

owned subsidiary of FSAH, a New York corporation.<sup>1</sup> FSAH is a holding company primarily engaged, through its direct wholly-owned subsidiary, Financial Security Assurance Inc. ("FSA"), in the financial guarantee insurance business. FSAH is an indirect, approximately 98.9%-owned subsidiary of Dexia S.A., a publicly owned Belgium corporation ("Dexia"), the shares of which are listed and traded on Euronext Brussels, Euronext Paris and the Luxembourg stock exchange. Dexia is primarily engaged through its operating subsidiaries in the banking and investment management business in Europe.

2. FSA is a New York stock insurance corporation that is a leading insurer of asset-backed and municipal obligations. FSA is licensed to do business as an insurance company in all 50 states, the District of Columbia, the Commonwealth of Puerto Rico, Guam and the U.S. Virgin Islands. FSAH depends primarily on dividends and other payments from FSA to pay dividends on its capital stock, to pay principal and interest on its indebtedness and to pay its operating expenses.

3. Applicant was organized to issue and sell municipal investment contracts and similar investment agreements (together, the "MICs"). Applicant presently sells MICs on a private placement basis primarily to state or local government entities or agencies and trustees for bond issues of such entities or agencies (collectively, the "MIC holders") for the investment of proceeds from municipal bond offerings.

4. MICs are debt securities that provide for an agreed-upon rate of return on the principal invested. MICs may be collateralized by U.S. Treasury or other high quality securities. Municipal bond issuers find MICs attractive because their bonds are often issued to finance projects for which the issuer does not need the full proceeds of the issue immediately. A MIC holder may also purchase a MIC as a means of investing amounts on deposit in debt service reserve funds and other similar funds held by the MIC holder. MICs provide the municipal bond issuer with a guaranteed yield that is advantageous relative to the interest rate on the bonds

and can be structured to provide draw-downs to meet the municipality's needs.

5. Because of restrictions on their permitted investments, some municipalities are expected to request that Applicant enter into MICs styled as repurchase agreements (each, a "Repo"), which would provide such municipalities with the economic equivalent of entering into a collateralized MIC. Applicant considers entering into such Repos to be equivalent to issuing a MIC in the form of a collateralized investment contract and will treat the proceeds generated thereby the same as any other proceeds raised in a debt issuance (hereinafter, any reference to "MIC" shall include such Repos).

6. The proceeds of MIC sales will be loaned to FSAH and/or its direct and indirect subsidiaries (collectively, the "Recipients") for use in financing their respective business activities. It is anticipated that substantially all of the proceeds from the MICs will be loaned by Applicant to the Recipients contemporaneously with the issuance of the related MIC, but in no event will less than 85 percent of such proceeds be loaned later than six months after Applicant's receipt of such proceeds. It also is anticipated that substantially all loans to Recipients will be collateralized by the Recipients themselves.

7. Pursuant to an insurance and indemnity agreement with FSA (the "Agreement"), Applicant's obligations under each MIC issued by it will be fully insured by a financial guarantee policy (each, a "Policy") issued by FSA. The Policy provides that in the event of default by Applicant on the payment of principal, premium (if any) and interest on the MIC, FSA will make the scheduled payment. In addition, the MIC holder may institute legal proceedings directly against FSA to enforce such payment without first proceeding against Applicant. The Agreement requires Applicant to reimburse FSA for any payments made by FSA under the Policies.

8. In order to secure its performance under the Agreement, Applicant will rehypothecate all collateral received in respect of loans of proceeds to Recipients either directly to FSA or to one or more trustees, custodians, collateral agents or other similar agents acting for the benefit of FSA under one or more trust, custody, collateral agency or other similar agency agreements. With respect to MICs in the form of collateralized investment contracts or Repos, however, the collateral pledged to secure the related loan of proceeds will be rehypothecated to the MIC holder.

9. Applicant may come within the definition of investment company under section 3(a) of the Act to the extent that its loans to FSAH and the other Recipients may be considered as investing or reinvesting in debt securities of FSAH and the other Recipients. Applicant currently is relying on the exception from the Act provided by section 3(c)(1). It will be unable to continue to do so, however, at such time as the 100 owner limit contained therein is exceeded or if Applicant were to make a public offering of its securities.

#### **Applicant's Legal Analysis**

1. Applicant requests an order under section 6(c) of the Act for an exemption from all provisions of the Act. Rule 3a-5 under the Act provides an exemption from the definition of investment company for certain companies organized primarily to finance the business operations of their parent companies or companies controlled by their parent companies.

2. Rule 3a-5(b)(2)(i) in relevant part defines a "parent company" to be a corporation, partnership, or joint venture that is not considered an investment company under section 3(a) or that is excepted or exempted by order from the definition of investment company by section 3(b) or by the rules or regulations under section 3(a). Applicant states that because FSAH relies on an exception in section 3(c)(6) of the Act as an insurance holding company, FSAH would not qualify as an eligible parent company under rule 3a-5.

3. Rule 3a-5(b)(3)(i) in relevant part defines a "company controlled by the parent company" to be a corporation, partnership, or joint venture that is not considered an investment company under section 3(a) of the Act or that is excepted or exempted by order from the definition of investment company by section 3(b) of the Act or by the rules and regulations under section 3(a). FSAH engages in certain activities (including certain investment activities) through wholly-owned subsidiaries that have no outstanding securities other than those owned directly or indirectly by FSAH. Such subsidiaries would be eligible for exemption under rule 3a-3 under the Act, except that FSAH, as a section 3(c)(6) exempt company, is not an eligible parent of a rule 3a-3 exempt company.<sup>2</sup> In addition, Applicant might

<sup>1</sup> Applicant also requests relief for any other wholly-owned finance subsidiary of FSAH that FSAH establishes in the future. Applicant is the only wholly-owned finance subsidiary of FSAH that presently intends to rely on the requested order. Any other wholly-owned finance subsidiary of FSAH that subsequently relies on the requested order will comply with the terms and condition stated in the application.

<sup>2</sup> Rule 3a-3 generally exempts an issuer from the definition of investment company if all of its outstanding securities (other than short-term paper, directors' qualifying shares, and debt securities owned by the Small Business Administration) are owned by an eligible parent company. A parent