COMMONWEALTH OF PENNSYLVANIA
GOVERNOR'S OFFICE OF GENERAL COUNSEL

February 12, 2014

Addison D. Braendel, Esquire
Baker & McKenzie LLP
300 East Randolph Street, Suite 5000
Chicago, IL 60601

Re: Stoltz Management Company

Dear Mr. Braendel:

This is in response to your letter to the Commonwealth of Pennsylvania Department of Banking and Securities (the "Department") in which you request an interpretive opinion under Section 604 of the Pennsylvania Securities Act of 1972 ("1972 Act"), 70 P.S. § 1-604, regarding Stoltz Management Company ("Stoltz"). Specifically, you request an interpretive opinion that, based upon the representations set forth in your letter, Stoltz is not engaged "in the business of advising others ... as to the advisability of investing in, purchasing or selling securities" as set forth in Section 102(j) of the 1972 Act, 70 P.S. § 1-102(j), and therefore would not be required to register as an investment adviser with the Department.

Background

You have indicated the following factual background, which is essentially quoted directly from your letter.

> Stoltz Management currently sponsors and operates (through affiliated general partner entities) five real estate funds:
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> - Stoltz Real Estate Fund I, L.P.,
> - Stoltz Real Estate Fund II, L.P.,
> - Stoltz Real Estate Fund III, L.P.,
> - Stoltz Real Estate Fund IV, L.P., and
> - Stoltz Core/Core-Plus Industrial Fund I, L.P. (collectively with the proceeding Funds, the "SREF Funds").
>
> The investors are institutional or high net worth individuals who meet the "qualified purchaser" definition under the Investment Company Act of 1940. The limited partnership interests in the SREF Funds were offered and sold pursuant to Regulation D under the Securities Act of 1933, and are "covered securities" as provided thereunder. Appropriate notice filings were made in Pennsylvania with respect to Pennsylvania investors.
>
> All of the SREF Funds are in the business exclusively of owning and operating commercial real estate assets. The real estate assets are located throughout the United States and include retail (malls, shopping centers, etc.), multi-family (apartments and townhouse complexes);

industrial (warehouses. distribution centers), and office assets. None of the SREF Funds invests in (i) any publicly traded securities (real estate-related or otherwise), (ii) any assets that are not real estate-related or (iii) any passive, non-management interests in real estate.

Most of the ownership is 100% through wholly-owned member-managed limited liability companies ("LLCs"). A minority of the assets are joint ventures, in which the SREF Fund does not own 100% of the entity that owns the real estate, although in each such case the SREF Fund's interest is either a general partner interest (in the case of limited partnerships) or a member interest with management authority (in the case of LLCs). As a result, for every single asset, the SREF Funds have *daily operating and management control* of the real estate asset in question.

Analysis

We note that under §1-102(j), an "investment adviser" is any person who, for compensation, advises others with respect to "securities."[1] We note further that while the definition of "security" under §1-102(t) does not include real estate,[2] general partner interests or cash, it does include any "note," "limited partnership interest," and "membership interest in a limited liability company of any class or series." 70 P.S. § 1-102(t).

Except as set forth below, all of the SREF Funds' assets are comprised of (i) real estate, (ii) general partner interests (in partnerships that own real estate), (iii) LLC membership interests that exactly meet the criteria of § 1-102(t)(v)(A)-(C) and (iv) cash. Nine assets (seven LLCs, one promissory note and one limited partnership interest) technically could constitute "securities" but should not, for the reasons set out below. Please note that in all eight of the assets discussed below, the ultimate asset is real estate.

LLCs

Specifically excluded from the definition of "security" in § 1-102(t) are LLC membership interests that (A) are not manager-managed, (B) the member undertakes in writing to participate in management, and (C) the member does participate in management. See 70 P.S, § 1·102(t)(v)(A)-(C). In all of the LLCs owned by the SREF Funds, the requirements in (A), (B) and (C) are satisfied, except in two cases, as provided below:

Case One: In one of the LLCs, the SREF Fund is designated the "Sponsor" and the third party joint venture partner is designated the "Managing Member." They functionally are co-general partners, as the Sponsor (i.e., the SREF Fund) is granted "the authority to conduct day-to-day operations" of the LLC, while the joint venture partner is given the authority of a managing member. Certain Major Decisions require the consent of both parties. Here, the functionality of the two roles is that of co-general partners. Hence, the criteria of § 1-102(t)(v)(B) and (C) are satisfied, and the requirement of (A) is functionally satisfied (day-to-day authority is exercised), if not facially satisfied. It is our opinion that the

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[1] Note that Stoltz Management currently relies on the "5 or fewer" exemption in §1-102(j)(vii), but is considering sponsoring a sixth real estate fund such that that exemption will no longer be available.

[2] We note that Regulation §102.202 regarding "real property" is not applicable to the real estate assets owned by the SREF Funds. None involve "rental pool arrangements" or require seller involvement post-closing.

exception nonetheless should apply in this instance because the "manager-managed" exclusion is intended to capture passive membership interests in LLCs that are managed by outside managers, which is not the case here. In other words, where the "purchaser" also has day-to-day management authority, the requirement in § 1-102(t)(v)(A) should be deemed satisfied.[3]

Case Two: In six of the LLCs, in order to satisfy certain lender requirements with respect to the particular real estate asset incurring the debt, an affiliate of Stoltz Management is designated as an "executive manager" (with day-to-day management authority) and a non-equity member is designated as an "independent manager" or "special member" (with no day-to-day management authority except in certain bankruptcy scenarios). When the loan is repaid, these limitations automatically disappear. In all these LLCs, the SREF Fund (i) owns 100% of the equity,[4] (ii) retains the right to remove and replace the executive manager at any time and (iii) has full authority to amend the LLC operating agreement at any time (except in certain ways adverse to the loan). It is our opinion these wholly-owned LLCs with an affiliated "executive manager" with day-to-day authority and a third party "independent manager" (with authority only in loan-adverse matters) satisfies in principal, if not technically, the non-passive policy objectives of § 1-102(t)(v)(A)-(C) and, in any event, for purposes of determining investment adviser status, these 100% owned LLCs do not constitute being engaged "in the business of advising others ... as to the advisability of investing in, purchasing or selling securities."[5]

Promissory Note

In one instance, a promissory note is held. The note is a senior loan with a mortgage on a real estate asset that is also held by a SREF Fund. While notes are, technically, securities, we note that contracts that "are secured by adequate property, *real* or personal ... " (emphasis added) are specifically carved out from application of the Pennsylvania Investment Company Act of 1933, as is real estate itself. See Section 6062.[6] It is our opinion that fully-secured notes on real estate (i.e., notes with mortgages) should be considered as real estate in this instance, as is the case here, the real estate that secures the note is also owned by the SREF Funds.

Limited Partnership Interests

In one instance, a de minimus limited partnership interest is held, where the SREF Fund also holds the general partner interest. This bifurcated holding structure was put in place for unrelated contractual and legal reasons, and it is our opinion that limited partnership interests should be disregarded as "securities" where the ultimate beneficial owner also owns the

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[3] This asset is designated for sale at the end of December 2013, and will no longer be owned when the sixth fund is established and the "5 or fewer" exemption is no longer available.

[4] Two assets are only 50% of the equity in the real estate.

[5] Note that if having an affiliated entity serving as a non-equity "executive manager" was determined to be fatal to the securities and investment adviser analyses, Stoltz Management and the SREF Funds in question can arrange to transfer those affiliated "executive managers" to be wholly-owned under the relevant SREF Fund, subject to receiving lender consent.

[6] Separately, we have assessed whether any of the SREF Funds constitutes an "investment company" under § 3(a)(1) of the Investment Company Act of 1940, as amended, and have concluded they do not because the SREF Funds are not engaged in the business of investing in securities.

general partner interest or, in the alternative, under such facts a person that holds both limited partnership interests and general partnership interests in the same partnership that owns real estate should not be deemed to be in the "business of advising others" with respect to "securities."

Otherwise, as stated above, all of the SREF Funds' assets are comprised of (i) real estate, (ii) general partner interests (in partnerships that own real estate), (iii) LLC membership interests that exactly meet the criteria of § 1-102(t)(v)(A)-(C) and (iv) cash.

Analysis

Section 301(c) of the 1972 Act provides that:

> It is unlawful for any person to transact business in this State as an investment adviser unless he is so registered or registered as a broker-dealer under this act or unless he is exempted from registration. It is unlawful for any person to transact business in this State as an investment adviser representative unless he is so registered or exempted from registration.

70 P.S. § 1-301(c). Section 102(j) of the 1972 Act defines "investment adviser" as follows:

> "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, issues or promulgates analyses or reports concerning securities....

70 P.S. § 1-102(j). It is noted at the outset that, as set forth in your letter, the interests in the SREF Funds were sold pursuant to Regulation D of the Securities Act of 1933 as "covered securities" and that all appropriate notice filings were made with the Department. The issue here is whether Stoltz's management of those funds constitutes investment advice requiring registration with the Department as an "investment adviser."

Based on the representations set forth in your letter, it appears that the management of the SREF Funds does not constitute "investment advice." Your letter does highlight specific instances in which the assets held by certain funds include instruments which could arguably constitute "securities" under the 1972 Act, and provides an explanation for the position that those instruments should be excluded from the definition of "security." Without addressing the merits of such positions, it appears that even if those instruments are securities, Stoltz's management of the funds does not involve providing advice regarding the value of those securities or the advisability of investing in, purchasing, or selling securities.[7]

Accordingly, it does not appear that Stoltz is engaged in the business of providing advice to others regarding securities or providing analyses/issuing reports about securities. Accordingly, based on the facts provided, Stoltz is not an "investment adviser" as defined in the 1972 Act.

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[7] It is noted that the instruments at issue here include certain limited liability company interests where Stoltz is the purchaser and co–manager, a promissory note secured by real estate owned by the SREF Funds, and a limited partnership interest in which the SREF Fund also is the general partner.

It should be noted, however, that this analysis is focused on the management of the funds as described in your letter. The interests held by investors in each fund constitute "securities" under Section 102(t) of the 1972 Act, 70 P.S. § 1-102(t), and accordingly the initial and any subsequent offer, sale or purchase of those securities is subject to the provisions of the 1972 Act.

Conclusion

Because the SREF Funds are in the business exclusively of owning and operating commercial real estate assets, Stoltz's management of those funds does not constitute providing advice "as to the value of securities or as to the advisability of investing in, purchasing or selling securities" under Section 102(j) of the 1972 Act.

The Department's analysis is based upon the facts as stated in this letter. Any change in the facts could result in an amendment or reversal of the Department's position. This letter has been authorized by the appropriate Department personnel and constitutes a duly authorized statement of the Department's position regarding the issues discussed herein. This letter may not be relied upon or construed as constituting legal advice.

Please do not hesitate to contact me if you have any further questions regarding this matter.

For the Commonwealth of Pennsylvania
Department of Banking and Securities:

Scott A. Lane
Senior Deputy Chief Counsel