

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION

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In the Matter of

THE TRUST FUND SPONSORED BY THE  
EPISCOPAL SCHOOL FOUNDATION COLLEGE  
AWARD PROGRAM, INC.

c/o Episcopal School Foundation  
College Award Program, Inc.,  
(Sponsor)  
3100 East Oakland Park Boulevard  
Fort Lauderdale, Florida

(812-2229)

(Investment Company Act of 1940)

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**FILED**

**OCT 25 1968**

**SECURITIES & EXCHANGE COMMISSION**

INITIAL DECISION

Sidney Gross  
Hearing Examiner

Washington, D.C.  
October 24, 1968

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Before: Sidney Gross, Hearing Examiner

Appearances: Lewis J. Mendelson and Allen B. Witz for the  
Division of Corporate Regulation

Frank E. Freeman for The Trust Fund Sponsored  
by the Episcopal School Foundation College  
Award Program, Inc.

This proceeding was instituted by the order of the Securities and Exchange Commission ("Commission") dated April 17, 1968, directing that a hearing be held on an application filed by The Trust Fund Sponsored by The Episcopal School Foundation College Award Program, Inc. ("applicant") pursuant to Section 6(c) of the Investment Company Act of 1940 ("Act").

The application and an amendment thereto filed during the course of the hearing assert that applicant is not an investment company within the meaning of the Act by virtue of the various exceptions provided by Section 3 of the Act. In the alternative, the application seeks exemption from certain sections of the Act, orders under other sections of the Act and complete exemption from registration under Section 6(c) of the Act.<sup>1/</sup>

The Commission's order of April 17, 1968 presents the following matters and questions for consideration:

- "(1) Whether Applicant is an investment company within the meaning of Section 3(a) of the Act;
- (2) Whether Applicant, pursuant to Section 3(c)(3), 3(c)(8) or 3(c)(12) of the Act, is excepted from the definition of an investment company;
- (3) Whether the granting of the requested exemptions and orders under the Act is (a) necessary or appropriate in the public interest, (b) consistent

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<sup>1/</sup> Section 6(c) authorizes the Commission to exempt any person, security or transaction from all provisions of the Act if it finds such exemption is "necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions" of the Act.

with the protection of investors, and (c) consistent with the purposes fairly intended by the policy and provisions of the Act; and

- (4) If the requested exemptions and orders are to be granted, what conditions, if any, should be imposed in the public interest and for the protection of investors."

After hearings were held at which applicant appeared by counsel, proposed findings of fact, conclusions of law and briefs were filed by counsel on applicant's behalf and by the Division of Corporate Regulation ("Division"). Applicant also filed a "Memorandum of Rebuttal".

The Episcopal School Foundation College Award Program, Inc. ("CAP") is a Florida non-profit membership corporation organized in April of 1966. Its sole business is the operation of a scholarship plan, offered to residents of Florida, which is authorized and regulated under the Florida Statutes.<sup>2/</sup> The Reverend Hunter Wyatt-Brown, Jr. is President and Executive Director of CAP and has operated it since its inception. Aaron I. Sanson ("Sanson") has been its Secretary since inception. Both are members of the Board of Directors.

The same scholarship plan was originally presented in 1965 by the Episcopal School Foundation (ESF) a non-profit corporation formed for the purpose of aiding the Episcopal Church in general and education in particular. In addition to the scholarship plan, ESF ran three religious schools. Rev. Wyatt-Brown is ESF's Executive Director and Sanson is its Secretary. Its Board of Trustees include

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<sup>2/</sup> Florida Statutes, Section 617.50 et seq.

a Bishop of a diocese of the Episcopal church and the majority of its members are communicants of the church. Having been advised that under Florida law a corporation offering a scholarship plan must have that objective as its sole purpose, ESF's Board of Trustees authorized the creation of CAP to succeed it as operator of the scholarship plan. All original subscribers of CAP's Articles of Incorporation were members of the ESF Board of Trustees.

### The Plan

The plan offers a program under which a person interested in a child's future education may become a member of CAP by paying a membership fee and by opening a savings account in a federally insured savings bank or savings and loan institution.<sup>3/</sup> Upon enrollment the member designates the child or candidate who is to be the beneficiary of the scholarship award. The child must be eight years of age or younger.<sup>4/</sup> The current membership fee is \$175.

The member creates his savings account by either a lump sum deposit or by making monthly, quarterly or annual deposits. CAP has issued deposit schedules indicating the required amount of each such

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<sup>3/</sup> In addition to Florida, scholarship plans have been offered in Pennsylvania by The College Award Foundation, a Delaware corporation ("CAF-Del") formed in November 1966, and in Iowa by The College Award Foundation, an Iowa corporation ("CAF-Iowa") formed in 1967. All agreements by CAF-Del and CAF-Iowa with their members have been assigned to CAP. Since all three plans are identical, all future references to the plan will be applicable to all three.

<sup>4/</sup> This fee has been increased at least twice from \$100 to \$120 and, thereafter, to the present figure.

payment into the member's savings account dependent upon the age of the candidate at the time of enrollment. Each of these savings accounts is calculated, computed at 4% interest, to produce the sum of \$664.79 when the candidate reaches college age regardless of how the deposits are made.

Upon subscribing to membership in the plan, the member assigns the interest from his savings account to a trustee, irrevocably.<sup>5/</sup> Currently, the trustee is the Atlantic National Bank of Jacksonville ("Atlantic").<sup>6/</sup> The interest earned by the member's saving account constitutes the fund from which scholarship payments are intended to be paid. "The monies in this trust fund are kept in cash interest-bearing savings accounts and are designated to the class of the scholarship candidate of the donor [member]."<sup>7/</sup>

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<sup>5/</sup> CAP's Regulations provide "Sponsor [member] shall donate by irrevocably assigning, until maturity date of Candidate's CAP Savings Plan, all right, title and interest in and to all earnings from his CAP Savings Account and direct the savings institution to transfer these earnings immediately on their accrual to the College Award Program Trust Fund (CAP Trust Fund)".

<sup>6/</sup> The State of Florida has approved the trust agreement entered into between CAP and Atlantic covering the funds created by CAP's Florida plan. CAP has also submitted to the State of Florida for its approval agreements pursuant to which Atlantic would act as trustee in respect of the funds created by the CAP-Del and CAF-Iowa plans. The State has not yet responded. The parties have stipulated that the trusts created by CAF-Del and CAF-Iowa may also be considered applicants in this proceeding. Accordingly, future references to the Trust Fund will include the CAF-Del and CAF-Iowa plans.

<sup>7/</sup> Applicant's brief, p. 5.

Pursuant to a cost analysis prepared by CAP, all administrative expenses connected with the plan are to be paid out of the \$175 enrollment fee charged each member. It is contemplated that \$115 will be allocated towards the cost of the sales program and \$60 to the cost of administration. 8/ No deductions of any kind may be made from the monies deposited by each member into the trust fund. The trustee's fees, which CAP computes at \$1.00 per investor per year, 9/ are payable out of the \$60 allocated to administration expenses.

The member always maintains sole control of and all right, title and interest in his savings account. If he completes the payments to that account pursuant to the plan and if his candidate survives, is graduated from high school and successfully completes his freshman collegiate year, the trust funds are to be used to pay the cost of the remaining three years of his college education. 10/

Upon enrollment each candidate is assigned a "maturity date", i.e., the year he is expected to enter college. 11/ Candidates having

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8/ CAP's cost analysis is predicated upon an estimated future enrollment of 5,000 members per year.

9/ The \$1.00 figure appears in CAP's cost analysis. Presumably, it is a simplification of the provision of the trust agreement pursuant to which CAP is to pay to the trustee for its services an annual fee of 1/2 of 1% on the first \$100,000 of principal, 1/3 of 1% on the next \$400,000 of principal and 1/4 of 1% on all above \$500,000, less 25% of the fees so computed.

10/ The plan contemplates that the member's savings account will be used to pay the cost of the candidate's freshman year.

11/ This is also the date on which the assignment to the trustee of interest earned by the member's savings account will terminate.

the same maturity dates are deemed to be in the same class. When a class enters its sophomore year the amount available in the trust for that class is divided into three parts -- one part for each of the remaining college years. One such part is divided by the number of eligible candidates in that class. The resulting sum is then paid directly to each candidate's college to cover the candidate's college expenses for the sophomore year.<sup>12/</sup>

However, in order that a candidate may participate in the benefits of the scholarship award the member must complete the savings account deposits prescribed by the plan and the candidate must successfully meet the academic requirements for advancement to the sophomore year. A candidate's ineligibility to participate may result in a number of ways including his permanent physical inability to continue his education,<sup>13/</sup> failure of the member to make the necessary installment payments into his savings account

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<sup>12/</sup> For the junior year the remaining fund is divided into two parts and one such part is divided by the number of candidates remaining in the class. For the senior year the fund is merely divided by the number of candidates in the class. Determination as to what constitutes "college expenses" is left to the discretion of each candidate's college. If a candidate's expenses exceed the amount of the scholarship award he is expected to make up the difference. If the entire amount of the award is not used by the candidate during any college year, the unused moneys are to be returned to the trustee who will add it to the funds of that candidate's class.

<sup>13/</sup> Arrangements for delayed entrance into college are made for temporary illness or service in the armed forces. Further, in the event of the death of a candidate prior to his "maturity date", the enrollment may be transferred to a younger child.



whether because of financial inability or voluntary termination of the plan, scholastic failure or dropout from high school or college by the candidate at any time for any reason. If scholastic failure or dropout occurs after the sophomore year, the candidate also becomes ineligible. The result of ineligibility is complete forfeiture of all monies paid into the trust by the member. The amount forfeited would, of course, vary with the age of the candidate on enrollment and the length of time the member continued his membership in good standing prior to either his termination of the plan or ineligibility of the candidate.

The record leaves no doubt that the success of the plan depends entirely upon forfeitures in substantial numbers in every class. Obviously, \$664.79 is hardly adequate to cover the cost of three years of college education. Both ESF and CAP recognized this in their sales literature which is replete with representations of anticipations and expectations, albeit no guarantees, of scholarship awards of \$1,500 per year for three years for each candidate. Some of the literature expands that figure to "\$4,500 to \$6,000". The forfeiture aspects of the plan are emphasized by the literature which explains that the success of the plan is made possible through interest obtained from the member's savings account "PLUS the added revenue accruing from student dropouts, PLUS the interest accumulated from certain sponsors who fail to follow through with their savings program \* \* \*." CAP's literature also includes charts

designating their source as "U.S. Dept. of Health, Education and Welfare", which demonstrate that out of 1,000 enrollees only 603 will enter college; of those 603, 312 will not qualify to enter the sophomore year, 90 will not qualify for their junior year and 36 will not qualify for their senior year. 14/

It is also evident from the testimony of George Ling, whose firm of consulting actuaries has been retained by CAF for actuarial research, that the meaningfulness of the program depends on dropouts or forfeitures. 15/ This report to CAF points out the need for forfeitures and the various means which might be employed to reduce "anti-selection" 16/, i.e., "Enrolling members at only the very early ages"; "High proportion of sales to \* \* \* the low income group; and "Flexible conditions for payment of enrollment fee". Moreover, the experience of the plan during the short time of its existence 17/

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14/ Data furnished by CAF to the State of Florida was interpreted by the State's actuary to have even more drastic forfeiture results as follows:

"Starters	1,000
Finish High School	625
College Sophomores	140
College Juniors	119
College Seniors	86"

15/ "If you enroll only those who you know will go to college and they are from wealthy families, the program is going to have no meaning."

16/ Ling's report defines anti-selection:

"'Anti-Selection' applicable to any financial situation may be defined as the obligation to individuals or groups, for a consideration, which include a high proportion of those who actually expect to benefit either to a greater degree or else sooner than is the average case.

For example, if an insurance company sells policies only to heart patients at standard (average) premium rates, sales records will be broken but so will the company before very long."

17/ Sales of the plan were suspended in September 1967 apparently awaiting the determination of this proceeding.

should not be disregarded in considering the degree of forfeitures. In about one and one-half years 3,777 memberships were sold in Florida, of which about 3,300 were still in effect at the time of the hearing. 173 memberships were sold in Pennsylvania in less than one year, of which 141 are still in effect and 33 were sold in Iowa in less than one year of which 25 are still in effect.

Applicant's Status under Section 3 of Act

Section 2(a)(8) of the Act defines a "company" to include "a trust, a fund." Obviously, the interest from members' savings accounts assigned to the trustee and funnelled into the CAP Trust Fund ("Trust Fund") constitutes a "fund". Indeed, the name of the applicant in this proceeding, The Trust Fund Sponsored By the Episcopal School Foundation College Award Program, Inc. is itself indicative of recognition by applicant that the fund is a company within the purview of the Act and within the holding of Prudential Insurance Co. v. S.E.C. 326 326 F. 2d 383, 387 (C.A. 3, 1964) that a fund, otherwise having no recognized identity as a legal entity, may nevertheless constitute a "company" as that term is defined in the Act.

Section 3(a)

The relevant provisions of Section 3(a) of the Act define an investment company as any issuer 18/ which

"(1) is or holds itself out as being primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities;"

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18/ Section 2(a)(21) of the Act defines "issuer" as "every person who issues or proposes to issue any security, or has outstanding any security which it has issued."

"(3) is engaged or proposes to engage in the business of investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 40 per centum of the value of such issuer's total assets (exclusive of government securities and cash items) on an unconsolidated basis." 19/

Applicant urges that the Trust Fund is not an investment company under Section 3(a), but offers no rationale other than the statements that "CAP and its Fund do not reinvest or trade in securities" and "they are not engaged in the business of investing, reinvesting, owning, holding, or trading in securities."

However, CAP's sales literature refers to the trust and its earnings. CAP's Regulations created Trust Fund and all contracts by CAP with its members refer to the Regulations. Its trust agreements with Atlantic have been furnished to the State of Florida. These agreements provide that the trustee shall manage, invest and reinvest the assets of Trust Fund. 20/ Atlantic, qua trustee, has no business other than the management of Trust Fund.

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19/ Section 3(a)(2) which relates to issuers engaged "in the business of issuing face-amount certificates of the installment type" is not applicable. Section 2(a)(15) defines a face-amount certificate as an obligation to pay a stated or determinable sum. "Face-amount certificates are contracts under which the company is bound to pay a fixed sum at maturity \* \* \*." Report of the Securities and Exchange Commission on the Public Policy Implications of Investment Company Growth, December 2, 1966, p. 37. CAP's representation of a \$4500 non-guaranteed scholarship award hardly falls within the category of a "fixed sum."

20/ The Regulations provide that "[CAP] shall contract with the Trustee that all such interest so assigned and deposited shall remain in said CAP Trust Fund and be managed, invested and reinvested until such time as the Trustee is authorized by [CAP] to make payments of scholarship awards." The trust agreements state that the trustee shall " \* \* \* manage, invest and reinvest the funds and all income and interest earned therefrom \* \* \* [and] payout for such scholarship purposes such amounts to such recipients and at such times as [CAP] shall designate \* \* \*"

Moreover, the trust funds are presently invested in savings accounts.<sup>21/</sup> Thus, Trust Fund is and holds itself out to the public, its members and the State of Florida as being engaged primarily in the business of investing and reinvesting.

The only question remaining under Section 3(a)(1)<sup>22/</sup> is whether the assets of Trust Fund constitute securities. Even assuming that the trust funds are not to be utilized for any purpose other than their deposit in interest bearing savings accounts, they, nevertheless, are securities under Section 2(a)(35) for the reasons (1) that the arrangement resulting in the creation of Trust Fund is an "investment contract" and (2) that the savings accounts into which the funds are deposited by the trustee are "evidence[s]"<sup>23/</sup> of indebtedness."

In determining whether Trust Fund is an investment company

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<sup>21/</sup> At one time the trust funds were invested in U. S. Government bonds. It is CAP's present intention that the trust funds be invested only in savings accounts. However, should it be determined that Trust Fund is excepted from the provisions of the Act, "we would like to be able to purchase savings certificates and, if possible, government bonds, or whatever we can that would be qualified to increase the interest earnings." (Testimony of Rev. Wyatt-Brown).

<sup>22/</sup> Under Section 3(a), "'investment company' means any issuer \* \* \*." Trust Fund is the issuer. Although CAP wrote the contracts which gave rise to the obligation to set up the fund and to the promises of scholarship awards, " \* \* \* the investment fund, the 'company' to which the investment interests relate, is the 'issuer' of those interests." The Prudential Insurance Company of America, 41 S.E.C. 335, 345 (1963); See also Prudential Ins. Co. v. S.E.C. supra, p. 388.

<sup>23/</sup> Section 2(a)(35) of the Act defines "security" to include "any \* \* \* evidence of indebtedness, \* \* \* investment contract, \* \* \*"

under the Act "we start with the premise that securities legislation must be broadly construed in order to insure the investing public a full measure of protection".<sup>24/</sup> As set forth above, the scholarship plan provides for management by the trustee of the interest proceeds of each member's savings account. CAF represents that such proceeds, calculated at \$664.79, will result in a scholarship fund for each candidate of at least \$4,500 representing a substantial profit to the member. It becomes readily apparent therefore, that the plan conforms to the Supreme Court's definition of an "investment contract" which is a security as defined in Section 2(a)(35).

"In other words, an investment contract for purposes of the Securities Act <sup>25/</sup> means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promotor or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise." S.E.C. v. Howey Co. <sup>26/</sup>

Moreover, as stated in Justice Brennan's concurring opinion in S.E.C. v. Variable Annuity Co., the controls of the Act "are of particular relevance to situations where the investor is committing his funds to the hands of others on an equity basis, with the view that the funds will be invested in securities and his fortunes will depend on the success of the investment."<sup>27/</sup> In Prudential v. S.E.C.

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<sup>24/</sup> Prudential Insurance Company v. S.E.C., supra, p. 386.

<sup>25/</sup> The definitions of "security" in the Securities Act of 1933 ("Securities Act") and in the Investment Company Act of 1940 are identical.

<sup>26/</sup> 328 U.S. 293, 299 (1945). See also S.E.C. v. Joiner Corp. 320 U.S. 344 (1943).

<sup>27/</sup> 359 U.S. 65, 79 (1959).

supra, the court adopted the same position <sup>28/</sup> in respect of the variable annuity contracts under which Prudential established a fund for investment in securities for the benefit and at the risk of purchasers of the contracts. And in S.E.C. v. Variable Annuity Co., supra, the court declared that the term "security" as defined in the Securities Act "is broad enough to include any 'annuity' contract." <sup>29/</sup> As relevant here, the relationship between CAF, its members and Trust Fund offers little meaningful difference from that of the insurance company, the variable annuity and its investors.

We now turn to the question whether the savings accounts maintained by Trust Fund constitute "evidence[s] of indebtedness." The crux of this problem is the nature of the obligation created by the savings accounts. Ordinarily, the relationship between a savings bank and its depositor is regarded simply as that of debtor and creditor absent an agreement to the contrary. <sup>30/</sup> Here, not only has no agreement to the contrary been shown, but under the law of Florida where the saving accounts are maintained, "depositors of [savings banks] in this state are creditors of the bank and have the same rights as depositors in other banks." <sup>31/</sup> The law is clear, therefore, that the savings accounts maintained by the trustee

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<sup>28/</sup> At pp. 386, 387.

<sup>29/</sup> At pp. 67, 68.

<sup>30/</sup> 9 C.J.S. Banks and Banking, ¶ 992.

<sup>31/</sup> Robinson v. Aird, 43 Fla. 30, 29 So. 633 (1901). See also Tcherepnin v. Knight, 389 U.S. 332, 334 (1967) where the implication is plain that even the more complex withdrawable capital share of a savings and loan institution would have constituted an evidence of indebtedness absent a state statute providing specifically that the holder thereof does not become a creditor.

represent evidences of indebtedness and securities under section 2(a)(35).

Appellant's reply brief contends that the member makes a gift of the interest from his savings account to the trust fund which he may cut off at any time; that the member has no right in these interest payments after they reach the trust and concludes, therefore, that "there are no investments made but merely gifts." On the other hand, applicant's brief admits that the candidate will receive the benefits of the member's "gift" if he qualifies. Obviously, applicant cannot have it both ways. It is the very essence of a gift that the donor retains no rights in a donation either for himself or for others. That here, the CAP member retains a right which he may forfeit at some future time negates the fundamental concept of a gift. Applicant's further argument that the member's contract with CAP "has nothing to do with any agreement with Trust itself" is untenable since CAP's sales literature refers to the trust and the contract or application through reference to CAP's Regulations and By-Laws 33/ provides for the maintenance of the trust

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32/"A savings bank pass book, like a bill of exchange or note, is for many purposes a chattel, and is not merely an evidence of debt but is representative of it. It imparts a liability of the bank to the depositor for the amount of money entered therein as deposited, an agreement to repay at such time and in such manner as he shall direct. . . ." 9 C.J.S. Banks and Banking ¶ 986.

33/ One form of contract executed by an applicant on November 8, 1966 provides that the application is "subject to the By-Laws of [CAP] which I have examined." The By-Laws include reference to the Regulations. In a different form, the application is "subject to the regulations pertaining to its College Award Program (which I have examined)." The preamble to the Regulations refers to an agreement between CAP and the member whereby the member "binds himself and his candidate to abide by these CAP Regulations. \* \* \*



from which the ultimate benefits of the contract are to be distributed.

Undoubtedly, under certain circumstances, a savings account may be deemed "cash" rather than investment securities in reaching a determination under Section 3(a)(3) whether the value of an issuer's investment securities exceeds 40% of its total assets. However, that treatment should properly be accorded only where the nature of the issuer's business and assets raise a legitimate question, but not where, as here, the maintenance of savings accounts is the issuer's principal business and sole means of fulfilling its obligations to its investors. In addition, since the savings accounts may not be utilized until the maturity dates of the various classes, their total lack of liquidity negates consideration of these accounts as "cash" within the meaning of Section 3(a)(3).

Under all the circumstances set forth above, it is concluded that Trust Fund is an investment company under Section 3(a) of the <sup>34/</sup> Act.

Section 3(c)(3)

This section excepts "any bank or insurance company" from investment company status. It also excepts

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<sup>34/</sup> On September 25, 1967 applicant filed "Form N-8A, Notification of Registration Filed Pursuant to Section 8(a) of the Investment Company Act of 1940."

"any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of moneys contributed thereto by the bank in its capacity as a trustee \* \* \*." 35/

Appellant asserts that it falls within the exception since the trust funds are held in trust by and administered by a national bank. Prudential v. S.E.C., supra, held that Prudential is separable from the variable annuity fund it operated and its exception from the Act as an insurance company did not extend or carry over to the fund. Atlantic is performing the functions of a trustee under a specific contract setting forth its duties and obligations. It, also, is separable from Trust Fund and its status as a bank is no more relevant in the instant matter than was Prudential's status as an insurance company in that case.

Nor is the common trust fund exception applicable to Trust Fund. In considering the same problem in Prudential v. S.E.C., supra, the court held that the Congress did not intend to include in the exception funds used for general public investment. It said:

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35/ The "common trust fund" excepted by Section 3(c)(3) is defined in H. Doc. 476, 76th Cong. (1939) (Report of the Commission on Common Trust Funds) as a number of small personal trusts or estates combined by a trustee bank or trust company into one larger fund for common administration and management. Regulation F of the Federal Reserve Board refers to the common trust fund as "investment funds held for true fiduciary purposes, \* \* \*." See, also, Prudential Insurance Co. of America, supra, p. 346, footnotes 24 and 25.

"\* \* \* Obviously, if as Prudential argues, the exemption of banks and insurance companies had been intended to include an exemption of funds set up by such companies, there would have been no need to provide for the additional specific exemption of funds set up by banks. Congress thus viewed such funds even though usually maintained as departments of the bank, as separate from the banking business. It rested this exemption on the special considerations that the funds were used for bona fide fiduciary purposes rather than as a medium for general public investment and had only a limited impact in the investment fund picture." 36/

CAP and its sister scholastic plans certainly were not set up or used for "bona fide fiduciary purposes." To the contrary they had been offered to the general public of Florida, Pennsylvania and Iowa and cannot, therefore, qualify for exception as common trust funds. It follows that the provisions of Section 3(c)(3) are not available to Trust Fund.

Section 3(c)(8)

Section 3(c)(8) excepts from the provisions of the Act:

"Any company 90 per centum or more of the value of whose investment securities are represented by securities of a single issuer included within a class of persons enumerated in paragraph (5), (6) or (7)."

Paragraphs (5) and (6) are obviously inapplicable. Paragraph (7), however, excepts any company primarily engaged in one of the businesses described in paragraph (3). Paragraph (3) includes "any bank." In view of applicant's intention to maintain all its funds in savings accounts which have been found above to constitute securities under Section 2(a)(35), question is raised whether the value

of applicant's securities are "represented by securities of a single issuer."<sup>37/</sup>

To translate the language of Section 3(c)(8) to the specifics of the matter before us, the "company" is Trust Fund. The "single issuer" is Atlantic, as a bank and not as trustee. The "Securities of a single issuer" as contemplated by Section 3(c)(8), would represent investment on an equity basis in the enterprise which is Atlantic, in all its underlying assets and in the results of Atlantic's operations as a bank. Trust Fund's savings accounts maintained in Atlantic and the interest earned by these savings accounts constitute nothing more than a debt owing by Atlantic to Trust Fund. This debt is a security of Trust Fund. It is not to be confused with a security of Atlantic.

Applicant, therefore, does not fall within the exclusionary provisions of Section 3(c)(8).

Section 3(c)(12).

Section 3(c)(12) excludes from the Act:

"Any company organized and operated exclusively for religious, educational, benevolent, fraternal, charitable, or reformatory purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual."

Applicant urges that it is an affiliate of the Episcopal Church. That the record is replete with evidence to the contrary is of little consequence inasmuch as Trust Fund would appear to be operated for educational purposes.

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<sup>37/</sup> It is assumed Atlantic maintains the savings account in its own bank. If they are on deposit in another bank the issue remains unaffected.

But Section 3(c)(12) contains two conditions i.e., that education is the exclusive purpose of the organization and that none of its earnings inure to the benefit of its shareholders. Statutes enacted prior to this section and which contain identical conditions have been the subject of both judicial and administrative determinations discussed below.

In Better Business Bureau of Washington v. U.S., 326 U.S. 279 (1956) the court indicated that a single non-educational purpose of the organization seeking exemption from social security taxes, if substantial in nature, would destroy the exemption provided by the Social Security Act. S.E.C. v. American Foundation for Advanced Education of Arkansas, 222 F. Supp. 828 (U.S.D.C., W.D. La., 1963) presented a request by an organization selling a scholarship plan for exemption from registration under Section 3(a)(4) of the Securities Act. The court, citing Better Business Bureau v. U.S., supra, found the substantial non-educational purpose which negated exclusivity of the educational purpose in the fact that the profits of the foundation were returned to its members in the form of the payment of the college expenses of the members' children and that the element of profit was the principal motivation for the members' participation, which "makes the application of the registration requirements of the Securities Act emphatically necessary here."

The Internal Revenue Service considered an application for exemption from Federal income tax under Section 501(c)(3) of the Internal Revenue Code by an organization offering a scholarship plan

similar in its pertinent aspects to that sold by CAP. The application was rejected on the ground that the agreements pursuant to which the organization paid scholarships to specifically named individuals designated by the subscriber served private rather than the public charitable and educational interests contemplated by the Code.<sup>38/</sup>

The Internal Revenue Code fathered the Social Security Act which was the subject matter of Better Business Bureau v. U.S., supra.<sup>39/</sup> Although the legislative history of the Investment Company Act makes little reference to Section 3(c)(12), the identity of language would indicate that that section also found its origin in the Code. It needs no extended discussion to demonstrate that CAP's plan, like those considered in S.E.C. v. American Foundation, supra and the Internal Revenue Ruling set forth above, lacks the exclusivity of educational purpose required by the Act since its ultimate end is the benefit of its private members. Section 3(c)(12) of the Act is, therefore, not available to applicant.

The scholarship plan has its genesis in the vastly increased cost of education at the college level in recent years and the inability of many parents to meet these financial burdens. Undoubtedly, solutions to this problem are urgently needed. However, where one

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<sup>38/</sup> Martens, Law of Federal Income Taxation, Revenue Ruling 67-367.

<sup>39/</sup> At p. 284.

possible solution involves the creation of an investment company as defined in the Act, exemptions from the Act and other relief sought by the investment company must be viewed in the context of the congressional declaration of policy set forth in Section 1 of the Act which expresses deep concern for the national public interest and the protection of investors. In enforcing this policy, the courts have consistently emphasized the need to effectuate the remedial purposes of securities legislation and, in that context, to construe it broadly in accordance with the "familiar canon of statutory construction,"<sup>40/</sup> to construe it "not technically and restrictively, but flexibly to effectuate its remedial purposes"<sup>41/</sup> in order not to thwart the statutory policy.<sup>42/</sup>

Consideration of applicant's requests for exemptions from the requirements of various provisions of the Act would be aided by a review of certain aspects of applicant's history which have not been mentioned heretofore. In September 1965 ESF formed Nationwide Service Corporation ("N.S.C.") as the sales organization through which its scholarship plan would be offered to the public. Rev. Wyatt-Brown was its President and a director but was relatively inactive. Professional management personnel were employed to operate N.S.C. and

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<sup>40/</sup> Tcherepnin v. Knight, supra; S.E.C. v. Ralston Purina Co., 346 U.S. 119 (1953).

<sup>41/</sup> S.E.C. v. Capital Gains Bureau, 375 U.S. 180, 195 (1963); Prudential Insurance Co. v. S.E.C., supra; Cf. S.E.C. v. Joiner Corp., supra.

<sup>42/</sup> S.E.C. v. Howey Co., supra.

originally the plan was sold through N.S.C.'s salesmen. Later the plan was sold through area agents and other organizations which were supposedly supervised by N.S.C. Apparently, however, both the N.S.C. management and the personnel engaged in selling the plan lacked suitable training or had other shortcomings. Some of the advertisements placed for the hiring of salesmen were "very bad" and it was evident that "mistakes" had been made by N.S.C. in the sale and distribution of the plan.<sup>43/</sup> For these reasons Rev. Wyatt-Brown, upon the suggestion of his bishop, resigned his presidency of St. Anne's College and devoted his full time to N.S.C. to "bring some order into the sale of enrollments."<sup>44/</sup>

Under the original agreement N.S.C. undertook, among other things, to maintain enrollment and membership records and keep records of candidates' accounts. CAP's inter-office memoranda disclose that N.S.C. failed to satisfactorily furnish this service, for which it had been paid, leaving CAP in an embarrassing position as to year end 1966 figures which it required for distribution to its membership and others. CAP also had additional problems. But, with the exception of the representation of a scholarship award of \$4,500 for each candidate, the errors in the past history of the scholarship plan as administered by ESF and CAP are not now of great moment since steps have been taken which appear on their face to be adequate to remedy those mistakes.

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<sup>43/</sup> Literature and advertising material were placed with various Florida newspapers, distributed through the mails and made available at churches and banks.

<sup>44/</sup> Rev. Wyatt-Brown is no longer associated with N.S.C. in any capacity.



Rev. Wyatt-Brown and Mr. Sanson who administer the plan and Bishop James L. Duncan, a member of the board of directors, are people of high integrity, sincerely dedicated in their efforts to make higher education more readily available. They are now making a new and what they consider to be a genuine attempt to correct past faults in the sale and administration of the plan. To that end they have entered into agreements with an accounting firm in order to overcome their earlier bookkeeping shortcomings, with an actuarial firm to put to appropriate use the experience of the plan as the years progress and have stated that they will not enter into a sales agreement with any organization which is not a member of the National Association of Securities Dealers, Inc. ("NASD").

CAP's ability to maintain the accounting, actuarial and other necessary services is predicated upon an estimated 5,000 enrollees per year, each to pay the \$175 enrollment fee. As indicated above, CAP's projections envisage that \$60 of this fee will be retained by it for payment of costs of administration of the plan and the remaining \$115 will be paid to a sales organization to cover expenses of sale of the plan. Applicant states that N.S.C., now under new management, will be given preferred consideration if it becomes a member of the NASD. CAP also offers not to re-engage in business until such time as proper new actuarial studies are made to update its current figures. To the extent, however, that an enrollment of 5,000 new members for each year is basic to the success of CAP's current undertakings for administrative services and to the extent that such

an enrollment is essential to achievement, through increased numbers of forfeitures, of its representations of \$4,500 scholarships, CAI offers little reason other than hope for its anticipation of enrollments in such numbers. Certainly, its past experience in Florida, Pennsylvania and Iowa does not warrant such expectations.

Section 6(c) of the Act authorizes the Commission to exempt persons from the provisions of the Act if and to the extent that such exemptions are necessary or appropriate in the public interest and consistent with the protection of investors and the policies of the Act.

Obviously, the representation of a \$4,500 scholarship award is the major inducement to membership in the plan.<sup>45/</sup> It is readily apparent, however, that this representation is not predicated upon the reasonable basis in fact required under the securities laws.<sup>46/</sup> Nor does the fact that the representation is not couched in terms of guarantee offer exoneration.<sup>47/</sup>

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<sup>45/</sup> The plan's sales literature shows \$1,700 and \$1,400 as the current one year costs for southern and midwest state universities respectively, with the cost at private schools far exceeding these figures. Its literature projects the cost of 4 years of college by 1982 at \$18,800.

<sup>46/</sup> Alexander Reid & Co., Inc., 40 S.E.C. 986 (1962); Billings Associates, Inc., Securities Exchange Act Release No. 8217 (Dec. 18, 1967); Richard Bruce & Co., Inc., Securities Exchange Act Release No. 8303 (April 30, 1968); Norman Pollisky, Securities Exchange Act Release No. 8381 (Aug. 13, 1968).

<sup>47/</sup> James DeMammos, Securities Exchange Act Release No. 8090 (June 2, 1967).

The computations which resulted in the \$4,500 figure are set forth in a submission by CAP to the State of Florida. These computations purport to present an admixture of statistics and actuarial assumptions. They use a base of 1,000 and project the rate of survival of members and candidates in the plan, from year to year, based upon statistics as to parents who die, children who die, parents who quit the plan, grammar and high school dropouts, college enrollees and college dropouts. Insurance mortality tables are used for the death categories. The school dropout figures rest on statistics of the Department of Health, Education and Welfare ("HEW"). The projections for parents who quit the plan are derived from information indicating a 50% dropout rate for long-term annuity contracts. In utilizing this 50% or 500 figure, CAP's computations arbitrarily divide 500 by 16 years arriving at 31.25 parents who will quit the plan each year. These computations were prepared in 1963 and submitted to the State about 1966.

In determining the reasonableness of the \$4,500 representation, it is significant that the HEW statistics upon which CAP's projections were based covered the periods 1942-1950 through 1954-1962. These statistics showed that out of 1,200,000 high school graduates in 1950 about 32% entered college. However, they also demonstrated that out of 1,000 in the 1954-1962 period, 636 graduated from high school and 336 or over 52% entered college. Nevertheless, in its presentation to the State, CAP selected the 32% figure as the base for its projections obviously affording a potentially greater monetary

realization for the scholarship award than use of the available statistics for the later period would have shown. It is also noted that statistical material received by Rev. Wyatt-Brown after CAP's filing with the State indicates that for the year 1965, 55.3% of high school graduates entered college, a still higher figure. Whatever may be CAP's justification for failure to use this material, it nevertheless is evidence of a continuing trend of a higher proportion of college entrants.

Further the national statistics utilized by CAP do not necessarily have any relationship or applicability to the persons who become members of CAP. The national statistics represent a cross-section of the general population without regard to specific desires or intentions of the people composing that cross-section to give their children a higher education. Where the incentive to do so is sufficiently alive to cause an individual to join CAP, it is reasonable to assume that the likelihood of his achieving that purpose is far greater than that shown by the national statistics. It follows that the computation of a \$4,500 scholarship award based upon national statistics may not reasonably be expected to prove realistic. In addition, no justification appears for spreading the projected 50% of parents who would quit the plan equally throughout the 16 years of the plan. Ling testified he "would suspect" that such quitting would occur in the early years of the plan. Logic would support

his suspicion and on this basis the amount available for the candidates as computed by CAP would be further reduced.

The foregoing supports the conclusion that CAP's representation to the public that \$4,500 would be available to the eligible candidate was made without reasonable basis in fact and therefore, contrary to the requirements of the securities laws.

No matter how well-intentioned the principals of CAP may have been, it is fundamental that the securities laws must be administered for the benefit and protection of investors. To further that end it has been held, repeatedly, that because a security is "intricate merchandise," the proscription of the anti-fraud provisions of the securities laws extend beyond common-law fraud;<sup>48/</sup> that in the public sales of securities the seller impliedly

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<sup>48/</sup> Alexander Reid, 40 S.E.C. 986, 989.

represents that his statements "are responsibly made on the basis of actual knowledge and careful consideration"; and that it is not a sufficient excuse that a seller of securities personally believes the representation made without adequate basis.<sup>49/</sup> Moreover, since the success of the plan depends upon forfeitures, its very nature would appear to necessitate recommendation of the security to persons for whom it would be unsuitable<sup>50/</sup> and, consequently, inconsistent with the well-established "basic obligation \* \* \* to deal fairly with the investing public."<sup>51/</sup>

In view of the foregoing, the circumstances surrounding the representation of a \$4,500 scholarship award raise serious question whether the granting of any exemptions sought by applicant other than those of an entirely innocuous nature, as they relate to the interests of investors, would be in the national public interest.

As relevant here, Section 14(a) of the Act prohibits an investment company from making a public offering of securities unless it has a net worth of at least \$100,000.

A letter from CAP to an official of the State of Florida dated April 22, 1968, states that the corpus of the trust (presumably

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<sup>49/</sup> Ibid, pp. 990, 991

<sup>50/</sup> Gerald M. Greenberg, 40 S.E.C. 133, 137 (1960); Cf. Rule 15b10-3 promulgated under the Securities Exchange Act of 1934.

<sup>51/</sup> Richard Bruce & Co., Inc., supra.

all three plans) amounts to over \$52,200 including contributions for the first quarter of 1968. The letter shows the following breakdown of trust funds as of December 31, 1967: Pennsylvania <sup>52/</sup> \$700.60; Iowa \$5.55 and Florida \$32,681.24.

The Reports of the Senate and the House of Representatives both commented adversely on the fact that at that time little capital was needed to organize investment companies. Section 14(a) was enacted "To put a brake on the irresponsible formation of investment companies \* \* \*." <sup>53/</sup> Thus, the basic purposes of Section 14(a) are something more than "simply to indicate a public acceptance of the responsibility of the promoters of investment companies," as applicant understands it. The intent of the section is, rather, to assure at least some element of financial responsibility of the promoters of an investment company and to afford investors the protection envisaged by the section despite themselves and without regard to the public acceptance to which applicant refers.

Although Trust Fund is the investment company to which Section 14(a) is directed, CAP's financial condition is also relevant to the extent that it reflects the plan's prospects for the future. CAP's liquid assets are minimal. Its balance sheet as of March 31,

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<sup>52/</sup> The CAP-Del plan was sold only in Pennsylvania.

<sup>53/</sup> Senate Report No. 1775, 76th Cong., 3rd Sess., June 6, 1960, p. 6 (Senate Report); House of Representatives Report No. 2639, 76th Cong., 3rd Sess., June 18, 1950, p. 8 (House Report).

<sup>54/</sup> Senate Report p. 13.

1968 shows an overall deficit of \$13,096.94 and includes assets of \$15,858.92 consisting of furniture and fixtures and accounts receivable of \$8,260.04, both of doubtful value. Under the Florida Statutes <sup>55/</sup> CAP is required to deposit with the Insurance Commissioner securities of the value of \$50,000 to assure performance of its obligations to its members; \$25,000 in such securities on or before April 1, 1968 and a similar amount on or before April 1, 1969. CAP has no securities of the nature contemplated by the State's deposit requirements. It has requested the State to waive the first deposit in view of its inoperative status. As of the close of the record the State had not responded. <sup>56/</sup>

In view of the limited assets of Trust Fund for the Florida plan, the minute assets of the Iowa and Pennsylvania plans and the precarious financial condition of CAP, the granting of an exemption from Section 14(a) would nullify the protections of the Act and adversely affect the interests of investors. Accordingly, the request for exemption from the provisions of Section 14(a) of the Act is denied.

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<sup>55/</sup> Section 617.561.

<sup>56/</sup> Since the statute requires the deposit to be made by the corporation rather than Trust Fund a deposit of \$50,000, rather than that of \$150,000 asserted by the Division, would suffice even if the CAP-Del and CAF-Iowa trust agreements should be approved.



Section 16(a)

This section provides that all directors of a registered investment company be elected by shareholders of the company at an annual meeting or a special meeting called for that purpose. Applicant seeks exemption from Section 16(a) to the extent that the Florida law requires that four organizations, i.e., the Florida Congress of Parents and Teachers, Florida Education Association, Florida Bankers Association and Florida Savings and Loan League each have the right to appoint a representative on CAP's board of directors.

Trust Fund is a registered management company.<sup>57/</sup> It is unincorporated and has no board of directors. Under these circumstances, Section 10(h) of the Act requires, among other things, that the depositor shall have a board of directors no more than 60 per centum of the members of which are officers or employees of the depositor. CAP's charter provides for not less than 7 or more than 18 directors. So long as the duly elected members of CAP's board constitute a majority, CAP's "corporate democracy," to which the Division refers, will be preserved. CAP should insure, by amendment to its by-laws, a continuing majority of elected members in the event the above named organizations decide to exercise their right to appoint members to CAP's board. In other respects

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<sup>57/</sup> Section 4 of the Act classifies investment companies as either a face-amount certificate company, a unit investment trust or a management company. Trust Fund is not a face-amount certificate company. (See fn. 18). Trust Fund is not a unit investment trust which, by definition in Section 4(2) of the Act, issues only redeemable securities. The plan's forfeiture provisions are patently inconsistent with the concept of a redeemable security. Under Section 4(3), if trust company is neither of the others, it is a "management company."

CAP's board should observe the provisions of Section 10(h), where applicable. Moreover, applicant has undertaken not to deviate from the investment policies described in its application <sup>58/</sup> without an order of the Commission permitting such deviation as well as the majority vote of its membership as provided by Section 13 of the Act.

The conflict anticipated by the Division if the Bankers Association and the Florida Savings and Loan League should appoint members to the board would be de minimus in view of Trust Fund's investment policies. Further, if the majority vote of the membership is obtained for a change in investment policy pursuant to Section 13 of the Act, an order of the Commission approving such change should not be required. Exemption from Section 16(a) of the Act on the conditions indicated above including the applicant's undertaking would not adversely affect the interest of investors. The exemption is, therefore, granted.

Section 27(c)(1)

This section declares it to be unlawful for any registered investment company issuing periodic payment plan certificates,

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58/ The application states:

"It is intended that Applicant's assets will continue to be invested in United States Government Securities, including securities issued by agencies of the United States and/or fully guaranteed or insured by such agencies and in Certificates of Deposit of Federally insured banks \* \* \*;" and, if its pending request of the Internal Revenue Service for exemption from Federal income taxation is denied, Applicant reserves the right to invest in tax-exempt municipal bonds.

or for any depositor for such company to sell such certificates<sup>59/</sup> unless they are redeemable securities. Applicant urges that the effect of the literal application of Section 27(c)(1) would be to destroy the entire contractual arrangement and seeks an exemption from the provisions of that section.

Since, as heretofore demonstrated, it is inherent in the plan that its success depends upon forfeitures, its securities are not redeemable. Such forfeitures, occurring late in the life of a member's plan when large amounts have been invested, would enhance the possibilities of success of the plan. Indeed, it is doubtful whether the plan would have even the barest chance of success if all or most forfeitures took place when the members' losses would be minimal. It is also noteworthy that the amount of a member's overall loss through forfeiture would include not only the interest from his savings account but, also, his \$175 enrollment fee.

The legislative history of the Act reflects the deep concern of the Congress with the matter of forfeitures. In testimony before the Senate<sup>60/</sup> at least two witnesses condemned the forfeitures resulting from investments in face amount installment certificates.

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<sup>59/</sup> It is immaterial whether shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets of the enterprise. S.E.C. v. Howey Co., supra, p. 299.

<sup>60/</sup> Hearings on S. 3580 Before a Subcommittee of Senate Committee on Banking and Currency, 76th Cong., 3rd Sess. ("Senate Hearings") p. 300.

The Reports of both the Senate and the House <sup>61/</sup> took cognizance of the practices which resulted in forfeitures and substantial losses, pointing to companies which sold to investors in low income brackets who invariably had great difficulty meeting their installment payments and to the high lapse experience of investors. In enacting Section 27(c)(1) the Congress made appropriate provision to relieve this situation by prohibiting forfeitures, admonishing that "Periodic payment plan certificates must be redeemable securities." <sup>62/</sup>

To grant applicant's request for exemption from the provisions of Section 27(c)(1) would serve only to perpetuate the incidence of forfeitures which the Congress decried. It is not enough to say, in respect of forfeitures, that the investor is aware of the risk he takes. To whatever extent and under whatever conditions full disclosure may be the sine qua non of the federal securities laws, here the Congress specifically excluded forfeitures from any periodic payment plan as adverse to the national public interest and the interest of investors. Applicant's assertion that the members' savings accounts are always available to and redeemable by the members carries little persuasion since it was never intended that these savings accounts would be at risk and they do not constitute assets of Trust Fund.

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<sup>61/</sup> Senate Report p. 10. House Report p. 8.

<sup>62/</sup> Senate Report p. 19.

In the light of the foregoing and the manifest adverse effect of forfeitures on the interests of investors, exemption from the provisions of Section 27(c)(1) is denied.

Section 26(a)(2)(A) and 26(a)(2)(B)

The pertinent provisions of this section prohibits the sale of securities issued by a registered unit investment trust unless the trustee, if not otherwise remunerated, may charge against or collect from the income or corpus of the trust fees for its services and remuneration for its expenses theretofore performed or incurred. Section 27(c)(2) requires any registered investment company issuing periodic payment plan certificates to deposit the proceeds of such payments with a trustee under an indenture or agreement containing, in substance, the provisions required by Section 26(a)(2).<sup>63/</sup>

Under the Florida statutes,<sup>64/</sup> the trust funds shall "be used exclusively and solely for scholarships \* \* \*". CAP's by-laws so limit the use of the trust funds and the trust agreements exempt the trust funds from use for payment of the trustee's fees and charges, such payment being assumed by CAP out of the administrative fees paid by the members.

Section 26 was designed to remedy the situation in which a sponsor abandons the enterprise and no provision is made for remuneration of the trustee, thus creating an "orphan trust".<sup>65/</sup> But, CAP

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<sup>63/</sup> The application for exemption concedes that Section 27(c)(2) makes Section 26 applicable to applicants trust agreement.

<sup>64/</sup> Section 617.56.

<sup>65/</sup> Senate Hearings, p. 300; Senate Report, p. 19; House Report, p. 22.

and the Trust Fund are supervised by the State under a statute specifically designed to cover enterprises engaged in the sale of educational plans. The statute includes remedies which adequately protect against the possibility of an orphan trust.<sup>66/</sup> Under these circumstances the congressional intent is preserved and the interest of the investor protected by the Florida law. A requirement for a change in the trust agreement which would conflict with that law appears unnecessary. Accordingly, the exemption is granted.

Section 30(d)

This section requires the transmission of semi-annual financial reports by Trust Fund to the members of the plan.

Section 30(a) requires the filing of annual reports with the Commission and Florida law provides for the filing of annual reports of financial condition with the Insurance Commissioner. Applicant says this is enough; that the filing of a semi-annual report would add unnecessary expense and contribute no meaningful information to the members. But applicant overlooks the poor financial condition of CAP and the various problems raised for it by this proceeding. Until such time as the plan and Trust Fund become stabilized, the membership should be furnished financial information as often as is feasible in order that they may be in a position to reach an independent judgment as to the plan's

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<sup>66/</sup> The Statute requires (1) the \$50,000 deposit referred to above; (2) deposit of additional sums if the \$50,000 deposit is deemed insufficient (Section 617.62); the filing of annual financial statements (Section 617.58); and institution of liquidation proceedings by the Commissioner of Insurance when the corporation is insolvent or the further transaction of business is hazardous to the public, the members or the trustees (Section 617.60).

prospects for success. The request for exemption is denied.

Section 18(i)

This section, as relevant here, requires that every share of stock issued by a registered closed-end company shall have equal voting rights. Applicant requests that the Commission issue an order permitting voting rights as set forth in CAP's by-laws which provide that each member have one vote for each candidate he sponsors. Division opposes the request asserting that the by-laws do not permit members to vote in relation to the amounts they have invested.

A perusal of the installment deposit schedules discloses that the amount invested by each member utilizing the installment plan would, of necessity, change frequently. Furthermore, these changes would vary depending upon the type of plan the member followed -- monthly, quarterly or annual. Thus, the number of votes of each member would be subject to such constant variation as to make adherence to Section 18(i) cumbersome and unwieldy, if at all possible.

The scholarship plan is far removed from the usual investment concept contemplated by Section 18(i). The goal of each member is the realization of the scholarship award for his candidate. The trust funds may not be used for any other purpose. Since each member who fully complies with the plan will ultimately invest the same amount for each qualified candidate, the public interest would not be affected adversely by acceptance of the plan's voting provisions in lieu of the

virtually unmanageable arrangement which would result from compliance with Section 18(i). Applicant's request for an appropriate order is granted.

Section 23(b)

Applicant requests an order permitting it to sell its shares below net asset value, contrary to Section 23(b) of the Act, until its next annual meeting at which time it will seek its members' approval of continuation of the present selling procedure. Division argues that the section was designed to prevent dilution of existing shareholders' interest in closed-end companies by sales below net asset value and that new investors would participate in applicant's assets and earnings without paying a pro-rata share.

However, as shown above, a member may not realize on any of Trust Fund's assets or earnings until his candidate has qualified for the scholarship award. The investment of all members sponsoring successful candidates would be identical. Although the Division's position would have substance where marketable securities are issued, enforcement of Section 23(b) under the circumstances present here would not appear to add to the protection of investors.

Applicant's request, conditioned on membership approval of present selling procedures at the next annual meeting, is granted. Accordingly,



IT IS ORDERED that applicant's request that it be declared not to be an investment company within the purview of Section 3(a) of the Act be, and it hereby is, denied; and

IT IS FURTHER ORDERED that applicant's request for exception from investment company status under Sections 3(c)(3), 3(c)(8) and 3(c)(12) of the Act be, and it hereby is, denied; and

IT IS FURTHER ORDERED that applicant's request for exemption from the provisions of Sections 14(a), 27(c)(1) and 30(d) of the Act be, and it hereby is, denied; and

IT IS FURTHER ORDERED, pursuant to Section 6(c) of the Act, that

(A) applicant's request for exemption from the provisions of Section 26(a)(2)(A) and 26(a)(2)(B) of the Act be, and it hereby is, granted.

(B) applicant's request for exemption from Section 16(a) of the Act be, and it hereby is, granted to the following extent:

(1) on condition that CAP amend its by-laws to insure (a) a continuing majority of elected members of its Board of Directors, and (b) that no more than 60% of the members of its Board of Directors shall be officers or employees of CAP, and (c) on condition that CAP shall conform to such other provisions of Section 10(h) of the Act as may become applicable; and

(2) on the further condition that applicant shall not deviate from the investment policies set forth in its application.

(C) in respect of Section 18(i) of the Act, voting rights of members as presently set forth in CAP's by-laws, i.e., each investor has one vote for each candidate he sponsors, be, and they hereby are, permitted.

(D) in respect of Section 23(b) of the Act, CAP's present procedure of selling memberships below asset value be, and it hereby is, permitted until the next annual meeting of the membership at which time the members' approval of such procedure will be sought and may be continued only in the event such approval is obtained.<sup>67/</sup>

This order shall become effective in accordance with and subject to the provisions of Rule 17(f) of the Commission's Rules of Practice.

Pursuant to Rule 17(b) of the Commission's Rules of Practice, a party may file a petition for Commission review of this initial decision within 15 days after service thereof on

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67/ To the extent that the proposed findings and conclusions submitted to the Hearing Examiner are in accord with the views set forth herein they are accepted, and to the extent they are inconsistent therewith they are expressly rejected. Division's brief requests that no exemption be granted from the provisions of Sections 22(d), 27(a)(1), 27(a)(2) and 27(a)(3). However, these requests have not been considered. Neither the application nor the order for proceedings refer to these sections and although the order authorizes specific additional matters and questions, the matters covered by these sections were not raised during the course of the hearing.

him. Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each party unless he files a petition for review pursuant to Rule 17(b) or the Commission, pursuant to Rule 17(c), determines on its own initiative to review this initial decision as to him. If a party timely files a petition to review or the Commission takes action to review as to a party, this initial decision shall not become final as to that party.

A handwritten signature in black ink, appearing to read "Sidney Gross". The signature is written in a cursive, flowing style with a large initial 'S'.

Sidney Gross  
Hearing Examiner

Washington, D. C.  
October 24, 1968