August 31, 2004

Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street NW
Washington, DC 20549-0609

Re: File No S7-30-04: Proposed Registration Under the Advisers Act of Certain Hedge Fund Advisers

On July 20, 2004, the Securities and Exchange Commission (the "Commission") published proposed rules that would require many offshore hedge fund advisers to register under the Investment Advisers Act of 1940 (the "Act") by counting investors in private funds as "clients" for purposes of the Section 203(b)(3) "private adviser" exemption. Currently an offshore adviser may count each United States hedge fund it manages as a single client for purposes of Section 203(b)(3). The proposed rules would require an offshore adviser to look through most of its hedge funds (U.S. funds and offshore funds) to count each United States investor in the funds as a client for purposes of this exemption. I am respectfully seeking clarification on the application of the Act to dealings between an offshore adviser, its offshore hedge funds and those funds' investors, as more fully described below, and would respectfully request that the Commission specifically address this matter in any public release that adopts the proposed rules or any revised version of such proposed rules.

General Obligations

In the proposing release, the Commission states that it is not changing its position of generally not applying most of the substantive provisions of the Act to dealings between an offshore adviser registered under the Act (a "registered offshore adviser") and its offshore clients, citing the principles first set forth in the Uniao de Banco de Brasileiros S.A., SEC Staff No-Action Letter (July 28, 1992) ("*Unibanco*"). The release also explains that the proposed rules were drafted to ensure this general position would continue to apply to relationships between a registered offshore adviser and its offshore hedge funds by expressly permitting a registered offshore adviser to treat its offshore private funds as clients (as opposed to investors in the funds) for all purposes of the Act aside from determining the Section 203(b)(3) exemption and from the application of Sections 206(1) and 206(2), two of the Act's antifraud provisions.

In *Unibanco*, the Division of Investment Management (the "Staff") said it would not recommend enforcement action to the Commission if the registered offshore adviser provided advisory services to its offshore clients solely in accordance with applicable foreign law without complying with the Act. However, this favorable response was conditioned on the offshore adviser undertaking to do the following with respect to its offshore clients: (i) maintain books and records in accordance with Act, (ii) ensure records clearly reflect advice to clients (iii) make books and records available to the Commission for inspection, and (iv) provide the Commission with access to its employees upon request. The Staff has reaffirmed a position of limited extraterritorial application of the Act in a number of subsequent no-action letters. In these letters the Staff continued to condition its favorable response on offshore advisers undertaking to comply with recordkeeping requirements of the Act with respect to their offshore clients and to make all of their books, records and employees available to the Commission for routine inspections. However, these no-action positions were dependent on the specific details of each no-action request and, as a result, there is some ambiguity as to the extent to which the Staff believes the Act should generally not apply to dealings between a registered offshore adviser and its offshore clients. For example, some no-action positions have permitted the registered offshore adviser to *generally* not comply with the Act based on, among other things, the adviser undertaking to comply with *all* of the record keeping requirements of the Act with respect to its offshore clients.[1] Other no-action positions *specifically identified* the provisions of the Act the registered offshore adviser did not need to comply with and were based in part on undertakings to only comply with *certain* recordkeeping requirements of the Act with respect to offshore clients.[2]

[1] *See Unibanco* and Mercury Asset Management plc, SEC Staff No-Action Letter (April 16, 1993).
[2] *See* The National Mutual Group, SEC Staff No-Action Letter (March 8, 1993) ("*NMG*") and Murray Johnstone Holdings Ltd., et al., SEC Staff No-Action Letter (October 7, 1994) ("*Murray Johnstone*").

- *In light of the Staff's statement in 1992 that after a period of providing no-action advice with respect to the principles applied in Unibanco it would recommend that the Commission codify an approach,[3] the fact specific case by case analysis that has occurred over the last 12 years and the significant number of offshore advisers that may be required to register under Act if the proposed rules are finalized in their present form, I respectfully request that the Commission clarify what the obligations of offshore advisers would be under the proposed rules with respect to their dealings with offshore hedge funds and those funds' investors.*

- *To what extent, if at all, would the Staff apply those substantive provisions of the Act that were adopted after it took its positions in these no-action letters, such as rules addressing proxy voting and compliance policies and procedures?*

Antifraud

The Staff explained in *Unibanco* and its no-action letter progeny that limited application of the Act to dealings between a registered offshore adviser and its offshore clients is based on a "conduct and effects" jurisdictional approach, whereby the substantive provisions of the Act generally do not govern such dealings unless the offshore adviser's activities with its offshore clients involve the requisite conduct or effects in the United States, or effects on United States clients. However, the Staff has also maintained that dealings between a registered offshore adviser and its offshore clients always have the potential to have a significant effect on the adviser's United States clients or on the United States markets, and for this reason it has consistently conditioned its no-action positions on maintaining the ability to effectively monitor registered offshore advisers by requiring them to comply with recordkeeping requirements of the Act with respect to their offshore clients and to make all of their books, records and employees available for inspection by the Commission. Where activities between an offshore adviser and its offshore clients have the requisite conduct or effects in the United States, or effects on United States clients, the Staff has stated that the Commission has the ability to take enforcement action under the antifraud provisions of the Act.[4]

The implication of the proposing release is that the conduct and effects approach to the application of the Act would continue to apply to dealings between a registered offshore adviser and its offshore hedge funds. However, the proposed rules would apparently subject a registered offshore adviser to Sections 206(1) and 206(2) with respect to all investors in most of its offshore hedge funds, regardless of whether its dealings with these investors involve conduct or effects in the United States, or effects on United States clients, as would be required under the principles applied in *Unibanco* and its no-action letter progeny.

- *It appears that the proposed rules would therefore enhance the application of the antifraud provisions of the Act to offshore advisers of most offshore hedge funds. Accordingly, I respectfully request that the Commission clarify whether it has intended to create a "Unibanco Plus" regime regarding the application of Sections 206(1) and 206(2) of the Act to dealings between an offshore adviser and most of its offshore hedge funds. If that is not the case, the Commission should likewise clarify this point.*

Brochure Delivery

The proposed rules would permit a registered offshore adviser of an offshore private fund to treat the fund as its client (and not the investors therein) for all purposes of the Act save for determining if it is exempt from registration and for purposes of Sections 206(1) and 206(2). It would therefore appear that an offshore adviser would not have an obligation to deliver a brochure to U.S. investors in its offshore private funds.

- *I respectfully request that the Commission clarify whether it has intended to permit an offshore adviser to not deliver a brochure to U.S. investors in its offshore private funds.*

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[3] *See* SEC Staff Report, Protecting Investors: A Half-Century of Investment Company Regulation, Chapter 5, The Reach of the Investment Advisers Act of 1940 (May 1992) ("*Protecting Investors Report*")

[4] *See Protecting Investors Report*, *NMG* and *Murray Johnstone*.

Best regards,

David Goldstein
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