

Investment Advisers Act of 1940 -- Section 206 -- Rule 206(4)-1, 204-2(A)(16)

September 13, 1996

Horizon Asset Management, LLC

TOTAL NUMBER OF LETTERS: 2

**SEC-REPLY-1:
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

September 13, 1996

**Our Ref. No. 96-309
Horizon Asset Management, LLC
File No. 801-50502**

**RESPONSE OF THE OFFICE OF CHIEF COUNSEL
DIVISION OF INVESTMENT MANAGEMENT**

Your letter of June 3, 1996 requests our assurance that we would not recommend enforcement action to the Commission under section 206 of the Investment Advisers Act of 1940 (the "Advisers Act") or rule 206(4)-1 thereunder if Horizon Asset Management, LLC ("Horizon"), a registered investment adviser, includes in its advertisements performance data reflecting the performance achieved by an investment adviser previously owned and operated by one of Horizon's managers.

You state that Horizon will manage accounts using a three-person advisory committee. You represent that one of the members of the committee (the "Controlling Manager") will make all investment decisions with respect to Horizon's accounts, and that the other committee members will only advise the Controlling Manager prior to his making these decisions. You state that, notwithstanding the other committee members, the Controlling Manager will have final decision-making authority over the investment portfolios.

The Controlling Manager previously owned and operated another registered investment adviser (the "Predecessor Firm"). You represent that the Controlling Manager was principally responsible for all investment decisions made by that firm. Horizon proposes to advertise the composite performance of all the Predecessor Firm's accounts that had the same investment objectives and were managed using the same investment strategies as accounts that Horizon will manage. You represent that Horizon will make appropriate disclosures to potential clients, including disclosure relating to the source of the results, and that Horizon will keep those books and records of the Predecessor Firm that are necessary to substantiate the performance results, in accordance with rule 204-2(a)(16) under the Advisers Act. n1

Section 206(4) of the Advisers Act prohibits an investment adviser from engaging in any act, practice, or course of business that the Commission, by rule, defines as fraudulent, deceptive, or manipulative. Rule 206(4)-1(a)(5) under the Advisers Act provides that it is a fraudulent, deceptive or manipulative act for any investment adviser to distribute, directly or indirectly, any advertisement that contains any untrue statement of material fact or that is otherwise false or misleading.

The staff takes the position that an investment adviser advertisement that includes prior performance results of accounts managed by a predecessor entity would not, in and of itself, be misleading under rule 206(4)-1(a)(5) provided that (1) (the person or persons who manage accounts at the adviser were also those primarily responsible for achieving the prior performance results, n2 (2) the accounts managed at the predecessor entity are so similar to the accounts

currently under management that the performance results would provide relevant information to prospective clients, (3) all accounts that were managed in a substantially similar manner are advertised unless the exclusion of any such account would not result in materially higher performance, n3 (4) the advertisement is consistent with staff interpretations with respect to the advertisement of performance results, n4 and (5) the advertisement includes all relevant disclosures, including that the performance results were from accounts managed at another entity.

The primary issue raised by your request relates to the first factor noted above: whether Horizon may use the Predecessor Firm's performance results notwithstanding that the Controlling Manager is part of an advisory committee at Horizon. You assert that, even though the Controlling Manager will be a member of Horizon's advisory committee, Horizon's use of the Predecessor Firm's performance results would not be misleading because the same person who was principally responsible for investment decisions at the Predecessor Firm also will be principally responsible for such decisions at Horizon.

The staff has taken the position that it may be misleading for an adviser to advertise the performance results of accounts managed at an employee's prior place of employment when the employee had been one of several persons responsible for selecting the Securities for those accounts. n5 Conversely, it may be misleading for an employee's new firm to use the performance results of an account he previously managed if at the new firm the manager is one of several persons responsible for managing accounts. In this case, however, the fact that the Controlling Manager will be a member of an advisory committee does not necessarily mean that including the Predecessor Firm's performance results in an advertisement would be misleading, if the Controlling Manager is the person actually responsible for making the investment decisions, and those decisions need not be made with the consensus of the other members of the committee.

Accordingly, based on the facts and representations set forth in your letter and described above, we would not recommend enforcement action to the Commission under section 206 of the Advisers Act or rule 206(4)-1 thereunder if Horizon includes performance data of the Predecessor Firm in its advertisements, provided that the advertisements are not otherwise false or misleading. Because this response is based on the facts and representations in your letter, you should note that any different facts or representations might lead to a different conclusion.

Rochelle Kauffman Plesset
Senior Counsel

Footnotes

n1 Telephone conversation of August 14, 1996 between Rochelle Kauffman Plesset and Robert J. Ahrenholz, counsel to Horizon. Rule 204-2(a)(16) generally requires an investment adviser to keep all documents that are necessary to form the basis for or demonstrate the calculation of the performance or rate of return of managed accounts that is included in advertisements. This requirement also applies to the use by an investment adviser of a predecessor's performance data. Great Lakes Advisors (pub. avail. Apr. 3, 1992).

n2 See, e.g., Bramwell Growth Fund (pub. avail. Aug. 7, 1996); Conway Asset Management, Inc. (pub. avail. Jan. 27, 1989).

n3 The staff previously had taken the position that it may not be misleading to exclude the performance of accounts if the performance results of the omitted accounts are not materially different from the results of the accounts that are to be advertised. E.g., Conway Asset Management, Inc. The staff is clarifying this position in light of a letter issued recently to an adviser that wished to use performance that reflected the deduction of a model fee when the resulting performance figures would be no higher than those that would have resulted had actual fees been deducted. See J.P. Morgan Investment Management, Inc. (pub. avail. May 7, 1996).

n4 See, e.g., Clover Capital Management, Inc. (pub. avail. Oct. 28, 1986).

n5 Great Lakes Advisors, Inc.

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Investment Advisers Act of 1940 -- Section 206(4) -- Rule 206(4)-1, 204-2(A)(16)

June 3, 1996

**Securities and Exchange Commission
Division of Investment Management
Office of Chief Counsel
450 Fifth Street, N.W.
Washington, D.C. 20549**

Attention: Rochelle Kauffman Plesset, Esq. Re: Horizon Asset Management, LLC

Ladies and Gentlemen:

We are counsel to Horizon Asset Management, LLC ("Horizon") which has recently registered as an Investment Adviser under the Investment Advisers Act of 1940 ("the Act"). Horizon has requested that we obtain the advice of the staff (the "Staff") of the Securities and Exchange Commission (the "Commission") as to whether the Staff will recommend the Commission take any enforcement action under the Act, particularly Section 206 and Rule 206(4)-1 promulgated thereunder, against Horizon by virtue of its use of performance data from an investment adviser previously owned and operated by one of Horizon's managers, as described below. This letter supersedes and replaces our letter to you dated May 7, 1996 concerning this matter.

Background

Horizon was formed as a limited liability company under Colorado law on April 30, 1996. Horizon's application on Form ADV with the Commission was effective May 20, 1996. It is proposed that an advisory committee (the "Committee") for Horizon will consist of three persons. One of the members of the Committee (the "Controlling Manager") will be solely responsible for all investment decisions of the Committee. The other two members of the Committee will have various responsibilities with respect to Horizon, including providing advice to the Controlling Manager with regard to portfolio management. The Controlling Manager will have final decision making authority and the ability to manage investment portfolios notwithstanding any advice provided by the other members of the Committee.

The Controlling Manager previously owned and operated an investment adviser (the "Predecessor Firm") unaffiliated with Horizon. While employed by the Predecessor Firm, the Controlling Manager was substantially responsible for all investment decisions made by that firm. The Controlling Manager, through the responsibilities described above, will be in substantially the same position while employed by Horizon. Horizon will use the same investment strategies and has the same investment objectives as the Predecessor Firm.

Horizon proposes to include the investment performance results of the Predecessor Firm in connection with certain of its advertisements. In regard to such use, Horizon will make appropriate disclosure to potential investors under the Act as to the source of such results.

Analysis

The Staff has previously taken the position that under various circumstances the performance results of a prior firm may be provided to prospective clients of a subsequent investment adviser. Taurus Advisory Group, Inc. (pub. avail. July 15, 1993); Conway Asset Management (pub. avail. January 27, 1989) ("Conway"); Growth Stock Outlook Trust, Inc. (pub. avail. April 15, 1986). In Conway, the Staff took the position that the use of prior performance results of a predecessor advisor by a subsequent investment adviser would not be misleading if: 1) no individual or entity other than the individual at issue played a significant part in the performance of the previous investment adviser's accounts and 2) the results of the accounts to be advertised were not materially different from the results of those accounts which did not become part of the subsequent adviser.

Although there was no controlling manager situation in Conway, the relevant circumstances of Horizon are substantially identical to those presented in Conway. No individual other than the Controlling Manager played a significant part in the performance of Predecessor Firm's accounts and, by virtue of the responsibilities described above, the Controlling Manager will control investment decisions made by Horizon. Further, Horizon does not seek to advertise results of prior accounts which are materially different from those to be advertised.

We do not believe that the analysis in Great Lakes Advisors, Inc. (pub avail. April 3, 1992) is applicable since in that case the investment decisions of the predecessor advisor were made by a committee of three or four persons where the person changing positions did not have the power on such committee that the Controlling Manager will have on Horizon's Committee.

It is our opinion that, to the extent Horizon uses an "advertisement" (as defined in Rule 206(4)-1(b)) in connection with providing the past performance results of the Predecessor Firm, such information would not, in and of itself, be false or misleading under Rule 206(4)-1(a)(5). Because the past performance results are based on the Controlling Manager's efforts and the Controlling Manager will continue those efforts at Horizon, clients of Horizon will not be misled by having the past performance results available. In this regard, because the Controlling Manager owned the Predecessor Firm the Controlling Manager will have access to the necessary books and records to ensure the accuracy of the past performance results.

Request for Advice

Under the circumstances described above, we request advice from the Staff on behalf of Horizon whether enforcement action would be recommended to the Commission under the Act if Horizon were to advertise performance results of the Predecessor Firm.

If you have any questions or comments, please do not hesitate to contact the undersigned.

Sincerely yours,

Robert J. Ahrenholz