



State of Utah

DEPARTMENT OF COMMERCE
DIVISION OF SECURITIES

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July 25, 1996

Mr. James R. Kruse
Kruse, Landa & Maycock, L.L.C.
Eighth Floor, Bank One Tower
50 West Broadway
Salt Lake City, UT 84101-2034

Re: WestMed Physician Network, Inc. a Utah Corporation
File #005-4924-47/A54673-47
Request for No-Action Letter

Dear Mr. Kruse:

This letter is in response to your letters dated April 29, June 13 and July 18, 1996 wherein you requested the Utah Division of Securities ("Division") issue a No-Action Letter regarding the proposed offer and sale by WestMed Physician Network, Inc., ("WestMed") for earned membership units in WestMed without complying with the registration and prospectus delivery requirements of the Utah Uniform Securities Act ("Act").

Based on the facts presented in your letters, and in reliance upon your opinion as counsel, the Division will not recommend any enforcement or administrative action should the transactions proceed as outlined in your letters. To avoid unnecessary restatement or summarization of the facts set forth in your letters, the Division's response is attached to a photocopy of your letters.

This response does not purport to express any legal conclusions regarding the applicability of statutory or regulatory provisions of federal or state securities laws to the questions presented. It merely expresses the Division's opinion on enforcement or other administrative actions.

As this recommendation is based upon the representations made to the Division, any different facts or conditions of a material nature might require a different conclusion. Furthermore, this No-Action Letter relates only to the referenced issuers and memberships and shall have no value for future similar offerings and does not absolve any party involved from complying with the anti-fraud provisions contained in § 61-1-1 of the Act.

Very Truly Yours,

UTAH DEPARTMENT OF COMMERCE
DIVISION OF SECURITIES



S. Anthony Taggart
Director of Corporate Finance

cc: Mark Griffin, Director



KRUSE, LANDA & MAYCOCK, L.L.C.

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June 13, 1996

Mr. S. Anthony Taggart
Director of Corporate Finance
State of Utah Securities Division
Department of Commerce
160 East 300 South
Salt Lake City, Utah 84111

HAND DELIVERY

Re: WestMed Physician Network, Inc., a Utah corporation
Division File No. A54673-47

Dear Mr. Taggart:

This is in response to your letter of May 14, 1996, respecting the above matter in which you request additional information in three specific areas.

In the course of refining the business plan of WestMed Physician Network, Inc. ("Physician Network"), a limited number of changes to the overall structure have been determined. Those changes are summarized in the following response. Where information in the following is inconsistent with the previous request, the information in the previous request is superseded by the following.

To facilitate your review of the enclosed, each of the three numbered comments in your letter of May 14, 1996, is quoted below, followed by our response.

- 1) The Division requests a copy of the Applicant's Member Agreement and the Disclosure Statement.

Response: The Applicant's Member Agreement has not been finalized, pending a substantive response to this request for an Interpretive Opinion from the Utah Division of Securities (the "Division"). When the agreement is drafted, it will be drafted in conformity with the representations made to the Division in connection with its request for an interpretive opinion.

A draft disclosure statement outlining the purpose and intent of Physician Network is enclosed. This draft is being developed for delivery to Utah Medical Association member physicians as an introduction to Physician Network. You will note that this reflects certain structural changes to Physician Network and its proposed relationship with WestMed Management, Inc. ("Management") in the following particulars:

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- (a) *The line of demarcation between Physician Network and Management has now been delineated more precisely. Physicians who are members in good standing of the Utah Medical Association and who are licensed, active practitioners in the state of Utah will be eligible for membership in Physician Network. They will not be eligible for participation as stockholders of Management. This change was implemented in an effort to avoid potential conflicts of interest for physicians who otherwise might be members of Physician Network as well as stockholders of Management. Management would be owned by investors that together would own all of the rights to profits in Management and to receive its assets upon liquidation and liquidation. As noted above, Utah Medical Association members who are licensed physicians active in practice in Utah and who, therefore, are eligible for membership in Physician Network, would be excluded from investing in Management. However, in order to ensure that the views of Physician Network are considered in the operation of Management, Management would issue to Physician Network one share of Management preferred stock:*
- (i) *with the right to elect up to 30% of the members of the whole board of directors of Management;*
 - (ii) *with the right to vote the single share of preferred stock with all other issued and outstanding shares of Management, voting together as a single class, with the share of preferred stock issued to Physician Network constituting 30% of the voting power of all voting securities outstanding; and*
 - (iii) *with no right to participate in dividends or in distributions upon liquidation and dissolution of Management.*

The purpose of the foregoing is to enable the physician members of Physician Network to have a voice in Management. That voice would be limited to no more than 30% of representation on the board of directors or shareholder votes of Management in an effort to comply with various anti-trust considerations. In addition, Management would implement a confidentiality discipline so that Physician Network and its representatives would be precluded from access to financial, demographic, and physician fee information that would be necessary for Management to conduct its activities appropriately.

Physician Network would be operated without any expectation of generating profits but with the intent of limiting revenues to amounts sufficient to cover related costs as discussed in response to item 3 below. In order to formalize the limitation on the participation in income-generating activities insofar as they relate to the relationship with Management, the Articles of Incorporation of Physician Network would expressly prohibit its ownership of securities in any

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corporation, limited liability company, or other for-profit enterprise, save and except the ownership of a single share of preferred stock of Management.

- (c) *Even through Physician Network would not be organized with the expectation of generating profits for its members, there is a desire to provide for the eventuality that at some time Physician Network may desire to alter its structure and become a traditional equity participant in Management. Therefore, in addition to the ownership of one share of preferred stock in Management, Management would grant to Physician Network an option at a fixed price to purchase a specified number of shares of common stock of Management, exercisable for a specified period, expressly subject to satisfying certain requirements under the Utah Uniform Securities Act (the "Utah Act"). For example, if Management were initially capitalized with \$1,400,000 and had 700,000 shares outstanding, Physician Network could have the option to purchase 300,000 shares (i.e., 30% of the 1,000,000 shares that would then be issued and outstanding after exercise of such option) for \$600,000, or \$2.00 per share, exercisable for one -year commencing at the end of the first fiscal quarter in which Management reports a net profit from operations, subject to satisfying applicable requirements of the Utah Act.*

Such requirements under the Utah Act would expressly provide that the option could not be exercised unless Physician Network prepared either a proxy statement or application for registration. Such a proxy statement or application for registration would enable the Physician Network members to convert Physician Network, organized without the intent to generate profits in which its members could participate, into an entity that could generate profits, thereby resulting in potential gain to its members. This would, of course, be a fundamental change from the representations made in connection with this request for an Interpretive Opinion. Such a change in fundamental purpose could only be implemented if Physician Network hereafter satisfied the disclosure requirement appropriate in the circumstances. This would be effected by filing either a proxy statement or application for registration of securities with the Division for its review prior to seeking Physician Network stockholder approval of an amendment to its Articles of Incorporation, bylaws, or other organic documents to enable Physician Network to own stock in a for-profit corporation or other entity. Recognizing that such a vote would essentially constitute an investment decision within the theoretical context of the Utah Act, if deemed appropriate after consultations with the Division, alternatively Physician Network would file an application for registration of securities covering the change in the fundamental character of Physician Network which would be tantamount to the issuance of a new security. In any event, Physician Network would file a proxy statement or application for registration, or perhaps a combination thereof, with the Division for its review, pay the required fees,

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and circulate it to Physician Network members only after it has been declared effective by the Division. Only after completing such Division process would Physician Network members be entitled to take action to change the nature of Physician Network to permit exercise of the option to purchase an equity position in Management. If the Physician Network duly adopted the proposed change in its fundamental nature, Physician Network could then exercise such option to purchase Management equity. Of course, Physician Network acknowledges that it would also be required to comply with the registration provisions of the Utah Act in connection with any efforts to raise any capital that may be required to fund exercise of the option.

- 2) The Division requests additional information concerning the agreement and structure of the relationship between the Applicant and WestMed Management, Inc., pertaining to the 30% ownership by physicians.

Response: The 30% ownership by Physician Network, as revised, is discussed in response to item 1.

The contractual relationship between Physician Network and Management has not been completed. Initially, the organizers of Physician Network and Management will outline in detail the terms of the contract between them, specifying both the services to be provided by Management to Physician Network and the initial fees to be charged, consistent with the principles set forth in the disclosure statement attached. The precise terms of that agreement will be disclosed to members of the Utah Medical Association in active practice in Utah before they are invited to become Physician Network members. The nature of the services provided and the amount charged will be determined with reference to similar services provided within the healthcare industry by others in arm's length transactions. Companies within the healthcare industry, both in Utah and in other states, provide management, negotiating, and other services similar to those to be provided by Management to independent physician networks so that competitive models are available for guidance.

It is anticipated that the original agreement between Physician Network and Management will be for a term of not to exceed three to five years to enable continuity and predictability in the initiation of their respective business activities. Thereafter, Physician Network would be free to obtain management services from any management company that may provide the required services. In that regard, Physician Network will be managed exclusively by its members, without participation of Management. As noted above, there are a number of companies that provide management services to independent physician networks, and Physician Network will be able to negotiate with all of such possible providers in order to replace Management, should Physician Network desire to do so.

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In its selecting a firm to provide management services, Physician Network presumably will consider the services required and the related fees charged. Physician Network would likely also consider, of course, that ultimately it may have the right to obtain an equity position in Management by virtue of the option to purchase common stock as discussed above. In considering that factor in their search for a manager, Physician Network directors and members should not be subject to conflicts of interest because none of its members will have been permitted to be stockholders in Management.

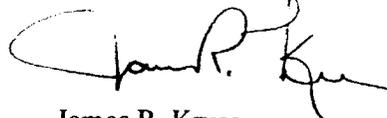
- 3) The Division requests more information regarding the manner in which the Applicant plans to reduce revenues to avoid excess accumulations of capital used for operations, and reasonable reserves.

Response: Physician Network's revenues will be derived from fees charged its members. Those fees will generally be on a percentage of individual physician revenue depending on the nature of the managed care contracts involved. For example, relatively complex capitated arrangements requiring greater management responsibilities will generally necessitate a higher fee than services in connection with the periodic review of preferred provider arrangements. Since Physician Network will be managed exclusively by its practicing physician members and will be precluded from distributing earnings to its members, Physician Network's single focus should be on minimizing fees to be paid by its individual members.

I hope that the foregoing is responsive to your requests. If you desire additional information, please so advise.

Very truly yours,

KRUSE, LANDA & MAYCOCK, L.L.C.



James R. Kruse

JRK:sp

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April 29, 1996

State of Utah Securities Division
Department of Commerce
160 East 300 South
Salt Lake City, Utah 84111

HAND DELIVERY

Attention: Mr. S. Anthony Taggart, Director of Corporate Finance

Re: *Request for Interpretive Response on Organization
of WestMed Physician Network, Inc., a Utah corporation*

Dear Mr. Jenkins:

This letter constitutes a formal request for an interpretive response from the Utah Securities Division (the "Division") to the effect that the membership units (a "Membership" or the "Memberships") proposed for sale by WestMed Physician Network, Inc. ("WPN"), a corporation being organized under the laws of the state of Utah, are not securities, as that term is defined in section 61-1-13(22) of the Utah Uniform Securities Act (the "Act").

FACTS

The organizers of WPN intend to file Articles of Incorporation with the Utah Division of Corporations and Commercial Code of the Department of Commerce to incorporate WPN. In order to avoid the use of "stock" and "share" terminology for the reasons set forth below, WPN proposes that its articles of incorporation shall provide that voting rights and ownership interests in WPN will be evidenced by Memberships.

It is the intent that this corporation function as what has come to be known in the health care industry as a "physicians' organization" or "PO." The purpose of the organization is to bring physicians together as a group in order for them to compete more effectively in the contract managed care environment currently prevalent in the health care community. This means supporting the efforts of physicians to improve their practice procedures and efficiencies; joining with other physicians and other health care providers across geographic boundaries to provide open access and a range of services; joining with payor organizations and employers to develop strategies for reducing costs, improving efficacy of care, and establishing long-term, health care relationships; educating consumers; utilizing the health care system more appropriately; and selecting and supporting those hospitals and other health care providers that provide the best care in the most efficient manner.

All members of WPN will be required to be residents of and physicians ("Physicians") licensed in the state of Utah. Ownership of the Memberships will not be available to members of the health care industry who are not licensed physicians. Notwithstanding the foregoing, however, at some point, WPN may consider opening membership to other licensed health care professionals such as dentists. One of the principal ongoing activities of WPN will be to maintain a current database of health care information respecting the nature of professional services provided (e.g., average length of patient hospital stay; number, nature, and sequence of laboratory tests; adherence to established treatment protocols; and similar objective data available within the industry) by its members in order to monitor and maintain the quality of health care provided.

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Only one Membership at \$4,000¹ per Membership will be sold to each qualifying Physician/purchaser. The Memberships will be sold to entities, provided that one Membership must be purchased for each qualifying Physician/Member within the entity. No commissions or fees will be charged or paid in connection with the sale of the Memberships. The Memberships will have the right to vote on corporate matters, with each Membership entitled to one vote.

At the time of purchasing a Membership, each Physician will be advised in writing that a Membership in WPN should not be viewed or acquired as an investment and should not be purchased with the expectation of deriving any dividends or similar profits from owning a Membership. Each Physician will be required to acknowledge in writing that the Membership interest evidences membership only and should not be considered a financial interest or investment. Physicians will be motivated to join WPN because of their understanding of the managed care market, the benefits of physicians' organizations, the professional desire to improve the health care they provide, and their desire to survive in an increasingly competitive market by enhancing their bargaining position through collective action.

At the time of purchase, each member will be required to enter into a Member Agreement which limits transferability of the Memberships, specifies minimum practice quality as a requirement for continuing participation, mandates active involvement in management, and other matters. The restrictions on transfer in the Member Agreement will include an absolute prohibition of any sale of Memberships other than back to WPN, mandate a forced sale to WPN if the Physician/member ceases to practice medicine in Utah or on the occurrence of other specified events, and provide for the purchase of the interest of a spouse of a Physician/Member in the event of termination of a marital relationship. The price at which the Memberships are to be sold is fixed by the Member Agreement at the price paid by the Physician, except when the Physician/Member ceases to practice medicine in Utah or on the occurrence of other specified events, in which case the price is fixed at \$100 per Membership. Any purported pledge or hypothecation of the Memberships will be void. Certificates for Memberships will bear a legend noting the restrictions set forth in the Member Agreement. Alternatively, WPN may elect not to issue certificates for Memberships as contemplated by section 16-10a-627 of the Utah Revised Business Corporation Act, in which case WPN shall send members a written statement of the restrictions on transfer as provided in the notice requirement of the statute. At the request of the Division, prior to use, a copy of the form of Member Agreement will be submitted to the Division for comment to assure its conformance with the representations set forth herein.

WPN will have a symbiotic, contractual relationship with a separately organized, owned, and capitalized management corporation, WestMed Management Group, Inc. ("WestMed Management") that will provide management and marketing services to WPN as well as individual Physicians with a view toward improving the quality and cost efficiency of medical services they provide to their patients and payors through a coordinated infrastructure. Because of considerations under applicable anti-trust requirements, the Management Corporation will not be owned more than 30% by Physicians. WPN will pay the Management Corporation for services provided on terms to be agreed upon between them in arm's length negotiations.

With the management advice and assistance of WestMed Management, WPN, as the organizational entity that links together the otherwise independent Physicians, will enter into managed care contracts to provide medical services as agreed. These agreements with third-party payors will determine the nature and extent of services

¹ In the first 90 days after being introduced and invited to join IPN, Physicians will be allowed to purchase the Memberships at a cost of \$2,500 per Membership and during the next 90 days at a cost of \$3,000 per Membership.

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Physician/Members will contract with WPN to provide their services, on a pre-determined fee basis, to entities and employers with which WPN contracts to provide services. These contracts will enable WPN, as representative of a cohesive physicians' group, to negotiate effectively with third party payors and large employers as well as hospitals and others to provide medical services on a cost-efficient, competitive basis. The relationship among the various participants in the health care equation--hospitals, surgery centers, insurers, self-insured groups, physicians' organizations, and other providers--may take many forms, including straightforward fee-for-service contracts, capitated service and payment plans, joint ventures, and other hybrid, cooperative arrangements. By rendering services, individual Physicians will generate income for their personal medical practices. WPN will generate revenues based on health care services provided by its Physician/Members and its contractual relationship within the industry. Revenue will be used to deliver ongoing general and administrative expenses, for maintaining Physician credentialing, for monitoring health care services provided, and for negotiating agreements with hospitals, third party payors, employee groups, or others. In the event that revenue to WPN for an extended period exceeds the requirements of WPN for operating expenses and reasonable reserves, WPN anticipates that it will reduce its revenues to avoid excess accumulations. No dividends will be declared or paid to Physician/Members. WPN expects that the only circumstances under which Members will receive distributions on their Memberships will be pursuant to their rights as the holders of the only class of authorized shares which must be entitled to receive the net assets of the corporation on dissolution as provided in section 16-10a-601 of the Utah Revised Business Corporation Act ("URBCA").

The funds received from the sale of Memberships will be utilized solely to capitalize the operations of WPN, which will consist primarily of recruiting and contracting with Physicians, contracting with third party payors such as insurance companies and health plans, and maintaining the database necessary to support WPN's Physician incentive and other functions.

One of the primary objectives of the Member Agreement is to ensure that the voting control of WPN remains in the hands of active members of the medical community. Prospective Physician purchasers will be advised that the Memberships are not to be viewed as an investment, but as a membership in a network essential to enable them to compete in the managed care market.

WPN will raise its initial capital from the Physician/Members who will utilize the network. Physician/Members will be expected to be active in the operation of WPN, particularly in developing and managing practice improvements programs and ongoing peer utilization review. The success of the network will depend on Physician/Members becoming active participants in the operation of the network.

For your convenience in reviewing this request, enclosed are copies of recent Securities and Exchange Commission letters and other materials cited in the discussion below.

Discussion

Section 61-1-13(22) of the Act defines the term "security" as any ". . . stock; treasury stock; . . . transferable share; investment contract; . . . or, in general, any interest or instrument commonly known as a 'security,' or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guaranty of, or warrant or right to subscribe to or purchase any of the foregoing."

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The above definition of a security is not materially different from the one contained in Section 2(1) of the Securities Act of 1933 (the "1933 Act"). Accordingly, the Utah courts have relied on federal case law interpreting Section 2(1) of the 1933 Act in order to interpret the term "security" as contained in Section 61-1-13(22) of the Act. *Payable Accounting Corp. v. Utah Securities Commission ex rel. McKinley*, 667 P.2d 15 (Utah 1983). This position is supported by Section 61-1-27 of the Act which provides, "This chapter may be so construed as to effectuate its general purpose to make uniform the law of those states which enact it and to co-ordinate the interpretation and administration of this chapter with the related federal regulation."

In *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 851 (1975), the United States Supreme Court stated:

We reject at the outset any suggestion that the present transaction, evidenced by the sale of shares called "stock," must be considered a security transaction simply because the statutory definition of a security includes the words "any . . . stock." Rather we adhere to the basic principle that has guided the Court's decisions in this area:

[I]n searching for the meaning and scope of the word "security" in the Act[s], form should be disregarded for substance and the emphasis should be on economic reality." *Tcherepnin v. Knight*, 389 U.S. 332, 336 (1967). See also *Howey, supra*, 328 U.S., at 298 [footnote omitted].

In *Landreth Timber Co. v. Landreth*, 471 U.S. 681 (1985), the court set forth the following characteristics traditionally associated with stock: ". . . (i) the right to receive dividends contingent upon an apportionment of profits; (ii) negotiability; (iii) the ability to be pledged or hypothecated; (iv) the conferring of voting rights in proportion to the number of shares owned; and (v) the capacity to appreciate in value." (472 U.S. at 686 (citing *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 851 (1975))). The Memberships to be offered and sold by WPN are not the equivalent of "stock" for the purposes of applying Section 61-1-13(22)(b) of the Act or Section 2(1) of the 1933 Act because they do not possess the characteristics of stock as identified by the *Landreth* court.

First, the Physicians/Members will have no expectations of receiving distributions of income (dividends) based on ownership of the Memberships, because no dividends will be paid. The participation of the Members in the value of WPN is limited only to the right required of the holders of the stock of a corporation to share in the net assets of the corporation upon dissolution as provided by statute. URBCA § 16-10a-601.

Second, the Membership interests will not be negotiable or freely transferable. As summarized above, the Member Agreements will contain an absolute prohibition of any sale or transfer of Memberships other than back to WPN under certain circumstances.

Third, any purported pledge or hypothecation of the Memberships is void.

Fourth, the Members will not have any expectation of profit rights. By profits, the court has meant either capital appreciation resulting from the development of the initial investment or a participation in earnings resulting from the use of investors' funds. Due to the fact that the Member Agreement prohibits the transfer of Memberships to a third party and requires that the Memberships be sold back to WPN at a price equal to the price the individual Physician originally paid for them (except in limited circumstances in which the price is fixed at \$____), there is no possibility for a Physician/Member to profit from the ownership of Memberships. Finally, due to the fact that only

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one Membership will be sold to each Physician/purchaser, no member will have the ability to accumulate a larger ownership or voting interest than the other members.

In summary, the Memberships will lack the characteristics identified by the *Landreth* court as traditionally being associated with stock. Physician/Members will not acquire a Membership in order to profit from the holding of such Membership, but will acquire Memberships to derive substantial personal benefits from the services to be provided by WPN.

Since the Memberships will not fall plainly within the usual concept or definition of "stock," consideration must be given to whether the Memberships would otherwise be deemed "securities" by reason of being "investment contracts" or "instruments commonly known as securities" for purposes of Section 61-1-13(22) of the Act. In *Landreth*, the court suggested that the proper test for determining whether a particular instrument which is not clearly within the definition of "stock" as set forth in Section 2(1) of the 1933 Act or which is otherwise of an unusual nature as an "investment contract" or an "instrument commonly known as a security" is the "economic realities" test set forth in *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946). In evaluating the economic realities of a transaction, the test is whether the "scheme involves an investment of money with profits to come solely from the efforts of others." *SEC v. W.J. Howey Co.*, 328 U.S. 293 at 301 (1946). See also *Payable Accounting Corp.*, 667 P.2d 15 at 20.

In a number of no-action letters, the staff of the Securities and Exchange Commission has applied the *Howey* test to transactions similar to the one at issue here and has determined that such transactions do not fall within the definition of a "security." See *Collision Automotive Repair Services*, SEC No-Action Letter (available July 7, 1992); *Certified Physicians of Indiana, P.C.*, SEC No-Action Letter (available June 4, 1990); *Kingsboro Medical Group, P.C.*, SEC No-Action Letter (available October 27, 1989); *Arizona Dental IPA, Ltd.* SEC No-Action Letter (available May 1, 1987); *Northwest Practitioners' Associates, Inc.*, SEC No-Action Letter (available October 16, 1986); *Desert Physician Association, Inc.*, SEC No-Action Letter (available June 23, 1986); *Central Florida Medical Affiliates*, SEC No-Action Letter (available April 22, 1985). These no-action letters delineate the following factors to be used in the *Howey* test: (1) whether membership is held out as a financial investment; (2) whether members will have the requisite knowledge and expertise to evaluate the risks and merits of memberships; (3) the degree of control members exercise; and (4) whether revenues are based on members' own efforts.

The *Howey* test, as explained by the court in *Forman*, "embodies the essential attributes that run through all of the court's decisions defining a security." 421 U.S. at 852. The appellate courts have modified the fourth leg of the *Howey* test to mean that "the effort made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise." *SEC v. Glen W. Turner Enterprises, Inc.*, 474 F.2d 476 (9th Cir. 1973); *Lino v. City Investing Co.*, 487 F.2d 689 (3rd Cir. 1973).

Applying the *Howey* test to the characteristics of interests represented by the Memberships to be offered and sold by WPN, the Memberships will not be an "investment contract" or "other instrument commonly known as a security." The WPN Memberships will be evidences of personal service participation, not an investment. While the Physicians who acquire the Memberships will do so in exchange for money, the Physicians to whom such the Memberships will be offered will be informed not to expect, and will not have any reasonable expectation of deriving, profits from the ownership of the Memberships. Income that is generated by the operation of WPN will be used to fund its general and administrative requirements and its physician practice improvement programs. If excess cash is accumulated, the amount charged will be reduced to reduce the accumulation. However, WPN will

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not pay to its Physician/Members any dividends or make any distributions to them based on their Membership ownership.

The fact that WPN will have the right under the Member Agreement to repurchase the Memberships at the price paid by the Physician to purchase the Memberships, except in certain circumstances when the price is fixed at \$100, coupled with the limitation on distributions on liquidation and dissolution, makes any realization of capital appreciation too speculative and insubstantial to create in the mind of any reasonable purchaser an expectation of profit in the sense found necessary in *Howey*. Purchasers will not be attracted to WPN because of financial returns on the purchase of their Memberships. Rather they will purchase due to the prospect of being members of an integrated managed health care network that will negotiate with payors of health care services. The primary incentive will be the ability of physician health care providers to control their own destiny in an environment that is increasingly being dominated by managed care arrangements that heretofore have typically been controlled by hospitals, insurance companies, or others with established economic power bases. Accordingly, Physician/Members will possess the requisite knowledge and expertise to evaluate the risks and merits of membership in WPN. WPN Physician/Members will exercise control over WPN and will be required to participate actively as a condition of continued membership. Specifically, they will exercise control in the selection of payors with whom WPN contracts and the terms of those contracts. Additionally, Physician/Members will control the qualification and admittance of the Members of WPN.

Finally, any revenues or profits of the Physician/Members will not be derived solely or even substantially from the efforts of others, but rather from the quality and frequency of the direct provision of medical services by the Physicians themselves. The health care service contracts and other arrangements entered into will all be based economically on the personal professional services provided by Physician/Members, whether those services are paid for on a fee-for-service, capitated, or other basis. In *Forman*, the court explained that when a purchaser is motivated by a desire to use or consume the item purchased, the securities laws do not apply. *Forman*, 421 U.S. at 582. Physician/Members of WPN are similar to the cooperative housing common stock purchasers in *Forman* in that their purchase is motivated by a desire to use or consume the item purchased. WPN Physician/Members will use WPN as a means of increasing their own business. The "undeniably significant" effort in producing a Physician/Member's "profit" will be the effort of that individual member through the practice of medicine in substantially the same manner as before joining WPN. The Physician/Members will obtain benefit by practicing more effectively and efficiently, not by any economic interest in WPN in the form of a Membership. Where an enterprise merely allows a professional person to enhance his ability to earn income in the practice of his profession, the relationship avoids the fourth leg of the *Howey* test, thus making the interest under consideration not a "security" within the meaning of the securities laws. *Queens-Long Island Medical Group, P.C.*, SEC No-Action Letter (available November 6, 1990); *Bronx Cross County Medical Group, P.C.*, SEC No-Action Letter (available August 18, 1989); *IPA of Richmond County, Inc.*, SEC No-Action Letter (available November 17, 1986). Accordingly, the Memberships are not "securities" under the *Howey* analysis.

The foregoing "common enterprise" analysis is based on the concept of horizontal commonality where multiple investors pool their investments and receive pro rata profits. See *Wals v. Fox Hill Development Corp.*, ¶ 98,085, p. 98,713 (D.C.E.D. Wisc. 1993). Some courts will also allow vertical commonality to satisfy the "common enterprise" prong of the *Howey* test. Vertical commonality exists where the profits and losses of the investor and the promoter are interdependent. (See *Wals*, at p. 98,714.) Although it does not appear that the vertical commonality analysis is recognized in the Utah courts, if such an analysis were used here, again, a common enterprise would not be found. The individual Physician/Member will realize little if any financial reward from his membership in WPN if he or she is not individually a successful medical practitioner. The organizers and managers

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State of Utah Securities Division
Department of Commerce
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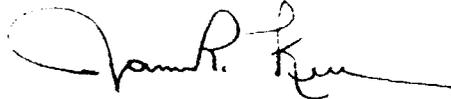
of WPN could be successful in providing an environment in which success could be obtained and yet any one Physician/Member could fail due to his or her individual efforts. It is clear, therefore, that profits and losses of WPN and the individual Physician/Member are not interdependent.

As a general public policy matter, it is noteworthy that the Commission as well as a number of states now have analyzed the legal and practical circumstances surrounding physicians' organizations and with a relatively uniform approach have determined that their organization and operation are unique and outside the parameters of the commercial areas that the securities laws were intended to regulate. The letters cited above support this generalization.

On the basis of the above-stated facts and legal analysis, we request an interpretive response from the Division to the effect that the Memberships of WPN do not constitute "securities" under the definition of that term under the Act.

Very truly yours,

KRUSE, LANDA & MAYCOCK, L.L.C.



James R. Kruse

JRK:sp