October 14, 1997
Our Ref. No. 97-360-CC
The BSC Employee Fund, L.P.
File No. 811-9168

RESPONSE OF THE OFFICE OF CHIEF COUNSEL
DIVISION OF INVESTMENT MANAGEMENT

By letter dated September 24, 1997, you request our guidance as to whether The BSC Employee Fund, L.P. (the "Partnership"), an employees' securities company as defined in Section 2(a)(13) of the Investment Company Act of 1940 (the "Act"), may treat its unfunded capital commitments as "investments" for purposes of Rule 2a51-1 under the Act.[1]

You state that the Partnership was created for the benefit of certain employees, officers, and directors ("Eligible Employees") of The Bear Stearns Companies, Inc. ("BSC") and any entities controlled directly or indirectly by BSC ("Bear Stearns"). Interests in the Partnership have been offered and sold to Eligible Employees without registration pursuant to Section 4(2) of the Securities Act of 1933 ("Securities Act").[2] The Partnership invests in private investment vehicles that typically are excluded from the definition of "investment company" under Section 3(c)(1) or Section 3(c)(7) of the Act ("Acquisition Funds").

You represent that the Partnership has binding capital commitments from its limited partners, payable on demand to the Partnership, in excess of $25 million in cash. You state that, in lieu of calling the capital commitments of the Eligible Employees who are admitted to the Partnership as limited partners on an up-front basis, the Partnership proposes to draw down the capital of the limited partners over time, roughly in parallel to capital calls issued by the Acquisition Funds.[3]

The Partnership and its general partner received an order[4] under Section 6(b)[5] of the Act exempting them from particular provisions of the Act to permit them to engage in certain

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1 Rule 2a51-1 defines the term "investments" for purposes of Section 2(a)(51) of the Act, which in turn defines the term "qualified purchaser."

2 Section 4(2) exempts transactions by an issuer not involving any public offering from the registration requirements of the Securities Act.

3 You state that the Partnership expects to draw under a credit facility provided by Bear Stearns to fund a portion of the Partnership's investment program. Pursuant to Rule 2a51-1(e) under the Act, you represent that amounts to be drawn under the credit facility have been deducted for purposes of calculating the total amount of "investments" held or to be held by the Partnership.

4 The BSC Employee Fund, L.P., Investment Company Act Release Nos. IC-22656 (May 7, 1997) (notice) and IC-22695 (June 3, 1997) (order).

5 Section 6(b) of the Act provides that the Commission shall exempt employees' securities companies from the provisions of the Act to the extent that such exemption is consistent with the protection of investors.

affiliated and joint transactions. In their application, applicants discussed the proposed investments of the Partnership and the manner in which the Partnership would draw down the limited partners' capital.

Discussion

In order to invest in securities issued by a company excluded from the definition of "investment company" under Section 3(c)(7) of the Act ("Section 3(c)(7) Company"), an investor must be a "qualified purchaser." Section 2(a)(51)(A)(iv) of the Act generally defines "qualified purchaser" as any person who in the aggregate owns and invests on a discretionary basis not less than $25 million in investments. Rule 2a51-1(b) under the Act defines "investments" for purposes of Section 2(a)(51). Subparagraph (6) of that provision states that the term "investments" includes:

> In the case of a Prospective Qualified Purchaser that is a Section 3(c)(7) Company, a company that would be an investment company but for the exclusion provided by Section 3(c)(1) of the Act . . ., or a commodity pool, any amounts payable to such Prospective Qualified Purchaser pursuant to a firm agreement or similar binding commitment pursuant to which a person has agreed to acquire an interest in, or make capital contributions to, the Prospective Qualified Purchaser upon the demand of the Prospective Qualified Purchaser.

You maintain that the nature of the subscription agreements is such that the Partnership qualifies as a "qualified purchaser" for purposes of Section 2(a)(51)(A)(iv) of the Act if the Partnership includes in the amount of its "investments" the amounts payable to the Partnership by its limited partners pursuant to the subscription agreements. You question whether the Partnership's unfunded capital commitments constitute investments because the Partnership is not a Section 3(c)(7) Company, is not excluded from the Act under Section 3(c)(1), and is not a commodity pool. You note that the Commission stated in the release adopting Rule 2a51-1 that "a Prospective Qualified Purchaser that is a privately offered fund . . . may treat as investments unfunded capital commitments (*i.e.*, firm agreements by investors to provide these Prospective Qualified Purchasers with cash upon request)."[6] While the adopting release used the phrase "privately offered funds," Rule 2a51-1(b)(6) refers to Section 3(c)(7) Companies, companies excluded from the Act under Section 3(c)(1) of the Act, and commodity pools. You maintain that the policy articulated in the adopting release applies equally to the Partnership, which offers its interests on a private basis to management personnel who expect to be able to defer the funding of their capital commitments until such time as the Partnership is able to invest the capital in the Partnership's underlying investments.

You represent that if the Partnership is unable to treat its unfunded capital commitments as investments under Rule 2a51-1, its ability to implement its investment program may be adversely affected, because the Partnership may have to defer investing in Section 3(c)(7) Companies until

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[6] Privately Offered Investment Companies, Investment Company Act Release No. 22597 (Apr. 3, 1997) ("adopting release").

its investment portfolio otherwise increases to $25 million. Alternatively, you maintain that forcing the Partnership to draw its limited partners' cash capital immediately to enable the Partnership to meet the $25 million investment threshold could disadvantage the limited partners.

Analysis

We agree that the policy articulated in the adopting release that "privately offered fund[s] . . . may treat as investments unfunded capital commitments . . ." applies equally to privately offered employees' securities companies such as the Partnership. These companies have access to cash that will be used for investment purposes, through the commitments that reflect investors' assessments of the investment expertise of the sponsor of the employees' securities company. Thus, an employees' securities company may treat its firm agreements or similar binding commitments pursuant to which investors have agreed to acquire interests in, or make capital contributions to, a qualified purchaser upon the demand of the qualified purchaser as "investments" for purposes of Rule 2a51-1 under the Act. This response is based on the facts and representations contained in your letter. You should note that different facts and circumstances may require a different conclusion.

Sarah A. Buescher

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September 24 1997

VIA MESSENGER

Office of the Associate Director (Chief Counsel)
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Securities and Exchange Commission
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Investment Company Act/
Sections 2(a)(51)(A) and
3(c)(7); Rule 2a51-1

Attention: Karen L. McMillan, Esq.

Dear Ms. McMillan:

We are writing to seek clarification from the Division of Investment Management of an interpretive issue that has arisen regarding the definition of the term "investments" for purposes of Rule 2a51-1 under the Investment Company Act, as amended (the "Act"). This issue has arisen in the course of our representation of The BSC Employee Fund, L.P. (the "Partnership"), to which the Commission has granted an order (the "Order") pursuant to Section 6(b) of the Act exempting the Partnership from certain provisions of the Act.[1] Resolution of the issue is relevant to the question of whether the Partnership (and similar future partnerships) may be deemed a "Qualified Purchaser" for purposes of Section 2(a)(51(A) of the Act and, accordingly, whether the Partnership may invest in vehicles that are excluded from the definition

[1] See The BSC Employee Fund, L.P., Investment Company Act Release Nos. 22656 (May 7, 1997) (notice) and 22695 (June 3, 1997) (order). Although we believe that the facts pertinent to the resolution of the issue raised by this letter are fully set forth herein, a more complete description of the Partnership and its proposed activities may be found in Investment Company Act Release No. 22656.

of "investment company" (and similar future partnerships) by operation of Section 3(c)(7) of the Act.

The Partnership has been formed for the benefit of eligible employees, officers and directors ("Eligible Employees") of The Bear Stearns Companies Inc. ("BSC") and entities controlled directly or indirectly by BSC (BSC and such entities being referred to collectively as "Bear Stearns") and is intended to be a means of rewarding and retaining these individuals. Each Eligible Employee must at the time of his or her subscription for a limited partnership interest in the Partnership be a Managing Director or Senior Managing Director of Bear Stearns or a Bear Stearns director or senior officer and must also be an "accredited investor" meeting the income requirements set forth under Rule 501(a)(6) of Regulation D under the Securities Act of 1933 as amended (the "Securities Act").[2] By virtue of their employment by Bear Stearns, Eligible Employees are also sophisticated professionals engaged in various aspects of the investment banking and securities business. Interests in the Partnership have been offered and sold on a private basis to Eligible Employees in reliance on the exemption from the registration requirements of the Securities Act set forth in Section 4(2) thereof. The Partnership is investing its capital in a number of closed-end private investment funds which are typically excluded from the definition of "investment company" by operation of Section 3(c)(1) of the Act or, potentially, Section 3(c)(7) thereof ("Acquisition Funds"). The Acquisition Funds in which the Partnership proposes to invest have been identified by Bear Stearns through the Partnership's general partner, which is a wholly owned subsidiary of BSC and whose Board of Directors is comprised exclusively of senior management personnel of Bear Stearns.

Pursuant to the subscription agreements in which Eligible Employees agreed to subscribe for limited partnership interests in the Partnership, the Partnership received binding contractual commitments from its limited partners for approximately $30.0 million in cash, to be contributed to the Partnership on demand of the Partnership.[3] The Partnership is drawing on these capital commitments over time, roughly in parallel fashion to capital calls issued by the Acquisition Funds in which the Partnership itself is investing. The nature of the subscription agreements is such that the Partnership qualifies as a "Qualified Purchaser" for purposes of Section 2(a)(51)(A)(iv) of the Act, if the Partnership includes in the amount of its "investments" (calculated as provided in Rule 2a-51-1(b)(6) under the Act) the amounts payable to the Partnership by its limited partners pursuant to the subscription agreements.

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2 The sole exception to these offering and eligibility requirements relate to a very limited number of BSC employees (five or fewer) who have been intimately involved in the organization of the Partnership and its investment program.

3 The Partnership also expects to draw under a credit facility provided by Bear Stearns to fund in part the Partnership's investment program. Pursuant to Rule 2a51-1(e), amounts to be drawn under the credit facility have been deducted for purposes of calculating the total amount of "investments" held or to be held by the Partnership.

We believe that the Partnership should be permitted to include the capital commitments of its limited partners in calculating the amount of its "investments" for purposes of Section 2(a)(51)(A)(iv) of the Act. In the Investment Company Act Release adopting Rule 2a51-1 (Investment Company Act Release No. 22597) (the "Section 3(c)(7) Adopting Release"), the Commission stated that a "Prospective Qualified Purchaser that is a privately offered fund . . . may treat as investments unfunded capital commitments," given that "the fund has access to cash that will be used for investment purposes, through commitments that reflect investors' assessment of the fund sponsor's investment expertise." That policy is precisely applicable to the case of the Partnership, in which interests have been offered on a private basis under Section 4(2) of the Securities Act to highly sophisticated management personnel of an investment banking firm and where the limited partners (i) are relying on Bear Stearns to identify, and invest their capital in, a diversified portfolio of Acquisition Funds, and (ii) expect to be able to defer funding their capital commitments until such time as the Partnership is able to invest that capital in the Partnership's underlying investments. However, Rule 2a51-1(b)(6), in contrast to the Section 3(c)(7) Adopting Release, speaks only to whether commodity pools or entities excluded from the definition of "investment company" by operation of Section 3(c)(1) or Section 3(c)(7) of the Act may treat their capital commitments as investments. Rule 2a51-1(b)(6) does not specifically address whether privately offered employee securities companies such as the Partnership, which have received exemptive orders under Section 6(b), may also treat their capital commitments as investments.

If the Partnership is unable to treat the capital commitments of its limited partners as "investments" for purposes of Section 2(a)(51)(A)(iv) of the Act, its ability to implement its investment program may be adversely affected. This is because investment by the Partnership in entities relying on the Section 3(c)(7) exclusion may have to be deferred until such time as the Partnership's investment portfolio otherwise increases to $25.0 million in size. Such a result may effectively preclude the Partnership from investing in a number of otherwise attractive Section 3(c)(7) funds. On the other hand, forcing the Partnership to draw its limited partners' cash capital commitments immediately, which would enable compliance with the $25.0 million in investments test, would appear to be wholly unnecessary and punitive to the limited partners.

As an interpretive matter, we believe, and ask the Staff to concur, that, for purposes of Rule 2a51-1(b)(6), capital commitments made in respect of privately offered employee securities companies which have received orders under Section 6(b) (and, potentially, Section 6(e)) should be treated identically to capital commitments made in respect of Section 3(c)(1) companies, Section 3(c)(7) companies or commodity pools. Alternatively, to the extent the Staff is not prepared to make a blanket determination for purposes of Rule 2a-51-1(b)(6) that a company that has received a Section 6(b) order may treat unfunded capital commitments as if it were a Section 3(c)(1) or Section 3(c)(7) company, we believe that the Partnership, in light of the representations made herein about the sophistication of the limited partners and Bear Stearns, and in light of the Partnerships investment program of investing in Section 3(c)(1) and Section

3(c)(7) funds, should be allowed to treat its unfunded capital commitments as investments pursuant to Rule 2-51-1(b)(6).

If for any reason you do not concur in our conclusion, we respectfully request a conference with the Staff before any adverse written response is given to this letter. Should you or any member of the Staff have any questions concerning the foregoing or need further information or clarification, please call either me at (202) 637-2237 or John Hart of the New York office of this firm at (212) 906-1290. Thank you very much for your consideration of this request.

Very truly yours,

John D. Watson, Jr.
of LATHAM & WATKINS

cc: David Grim, Esq.
Mercer Bullard, Esq.

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