ARIZONA CORPORATION COMMISSION

SECURITIES DIVISION
1300 West Washington, Third Floor
Phoenix, AZ 85007-2996
TELEPHONE: (602) 542-4242
FAX: (602) 594-7470

July 22, 1998

Mr. Thomas F. Hyde
The Hyde Law Corporation
One Maritime Plaza, Suite 1600
San Francisco, CA 94111

RE: Stock Farm Club, Inc.
S-56366-NOAC
A.R.S. § 44-1801(23)

Dear Mr. Hyde:

On the basis of the facts set forth in your letter of October 29, 1997, and in telephone discussions with the staff, and in reliance upon your opinion as counsel, the Securities Division will not recommend enforcement action for violation of the registration provisions of the Securities Act of Arizona should the transaction take place as represented.

As this position is premised upon the facts set forth in your letter, it should not be relied on for any other set of facts or by any other person. This response does not express any legal conclusion concerning the applicability of A.R.S. § 44-1801(23).

We have attached a photocopy of your letter for your reference.

Very truly yours,

Michael G. Burton, Sr.

MICHAEL G. BURTON, SR.
Director of Securities

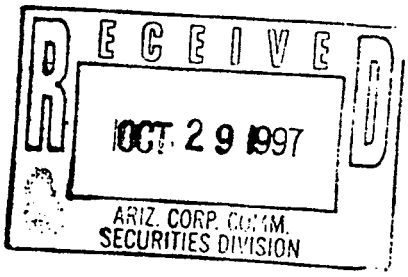
MGB:ctf
Attachment

THE HYDE LAW
CORPORATION

One Maritime Plaza, Suite 1600
San Francisco, California 94111
Telephone: (415) 392-0215
Facsimile: (415) 391-2485

Thomas F. Hyde

October 28, 1997



VIA FEDERAL EXPRESS

Arizona Corporation Commission
Securities Division
1300 West Washington, third Floor
Phoenix, AZ 85007-2996

Re: Stock Farm Club

Dear Arizona Corporation Commission:

We represent Stock Farm Club, Inc. a Montana non-profit corporation, which will own and operate a private golf club and attendant facilities in Hamilton, Montana (the "Club"). I hereby respectfully request that the Arizona Corporation Commission issue a "no-action" or similar interpretative opinion determining that a membership interest in the Club is not a "security" within the meaning of A.R.S. Section 44-1801.22.

BACKGROUND

The Club intends to sell two principal types of memberships: regular memberships and ranch (or social) memberships. Purchasers of memberships will pay an initiation fee to be determined by Stock Farm LLC, which is the owner and developer of the property upon which the Club is located. The amount of the initiation fee will vary depending on demand and other circumstances. It is expected that regular memberships will sell for approximately $40,000 and social memberships for $5,000.

Stock Farm LLC is also the developer of a subdivision that surrounds the Club. Although the Club is a potential amenity for buyers of the lots by virtue of its proximity, lot ownership does not include any right to use the Club or to become a member. However, lot owners are entitled to a priority for consideration on any waiting list for the purchase or sale of a membership.

The Club's board of directors will be appointed by Stock Farm LLC until the earlier of the sale of 300 regular memberships or December 31, 2003. Thereafter, the board of directors will be

elected, with each regular membership entitled to one vote, including those memberships remaining to be sold. Although the regular memberships are proprietary, the board of directors of the Club retains the right to establish the selling price for such membership, as well as the amount of a transfer fee payable to the Club. The offering materials to prospective members make it clear that they should not be purchasing a membership for investment, but rather for social and recreational use. Although the memberships fees will be remitted by the Club to Stock Farm LLC in payment of the purchase of the golf club and related facilities, none of those funds are needed to complete the golf course and the attendant facilities. All funds needed to complete the golf course will come from the existing financial resources of Stock Farm LLC. The Club is approximately 50% completed and is expected to open in the Fall of 1998.

A social membership will entitle such member to use all of the facilities of the Club other than the golf course, golf practice facilities, etc. Social members will be non-voting and will not be proprietary.

DISCUSSION

It is our opinion that the memberships proposed to be sold by the Club do not constitute securities. The term "security" encompasses not only equity instruments (such as shares of stock) and debt instruments (such as notes and debentures) but also a myriad of contractual arrangements which, although on their face not appearing to be traditional securities, involve arrangements, the essence of which is the investment by an essentially passive investor in a business venture managed by another. These investment arrangements all entail the issuance and sale of a participation and a profit-sharing arrangement or an "investment contract" which, of course, are securities. The memberships in the Club do not fit within the concept of investment contracts.

In SEC v. W. J. Howey Co., 328 U.S. 293 (1946), the Supreme Court held that "an investment contract for purposes of the Securities Act means a contract, a transaction or a scheme whereby (1) a person invests his money (2) in a common enterprise and (3) is led to expect profits (4) solely from the efforts of the promoter or a third party ...." 328 U.S. at 298-99. While parts (1) and (2) of the Howey test have remained relatively constant over the years, parts (3) and (4) have undergone change through subsequent judicial interpretation.

The Supreme Court case that perhaps best delineates the scope of the term "investment contract" was United Housing

Foundation, Inc. v. Forman, 421 U.S. 837 (1975). Forman involved the sale of shares of a low-income co-op. A purchaser had to buy "shares" in an affiliated company. The sole purpose of acquiring the shares was to enable the purchaser to occupy an apartment. The shares were explicitly applied to the apartment. Any tenant who wanted to terminate his or her tenancy, or who was forced to move out, had to offer his or her stock to the issuer at its initial selling price. In the event the issuer refused to repurchase the stock, the tenant could not sell it to a third party for more than the initial purchase price plus a fraction of the portion of the mortgage he or she had paid off. The court emphasized the "economic realities" of the transaction and held that the co-op stock did not constitute an investment contract and, hence, did not have to be registered.

In discussing the investment contract issue, the Court stated,

> "The touchstone [of an investment contract] is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others. By profits, the Court has meant either capital appreciation, ... or a participation in earnings resulting from the use of investors' funds .... In such cases the investor is 'attracted solely by the prospects of a return' on his investment [citing Howey]. By contrast, when a purchaser is motivated by a desire to use or consume the item purchased ... the securities laws do not apply." Forman at 852-853.

With respect to memberships in the Club, any profit potential is highly remote and the main motivation is clearly the use of the facilities. Although purchasers of memberships may be able to eventually sell their memberships, any sale is subject to severe restrictions. The Club and not the member sets the purchase price. Because the Club may impose a transfer fee of any amount, there should be no realistic expectation of a profit. As with most private clubs, transfers of memberships will not be permitted except to a candidate who has received the prior approval of the Club's membership committee. In addition, until all original memberships have been sold, a purchasing member who desires to transfer his or her membership may only do so at the rate of one existing membership for every ten original memberships that are sold by the Club.

In Tcherepnin v. Knight, 389 U.S. 332 (1967), the Court identified the right to receive "dividends contingent upon an

apportionment of profits" as the most common feature of stock (389 U.S. at 339). Further, in Landreth Timber Co. v. Landreth, 471 U.S. 681 (1985), the Court set forth several other characteristics traditionally associated with stock: (i) negotiability, (ii) the ability to be pledged or hypothecated, (iii) voting rights in proportion to the number of shares owned, and (iv) the ability to appreciate in value. 471 U.S. at 686.

Memberships in the Club do not have dividend or distribution of income rights and may not be pledged or hypothecated. In addition, memberships are not transferable, except under certain limited circumstances pursuant to the restrictions set forth above. Although memberships conceivably could increase in value, each member will be informed, prior to purchasing a membership, that the acquisition of the membership should be made only for his or her personal use and not for investment or with any expectation of economic benefit.

Each prospective member will be expected to sign a subscription agreement in which such person represents, among other things, that the person recognizes "that the Club ... will not be operated as a business for profit, but rather as a social and recreational club," and that such person "will not be able to resell readily the membership purchased hereunder because ... the club will control and set the selling price of the memberships and will permit a sale only to approved individuals ...."

The ability of a member to realize a profit is so restricted and contingent that it cannot reasonably form the basis of a profit motive to acquire a membership. As in Forman, the overwhelming motivation for a person's acquiring a membership will be a "desire to use or consume the item purchased." Here, a member's primary expectation is to acquire a membership for the purpose of enjoying the golf and recreational facilities, not for the prospect of a return on investment. Therefore, the memberships should not be treated as equivalent to "stock."

The Securities and Exchange Commission has issued a long line of no action letters with respect to facts substantially similar to the facts described above and, in particular, where members could possibly realize a profit on the transfer of memberships under restricted and limited circumstance. See, The Club at Cuscowilla, Inc. (April 18, 1997); Lockwood Folly Country Club, Inc. (April 3, 1996); Bent Creek Country Club, Inc (September 23, 1993); Whale Rock Country Club, Inc. (February 26, 1993); Fisher Island Club, Inc. (January 27, 1993); River Hills Country Club, Inc. (November 4, 1992); Lake Forest Country Club, Inc. (August 3, 1992); WGS, Inc. (June 26, 1992); Garrison Golf

Club, Inc. (March 20, 1992); River's Bend Golf and Country Club, Incorporated (February 3, 1992); Whispering Oaks Equity Membership Club, Incorporated (February 8, 1991); Beaverbrook Golf and Country Club, Inc. (May 30, 1990); The Windsor Club, Inc. (May 17, 1990); and Ibis Country Club, Incorporated (March 30, 1990).

Finally, the Supreme Court has suggested that the "risk capital test," a test which was sometimes applied by certain courts in determining what is a "security" as first articulated in Silver Hills Country Club v. Sobieski, 55 Cal. 811, 361 P.2d 906 (Cal. 1961), offers no useful analysis once a Howey test has been made; rather, the "'risk capital' approach ... is virtually identical to the Howey test." Reves v. Ernst & Young, 494 U.S. 56, 64 (1990). This is so because a risk capital test requires that the seller solicit "risk capital for which to develop a business for profit." 361 P.2d at 908.

To the extent that the risk capital test for determining the existence of a security may still influence the evaluation of this request, we believe that the memberships in the Club would not be deemed to be securities under that test. In the Silver Hills case, the developer used the proceeds from the sale of memberships as the primary means of financing the construction of the facilities. Moreover, the club in Silver Hills was to be organized as a "for profit" business, whereas the Stock Farm Club is a nonprofit organization. In the present situation, neither the Club nor the promoter is dependant upon the proceeds of the sale of memberships in order to construct or operate the Club. The purchasers of memberships are not being solicited to provide the risk capital with which to complete the Club's facilities. Stock Farm LLC has the financial ability and the capacity to complete the Club's facilities independent of the receipt of any proceeds from the sale of memberships.

The foregoing structure is consistent with previous no-action letters involving the sale of club memberships in which the club was permitted to use proceeds from the sale of memberships to construct the club facilities, so long as the completion of such facilities was not dependent on the sale of such memberships. See, e.g., The Club at Cuscowilla, Inc. (April 18, 1997); Olde Florida, Ltd. (November 30, 1990); Cutter Sound Yacht & Golf Club, Inc. (July 30, 1990); Laurel Creek Country Club, Inc. (November 3, 1989); The Black Diamond Club Incorporated (November 20, 1989); River Run Club (August 18, 1988); River Oak's Club Incorporated (July 27, 1987); and Palm-Aire Country Club at Sarasota, Inc. (October 17, 1985).

CONCLUSION

In view of the foregoing, we respectfully request your confirmation that the Arizona Corporation Commissioner will not recommend any action if any memberships are offered or sold in the manner described herein without prior notification or registration.

Stock Farm LLC plans to commence offering memberships to Arizona residents in the Club promptly upon receipt of a favorable response from your office. We would appreciate your faxing your response to the undersigned at (415) 391-2485. If, for any reason, you conclude you cannot respond affirmatively to our request for a no-action letter, we would appreciate the opportunity to discuss the matter with you prior to the preparation of your response and ask you to call the undersigned at (415) 392-0215.

Thank you for your consideration.

Very truly yours,

THE HYDE LAW CORPORATION

Thomas F. Hyde

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