RICHARD J. SHAKER

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SEC LETTER

Advisers Act Secs. 203(b); 206

July 1, 1977

Richard J. Shaker
10614 Fable Row
Columbia, Maryland 21044

Dear Mr. Shaker:

In response to your letter received by the Commission on April 18, 1977, we wish to make clear that under the Investment Advisers Act of 1940 ('Act'), no investment adviser, unless exempted from registration pursuant to Section 203(b) of the Act, may, by use of the mails or of any means or instrumentality of interstate Commerce, effect or perform any investment advisory contract if such contract provides for compensation to the investment adviser on the basis of a share of capital gains upon or capital appreciation of the funds or any portion of the funds of a client.

Under Section 203(b), besides exemptions for advisers whose only clients are insurance companies and advisers who do not give advice with respect to securities listed or admitted to unlisted trading privileges on any national securities exchange and whose clients all reside in the State within which the adviser maintains his principal office and place of business, there is an exemption for any investment adviser who during the course of the preceding twelve months has had fewer than fifteen clients and who neither holds himself out generally to the public as an investment adviser nor acts as an investment adviser to any investment company registered under the Investment Company Act of 1940.

Though an adviser manages the assets of fewer than fifteen limited partnerships he may not be entitled to the latter exemption if there are fifteen or more members of such partnerships and if it would be appropriate under all the facts to consider the members of the partnerships his clients for the purposes of determining whether the exemption is available. Nor would the exemption be available to a person who gives advice to fifteen or more clients through corporations or other entities each of which has less than fifteen clients.

Even if an investment adviser has fewer than fifteen clients, he is not entitled to the exemption if he holds himself out generally to the public as an investment adviser. A person who writes letters or makes calls to friends and relatives informing them that he is available for investment advisory work may be deemed to be holding himself out to the public as an investment adviser as may a person who maintains a listing in the telephone directory or on a building directory as an investment adviser or who uses that term on his stationary.

An adviser who is not exempt from registration and is, therefore, subject to the prohibition against fees based on capital gains, cannot escape the prohibition by not registering under the Act. The prohibition applies to him whether he registers under the Act or not.

Even if an adviser is exempt from registering under the Act, the anti-fraud provision of the Act and the rules thereunder would still be applicable. I am enclosing a copy of a recent letter which contains some general remarks on the applicability of the anti-fraud section and rules to the use of performance figures in presentations to clients or prospective clients.

It is not clear from the facts presented in your letter whether the interests in the limited partnerships you propose to manage would be offered to the public and, thus, be required to be registered under the Securities Act of 1933, and whether the partnerships themselves would be investment companies required to be registered under the Investment Company Act of 1940.

In view of the problems and questions presented by your proposal, you should consider seeking the advice of competent counsel.

Sincerely,

Stanley B. Judd
Assistant Chief Counsel

INCOMING LETTER

April 16, 1977

Securities and Exchange Commission
Washington, D.C.

Gentlemen:

I am planning to manage some limited partnerships and, in at least some cases, charge a fee based on profit. I understand that I cannot register with the S.E.C. if I wish to charge a fee of this sort and that I am then precluded from advertising and representing myself to the general public as a securities account advisor. I have some questions regarding these points, and I hope that, like the Internal Revenue Service, you are willing to answer these questions. My volume is too small, and my fee structure too low, to be able to afford to consult a securities lawyer.

(1) May I mention to relatives and friends that I am forming such partnerships? May write letters to them announcing this? May I write a prospectus describing the goals of the partnership to show them? After the partnerships have been operating, may I quote their performance? Does your agency review such a prospectus even if an advisor cannot be registered with you since he is charging a performance fee?

(2) May I form a corporation and register the corporation with the S.E.C. as a registered investment advisor and continue to manage my performance fee partnerships under my personal name?

(3) Is there someone in your employ who would be willing to discuss with me these and related questions?

I would appreciate a written reply and, if possible, some indication of the answers to the questions above. I can be reached at home during the evening (301–730–1760) and I would be willing to visit you and meet with anyone whom you designate: however, I would hope that these questions could be answered through correspondence.

Sincerely yours,

Richard J. Shaker