DIRK KEMPTHORNE
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STATE OF IDAHO
DEPARTMENT OF FINANCE
700 W. STATE STREET, 2ND FLOOR
P.O. BOX 83720
BOISE, IDAHO 83720-0031
Website: finance state.id.us

February 21, 2002

[redacted]

Re: [redacted]

Dear [redacted]:

This is in reference to the request of [redacted] (the Fund) that this Department take a no enforcement action position with regard to the Fund's investment advisory activities.

We concur with your letter of February 11, 2002 that, given the Fund's structure as a venture capital fund, it should be excluded from the investment adviser registration requirements of the Idaho Securities Act (the Act). Therefore, the Department agrees to take a no enforcement action position with regard to the Fund's investment advisory activities in Idaho. It should be noted that although we are willing to take a no enforcement action position in this matter, we consider the Fund to be an investment adviser as defined by Section 30-1402(6) of the Act and subject to the various sales practice and anti-fraud provisions of the Act and the Investment Adviser Act of 1940.

The Department's no enforcement action position is predicated upon the facts and representations contained within your letter of February 11, 2002. Should these facts and/or representations change or prove to be inaccurate, our no enforcement action position may also change.

Sincerely,

PATRICIA R. HIGHLEY
Senior Securities Analyst
Idaho Department of Finance

[redacted]

[redacted]

[redacted]

[redacted]

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DEPARTMENT OF ...

February 11, 2002

Marilyn Chastain
State of Idaho
Department of Finance
700 W. State Street, 2nd Floor
P.O. Box 83720
Boise, Idaho 83720-0031

Re: [redacted]

Dear Ms. Chastain:

This firm represents [redacted] a Delaware limited liability company (referred to herein as [redacted]") and [redacted], an Idaho corporation (referred to herein as [redacted]"). [redacted] is the general partner of the venture capital fund [redacted] a Delaware limited partnership (referred to herein as the "Fund"). In conjunction with [redacted] participates in the management of the Fund pursuant to a written Management Agreement between it and the Fund.

The purpose of this letter is to seek, based upon and limited to the specific facts presented, a no-action ruling from the Department of Finance under Idaho Code Section 30-1402(6)(i) and under Section 12.01.08.125 of the Idaho Administrative Procedure Act that [redacted], [redacted], and their members and employees do not need to register as investment advisors under the Idaho Securities Act in connection with and limited to the management of the Fund by [redacted] and [redacted]

The Fund is a venture capital fund, the purpose of which is to make investments in Idaho and the Intermountain region in early stage and emerging growth companies. [redacted] is the general partner of the Fund, and [redacted] has two members, [redacted], a Delaware corporation, and [redacted] The principal place of business of the Fund, [redacted] and [redacted] is Boise, Idaho. The Fund has the following attributes:

- The fund has raised and may raise additional money from the offering and sale of limited partnership interests pursuant to an exemption under SEC Regulation D, which will limit the number of investors and limit the investors to accredited and sophisticated investors. To date, the Fund has only accepted subscriptions from accredited investors.

- The minimum investment for individual investors is $250,000, and the minimum investment for institutions is $1,000,000. The Fund has allowed lesser investment amounts for its Advisory Board and professional service providers, all of whom are accredited investors.

- The Fund will not engage in any public solicitation or general advertising to potential investors.

- In connection with the purchase of a limited partnership interest, each limited partner enters into a commitment to fund a specific total amount. The limited partner then makes an initial 15% deposit with the Fund, and capital calls are made against each limited partner's commitment as needed to fund investments made by the Fund.

- The Fund has a maximum commitment amount of $30,000,000.

- Each limited partner investment has and will be documented through a formal investor questionnaire and subscription agreement to ensure compliance with the Regulation D exemption from registration.

- [redacted] required to provide quarterly written reports to all of the limited partners.

- The Limited Partnership Agreement vests control and management of the Fund in the general partner [redacted], but provides that management services shall be provided by [redacted] pursuant to the terms of a written management agreement.

- The investment objectives of the fund are to make early stage (first institutional round of investment) equity investments in privately held companies.

- All investment decisions will be made based upon the investment objectives of the Fund, and not the individual investment objectives of a limited partner.

- The Fund is prohibited from reinvesting proceeds realized from an investment in a portfolio company (except certain short term liquid investments).

- Subject to working capital needs and other limitations set forth in the Limited Partnership Agreement, the Fund is required to distribute cash profits to its limited partners within 90 days of the closing of a sale transaction involving one of the Fund's portfolio companies.

- The Fund is closed to new Limited Partners within six months of the closing of the initial investment level. Limited Partners investing after this time are required to bear a pro rata share of the Fund costs attributed to prior investors.

- The stated duration of the Fund is 10 years, with a maximum duration of 12 years, after which time it must be dissolved.

- Limited Partners do not have the right to redeem or withdraw their investment in the Fund.

- Management Fees paid to [redacted] are based solely on a percentage of the total commitments of the limited partners: 3% during the first two years; 2.5% during the third and fourth year; 2% during fifth and sixth year; 1.5% during the seventh and eighth year; and 1% thereafter. There are no "performance" fees.

- The Fund's Limited Partnership Agreement provides for the creation of an advisory committee, which currently consists of the following members: (1) [redacted], [redacted], (2) [redacted], (3) [redacted] (4) [redacted] (5) [redacted] (6) [redacted] (7) [redacted] (8) [redacted] (9) [redacted] (10) [redacted] (11) [redacted] (12) [redacted] (13) [redacted]

[redacted] and (14) [redacted].

Although it is not easy to define "venture capital," all of these factors combined clearly distinguish the Fund from a typical mutual fund or hedge fund. The Fund is not used for investing and reinvesting in publicly traded securities, bonds, or other types of marketable securities. Nor does the Fund allow investors to put money in and then cash out at their discretion. Rather, the Fund will make limited equity investments in private companies, and those investments will remain in place until a liquidity event occurs or the Fund terminates after 10 to 12 years. These investments are truly "private equity" investments in the sense that they are illiquid and long term. Once an investment is made, the Fund is usually involved with the company in other ways, such as board representation and providing other advice and support. When a "liquidity event" occurs, the profits are distributed to the partners. In addition, if requested by the Department, the Fund would agree to limit its investments to no more than 40 portfolio companies over the life of the Fund.

Neither [redacted] nor [redacted] intends to register as an investment advisor under the Federal Investment Advisor's Act of 1940 (the "Act") for three reasons. First, Section 203(b)(1) of the Act exempts from registration, "Any investment advisor all of whose clients are residents of the State within which such investment advisor maintains his or its principal office and place of business, and who does not furnish advice or issue analysis or reports with respect to securities listed or admitted to unlisted trading privileges on any national securities exchange." The Fund is the only client of [redacted] and [redacted] and the principal place of business of the Fund, [redacted], and [redacted] is Boise, Idaho. The exemption set forth in Section 203(b)(1) therefore applies.

Second, Section 203(b)(3) of the Act exempts from registration, "Any investment advisor 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 advisor nor acts as an investment advisor to any investment company . . ." In addition, Section 275.203(b)(3)-1 of the Code of Federal Regulations, subsection (a)(2)(i) defines a "single client" as, "A corporation, general partnership, limited partnership, limited liability company, trust, . . . or other legal organization . . . that receives investment advice based upon its investment objectives rather than the individual investment objectives of its shareholders, partners, limited partners, members or beneficiaries . . ." Under this definition of single client, the relationship of [redacted] and [redacted] to the Fund is that of the relationship between an investment advisor and a single client. For that reason, [redacted] and [redacted] are exempt from registration under Section 203(b)(3).

Third, Section 203A(a) of the Act **prohibits** certain investment advisors from registering under the Act. Section 203A(a) states:

> (1) In general--No investment advisor that is regulated or required to be regulated as an investment advisor in the State in which it maintains its principal office and place of business shall register under Section 203, unless the investment advisor--
>
> > (A) has assets under management of not less than $25,000,000, or such higher amount as the Commission may, by rule, deem appropriate in accordance with the purposes of this title; or
> >
> > (B) is an advisor to an investment company registered under Title 1 of this Act.
>
> (2) Definition--For purposes of this subsection, the term "assets under management" means the securities portfolio with respect to which an investment advisor provides continuous and regular supervisory or management services.

Here, although the Fund has commitments of $21,333,333, and is authorized to accept commitments up to $30,000,000, it currently does not have $25,000,000 under management. The Idaho Securities Act applies to [redacted] and the [redacted]. [redacted] and [redacted] are therefore prohibited from registering as an investment advisor under the Act.

Neither the Idaho Securities Act set forth in Chapter 14 of Title 3 of the Idaho Code nor 12.01.08 of the Idaho Administrative Procedure Act contains exemptions from registration similar to Section 203(b) of the 1940 Act. Absent a no-action determination from the Department of Finance, [redacted] and [redacted] would be required to register with and be regulated by the Department of Finance. However, the public policy behind the exemptions set forth in Section 203(b) of the 1940 Act are instructive in this case and provide ample justification for a no-action determination.

As noted above, the SEC defined "single client" in Regulation 275.203(b)(3)-1 to mean a limited partnership, and to exclude the limited partners as counting as clients of an investment advisor. By defining a single client as a limited partnership, Section 203(b)(3) of the Act exempts from registration advisors to a single limited partnership, such as the Fund. The policies behind defining single client to mean a limited partnership were set forth in the SEC's Investment Advisors Act Release No. 956, February 25, 1985, CCH Federal Securities Law Reporter, ¶ 83,742 (1984-85). In Release No. 956, the SEC indicated that sufficient safeguards exist in with limited partnerships such as the Fund that registration under the Investment Advisor Act regulation is not necessary:

> First, because of Section 203(b)(3) itself, the proposed rule would not be available to a general partner who holds himself out to the

> public as an investment advisor who is an investment advisor to a registered investment company or to a BDC which has elected to be treated as such under the Investment Company Act. Second, where the limited partnership is an investment company required to be registered but for the exemption provided by Section 3(c)(1) of the Investment Company Act, that section would restrict the limited partnership to no more than 100 limited partners. Section 3(c)(1) also might, in the absence of material differences between partnerships, similarly limit the total number of partners in all partnerships advised by a general partner. Finally, the nonpublic offering requirement of Section 3(c)(1) would, as a practical matter, limit participation to investors who, by themselves or with personal representatives, are sophisticated or who are accredited investors.

All of these factors are present in this case, and all of these factors weigh against requiring [redacted] and [redacted] from registering as investment advisors with the Department of Finance.

The Idaho Securities Act requires investment advisors to register with the Department of Finance. The Idaho Securities Act does not have exemptions from registration similar to those set forth in Section 203(b) of the 1940 Act. However, Idaho Code Section 30-1402(6)(i) states that the term "investment advisor" does not include "(i) such other persons not within the intent of this subsection as the director may, by rule or order, designate." This concept is repeated in Section 12.01.08.125 of the Idaho Administrative Procedure Act, which states: "The Director may, either upon request or upon his own motion, waive or modify the application of any particular section to a particular salesman, broker dealer or investment advisor when, in his opinion, just and reasonable cause exists for such action and the waiving or modifying of such rule would not be contrary to the provisions of the Act or to the public interest." We respectfully submit that good cause exists pursuant to Section 30-1402(6)(i) and Section 12.01.08.125 of the IDAPA to exempt [redacted] and [redacted] from registration as investment advisors under the Idaho Securities Act. The Fund is a detailed, well-managed, and sophisticated investment mechanism. The exemption from securities registration under Regulation D, coupled with the investment requirements set by the Fund, requires institutional, accredited, or sophisticated investors in prescribed numbers. From a regulatory standpoint, there is very little to be gained in investor protection from requiring registration as investment advisors that will not be accomplished and safeguarded pursuant to the disclosure requirements already imposed by Regulation D.

For these reasons, the same rational adopted by the SEC in connection with the promulgation of Regulation 275.203(b)(3)-1 applies in this case. Just as the federal statutory and regulatory framework would exempt [redacted] and [redacted] from registration, so

should the Department of Finance exempt [redacted] and [redacted] from registration as investment advisors. We therefore request that the Department of Finance issue a no-action letter indicating that neither [redacted] nor [redacted] needs to register as an investment advisor under the Idaho Securities Act. We understand that any no-action letter would be limited to the facts and circumstances as presented in this case.

Thank you for your attention to this matter, and please do not hesitate to contact us if there is any additional information we can provide.

Sincerely,

[redacted]

[redacted]