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THE INCHOATE MEANING OF "COVERED SECURITY" UNDER THE SECURITIES ACT OF 1933 — A LOOK AT A BANK "IN ORGANIZATION"

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I. INTRODUCTION**

Following the formation of 1,000 new banks between 2000 and 2008, the downturn in the economy, which began at the end of that period, witnessed 465 bank failures from 2008 to 2012.[1] More recently, there has been considerable consolidation in the banking industry through mergers and acquisitions, and as of year-end 2018, there were fewer than 5,600 banks chartered under federal and state laws, down from 8,000 banks in 2010.[2] Perhaps as a result of that consolidation, the Federal Deposit Insurance Corporation ("FDIC") stated in 2019 that it was encouraging the formation of new banks.[3] In 2018, the FDIC approved fourteen applications for deposit

** The onset of the COVID-19 pandemic has disrupted conventional and historic ways that business has been conducted in the United States (and around the world), and the commercial banking industry is not immune to such disruption. Thus, new bank formations and the raising of capital for a de novo bank are likely to be hamstrung by current events. Nevertheless, this Article continues to focus on an essential question in the application of the National Securities Markets Improvement Act.

1. *E.g.*, Fed. Deposit Ins. Corp., Div. of Risk Mgmt. Supervision, *De Novo Banks: Economic Trends and Supervisory Framework*, SUPERVISORY INSIGHTS, Summer 2016, at 3, 3 [hereinafter FDIC, *De Novo Banks*], https://www.fdic.gov/regulations/examinations/supervisory/insights/sisum16/si_summer16.pdf; *Bank Failures in Brief — Summary 2001 Through 2021*, FED. DEPOSIT INS. CORP., https://www.fdic.gov/bank/historical/bank/ (last updated Feb. 18, 2021).

2. Evan Sparks, *A Fresh Perspective*, ABA BANKING J. (Dec. 5, 2018), https://bankingjournal.aba.com/2018/12/a-fresh-perspective/; Am. Bankers Ass'n, Comment Letter on the FDIC's Deposit Insurance Application Process (Feb. 7, 2019), https://www.fdic.gov/regulations/laws/federal/2018/2018-deposit-insurance-application-process-3064-za03-c-004.pdf.

3. Jelena McWilliams, Chairman, Fed. Deposit Ins. Corp., Remarks at the CATO Summit on Financial Regulation: If You Build It, They Will Come (June 12, 2019), https://www.fdic.gov/news/speeches/spjun1219.html; *see also* Monica C. Meinert, *A New Dawn for De Novo Banks*, ABA BANKING J. (Dec. 10, 2018), https://bankingjournal.aba.com/2018/12/a-new-dawn-for-de-novo-banks/; *cf.* Am. Bankers Ass'n, *supra* note 2 (commenting on the FDIC's RFI regarding its Deposit Insurance Application Process to encourage new bank formation). Frequently, new banks are formed after a merger of two relatively large banks. On February 7, 2019, BB&T and SunTrust Banks commenced a merger that, when completed, would make it the largest bank merger in a decade and the post-merger resulting bank the sixth-largest bank in the country. Michael J. de la Merced & Emily Flitter, *The Financial Crisis Put a Chill on Big Bank Deals. That Ended Thursday.*, N.Y. TIMES (Feb. 7, 2019), https://www.nytimes.com/2019/02/07/business/dealbook/bbt-suntrust-bank-mergers.html. The merger was completed on December 6, 2019. Typically, senior executives of the merging banks, such as market presidents or city executives, have the managerial experience and community connections to organize and operate a new bank. Hilary Burns, *Will BB&T-SunTrust Start a De Novo Wave?*, AM. BANKER (Mar. 12, 2019, 2:21 PM), https://www.americanbanker.com/news/will-bb-t-suntrust-merger-start-a-de-novo-wave.
Often, such persons who leave larger banks wish to have a greater impact in a smaller (de novo) bank or closer contact with the community or are unsettled or "disenchanted" with the transaction. *Id.* Thus, in addition to the FDIC's general encouragement of new bank formations, the country's largest bank merger in a decade may well lead to a

insurance for new bank charters (*i.e.*, "de novo" banks), the largest number in a decade.[4] While some stated a belief that the number of new banks chartered in 2019 would diminish compared to 2018,[5] 2019 witnessed a robust number of de novo bank applications with twenty-one applications for new banks filed in 2019.[6] Significantly, the Chairman of the FDIC, Jelena McWilliams, declared that "a dynamic banking sector needs new startups entering the marketplace," and the FDIC "wants to see more de novo banks."[7]

A key component in the organization of a new bank is the raising of funds to capitalize the bank. The FDIC's position generally is that the bank, once in operation, must be able to maintain at least an eight percent capital to assets ratio for the first three years of operation.[8] Some states, like Alabama,

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significant increase in new bank charters. *See id.* (suggesting that the BB&T merger with SunTrust could lead to a wave in new bank formations).

4. *Decisions on Bank Applications*, FED. DEPOSIT INS. CORP. [hereinafter FDIC, *Decisions on Bank Applications*], https://www.fdic.gov/regulations/laws/bankdecisions/depins/index.html (last updated Mar. 10, 2021); *see, e.g.*, Paul Davis, *Organizers Planning New Bank in New York Area*, AM. BANKER (Dec. 2, 2019, 10:49 AM), https://www.americanbanker.com/news/organizers-planning-new-bank-in-new-york-area (stating organizers filed an application for a new bank in New Jersey); Paul Davis, *Organizers Planning Bank in Southern California*, AM. BANKER (Nov. 12, 2019, 6:03 PM), https://www.americanbanker.com/news/organizers-planning-bank-in-southern-california (reporting that a charter application was filed on November 4, 2019 for a California bank in Temecula, California). *But see* Hilary Burns, *Will De Novo Activity Pick Up in 2019? Don't Bet on It*, AM. BANKER (Dec. 21, 2018, 1:33 PM) [hereinafter Burns, *Will De Novo Activity Pick Up in 2019?*], https://www.americanbanker.com/news/will-de-novo-activity-pick-up-in-2019-think-again.

5. Burns, *Will De Novo Activity Pick Up in 2019?*, *supra* note 4.

6. FDIC, *Decisions on Bank Applications*, *supra* note 4; Maria Tor & Lauren Sullivan, *Despite High Growth, Some States Have Zero Postcrisis De Novo Banks*, S&P GLOB. (Dec. 17, 2019), https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/despite-high-growth-some-states-have-zero-postcrisis-de-novo-banks-55919993; *see* Paul Davis, *Utah De Novo Gets Conditional OK from FDIC*, AM. BANKER (Dec. 30, 2019, 11:07 AM), https://www.americanbanker.com/news/proposed-utah-de-novo-receives-fdic-approval-for-deposit-insurance (stating that the final number of de novo approvals is nine). As of December 17, 2020, eight new banks had opened in 2020. FDIC, *Decisions on Bank Applications*, *supra* note 4.

7. Jelena McWilliams, *We Can Do Better on De Novos*, AM. BANKER (Dec. 7, 2018, 10:00 AM), https://www.americanbanker.com/opinion/fdic-chairman-jelena-mcwilliams-we-can-do-better-on-de-novos. The growing concerns over COVID-19 have made it harder for organizers to line up initial capital for a new bank, and the number of new banks will not match what it was in recent years, but there will likely be new banks formed in certain markets. Ken McCarthy, *De Novo Activity Has Gone Silent. What Happened?*, AM. BANKER (Mar. 5, 2020, 9:00 PM), https://www.americanbanker.com/news/de-novo-activity-has-gone-silent-what-happened?.

8. FED. DEPOSIT INS. CORP., DIV. OF RISK MGMT. SUPERVISION, APPLYING FOR DEPOSIT INSURANCE: A HANDBOOK FOR ORGANIZERS OF DE NOVO INSTITUTIONS 19 (2019) [hereinafter FDIC, HANDBOOK FOR DE NOVO INSTITUTIONS], https://www.fdic.

have in the past required a nine percent ratio, and frequently the organizers themselves prefer a capital-to-assets ratio well in excess of ten percent to provide a cushion for the business conducted by the bank.[9]

The capital required to form a new bank is raised generally in the organization phase through the sale of common stock to be issued by the bank to be formed.[10] The sale of such stock triggers issues under both state and federal securities laws as to the registration (or exemption) requirements for the sale of securities to the investors that are providing the capital for the new bank.[11] In the area of the issuance and sale of securities, a bank security

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gov/regulations/applications/depositinsurance/handbook.pdf.

9. *See* STATE OF ALA. STATE BANKING DEP'T, GENERAL INFORMATION: ALABAMA STATE-CHARTERED BANK FORMATION 1, http://www.banking.alabama.gov/pdf/bank_charter/GeneraldescriptionofconditionsforformationofanAlabama1.pdf (last visited Feb. 26, 2021) (stating the leverage ratio as nine percent for Alabama state-chartered member banks); *see, e.g.*, Hilary Burns, *De Novo Activity's Up, but Organizers Face Familiar Obstacles*, AM. BANKER (Jan. 24, 2019, 1:51 PM), https://www.americanbanker.com/news/de-novo-activitys-up-but-organizers-face-familiar-obstacles (stating that organizers of banks may face difficulty in raising capital to form a new bank).

10. *See* OFF. OF THE COMPTROLLER OF THE CURRENCY, COMPTROLLER'S LICENSING MANUAL: CHARTERS 25–29 (2019), https://www.occ.gov/publications-and-resources/publications/comptrollers-licensing-manual/files/charters.pdf (providing the requirements for raising capital as new banks); *see also* Donald M. Zupanec, Annotation, *Validity, Construction, and Effect of Statutory Provisions Concerning Capital Requisites of State Incorporation of Bank*, 79 A.L.R.3d 1190 § 2 (1977) (explaining the normal method of forming a bank).

11. The Securities Act of 1933, as amended, provides, among other things, that no person may offer to sell or sell a security unless the sale is registered with the U.S. Securities and Exchange Commission ("SEC"), or an exemption from such registration is available. 15 U.S.C. §§ 77c–77e. The SEC has stated:

> The federal registration of securities offerings requires the issuer of the securities to disclose all material information relevant to an informed investment decision. This disclosure must be presented in a registration statement filed with the Commission. No sales of securities in a registered offering may occur until the Commission declares the registration statement effective. A registration statement typically becomes effective by order of the Commission. In declaring a registration statement effective under the Securities Act, the Commission does not consider the merits of the offering, but whether all material information is disclosed.

SEC, REPORT ON THE UNIFORMITY OF STATE REGULATORY REQUIREMENTS FOR OFFERINGS OF SECURITIES THAT ARE NOT "COVERED SECURITIES" (1997) [hereinafter SEC, REPORT ON UNIFORMITY], https://www.sec.gov/news/studies/uniformy.htm. States have similar provisions. *See generally* UNIF. SEC. ACT (UNIF. L. COMM'N 2002) (amended 2005) (providing a model statute of securities regulation that states can use). The Uniform Securities Act ("Revised Uniform Securities Act") provides exemptions from registration for certain transactions, such as securities not involving a public offering (corresponds with Section 4(a)(2) of the 1933 Act), and certain types of securities, including U.S. government securities (corresponds with Section 3(a)(2) of the 1933 Act). *Id.* §§ 201, 202; *see also* 15 U.S.C. §§ 77c, 77d. For a discussion of state exemptions from registration for securities issued by a bank, see *infra* notes 33 through 38 and accompanying text.

has a special place that is frequently overlooked and seldom analyzed.

In 1996, Congress passed the National Securities Markets Improvement Act of 1996 ("NSMIA").[12] Among other things, NSMIA amended Section 18 of the Securities Act of 1933 ("1933 Act").[13] Section 18(a) provides in part that no state may require the registration or qualification of securities if the security is a "covered security" or "will be a covered security upon completion of the transaction."[14] The purpose of NSMIA was to "modernize" the nation's "scheme of securities regulation [in order] to promote investment, decrease the cost of capital, and encourage competition."[15] NSMIA preempted state registration over a variety of securities, including securities listed on a national securities exchange, securities issued by a registered investment company, securities sold to "qualified purchasers," as defined by the Securities and Exchange Commission ("SEC"), and securities sold subject to exemption from registration under SEC Regulation D, Rule 506 ("SEC Rule 506").[16] Much of the focus of this preemption has been placed on the issuance of securities pursuant to SEC Rule 506,[17] the federal exemption from registration that typically relates to "private placements."[18] Although NSMIA's preemption has generated a great deal of commentary about its impact on such exempt offerings,[19] other provisions of Section 18 of the 1933 Act have received

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12. National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290, 110 Stat. 3416 (codified as amended in scattered sections of 15 U.S.C. (2006)).

13. Securities Act of 1933 § 18, 15 U.S.C. § 77r.

14. *Id.* (codified as amended at 15 U.S.C. § 77r(a)); *see infra* note 27 and accompanying text. For ease of reference, the citations to the 1933 Act are generally to the statutory sections, not to the U.S. Code sections.

15. *See* H.R. REP. NO. 104-864, at 39 (1996) (Conf. Rep.).

16. National Securities Markets Improvement Act § 102(a), 15 U.S.C. § 77r(a)–(b); *see* Rutheford B. Campbell, Jr., *The Role of Blue Sky Laws After NSMIA and the JOBS Act*, 66 DUKE L. J. 605, 607 n.3 (2016) [hereinafter Campbell, *The Role of Blue Sky Laws*].

17. *See* National Securities Markets Improvement Act § 102(a), 15 U.S.C. § 77r(b)(4) (exempting securities offered pursuant to Rule 506 from applicable state law).

18. 17 C.F.R. § 230.506(b) (2020). SEC Rule 506(c) also allows an exemption for certain public offers only to "accredited investors," with certain verification procedures of investor qualifications and other requirements. *See id.* § 230.506(c).

19. *See generally, e.g.*, Linda M. Stevens, Comment, *The National Securities Markets Improvement Act (NSMIA) Savings Clause: A New Challenge to Regulatory Uniformity*, 38 U. BALT. L. REV. 445 (2009) (discussing how NSMIA preemption challenges regulatory uniformity); Martin Fojas, Note, *Ay Dios NSMIA! Proof of a Private Offering Exemption Should Not Be a Precondition for Preempting Blue Sky Law Under the National Securities Markets Improvement Act*, 74 BROOK. L. REV. 477 (2009) (arguing that NSMIA preemption should not require "proof of a private offering exemption"); Robert N. Rapp & Fritz E. Berckmueller, *Testing the Limits of NSMIA*

little attention. Among the other securities that enjoy the benefit of state preemption as a "covered security" are the types of securities set forth in Section 18(b)(4)(E), which include a "bank" security exempt from registration with the SEC by Section 3(a)(2) of the 1933 Act.[20] In particular, whether a security *to be issued* by a bank in organization is a covered security and, thus, is exempt from registration under federal law and a beneficiary of preemption under state law is not totally resolved.[21]

This Article focuses upon the interplay between the status of a bank security as a covered security under NSMIA and its status as a security exempt from registration under most state securities laws. This interplay is crucial because satisfaction requires compliance not only with federal law but also with the securities act in every state where the securities will be offered and sold. Thus, the discussion that follows addresses two principal topics: (1) whether, and how, a security issued by a bank to be formed (*i.e.*, a bank "in organization" or a de novo bank) may or may not be a "covered security" entitled to state preemption under NSMIA; and (2) whether a security to be issued by a bank in organization in any case is exempt as a bank security under applicable state securities laws. This second topic is compounded by the fact that, as noted in Part II, virtually all states (apart from NSMIA) provide exemptions from registration for a security issued by a bank while, at the same time, forty-six states also mirror NSMIA and exempt securities that are federal covered securities under Section 18(a) of the 1933 Act. The myriad of forms of state securities statutes that exempt (i) securities issued by banks, or (ii) securities that will be issued by banks, or (iii) securities that are "federal covered securities" under NSMIA, means that for those organizing a bank and seeking necessary capital to receive a bank charter, the roadway to the issuance of securities under federal and state law is circuitous and marked by caution.

Preemption: State Authority to Determine the Validity of Covered Securities and to Regulate Disclosure, 63 BUS. LAW. 809 (2008) (commenting on blue sky laws and "the intended scope of NSMIA preemption"); Rutheford B. Campbell Jr., *The Impact of NSMIA on Small Issuers*, 53 BUS. LAW. 575 (1998) [hereinafter Campbell, *The Impact of NSMIA*] (noting how NSMIA could be used to offer much-needed support to small issuers). One observation about NSMIA is that while NSMIA was supposed to "revolutionize" the securities registration process, NSMIA's effectiveness "has been limited to exempt private offerings made under Rule 506 of Regulation D." Jeffery D. Chadwick, Comment, *Proving Preemption by Proving Exemption: The Quandary of the National Securities Markets Improvement Act*, 43 U. RICH. L. REV. 765, 766 (2009).

20. Securities Act of 1933 § 18(b)(4)(E), 15 U.S.C. § 77r(b)(4)(E) (exempting from state regulation classes of securities under Section 3(a)(2), which include "any security issued or guaranteed by any bank"); *see also id.* § 3(a)(2), 15 U.S.C. § 77c(a)(2).

21. *See infra* notes 36–37 and accompanying text.

II. NSMIA AND THE BANK IN ORGANIZATION

At first glance, the ability of a de novo bank to issue a bank security without running afoul of the federal securities laws and to receive the benefit of state preemption under NSMIA seems reasonably certain. Section 3(a) of the 1933 Act contains a list of securities that are exempt from registration.[22] Among those securities are securities "issued or guaranteed by any bank."[23] The rationale for the exemption afforded to a bank security (as well as the other securities listed in Section 3(a)), as stated by the SEC, is that the exemption for such securities is based on an "alternative regulatory scheme" or federal policy.[24] Thus, because banks are heavily regulated under federal and state law, the federal exemption utilized by banks appropriately appears as an exempt security in Section 3(a) of the 1933 Act.[25]

NSMIA does not itself create new federal exemptions from registration but instead addresses the types of securities entitled to preemption from state registration requirements.[26] Section 18(a) of the 1933 Act establishes preemption as follows:

> **Scope of Exemption**. Except as otherwise provided in this section, no law, rule, regulation, or order, or other administrative action of any State or any political subdivision thereof —
>
> (1) requiring, or with respect to, registration or qualification of securities, or registration or qualification of securities transactions, shall directly or indirectly apply to a security that —
>
> (A) is a covered security; or
>
> (B) will be a covered security upon completion of the transaction.[27]

22. Securities Act § 3(a), 15 U.S.C. § 77c(a).

23. *Id.* § 3(a)(2).

24. SEC, REPORT ON UNIFORMITY, *supra* note 11; *cf.* 1 A.A. SOMMER, JR., FEDERAL SECURITIES ACT OF 1933 § 3.03(4)(a) (Matthew Bender, rev. ed.) (stating that banks are some of the most highly regulated entities in the country). Banks are chartered and regulated by the Office of the Comptroller of the Currency ("OCC"). State banks are chartered and regulated by the state banking authority where the state bank is acquired but a state bank also has a primary federal regulator: either the Board of Governors of the Federal Reserve System, for state "member banks," or the Federal Deposit Insurance Company ("FDIC"), for state "non-member" banks. The deposits of both national and state banks are insured by the FDIC. *See* RICHARD SCOTT CARNELL ET AL., THE LAW OF FINANCIAL INSTITUTIONS 60–63 (5th ed. 2013) (highlighting the "baroque" system of financial regulatory bodies in the United States and delineating between the roles of the OCC, FDIC, Fed, and state regulators).

25. SOMMER, *supra* note 24, § 3.03(4)(b).

26. *See* National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290, § 102(a), 110 Stat. 3416, 3417 (1996) (codified as amended at 15 U.S.C. § 77r(a)).

27. Securities Act of 1933 § 18(a), 15 U.S.C. § 77r(a).

Section 18(b) furnishes a list of what constitutes a "covered security,"[28] and Section 18(b)(4)(E) specifies that with limited exceptions securities exempt from registration under Section 3(a) of the 1933 Act (*e.g.*, one of which is a bank security) is a covered security.[29]

While NSMIA mandates that states may not require the registration of a covered security under state law, Section 18(c)(2) of the 1933 Act enables states to call for a notice filing and the payment of filing fees for the covered securities offered in such states.[30] Section (18)(c)(1) also preserves the right of state securities authorities to pursue enforcement actions for fraud in the sale of a covered security.[31] Thus, even under NSMIA, a state securities regulator may nevertheless require that a notice filing be made with that regulator before a covered security may be offered or sold in the state.[32]

Just as the 1933 Act contains a complete exemption from registration for securities issued or guaranteed by a bank, state securities laws provide a similar exemption. The Revised Uniform Securities Act of 2002 sets forth in Section 201(3) an exemption for a security issued by a banking institution organized under the laws of the United States (*e.g.*, a national bank chartered by the Office of the Comptroller of the Currency ("OCC")) and a security issued by a depository institution with accounts insured by the FDIC (*e.g.*, a state-chartered bank).[33] Whether a bank follows the Revised Uniform Securities Act, however, most states also provide their own separate exemptions for bank securities that require no notice or other filing with the applicable state securities authorities because the state statutory exemption for a bank security is generally a self-executing exemption.[34] Thus, a bank security receives special treatment in two ways: (1) NSMIA preempts state

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28. *Id.* § 18(b).

29. *Id.* § 18(b)(4)(E).

30. *Id.* § 18(c)(2).

31. *Id.* § 18(c)(1). For a discussion of the ability of states to enforce antifraud rules, and a critique of Congress's failure to provide a complete preemption of state authority to require registration, see Campbell, *The Role of Blue Sky Laws*, *supra* note 16, at 613–17.

32. *See* Campbell, *The Role of Blue Sky Laws*, *supra* note 16, at 613–14.

33. UNIF. SEC. ACT § 201(3) (UNIF. L. COMM'N 2002) (amended 2005). The deposits of both national and state banks are insured by the FDIC. Most securities that are exempt from registration under Section 3 of the 1933 Act are also exempt from registration under state securities statutes. *See* 2 THOMAS LEE HAZEN, THE LAW OF SECURITIES REGULATION § 8:14 (7th ed. 2016), Westlaw (databased updated Dec. 2020). Appendix A of Hazen's treatise sets forth the applicable statutory references for exemptions for a bank security in all fifty states plus the District of Columbia. *See* 7 *id.* app.

34. *See infra* note 87; *see, e.g.*, ALA. CODE § 8-6-10(3) (2019); CAL. CORP. CODE § 25100(c) (West 2020); FLA. STAT. § 517.051(3)(a), (5) (2020); GA. CODE ANN. § 10-5-10(3)(B) (2020); MASS. GEN. LAWS ch. 110A, § 402(a)(3) (2019); VA. CODE ANN. § 13.1-514.A.3 (2020).

registration of the bank security as a "covered security"; and (2) all states apart from NSMIA provide some type of exemption from state registration requirements for securities issued by a bank under state blue sky laws, except for Nebraska.[35] The clarity of the status of a "bank" security as a covered security entitled to preemption from state law registration requirements, however, diminishes respecting a covered security that falls under Section 18(a)(1)(B) of the 1933 Act — *i.e.*, a security that "will be a covered security upon completion of the transaction."[36] Such clarity is called into question at least in part because Section 18(a)(1)(B) has not been examined in the context of a bank in organization. For example, it has been noted that while NSMIA identifies the classes of covered securities, Congress "made no provision for any determination as to the validity of a claim that a security in an offering is, in fact, a 'covered security.'"[37] Thus, whether securities to be issued by a bank in organization are entitled to covered security status under NSMIA is a question not fully answered by the language of NSMIA and, accordingly, the relationship between NSMIA and state exemptions for a bank security has yet to be examined.[38] Before focusing further upon that

35. Nebraska also does not have a separate exemption for a bank security, but bank securities receive federal covered security status under Nebraska Law. *See infra* note 116.

36. Securities Act of 1933 § 18(a)(1)(B), 15 U.S.C. § 77r(a)(1)(B).

37. Rapp & Berckmueller, *supra* note 19, at 811–12.

38. New York law ("Martin Act") differs from most other state securities acts in that it does not require the registration of securities offerings — with limited exceptions — and instead obligates issuers and others selling securities to register as securities dealers. *See* N.Y. GEN. BUS. LAW § 359-e (McKinney 2021) (detailing definitions and registration requirements regarding the sale or purchase of securities for dealers, brokers, or salesmen). The Martin Act generally does not provide for exemptions for securities offerings as other states do, such as exemptions for private placements or Regulation D offers, although it does provide an exemption for bank securities. *Id.* § 359-f.1(c), (f). The New York State Bar Association has criticized the Martin Act as being in conflict with federal law and the laws of other states because it does not specifically address the question of securities as covered securities. Comm. on Sec. Regul. of the N.Y. State Bar Ass'n, *Private Offering Exemptions and Exclusions Under the New York State Martin Act and Section 18 of the Securities Act of 1933*, N.Y. BUS. L.J., Fall 2002, at 10, 10, https://nysba.org/app/uploads/2020/07/Private-Offering-Exemptions-and-Exclusions.pdf. The Report notes the interplay between NSMIA's preemption of state registration requirements for covered securities and state law and criticizes the Martin Act as being in conflict with NSMIA. *Id.* at 13. It states that "New York State may not require the registration of issuers as dealers as a way of indirectly requiring registration of transactions in covered securities." *Id.* At the same time, effective December 2, 2020, the Office of the Attorney General of the State of New York adopted guidance for issuers selling Regulation D covered securities by permitting them to file a Form D, with a filing fee, to bring New York in line with most other states regarding exempt offerings under Regulation D. STATE OF N.Y., OFF. OF THE ATT'Y GEN., GUIDANCE ON MANDATORY FILING OF FORM D WITH ELECTRONIC FILING DEPOSITORY FOR FEDERAL COVERED REGULATION D DEALERS (13 NYCRR 10.1(A)(3) AND 10.11(B)) 1 (2020), https://ag.ny.

relationship, however, the chartering process of a de novo bank and the application of NSMIA to the chartering process should be explored.

III. THE BANK CHARTERING PROCESS

Although bank securities are exempt from registration under the 1933 Act and are generally, but not uniformly, exempt under the securities laws of all fifty states and the District of Columbia,[39] the question nevertheless arises as to whether securities offered by a bank in organization are exempt from registration under state and federal law. Typically, a bank in organization is formed under the chartering authority of either the OCC, for national banks,[40] or for state banks, the state where the bank will be headquartered.[41] The deposits of all banks (both national and state) are insured by the FDIC.[42] As part of the application process for the organization of a de novo bank the organizers must submit to the chartering authority a detailed application outlining, among other things, the business plan of the bank, pro forma financial statements showing projected operations, the amount of capital to be raised, and detailed financial and biographical information on the proposed directors and executive officers.[43] An application for deposit insurance must also be submitted to the FDIC for both national and state banks to be formed.[44] This review process by the banking regulators can

gov/sites/default/files/part10-efd-formd-guidance.pdf. The Texas Securities Act is similar to New York's Martin Act in that it requires the registration of dealers (including issuers) to sell securities. A "dealer" includes "any issuer" who offers for sale or sells its own security. TEX. REV. CIV. STAT. ANN. art. 581-4, § C (West 2019); TEX. REV. CIV. STAT. ANN. art. 581-7 § A (West 2019).

39. Some states exempt securities issued by a bank, regardless of whether the bank is a national bank, a bank organized under the law of the state in question, or under the law of any other state. *See, e.g.*, COLO. REV. STAT. § 11-51-307(1)(c) (2020); GA. CODE ANN. § 10-5-10(3); MD. CODE ANN., CORPS. & ASS'NS § 11-601(3) (LexisNexis 2021); VA. CODE ANN. § 13.1-514A.3. Other states exempt securities issued by a national bank or only a bank organized in that state but do not grant an exemption for banks organized under the laws of other states. *See infra* note 87; *see, e.g.*, ARIZ. REV. STAT. ANN. § 44-1843A.2 (2021); CAL. CORP. CODE § 25100(c); LA. STAT. ANN. § 51:708(3) (2020); OR. REV. STAT. ANN. § 59.025(3), (6) (2019).

40. 12 U.S.C. § 27(b).

41. *See supra* note 24.

42. 12 U.S.C. § 1815(a).

43. *See* OFF. OF THE COMPTROLLER OF THE CURRENCY, *supra* note 10, at 23–24 (highlighting factors that the OCC considers in approving bank charter applications); FDIC, HANDBOOK FOR DE NOVO INSTITUTIONS, *supra* note 8, at 13–17; *see also* FDIC, *De Novo Banks*, *supra* note 1, at 4–5.

44. *See* FDIC, *De Novo Banks*, *supra* note 1, at 4–5. For a helpful overview of the bank chartering process, see Am. Bankers Ass'n, *supra* note 2.

take months to complete.[45] During that time, the organizers of the bank (typically the proposed directors and executive officers) contact potential investors about investing in the common stock of the bank once the bank in organization receives regulatory approval to open and obtains its charter. Normally, regulatory approval is a "conditional approval" with the major condition being the raising of the minimum capital required to open the bank.[46] During this time, when subscriptions for the common stock of the bank to be formed are being received from investors, the question arises as to whether the solicitations and receipt of such subscriptions by the bank in organization must be registered under either applicable state securities acts or the 1933 Act.

As already noted, under NSMIA, Section 18(a) of the 1933 Act specifies that no law, rule, or regulation of any state requiring registration of securities shall apply not only to a security that is a covered security,[47] but also to a security that "will be a covered security upon completion of the transaction."[48] Section 18(b)(4)(E) then states that a covered security is, among other things, a security that is exempt from registration under Section 3(a)(2) of the 1933 Act, and that Section includes a bank security.[49]

Section 18(a)(1)(B) thus implies, if not expressly provides, that the offer of a security that will become a covered security upon completion of a transaction, such as happens with a bank in organization, is not subject to state registration requirements.[50] This conclusion follows because Section 18(b)(4)(E) designates a bank security as a covered security, and Section 18(a)(1) preempts state registration requirements both for covered securities and a security that will become a covered security upon completion of the transaction.[51] Accordingly, a security to be issued by a bank, once formed, should be entitled under NSMIA to preemption from state registration, albeit a state may require a notice filing for the bank in organization.[52] The

45. *See* OFF. OF THE COMPTROLLER OF THE CURRENCY, *supra* note 10, at 34.

46. *Id.* at 39–40.

47. *See* Securities Act of 1933 § 18(a)(1)(A), 15 U.S.C. § 77r(a)(1)(A).

48. *Id.* § 18(a)(1)(B).

49. *Id.* § 18(b)(4)(E); *see id.* § 3(a)(2).

50. *Id.* § 18(a)(1)(B).

51. *See id.* § 18(a)(1), (b)(4)(E).

52. A.A. Sommer, *Introduction to the National Securities Markets Improvement Act of 1996*, *in* THE NATIONAL SECURITIES MARKETS IMPROVEMENT ACT OF 1996 3, 4 (Matthew Bender ed., 1996). The legislative history of NSMIA does not expressly address this issue, and there seems to be little commentary or focus on this matter. One noted commentator has simply said that NSMIA lists those securities (including bank securities) that are covered securities and that a covered security is defined as, among other things, "a security that will become a covered security under any of the foregoing definitions of covered security upon completion of the transaction." *Id.*

foregoing seems simple and logical, but the logic is inconclusive because Congress granted no explicit path for determining whether or how a covered security is present.[53]

Similarly, the SEC has not taken an official position regarding the interpretation or application of Section 18(a)(1)(B). However, in response to an inquiry regarding whether the SEC has voiced an opinion regarding how Section 18(a)(1)(B) might apply to a bank in organization, the staff has stated informally that SEC no-action letters pre-dating the passage of NSMIA would be the most likely source expressing the staff's views.[54] In other words, the staff's pre-NSMIA views outline how, and whether, a security of a bank in organization is entitled under the 1933 Act to the exemption from registration as a *bank* security under Section 3(a)(2).[55] The SEC has a number of no-action letters which speak to this issue and which reinforce the concept that a bank in organization may seek and accept subscriptions for the stock to be issued upon the formation of the bank in reliance on the exemption for a bank security under the 1933 Act.[56] Analyzing these letters provides a foundation for determining how to apply the language in NSMIA Section 18(a)(1)(B) to whether a security will be a covered security upon completion of the transaction.[57]

In *County First Bank*,[58] the organizers sought a no-action position from the SEC that they could seek subscriptions, with funds placed in escrow, in reliance on the exemption for a bank security under Section 3(a)(2) of the 1933 Act, for a bank to be formed under Maryland law.[59] According to the no-action request, the subscription funds would be placed in escrow with an independent bank, with funds invested in government-backed or money-market funds.[60] Such funds would not be released until the State of Maryland

53. *See* sources cited *supra* note 19 and accompanying text.

54. Telephone Interview with SEC Staff Member (Sept. 25, 2019) (on file with author). The SEC has a procedure pursuant to which requests for Interpretive Advice may be submitted by e-mail with a staff response within one day.

55. *See id.*

56. *See, e.g.*, County First Bank, SEC Staff No-Action Letter, 1989 WL 245807 (Mar. 31, 1989); Bank of World, SEC Staff No-Action Letter, Fed. Sec. L. Rep. (CCH) ¶ 77,503, 1983 WL 28341 (June 6, 1983).

57. *See generally* County First Bank, *supra* note 56 (stating staff will not recommend that the Commission take any action for a proposed pre-organizational public offering by County First Bank in which the bank is relying on exemption for bank securities); Bank of World, *supra* note 56 (stating staff will not recommend enforcement action for issuance of pre-organizational subscriptions by Bank of World in which funds would only be collected upon conditional approval by the state regulator).

58. County First Bank, *supra* note 56.

59. *Id.*

60. *Id.*

Bank Commissioner ("Commissioner") issued a certificate for the bank to conduct business and the FDIC had granted approval for deposit insurance.[61] Specifically, under Maryland law, the organizers of the bank were required to file the bank's proposed articles of incorporation, certain economic information about the proposed bank, and biographies of its directors with the Commissioner.[62] If the Commissioner approved the articles of incorporation, the organizers were then required to provide a certified list of stockholders and the number of shares for which subscriptions were received.[63] The organizers raised initial funds for the proposed bank to defray organizational costs followed by a "public subscription offering" commenced after filing the documents noted above with the Commissioner.[64] The SEC staff agreed that the exemption from registration found in Section 3(a)(2) was available and granted the no-action request.[65] The staff remarked in particular that the bank and its organizers would be subject to regulations issued by the Commissioner and that "there will be no risk of loss of funds invested in the public pre-organizational common stock subscription offering."[66]

An earlier no-action letter dealt with Pennsylvania law.[67] In *Bank of World*,[68] a Pennsylvania state-chartered bank was in organization and requested a no-action letter from the SEC staff for the issuance of stock through pre-organization subscriptions.[69] The request explained that the bank in formation would not distribute an offering circular or collect any subscription funds until it had received conditional approval from the

61. *Id.*

62. *Id.*

63. *Id.*

64. *Id.*

65. *Id.*

66. *Id.* The staff had previously taken the same position in similar circumstances. *See, e.g.*, Commerce Bank Corp., SEC Staff No-Action Letter, 1988 WL 235078 (Sept. 19, 1988) (noting that investors have an "absolute right" to withdraw subscription funds from escrow if the bank in organization does not receive state and federal approval, and finding that the investor had an absolute right to withdraw subscriptions if a bank charter was not granted under Maryland law); The Springs Bank, SEC Staff No-Action Letter, 1987 WL 108290 (June 15, 1987) (stating that the proposed bank's organizers immediately began the offer and sale of subscriptions after filing its application with the Florida banking authorities, and subscription funds held in escrow would be returned to subscribers if the bank was unable to obtain a charter and commence operations under Florida law). The cover letter in the Springs Bank request stated that it is not clear at what point "a bank in the process of organization" becomes a "banking institution" under Section 3(a)(2) of the 1933 Act. *See id.*; *see also infra* Part VI.

67. Bank of World, *supra* note 56.

68. *Id.*

69. *Id.*

Pennsylvania banking regulator for the charter.[70] Thereafter, subscription funds would be placed in escrow and the funds would be returned to investors if the Pennsylvania regulator so directed.[71] As the letter from the bank in organization stated: "there [is] no risk of loss [to the investor] during the subscription period."[72] The SEC staff granted the no-action request that the exemption for bank securities under Section 3(a)(2) of the 1933 Act could be followed.[73] As with *County First Bank*, the staff noted particularly that the organization of a bank is governed by Pennsylvania law and there would be "no risk of loss of funds invested in pre-organizational subscriptions."[74]

The foregoing analysis of whether a security of a bank in organization is entitled to NSMIA preemption seems simple enough, but it is compounded by the fact that some state securities regulators do not follow the same logic employed by the SEC staff in the foregoing no-action letters and do not view securities to be issued by a bank in organization to be either "bank" securities subject to a state exemption or covered securities under NSMIA.[75] In addition, some state securities statutes contain language similar to that in Section 18(a)(1)(B) of the 1933 Act to include banks in organization under the state law exemption for bank securities, while other state statutes providing for a bank security exemption do not incorporate such language, leaving open the question of whether a bank in organization may rely on the state exemption in question for bank securities.[76] As outlined further below, some states have explicitly ruled that the exemption is not applicable to a bank in organization.[77] While a clear purpose of NSMIA is to "eliminate duplicative and unnecessary regulatory burdens"[78] in the sale of securities,

70. *Id.*

71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.* A more recent SEC no-action letter involved an analogous situation in which distressed assets of credit unions in danger of failure were to be placed in special purpose entities ("SPEs"). The SPEs would sell securities of the SPE to investors. The securities would be guaranteed by the full faith and credit of the National Credit Union Administration ("NCUA"). NCUA submitted a no-action request to the SEC stating that the investments in the SPEs were exempt from registration under Section 3(a)(2) of the 1933 Act, which, among other things, exempts securities issued or guaranteed by any person controlled or supervised by an instrumentality of the United States. The SEC staff agreed the securities could be sold to investors who had been given information describing, among other things, the assets held in the SPEs and the guaranty program. *See* Corporate Credit Union Legacy Assets Resolution Program of the National Credit Union Administration, SEC Staff No-Action Letter, 2010 WL 3737921 (Sept. 24, 2010).

75. *See supra* notes 37–38 and accompanying text.

76. *See infra* note 87.

77. *See infra* notes 109–14 and accompanying text.

78. H.R. REP. NO. 104-864, at 39 (1996) (Conf. Rep.); *see also* Campbell, *The Role*

NSMIA has been criticized for failing to eliminate such burdens.[79] It has been argued that small businesses are subject to the same state rules after NSMIA as they were before it was passed.[80] This argument mirrors the issues confronted by the organizers of a bank as to whether NSMIA preempts the state regulatory burdens in the formation of a de novo bank or whether, despite NSMIA, state securities authorities may still apply state registration requirements for banks in organization.

IV. THE INTERPLAY BETWEEN NSMIA AND STATE LAW

Section 201(3)(B) of the Revised Uniform Securities Act contains a concept similar to Section 18(a)(1)(B) by exempting from state registration "a security issued by and representing *or that will represent* [emphasis added] an interest in or a direct obligation of . . ." a banking institution organized under federal law (*e.g.*, a national bank) or a depository institution with deposits insured by the FDIC (*e.g.*, a state bank).[81] The emphasized language of the Revised Uniform Securities Act plainly provides that a security to be issued by a bank in organization is exempt from registration.[82] The official comments to the Revised Uniform Securities Act do not address this issue, however, and they only refer to Section 18(b)(4)(C) (now 18(b)(4)(E)) of NSMIA.[83] Nevertheless, the Revised Uniform Securities Act appears to be asserting, consistent with NSMIA Section 18(a)(1)(B), that a security of a bank in organization will have the benefit of the exemption as a bank security inasmuch as the bank in organization is offering a security that, in the organization phase, "will represent" a bank security upon the

of Blue Sky Laws, *supra* note 16, at 627–30 (analyzing the inefficiencies in securities regulation before the enactment of NSMIA).

79. *See* Stevens, *supra* note 19, at 446–47 (arguing that the "savings clause" of NSMIA, which allows states to investigate securities fraud, has been used by states as a "loophole" to enforce disclosure requirements and defeat the purpose of NSMIA). It has also been argued that "state securities registration requirements . . . are ineffective in protecting investors." *E.g.*, Fojas, *supra* note 19, at 484.

80. *See* Campbell, *The Impact of NSMIA*, *supra* note 19, at 581. *But see* Campbell, *The Role of Blue Sky Laws*, *supra* note 16, at 627 n.118 (noting that NSMIA does not preempt a state's ability to prosecute securities fraud, allowing states to "enjoy [the] efficiencies" afforded to federal authorities in prosecuting "bad acts"). However, that NSMIA does not preempt a state's ability to prosecute securities fraud is a positive feature. "States may actually enjoy efficiencies compared to federal authorities in prosecuting . . . bad acts." *Id.* For example, the proximity of state regulators to the actual participation of the fraud may make the detection and gathering of information less expensive.

81. UNIF. SEC. ACT § 201(3)(B), (C) (UNIF. L. COMM'N 2002) (amended 2005).

82. *Id.* § 201(3)(B).

83. *See id.* § 201(3) cmt. 3.

grant of the bank charter.[84] Louis Loss and Joel Seligman stated without equivocation that "[t]he Revised Uniform Securities Act totally exempts preorganization certificates or subscription agreements of depository institutions subject to state or federal supervision."[85] Thus, in those states that follow the Revised Uniform Securities Act, even without NSMIA preemption contained in Section 18(a)(1)(B) of the 1933 Act, a bank in organization should be free to utilize the applicable state law exemption for a bank security.[86]

Not all states have adopted the Revised Uniform Securities Act, however. The exemption under many state securities acts for a bank security declares only that a security issued by any bank organized under federal law or the laws of the state in question is exempt from registration, and it does not address a security that "will represent" a bank security.[87]

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84. *See id.* § 201(3) (including in the list of exempt securities a security "that will represent an interest in . . . a banking institution . . . .").

85. LOUIS LOSS & JOEL SELIGMAN, FUNDAMENTALS OF SECURITIES REGULATION 21 n.51 (3d ed. 1995).

86. *See* UNIF. SEC. ACT § 201(3)(B).

87. The following states have adopted the language or substantially similar language from the Revised Uniform Securities Act that exempts a security issued by, or that "will represent" a security issued by, a bank: Alaska, Connecticut, Florida, Georgia, Hawaii, Idaho, Indiana, Iowa, Kansas, Maine, Michigan, Minnesota, Mississippi, Missouri, New Hampshire, New Mexico, North Dakota, Oklahoma, South Carolina, South Dakota, Vermont, Wisconsin, and Wyoming. *See, e.g.*, CONN. GEN. STAT. § 36b-21(a)(3) (2019); GA. CODE ANN. § 10-5- 10(3) (2020); IND. CODE § 23-19-2-1(3)(B) (2020); MINN. STAT. § 80A.45(3)(B) (2020); N.M. STAT. ANN. § 58-13c-201.C(2) (West 2021); WIS. STAT. ANN. § 551.201(3)(b) (2021). The securities acts in the following states, while exempting a security issued by a bank, do not contain language purporting to exempt a security that will represent a bank security: Alabama, Arizona, Arkansas, California, Colorado, Delaware, District of Columbia, Illinois, Kentucky, Louisiana, Maryland, Massachusetts, Montana, Nevada, New Jersey, New York, North Carolina, Ohio, Oregon, Pennsylvania, Rhode Island, Tennessee, Texas, Utah, Virginia, Washington, and West Virginia. *See, e.g.*, ALA. CODE § 8-6-10(3) (2019); CAL. CORP. CODE § 25100(c) (West 2020); DEL. CODE ANN. tit. 6 § 73-207(a)(3) (2021); LA. STAT. ANN. § 51:708(3) (2020); N.C. GEN. STAT. § 78A-16(3) (2020); TENN. CODE ANN. § 48-1-103(a)(3) (2019); WASH. REV. CODE § 21.20.310(3) (2020). Nebraska's law does not explicitly exempt a bank security, but it exempts a federal covered security if no commission is paid. NEB. REV. STAT. § 8-1108.02(6) (2020); *see infra* note 116. As stated, some state exemptions apply to national bank securities — and only to securities issued by banks organized under the laws of that particular state — but not to securities of banks in other states. *See supra* note 39. The Uniform Securities Act of 1956, as amended, while providing an exemption from registration for a federal covered security, does not state in its exemption for a security issued by a bank that the exemption is also for a security that "will represent" a bank security. UNIF. SEC. ACT § 402 (UNIF. L. COMM'N 1956) (amended 1958). The official comment to that section states that the exemption applies only if the security represents an interest in the "particular issuer." This may imply that an interest in a bank to be formed is not exempt. *Id.* § 402(a)(3) cmt.

Given the language from NSMIA that state registration requirements are preempted for a security that is a covered security, or a security that will be a covered security upon completion of the transaction, together with the "prospective language" in those state securities laws that follow the Revised Uniform Securities Act and exempt bank securities or a security that "will represent" a bank security, it seems clear that a bank in organization may (without considering NSMIA's impact) offer in those states securities of the bank that will come into existence on the date the bank charter is granted.[88] The foregoing, while seemingly straightforward, does not completely answer the question of whether state blue sky registration requirements apply to securities offered by banks in organization. Many states, as already noted, do not follow the most recent version of the Revised Uniform Securities Act's exemption for a security "that will represent" a bank security, and for those states, the offer of securities of a bank in organization may (without considering NSMIA's impact) still present registration questions under state law.[89] Even for states that follow the Revised Uniform Securities Act, a state registration issue for a bank in organization could be present, as explained below.[90]

A. State Recognition of "Federal Covered Securities"

Under Section 18(a)(1)(B) of NSMIA, a security offered by a bank in organization, while not a "bank" security when offered but a bank security "upon completion of the transaction," should be entitled to federal covered security status. If so, then securities offered by a bank in organization ought to receive preemption of state registration requirements, subject to any applicable state notice filing requirements.

Most states themselves have exemptions from registration for federal covered securities.[91] Such states generally define a federal covered security as a "security that is, or upon completion of a transaction will be, a covered

88. *See* 15 U.S.C. § 77r (establishing preemption of state regulation of securities offerings); UNIF. SEC. ACT § 201 (detailing securities that are exempt from registration).

89. *See supra* note 87.

90. *See infra* Part V.

91. The following states have exemptions from registration for a "federal covered security": Alaska, Arkansas, Arizona, California, Connecticut, Delaware, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Washington, West Virginia, Wisconsin, and Wyoming. *See, e.g.*, GA. CODE ANN. § 10-5-2(9); KAN. STAT. ANN. § 17-12a301(l) (2020); ME. REV. STAT. ANN. tit. 32, § 16301.1 (2021).

security under Section 18(b)" of the 1933 Act.[92] Thus, the language in such state statutes addressing a security that is or "upon completion" of a transaction is a federal covered security reinforces the concept under state law that a bank in organization may seek and accept subscriptions for the securities to be issued by the bank when formed.[93] Yet, there are only a few interpretations (official or informal) by state securities administrators as to how the federal covered securities definition should be applied to a security that will be a federal covered security upon completion of the transaction.

The states that recognize a statutory exemption for a federal covered security generally provide by statute or regulation that the state securities regulator may require a notice filing for a covered security.[94] Such notice filings are frequently made for SEC Rule 506 offers and certain other types of federal covered securities, but no notice filing is typically required for a federal covered security that is a bank security.[95] For example, Texas requires a notice filing for federal covered securities offered in Texas, but the Texas Administrative Code provides that the filing requirement does not apply to federal covered securities that are exempt from registration under the Texas Securities Act.[96] The Texas Securities Act exempts from registration securities issued by a national bank or a bank organized under state law.[97]

One state that has furnished informal, non-binding advice about a bank in

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92. *See, e.g.*, GA. CODE ANN. § 10-5-2(9); KAN. STAT. ANN. § 17-12a301(l)); *id.* § 17-12a102(7); ME. REV. STAT. ANN. tit. 32, § 16301.1.

93. *See, e.g.*, GA. CODE ANN. § 10-5-2(9); KAN. STAT. ANN. § 17-12a301(l); ME. REV. STAT. ANN. tit. 32, § 16301.1.

94. *See, e.g.*, OR. REV. STAT. ANN. § 59.049(2) (2019); KAN. STAT. ANN. § 17-12a302(c).

95. *See, e.g.*, COMM'R OF SEC. STATE OF GA., UNIFORM ACT IMPLEMENTATION ORDER 2009-03: ORDER REQUIRING ENTITIES ISSUING FEDERAL COVERED SECURITIES IN GEORGIA TO MAKE NOTICE FILING 1 (2009), https://sos.ga.gov/admin/files/Uniform_Act_Implementation_Order_2009-03.pdf; GA. CODE ANN. § 10-5-2(9); KAN. STAT. ANN. § 17-12a302(c); ME. REV. STAT. ANN. tit. 32, § 16302(5); MASS. GEN. LAWS ch. 110A, § 306(c) (2019); OR. REV. STAT. ANN. § 59.049(2), (3).

96. 7 TEX. ADMIN. CODE § 114.1(b) (2021).

97. TEX. REV. CIV. STAT. ANN. art. 581-5, § L (West 2019). The Arkansas Securities Commission, following the passage of NSMIA, adopted regulations providing that, in keeping with NSMIA, certain covered securities, such as securities issued by an investment company or pursuant to SEC Regulation D, would be subject to a notice filing and payment of a fee, but it did not address the status of other covered securities such as a bank security. STATE OF ARK. SEC. DEP'T, ORDER NO. 98-031-S: ORDER WAIVING REQUIREMENTS PURSUANT TO ARK. CODE ANN. § 23-42-509(f) (1998), http://www.securities.arkansas.gov/!userfiles/Orders/1998/98_031_S.htm. The Illinois statute provides that all issuers of any covered security (with limited exceptions not including bank securities) shall annually file a notification with the secretary of state and pay a prescribed filing fee. ILL. ADMIN. CODE tit. 14, § 130.293(a) (2021).

organization is Oregon. The Oregon Securities Act exempts securities issued by a national bank or a bank issued under Oregon law.[98] Oregon grants an exemption for federal covered securities provided that a notice filing is made with the State of Oregon but provides that no notice filing is required for certain federal covered securities, including bank securities.[99] In response to an informal written inquiry regarding the applicability of the Oregon exemption for a security to be issued by a national bank in organization, the staff of the Oregon Department of Consumer and Business Services stated that while no bank exemption would be available for securities offered by a national bank in organization, it was possible that such a security would be exempt under Section 3(a)(2) and fall under the definition of covered security under Section 18 of the 1933 Act.[100] The Department noted that Oregon is "preempted from requiring the registration of a security that is or *would be* a federal covered security."[101] The Department also stated that the analysis would turn on "whether the security 'would be' a federal covered security,"[102] and emphasized that that is a question of federal law.[103]

The foregoing response from Oregon is insightful in that it highlights that in addition to state securities law exemptions for a bank security, a federal covered security is preempted from state registration or filings apart from notice filings and the payment of a filing fee, as NSMIA provides.[104] The response also mirrors the question as to how NSMIA's Section 18(a)(1)(B) should be applied.[105] Thus, the real issue reverts to whether a federal covered

98. OR. REV. STAT. ANN. § 59.025(3), (6). Note that the statutory bank exemption does not apply to state banks organized in states other than Oregon. Thus, the status of a security of a bank to be formed as a covered security under NSMIA is all the more important where state securities registration exemptions apply only to securities issued by a national bank or by the bank organized under the laws of the state in question, but *not* under the laws of other states. *See infra* notes 100–08 and accompanying text.

99. *See* OR. REV. STAT. ANN. § 59.049(2); OR. ADMIN. R. 441-049-1001(3) (2020).

100. E-mail from Staff, Or. Dep't of Consumer & Bus. Servs., to author (Jan. 25, 2019, 10:12 AM) (on file with author).

101. *Id.*

102. *Id.* The staff noted that a notice of filing would be required under OR. ADMIN. R. 441-049-2041(1)(a) with a filing fee. *Id.* Wisconsin has a summary statement about "federal covered securities," and it states that "federal covered securities" includes a list of securities noted in the statement as covered securities under NSMIA, one of which is a security sold pursuant to Section 3(a) of the 1933 Act. Significantly, the statement concludes that covered securities entitled to NISMIA preemption include "[s]ecurities that will be federal covered securities under any of the above upon completion of the transaction." *Federal Covered Securities*, STATE OF WISC. DEP'T OF FIN. INSTS., https://www.wdfi.org/fi/securities/regexemp/covered_securities (last visited Feb. 28, 2021).

103. E-mail from Staff, Or. Dep't of Consumer & Bus. Servs., *supra* note 100.

104. *See* 15 U.S.C. § 77r(a)(1)(A).

105. *See* E-mail from Staff, Or. Dep't of Consumer & Bus. Servs., *supra* note 100

security is present.

B. State Exemptions Only for "Bank" Securities

Apart from NSMIA, however, securities offered by a bank in organization should also be entitled to status as a bank security under state blue sky laws, even for those state laws that do not provide that the exemption applies to a security that will represent a bank security.[106] A state that has taken a different approach, however, and published reasonably detailed official guidance on this issue is Alabama. The Alabama Securities Act at Section 8-6-10(3)[107] provides an exemption for "any security" issued by a national bank or a bank organized under the laws of Alabama. The statute says nothing about a security that "will represent" a security of a bank.[108]

The Alabama Securities Commission ("Alabama Commission") in a policy statement concedes that NSMIA expanded the exemption for bank securities as a "covered security."[109] The Alabama policy also states, however, that the Alabama Commission's position is that "the status of covered security is not available for securities issued by a bank in the process of organization."[110] The Alabama policy does not address the language in Section 18(a)(1)(B) of NSMIA regarding a security that "will be" a covered security.[111] The Alabama policy further states that if any securities are to be "sold to generate funds that will be *used or placed at risk* before the formal incorporation of the bank," those securities must find an exemption from registration other than the exemption for a bank security or else be registered under the Alabama Securities Act.[112] The Alabama policy then provides a

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(indicating it is the state government's interpretation that Section 18(a)(1)(B) preempts state securities registration requirements).

106. The states where the security of the bank in organization is offered could require a notice filing. *See, e.g.*, ALA. CODE § 8-6-10(3) (2019) (noting one state where the security of the bank in organization is subject to supervision by federal laws or by state laws).

107. *Id.*

108. *See generally id.* (finding no mention of securities that represent the security of a bank). Between 2002–2004, the author was the Chairman of the Advisory Committee for the Alabama Law Institute, which submitted a revision of the Alabama Securities Act for consideration to the Alabama Legislature. The Advisory Committee did not include in its proposal the exemption for a bank security that "will represent an interest in" the security.

109. *Alabama Securities Commission Policy on Sales of Securities of De Novo Banks*, ALA. SEC. COMM'N, https://asc.alabama.gov/Policies/5-6-03%20Sales_of_Securities-DE_NOVO.aspx (last visited Feb. 28, 2021).

110. *Id.*

111. *See generally id.* (containing no mention of the Section 18 language in NSMIA).

112. *Id.* (emphasis added).

notice filing procedure for such securities that requires placing funds in escrow with a third-party depository institution, not accepting funds until the primary state or federal banking regulator has determined that the charter application is substantially complete, and the subscription funds are held in escrow until the bank charter is issued.[113] The Alabama policy also requires a notice filing with the Alabama Commission containing the offering circular and subscription agreement.[114]

Alabama is not the only state whose state securities regulator has addressed the state exemption for securities offered by a bank "in organization," but state securities administrators addressing the issue have taken varying positions. Some states have no-action or interpretive letters expressly declaring that the state statutory bank exemption in question is available for a bank in organization.[115] Other states have opined that a bank in organization does not qualify for the exemption of a bank security.[116]

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113. *Id.*

114. *Id.*; *see also Policy Statement*, ALA. SEC. COMM'N, https://asc.alabama.gov/Policies/ASC_Policy_Statement.aspx (last visited Feb. 28, 2021) (stating that a "bank in formation is not yet a bank" and, therefore, "any security issued by a bank in formation is a security subject to registration").

115. *See, e.g.*, [Bank in Organization] Blue Sky L. Rep. (CCH) ¶ 31,631, 2015 WL 8571932 (Sept. 1989) (finding that Massachusetts has stated that although a bank in organization may not yet have been issued its charter, it is "subject to regulation" by the appropriate banking authorities and therefore would qualify for an exemption under the Massachusetts Uniform Securities Act).

116. Pennsylvania has a regulation stating that a "bank" does not include a bank in organization. *See* 10 PA. CODE § 102.021(a) (2021) ("The term [bank] does not include: . . . [a] bank-in-organization if the state or Federal regulator with primary authority over the bank-in-organization determines that it is not a bank under the law governing that bank-in-organization."). An earlier Pennsylvania interpretation had stated that for purposes of determining whether a security issued by a bank in organization was exempt under Pennsylvania law, the position of the Pennsylvania Department of Banking that "a bank becomes a bank as of the time the Articles of Incorporation are filed" means that a bank in organization becomes a "bank." *See* [Exemption Request — "Bank" Exemption] Blue Sky L. Rep. (CCH) ¶ 48,679T, 2015 WL 8572662 (Apr. 3, 1989). Nebraska permits a bank in organization to utilize the exemption for a federal covered security without a notice filing. The staff of the Nebraska Department of Banking and Finance has confirmed informally that the Nebraska Securities Act was amended to remove the state exemption from registration for a bank security because NSMIA provided preemption for such a security. *See* E-mail from Staff, Neb. Dep't of Banking & Fin., to author (Oct. 21, 2019, 4:47 PM) (on file with author). Prior to the passage of NSMIA, Nebraska had ruled that in order for a security to be issued by a bank in organization to qualify for an exemption from registration, the "entity" must have obtained the charter issued by the appropriate regulatory agency. *See* Interpretative Opinion No. 5 — Financial Institution Offerings and the Sections 8-1110(3), 8-1110(4) and 8-1110(5) Exemptions, Blue Sky L. Rep. (CCH) ¶ 37,456, 2015 WL 8572140 (Mar. 27, 1978, rev. July 1, 1985). "Therefore, securities issued by an entity formed for the purpose of applying for a charter to operate [as a bank] and for which no such charter has yet been issued, are *not exempt*

Some states have provided informal, non-binding advice. Arkansas and Virginia seem to recognize that a bank in organization may utilize the exemption for a bank security.[117] Maryland, Oregon, and Washington have informally advised that a bank in organization is not entitled to the bank security exemption, but Oregon has also informally stated that a security for a bank in organization should be considered a federal covered security.[118] Finally, the Rhode Island Uniform Securities Act exempts a subscription agreement for a bank in organization as a transaction exemption.[119]

At the same time, even under those state securities acts that do not contain the language from the Revised Uniform Securities Act that a security is exempt if "it will represent an interest in" a bank,[120] a bank in organization should be able to solicit and offer securities of the bank to be formed under the state statutory exemption for a bank security.[121] Conversely, it is also possible for banks in organization offering securities in states that contain the language that the security "will represent" an interest in a bank to run afoul of the registration provisions under the state securities statute.[122] Much of the analysis as to whether a security of a bank in organization is entitled *either* to a state exemption for a bank security *or* to preemption under NSMIA must focus upon whether, upon completion of the bank organization process, a security of a "bank" will be sold.

While not addressing bank securities as covered securities, some courts and commentators have stressed that a mere allegation of covered security status is insufficient to obtain NSMIA's preemption.[123] For example, in

securities . . . ." *Id.*

117. E-mail from Staff, Ark. Sec. Dep't, to author (Jan. 23, 2019, 9:50 AM) (on file with author); Telephone Interview with Staff, Va. State Corp. Comm'n (Jan. 23, 2019) (on file with author).

118. *See* OR. REV. STAT. ANN. § 59.025(1)–(3) (2019); *see also* E-mail from Staff, Md. Div. Sec., to author (Jan. 23, 2019, 9:16 AM) (on file with author); E-mail from Staff, Wash. Dep't Fin. Insts., to author (Jan. 29, 2019, 3:02 PM) (on file with author).

119. 7 R.I. GEN. LAWS § 7-11-402(12) (2020). Securities exemptions generally fall into two categories: an exemption for the security itself or an exemption for the type of transaction in which any security might be issued. *See supra* note 11 and accompanying text.

120. UNIF. SEC. ACT § 201(3) (UNIF. L. COMM'N 2002).

121. *See supra* note 87 (listing states with an exemption for bank securities but not specifically securities that "will represent" a bank security).

122. *See supra* note 87 (listing states with an exemption for securities that "will represent" a security issued by a bank).

123. *See, e.g.*, 1 THE LAW OF SECURITIES REGULATION, *supra* note 33, § 4.8 (asserting that in order to establish preemption for a Regulation D offering, "it must be shown that the applicable federal exemption [is] in fact available to the offering [and] [i]t is not sufficient to allege that the securities were offered in purported compliance with the exemption").

Buist v. Time Domain Corp.,[124] a claim that securities offered in an SEC Rule 506 private placement were entitled to NSMIA preemption from the Alabama Securities Act was rejected because the offer and sale of the securities did not satisfy the exemption requirements of SEC Rule 506.[125] Therefore, no covered security was present.[126] Thus, while NSMIA preempts state securities registration requirements for covered securities, the offering must be for a security that qualifies as a "covered security."[127] With the foregoing warnings, there are two situations where registration and exemption requirements must be followed or else an exemption other than one for a bank security or a federal covered security must be utilized.

V. EXCEPTIONS TO "COVERED SECURITY" STATUS

First, organizers of a bank typically provide "seed money" for the organizational expenses of the bank in organization.[128] These expenses include legal, accounting, and consulting costs and often include compensation to be paid to certain organizers who have left current jobs with a previous bank employer to work full-time on the de novo project.[129] Such

124. 926 So. 2d 290 (Ala. 2005).

125. *Id.* at 294–95, 298; *see also* Brown v. Earthboard Sports USA, Inc., 481 F.3d 901, 911 (6th Cir. 2007) (observing that "spurious boilerplate language" to a subscription agreement purporting to create covered security status does not in itself create a "covered security"). *But see* Channa's Corp. v. Gilmore, 539 F. Supp. 2d 1299, 1304–05 (W.D. Wash. 2003) (holding that the failure to file a Form D for an SEC Rule 506 offering does not eliminate the security as a "covered security" entitled to state preemption under NSMIA).

126. *Buist*, 926 So. 2d at 298; *see also* Hamby v. Clearwater Consulting Concepts, LLLP, 428 F. Supp. 2d 915, 920–21 (E.D. Ark. 2006) ("[T]he only way to assert federal preemption is to first show that an exemption from federal registration actually applies."). *See generally* Chadwick, *supra* note 19 (discussing helpful case law and theories behind the argument that if there is no valid exemption under the 1933 Act, there can be no preemption of state law under NSMIA); *Securities Act Rules: Questions and Answers of General Applicability*, SEC, https://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm (last updated Nov. 6, 2017) (question 257.08) (stating that a security does not lose covered security status if an issuer fails to file a Form D).

127. *See Buist*, 926 So. 2d at 294.

128. *See* Fed. Deposit Ins. Corp., *Application Handbook and Procedures Manual for Deposit Insurance Application*, Fed. Banking L. Rep. (CCH) ¶ 38,045, 2017 WL 3082088 (Dec. 6, 2018) [hereinafter FDIC, *Application Handbook*] (describing stock benefits provided to organizers in return for seed money for organizational funds); Fed. Deposit Ins. Corp., *Statement of Policy Regarding Applications for Deposit Insurance*, Fed. Banking L. Rep. (CCH) ¶ 54,571, 2015 WL 6172358 (July 1998) [hereinafter, FDIC, *Statement of Policy*] (including "seed money" in funds placed at risk in the organizational fund).

129. *See* FDIC, *Statement of Policy*, *supra* note 128 (including "the market value of legal, accounting, and other professional services rendered" in organizational expenses funded by seed money).

expenses are generally funded by the organizers (those persons who will be directors and executive officers of the bank when formed) either through the contribution of cash by such persons to cover the organization costs or by such persons' personally guaranteeing a loan to the organizing entity from a commercial bank to fund the expenses.[130] In the former case, the organizers will receive securities of the bank (when formed) in exchange for their contributions to capital.[131] In the latter case, the loan will normally be paid from the proceeds of the capital in the bank when formed.[132] In either situation, however, it should be clear that the organizers have purchased a security.[133] As such, the funds provided or guaranteed by the organizers are funds that are "at risk" before the bank has been formed, and the security represented by the investment of such funds must have an exemption from registration under state and federal law other than the exemption for a "bank" security.[134] In the circumstance of raising "seed" money to organize a bank, the utilization of an exemption other than the bank securities exemption to raise the funds is workable because of the small number of "investors" involved and because those investors are the persons putting the project together.[135]

The second area where the bank securities exemption presents greater difficulty for the use of the bank exemption is where the required funds necessary to capitalize and charter the bank are obtained during the organization/regulatory application process. In that circumstance, the bank in organization seeks investors to provide the needed capital to charter the bank and offers common stock of the bank to be formed.[136] The amount

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130. *See* 12 C.F.R. §5.20(g)(1), (3)(i) (2020) (noting that the board is usually comprised of most of the organizers who should have a financial commitment to the institution's success).

131. *How to Raise Capital When Starting a New Bank*, BMA (Dec. 20, 2019), https://bmabankingsystems.com/how-to-raise-capital-when-starting-a-new-bank/ (noting organizers may be required to raise fifteen percent securities-based capital).

132. *See generally* FDIC, *Application Handbook*, *supra* note 128 (describing the requirements for raising capital).

133. The contribution of capital by the organizers is obviously a security. The loan guarantee is an "investment contract" under Section 2(a)(1) of the 1933 Act. Securities Act of 1933 § 2(a)(1), 15 U.S.C. § 77b(a)(1). It should be noted that this analysis applies to a determination as to whether there is an exemption for a "bank" security under either federal or state law. *See* 1 THE LAW OF SECURITIES REGULATION, *supra* note 33, § 1.50 (detailing the test used by the courts to determine whether a security exists).

134. Normally, the applicable exemption is the private placement under Section 4(a)(2) of the 1933 Act or SEC Rule 506(b) of SEC Regulation D. *See* Securities Act of 1933 § 4(a)(2), 15 U.S.C. § 77d(a)(2); 17 C.F.R. § 230.506(b) (2020).

135. *See infra* Part VIII for a discussion of "integration" issues in this circumstance.

136. *See* OFF. OF THE COMPTROLLER OF THE CURRENCY, *supra* note 10, at 27–28.

raised can often equal or exceed $20 million.[137] Whether this process involves the issuance of a bank security that allows an exemption from registration under *state* law depends on the circumstances. The Alabama policy referred to above treats the offer of a security of a bank in formation as a "sale" and assumes that funds are "at risk."[138] Therefore, a sale occurs *before* the bank receives its charter from either the OCC or the Alabama State Banking Department.[139] Typically, a "sale" includes "every contract of sale" of a security for "value" and it is that sale of the security that must be registered.[140]

If the sale of a security of a bank in organization includes a sale of something other than a bank security, the exemption for a bank security in that state is not available regardless of whether the state securities act in question exempts a bank security or a security that will represent an interest in a bank.[141] Thus, neither "covered security" status under NSMIA nor a "bank" security exemption under state law may be relied upon. But whether a bank security is present in such sales activity begs the question of whether the exemption for a bank security may be utilized, and that leads to the second situation. Determining if a bank security is the only security being offered, and thus if a bank security exemption is available, hinges upon when and how, an investor's money is put "at risk."[142] The documentation governs that determination.[143] Usually the securities of the de novo bank are sold

137. *See id.* at 40–41 (specifying the OCC has conditions for approval, including a minimum capital amount); *see, e.g.*, Hilary Burns, *North Carolina De Novo Receives FDIC Approval*, AM. BANKER (Feb. 13, 2019, 11:13 PM), https://www.americanbanker.com/news/north-carolina-de-novo-receives-fdic-approval (requiring organizers to raise $20 million); Paul Davis, *Community Banking Group Files to Open Atlanta Area Bank*, AM. BANKER (Jan. 7, 2019, 10:55 AM), https://www.americanbanker.com/news/group-files-to-open-atlanta-area-bank (noting organizers' plan to raise between $18 million and $25 million); Paul Davis, *FDIC Paves Way for Another De Novo Effort in North Carolina*, AM. BANKER (Dec. 31, 2018, 4:53 PM), https://www.americanbanker.com/news/fdic-paves-way-for-another-de-novo-effort-in-north-carolina (requiring $25.5 million).

138. ALA. SEC. COMM'N, *supra* note 109.

139. *See id.*; ALA. CODE § 8-6-10(3) (2019); 12 C.F.R. § 5.20(i)(6) (2020) ("A proposed national bank may offer and sell securities prior to the OCC preliminary approval of the proposed national bank's charter application . . . ."); *supra* notes 106–14 and accompanying text.

140. UNIF. SEC. ACT § 102(26) (UNIF. L. COMM'N 2002) (amended 2005); *see infra* Part VI.

141. *See infra* note 150; *see also* ALA. SEC. COMM'N, *supra* note 109 ("If any securities are to be sold to generate funds that will be used or placed at risk before the formal incorporation of the bank, then the sale of those securities must have an exemption other than Ala. Code § 8-6-10(3) . . . .").

142. *See, e.g.*, ALA. SEC. COMM'N, *supra* note 109.

143. *See infra* notes 147–52 and accompanying text.

utilizing an offering circular describing such items as the bank to be formed, its business plan, geographic market, biographical and compensation information of officers and directors, articles and bylaws, and regulatory environment.[144] In short, the offering circular contains material information needed by the investor to make an informed investment decision about the bank.[145] Again, what is the nature of the security as to which an investment decision is made? That decision must relate only to a bank security and nothing more. It is essential that the offering circular makes that clear and the subscription agreement signed by the investor should provide the legal framework for the conclusion that the investor's funds are only at risk for a bank security.[146]

For example, each investor signs the subscription agreement which sets forth the number of shares the investor wishes to purchase.[147] The subscription agreement may also contain certain representations and warranties by the investor regarding the investor's financial status, confirmation of receipt of the offering circular, an acknowledgment by the investor that the subscription agreement is subject to acceptance by the bank in formation, and that the subscription funds will be held in escrow by an independent third-party depository institution to be released only upon the chartering of the bank by the appropriate regulatory authorities.[148] Consequently, when prepared in the foregoing format, the documents of the bank in organization demonstrate that the investor's funds are not at risk for any security other than a bank security.[149] If the bank is not chartered, the investor receives a full refund of the investor's money.[150] It seems illogical

144. *See* Statement of Policy on the Use of Offering Circulars, 61 Fed. Reg. 46,807, 46,808 (Sept. 5, 1996); *see also supra* Part III.

145. There are a variety of ways an investor or a securities authority may initiate a claim for fraud in the sale of a security. Under federal law, even outside a registration requirement, a person who offers or sells a security by means of untrue statements or material facts, or by omissions of material facts, is liable to the persons purchasing the security. *See* 15 U.S.C. §§ 77l, 78j; 17 C.F.R. § 240.10b-5 (2020). There are similar provisions under state securities laws. *See* Campbell, *The Role of Blue Sky Laws*, *supra* note 16, at 618–26.

146. Statement of Policy on the Use of Offering Circulars, 61 Fed. Reg. at 46,808 (explaining that offering circulars should notify investors that the securities for sale are not insured and the investments are at risk of loss).

147. *See id.* ("The subscription order form should provide specifically designated blank spaces for dating and signing.").

148. *See id.*

149. *Cf.* 15 U.S.C. § 77l (stating when one might be civilly liable for bank securities).

150. Sometimes the subscription agreement states that the subscription is not revocable by the investor. That can present problems for the bank in organization if an amendment to the offering circular contains new material information that the investor does not like. Also, if an investor wants to terminate a subscription prior to the issuance

to argue in such circumstances that a bank securities exemption is not available or that a security other than a bank security is being offered or sold. The essence of the registration obligation under both federal and state law is to provide the purchaser of the security with all material information about the investment.[151] The investment in this situation is only for a bank security.[152]

VI. THE CONTEXT OF A SALE

Some arguments have been made that for a bank in organization, whether the state bank security exemption is available depends on the status of the regulatory application.[153] Such status was considered by the SEC staff in the *Bank of World* no-action letter.[154] For example, one commentator has observed that if the bank's capital must be raised *before* the bank in organization may apply for a bank charter from its regulatory authority, the bank securities exemption is not available.[155] "On the other hand, if the regulation and supervision of the banking agency attaches from the outset of the organizational process then the securities should be exempt."[156] Yet, this approach does not fully solve the problem or address the practicalities of the bank chartering process. Once the charter application is filed with the appropriate agency, the agency commences a thorough scrutiny of the proposed bank, its business, and organizers, including obtaining fingerprint cards and conducting background checks on the organizers with various agencies.[157] This process should bring sufficient regulatory oversight over the bank in organization to allow it to utilize the state law exemptions for a

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of the securities, it is better to make a refund rather than have a disgruntled shareholder at the commencement of the charter. Finally, allowing the investor to withdraw a subscription at any time reinforces the argument that no "sale" of a security other than a bank security has been made.

151. *See supra* note 11.

152. Long before NSMIA was enacted, the SEC staff dealt with this issue in a series of no-action letters. *See supra* notes 58–74 and accompanying text.

153. *See* County First Bank, *supra* note 56; Bank of World, *supra* note 56; *see, e.g.*, [Bank in Organization], *supra* note 115 (noting that a bank in organization, and its potential exemptions, is subject to the regulatory schemes of Massachusetts banking authorities).

154. *See* Bank of World, *supra* note 56.

155. JOSEPH C. LONG ET AL., BLUE SKY LAW § 6:18, Westlaw (database updated Nov. 2020).

156. *Id.*

157. *See* OFF. OF THE COMPTROLLER OF THE CURRENCY, COMPTROLLER'S LICENSING MANUAL: BACKGROUND INVESTIGATIONS 1 (2019), https://www2.occ.gov/publications-and-resources/publications/comptrollers-licensing-manual/files/background-investigations-licensing-manual.pdf; *supra* Part III.

bank security.[158] Generally, the organization process commences with the preparation of the applications, and the capital raise sometimes unfolds *before* the applications are filed or else when the applications are merely in the review process by regulators.[159] While the SEC staff in *Bank of World* observed that an offering circular would not be distributed until the OCC had granted conditional approval, thereby furnishing comfort that a bank charter is likely to be received, this fact does not seem by itself to protect investor funds.[160] Protection against risk of loss during the subscription period is achieved by the terms of the offering, particularly the subscription agreement and the escrow of subscription funds.[161] The real issue to be addressed is when the investor funds are *at risk*.[162] While delaying the capital raise until conditional approval is received from the chartering authority, as set forth in *Bank of World*, gives some regulatory oversight to the process, such delay still does not fully recognize the circumstances at issue.[163] At what point does an investor's fund become at risk and for what entity?

Perhaps the key question to consider here can be found in both the 1933 Act and most state securities acts. That question is whether the collection of subscriptions or a "preorganization certificate" for a de novo bank must be registered. Under the 1933 Act and most state securities laws, the definition of "security" includes a "preorganization certificate" and a "subscription."[164] At the same time, even if the subscriptions to acquire a security in the bank to be formed are deemed "securities," the prohibition in the 1933 Act and state securities statutes relates to the conducting of a "sale" of or an "offer to

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158. *See supra* Part III; *see also* OFF. OF THE COMPTROLLER OF THE CURRENCY, *supra* note 10, at 26.

159. *See supra* Part III; *see also* County First Bank, *supra* note 56 (seeking an SEC no-action letter where organizers "intend" to submit an application to Maryland officials); *see also* Bank of World, *supra* note 56 (seeking a no-action letter while application is under review by Pennsylvania officials).

160. *See* Bank of World, *supra* note 56.

161. *See id.* (recommending no-action where the organizing bank's application was under review by a state agency and an escrow account was established); County First Bank, *supra* note 56 (recommending no-action where organizing bank "will be" under review by state authorities and an escrow account was established).

162. *See* Bank of World, *supra* note 56 (outlining steps the bank will take once the conditional approval is granted).

163. *See id.* (stating that upon granting the conditional approval, the Bank will be required to raise capital).

164. *See* Securities Act of 1933 § 2(a)(1), 15 U.S.C. § 77b(a)(1); *see also* UNIF. SEC. ACT § 102(28) (UNIF. L. COMM'N 2002) (amended 2005) (defining security to include a "preorganization certificate or subscription"). The Rhode Island Securities Act exempts from registration an offer to sell a preorganization certificate or subscription agreement with a depository institution. *See* 7 R.I. GEN. LAWS § 7-11-402(12) (2020); *see also supra* note 119 and accompanying text.

sell" such security without registration or an exemption from registration.[165] Thus, the registration requirements under federal and state law generally apply to the sale *or* the offer to sell a security.[166] Both the 1933 Act and most states define "sell" or "sale" to include a contract to sell or to dispose of a security "for value."[167] An offer also includes an attempt to offer or solicitation of an offer to buy a security "for value."[168] Assuming a subscription agreement to acquire a security of the bank when formed is considered to be a "security," that security is hardly offered or sold for "value."[169] The only value being transmitted (and held in escrow) is for a bank security. The "subscription" itself is an offer to buy, but it is only an offer to buy a bank security, not a preorganization certificate. This argument is also reinforced under both the 1933 Act and most state securities acts, in which the definition sections of such acts are qualified by the language "unless the context otherwise requires."[170] It seems obvious that the context of an offering of securities in a bank to be formed, where no investor's money is at risk until the bank is chartered, leads to a clear conclusion that no sale or offer of anything in this context applies to anything other than a bank security.[171]

VII. REGISTRATION OBLIGATIONS WITH THE BANK REGULATORS

Although bank securities are exempt under Section 3(a)(2) of the 1933 Act from registration with the SEC, a bank issuing its securities must nevertheless consider whether it must register the sale of its securities with its primary federal bank regulator or utilize an exemption from registration. This question arises because the primary federal regulator for a bank may itself impose registration requirements for the issue of securities by banks under the federal banking regulator's jurisdiction. Thus, a national bank issuing securities must file a registration statement with the OCC or utilize

165. *See* 15 U.S.C. § 77e; UNIF. SEC. ACT §§ 201–202.

166. *See* 15 U.S.C. § 77e; UNIF. SEC. ACT § 301.

167. *See* 15 U.S.C. § 77b(a)(3); UNIF. SEC. ACT § 102(26).

168. *See* 15 U.S.C. § 77b(a)(3); UNIF. SEC. ACT § 102(26).

169. *See* 15 U.S.C. § 77b(a)(3); UNIF. SEC. ACT § 102(26).

170. *See* 15 U.S.C. § 77b; *see, e.g.*, NEV. REV. STAT. § 463.1598 (2020); N.M. STAT. ANN. § 58-13C-102 (West 2021); VT. STAT. ANN. tit. 9, § 5102 (2021).

171. For a helpful discussion of the concept of "unless the context otherwise requires," see Gary M. Brown, *Reach of Securities Act Regulation*, *in* SODERQUIST ON THE SECURITIES LAWS § 5:2:3 (5th ed. 2006 & Supp. 2011). It should be emphasized that while offers to sell a security are subject to registration requirements under Section 5 of the 1933 Act, if the security being offered is exempt from registration under Section 3 of the 1933 Act, the registration requirements of Section 5 do not apply. *See* 15 U.S.C. §§ 77c, 77e. Thus, the issue resolves as to whether a bank security is being offered or some other security is being offered for value.

an exemption from registration.[172] The OCC has promulgated regulations that essentially state that the OCC adopts the rules and regulations of the SEC that relate to registration statements, exemptions, and other matters — such as the integration of offerings — and that in such regulations, references to the term "SEC" or "Commission" shall be deemed to refer to the OCC.[173]

For state banks, the situation is less structured. With state banks that are not members of the Federal Reserve System, a state bank issuing securities is required to conform to a policy statement issued by the FDIC that encourages banks to follow the rules and regulations of the SEC mandating proper disclosure and the use of exemptions.[174] However, the policy statement does not require the bank to make any filing with the FDIC.[175]

State banks that are members of the Federal Reserve System are not subject to any specific Federal Reserve regulation or policy regarding the issuance of their securities.[176] One other clarification should be noted. The analysis of whether a security of a bank in organization is a covered security under NSMIA, or is otherwise exempt from registration under state blue sky laws, only applies to a security of a "bank" — not to a security of a bank holding company. Frequently, when organizers form a bank and file applications for the bank charter, they only file applications for the bank to be formed without a holding company structure.[177] It is that situation of a "stand alone" bank in organization upon which this Article focuses. However, sometimes as part of the organization process, the organizers not only organize the bank, but they also form at the same time a separate company (a "bank holding company") to own 100 percent of the voting stock of the bank to be organized so that the bank will be a wholly-owned subsidiary of the parent bank holding company. A bank holding company is defined under the Bank Holding Company Act of 1956, as amended, as,

172. *See* 12 C.F.R. § 16.3 (2020).

173. *See id.* § 16.2(n).

174. *See* Statement of Policy on the Use of Offering Circulars, 61 Fed. Reg. 46,807, 46,808 (Sept. 15, 1996) (laying out the requirements for insured state nonmember banks that publicly distribute bank securities).

175. *See id.* The FDIC Policy Statement does not impose the burden of filing "and allows for certain flexibility, the FDIC believes [relieving this burden] will be beneficial to small banks." *Id.*

176. *See* Bank of World, *supra* note 56 (requesting that the "state-chartered Federal Reserve member bank in formation" have the ability to sell subscriptions without complying with registration requirements).

177. *Bank Holding Companies*, FED. RSRV.: P'SHIP FOR PROGRESS, https://www.fedpartnership.gov/bank-life-cycle/manage-transition/bank-holding-companies (last visited Feb. 28, 2021) ("Relatively few [bank holding companies], however, are formed by banks while the bank itself is in the organizational phase.").

among other things, a company that "controls" a bank.[178] A bank holding company is not a "bank," however, and its securities are not exempt securities under Section 3(a)(2) of the 1933 Act or generally under state blue sky laws that provide exemptions for "bank" securities.[179] In this situation, the organizers raise funds by the sale of stock of the company that will be the parent company to the bank to be formed. A separate exemption for the sale of the bank holding company securities must be found[180] or the offer of the bank holding company securities must be registered under federal and state law.[181]

VIII. THE CONCEPT OF "INTEGRATION" IN CAPITAL FORMATION

Another issue to be considered is whether the sale of securities for organizational costs should be considered part of the actual sale of bank securities when the bank charter is granted. As explained above,[182] the securities issued to raise the seed money are not bank securities and generally would be issued pursuant to an exemption from registration as a private placement under Section 4(a)(2) of the 1933 Act or SEC Rule 506(b).[183] Such exemptions should be readily available because the organizers of a bank typically qualify as "accredited investors" under the net worth test of Regulation D, the income test of Regulation D, or their status as directors of the bank in organization.[184] At the same time, if the securities for the seed money are issued pursuant to an exemption from registration such as SEC

178. 12 U.S.C. § 1841(a)(1). The bank holding company structure has certain advantages over a stand-alone bank in that, among other things: (i) bank holding companies can engage in certain bank-related activities that banks may not; (ii) bank holding companies can incur debt and downstream the proceeds to the subsidiary bank as primary capital for the bank — not as debt for the bank; and (iii) bank holding companies can repurchase shares of its stock (within regulatory requirements) thereby creating a "market" for its stock, if no public market exists, while banks may generally not repurchase their shares.

179. One exception is Louisiana, which exempts securities issued by a bank holding company organized under the laws of Louisiana. *See* LA. STAT. ANN. § 51:708(3) (2020) (exempting a security issued by a national bank, or bank organized under Louisiana law, *or* "any bank holding company organized under the laws of Louisiana that controls one or more banks whose principal place of business is in Louisiana . . . .").

180. Such as SEC Rule 506 or SEC Rule 147A for intrastate offers. 17 C.F.R. § 230.506 (2020); *id.* § 230.147A.

181. *See* 15 U.S.C. § 77c(a)(11); *see also supra* author biographical note. Of the thirteen de novo banks for which the author was counsel, six were organized with no bank holding company.

182. *See* Bank of World, *supra* note 56.

183. *See* Securities Act of 1933 § 4(a)(2), 15 U.S.C. § 77d(a)(2); 17 C.F.R. § 230.506(b).

184. *See* 17 C.F.R. § 230.501(a).

Rule 506(b) which, among other things, limits the number of non-accredited investors to thirty-five and prohibits a public offering or general solicitation, integration of the seed money offering with the offering of the exemption for bank securities (*i.e.*, a combination of the two offerings) could result in the loss of one or both exemptions under either state or federal law.[185] On November 2, 2020, the SEC adopted amendments to a number of its rules (the "2020 Release"), including its integration standards, "to simplify, harmonize, and improve certain aspects of the exempt offering framework to promote capital formation while preserving or enhancing important investor protection."[186] As the 2020 Release states, the "current exempt offering framework is complex," and the integration of offerings is one of those complex areas.[187] The new integration rule became effective on March 15, 2021.[188] Before examining the application of the 2020 Release's new integration framework, however, a look at the integration concept that has been in place for more than a half-century may be helpful.

A. Sixty Years of History and Uncertainty

The SEC issued a release in 1962 discussing the "integration" of exempt offers and establishing factors to determine whether two exempt offerings would be integrated (the "1962 Release").[189] Essentially, the SEC's position in the 1962 Release was that if two exempt offerings of securities are integrated, then the integrated offers as a whole must satisfy all requirements for an exemption, or else the integrated offer must be registered.[190] This issue most frequently arose when an issuer undertook two separate offerings of securities, each of which was intended to be exempt from registration, but when combined did not satisfy an exemption.[191]

If the funds raised for seed money for a bank in organization were combined with the actual sale of the bank securities when the bank was

185. *See id.* § 230.506(b).

186. Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, Securities Act Release No. 10,884, Exchange Act Release No. 90,300, Investment Company Act Release No. 34,082, 86 Fed. Reg. 3496, 3496 (Jan. 14, 2021).

187. *Id.* at 3499.

188. *Id.* at 3496.

189. *See* Non-Public Offering Exemption, Securities Act Release No. 4552, 1962 WL 69540 (Nov. 6, 1962); 17 C.F.R. § 230.502(a).

190. *See* Non-Public Offering Exemption, 1962 WL 69540.

191. For example, two offers under SEC Rule 506(b) are made, each with thirty-five non-accredited investors. If the offers are integrated into one, then the offer would have seventy non-accredited investors and violate SEC Rule 506(b)(2)(i), which limits the number of non-accredited investors to a maximum of thirty-five. *See* 17 C.F.R. § 230.506(b)(2)(i).

chartered, a judgment had to be made that the offer of the securities representing seed money had a valid exemption and would not be integrated with the offering of the bank securities.[192] If the sales were made more than six months apart, generally there would be no integration issue because the separation of the offerings by six months created a "safe harbor" from integration.[193] As was often the case, however, if the sale of securities representing the seed money was made within six months of the sale of the bank securities following the chartering of the bank, an integration analysis needed to be made.[194] Until adoption of the 2020 Release, SEC Rule 502(a) provided five factors to determine whether two exempt offerings should be integrated:

(a) Whether the sales are part of a single plan of financing;
(b) Whether the sales involve issuance of the same class of securities;
(c) Whether the sales have been made at or about the same time;
(d) Whether the same type of consideration is being received; and
(e) Whether the sales are made for the same general purpose.[195]

Arguably, factors (a), (c), and (d) would suggest the offerings should be integrated. Factor (b) suggests no integration since the seed money is clearly not a bank security, even though it represents equity. Factor (e) (and even factor (a)) can be argued either way. The seed money can be said to represent capital for the bank when chartered. At the same time, if the bank is not chartered, the seed money only represents the costs of organization, and the actual capital necessary to charter the bank comes from the issuance of the bank securities. The organization costs are almost always funded by the organizers, which typically are a close-knit, small group of people who are accredited investors.[196] The SEC staff has stated that if the investors in a private offering, such as SEC Rule 506(b), are solicited by a concurrent registration statement, the two offerings would be integrated.[197] The foregoing integration factors, however, were used to determine whether two or more *exempt* offerings should be integrated as a single offering.[198]

Prior to the 2020 Release, there was another avenue to follow in the

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192. *See id.* § 230.502(a).

193. *See id.*

194. *See id.*

195. *Id.*

196. *See supra* notes 133–35 and accompanying text.

197. *See Securities Act Rules: Questions and Answers of General Applicability*, *supra* note 126 (discussing in question 256.34 the impact a general solicitation has on a private offering under SEC Rule 506(b)).

198. *See Securities Act Sections: Questions and Answers of General Applicability*, SEC, https://www.sec.gov/corpfin/securities-act-sections (last updated Nov. 13, 2020) (question 139.25).

approach to the integration issue. The most practical and commonly used alternative was to treat the raising of seed money from the organizers as an exempt offering under SEC Rule 506(b) (or some other appropriate exemption).[199] Following the raising of seed money from the organizers, the organizers could then turn attention to the solicitation of subscriptions for the securities in the bank to be formed.[200] The SEC stated in a 2007 release (the "2007 Release"), which continues to have validity today, that "a completed private placement that was exempt from registration under Securities Act Section 4(2) [will not] be integrated with a public offering of securities that is registered" under the 1933 Act if certain conditions are satisfied.[201] In the 2007 Release, the SEC made it clear that if investors in the exempt private placement were not solicited by the registration statement, then the two offerings would not be integrated.[202] For example, if the private placement investors become interested in the private placement through a means other than the registration statement, such as through a substantive, pre-existing relationship with the company or contact "by the company or its agents outside of the public offering effort," then no integration should occur.[203]

In the situation of a bank in organization, the organizing directors, who are themselves organizing the bank and providing the seed money, fit within the category of investors who have a pre-existing relationship with the "company" and are solicited otherwise than through a public offering.[204] Because a security issued by a bank is a security exempt from registration under Section 3(a)(2) of the 1933 Act, such a security may be offered in a

199. *See* Revision of Rule 504 of Regulation D, the "Seed Capital" Exemption, Securities Act Release No. 7541, 63 Fed. Reg. 29,168, 29,169 (May 28, 1998) (describing the "seed capital" exemption); *cf.* Revisions of Limited Offering Exemptions in Regulation D, Securities Act Release No. 8828, Investment Company Act Release No. 27,922, 72 Fed. Reg. 45,116, 45,117, 45,134 (Aug. 10, 2007) (discussing whether the "seed capital" exemption should be changed to avoid abuse).

200. *Cf.* Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, Securities Act Release No. 10,884, Exchange Act Release No. 90,300, Investment Company Act Release No. 34,082, 86 Fed. Reg. 3496, 3497 n.9 (Jan. 14, 2021) (discussing the JOBS Act, which pushed "to eliminate the prohibition against general solicitation or general advertising for offers and sales of securities to accredited investors").

201. Revisions of Limited Offering Exemptions in Regulation D, 72 Fed. Reg. at 45,129.

202. *See id.* ("[N]otwithstanding the availability of the information in the registration statement, companies may continue to conduct concurrent private placements without those offerings necessarily being integrated with the ongoing public offering.").

203. *Id.*

204. *See id.* (discussing the applicability of the Section 4(2) exemption to investors with a pre-existing relationship).

public fashion.[205] Accordingly, the offer of bank securities to be issued upon the chartering of the bank, generally offered as a "public offering," while not subject to a registration statement filed with the SEC but rather are subject to the rules of the appropriate federal bank regulatory agencies,[206] should not be a factor to cause integration of the two offers as long as the funds raised as seed money are limited to the organizers.

Moreover, SEC Rule 152 (prior to its amendment in the 2020 Release, as explained below) provided that a completed private placement exempt under the 1933 Act would not be integrated with a subsequent public offering.[207] Prior to its replacement by the 2020 Release, SEC Rule 152 read in full as follows:

> The phrase *transactions by an issuer* not involving any public offering in section 4(a)(2) shall be deemed to apply to transactions not involving any public offering at the time of said transactions although subsequently thereto the issuer decides to make a public offering and/or files a registration statement.[208]

Note that the rule applied not only to a subsequent registration statement but also to a "public offering."[209]

Over the years, the SEC staff has expressly addressed the integration issue in the context of a bank in organization.[210] As previously noted in *County*

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205. *See* Securities Act of 1933 § 3(a)(2), 15 U.S.C. § 77c(a)(2); *see also id.* § 3(b)(2).

206. *See supra* notes 172–75 accompanying text. This discussion assumes that the offer of a security in a bank to be formed is conducted as a public offer. For state banks, both the FDIC and Federal Reserve permit banks to offer securities in a widespread (*i.e.*, public) manner without any exemption or filing requirements. As a practical matter, the offer of seed money by using SEC Rule 506(b), which prohibits a public offer, would be destroyed if integrated with the public offering of the securities of the bank upon organization due to the public nature of the offering of the bank securities. The OCC follows the SEC exemption and registration requirements, and a national bank in formation would normally file a registration statement with the OCC, thus constituting a public offer and leading to a similar integration analysis. *See supra* notes 172–73 and accompanying text. But even if the funds to capitalize the de novo national bank are sought by an exemption from registration, the integration of the two offers should be able to be avoided, either by the use of two distinct exemptions from registration or by the use of one exemption for the entire capital raised, such as SEC Rule 506(b), with no more than thirty-five non-accredited investors. It is also assumed that the foregoing integration analysis would generally be followed for state law purposes.

207. *See* 17 C.F.R. § 230.152 (2020).

208. *Id.* (citation omitted).

209. *Id.* The SEC staff previously stated that SEC Rule 152 did not require that the subsequent public offering be made pursuant to a registration statement. Vintage Group., Inc., SEC Staff No-Action Letter, Fed. Sec. L. Rep. (CCH) ¶ 78,700, 1988 WL 234292 (May 11, 1988).

210. *See generally* County First Bank, *supra* note 56 (serving as an example of the SEC applying SEC Rule 152 to conclude whether two offerings should be integrated).

First Bank, the organizers of the Maryland bank conducted a private offering under SEC Rule 506 to raise funds to satisfy the organizational costs of the bank to be formed.[211] The organizers planned to commence a "public offering" within six months after the close of the private offering.[212] The staff in *County First Bank* addressed whether the two offerings should be integrated.[213] If integrated, the public offering of the security of the bank to be formed would be integrated with the private offering in which the organizers provided "seed money" for the organization process, and there would be no exemption for the private offering.[214]

The no-action request on behalf of the bank in organization argued that under SEC Rule 152, the two offerings would not be integrated.[215] The private offering was conducted as a transaction not involving a public offering and met the requirements of SEC Rule 506.[216] Within six months, the public offering for the bank securities commenced and was structured as a "bona fide offering of securities to the public, as required by SEC Rule 152, notwithstanding the fact that the securities offered may be exempt from registration by virtue of Section 3(a)(2)."[217] The staff agreed stating that "we are relying on our view that under SEC Rule 152, a public offering that follows an offering otherwise exempt under Rule 506 of Regulation D does not vitiate the [limited] registration exemption of Rule 506."[218]

More significantly, the SEC has noted that "companies may *continue* to conduct concurrent private placements without those offerings necessarily being integrated with the ongoing public offering."[219] The SEC stated that

211. *See id.* ("Each investment unit consisted of 250 shares of common stock of the Bank and a warrant to purchase up to 140 additional shares . . . .").

212. *Id.*

213. *See id.* (analyzing the integration of the offerings based on Rule 152 and addressing SEC Rules 501, 502, 503, and 506 under Regulation D).

214. *See id.* (noting that if an offering does not qualify for the safe harbor of SEC Rule 502(a), then it may be integrated after the "five factors" are applied).

215. *See id.* (applying SEC Rule 152, offering two historical examples of similar SEC Rule 152 conclusions, and finally concluding that the offerings will not be integrated).

216. *See id.*

217. *Id.*

218. *Id.*

219. *See* Revisions of Limited Offering Exemptions in Regulation D, Securities Act Release No. 8828, Investment Company Act Release No. 27,922, 72 Fed. Reg. 45,116, 45,129 (Aug. 10, 2007). The SEC has taken similar positions on integration regarding other types of exemptions from registration. For example, the SEC has stated that "an issuer conducting a concurrent exempt offering for which general solicitation is not permitted will need to be satisfied that purchasers in" a Rule 147 or 147A offering (which apply to offers in only one state) were not solicited by such offerings. Exemptions to Facilitate Intrastate and Regional Securities Offerings, Securities Act Release No. 10,238, Exchange Act Release No. 79,161, 81 Fed. Reg. 83,494, 83,507 (Nov. 21, 2016);

"filing a registration statement does not, *per se*, eliminate a company's ability to conduct a concurrent private offering," and whether the public offering would affect the exemption for the private placement would depend on "whether the investors in the private placement were solicited by the registration statement or through some other means that would otherwise not foreclose the availability of the Section 4(2) exemption."[220] The SEC stated in its release that:

> For example, if a company files a registration statement and then seeks to offer and sell securities without registration to an investor that became interested in the purportedly private offering by means of the registration statement, then the Section 4[(a)](2) exemption would not be available for that offering. On the other hand, if the prospective private placement investor became interested in the concurrent private placement through some means other than the registration statement that did not involve a general solicitation and otherwise was consistent with Section 4[(a)](2), such as through a substantive, pre-existing relationship with the company or direct contact by the company or its agents outside of the public offering effort, then the prior filing of the registration statement generally would not impact the potential availability of the Section 4[(a)](2) exemption for that private placement and the private placement could be conducted while the registration statement for the public offering was on file with the Commission.[221]

It is axiomatic that in the formation of a bank, the organizers who provide seed money are not solicited by the subsequent offering of the securities of the bank to be formed.[222] The SEC staff in the Division of Corporation Finance addressed similar issues in its informal interpretations. In Question 256.34 of the Compliance and Disclosure Interpretations, the staff opined

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see also Amendments for Small and Additional Issues Exemptions Under the Securities Act (Regulation A), Securities Act Release No. 9741, Exchange Act Release No. 74,578, Investment Company Act Release No. 2501, 80 Fed. Reg. 21,806, 21,819 (Apr. 20, 2015) (stating that "an issuer conducting a concurrent exempt offering for which general solicitation is not permitted will need to be satisfied that purchasers . . . were not solicited by means" of a Regulation A offering, which allows public solicitation).

220. Revisions of Limited Offering Exemptions in Regulation D, 72 Fed. Reg. at 45,129.

221. *Id.* The SEC's view is significant for a bank in organization because the organizers may have to provide seed money for the organization process, even during the application process and the capital raised in the "public offer. *See supra* Part III.

222. *See supra* Part III. It should be noted that while the release quoted above normally speaks of integrating an exempt offer with securities issued pursuant to a registration statement filed with the SEC (permitting a public offer), the exemption for a bank security under the 1933 Act permits a public offer of such security without a registration statement, which should mean that the integration analysis between an exempt offer of a security and a concurrent public offer of such security (registered or not) should apply.

that offers and sales of securities made in reliance on SEC Rule 506(b), which does not allow public advertising or general solicitation, as long as all requirements of SEC Rule 506(b) were satisfied, would not be integrated with subsequent offers and sales of securities under SEC Rule 506(c), which allows general solicitation.[223]

B. The 2020 Release and Integration Made "Clear"

In the 2020 Release, the SEC adopted a new Rule 152 ("New Rule 152") to address the complicated integration process and the varying views of integration expressed by the SEC and its staff over many years.[224] As the SEC pointed out, the integration framework for both registered and exempt offerings "consists of a mixture of rules and Commission guidance for determining whether multiple securities transactions should be considered part of the same offering."[225] The SEC admitted in the 2020 Release that Rule 502(a) of Regulation D, relying on the 1962 Release, provided a safe harbor for exempt offerings that were six months apart, but for offerings occurring within six months of each other there was, as outlined in Section VIII.A, no "bright-line test" upon which to judge integration.[226] Thus, the 2020 Release repealed the integration concepts first set forth in the 1962 Release. The SEC did not, however, eliminate the guidance set forth in the 2007 Release. Rather, such guidance was codified and expanded by New Rule 152.[227] Accordingly, the 2007 Release provides background on, and factors to consider in, an analysis of the integration process, especially respecting various elements that may be employed to analyze the possible integration of exempt and public offers.[228]

As set forth in the 2020 Release, New Rule 152 is designed to "modernize and simplify the Securities Act integration framework for registered and

223. *Securities Act Rules: Questions and Answers of General Applicability*, *supra* note 126 (question 256.34); *see also Securities Act Sections: Questions and Answers of General Applicability*, *supra* note 198 (stating in question 139.25 that if investors in a private offering have a "substantive, pre-existing relationship" with the company, then a "registration statement would not have served as a general solicitation for the private offering").

224. *See supra* note 187 and accompanying text.

225. Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, Securities Act Release No. 10,884, Exchange Act Release No. 90,300, Investment Company Act Release No. 34,082, 86 Fed. Reg. 3496, 3499 (Jan. 14, 2021).

226. *Id.*

227. *Id.* at 3505.

228. Revisions of Limited Offering Exemptions in Regulation D, Securities Act Release No. 8828, Investment Company Act Release No. 27,922, 72 Fed. Reg. 45,116, 45,129–30 (Aug. 10, 2007).

exempt offerings . . . ."[229] New Rule 152 provides "four safe harbors applicable to all securities offerings" and also sets forth a general set of integration principles if a safe harbor does not apply.[230]

i. General Principles

New Rule 152(a) prescribes a non-exclusive method for an issuer to determine whether two offers should be integrated if the safe harbors, to be discussed below, are not applicable.[231] It specifies that if the issuer can establish, "based on the particular facts and circumstances," that each offering either complies with the registration requirements of the 1933 Act or that "an exemption from registration is available for the particular offering," no integration will occur.[232] To make that determination for an exempt offering that prohibits general solicitation:

> The issuer must have a reasonable belief, based on the facts and circumstances, with respect to each purchaser in the exempt offering . . . , that the issuer . . . either (i) [d]id not solicit such purchaser through the use of general solicitation; or (ii) [e]stablished a substantive relationship with such purchaser prior to the commencement of the exempt offering prohibiting general solicitation.[233]

These factors are similar to the analysis that an issuer would have employed prior to the adoption of the 2020 Release.[234] They provide, however, more clarity in an exempt offering prohibiting general solicitation, and without an uncompromising time-frame, if the issuer has a reasonable belief that the issuer did not solicit the purchaser through general solicitation or else had a substantive relationship with the purchaser prior to commencement of the exempt offering.[235] With respect to the offering of securities of a bank to be formed, this reasonable belief test should be workable in a manner similar to the factors set forth above.[236]

229. Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, 86 Fed. Reg. at 3499.

230. *Id.* at 3500.

231. *See id.* 3500–01.

232. *Id.* at 3500.

233. *Id.* New Rule 152(a)(2) also offers guidance on two concurrent offers permitting general solicitation, something which could be possible, but not likely, in a de novo bank formation. *See id.*

234. *See supra* notes 201–03 and accompanying text.

235. Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, 86 Fed. Reg. at 3500.

236. *See supra* note 203 and accompanying text.

ii. Safe Harbors

Equally significant, however, with respect to the offering of a security of a bank to be formed, one or more of the safe harbors established by New Rule 152 should be available. Rule 152(b)(1) provides that "no integration analysis under paragraph (a) of [New Rule 152] is required, if any" offering (such as the raising of seed money through an SEC Rule 506(b) exempt offering) is made more than thirty calendar days "before commencement of any other offering."[237] Such "other offering" could include the commencement of the public offer of the security of the bank to be formed.[238] It should be feasible for the organizers of the de novo bank to have the necessary seed money raised and in place through an exempt offering at least thirty days before the "public offer" is undertaken for the capital required under banking regulation requirements.

New Rules 152(b)(3) and (4) may also apply. Under Rule 152(b)(3)(i), an offering pursuant to a filed registration statement will not be integrated with a prior completed offering for which general solicitation is not permitted.[239] Securities offered publicly by a national bank in organization must be made subject to a registration statement filed with the OCC.[240] New Rule 152(b)(3)(i) would clearly be available in that situation and would likely be available for "public" offers of bank securities to be issued by a state-chartered bank, even though no registration statement is required.[241] If such rule is not available for a state-chartered bank, however, Rule 152(b)(4) specifies that an offer and sale "made in reliance on an exemption for which general solicitation is permitted will not be integrated if made *subsequent* to any *terminated or completed* offering."[242] This safe harbor should apply to a public offer of a security of a bank to be formed (whether a national bank or a state-chartered bank) as long as it is made subsequent to the completion of the raising of the seed money for the organizational expenses in an exempt offering.[243]

It is significant that with the safe harbors of Rules 152(b)(3)(i) and (4), no waiting period is required following the "completion" of the prior offering.[244]

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237. Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, 86 Fed. Reg. at 3595.

238. *Id.*; *see also supra* notes 207–09 and accompanying text.

239. Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, 86 Fed. Reg. at 3595.

240. *See supra* notes 172–73 and accompanying text.

241. *See supra* notes 174–75 and accompanying text.

242. Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, 86 Fed. Reg. at 3595 (emphasis added).

243. *See generally* Part III (describing the chartering process).

244. Facilitating Capital Formation and Expanding Investment Opportunities by

As for when an offering is "completed," New Rule 152(d) stipulates that an offering is completed, among other things, when the issuer ceases efforts to make further offers to sell the issuer's securities under such offering.[245] The rule specifically says that, respecting a Regulation D offering, the offering ceases when the issuer has "a binding commitment" to sell all securities to be sold under the offering or the issuer has ceased to make offers, whichever is later.[246] Thus, as long as the organizers of a de novo bank complete the raising of the seed money for organizational expenses *before* commencement of the public offering to sell the securities of the bank to be formed, no integration should be made.[247]

New Rule 152, therefore, provides clarity on how exempt and public offers are to be integrated, and it should present helpful guidance regarding the offer of securities of a bank to be formed. As the SEC itself has concluded, under the integration principle of New Rule 152(a), "issuers may conduct concurrent . . . offerings . . . involving an offering prohibiting general solicitation and another offering permitting general solicitation, without integration concerns, so long as the provisions of Rule 152(a)(1) and all other conditions of the applicable exemptions are satisfied."[248] As for the application of the four safe-harbors of New Rule 152(b), the SEC has said that "[f]or offers and sales meeting the conditions of these safe harbors, the issuer would not need to conduct any further integration analysis."[249] As is typical regarding any SEC exemption, however, the SEC has emphasized that no provision of the New Rule 152 will "have the effect of avoiding integration for any transaction or series of transactions that, although in technical compliance with the rule, is part of a plan or scheme to evade the registration requirements of the [1933] Act."[250]

Improving Access to Capital in Private Markets, 86 Fed. Reg. at 3595 (noting that "no integration analysis" is required where these safe harbor exceptions apply).

245. *Id.*

246. *Id.* at 3596.

247. Under new Rule 152(c), an offering is "commenced" at the time of the first offer by the issuer or its agents. *Id.* at 3595.

248. *Id.* at 3505.

249. *Id.* at 3506.

250. *Id.* at 3504. It should be noted that the 2020 Release also adopted other rules and amendments to existing regulations that may apply to the offering of securities of a de novo bank. Two rules have a part to play in the integration context. The first rule, Rule 148, exempts from the general solicitation concept limited communications made in certain seminars sponsored by institutions, such as colleges or universities or governmental entities, in which more than one issuer participates. *Id.* at 3594–95. At such meetings, a specific offering of securities by the issuer is not made and the sponsor does not, among other things, make investment recommendations or provide advice to attendees, charge entrance fees for attendees, or receive any compensation from issuers for making introduction of attendees. *Id.* at 3594. In the 2020 Release, the SEC also

The ability of organizers of a bank in organization to raise necessary seed money followed by a public offering of securities of the bank to be formed need not present difficult integration issues for state or national de novo banks. As already noted,[251] neither the Federal Reserve nor the FDIC have filing or registration requirements for public offers of bank securities or for exemptions.[252] Thus, under New Rule 152, a legitimate exemption for the raising of the seed money should not pose an integration issue for state banks in organization.

For national banks in organization, the situation is slightly more complex because the OCC adopts the SEC's securities registration and exemption rules.[253] Nevertheless, New Rule 152 provides clear guidance for determining whether any integration issues exist between the raising of seed money by bank organizers and the raising of the necessary capital to form the bank when the OCC grants the bank charter.[254]

IX. CONCLUSION

The process of chartering a new bank is complicated and time-consuming. The OCC (for national bank charters), the state chartering authorities (for state banks), and the FDIC (which insures the deposits of both national and state banks) all heavily scrutinize a de novo bank's business plan and

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adopted Rule 241 to permit an issuer to make limited solicitations of interest from potential investors. *Id.* at 3596. Rule 241(a) permits an issuer before determining which exemption from registration will be relied upon to communicate orally or in writing whether there is an interest. *Id.* Money or other consideration may not be accepted nor may any binding commitment be in place until the issuer decides which exemption will be employed. *Id.* The issuer must state for the potential investor that the issuer is considering an offer but has not decided upon a specific exemption, no money is solicited, and a person's indication of interest involves no obligation to invest. *Id.* Rule 241(c) permits the issuer to provide a means by which the person may indicate interest and provide a name, address, telephone number, or e-mail address. *Id.* Rule 241 would most likely be useful to organizers of a de novo bank in the raising of seed money in the early stages of formation. The rule would give comfort to organizers seeking to select a group of directors and executive officers for the new bank that the seed money is likely to be available. Rule 148, however, is not likely to be of particular benefit to a group of de novo organizers who might make a presentation inasmuch as organizers of de novo banks wish to organize a bank where a new bank is deemed by the bank regulators to be needed and would not want to be participating in a pool of potential de novo bank "issuers" seeking interest for a bank to be formed in the same geographic area. On the other hand, if other types of issuers not competing with banks were present to make a presentation, a de novo bank presentation could be feasible.

251. *See supra* Part VII.

252. *See supra* Part VII.

253. *See supra* note 173 and accompanying text.

254. Because the OCC expressly follows the SEC's rules, New Rule 152 should be readily applied to the de novo national bank. *See supra* note 172 and accompanying text.

projections for future growth, the experience, legal backgrounds, and capabilities of the persons who will serve as directors and officers of the new bank, and the capital to support the new anticipated growth. Sufficient capital is a lynchpin for the foundation of a new bank.

Section 3(a) of the 1933 Act exempts bank securities from the registration requirements of the 1933 Act, and SEC no-action letters have provided practical guidance for the use of Section 3(a) for the offer of securities of banks in formation. NSMIA has also established a path under federal law for a bank in organization to solicit subscriptions in all fifty states for the securities issued by the bank when chartered. This is particularly true in those states where securities laws also provide an exemption for a federal covered security. While states can require notice filings of banks in organization, few do require such filings for that situation. For those states whose securities acts exempt securities of a bank or a security that "will become" a bank security, the capital raising process for a bank in organization should be entitled under NSMIA to proceed without concern over whether the state securities administrator may take issue with the exemption used in the offering.

In those states where the state statute only speaks to an exemption for a "bank," and no separate exemption is expressly granted for a federal covered security, NSMIA clearly affords protection from a state authority that would argue that a bank in organization is not entitled to rely on that state's exemption for a bank security. There is a key point here under NSMIA: if a security offered by a bank in organization is a covered security under NSMIA, it is entitled to preemption of *any* state registration laws, subject to the right of a state to require a notice filing. Apart from NSMIA, in those states that only exempt from registration securities of banks that are already in existence, as interpreted by some state securities authorities, there is still a reasonable basis for relying on the state exemption in any case. To emphasize, however, even in those states whose securities exemptions for a bank security only speak to a bank security, and not also prospectively to a bank security upon completion of the transaction, the security is entitled to NSMIA's federal preemption. As one comment has observed, "[t]he simple fact is that federal preemption is a viable alternative to the patchwork quilt of multi-state regulation."[255] That is not a conclusion that some state securities administrators may want to hear, but such conclusion seems evident under Section 18(a)(1)(B) of the 1933 Act.

All of the foregoing assumes, of course, that it is a bank security, and not a bank holding company security, that is being offered and that in the

255. Chadwick, *supra* note 19, at 771.

organization process the framework is established by the organizers to ensure that the context does not create doubts as to whether something other than a bank security is being "offered" or "sold" for value. An escrow arrangement with an independent bank or third-party to hold subscription funds to be released only upon formation of the bank (or otherwise upon a termination of the offering prior to the chartering of the bank), disclosure to the potential investors that the only security offered is that of a bank (albeit one to be formed), and subscription agreements from investors acknowledging the foregoing all should make it clear that an investor's funds are only at risk for a security of the bank. After all, the securities laws, both federal and state, are designed to protect investor funds, and what needs protection in this instance is the funds that are invested in the bank.