DUCKWORTH CAPITAL MANAGEMENT, INC.

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July 15, 2009

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20459-1090

Re: Amendments to Custody Rule; File Number S7-09-09

Dear Ms. Murphy:

Thank you for the opportunity to comment on the Securities and Exchange Commission's ("Commission" or the "SEC") proposed amendments to Rule 206(4)-2 of the Advisers Act ("Custody Rule"). Duckworth Capital Management, Inc. is a small investment adviser registered with the State of Nevada and we currently provide investment management services to a single limited partnership client ("Hedge Fund"). Because we are under common control with the Hedge Fund's general partner, we are deemed to have custody of the Hedge Fund's assets and are therefore required to comply with the Custody Rule under Nevada law. The Hedge Fund's assets are held at a third-party custodian and we comply with the Custody Rule by having the custodian deliver quarterly account statements directly to each limited partner of the Hedge Fund.

<u>Proposed Amendments</u>

In our opinion, the Commission's proposed amendments to the Custody Rule would impose significant costs on advisers to hedge funds and/or limited partners of hedge funds without providing any significant benefit in reducing potential fraud.

Quarterly Statements from Custodian. In our case, an annual surprise audit will not provide any value to the limited partners of the Hedge Fund. They already receive a statement of the Hedge Fund's account directly from the fund's custodian every quarter. It is unclear what new information an auditor conducting a surprise inspection is going to provide to the limited partners. Is the auditor going to confirm the existence of the assets held at the custodian? Through the quarterly statements sent directly by the custodian, the limited partners are able to verify those facts *four* times per year at an annual cost to the fund of $280.[1] It is not clear what benefit the limited partners would receive for the $8,000 they would pay every year for a surprise audit.[2]

[1] The Hedge Fund's custodian charges an aggregate $280 per year ($20 per limited partner) to mail the quarterly account statement to each limited partner. There are currently fourteen limited partners.

[2] The partnership agreement would allow the surprise audit expense to be charged as a partnership expense.

Annual Audited Financial Statements. For hedge funds that comply with the Custody Rule by distributing audited financial statements to the limited partners, the Commission's proposed amendments to the Custody Rule lack practical value. Although the audit of a hedge fund is performed on a test basis overall, the auditors confirm *every* asset on the balance sheet of the fund as a practical matter. There are two reasons why: First, the largest malpractice exposure for an audit firm is a balance sheet that presents nonexistent assets. Second, Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" (FAS 157) requires a categorization of the fund's portfolio assets into Level 1, 2 or 3 based on each asset's valuation assumptions. As a result, the auditors scrutinize the valuation assumptions behind all securities presented on the balance sheet in addition to verifying the existence of the securities. A surprise audit - which requires confirmation of every asset – is simply going to duplicate what the fund's auditors have done as a practical matter in auditing the financial statements.

Alternative Approach

In our opinion, the SEC can develop a more effective Custody Rule. There are essentially two sources of hedge fund fraud: (1) related party custodians and (2) related party/unscrupulous fund auditors.

Instead of implementing the Commission's proposed changes, we recommend making two changes to the existing Custody Rule. First, prohibit investment advisers from using related-party custodians and require a third-party custodian. This would help prevent future Madoff frauds.[3]

Second, modify Rule 206(4)-2(b)(3) to require any hedge fund relying on the annual audited financials exception to the Custody Rule to use an auditor registered with the Public Company Accounting Oversight Board (PCAOB). Requiring a PCAOB registered auditor would help prevent future Bayou Management frauds where related-party or questionable fund auditors are used.[4]

[3] *See* SEC v. Bernard L. Madoff, et al., Litigation Release No. 20889 (Feb. 9, 2009) (where the heart of the fraud appears to be the dual role of Bernard L. Madoff Investment Securities LLC serving as investment adviser and custodian of client assets).

[4] *See* SEC v. Samuel Israel III; Daniel E. Marino; Bayou Management, LLC, et al., Litigation Release No. 19406 (Sep. 29, 2005) (where it was alleged that a sham accounting firm was created to fabricate annual "independent" audits of the funds).

Conclusion

The majority of investment advisers, including our firm, operate by having a third-party custodian distribute quarterly account statements directly to the client. Such advisers also typically debit the client's account for management fees in arrears.

The recent frauds have not involved these types of investment advisers. The Commission's approach in requiring *all* investment advisers with custody to undergo an annual audit is an inefficient solution to the problem and the client is ultimately going to pay for that inefficiency as the additional audit costs are passed along. That is not good policy. Instead, the Commission should focus on the sources of the recent frauds and make changes to the Custody Rule to address them. We hope that you will consider our proposals outlined above.

If you would like to discuss any of the above details, please feel free to give me a call at (775) 831-1048.

Sincerely yours,

Russel B. Duckworth, CFA
President