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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

In the Matter of

Full Value Advisors, LLC et al.
60 Heritage Drive
Pleasantville, NY 10570

APPLICATION FOR AN ORDER PURSUANT TO §13(f)(2) OF THE
SECURITIES EXCHANGE ACT OF 1934 (THE "1934 ACT") FOR EXEMPTION
FROM RULE 13f-1 OF THE 1934 ACT

File No. -----

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UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

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This is an application for an order pursuant to §13(f)(2) of the 1934 Act to exempt the Applicants from the reporting requirements set forth in rule 13f-1 of the 1934 Act. Involuntary compliance with the filing requirement of rule 13f-1 would, by requiring the Applicants to publicly disclose their trade secrets, constitute a "taking" of their property without just compensation in violation of the Fifth Amendment to the Constitution. An exemption from the filing requirement of rule 13f-1 is necessary to avoid such a violation. As set forth herein, the requested relief is also consistent with the public interest and the protection of investors and with the purposes of §13(f).

Section §13(f)(1) of the 1934 Act generally requires every institutional investment manager that exercises investment discretion over accounts holding equity securities having an aggregate fair market value on the last trading day in any of the preceding twelve months of at least \$100,000,000 to file reports with the Commission disclosing, among other things, each equity security held in such form as the Commission, by rule, may prescribe. Rule 13f-1 of the 1934 Act requires each such institutional investment manager to file a report on Form 13F with the Commission within 45 days after the last day of such calendar year and within 45 days after the last day of each of the first three calendar quarters of the subsequent calendar year.

Section 13(f)(2) of the 1934 Act states: "The Commission, by rule or order, may exempt, conditionally or unconditionally, any institutional investment manager or security or any class of institutional investment managers or securities from any or all of the provisions of this subsection or the rules thereunder."

Section 13(f)(4) of the 1934 Act states: "In exercising its authority under this subsection, the Commission shall determine (and so state) . . . in granting an exemption, that its action is consistent with the protection of investors and the purposes of this subsection. In exercising such authority the Commission shall take such steps as are within its power, including consulting with the Comptroller General of the United States, the Director of the Office of Management and Budget, the appropriate regulatory agencies, Federal and State authorities which, directly or

indirectly, require reports from institutional investment managers of information substantially similar to that called for by this subsection, national securities exchanges, and registered securities associations, (A) to achieve uniform, centralized reporting of information concerning the securities holdings of and transactions by or for accounts with respect to which institutional investment managers exercise investment discretion, and (B) consistently with the objective set forth in the preceding subparagraph, to avoid unnecessarily duplicative reporting by, and minimize the compliance burden on, institutional investment managers. Federal authorities which, directly or indirectly, require reports from institutional investment managers of information substantially similar to that called for by this subsection shall cooperate with the Commission in the performance of its responsibilities under the preceding sentence.”

I. Preface

Truly good investment ideas are simply rare commodities, particularly so when price discipline is so infused into our decision making process. We expend considerable research effort, through a combination of company visits, industry conferences, and trade shows. This face-to-face, hands-on research is intrinsic to our investment process and critical to our ability to analyze the merits of investments under consideration.

Oak Value Fund

As administered, there is no rational relationship between the disclosure scheme of §13(f)(1) and any legitimate government interest.

The legislative history of §13(f) indicates that its primary purpose was to fill an information gap about the activities of institutional investment managers that would enable the Commission to devise regulatory initiatives.¹ However, the Commission has never used the data in 13F filings for that purpose. Therefore, despite Congress’ intent in 1975 when it adopted §13(f), there has been no actual connection between the disclosure scheme of §13(f)(1) and any regulatory use of the resultant data disclosures.

The secondary asserted government interest underlying the disclosure scheme of §13(f)(1) is to “increase investor confidence in the integrity of the United States

¹ Among the uses for this information that were suggested for the SEC were to analyze the effects of institutional holdings and trading in equity securities upon the securities markets, the potential consequences of these activities on a national market system, block trading and market liquidity, direct trading between institutions in the “fourth” market, and the effect of institutional trading on brokerage services. See generally Hearings on Securities Act Amendments of 1975 Before the Subcomm. on Oversight and Investigations and the Subcomm. on Consumer Protection and Finance of the House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess. 545 (1977) (Statement of the Securities and Exchange Commission) (“SEC Statement”)

securities markets.”² The government does have a legitimate interest in adopting laws or regulations that actually improve the integrity of the United States securities markets. However, that is not the objective of §13(f). Moreover, to the extent that §13(f) achieves its objective, investors will be overconfident in the integrity of securities markets. That undermines the primary goal of the federal securities laws, i.e., protecting investors because they will be less likely to conduct due diligence reviews before making inherently risky investment decisions.³ In other words, if §13(f)(1) does increase investor confidence⁴ (which is doubtful) the result is greater losses for investors.⁵

On the other hand, many §13(f)(1) filers and their clients are subjected to actual harm. That harm is explained in an article in the March 11, 2006 edition of The Hartford Courant by Ritu Kalra entitled: “Digging In On Hedge Funds; Lawmakers Try Another Tack After Bill Dies,” concerning a proposed state law to require Connecticut-based hedge funds to disclose their investments:

And disclosing detailed holdings could wipe out a hedge fund’s competitive advantage, the industry pointed out. That would hurt rather than help investors.

“When a drug company has a breakthrough, the U.S. patent office trademarks [sic] their discovery. That same patent protection does not exist for hedge funds, who are out there uncovering inefficient markets. The only protection against their discovery is secrecy,” said Steve McMenamin, managing partner of Indian Harbor LLC, which matches hedge funds with potential investors. “It’s not that they’re doing anything wrong. They’re just trying to protect themselves and their investors.”

Unless exempted from §13(f)(1), the Applicants would have to publicly disclose their trade secrets without compensation in violation of the Taking Clause of the Fifth Amendment of the Constitution.

II. The Applicants

The Applicants are Full Value Advisors, LLC and any other institutional investment

² (“Congress believed that this institutional disclosure program would increase investor confidence in the integrity of the United States securities markets.”) Division of Investment Management: Frequently Asked Questions About Form 13F, May 2005

³ See The Government Should Not Try to Promote “Investor Confidence” by Alex J. Pollock, American Enterprise Institute for Public Policy Research, Financial Services Outlook April 2005 at http://www.aei.org/publications/pubID.22232,filter.all/pub_detail.asp (“Efforts to encourage investor confidence are fundamentally misguided. A skeptical disposition . . . is much better for investors and for the proper functioning of securities markets and the economy as a whole.”)

⁴ Even if investor confidence was a legitimate government interest, there is no rational relationship between §13(f)(1) and greater investor confidence as will be discussed herein.

⁵ To illustrate the point, consider two options, both of which could increase a pilot’s confidence: intensive flight training or a heavy bout of drinking. The former increases airline safety; the latter decreases it.

managers that in the future may be controlling, controlled by, or under common control with Full Value Advisors, LLC. Full Value Advisors, LLC is the investment manager for Full Value Partners L.P., a private investment fund that holds equity securities with an aggregate fair market value on March 31, 2006 of more than \$100 million. Therefore, absent the requested relief, Full Value Advisors, LLC will be required to file a Form 13F by February 14, 2007.

The Applicants are value oriented activist investors. They seek to acquire meaningful stakes in publicly traded companies whose stocks they have concluded, after extensive research, are undervalued and to influence management to take action to increase the stock prices. To that end, since 1996 the Applicants have conducted more than 20 proxy contests and submitted numerous shareholder proposals pursuant to rule 14a-8 of the 1934 Act.

III. Analysis

In 1975, Congress adopted §13(f) of the 1934 Act. §13(f)(3) authorizes “the Commission, as it determines to be necessary or appropriate in the public interest or for the protection of investors, [to] delay or prevent public disclosure of any such information in accordance with section 552 of Title 5.” However, it does not compel the Commission to prevent public disclosure of trade secrets nor does it provide for compensation to an institutional investment manager whose trade secrets are disclosed. In addition, §13(f)(1) is not rationally related to any legitimate government interest. The fact that confidentiality treatment may be sought on a case-by-case basis does not cure its fundamentally constitutional infirmity, i.e., it serves to take our private property, i.e., our trade secrets without providing any compensation.

The Fifth Amendment of the Constitution states: “[N]or shall private property be taken for public use, without just compensation.” The Supreme Court has determined that a trade secret is private property “protected by the Taking Clause of the Fifth Amendment.”⁶ The Applicants’ equity holdings are trade secrets that are protected by the Taking Clause of the Fifth Amendment. Since §13(f) of the 1934 Act allows the Commission to exercise its discretion to require the Applicants to place their trade secrets in the public domain without any intent to pay them “just compensation” it represents a potentially unconstitutional “taking.” An order pursuant to §13(f)(2) exempting the Applicants from filing Form 13F would cure this constitutional infirmity.

In Ruckelshaus v. Monsanto Co., 467 U.S. 986 (1984), the Supreme Court considered whether data required to be submitted to the Environmental Protection Agency (“EPA”) for registration of a pesticide could be (i) used by the agency to evaluate pesticides created by competitors of the original submitter and (ii) publicly disclosed by the agency. Monsanto sued for injunctive and declaratory relief, alleging that each of these provisions of the enabling law effected a “taking” of its intellectual property without just compensation. In its opinion, the Court stated: “In deciding this case, we

⁶ Ruckelshaus v. Monsanto Co., 467 U.S. 986 (1984)

are faced with four questions: (1) Does Monsanto have a property interest protected by the Fifth Amendment's Taking Clause in the health, safety, and environmental data it has submitted to EPA? (2) If so, does EPA's use of the data to evaluate the applications of others or EPA's disclosure of the data to qualified members of the public effect a taking of that property interest? (3) If there is a taking, is it a taking for a public use? (4) If there is a taking for a public use, does the statute adequately provide for just compensation?"

With respect to rule 13f-1, the third and fourth Monsanto questions can be dispensed with quickly, i.e., if rule 13f-1 effects a taking of a trade secret, it is indisputable that (1) the taking is for public use and (2) the statute does not provide for (nor is there any evidence that Congress intended to pay) compensation for the taking. Therefore, if rule 13f-1 effects a taking of a trade secret, it would be *ultra vires* of the Taking Clause. We now consider the first two Monsanto questions.

Do the Applicants have a property interest protected by the Fifth Amendment's Taking Clause in the disclosures they would be required to make by rule 13f-1 of the 1934 Act?

The Applicants generally do not publicly disclose their investments. Moreover, the Applicants generally do not disclose their investments to investors in their funds nor do they provide a condensed schedule of such investments in their funds' financial statements, much less a complete schedule, even though a condensed schedule is required to obtain an unqualified audit opinion. Their funds' financial statements contain the following explanatory note:

On May 15, 1995, the Accounting Standards Division of the American Institute of Certified Public Accountants issued Statement of Position 95-2 which requires that the financial statements of private investment partnerships must, in order to conform with generally accepted accounting principles, include a condensed schedule of investments.

In a discussion of the factors considered prior to issuance of SOP 95-2, the Accounting Standards Executive Committee (AcSEC), which is the senior technical body of the Institute authorized to speak for the Institute in the area of financial accounting and reporting, stated: "AcSEC acknowledges that disclosure can produce certain detriments, but AcSEC believes that the need for adequate disclosure outweighs the possibility of negative results." The general partner believes that such disclosure could reveal proprietary trading strategies and possible targets of shareholder activism by the Partnership, the confidentiality of which is important to achieve the best results for investors and therefore, has elected not to include a condensed schedule of investments.

In Monsanto the Supreme Court concluded that "to the extent that Monsanto has an interest in its health, safety, and environmental data cognizable as a trade-secret property right under Missouri law, that property right is protected by the Taking

Clause of the Fifth Amendment.” The Applicants’ investments are trade secrets⁷ and, like Monsanto’s proprietary data, are protected by the Taking Clause of the Fifth Amendment.

Would the disclosures required by §13(f)(2) effect a taking of that property interest?

The entire value of a trade secret lies in its secrecy. Once a trade secret is publicly disclosed, its owner loses its entire economic value even though the owner can continue to use it.

The Monsanto court identified three non-exclusive factors to determine when a governmental action goes beyond “regulation” and effects a “taking” -- “the character of the governmental action, its economic impact, and its interference with reasonable investment-backed expectations.” It found that, barring a promise not to disclose confidential data, “as long as Monsanto is aware of the conditions under which the data are submitted, and the conditions are rationally related to a legitimate Government interest, a voluntary submission of data by an applicant in exchange for the economic advantage of a registration can hardly be called a taking.”

There are fundamental differences between §13(f)(1) of the 1934 Act and each of the three iterations of the statute that the Court considered in Monsanto that support our contention that the disclosure scheme of Section §13(f)(1) goes “too far” in the direction of a “taking.”⁸ First, the disclosure required by Section §13(f)(1) is mandatory, not voluntary. Second, a 13F filer immediately loses the entire economic value of its trade secrets while gaining nothing in exchange. Third, there is no rational relationship between the disclosure scheme of §13(f)(1) and any legitimate government interest. Finally, the passage of the EEA in 1996 indicates Congress’s

⁷ In Monsanto, the court applied the definition of a trade secret in the Restatement of Torts: “any formula, pattern, device or compilation of information which is used in one’s business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it.” The Economic Espionage Act of 1996 (“EEA”), a post-Monsanto law that criminalizes the theft or misappropriation of trade secrets, defines a “trade secret” as “all forms and types of financial, business, scientific, technical, economic, or engineering information, including patterns, plans, compilations, program devices, formulas, designs, prototypes, methods, techniques, processes, procedures, programs, or codes, whether tangible or intangible, and whether or how stored, compiled, or memorialized physically, electronically, graphically, photographically, or in writing if -- (A) the owner thereof has taken reasonable measures to keep such information secret; and (B) the information derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable through proper means by, the public.”

⁸ Pennsylvania Coal Co. v. Mahon, 260 U.S. 393 (1922) (“The general rule at least is that while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking. It may be doubted how far exceptional cases, like the blowing up of a house to stop a conflagration, go -- and if they go beyond the general rule, whether they do not stand as much upon tradition as upon principle. Bowditch v. Boston, 101 U.S. 16. In general it is not plain that a man’s misfortunes or necessities will justify his shifting the damages to his neighbor’s shoulders. Spade v. Lynn & Boston Ry. Co., 172 Mass. 488, 489, 52 N. E. 747, 43 L. R. A. 832, 70 Am. St. Rep. 298. We are in danger of forgetting that a strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change.”)

post-Monsanto view that the public interest is served by protecting trade secrets from unauthorized use without a compelling reason.

A. The disclosure required by Section §13(f)(1) is not voluntary.

In Monsanto, the Court found that Monsanto voluntarily submitted confidential data to the EPA under the regulatory apparatus established under the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA), 7 U.S.C. § § 136 et seq. By contrast, the disclosure required by Section §13(f)(1) is mandatory.

B. A 13F filer does not obtain an economic advantage in exchange for making the required disclosure.

Unlike the disclosure schemes challenged in Monsanto, Section §13(f) is not a regulatory scheme with burdens and benefits for a 13F filer. A 13F filer only has a burden. (The Applicants anticipate an argument that a 13F filer “benefits” by being able to conduct its business. However, courts have rejected that argument.)

The Monsanto Court said: “This Court has stated that a sovereign, ‘by *ipse dixit*, may not transform private property into public property without compensation This is the very kind of thing that the Taking Clause of the Fifth Amendment was meant to prevent.’ Webb’s Fabulous Pharmacies, Inc. v. Beckwith, 449 U.S., at 164.” There is no reason that this principle should not apply equally to intellectual property like a trade secret and to physical property.

In Philip Morris, Inc. v. Reilly, 113 F. Supp. 2d 129 (2000), the United States District Court for the District of Massachusetts considered a challenge to a statute that required manufacturers of tobacco products to publicly disclose all the ingredients in their tobacco products sold in Massachusetts. According to the District Court:

The Disclosure Act would require the plaintiffs to provide the DPH with a list of the ingredients used in any tobacco products sold within the Commonwealth. The list for each brand would identify the ingredients used in that brand ranked “in descending order according to weight, measure, or numerical count.” In addition to the ingredient list, each brand’s “nicotine yield rating,” which is the estimated amount of nicotine an average consumer would ingest by using the product, must also be revealed. See Mass. Gen. Laws ch. 94, § 307B. Both the ingredient list and nicotine yield rating for each brand “shall” become public record, in full or redacted form, if two conditions are met. First, the DPH must determine that “there is a reasonable scientific basis for concluding that the availability of such information could reduce risks to public health.” Second, the Attorney General of the Commonwealth must advise the DPH that the public release of the information would not cause an unconstitutional taking of property. See *id.*; Mass. Regs. Code tit. 105, § 660 et seq. (the “implementing regulations”).

Because the District Court's analysis of the merits in Reilly is so relevant to this application, it is reproduced below in its entirety (excluding footnotes).

What happens when the State orders a person to disclose for publication a commercial trade secret? According to the plaintiffs, what happens is that the State "takes" a private property interest from its owner in service of a public good. When a State "takes" private property, the Constitution requires that "just compensation" be made for the property owner's loss. Neither the Disclosure Act nor any other provision of Massachusetts law provides for the payment of compensation to the plaintiffs for whatever loss they would sustain by reason of the publication of their commercial trade secrets. In fact, it seems clear from the Act that Massachusetts does not intend to pay compensation; as noted above, the public disclosure of the plaintiffs' ingredient information is conditioned on the state Attorney General's advice that Massachusetts can disclose it without paying compensation. Since in the absence of compensation Massachusetts may not "take" the property, within the meaning of that term as used in the Fifth Amendment, the heart of the present controversy is whether the Disclosure Act accomplishes a "taking."

Some governmental acts, such as the explicit use of the inherent sovereign power of eminent domain, are unambiguously and uncontroversially "takings." Here, however, rather than acknowledging that it is "taking" private property for public use, Massachusetts to the contrary insists that it is not. The defendants say that the Disclosure Act is a valid exercise of the Commonwealth's traditional police power to promote and protect the public health. Regulation imposed under authority of the police power necessarily limits what individuals may do with their private property, especially in commercial activity; indeed, that is the whole point of exercising the police power. Collaterally, though it is not an intended objective of the police power, it is often a necessary consequence of its exercise that the economic value of the regulated property or activity may be diminished, sometimes drastically, with the property owner having no right to compensation for the loss. See e.g., *Andrus v. Allard*, 444 U.S. 51, 62 L. Ed. 2d 210, 100 S. Ct. 318 (1979) (upholding prohibition of sale of eagle feathers).

On the other hand, "while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking." *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 415, 67 L. Ed. 322, 43 S. Ct. 158 (1922). How far is "too far?" That depends. The question cannot be answered by application of a "set formula"; rather, in every case in which a regulatory taking is claimed there must be an "essentially ad hoc, factual inquiry." *Penn Cent. Transp. Co. v. New York*, 438 U.S. 104, 124, 57 L. Ed. 2d 631, 98 S. Ct. 2646 (1978). See also, *Pennsylvania Coal*, 260 U.S. at 416 ("This is a question of degree -- and therefore cannot be disposed of by general propositions.") Whether there has been a "regulatory taking" is evaluated by considering, on the particular facts of each case, "the character of the

governmental action, its economic impact, and its interference with reasonable investment-backed expectations.” *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1005, 81 L. Ed. 2d 815, 104 S. Ct. 2862 (1984) (quoting *Prune Yard Shopping Ctr. v. Robins*, 447 U.S. 74, 83, 64 L. Ed. 2d 741, 100 S. Ct. 2035 (1980)). The inquiry must take into account the “specific property, and the particular estimates of economic impact an ultimate valuation relevant in the unique circumstances.” *Keystone Bituminous Coal Ass’n v. DeBenedictis*, 480 U.S. 470, 495, 94 L. Ed. 2d 472, 107 S. Ct. 1232 (1987).

The defendants rely heavily on the first factor in the evaluation -- the character of the governmental action involved -- and emphasize, rightly, that the Commonwealth has broad police power to regulate matters bearing on the public health or welfare. It is certainly true that the police power is traditionally a broad power, and economic actors like the plaintiffs must always accept that their interests may be required to yield to an appropriate exercise of that power. But there is a limit, and a State cannot truncate the inquiry simply by playing the “police power” trump. Even properly motivated exercises of the police power can go “too far” and result in a taking of property for which compensation must be made. See *Pennsylvania Coal*, 260 U.S. at 415-16. See also *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1015, 120 L. Ed. 2d 798, 112 S. Ct. 2886 (1992) (“If...the uses of private property were subject to unbridled, uncompensated qualification under the police power, ‘the natural tendency of human nature [would be] to extend the qualification more and more until at last private property disappeared,’”) (quoting *Pennsylvania Coal*, 260 U.S. at 415) (alterations in *Lucas*).

One of the considerations endorsed by the Supreme Court for deciding whether an exercise of the police power has gone “too far” is to ask whether the effect of the governmental action is to deprive the property owner of “economically viable use” of the property. See *Lucas*, 505 U.S. at 1014-16 (quoting *Agins v. City of Tiburon*, 447 U.S. 255, 260, 65 L. Ed. 2d 106, 100 S. Ct. 2138 (1980)). In the present case, that question could receive an ambiguous answer, depending on how broadly the property interest is defined. On the one hand, the plaintiffs may continue to manufacture products in accordance with their existing ingredient recipes, so they retain the economic use of the information, though after publication it may also be used by others as well. In this broader sense, the economic value of the information may be significantly lessened, but it is not eliminated. See *Dolan v. City of Tigard*, 512 U.S. 374, 385 n.6, 129 L. Ed. 2d 304, 114 S. Ct. 2309 (1994). On the other hand, the publication of secret product information would entirely deprive the holder of the economic value and viability of the secrecy of the information. If, then, the relevant property interest is the secrecy of the trade secret, it would be fair to say that the owner is deprived of all economically viable use of that property interest, since publication extinguishes the interest by destroying the secrecy. The latter scope of definition is the appropriate one. In *Monsanto*, for example, the takings question concerned the company's loss

of the secrecy of its data, not its ability to continue to use the data at all. Monsanto retained the use of this information, but others also could use it.

The Supreme Court has consistently recognized that one of the fundamental attributes of private property is the owner's right to exclusive use of the property. See *Nollan v. California Coastal Com'n*, 483 U.S. 825, 831, 97 L. Ed. 2d 677, 107 S. Ct. 3141 (1987) (citing *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 433, 73 L. Ed. 2d 868, 102 S. Ct. 3164 (1982) and *Kaiser Aetna v. United States*, 444 U.S. 164, 176, 62 L. Ed. 2d 332, 100 S. Ct. 383 (1979)). Exclusivity is more than just an important aspect of a proprietary interest in a trade secret. It is the very source of the proprietary interest itself. Through secrecy, the owner excludes others from the use of the information. If the veil of secrecy is lifted, exclusivity is extinguished and the proprietary interest essentially vanishes. The Court has consistently held that the extinction of a property interest -- even an intangible one such as an interest in a trade secret -- may constitute a taking. See *Monsanto*, 467 U.S. at 1003 (citing *Armstrong v. United States*, 364 U.S. 40, 44, 4 L. Ed. 2d 1554, 80 S. Ct. 1563 (1960) (extinction of materialman's lien); *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 596-602, 79 L. Ed. 1593, 55 S. Ct. 854 (1935) (extinction of real estate lien); *Lynch v. United States*, 292 U.S. 571, 579, 78 L. Ed. 1434, 54 S. Ct. 840 (1934) (abrogation of valid contracts)).

The other prominent factors for this regulatory takings analysis -- the economic impact of the governmental action and its interference with reasonable investment-backed expectations -- weigh here in the plaintiffs' favor. On the summary judgment record, it is clear that the plaintiffs have made substantial investments in the development and protection of their brand-specific ingredient information, and that there would be a substantial loss of competitive advantage if they were required to disclose that information for publication by the Commonwealth.

The defendants urge, however, that the plaintiffs can avoid the loss of their trade secrets simply by withdrawing from sale in Massachusetts any product manufactured using the secrets. Under the Disclosure Act, the plaintiffs only need to disclose ingredient information with regard to products sold in Massachusetts. By offering their products for sale in Massachusetts, the defendants argue, the plaintiffs implicitly accept the disclosure requirement. If they wish to avoid the disclosure requirement, they may refrain from selling tobacco products in the Commonwealth.

The argument must be rejected. In the first place, it represents an incorrect application of the Supreme Court's decision in *Monsanto*. In that case, the Court held that Monsanto's voluntary submission of confidential data to the Environmental Protection Agency ("EPA") under the regulatory apparatus established under the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA), 7 U.S.C. § § 136 et seq., did not constitute a taking within the scope

of the Fifth Amendment. As is not unusual with intricate regulatory schemes, there was some good news and some bad news for the regulated companies under FIFRA. Though it imposed some burdens and obligations, the regulatory regime conferred some benefits as well. The exchange was both voluntary enough and fair enough, in the judgment of the Supreme Court, that it could not be said that Monsanto's property interest in its confidential information had been "taken" by the government.

This case is different. Here, there is no regulatory scheme with both burdens and benefits; there is only burden. The burden is that the plaintiffs must disclose their trade secrets. The proposed "benefit" is that they may continue to do what they had been doing without burden before the enactment of the Disclosure Act, selling their products within Massachusetts. That "benefit" is not similar to the give-and-take exchange that the Court approved in *Monsanto*. See *Philip Morris*, 159 F.3d at 679 ("Permission to continue operating a lawful business is not the type of government benefit on which a Monsanto-type exchange validly may be predicated."); *id.* at 677 ("The mere granting of permission to engage in routine activities, incident to existing property rights, does not afford compensation sufficient to support a Monsanto-like exchange."). See also *Nollan*, 483 U.S. at 833-34 n.2 (explaining *Monsanto* and stating that the government's "announcement that the application for (or granting of) [a building] the permit will entail the yielding of a property interest cannot be regarded as establishing the voluntary 'exchange' ...that we found to have occurred in *Monsanto*") (citations omitted).

The defendants have also suggested that since Massachusetts law creates the protection for trade secrets, Massachusetts may withdraw that protection. (Here, of course, any withdrawal would be highly selective, not abolishing the law of trade secrets for Massachusetts but rather only withdrawing trade secret protection for a particular category of disfavored (but legal) products, while leaving it intact for all others.) This argument rests on the positivist notion that since, in a broad sense, all property rights emanate from the State, the State is free to take them away whenever it determines to do so. That proposition must be rejected. As one commentator has noted:

To the degree that private property is to be respected in the face of republican and positivist visions, it becomes necessary to resist even an explicit government proclamation that all property acquired in the jurisdiction is held subject to government's limitless power to do with it what government wishes. Indeed, government must be denied the power to give binding force to so sweeping an announcement, whether explicit or implicit, if we are to give content to the just compensation clause as a real constraint on federal power and, through the fourteenth amendment, on state and local power. But this shows that the expectations protected by the clause must have their source outside

positive law. Grounded in custom or necessity, these expectations achieve protected status not because the state has deigned to accord them protection, but because constitutional norms entitle them to protection. Laurence H. Tribe, American Constitutional Law, 608 (2d ed. 1988).

In summary, then, the record establishes that the plaintiffs have valuable property interests in confidential brand-specific ingredient information; the confidential information qualifies as trade secret information under the laws of Massachusetts; the inevitable effect of the Disclosure Act will be to compel the public disclosure of some or all of the trade secrets; by destroying the secrecy of the information, public disclosure deprives the plaintiffs of their property interest in the trade secrets; the Commonwealth's deprivation of the property interest in the secrets is a "taking" for which the Fifth and Fourteenth Amendments require just compensation to be made; there is neither provision for, nor a prospect of, compensation to the plaintiffs for the taking that would be effected by the Disclosure Act; and therefore, the plaintiffs are entitled to an injunction preventing the taking without compensation, that is, preventing the defendants from acting to enforce the provisions of the Disclosure Act requiring the plaintiffs to submit brand-specific ingredient information.

In Nollan v. California Coastal Comm'n, 483 U.S. 825 (1987), the United States Supreme Court barred the State of California from conditioning a rebuilding permit on the property holder granting an easement to the public. Justice Scalia, writing for the majority, addressed and rejected the argument that Monsanto authorizes the legislature to place any property (including a trade secret) in the public domain as a condition of the holder's using it:

[In his dissent], Justice Brennan also suggests that the Commission's public announcement of its intention to condition the rebuilding of houses on the transfer of easements of access caused the Nollans to have "no reasonable claim to any expectation of being able to exclude members of the public" from walking across their beach. Post, at 857-860. He cites our opinion in Ruckelshaus v. Monsanto Co., 467 U.S. 986 (1984), as support for the peculiar proposition that a unilateral claim of entitlement by the government can alter property rights. In Monsanto, however, we found merely that the Takings Clause was not violated by giving effect to the Government's announcement that application for "the right to [the] valuable Government benefit," id., at 1007 (emphasis added), of obtaining registration of an insecticide would confer upon the Government a license to use and disclose the trade secrets contained in the application. Id., at 1007-1008. See also Bowen v. Gilliard, ante, at 605. But the right to build on one's own property - even though its exercise can be subjected to legitimate permitting requirements - cannot remotely be described as a "governmental benefit." And thus the announcement that the application for (or granting of) the permit will entail the yielding of a property interest cannot be regarded as establishing the voluntary "exchange," that we found to have occurred in Monsanto. Nor are the Nollans'

rights altered because they acquired the land well after the Commission had begun to implement its policy. So long as the Commission could not have deprived the prior owners of the easement without compensating them, the prior owners must be understood to have transferred their full property rights in conveying the lot.

C. There is no rational relationship between the disclosure scheme of §13(f)(1) and any legitimate government interest.

In both Monsanto and Philip Morris the asserted goal of the challenged statutes was improving public health which is clearly a compelling government interest. In Monsanto, the challenged law was intended to insure the safety of pesticides used in the United States. In Philip Morris, the legislative goal was to reduce the incidence of smoking in Massachusetts. It is easy to conclude that a legislator could rationally believe that adoption of each of these laws would promote public health.

By contrast, the disclosure scheme of §13(f)(1) is not rationally related to any legitimate government interest.

According to a report⁹ prepared by the staff in 1983, the sole justification for §13(f) is the following:

Although the Commission does not plan to make extensive use of information that could be gathered under Section 13(f) at the present time, we do believe that disclosure of holdings of institutional managers is in the public interest for the reasons set forth in the Senate Report: making information about institutional holdings available so that individuals and other investors can draw their own conclusions from it and enhancing public confidence in the institutions and the markets by enabling the public to assess for itself the concentration and influence of institutional managers in the market.

There is no possible conclusion that any investor could reasonably draw from 13F filings that would “[enhance] public confidence in the institutions and the markets.” Therefore, the assertion that investor confidence is enhanced through conclusions investors may draw from 13F reports fails to satisfy even the modest “rational basis” standard for regulatory restrictions on the use of one’s private property.

The real purpose of §13(f)(2), i.e., legitimizing plagiarism of proprietary investment strategies, is hidden elsewhere in The Staff Report: “The benefits of Section 13(f) information to the public have not been measured¹⁰, and some representatives of the securities industry have suggested that Section 13(f) should be repealed. However,

⁹ Report of the Staff of the Securities and Exchange Commission on the Operation of Section 13(f) of the Securities Exchange Act of 1934 at 17 (Nov. 29, 1983) (report in response to a letter from the Hon. John D. Dingell, Chairman of the Subcommittee on Oversight and Investigations of the House Committee on Energy and Commerce) (unpublished) (“SEC Staff Report”)

¹⁰ The most likely reason no objective assessment of the “benefits” has been made is that there are no legitimate benefits to measure.

there is demonstrable public demand for this information.” (emphasis added) Justice Holmes, writing for the Supreme Court in Pennsylvania Coal Co. v. Mahon, 260 U.S. 393, 415 (1922) forcefully rejected that argument:

The protection of private property in the Fifth Amendment presupposes that it is wanted for public use, but provides that it shall not be taken for such use without compensation. . . . When this seemingly absolute protection is found to be qualified by the police power, the natural tendency of human nature is to extend the qualification more and more until at last private property disappears. But that cannot be accomplished in this way under the Constitution of the United States.

In sum, there is no evidence that public confidence in the markets is enhanced by conclusions investors draw from 13F filings. In fact, all the evidence indicates that 13F filings are used by the public for only one reason: to obtain, without compensation, the trade secrets of successful filers. Absent §13(f)(2), obtaining our trade secrets, unless authorized by us, would constitute trade secret misappropriation and subject the user to civil and criminal penalties. For example, if the Applicants had under management equity securities having an aggregate fair market value of less than \$100,000,000, it would be illegal for anyone, without authorization, to obtain and use the very same information that §13(f)(2) will force us to place in the public domain (unless we receive an exemption). If effect, once the \$100,000,000 threshold is reached, §13(f)(2) destroys our trade secrets without any rational reason. The simple truth is that 13F filings allow anyone to analyze and use the strategies of institutional investment managers without paying any compensation for the manager’s data. In essence, Section 13(f) legalizes the misappropriation of trade secrets by transforming trade secret piracy into trade secret entitlement.¹¹ Moreover, the suggestion that 13F filings are routinely used for any legitimate purpose is disingenuous.¹²

It is an axiom that every investor in the world is potentially competing with every other investor. All individual investors and those institutional investment managers with less than \$100 million under management are protected by the EEA and other laws from misappropriation of their trade secrets, including their investment holdings. Rule 13f-1 discriminates against institutional investment managers with \$100 million or more under management by exposing their trade secrets to the public (without any offsetting benefit), thereby placing them and their clients at a competitive disadvantage. The following are some examples from financial publications and

¹¹ P.J. O’Rourke also deconstructed the basis of the SEC Staff Report’s “demonstrable public demand” justification for retaining §13(f) by wryly observing: “The whole idea of our government is this: If enough people get together and act in concert, they can take something and not pay for it.” (O’Rourke, *Parliament of Whores* (1991) p. 232.)

¹² §13(f) requires a 13F filer to report a snapshot of its holdings on a quarterly basis and allows a 45-day delay. However, public investors can benefit from reading even stale data. Otherwise, it would be irrational to require the disclosure of stale data. Conversely, if a 13F filer’s holdings have any value at all at the time a filing is required, the Fifth Amendment requires that fair compensation be paid to the filer.

services that illustrate how 13F filings are actually –and illegitimately -- used by investors in the real world:

- Institutional money managers with discretion over \$100 million or more must file a Form 13F with the SEC listing all publicly-traded U.S. equities held – including the number of shares owned and the fair market value – no later than 45 days after the end of each calendar quarter. From these filings, we track and seek insight from the holdings of an elite cadre of hedge-fund managers, from better known investors such as Omega Advisors’ Lee Cooperman and Baupost Group’s Seth Klarman to those less well-known like Stephen Mandel of Lone Pine Capital. The list of investors tracked evolves as we add names of those we believe bear watching. (emphasis added) -- Value Investor Insight, November 30, 2005
- You can tap into the thinking of the smartest fund managers. Hey, this worked the first two times we tried it. The world’s best mutual fund managers work in fishbowls -- there's a wealth of data available on how they invest. Two years ago we first took the portfolios of the winningest managers and overlapped their biggest holdings to find a batch of winners. Simple thesis: If a lot of smart guys like the same stock, it must be worth holding. . . . This year’s cut: 23 funds that mostly own shares of large companies, 21 that like smaller companies and 19 that invest internationally. In this exercise expenses and loads are irrelevant, since you’re not buying the funds, just stealing the ideas.” (emphasis added) – “Picks of the Pros” by Christopher Hellman, Forbes, January 9, 2006
- I like learning from the stock picks and styles of others. I spent five years studying every aspect of Warren Buffett's approach, and the result was my second book, Trade Like Warren Buffett. I looked at every stage of his career from the 1950s on (hedge fund days, early Berkshire, later Berkshire, his personal portfolio, etc.), and had conclusions very different from the usual value-based books about him. I hope the process made me a better investor, and time will tell.

Along these lines, I like looking at the 13F-HR. These are filings from institutions/funds with greater than \$100 million in stock holdings, which are required by the SEC every quarter.

I plan to pick an investor once every so often and do an article based on his 13F-HR filings to get a sense of their approach and a look at their picks.

The first of these efforts will be on J.L. Berkowitz & Co., which filed its latest 13F-HR on Jan. 18. You can read the exploits of the young Jeff Berkowitz in Jim Cramer's Confessions of a Street Addict. If you read only one chapter in the book, read Jim's description of his experiences in September 1998. If you read two chapters, then also read his description of his first week in the hedge

fund business. (Jim's hedge fund, Cramer Berkowitz, evolved into Berkowitz & Co.)

I'm not going to go over all the positions (there are more than 100 of them), and I'm going to focus on his largest tech positions, although he has a fair number of positions that are in more industrial areas. On the whole, it seems Berkowitz & Co. goes for tech stocks with the following characteristics. . . .
-- "Use This Filing to Trade Like Jeff Berkowitz" by James Altucher, Real Money (<http://www.thestreet.com/comment/investing/10271190.html>), March 1, 2006

- Follow the "profit trail" of the Big Money. The logic behind *Big Money Watch* is flawless ... and it has already earned handsome profits for our subscribers. *Here's our system in a nutshell...* You know that the "big money" on Wall Street - the top money managers at the nation's largest mutual funds, hedge funds, brokerages, and pension funds ... generate superior returns that put *your* stock broker to shame. They have to - because their jobs depend on it! When you and I buy a stock, we are risking thousands of dollars of our own money ... and while losing really hurts, no one's going to fire us if a stock we buy goes down. But when a large institutional investor buys a stock, he is putting millions of dollars of capital - not to mention his own job—at risk. Therefore, these institutional investors spend a fortune on research - gathering intelligence that you and I, as individual investors, could never afford to buy. So the idea occurred to me one day ... Why settle for the inferior research - the analyst reports - that other individual investors use to pick stocks ... especially when the big money managers are required by law to file a quarterly "13F" form that discloses their current holdings (they also must file a 13G when their ownership position surpasses 5% of a company's shares). And that's how my new investment advisory service, *Big Money Watch*, was born! What we do is simple: 1. Continually compare the performance of all of the big money managers ... to determine the 15 pros who are at the top of their game today. (Some managers remain winners for a long time. But many run hot and cold.) 2. Keep running portfolios of all the stock picks of these top 15 money managers ... those with the best performance right now. 3. Select their top picks ... the "best of the best" ... and invest only in those stocks for our own Model Portfolio. (emphasis added) – Big Money Watch (<http://www.bigmoneywatch.com>)

- GuruFocus Tracks the Stock Picks of Gurus.

Only a handful of people in this world can qualify as investment guru. We have carefully identified a number of investment gurus based on their long outstanding performance; 2. Manage more than \$1 billion; 3. Low portfolio turnover. If you are aware of other investors who are not in our Guru Hall of Fame, please inform us at the Forum for Suggesting Gurus.

GuruFocus tracks the stock picks of Warren Buffett, George Soros and other guru investors like Bill Nygren, Mason Hawkins, Ken Fisher, David Dreman, Martin Whitman, James Gipson, Robert Rodriguez, Ronald Muhlenkamp, Wallace Weitz, William, Ruane, Edward Lampert, Edward Owens, Richard Aster, Jr, Robert Olstein, John Keeley, Brian Rogers and Tweedy, Browne.
(<http://www.gurufocus.com/>)

D. The Passage of the EEA demonstrates that protection of trade secrets is in the public interest.

Prior to 1996, trade secrets could only be protected from misappropriation at the state level. On October 11, 1996, President Clinton signed the EEA into law “because of the increased recognition of the increasingly important role that intellectual property plays in the well-being of the American economy.”¹³ Among other things, the EEA makes the misappropriation of trade secrets a federal crime. In a letter to Senator Orrin G. Hatch dated October 1, 1996, Attorney General Janet Reno stated the rationale for the EEA: “The need for this law cannot be understated as it will close significant gaps in federal law, thereby protecting proprietary economic information and the health and competitiveness of the American economy.”

Section 1832 of the EEA makes it a federal crime for any person to convert a trade secret to his own benefit or the benefit of others. The EEA defines the term “trade secret” to include “all forms and types of financial, business, scientific, technical, economic, or engineering information . . . if (A) the owner thereof has taken reasonable measures to keep such information secret; and (B) the information derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable through proper means by the public.”

As we have shown, the Applicants’ securities positions are trade secrets under the EEA’s (or any other) definition. There is no evidence in the legislative history of §13(f) that Congress considered its impact on the owners of trade secrets. However, in passing the EEA twenty-one years later, Congress forcefully demonstrated its belief that it is in the public interest to protect trade secrets. Therefore, to the extent that the disclosure required by rule 13f-1 is inconsistent with that view, an exemption pursuant to §13(f)(2) is in the public interest.

IV. Requested Relief

Section 13(f)(2) of the 1934 Act states: “The Commission, by rule or order, may exempt, conditionally or unconditionally, any institutional investment manager or security or any class of institutional investment managers or securities from any or all of the provisions of this subsection or the rules thereunder.” Section 13(f)(4) of the 1934 Act states: “In exercising its authority under this subsection, the Commission

¹³ Theft of Commercial Trade Secrets, U.S. Department of Justice,
(<http://www.usdoj.gov/criminal/cybercrime/ipmanual/08ipma.htm>)

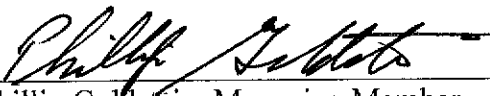
shall determine (and so state) . . . in granting an exemption, that its action is consistent with the protection of investors and the purposes of this subsection.”

As explained in Section III of this Application, rule 13f-1 does not serve its primary intended purpose, i.e., to fill an informational void for the Commission. There is no evidence its secondary purpose of increasing investor confidence is achieved and there is a serious question as to whether that is even a legitimate governmental goal. Moreover, there is no evidence that rule 13f-1 protects any investors. To the contrary, the investors in an entity advised by the Applicants may be harmed if the Applicants’ trade secrets are accessed by other investors with whom it competes. Also, as explained in Section III, unless an exemption from rule 13f-1 is granted, the Applicants’ trade secrets will be taken for public use¹⁴ without compensation in violation of the Fifth Amendment to the Constitution. Because the relief requested is consistent with the protection of investors and the purposes of §13(f) of the 1934 Act and to avoid offending the Fifth Amendment to the Constitution, an unconditional exemption from the filing requirement of rule 13f-1 of the 1934 Act is required.

V. Conclusion

The Applicants believe fair consideration of this application requires that the Commission consult, in addition to the agencies and authorities specified in §13(f)(4), the Department of Justice because of its expertise in trade secrets law, a key element of this application. If the Department of Justice concurs with our legal analysis, the Commission should either issue the requested order or declare a moratorium on enforcement of rule 13f-1 until it makes a determination that no compensation is due in connection with any filings required under rule 13f-1. Finally, we request that the Commission assure us that it will take no enforcement action against the Applicants in connection with filings required under rule 13f-1 until we have exhausted our administrative remedies.

This application is being filed in accordance with Rule 0-3 of the 1934 Act.



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¹⁴ The Commission has implicitly acknowledged that §13(f)(1) may impair the value of trade secrets. “Congress also recognized that, in some instances, disclosure of certain types of information could have harmful effects, not only on an investment manager, but also on the investors whose assets are under its management.” (Commission Notice: Re: Section 13(f) Confidential Treatment Requests June 17, 1998)