

MAR 22 2002



02025738

NOTICE OF SALE OF SECURITIES PURSUANT TO REGULATION D, SECTION 4(6), AND/OR UNIFORM LIMITED OFFERING EXEMPTION

SEC USE ONLY
Prefix
Serial
DATE RECEIVED

Name of Offering (check if this is an amendment and name has changed, and indicate change.)

21-41384

Filing Under (Check boxes) that apply: Rule 504 Rule 505 Rule 506 Section 4(6) ULOE

Type of Filing: New Filing Amendment

A. BASIC IDENTIFICATION DATA

Enter the information requested about the issuer

Name of Issuer (check if this is an amendment and name has changed, and indicate change.)

Emergence Partners LP

Address of Executive Offices (Number and Street, City, State, Zip Code) Telephone Number (Including Area Code)
4 Hamilton Landing, Hangar 4, #205, Novato, CA 94949 (415) 315-1252

Address of Principal Business Operations (Number and Street, City, State, Zip Code) Telephone Number (Including Area Code)
(if different from Executive Offices)

Brief Description of Business

Trading and Investing in Securities

1170148

Type of Business Organization

- corporation limited partnership, already formed other (please specify):
business trust limited partnership, to be formed

PROCESSE

APR 11 2002

Actual or Estimated Date of Incorporation or Organization: Month Year Actual Estimated
0 2 0 2

Jurisdiction of Incorporation or Organization: (Enter two-letter U.S. Postal Service abbreviation for State: DE
CN for Canada; FN for other foreign jurisdiction)

THOMSON FINANCIAL

GENERAL INSTRUCTIONS

Federal:
Who Must File: All issuers making an offering of securities in reliance on an exemption under Regulation D or Section 4(6), 17 CFR 230.501 et seq. or 15 U.S.C. 77d(6).
When To File: A notice must be filed no later than 15 days after the first sale of securities in the offering. A notice is deemed filed with the U.S. Securities and Exchange Commission (SEC) on the earlier of the date it is received by the SEC at the address given below or, if received at that address after the date on which it is due, on the date it was mailed by United States registered or certified mail to that address.
Where to File: U.S. Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549.
Copies Required: Five (5) copies of this notice must be filed with the SEC, one of which must be manually signed. Any copies not manually signed must be photocopies of the manually signed copy or bear typed or printed signatures.
Information Required: A new filing must contain all information requested. Amendments need only report the name of the issuer and offering, any changes thereto, the information requested in Part C, and any material changes from the information previously supplied in Parts A and B. Part E and the Appendix need not be filed with the SEC.
Filing Fee: There is no federal filing fee.

State:
This notice shall be used to indicate reliance on the Uniform Limited Offering Exemption (ULOE) for sales of securities in those states that have adopted ULOE and that have adopted this form. Issuers relying on ULOE must file a separate notice with the Securities Administrator in each state where sales are to be, or have been made. If a state requires the payment of a fee as a precondition to the claim for the exemption, a fee in the proper amount shall accompany this form. This notice shall be filed in the appropriate states in accordance with state law. The Appendix to the notice constitutes a part of this notice and must be completed.

ATTENTION

Failure to file notice in the appropriate states will not result in a loss of the federal exemption. Conversely, failure to file the appropriate federal notice will not result in a loss of an available state exemption unless such exemption is predicated on the filing of a federal notice.

Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.

- Each promoter of the issuer, if the issuer has been organized within the past five years;
- Each beneficial owner having the power to vote or dispose, or direct the vote or disposition of, 10% or more of a class of equity securities of the issuer;
- Each executive officer and director of corporate issuers and of corporate general and managing partners of partnership issuers; and
- Each general and managing partner of partnership issuers.

Check Box(es) that Apply:  Promoter  Beneficial Owner  Executive Officer  Director  General and/or Managing Partner

Full Name (Last name first, if individual)

North Bay Technology Partners LLC

Business or Residence Address (Number and Street, City, State, Zip Code)

4 Hamilton Landing, Hangar 4, #205, Novato, CA 94949

Check Box(es) that Apply:  Promoter  Beneficial Owner  Executive Officer  Director  General and/or Managing Partner

Full Name (Last name first, if individual)

Lupatkin, Bruce M.

Business or Residence Address (Number and Street, City, State, Zip Code)

4 Hamilton Landing, Hangar 4, #205, Novato, CA 94949

Check Box(es) that Apply:  Promoter  Beneficial Owner  Executive Officer  Director  General and/or Managing Partner

Full Name (Last name first, if individual)

Business or Residence Address (Number and Street, City, State, Zip Code)

Check Box(es) that Apply:  Promoter  Beneficial Owner  Executive Officer  Director  General and/or Managing Partner

Full Name (Last name first, if individual)

Business or Residence Address (Number and Street, City, State, Zip Code)

Check Box(es) that Apply:  Promoter  Beneficial Owner  Executive Officer  Director  General and/or Managing Partner

Full Name (Last name first, if individual)

Business or Residence Address (Number and Street, City, State, Zip Code)

Check Box(es) that Apply:  Promoter  Beneficial Owner  Executive Officer  Director  General and/or Managing Partner

Full Name (Last name first, if individual)

Business or Residence Address (Number and Street, City, State, Zip Code)

Check Box(es) that Apply:  Promoter  Beneficial Owner  Executive Officer  Director  General and/or Managing Partner

Full Name (Last name first, if individual)

Business or Residence Address (Number and Street, City, State, Zip Code)

(Use blank sheet, or copy and use additional copies of this sheet, as necessary.)

Answer also in Appendix, Column 2, if filing under ULOE.

2. What is the minimum investment that will be accepted from any individual? ..... \$5,000,000  
 \*The minimum investment may be waived by the General Partner in its sole discretion
3. Does the offering permit joint ownership of a single unit? .....  Yes  No
4. Enter the information requested for each person who has been or will be paid or given, directly or indirectly, any commission or similar remuneration for solicitation of purchasers in connection with sales of securities in the offering. If a person to be listed is an associated person or agent of a broker or dealer registered with the SEC and/or with a state or states, list the name of the broker or dealer. If more than five (5) persons to be listed are associated persons of such a broker or dealer, you may set forth the information for that broker or dealer only..

Full Name (Last name first, if individual)

Business or Residence Address (Number and Street, City, State, Zip Code)

Name of Associated Broker or Dealer

States in Which Person Listed Has Solicited or Intends to Solicit Purchasers

(Check "All States" or check individual States) .....  All States

[AL]	[AK]	[AZ]	[AR]	[CA]	[CO]	[CT]	[DE]	[DC]	[FL]	[GA]	[HI]	[ID]
[IL]	[IN]	[IA]	[KS]	[KY]	[LA]	[ME]	[MD]	[MA]	[MI]	[MN]	[MS]	[MO]
[MT]	[NE]	[NV]	[NH]	[NJ]	[NM]	[NY]	[NC]	[ND]	[OH]	[OK]	[OR]	[PA]
[RI]	[SC]	[SD]	[TN]	[TX]	[UT]	[VT]	[VA]	[WA]	[WV]	[WI]	[WY]	[PR]

Full Name (Last name first, if individual)

Business or Residence Address (Number and Street, City, State, Zip Code)

Name of Associated Broker or Dealer

States in Which Person Listed Has Solicited or Intends to Solicit Purchasers

(Check "All States" or check individual States) .....  All States

[AL]	[AK]	[AZ]	[AR]	[CA]	[CO]	[CT]	[DE]	[DC]	[FL]	[GA]	[HI]	[ID]
[IL]	[IN]	[IA]	[KS]	[KY]	[LA]	[ME]	[MD]	[MA]	[MI]	[MN]	[MS]	[MO]
[MT]	[NE]	[NV]	[NH]	[NJ]	[NM]	[NY]	[NC]	[ND]	[OH]	[OK]	[OR]	[PA]
[RI]	[SC]	[SD]	[TN]	[TX]	[UT]	[VT]	[VA]	[WA]	[WV]	[WI]	[WY]	[PR]

Full Name (Last name first, if individual)

Business or Residence Address (Number and Street, City, State, Zip Code)

Name of Associated Broker or Dealer

States in Which Person Listed Has Solicited or Intends to Solicit Purchasers

(Check "All States" or check individual States) .....  All States

[AL]	[AK]	[AZ]	[AR]	[CA]	[CO]	[CT]	[DE]	[DC]	[FL]	[GA]	[HI]	[ID]
[IL]	[IN]	[IA]	[KS]	[KY]	[LA]	[ME]	[MD]	[MA]	[MI]	[MN]	[MS]	[MO]
[MT]	[NE]	[NV]	[NH]	[NJ]	[NM]	[NY]	[NC]	[ND]	[OH]	[OK]	[OR]	[PA]
[RI]	[SC]	[SD]	[TN]	[TX]	[UT]	[VT]	[VA]	[WA]	[WV]	[WI]	[WY]	[PR]

(Use blank sheet, or copy and use additional copies of this sheet, as necessary.)

already sold. Enter "0" if answer is "none" or "zero." If the transaction is an exchange offering, check this box  and indicate in the columns below the amounts of the securities offered for exchange and already exchanged.

Type of Security	Aggregate Offering Price	Amount Already Sold
Debt .....	\$ _____	\$ _____
Equity .....	\$ _____	\$ _____
<input type="checkbox"/> Common <input type="checkbox"/> Preferred		
Convertible Securities (including warrants) .....	\$ _____	\$ _____
Partnership Interests .....	\$ <u>100,000,000</u>	\$ _____
Other (Specify _____) .....	\$ _____	\$ _____
Total .....	\$ <u>100,000,000</u>	\$ _____

Answer also in Appendix, Column 3, if filing under ULOE.

2. Enter the number of accredited and non-accredited investors who have purchased securities in this offering and the aggregate dollar amounts of their purchases. For offerings under Rule 504, indicate the number of persons who have purchased securities and the aggregate dollar amount of their purchases on the total lines. Enter "0" if answer is "none" or "zero."

	Number Investors	Aggregate Dollar Amount of Purchases
Accredited Investors .....	_____	\$ _____
Non-accredited Investors .....	_____	\$ _____
Total (for filings under Rule 504 only) .....	_____	\$ _____

Answer also in Appendix, Column 4, if filing under ULOE.

3. If this filing is for an offering under Rule 504 or 505, enter the information requested for all securities sold by the issuer, to date, in offerings of the types indicated, in the twelve (12) months prior to the first sale of securities in this offering. Classify securities by type listed in Part C - Question 1.

Type of offering	Type of Security	Dollar Amount Sold
Rule 505 .....	_____	\$ _____
Regulation A .....	_____	\$ _____
Rule 504 .....	_____	\$ _____
Total .....	_____	\$ _____

4 a. Furnish a statement of all expenses in connection with the issuance and distribution of the securities in this offering. Exclude amounts relating solely to organization expenses of the issuer. The information may be given as subject to future contingencies. If the amount of an expenditure is not known, furnish an estimate and check the box to the left of the estimate.

Transfer Agent's Fees .....	<input type="checkbox"/>	\$ _____
Printing and Engraving Costs .....	<input checked="" type="checkbox"/>	\$ <u>5,000</u>
Legal Fees .....	<input checked="" type="checkbox"/>	\$ <u>15,000</u>
Accounting Fees .....	<input checked="" type="checkbox"/>	\$ <u>5,000</u>
Engineering Fees .....	<input type="checkbox"/>	\$ _____
Sales Commissions (specify finders' fees separately) .....	<input type="checkbox"/>	\$ _____
Other Expenses (identify) <u>Filing Fees</u> .....	<input checked="" type="checkbox"/>	\$ <u>5,000</u>
Total .....	<input checked="" type="checkbox"/>	\$ <u>40,000</u>

"adjusted gross proceeds to the issuer."

\$ 99,960,000

5. Indicate below the amount of the adjusted gross proceeds to the issuer used or proposed to be used for each of the purposes shown. If the amount for any purpose is not known, furnish an estimate and check the box to the left of the estimate. The total of the payments listed must equal the adjusted gross proceeds to the issuer set forth in response to Part C - Question 4.b above.

	Payments to Officers, Directors, & Affiliates	Payments To Others
Salaries and fees .....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
Purchase of real estate .....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
Purchase, rental or leasing and installation of machinery and equipment .....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
Construction or leasing of plant buildings and facilities .....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
Acquisition of other businesses (including the value of securities involved in this offering that may be used in exchange for the assets or securities of another issuer pursuant to a merger) .....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
Repayment of indebtedness .....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
Working capital .....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
Other (specify): <u>Purchase of Securities</u> .....	<input type="checkbox"/> \$ _____	<input checked="" type="checkbox"/> \$ 99,960,000
.....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
.....	<input type="checkbox"/> \$ _____	<input type="checkbox"/> \$ _____
Column Totals .....	<input type="checkbox"/> \$ _____	<input checked="" type="checkbox"/> \$ 99,960,000
Total Payments Listed (column totals added) .....	<input checked="" type="checkbox"/> \$ 99,960,000	

**D. FEDERAL SIGNATURE**

The issuer has duly caused this notice to be signed by the undersigned duly authorized person. If this notice is filed under Rule 505, the following signature constitutes an undertaking by the issuer to furnish to the U.S. Securities and Exchange Commission, upon written request of its staff, the information furnished by the issuer to any non-accredited investor pursuant to paragraph (b)(2) of Rule 502.

Issuer (Print or Type) Emergence Partners LP	Signature 	Date 3/20/02
By: North Bay Technology Partners LLC	Name of Signer (Print or Type) Bruce M. Lupatkin	Title of Signer (Print or Type) Managing Member

**ATTENTION**

Intentional misstatements or omissions of fact constitute federal criminal violations. (See 18 U.S.C. 1001.)

of such rule? .....

2 X

See Appendix, Column 5, for state response.

- 2. The undersigned issuer hereby undertakes to furnish to any state administrator of any state in which this notice is filed, a notice on Form D (17 CFR 239.500) at such times as required by state law.
- 3. The undersigned issuer hereby undertakes to furnish to the state administrators, upon written request, information furnished by the issuer to offerees.
- 4. The undersigned issuer represents that the issuer is familiar with the conditions that must be satisfied to be entitled to the Uniform limited Offering Exemption (ULOE) of the state in which this notice is filed and understands that the issuer claiming the availability of this exemption has the burden of establishing that these conditions have been satisfied.

The issuer has read this notification and knows the contents to be true and has duly caused this notice to be signed on its behalf by the undersigned duly authorized person.

Issuer (Print or Type) Emergence Partners LP By: North Bay Technology Partners LLC	Signature 	Date 3/20/02
Name (Print or Type) Bruce M. Lupatkin	Title (Print or Type) Managing Member	

*Instruction:*  
 Print the name and title of the signing representative under his signature for the state portion of this form. One copy of every notice on Form D must be manually signed. Any copies not manually signed must be photocopies of the manually signed copy or bear typed or printed signatures.

1 State	2 Intend to sell to non-accredited investors in State (Part B-Item 1)		3 Type of security and aggregate offering price offered in state (Part C-Item 1)	4 Type of investor and amount purchased in State (Part C-Item 2)				5 Disqualification under State ULOE (if yes, attach explanation of waiver granted) (Part E-Item 1)	
	Yes	No		Number of Accredited Investors	Amount	Number of Non-Accredited Investors	Amount	Yes	No
AL									
AK									
AZ									
AR									
CA									
CO									
CT									
DE									
DC									
FL									
GA									
HI									
ID									
IL									
IN									
IA									
KS									
KY									
LA									
ME									
MD									
MA									
MI									
MN									
MS									
MO									

1 State	2 Intend to sell to non-accredited investors in State (Part B-Item 1)		3 Type of security and aggregate offering price offered in state (Part C-Item 1)	4 Type of investor and amount purchased in State (Part C-Item 2)				5 Disqualification under State ULOE (if yes, attach explanation of waiver granted) (Part E-Item 1)	
	Yes	No		Number of Accredited Investors	Amount	Number of Non-Accredited Investors	Amount	Yes	No
MT									
NE									
NV									
NH									
NJ									
NM									
NY									
NC									
ND									
OH									
OK									
OR									
PA									
RI									
SC									
SD									
TN									
TX									
UT									
VT									
VA									
WA									
WV									
WI									
WY									
PR									



LIMITED PARTNERSHIP INTERESTS  
OF

# Emergence Partners LP

A Delaware Limited Partnership

Confidential Private Offering Memorandum

February 2002

THE SECURITIES OFFERED HEREBY HAVE NOT BEEN REGISTERED OR QUALIFIED FOR SALE UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), OR ANY STATE'S SECURITIES LAWS. THEY ARE OFFERED PURSUANT TO EXEMPTIONS FROM SUCH REGISTRATION AND QUALIFICATION. THIS MEMORANDUM HAS NOT BEEN FILED WITH OR REVIEWED BY THE SECURITIES AND EXCHANGE COMMISSION AND NEITHER THAT COMMISSION NOR ANY STATE SECURITIES ADMINISTRATOR HAS PASSED UPON OR ENDORSED THE MERITS OF AN INVESTMENT IN THE PARTNERSHIP OR THE ACCURACY OR THE ADEQUACY OF THE INFORMATION CONTAINED IN THIS MEMORANDUM. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE. THIS MEMORANDUM DOES NOT CONSTITUTE AN OFFER TO SELL OR A SOLICITATION OF AN OFFER TO BUY INTERESTS IN THE PARTNERSHIP IN ANY STATE OR JURISDICTION IN WHICH SUCH AN OFFER OR SOLICITATION IS UNLAWFUL.

LIMITED PARTNERSHIP INTERESTS ARE BEING OFFERED TO PERSONS WHO ARE "ACCREDITED INVESTORS" UNDER THE SECURITIES ACT AND REGULATION D PROMULGATED THEREUNDER AND "QUALIFIED CLIENTS" UNDER RULE 205-3 PROMULGATED UNDER THE INVESTMENT ADVISERS ACT OF 1940, AS AMENDED. LIMITED PARTNERSHIP INTERESTS ARE BEING OFFERED TO ELIGIBLE PURCHASERS WITH A MINIMUM CAPITAL CONTRIBUTION OF \$5,000,000, WHICH THE GENERAL PARTNER MAY REDUCE IN ITS SOLE DISCRETION.

AN INVESTMENT IN THIS LIMITED PARTNERSHIP INVOLVES A SIGNIFICANT RISK OF LOSS. See "INVESTMENT RISK FACTORS."

Memorandum No. \_\_\_\_\_

Recipient's Name \_\_\_\_\_

This Confidential Private Offering Memorandum is being given to the recipient solely for the purpose of his or her evaluation of an investment in the limited partnership interests described herein. It may not be reproduced or distributed to anyone else (other than the identified recipient's professional advisers). The recipient, by accepting delivery of this Memorandum, agrees to return it and all related documents to the General Partner if the recipient does not subscribe for a limited partnership interest.

### **NORTH BAY TECHNOLOGY PARTNERS LLC**

Hangar 4, Suite 205  
4 Hamilton Landing  
Novato, CA 94949  
415.315.1252 (T)  
415.315.1253 (F)

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## INTRODUCTION

This Memorandum relates to an offering of limited partnership interests (the "Interests") by Emergence Partners LP, a Delaware limited partnership (the "Partnership"), to a limited number of sophisticated long-term investors. The minimum capital contribution to the Partnership is \$5,000,000, which the General Partner may reduce in its sole discretion.

North Bay Technology Partners LLC, a Delaware limited liability company, will serve as the general partner (the "General Partner") of the Partnership with responsibility for providing to the Partnership investment advice and management. The Interests are offered subject to the right of the General Partner, in its sole discretion, to reject any subscription in whole or in part.

The Partnership will seek to generate significant long-term capital appreciation by investing in "orphan" companies that the General Partner believes hold the potential to emerge as future leaders in dynamically expanding areas within technology. The types of companies the Partnership will typically invest in are those that are currently being ignored by traditional Wall Street interests owing to the collapse of technology stock valuations coming off the tech spending and IPO bubble of 1999 and early 2000. The Partnership's holdings will consist principally, but not solely, of equity and equity-related securities of technology companies that prematurely went public during this financing bubble. The Partnership's strategy can therefore be characterized as public venture investing in that the analytical discipline required to assess successfully these companies is similar to that required to evaluate a venture-stage company. Although common stocks of companies listed on U.S. securities exchanges or traded on the over-the-counter market will be the Partnership's primary investment vehicles, preferred stocks, convertible securities, warrants, options, derivatives, bonds and other fixed income securities, securities of non-U.S. issuers, and money market instruments may also be owned or shorted when the General Partner believes such investments would be advantageous to the Partnership. The Partnership may engage in short selling and may utilize options, options on stock indices, derivatives, financial instruments and other securities both to capture the potential for growth and manage the Partnership's risk by hedging the Partnership's portfolio. The Partnership will not employ leverage in its investment program.

THIS MEMORANDUM HAS NOT BEEN FILED WITH OR REVIEWED BY THE SECURITIES AND EXCHANGE COMMISSION. IN MAKING AN INVESTMENT DECISION INVESTORS MUST RELY ON THEIR OWN EXAMINATION OF THE PERSON OR ENTITY CREATING THE SECURITIES AND THE TERMS OF THE OFFERING, INCLUDING THE MERITS AND RISKS INVOLVED. THESE LIMITED PARTNERSHIP INTERESTS HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS DOCUMENT. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THESE LIMITED PARTNERSHIP INTERESTS ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER THE SECURITIES ACT AND APPLICABLE STATE SECURITIES LAWS, PURSUANT TO REGISTRATION OR EXEMPTION THEREFROM. INVESTORS SHOULD BE AWARE THAT THEY WILL BE REQUIRED TO BEAR THE FINANCIAL RISKS OF THIS INVESTMENT FOR AN INDEFINITE PERIOD OF TIME.

NO REPRESENTATIONS OR WARRANTIES OF ANY KIND ARE MADE OR INTENDED, AND NONE SHOULD BE INFERRED, WITH RESPECT TO THE ECONOMIC RETURN OR THE TAX CONSEQUENCES FROM AN INVESTMENT IN THE PARTNERSHIP. NO ASSURANCE CAN BE GIVEN THAT EXISTING LAWS WILL NOT BE CHANGED OR INTERPRETED ADVERSELY. PROSPECTIVE INVESTORS ARE NOT TO CONSTRUCT THIS MEMORANDUM AS LEGAL OR TAX ADVICE. EACH INVESTOR SHOULD CONSULT HIS OWN COUNSEL AND

ACCOUNTANT FOR ADVICE CONCERNING THE VARIOUS LEGAL, TAX AND ECONOMIC MATTERS CONCERNING HIS INVESTMENT.

NO OFFERING LITERATURE OR ADVERTISING IN ANY FORM SHALL BE EMPLOYED IN THE OFFERING OF THESE LIMITED PARTNERSHIP INTERESTS EXCEPT FOR THIS MEMORANDUM AND THE EXHIBITS ATTACHED HERETO. NO PERSON OTHER THAN THE GENERAL PARTNER HAS BEEN AUTHORIZED TO MAKE REPRESENTATIONS, OR GIVE ANY INFORMATION, WITH RESPECT TO THESE LIMITED PARTNERSHIP INTERESTS, EXCEPT THE INFORMATION CONTAINED HEREIN, AND ANY INFORMATION OR REPRESENTATION NOT EXPRESSLY CONTAINED HEREIN OR OTHERWISE SUPPLIED BY THE GENERAL PARTNER IN WRITING MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY THE PARTNERSHIP OR ANY OF ITS PARTNERS. ANY FURTHER DISTRIBUTION OR REPRODUCTION OF THIS MEMORANDUM, IN WHOLE OR IN PART, OR THE DIVULGENCE OF ANY OF ITS CONTENTS, IS PROHIBITED.

A PROSPECTIVE INVESTOR SHOULD NOT SUBSCRIBE FOR LIMITED PARTNERSHIP INTERESTS UNLESS SATISFIED THAT HE AND/OR HIS REPRESENTATIVE HAS ASKED FOR AND RECEIVED ALL INFORMATION WHICH WOULD ENABLE HIM TO EVALUATE THE MERITS AND RISKS OF THE PROPOSED INVESTMENT.

THE PARTNERSHIP SHALL MAKE AVAILABLE TO EACH INVESTOR OR HIS AGENT, DURING THIS OFFERING AND PRIOR TO THE SALE OF ANY INTERESTS, THE OPPORTUNITY TO ASK QUESTIONS OF AND RECEIVE ANSWERS FROM ANY PERSON AUTHORIZED TO ACT ON BEHALF OF THE PARTNERSHIP CONCERNING ANY ASPECT OF THE PARTNERSHIP AND ITS PROPOSED BUSINESS AND TO OBTAIN ADDITIONAL INFORMATION, TO THE EXTENT THE PARTNERSHIP POSSESSES SUCH INFORMATION OR CAN ACQUIRE IT WITHOUT UNREASONABLE EFFORT OR EXPENSE.

## SUMMARY OF THE OFFERING

The following is only a summary of the information contained in this Memorandum. It is qualified in its entirety by the remainder of this Memorandum, including the Partnership's Agreement of Limited Partnership (the "*Partnership Agreement*") and the other exhibits to this Memorandum. Prospective investors should consult their own advisers as to the consequences of an investment in the Partnership.

**Partnership and General Partner** Emergence Partners LP (the "*Partnership*") is a Delaware limited partnership, formed in February of 2002. Its sole general partner is North Bay Technology Partners LLC, a Delaware limited liability company (the "*General Partner*"). The General Partner has sole and complete authority to manage the Partnership's activities.

**Investment Objectives** The Partnership will seek to generate significant long-term capital appreciation by investing in "orphan" companies that the General Partner believes hold the potential to emerge as future leaders in dynamically expanding areas within technology. The types of companies the Partnership will typically invest in are those that are currently being ignored by traditional Wall Street interests owing to the collapse of technology stock valuations coming off the tech spending and IPO bubble of 1999 and early 2000.

The Partnership's investments in equity securities will focus primarily on common stocks and may include securities issued by foreign as well as domestic companies. The Partnership may engage in short selling and may utilize options, derivatives and other financial instruments and securities both to capture the potential for growth and manage the Partnership's risk by hedging its portfolio.

**The Offering** The Partnership is offering up to \$100 million of limited partnership interests ("*Interests*") to investors who meet the definitions of (1) "Accredited Investors" under Regulation D under the Securities Act, and (2) "Qualified Clients" under Rule 205-3 under the Investment Adviser Act of 1940, as amended (the "Advisers Act"). The minimum initial investment is \$5,000,000. The General Partner may waive or reduce certain of these requirements in particular cases. The offering will continue until the General Partner suspends or terminates it. Limited Partners will be admitted as of the first day of each calendar quarter or more frequently, in the General Partner's discretion.

**Liquidity** Limited Partners generally may withdraw all or part of their capital on 60 days notice as of the end of any calendar quarter following the third anniversary of their admission to the Partnership, or at such other times as the General Partner, in its sole discretion, shall determine. Payment on withdrawals generally will be made within 30 days after the effective date of withdrawal, although 10% of any withdrawal that represents more than 90% of a Limited Partner's capital may be withheld

until completion of the Partnership's year-end financial statements for the year in which the withdrawal occurs. Withdrawals may be made in any combination of cash and securities, in the General Partner's sole discretion. Transaction costs involved in a withdrawal may be charged to the withdrawing Partner.

The General Partner may withhold payment of all or any part of the amount withdrawn by a Limited Partner to establish such reserves for contingencies as the General Partner, in its sole discretion, may deem advisable.

The General Partner may, in its sole discretion, terminate for any reason the interests of any Limited Partner in the Partnership at any time, upon notice to such Limited Partner. A Limited Partner whose Interest is terminated by the General Partner shall be treated as a withdrawing Limited Partner as of the termination date.

**Fees and Other  
Expenses**

For the General Partner's services in managing the Partnership's investments and other affairs, the General Partner receives a Management Fee at a rate of 0.50% per quarter of the balance in each Limited Partner's Capital Account. The Management Fee is calculated and paid quarterly in advance based on the balance in the Limited Partners' Capital Accounts on the first day of each quarter.

The Partnership will pay (or reimburse the General Partner for) (a) all reasonable expenses related to the Partnership's organization, including, but not limited to, legal and accounting fees, government filing fees, and other expenses of the offering of Interests in the Partnership, (b) any reasonable legal, accounting and audit fees and expenses, including those associated with regulatory compliance matters and investigating potential investments or maximizing return on existing investments and (c) reasonable custodial fees, interest on borrowed funds, transfer taxes, brokerage commissions, fees and expenses for consulting, the cost of business travel related to the Partnership, research and statistical services and any extraordinary expenses such as litigation expenses. The organizational expenses of the Partnership may be amortized over a period of 60 months. If the organizational expenses of the Partnership are considered material, their amortization may result in the Partnership receiving a qualified audit report. The General Partner will pay all other expenses related to the administration of the Partnership, including, but not limited to, salaries of employees, supplies, office space and administrative services. The Partnership may use "soft" dollar commissions or rebates of commissions generated by the payment of brokerage commissions by the Partnership to pay for research and brokerage services within the "safe harbor" provided by Section 28(e) of the Securities Exchange Act of 1934.

**Incentive Allocation** In addition to its proportionate share of Net Profits and Net Losses based on its Capital Account balance, the General Partner receives an Incentive Allocation equal to 20% of the Net Profits (realized and unrealized) allocated to each Limited Partner's Capital Account for the applicable fiscal period

The Incentive Allocation of Net Profits to the General Partner is subject to a loss carryforward limitation (or "high-water mark"), so that no Incentive Allocation is made to the General Partner until prior Net Losses allocated to the Limited Partners are recouped. The Incentive Allocation of Net Profits to the General Partner shall be adjusted to take into account any distributions to, or withdrawals by a Limited Partner, with the amount of prior Net Losses that must be offset before an Incentive Allocation is made to the General Partner being reduced in proportion to the distribution or withdrawal. Incentive Allocations are generally made at the end of each calendar year and when a Limited Partner withdraws. Once made, Incentive Allocations will not be reversed, even if a Limited Partner experiences Net Losses in subsequent periods.

**Allocations of Profits and Losses** Net Profits or Net Losses of the Partnership, which include unrealized appreciation or depreciation in the Partnership's investments and realized investment gains or losses and income and expense, will generally be allocated at the end of each fiscal period among the Capital Accounts maintained for the Partners in proportion to the relative values of such Capital Accounts at the beginning of such fiscal period, except for the Incentive Allocation of Net Profits to the General Partner, as described above.

**Sales Commissions** There will be no sales commissions charged on sales of Interests. The General Partner may make payments to third parties for providing marketing services to the Partnership, assisting in the maintenance of investor relations, and performing related services; provided, however, that such payments will not be borne by the Partnership. Compensation paid to such third parties will generally be made by payment of a portion of the fees or allocations received by the General Partner.

**Admission of New Partners** Limited Partners may be admitted to the Partnership at such times as the General Partner in its sole discretion shall determine.

**Distributions** The General Partner may, in its sole discretion, make distributions in cash or in kind (a) in connection with a withdrawal of capital from the Partnership by a Partner and (b) at any time to all the Partners on a pro rata basis in accordance with the Partners' Partnership percentages. At the request of the Limited Partners, the General Partner will make annual tax distributions sufficient to cover tax liabilities associated with realized gains allocated to the Limited Partners, otherwise it is the intention of the General Partner not to distribute the

current income of the Partnership.

<b>Term</b>	The Partnership shall continue through December 31, 2032, unless terminated earlier at the election of the General Partner.
<b>Reports</b>	Each Partner will receive annual audited financial statements and periodic summaries of the Partnership's performance plus copies of his or her Schedule K-1 to the Partnership's tax return.
<b>Special Risks</b>	An investment in the Interests should be viewed as a non-liquid investment that involves a high degree of risk. A subscription to purchase Interests should be considered only by investors who have carefully read this Memorandum.
<b>Conflicts of Interest</b>	The Partnership is subject to various conflicts of interest arising out of its relationship with the General Partner. The General Partner, its members and affiliates may engage in all manner of other activities, including acting as investment adviser to other persons, entities or accounts, some of which may have the same or similar investment objectives as the Partnership.
<b>Regulation Matters</b>	The Partnership is not presently, and does not intend in the future to become, registered as an investment company under the Investment Company Act of 1940, as amended and therefore will not be required to adhere to certain investment policies under such act. The General Partner is registered as an investment adviser under the laws of the State of California.
<b>Tax Status of the Partnership</b>	The Partnership will be classified as a partnership for federal income tax purposes, with the result that no federal income tax will be paid by the Partnership as an entity. Instead, each Limited Partner will be required to report on his federal income tax return his allocable share of the income, gains, losses, deductions and credits of the Partnership, whether or not any actual distribution is made to such Limited Partner during his taxable year. For a detailed discussion of the federal income tax consequences of an investment in the Partnership, see "Certain Federal Income Tax Consequences" below.
<b>ERISA and Other Tax-Exempt Entities:</b>	Entities subject to the Employee Retirement Income Security Act of 1974, as amended ("ERISA") and other tax-exempt entities may purchase Interests. However, investment in the Partnership by such entities requires special consideration. Since the Partnership does not intend to utilize leverage, tax-exempt Limited Partners should not realize any "debt financed income" and thus should not incur an income tax liability with respect to "unrelated business taxable income" as a consequence of investing in the Partnership. Trustees or administrators of such entities should consult their own legal and tax advisers.
<b>Additional Information</b>	Prospective Limited Partners are invited and strongly recommended to meet with the General Partner for a further explanation of the terms and conditions of this Offering and to

obtain any additional information necessary to verify the information contained in this Memorandum, to the extent the General Partner possesses such information or can acquire it without unreasonable effort or expenses. Requests for such information should be directed to the General Partner, North Bay Technology Partners LLC, Hangar 4, Suite 205, 4 Hamilton Landing, Novato, California 94111, Attn: Theodore J. Lucas, telephone: (415) 315-1252.

## USE OF PROCEEDS

The entire net Proceeds from the sale of the Interests will be invested for the account of the Partnership. The Partnership will pay or reimburse the General Partner all organizational and syndication expenses incurred by the General Partner pertaining to the sale of the Interests.

## INVESTMENT OBJECTIVE AND STRATEGY

### General

The Partnership will seek to generate significant long-term capital appreciation by investing in "orphan" companies that the General Partner believes hold the potential to emerge as future leaders in dynamically expanding areas within technology.

The Partnership's holdings will typically - but not exclusively - represent select technology companies that prematurely went public during the IPO bubble of 1999/2000. Many of the companies from the tech IPO bubble are currently trading at valuations that suggest their demise due to inferior business models and technology, a lack of end-user demand and skepticism concerning the availability of external financing prior to profitability. Among this universe, however, are companies with both tangible and intangible assets (e.g., intellectual property, technology, brand, access to distribution channels, management team, balance sheet viability, etc.) that provide the basis for not only survival, but to ultimately become highly profitable, market-leading companies. The General Partner believes that identifying and investing in select companies in the context of the current market environment - where the market has indiscriminately destroyed valuations for smaller tech companies across the board - provides an opportunity to generate significant capital growth over the next three to five years.

The General Partner's approach will be one of public venture investing, based on similarities between the inherent return potential of the strategy and the analytical discipline required to successfully evaluate and manage a portfolio of these companies versus that of a venture capital fund.

### Investment Opportunity

Sixty-one percent of all IPO financing in technology over the last 20 years occurred between 1998 and 2000. In this same period, approximately 80% of all the venture capital funding over the last 20 years occurred. The euphoria in the market and investors' demand for tech IPOs caused underwriting standards to slip to an all-time low and many companies requiring more extensive venture-stage incubation went public prematurely. As of year-end 2002, less than 17% of all tech IPOs from 1998 to 2000 were trading above their offering price. Based on experience through technology cycles over the last 20 years, the General Partner believes that investing in select "orphan" companies following a boom-bust cycle presents the opportunity for significant returns.

The essence of the Partnership's strategy is to identify and own the select emerging tech companies that will drive the next cycle of market capitalization creation. The current valuation environment for smaller tech companies provides an opportunity to do this at price entry points with extremely favorable risk/return characteristics.

There are over 1,500 publicly-traded technology companies in the U.S., the majority of which are under \$1 billion in market capitalization. Coverage by Wall Street research analysts (earnings estimates, buy/sell recommendations) is limited to less than half this universe, leading to substantial inefficiencies in the pricing of the majority of tech stocks. Of the minority of tech stocks covered by Wall Street, the conflict of interest inherent in trying to win underwriting business severely restricts analysts from stating a negative view on the companies they cover.

At year-end 2001, major technology-focused indices were between 60% and 80% lower than their March 2000 highs (this takes into account the sharp rally in Q4 2001). The cap-weighted nature of most tech indices (and attending emphasis on large cap names) obscures the deep damage beyond the largest technology companies. As of month-end September 2001, more than 80% of all US public technology companies were trading more than 90% off highs of early 2000.

Unprecedented across-the-board valuation compression among tech companies outside of the top-50 largest market cap names provides a distinct opportunity for investors that can discern between real businesses and hype.

It is critical to contrast the culmination of speculative sentiment in March 2000 (when unprecedented valuation levels for technology stocks left little room for potential upside, but the same unrealistic growth expectations that drove valuation excesses set the stage for substantial potential downside) against conditions today. Current valuations suggest an inversion of risk and return characteristics and offer a much more fertile environment for selectively building a long portfolio that houses substantial mid- to long-term return potential. This is particularly true of smaller to mid-cap tech companies that have suffered the greatest price deterioration. In other words, the General Partner believes there is more potential upside among select emerging technology companies than there was during the market's peak in early 2000, and significantly less downside risk.

The General Partner believes that the current lack of risk capital and depressed valuation environment among smaller technology companies sets the stage for substantial wealth creation for investors who are equipped with an informational advantage and are willing to take risk.

### **Investment Criteria**

The General Partner's investment process begins with a conceptual framework identifying industry-wide changes prompted by emerging end markets. This framework is utilized to identify the sectors and themes - and companies within these areas - that present the greatest potential for growth. In evaluating specific companies for investment, the General Partner utilizes a structured and detailed bottoms-up research process that involves analyzing the prospects and business models of specific companies, including discussions with management, competitors and suppliers in an effort to better understand how specific firms may be positioned. Investment criteria used by the General Partner will include the following:

- ◆ *Market Opportunity.* Significant and rapidly growing market opportunity fitting with the General Partner's overall framework of macro trends in technology and evolution in end-market demand.
- ◆ *Balance Sheet.* Financial condition and operational sustainability - high confidence that current financial resources provide adequate runway and a buffer to the period in the future that the company becomes cash flow positive if not already the case.
- ◆ *Technology.* Technical viability of the company's product set: architectural robustness, intellectual property, ability to create user lock-in, potential network effects, forward-looking product / R&D pipeline, fit with emerging protocols and standards, interoperability, strength of value proposition to end user, current and future potential competitive threats, etc.
- ◆ *Management and Strategic Framework.* Strong leadership with track record and clear roadmap of how to capture opportunities available to the company and create and sustain profitability and defend its market position.

- ◆ *Distribution Platform* A strong and effective distribution platform with multiple channels as evidenced by current client base, historical growth and client pipeline; evolving brand value.
- ◆ *Catalysts*. To trigger investment, catalysts must exist that can unlock value in the short-term. These can include accelerating revenue/earnings growth, initiation of analyst coverage, new product introductions, major client acquisitions/licensing deals/partnerships, mergers, etc.

### **Portfolio Structure and Risk Parameters**

The General Partner anticipates that the core long portfolio of the Partnership will consist of between 25 to 50 positions, with a gross exposure of between 25% to 100%. Long positions at initiation will not exceed 5% of the Partnership's portfolio and short positions at initiation will not exceed 2%. The Partnership's maximum single position exposure will not exceed 15%. The Partnership's position size in a company expressed as a percentage of the average daily trading volume for the company over the prior three months generally will not be more than 50 percent, and its position size as a percentage of the company's total market capitalization generally will not be more than 10 percent.

The Partnership's investments will consist primarily of common stocks of companies listed on U.S. securities exchanges or traded on the over-the-counter market. However, the Partnership may invest in all manner of other securities, including, but not limited to, preferred stocks, convertible securities, warrants, options and derivatives such as swaps, caps, collars and floors, and may invest in the securities of non-U.S. issuers. Cash balances which are not committed to the Partnership's investment program normally are invested in prime quality short-term debt instruments of public or private issuers, in "money-market" mutual funds having portfolios consisting primarily of such debt instruments or in an account which earns interest at prevailing short-term rates. The Partnership may also invest in convertible bonds, corporate bonds, government debt and other fixed income instruments.

While the General Partner typically will try to minimize risk in selecting investments, it should be understood that the risk management techniques which may be utilized by the General Partner cannot provide any assurance that the Partnership will not be exposed to risks of significant investment losses.

The Partnership may from time to time lend securities from its portfolio to brokers, dealers and financial institutions and receive collateral in the form of cash or securities in an amount at least equal to the current market value of the loaned securities. Such lending of the Partnership's securities is designed to enhance the total return of the Partnership.

The Partnership will not utilize leverage in its investment program. However, the Partnership may "borrow" securities to effect short sales using margin accounts. The Partnership may thus be "leveraged" in the sense that the market value of its short positions could exceed its equity.

THE PARTNERSHIP'S INVESTMENT PROGRAM IS SPECULATIVE AND ENTAILS SUBSTANTIAL RISKS. MARKET RISKS ARE INHERENT IN ALL SECURITIES TO VARYING DEGREES. NO ASSURANCE CAN BE GIVEN THAT THE PARTNERSHIP'S INVESTMENT OBJECTIVE WILL BE REALIZED.

THE DESCRIPTIONS CONTAINED HEREIN OF SPECIFIC ACTIVITIES WHICH MAY BE ENGAGED IN BY THE PARTNERSHIP SHOULD NOT BE CONSTRUED AS IN ANY WAY LIMITING THE PARTNERSHIP'S INVESTMENT ACTIVITIES. THE PARTNERSHIP MAY ENGAGE IN INVESTMENT ACTIVITIES NOT DESCRIBED HEREIN WHICH THE GENERAL PARTNER CONSIDERS APPROPRIATE.

## MANAGEMENT OF THE PARTNERSHIP; PORTFOLIO MANAGER

The General Partner of the Partnership is North Bay Technology Partners LLC, a Delaware limited liability company registered as an investment adviser under the laws of the State of California. The General Partner is responsible for the management of the Partnership's portfolio and for the day-to-day operation of the Partnership.

In making its investment decisions for the Partnership, the General Partner will rely primarily on Bruce M. Lupatkin, the principal of the General Partner. Mr. Lupatkin will serve as the portfolio manager of the Partnership and, as such, will have direct and primary responsibility for all investment decisions of the Partnership. Mr. Lupatkin will be assisted in the investment process by an Investment Committee comprised of Charles R. Schwab, Jr. and Theodore J. Lucas.

### **Bruce M. Lupatkin** **Portfolio Manager and Member of Investment Committee**

Mr. Lupatkin is the principal of the General Partner. In that capacity, he has served as the Portfolio Manager of North Bay One, L.P. since 1998 and as the Portfolio Manager of MCP North Bay Technology Master Fund, Ltd., a hedged technology strategy focused on emerging leaders in technology and communications infrastructure, since 2001.

Mr. Lupatkin was formerly Director of Research for Hambrecht & Quist (H&Q) a major bracket investment banking firm specializing in technology, life sciences, branded consumer and services companies. Mr. Lupatkin was the Director of Research and Technology Strategist for H&Q from 1994 to 1998. From 1992 to 1994, Mr. Lupatkin was co-director of Research and Technology Strategist (responsible for the technology, consumer and services segments of the H&Q research department). Mr. Lupatkin served on H&Q's Commitment Committee (the group responsible for selecting the underwriting and private placement commitments made by H&Q), as well as the firm's Operating Committee (the group responsible for all management facets of H&Q). From 1984 to 1992, Mr. Lupatkin was a leading technology analyst for H&Q covering a wide array of industry groups, including defense electronics, the personal computer industry and the enterprise software industry. Prior to at H&Q, Mr. Lupatkin was a technology analyst at Boettcher & Co., a regional investment banking boutique, and a Systems Engineer at IBM.

Mr. Lupatkin holds a BA from the University of Michigan and an MBA from the University of Texas.

### **Charles R. Schwab, Jr.** **Member, Investment Committee**

Mr. Schwab, Jr. has been managing proprietary capital for over 12 years on an institutional basis as well as more recently on behalf of the Charles Schwab family. Since 1998 he has been managing the private venture investments of the family primarily through Chess Ventures, LLC and its predecessor, the Kensington Value Fund. The investment focus of these funds has principally centered around providing capital to high growth emerging companies. From 1994 to 1998 Mr. Schwab, Jr. managed family and external capital in a fund that involved a variety of arbitrage strategies. Between 1990 and 1994, Mr. Schwab, Jr. worked for Banque Paribas in both London and New York. While at this institution, he was a Vice President in the High Yield and Equity Arbitrage Group. The group's investment strategies included distressed investing, capital structure arbitrage, merger arbitrage, spin-offs and recapitalizations. Prior to Banque Paribas, he worked with Continental Bank, now part of Bank of America, as part of the team whose responsibilities included sales and trading of short-term debt instruments.

Mr. Schwab, Jr. currently serves on numerous boards, including Integration Associates, a semiconductor company that designs custom analog ASIC solutions, and Digital Persona, a network and enterprise hardware security company.

Mr. Schwab, Jr. earned a BA in Economics and History from Northwestern University and an MBA in Finance from the University of Chicago Graduate School of Business.

**Theodore Lucas**  
**Member, Investment Committee**

Mr. Lucas is a principal of MCP Chess Group LLC, a multi-strategy investment management firm. He was formerly a Director of Mint Investment Management Company LLC, an affiliate of ED&F Man Group PLC, which manages over U.S. \$5 billion in alternative strategy assets. Previously, Mr. Lucas was a Director of BZW and Barclays Capital Group, working in capital markets and corporate finance, and a Vice President of Lehman Brothers in New York, where he worked in the investment banking group. Mr. Lucas began his career at NYNEX (now Verizon) on the acquisition team for the wireless network business. In these various roles, Mr. Lucas developed extensive experience in valuation, financing and risk management.

Mr. Lucas holds a BA in Economics and Business Administration from Gordon College in Wenham, Massachusetts and attended the Executive Program at Columbia University.

Pursuant to the Partnership Agreement, the General Partner does not have to devote its full time to the business of the Partnership and the principal of the General Partner will devote as much time to the business of the Fund as he, in his sole discretion, deems advisable. In addition, the General Partner has the right, without the consent of the Limited Partners, to admit additional General Partners at the commencement of any calendar quarter or any other times as the General Partner determines. The Limited Partners do not have any right to participate in the management of the Partnership and have limited voting rights.

#### **BROKERAGE PRACTICES**

In the course of the Partnership's investment activities the Partnership may incur substantial brokerage commissions and other transaction expenses. The General Partner has complete discretion in deciding what brokers and dealers the Partnership will use and in negotiating rates of brokerage compensation. In addition to using brokers as "agents" and paying commissions, the Partnership may buy or sell securities directly from or to dealers acting as principals at prices that include markups or markdowns.

#### **Best Execution**

In choosing brokers and dealers, the General Partner will not be required to consider any particular criteria. The General Partner will seek the best combination of brokerage expenses and execution quality but, as discussed below, the General Partner is not required to select the broker or dealer that charges the lowest transaction cost, even if that broker provides execution quality comparable to other brokers or dealers. In evaluating "execution quality," historical net prices (after markups, markdowns or other transaction-related compensation) on other transactions will be a principal factor, but other factors will also be relevant, including: the execution, clearance, and settlement and error correction capabilities of the broker or dealer generally and in connection with securities of the type and in the amounts to be bought or sold; the broker's or dealer's willingness to commit capital; reliability and financial stability; the size of the transaction; availability of securities to borrow for short sales; and the market for the security.

**"Research."** Under Section 28(e) of the Securities Exchange Act of 1934, the General Partner's use of the Partnership's commission dollars to acquire "research" products and services is not a breach of the General Partner's fiduciary duty to the Partnership--even if the brokerage commissions paid are not the lowest available--as long as (among other requirements) the General Partner determines that the commissions are reasonable in relation to the value of the brokerage services and the "research" acquired. For these purposes, "research" means services or products used to provide lawful and appropriate assistance to the General Partner in making investment decisions for all of its clients. The types of "research" the General Partner may acquire include: research reports on or other information about particular companies or industries; economic surveys and analyses; recommendations as to specific securities; financial publications; portfolio evaluation

services; financial database software and services; computerized news and pricing services; quotation equipment and other computer hardware for use in running software used in investment decision making; investment conferences; and other products or services that may enhance the General Partner's investment decision making. Section 28(e)'s "safe harbor" applies to the use of Partnership "soft dollars" even when the "research" acquired is used in making investment decisions for the General Partner's clients other than the Partnership.

The "safe harbor" is not available where the transactions that compensate a broker-dealer for "research" services or products are effected on a principal basis, with a markup or markdown paid to the broker-dealer (e.g., in transactions with market makers).

The General Partner intends generally to consider the amount and nature of research, execution and other brokerage services provided by brokers as well as the extent to which such services are relied on, and attempt to allocate a portion of the brokerage business of the Partnership and the other accounts it manages or advises on the basis of that consideration. The investment information received from brokers, however, may be used by the General Partner, its affiliates or principals in servicing other accounts, but not all such information may be used by the General Partner in connection with the Partnership. The General Partner believes that such an allocation of brokerage business helps the Partnership to obtain research and execution capabilities and provides other benefits to the Partnership.

### **Aggregation of Orders**

The General Partner may aggregate sale and purchase orders of securities held by the Partnership with similar orders being made simultaneously for other accounts or entities if, in the General Partner's reasonable judgment, such aggregation is reasonably likely to result in an overall economic benefit to the Partnership based on an evaluation that the Partnership is benefitted by relatively better purchase or sale prices, lower commission expenses or beneficial timing of transactions, or a combination of these and other factors. In many instances, the purchase or sale of securities for the Partnership will be effected simultaneously with the purchase or sale of like securities for such other accounts or entities. Such transactions may be made at slightly different prices, due to the volume of securities purchased or sold. In such event, the average price of all securities purchased or sold in such transactions may be determined, and at the General Partner's sole discretion, the Partnership may be charged or credited, as the case may be, the average transaction price.

### **Prime Brokerage, Custody, Clearing and Settling**

The Partnership obtains custodial, clearing, and related services through what is known as a "prime brokerage" arrangement. Under such an arrangement, a single brokerage firm (the "*Prime Broker*") maintains custody of the Partnership's assets (either directly or through its clearing brokerage firm), provides margin credit and locates securities to borrow to facilitate short sales, and provides related services, but allows the Partnership to use other broker-dealers to execute transactions. This permits the General Partner to seek valuable research and to compare execution quality and commission rates, while maintaining only one custodial relationship. And by using a brokerage firm the Partnership may avoid paying custodial fees that banks charge other institutional investors. The Prime Broker is compensated through interest on credit balances, margin borrowings, stock loans, and brokerage commissions. Under such an arrangement, the Prime Broker, among other things, (i) arranges for the receipt and delivery of securities bought, sold, borrowed, and lent; (ii) makes and receives payments for securities; (iii) maintains custody of cash and securities; (iv) delivers cash to the Partnership's bank accounts; (v) tenders securities in connection with tender offers, exchange offers, mergers, or other corporate reorganizations; and (vi) provides detailed portfolio and related reports.

The Fund's Prime Broker is Morgan Stanley & Co. The General Partner may change the Partnership's Prime Broker, alter the terms of the Partnership's arrangements with the Prime Broker, or make alternative arrangements to receive the services currently provided by the Prime Broker, all in the General Partner's absolute discretion.

## Disbursement Procedures

As a safekeeping measure, the Partnership will agree with its Prime Broker as to specific procedures the General Partner must follow in order to be paid its Management Fee, withdraw capital from the Partnership, or be reimbursed for expenses it has paid on behalf of the Partnership. Under such an agreement, the Prime Broker may not transfer any Partnership assets to the General Partner or its affiliates for any reason until the Partnership's "independent representative" has provided a letter directly to the Prime Broker confirming that it has performed certain procedures to verify that the calculation of the Management Fee conforms to the Partnership Agreement and is mathematically accurate, and, for proposed withdrawals of capital, that the amount to be withdrawn is less than the withdrawing partner's capital account balance. Kathryn Yulish, a certified public accountant with offices at 2 Turquoise Way, San Francisco, California 94131, will serve as the independent representative. The Partnership, acting through the General Partner may change the independent representative at any time by written notice to the Prime Broker.

### CUSTODY OF THE PARTNERSHIP'S ASSETS

The General Partner will not have custody of the assets of the Partnership. The General Partner may only entrust the assets of the Partnership to the custody of a brokerage firm that is a member of either the New York or American Stock Exchange, a United States bank or trust company, an overseas branch of a United States bank, or another custodian which would be acceptable to an investment company registered under the Investment Company Act of 1940.

### NET ASSET VALUE

In connection with the determination of the net asset value of the Partnership, portfolio securities shall be valued as follows:

1. Listed portfolio securities are valued at the last reported sales price on the date of determination during the regular trading session on the principal exchange on which such securities are traded or, if not available, at the mean between the exchange quoted bid and asked prices.
2. Over-the-counter securities are valued at the last reported sales price on the date of determination during the regular trading session if available through the facilities of a recognized interdealer quotation system (such as securities in the NASDAQ National Market List).
3. If the last reported sales price is not available, over-the-counter securities are valued at the "bid" price if held long by the Partnership or the "asked" price if held short by the Partnership.
4. In the case of securities that are not readily marketable or in the absence of quoted values, such securities will be valued as the General Partner, in its sole discretion, may reasonably determine;
5. Any security in the form of an exchange listed option will be valued at the mean between the closing "bid" and "asked" prices.
6. Forward currency exchange contracts will be valued at the current cost of covering or offsetting such contracts.

All other securities shall be assigned the value that the General Partner in good faith determine to reflect the fair market value thereof. The General Partner may use methods of valuing securities other than those set forth herein if the General Partner believes the alternate method is preferable in determining the fair value of such securities.

## LIABILITY

A Limited Partner's liability to the Partnership is limited to the amount it has contributed to the capital of the Partnership. The Interests will be non-assessable, except as may otherwise be provided under Delaware law. Once an Interest has been paid for in full, the holder of that Interest will have no further obligation to make additional capital contributions to the Partnership.

Under Delaware law, when a Limited Partner has rightfully received the return, in whole or in part, of his capital contribution, he is nevertheless liable for any sum, not in excess of such return with interest, necessary to discharge Partnership liabilities to all creditors of the Partnership who extended credit or whose claims arose before such return.

## INVESTMENT RISK FACTORS

Prospective investors should carefully consider the risks involved in an investment in the Partnership, including but not limited to those discussed below. Many of these risks are discussed more fully elsewhere in this Memorandum. Prospective investors should consult their own legal, tax, and financial advisers as to all these risks and an investment in the Partnership generally.

### GENERAL

**Reliance on the General Partner.** The success of the Partnership depends on the ability of the General Partner and the members of the Investment Committee to develop and implement investment strategies to achieve the Partnership's investment objectives. The Partnership's investment performance could be materially adversely affected if Bruce M. Lupatkin, Charles R. Schwab, Jr. or Theodore J. Lucas cease to be involved in the active management of the Partnership's portfolio. The General Partner has wide latitude in making investment decisions and Limited Partners have no right or power to take part in such decisions or the Partnership's management.

**Operating Deficits.** The expenses of operating the Partnership (including Management Fees payable to the General Partner) could exceed its income. This would require that the difference be paid out of the Partnership's capital, reducing the Partnership's investments and potential for profitability.

**Lack of Operating History.** The Partnership is a newly formed entity and has no operating history upon which investors can evaluate its future performance. The past investment performance of the General Partner and the members of the Investment Committee is not necessarily indicative of the future results of an investment in the Partnership. There can be no assurance that the Partnership will achieve its investment objective.

### INVESTMENT RISKS

All securities investing and trading activities risk the loss of capital. While the General Partner will attempt to moderate these risks, there can be no assurance that the Partnership's investment and trading activities will be successful or that Limited Partners will not suffer losses. The following discussion describes some of the more significant risks associated with the Partnership's proposed activities.

**General Economic and Market Conditions.** The success of the Partnership's activities may be affected by general economic and market conditions, such as interest rates, availability of credit, inflation rates, economic uncertainty, changes in laws, and national and international political circumstances. These factors may affect the level and volatility of securities prices and the liquidity of the Partnership's investments. Unexpected volatility or illiquidity could impair the Partnership's profitability or result in losses.

**Speculative Purchase of Securities.** The Partnership will make certain speculative purchases of securities of companies that the General Partner believes to be undervalued or that may be the subject of acquisition attempts, exchange offers, cash tender offers or corporate reorganizations. There can be no assurances that securities which the General Partner believes to be undervalued are in fact undervalued, or that undervalued securities will increase in value. Further, in such cases, a substantial period of time may elapse between the Partnership's purchase of the securities and the acquisition attempt or reorganization. During this period, a portion of the Partnership's funds would be committed to the securities purchased, and the Partnership may finance such purchase with borrowed funds on which it would have to pay interest.

**Small Companies.** The Partnership will invest a substantial portion of its assets in small and/or less well-established companies. While smaller companies generally have potential for rapid growth, they often involve higher risks because they lack the management experience, financial resources, product diversification, and competitive strength of larger corporations. In addition, in many instances, the frequency and volume of their trading is substantially less than is typical of larger companies. As a result, the securities of smaller companies may be subject to wider price fluctuations. In addition, due to thin trading in some of those stocks, an investment in those stocks may be considered less liquid than an investment in many large-capitalization stocks. When making large sales, the Partnership may have to sell portfolio holdings at discounts from quoted prices or may have to make a series of small sales over an extended period of time due to the trading volume of smaller company securities.

**Non-U.S. Securities; Non-U.S. Currencies.** The Partnership may invest a portion of its assets in securities of non-U.S. issuers and in other financial instruments denominated in various currencies. The Partnership may purchase securities of issuers in any country, developed or undeveloped. In addition, in order to hedge foreign currency exchange rate risks which may arise from the purchase of such securities or other reasons incidental to the Partnership's business, the Partnership may invest in foreign currencies and foreign currency-related products. These types of investments entail risks in addition to those involved in investments in securities of domestic issuers. Investing in non-U.S. securities may represent a greater degree of risk than investing in U.S. securities due to exchange rate fluctuations, possible exchange controls, less publicly-available information, different accounting and auditing standards, more volatile markets, less securities regulation, less favorable tax provisions (including possible withholding taxes), political and social upheaval, war or expropriation. Non-U.S. securities also may be less liquid and more volatile than U.S. securities and may involve higher transaction and custodial costs. In addition, hedging foreign currency exchange rate risk entails additional risk since there may be an imperfect correlation between the Partnership's portfolio holdings of securities denominated in a particular currency and the Partnership's portfolio holdings of currencies and foreign currency related products purchased by the Partnership to hedge any exchange rate risk. Such imperfect correlation may prevent the Partnership from achieving the intended hedge or expose the Partnership to additional risk of foreign exchange rate loss.

**Foreign Currency Risks.** The Partnership's investment in non-U.S. securities denominated in foreign currencies may be affected favorably or unfavorably by exchange control regulations or changes in the exchange rate between such currencies and the U.S. dollar. Changes in foreign currency exchange rates influences values within the Partnership's portfolio. Changes in foreign currency exchange rates may also affect the value of dividends and interest earned, gains and losses realized on the sale of securities and net investment income and gains, if any, of the Partnership. The rate of exchange between the U.S. dollar and other currencies is determined by the forces of supply and demand in the foreign exchange markets. These forces are affected by international balance of payments and other economic and financial conditions, government intervention and other political and diplomatic conditions, speculation and other factors.

**Trading in Options Generally.** The Partnership may purchase and sell ("write") options on securities, currencies and commodities on national and international exchanges and over-the-counter markets. The seller ("writer") of a put option which is covered (e.g., the writer has a short position in the underlying instrument) assumes the risk of an increase in the market price of the underlying instrument above the sales price (in establishing the short position) of the underlying instrument, plus the premium received, and gives up the opportunity for gain on the underlying instrument below the exercise price of the option. The seller of an

uncovered put option assumes the risk of a decline in the market price of the underlying instrument below the exercise price of the option. The buyer of a put option assumes the risk of losing its entire investment in the put option. If the buyer of the put holds the underlying instrument, the loss on the put will be offset in whole or in part by any gain on the underlying instrument.

The writer of a call option which is covered (e.g., the writer has a long position in the underlying instrument) assumes the risk of a decline in the market price of the underlying instrument below the value of the underlying instrument less the premium received, and gives up the opportunity for gain on the underlying instrument above the exercise price of the option. The seller of an uncovered call option assumes the risk of a theoretically unlimited increase in the market price of the underlying instrument above the exercise price of the option. The buyer of a call option assumes the risk of losing its entire investment in the call option. If the buyer of the call sells short the underlying instrument, the loss on the call will be offset, in whole or in part, by any gain on the short sale of the underlying instrument.

Options may be cash settled, settled by physical delivery or by entering into a closing transaction. In entering into a closing purchase transaction, the Master Fund may be subject to the risk of loss to the extent that the premium paid for entering into such closing purchase transaction exceeds the premium received when the option was written. In addition, the correlation between option prices and the prices of underlying securities may be imperfect and the market for any particular option may be illiquid at a particular time.

**Stock Options.** The Partnership may engage in various types of options transactions, including the writing of put and call options on securities. Trading in options may be used to reduce the risks attendant to short-selling, to reduce overall market exposure, or to establish or increase long or short positions. Options trading is speculative and involves a high degree of risk. The leverage offered by trading in options could cause the value of an investment in the Partnership to be subject to more frequent and wider fluctuations than would be the case if the Partnership did not invest in options. If the Partnership purchases a put or a call option, it may lose the entire premium paid. If the Partnership writes a "naked" put or call option, it may incur unlimited losses (in the case of a call option) or losses limited to the strike price of the option (in the case of a put option). If the Partnership writes a covered put or call option, the Partnership will limit its opportunity to profit from an increase (in the case of calls) or decrease (in the case of puts) in the market value of the underlying security.

Stock options that may be purchased by the Partnership include options not traded on a securities exchange. Options not traded on an exchange are not issued by The Options Clearing Corporation; therefore, the risk of non-performance by the obligor on such an option may be greater and the ease with which the Partnership can dispose of such an option may be less than in the case of an exchange traded option issued by The Options Clearing Corporation.

The Partnership also may purchase put and call options on stock indices as a hedge against general movements in the securities market or as a hedge against individual positions, on a temporary basis or otherwise. A stock index option is a contract which gives the buyer the right to buy, in the case of a call, or sell, in the case of a put, a specified amount of the stock index at the option exercise price. For example, the Partnership may purchase put options on an index in anticipation of a decrease in the market value of the securities underlying the index. The use of options on stock indices enables the Partnership to quickly obtain exposure to the equity markets as a hedge against general movements in the securities market or to establish positions which the General Partner believes may increase the return of the Partnership. Furthermore, if the General Partner anticipates a short-term change in stock prices, the purchase of options on stock indices might reduce the need to liquidate positions and possibly repurchase such positions at a later time.

**Derivative Transactions.** The Partnership may engage in derivative transactions such as swaps, collars, caps, floors and forwards both for hedging purposes and as an alternative to direct investments in the underlying securities. The risks associated with derivative transactions are potentially greater than those associated with the direct purchase or sale of the underlying securities because of the additional complexity and potential for leverage. In addition, derivatives may create credit risk (the risk that a counterparty on a

derivative transaction will not fulfill its contractual obligations), as well as legal, operations, reputational and other risks beyond those associated with the direct purchase or sale of the underlying securities to which their values are related.

**Short Sales.** The Partnership will effect short sales of securities as part of its hedging strategy in a given investment or in those instances when the General Partner is of the belief that a given security is over-priced. Short sales are transactions in which the Partnership sells a security or other asset which it does not own (by borrowing such security), in anticipation of a decline in the market value of the security or such asset. Although the Partnership's gain is limited by the price at which it sold the security short, losses from short sales may be unlimited if the price of the security sold short will continue to appreciate. Additionally, even though the Partnership secures a "good borrow" of the security sold short at the time of execution, the lending institution may recall the lent security at any time, thereby forcing the Partnership to purchase the security at the then prevailing market price which may be higher than the price at which such security was originally sold short by the Partnership.

**Concentration of Investments.** The Partnership may at certain times assume concentrated investment positions (relative to its capital) with the result that a loss in any such position could have a material adverse impact on the Partnership's capital. It is the General Partner's intention, however, to limit the Partnership's long positions at the time of initiation to not more than five percent of the portfolio and to limit the Partnership's short positions at the time of initiation to not more than two percent of the portfolio, with the maximum single position exposure at any one time being not more than 15 percent.

**Loans of Portfolio Securities.** The Partnership may from time to time lend securities from its portfolio to brokers, dealers and financial institutions and receive collateral in the form of cash or securities in an amount equal to at least 100% of the current market value of the loaned securities, including any accrued interest or dividend receivable. The Partnership will retain all rights of beneficial ownership as to the loaned portfolio securities, including voting rights and rights to interest or other distributions, and will have the right to regain record ownership of loaned securities to exercise such beneficial rights. Such loans will be terminable at any time. The Partnership may pay finders', administrative and custodial fees to persons unaffiliated with the Partnership in connection with the arranging of such loans.

**Overall Investment Risk.** All securities investments risk the loss of capital. The nature of the securities to be purchased and traded by the Partnership and the investment techniques and strategies to be employed by the General Partner may increase this risk. While the General Partner will use its best efforts in the management of the Partnership's portfolio, there can be no assurance that the Partnership will not incur losses. Many unforeseeable events, including actions by various government agencies, and domestic and international economic and political developments, may cause sharp market fluctuations which could adversely affect the Partnership's portfolio and performance.

**Portfolio Turnover.** The Partnership has not placed any limits on the rate of portfolio turnover and portfolio securities may be sold without regard to the time they have been held when, in the opinion of the General Partner, investment considerations warrant such action. A high rate of portfolio turnover involves correspondingly greater expenses than a lower rate.

**Limited Liquidity of Some Investments.** Some of the securities in which the Partnership invests may be or become relatively illiquid, because they are thinly traded, they are subject to transfer restrictions, or the circumstances of the Partnership's ownership of them (e.g., the Partnership and other accounts the General Partner manages hold a large block) give rise to practical or regulatory limits on the Partnership's ability to liquidate quickly. The Partnership may not be able promptly to liquidate those investments if the need should arise, and its ability to realize gains, or to avoid losses in periods of rapid market activity, may therefore be affected. In addition, the value assigned to such securities for purposes of determining Limited Partners' partnership percentages and determining Net Profits and Net Losses may differ from the value the Partnership is ultimately able to realize.

**Insolvency of Brokers and Others.** The Partnership will be subject to the risk of failure of the brokerage firms that execute its trades, the clearing firms that such brokers use, or the clearing houses of which such clearing firms are members.

## **PARTNERSHIP RISKS**

**Illiquidity of Interests.** The Interests may be acquired for investment purposes only and not with a view to their resale or other distribution. The Interests will not be registered under the Securities Act in reliance on an exemption under Section 4(2) of the Securities Act and Regulation D promulgated thereunder. The Partnership Agreement substantially restricts the transferability or assignability of the Interests or withdrawal from the Partnership.

The General Partner's consent is a condition to any transfer or assignment, and such consent is within its sole discretion. In addition, withdrawals by a Limited Partner may only be made after a three-year lock-up and then only as of the last business day of a calendar quarter by giving not less than 60 days prior written notice to the General Partner (unless such notice is waived by the General Partner in its sole discretion). If, as a result of some change in circumstances, arising from an event not presently contemplated, a Limited Partner wishes to transfer all or part of his Interests, and even if all conditions to such a transfer are met, he may find no transferee for his Interest due to market conditions or the general illiquidity of the Interests.

The General Partner may require any Limited Partner to withdraw all or a portion of its Capital Contribution at any time if it deems such withdrawal to be in the best interest of the Partnership. All such required withdrawals are in the sole discretion of the General Partner and may be required of any one or more Limited Partners at any time.

**Limitations on the Obligations of the Principals of the General Partner.** The principals of the General Partner will devote only such time to Partnership matters as they, in their sole discretion, deem appropriate. The General Partner will have the sole right to conduct the operations of the Partnership in such manner as it deems proper. The Limited Partners will have no such authority and will be dependent upon the judgment and skill of the General Partner.

**Risks Associated With Incentive Allocation.** The Incentive Allocation could encourage the General Partner to make investments on behalf of the Partnership that are riskier or more speculative than it would if it were receiving only a flat fee. Further, the General Partner will receive Incentive Allocations as to unrealized gains that may never be realized and will not return an Incentive Allocation paid for a period in which there is a Net Profit, even if in a subsequent period the Partnership does not earn a Net Profit or suffers a Net Loss. As a result, the Incentive Allocation may be greater than it would be if it were based solely on realized gains.

**Effect of Substantial Withdrawals.** Substantial withdrawals by Limited Partners within a short period of time could require the Partnership to liquidate securities positions more rapidly than would otherwise be desirable, possibly reducing the value of the Partnership's assets and/or disrupting the General Partner's investment strategy. Reduction in the size of the Partnership could make it more difficult to generate a positive return or to recoup losses due to, among other things, reductions in the Partnership's ability to take advantage of particular investment opportunities or decreases in the ratio of its income to its expenses.

**Potential Mandatory Withdrawal.** The General Partner may, in its sole discretion at any time, require a Limited Partner to withdraw all or a portion of his or her capital account balance. Such mandatory withdrawal could result in adverse tax and/or economic consequences to such Limited Partner.

## **OTHER RISKS**

**Tax Considerations.** For a more detailed discussion of the income tax considerations associated with an investment in the Partnership, see the discussion below under "Certain Federal Income Tax Considerations."

*Limitations on Deductions.* Tax laws in certain cases may limit a Partner's ability to deduct certain losses and expenditures allocable to such Partner.

*Foreign Investors.* The Partnership may be subject to certain reporting and withholding obligations as to foreign investors. Such investors should consult with their own advisers regarding the federal, state, and foreign income tax consequences of an investment in the Partnership.

**Tax Exempt Investors; Limitations on Investments.** Certain prospective Limited Partners may be subject to federal and state laws, rules and regulations which may regulate their participation in the Partnership, or their engaging directly, or indirectly through an investment in the Partnership, in investment strategies of the types which the Partnership utilizes from time to time. While the Partnership believes its investment program is generally appropriate for tax-exempt organizations for which an investment in the Partnership would otherwise be suitable, each type of exempt organization may be subject to different laws, rules and regulations, and prospective Limited Partners should consult with their own advisers as to the advisability and tax consequences of an investment in the Partnership. Investments in the Partnership by entities subject to ERISA, and other tax-exempt entities require special consideration.

It is the intention of the General Partner to ensure that the aggregate investment by benefit plan investors in the Partnership is less than 25% of the value of the Partnership's Interests, so that such participation by benefit plan investors will not be considered "significant" under applicable Department of Labor regulations, and, as a result, the underlying assets of the Partnership will not be deemed plan assets for purposes of such regulations.

## **Regulatory Matters**

*Investment Company Regulation.* The General Partner believes that, by virtue of section 3(c)(1) of the Investment Company Act the Partnership should not be deemed to be an "investment company" and, accordingly, should not be required to register as such under the Investment Company Act.

Currently, section 3(c)(1) of the Investment Company Act excludes from regulation certain private investment companies (i) whose outstanding securities are beneficially owned by not more than 100 persons, and (ii) are not making and do not presently propose to make a public offering of their securities.

*Private Offering Exemption.* The Partnership intends to offer Interests on a continuing basis without registration under any securities laws in reliance on an exemption for "transactions by an issuer not involving any public offering." While the General Partner believes reliance on such exemptions is justified, there can be no assurance that factors such as the manner in which offers and sales are made, concurrent offerings by other partnerships, the scope of disclosure provided, failures to make notice filings, or changes in applicable laws, regulations, or interpretations will not cause the Partnership to fail to qualify for such exemptions under Federal or one or more states' laws. Failure so to qualify could result in the rescission of sales of Interests at prices higher than the current value of those Interests, potentially materially and adversely affecting the Partnership's performance and business. Further, even nonmeritorious claims that offers and sales of Interests were not made in compliance with applicable securities laws could materially and adversely affect the General Partner's ability to conduct the Partnership's business.

*Other.* The Partnership and the General Partner will be subject to various other securities and similar laws and regulations that could limit some aspects of the Partnership's operations or subject the Partnership or the General Partner to the risk of sanctions for noncompliance. Investors that are employee benefit plans should also consider certain factors discussed under "ERISA Considerations".

THE FOREGOING LISTS OF INVESTMENT RISK FACTORS DO NOT PURPORT TO BE A COMPLETE EXPLANATION OF THE RISKS INVOLVED IN THIS OFFERING. POTENTIAL INVESTORS MUST READ THE ENTIRE MEMORANDUM AND ALL EXHIBITS BEFORE DETERMINING WHETHER TO INVEST IN THE PARTNERSHIP. ALL POTENTIAL INVESTORS

MUST OBTAIN PROFESSIONAL GUIDANCE FROM THEIR TAX AND LEGAL ADVISERS IN EVALUATING ALL OF THE TAX IMPLICATIONS AND RISKS INVOLVED IN INVESTING IN THE PARTNERSHIP.

#### POTENTIAL CONFLICTS OF INTEREST

In the conduct of the Partnership's business, conflicts may arise between the interests of the General Partner and those of Limited Partners. While the General Partner is accountable to the Partnership as a fiduciary and, consequently, must exercise good faith and integrity in handling the Partnership's business, prospective investors should be aware of the potential for such conflicts of interest.

#### Other Business Relationships

The General Partner devotes as much of the time and resources of its members, managers, officers and employees to the activities of the Partnership as the General Partner deems necessary and appropriate. The Partnership Agreement does not restrict the General Partner from forming additional investment partnerships or from engaging in other business activities, even though those activities may be in competition with the Partnership and/or may involve substantial time and resources of the General Partner. The General Partner also serves as the general partner of North Bay One, L.P. and MCP North Bay Technology Fund, L.P., and as the investment manager of MCP North Bay Technology Master Fund, Ltd. and MCP North Bay Technology Fund, Ltd., offshore investment funds formed in 2001.

The General Partner believes that its management activities for the Partnership and its other advisory clients will be complementary to a large extent, and that the Partnership may benefit from participating in investment opportunities along with those other clients. However, conflicts of interest could arise in connection with securities transactions the General Partner effects on behalf of the Partnership, transactions it effects for its other clients, and transactions the General Partner and its affiliates and employees enter into for their own accounts. Transactions entered into on behalf of these various parties may differ in substance, timing, and amount, due to, among other things, differences in investment objectives, abilities to take advantage of particular investment opportunities, or other factors affecting the appropriateness or suitability of particular investment activities. Differences in transactions could also be due to limitations on the size or availability of particular investment or transactional opportunities. The General Partner allocates transactions and opportunities among the various accounts in a manner it believes to be as equitable as possible, considering each account's objectives, programs, limitations and capital available for investment, but all accounts may not necessarily invest in the same securities. Neither the General Partner nor its affiliates and employees has any obligation to provide the Partnership or any other client with any particular investment opportunity or to refrain from taking advantage of an investment opportunity that could be beneficial to the Partnership.

When the Partnership, other of the General Partner's clients, and/or other accounts in which the General Partner or its affiliates are involved effect transactions in the same security at the same time, the General Partner is authorized to combine purchase and sale orders on behalf of the Partnership with orders for other accounts for which it has trading authority, including its own accounts, and to allocate the securities or proceeds arising out of those transactions (and the related transaction expenses) on an average price basis among the various participants in the transactions. While the General Partner believes combining transaction orders in this way is generally, over time, advantageous to all participants, in particular cases the average price could be less advantageous to the Partnership than if the Partnership had been the only account effecting the transaction or had completed its transaction before the other participants. Because of the General Partner's interest in the Partnership (including the Incentive Allocation), there could be circumstances in which the Partnership's transactions may not, under certain laws and regulations, be combined with those of some of the General Partner's other clients, and the Partnership may obtain less advantageous execution than such other clients.

## **Investment and Transaction Opportunities**

Conflicts of interest could also arise in connection with securities transactions for the accounts of the Partnership, other investment vehicles in which the General Partner and/or its officers and shareholders are involved, any other advisory clients the General Partner may have, and the General Partner or its officers, employees, and shareholders themselves. These transactions could differ in substance, timing, and amount, due to, among other things, differences in investment objectives or other factors affecting the appropriateness or suitability of particular investment activities to the Partnership or other clients, or to limitations on the availability of particular investment or transactional opportunities. The General Partner will allocate transactions and opportunities among its various accounts in a manner it believes to be as equitable as possible, considering each account's objectives, programs, limitations, and capital available for investment, but all accounts may not necessarily invest in the same securities. Further, neither the General Partner nor its officers, employees or shareholders have any obligation to provide the Partnership or any other account with any particular investment opportunity or to refrain from taking advantage of an investment opportunity that could be beneficial to the Partnership.

If the Partnership and other investment portfolios the General Partner manages seek to buy or sell the same security at the same time, the General Partner may combine purchase and sale orders on behalf of the Partnership with orders for those other portfolios, and allocate the securities or proceeds arising out of those transactions (and the related transaction expenses) on an average price basis among the various participants in the transactions. While the General Partner believes combining transaction orders in this way is, over time, advantageous to all participants, in particular cases the average price could be less advantageous to the Partnership than if the Partnership had been the only account effecting the transaction or had completed its transaction before the other participants. Because of the General Partner's interest in the Partnership (including the Incentive Allocation), there could be circumstances in which the Partnership's transactions may not, under certain laws and regulations, be combined with those of some of the other accounts the General Partner manages, and the Partnership may obtain less advantageous execution than such other accounts.

### **Selection of Brokers**

The General Partner may receive nonmonetary benefits from brokers and dealers who effect transactions for the Partnership and the General Partner's other clients. These may take the form of investment research used in the management of all the General Partner's client accounts (not just the Partnership), referrals of investors in the Partnership or clients, and other services that benefit the General Partner rather than, or in addition to, the Partnership. Such benefits could create an incentive for the General Partner to select brokers or dealers to perform transactional services for the Partnership on the basis of the benefits provided to the General Partner rather than solely the quality of the transactional services and the price charged the Partnership. See "Brokerage and Transactional Practices."

### **General Partner Incentive Allocation**

The structure of the Incentive Allocation may involve a conflict of interest, because it may create an incentive for the General Partner to cause the Partnership to make riskier or more speculative investments than it otherwise would. In some cases, the Incentive Allocation together with the fees charged by the General Partner may be greater than the total fees and other benefits provided to other investment advisers for similar services; in other cases the benefits to the General Partner may be lower.

### **Transactions between the General Partner and the Partnership**

The Partnership will not purchase any securities from or sell any securities to the General Partner (other than interests in the Partnership, on the terms described in this Confidential Private Offering Memorandum). In addition, the General Partner will not borrow from the Partnership and will not use the Partnership's funds or securities as compensating balances for its own benefit or commingle such funds or securities with the

funds of any other person (except to the extent combining purchase and sale orders for various clients described above could be considered to involve such commingling).

### **No Separate Representation**

The General Partner has been represented by Wolf, Block, Schorr and Solis-Cohen LLP in connection with the formation of the Partnership. That law firm has not acted on behalf of the Partnership or any Limited Partner, and the Partnership is not separately represented by counsel.

## **WHO SHOULD INVEST; SUBSCRIPTIONS**

Subscriptions for Interests will be accepted at the discretion of the General Partner.

The minimum investment is \$5,000,000 and the minimum additional capital contribution is \$100,000. The General Partner may waive or reduce these requirements in particular cases and may change them as to new investors in the future. The Partnership will pay no sales commissions in connection with sales of Interests. However, the General Partner may direct a portion of the Partnership's portfolio brokerage business to broker-dealers who introduce Limited Partners to the Partnership and may pay finders' fees or commissions at its own expense to such persons.

### **Eligible Investors**

This is a speculative investment in unregistered limited partnership Interests. The Partnership will follow an aggressive investment strategy which, if unsuccessful, could involve substantial losses. The investment will have limited liquidity, there will not be any public market for the Interests, and the sale or transfer of the Interests will be severely restricted. An investment in the Partnership will entail substantial market risk and may not be appropriate for certain investors.

The Interests are designed to be exempt from registration under the Securities Act pursuant to Regulation D thereunder and the Partnership is designed to be exempt from registration under the Investment Company Act pursuant to Section 3(c)(1) thereunder.

Subscriptions which would jeopardize any of these exemptions will be rejected by the General Partner. Each prospective investor will be required to satisfy the admission standard described in "Admission Standards" below and to represent that such investor:

- ◆ is investing in the Partnership for its own account, for investment purposes only, and not with a view to distribution;
- ◆ is a sophisticated investor (or has a qualified purchaser representative) capable of evaluating the risks and merits of an investment in the Partnership;
- ◆ has had access to sufficient information needed to make an investment decision about the Partnership;
- ◆ can tolerate the illiquidity which is characteristic of the Interests; and
- ◆ meets the definitions of an (1) "Accredited Investor" as set forth in Regulation D under the Securities Act; and (2) "Qualified Client" as defined in Rule 205-3 under the Investment Advisers Act.

## Admission Standards

### “Qualified Client” Standard

Generally, Interests will be sold only to investors who are eligible to enter into a performance fee arrangement under the Investment Advisers Act. Currently, eligible investors are persons that have either at least \$750,000 under management with the General Partner immediately after investing, or have a net worth at the time of investing in excess of \$1,500,000.

### “Accredited Investor” Standard

In addition, the Interests will generally be sold only to “accredited” investors. To qualify as an accredited investor, an investor must satisfy the definition of accredited investor under Rule 501(a) promulgated by the SEC under the Securities Act. Currently, to be treated as an accredited investor, a purchaser must satisfy one of the following tests:

(a) Individuals. If the purchaser is an individual, the purchaser must represent that he or she has a net worth in excess of \$1,000,000 or had an individual income in excess of \$200,000 (or joint income with his or her spouse in excess of \$300,000) in each of the preceding two years and has a reasonable expectation of reaching the same level of income in the current year.

(b) Corporations, Partnership and other Entities. A corporation, partnership, an organization described in Section 501(c)(3) of the Internal Revenue Code, or a Massachusetts or similar business trust will be treated as an accredited investor if it was not formed for the specific purpose of acquiring the Interests and it has total assets in excess of \$5,000,000.

(c) Certain Qualified Plans. A Qualified Plan will be treated as an accredited investor if (1) all the plan's participant's are accredited investors, or (2) the investment decision is made by a plan fiduciary that is either a bank, an insurance Partnership or a registered investment adviser, or (3) it has total assets in excess of \$5,000,000.

(d) Trusts. A revocable trust will generally be treated as an accredited investor if each grantor is an accredited investor and the grantors may amend or revoke the trust at any time. An irrevocable trust will generally be treated as an accredited investor if (1) it has total assets in excess of \$5,000,000 and was not formed for the specific purpose of acquiring the Interests and its investment in the Interests is directed by a person experienced in financial and business matters who is capable of evaluating the merits and risks of such investment, or (2) the trustee of the trust is a bank, and it makes the decision to invest in the Interests on behalf of the trust.

(e) Other Purchasers. Other accreditation standards are described in the Subscription Agreement.

### Suitability

Satisfaction of the above Admission Standards and the ability to make the other representations in the Subscription Agreement do not necessarily mean that Interests are a suitable investment for a prospective investor. Prospective investors should carefully evaluate whether an investment in the Partnership is suitable for their particular circumstances and investment needs. In doing so, they should consult with such legal, tax, and financial advisors as they consider appropriate, and should avail themselves of the opportunity to ask questions of the General Partner.

Each investor must, either alone or with the assistance of a “purchaser representative,” have sufficient knowledge and experience in financial and business matters generally and in securities investment in particular to allow him or her to evaluate the merits and risks of investing in the Partnership. In addition, each investor

should have sufficient funds, beyond those he or she intends to invest in the Partnership, to meet personal needs and contingencies. Investors should expect that they will not have access to the funds invested in the Partnership for extended periods and should be capable of absorbing a loss or reduction in the value of their investments.

Interests may be a suitable investment for certain qualified retirement plans. However, such prospective investors should carefully consider the appropriateness of such an investment. See the discussion under the heading "ERISA Considerations" for additional discussion of legal issues to be considered by qualified retirement plan investors.

### **Method of Subscription**

To subscribe to purchase an Interest, an investor must complete, date, and sign the Subscription Agreement accompanying this Memorandum, deliver the signed Subscription Agreement to the General Partner and make payment in accordance therewith. The General Partner reserves the right to accept or reject any subscription in whole or in part in its sole discretion for any reason whatsoever and to withdraw this offering at any time.

## **SECURITIES REGULATORY MATTERS**

The Partnership and the General Partner are subject to various federal and state securities and other laws that may limit the Partnership's activities and, under certain circumstances, subject the Partnership to substantial sanctions if it did not comply. In addition, other securities and similar laws would subject the Partnership to further restrictions if the Partnership did not adhere to the requirements for exemptions from some or all of the provisions of those laws.

### **The Investment Company Act of 1940**

If the Partnership were considered an "investment company" within the meaning of the Investment Company Act, it would be subject to numerous requirements and restrictions relating to its structure and operation. If the Partnership were required to register as an investment company and to comply with these requirements and restrictions, it would have to make significant changes in its proposed structure and operations, which could adversely affect its business.

The Partnership operates under an exclusion from investment company regulation for a certain type of "private investment company" in reliance on Section 3(c)(1) of the Investment Company Act. That section excludes issuers whose securities are beneficially owned by not more than 100 persons and have not been offered publicly. Should private investment company exclusions cease to be available to the Partnership, the Partnership and the General Partner could be subject to legal action by the SEC and others, possibly resulting in financial losses to the Partnership and the termination of the Partnership's business.

Although the General Partner believes registration and regulation under the Investment Company Act would impair the Partnership's ability to achieve its investment objectives, the Investment Company Act does provide protections that will not be available to investors in the Partnership. For example, a registered investment company must have a board of directors, a majority of which, as a practical matter, must be independent of its investment adviser (the General Partner), and is restricted in its relationship with and compensation to its affiliates (such as the General Partner) and in its capital structure. In addition, the Investment Company Act requires an investment company to state definite policies as to certain enumerated types of activities and, in some cases, forbids the investment company from changing those policies without shareholder approval. By contrast, the Partnership's investment activities provide the General Partner with extremely broad discretion to determine and to change the Partnership's investment program without consulting Limited Partners.

## Securities Dealer Status

The General Partner believes the Partnership is not a "dealer" within the meaning of the Securities Exchange Act of 1934 and, accordingly, does not intend to register the Partnership as such. However, it is possible that the SEC or a court could reach a different conclusion. In such an event, the Partnership could be fined and could be prevented from continuing its business, either temporarily or permanently. If the Partnership were required to register as a "dealer," its operating expenses would increase significantly, its activities would be restricted, and its profitability would suffer.

## Investment Adviser Regulation

The General Partner is registered as an investment adviser with the State of California.

## ERISA CONSIDERATIONS

### General

Fiduciaries and other persons who are proposing to invest in the Interests on behalf of retirement plans, IRAs and other employee benefit plans ("Plans") covered by the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), or the Internal Revenue Code of 1986, as amended (the "Code"), should give appropriate consideration to, among other things, the role that an investment in the Partnership plays in the Plan's portfolio, taking into consideration whether the investment is designed reasonably to further the Plan's purposes, the investment's risk and return factors, the portfolio's composition with regard to diversification, the liquidity and current return of the total portfolio relative to the anticipated cash flow needs of the Plan, the projected return of the total portfolio relative to the Plan's objectives and the limited right of Limited Partners to withdraw all or any part of their capital or to transfer their Interests.

### Plan Asset Regulation

The United States Department of Labor has adopted regulations which treat the assets of certain pooled investment vehicles, such as the Partnership, as "Plan Assets". However, under those regulations, the underlying assets of the Partnership are not considered Plan Assets if "Benefit Plan Investors" hold less than 25% of the outstanding value of any class of equity interest of the Partnership. "Benefit Plan Investors" include employee benefit plans as defined in Section 3(3) of ERISA (whether or not subject to Title I of ERISA), plans described in Section 4975(e)(1) of the Code, government plans, church plans and entities the underlying assets of which include Plan Assets by reason of investment therein by Benefit Plan Investors. In applying this exception to the Partnership, the value of any equity interest held by a person who has discretionary authority or control with respect to the assets of the Partnership (including the General Partner and certain members, officers and employees of the General Partner) or any other person who provides investment advice for a fee (direct or indirect) with respect to such assets, or an affiliate of any such person, is disregarded in determining whether the equity participation by Benefit Plan Investors is 25% or less. In order to prevent the assets of the Partnership from being considered Plan Assets under ERISA, it is the intention of the General Partner to monitor the investments in the Partnership and prohibit the acquisition or transfer of any Interests in the Partnership by any investor, including a Benefit Plan Investor, unless, after giving effect to such an acquisition or transfer, the total proportion of Interests in the Partnership owned by Benefit Plan Investors is less than 25% of the aggregate value of any class of equity interest of the Partnership (determined, as described above, by excluding certain interests held by the General Partner, other fiduciaries and affiliates).

If the Partnership's assets were considered Plan Assets, then, under ERISA and the Code, the General Partner would be a fiduciary, and certain members, officers and employees of the General Partner as well as certain affiliates would become "parties in interest" and "disqualified persons" with respect to the investing Plans, with the result that the rendering of services to certain related parties or the lending of money or other extensions of credit, or the sale, exchange or leasing of property by the Partnership or certain related parties,

or the payment of certain fees, as well as certain other transactions, might be deemed to constitute prohibited transactions. Additionally, individual investment in Interests by persons who are fiduciaries, and/or parties-in-interest and disqualified persons, to a Plan might be deemed to constitute prohibited transactions under such circumstances.

### **Representation by Plans**

The fiduciaries of each Plan proposing to invest in the Partnership will be required to represent that they have been informed of and understand the Partnership's investment objectives, policies and strategies and that the decision to invest Plan Assets in the Partnership is consistent with the provisions of ERISA and/or the Code that require diversification of Plan Assets and impose other fiduciary responsibilities.

## **SUMMARY OF THE PARTNERSHIP AGREEMENT**

The rights and obligations of Partners are governed by the Partnership Agreement. The following briefly summarizes certain provisions of the Partnership Agreement that are not described elsewhere in this Memorandum. Prospective investors are urged to read the Partnership Agreement in its entirety before subscribing.

**General.** The Partnership has been organized as a limited partnership under the Delaware Revised Limited Partnership Act. North Bay Technology Partners LLC is the sole General Partner. The Partnership Agreement provides that the General Partner will have complete control of the business of the Partnership and that the Limited Partners will have no power to take part in the management of the Partnership.

**Size of Offering.** The Partnership is offering up to \$100 million limited partnership Interests. Each Limited Partner will be required to contribute a minimum of \$5,000,000, which amount the General Partner may increase or decrease at any time in its sole discretion. The number of Partners will not be more than 100. Limited Partners will be admitted to the Partnership at the beginning of calendar quarter or at such other times as the General Partner shall determine.

**Term of Partnership.** The Partnership shall continue until December 31, 2032, unless terminated earlier by the General Partner in its sole discretion.

**Capital Contributions.** All funds will be contributed in cash or at the discretion of the General Partner, in kind, at the time of admission of a Limited Partner to the Partnership.

**Maintenance of Capital Accounts; Tax Allocations.** The Partnership will maintain Capital Accounts for the Partners in accordance with Section 704(b) of the Internal Revenue Code of 1986, as amended (the "Code"), the Treasury Regulations thereunder and certain principles set forth in the Partnership Agreement.

**Allocation of Profits and Losses.** Net Profits or Net Losses of the Partnership, which include unrealized appreciation or depreciation in the Partnership's investments and realized investment gains or losses and income and expense, will generally be allocated at the end of each fiscal period among the Capital Accounts maintained for the Partners in proportion to the relative values of such Capital Accounts at the beginning of such fiscal period, except for the incentive allocation of Net Profits to the General Partner, as described below. In the event a Partner withdraws all of his or her capital from the Partnership, the General Partner has the discretion to make a special allocation to said Partner for federal income tax purposes of the capital gains recognized by the Partnership in such a manner as will reduce the amount, if any, by which such Partner's capital account exceeds the federal income tax basis of such Partner in his or her Interest.

**Incentive Allocation.** The General Partner receives an incentive allocation equal to twenty percent (20%) of the Net Profits (realized and unrealized) allocated to each Limited Partner's Capital Account in the Partnership for the applicable fiscal period.

The incentive allocation of Net Profits to the General Partner is subject to a loss carryforward limitation, so that no incentive allocation is made to the General Partner until prior Net Losses allocated to the Limited Partners are recouped. Such allocation of Net Profits to the General Partner shall be adjusted to take into account any distributions to or withdrawals by a Limited Partner, with the amount of prior Net Losses that must be offset before an incentive allocation is made to the General Partner being reduced in proportion to the distribution or withdrawal. The General Partner's incentive allocation is made as of the end of each calendar year or when a Limited Partner withdraws from the Partnership and is not affected by Net Losses in a subsequent fiscal period.

The General Partner may, in its sole discretion, waive all or any part of its Net Profits interest to certain Limited Partners.

**Management Fee.** The General Partner receives from the Partnership a quarterly management fee, paid in advance, calculated at the rate of one-quarter of two percent (0.50%) of the net assets of the Partnership as of the first day of each calendar quarter (the "Management Fee"). The Management Fee shall be adjusted pro rata to account for contributions and withdrawals made during the calendar quarter. The Manager may, in its sole discretion, waive all or part of the Management Fee otherwise due with respect to any Limited Partner's investment.

**Distributions.** The General Partner may, in its sole discretion, make distributions in cash or securities (i) in connection with a withdrawal of funds from the Partnership by a Partner and (ii) at any time to all of the Partners on a pro rata basis in accordance with the Partners' Partnership percentages. At the request of the Limited Partners, the General Partner will make annual tax distributions sufficient to cover tax liabilities associated with realized gains allocated to the Limited Partners; otherwise it is the intention of the General Partner not to distribute the current income of the Partnership. No Partner shall have the right to receive distributions in property other than cash.

**Withdrawals.** Except as otherwise provided herein, each Limited Partner shall have the right to withdraw, in whole or in part, his or her Closing Capital Account from the Partnership as of the last business day of each calendar quarter following the third anniversary of such Limited Partner's admission to the Partnership, or at such other times as the General Partner shall determine (each a "Withdrawal Date"), by giving not less than 60 days prior written notice to the General Partner. Payment on withdrawals generally will be made within 30 days after the Withdrawal Date, although 10% of any withdrawal that represents more than 90% of a Limited Partner's capital may be withheld until completion of the Partnership's year-end financial statements for the year in which the withdrawal occurs. Withdrawals may be paid in any combination of cash and securities, in the General Partner's sole discretion.

The General Partner may withhold payment of all or any part of the amount withdrawn to establish such reserves for contingencies as the General Partner, in its sole discretion, may deem advisable.

The General Partner may, in its complete discretion, terminate for any reason the interests of any Limited Partner in the Partnership at any time upon notice to such Limited Partner. A Limited Partner whose Interest is terminated by the General Partner shall be treated as a withdrawing Limited Partner as of the termination date.

The General Partner may withdraw any or all of its Capital Account at the end of any calendar month (or at such other times as it may determine) upon written notice to the Partnership.

**Expenses.** The Partnership will pay (or reimburse the General Partner for) (a) all reasonable expenses related to the Partnership's organization, including, but not limited to, legal and accounting fees, government filing fees, syndication and other expenses of offering the Interests, (b) any reasonable legal, accounting and audit fees and expenses, including those associated with investigating potential investments or maximizing return on existing investments and (c) reasonable custodial fees, interest on borrowed funds, transfer taxes, brokerage commissions, fees and expenses for consulting, the cost of business travel related to the

Partnership, research and statistical services and any extraordinary expenses such as litigation expenses. The General Partner will pay all other expenses related to the administration of the Partnership, including, but not limited to, salaries of employees, supplies, office space and administrative services. The Partnership may use "soft" dollar commissions or rebates of commissions generated by the payment of brokerage commissions by the Partnership to pay for research and brokerage services within the "safe harbor" provided by Section 28(e) of the Securities Exchange Act of 1934.

**Transferability of Limited Partnership Interests.** A Limited Partner may not, without the consent of the General Partner, voluntarily or involuntarily, sell, assign, or transfer its interest in the Partnership (or any portion thereof). It is anticipated that the General Partner will only consent to a transfer where such transfer is necessitated due to the bankruptcy, death or similar event of a Limited Partner.

**Allocation of Investment Opportunities; Conflicts of Interest.** The General Partner and its affiliates will be subject to a number of potential conflicts of interest with the Partnership.

**Reports.** After the end of each calendar year of the Partnership each Partner will receive: (i) an annual audited report prepared in accordance with generally accepted accounting principles (except that the Partnership may amortize its organizational expenses over a period of 60 months); and (ii) a statement of such Partner's Capital Account and annual tax information necessary for completion of such Partner's tax returns. Each Partner will also receive certain periodic reports as the General Partner may deem appropriate.

**Indemnification.** The General Partner shall not be liable, responsible or accountable in damages or otherwise to the Partnership or any of the Limited Partners for any act or omission performed or omitted by it in good faith on behalf of the Partnership and in a manner reasonably believed by it to be within the scope of the authority granted to it by the Partnership Agreement, except when such action or failure to act constitutes willful misconduct or gross negligence. The General Partner, including its members, employees and other representatives (each an "Indemnified Party"), shall be indemnified by the Partnership for any losses or expenses suffered or sustained by them as a result of, or in connection with, any act performed by them within the scope of the authority conferred upon them by the Partnership Agreement, including without limitation the amount of any judgment or settlement and reasonable attorneys' fees and other costs or expenses incurred in connection with the defense of any actual or threatened action or proceeding; provided, however, that such indemnity shall be payable only if the Indemnified Party, (a) acted in good faith and in a manner it reasonably believed to be in, or not opposed to, the best interests of the Partnership, and (b) had no reasonable grounds to believe that its conduct was grossly negligent or unlawful. No indemnification may be made in respect of any claim, issue or matter as to which the Indemnified Party shall have been adjudged to be liable for willful misconduct or gross negligence in the performance of its duties to the Partnership unless, and only to the extent that, the court in which such action or suit was brought determined that in view of all the circumstances of the case, despite the adjudication of liability for willful misconduct or gross negligence, the Indemnified Party is fairly and reasonably entitled to be indemnified for those expenses which the court deems proper. The Partnership Agreement also provides that the Partnership will advance to the Indemnified Party reasonable attorneys' fees and other costs and expenses incurred in connection with the defense of any action or proceeding arising out of such conduct. In the event such advance is made by the Partnership, the Indemnified Party will agree to reimburse the Partnership to the extent that it is determined that it was not entitled to indemnification. Any indemnity shall be paid from, and only to the extent of, assets of the Partnership, and no Limited Partner shall have any personal liability on account thereof.

IN THE OPINION OF THE SECURITIES AND EXCHANGE COMMISSION, INDEMNIFICATION FOR LIABILITIES ARISING UNDER THE SECURITIES ACT OF 1933 IS AGAINST PUBLIC POLICY AND IS THEREFORE UNENFORCEABLE. NO PERSON WILL BE EXCULPATED OR EXONERATED FROM LIABILITY OR INDEMNIFIED AGAINST LOSS FOR VIOLATIONS OF FEDERAL OR STATE SECURITIES LAWS OR FOR ANY OTHER INTENTIONAL OR CRIMINAL WRONGDOING.

**Amendment of Agreement of Limited Partnership.** The Partnership Agreement may be amended by the sole action of the General Partner in any manner which does not adversely affect any Limited Partner. The Partnership Agreement may also be amended by certain action taken by both (i) the General Partner and (ii) a majority of interests of the Limited Partners at the time of the amendment, provided that such amendment does not increase the share of Net Profits payable to the General Partner or change the method of making amendments to the Agreement.

## CERTAIN FEDERAL INCOME TAX CONSEQUENCES

The following paragraphs summarize certain federal income tax aspects of an investment in the Partnership by investors. The discussion is based on certain provisions of the Internal Revenue Code of 1986, as amended (the "Code"), the applicable Treasury Regulations promulgated or proposed thereunder (hereinafter the "Regulations"), current positions of the Internal Revenue Service ("IRS") contained in published Revenue Rulings and Revenue Procedures, current administrative positions of the IRS and existing judicial decisions, all of which are subject to changes or modifications at any time. The Partnership will not request any rulings from the IRS on the tax consequences described below or any other issues. A court might reach a contrary conclusion with respect to the issues addressed if the matter were contested. Future legislation, administrative action or court decisions may significantly change the conclusions expressed herein, and any such legislation, action or decisions may have a retroactive effect with respect to the transactions contemplated herein.

THE INCOME TAX LAWS APPLICABLE TO PARTNERSHIPS ARE EXTREMELY COMPLEX, AND THE FOLLOWING SUMMARY IS NOT EXHAUSTIVE AND DOES NOT CONSTITUTE TAX ADVICE. A PERSON CONSIDERING INVESTING IN THE PARTNERSHIP MUST CONSULT HIS TAX ADVISER IN ORDER TO FULLY UNDERSTAND THE FEDERAL, STATE, LOCAL AND FOREIGN INCOME TAX CONSEQUENCES OF SUCH AN INVESTMENT IN HIS PARTICULAR SITUATION. NO REPRESENTATION IS MADE AS TO THE TAX CONSEQUENCES OF THE OPERATION OF THE PARTNERSHIP.

### **Tax Status of the Partnership**

The federal income tax consequences of an investment in the Partnership will depend in part upon the Partnership being recognized as a partnership for federal income tax purposes and not as an association taxable as a corporation. No ruling will be sought from the IRS nor will an opinion be sought that the Partnership is taxable as a partnership for federal income tax purposes. Pursuant to Treasury Regulations, the General Partner intends to cause the Partnership to be classified as a partnership for federal income tax purposes.

### **Publicly Traded Partnerships**

The Revenue Act of 1987 (the "1987 Act") enacted various provisions which affect any partnership that is classified as a publicly traded partnership. Under current Regulations the Partnership will not be classified as a publicly traded partnership because it will at no time have more than 100 partners and interests in the Partnership will be issued in transactions that are not required to be registered under the Securities Act of 1933.

### **General Principles of Partnership Taxation**

It is assumed in the following discussion that, as discussed in "Tax Status of the Partnership" herein, the Partnership will be treated as such for federal income tax purposes.

Section 721(a) of the Code provides generally that no gain or loss is recognized by a partnership or any of its partners upon the contribution of property to the partnership in exchange for an interest in the partnership. Under section 721(b) of the Code, this general nonrecognition rule does not apply to the gain realized on a

transfer of property to a partnership if (i) more than 80 percent of the value of the partnership's assets (excluding cash and nonconvertible debt obligations) immediately after the transfer are held for investment and consist of money, stocks and other equity interests in corporations, evidences of indebtedness, options, forward or futures contracts, notional principal contracts and derivatives, foreign currency, certain interests in precious metals, interests in a regulated investment company, real estate investment trust, common trust fund, or publicly traded partnership, or other interests in noncorporate entities that are convertible into or exchangeable for any of the foregoing; and (ii) the transfer results, directly or indirectly, in diversification of the transferor's interests. A transfer of stocks or securities to a partnership will not be treated as resulting in a diversification of the transferor's interests for these purposes, and consequently will not trigger recognition of the gain, if each transferor transfers a diversified portfolio of stocks and securities, which is generally defined as a portfolio not more than 25 percent of the value of which is invested in the stocks or securities of any one issuer (other than the Government) and not more than 50 percent of the value of which is invested in the stocks and securities of five or fewer non-government issuers.

Section 701 of the Code provides that no federal income tax will be paid by the Partnership as an entity. Each Limited Partner will report on his federal income tax return his allocable share, determined by the Partnership Agreement, of the income, gains, losses, deductions and credits of the Partnership, whether or not any actual distribution is made to such Partner during his taxable year. A Limited Partner will generally be entitled to deduct on his personal income tax return his allocable share of Partnership losses, if any, but only to the extent of the tax basis of his partnership Interest at the end of the Partnership year in which such losses occur. A Partner's right to currently deduct losses from the Partnership's operations will be further limited to the amount for which the Partner is considered "at risk".

Generally, the taxable revenue of the Partnership will be computed in the same manner as the taxable revenue of an individual. Section 703. The character of any items of revenue, including but not limited to income, gain, loss, deduction or credit included in the Partnership's tax return will be reported as though the Partner realized those items directly from the same source as the Partnership. The Partnership Agreement will determine the Partner's share of such items.

Section 704 of the Code provides that a Partner's share of any item of income, gain, loss, deduction or credit will be governed by the Partnership Agreement unless the Partnership Agreement does not allocate such item or unless the allocation does not have substantial economic effect. The General Partner believes the basic allocations under the Partnership Agreement have substantial economic effect within the meaning of Section 704 of the Code and the Treasury Regulations promulgated thereunder. However, in the event a Partner withdraws all of his Capital Account from the Partnership, the Partnership Agreement permits the General Partner, in its sole discretion, to make a special allocation to the withdrawing Partner of capital gains recognized by the Partnership so as to reduce the amount, if any, by which such Partner's Capital Account exceeds his tax basis in his Partnership Interest before such allocation. If made, such special allocation may not have substantial economic effect. The Partnership Agreement provides that the General Partner may make amendments to the extent necessary to comply with the substantial economic effect test. In the event the allocations are determined not to have substantial economic effect, then each Partner's share of an item will be allocated in accordance with the Partner's respective interest in the Partnership. This could result in a Partner recognizing a greater or lesser amount of an item than he would have recognized under the Partnership Agreement. The timing in which a Partner recognizes a particular item could also be different than he would have recognized under the Partnership Agreement.

### **Partnership Not a Dealer**

Because the Partnership will purchase and sell securities for its own account and not for the account of others, will not hold itself out as a dealer, will not have any salesmen, and will not maintain an inventory of securities for tax purposes, it is anticipated that the operations of the Partnership will not be such as to render the Partnership a dealer. There can be no assurance that the IRS will not determine that, for tax purposes, the Partnership is a dealer (or should for other reasons be comparably treated). In the event the IRS were to

prevail on this issue, transactions which would otherwise have received capital gain or loss treatment may result in ordinary income or loss.

## **Gains or Losses**

Generally, the gains and losses realized by a trader or investor on the sale of securities are capital gains and losses. Thus, the Partnership expects that its gains and losses from its securities transactions typically will be capital gains and capital losses. These capital gains and losses may be long-term or short-term depending, in general, upon the length of time the Partnership maintains a particular investment position and, in some cases, upon the nature of the transaction. Property held for more than one year generally will be eligible for long-term capital gain or loss treatment. The maximum rate of federal income tax for individuals on long-term capital gains is 20 percent (except on certain sales of real property, collectibles, and qualified small business stock). The application of certain rules relating to short sales, to so-called "straddle" and "wash sale" transactions and to "Section 1256 contracts" may serve to alter the manner in which the Partnership's holding period for a security is determined or may otherwise affect the characterization of gain or losses as long-term, short-term, or ordinary, and also the timing of the realization of certain gains or losses.

The Partnership may realize ordinary income from interest and dividends on its investments.

## **Section 1256 Contracts**

In the case of "Section 1256 contracts," the Code generally applies a "mark to market" system of taxing unrealized gains and losses on such contracts and otherwise provides for special rules of taxation. A Section 1256 contract includes certain regulated futures contracts, certain foreign currency forward contracts, and certain options contracts.

Under these rules, Section 1256 contracts held by the Partnership at the end of each taxable year of the Partnership may be treated for federal income tax purposes as if they were sold by the Partnership for their fair market value on the last business day of such taxable year. The net gain or loss, if any, resulting from such deemed sales (known as "marking to market"), together with any gain or loss resulting from actual sales of Section 1256 contracts, must be taken into account by the Partnership in computing its taxable income for such year. If a Section 1256 contract held by the Partnership at the end of a taxable year is sold in the following year, the amount of any gain or loss realized on such sale will be adjusted to reflect the gain or loss previously taken into account under the "mark to market" rules.

Capital gains and losses from such Section 1256 contracts generally are characterized as short-term capital gains or losses to the extent of 40% thereof and as long-term capital gains or losses to the extent of 60% thereof. Such gains and losses will be taxed under the general rules described above. Gains and losses from certain foreign currency transactions will be treated as ordinary income and losses.

## **Short Sales/Constructive Sales**

Gain or loss from a short sale of property is generally considered as capital gain or loss to the extent the property used to close the short sale constitutes a capital asset in the Partnership's hands. Except with respect to certain situations where the property used by the Partnership to close a short sale has a long-term holding period on the date of the short sale, special rules would generally treat the gains on short sales as short-term capital gains. These rules may also terminate the running of the holding period of "substantially identical property" held by the Partnership. Moreover, a loss on a short sale will be treated as a long-term capital loss if, on the date of the short sale, "substantially identical property" has been held by the Partnership for more than twelve months.

Section 1259 of the Code requires that the Partnership recognize gain on the constructive sale of any appreciated financial position in stock, a partnership interest, or certain debt instruments. A constructive sale of an appreciated financial position occurs if, among other things, the Partnership enters into (1) a short sale

of the same or substantially identical property (a transaction commonly known as a "short sale against the box"), (2) an offsetting notional principal contract with respect to the same or substantially identical property, or (3) a futures or forward contract to deliver the same or substantially identical property. Exceptions to the foregoing apply to certain transactions closed within 30 days after the close of the taxable year if the underlying appreciated financial position remains "unhedged" for at least 60 days thereafter, and to transactions involving certain contracts to sell stock, debt instruments, or partnership interests if the contract settles within one year. Future Treasury regulations will determine the extent to which the constructive sale provision will apply to other commonly encountered transactions, such as identified hedging or straddle transactions under Sections 1092, 1221 and 1256 of the Code and "collar" transactions.

### **Effect of Straddle Rules on Partners' Securities Positions**

The Service may treat certain positions in securities held (directly or indirectly) by a Partner and its indirect interest in similar securities held by the Partnership as "straddles" for federal income tax purposes. The application of the "straddle" rules in such a case could affect a Partner's holding period for the securities involved and may defer the recognition of losses with respect to such securities. In addition, if either of the Partner's positions in such a transaction is an "appreciated financial position", application of the "straddle" rules may trigger a constructive sale of that position under the rules described above.

### **Conversion of Ordinary Income to Capital Gain**

Section 1258 of the Code recharacterizes capital gain from a "conversion transaction" as ordinary income, with certain limitations. Conversion transactions are defined as transactions in which substantially all the expected return is attributable to the time value of money and either (a) the transaction consists of the acquisition of property by the taxpayer and a substantially contemporaneous agreement to sell the same or substantially identical property in the future; (b) the transaction qualifies as a "straddle" (within the meaning of Section 1092(c) of the Code); (c) the transaction is one that was marketed or sold to the taxpayer on the basis that it would have the economic characteristics of a loan but the interest-like return would be taxed as capital gain; or (d) the transaction is described as a conversion transaction in Treasury regulations. The amount of gain so recharacterized will not exceed the amount of interest that would have accrued on the taxpayers' net investment for the relevant period at a yield equal to 120% of the "applicable rate".

### **Partner's Deduction of Partnership Losses**

Under Section 704(d) of the Code, a Partner is permitted to deduct his share of Partnership losses only to the extent of his adjusted basis in his Partnership interest at the end of the Partnership year in which the losses occurred. Any excess of Partnership losses over the Partner's adjusted basis must be carried over and may be deducted in subsequent taxable years at the time, and to the extent, that the Partner's basis in his Partnership Interest exceeds zero.

Generally, a Partner's tax basis for his interest in the Partnership at a particular time represents the sum of (a) the total amount of money he contributed to the Partnership, plus (b) the adjusted basis of any property contributed by him, plus (c) the Partner's share of partnership net income, minus (d) the Partner's share of partnership tax losses and distributions, plus (e) the Partner's pro rata share of certain Partnership liabilities.

Under the Section 752 Regulations, how the Partnership's liabilities are allocated to the Partners depends on whether the liability is recourse or non-recourse. A liability that is recourse to the Partnership is allocated among the General Partners in the manner that they share losses. A non-recourse liability is allocated to a limited partner except to the extent a limited partner is required to contribute additional capital to the Partnership. Non-recourse liabilities are allocated among the Partners based on their sharing of profits of the Partnership.

## **Limitation of Losses to Amounts at Risk**

Section 465 of the Code limits certain taxpayers' losses from certain activities to the amount they are "at risk" in the activities. Taxpayers subject to the "at risk" rules are individuals, an S corporation and certain closely-held corporations. The activities subject to the "at risk" limitations are all activities except the holding of real estate. A Partner subject to the "at risk" rules will not be permitted to deduct in any year losses arising from his interest in the Partnership to the extent the losses exceed the amount he is considered to have "at risk" in the Partnership at the close of that year.

A taxpayer is considered to be "at risk" in any activity to the extent of his cash contribution to the activity, his basis in other property contributed to the activity and his personal liability for repayments of amounts borrowed for use in the activity. With respect to amounts borrowed for use in the activity, the taxpayer is not considered to be "at risk" even if he is personally liable for repayment if the borrowing was from a person who has an "interest" in the activity other than an interest as a creditor. Even if a taxpayer is personally liable for repayment of amounts borrowed for use in the activity, and even if the amount borrowed is borrowed from a person whose only interest in the activity is an interest as a creditor, a taxpayer will not be considered "at risk" in the activity to the extent his investment in the activity is protected against loss through guarantees, stop loss agreements, or other similar arrangements.

Each Limited Partner will be at risk initially for the amount of his capital contribution. A Partner's amount "at risk" will be increased by his income from the Partnership and will be decreased by his losses from the Partnership and distributions to him. If a Partner's amount "at risk" decreases to zero, he can take no further losses until he has an "at risk" amount to cover the losses. A Partner is subject to a recapture of losses previously allowed to the extent that his amount "at risk" is reduced below zero (limited to loss amounts previously allowed to the Partner over any amounts previously recaptured). The potential recapture effects of distributions of Partnership debts, if any, are uncertain, and the ultimate interpretation of the new recapture mechanism may have adverse affects upon a Limited Partner.

## **Passive Losses**

Section 469 of the Code prohibits individuals, trusts, estates, personal service corporations, and certain closely-held C corporations from deducting "passive activity losses" from other income. A passive activity is one that involves the conduct of any trade or business in which the taxpayer does not materially participate. Limited Partnership interests are treated as interests in a passive activity without regard to whether the taxpayer materially participates in the activity. Proposed and Temporary Treasury Regulations provide that the trading of personal property such as stocks, bonds and other securities, for the account of owners of interests in the activity, will not be treated as a passive activity. Temp. Reg. §1.469-1T(e)(6). Accordingly, a Limited Partner's distributive share of items of income, gain, deduction, or loss from the Partnership will not be available to offset passive losses from sources outside the Partnership. Partnership gains allowable to Limited Partners will, however, be available to offset losses with respect to "portfolio" investments. Moreover, any Partnership losses allocable to Limited Partners will be available to offset other income, regardless of source. Final Treasury Regulations may modify the Proposed and Temporary Regulations and such regulations may be retroactive in effect.

## **Sale of Interests**

Although the sale and transfer of a Limited Partnership Interest is severely restricted under the Partnership Agreement, in the event a Limited Partner does sell its Partnership Interest, the gain or loss recognized by a Limited Partner who is neither a dealer in securities nor in partnership interests should be treated as capital gain or loss. Gain or loss realized from the sale of a Partnership Interest which has been held for more than one year will generally be taxable as long-term capital gain or loss. The maximum rate of tax on long-term capital gain is 20 percent.

That portion of the selling Partner's gain allocable to "unrealized receivables" as defined in Section 751 would be treated as ordinary income. Included in "unrealized receivables" is any market discount bond and short-term obligations, but only to the extent they would have given rise to ordinary income if the selling Partner's proportionate share of the Partnership's properties had been sold at that time. Transfers of Partnership Interests by reason of death, gifts, transfers in certain tax free transactions and involuntary conversions in certain circumstances will not be subject to ordinary income treatment.

If the sale or other transfer of a Partnership Interest was made other than at the end of any taxable year, the profits and losses of the Partnership for the entire taxable year will be allocated between the transferor and the transferee based on the period of time during the taxable year that the Partnership Interest was owned.

If 50% or more of the total Interests in the capital and profits of the Partnership are sold or exchanged within any consecutive 12-month period, the Partnership will be considered terminated for federal income tax purposes. Termination will cause the Partnership's taxable year to end with respect to all Partners and could have potentially adverse federal income tax consequences, including a change in the adjusted tax basis of Partnership property and the bunching of taxable income within one taxable period.

### **Profit Motive**

Section 183 of the Code provides limitations for deductions attributable to an "activity not engaged in for profit". The term "activity not engaged in for profit" means any activity other than one that constitutes a trade or business or one that is engaged in for the production or collection of income or for the management, conservation, or maintenance of property held for the production of income. The determination of whether an activity is engaged in for profit is based on all the facts and circumstances and no one factor is determinative.

Section 183 of the Code creates a presumption that an activity is engaged in for profit if, for any three or more years out of five consecutive taxable years, the gross income derived from such activity exceeds the deductions attributable thereto. Thus, while it is the general intention of the Partnership to seek and maintain economic profit, if the Partnership fails to produce a profit in at least three of five consecutive years, this presumption will not be available and the possibility of successful challenge by the IRS substantially increased. If Section 183 of the Code is successfully asserted by the IRS, no deduction will be allowed.

Since the test of whether an activity is deemed to be engaged in for profit is based on the facts and circumstances existing from time to time, no assurance can be given that Section 183 of the Code may not be applied in the future to disallow deductions taken by the investors with respect to their interest in the Partnership.

It should be noted that, if the IRS were to challenge the Partners' deduction of Partnership losses for lack of profit motive, each Partner could have the burden of proving that the Partnership did in fact enter into the transaction with a reasonable expectation of profit and that his own investment in the Partnership was made with the requisite profit motive.

### **Alternative Minimum Tax**

In certain cases a Partner's tax savings from the deduction of losses from the Partnership may be reduced by the alternative minimum tax ("AMT").

Potential investors in the Partnership should consult their personal tax advisors to determine whether an investment in the Partnership may subject them to the alternative minimum tax or an increased alternative minimum tax.

## **Reimbursement of Costs**

The General Partner will be entitled to reimbursement for certain expenditures relating to the business of the Partnership. Pursuant to Section 707(c) of the Code, a payment to a partner for services, determined without regard to the income of the partnership, is deductible by the partnership if it is an ordinary and necessary business expense which is reasonable in amount. Therefore, there can be no assurance that the IRS will not take the position that the fees payable to the General Partner or the amounts reimbursed to the General Partner are not deductible by the Partnership in whole or in part. Due to the factual nature of the issue, the General Partner cannot predict the outcome of any challenge as to the reasonableness of the fees paid to the General Partner or as to the characterization of the fees for federal income tax purposes.

Under the Tax Reform Act of 1986, investment expenses (e.g., investment advisory fees) of an individual are deductible only to the extent they exceed 2% of his adjusted gross income. Pursuant to Temporary Regulations issued by the Treasury Department, this limitation on deductibility would not apply to an individual Limited Partner's share of the investment expenses of the Partnership to the extent that the Partnership is engaged in a trade or business within the meaning of the Code.

Whether the Partnership will be held to be engaged in a trade or business or in an investment activity will depend on the extent and nature of the Partnership's trading activity in any taxable year. This issue is largely resolved on an analysis of facts, many of which will be known only in the future. Moreover, it is unclear what legal standards would be applied to those facts.

The consequences of this limitation will vary depending upon the personal tax situation of each taxpayer. Accordingly, noncorporate Limited Partners should consult their tax advisors with respect to the application of this limitation.

## **Adjustment of Cost Basis of Partnership Assets**

The Partnership may agree, in the sole discretion of the General Partner, to make the election permitted under Section 754 of the Code to have the cost basis of its assets adjusted in the case of a distribution of property or in the case of a transfer of any Partnership Interest or interest therein.

In the case of such a transfer, such election will affect only the transferee party by requiring an adjustment of the basis of Partnership property which will reflect the difference between the cost to him of the Partnership Interest and his proportionate share of the Partnership's basis for its underlying property. Such adjustment may produce a difference between the amount of gains or losses on sales and other dispositions of Partnership property reportable by the transferee Partner, and the amount thereof reportable by other Limited Partners. Because the Partnership may have "unrealized receivables" (as defined in Section 751 of the Code) at the time of any transfer, the failure to make such an election may have adverse tax consequences to a potential transferee. Thus, if the General Partner does not agree in advance to make the election under Section 754 of the Code, the number of prospective transferees of a Partnership Interest may be limited. It should also be noted that once the election under Section 754 of the Code is made, it is applicable to all other and subsequent transfers and may not be revoked without the consent of the IRS.

## **Limitations on Interest Deductions**

Section 265(a)(2) of the Code disallows any deduction for interest paid by a taxpayer on indebtedness incurred or continued for the purpose of purchasing or carrying tax-exempt obligations. In Revenue Procedure 72-18, 1972-1 C.B. 740, the IRS stated that the proscribed purpose will be deemed to exist with respect to indebtedness incurred to finance a "portfolio investment," and that a limited partnership interest will be regarded as a "portfolio investment." Therefore, in the case of a Limited Partner owning tax-exempt obligations, the IRS might take the position that his allocable portion of any interest expense of the Partnership, or any interest expense incurred by him to purchase or carry a Partnership Interest, should be

considered as incurred to enable him to continue to carry tax-exempt obligations, and that the Limited Partner would not be allowed to deduct all or a portion of such interest.

In general, Section 163(d) of the Code limits the amount of investment interest (other than qualified residence interest and interest expense taken into account in determining income or loss arising from passive activities) that a noncorporate taxpayer can deduct in any taxable year to the net investment income of the taxpayer for the year. Net investment income is the excess of gross income from property held for investment plus any net short-term gain attributable to the disposition of property held for investment over investment expenses (other than interest) which are directly connected with the production of investment income. Net investment income does not include any income that is considered to arise from passive activities.

In the case of the Partnership, each Partner must take into account separately his share of the Partnership's investment interest. If a Partner cannot deduct his investment interest because of the limitations imposed by Section 163(d) of the Code, such excess may be carried forward to future years, when the same limitations would apply.

### **Tax-Exempt Investors**

The Partnership may have income which if derived directly by a Partner that is exempt from tax under Section 501(a) of the Code would be considered unrelated business taxable income, as defined in Section 512(a) of the Code. In addition, a Partner that is an exempt organization under Section 501(a) of the Code will be subject to tax on its "unrelated debt-financed income" pursuant to Section 514 of the Code. Each potential investor that is tax-exempt is urged to consult its own tax advisor about the tax consequences to it of an investment in the Partnership.

### **Audits**

The tax treatment of items of Partnership income, loss, deductions and credit will be determined in the unified audit of the Partnership and in subsequent unified administrative judicial proceedings, rather than in separate proceedings for each of the Partners. Generally, all Partners will be bound by the decision in the unified proceedings. The General Partner, as the "Tax Matters Partner" will represent the Partnership in the unified proceedings. The Tax Matters Partner will have considerable authority to make decisions affecting the tax treatment and procedural rights of all of the Partners. For example, it will decide how to report the Partnership's items on its tax returns. All Partners are required on their own returns, to treat Partnership items in a manner that is consistent with the treatment of the items on the Partnership's return (or attach a statement to the return identifying the inconsistency). In addition, the General Partner will have the right on behalf of all Partners to extend the statute of limitations with respect to the Partners' tax liability on Partnership items.

Simplified unified audit procedures are available to "electing large partnerships". Whether the Partnership will be eligible to elect the application of these procedures cannot be determined at present. The decision to become an "electing large partnership" shall, in any event, be made solely by the General Partner.

An audit of the Partnership may result in the disallowance, reallocation, deferral or allocation of income or losses claimed by the Partnership. Any such change may require that a Partner pay additional tax and interest.

An audit of the Partnership's information tax return may cause an audit of the individual income tax returns of a Partner. Hence, any audit might result in adjustments by the IRS to a Partner's items of income or loss unrelated to the Partnership.

The legal and accounting costs incurred in connection with any audit of the Partnership's tax returns will be borne by the Partnership. Partners will bear the costs of audits of their own returns.

## **Penalties and Interest on Deficiencies**

Section 6662 of the Code imposes a penalty of twenty percent of any substantial understatement of federal income tax. There is a substantial understatement of income tax for any taxable year if the amount of the understatement exceeds the greater of ten percent (10%) of the tax required to be shown on the return for the year or \$5,000. In the case of a Partnership item not attributable to a tax shelter, the amount of understatement does not include any portion of the understatement attributable to (a) the treatment of any item if there was substantial authority for such treatment, or (b) any item with respect to which the relevant facts affecting the item's tax treatment were adequately disclosed in the Partnership's return. In the case of a tax shelter, the penalty for substantial understatements of income tax may be avoided only if a more rigorous set of standards is satisfied. The General Partner believes that the Partnership is not a tax shelter within the standards set forth by certain Treasury Regulations regarding the substantial understatement penalty.

Any additional federal income tax due as a result of any such adjustment will bear interest. Interest will be compounded daily and the rates are adjusted quarterly, determined during the first month of each quarter to take effect the following quarter, and are based upon the federal short-term interest rate plus three percentage points. If the deficiency is deemed to be attributable to a "tax motivated transaction" the deficiency relating to a Partnership item may bear interest at 120% of the normal rate.

## **State and Local Taxes**

In addition to the federal income tax consequences described above, prospective investors should consider potential state and local tax consequences of an investment in the Partnership. An investor's distributive share of the taxable income or loss of the Partnership may be required to be included in determining his reportable income for state or local tax purposes in the state or locality in which he is a resident. In addition, other states or localities in which the Partnership may operate may require the filing of returns by nonresident partners and impose a tax on nonresident partners determined with reference to their pro rata share of Partnership income derived from the state or locality.

Each investor must consult his or her tax advisor for advice as to state and local taxes which may be payable in connection with an investment in the Partnership.

### **PRIME BROKER**

The Partnership's Prime Broker is Morgan Stanley & Co., 1585 Broadway, New York, New York 10036.

### **COUNSEL**

Wolf, Block, Schorr and Solis-Cohen LLP, 250 Park Avenue, New York, New York 10177, has acted as counsel to the General Partner in connection with this offering of Interests.

### **CERTIFIED PUBLIC ACCOUNTANTS**

The Partnership has retained Rothstein Kass & Company, 44 Montgomery Street, San Francisco, California 94104, as its independent auditors.

### **ADDITIONAL INFORMATION**

The General Partner is available to answer prospective investors' questions and will make available any additional information to the extent such information can be obtained without unreasonable effort or expense.

Prospective investors and/or their advisers are invited to communicate with the General Partner at the office, or by telephone at the telephone number, identified in the Summary.