

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 80-139

July 17, 1980

POLICY STATEMENT

Sale of Bank Holding Company Commercial Paper

**TO ALL BANK HOLDING COMPANIES IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:**

The Board of Governors has established the Federal Reserve System's supervisory policy regarding the involvement of a subsidiary bank in the sale of affiliated holding company commercial paper. The policy addresses the concern that individual depositors or investors may purchase bank holding company (or nonbank subsidiary) commercial paper with the misunderstanding that it is an insured deposit or obligation of the subsidiary bank.

For your information, the policy statement is printed on the following pages. Any questions concerning the document should be directed to Sherry L. Conley, Senior Attorney, of our Holding Company Supervision Department, Ext. 6182.

Sincerely yours,

Robert H. Boykin

First Vice President

FEDERAL RESERVE SYSTEM

POLICY STATEMENT

(Sale of Bank Holding Company Commercial Paper)

The sale of bank holding company (or nonbank subsidiary) commercial paper by an affiliated bank to depositors or other investors creates the possibility that individuals may purchase such paper with the misunderstanding that it is an insured deposit or obligation of the selling bank. The Board of Governors believes that the manner in which commercial paper is sold should not lead bank customers or investors to construe commercial paper as an insured bank obligation or an instrument which may be higher in yield but equal in risk to insured bank deposits. All purchasers of commercial paper should clearly understand that such paper is an obligation of the parent company or nonbank subsidiary and that the quality of the investment depends upon the risks and operating characteristics associated with the holding company and its activities.

In light of these considerations, commercial paper obligations issued by holding companies should prominently indicate in bold type on their face 1) that they are not obligations of a bank; and 2) that they are not insured by the Federal Deposit Insurance Corporation. In cases where purchasers do not take physical possession of the obligation, they should be provided with a printed advice which also states that the holding company paper is not an obligation of a bank and is not insured by the FDIC. Those employees engaged in the sale of the paper should also convey this information verbally to each purchaser. In addition, any commercial banking subsidiary involved in the marketing of holding company commercial paper should separate the sale of such paper from the retail deposit-taking function. Thus, for example, commercial paper should not be sold at teller windows or at areas designated for opening retail deposit accounts. Similar procedures should

also be followed for the issuance or sale of commercial paper of nonbank subsidiaries of bank holding companies where the nonbank subsidiary has a name similar to that of any of its affiliate banks or there is a possibility that investors may confuse the obligations of the nonbank subsidiary with those of the holding company or any of its subsidiary banks.

Commercial paper is generally defined as notes, with original maturities not exceeding nine months, that are usually offered and sold to institutional investors, rather than to the general public, in minimum denominations of \$25,000 (although some direct placers sell commercial paper in denominations as low as \$10,000). In order to qualify for the "commercial paper" exemption from the registration requirements of the Securities Act of 1933, the proceeds may be used only for current transactions. Obligations that are payable on demand or have provisions for automatic roll-over do not satisfy the nine-month maturity standard. The Board cautions bank holding companies and nonbank subsidiaries issuing commercial paper that the specific characteristics of commercial paper which allow exemption from the registration requirements of the Securities Act of 1933 define the terms of issue and the use of proceeds from the sale of commercial paper, and companies should only issue commercial paper and use the proceeds pursuant to those provisions.

Bank holding companies should also note that on March 14, 1980 the Board established interest rate limitations on debt instruments that are issued by a bank holding company in denominations of \$100,000 or less and with original maturities of four years or less. Similar action was taken by the FDIC. These limitations apply only to obligations required to be registered with the Securities and Exchange Commission under the Securities Act of 1933 and, consequently, they do not apply to commercial paper issued by a parent bank holding company. In the

Board's view, debt obligations issued by a bank holding company in denominations of less than \$10,000 ordinarily will not qualify for the commercial paper exemption from registration under the Securities Act of 1933. Accordingly, in the absence of any other exemption provision, such debt obligations will be subject to the interest rate limitations set forth in Section 217.7 of the Board's Regulation Q and Section 329.6 of the regulations of the FDIC.