

DEPARTMENT OF CORPORATIONS*Business Services and Consumer and Investor Protection*

Preston DuFauchard
California Corporations Commissioner
San Francisco, California

IN REPLY REFER TO:
FILE NO: OP 7132

COMMISSIONER'S OPINION 10/1 C

THIS INTERPRETIVE OPINION IS ISSUED BY THE CALIFORNIA CORPORATIONS COMMISSIONER PURSUANT TO CORPORATIONS CODE SECTION 25618 OF THE CORPORATE SECURITIES LAW OF 1968. IT IS APPLICABLE ONLY TO THE TRANSACTION IDENTIFIED IN THIS OPINION REQUEST, AND MAY NOT BE RELIED UPON IN CONNECTION WITH ANY OTHER TRANSACTION.

Mr. Lawrence S. Leibowitz
Lehman & Eilen, LLP
50 Charles Lindbergh Blvd.
Uniondale, New York 11553-3612

Dear Mr. Leibowitz:

Your request for an interpretive opinion dated June 3, 2010, has been considered by the California Corporations Commissioner. Your letter raises the question whether your client, the general partner of a limited partnership, must register as an investment adviser, under the circumstances described in your letter. We hereby grant your request for an interpretive opinion, and we concur that the general partner of a limited partnership need not register as an investment adviser under the limited circumstances, and subject to the conditions, described in your letter, as set forth below.

BACKGROUND

You represent that your client, Anvik Advisers LLC ("Advisers") is registered in the State of New Jersey as an investment adviser, and has also applied for a certificate with the Department of Corporations ("Department") as an investment adviser under Section 25230 of the Corporate Securities Law of 1968, as amended ("CSL," Corporations Code Section 25000 et seq.). Advisers intends to provide investment advisory services to an investment partnership, Anvik Capital Partners LP (the "Fund"), which is organized as a limited partnership. Investors are limited partners of the fund. Anvik GP LLC ("GP") is the general partner of the fund. Advisers and GP have common ownership.

In addition, you represent that GP handles the business and administrative aspects of the Fund, and designates the investment adviser to the Fund, but does not itself manage the Fund's investments. Advisers, as the investment adviser to the Fund,

manages the Fund's investments and receives a management fee equal to one and one quarter percent (1.25%) per annum ("management fee"), based upon the value of the Fund's assets as of the close of the business of the previous quarter. You also represent that GP receives an annual fee equal to twenty percent of the net profits ("performance fee" or "performance allocation") allocated to the limited partners of the Fund, subject to specified limitations.

You represent that any individual engaged in the activities of an investment adviser representative on behalf of the Fund, including any solicitation activities, will be registered as Advisers' representatives. You further represent that any such individual performing these functions through GP will be registered as Advisers' representative, and that all such individuals will be subject to the supervision and oversight of Advisers, regardless of whether their direct employment is through Advisers or GP.

LEGAL ISSUE

Advisers and GP request the Department's concurrence that GP is not required to obtain a certificate as an investment adviser, notwithstanding GP's receipt of compensation based on a share of capital gains of the fund.

CSL LICENSING AND REPORTING REQUIREMENTS

Section 25230 of the CSL provides that it is unlawful for any investment adviser to conduct business in this state unless the investment has secured from the Commissioner a certificate authorizing it to do so, unless the investment adviser is registered under the Investment Advisers Act of 1940 (15 USCA §§ 80b-1 et seq.). Under Section 25009 of the CSL, the term "investment adviser" is defined to mean, in part:

"Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing or selling securities, or who, for compensation and as a part of a regular business, publishes analyses or reports concerning securities."

As a threshold matter, GP will be receiving a performance fee, which would satisfy the "compensation" element of Section 25009(a).¹ However, you also represent that that GP will not be providing investment advisory services to the fund or its clients. Accordingly, GP does not appear to fall within the "advising others" portion of the definition. Thus, GP does not appear to fall within the statutory definition of the term "investment adviser."

¹ As stated in Commissioner's Release No. 80-C (issued December 21, 1984; revised May 25, 1993), "[t]he 'for compensation' element of the definition of 'investment adviser' is satisfied by the receipt, or expected receipt, of any economic benefit, whether in the form of an advisory fee, commissions, or any other fee relating to the services rendered."

However, Subsection (b) of Section 25230 of the CSL provides that investment adviser representatives and associated persons of investment advisers must comply with the rules adopted by the Commissioner regarding their qualifications and employment by an investment adviser, before engaging in any specified activities, including offering or negotiating for the sale of investment advisory services of the investment adviser. Section 25230 seeks to ensure that investment advisers and individuals employed by investment advisers are appropriately qualified and licensed, as applicable, to provide advisory services to the investing public.

In the instant case, Advisers, not GP, is solely providing advisory services to the Funds. However, GP is performing "general partner" functions, including potentially soliciting investors, which may be characterized as the activities of an "investment adviser representative" or "person associated with an investment adviser."

Section 25009.5 defines the term "investment adviser representative" or associated person of an investment adviser" to mean, in part:

"Investment adviser representative" or "associated person of an investment adviser" means any partner, officer, director of (or a person occupying a similar status or performing similar functions) or other individual, except clerical or ministerial personnel, who is employed by or associated with, or subject to the supervision and control of, an investment adviser that has obtained a certificate or that is required to obtain a certificate under this law, and who does any of the following:

(1) Makes any recommendations or otherwise renders advice regarding securities.

(2) Manages accounts or portfolios of clients.

(3) Determines which recommendation or advice regarding securities should be given.

(4) Solicits, offers, or negotiates for the sale or sells investment advisory services.

(5) Supervises employees who perform any of the foregoing."

You represent that GP may perform some of the enumerated activities set forth above, including soliciting sales of Fund interests. However, as discussed in your request, although Section 25009.5(a) of the CSL refers to "persons," which as defined in Section 25013 of the CSL includes legal persons, the scope of the section is limited by the references to natural persons (i.e., partners, officers, and directors). You represent that all persons engaged in activities described in Section 25009.5 on behalf of the Fund will be registered as Advisers' representatives, and be subject to the supervision of Advisers. Therefore, any concerns regarding unregistered persons engaging in solicitation activities on behalf of an investment adviser are significantly reduced. Accordingly, although GP will not be registered with the Department as Advisers' representative, only individuals registered with the Department will be engaged in investment advisory solicitation activities on behalf of the Fund.

FEDERAL LAW

You have brought to the Department's attention a "no-action letter" issued by the Securities and Exchange Commission regarding whether registration is required under the Investment Advisers Act of 1940 (the "Advisers Act") for general partners of limited partnerships in circumstances identical to that set forth in your request.² The Commissioner frequently looks to the Securities and Exchange Commission for guidance on interpretations of securities laws, due to the similarities of state and federal law.³ (Commissioner's Opinion Nos. 91/1C, 95/1C).

In an SEC no-action letter dated December 8, 2005, to the American Bar Association Section of Business Law (the "ABA Letter"), SEC staff responded to the question of whether a special purpose vehicle ("SPV") established to act as a private fund's general partner or managing member must register as an investment adviser, where the investment adviser to the fund is already registered with the SEC. The facts presented to the SEC were that the SPV's formation documents designate the investment adviser to manage the private fund's assets, and that the SPV has no employees or other persons acting on its behalf other than officers, directors, partners or employees of the adviser. The SEC staff indicated it would not recommend enforcement action under sections 203(a) or 208(d) of the Advisers Act against a registered investment adviser and an SPV, if the SPV does not register as an investment adviser with the SEC, provided that all of the investment advisory activities of the SPV are subject to the Advisers Act and the rules thereunder, and the SPV is subject to examination by the SEC.

In particular, the SEC indicated that any investment advisory fee, including a performance fee or any allocation of a fee that the SPV receives from the private fund, would have to be consistent with the Advisers Act (e.g., section 205 of the Advisers Act). The SEC further indicated that the SPV would make and keep the books and records required under the Advisers Act, and provide the Commission's staff with access to its books and records, as if those requirements applied directly to the SPV. Specifically, the SEC staff indicated that the registered investment adviser would subject the SPV, its employees and persons acting on its behalf to the adviser's supervision and control. For example, all of the employees of the SPV and persons acting on its behalf would be subject to the registered investment adviser's code of ethics under Rule 204A-1 and compliance procedures and practices under Rule 206(4)-7.

Thus, according to the SEC's staff, the SPV, its employees and persons acting on its behalf would be "persons associated with" the registered investment adviser (as that term is defined in Section 202(a)(17) of the Advisers Act) so that the Commission could

² American Bar Association Section of Business Law, SEC No-Action Letter, 2005 WL 3334980 (2005). As noted in your request, the no-action letter was issued in the context of the adoption of rule 203(b)(3)-2 under the Investment Advisers Act of 1940, which was subsequently vacated by Goldstein v. SEC, 451 F.3d 873, 877 (D.C. Cir. 2006).

³ See, however, Commissioner's Opinion No. 88/3C, providing that while SEC "no-action" letters are instructive, the letters are the interpretation of the SEC staff and not the Commission itself.

enforce the requirements of the Advisers Act against the SPV, those persons, and the registered adviser. (See, e.g., sections 203(e) and (f) of the Advisers Act.) In addition, the SPV would look to and essentially rely upon the investment adviser's registration with the Commission in not registering itself. (For example, according to the staff, any disciplinary history that the SPV would have been required to disclose on Form ADV, had it registered as an investment adviser, would be disclosed on the registered investment adviser's Form ADV.) The SEC's no-action position is consistent with a previous no-action letter sanctioning this type of investment fund structure.⁴

You have undertaken that GP and its associated persons will comply with the requirements set forth in the ABA letter.

SHARING OF ADVISER FEES

The receipt by GP of a performance fee also raises the question of whether the compensation is in fact for advisory services, and thus whether advisory fees are being shared with unlicensed persons. The Securities and Exchange Commission has questioned whether the sharing of advisory fees with unlicensed persons creates a conflict of interest and violates an adviser's fiduciary duties, and as a result limits the sharing of fees to licensed persons, investment adviser representatives, associated persons of investment advisers, and solicitors.⁵ Unlicensed persons not otherwise associated with an investment adviser generally may not share in adviser fees.⁶

In this instance, Advisers and GP are under common ownership and control, and thus only licensed persons are ultimately receiving adviser fees. Accordingly, fee sharing concerns are significantly reduced. However, the formation of a business entity whose ownership and control overlaps with a licensed entity should not allow licensed persons to circumvent protections set forth in the CSL.⁷ For example, an overly narrow reading of the limitations on performance fees set forth in Section 25234(a)(1) of the CSL results

⁴ The SEC addressed the issue in a no-action letter dated September 26, 1995, to Thomson Advisory Group LP, which involved a master partnership and several affiliated subpartnerships. The master partnership and the operating subpartnerships were registered as investment advisers. The request was for confirmation that the general partners of the master partnership and the operating subpartnerships need not register as investment advisers. All of the advisory activities were to be conducted solely by registered entities, and all persons who would be engaged in advisory activities were employees, officers and/ or managing directors of a registered entity. In granting no-action relief, the SEC staff referred to past Commission expressions of concern about structural arrangements in which a registered investment adviser is merely a conduit for advisory services provided by personnel of an unregistered affiliate, but recognized that there are often valid business reasons for a company to form a separate registered entity.

⁵ Investment Advisers Act of 1940, Releases Nos. 615 & 688.

⁶ SEC Rule 206(4)-3, Investment Advisers Act of 1940.

⁷ Although this request analyzes the indirect *receipt* of compensation for investment advisory services, the Department has previously provided guidance on the indirect *payment* of compensation for investment advisory services. Specifically, the Department has stated that to satisfy the "for compensation" element of "investment adviser," "[i]t is not necessary that an [investment] adviser's compensation be paid directly by the person receiving advisory services, but only that the investment adviser receive compensation from some source for his services." (Commissioner's Release No. 80-C). Similarly, whether compensation is received indirectly will not affect the analysis of whether a person is engaged in investment advisory services.

in a situation where licensed advisers are subject to compensation limitations, while their unlicensed affiliated entities are not.⁸ Ultimately, the principals of a licensed investment adviser are indirectly receiving a performance fee. Accordingly, these persons, and by extension GP, remain subject to Section 25234(a)(1) and any rules promulgated thereunder. Additionally, all information regarding the performance allocation distribution must be fully disclosed to limited partners of the Fund.

CONCLUSION

Based on the limited facts set forth above, and provided that GP complies with the conditions specified in the ABA letter and their equivalent rules under California law, GP may look to Advisers' registration, and is not required to be licensed separately under Section 25230 of the CSL. This opinion is limited to the facts as specifically represented to the Commissioner in your correspondence. Any change in the facts as represented in your correspondence may compel a different conclusion.

Dated: October 18, 2010
Sacramento, California

PRESTON DuFAUCHARD
California Corporations Commissioner

By _____
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Deputy Commissioner
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⁸ Section 25234(a)(1) of the Corporations Code only refers to the term "investment advisers."