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29 June 2004

Jennifer A. Lewis, Esq.  
GARDNER CARTON & DOUGLAS  
1301 K Street, N.W.  
Suite 900, East Tower  
Washington, D.C. 20005-3317

Re: American Pharmacy Cooperative, Inc.  
No-Action Letter No. 04-90000322-NA005

Dear Ms. Lewis:

We are in receipt of your letter dated 23 June 2004 wherein you request that the Arkansas Securities Department (the Department) adopt a no action position regarding the stock of your client, American Pharmacy Cooperative, Inc. (the Cooperative), opining that it is not a security within the definition of security found in the Arkansas Securities Act (the Act) at Ark. Code Ann. § 23-42-102(15)(A) (Supp. 2003).

You have represented that the Cooperative is an Alabama corporation run as a cooperative for retail pharmacists. Its primary purpose is to enable member pharmacists to aggregate their buying power and negotiate discounts on the purchase of pharmaceutical products from their manufacturers. The negotiation of prices of products from various manufacturers is conducted by Dohman Distribution Partners Southeast (the Vendor), a limited liability company in Birmingham, Alabama. Member pharmacists order their products directly from the Vendor and pay a price representing the negotiated price, a mark-up percentage, plus 1%, which is remitted to the Cooperative. From this 1% mark up, the Cooperative pays an annual patronage dividend to member pharmacists based not on the amount of stock owned, but on the volume of business transacted with the Cooperative.

To be a member of the Cooperative, your letter states that retail pharmacists must purchase 100 shares of common stock in the Cooperative for \$1,500 and pay a one-time, non-refundable \$500 membership fee. Regardless of the number of shares a member has, you state, including the shares of any member's affiliates, each member has only one vote on all matters coming before the Cooperative, and this is true, also, regardless of the amount of business each member does with the Cooperative. According to the articles of incorporation and the bylaws, the stock is not transferable and can only be sold back to the Cooperative at the price the member originally paid for it. The redemption or buying back of the stock must take place when the

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member dies, when the member ceases doing business as a retail pharmacist, when a member ceases to do business through the Cooperative or when a member is determined by the Cooperative's board of directors to be out of compliance with the Cooperative's rules and standards. No dividends are paid on the stock, you state, and the only instance in which a member could receive for his or her stock more than was originally paid for it is in the unlikely event of liquidation of the Cooperative's assets and a pro rata distribution to members according to the shares of stock issued.

Citing *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837 (1975), holding that the name, stock, does not always warrant the conclusion that an instrument is a security, several no action letters of the Department and the Securities and Exchange Commission, you opine that shares of commons stock in the Cooperative are not securities as defined in the Act at § 23-42-102(15)(A) and ask that the Department issue a no action letter agreeing with that position.

You cite *Forman* for the five characteristics it identifies of stock as a security, to wit: 1) the right to receive dividends as an apportionment of profits, 2) negotiability, 3) the ability of the stockholder to pledge or hypothecate shares, 4) voting rights in proportion to the number of shares owned and 5) the capacity of the shares to appreciate in value.

The definition of security found at § 23-42-102(15)(A) is virtually identical to that under federal law. *Casali v. Schultz*, 292 Ark. 602, 732 S.W.2d 836 (1987); *Hogg v. Jerry*, 299 Ark. 283, 773 S.W.2d 84 (1989). Merely naming an instrument stock has also been held not to be determinative in Arkansas law. See *Cook v. Wills*, 305 Ark. 442, 808 S.W.2d 758 (1991). Five significant factors inherent in securities under the Act have been identified:

1) the investment of money or money's worth, 2) investment in a venture, 3) the expectation of some benefit to the investor as a result of the investment, 4) contribution towards the risk capital of the venture, and 5) the absence of direct control over the investment or policy decisions concerning the venture

*Cook v. Wills*, *supra*, 305 Ark. at 447, citing *Smith v. State*, 266 Ark. 861, 587 S.W.2d 50 (1979), and *Schultz v. Rector, Phillips, Morris, Inc.*, 261 Ark. 769, 552 S.W.2d 4 (1977).

These are the five factors that define an investment contract set forth in *Securities and Exchange Commission v. Howey*, 328 U.S. 293 (1946), which is also mentioned in your letter.

The crux of your position is that the shares of stock of the Cooperative in question are not securities either as traditional stock, or as an investment contract.

From the representations made in your letter, we can conclude that there is no investment

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of money in a venture with the expectation of profits to be derived solely from the efforts of others. The instrument purchased cannot be freely bought and sold, even though it is named a stock. There is but one way this stock can be sold, and that is back to the Cooperative for the same amount the member purchased it. There is also only one way that the member can receive more money for his or her stock than he or she paid for it, and that is in a pro rata distribution of assets upon dissolution and liquidation of assets. The Staff of the Department agrees that this possibility is not enough to make the stock in question negotiable. We know also from your letter that no dividends are payable on this stock, there are no voting rights attached to each share of stock and the stock will not appreciate in value.

It thus appears that the purchase of the Cooperative's stock in this situation is in the nature of a membership fee than an investment in traditional stock. What the purchasers of this stock expect is not profits, but lower prices for the necessary supplies, inventory and equipment needed for a retail pharmacy. What is shown is not a profitable business, but a cooperative association of professionals.

The Department has taken no actions positions in similar situations in at least four other instances, to wit: *Associated Pharmacies, Inc.*, No. 01-010 (18 December 2001), *TruServ Corporation*, No. 01-005 (6 July 2001), *Energy Co-Opportunity, Inc.*, No. 00-001 (4 January 2000), and *Professional Veterinary Products, Ltd.*, No. 96-13 (3 October 1996).

Accordingly, the Staff will recommend that the Arkansas Securities Commissioner take no enforcement action against American Pharmacy Cooperative, Inc. for not registering its stock or filing a proof of exemption for it if the facts remain as stated in your letter.

Please note that the position of the Department is based solely upon the representations made to us in your letter and applies only to the facts set out therein. Different facts or circumstances might and often would require a different response. The position expressed deals only with anticipated enforcement action by the Department and does not purport to be a legal opinion.

With best regards,

(signed)

Theodore Holder  
ASSISTANT SECURITIES COMMISSIONER