



## **Section 3(a)(2) Bank Note Programs**

**Teleconference**

**Thursday, February 16, 2017**

**12:00 PM – 1:00 PM EST**

**Presenters:**

**Bradley Berman, Of Counsel, Morrison & Foerster LLP**

**Jack McSpadden, Jr., Managing Director, Citigroup Global Markets Inc.**

- 1. Presentation**
- 2. “Frequently Asked Questions about Section 3(a)(2) Bank Note Programs”**

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# Bank Note Programs

Presented By

Bradley Berman  
Morrison & Foerster LLP

Jack D. McSpadden, Jr.  
Citigroup Global Markets Inc.

**February 16, 2017**

# Topics for Presentation

- Section 3(a)(2) bank note programs
- Rule 144A bank note programs

# Bank Debt Financing Activities

- Type of bank debt issuances
  - Senior unsecured debt
  - Senior secured debt
  - Subordinated debt
  - Structured debt (e.g., equity-linked and commodity-linked notes)
- Issuing entities:
  - U.S. banks
  - Home offices of foreign banks
  - U.S. branches of foreign banks
  - Other affiliated entities of foreign banks
  - U.S. branches of foreign banks as guarantors
- Issuance formats
  - Section 3(a)(2) offerings
  - Rule 144A offerings

# Section 3(a)(2) Offerings

# Section 3(a)(2) Bank Note Programs

A Section 3(a)(2) bank note program is a medium-term note program that enables an issuing bank to offer debt securities on a regular and/or continuous basis.

- The issuer (or a guarantor of the notes) must be a “bank,” as defined in Section 3(a)(2) of the Securities Act of 1933.
- Bank note programs are exempt from registration under the Securities Act.

# Types of Securities Issued

- Senior or subordinated.
- Fixed or floating rate, zero-coupon, non-U.S. dollar denominated, amortizing, multi-currency or indexed (structured) securities.
  - Common reference rates for floating rate bank notes include LIBOR, EURIBOR, the prime rate, the Treasury rate, the federal funds rate and the CMS rate.
- Most bank note programs are rated “investment-grade” by one or more nationally recognized rating agencies.
- Section 3(a)(2) structured notes can be linked to reference assets not always seen in registered programs:
  - complex underlying assets;
  - credit-linked notes;
  - small-cap stocks; and
  - non-U.S. stocks that do not trade on U.S. exchanges.

# Section 3(a)(2) and Offerings by Banks

- Section 3(a)(2) of the Securities Act exempts from registration under the Securities Act any security issued or guaranteed by a “bank.”
- Basis: banks are highly regulated, and provide adequate disclosure to investors about their finances in the absence of federal securities registration requirements. Banks are also subject to various capital requirements that may increase the likelihood that holders of their debt securities will receive timely payments of principal and interest.



# What Is a “Bank”?

- Under Section 3(a)(2), the institution must meet both of the following requirements:
  - It must be a national bank or any institution supervised by a state banking commission or similar authority; and
  - Its business must be substantially confined to banking.
- Examples of entities that do not qualify:
  - Bank holding companies
  - Finance companies
  - Investment banks
  - Foreign banks
  - Representative office of a non-U.S. bank
- Regulated U.S. branches and agencies of foreign banks may qualify.

# Guarantees

- Another basis for qualification as a bank: securities *guaranteed* by a bank.
  - Not limited to a guaranty in a legal sense, but also includes arrangements in which the bank agrees to ensure the payment of a security.
  - The guaranty or assurance of payment, however, has to cover the entire obligation; it cannot be a partial guarantee or promise of payment, and it must be unconditional.
  - Again, guarantees by foreign banks (other than those of an eligible U.S. branch or agency) would not qualify for this exception.
  - The guarantee is a legal requirement to qualify for the 3(a)(2) exemption; investors will not be looking to the U.S. branch for payment/credit. Investors will look to the home office.
  - Finance companies can issue under Section 3(a)(2), if the securities are guaranteed by a bank.

# Non-U.S. Banks/U.S. Offices

- U.S. branches/agencies of foreign banks are conditionally entitled to rely on the Section 3(a)(2) exemption.
- 1986: the SEC takes the position that a foreign branch/agency will be deemed to be a “national bank” or a “banking institution organized under the laws of any state” if “the nature and extent of federal and/or state regulation and supervision of that particular branch or agency is substantially equivalent to that applicable to federal or state chartered domestic banks doing business in the same jurisdiction.”
- As a result, U.S. branches/agencies of foreign banks are frequent issuers or guarantors of debt securities in the U.S. Most issuances or guarantees occur through the NY branches of these banks.
- A list of U.S. branches of foreign banks by branch size can be found at <http://www.federalreserve.gov/releases/iba/201206/bycntry.htm>

## **Examples of Issuing Entities:**

- U.S. branch as direct issuer: UBS, CS, NAB, CBA and ANZ
- U.S. branch as guarantor, headquarters as issuer: BNP, Rabo, SocGen, Svenska
- U.S. branch as guarantor, SPV/Cayman branch as issuer: BNP
  - More banks are using a guarantee structure to allow greater flexibility for use of proceeds.

## **Which Regulator?**

- Most U.S. branches have elected the N.Y. State Department of Financial Services (“NYDFS”) as their primary regulator with their secondary regulator the Federal Reserve.
- Some U.S. branches have opted for the Office of the Comptroller of the Currency (“OCC”) as their primary regulator.

# OCC Registration/Disclosure

- National banks or federally licensed U.S. branches/agencies of foreign banks regulated by the OCC are subject to the OCC's securities offering (Part 16) regulations.
- Part 16 of OCC regulations provides that these banks or banking offices may not offer and sell their securities until a registration statement has been filed and declared effective with the OCC, unless an exemption applies.
- An OCC registration statement is generally comparable in scope and detail to an SEC registration statement; as a result, most bank issuers prefer to rely upon an exemption from the OCC's registration requirements. Section 16.5 provides a list of exemptions, which includes:
  - Regulation D offerings
  - Rule 144A offerings to QIBs
  - Regulation S offerings outside of the United States
- General solicitation would be allowed for Regulation D offerings and Rule 144A offerings; the Rule 506 "bad actor" disqualifications would also apply.

# Part 16.6 of the OCC Regulations

- 12 CFR 16.6 provides a separate partial exemption for offerings of “non-convertible debt” to accredited investors in denominations of \$250,000 or more.
- Federal branches/agencies, as issuers, may rely on this exemption by furnishing to the OCC parent bank information which is required under Exchange Act Rule 12g3-2(b), and to purchasers the information required under Securities Act Rule 144A(d)(4)(i).
- The securities are “investment grade” – the new definition focuses on the probability of repayment, rather than an external investment-grade rating (Dodd-Frank Act requirement).
- The offering document and any amendments are filed with the OCC no later than the fifth business day after they are first used.

# Accredited Investors

Most bank notes are sold to institutional accredited investors:

- Banks, dealers, insurance companies, registered investment companies or business development companies, small business investment companies and government and employee benefit plans;
- Private business development companies;
- IRC Section 501(c)(3) entities, corporations, business trusts or partnerships;
- Trusts directed by sophisticated persons; and
- Any entity in which all equity owners are accredited investors.

Directors, executive officers or general partners of the issuer of the bank notes and high net worth individuals are also accredited investors, but bank notes are generally not sold to natural persons.

# FDIC Policy Statement

Statement of Policy Regarding the Use of Offering Circulars in Connection with Public Distribution of Bank Securities for state non-member banks (the “FDIC Policy”)

Which banks are affected?

- State banks and state-licensed branches of foreign banks with insured deposits.

What does the FDIC Policy do?

- Requires that an offering circular include prominent statements that the securities are not deposits, are not insured by the FDIC or any other agency, and are subject to investment risk.
- States that the offering circular should include detailed prospectus-like disclosure, similar to the type contemplated by Regulation A or the offering circular requirements of the former Office of the Thrift Supervision (the “OTS Regulations”).
  - The OTS Regulations require minimum denominations of \$100,000.
  - The FDIC Policy has not been updated to reflect the elimination of the OTS.
  - Bank issuers include offering circular disclosure that is more detailed than that required by the FDIC Policy.



# New York Regulatory Requirements

New York branches or agencies of foreign banks should contact the NYDFS prior to issuing bank notes.

- An agency of a foreign bank subject to New York banking regulations would have to obtain a pre-offer no-objection letter from the Superintendent of the NYDFS, and would be able to sell only to certain authorized institutional purchasers in minimum denominations of \$100,000.
- New York branches of foreign banks issue bank notes in \$250,000 minimum denominations in order to avoid the notes being viewed by a regulator as an impermissible retail deposit.
  - This limitation does not apply when the New York branch is a guarantor and the issuing entity is the foreign bank.

# FINRA Requirements

- Even though securities offerings under Section 3(a)(2) are exempt from registration under the Securities Act, public securities offerings conducted by banks must be filed with the Financial Industry Regulatory Authority for review under Rule 5110(b)(9), unless an exemption is available.
- Exemption: the issuer has outstanding investment grade rated unsecured non-convertible debt with a term of issue of at least four years, or the non-convertible debt securities are so rated.

- If an affiliated dealer is an agent for the offering, there is “prominent disclosure” in the offering document with respect to the conflict of interest caused by that affiliation and the bank notes are rated investment grade or in the same series that have equal rights and obligations as investment grade rated securities, then no filing will be required.
- Transactions under Section 3(a)(2) must also be reported through FINRA’s Trade Reporting and Compliance Engine. TRACE eligibility provides greater transparency for investors. Rule 144A securities are also TRACE reported.

# Denominations

- The 3(a)(2) exemption does not require specific minimum denominations in order to obtain the exemption.
- However, for a variety of reasons, denominations may at times be significantly higher than in retail transactions:
  - Offerings targeted to institutional investors.
  - Complex securities.
  - Relationship to 16.6's requirement of \$250,000 minimum denominations.
- New York regulated agencies and branches.

# Blue Sky Regulation

- Securities issued under Section 3(a)(2) are considered “covered securities” under Section 18 of the Securities Act.
- However, because bank notes are not listed on a national securities exchange, states may require a notice filing and a fee in connection with an offering of bank notes.
- Generally, blue sky filings are not needed in any state in which the securities are offered.
- State blue sky laws should be examined to ensure that either no notice filing or fee is required, or the state’s existing exemption for securities issued by banks does not require a filing.
- A state may not view an agency of a foreign bank, whose securities are eligible for the Section 3(a)(2) exemption, as within the state’s exemption for securities issued by banks.
- Rule 144A offerings of bank notes will fall within a state’s institutional purchaser exemption.

# Section 3(a)(2) Offering Documentation

- The offering documentation for bank notes is similar to that of a registered offering.
- Base offering document, which may be an “offering memorandum” or an “offering circular” (instead of a “prospectus”).
- For foreign issuers:
  - IFRS financials or “home country” GAAP financials are acceptable;
  - Consider whether a reconciliation footnote or explanation is helpful if non-US GAAP or non-IFRS is used;
  - US GAAP financials may be used;
  - Annual audited and at least semi-annual unaudited financial statements; and
  - Consider including Guide 3 statistical disclosures.
- The base document is supplemented for a particular offering by one or more “pricing supplements” and/or “product supplements.”
- These offering documents may be supplemented by additional offering materials, including term sheets and brochures.

# Rule 144A Offerings

# Why Are Rule 144A Offerings Attractive to Non-U.S. Banks?

- Rule 144A provides a clear safe harbor for offerings to institutional investors.
- Does not require extensive ongoing registration or disclosure requirements.
- “Benchmark” sized issuances have good liquidity in the Rule 144A market.
- A U.S. bank may use a Rule 144A program for marketing reasons – a desire to be clearly identified with the QIB market.
- OCC Part 16.5: OCC regulated banks can issue in minimum denominations of less than \$250,000 (a Section 3(a)(2) exempt security issued as a Rule 144A transaction).



# Rule 144A – Overview

- Rule 144A provides a non-exclusive safe harbor from the registration requirements of Section 5 of the Securities Act for resales of restricted securities to “qualified institutional buyers” (QIBs).
- The premise: not all investors are in need of the protections of the prospectus requirements of the Securities Act.
- The rule applies to offers made by persons other than the issuer of the securities (i.e., “resales”).
- The rule applies to securities that are not of the same class as securities listed on a U.S. securities exchange or quoted on an automated inter-dealer quotation system.
- A reseller may rely on any applicable exemption from the registration requirements of the Securities Act in connection with the resale of restricted securities (such as Regulation S or Rule 144).

# Types of Rule 144A Offerings

- Rule 144A offering for an issuer that is not registered in the U.S. – usually a standalone.
- Rule 144A continuous offering program
  - Used for repeat offerings, often by financial institution and insurance company issuers, to institutional investors.
  - Often used for structured products sold to QIBs.

# How Are Rule 144A Offerings Structured?

- The issuer initially sells restricted securities to investment bank(s) as “initial purchasers” in a Section 4(a)(2) or Regulation D private placement.
- The investment bank reoffers and immediately resells the securities to QIBs under Rule 144A.
- Issuer → Initial Purchaser → QIBs
- Often combined with a Regulation S offering.

# Conditions for Rule 144A Offering

- Reoffers or resales only to a QIB, or to an offeree or purchaser that the reseller reasonably believes is a QIB.
- Reseller must take steps to ensure that the buyer is aware that the reseller may rely on Rule 144A in connection with such resale.
- The securities reoffered or resold (a) when issued were not of the same class as securities listed on a U.S. national securities exchange or quoted on a U.S. automated inter-dealer quotation system and (b) are not securities of an open-end investment company, UIT, etc.
- For an issuer that is not an Exchange Act reporting company or exempt from reporting pursuant to Rule 12g3-2(b) under the Exchange Act, the holder and a prospective buyer designated by the holder must have the right to obtain from the issuer, upon the holder's request, certain reasonably current information.

# What Is a QIB?

- The following qualify as “QIBs”:
  - Any corporation, partnership or other entity (but not an individual) that owns and invests on a consolidated basis \$100 million in the aggregate in securities of non-affiliates (other than bank deposits and loan participations, repurchase agreements and securities subject thereto, and currency, interest rate and commodity swaps);
  - Registered dealers that own or invest \$10 million of such non-affiliate securities or are engaged in “riskless principal transactions” on behalf of QIBs (to qualify, the QIB must commit to the broker-dealer that the QIB will simultaneously purchase the securities from the broker-dealer);
  - Any investment company that is part of a “family” that has the same investment adviser and together own \$100 million of such non-affiliate securities; and
  - Any U.S. or foreign bank or S&L that owns and invests on a consolidated basis \$100 million in such non-affiliate securities and has a net worth of at least \$25 million
- A QIB can be formed solely for purpose of conducting a Rule 144A transaction.

# How Can a Reseller Ascertain a Person Is a QIB?

- A reseller may rely on the following (as long as the information is no more than 16 months old):
  - the purchaser's most recent publicly available annual financial statements;
  - information filed with the SEC or another government agency or self-regulatory organization;
  - information in a recognized securities manual, such as Moody's or S&P;
  - certification by the purchaser's chief financial or other executive officer specifying the amount of securities owned and invested as of the end of the purchaser's most recent fiscal year; and
  - a QIB questionnaire.
- The SEC acknowledges that the reseller may use other information to establish a reasonable belief of eligibility.

# Rule 144A – Legending

- The reseller will make the buyer aware that the security is a Rule 144A security by:
  - Legending the security (i.e., the security must include language that it is not registered under the Securities Act);
  - Including an appropriate statement in the offering memorandum;
  - Obtaining an agreement that the purchaser understands that the securities must be resold pursuant to an exemption or registration under the Securities Act; and
  - By obtaining a restricted CUSIP number

# Current Information Requirements

- For securities of a non-public company, the holder and a prospective purchaser designated by the holder have the right to obtain from the issuer, upon request, the following information:
  - A brief statement of the nature of the business of the issuer, and its products and services;
  - The issuer's most recent balance sheet and profit and loss and retained earnings statements, and similar financial statements for such part of the two preceding fiscal years as the issuer has been in operation; and
  - The financial statements should be audited, to the extent reasonably available.
- The information must be “reasonably current.”



# Rule 159: “Time of Sale Information”

- Although Rule 159 under the Securities Act is not expressly applicable to Section 3(a)(2) or Rule 144A offerings, many investment banks apply the same treatment, in order to help reduce the risk of liability.
- Use of term sheets and offering memoranda supplements, to ensure that all material information is conveyed to investors at the time of pricing.
- Counsel is typically expected to opine as to the “disclosure package,” as in the case of a public offering.

# Comparison of Section 3(a)(2) to Rule 144A

	Section 3(a)(2)	Rule 144A
<b>Required issuer:</b>	Need a US state or federal licensed bank as issuer or as guarantor	No specific issuer or guarantor is required
<b>Exemption from the Securities Act:</b>	Section 3(a)(2)	Section 4(a)(2) / Rule 144A
<b>FINRA Filing Requirement:</b>	Subject to filing requirement and payment of filing fee (but an investment grade rating exemption is available)	Not subject to FINRA filing
<b>Blue Sky:</b>	Generally exempt from blue sky regulation	Generally exempt from blue sky regulation
<b>Listing on a non-U.S. exchange:</b>	May be listed if issued in compliance with Part 16.6	No
<b>“Restricted”</b>	No; considered “public” and therefore eligible for bond indices, TRACE reporting	Yes, but subject to TRACE reporting

	Section 3(a)(2)	Rule 144A
<b>Required governmental approvals:</b>	Banks licensed by the OCC are subject to the Part 16.6 limitations, unless an exemption is available.	Generally none.
<b>Permitted Offerees:</b>	All investors, which means that there is a broader market. However, banks licensed by the OCC are subject to the Part 16.6 limitations, unless an exemption is available. Generally, sales to institutional “accredited investors.”	Only to QIBs. No retail.
<b>Minimum denominations:</b>	All denominations, subject to some limitations. However, banks licensed by the OCC are subject to a \$250,000 minimum denomination requirement under Part 16.6.	No minimum denominations requirement. Generally set at \$200,000 for Regulation S/Prospectus Directive purposes.
<b>Role of Manager/Underwriter:</b>	Either agented or principal basis.	Must purchase as principal.
<b>'40 Act:</b>	“Banks” not considered investment companies. Foreign banks will want to review 1940 Act guidance.	Non-bank issuer should consider whether there is a 1940 Act issue.
<b>Settlement:</b>	Through DTC, Euroclear/Clearstream.	Through DTC, Euroclear/Clearstream

## Comparison of Section 3(a)(2) to Rule 144A, cont'd

# 1940 Act Issues

Investment companies are subject to registration under the Investment Company Act of 1940, unless an exemption is available.

An investment company is defined broadly as an entity that holds itself out as being engaged primarily, or proposing to engage, in “investing, reinvesting or trading in securities” and also includes entities engaged, or that propose to engage, in the business of investing, reinvesting, owning, holding or trading in securities if securities represent 40% or more of the value of its total assets (excluding cash and government securities).

- As a result, issuers that are banks or specialized finance companies may inadvertently fall within the definition of an “investment company.”

# 1940 Act Issues – Exemptions

## Exemptions:

- U.S. banks are exempted under Section 3(c)(3) of the 1940 Act.
- Foreign banks are exempted under Rule 3a-6 under the 1940 Act, subject to certain conditions.
- U.S. branches or agencies of foreign banks are exempted under an interpretive release (1940 Act Release No. 17681 (Aug. 17, 1990)).
- Finance subsidiaries of U.S. or foreign banks are exempted under Rule 3a-5, subject to certain conditions.

Rule 3a-6 defines a “foreign bank” as a banking institution incorporated or organized under the laws of a country other than the United States, or a political subdivision of a country other than the United States, that is:

- Regulated as such by that country's or subdivision's government or any agency thereof;
- Engaged substantially in commercial banking activity; and
- Not operated for the purpose of evading the provisions of the Act.

# 1940 Act Issues – Rule 3a-6

“Engaged substantially in commercial banking activity” means engaged regularly in, and deriving *a substantial portion of its business from, extending commercial and other types of credit, and accepting demand and other types of deposits*, that are customary for commercial banks in the country in which the head office of the banking institution is located.”

The SEC’s Division of Investment Management, in a no-action letter, interpreted the “substantial portion” language:

We believe, however, that the banking activities in which a foreign bank engages clearly must be more than nominal to satisfy the "substantial" standard in the rule. In addition, in order to meet this standard, we generally would expect a foreign bank: (1) to be authorized to accept demand and other types of deposits and to extend commercial and other types of credit; (2) to hold itself out as engaging in, and to engage in, each of those activities on a continuous basis, including actively soliciting depositors and borrowers; (3) to engage in both deposit taking and credit extension at a level sufficient to require separate identification of each in publicly disseminated reports and regulatory filings describing the bank's activities; and (4) to engage in either deposit taking or credit extension as one of the bank's principal activities.

# Launching a Bank Note Program

Where do we start?

- Does the bank have an affiliated dealer that may be the lead dealer for the program?
- If the affiliated dealer does not have expertise in the particular market (e.g., structured products), an unaffiliated dealer with expertise should be brought in;
  - If the bank is planning on issuing structured products, it should engage a dealer that is familiar with FINRA's suitability rules and has internal compliance procedures in place for sales of structured products;
  - The dealer may have particular views as to acceptable financial statements, if a foreign bank is the issuer;
- If the dealer plans on distributing through third-party dealers, the issuer should inquire about the dealer's "know your distributor" policies;
- If the issuer uses an affiliated dealer, the appropriate FINRA filing exemption must be used; and
- Dealer's counsel will want to start its diligence early in the process in order to identify any potential issues.

# Launching a Bank Note Program – Offering Circular

## Documentation

- The offering circular tends to have information similar to that in a registered offering, due to 10b-5 concerns.
  - OCC 16.6 content requirements:
    - description of the business of the issuer similar to that in a Form 10-K;
    - description of the terms of the notes;
    - use of proceeds; and
    - method of distribution.
- Branches or agencies of foreign banks' disclosure is very limited, usually the address, primary business lines, the date of establishment and a discussion of the regulatory oversight of the issuer; disclosure about the parent or headquarters is usually sufficient;
- If a guarantee structure is used, a description of the guarantee; and
- Product and pricing supplements for particular structures of structured notes.



# Launching a Bank Note Program – Distribution Agreement

- Very similar to an MTN distribution agreement for a registered offering;
- Which deliverables, and when? Comfort letters, officers' certificates, opinions and 10b-5 letters:
  - Negotiate the scope of opinions early in the process;
  - Will multiple counsel give opinions (U.S., non-U.S., internal, underwriters' counsel)?
  - Plan for future regular diligence session with the agents.
- Does the issuer have a designated underwriters' counsel?
  - If so, they will have a view as to the form of the distribution agreement.

# Opinion Issues – Section 3(a)(2) and U.S. Branches of Foreign Banks

In the SEC's 1986 release confirming that securities issued by a U.S. branch or agency of a foreign bank are within the Section 3(a)(2) exemption, reference was made to a series of previous no-action letters confirming that debt securities sold in minimum denominations ranging from \$25,000 to \$100,000 or sold only to certain types of sophisticated investors were exempt under Section 3(a)(2).

The release also stated that the SEC would no longer express any view, or issue any no-action letters, regarding whether debt securities issued or guaranteed by a U.S. branch or agency of a foreign bank must satisfy any minimum denomination requirement, be sold to any type of investor or be principal protected, nor does the release require that such debt securities be subject to any of those limitations.

Consequently, in opining on the availability of the Section 3(a)(2) exemption for notes issued or guaranteed by a U.S. branch or agency of a foreign bank, many firms will issue an opinion stating that the notes “should be exempt,” rather than the notes “are exempt.”

# Launching a Bank Note Program – Paying Agency Agreement

- Who will be the paying agent? Will it be an affiliate of the bank?
- Usually, the form of paying agency agreement will be suggested by the paying agent.
- Generally, indentures are not used.
  - Disclosure should clearly point out the differences between an indenture and a paying agency agreement; i.e., no trustee in a fiduciary relationship with the note holders.

# Liability Concerns

# Securities Liability – Rule 144A and Section 3(a)(2)

- Neither Rule 144A offerings or securities offerings of, or guaranteed by, a bank under Section 3(a)(2) are subject to the civil liability provisions under Section 11 and Section 12(a)(2) of the Securities Act.
- Rule 144A offerings and offerings under Section 3(a)(2) are subject to Section 10(b) of the Exchange Act and the anti-fraud provisions of Rule 10b-5 of the Exchange Act.
- Impact on offering documents, and use of offering circulars to convey material information and risk factors.

# Liability Under the Exchange Act

- Rule 10b-5 applies to registered and exempt offerings.
- Rule 10b-5 of the Exchange Act prohibits:
  - the use of any device, scheme, or artifice to defraud;
  - the making of any untrue statement of a material fact or the omission of a material fact necessary to make the statements made not misleading; or
  - the engaging in any act, practice, or course of business that would operate to deceive any person in connection with the purchase or sale of any securities.
- To bring a successful cause of action under Rule 10b-5, the plaintiff must prove:
  - that there was a misrepresentation or failure to disclose a material fact,
  - that was made in connection with plaintiffs' purchase or sale of a security,
  - that defendants acted with "scienter," or the intent or knowledge of the violation,
  - that plaintiffs "relied" on defendants' misrepresentation or omission, and
  - that such misrepresentation or omission caused plaintiffs' damages.

# FREQUENTLY ASKED QUESTIONS ABOUT SECTION 3(a)(2) BANK NOTE PROGRAMS

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## Understanding Section 3(a)(2) Bank Note Programs

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### *What is a Section 3(a)(2) bank note program?*

A Section 3(a)(2) bank note program is a medium-term note (“MTN”) program that enables an issuing bank to offer debt securities on a regular and/or continuous basis. The issuer (or a guarantor of the notes) must be a “bank,” as defined in Section 3(a)(2) of the Securities Act of 1933 (the “Securities Act”). Bank note programs are exempt from registration under the Securities Act.

### *What is Section 3(a)(2)?*

Section 3(a)(2) exempts any security issued or guaranteed by a bank from registration under the Securities Act. This exemption is based on the principle that, whether chartered under state or federal law, banks are highly and relatively uniformly regulated, and as a result will typically provide adequate disclosure about their business and operations, even in the absence of federal securities registration requirements. In addition, banks are also subject to various capital requirements that may help increase the likelihood that holders of their debt securities will receive timely principal and interest payments.

### *What is a “bank”?*

Section 3(a)(2) broadly defines a “bank” to mean any national bank, or any banking institution organized under the law of any State, territory, or the District of Columbia, the business of which is substantially confined to banking and is supervised by the State or territorial banking commission or similar official. To qualify as a bank under Section 3(a)(2), the institution must meet two requirements: (i) it must be a national bank or any institution supervised by a state banking commission or similar authority; and (ii) its business must be substantially confined to banking. Therefore, securities issued by bank holding companies, finance companies, investment banks and loan companies are not exempt from registration under Section 3(a)(2). Even though many investors may think of them as banks, their businesses are not substantially confined to banking. A securities offering by any of these institutions must be registered under the Securities Act unless the offering falls under another exemption from registration.

### *Is a non-U.S. bank eligible for a Section 3(a)(2) bank note program?*

No; however, for purposes of the exemption from registration provided by Section 3(a)(2), the Securities and Exchange Commission (the “SEC”) deems a branch

or agency of a foreign bank located in the United States to be a “national bank,” or a “banking institution organized under the laws of any State, Territory, or the District of Columbia,” provided that the nature and extent of federal and/or state regulation and supervision of the particular branch or agency is substantially equivalent to that applicable to federal or state chartered domestic banks doing business in the same jurisdiction. The determination with respect to the requirement of “substantially equivalent regulation,” as well as the determination as to whether the business of the branch or agency in question “is substantially confined to banking and is supervised by the State or territorial banking commission or similar official” is the responsibility of issuers and their counsel. These determinations are made with regard to the banking regulations in effect at the time the securities are issued or guaranteed.

*Source:* Securities Issued or Guaranteed by United States Branches or Agencies of Foreign Banks, SEC Release No. 33-6661 SEC Docket (1973-2004), 36 SEC-DOCKET 746-1 (September 23, 1986).

***Can the issuer be a finance company, if the securities are guaranteed by a bank?***

Yes. As noted above, the Section 3(a)(2) exemption is also available for securities “guaranteed” by a bank. Whether an offering is guaranteed by a bank is interpreted broadly by the SEC. The staff of the SEC has taken the position in no-action letters that the term “guarantee” is not limited to a guaranty in a legal sense, but also includes arrangements in which the bank agrees to ensure the payment of a security. However, in a typical guaranteed offering, a bank’s affiliate will serve as issuer of the relevant securities, and the entity

that is a bank will execute a written guarantee of the payment obligations on those securities. Guarantees by a foreign bank (other than those by an eligible U.S. branch or agency) would not qualify for the Section 3(a)(2) exemption.

***What are the differences between a Section 3(a)(2) bank note program and a registered MTN program?***

There are more similarities than differences between the two programs. For a description of a registered MTN program, please see “Frequently Asked Questions About Medium-Term Note Programs,” which can be found at <http://media.mofo.com/files/Uploads/Images/080818FAQsMTN.pdf>. Relevant differences between the two programs will be discussed in this FAQ.

***What types of securities normally are sold through a Section 3(a)(2) bank note program?***

A wide variety of securities can be offered through a Section 3(a)(2) bank note program. Bank notes can be senior or subordinated, fixed or floating rate, zero-coupon, non-U.S. dollar denominated, amortizing, multi-currency or indexed (structured) securities. Common reference rates for floating rate bank notes include LIBOR, EURIBOR, the prime rate, the Treasury rate, the federal funds rate and the CMS rate. Most bank note programs are rated “investment-grade” by one or more nationally recognized rating agencies.



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**Regulations Governing Offerings  
Under Bank Note Programs**

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*Which U.S. or state regulations govern offerings under a Section 3(a)(2) bank note program?*

The Office of the Comptroller of the Currency (OCC) regulates disclosure in connection with offers and sales of securities by national banks and federally licensed U.S. branches and agencies of foreign banks (but not state banks). 12 C.F.R. Part 16, the OCC's Securities Offering Disclosure Rules (the "OCC Regulations"), provides that these banks may not offer and sell their securities until a registration statement has been filed and declared effective with the OCC, unless an exemption applies. Issuers are required to follow the form requirements of the form that they would use to register securities under the Securities Act if they were not exempt from such registration.

The OCC Regulations provide an exemption from the registration requirements if the securities would be exempt from registration under the Securities Act *other* than by reason of Sections 3(a)(2) or 3(a)(11), or the securities are offered in transactions that satisfy certain exemptions under the Securities Act, including the following:

- Regulation D offerings;
- Rule 144A offerings to qualified institutional buyers; and
- Regulation S offerings effected outside of the United States.

Rule 144A and Rule 506 of Regulation D now allow general solicitation or general advertising of offers, provided that the securities are sold only to accredited investors (in the case of Rule 506 offerings) or QIBs (in the case of Rule 144A offerings). In a Rule 506 offering,

the issuer must take reasonable steps to verify that the purchasers are accredited investors.

The disqualification provisions of Rule 506 prohibit the use of the exemption by certain bad actors and felons. The disqualification events apply to the issuer, persons related to the issuer and anyone who will be paid (directly or indirectly) remuneration in connection with the offering (placement agents and others).

The OCC Regulations also contain an exemption for offers and sales of nonconvertible debt securities if a number of conditions are met under Part 16.6, including:

- the issuer or its parent bank holding company has a class of securities registered under §15(d) of the Securities Exchange Act of 1934 (the "Exchange Act"), or, in the case of issuances by a federal branch or agency of a foreign bank, such federal branch or agency provides the Comptroller the information specified in Rule 12g3-2(b) under the Exchange Act and provides investors with the information specified in Rule 144A(d)(4)(i) under the Securities Act;
- all offers and sales are to "accredited investors," as defined in Rule 501 under the Securities Act;
- the securities are "investment grade," as discussed below;
- the securities are sold in a minimum denomination of \$250,000 and are legended to provide that they cannot be exchanged for securities in smaller denominations;
- prior to or simultaneously with the sale of the securities, the purchaser receives an offering

document that contains a description of the terms of the securities, the use of proceeds and the method of distribution, and incorporates certain financial reports or reports filed under the Exchange Act; and

- the offering document and any amendments are filed with the OCC no later than the fifth business day after they are first used.

The current definition of “investment grade,” which came into effect on January 1, 2013, does not require a specific rating for the relevant bank notes. Rather, the condition will be satisfied if the issuer of a security has “adequate capacity to meet financial commitments under the security for the projected life of the asset or exposure. An issuer has an adequate capacity to meet financial commitments if the risk of default by the obligor is low and the full and timely repayment of principal and interest is expected.” An existing investment grade rating could be one factor that offering participants may take into consideration in determining whether an issue of bank notes is “investment grade” for purposes of the OCC Regulations. *See also* the discussion below under “*Are any filings with FINRA required under the Corporate Financing Rule?*”

*Source:* 12 C.F.R. Part 16; Alternatives to the Use of External Credit Ratings in the Regulations of the OCC, 77 Fed. Reg. 35,253 (2012).

The OCC’s Subordinated Debt Comptroller’s Licensing Manual (the “Licensing Manual”) contains certain requirements if a national bank intends to count subordinated debt as Tier 2 capital. Among other requirements, the subordinated bank notes must have an original weighted average maturity of at least five years, and the note itself must bear a legend that it is not

a deposit and is not insured by the FDIC. Appendix A to the Licensing Manual contains other provisions that must be included in the subordinated bank note and, consequently, are usually included in the relevant section of the offering document describing the subordination provisions.

*Source:* Subordinated Debt – Comptroller’s Licensing Manual (November 2003), available at <http://www.occ.gov/publications/publications-by-type/licensing-manuals/subdebt.pdf>.

For state banks and state-licensed branches of foreign banks with insured deposits, the Federal Deposit Insurance Corporation (FDIC) adopted a Statement of Policy Regarding the Use of Offering Circulars in Connection with Public Distribution of Bank Securities for state non-member banks (the “FDIC Policy”). The FDIC Policy requires that an offering circular include prominent statements that the securities are not deposits, are not insured by the FDIC or any other agency, and are subject to investment risk. The FDIC Policy states that the offering circular should include detailed prospectus-like disclosure, similar to the type contemplated by Regulation A or the offering circular requirements of the Office of Thrift Supervision (“OTS”) (the “OTS Regulations”). Although the Dodd-Frank financial regulatory reforms mandated that the supervisory functions of the OTS be shifted to the OCC, the FDIC Policy predates the Dodd-Frank changes and therefore continues to refer to the OTS’s requirements.

The FDIC Policy further states that the goals of the Policy will be met if the securities are offered and sold in a transaction that, among other options: (i) satisfied the requirements of Regulation D of the Securities Act relating to private offers and/or sales to accredited investors; or (ii) satisfied the information and disclosure

requirements of the OTS Regulations, which require that debt securities be issued in denominations of \$100,000 or more. If an offering meets these requirements, it will be deemed to satisfy the FDIC Policy's requirements. Nonetheless, an issuer may still want to include more detailed disclosure, as the policy emphasizes the applicability of the anti-fraud provisions of the Securities Act and Exchange Act to offerings by banks.

*Source:* See 61 Fed. Reg. 46808 (1996). The FDIC Policy was most recently revised in August 1996, and may be found at <https://www.fdic.gov/news/news/financial/1996/fi19680.pdf>. The OTS Regulations may be found at 12 C.F.R. Part 563g.

State banks may also be subject to state banking regulations, including pre-issuance approval. For example, Section 5-5A-16 of Title 5, Banks and Financial Institutions, requires an Alabama state bank to obtain the prior written approval of the banking superintendent prior to the issuance of capital debentures, and O.C.G.A. Section 7-1-419 requires shareholder approval for a Georgia state bank to issue subordinated securities. State regulatory consultation, pre-approval or non-objection may also be required for issuance of "novel" or unusual debt instruments issued by state banks. Issuance of debt by New York branches or financing subsidiaries of foreign banks may require pre-issuance consultation with the New York State Department of Financial Services (the "NYDFS").

*Source:* New York State Banking Department Staff Interpretation of January 12, 2005.

An agency of a foreign bank subject to New York banking regulations would have to obtain a pre-offer no-objection letter from the Superintendent of the

NYDFS, and would be able to sell only to certain authorized institutional purchasers in minimum denominations of \$100,000.

*Source:* N.Y. Banking Law § 202-a(1) (McKinney 2014); N.Y. Comp. Codes R. & Regs. tit. 3, §§ 81.1-3 (2015).

***Are any filings under the state securities, or Blue Sky, laws required?***

Securities issued under Section 3(a)(2) are considered "covered securities" under Section 18 of the Securities Act. As a result, no state filings or fees may be required in offerings of Section 3(a)(2) bank notes. However, states may require certain notice filings and charge filing fees in connection with an offering. Most states do not require registration for bank notes offered by a foreign bank through its U.S. branch or agency under the principles of comity, on the theory that the domestic branch or agency is subject to oversight and regulation by U.S. banking authorities.

***Do banks become subject to Exchange Act reporting if they issue securities under a Section 3(a)(2) bank note program?***

Debt securities issued by banks under Section 3(a)(2) are not subject to the reporting requirements under the Exchange Act, which only requires registration of, and periodic reporting with respect to, equity securities issued by a bank.

***On what basis will a bank become liable to investors in its bank notes?***

Offerings under Section 3(a)(2) are subject to Section 10(b) of the Exchange Act and the anti-fraud provisions of Rule 10b-5 under the Exchange Act. Moreover, investors may have a fraud-based cause of action under state common or statutory law. Therefore, when

considering an offering under Section 3(a)(2), a bank (and its underwriters) must take into consideration what disclosure is necessary to avoid liability under the anti-fraud provisions, even if the document does not need to comply with the specific form requirements of the SEC or another regulator. As a result, the form and content of bank note offering documents issued under Section 3(a)(2) are similar in many respects to that used for a registered offering. Securities offerings by a bank or guaranteed by a bank under Section 3(a)(2) are not subject to the civil liability provisions under Section 11 and Section 12(a)(2) of the Securities Act.

***Are any filings with FINRA required under the Corporate Financing Rule?***

Even though securities offerings under Section 3(a)(2) are exempt from registration under the Securities Act, public securities offerings conducted by banks must be filed with the Financial Industry Regulatory Authority, Inc. (“FINRA”) for review under FINRA Rule 5110(b)(9), unless an exemption is available. For purposes of Rule 5110, a Section 3(a)(2) bank note program is a “public offering.” One exemption from filing under Rule 5110 is that the issuer has outstanding investment grade rated unsecured non-convertible debt with a term of issue of at least four years, or that the issuance of non-convertible debt securities is so rated.

A slightly different exemption is applicable to bank note programs in which a broker-dealer affiliate of the issuer participates in the offering. That participation constitutes a “conflict of interest” for purposes of FINRA Rule 5121, and occurs frequently when the issuer is part of a large financial institution with an affiliated broker-dealer participating in the program. If the offering documents have the prominent conflicts of

interest disclosure required by Rule 5121 and the securities are either investment grade rated or in the same series that have equal rights and obligations as investment grade rated securities, then no filing under Rule 5110 would be required. “Prominent disclosure” for purposes of FINRA Rule 5121 means that the offering document include disclosure on the front page that a conflict of interest exists, with a cross-reference to the discussion within the offering document, and disclosure in any summary of the offering document.

If there are no outstanding securities of a national bank in the same series that are rated investment grade and have equal rights and obligations as the bank notes to be issued, the proposed offering is to be issued under Part 16.6 of the OCC Regulations and there is a “conflict of interest” within the meaning of FINRA Rule 5121, then the issuer must obtain an investment grade rating for the offered securities in order to avoid a filing under FINRA Rule 5110. This would be the case even if the national bank has made the “investment grade” determination discussed above under “Which U.S. or state regulations govern offerings under a Section 3(a)(2) bank note program?”

Source: FINRA Rules 5110 and 5121; FINRA Notice 09-49.

***What other FINRA requirements are applicable to offerings from a bank note program?***

- *Suitability:* FINRA members selling Section 3(a)(2) bank notes are subject to FINRA Rule 2111, the suitability rule. Under Rule 2111, a member firm or registered representative must perform a reasonable basis suitability determination before recommending a transaction or investment strategy involving a

security. A reasonable basis suitability determination is necessary to ensure that a transaction or investment strategy is suitable for at least some investors. That determination will be more complicated with respect to structured bank notes, as compared to fixed or floating rate bank notes.

- *Communication rules:* Under FINRA Rule 2210, “Communications with the Public,” certain “retail communications” (as defined in the rule) published or used broadly by a new FINRA member firm relating to a Section 3(a)(2) bank note program would have to be filed with FINRA no later than ten business days prior to their first use. Under a proposed amendment to Rule 2210, this pre-use filing requirement would be changed to require a filing within 10 business days of first use and apply only to new member firms’ websites and material changes to their websites. All retail communications are subject to approval by a principal of the member firm prior to first use or filing with FINRA. Institutional communications must be subject to a member firm’s written procedures designed to ensure that the communications comply with applicable FINRA standards. All member communications, including those relating to a Section 3(a)(2) bank note program, must be based on principles of fair dealing and good faith, must be fair and balanced, and must provide a sound basis for evaluating the facts in regard to any particular bank note. The communications may not omit any material fact or qualification if the omission, in light of

the context of the material presented, would cause the communication to be misleading.

- *TRACE reporting:* Transactions under Section 3(a)(2) must be reported through the Trade Reporting and Compliance Engine (TRACE). All brokers and dealers who are FINRA members have an obligation to report Section 3(a)(2) transactions to TRACE.
- *FINRA filing requirements for private placements:* FINRA Rule 5123 requires members selling securities issued by non-members in a private placement to file the private placement memorandum, term sheet or other offering documents with FINRA within 15 days of the date of the first sale of securities, or indicate that there were no offering documents used. Bank notes offered under Section 3(a)(2) are exempt from these filing requirements.

***How does a bank issuing Section 3(a)(2) bank notes avoid becoming an “investment company” required to be registered under the Investment Company Act of 1940?***

Every investment company is subject to registration and regulation pursuant to the Investment Company Act of 1940 (the “Investment Company Act”), unless it is exempt from the registration requirements. An investment company is defined broadly as an entity that holds itself out as being engaged primarily, or proposing to engage primarily, in the business of “investing, reinvesting or trading in securities” and also includes entities engaged, or that propose to engage, in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to own “investment securities” having a value exceeding 40%

or more of the value of its total assets (excluding cash and government securities) on an unconsolidated basis. As a result, issuers that are banks or specialized finance companies may inadvertently fall within the definition of an “investment company.”

The Investment Company Act and the rules thereunder exempt U.S. banks and foreign banks from the requirements to register as an investment company. U.S. agencies or branches of foreign banks that issue bank notes are exempt from the requirement to register under the Investment Company Act under an SEC interpretive release, provided that the nature and extent of federal and/or state regulation and supervision of the particular branch or agency are substantially equivalent to those applicable to banks chartered under federal or state law in the same jurisdiction.

Finance subsidiaries of U.S. or foreign banks are also exempt from registration under the Investment Company Act, subject to certain conditions.

Rule 3a-5(a) provides that a “finance subsidiary will not be considered an investment company under Section 3(a) of the Investment Company Act and securities of a finance subsidiary held by the parent company or a company controlled by the parent company will not be considered “investment securities” under Section 3(a)(1)(C) of the Investment Company Act” if certain conditions are met. Rule 3a-5 defines “finance subsidiary,” “parent company” and a “company controlled by the parent company,” and also sets forth the conditions precedent for being a “finance company” within the meaning of that Rule.

*Source:* Sections 3(c)(3) and 2(a)(5) of the 1940 Act, Rules 3a-5 and 3a-6 under the 1940 Act and Status under the Investment Company Act of United States Branches

or Agencies of Foreign Banks Issuing Securities, 1940 Act Release No. 17681 (Aug. 17, 1990).

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### Considerations for Structured Bank Notes

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#### *What are some of the differences between SEC registered structured notes and structured bank notes?*

Because bank notes are not subject to the SEC’s registration requirements, structured bank notes sometimes are linked to different types of assets than registered structured notes, particularly when the investor is sufficiently sophisticated to understand the relevant risks. For example, because bank notes are not subject to the “strict liability” provisions of Sections 11 and 12 of the Securities Act, an issuer may be more comfortable linking the bank note to a complex underlying asset or investment strategy, which may be difficult to describe adequately in the context of a registered offering. In addition, registered offerings of equity-linked structured bank notes are typically linked only to large-cap U.S. stocks due to the “Morgan Stanley” SEC no-action letter. Some bank notes may be linked to debt securities (credit-linked notes), small-cap stocks, or securities that are traded only on non-U.S. exchanges.

*Source:* Morgan Stanley & Co. Incorporated, June 24, 2006. Under the terms of this no-action letter, if a linked stock does not satisfy the specified requirements, the issuer of the structured note must include in the prospectus for the structured notes detailed information about the issuer of the underlying stock (the “underlying stock issuer”). Issuers are reluctant to include this type of information, as they would face the possibility of securities law liability for their own

documents if the relevant information about the underlying stock issuer was incorrect.

***Do the SEC's estimated initial value disclosure requirements for structured notes apply to bank notes?***

No, since the SEC's Regulation S-K and related guidance does not technically apply to non-registered offerings. However, in practice, issuers of structured bank notes include estimated initial value disclosure in the related offering documents. The SEC's sweep letter on structured note offerings disclosure can be found at: <http://www.sec.gov/divisions/corpfina/guidance/structurednote0412.htm> (see items 2 and 3). The SEC's follow up letter to structured note issuers can be found at: <http://media.mofo.com/files/Uploads/Images/130221-SEC-Follow-up-Letter-to-Issuers.pdf>.

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**Setting Up a Bank Note Program**

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***What offering documents are used in a Section 3(a)(2) bank note program?***

As a result of the applicable liability provisions described above, the offering documentation for bank notes is somewhat similar to that of a registered offering. An issuer typically has a base offering document, usually called an "offering memorandum" or an "offering circular" (instead of a "prospectus"). That base document is supplemented for a particular offering by one or more "pricing supplements" that set forth the terms of the takedowns from the program. For offerings of more complex bank notes, such as "structured bank notes," different forms of "product supplements" may be used. The form of these documents is not subject to the relevant SEC form rules, and may vary somewhat from those used in a registered

offering. However, the content (as well as the types of documents incorporated by reference) tends to be somewhat similar.

A U.S. bank will incorporate by reference into the offering circular the Exchange Act reports filed by its parent bank holding company, together with the bank's Call Reports.

These offering documents may be supplemented by additional offering materials, including term sheets and brochures. Because these offerings are not registered with the SEC, these additional documents are not subject to the SEC's "free writing prospectus" rules that apply to registered offerings or FINRA's filing rules under FINRA Rule 2210(c). However, in order to ensure that the disclosure is adequate, the issuers and underwriters that use these documents are careful about their content.

***Are there specific form and content requirements that apply to the offering documents for a Section 3(a)(2) bank note program?***

Generally, no; because these offerings are not registered under the Securities Act, the disclosure requirements of Regulation S-K and Regulation S-X are not applicable to them. However, especially when the notes are expected to be sold in part or entirely to retail investors, issuers and underwriters will typically attempt to ensure that the disclosures are as robust as they are in the case of registered offerings, and that all material information about the issuer and the relevant securities is conveyed to investors prior to their investment decision.

***What agreements must a bank enter into to establish a Section 3(a)(2) bank note program?***

In addition to the disclosure documents, the following documents are typically used to establish a bank note program:

- one or more paying agency agreements with a paying agent;
- a distribution agreement between the issuer and the selling agents or dealers; and
- an administrative procedures memorandum, which describes the exchange of information, settlement procedures, and responsibility for preparing documents among the issuer, the selling agents, the paying agent, and the applicable clearing system in order to offer, issue and close each issuance in the series of securities.

Additional agreements for a bank note program may include a calculation agency agreement or an exchange rate agency agreement.

In addition, at the time a program is established, the issuer generally is required to furnish a variety of documents to the selling agents, as would be the case in a typical underwritten or syndicated offering:

- officer's certificates as to the accuracy of the disclosure documents;
- legal opinions as to the authorization of the program, the absence of misstatements in the offering documents, the applicability of the Section 3(a)(2) exemption and similar matters; and
- a comfort letter (or agreed upon procedures letter) from the issuer's independent auditors (for a U.S. bank, the comfort letter may cover

the parent bank holding company's financial statements and exclude the bank's call reports).

In the case of a U.S. bank that incorporates by reference the Exchange Act reports of its parent bank holding company, an officers' certificate and a representations certificate from the parent company will also be delivered at the program establishment. The representations certificate will confirm, among other items, that the parent bank holding company has authorized the incorporation by reference of its Exchange Act reports into the offering circular.

Depending upon the arrangements between the issuer and the selling agents, some or all of these documents will be required to be delivered to the selling agents on a periodic basis as part of the selling agents' ongoing due diligence process. Some or all of these documents also may be required in connection with certain takedowns, such as large syndicated offerings of bank notes.

***Is an indenture required for a Section 3(a)(2) bank note program?***

No; however, some selling agents may require an indenture. Because banks are under extensive regulation from their respective regulatory authorities, most selling agents are comfortable with an issuing and paying agency agreement (IPA). An IPA differs from an indenture in that the issuing and paying agent does not stand in a fiduciary relationship to the bank note holders, as opposed to a trustee under an indenture governed by the Trust Indenture Act of 1939. Bank note holders must act independently without benefit of a trustee. For example, if a bank note issuer were to default with respect to payment of principal on its bank note, each bank note holder would have to individually



declare an event of default and demand acceleration under the IPA, a role carried out by the trustee on behalf of the note holders under an indenture.

*Are there any minimum denominations for bank note offerings?*

Banks have often issued Section 3(a)(2) bank notes in minimum denominations of \$100,000 or greater. The Securities Act, however, contains no requirements regarding minimum denominations for such securities. A review of several no-action letters reveals that the SEC has not directly conditioned the granting of any no-action letter on a bank security being issued in a denomination of \$100,000 or greater. While issuers have identified large denominations in no-action letter requests as an argument in their favor, the SEC has not issued any statement indicating that issuances under Section 3(a)(2) are or should be conditioned on compliance with any minimum denomination requirements. In fact, the SEC has granted no-action letters in connection with the issuance of debt securities under Section 3(a)(2) in denominations as low as \$1,000.

*Source:* The Sumitomo Bank, Limited, SEC No-Action Letter (June 4, 1973); McDonald & Co. Securities, Inc., SEC Staff No-Action Letter (Mar. 11, 1985) and Fireside Thrift Co., SEC No-Action Letter (Apr. 5, 1989).

Because broker-dealers are subject to FINRA's suitability rules when recommending sales of bank notes, banks prefer to issue structured or otherwise "complex" bank notes in large minimum denominations in order to reduce the likelihood that retail investors will purchase the bank notes.

As discussed above, Section 16.6(a)(3) of the OCC Regulations exempts the sale of nonconvertible debt from registration with the OCC if, among other conditions, the debt is sold in minimum denominations of \$250,000.

Under the FDIC Policy, if an offering circular satisfies the requirements of the OTS Regulations, it does not need to include any statements which the FDIC otherwise requires. The OTS Regulations require a savings association to file an offering circular before the offer or sale of any security. Debt securities issued in denominations of \$100,000 or more, however, are exempt from such registration.

As discussed above, an agency of a foreign bank subject to New York banking regulations would be able to sell only to certain authorized institutional purchasers in minimum denominations of \$100,000.

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By Bradley Berman, Of Counsel,  
Lloyd S. Harnetz, Partner,  
and Jay G. Baris, Partner,  
of Morrison & Foerster LLP

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