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GOVERNOR



GAVIN M. GEE
DIRECTOR

STATE OF IDAHO
DEPARTMENT OF FINANCE
700 W. STATE STREET, 2ND FLOOR
P. O. BOX 83720
BOISE ID 83720-0031
<http://www2.state.id.us/finance/dof.htm>

August 17, 2001

Re: FDIC- Insured Deposit Products under the Idaho Securities Act

Dear M

This is in response to your letter of July 23, 2001 requesting the Department take a "no-action" position with regard to an exclusion of Bank certificates of deposit ("CDs") from the definition of a security under the Idaho Securities Act ("Act"). In addition, you requested relief pursuant to the salesman registration requirements set forth in the Act.

It is our understanding that Bank, (" Bank') is a FDIC-insured, federal savings bank subsidiary of The Corporation. Bank wishes to offer deposit and loan products and services to customers in Idaho through a network of independent agents, personal financial representatives, insurance agents, telemarketers, and the Internet (" Exclusive Agents").

Many Exclusive Agents will be compensated on the amount of assets placed and maintained with Bank over a one year time period. Exclusive Agents would provide information to prospective customers and then refer them to an representative to complete the transaction.

The Bank deposit products that will be marketed by the Exclusive Agents are conventional, FDIC-insured deposits (checking accounts, savings accounts, money market accounts, and non-negotiable CDs).

Our Department does not concur with your conclusion that certificates of deposit issued by Bank are not securities. However, it appears that the certificates of deposit issued by Bank would be considered exempt securities under the Act.

Banks and S&L's (208) 332-8005
Credit Unions (208) 332-8003
Money Transmitters (208) 332-8003
Supporting Services (208) 332-8001

PHONE: (208) 332-8000
FAX: (208) 332-8098
Director's Fax: (208) 332-8097
Securities Fax: (208) 332-8099

Securities (208) 332-8004
Mortgage Companies (208) 332-8004
Finance Companies (208) 332-8002
Collection Agencies (208) 332-8002

EQUAL OPPORTUNITY EMPLOYER

apply to any security issued by and representing an interest in or a debt of, or guaranteed by, any bank organized under the laws of the United States or any bank, savings institution or trust company organized or chartered as such and under the jurisdiction and supervision of the superintendent of banks of any state.

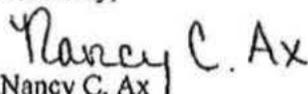
As reflected in §30-1402(2)(a)(i) of the Act, employees of _____ involved in the offer and sale of the CDs would not be required to register as salesman. However, persons who are not employees of the bank are not excluded from the salesman definition under §30-1402(2)(a)(i) of the Act. Therefore, those individuals will need to register pursuant to Section 30-1406 of the Act in order to offer and sell the CDs.

Given the basis of compensation to be paid to the Exclusive _____ agents, the limited protection of FDIC deposits, and the unspecified compliance plan established to seek to ensure Exclusive _____ Agents compliance with all applicable laws and regulations, the Department does not believe the granting of a no-action position would be in the best interest of Idaho residents. Hence, the CD's issued by _____ Bank are considered securities and are subject to the antifraud provisions of the Act. Furthermore, non-bank employees offering these securities must comply with the Act's salesman registration requirements.

Please be aware that the position taken in this letter is based solely on the facts and circumstances presented in the July 23, 2001 letter. Should the facts change or be altered in a material way, our view may be different.

If you have any questions regarding this matter, please contact the undersigned.

Sincerely,


Nancy C. Ax
Securities Analyst

General Counsel

July 23, 2001

VIA EXPRESS MAIL

Mr. Gavin Gee
Department of Finance
Joe R. Williams Building
700 West State Street
Boise, Idaho 83720

Re: FDIC-Insured Deposit Products under the Idaho Securities Act

Dear Mr. Gee:

Bank, Deerfield, Illinois ("Bank"), an FDIC-insured, federal savings bank subsidiary of The Corporation ("Corporation"), requests that the Idaho Department of Finance, Securities Bureau (the "Bureau") provide an exception under § 30-1402 of the Idaho Securities Act (the "Idaho Act"), in the form of a no-action letter to Bank stating that certificates of deposit ("CDs") issued by Bank are not securities under the Idaho Act. In support of this ruling request, we are providing a short description of the proposed deposit activities of Bank in Idaho. We also are providing a short analysis of these activities as they relate to the Idaho Act. We are requesting this relief so that these products can be sold without the necessity of complying with the licensing requirements provided for in the Idaho Act. Pursuant to the Policy Statement dated October 16, 1989 under the Idaho Act (CCH ¶21,486), we enclose a check in the amount of \$50.00 made payable to the Idaho Department of Finance.

I. Background and Description of Products Marketed by Exclusive Agents

Bank was established on November 18, 1998, as an FDIC-insured federal savings bank subsidiary of . As a federal savings bank, Bank is chartered, regulated, and examined by the Office of Thrift Supervision (the "OTS") pursuant to federal law.

Bank plans to provide deposit and loan products and services to customers in Idaho primarily through exclusive network of independent agents and personal financial representatives ("PFRs," and collectively with the independent agents, "Exclusive Agents"), as authorized by the Home Owners' Loan Act (12 U.S.C. §§ 1461 et seq.)¹

¹ Those individuals who are on track to become PFRs are designated "Exclusive Financial Specialists," and they have a limited period of time in which to pass the Series 6 and Series 63 exams. After they have passed these exams, the Exclusive Financial Specialists become PFRs.

Bank intends to use its Exclusive Agents to provide these products and services to customers in all fifty states. Bank's deposit and loan products and services will be available throughout the United States via the Internet, mail, telemarketing and call centers.

The network of Exclusive Agents is composed primarily of individuals who sell insurance products. However, Exclusive Agents are not employees of Exclusive Agents are generally prohibited from selling insurance and financial products issued by non- organizations.² In addition, certain Exclusive Agents currently are registered representatives of , a registered broker-dealer, and, as such, is authorized to sell variable products and mutual funds in Idaho (hereinafter referred to as "Registered Exclusive Agents").

) and will enter into a separate agreement with Bank for the use of Exclusive Agents to market Bank products and services. Under the terms of that agreement, Exclusive Agents will offer Bank's products to customers and will be compensated by Bank through the compensation system. Bank will reimburse the aggregate amount of compensation paid, and also pay a fee for the use of their compensation systems. PFR's will receive a fee based on the initial amount of the CD and the average balance maintained over a one year period after the deposit. Independent agents will receive a fee based on the deposit amount and the type of account referred.

It is expected that Exclusive Agents will provide information and brochures regarding the products and services offered by Bank primarily through mailings and through telephone and personal contacts with customers. Exclusive Agents also will display Bank product brochures in their offices. Because none of the Bank products will be "sold" by Exclusive Agents, Exclusive Agents will refer customers to an Bank representative who will assist the customer in obtaining a desired product or service. The majority of customer services will be provided by representatives at Bank rather than the Exclusive Agents. The Exclusive Agents will not accept any cash deposits or make any withdrawals on behalf of Bank customers.

The Bank deposit products that will be marketed by Exclusive Agents are conventional, FDIC-insured deposits (checking accounts, savings accounts, money market accounts, and non-negotiable CDs). Exclusive Agents will not create a secondary market with respect to the sale of CDs issued by Bank or otherwise add enhancements or features that might cause the deposits to be considered "securities" for purposes of federal securities laws.³

² Exclusive Agents are only permitted to sell products issued by non- organizations where has formally authorized the sale of such products.

³ Cf. Gary Plastic Packaging Corp. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 756 F.2d 230 (2d Cir. 1985) (CD program with special enhancements, including a secondary market for bank-issued certificates of deposit and monitoring of financial conditions of banks issuing certificates of deposit, resulted in the sale of "securities" under the federal securities

II. Ruling Request Regarding the Status of CDs as Securities

We believe that it would be appropriate for the Bureau to issue a no-action letter that indicates that the CDs issued by _____ Bank are not securities for the following reasons:

- the U.S. Supreme Court has deemed FDIC-insured CDs not to be securities
- both the Idaho Act and the Uniform Securities Act are silent as to whether CDs fall within the definition of a “security,” and
- the federal regulatory framework that applies to _____ Bank affords adequate protections to Idaho residents who do business with _____ Bank and its Exclusive Agents.

A. Federal Securities Laws

The federal securities laws generally do not treat an FDIC-insured CD as a “security.” _____ Bank “CDs” are not specifically included in the list of covered instruments in the definition of “security” under the Securities Act of 1933 (the “1933 Act”) or the Securities Exchange Act of 1934 (the “1934 Act”).⁴ In addition, the United States Supreme Court held in Marine Bank v. Weaver, 455 U.S. 551 (1982) that FDIC-insured CDs are not “securities” within the meaning of the 1934 Act. In reaching its conclusion, the Court explained that the CDs at issue were issued by a federally regulated bank subject to a comprehensive set of federal regulations. The Court noted that the CDs were protected by reserve, reporting, and examination requirements under the federal banking laws that are designed to protect the solvency of banks. In addition, the Court emphasized that the FDIC insures such deposits and, as a result, a purchaser of a CD is virtually guaranteed payment in full. The Court determined that, in light of the protections provided by the comprehensive federal bank regulatory system, treatment of CDs as securities was unnecessary.

B. Uniform Securities Act and the Idaho Act

The definition of “security” under the Idaho Act is virtually identical to the definition of “security” under the Uniform Securities Act and federal law. See § 2(1) of the 1933 Act (15 U.S.C. § 77b(1)), § 3(a)(10) of the 1934 Act (15 U.S.C. § 78c(a)(10)), and I.S.A. § 30-1402(12). The Idaho Act defines the term “security” to include, among other instruments,

any note, stock, treasury stock, bond, debenture, evidence of indebtedness, . . . investment contract, [and] voting-trust certificate.

⁴ laws).
⁴ See section 2(1) of the 1933 Act (15 U.S.C. § 77b(1)), and section 3(a)(10) of the 1934 Act (15 U.S.C. § 78c(a)(10)).

FDIC-insured deposits are not specifically included in the definition of "securities" in either the Idaho Act or the Uniform Securities Act. See I.S.A. § 30-1402(12) and Uniform Sec. Act § 401(1).⁵

We have located no binding Idaho authority that states that an FDIC-insured CD issued by a federal savings bank is a security under the Idaho Act. Although the Bureau has issued a policy statement which states that brokered, negotiable certificates of deposit constitute securities under the Idaho Act,⁶ Section 30-1457 of the Idaho Act provides that the Idaho Act is to be construed to "effectuate its general purpose to make uniform the law of those states which enact similar statutes and to coordinate the interpretation and administration of [the] act with the related federal regulations." In Department of Finance v. Engle, 950 P.2d 249 (Ida. 1997), the Supreme Court of Idaho noted that the definition of "security" under the Idaho Act mirrored that of federal law, and, as a result of the guidance provided in Section 30-1457 of the Idaho Act, construed similar language in the federal securities statutes to determine the meaning of "investment contract" as used in the Idaho Act.⁷ Therefore, in light of both the directive given in Section 30-1457 of the Idaho Act to coordinate interpretation of the Idaho Act with related federal regulations and prior case law, we believe that an Idaho state court addressing this issue as a matter of first impression would likely consider the Supreme Court's decisions in Marine Bank and Gary Plastic Packaging Corp. and rule that the FDIC-insured CDs issued by a federal savings bank are not securities under the Idaho Act.

C. Protections for Customers of Bank

Under the regulatory framework applicable to insured depository institutions, depositors of Bank would be afforded the full benefit of the comprehensive set of federal regulations governing deposit activities of Bank – even where customers of Bank deal with Exclusive Agents. Bank must conduct its deposit activities in a manner consistent with applicable federal laws and regulations, including, but not limited to, the disclosure and other requirements of the Truth in Savings Act (12 U.S.C. §§ 4301 et seq.).⁸ The OTS also has the authority to conduct on-site examinations at the office of any Exclusive Agent to review the agent's compliance with federal banking laws (12 U.S.C. § 1464(d)(7)(D)(i)). As a condition to participation in the marketing of Bank products, Exclusive Agents must agree to act in accordance with all applicable laws and regulations and all guidelines, procedures,

⁵ Other states have relied on the rationale of Marine Bank in interpreting their respective definitions of "security." See, e.g., Wrede v. Exchange Bank of Gibbon, 531 N.W.2d 523 (Neb. 1995) (Nebraska Supreme Court held that an FDIC-insured CD would not fall within the ambit of Nebraska securities laws); Ayala v. Jamaica Savings Bank, 468 N.Y.S.2d 306 (1983) (New York Supreme Court, Queens County found that time deposits are not securities under New York law, which does not follow the Uniform Securities Act).

⁶ Policy statement dated July 24, 1984 (CCH ¶21,460).

⁷ Department of Finance v. Engle, 950 P.2d 249, 253 (Ida. 1997); See also State of Idaho v. Gertsch, 2000 Ida. App. LEXIS 92 (Ida. 2000) (Court of Appeals of Idaho examined corresponding federal securities statutes and interpretive case law to determine whether certain transactions involved investment contracts under the Idaho Act).

⁸ Other requirements include the anti-tying provisions of the Bank Holding Company Act Amendments of 1970 (12 U.S.C. §§ 1971 et seq.).

and policies established by Bank, and must successfully complete training required by Bank. Bank, moreover, has established a comprehensive compliance plan to seek to ensure Exclusive Agents' compliance with all applicable laws and regulations.

Further, because the CDs issued by Bank are FDIC-insured, depositors generally are guaranteed payment in full.⁹ Such a guarantee eliminates risk to depositors, and supports a conclusion that these deposits do not require protections afforded by Idaho securities laws. Finally, Exclusive Agents will not accept cash deposit funds from customers of Bank and will not have custody or possession of customer funds in connection with the deposits (other than perhaps mailing a customer's deposit at the request of the customer). This arrangement reduces the potential for loss or theft of deposit funds, and reduces risk to depositors of Bank.

Accordingly, for the above reasons, we request that the Division provide Bank a no-action letter stating that CDs sold by Bank are not "securities" under the Idaho Act. We further request that the Division specify that its ruling applies regardless of whether the amount a customer has on deposit with the Bank exceeds the FDIC insurance limit.

III. Ruling Request Regarding Registration of Exclusive Agents

In the event the Bureau declines to find that the CDs issued by Bank are not securities, we request that the Bureau provide Bank with written assurance that Exclusive Agents will not be required to register as salesmen of Bank.

As you know, I.S.A. § 30-1406 makes it unlawful for any person to transact business in Idaho as a broker-dealer or salesman unless the person is registered under the Idaho Act. "Salesman" means any individual other than a broker-dealer who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales of securities. I.S.A. § 30-1402(2). "Broker-dealer" means any person engaged in the business of effecting transactions in securities for the account of others or for his own account. I.S.A. § 30-1402(3). However, the definition of "broker-dealer" does not include any salesman or issuer. §30-1402(3)(a). "Issuer" is defined as any person who issues or proposes to issue any security. I.S.A. § 30-1402(7). "Security" is defined to include, among other things, any note, stock, treasury stock, bond or evidence of indebtedness. I.S.A. §30-1402(12).

Bank does not fall within the definition of broker-dealer because it is an issuer of securities. Exclusive Agents may fall under the definition of "salesman" if they sell CDs because they represent an issuer, Bank, in effecting or attempting to effect the purchase or sale of securities. None of the exceptions from the definition of "salesman" provided for in § 30-1402(2) apply to the Exclusive Agents. Consequently, all Exclusive Agents appear to need to be registered under the Idaho Act to engage in such activities.

⁹ 12 U.S.C. § 1815. Due to the \$100,000 limit on FDIC deposit insurance, the account(s) of some depositors of Bank are not fully insured by the FDIC.

We request that the Bureau provide written assurances to Bank that the Bureau will not recommend enforcement action against Bank or its Exclusive Agents if the Exclusive Agents do not register as salespersons with the Bureau under I.S.A. § 30-1402(2) as a result of offering for sale or selling CDs issued by Bank in Idaho. The Division should grant this request because registration of the Exclusive Agents under I.S.A. § 30-1402(2) will not afford any additional protections to investors in Idaho. Registration of Exclusive Agents will not afford additional protections to Idaho investors due to:

- the nature of products sold,
- the existing protections afforded by the banking regulatory system applicable to Bank and the Exclusive Agents,
- the limited participation by the Exclusive Agents in the sales process, and
- the fact that registration by Exclusive Agents under the Idaho Act would be duplicative for some Exclusive Agents.

The CDs issued by Bank are relatively safe and simple instruments, the terms of which are well understood by the general public. The CDs also are generally safe because they are FDIC-insured, which means that depositors generally are guaranteed payment in full. Such a guarantee eliminates risk to depositors, and supports a conclusion that the sales of these deposit products do not require the protections afforded by the Idaho Act.

The availability of FDIC insurance for the Bank CDs provides the Bureau a basis to issue the no-action letter requested. For example, the availability of FDIC insurance was key to the U.S. Supreme Court's holding that a CD issued by a bank was not a security under the Securities and Exchange Act of 1934. See *Marine Bank v. Weaver*, 455 U.S. 551 (1982).

These "conventional" or "plain vanilla" CDs are no different than CDs sold by bank employees at bank branches throughout Idaho, and the employees of those banks are not registered under I.S.A. § 30-1402(2). The CDs sold by Bank and its Exclusive Agents are not so-called "brokered CDs" that have received much press recently. For a discussion of brokered CDs, see "Brokered CDs-A Wolf in Sheep's Clothing?" which I have included as "Exhibit A."

Besides the relative safety and simplicity of the Bank CDs, the Bureau should grant this request because the sale of CDs by Bank and its Exclusive Agents is already subject to a comprehensive set of regulations. The Bureau should grant this request for a no-action letter because of the limited participation by the Exclusive Agents in the sale of the CDs. Exclusive Agents will not accept cash deposit funds from customers of Bank and will not have custody or possession of customer funds in connection with the deposits (other than perhaps mailing a customer's deposit at the request of the customer). This arrangement reduces the potential for loss or theft of deposit funds, and reduces risk to depositors of Bank.

Requiring Idaho securities licensing of Exclusive Agents would also be duplicative for PFRs who are already licensed as salespersons of AFS, a broker-dealer selling variable

insurance products and mutual funds. The PFRs have already demonstrated their knowledge of the securities industry and applicable laws by passing both the NASD Series 6 and 63 exams.

As an example of another state that has granted similar no-action relief to State Farm Bank, F.S.B. with respect to the sale of conventional, FDIC-insured CDs, I have included as "Exhibit B" a copy of a letter recently issued to State Farm Bank from the Kentucky Department of Financial Institutions. In that letter, Kentucky concluded that it would take no enforcement action to require agent and broker-dealer registration for State Farm Insurance Company agents who facilitate the offer and sale of CDs issued by State Farm Bank. Kentucky based its ruling on the fact that the State Farm Bank CDs were ordinary CDs similar to those offered by other banks, savings and loan companies, and credit unions, and the fact that State Farm Bank's CDs were not brokered CDs. The types of CDs that State Farm Bank proposes to sell are substantially identical to the types of CDs that Bank proposes to sell.

* * *

We hope that this discussion is helpful and that you are able to provide Bank with a no action letter as requested. If you are unable to provide a no action letter as described, we request the opportunity to meet with you and discuss the issues raised in this letter.

Sincerely,

General Counsel

cc: