates in footnote 16 of its Release that, upon request, registrants must provide copies of records retained on electronic storage media in a format and coding structure (e.g., ASCII) specified by the Commission in its request. If the registrant has retained the facilities (such as viewers, etc.) through which the images can be reproduced and accessed by the Commission, the registrant should not also be

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<sup>2</sup> The Release states "that the Commission's current rules for recordkeeping permit storage of computer generated records in ASCII or EBCDIC format only and that these formats generally do not allow storage of paper records or electronic images, such as webpages, since such records or images are not normally written in ASCII or EBCDIC format. Therefore, these records would be required to be retained in hardcopy form." See Interpretation Regarding Use of Electronic Media by Commodity Pool Operators and Commodity Trading Advisors, 61 Fed. Reg. 42146 (August 14, 1996).



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required to produce such record in a Commission specified machine-readable format, especially where the Commission-specified format and structure may be incompatible or not capable of displaying the images as transmitted. Accordingly, we believe the requirements of proposed §1.31(b)(2)(ii) and (b)(3)(i) should be alternative rather than both mandatory and also believe these requirements should pertain only to such records during the period in which they are required to be readily accessible.

Thank you again for the opportunity to comment on the proposed amendments to Regulation 1.31. If you have any questions regarding the foregoing, or wish to discuss our letter in greater detail, please do not hesitate to contact us.

Sincerely yours,



John G. Gaine  
President

