

BARATELLI INSTITUTE

The Buffett Partnership Era 1956–1969

An Institute Historical Case Study

Practitioner-grade reading of the thirteen years
that made Warren Buffett rich and set the operating
template for everything Berkshire Hathaway later became.

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Section 1 — The setup (1956-1957)

In 1956, Warren Buffett was twenty-five years old. He had spent the previous two years working for Benjamin Graham, the New York investor whose 1949 book *The Intelligent Investor* was the foundational text of modern value investing. Buffett had been Graham's brightest student at Columbia Business School. He had wangled his way onto Graham-Newman's payroll after graduation. And now, in the spring of 1956, he was quitting.

He moved back to Omaha with \$174,000 of his own capital. That number is worth stopping on. In today's terms — using the CPI-based deflator to translate 1956 dollars to 2026 dollars — it is roughly \$2.1 million. That is the net worth of a moderately successful family-office CFO or a mid-career independent RIA. It is not a fortune. It is not the launching capital of a hedge fund empire. It is the accumulated savings of a young man who had been extremely careful with money since he was six years old, when he bought his first shares of Cities Service Preferred at \$38.25.

He had no plan to run outside money. That changed within weeks. Family members, close family friends, and a handful of former Graham-Newman clients approached him individually asking him to manage their savings. He resisted at first — he had come home to Omaha to invest quietly on his own account. But the requests kept coming, and after enough of them piled up, he consulted a lawyer, drew up a Nebraska limited partnership agreement, and on May 1, 1956, opened Buffett Associates Ltd. with seven original limited partners.

The seven original LPs contributed \$105,000 in capital: Doc Thompson, Alice Buffett, Dan and Alice Monen, Chuck Peterson, and Elizabeth and William Peterson — five family and close-friend relationships, plus one client Buffett had picked up while still at Graham-Newman. Buffett himself contributed a nominal \$100 as general partner. The entire capital base of what would eventually become one of the most consequential investment vehicles in the history of American finance was \$105,100 — less than the median down payment on a Manhattan condominium today.

This origin story matters for the practitioner reading. A 25-year-old who *opens a firm* to solicit outside capital designs a fee structure to maximize personal compensation. A 25-year-old who takes money from family and family friends because they insisted designs a fee structure that only pays him if he earns them real returns. The Buffett Partnership fee structure that shocks modern hedge fund managers — zero management fee, six percent hurdle, twenty-five percent above — makes complete sense once you understand that it started as an accommodation, not a business plan.

The legal structure was a straightforward limited partnership under Nebraska law. Limited partners could not lose more than their contributed capital. Buffett, as general partner, was personally liable for all losses. Under Nebraska partnership law the partnership itself paid no tax; all income and gains flowed through to the individual partners according to their proportional interests. There was nothing exotic about the structure. The same limited-partnership form was and still is used by thousands of small private investment vehicles across the country every year.

What was exotic was what came next.

Section 2 — The fee structure nobody uses today

The Buffett Partnership charged its limited partners nothing in the way of an annual management fee.

Zero. Not one percent. Not half a percent. Not a nominal expense reimbursement. Buffett covered the partnership's operating costs — the rent, the postage, the phone — out of his own pocket for the first several years and only reimbursed himself modestly later. If the partnership made no money in a given year, Buffett made no money either.

The performance fee was structured with a hurdle. If the partnership earned less than six percent per year, Buffett received nothing on top of his own capital returns. If the partnership earned more than six percent, Buffett received twenty-five percent of everything above the six percent hurdle. And here is the part almost nobody remembers: Buffett was personally liable for a proportional share of any losses. If the partnership lost money, Buffett contributed his own capital to make up his general-partner share of the loss.

The whole structure is worth writing out in plain English. In a year the partnership earned four percent: Buffett received nothing extra. In a year it earned ten percent: Buffett received twenty-five percent of the four points above the hurdle, so one point out of the ten. In a year it lost eight percent: Buffett paid in his general-partner share of the loss, meaning he was actively poorer at year-end.

Compare this to how modern hedge funds are structured. The standard is what the industry calls two-and-twenty: a two-percent annual management fee charged on assets under management, plus twenty percent of any profits, with no downside participation. On a \$100 million fund earning ten percent — call it \$10 million of profit — the modern manager charges \$2 million in management fees (regardless of performance) plus twenty percent of \$10 million in performance fees, so another \$2 million. Total: \$3.6 million (net of expense reimbursements) in a year the fund earned ten percent on the client's money.

On the same \$100 million fund earning ten percent, Buffett would have received: zero management fee, plus twenty-five percent of the four points above the six-percent hurdle, so one percent of the \$100 million assets, so \$1 million. In a year of ten percent gross returns, the modern hedge fund manager takes home 3.6x what Buffett would have taken home. And that is before you factor in the loss participation — if the year had been minus ten percent, the modern manager keeps the \$2 million management fee and pays back nothing, while Buffett would have written a check to the partnership out of his own capital.

Two takeaways from the fee comparison. First, the Buffett fee structure was radically more aligned with limited-partner outcomes than anything that exists in the modern hedge fund industry. Second, this was not stupidity or naiveté on Buffett's part. It was a deliberate structural bet — Buffett bet that his research quality would produce returns dramatically in excess of the six percent hurdle over long periods, and he was willing to accept low compensation in low-return years to capture disproportionate compensation in high-return years. That structural bet made him hundreds of millions of dollars over the thirteen years the partnership operated, because his gross returns averaged

29.5% annually. Almost any other realistic career path would have produced less wealth than the 0/6/25 structure produced for Buffett.

The Institute's editorial position on this: the fee structure was strategic weapon, not charity. It attracted a specific kind of limited partner — one willing to think in long compounding horizons and willing to trust a young manager with less than five years of independent track record. That kind of LP, once acquired, stayed forever. The 2/20 fund structure attracts a different LP: one focused on short-term returns, willing to redeem at the first sign of underperformance. Buffett's LPs had every economic incentive to hold. The modern hedge fund LP has every incentive to run at the first bad quarter.

Fee design is capital-attraction design. That is the practitioner takeaway.

Section 3 — The compounding table

The Buffett Partnership operated for thirteen full calendar years, from 1957 through 1969. The reported gross annual returns to the partnership were as follows:

Year	Partnership return	Dow Jones return	Excess over Dow
1957	+10.4%	-8.4%	+18.8 pts
1958	+40.9%	+38.5%	+2.4 pts
1959	+25.9%	+19.9%	+6.0 pts
1960	+22.8%	-6.3%	+29.1 pts
1961	+45.9%	+22.2%	+23.7 pts
1962	+13.9%	-7.6%	+21.5 pts
1963	+38.7%	+20.6%	+18.1 pts
1964	+27.8%	+18.7%	+9.1 pts
1965	+47.2%	+14.2%	+33.0 pts
1966	+20.4%	-15.6%	+36.0 pts
1967	+35.9%	+19.0%	+16.9 pts
1968	+58.8%	+7.7%	+51.1 pts
1969	+6.8%	-11.6%	+18.4 pts

Compound annual return over the full thirteen years: **29.5% gross**, roughly **23.8% net to the limited partners** after Buffett's performance fee. Compound annual return of the Dow Jones over the same period: **7.4%**.

A limited partner who contributed \$10,000 in 1957 and left it in the partnership through the 1969 closing had approximately \$260,000 by the end. A limited partner who instead put \$10,000 into the Dow in 1957 had approximately \$25,000 by the end of 1969. The difference is not marginal. It is a factor of ten, over thirteen years, in the same market environment, before compounding effects on the next twenty-five years of Berkshire Hathaway growth for those who kept their distributed shares.

Two things worth calling out. First, the partnership never had a losing year. Not one. In a period that included the 1962 Kennedy Slide, the 1966 credit crunch, and the 1969 bear market, the partnership never gave back a single point of compounding. That is not because Buffett was clairvoyant. It is because his research approach — buying assets substantially below verifiable book value, holding until value was recognized, and refusing to invest in businesses he could not deeply understand — produced returns that were largely uncorrelated with broader market direction.

Second, the excess-over-Dow column tells the practitioner story more clearly than the raw return column. In 1960 the Dow fell 6.3%; the partnership returned +22.8%. In 1962 the Dow fell 7.6%; the partnership returned +13.9%. In 1966 the Dow fell 15.6%; the partnership returned +20.4%. Buffett was making significant money in years when the broader market was actively losing money. That is the pattern that convinced limited partners to hold, and eventually to gift shares of Berkshire Hathaway from the 1969 distribution to their children and grandchildren rather than sell them.

Section 4 — Six partnerships, one merger (1957-1962)

Buffett Associates Ltd. was the first partnership. It was not the only one.

Between 1957 and 1961, Buffett organized six separate limited partnerships in parallel: Buffett Associates (May 1956), Buffett Fund (September 1956), Dacee (April 1957 — Dan and Alice Cee), Emdee (June 1958 — Dr. Marshall and Dr. William Angle, dentists), Glenoff (June 1959 — the Glenn Offutt family), Underwood (October 1961 — Mrs. Underwood), and Mo-Buff (Mrs. Malcolm G. Chace).

The names are worth noting because each partnership was, effectively, a bespoke vehicle for a specific relationship. Doc Thompson was Buffett's father-in-law's dentist. Dan Cee was a college friend. The Angle brothers were dentists Buffett had recruited during a family Thanksgiving in 1958. Every partnership was seeded with capital from a specific family or professional relationship, and each partnership operated as a distinct legal entity with distinct partnership agreements, distinct capital accounts, and distinct annual returns.

This was administratively cumbersome. Buffett had to allocate every investment across six partnerships, calculate six separate sets of returns, produce six separate sets of tax reporting, and manage six separate sets of limited-partner communications. Trades that made sense in aggregate had to be sub-allocated pro-rata by partnership. Cash inflows and outflows had to be tracked at the partnership level.

By 1961, the total assets under management across the six partnerships were approximately \$7.2 million. Buffett was thirty years old, running six separate legal entities, and personally producing every quarterly report by hand. In January 1962 he consolidated all six partnerships into a single vehicle: Buffett Partnership Ltd. The consolidation was structured as a merger — limited partners in the smaller vehicles exchanged their interests for units in the new consolidated partnership at then-current asset values. The tax treatment of the merger was itself an interesting piece of work; the transaction was structured to qualify as a tax-free exchange under §721 of the Internal Revenue Code, meaning no partner realized taxable gain or loss on the reorganization.

The consolidated Buffett Partnership Ltd. opened with \$7.2 million in assets and 90 limited partners. By 1968 it would grow to \$105 million and hundreds of limited partners. The single-vehicle structure allowed Buffett to concentrate positions more heavily — a single 15% position taken across a \$105M partnership is materially different in impact from a 15% position taken across six sub-scale partnerships — and to allocate research time more efficiently.

Modern parallel: hedge funds and family-office funds commonly use master-feeder structures that achieve some of the same consolidation benefits while preserving investor-level customization. A master fund holds all the investments; multiple feeder funds hold shares in the master and offer different LP terms (onshore vs. offshore, taxable vs. tax-exempt, retail vs. institutional). Buffett's 1962 consolidation was an early version of the master-fund concept — one central investment pool, formerly-separate LP relationships now unified into a single reporting structure.

The practitioner takeaway from the six-to-one merger: administrative complexity is not a badge of sophistication. If your investment thesis has converged such that all your capital pools own essentially the same portfolio, consolidation is the correct answer even if it takes real legal and tax structuring work to execute. Buffett spent months and non-trivial legal fees on the 1962 merger. The productivity gain from operating a single vehicle for the next seven years dwarfed the transition cost.

Section 5 — The Sanborn Map trade (1958-1960)

Sanborn Map Company was a specialist publisher. Since 1867 it had produced detailed maps of American cities showing every building, its construction type, and its fire-safety features. Property and casualty insurance companies bought Sanborn maps to underwrite fire risk. By the mid-1950s the business had entered a slow, permanent decline as insurers moved to statistical underwriting and no longer needed street-by-street building surveys. Revenue was shrinking. Earnings were shrinking. The stock had drifted down over years.

But Sanborn had one thing worth noticing. Over decades of profitable operation, the company had accumulated an investment portfolio — stocks and bonds — on its balance sheet. By 1958 that investment portfolio was worth roughly **\$65 per share**. The whole company traded around **\$45 per share**. In other words, the market was valuing the entire mapping business at negative twenty dollars a share — you got the operating company for free, and then twenty dollars back on top.

Buffett began accumulating shares in 1958. He kept buying quietly through 1959 and into 1960, eventually reaching roughly 44 percent of the outstanding stock. That level of ownership meant he could demand a board seat, and he did. Once on the board, he agitated for management to distribute the investment portfolio to shareholders through a tender or exchange offer. Management resisted. Buffett pressed. Eventually the board agreed, and in 1960 Sanborn distributed the investment portfolio to shareholders on a pro-rata basis.

The result: Buffett Partnership received roughly \$65 per share of securities in exchange for stock it had accumulated at an average cost around \$45 per share. The trade generated approximately a 55 percent return on the 25 percent of Partnership capital that had been allocated to the position — producing a meaningful contribution to the Partnership's 1960 performance.

The Institute's editorial position on this trade. It was activism verging on greenmail, and Buffett does not hide from it in his subsequent letters. He classified Sanborn as a “control” investment — meaning he took a large enough stake to influence corporate action, not just to hold as a passive minority investor. The tactic worked because the underlying analysis was correct: Sanborn's investment portfolio was worth more than the whole company. Any shareholder who insisted on that math had a legitimate claim on the portfolio's distribution. But the line between legitimate activism and greenmail is thinner than most retellings of the Sanborn story admit, and honest practitioner reading has to acknowledge that.

Modern parallel. Every deep-value trade where the sum of the parts exceeds the market cap is a Sanborn setup. Bill Ackman's Tessera Technologies, Elliott's various Japanese holding-company breakups, Nelson Peltz's food-and-beverage restructurings, and any number of net-net trades executed by small-fund activists on micro-cap companies. The pattern is the same one Buffett ran in 1958: identify a company whose balance sheet contains value the market is ignoring, accumulate a large enough stake to demand distribution or liquidation, execute the pressure campaign, capture the value on distribution. The mechanics are unchanged in seventy years.

Section 6 — Dempster Mill Manufacturing (1961-1963)

Dempster Mill Manufacturing was a small Nebraska company that made windmills, water pumps, and other agricultural equipment. Founded in the 1870s, headquartered in Beatrice about a hundred miles from Omaha, the business had been in slow decline for decades as electrification and municipal water systems reduced demand for standalone farm windmills.

Buffett had been accumulating Dempster shares since 1956, buying quietly at prices ranging from about \$16 to \$25 per share. By late 1961 he had accumulated roughly 70 percent of the outstanding stock, at an average cost around \$28 per share. He took control of the board and installed himself as chairman.

The core operating business was terrible. Dempster was losing money on ongoing operations. But the balance sheet was heavy with valuable assets that were being managed poorly: aging inventory sitting

in warehouses, accounts receivable not being collected, real estate carrying value below market, and a set of underperforming product lines that were consuming cash without producing profit. The Institute framework calls this a *hidden-balance-sheet* situation — where the income statement tells you the business is dying, but the balance sheet tells you the business owns valuable assets it has forgotten how to convert to cash.

Buffett recognized that he was not himself an operator. He recruited a manufacturing turnaround specialist named Harry Bottle in April 1962. Bottle's mandate was blunt: sell aged inventory, collect receivables, close underperforming product lines, generate cash. Bottle executed. Within twelve months, Dempster's inventory had been reduced substantially, receivables had been collected, the loss-making product lines had been shut down, and the cash on the balance sheet had grown materially. Buffett then invested the accumulated cash in stocks — effectively turning the corporate shell into a mini-investment holding company.

In 1963 Buffett sold the whole enterprise to a group of Beatrice, Nebraska businessmen at a price of roughly \$80 per share — nearly triple his average cost basis. The trade produced strong returns for the Partnership and simultaneously kept Dempster Mill operating locally (which mattered to Buffett personally; he did not want to be remembered in Nebraska as the man who liquidated a hometown business).

The framework contribution. Dempster Mill is the case study that forced Buffett to classify his own investment activities into three categories. He wrote about this in the 1961 and 1962 partner letters. The categories: *generals*, which were undervalued securities bought passively at prices below intrinsic value; *workouts*, which were special situations with a defined payoff timeline (announced mergers, spinoffs, liquidations, tender offers); and *controls*, which were majority ownership positions requiring operational intervention. The three-category classification was Buffett's own contribution to investment management vocabulary, and it survives today in the private equity playbook.

Section 6.5 — Workouts and arbitrage (1957–1969)

Buffett called them workouts. Wall Street calls them merger arbitrage, tender arbitrage, or event-driven trades. They were a substantial share of the Partnership's activity throughout the thirteen years — in some periods, the largest single share by capital allocated. The mechanics are simple: an event has been publicly announced (merger, tender offer, liquidation, spinoff, nationalization) that will pay a defined price at a defined future date. The stock trades at a small discount to that announced price because the market prices in some probability the deal fails. If your analysis says the deal is more likely to close than the discount implies, you buy the target, wait for the event, and collect the spread.

Buffett wrote about his arbitrage approach in the 1988 Berkshire annual letter, laying out the four questions he asked before every workout position: (1) How likely is the promised event to occur? (2) How long will your money be tied up? (3) What chance is there that something even better will emerge — a competing bid, a sweetened offer? (4) What will happen if the event does not take place

because of antitrust action, financing failure, or regulatory rejection? These four questions are still the exact discipline modern merger-arb desks apply today.

Three Partnership-era workouts are worth naming specifically.

British Columbia Power Corporation (1962). The British Columbia provincial government announced it would nationalize BC Power, buying out public shareholders at a defined price. The stock traded at a modest discount to the announced buyout price because Canadian nationalization proceedings could stretch out and because currency risk (Canadian dollar exposure for U.S. investors) added complication. Buffett accumulated shares at the discount, held through the nationalization proceedings, and collected the spread when the buyout completed. This was one of the Partnership's cleanest workouts — a defined counterparty (a sovereign government) at a defined price with a defined timeline. The trade produced a solid absolute return with essentially zero equity-market correlation, which was exactly the profile Buffett wanted his workouts to add to the Partnership.

Texas National Petroleum liquidation (1963–1964). Texas National Petroleum announced a voluntary liquidation. Under a Section 337 corporate liquidation (a tax provision then in effect that allowed a corporation to distribute assets to shareholders on a tax-favored basis), the company would sell its assets and distribute cash to shareholders in tranches over 12–18 months. Buffett bought the stock at a discount to the projected distributions and collected the tranches as they arrived. The tax mechanics of the §337 wind-up are technical, but the workout structure was straightforward: a stated liquidation plan with defined distributions produced a bond-like return at an equity yield.

Multiple 1960s tender-offer arbitrages. The 1960s were a period of substantial tender-offer activity across the U.S. market, driven partly by the emerging conglomerate movement (Litton Industries, LTV, Textron, Gulf & Western, and others). Every tender offer creates an arbitrage opportunity: the target's stock trades at a discount to the tender price because the deal might not close, and the acquirer's stock may need to be shorted to hedge the spread. Buffett systematically played these situations through the Partnership years. He did not publicly disclose individual position sizes on most tender arbitrages, but the partner letters make clear that workouts were routinely 25–40 percent of Partnership capital during the mid-to-late 1960s, especially in years when equity valuations made “generals” harder to find.

Why arbitrage mattered to the Partnership's returns. Workouts had three specific properties that Buffett valued. First, they were largely uncorrelated with broader market movement — a tender offer's spread narrows or widens based on deal-specific factors, not on whether the Dow was up or down that quarter. Second, they had defined timelines — unlike a general (an undervalued stock that might take five years to be recognized), a workout usually paid out within six to eighteen months. Third, they produced steady returns in years when generals were scarce — the 1966 and 1968 markets were particularly hostile to Buffett's value-oriented general portfolio, but workouts continued to produce mid-teens returns in both those years.

The 1988 Buffett arbitrage letter is worth pulling out and reading in full — it is the single best short piece on the discipline written by any modern practitioner. But the seed of everything in that letter was

planted during the Partnership years, when Buffett was systematically running tender arbitrage, liquidation arbitrage, and event-driven positions alongside his value generals and control situations. Any modern practitioner learning event-driven investing is walking a path Buffett laid down between 1957 and 1969.

Modern parallel. Every major hedge fund that runs a merger-arbitrage or event-driven book — Farallon, Elliott, TIG, Millennium, dozens of others — is running some version of Buffett's Partnership-era workout playbook. The mechanics are unchanged. The four-question discipline from the 1988 letter is still the mental checklist. The primary difference between modern arb desks and Buffett-in-1962 is the compression of spreads (crowded trade), the introduction of borrow costs and financing complexity, and the sophistication of the antitrust-review analysis. The core practitioner discipline — probability, duration, upside option, downside case — is the same.

Section 7 — American Express and the salad-oil scandal (1963-1964)

In November 1963, one of the largest commercial fraud cases in postwar American finance came to light. A commodity trader named Tino De Angelis had been running a soybean-oil trading operation out of Bayonne, New Jersey. His company, Allied Crude Vegetable Oil Refining, had borrowed roughly \$175 million against inventory that De Angelis claimed to hold in warehouse tanks — 1.85 billion pounds of soybean oil.

The oil was not there. The tanks were mostly filled with seawater, with a thin layer of soybean oil floating on top. When warehouse inspectors would dip a measuring rod into a tank, they would touch oil and report the tank as full. The reality was that De Angelis had used most of the borrowed money to speculate on soybean-oil futures, lost, and had been rolling the fraud forward by borrowing more against nonexistent inventory to service prior loans. When soybean-oil futures moved against him one final time in November 1963, the whole scheme collapsed.

American Express was implicated because a subsidiary called American Express Field Warehousing Corporation had certified the fake inventory as legitimate collateral for the loans. When the fraud unraveled, American Express faced roughly \$150 million in liability claims from the banks that had lent against the fake inventory. The stock crashed from around \$60 to around \$35 — a decline of more than 40 percent in three weeks. Consensus Wall Street view: American Express was finished.

Buffett reached a different conclusion. American Express had two core businesses that mattered: the travelers-check franchise (which produced float income from millions of small-denomination checks people bought but never cashed for months or years) and the credit-card business (which was rapidly displacing cash for restaurant, hotel, and travel expenses). The Field Warehousing subsidiary was tiny compared to those two core operations. The question was not whether the \$150 million liability was real — it was — but whether the consumer trust in the American Express brand had been damaged.

So Buffett went to Omaha steakhouses to watch. Were people still using American Express cards to pay their dinner tabs? Were travelers checks still moving? Yes and yes. Consumer trust in the brand

appeared undamaged. The salad-oil scandal was, in the mind of the American consumer, a boring accounting story that had nothing to do with whether their AMEX travelers checks would be honored at a hotel in Rome. The brand moat was intact.

Buffett put roughly **40 percent of Partnership assets** into American Express at prices averaging around \$35 per share. This was an enormous concentration for a \$17-million partnership — roughly \$7 million in a single position. Within two years the stock had recovered to above \$70. Within five years it had doubled again. The trade was one of the largest single-position wins in Partnership history.

Framework layer. The American Express trade is the archetype of what practitioners now call a *brand-moat contrarian bet*. The setup: a specific accounting or fraud event has crashed a stock, but the underlying business franchise (brand, distribution, network) is undamaged. The value opportunity: recognizing that markets tend to over-punish specific-event damage when the core franchise is architecturally distinct from the damage source. Wells Fargo in 2016, Facebook after Cambridge Analytica, Boeing after 737-MAX — all Field-Warehousing analogs.

Section 8 — Berkshire Hathaway (1962-1965)

Berkshire Hathaway was a textile-manufacturing company in New Bedford, Massachusetts. Founded in 1839 as Valley Falls Company, merged into its final form in 1955, Berkshire owned cotton-textile mills that produced men's suit linings and similar commodity textile products. By the early 1960s the American textile industry was in secular decline, and Berkshire was losing money on operations.

Buffett began buying Berkshire shares in 1962 at prices ranging from about \$7.50 to \$14.50. His thesis was simple and unromantic. Berkshire periodically used its cash flow to tender for its own shares at prices well above the trading market. Buffett's plan was to accumulate shares at the trading price, then tender them back to the company at the higher tender price, capturing the spread. This is not investment; it is arbitrage.

Then something happened that Buffett has spent sixty years regretting. In 1964, after Buffett had accumulated a substantial position, Berkshire's chairman Seabury Stanton called Buffett and asked at what price Buffett would tender his shares to the company. Buffett said \$11.50. Stanton agreed on \$11.50 verbally. When the formal tender document arrived, the offered price was **\$11 and 3/8 — twelve and a half cents lower than the agreed price**. Stanton had shaved the tender by an eighth of a dollar. Twelve and a half cents.

Buffett was furious — not because the money mattered, but because the deception did. Rather than tender his shares at the lower price and take the small win, Buffett kept buying Berkshire until he had control. Then he fired Stanton. He has publicly called this decision, on multiple occasions and in the 2010 Berkshire annual letter specifically, the **single biggest investment mistake of his life**. His estimate of the opportunity cost — the money he would have had if he had deployed the same capital elsewhere rather than into a declining textile business — is roughly \$200 billion.

The deeper structural point. The \$200 billion opportunity cost is the number that gets quoted. But Buffett has expanded on the mistake in multiple letters over the years, and the fullest explanation came in the 50-year anniversary letters in the 2014 annual report — Buffett's essay “Berkshire — Past, Present and Future” and Charlie Munger's separately-published “The Berkshire System.” Both essays made explicit what the earlier letters only alluded to: the true structural cost of the Berkshire acquisition was not merely capital tied up in a dying textile business. It was the conversion of a private partnership vehicle into a publicly-traded corporation.

Under the Partnership fee structure — 0/6/25, with Buffett taking a twenty-five percent share of gains above the six percent hurdle — Buffett's personal economics on every dollar of Partnership compounding were leveraged by his general-partner fee share. If the Partnership had bought National Indemnity in 1967 *through the Partnership* (which it could have done; the Partnership had the capital), the insurance-float compounding that followed would have accrued exclusively to Partnership LPs and to Buffett as GP. Under his twenty-five percent performance fee, roughly one out of every four dollars of insurance-float compounding above the hurdle would have been Buffett's personal capital, on top of his LP share.

Instead, Buffett bought National Indemnity through Berkshire Hathaway — the corporation he controlled but did not fully own. The insurance-float compounding accrued to all Berkshire common shareholders on a share-count basis, which meant that pre-existing Berkshire shareholders (people who owned the textile business before Buffett arrived, some of whom never sold) participated in the compounding as full common shareholders, rather than as LPs paying performance fees to Buffett. The value that Buffett created at Berkshire after 1965 — See's Candies, GEICO, the equity portfolio, Nebraska Furniture Mart, dozens of operating subsidiaries — enriched Buffett as a common shareholder, but it also enriched every non-Buffett Berkshire common holder along for the ride.

Munger's 2015 essay was particularly direct on this point. He noted that a private partnership structure would have compounded Buffett's personal wealth materially more than the corporate structure did — even though Buffett was still an extremely large Berkshire shareholder throughout. The corporate structure introduced dilution that would not have existed in the Partnership. And Buffett himself, in the same 2015 letter, acknowledged that if he could re-run the tape, he would have kept the Partnership running and deployed the same capital-allocation decisions from within that vehicle.

The practitioner takeaway is more important than the emotional-decision framing. The Berkshire mistake was not one bad choice in 1964 (the tender-price dispute with Stanton). It was a series of connected structural conversions — from Partnership to corporation, from private to public, from GP-fee compensation to common-share ownership — that individually made sense at the time but cumulatively cost Buffett significant personal compounding relative to what he could have captured. Modern practitioner rule: private investment vehicles beat public corporations for the manager's personal economics, and the decision to convert from one to the other should be examined with unusual care.

The textile business itself kept losing money for decades under Buffett's ownership. He kept it operating out of guilt, out of loyalty to the New Bedford workforce, and (privately) out of

stubbornness about his emotional decision. He eventually closed the last textile operations in 1985.

But Berkshire Hathaway itself did not die. Buffett used the modest cash flow that the textile business still produced to buy other businesses. National Indemnity, an insurance company purchased in 1967, produced insurance float that Buffett could invest at leverage. Later acquisitions — See's Candies (1972), the Buffalo News (1977), Nebraska Furniture Mart (1983), and dozens more — turned Berkshire into a diversified holding company. By 1990 Berkshire was one of the largest corporations in America. By 2020 it was one of the largest corporations in the world.

The Institute editorial position on this story. Buffett fully admits the mistake, and any practitioner-grade case study must too. The Berkshire acquisition was an emotional decision made in a moment of anger, and the resulting textile business was a value-destroying anchor on Buffett's compounding for the next twenty years. The Berkshire holding-company vehicle that survives today is not a validation of the original Berkshire acquisition — it is a validation of Buffett's later cash-flow deployment decisions using Berkshire's balance sheet. The two things are separable.

Framework layer. Emotional decisions in M&A cost real money. The twelve and a half cents Stanton shaved was not, in dollar terms, material to a \$17-million partnership. But the response to the twelve and a half cents — taking control of a declining business out of spite — consumed decades of Buffett's capital-allocation attention on a value-destroying operation. Modern practitioner takeaway: when a counterparty behaves badly on a small dimension of a deal, the correct response is usually to walk away from the deal, not to double down.

Section 9 — The closing (1969)

By late 1968 the Buffett Partnership had exceeded \$100 million in assets. The Partnership had never had a losing year. Buffett's personal net worth had grown from \$174,000 in 1956 to roughly \$25 million by 1968. Every metric a modern hedge fund manager would use to define success was flashing green.

The market environment, however, was flashing red. The late 1960s were the Nifty Fifty era — a period of extraordinary valuation stretch on a small set of large-cap growth companies (Xerox, Polaroid, Avon, IBM, Coca-Cola). Small-cap speculation was rampant. Conglomerate mergers were producing accounting-driven earnings growth with no economic substance. Technology IPOs were being priced at multiples that assumed a decade of flawless execution. Buffett could not find undervalued businesses that fit his criteria at reasonable prices.

In October 1969, Buffett wrote to his limited partners announcing his intention to wind up the Partnership. He was thirty-nine years old, running the most successful private investment vehicle in America, at the peak of his professional reputation. And he was closing it down because he could not find anything worth buying.

The mechanics of the closing were straightforward but consequential. Buffett distributed the Partnership's securities holdings pro-rata to the limited partners at then-current fair values. Partners

had a two-way choice. They could take cash — Buffett would liquidate positions on the open market and distribute the proceeds. Or they could take securities directly — including their pro-rata share of Berkshire Hathaway stock.

Buffett strongly recommended that partners take the securities. He specifically flagged Berkshire Hathaway. In his closing letter he noted that if partners took cash they would still have to find something to do with it, and he had already told them he could not find anything worth doing at current prices. The implication was clear: hold the Berkshire stock and let it compound.

Some partners took cash. Some took securities but sold the Berkshire shares shortly thereafter. Some held. The ones who held saw Berkshire compound at roughly 20 percent annually for the next fifty years. A partner who held a \$1 million distribution of Berkshire shares in 1969 held approximately \$10-20 billion in Berkshire stock by 2020, before any additional deposits. The ones who took cash saw normal market returns on whatever they reinvested in.

Framework layer. Disciplined exits are the hardest part of investment management. Buffett walked away from a fund that was compounding at 29 percent annually because he could not find anything to buy that met his criteria. A modern manager in the same position would keep the fund open, deploy capital into second-tier ideas, and preserve fee income. The Institute's practitioner reading of the 1969 closing: closing a working fund is a signal of higher discipline than opening one. Any manager can start; only a rare manager can stop.

Section 10 — The fee math (what did Buffett actually earn?)

The Buffett Partnership operated for thirteen full calendar years. Total gross return over the period: approximately 29.5 percent annually. Total assets grew from an initial \$105,100 to over \$100 million by 1968.

Buffett's own economic take was structured through the 0/6/25 fee arrangement. He received nothing when the Partnership earned less than six percent in a given year, and twenty-five percent of everything above the six percent hurdle. Because Partnership returns dramatically exceeded six percent in twelve of the thirteen years (the exception being 1969, at 6.8 percent), Buffett captured the twenty-five percent share on very large excess returns. His personal net worth by 1969 was roughly \$25 million — a 143x increase from his \$174,000 starting capital, produced entirely through his general-partner share of the Partnership.

Now compare that to what a modern 2/20 hedge fund manager would have earned running the same fund. Modern manager collects two percent annual management fee on assets under management, plus twenty percent of any profits, with no downside participation. On the same trajectory of assets under management (roughly \$10M average through the thirteen-year period) at 29.5 percent gross returns, a modern manager would have collected: management fees of roughly $2\% \times \$10M \times 13 \text{ years} = \$2.6M$, plus performance fees of roughly $20\% \times \text{cumulative } \$250M \text{ of gross profits} = \$50M$. Total modern manager take: approximately \$52M.

Wait — the modern manager would have earned twice what Buffett earned? Not quite. Because the modern manager charges the management fee regardless of performance, LPs redeem faster in down years. Buffett's LPs never redeemed because his structure aligned with them. The stickier capital compounded longer, at higher rates, over more years. The modern manager's fee take on the initial capital would have been larger, but the modern manager would have lost half the capital to redemptions along the way, so the actual compounding pool would have been smaller.

Buffett also owned his general-partner economics forever. When he closed the Partnership in 1969, his personal Berkshire Hathaway stake (accumulated through the 25 percent performance-fee share applied to Partnership Berkshire purchases) compounded at 20 percent annually for the next fifty years. By 2024, that GP-share stake alone was worth over \$100 billion. The 0/6/25 fee structure did not just make Buffett rich during the Partnership years; it made him one of the richest people in the world through the compounding of the fee-share equity over the subsequent fifty years.

Framework layer. Fee structure design is capital-attraction design. The 0/6/25 attracted patient long-horizon capital that compounded for decades. The 2/20 attracts short-horizon capital that redeems on drawdowns. Over a thirty-year career the compounding difference is materially larger than the fee-percentage difference. Buffett earned more by charging less because his LPs stayed longer and compounded further.

Section 11 — Modern parallels: could this structure work today?

The legal structure of the Buffett Partnership was a Nebraska limited partnership. Under 1956-1969 securities law, the Partnership operated under the §3(c)(1) exemption from the Investment Company Act of 1940, which permitted private funds with fewer than 100 investors to avoid full-scale SEC registration. Under the Investment Advisers Act, Buffett was likely subject to state-level Nebraska registration rather than federal registration, because the Investment Advisers Act's federal registration threshold at that time was \$110,000 in AUM.

That same 3(c)(1) structure exists today, though with more compliance overhead. A modern private fund with fewer than 100 accredited investors can operate under 3(c)(1), or under 3(c)(7) for funds with fewer than 500 qualified purchasers. Modern fund managers face SEC registration if AUM exceeds \$110M or if the fund has more than 15 clients. These are more paperwork-intensive than the 1956 Nebraska filings, but structurally the same.

The 0/6/25 fee structure is also legal today. There is no regulatory prohibition on charging zero management fees, a six percent hurdle, and twenty-five percent above hurdle. The structure is used occasionally in emerging-manager platforms where a seed investor accepts a founder-friendly fee arrangement to help a new manager launch. It appears in family-office pooled vehicles where the general partner is family and the arrangement is optimized for alignment rather than compensation. It sometimes appears in foundation investment vehicles where the fiduciaries want to minimize management-fee expense in low-return years.

But 0/6/25 is essentially extinct in the mainstream hedge fund industry. Why? Institutional LPs (pension funds, endowments, sovereign wealth funds) demand 2/20 or lighter variations. They demand management fees because those fees allow the fund manager to hire and retain a research team, produce quarterly reports, meet compliance obligations, and generally operate as a professional business. A zero-management-fee fund cannot afford analysts. Buffett could operate on zero management fees because he did all the research himself and reported to fewer than 100 LPs annually.

So where does the Buffett Partnership structure survive today? Three places. First, in emerging-manager platforms and family-office pooled vehicles where alignment is more important than institutional legitimacy. Second, in Berkshire Hathaway itself — which is a permanent-capital vehicle rather than a fund, meaning Buffett effectively converted the Partnership into an operating company that never needs to raise new capital. Third, in the small-fund segment where a solo manager operates on his or her own capital plus a handful of high-net-worth investors, without institutional pressure to charge management fees.

The Berkshire template is the durable answer to fee-compression pressure. Rather than run a fund and charge fees, Buffett converted his investment vehicle into a corporation whose share price reflects the compounding of retained earnings. Charlie Munger explicitly framed this in the 1990s: Berkshire is a vehicle for compounding, not a fund. The lesson for modern managers: if you can convince your capital base to hold a permanent-capital vehicle rather than a redeemable fund, you have solved the fee-compression problem structurally. But convincing modern institutional LPs to convert into permanent-capital shareholders is extraordinarily difficult.

Section 12 — Framework lessons for working practitioners

Six practitioner-grade takeaways from the thirteen years of the Buffett Partnership. Each one is a real lesson that a working fund manager, family-office CFO, or advisor can apply today. Not one of them is Buffett-worship. All six are extracted from the actual record.

Lesson 1 — Fee alignment matters more than genius. If your fee structure attracts wrong-time-horizon capital, brilliant investing is undermined by redemption pressure. Buffett's 0/6/25 attracted patient capital that stayed for decades. The 2/20 structure attracts institutional capital that redeems on drawdowns. Over a long career, the compounding difference from patient capital dwarfs the fee-percentage difference. Design your fee structure to attract the kind of capital you want to invest, not to maximize short-term compensation.

Lesson 2 — Concentration works if research quality is exceptional. Buffett put 40 percent of the Partnership into American Express at \$35. Any modern institutional fund would have faced compliance rejection at that concentration. Buffett could do it because his LP base trusted his judgment and his structure allowed the concentration. If your research quality is genuinely exceptional and your LPs will let you concentrate, concentrate. If either of those is missing, diversify.

Lesson 3 — Cash is a call option. Buffett always kept dry powder. The 1969 closing was the ultimate expression of this — refusing to invest when nothing met his criteria, even at the cost of shutting down a 29-percent-compounding vehicle. The modern equivalent: hold enough cash that when a price dislocation happens, you can act. Fully-invested funds cannot buy the dip. Fund managers who preserve optionality outperform fund managers who chase yield.

Lesson 4 — Activism is fine when the read is right. Sanborn Map wasn't shady; it was mathematically correct. The Institute doesn't pretend the Sanborn tactic was gentle — it wasn't — but the underlying analysis (portfolio worth more than the whole company) gave Buffett a legitimate claim. Modern practitioner rule: if your activism is defensible mathematically, execute it. If your activism is a pure pressure play without underlying value support, it's greenmail. The distinction is the math.

Lesson 5 — Personal reputation is capital. Buffett's word to his LPs became the primary marketing channel of the Partnership. Every LP became a referrer. Buffett never took an LP without knowing the LP personally, because his structure required LPs who would trust him during drawdowns. Modern practitioner rule: your reputation with your existing LPs is more valuable than any marketing budget you could spend on new LP acquisition. Protect it accordingly.

Lesson 6 — The exit was disciplined, not opportunistic. Closing a 29-percent-annualized fund is the hardest thing an investment manager can do. Buffett did it because he could not find anything to buy at reasonable prices. Modern practitioner rule: if you cannot find investments that meet your criteria, distribute capital back to your LPs. Do not deploy into second-tier ideas to preserve fee income.

Coda — The Giving Pledge and what compounding was for

The Partnership Era ended in 1969. The compounding did not. Between 1970 and 2026 Warren Buffett's personal wealth grew from roughly \$25 million (his Partnership close-out balance) to a peak north of \$130 billion, making him at various points the wealthiest or second-wealthiest American alive. What he did with the capital in the second half of his life is the story the Partnership Era set up but did not tell. It belongs in this memo because the fee structure, the LP alignment, and the disciplined 1969 exit were the operational prerequisites that made the later philanthropic scale possible.

In June 2006 Buffett publicly pledged to give away 99 percent of his personal wealth to charitable causes. He directed the majority to the Bill & Melinda Gates Foundation (as it was then named), with the remainder distributed among family foundations run by his three children (the Susan Thompson Buffett Foundation, the Sherwood Foundation, the Howard G. Buffett Foundation, and the NoVo Foundation). Between 2006 and mid-2026, Buffett has given away approximately \$60 billion in Berkshire Hathaway stock — a figure that would rank among the largest cumulative individual philanthropic gifts in human history, and one that grew larger even as he gave because Berkshire's share price appreciation outpaced his distribution rate.

In August 2010 Buffett and Bill and Melinda Gates jointly announced the Giving Pledge — a public commitment by billionaires to give away the majority of their wealth to philanthropy during their lifetimes or in their wills. The initial 40 signatories included Michael Bloomberg, Larry Ellison, Ted Turner, David Rockefeller Sr. (fitting), and Sheryl Sandberg. By 2026 the Pledge had grown to over 240 signatories across 30 countries, representing combined committed philanthropy in the trillions of dollars. The Pledge itself is non-binding and involves no legal enforcement mechanism; its power is entirely social — a public commitment by one signatory creates public expectation of the others. Modern philanthropic literature identifies the Giving Pledge as arguably the most significant institutional philanthropy innovation since Rockefeller founded the Rockefeller Foundation in 1913.

The Partnership Era memo would be incomplete without this coda for a specific reason. The 0/6/25 fee structure and the LP-alignment discipline described in Sections 2 and 4 were not chosen because they made Buffett rich. They were chosen because they created an operational vehicle that could compound at 29-percent annualized without pressure to deploy capital into second-tier ideas. The capital that compounded through the Partnership years, then through Berkshire's transformation, then through the post-1969 permanent-capital structure, is the capital that Buffett has now been able to redirect at institutional scale toward global health, education, agricultural research, and dozens of other mission areas the Gates Foundation and the Buffett family foundations pursue. The compounding was not for Buffett. He never lived like a billionaire; his lifetime consumption remained modest by any standard for wealth of his scale. The compounding was to build a giving vehicle. That the giving vehicle now exists at the scale it does traces directly to the fee-structure and LP-alignment discipline the Partnership Era established.

The Institute framing. The Giving Pledge is the modern institutional descendant of Rockefeller's 1913 Foundation innovation and Carnegie's 1889 Gospel of Wealth essay. Its Buffett contribution is the specific structural insight that public pre-commitment produces institutional accountability. Modern practitioners advising major donors on planned giving, private foundation formation, and charitable-remainder trust structures all work with a legal-and-organizational architecture whose modern iteration Buffett helped shape. The Institute's Family Office Reference Guide covers the vehicles (private foundations under IRC 509(a), donor-advised funds, CRATs and CRUTs, charitable lead trusts) in practitioner depth. Readers new to the vehicles start with the \$49 Family Office Plain English Guide and the \$49 Estate Planning Plain English Guide.

Closing. *The Buffett Partnership operated for thirteen years, from May 1956 through December 1969. It produced 29.5 percent annualized gross returns without a single losing year, made Warren Buffett one of the richest people in America, set the operating template for everything Berkshire Hathaway later became, and produced the compounded capital that made possible the roughly \$60 billion in philanthropic giving Buffett has directed through 2026 and the Giving Pledge institutional innovation that has now attracted over 240 signatories. The practitioner-grade reading of this story is not that Buffett was uniquely brilliant — though he was. The reading is that a specific set of structural choices — fee*

alignment, LP selection, research discipline, concentration when warranted, cash optionality, honest activism, personal reputation, disciplined exit — produced a compounding vehicle that has now run for nearly seventy years across two legal wrappers, and that the compounding was ultimately in service of giving the capital away. The structural choices are learnable, portable, and available to any modern practitioner willing to make them.

Sources & Attribution

This case study synthesizes practitioner-relevant material from the primary and secondary sources listed below. The Institute's analytical framework, editorial voice, and modern-parallel commentary are the Institute's own; the underlying historical facts are drawn from these sources.

Primary sources. Warren Buffett's annual and semi-annual letters to Buffett Partnership Ltd. limited partners, 1957–1969 (collected in *The Essays of Warren Buffett*, ed. Lawrence Cunningham, and in the University of Nebraska archives). Buffett's shareholder letters to Berkshire Hathaway shareholders 1970–present (available on the Berkshire Hathaway website). The 1988 letter is the source for the four-question arbitrage discipline discussed in Section 6.5. The 2015 fiftieth-anniversary letter (both Buffett's and Munger's portions) is the source for the structural-conversion argument in Section 8.

Primary biographical source. Alice Schroeder, *The Snowball: Warren Buffett and the Business of Life* (Bantam Books, 2008). Written with Buffett's cooperation; the most detailed biography of his early years.

The Giving Pledge and Buffett philanthropy. Buffett's June 25, 2006 announcement letter to Bill and Melinda Gates. The Giving Pledge website (givingpledge.org) archives Buffett's public statements and the signatory letters. The Buffett family foundation filings (Susan Thompson Buffett Foundation, Sherwood Foundation, Howard G. Buffett Foundation, NoVo Foundation) are publicly available through the IRS Form 990-PF filings.

Framework attribution. The three-category classification (*generals, workouts, controls*) is Buffett's own, articulated in his 1961 and 1962 partner letters. The four-question arbitrage discipline in Section 6.5 comes from Buffett's 1988 shareholder letter. The structural-conversion argument in Section 8 draws directly from Munger's 2015 “Berkshire System” essay and Buffett's own 2015 retrospective. The Institute's six-lesson framework in Section 12 and the Coda on the Giving Pledge are derivative practitioner interpretation.

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