AlphaSimplex Group comments on proposed SEC derivatives rule

On March 28, 2016, AlphaSimplex Group, LLC ("AlphaSimplex") submitted a comment letter on the Securities and Exchange Commission's (the "Commission") Release No. IC-31933 on the Use of Derivatives by Registered Investment Companies and Business Development Companies (the "Release").

We applaud the Commission on the thoroughness of the Release and the clarity with which it was written. We also support the goal of having a single source of guidance for the use of derivatives by mutual funds. We support the aspects of proposed rule 18f-4 (the "Proposed Rule") that would require a formalized, board-approved derivatives risk management program, the designation of and reporting to the board by a derivatives risk officer, and the maintenance and daily monitoring of qualifying coverage assets.

However, we also believe the Proposed Rule, as drafted, has unintended adverse consequences and that there are alternate approaches that would better protect investors and achieve the Commission's objectives. In our comment letter, we focused on three key points:

1) The potential for the Proposed Rule to increase, rather than decrease, risk to investors;
2) The inability of the Proposed Rule to properly protect investors because it does not take into account the risk of different derivative instruments; and
3) The consequences of eliminating retail investor access to managed futures and similar liquid alternative funds that help investors manage their portfolio risk.

In conclusion, AlphaSimplex supports the Commission's objectives and many of the aspects of the Proposed Rule. However, we are concerned that, without adjustment, the strict gross notional-based portfolio limit will lead to unintended adverse consequences and deprive retail investors of important tools to help manage overall portfolio risk. A gross notional test is simply not the most effective way to achieve the Commission's objectives. Modifying the Proposed Rule to implement a risk-based approach and limit a fund's derivative risk-adjusted notional exposure to 150% of a fund's NAV plus the percentage of cash and cash equivalents in the portfolio would treat all funds equally and reduce the potential for unintended consequences.

Our full comment letter can be found at the following link to the SEC website:
https://www.sec.gov/comments/s7-24-15/s72415-138.pdf

Now that the official comment period is closed, the Commission will read and evaluate all the comment letters. The Commission can then take several actions, including drafting a final rule for adoption (which may or may not include significant changes to the Proposed Rule), re-opening the comment period, issuing a new proposed rule, or withdrawing the Proposed Rule altogether. Once a final rule is adopted, it is not uncommon for the rule to contain a delayed adoption date to allow for a smooth transition into the new rule. Given the complexity of the Proposed Rule and the number of comments, we do not expect a final rule to be fully effective (i.e., implemented) before mid-2017, **so there is no immediate or short term impact on any fund.**