News Bulletin

January 22, 2013

OCC Regulations Affecting Bank Note Offerings Become Effective

On January 1, 2013, the new regulations of the Office of the Comptroller of the Currency (the "OCC") amending Part 16.6 of the OCC's securities offering rules became effective. These rules govern the exemption from OCC registration of certain types of offerings of bank notes. The amendments were designed to remove the references to credit ratings in Part 16.6.

The rule revisions may be found at the following link: http://www.gpo.gov/fdsys/pkg/FR-2012-06-13/html/2012-14169.htm.

Part 16.6 of the OCC Rules

Bank notes enjoy an exemption from registration under Section 3(a)(2) of the Securities Act of 1933 (the "Securities Act"). However, national banks and U.S. federal branches and agencies of non-U.S. banks are subject instead to the OCC's registration rules, which require OCC registration of bank note offerings unless an exemption is available.

A widely used exemption from OCC registration is Part 16.6. Part 16.6 provides an abbreviated registration regime for certain debt securities ("non-convertible debt") that satisfy the following criteria:

- the bank issuing the debt has securities registered under the Securities Exchange Act of 1934 (the "Exchange Act") or is a subsidiary of a bank holding company that has securities registered under the Exchange Act;
- the debt is offered and sold only to "accredited investors" (as that term is defined in Regulation D under the Securities Act);
- the debt is sold in minimum denominations of $250,000, and each applicable note or debenture is legended to provide that it cannot be exchanged for notes or debentures in smaller denominations;
- the debt is "investment grade", as discussed in this alert;
- prior to or simultaneously with the sale of the debt, each purchaser receives an offering document that contains a description of the terms of the debt, the use of proceeds, and method of distribution, and incorporates certain specified reports filed by the bank and/or its bank holding company; and
- the offering document and any amendments are filed with the OCC no later than the fifth business day after they are first used.

Final Amendment

The revisions to Part 16.6 arise from Section 939A of the Dodd-Frank Act, which requires federal agencies to review, and potentially remove, references to credit ratings from their rules. The amendments replace the "investment grade rating" condition of Part 16.6 with a new revised condition that the notes must be "investment grade."

The new definition for "investment grade" has been adopted substantially as proposed in November 2011. This new investment grade test does not require a specific rating for the relevant 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."

This test is somewhat subjective in nature, and does not provide specific parameters for making this determination. In addition, the longer the term of the debt in question, the harder it will be for an issuer to satisfy itself that this condition is satisfied.

Effect of Amendment

The new condition may impose a degree of uncertainty on offerings and programs that are intended to qualify under Part 16.6. Instead of the prior objective standard—the notes have an investment grade rating—offering participants would need to make a determination that the new standard described above is satisfied.

An existing investment grade rating could be one factor that offering participants take into consideration. In addition, according to the OCC's adopting release, apparently mainly referring to the OCC's related revised rules for permissible investments:

> "When determining whether a particular security is 'investment grade,' the OCC expects national banks to consider a number of factors, to the extent appropriate. While external credit ratings and assessments remain valuable sources of information and provide national banks with a standardized credit risk indicator, if a national bank chooses to use credit ratings as part of its 'investment grade' determination and due diligence, the bank should, consistent with existing rules and guidance, supplement the external ratings with a degree of due diligence processes and additional analyses that are appropriate for the bank's risk profile and for the size and complexity of the instrument. In other words, a security rated in the top four rating categories by an NRSRO is not automatically deemed to satisfy the revised 'investment grade' standard.
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> Importantly, the proposal did not include a requirement that a national bank consider external credit ratings to make an 'investment grade' determination. Therefore, a national bank could rely on other sources of information, including its own internal systems and/or analytics provided by third parties, when conducting due diligence and determining whether a particular security is a permissible and appropriate investment."

In cases in which the offering participants were uncertain as to the availability of the exemption, the parties may seek to restructure the offering to comply with another exemption from the OCC's offering rules, such as Part 16.5(e) (which provides an exemption if the offering complies with Rule 144A under the Securities Act), or Part 16.7(a)(1) (which provides an exemption if the offering complies with Regulation D under the Securities Act).

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