

ACT ICA
SECTION _____
RULE 3a-2
PUBLIC AVAILABILITY 6/12/98



June 12, 1998
Our Ref. No. 98-324-CC
OnePoint Communications
Corp. and OnePoint
Communications, LLC
File No. 132-3

RESPONSE OF THE OFFICE OF CHIEF COUNSEL
DIVISION OF INVESTMENT MANAGEMENT

Your letter of June 11, 1998 requests assurance that the staff would not recommend enforcement action to the Commission against OnePoint Communications Corp.¹ and OnePoint Communications, LLC (collectively, the "Company") under Section 7 of the Investment Company Act of 1940 (the "Act") if the Company relies on Rule 3a-2 under the Act for a one-year period beginning on the date on which it ceases to be excluded from the definition of investment company under Section 3(c)(1) of the Act.

Facts

You state that the Company is a rapidly growing provider of bundled telephony and video services to residents of multi-dwelling unit buildings ("MDUs"). The Company was founded in March 1996 with a joint investment by a venture capitalist (the "Founder") and a subsidiary of a regional Bell operating company (the "Bell Investor"). You represent that the Founder and the Bell Investor are the sole beneficial owners of the Company's equity interests. You state that the Company has financed its development with equity funding provided by the Bell Investor and the Founder, as well as by secured bank borrowings from a single bank.

You represent that the Company, directly or through its subsidiaries, has been primarily engaged since its inception in the telecommunications business. You state that the primary activities of the Company have consisted of the procurement of regulatory authorizations to provide telephony services; the negotiation of long-term contracts providing preferential rights for on-site marketing of telephony and video services with national real estate investment trusts and other MDU property owners, developers, and managers; the hiring of management and other key personnel; the raising of capital; the development, acquisition, and integration of customer service, billing, and other back office systems; the identification of potential acquisition targets in the private cable market; and the negotiation of telephony resale agreements with incumbent local exchange carriers. You state that the Company began its marketing efforts in a limited number of MDUs in July 1997 and began actively marketing its services in January 1998. You represent that, as of March 31, 1998, the Company had 2,613 subscribers for its telephony services and 572 subscribers for its video services.

¹ OnePoint Communications Corp. is the successor by merger to OnePoint Communications, LLC.

You represent that the Company's operations are conducted through its subsidiaries. You state that one of the Company's wholly owned subsidiaries owns interests in two telecommunications related companies (the "Strategic Subsidiaries") that may be deemed not to be "majority-owned subsidiaries" of the Company under Section 2(a)(24) of the Act.² You assert that these interests in the Strategic Subsidiaries could cause the Company to be deemed to be an "investment company" under Section 3(a)(1)(C) of the Act.³

You state that, regardless of the Company's status under Section 3(a)(1)(C) of the Act, the Company has been and currently is excluded from the definition of investment company by Section 3(c)(1) of the Act.⁴ You represent that the Company recently has made a securities offering in reliance on Section 4(2) of the Securities Act of 1933 (the "Securities Act") with immediate resales pursuant to Rule 144A under the Securities Act.⁵ You further state that the Company expects to follow this private offering of its securities with a registered exchange offer under the Securities Act. You acknowledge that at such time as the Company is deemed to presently propose to make the registered exchange

² Section 2(a)(24) of the Act defines a "majority-owned subsidiary" of a person to mean a company 50% or more of the outstanding voting securities of which are owned by the person, or by a company which is a majority-owned subsidiary of the person.

³ Section 3(a)(1)(C) of the Act defines "investment company" to include any issuer that 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% of the issuer's total assets (exclusive of Government securities and cash items) on an unconsolidated basis. Section 3(a)(2) of the Act defines "investment securities" to include all securities except, as relevant here, securities issued by majority-owned subsidiaries which (i) are not investment companies, and (ii) are not relying on the exception from the definition of investment company in Section 3(c)(1) or 3(c)(7) of the Act.

You state that, to the extent that the Strategic Subsidiaries are not deemed "majority-owned subsidiaries" of the Company, the ownership interests in the Strategic Subsidiaries would be deemed to be "investment securities." As a result, the Company may be deemed to hold "investment securities" having a value in excess of 40% of the value of the assets of the Company, thereby meeting the definition of "investment company" under Section 3(a)(1)(C) of the Act.

⁴ Section 3(c)(1) of the Act excludes from the definition of investment company any issuer the securities of which are beneficially owned by not more than 100 persons and which is not making and does not presently propose to make a public offering of its securities.

⁵ Section 4(2) of the Securities Act provides an exemption from the registration provisions of the Securities Act for transactions by an issuer not involving any public offering. Rule 144A under the Securities Act provides an exemption from the registration provisions of the Securities Act for private resales of certain securities to sophisticated institutions, known as "qualified institutional buyers."

offering, Section 3(c)(1) of the Act will no longer be available to the Company.⁶ You state that the Company is concerned that following such transactions and the loss of Section 3(c)(1) status, the Company could be viewed as an investment company until it uses its newly raised capital in its bundled telephony and video services operating business. As a result, you request that the staff confirm that the Company will not be deemed to be an investment company in reliance on Rule 3a-2 under the Act for a one-year period beginning on the date that Section 3(c)(1) of the Act is no longer available to the Company.

Analysis

Rule 3a-2 under the Act is a safe harbor that deems transient investment companies not to be investment companies under the Act for a period not to exceed one year, provided that specified safeguards are satisfied. Rule 3a-2(a) requires any issuer that relies on the rule to have a *bona fide* intent to be engaged primarily, as soon as is reasonably possible within the one-year time period, in a business other than that of investing, reinvesting, owning, holding, or trading in securities. This intent must be evidenced by the issuer's business activities as well as an appropriate resolution of the issuer's board of directors. The purpose of Rule 3a-2 is to temporarily relieve certain issuers that are in transition to a non-investment company business from regulation under the Act.⁷

Rule 3a-2(b) under the Act states that the time period during which an issuer can rely on the rule begins on the earlier of the date on which the issuer (i) owns securities and/or cash exceeding 50% of the value of such issuer's total assets on either a consolidated or unconsolidated basis, or (ii) owns or proposes to acquire investment securities having a value exceeding 40% of the value of the issuer's total assets (excluding Government securities and cash items) on an unconsolidated basis. You state that the wording of Rule 3a-2(b) under the Act concerning the start of the one-year period could be interpreted to suggest that the time period has already begun due to the Company's investments in the Strategic Subsidiaries or otherwise, even though the Company has been excluded from the definition of investment company by virtue of Section 3(c)(1) of the Act.

In the release adopting Rule 3a-2, the Commission stated that "the Commission believes that the one-year period should be measured from the time an issuer has the characteristics which would cause it to be defined as an investment company."⁸ You

⁶ You have not asked, and this letter expresses no opinion regarding, when the Company will be deemed to presently propose to make a public offer for purposes of Section 3(c)(1) of the Act. If the Company has in fact presently proposed to make a public offering of its securities, the period during which the Company can rely on Rule 3a-2 pursuant to this letter already has begun.

⁷ Investment Company Act Release No. 10943 (Nov. 16, 1979) (proposing Rule 3a-2).

⁸ Investment Company Act Release No. 11552 (Jan. 14, 1981) (adopting Rule 3a-2).

assert that an issuer, such as the Company, that has relied upon Section 3(c)(1) of the Act cannot have "the characteristics which would cause it to be an investment company" because Section 3(c)(1) specifically excludes such a company from the definition of investment company.

Based on the facts and representations in your letter, the staff would not recommend enforcement action to the Commission under Section 7 of the Act if the Company relies on Rule 3a-2 under the Act for a one-year period beginning on the date on which it ceases to be excluded from the definition of investment company under Section 3(c)(1) of the Act. Our position is based particularly on your representations that:

(i) The Company, directly or through its subsidiaries, has been primarily engaged since its inception in the telecommunications business;

(ii) The Company's offering memorandum for the private offering states, and the registration statement for the public offering will state, that the indenture governing the notes offered prohibits the Company from engaging in any business other than the telecommunications business;

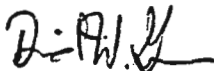
(iii) The period during which the Company will rely on Rule 3a-2 under the Act begins on the date that the Company proposes to make a public offering of its securities for purposes of Section 3(c)(1) of the Act;

(iv) During the period in which the Company relies on Rule 3a-2 under the Act, it will comply with all of the requirements of the rule except paragraph (b);

(v) During the period in which the Company relies on Rule 3a-2 under the Act, it will invest the proceeds of its public offering, in order to preserve their value pending their investment in the Company's telecommunications business, in Government securities, certificates of deposit, or other securities appropriate for the purpose; and

(vi) During the period in which the Company relies on Rule 3a-2 under the Act, the Company will not hold itself out as being engaged primarily in the business of investing, reinvesting, or trading in securities.

This response expresses the Division's position on enforcement action only and does not express any legal conclusions on the issues presented. Because this position is based on the facts and representations in your letter, you should note that any different facts or circumstances might require a different conclusion.



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Rule 3a-2 under the Investment Company Act of 1940

June 11, 1998

Douglas Scheidt
Chief Counsel, Division of Investment Management
Securities and Exchange Commission
450 5th Street, N.W.
Washington, DC 20549

Re: Request for an Interpretation of Rule 3a-2 under the
Investment Company Act of 1940

Dear Mr. Scheidt:

On behalf of our clients, OnePoint Communications Corp.¹ and OnePoint Communications, LLC (referred to collectively as the "Company"), we respectfully request that the staff ("Staff") of the Securities and Exchange Commission ("Commission") confirm that it will not recommend that the Commission take enforcement action under Section 7 of the Investment Company Act of 1940 (the "1940 Act") if the Company relies on Rule 3a-2 under the 1940 Act for a one year period commencing on the date on which it ceases to be excluded as an investment company by reason of Section 3(c)(1) of the 1940 Act.

CORPORATE STRUCTURE

The Company is a rapidly growing provider of bundled telephony and video services to residents of multi-dwelling unit buildings ("MDUs") that was founded in March 1996 with a joint investment by a venture capitalist (the "Founder") and a subsidiary of a regional Bell

¹ OnePoint Communications Corp. is the successor by merger to OnePoint Communications, LLC.

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operating company (the "Bell Investor").² The Founder and the Bell Investor are the sole beneficial owners of the Company's equity interests. To date, the Company has financed its development with equity funding provided by the Bell Investor and the Founder and secured bank borrowings from a single bank.

The Company directly or through its subsidiaries has been primarily engaged in the telecommunications business since its inception. The primary activities of the Company from its inception have consisted of the procurement of regulatory authorizations to provide telephony services, the negotiation of telephony and video Rights of Entry for MDUs, the hiring of management and other key personnel, the raising of the capital referred to above, the development, acquisition and integration of customer service, billing and other back office systems, the identification of potential acquisition targets in the private cable market and the negotiation of telephony resale agreements with incumbent local exchange carriers. The Company commenced its marketing efforts in a limited number of MDUs in July 1997 and began actively marketing its services in January 1998 in Washington/Baltimore/ Philadelphia, in February 1998 in Atlanta and Chicago, and in March 1998 in Charlotte/Raleigh/Durham, Denver and Phoenix. As of March 31, 1998, the Company had 2,613 subscribers for its telephony services and 572 subscribers for its video services.

INVESTMENT COMPANY ACT STATUS

The Company's operations are conducted through its several subsidiaries. One of the Company's wholly-owned subsidiaries (the "Owner Subsidiary") owns interests in two companies that could cause the Company to be viewed as an "investment company" pursuant to Section 3(a)(1) of the 1940 Act.

² The Company, through several subsidiaries, currently offers bundled telephony and video services to MDU residents in high growth, densely populated urban and suburban markets through "Rights of Entry," which are long-term contracts providing preferential rights for on-site marketing of telephony and video services with national real estate investment trusts and other MDU property owners, developers and managers.

In early 1997, the Owner Subsidiary acquired a 50% equity interest in a limited liability company ("CableCo") which has Rights of Entry to provide private cable television service to approximately 64,000 units in 100 MDUs and three franchise cable areas in the Washington, D.C. metropolitan area. The Owner Subsidiary currently holds an approximately 45% equity interest in CableCo. The Owner Subsidiary's investment in CableCo was designed as a strategic investment in furtherance of the Company's goal to provide telephony and video services. For example, the Company is leveraging its strategic relationship with CableCo by marketing telephony services to residents of MDUs currently receiving video services from CableCo. The Company has also partnered with CableCo to develop integrated customer care and billing capabilities designed to support both telephony and video services. However, the management structure of CableCo (under which the Owner Subsidiary may elect 40% of its board of managers) means that CableCo may not be a "majority-owned subsidiary," as such term is defined in Section 2(a)(24) of the 1940 Act. In December 1997, the Owner Subsidiary also acquired a strategic 50% equity interest in another telecommunications-related company (together with CableCo, the "Strategic Subsidiaries"), also with the right to elect 40% of the board.

To the extent that the ownership interests in the Strategic Subsidiaries are deemed securities and such Subsidiaries are not deemed "majority-owned subsidiaries," the ownership interests then would be viewed as "investment securities."³ As a result, the Company may in the past be deemed to have held "investment securities" having a value exceeding 40% of the value of the assets of the Company for purposes of Section 3(a)(1)(C) of the 1940 Act.⁴

³ Section 3(a)(2) of the 1940 Act defines the term "investment securities" to include all securities except (A) Government securities, (B) securities issued by employees' securities companies, and (C) securities issued by majority-owned subsidiaries of the owner which (i) are not investment companies and (ii) are not relying on the exemption from the definition of investment company in paragraph (1) or (7) of Section 3(c).

⁴ Section 3(a)(1)(C) defines the term "investment company" to mean any issuer which 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

(continued...)

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Regardless of the Company's status under any part of Section 3(a)(1), the Company has not been and currently is not an investment company by reason of the "private investment company" exclusion in Section 3(c)(1) of the 1940 Act. This is because since its inception (i) the Company's securities (other than short-term paper) have been beneficially owned by not more than one hundred persons and (ii) the Company has not made or proposed to make a public offering of its securities.

POSSIBLE PUBLIC OFFERING

The Company recently has made a securities offering in reliance on Section 4(2) of the Securities Act of 1933 (the "1933 Act") with immediate resales pursuant to Rule 144A under the 1933 Act which it expects would be followed by a registered exchange offer under the 1933 Act. At such time as the Company is deemed to presently propose to make the registered exchange offer, the Section 3(c)(1) "private investment company" exclusion will no longer be available to the Company. As is the case with many early-stage or "start-up" companies, the Company is concerned that following such transactions and loss of Section 3(c)(1) status, the Company could be viewed as an investment company until it has deployed its newly raised liquidity in its bundled telephony and video services operating business.

REQUESTED INTERPRETATION

At such time as the Company is deemed to presently propose to make the registered exchange offer, and accordingly loses its Section 3(c)(1) "private investment company" status, the Company intends to rely on the "transient investment company" exclusion in 1940 Act Rule 3a-2. Rule 3a-2 deems an issuer not to be an investment company for purposes of Sections 3(a)(1)(A) or 3(a)(1)(C) "during a period of time not to exceed one year" provided that the issuer has a *bona fide* intent to engage as soon as reasonably possible (but in any event by the termination of the 1-year period) in a business other than that of investing, reinvesting, owning, holding or trading in securities.

⁴ (...continued)

exceeding 40% of the value of such issuer's total assets (exclusive of Government securities and cash items) on an unconsolidated basis.

After completing its reliance on Rule 3a-2, the Company directly or through its subsidiaries intends to be primarily engaged in the telecommunications business. In this regard, the Company's offering memorandum for the private offering states, and the registration statement for the public offering will state, that the Indenture governing the notes offered prohibits the Company from engaging in any business other than the telecommunications business.

The Company will meet the conditions of Rule 3a-2. The Company has a *bona fide* intent to be engaged primarily in the business of providing bundled telephony and video services. In addition to the business activities described above, the Company's board of directors has adopted a resolution of the kind contemplated by Rule 3a-2(a)(2).⁵ The Company also has not relied on Rule 3a-2 at any time during the past 3-year period. The Company is concerned, however, that the language in paragraph (b) of Rule 3a-2 concerning the commencement of the 1-year time period could be interpreted to suggest that the time period has already commenced due to the investments in the Strategic Subsidiaries or otherwise, even though the Company to date has not been an investment company.

Accordingly, the Company seeks the Staff's concurrence that the 1-year time period provided by Rule 3a-2 does not commence until the Section 3(c)(1) exclusion is no longer available to the Company. This interpretation is consistent with the Commission's own explanation of the 1-year time period provided in Rule 3a-2. In its final Rule 3a-2 rulemaking, the Commission said that "the Commission believes that the one year period should be measured *from the time an issuer has the characteristics which would cause it to be defined as an investment company.*" *Final Rule on Transient Investment Companies*, 46 Fed. Reg. 6883 (Jan. 22, 1981) (emphasis added). A company the securities of which (other than short-term paper) are

⁵ During the time it relies on Rule 3a-2, the Company will not actively invest and reinvest in securities and hold itself out as being in the business of investing, reinvesting or trading in securities. See *Final Rule on Transient Investment Company*, 46 Fed. Reg. 6883, n.8 (Jan. 22, 1981). In this regard, following receipt of the proceeds from the public offering, One Point will temporarily invest such proceeds in government securities, certificates of deposit, or other securities appropriate in order to preserve their value pending their investment in the telecommunications business.

beneficially owned by not more than 100 persons and which is not making nor presently proposing to make a public offering of its securities cannot have "the characteristics which would cause it to be defined as an investment company" since Section 3(c)(1) explicitly excludes such a company from the definition of "investment company."

The Staff has, at least implicitly, applied this reasoning in determining the point at which an issuer will no longer be viewed as relying on Rule 3a-2. In several no-action letters, the Staff extended the 1-year time period where companies intended to become *subsequently* eligible for the real estate exclusion from the investment company definition in Section 3(c)(5)(C) of the 1940 Act. See *Medidentic Mortgage Investors*, 1984 WL 45320 (May 23, 1984); *Metropolitan Realty Corporation*, 1989 WL 246525 (Nov. 15, 1989). The Staff clearly viewed the intent to operate under the Section 3(c) exclusion as a *bona fide* intent to enter into a business other than that of investing, reinvesting, owning, holding or trading in securities. Accordingly, at the point when the issuers began to rely on a Section 3(c) exclusion the Staff considered Rule 3a-2 as no longer applicable, and did not consider relevant whether or not the issuers continued to own securities in excess of the threshold levels in Rule 3a-2(b). Logic dictates that the reciprocal of this must also be true. That is, an issuer which historically has relied on Section 3(c)(5)(C) but which no longer satisfies the asset composition requirements of that Section as articulated by the Staff would have under Rule 3a-2 one year from the loss of its Section 3(c)(5)(C) exclusion to become engaged in a non-investment company business. Similarly, a company operating initially pursuant to another Section 3(c) exclusion, in this case Section 3(c)(1), should not be viewed as triggering the start of the Rule 3a-2 one-year period prior to losing the statutory exclusion merely because the company might have theretofore held securities that exceeded the Rule 3a-2 thresholds.

Nothing in the Rule 3a-2 rulemakings suggests that start-up companies operated initially pursuant to the private investment company exclusion in Section 3(c)(1) are less entitled than any other non-investment company historically investing in securities but in transition (e.g. a former Section 3(c)(5) factoring company, sales finance company or real estate lender or a former Section 3(c)(2) broker-dealer) to rely on Rule 3a-2 for the full 1-year period measured from the date of loss of the Section 3(c) exclusion.

This interpretation is supported by the general intent of Rule 3a-2 -- to relieve start-up and other companies in transition from the significant operational modifications which

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might be necessary to comply with the Investment Company Act. See *Proposed Rule on Transient Investment Companies*, 44 Fed. Reg. 67153 (Nov. 23, 1979). If the Rule 3a-2(b) thresholds were measured for start-up companies without reference to the availability of other exemptions or exclusions, then the Rule 3a-2 exemption would not be available at the time start-up companies most need it (i.e. when their private capital resources have been exhausted and they must raise public capital), and would generally be duplicative of the Section 3(c)(1) "private investment company" exclusion, since the vast majority of start-up companies will initially have fewer than 100 security holders and are not able to make a public offering until they have established a business.

In light of the foregoing, we respectfully request that the Staff issue a letter confirming that it will not recommend that the Commission take enforcement action under Section 7 of the 1940 Act if the Company relies on Rule 3a-2 for a 1-year period commencing on the date that the exclusion in Section 3(c)(1) of the 1940 Act is no longer available, provided that all of the conditions of Rule 3a-2 are otherwise met.

Sincerely yours,



Maureen A. Donley-Hoopes

MDH:blf

cc: K. McMillan
D. Grim