

# American Federation of Labor and Congress of Industrial Organizations



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May 15, 2007

*Via electronic & U.S. mail*

Mr. John White, Director  
Division of Corporation Finance  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Mr. Andrew Donohue, Director  
Division of Investment Management  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

***Re: The Blackstone Group L.P. Initial Public Offering***

Dear Messrs. White and Donohue:

We are writing regarding the proposed public offering of The Blackstone Group L.P. ("Blackstone LP") to urge the U.S. Securities and Exchange Commission to make a detailed inquiry into whether it is an investment company. The Blackstone Group, an investment and advisory firm, organized Blackstone LP to be a publicly-traded limited partnership. We believe, based on the limited information provided in the Blackstone LP preliminary prospectus ("Prospectus"), that it is an investment company and should be subject to the Investment Company Act of 1940.

If Blackstone LP can avoid coverage under the Investment Company Act of 1940 ("Act"), it appears to us only a matter of time before other investment companies rely upon the devices used by Blackstone LP to avoid regulation under the Act.

Blackstone LP is an investment company for the following reasons:

- More than 40 percent of its unconsolidated assets consist of contracts creating direct interests in and call options on Blackstone Group's real estate and marketable alternative asset funds, all of which themselves are investment companies. These interests are securities. The Act requires any public whose assets are 40 percent investment securities to register as an investment company.
- The majority of the remainder of its assets are contracts creating interests in and call options on Blackstone Group's private equity funds, each of which is relying on exemptions under Sections 3(c)(1) and 3(c)(7) of the Act. Securities in funds relying on such exemptions are not themselves exempt from the definition of an investment security pursuant to Section 3(a)(2) of the Act.
- The structure of the Blackstone Group's family of funds strongly suggests that Blackstone LP does not in fact control in any meaningful sense the management of the Blackstone funds, and so Blackstone LP cannot rely on exemptions for the active managers of operating companies.<sup>1</sup>
- Were the Commission to accept Blackstone Group's assertion that Blackstone LP does indeed control the Blackstone funds, the Commission would also have to conclude that Blackstone LP is the continuation of the Blackstone Group under another name, a business which has held itself out for years as an investment company.
- Blackstone LP's tax position that it is a passive investor is inconsistent with its assertion that it is entitled in any way to treatment as an active manager of operating companies.

The Act exists to address Congress's concern that "the national public interest and the interest of investors are adversely affected when investors purchase, pay for, exchange, receive dividends upon, vote, refrain from voting, sell, or surrender securities issued by investment companies, without adequate, accurate, and explicit information, fairly presented, concerning the character of such securities and the circumstances, policies, and financial responsibility of such companies and their management."<sup>2</sup> It was drafted to address the essential differences between direct investments in public companies and participating in pooled investment vehicles, and the resulting necessity that investment companies be subject to enhanced disclosure and reporting requirements.

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<sup>1</sup> Blackstone funds "refers to the corporate private equity funds, real estate opportunity funds, funds of hedge funds, mezzanine funds, senior debt vehicles, proprietary hedge funds and closed-end mutual funds managed by Blackstone" Group. Amended S-1 filed May 1, 2007. Page iii.

<sup>2</sup> The Investment Company Act of 1940 §1(b).

“The fundamental purpose undergirding the Securities Acts is ‘to eliminate serious abuses in a largely unregulated securities market.’<sup>3</sup> In defining the scope of the market that it wished to regulate, Congress painted with a broad brush.... Congress’ purpose in enacting the securities laws was to regulate investments, in whatever form they are made and by whatever name they are called.”<sup>4</sup>

These powers exist precisely so the Commission can seek to protect the integrity of the investment company regulatory structure when faced with offerings, such as that of Blackstone LP, designed to evade the Act.

## **I. Structure of Blackstone LP**

- A. Blackstone LP will be managed by the same individuals who manage the Blackstone funds—these individuals will have no financial interest in or legal duties to Blackstone LP.

Blackstone LP will be a limited partnership with 100 percent of the limited partnership interests held by the public.<sup>5</sup> Blackstone Management Group LLC (“Blackstone Management”) is the general partner of Blackstone LP—but will hold no economic interest in Blackstone LP.<sup>6</sup> Senior managing directors hold a 100 percent equity interest in Blackstone Management’s \$1 in assets.<sup>7</sup> Blackstone Management’s only business will be managing the day-to-day operations of Blackstone LP.

Blackstone LP will be the 100 percent owner of a group of Delaware and Alberta corporations and limited partnerships. These corporations and limited partnerships are named “Blackstone Holdings I G.P.” through “Blackstone Holdings V G.P.” These companies collectively are referred to in the Prospectus as Blackstone LP’s wholly-owned subsidiaries. These entities are the general partners of three Delaware and two Alberta limited partnerships titled “Blackstone Holdings I L.P.” through “Blackstone Holdings V L.P.” These entities are referred to in the Prospectus as “Blackstone Holdings.” The majority of the economic interest in Blackstone Holdings is held by the senior managing directors and other existing owners of Blackstone Group. The operating management of Blackstone Holdings rests in Blackstone Group Management LLC, an entity which is also wholly-owned and controlled by the senior managing directors of Blackstone Group.<sup>8</sup>

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<sup>3</sup> United Housing Foundation, Inc. v. Forman, 421 U.S. 837, 849 (1975).

<sup>4</sup> Reves v. Ernst & Young, 494 U.S. 56, 60-61 (U.S. 1990).

<sup>5</sup> Amended S-1 filed May 1, 2007. Page 15.

<sup>6</sup> According to Delaware Division of Corporations, Blackstone LP and its general partner, Blackstone Management LLC were organized March 12, 2007. See *Delaware Division of Corporations – Online Services* at <https://sos-res.state.de.us/tin/controller>; accessed May 10, 2007. See also Amended S-1 Filed May 1, 2007.

<sup>7</sup> Amended S-1 filed May 1, 2007. Page F-5.

<sup>8</sup> Amended S-1 filed May 1, 2007. Pages 66-71.

The Blackstone LP partnership agreement provides for Blackstone LP to reimburse Blackstone Management for expenses accrued in performing its management functions. However, Blackstone LP will not pay Blackstone Management any fees. In light of these facts, it appears that Blackstone Management will have no revenue-generating function. Neither Blackstone LP nor Blackstone Management will produce income for the benefit of Blackstone Group's senior managing directors or existing owners.<sup>9</sup> However, these same individuals have substantial interests in the intermediate entities in the Blackstone Group structure, the Blackstone Holdings.<sup>10</sup>

Substantially all the assets of Blackstone LP will be (1) the investment advisers of all of Blackstone Group's investment funds; (2) the entities that are the managing members of the general partners of Blackstone Group's actively investing carry funds and the historical carry funds that still have a meaningful amount of unrealized investments;<sup>11</sup> (3) the entity that is the manager of Blackstone Group's senior debt vehicles; (4) the entities that are the managing members of the general partners of Blackstone Group's funds of hedge funds, distressed securities hedge fund and equity hedge fund; (5) the investment advisers of the distressed securities hedge fund and the equity hedge fund; (6) Blackstone Advisory Services L.P.; and (7) Park Hill Group. We will analyze the economic content of these assets below.

After the public offering, Blackstone Management will be responsible for Blackstone LP's management and operation and, through Blackstone LP's subsidiaries and general partnership interests, will conduct the business that the Blackstone Group operating companies currently conduct.<sup>12</sup> It is unclear, legally, how Blackstone Management will conduct these investment advisory businesses since neither Blackstone Management nor Blackstone LP is a registered investment advisor.<sup>13</sup>

Blackstone LP's structure seems intended to create an arrangement the Act was explicitly drafted to prevent—"when investment companies are organized, operated, managed, or their portfolio securities are selected, in the interest of directors, officers, investment advisers, depositors, or other affiliated persons...rather than in the interest of all classes of such companies' security holders."<sup>14</sup>

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<sup>9</sup> Amended S-1 filed May 1, 2007. Page 17.

<sup>10</sup> Amended S-1 filed May 1, 2007. Page 15.

<sup>11</sup> Blackstone Capital Partners V, Blackstone Real Estate Partners VI, Blackstone Real Estate Partners International II, Blackstone Mezzanine Partners II, Blackstone Capital Partners IV, Blackstone Communications Partners, Blackstone Real Estate Partners IV, Blackstone Real Estate Partners V, Blackstone Real Estate Partners International I and Blackstone Mezzanine Partners I.

<sup>12</sup> Amended S-1 filed May 1, 2007; Page F-3.

<sup>13</sup> Since Blackstone LP is holding itself out to the public as an investment advisor, it does not fall within the exemption from registration provided by §203(b)(2) of the Investment Advisers Act of 1940.

<sup>14</sup> Investment Company Act of 1940 §1(b)(2).

- B. Blackstone LP's assets consist of general partnership interests in the returns from the Blackstone funds.

Blackstone LP reports that it will have \$5.206 billion in assets, on a deconsolidated basis. Of those assets, \$4.333 billion, or 83.23 percent, are "investments at fair value."<sup>15</sup> These investments are comprised of (1) \$900 million resulting from the deconsolidation and the application of fair value accounting; (2) \$2.276 billion in general partners' interests in the Blackstone funds; and (3) \$1.155 billion in employee funds.

- C. Economically, Blackstone LP's assets consist primarily of direct interests in the Blackstone funds in the form of general partners' contributed capital and employee funds and call options on those funds in the form of carried interest.

The employee funds and the general partners' contributed capital are clearly investment securities for purposes of the Act. These assets represent direct interests in the Blackstone funds which are all either registered as investment companies under the Act or operating under exemptions for privately-held investment companies that do not apply here.<sup>16</sup> They appear to be economically identical to the limited partnership interests held by third-party investors in the Blackstone funds.

A large portion of Blackstone LP's assets are the estimated fair value of Blackstone LP's carried interests in the Blackstone funds.<sup>17</sup> Carried interest entitles the general partners to a portion, generally 20 percent, of the investment returns of the Blackstone funds.<sup>18</sup> It is our understanding that generally when an investment manager receives carried interest, investment returns must exceed a contractually agreed upon benchmark before the investment manager is entitled to carried interest.

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<sup>15</sup> "Investors in our common units should note that Blackstone's corporate private equity and real estate opportunity funds have historically been consolidated into Blackstone's financial statements, notwithstanding that Blackstone has only a minority interest in these funds. Consequently, our historical financial statements do not reflect the net asset value of our investments in such funds, but reflect rather on a gross basis the assets, liabilities, revenues, expenses and cash flows of these funds. We intend to deconsolidate all of our funds that have historically been consolidated in our financial statements with the exception of four of our funds of hedge funds. Accordingly, we will no longer record the non-controlling interests' share of these fund's partners' capital and net income.... We believe that the deconsolidation of these funds by means of granting investors in these funds general partner removal rights or liquidation rights, as the case may be, will result in our financial statements reflecting our alternative asset management business, including our management fee, incentive fee and performance fee revenues, in a manner that reflects both how our management evaluates our business and the risks of the assets and liabilities of our firm. Accordingly, we believe that deconsolidating these funds will provide investors reviewing our financial statements an enhanced understanding of our business." Amended S-1 filed May 1, 2007. Page 5.

<sup>16</sup> Amended S-1 filed May 1, 2007. Page 160.

<sup>17</sup> See "Notes to Unaudited Condensed Consolidated Pro Forma Statement of Financial Condition: Adjustments for Deconsolidation of Blackstone Funds." Amended S-1 filed May 1, 2007. Page 83.

<sup>18</sup> Amended S-1 filed May 1, 2007. Page 101.

This fair value estimate is largely based on estimates of Blackstone LP's contractual entitlement to future returns on investments made by the Blackstone funds. Economically, the carried interests are call options on the pools of securities that are held by the Blackstone funds. Since call options are securities under the Act, Blackstone LP's general partnership interests are securities.

## **II. Blackstone LP's assets are investment securities.**

Blackstone LP asserts that it is offering to the public an interest in the income from an asset management business. This is not true. Blackstone LP is a vehicle for offering interests in managed assets, assets which are securities.

Blackstone LP's assets are almost entirely shares of pools of direct interests in and call options on pools of securities.<sup>19</sup> Consequently, Blackstone LP should be regulated as an investment company under the Act. Any other conclusion would allow investment companies to sell shares to the general public by inserting otherwise purposeless general partnership interests between the investment company and the publicly-offered company.

A. Blackstone LP says these interests are not securities because they are in the form of interests in general partners of limited partnerships.

Blackstone LP states in its Prospectus that it does not "believe the equity interests of The Blackstone Group L.P. in its wholly-owned subsidiaries or the general partner interests of these wholly-owned subsidiaries in the Blackstone Holdings partnerships are investment securities"<sup>20</sup> Blackstone LP offers no supporting evidence or argument other than this statement for why Blackstone LP should not be treated as an investment company under the Act.

B. There is no statutory exemption for general partners of limited partnerships, and there is specific statutory coverage for any economic arrangement with the content embodied in the subsidiary structure of Blackstone LP.

General partnership interests are not per se excluded from the definition of securities under the Act. The distinction between general partnership interests and limited partnership

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<sup>19</sup> See Investment Company Act of 1940, §2a-36. "'Security' means any note, stock, treasury stock, security future, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, *any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof)*, or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing." [emphasis added]

<sup>20</sup> Amended S-1 filed May 1, 2007; Page 57.

interests is often used to determine whether a partnership interest is an “investment contract” and therefore an investment security under the securities laws.<sup>21</sup> In this case, however, Blackstone LP’s general partnership interests fall within the statutory definition of a security—they are direct interests in and call options on a group of securities.

Specifically, they are an “option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof).”<sup>22</sup>

**III. The Investment Company Act of 1940 requires any public company whose unconsolidated assets are more 40 percent investment securities to register as an investment company. Eighty-three (83) percent of Blackstone LP’s assets are investment securities for purposes of determining whether it is an investment company under the Act.**

It appears, from the financial statements included in the Prospectus, that after the IPO Blackstone LP will have, on a deconsolidated basis, \$5.21 billion in total assets, \$4.33 billion of which will be investment securities.<sup>23</sup> In other words, 83.1 percent of Blackstone LP’s unconsolidated assets are interests in and call options on groups of securities in the Blackstone funds that are either registered investment companies or are exempt from the registration pursuant to section 3(c)(1) or 3(c)(7) of the Act. Securities issued by funds which rely on those exemptions are not exempt from being categorized as investment securities for purposes of determining whether a company which holds them is an investment company.<sup>24</sup>

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<sup>21</sup> “Security” means any note, stock, treasury stock, security future, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a “security”, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.” § 2a-36 of the Investment Company Act of 1940.

<sup>22</sup> Investment Company Act of 1940, §2(b)(36).

<sup>23</sup> S-1 filed May 1, 2007. Page 5.

<sup>24</sup> 1. When used in this title, “investment company” means any issuer which--

- A. is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities;
- B. is engaged or proposes to engage in the business of issuing face-amount certificates of the installment type, or has been engaged in such business and has any such certificate outstanding; or
- C. is engaged or proposes to engage in the business of investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 40 percentum of the value of such issuer’s total assets (exclusive of Government securities and cash items) on an unconsolidated basis.

2. As used in this section, “investment securities” includes all securities except (A) Government securities, (B) securities issued by employees’ securities companies, and (C) securities issued by majority-owned

As noted earlier, we believe that Blackstone LP's general partnership interests in the Blackstone funds are most appropriately characterized as call options. These interests are investment securities for purposes of determining whether 40 percent of Blackstone LP's assets are investment securities, and Blackstone LP falls within the definition of an investment company under Section 3a-1 of the Act.

Blackstone LP has not disclosed the proportion of its deconsolidated assets that are attributable to interests in each category of the Blackstone funds. The absence of this material information makes it difficult to analyze this offering. *In the analysis below, we are estimating the proportions based on the composition of Blackstone Group's assets under management.*

#### A. Marketable Alternative Asset Management Assets

We estimate that claims on "marketable alternative asset" funds account for \$1.6 billion, or 30 percent, of Blackstone LP's investment assets. These funds include funds of hedge funds, mezzanine funds, senior debt vehicles, proprietary hedge funds and publicly-traded closed-end mutual funds.<sup>25</sup> Each of these businesses is either registered as an investment company under the Act or relies on exceptions from the registration requirements that are available to companies that do not sell securities to the general public.<sup>26</sup> When determining whether 40 percent of Blackstone LP's assets are investment securities, Blackstone LP must include securities issued by its investment company subsidiaries, regardless of whether the investment company qualifies for such an exemption from registration.<sup>27</sup>

#### B. Real Estate Assets

We estimate that \$1 billion, or 19 percent, of Blackstone LP's assets are invested in Blackstone Group's real estate funds. Real estate is generally considered an investment security unless the purchaser retains direct control of the property and is not directly involved in managing the property.<sup>28</sup> In contrast, "when a purchaser is motivated by a desire to use or consume the item purchased—to occupy the land or to develop it themselves'... the securities laws do not apply."<sup>29</sup>

Blackstone Group's real estate investment strategy is to select "properties that suffer from temporary or correctable flaws in their tenancy, physical attributes, capital structures, market position and/or management. By exploiting the pricing and operating inefficiencies inherent in

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subsidiaries of the owner which (i) are not investment companies, and (ii) are not relying on the exception from the definition of investment company in paragraph (1) or (7) of subsection (c).

<sup>25</sup> Amended S-1 filed May 1, 2007. Page 2.

<sup>26</sup> Amended S-1 filed May 1, 2007. Page 160.

<sup>27</sup> See supra n. 22.

<sup>28</sup> *Fargo Partners v. Dain Corp.* 540 F2d 912.

<sup>29</sup> *United Housing Found., Inc. v. Forman*, 421 U.S. 837, 852-853 (U.S. 1975).

assets of this nature and employing intensive asset management to correct the identified flaws, [Blackstone Group] can reposition such assets for subsequent sale to institutional investors at attractive pricing.”<sup>30</sup> Blackstone Group’s explanation of the investment strategies applied for real estate investments leads to the conclusion that most, if not all, of its real estate holdings are passive investments.

To the extent that a Blackstone Group entity manages or controls the properties held in the Blackstone Group’s real estate investment portfolios, these functions are performed by the investment advisers, not Blackstone LP or its general partner.<sup>31</sup> Blackstone LP’s assets that are invested in the real estate funds, therefore, are investment securities within the Act definition.

### C. Corporate Private Equity Assets

We estimate that Blackstone LP has \$1.7 billion in claims on Blackstone Group’s corporate private equity funds, which constitute 33.7 percent of Blackstone LP’s total assets. Since these funds rely on exemptions under section 3(c)(1) or 3(c)(7) of the Act, these assets are not exempt from being categorized as investment securities for purposes of determining whether Blackstone LP is an investment company.<sup>32</sup>

Assets that are invested in the corporate private equity business may escape characterization as investment securities if Blackstone LP maintains an active role in the day-to-day management of the Blackstone funds’ portfolio companies. However, the Prospectus’ explanation of the structure and operation of Blackstone Group’s investment funds forecloses this possibility.<sup>33</sup> The day-to-day operations of the Blackstone funds are managed by the funds’ registered investment advisers, and the general partners make “all policy and investment decisions.”<sup>34</sup> Blackstone LP will not be, in any sense, the active manager of any of the Blackstone funds. A further analysis of this point follows.

The Investment Company Act of 1940 requires any public company whose unconsolidated assets are more than 40 percent investment securities to register as an investment company. More than 40 percent of the assets of Blackstone LP consist of contracts creating direct interests in and call options on Blackstone Group’s real estate and marketable alternative asset funds, all of which themselves are investment companies. The majority of the remainder of Blackstone LP’s assets are contracts creating interests in and call options on Blackstone Group’s private equity funds, each of which is relying on exemptions under Sections 3(c)(1) and 3(c)(7) of the Act. Securities in funds relying on such exemptions are not themselves exempt from the definition of an investment security pursuant to Section 3(a)(2) of the Act.

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<sup>30</sup> Amended S-1 filed May 1, 2007. Page 147.

<sup>31</sup> Amended S-1 filed May 1, 2007. Page 160.

<sup>32</sup> See supra n. 22.

<sup>33</sup> Amended S-1 filed May 1, 2007. Page 160.

<sup>34</sup> Amended S-1 filed May 1, 2007. Page 160.

**IV. Blackstone LP will not be the active manager of any of Blackstone Group's funds, and in particular the private equity funds.**

- A. Blackstone LP acts through its general partner, but the general partner itself has no economic interest in Blackstone LP.

Blackstone Management will serve as the general partner of Blackstone LP and be responsible for Blackstone LP's management and operations. However, Blackstone Management will have no economic interest in Blackstone LP. Blackstone Management is wholly-owned and operated by Blackstone Group's senior managing directors and founders.<sup>35</sup> Since Blackstone Management's sole enterprise is the management of Blackstone LP and Blackstone Management has no duty to act in the interest of Blackstone LP, there is no basis to conclude that Blackstone Management, despite its status as general partner of Blackstone LP, will indeed act in Blackstone LP's interest.<sup>36</sup>

- B. The individuals who own and control the general partner simultaneously have large economic interests in Blackstone Holdings, which directly or through other general partners controls the operating entities which manage the Blackstone funds.

Blackstone Holdings are limited partnerships located in the corporate structure in between Blackstone LP and the Blackstone funds. Substantially all of the assets of Blackstone LP are held through Blackstone Holdings, but Blackstone LP is not the majority economic interest in Blackstone Holdings. As shown in the chart on page 69 of the Prospectus, senior managing directors and other existing owners of Blackstone Group are the majority investors in Blackstone Holdings level and have no economic interest in Blackstone LP.

Prior to the IPO, Blackstone Group's existing owners will contribute their interests in Blackstone Group's operating entities to Blackstone LP and, in exchange, will receive partnership units in Blackstone Holdings.<sup>37</sup> After the public offering, Blackstone Group's employees and other existing owners will have the option to trade their partnership units in Blackstone Holdings for common units of Blackstone LP, however, there will be no automatic conversion. Blackstone Group's employees will still be required to hold minimum interests in Blackstone Holdings. Equity incentive awards granted to Blackstone Group employees will continue to be units of the Blackstone Holdings, not units of Blackstone LP.<sup>38</sup> As a result, Blackstone Group's senior managing directors and other employees will maintain significant economic interests in Blackstone Holdings and have no interest in Blackstone LP.

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<sup>35</sup> Amended S-1 filed May 1, 2007. Page 14.

<sup>36</sup> Amended S-1 filed May 1, 2007. Page 53.

<sup>37</sup> Amended S-1 filed May 1, 2007. Page 17.

<sup>38</sup> Amended S-1 filed May 1, 2007. Page 98.

The primary difference between partnership interests in Blackstone Holdings and common units of Blackstone LP is that investors in Blackstone Holdings have a more direct interest in the returns from the Blackstone funds. Blackstone LP's unitholders will receive distributions on the income from the Blackstone funds only after Blackstone Management extracts money to pay business expenses or reinvest in the Blackstone funds.<sup>39</sup> With this in mind, it seems that the only reason someone who holds a partnership interest in Blackstone Holdings would exchange that interest for a common unit of Blackstone LP is if they are seeking to liquidate their interests in the Blackstone Holdings.

C. Blackstone LP has only a minority interest in Blackstone Holdings.

The public offering of Blackstone LP was structured to preserve the management structure of Blackstone Group and the economic interests of the existing owners. Blackstone LP's common unitholders' economic interests in Blackstone Holdings will be secondary to the interests of the existing owners.<sup>40</sup> They will also lack meaningful voting rights and will have almost no authority to influence management decisions related to Blackstone LP or the Blackstone funds.<sup>41</sup>

D. The offering document makes clear that in cases of conflicts between the interests of Blackstone Holdings and the interests of Blackstone LP, the individuals who control Blackstone Holdings are under no obligation to act in the interests of Blackstone LP.

According to the Prospectus, if conflicts arise between the interests of Blackstone LP's common unitholders and Blackstone Management, Blackstone Group's existing owners or investors in the Blackstone funds, Blackstone Management has no duty to act in the best interests of Blackstone LP.<sup>42</sup>

E. Blackstone Management LLC is not obligated to act in the interests of Blackstone LP and is free to act in the interests of the individuals who are the majority holders of Blackstone Holdings.

As noted above, Blackstone Management, the entity responsible for Blackstone LP's day-to-day business operations, asserts it has no fiduciary duties to Blackstone LP and the structure of the offering restricts any legal remedies available to Blackstone LP.<sup>43</sup> In doing so, Blackstone Management reserves the right to make business decisions that benefit Blackstone Group's senior managing directors and existing owners and adversely effect Blackstone LP.

F. These facts lead inescapably to the conclusion that it is the individuals associated with

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<sup>39</sup> Amended S-1 filed May 1, 2007. Page 17.

<sup>40</sup> Amended S-1 filed May 1, 2007. Page 70.

<sup>41</sup> Amended S-1 filed May 1, 2007. Page 52.

<sup>42</sup> Amended S-1 filed May 1, 2007. Page 53.

<sup>43</sup> Amended S-1 filed May 1, 2007. Page 17.

the Blackstone Group, in their individual capacities, and through the Blackstone Holdings, who are the active managers of the Blackstone funds, not Blackstone LP.

Under no circumstances should the Commission ascribe whatever powers Blackstone Group's senior managing directors and other employees have over the Blackstone funds to Blackstone LP. After the public offering is complete, the actual management of Blackstone Group's investment funds will continue to be performed by Blackstone Group's operating entities, and Blackstone Group's employees and existing owners will continue to extract investment returns from these operating entities.

With all of these factors in mind, it becomes clear that this new corporate structure serves no practical purpose aside from creating a mechanism for Blackstone Group to sell its shares to the public without being regulated by the Commission or losing pass-through tax treatment.

This "advisory business" Blackstone Group seeks to sell to the public is not registered as an investment adviser under the Investment Advisers Act of 1940 and its general partner is not a registered investment adviser. There is not one individual within this new corporate structure that has any legal or economic interest that is aligned with the interests of Blackstone LP's unitholders.

**V. If Blackstone LP is a continuation of Blackstone Group and not a passive vehicle, since Blackstone Group has held itself out for years as an investment company, then Blackstone LP is an investment company.**

"Any issuer which is or holds itself out as being engaged, primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities" is an investment company under §3a-1(A) of the Act.

The Blackstone Group has historically operated the Blackstone funds under exemptions from the Act applicable to companies that do not sell shares to the general public. The Blackstone Group has a 20-year history and is well known in the investment community as a company that pools assets from high net worth individuals and institutional investors and invests in securities. Blackstone Group's own website identifies the company as "a leading global investment and advisory firm."

It does not appear that the publicly-traded Blackstone LP's business model will be any different from that of The Blackstone Group, which is and always has been an investment company, except to the extent, which we address above, that the actual management of Blackstone funds does not reside in Blackstone LP.

Section 48a of the Act provides that "[i]t shall be unlawful for any person, directly or indirectly, to cause to be done any act or thing through or by means of any other person which it would be unlawful for such person to do under the provisions of this title or any rule, regulation,

or order thereunder.” Blackstone Group cannot, through Blackstone LP, sell interests in its pooled investment vehicles to the public without first registering these securities with the Commission or obtaining an exemption.

**VI. Blackstone LP’s assertion that it is an active operating management entity is inconsistent with its tax position.**

Blackstone LP states in its Prospectus that it will be seeking capital gains tax treatment for its carried interest income. If that income was really being generated by active management activity, claiming capital gains treatment for tax purposes would be inappropriate. Blackstone Group’s current structure allows it pass-through tax treatment. This treatment is not available to publicly-traded partnerships under §7704. Blackstone LP attempts to maintain pass-through tax treatment after the IPO through reliance on §7704(c), which allows publicly-traded partnerships that earn at least 90 percent of their net income from dividends, interest, capital gains from the sale or other disposition of stocks and securities, and certain other forms of investment income to maintain pass-through tax treatment.

We cannot see how Blackstone LP can be eligible for pass-through treatment under §7704 and not be a prima facie investment company under Rule 3a-1 of the Act.

**VII. Blackstone Group is not wholly precluded from selling its shares in the public market, However, it must do so within the boundaries defined by Congress.**

Congress has created special rules that apply to private equity companies that wish to sell their shares on the public market.<sup>44</sup> Congress has created laws providing for the creation of “Business Development Companies” that allow private equity companies to offer shares to the general public provided that they register under the Act and comply with regulatory requirements designed to address investor protection issues specific to these types of enterprises. American Capital Strategies, Ltd. (“ACAS”) is an example of a private equity company that is registered under the Act.

According to the American Capital Strategies, Ltd. (“ACAS”) prospectus filed March 30, 2007, ACAS is the second largest publicly-traded alternative asset manager in the United States.<sup>45</sup> ACAS, like Blackstone Group, includes an investment advisory business and an investment portfolio. ACAS provides asset management services to the ACAS investment funds through wholly-owned consolidated operating subsidiaries or wholly-owned portfolio companies. The ACAS investment funds include private equity, real estate and alternative asset management businesses.

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<sup>44</sup> Definition of Eligible Portfolio Company under the Investment Company Act of 1940. File No. S7-37-04. SEC Release No. IC-27538; 17 CFR Part 270; RIN 3235-AJ31. 2006 SEC LEXIS 2469. October 25, 2006.

<sup>45</sup> <http://www.sec.gov/Archives/edgar/data/817473/000119312507091970/dn2.htm>

ACAS, like Blackstone Group, qualifies for pass-through tax treatment. As a regulated investment company, ACAS is not subject to federal income tax on the portion of its taxable income and capital gains it distributes to stockholders. Unlike Blackstone Group, ACAS maintains this favorable tax treatment through compliance with Subchapter M of the Internal Revenue Code, which is only available to companies that comply with source of income, diversification or distribution requirements defined in Subchapter M and are regulated under the Act.

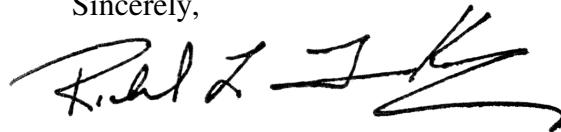
The business models of ACAS and Blackstone LP are nearly identical. It looks like the major difference between the two companies is that ACAS has chosen to comply with the Internal Revenue Code and the Act. If the Commission allows Blackstone Group to proceed with the proposed public offering, we fear it is only a matter of time before other publicly-traded investment companies may circumvent regulation.

### **VIII. Conclusion**

The Commission has an obligation to ensure that the Act is not evaded or undermined. While important aspects of the Blackstone LP Prospectus are unclear or opaque, there appears to be significant evidence in the Prospectus that Blackstone LP is attempting to evade the coverage of the Act by using a variety of devices, including layers of purposeless limited partnerships, to hide the simple fact that Blackstone LP is a vehicle for selling to the public a mix of direct interests in and call options on Blackstone funds without complying with the disclosure, fee regulations and other investor protections provided by the Act.

This strategy, if successful, could be duplicated by any number of issuers. Consequently, we urge the Commission to require Blackstone LP to register as an investment company before allowing it to sell its securities to the public. If we can be of further assistance to the Commission staff in this matter, please contact Damon Silvers at 202-637-3953. Thank you.

Sincerely,

A handwritten signature in black ink, appearing to read "Richard L. Trumka", with a stylized flourish at the end.

Richard L. Trumka

RLT/me  
opieu #2, afl-cio

cc: Chairman Christopher Cox  
Commissioner Paul S. Atkins  
Commissioner Roel C. Campos  
Commissioner Annette L. Nazareth  
Commissioner Kathleen L. Casey  
Stephen A. Schwarzman, The Blackstone Group Chairman and CEO