1985 WL 53894 (S.E.C. No - Action Letter)

(SEC No-Action Letter)

***1 Podiatric**
Assurance
Company

Publicly Available February 19, 1985

SEC LETTER

1934 Act / s 12(g)
1940 Act / s 3(a)
1933 Act / s 2(1)

January 18, 1985
Publicly Available February 19, 1985

We would not recommend that the Commission take any enforcement action under the Investment Company Act of 1940 ("1940 Act") if the proposed **Podiatric Assurance** Company ("Company") is operated without being registered under the 1940 Act in reliance upon your opinion as counsel that the Company is not an investment company under section 3 of the 1940 Act. This position is based on the representations made in your letter of November 23, 1984.

The Division of Corporation Finance has advised us that it will not recommend enforcement action to the Commission if, in reliance upon your opinion as counsel that registration is not required, the Company proceeds with the offer and sale of memberships and the writing and delivery of insurance policies without compliance with the registration requirements of the Securities Act of 1933. In addition, that Division will not recommend enforcement action if the Company does not comply with the registration provisions of section 12(g) of the Securities Exchange Act of 1934.

Gerald T. Lins
Attorney

LETTER TO SEC

November 23, 1984

Office of the Chief Counsel
Divisions of Corporation Finance and Investment Management
Securities and Exchange Commission
Washington, D.C. 20549

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Attention: Divisions of Corporation Finance and Investment ManagementDear Sirs:

We represent the Academy of Ambulatory Foot Surgery (the “Academy”). The Academy is seeking to form the **Podiatric Assurance** Company (the “Company”), a captive insurance company, to provide malpractice insurance to some of its members. On behalf of the Academy and its members, we hereby request that we be advised that no action will be recommended by the Staff of the relevant Divisions of the Securities and Exchange Commission (the “Commission”) if the proposed offer and sale of membership interests in the Company proceed without registration under the Securities Act of 1933 (the “Securities Act”), the Securities Exchange Act of 1934 (the “Exchange Act”), or the Investment Company Act of 1940 (the “Investment Act”).

I. INTRODUCTION

The Board of Trustees of the Academy has recently approved the participation by members of its Ad Hoc Committee for Captive Insurance Company in the organization of the Company, an “Ordinary Company” under the laws of the Cayman Islands. The Company will offer malpractice coverage to Academy members who are licensed podiatrists practicing in the United States. The laws of the Cayman Islands do not specifically provide for the operation of the Company as a mutual association, and thus ownership of the Company will be evidenced by shares of capital stock issued to the Company's members. The Company will be managed by a Board of Directors selected by the Academy. Pursuant to a proposed management agreement with the Company, the day-to-day operations of the Company will be conducted by Johnson & Higgins Ltd. of the Cayman Islands (“Johnson & Higgins Ltd.”), a subsidiary of Johnson & Higgins, Inc., the insurance brokerage and management firm having offices in the United States and throughout the world.

***2** The formation of the Company has become necessary due to the diminished availability and increased cost of malpractice insurance in the conventional commercial market. This trend has long been evident throughout the healthcare industry and has had a particularly immediate and substantive impact on Academy members. In September 1984, the insurance company that currently writes most of the malpractice insurance of Academy podiatrists announced that it would not renew its malpractice coverage beyond the term of its current policies. The bulk of these policies lapse on january 31, 1985, and in no event continue beyond December 31, 1985.

In view of these conditions, the captive insurance company remains one of the few feasible alternatives for the provision of malpractice insurance to members of the Academy. The Company will accord to its insureds the same benefits as have been mentioned in other, similar proposals submitted to the Commission: (1) dependable, long-term and consistently-priced malpractice insurance; (2) minimal acquisition costs due to the elimination of sales commissions and overhead incident to the operation of large commercial insurance carriers; and (3) better and more thorough programs on loss prevention and other related topics.[FN1]

FN1 *See* Podiatry Insurance Co. of America (available July 7, 1980 on LEXIS, FedSec library, NoAct file).

End of Footnote(s).II. STRUCTURE AND OPERATIONS

The Company will be organized under the Cayman Islands Insurance law as a “Class B” insurer licensed to carry on an insurance business on foreign risks from within the Islands. Its organization and operations will be subject to review and regulation by the Cayman Islands Insurance Superintendent. Podiatrists and podiatric partnerships, professional corporations and professional associations will become the “members” of the Company by making membership contributions.

The by-laws of the Company will provide for a Board of Directors of from five to seven directors, which will in-

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clude practicing podiatrists insured by the Company and elected by members of the Academy. It is contemplated that the initial directors to be elected to the Board of Directors will reflect, to some extent, the national geographical distribution of Academy members.

All aspects of the Company's business will be professionally managed. Initially, the Company proposes to enter into a management agreement with Johnson & Higgins Ltd., which has had substantial previous experience in the organization and management of captive insurance companies for medical and other professional malpractice purposes. Under the proposed agreement, Johnson & Higgins Ltd. would be responsible on a day-to-day basis for general administration and underwriting services. Investment of the Company's funds will be managed by a professional funds manager, subject to guidelines established by an Investment Committee selected by the Company's Board of Directors. The Academy expects to use Bank of America NT & SA for all Company banking and financial management services, and Coopers & Lybrand (the Academy's independent public accountants) for accounting and auditing services.

***3** Annual premiums will be established according to generally accepted actuarial principles and will be payable to the Company. Premiums will vary for individual podiatrists based upon various factors, including location, type of practice, and previous claims history.

The Company's insurance policies will provide malpractice coverage of up to $100,000 for each claim and up to $300,000 as an annual aggregate for all claims. The policy form used by the Company will be a modified “claims made” policy. Members, on an individual basis, may be entitled to purchase “tail” coverage from the Company following retirement or termination of their policies for other reasons. The availability of and premiums for such “tail” coverage will vary in accordance with the Company's underwriting principles and rate schedule in effect when the policy is terminated.

Upon reaching a membership of 100 insureds (which the Academy hopes will occur within a year after the Company's formation), the Company will seek to enter into reinsurance agreements covering losses up to $1,000,000 for each claim and $1,000,000 in the aggregate for each policy. The reinsurance agreements are currently under negotiation.

Membership initially will be open to Academy members who are licensed podiatrists practicing in the United States, including podiatric partnerships, professional corporations or professional associations, all of whose partners, stockholders, or members, as the case may be, will be insured by the Company. As long as contributions are required as a condition of membership, any podiatrist who is a member of the Academy and is interested in becoming a member of the Company must tender a check in the amount of $5,000 as a membership contribution. The applicant will then submit an application and will be notified subsequently by the Company upon acceptance or rejection of his application by the Company and its Underwriting Review Committee. Membership contributions will be returned as soon as practicable to any applicant who is not accepted for membership.

III. PARTICIPATION

The organization of the Company requires the participation of both the Academy as well as its individual members. Accordingly, it is necessary to discuss in turn both the extent to which the members and the Academy will participate in the organization and operation of the Company.

A. The Members

All prospective members of the Company will be required to enter into an undertaking that relates to the level of their participation in the Company's programs. This undertaking will include a promise to cooperate with the

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Company in the administration of a safety and loss prevention program, and regular reporting to the Company (on a confidential basis) with regard to the members' malpractice claims activity and loss exposure.

Some of the Academy's members are now covered by insurance policies that will continue in effect beyond the Company's start-up phase. For this reason, although members generally will participate actively in the programs of the Company, the Company cannot, as a practical matter, require that members immediately acquire additional insurance written or reinsured by the Company. Rather, the by-laws of the Company will require any applicant seeking membership in the Company to meet customary objective insurance underwriting criteria and either (1) acquire or apply for malpractice insurance written by the Company or (2) represent an intention to acquire such insurance within a prescribed time period.

***4** With regard to those members that do not immediately acquire or apply for insurance written by the Company, the Company's by-laws will require that such members obtain such insurance no later than four years after being accepted as members. A member may, at its option within that period, apply for such insurance. If insurance coverage is denied on the basis of objective insurance underwriting criteria, the Company's by-laws will provide that, over the course of the next five years, the member who has been denied insurance coverage will be required to sell that membership interest in the Company to another eligible candidate for membership, subject to the Company's transfer restrictions mentioned below.

To comply with Cayman Islands laws regarding minimum paid-in capital and minimum capital surplus, initial membership contributions will be required of every member as a precondition to obtaining insurance or reinsurance by the Company of malpractice risks. Membership contributions will be noted by the Company's issuance of capital stock, as required by Cayman Islands law.

The membership contributions will be noninterest-bearing and the membership interest will be nontransferable except (1) as an incident to a business combination or reorganization of the Company or (2) if a member dies, is denied coverage or wishes to sell his, her or its interest to a person eligible for membership. Under these latter exceptions, a transfer may be made only to another person who meets the underwriting criteria for membership and who purchases such interest for a sum not to exceed the amount of the seller's original membership contribution. All members will be eligible to participate pro rata in any distribution in liquidation paid by the Company and in any dividends which the Board of Directors determines is in the best interests of the Company and would not reduce the Company's funds below the amount needed to provide adequate reserves or meet Cayman Islands regulatory requirements.

Although the Academy plans to encourage participation by its membership, it anticipates that approximately 50 members will participate in the initial organization of the Company. Initially, the amount of membership contributions to be assessed against each participating member will be $5,000. The Company may discontinue the assessment of membership contributions from prospective members upon determining that such contributions are no longer needed, or from time to time may vary the amount of membership contributions required. It is presently contemplated, however, that the Company, at least for the next few years, will continue to require membership contributions from prospective members as a condition of obtaining insurance coverage through their affiliation with the Company.

The Company does not intend to declare any dividends in the first few years of its operation. Thereafter, the Board of Directors is authorized to declare dividends for all members presently insured through their affiliation with the Company. Alternatively, the Board of Directors, may reduce future premiums or increase insurance

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coverage available to policyholders. Altered premium schedules and coverages will likely be preferred over cash dividends, should the financial resources of the Company warrant some form of readjustment.

B. The Academy

***5** The formation of a captive insurance company is an unprecedented step for Academy members. Moreover, it must be accomplished quickly to minimize the effects of lapsed coverage beginning January 31 of next year. Accordingly, the Academy itself has taken a leading role in the operation of the Company, and will participate in its organization. That participation will take two forms, as discussed below.

First, the Academy wishes to retain control over corporate decision-making to ensure that proper steps will be taken to secure the long-term viability and integrity of the Company and to ensure that the Company will serve both its members and insureds to the maximum extent possible. Second, the Academy will be required to help provide a substantial part of the initial financing necessary to organize the Company and commence its operations. Control by the Academy over the Company's operations will continue indefinitely, as the Academy possesses the experience and managerial expertise necessary to supervise the Company's operations through the Company's Board of Directors. The Academy's financial involvement in the Company will be short-term, existing only until the Company has an adequate number of individual members to provide sufficient capital for its operation.

It is proposed that the control and financial objectives of the Company will be achieved through the issuance of two classes of common stock. The Company's financial resources will be provided through the issuance of shares of Class “A” stock. In return for an initial contribution of $80,000 the Academy will be issued 80 shares of Class A common stock. Thereafter, up to approximately 300 shares of Class A common stock will be issued to subscribing members to evidence membership contributions. The Academy expects to retain ownership of its shares of Class A common stock for one to two years, the length of time the Academy estimates will be necessary for the Company to have sufficient individual members to provide adequate capital. The Academy also anticipates that upon reaching an appropriate level of membership contributions, the Academy could commence withdrawing its initial $80,000 contribution without the prospect of harm to the Company. It is currently anticipated that when an aggregate of approximately $300,000 has been contributed to the Company by its members, the Academy will gradually sell its shares of Class A common stock in $5,000 blocks to incoming members until the Academy's initial $80,000 contribution has been, in effect, “returned.” Thereafter, contributing members will simply be issued new shares of Class A common stock out of a total authorized capital of 1,000 shares, until the Board of Directors of the Company determines that membership contributions are no longer necessary. Thereafter, new members will not be required to make membership contributions to participate in the Company's insurance programs.

The simplest means of retaining control of the Company in the Academy consistent with Cayman Islands Company Laws is to create a second class of common stock. It is anticipated that the Academy will subscribe to all of the Class “B” common stock of the Company for a capital contribution of approximately $20,000. These Class B shares will have the right to elect all of the Company's directors, but will possess no dividend rights, will be non-transferable and will not participate in the distribution of assets upon liquidation beyond a return of initial paid-in capital. Using the exclusive voting rights connected with ownership of these shares, the Academy will exercise control over the Board of Directors of the Company without having to expend funds in an undertaking from which the Academy itself would derive no financial or insurance benefits.

C. Protection of Participant's Membership Contributions

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***6** The Academy and its members both wish to eliminate any unnecessary risk in the formation of the Company. Accordingly, the Academy will open an escrow account with a bank in the Cayman Islands as a repository for all initial membership contributions until an amount set by the Cayman Islands Insurance Superintendent has been deposited. This minimum amount of membership contribution will reflect the Superintendent's judgment not only as to what constitutes adequate financial reserves, but also as to the level of capitalization necessary to sustain the Company's operations under even extraordinary circumstances. The minimum capitalization necessary for a Cayman Islands Insurance Company is $120,000; it is expected that the Superintendent's figure (based on approximately 50 initial participants) will be closer to $300,000.

The Academy's escrow agreement will provide that when the amount specified by the Superintendent is reached, the funds will be released to the Company simultaneously with receipt of a certificate of authority and other relevant approvals from the Cayman Islands regulatory authorities. (At this time, the Academy will begin to sell its Class A shares to incoming insureds and gradually dispose of its equity interest as described above, until the Academy is left only with its Class B shares). These measures assure the participants that their money will be used only in the formation of a fully viable insurance company.

IV. LEGAL DISCUSSION

A. Registration Under the Securities Act of 1933

It is our opinion that, based upon these facts, neither the offer or sale of memberships in, nor writing and delivery of insurance policies by the Company constitute “securities” as that term is defined in Section 2(1) of the Securities Act of 1933 (the “1933 Act”).[FN2]

FN2 That section defines “security” as follows:
“any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest, or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a “security,” or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase any of the foregoing.”

End of Footnote(s).Insurance policies written by the Company constitute “insurance”, not securities, and fall within the exemptions that have been mentioned repeatedly in previous submissions to the Commission. According to the House of Representatives document reporting the 1933 Act, “Insurance policies are not to be regarded as securities subject to the [1933] Act.” [FN3]

FN3 H.R.Rep. No. 85, 73d, 1st Sess. 15 (1933).

End of Footnote(s).***7** Certain insurance policies are given an express exemption under Section 3(a)(8) of the 1933 Act. However, this has not been deemed to limit the applicability of the exemption to other policies. The Commission has maintained that insurance was not an intended or appropriate focus of regulation under the federal securities laws.[FN4] Accordingly, the Academy respectfully requests a finding consistent with these principles and a long line of other no action letters that the insurance policies written by the Company do not constitute securities.

FN4 See Hearings on S. 2408 Before the Subcomm. of the State Comm. on Banking and Currency, 81st Cong.,

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2d Sess. 33 (1950). As Professor Louis Loss, who testified on behalf of the Commission in 1950, has explained, the insertion of an express exemption for insurance policies "is a perfect example of how it sometimes does not pay to be too cautious. Without this exemption, and without any specific reference to insurance policies in the definition of 'security,' ... it is hardly conceivable that Congress would have subjected insurance policies to federal control sub silentio, even control which was merely of the disclosure variety." 1 Loss, Securities Regulation 497 (2d ed. 1961). See also Insurance Company of North America (available May 20, 1983 on LEXIS, FedSec library, NoAct file; Podiatry Insurance Company of America, supra note 1.

End of Footnote(s).The Company's shares issued to evidence membership contributions also fall outside the definition of security. That the shares are called "stock" is a matter of "tradition and convenience" [FN5] related solely to establishing the Company with a minimum of confusion and consistent with Cayman Islands law. It is customary in the Cayman Islands to use stock to reflect ownership by members and simply assures the Cayman Islands authorities that the shares issued reflect the membership contributions necessary to make the Company viable under Cayman Islands laws. If the Commission adheres to the "basic principle" that has guided the Supreme Court,[FN6] it should not, in our opinion, conclude that these shares are securities.

FN5 United Housing Foundation, Inc. v. Forman, 421 U.S. 837, 848, n. 13.

FN6 United Housing Foundation, Inc. v. Forman, supra, 421 U.S. at 848 ("[I]n searching for the meaning and scope of the word 'security' in the Act[s], form should be disregarded for substance and the emphasis should be on economic reality") (quoting Tcherepnin v. Knight, 389 U.S. 332, 336 (1967))

End of Footnote(s).The Court in Forman set forth the specific indicia of "securities" as that term is defined in the 1933 Act. Virtually none of these indicia characterize the Company's shares of Class A common stock. The shares carry only a theoretical right to receive dividends contingent upon profits; in fact, this right will not have any practical consequence for at least a few years, and any "return" members do receive will likely be in the form of reduced premiums on their malpractice coverage, contingent on the volume of insurance claims in a given year, and the Company's capacity to meet them.[FN7] The shares are not negotiable except to other podiatrists, and this negotiability is limited because membership in the Company is guaranteed to podiatrists meeting the requisite underwriting criteria for obtaining coverage. The shares cannot be pledged or hypothecated; they cannot appreciate in value. For every participant besides the Academy, the shares carry no voting rights.

FN7 Company dividends will evidence the same limited rights and reflect the same purpose as those discussed in Insurance Company of North America (available May 20, 1983 on LEXIS, FedSec Library, NoAct File).

End of Footnote(s).***8** Shares of Class B stock issued to the Academy will carry voting rights. However, these rights are not an attribute of the shares that reflect an inherent characteristic of "securities"; rather, these voting rights are merely a mechanism that allows the Academy to control the affairs of the Company for the benefit of the insureds. The Class "B" shares lack every other indication of "stock" mentioned above. They carry no dividend rights, and no liquidation rights beyond those necessary to return paid-in capital. The shares are not transferable. Indeed, the presence of voting rights does not change the economic substance of the Class B shares so as to make them any more like the "ordinary concept" [FN8] of a security than Class A Shares. We do not believe that the mere presence of voting rights should dictate that the 1933 Act must be applied to the Class B shares.

FN8 H.R. Report No. 85, supra note 3, at 11.

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End of Footnote(s).We wish to note that, by virtue of its ownership of Class A shares and Class B shares, the Academy will have both theoretical dividend rights and the voting rights of its Class B shares for an approximate period of one to two years. We emphasize this is a short-lived, unavoidable coincidence that should not alter the Commission's view of this transaction: these rights will coexist, but the Class A shares will be sold before any meaningful dividends accrue, and the ownership of both classes of shares is so strongly tied to the other managerial and organizational imperatives that are discussed herein, and that have nothing to do with any investment purpose, that there should be no question of applying the 1933 Act simply on the basis of this temporary simultaneity in ownership.

The shares cannot be termed “investment contracts” as that term is defined in the Securities laws. The members' contributions will be noninterest-bearing and nontransferable and hardly suggest any profit-making potential. The memberships are strictly a requirement of, and ancillary to, acquiring insurance in the wake of abandonment by the members' major commercial insurer. The “inducement to purchase” for these participants is to provide themselves with insurance, “not to invest for profit”.[FN9] The Academy, likewise, was induced to participate in the Company for reasons unrelated to making a profit. It is in fact impossible for the Academy to enjoy any “profit” from its membership interests; its Class A shares will be sold at cost to incoming members before any dividends accrue, and its Class B shares carry no dividend rights, very limited liquidation rights, and are not transferable.

FN9 Forman, 421 U.S. at 851.

End of Footnote(s).The reduction of insurance costs through the declaration of dividends is not part of an investment contract. It is a means of providing insurance at cost. It resembles the rental reductions afforded to purchasers of apartment cooperatives in Forman. The Supreme Court in Forman held that the availability of these reductions, though based on leases of commercial facilities owned by the cooperative, did not satisfy the “expectation of profit” requirement for an investment contract. The apartment purchasers were attracted to the cooperative by the prospect of acquiring living quarters (just as Company members are attached by the prospect of acquiring insurance), and not by financial returns on their investment.[FN10]

FN10 421 U.S. at 856-58.

End of Footnote(s).***9** Moreover, the contributions of the Academy and the individual podiatrists do not constitute “risk capital” as that term has been applied to definitions of “investments” and used for the purpose of defining investment contracts.[FN11] The escrow arrangement providing for the escrow of funds until such time as the viability of the Company is assured, eliminates any element of “risk” associated with the Company's formation.

FN11 Annot., 68 A.L.R. Fed. 89, 98.

End of Footnote(s).A long line of no-action positions taken by the Staff of the Commission in circumstances similar to those set forth in this letter supports our conclusion that the registration requirements of the Securities Act of 1933 are inapplicable to the sale of membership interests in captive insurance companies or insurance cooperatives.[FN12]

FN12 Insurance Company of North America, (available May 20, 1983, LEXIS, FedSec library, NoAct file); Health Ass'n Mutual Ins. Co., (available Nov. 23 1981 on LEXIS, FedSec library, NoAct file); Midwest Industrial Management Association, (available Oct. 16, 1981 on LEXIS, FedSec library, NoAct file); Grocery Manu-

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facturers of America Mutual Insurance Co. Ltd., (available Nov. 6, 1980 on LEXIS, FedSec library, NoAct file); Catholic Health Ass'n, (available May 29, 1981 on LEXIS, FedSec library, NoAct file); National Electrical Contractors' Ass'n, (available Apr. 13, 1981 on LEXIS, FedSec library, NoAct file); Grocery Manufacturers of America Mutual Insurance Co. Ltd., (available Nov. 6, 1980 on LEXIS, FedSec library, NoAct file); Podiatry Insurance Co. of America, (available July 7, 1980 on LEXIS, FedSec library, NoAct file); Chem-Spec Insurance Ltd., (available May 12, 1980 on LEXIS, FedSec library, NoAct file); Nuclear Electric Insurance Ltd., (available Feb. 28, 1980 on LEXIS, FedSec library, NoAct file); Medical Device Mutual Assurance and Reinsurance Co., Ltd., (available Aug. 31, 1979 on LEXIS, FedSec library, NoAct file); First Illinois Religious and Charitable Risk Pooling Trust, (available May 12, 1979 on LEXIS, FedSec library, NoAct file); Attorney's Liability Assurance Society Ltd., (available Feb. 12, 1979 on LEXIS FedSec library, NoAct file); Illinois Hospital Ass'n, (available Nov. 17, 1978 on LEXIS, FedSec library, NoAct file); Ancilla Domini Sisters (available Oct. 16, 1978 on LEXIS, FedSec library, NoAct file); Chicago Hospital Council (available Aug. 3, 1978 on LEXIS, FedSec library, NoAct file); Doctors Co., (available May 12, 1978 on LEXIS, FedSec library, NoAct file); Medical Inter-Insurance Exchange of New Jersey, (available May 5, 1978 on LEXIS, FedSec library, NoAct file); HAPI and the Physicians' Indemnity Plan, (available Feb. 23, 1978 on LEXIS, FedSec library, NoAct file); Cooperative of American Physicians, Inc., (available Jan. 28, 1977 on LEXIS, FedSec library, NoAct file); Total Health Care Services Corp., (available Oct. 7, 1976 on LEXIS, FedSec library, NoAct file); State Volunteer Mutual Insurance Co., (available Jan. 19, 1976 on LEXIS, FedSec library, NoAct file); Multihospital Insurance Ltd., (available Apr. 21, 1975 on LEXIS, FedSec library, NoAct file); National Business Services, Inc., (available Dec. 20, 1974 on LEXIS, FedSec library, NoAct file); General Assurance Services, Ltd., (available Dec. 16, 1974 on LEXIS, FedSec library, NoAct file).

End of Footnote(s).B. Registration Under the 1934 Act.

***10** Although the Company may have more than 500 members and $1,000,000 in assets if it meets the conditions to commencement of operations described above, in our opinion it will not be subject to the registration requirements of Section 12(g) of the Securities Exchange Act of 1934, as amended (the “1934 Act”). Section 12(g) of the 1934 Act provides that certain “issuers” with total assets exceeding $1,000,000 and a class of “equity securities” held of record by 500 or more persons must register such securities under the 1934 Act. However, Section 3(a)(8) of the 1934 Act defines “issuer” as “any person who issues or proposes to issue any security” and Section 3(a)(11) of the 1934 Act defines “equity security” as including “stock or similar security” and certain other instruments or rights each of which must, in itself, be a security.

Thus, to be subject to Section 12(g) of the 1934 Act, a company must issue “securities.” The definition of “security” in Section 3(a)(10) of the 1934 Act is identical in all pertinent respects to the definition of “security” in Section 2(1) of the 1933 Act. (See discussion of the 1933 Act above.) Accordingly, it is our view that the interests to be offered and sold are not “securities”; that the Company, therefore, will not be an “issuer” and will not have any “class of equity securities”; and that the Company, therefore, will not be subject to the registration requirements of Section 12(g) of the 1934 Act.

C. Registration Under the Investment Company Act of 1940.

Under Section 3(a) of Investment Company Act of 1940 (the “1940 Act”), an “investment company” is defined as any issuer satisfying one or more of subparagraphs (1), (2) or (3) of that Section. The term “issuer” is defined in Section 2(a)(22) as “every person who issues or proposes to issue any security, or has outstanding any security which it has issued.” The term “security” is defined in Section 2(a)(36) in the same manner as “security” is defined in Section 2(1) of the 1933 Act. Accordingly, for the reasons already discussed with regard to the 1933

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Act, it is our view that the interests to be offered and sold by the Company are not “securities” for purposes of the 1940 Act; that the Company is not an “issuer” under that statute; and that the Company, therefore, is not an “investment company.”

Even if the Company were to come within the “investment company” definition under Section 3(a), Section 3(b)(1) excludes “any issuer primarily engaged ... in a business or businesses other than that of investing, reinvesting, owning, holding or trading in securities.” Since, as described above, the Company's primary business will be insuring or reinsuring its members against malpractice risks, the Company falls within this statutory exclusion. Our conclusions in this regard draw support from a number of no-action positions taken by the Staff. [FN13]

FN13 See, e.g., Podiatry Insurance Co. of America, (available July 9, 1980 on LEXIS, FedSec library, NoAct file); Nuclear Electric Insurance Ltd., (available Feb. 12, 1980 on LEXIS, FedSec library, NoAct file); First Illinois Religious and Charitable Risk Pooling Trust, (available May 12, 1979 on LEXIS, FedSec library, NoAct file); Attorney's Liability Assurance Society, Ltd., (available March 8, 1979 on LEXIS, FedSec library, NoAct file); Illinois Hospital Ass'n, (available Dec. 20, 1978 on LEXIS, FedSec library, NoAct file); Great Northern Administrators, Inc., (available March 31, 1978 on LEXIS, FedSec library, NoAct file); HAPI and the Physicians' Indemnity Plan (available Feb. 23, 1978 on LEXIS, FedSec library, NoAct file); Cooperative of America Physicians, Inc., (available Feb. 7, 1977 on LEXIS, FedSec library, NoAct file); Total Health Care Services Corp., (available Oct. 7, 1976 on LEXIS, FedSec library, NoAct file); National Business Services, Inc., (available Feb. 18, 1975 on LEXIS, FedSec library, NoAct file).

End of Footnote(s).***11** Based on these facts and our conclusions with respect to the application of the 1933 Act, the 1934 Act and the 1940 Act, we respectfully request your advice as to whether you concur in our conclusions and as to whether the Commission Staff would recommend that no action be taken by the Commission if, as described above, the offer and sale of memberships and the writing and delivery of insurance policies is effected by the Company without compliance with the registration requirements of the 1933 Act, the 1934 Act, or the 1940 Act.

In order for the Company to begin operations by January 31, its organizers estimate that the required capital must, as a practical matter, be raised by at least January 1, 1985. To do so, the Company must first be able to distribute informational materials to prospective insureds. In view of this timetable, we respectfully request the most expeditious treatment possible on this matter, consistent with other demands that may be placed upon Staff resources.

In accordance with Securities Act Release No. 6269 (Dec. 5, 1980), we enclose seven additional copies of this letter for the Staff of each Division. If you have any questions or comments regarding our request, please call the undersigned or Keith C. Cochran at 206-682-5151. In addition, we specifically request that you contact us prior to your transmittal of a written response if, in that response, you decline to take a no-action position.

Sincerely,

BOGLE & GATES
Karl J. Ege

1985 WL 53894 (S.E.C. No - Action Letter)

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