Fed. Sec. L. Rep. P 77,607 (S.E.C. No - Action Letter), 1984 WL 48452

(SEC No-Action Letter)

Fiduciary Management Association, Incorporated

Publicly Available March 5, 1984

SEC LETTER

***1 1940 Act / s 206(4)–1)**

February 2, 1984
Publicly Available March 5, 1984

Our Ref. No. 83–126–CC

Fiduciary Management Associates, Inc.

File No. 801–15634–3

As Edward F. O'Keefe (pub.avail. March 14, 1978) and Anametrics Investment Inc. (pub.avail. April 5, 1977) make clear, information concerning performance would be misleading if it implies something about, or is likely to cause an inference to be drawn concerning, the experience of advisory clients, the possibility of a prospective client's having an investment experience similar to that which the information suggests was enjoyed by the adviser's clients, or the adviser's competence, when there are additional facts which the adviser knew or ought to have known which, if also disclosed, would prevent the implication from arising or the inference from being drawn. Because we do not know what **Fiduciary Management Associates**, **Inc**. ("FMA") or its president Philip E. Arnold ("Arnold") knows or ought to know concerning the performance data chart submitted by you, we cannot determine whether the chart is misleading. If no person other than Arnold played a significant part in the performance of accounts of clients of Investment and Capital Management, Inc. ("ICM") that were under Arnold's management ("Arnold's ICM accounts") and if the performance of those of Arnold's ICM accounts which became accounts of FMA managed by Arnold ("Arnold's FMA accounts") was not materially different from the performance of Arnold's ICM accounts which did not become Arnold's FMA accounts, information given to prospective clients of FMA concerning the performance of Arnold's ICM accounts which became Arnold's FMA accounts would not in and of itself be misleading.

Stanley B. Judd
Deputy Chief Counsel

LETTER TO SEC

April 6, 1983
Sidney L. Cimmet, Esquire
Chief Counsel
Division of Investment Management
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549
Re: **Fiduciary Management Associates**, **Inc**. ("FMA")

Re:File No. 801–15634

Dear Mr. Cimmet:

Fiduciary Management Associates, Inc. ("FMA") has asked us to obtain your advice that the staff will not recommend that the Commission take any enforcement action under the Investment Advisers Act of 1940 ("Advisers Act") against FMA and its directors and officers by virtue of its use of the attached performance data chart (the "Chart") in connection with the conduct of its business, including solicitation of new clients. [1] FMA has advised us as follows with respect to the relevant facts:

Fiduciary Management Associates, Inc.

***2** FMA is an Illinois corporation located at 135 S. LaSalle Street, Chicago, Illinois. Robert F. Carr, III is Chairman of the Board, and Philip E. Arnold is President. FMA commenced operations as an investment adviser in December 1980. It is registered as an investment adviser under the Advisers Act as well as under the laws of Illinois and other states. Both Carr and Arnold, prior to FMA's formation in December 1980, were officers of Investment and Capital Management, Inc. ("ICM"), another registered investment adviser. FMA offers advisory and investment management services only to sophisticated individuals and institutional clients.

During the period from April, 1980 to December, 1980, Mr. Arnold personally exercised the primary investment responsibility for a group of accounts while employed as Executive Vice President, Investments at ICM. A number of these accounts (the "Arnold/ICM accounts"), have been managed by FMA since its inception. Two of Arnold and Carr's former associates at ICM also became associated with FMA at its inception and continue to function as members of its investment strategy group.

Mr. Arnold's responsibilities in the management of the Arnold/ICM accounts were essentially no different than his present responsibilities regarding the management of FMA's accounts. Mr. Arnold, while associated with ICM, had full authority to make investment decisions for his accounts without supervision or approval from any other officer of ICM. Informal meetings of ICM, chaired by Mr. Arnold, were sporadically called to discuss general economic and investment trends, specific securities investments, and appropriate ratios of equity to fixed investment in balanced accounts. However, except in the most general way, these discussions did not affect the management of the Arnold/ICM accounts used in the 1975–1980 data in the Chart. [2]

The Performance Data Chart

The Chart was developed by FMA in response to requests from prospective clients for the performance record of Arnold and FMA regarding equity investments. Such historical information is considered essential to such investors in selecting an investment adviser. Typically, prospective clients require data from advisers covering a period of at least five years.

The Chart depicts only the performance of equity portfolios and the equity portion of balanced portfolios which Mr. Arnold actively managed at ICM and which he continued to manage after the inception of FMA. With regard to the 1975–1980 performance data, the Chart expressly states that, during that period, the accounts were not managed by FMA, but by Arnold while he was an officer of ICM. The Chart also segregates the performance of accounts in that period from FMA's performance as to those same accounts since its organization. The footnotes to the Chart specifically and fully disclose that the data for the period 1975–1980 include only the 1975–1980 performance of equity accounts over which Arnold had full discretion at ICM and which have subsequently become accounts of FMA. Footnote 4 states:

***3** "4. The term 'managed equity accounts' refers to fully discretionary employee benefit plan equity accounts and the designated equity position (including designated cash reserves) of balanced accounts. The statistics shown in this column consist of total rate of return for the years 1975 through 1980 of managed equity accounts which Philip E. Arnold, now President of FMA, personally managed during the period 1975–1982 in his capacity as Executive Vice President, Investments, for another investment firm by which he was then employed, and which accounts, after January 1, 1981, continued under management by FMA. The data for 1975–1980 are not, and should not be construed as, the performance data of FMA, which began business in December 1980. (emphasis supplied)

The performance data for the period January 1, 1981 to date consists of the total rate of return on the same managed equity accounts previously managed by Mr. Arnold, which since January 1, 1981, have been under FMA management, along with new accounts under FMA management."

The data in the Chart relates to all of the equity accounts of the type referred to above in order to provide prospective customers with an objective measure of the investment performance of Arnold and FMA. None of the equity accounts of that type managed by Arnold at ICM and subsequently managed by FMA have been omitted. The accounts which Arnold managed at ICM but which did not become accounts of FMA are not included, because they would not provide a continuity of comparison. Mr. Arnold believes, however, that the total rates of return achieved by those accounts from 1975 through 1980 were comparable to the rate of return for the accounts reflected in the Chart.

Issues Raised Under Section 206 and Rule 206(4)–1

In our view, use of the Chart raises two relevant issues. First, is it appropriate for Mr. Arnold to include in the Chart, on a fully disclosed basis, the performance results of accounts managed by him while he was an officer of a different investment adviser. Second, is there any potentially misleading aspect to the Chart or its presentation of performance information.

Based on the facts and circumstances involved, we are of the opinion that the Chart is not misleading, deceitful or fraudulent and its use would not violate Section 206 of the Advisers Act or Rule 206(4)–1 thereunder.

A. Use of Arnold/ICM Account Data

Under appropriate circumstances, an adviser may include in publicly disseminated documents data which represents the performance of its account managers for periods when such managers worked for other firms. The Commission's staff, to our knowledge, has not objected generally to such practice as part of its routine examinations of advisers. Moreover, the staff raised no objection when a newly registered adviser proposed to use the performance results achieved by a separate unregistered adviser which was a minority shareholder of the registered adviser. Investors Diversified Services, Inc. (pub.avail. October 29, 1981).

***4** We submit that FMA's use of the results of the Arnold/ICM accounts on a fully disclosed basis, is well within the acceptable standards. Arnold was primarily responsible for such accounts, his individual determinations were not significantly influenced by any other persons or resources at ICM and he has been primarily responsible for the same accounts at FMA. Indeed, the performance data of such accounts is more fairly attributable by far to Mr. Arnold than to ICM or any other person.

FMA's use of Arnold's performance data in the circumstances is a commonly accepted practice in the investment community. Investors are encouraged to look beyond the advisory organization to the individual who will make the actual investment decisions.[3] Moreover, if FMA cannot show the performance of its principal investment officer over a minimum five-year period, it cannot carry on any meaningful marketing activities among the institutional and sophisticated users of its services. Precluding FMA from using Arnold's past investment performance under these circumstances has broad anti-competitive implications which will effectively preclude new entrants with experienced personnel from entering the investment advisory field.

In our opinion, based on the facts and circumstances set forth in this letter and the disclosures made in the Chart, it is proper for FMA to portray Arnold's performance from 1975–1980 on the Chart and its use would not violate Section 206 of the Advisers Act or Rule 206(4)–1 thereunder.

B. Presentation of the Performance Data

The Anametrics Investment Inc., (avail. April 5, 1977) and Edward F. O'Keefe (avail. March 14, 1978) staff interpretive letters make clear that an adviser is not prohibited from disclosing its past performance “so long as such information is not false or misleading.” The letters give general examples of misleading performance materials, and reflect the staff's concern about the use of performance data, without noting the circumstances in which it arose, e.g., rising market or falling market. The letters also indicate the staff's concern that comparisons with indexes of performance must be fair, e.g., equity performance measured against an index of similar securities.

Based on the facts presented herein, we believe that no misleading implications arise from the presentation of data in the Chart. No information has been omitted which would materially alter the implications arising from the Chart. The Chart provides separate data as to the investment experience of accounts managed by Mr. Arnold while associated with both ICM and FMA. The performance data relating to the Arnold/ICM accounts specifically includes all equity accounts and the equity portions of balanced accounts (as specifically defined in the footnotes to the Chart) which he managed at ICM and which continued under his management at FMA. The accounts reflected in the Chart are representative of the accounts which Mr. Arnold managed at ICM prior to the formation of FMA in 1980. The relative size of the accounts managed by Arnold and FMA as reflected on the Chart does not appear to have any material impact on investment performance.

***5** Moreover, the performance data is not presented in isolation. Since Arnold and FMA select investments from a broad range of equities, the Chart includes the comparable performance of the two most widely regarded equity indexes, the Dow Jones Industrial Average and the Standard & Poor's 500 Stock Index. These indexes provide appropriate general comparative performance data for the years shown on the Chart.

Second, the Anametrics and O'Keefe letters question the use of the average performance of accounts. FMA uses a unit method of showing total rates of return. Information provided on the “time weighted rate of return” or “unit” method, is an objective method of presenting performance on a “total return” basis. The “unit” method of evaluating performance eliminates, among other things, the effect of additions and withdrawals of funds under management.

The information generated by the unit method of measurement is well recognized in the industry and is required by sophisticated investors, in making their decisions regarding the appointment of an adviser. According to the Ford Foundation Report (pp. 23–25, 63–65) this method, as employed in the Chart, is “used almost universally by the mutual funds and is now being widely adopted by investment managers for pension funds and private accounts” to provide “an accurate insight ... into what the investment record has actually been.” The method has been adopted by Evaluation Associates, Inc. with respect to its widely recognized Investment Manager Profiles for the equity category, which reports standardized investment performance results of more than 100 investment management organizations. This method was presented to the SEC staff which issued a no-action letter permitting its use, albeit limited to the specific situation. Evaluation Associates, Inc. (pub.avail. July 28, 1976).

Third, the Chart does not raise the concern expressed by the staff in Anametrics and O'Keefe regarding performance data limited to periods of special market characteristics, which, if undisclosed, would make the date misleading. The seven-year period covered by the Chart includes periods of both rising and falling stock prices. The general market characteristics over the period are described in FMA's brochure, of which the Chart is a part, as follows:

> "Since the late 1960s, investment markets have been subject to an accelerating rate of technological advance, important changes in the social and political environment and more volatile levels of inflation, as well as a significant internationalization of our domestic economy."

Moreover, because the performance data during the period is compared with Standard & Poor's 500 Stock Index, the Dow Jones Industrial Average and the Consumer Price Index, any peculiar market characteristics would also appear in those averages.

The specific objectives of all accounts under management, the stability or volatility of stock prices, and the diversification and size of such accounts cannot be provided without describing every account in detail. Such detail would render the Chart so complex as to be useless in terms of providing the information that FMA's clients and prospective clients seek in making an adviser appointment decision. The disclosure goals sought in Anametrics and O'Keefe, supra, are best accomplished by disclosure of investment philosophy, method and portfolio preference. These are all set forth in Part II of FMA's Form ADV on file with the Commission, are disseminated to each prospective investor, and periodically, as required by law, to each client, and also appear in FMA's brochure.

***6** It is our opinion that, both in general and in consideration of the special issues raised in the staff's no-action letters, FMA's use of the Chart is not misleading. The Chart, in conjunction with Part II of FMA's Form ADV and FMA's disclosures of its investment philosophy and approach, fosters the objectives of the securities laws in providing FMA's clients and prospective clients with the information they require in rendering a decision as to the appointment of an investment adviser.

If you have any questions or want to discuss these matters further, please do not hesitate to contact the undersigned or Arthur Brown. If you are unable to issue the requested response to this letter, we would appreciate the opportunity to meet with you prior to your issuing any response.

Very truly yours,

Richard M. Phillips

ENCLOSURE

PERFORMANCE DATA

TOTAL RATE OF RETURN (1)

EQUITY INVESTMENTS

	Standard & Poor's 500 Stock Index (2)	**Dow Jones Industrial Average (3)**	**Managed Equity Accounts (4)**	**Consumer Price Index**
1975	+37.3%	+45.0%	+38.3%	+ 7.0%
1976	+24.0	+23.0	+23.6	+ 4.8
1977	- 7.2	-12.9	- 3.4	+ 6.8

1978	+ 6.4	+ 2.8	+ 5.0	+ 9.0
1979	+18.7	+10.7	+32.4	+13.3
1980	+32.5	+22.1	+24.5	+13.5
1981	- 5.3	- 3.7	+ 6.8	+ 8.9
1982 (year-end)	+20.4	+25.8	+24.3	+ 3.9
Eight Year Compound Annual Return	+14.8	+12.8	+18.1	+ 8.3

***7** 1) The term "total rate of return" refers to the statistical measurement of return of investments, which includes both income (dividends and/or interest plus or minus price changes.

2) The Standard & Poor's 500 Stock Index is composed of 500 stocks in 92 industrial categories weighted on the basis of total market value.

3) The Dow Jones Industrial Average is composed of 30 large industrial companies weighted on the basis of the price level of the companies' shares.

4) The term "managed equity accounts" refers to fully discretionary employee benefit plan equity accounts and the designated equity portion (including designated cash reserves) of balanced accounts. The statistics shown in this column consists of total rate of return for the years 1975 through 1982 of managed equity accounts which Philip E. Arnold, now President of FMA, personally managed during the period 1975–1980 in his capacity as Executive Vice President, Investments, for another investment firm by which he was then employed, and which accounts, after January 1, 1981, continued under management by FMA. The data for 1975–1980 are not, and should not be construed as, the performance data of FMA, which began business in December, 1980.

The performance data for 1981 consists of the total rate of return on the same managed equity accounts previously managed by Mr. Arnold, which since January, 1981, have been under FMA management, along with new accounts under FMA management.

Footnotes

1 The use of an earlier version of the Chart was first questioned by the Chicago Regional Office during an examination of FMA. That office invited FMA to file for a no-action position, which has led to this letter.

2 Schedule F to ICM's Form ADV, which described these meetings, was not prepared or reviewed by Arnold. To the extent that the description in Schedule F suggests that the discussions were more closely related to Arnold's management of the Arnold/ICM accounts or that the results experienced by the Arnold/ICM accounts are not attributable to Arnold, it is not reflective of the actual ICM practices for the period 1975–1980 included in the Chart.

3 See, Managing Educational Endowments, Report of the Committee on Endowment Management to the Ford Foundation, Educational Endowment Series (1969) (hereafter "Ford Foundation Report"). That report points out at pages 45–46 that "[i]n choosing between investment managers, primary emphasis should be placed on who the responsible individual will be, on what his record has been in the past, and on whether there is any reason to suppose he will not be able to do as well in the future."

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