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January 20, 1993

Mr. John Emmett  
907 North Dallas Bank Tower  
12900 Preston Road at LBJ  
Dallas, Texas 75230-1397

RE: GemStar Inventory Consignment Program

Dear Mr. Emmett:

This is in response to your letter dated July 28, 1992, and received by this Agency August 4, 1992. Such letter was supplemented by your letter dated September 4, 1992. It will also serve to confirm our telephone conversation on January 20, 1993.

Your letters and supplemental materials describe a proposed program (the "Program") by GemStar Associates ("GemStar"), a Texas based entity, pursuant to which GemStar would offer cut gems to the public. The investor would enter into a Consignment Sales Agreement (the "Agreement") with GemStar. Under the Agreement, GemStar would become the exclusive agent of the investor for the purchase, packaging, marketing and sale of the gems. GemStar would sell the gems through fund-raising and commercial auctions on behalf of the investor. The investor would receive weekly remittances from GemStar as the gems were sold. GemStar would guarantee a 25% return on each gem and an inventory liquidation period of twelve months or less. Further, GemStar would agree to buy back any unsold inventory from the investor at the cost of the inventory plus 25%.

It is my understanding that it would be GemStar's responsibility to purchase the type, quality, weight, shape, cut, and mix of gems that, in GemStar's experience, would match bidder preferences and sell most efficiently. The investor would be reliant upon the knowledge of the market by GemStar's management

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and the representation by GemStar that, "even in a recession, GemStar's revenue system is consistent and predictable."

It appears that, under the Agreement, an investor may take possession of gems, but the literature stresses that the purchase, handling and resale of the gems would be effected by GemStar. All expenses pertaining to the selection and purchase of the gems from GemStar's suppliers, lead generation, marketing and promotion, sales, coordination, distribution, collection and reconciliation would be the responsibility of GemStar. The investor's only cost would be the wholesale purchase price of the gems and their packaging by GemStar.

It would appear from your letters and the enclosed literature that GemStar is offering a security, i.e., an investment contract. In Searsy v. Commercial Trading Corp., 560 S.W. 2d 637 (Tex. 1977), the Texas Supreme Court determined that an agreement is an investment contract if there is an investment of money in a common enterprise with an expectation of profits solely from the efforts of others. Please note that Section 4.A of the Texas Securities Act (the "Act") defines "security" to include investment contracts. In interpreting what is meant by the phrase "solely from the efforts of others" the Searsy court adopted the more realistic test of "whether the efforts made by those other than the investor are undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise."

Based upon the foregoing understanding, the staff of the State Securities Board is of the opinion that the program contemplates sales of ancillary investment contracts. Therefore, the interests in the program offered by GemStar must be registered for sale in Texas pursuant to Section 7 of the Act, unless some exemption from the registration provisions of the Act is available.

I trust this information answers your inquiry. Please feel free to write to call if you need further information.

Very truly yours,

RICHARD D. LATHAM  
Securities Commissioner

Denise Voigt Crawford  
General Counsel

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